

FEDERAL TRADE COMMISSION

16 CFR Part 910

RIN 3084-AB74

Non-Compete Clause Rule

AGENCY: Federal Trade Commission.

ACTION: Notice of proposed rulemaking.

SUMMARY: Pursuant to Sections 5 and 6(g) of the Federal Trade Commission Act, the Federal Trade Commission (“Commission”) is proposing the Non-Compete Clause Rule. The proposed rule would, among other things, provide 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; to maintain with a worker a non-compete clause; or, under certain circumstances, to represent to a worker that the worker is subject to a non-compete clause.

DATES: Comments must be received on or before [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE *FEDERAL REGISTER*].

ADDRESSES: Interested parties may file a comment online or on paper by following the instructions in the Request for Comment part of the **SUPPLEMENTARY**

INFORMATION section below. Write “Non-Compete Clause Rulemaking, Matter No. P201200” on your comment, and file your comment online at

<https://www.regulations.gov>, by following the instructions on the web-based form. If you prefer to file your comment on paper, mail your comment to the following address:

Federal Trade Commission, Office of the Secretary, 600 Pennsylvania Avenue NW, Suite

CC-5610 (Annex C), Washington, DC 20580.

FOR FURTHER INFORMATION CONTACT: Shannon Lane (202-876-5651),

Attorney, Office of Policy Planning, Federal Trade Commission.

SUPPLEMENTARY INFORMATION:

I. Overview of the Proposed Rule

A non-compete clause is a contractual term between an employer and a worker that typically blocks the worker from working for a competing employer, or starting a competing business, within a certain geographic area and period of time after the worker's employment ends. Non-compete clauses limit competition by their express terms. As a result, non-compete clauses have always been considered proper subjects for scrutiny under the nation's antitrust laws.¹ In addition, non-compete clauses between employers and workers are traditionally subject to more exacting review under state common law than other contractual terms, due, in part, to concerns about unequal bargaining power between employers and workers and the fact that non-compete clauses limit a worker's ability to practice their trade.²

In recent decades, important research has shed light on how the use of non-compete clauses by employers affects competition. Changes in state laws governing non-compete clauses have provided several natural experiments that have allowed researchers

¹ See, e.g., *U.S. v. Am. Tobacco Co.*, 221 U.S. 106, 181–83 (1911) (holding several tobacco companies violated Sections 1 and 2 of the Sherman Act due to the collective effect of six of the companies' practices, one of which was the "constantly recurring" use of non-compete clauses); *Newburger, Loeb & Co., Inc. v. Gross*, 563 F.2d 1057, 1082 (2d Cir. 1977) ("Although such issues have not often been raised in the federal courts, employee agreements not to compete are proper subjects for scrutiny under section 1 of the Sherman Act. When a company interferes with free competition for one of its former employee's services, the market's ability to achieve the most economically efficient allocation of labor is impaired. Moreover, employee-noncompetition clauses can tie up industry expertise and experience and thereby forestall new entry.") (internal citation omitted).

² See *infra* Part II.C.

to study the impact of non-compete clauses on competition. This research has shown the use of non-compete clauses by employers has negatively affected competition in labor markets, resulting in reduced wages for workers across the labor force—including workers not bound by non-compete clauses.³ This research has also shown that, by suppressing labor mobility, non-compete clauses have negatively affected competition in product and service markets in several ways.⁴

In this rulemaking, the Commission seeks to ensure competition policy is aligned with the current economic evidence about the consequences of non-compete clauses. In the Commission’s view, the existing legal frameworks governing non-compete clauses—formed decades ago, without the benefit of this evidence—allow serious anticompetitive harm to labor, product, and service markets to go unchecked.

Section 5 of the Federal Trade Commission Act (“FTC Act”) declares “unfair methods of competition” to be unlawful.⁵ Section 5 further directs the Commission “to prevent persons, partnerships, or corporations . . . from using unfair methods of competition in or affecting commerce.”⁶ Section 6(g) of the FTC Act authorizes the Commission to “make rules and regulations for the purpose of carrying out the provisions of” the FTC Act, including the Act’s prohibition of unfair methods of competition.⁷

Pursuant to Sections 5 and 6(g) of the FTC Act, the Commission proposes the Non-Compete Clause Rule. The proposed rule would provide it is an unfair method of competition—and therefore a violation of Section 5—for an employer to enter into or

³ See *infra* Part II.B.1.

⁴ See *infra* Part II.B.2.

⁵ 15 U.S.C. 45(a)(1).

⁶ 15 U.S.C. 45(a)(2).

⁷ 15 U.S.C. 46(g).

attempt to enter into a non-compete clause with a worker; maintain with a worker a non-compete clause; or, under certain circumstances, represent to a worker that the worker is subject to a non-compete clause.⁸

The proposed rule would define the term “non-compete clause” as a contractual term between an employer and a worker that prevents the worker from seeking or accepting employment with a person, or operating a business, after the conclusion of the worker’s employment with the employer.⁹ The proposed rule would also clarify that whether a contractual provision is a non-compete clause would depend not on what the provision is called, but how the provision functions. As the Commission explains below, the definition of non-compete clause would generally not include other types of restrictive employment covenants—such as non-disclosure agreements (“NDAs”) and client or customer non-solicitation agreements—because these covenants generally do not prevent a worker from seeking or accepting employment with a person or operating a business after the conclusion of the worker’s employment with the employer. However, under the proposed definition of “non-compete clause,” such covenants would be considered non-compete clauses where they are so unusually broad in scope that they function as such.¹⁰

The proposed rule would define “employer” as a person—as the term “person” is defined in 15 U.S.C. 57b-1(a)(6)—that hires or contracts with a worker to work for the person.¹¹ The proposed rule would define “worker” as a natural person who works,

⁸ See proposed § 910.2(a). For ease of reference, this NPRM employs the term “use of non-compete clauses” as a shorthand to refer to the conduct that the proposed rule would provide is an unfair method of competition.

⁹ See proposed § 910.1(b)(1).

¹⁰ See *infra* Part V (in the section-by-section analysis for proposed § 910.1(b)).

¹¹ See proposed § 910.1(c).

whether paid or unpaid, for an employer. The proposed rule would clarify that the term “worker” includes 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

In addition to prohibiting employers from entering into non-compete clauses with workers starting on the rule’s compliance date, the proposed rule would require employers to rescind existing non-compete clauses no later than the rule’s compliance date.¹³ The proposed rule would also require an employer rescinding a non-compete clause to provide notice to the worker that the worker’s non-compete clause is no longer in effect.¹⁴ To facilitate compliance, the proposed rule would (1) include model language that would satisfy this notice requirement¹⁵ and (2) establish a safe harbor whereby an employer would satisfy the rule’s requirement to rescind existing non-compete clauses where it provides the worker with a notice that complies with this notice requirement.¹⁶

The proposed rule would include a limited exception for non-compete clauses between the seller and buyer of a business.¹⁷ This exception would only be available where the party restricted by the non-compete clause is an owner, member, or partner holding at least a 25% ownership interest in a business entity.¹⁸ The proposed regulatory text would clarify that non-compete clauses covered by this exception would remain subject to federal antitrust law as well as all other applicable law.

¹² See proposed § 910.1(f).

¹³ See proposed § 910.2(b)(1).

¹⁴ See proposed § 910.2(b)(2)(A).

¹⁵ See proposed § 910.2(b)(2)(C).

¹⁶ See proposed § 910.2(b)(3).

¹⁷ See proposed § 910.3.

¹⁸ See proposed §§ 910.3 and 910.1(e).

The proposed rule would establish an effective date of 60 days, and a compliance date of 180 days, after publication of a final rule in the *Federal Register*.¹⁹

In this notice of proposed rulemaking (“NPRM”), the Commission describes and seeks comment on several alternatives to the proposed rule, including whether non-compete clauses between employers and senior executives should be subject to a different standard than non-compete clauses with other workers.²⁰ The Commission also assesses the benefits and costs of the proposed rule, the impact of the proposed rule on small businesses, and compliance costs related to the proposed rule’s notice requirement.²¹

The Commission seeks comment on all aspects of this NPRM. Comments must be received on or before [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE *FEDERAL REGISTER*].²²

II. Factual Background

A. What Are Non-Compete Clauses?

A non-compete clause is a contractual term between an employer and a worker that prevents the worker from seeking or accepting employment with a person, or operating a business, after the conclusion of the worker’s employment with the employer.²³ A typical non-compete clause blocks the worker from working for a

¹⁹ See proposed § 910.5.

²⁰ See *infra* Part VI.

²¹ See *infra* Parts VII–IX.

²² Pursuant to Section 22(d)(4) of the FTC Act, 15 U.S.C. 57b-3(d)(4), this NPRM was not included in the Commission’s Spring 2022 Regulatory Agenda because the Commission first considered it after the publication deadline for the Regulatory Agenda.

²³ See proposed § 910.1(b). The term “non-compete clause” has also been used to describe agreements between one or more business not to compete against one another, *see, e.g., Lumber Liquidators, Inc. v. Cabinets To Go, LLC*, 415 F. Supp. 3d 703, 709 (E.D. Va. 2009), as well as certain kinds of moonlighting during a worker’s employment, *see, e.g., In the Matter of the Investigation by Barbara D. Underwood, Att’y Gen. of the State of N.Y. of WeWork Companies, Inc.*, Assurance of Discontinuance No. 18-101 (Sept. 18, 2018) at Exhibit B. As underscored above, however, this proposed rule focuses only on post-employment restraints that employers impose on workers.

competing employer, or starting a competing business, within a certain geographic area and period of time after their employment ends. A non-compete clause may be part of the worker's employment contract or may be contained in a standalone contract. Employers and workers may enter into non-compete clauses at the start of, during, or at the end of a worker's employment.

If a worker violates a non-compete clause, the employer may sue the worker for breach of contract. An employer may be able to obtain a preliminary injunction ordering the worker, for the duration of the lawsuit, to stop the conduct that allegedly violates the non-compete clause. If the employer wins the lawsuit, the employer may be able to obtain a permanent injunction ordering the worker to stop the conduct that violates the non-compete clause; a payment of monetary damages from the worker; or both.²⁴ Where workers are subject to arbitration clauses,²⁵ the employer may seek to enforce the non-compete clause through arbitration.

The below examples of non-compete clauses from recent news reports, legal settlements, and court opinions are illustrative.

- A contractual term between a security guard firm and its security guards requiring that, for two years following the conclusion of the security guards' employment with the firm, the security guard may not "[a]ccept employment with or be employed by" a competing business "within a one hundred (100) mile radius" of the security guard's primary jobsite with the firm and stating that the security guards may not "[a]ssist, aid or in any manner whatsoever help any firm,

²⁴ Donald J. Aspelund & Joan E. Beckner, *Employee Noncompetition Law* § 8:2, § 8:22 (Aug. 2021).

²⁵ See, e.g., Alexander J.S. Colvin, Econ. Pol'y Inst., Report, *The Growing Use of Mandatory Arbitration* (Apr. 6, 2018).

corporation, partnership or other business to compete with” the firm. The non-compete clause also contains a “liquidated damages” clause requiring the security guard to pay the firm \$100,000 as a penalty for any conduct that contravenes the agreement.²⁶

- A contractual term between a glass container manufacturing company and its workers typically requiring that, for two years following the conclusion of the worker’s employment with the company, the worker may not directly or indirectly “perform or provide the same or substantially similar services” to those the worker performed for the company to any business in the U.S., Canada, or Mexico that is “involved with or that supports the sale, design, development, manufacture, or production of glass containers” in competition with the company.²⁷
- A contractual term between a sandwich shop chain and its workers stating that, for two years after the worker leaves their job, the worker may not perform services for “any business which derives more than ten percent (10%) of its revenue from selling submarine, hero-type, deli-style, pita and/or wrapped or rolled sandwiches” located within three miles of any of the chain’s more than 2,000 locations in the United States.²⁸

²⁶ Fed. Trade Comm’n, Complaint, *In re Prudential Sec., Inc. et al.*, Matter No. 221 0026 at ¶ 12–¶ 13 (December 28, 2022).

²⁷ Fed. Trade Comm’n, Complaint, *In re Ardagh Group S.A. et al.*, Matter No. 211 0182 at ¶ 9 (December 28, 2022).

²⁸ Dave Jamieson, *Jimmy John’s Makes Low-Wage Workers Sign ‘Oppressive’ Noncompete Agreements*, HuffPost (Oct. 13, 2014). The company agreed to remove the non-compete clause in 2016 as part of a settlement. Office of the Att’y Gen. of the State of N.Y., Press Release, *A.G. Schneiderman Announces Settlement With Jimmy John’s To Stop Including Non-Compete Agreements In Hiring Packets* (June 22, 2016).

- A contractual term between a steelmaker and one of its executives prohibiting the executive from working for “any business engaged directly or indirectly in competition with” the steelmaker anywhere in the world for one year following the termination of the executive’s employment.²⁹
- A contractual term between an office supply company and one of its sales representatives stating that, for two years after the sales representative’s last day of employment, the sales representative is prohibited from “engag[ing] directly or indirectly, either personally or as an employee, associate, partner, or otherwise, or by means of any corporation or other legal entity, or otherwise, in any business in competition with Employer,” within a 100-mile radius of the sales representative’s employment location.³⁰
- A contractual term between a nationwide payday lender and its workers stating that, for one year after the worker leaves their job, they are prohibited from performing any “consumer lending services or money transmission services” for any entity that provides such services, or to “sell products or services that are competitive with or similar to the products or services of the Company,” within a 15-mile radius of any of the payday lender’s 1,000 locations in the United States.³¹
- A contractual term between an online retailer and its warehouse workers prohibiting the workers, for 18 months after leaving their job, from “directly or

²⁹ *AK Steel Corp. v. ArcelorMittal USA, LLC*, 55 N.E.3d 1152, 1156 (Ohio Ct. App. 2016).

³⁰ *Osborne v. Brown & Saenger, Inc.*, 904 N.W.2d 34, 36 (N.D. 2017).

³¹ *People of the State of Ill. v. Check Into Cash of Ill., LLC*, Complaint, 2017-CH-14224 (Ill. Circuit Ct. Oct. 25, 2017), ¶ 29, ¶ 70, https://illinoisattorneygeneral.gov/pressroom/2017_10/Check_Into_Cash-Complaint.pdf.

indirectly . . . engag[ing] or support[ing] the development, manufacture, marketing, or sale of any product or service that competes or is intended to compete with any product or service sold, offered, or otherwise provided by” the retailer—or that is “intended to be sold, offered, or otherwise provided by [the retailer] in the future”—that the worker “worked on or supported” or about which the worker obtained or received confidential information.³²

- A contractual term between a medical services firm and an ophthalmologist stating that, for two years after the termination of the ophthalmologist’s employment with the firm, the ophthalmologist shall not engage in the practice of medicine in two Idaho counties unless the ophthalmologist pays the firm a “practice fee” of either \$250,000 or \$500,000, depending on when the ophthalmologist’s employment ends.³³

In addition to non-compete clauses, other types of contractual provisions restrict what a worker may do after they leave their job. These other types of provisions include, among others:

- Non-disclosure agreements (NDAs)—also known as “confidentiality agreements”—which prohibit the worker from disclosing or using certain information;

³² Spencer Woodman, Exclusive: *Amazon makes even temporary warehouse workers sign 18-month non-compete clauses*, The Verge (Mar. 26, 2015). The company removed the non-compete clause following the media coverage. Josh Lowensohn, *Amazon does an about-face on controversial warehouse worker non-compete contracts*, The Verge (Mar. 27, 2015).

³³ *Intermountain Eye & Laser Ctrs. P.L.L.C. v. Miller*, 127 P.3d 121, 123 (Idaho 2005).

- Client or customer non-solicitation agreements, which prohibit the worker from soliciting former clients or customers of the employer (referred to in this NPRM as “non-solicitation agreements”);³⁴
- No-business agreements, which prohibit the worker from doing business with former clients or customers of the employer, whether or not solicited by the worker;
- No-recruit agreements, which prohibit the worker from recruiting or hiring the employer’s workers;
- Liquidated damages provisions, which require the worker to pay the employer a sum of money if the worker engages in certain conduct; and
- Training-repayment agreements (TRAs), a type of liquidated damages provision in which the worker agrees to pay the employer for the employer’s training expenses if the worker leaves their job before a certain date.³⁵

These other types of restrictive employment covenants can sometimes be so broad in scope that they serve as *de facto* non-compete clauses.³⁶

In addition to restricting what workers may do after they leave their jobs, employers have also entered into agreements with other employers in which they agree not to compete for one another’s workers. These include no-poach agreements, in which

³⁴ The term “non-solicitation agreement” can also refer to a type of agreement between employers not to solicit one another’s employees. In this NPRM, however, the term refers only to contractual provisions between employers and workers prohibiting the worker from soliciting clients or customers of the employer.

³⁵ See, e.g., Norman D. Bishara, Kenneth J. Martin, and Randall S. Thomas, *An Empirical Analysis of Non-Competition Clauses and Other Restrictive Post-Employment Covenants*, 68 Vand. L. Rev. 1, 13 (2015); Uniform Law Comm’n, *Uniform Restrictive Employment Agreement Act*, Draft For Approval (2021) at § 2.

³⁶ See, e.g., *Wegmann v. London*, 648 F.2d 1072, 1073 (5th Cir. 1981); *Brown v. TGS Mgmt. Co., LLC*, 57 Cal. App. 5th 303, 306, 319 (Cal. Ct. App. 2020).

employers agree not to solicit or hire one another's workers, and wage-fixing agreements, in which employers agree to limit wages or salaries (or other terms of compensation).³⁷

The Commission seeks comment on its description in this Part II.A of non-compete clauses. The Commission also encourages workers, employers, and other members of the public to submit comments describing their experiences with non-compete clauses.

B. Evidence Relating to the Effects of Non-Compete Clauses on Competition

Non-compete clauses have presented challenging legal issues for centuries.³⁸ But only in the last two decades has empirical evidence emerged to help regulators and the general public understand how non-compete clauses affect competition in labor markets and product and service markets.

In the early 2000s, researchers began to shed new light on the impacts of non-compete clauses on innovation and productivity. As this new body of research was evolving, news reports revealed non-compete clauses were being imposed even on low-wage workers.³⁹ These reports surprised many observers, who had assumed only highly skilled workers were subject to non-compete clauses.⁴⁰ Researchers responded by applying the tools of economic research to better understand how employers were using non-compete clauses and how they were affecting competition.

1. Labor Markets

³⁷ Fed. Trade Comm'n & U.S. Dep't of Justice Antitrust Division, Antitrust Guidance for Human Resource Professionals (Oct. 2016) at 3.

³⁸ See *infra* Part II.C.

³⁹ See, e.g., Jamieson, *supra* note 28.

⁴⁰ See, e.g., Alan B. Kreuger & Eric A. Posner, The Hamilton Project, Policy Proposal 2018-05, *A Proposal for Protecting Low-Income Workers from Monopsony and Collusion* (February 2018) at 7.

The empirical research on how non-compete clauses affect competition shows that the use of non-compete clauses in the aggregate is interfering with competitive conditions in labor markets.

Labor markets function by matching workers and employers. Workers offer their skills and time to employers. In return, employers offer pay, benefits, and job satisfaction.⁴¹ In a well-functioning labor market, a worker who is seeking a better job—more pay, better hours, better working conditions, more enjoyable work, or whatever the worker may be seeking—can enter the labor market by looking for work. Employers who have positions available compete for the worker’s services. The worker’s current employer may also compete with these prospective employers by seeking to retain the worker—for example, by offering to raise the worker’s pay or promote the worker. Ultimately, the worker chooses the job that best meets their objectives. In general, the more jobs available—*i.e.*, the more options the worker has—the stronger the match the worker will find.

Just as employers compete for workers in a well-functioning labor market, workers compete for jobs. An employer who needs a worker will make it known that the employer has a position available. Workers who learn of the opening will apply for the job. From among the workers who apply, the employer will choose the worker that best meets the employer’s needs—in general, the worker most likely to be the most productive. In general, the more workers who are available—*i.e.*, the more options the employer has—the stronger the match the employer will find.

⁴¹ See, e.g., Dep’t of the Treasury, Report, *The State of Labor Market Competition* (March 7, 2022) at 3.

Through these processes—employers competing for workers, workers competing for jobs, and employers and workers matching with one another—competition in the labor market leads to higher earnings for workers, greater productivity for employers, and better economic conditions.

In a perfectly competitive labor market, if a job that a worker would prefer more—for example, because it has higher pay or is in a better location—were to become available, the worker could switch to it quickly and easily. Due to this ease of switching, in a perfectly competitive labor market, workers would easily match to the optimal job for them. If a worker were to find themselves in a job where the combination of their happiness and productivity is less than in some other job, they would simply switch jobs, making themselves better off.

However, this perfectly competitive labor market exists only in theory. In practice, labor markets deviate substantially from perfect competition. Non-compete clauses, in particular, impair competition in labor markets by restricting a worker's ability to change jobs. If a worker is bound by a non-compete clause, and the worker wants a better job, the non-compete clause will prevent the worker from accepting a new job that is within the scope of the non-compete clause. These are often the most natural alternative employment options for a worker: jobs in the same geographic area and in the worker's field of expertise. For example, a non-compete clause might prevent a nurse in Cleveland from working in the health care field in Northeast Ohio, or a software engineer in Orlando from working for another technology company in Central Florida. The result is less competition among employers for the worker's services and less competition among workers for available jobs. Since the worker is prevented from taking these jobs,

the worker may decide not to enter the labor market at all. Or the worker may enter the labor market but take a job in which they are less productive, such as a job outside their field.

Non-compete clauses affect competition in labor markets through their use in the aggregate. The effect of an individual worker's non-compete clause on competition in a particular labor market may be marginal or may be impossible to discern statistically. However, the use of a large number of non-compete clauses across a labor market markedly affects the opportunities of all workers in that market, not just those with non-compete clauses. By making it more difficult for many workers in a labor market to switch to new jobs, non-compete clauses inhibit optimal matches from being made between employers and workers across the labor force. As a result, where non-compete clauses are prevalent in a market, workers are more likely to remain in jobs that are less optimal with respect to the worker's ability to maximize their productive capacity. This materially reduces wages for workers—not only for workers who are subject to non-compete clauses, but for other workers in a labor market as well, since jobs that would otherwise be better matches for an unconstrained worker are filled by workers subject to non-compete clauses.

a. Estimates of Non-Compete Clause Use

Based on the available evidence, the Commission estimates that approximately one in five American workers—or approximately 30 million workers—is bound by a non-compete clause.

A 2014 survey of workers by Evan Starr, JJ Prescott, and Norman Bishara, which resulted in 11,505 responses, found 18% of respondents work under a non-compete

clause and 38% of respondents have worked under one at some point in their lives.⁴² Among the studies of non-compete clause use discussed here, this study has the broadest and likely the most representative coverage of the U.S. labor force.⁴³ Starr, Prescott, and Bishara also found that, among workers without a bachelor's degree, 14% of respondents reported working under a non-compete clause at the time surveyed and 35% reported having worked under one at some point in their lives.⁴⁴ For workers earning less than \$40,000 per year, 13% of respondents work under a non-compete clause and 33% worked under one at some point in their lives.⁴⁵ Furthermore, this survey shows 53% of workers who are covered by non-compete clauses are hourly workers.⁴⁶

Starr, Prescott, and Bishara also found, in states where non-compete clauses are unenforceable, workers are covered by non-compete clauses at approximately the same rate as workers in other states.⁴⁷ This suggests employers maintain non-compete clauses even where they likely cannot enforce them.

⁴² Evan P. Starr, James J. Prescott, & Norman D. Bishara, *Noncompete Agreements in the U.S. Labor Force*, 64 J. L. & Econ. 53, 53 (2021). A survey of workers conducted in 2017 by Payscale.com reached similar results. This survey estimated that 24.2% of workers are subject to a non-compete clause. Natarajan Balasubramanian, Evan Starr, & Shotaro Yamaguchi, *Bundling Employment Restrictions and Value Appropriation from Employees* 35 (2022), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3814403. This survey also found that non-compete clauses are often used together with other restrictive employment covenants, including non-disclosure, non-recruitment, and non-solicitation covenants. *Id.* at 17 (reporting that respondents that had a non-compete clause reported having all three of the other restrictive employment covenants 74.7% of the time). However, a key limitation of the Payscale.com survey is that it is a convenience sample of individuals who visited Payscale.com during the time period of the survey and is therefore unlikely to be fully representative of the U.S. working population. *Id.* at 13. While weighting based on demographics helps, it does not fully mitigate this concern.

⁴³ The final survey sample contained 11,505 responses, representing individuals from nearly every demographic in the labor force. *Id.* at 58.

⁴⁴ *Id.* at 63.

⁴⁵ *Id.*

⁴⁶ Michael Lipsitz & Evan Starr, *Low-Wage Workers and the Enforceability of Noncompete Agreements*, 68 Mgmt. Sci. 143, 144 (2021) (analyzing data from the Starr, Prescott, & Bishara survey).

⁴⁷ Starr, Prescott, & Bishara, *supra* note 42 at 81.

Other estimates of non-compete clause use cover subsets of the U.S. labor force. One study, a 2021 study by Rothstein and Starr, is based on National Longitudinal Survey of Youth (NLSY) data.⁴⁸ The NLSY consists of a nationally representative sample of 8,984 men and women born from 1980-84 and living in the United States at the time of the initial survey in 1997.⁴⁹ The survey is an often-used labor survey conducted by the Bureau of Labor Statistics, rather than a one-off survey directed solely at calculating the prevalence of non-compete clauses. Using this data, Rothstein and Starr estimate the prevalence of non-compete clauses to be 18%, which is comparable to the number estimated by Starr, Prescott, and Bishara.⁵⁰

Finally, four occupations have been studied individually: executives, physicians, hair stylists, and electrical and electronics engineers. Both Shi (2021) and Kini et al. (2021) estimate prevalence of non-compete clauses for executives. Shi (2021) finds the proportion of executives working under a non-compete clause rose from “57% in the early 1990s to 67% in the mid-2010s.”⁵¹ Kini et al. (2021) find that 62% of CEOs worked under a non-compete clause between 1992 and 2014.⁵² Lavetti et al. (2020) find 45% of physicians worked under a non-compete clause in 2007.⁵³ In a survey of independent hair salon owners, Johnson and Lipsitz (2021) find 30% of hair stylists

⁴⁸ Donna S. Rothstein & Evan Starr, *Mobility Restrictions, Bargaining, and Wages: Evidence from the National Longitudinal Survey of Youth 1997* (2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3974897.

⁴⁹ U.S. Bureau of Labor Statistics, *NLSY97 Data Overview*, <https://www.bls.gov/nls/nlsy97.htm>.

⁵⁰ Rothstein & Starr, *supra* note 48 at 7.

⁵¹ Liyan Shi, *Optimal Regulation of Noncompete Contracts* 27 (2022), https://static1.squarespace.com/static/59e19b282278e7ca5b9ff84f/t/626658ffb73adb2959bd4371/1650874624095/noncompete_shi.pdf.

⁵² Omesh Kini, Ryan Williams, & Sirui Yin, *CEO Noncompete Agreements, Job Risk, and Compensation*, 34 Rev. Fin. Stud. 4701, 4707 (2021).

⁵³ Kurt Lavetti, Carol Simon, & William D. White, *The Impacts of Restricting Mobility of Skilled Service Workers Evidence from Physicians*, 55 J. Hum. Res. 1025, 1042 (2020).

worked under a non-compete clause in 2015.⁵⁴ Finally, in a survey of electrical and electronic engineers, Marx (2011) finds that 43% of respondents signed a non-compete clause.⁵⁵

Some observers have stated that the use of non-compete clauses by employers appears to have increased over time.⁵⁶ However, there is no consistent data available on the prevalence of non-compete clauses over time.

While many workers are bound by non-compete clauses, many workers do not know whether their non-compete clause is legally enforceable or not. As part of their 2014 survey, Starr et al. asked surveyed individuals “Are noncompetes enforceable in your state?” Of the respondents, 37% indicated that they did not know whether or not their non-compete clause was enforceable.⁵⁷ Additionally, 11% of individuals were misinformed: they believed that non-compete clauses were enforceable in their state when they were not, or they believed that non-compete clauses were not enforceable when they were.⁵⁸

Starr et al. also find that only 10.1% of workers with non-compete clauses report bargaining over it.⁵⁹ Additionally, only 7.9% report consulting a lawyer, and only 11.4% of respondents thought that they still would have been hired if they had refused to sign

⁵⁴ Matthew S. Johnson & Michael Lipsitz, *Why Are Low-Wage Workers Signing Noncompete Agreements?*, 57 J. Hum. Res. 689, 700 (2022).

⁵⁵ Matt Marx, *The Firm Strikes Back: Non-Compete Agreements and the Mobility of Technical Professionals*, 76 Am. Socio. Rev. 695, 702 (2011). Calculated as 92.60% who signed a non-compete clause of the 46.80% who were asked to sign a non-compete clause.

⁵⁶ See, e.g., Rachel Arnow-Richman, *Cubewrap Contracts and Worker Mobility: The Dilution of Employee Bargaining Power via Standard Form Noncompetes*, 2006 Mich. St. L. Rev. 963, 981 n.59; John W. Lettieri, American Enterprise Institute, Policy Brief, *A Better Bargain: How Noncompete Reform Can Benefit Workers and Boost Economic Dynamism* (December 2020) at 2.

⁵⁷ J.J. Prescott & Evan Starr, *Subjective Beliefs About Contract Enforceability* 10 (2022), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3873638.

⁵⁸ *Id.* at 11.

⁵⁹ Starr, Prescott, & Bishara, *supra* note 42, at 72.

the non-compete clause.⁶⁰ Marx finds that only 30.5% of electrical engineers who signed non-compete clauses were asked to sign prior to accepting their job offer, and 47% of non-compete clause signers were asked to sign on or after their first day of work.⁶¹

b. Earnings – Effects on Workers Across the Labor Force

By inhibiting optimal matches from being made between employers and workers across the labor force, non-compete clauses reduce the earnings of workers. Several studies have found that increased enforceability of non-compete clauses reduces workers' earnings across the labor market generally and for specific types of workers.

Each of the studies described below analyzes the effects of non-compete clause enforceability on earnings. While different studies have defined enforceability of non-compete clauses in slightly different ways, each uses enforceability as a proxy for the chance that a given non-compete clause will be enforced.⁶²

These studies use “natural experiments” resulting from changes in state law to assess how changes in the enforceability of non-compete clauses affect workers' earnings. The use of a natural experiment allows for the inference of causal effects, since the likelihood that other variables are driving the outcomes is minimal.

First, a study conducted by Matthew Johnson, Kurt Lavetti, and Michael Lipsitz finds that decreasing non-compete clause enforceability from the approximate enforceability level of the fifth-strictest state to that of the fifth-most-lax state would

⁶⁰ *Id.*

⁶¹ Marx (2011), *supra* note 55 at 706. Forty-seven percent is calculated as the sum of 24.43% and 22.86%, the respective percentage of requests that were made on the first day or after the first day at the company.

⁶² All the studies described below rely on twelve concepts of enforceability based on Malsberger's “Non-Compete Clauses: A State-by-State Survey” and Kini et al. supplemented with data from Beck, Reed, and Riden LLP's state-by-state survey of non-compete clauses.

increase workers' earnings by 3-4%.⁶³ Johnson, Lavetti, and Lipsitz also estimate that a nationwide ban on non-compete clauses would increase average earnings by 3.3-13.9%.⁶⁴ The authors also find that non-compete clauses limit the ability of workers to leverage favorable labor markets to receive greater pay: when non-compete clauses are more enforceable, workers' earnings are less responsive to low unemployment rates (which workers may typically leverage to negotiate pay raises).⁶⁵

The second study of the effects of non-compete clause enforceability on earnings, conducted by Evan Starr, estimates that if a state that does not enforce non-compete clauses shifted its policy to that of the state with an average level of enforceability, earnings would fall by about 4%.⁶⁶ Unlike many of the other studies described here, this study does not use a change in enforceability of non-compete clauses to analyze the impact of enforceability. Rather, it examines the differential impact of enforceability on workers in occupations which use non-compete clauses at a high rate versus workers in occupations which use non-compete clauses at a low rate. While the Commission believes that this research design may be less informative with respect to the proposed rule than designs which examine changes in enforceability, the study's estimated effects are in line with the rest of the literature.

The third study, conducted by Michael Lipsitz and Evan Starr, estimates that when Oregon stopped enforcing non-compete clauses for workers who are paid hourly, their wages increased by 2-3%, relative to workers in states which did not experience

⁶³ Matthew S. Johnson, Kurt Lavetti, & Michael Lipsitz, *The Labor Market Effects of Legal Restrictions on Worker Mobility* 2 (2020), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3455381.

⁶⁴ *Id.*

⁶⁵ *Id.* at 36.

⁶⁶ Evan Starr, *Consider This: Training, Wages, and the Enforceability of Non-Compete Clauses*, 72 I.L.R. Rev. 783, 799 (2019).

legal changes. The study also found a greater effect (4.6%) on workers in occupations that used non-compete clauses at a relatively high rate.⁶⁷

The fourth study, conducted by Natarajan Balasubramanian, Jin Woo Chang, Mariko Sakakibara, Jagadeesh Sivadasan, and Evan Starr, found that when Hawaii stopped enforcing non-compete clauses for high-tech workers, earnings of new hires increased by about 4%.⁶⁸

The fifth and sixth studies both show that enforceable non-compete clauses reduce earnings for executives. One study, by Mark Garmaise, finds that decreased enforceability of non-compete clauses increases executives' earnings by 12.7%.⁶⁹ Another study, by Omesh Kini, Ryan Williams, and David Yin, finds that decreased enforceability of non-compete clauses led to lower earnings for CEOs when use of non-compete clauses is held constant. However, the study also finds use of non-compete clauses decreases when non-compete clause enforceability decreases. When that relationship is taken into account, decreased enforceability results in greater earnings for CEOs. For example, if the state which enforces non-compete clauses most strictly (Florida) hypothetically moved to a policy of non-enforcement, then a CEO who had a non-compete clause prior to the policy change would experience an estimated 11.4% increase in their earnings, assuming their non-compete clause was dropped.⁷⁰

⁶⁷ Lipsitz & Starr, *supra* note 46 at 143.

⁶⁸ Natarajan Balasubramanian, Jin Woo Chang, Mariko Sakakibara, Jagadeesh Sivadasan, & Evan Starr, *Locked In? The Enforceability of Non-Compete Clauses and the Careers of High-Tech Workers*, 57 J. Hum. Res. S349, S349 (2022).

⁶⁹ Mark J. Garmaise, *Ties that Truly Bind: Noncompetition Agreements, Executive Compensation, and Firm Investment*, 27 J. L., Econ., & Org. 376, 403 (2011). The reduction in earnings is calculated as $e^{-1.3575 \times 0.1} - 1$, where -1.3575 is taken from Table 4.

⁷⁰ Kini, Williams, & Yin, *supra* note 52 at 4731. The 11.4% increase is calculated as $e^X - 1$, where X is calculated as 9 times the coefficient on CEO Noncompete x HQ Enforce (0.047), where 9 is the enforceability index in Florida, plus the coefficient on CEO Noncompete (-0.144), plus 9 times the coefficient on HQ Enforce (-0.043).

Among the studies listed above, Johnson, Lavetti, and Lipsitz likely has the broadest coverage. The study spans the years 1991 to 2014, examines workers across the labor force, and uses all known common law and statutory changes in non-compete clause enforceability to arrive at its estimates. The study by Starr also covers the entire labor force, from 1996 to 2008. However, the Starr study is only able to compare effects for occupations that use non-compete clauses at a high rate to those that use them at a low rate. The next two studies cover just one legal change, and only a subset of the labor force: hourly workers in Oregon, in the case of Lipsitz and Starr, and high-tech workers in Hawaii, in the case of Balasubramanian et al. Finally, while the studies conducted by Garmaise and Kini et al. examine multiple legal changes, they focus solely on executives.

One limitation of studies of enforceability alone—*i.e.*, studies which do not consider the use of non-compete clauses—is that it is difficult to disentangle the effects of increased enforceability on workers who are subject to non-compete clauses and workers who are not subject to non-compete clauses. In other words, since effects are observed across the labor force (or some subset of it), they include both effects on workers with and without non-compete clauses. However, due to the research cited in the next subsection—indicating non-compete clauses reduce earnings for workers who are *not* subject to non-compete clauses—the Commission believes it is reasonable to conclude based on contextual evidence that the labor-force-wide effects described in the studies above include effects on both workers with and without non-compete clauses.

Three additional studies examine the association between non-compete clause use—rather than enforceability—and earnings. Using the 2014 survey described in Part II.B.1.a, Starr et al. find that the use of non-compete clauses is associated with 6.6%

higher earnings in the model including the most control variables among those they observe.⁷¹ Using the Payscale.com data, Balasubramanian et al. find that while non-compete clause use is associated with 2.1-8.2% greater earnings (compared with individuals with no post-contractual restrictions), this positive association is due to non-compete clauses often being bundled with non-disclosure agreements. Compared with individuals only using non-disclosure agreements, use of non-compete clauses is associated with a 3.0-7.3% *decrease* in earnings, though the authors do not disentangle this effect from the effects of use of non-solicitation and non-recruitment provisions.⁷² Finally, Lavetti et al. find that use of non-compete clauses among physicians is associated with greater earnings (by 14%) and greater earnings growth.⁷³ (The Commission notes, however, this study does not consider how changes in non-compete clause enforceability affect physicians' earnings. As described below in the cost-benefit analysis for the proposed rule, the Commission estimates the proposed rule may increase physicians' earnings, though the study does not allow for a precise calculation.⁷⁴)

However, the Commission does not believe that studies examining the association between non-compete clause use—rather than enforceability—and earnings are sufficiently probative of the effects of non-compete clauses on earnings. The Commission's concern is that non-compete clause use and earnings may both be determined by one or more confounding factors. It may be the case, for example, that employers who rely most on trade secrets both pay more and use non-compete clauses at

⁷¹ Starr, Prescott, & Bishara, *supra* note 42 at 75.

⁷² Balasubramanian, Starr, & Yamaguchi, *supra* note 42 at 40. The percentage range is calculated as $e^{-0.030} - 1$ and $e^{-0.076} - 1$, respectively.

⁷³ Lavetti, Simon, & White, *supra* note 53 at 1051. The increase in earnings is calculated as $e^{0.131} - 1$.

⁷⁴ See *infra* Part VII.B.1.a.ii.

a high rate (which would not necessarily be captured by the control variables observed in studies of non-compete clause use). This means these studies do not necessarily inform how restricting the use of non-compete clauses through a rule would impact earnings. This methodological limitation contrasts with studies examining enforceability of non-compete clauses, in which changes in enforceability are “natural experiments” that allow for the inference of causal effects, since the likelihood that other variables are driving the outcomes is minimal. A “natural experiment” refers to some kind of change in the real world that allows researchers to study the impact of the change on an outcome. In a natural experiment, the change is effectively random, uninfluenced by other factors which could have simultaneously affected the outcome. In such situations, it is therefore most likely the change itself caused any impact that is observed on the outcomes.

The belief that studies of non-compete clause use do not reflect causal estimates is shared by the authors of at least one of the studies of non-compete clause use. As noted in Starr et al., “Our analysis of the relationships between noncompete use and labor market outcomes . . . is best taken as descriptive and should not be interpreted causally.”⁷⁵ As a result, the Commission gives these studies minimal weight. The study of physicians conducted by Lavetti et al. partially mitigates this concern by comparing earnings effects in high- versus low-enforceability states, though this analysis compares only California and Illinois, meaning that it is impossible to disentangle underlying differences in those two states from the effects of non-compete clause enforceability.

c. Earnings – Effects on Workers Not Covered by Non-Compete Clauses

⁷⁵ Starr, Prescott, & Bishara, *supra* note 42 at 73.

As described above, non-compete clauses negatively affect competition in labor markets, thereby inhibiting optimal matches from being made between employers and workers across the labor force. As a result, non-compete clauses reduce earnings not only for workers who are subject to non-compete clauses, but also for workers who are not subject to non-compete clauses.

Two studies show non-compete clauses reduce earnings for workers who are not subject to non-compete clauses. The first study, a 2019 study of the external effects of non-compete clauses conducted by Evan Starr, Justin Frake, and Rajshree Agarwal, analyzed workers without non-compete clauses who worked in states and industries in which non-compete clauses were used at a high rate.⁷⁶ They find that, when the use of non-compete clauses in a given state and industry combination increases by 10%, the earnings of workers who do not have non-compete clauses, but who work in that same state and industry, go down by about 6.12% more when that state has an average enforceability level, compared with a state which does not enforce non-compete clauses.⁷⁷ In effect, this study finds when the use of non-compete clauses by employers increases, that drives down wages for workers who do not have non-compete clauses but who work in the same state and industry. This study also finds this effect is stronger where non-compete clauses are more enforceable.

The Commission notes that, similar to some of the studies described above, this study relies on use of non-compete clauses, as well as cross-sectional differences in enforceability of non-compete clauses, to arrive at their conclusions. While this approach

⁷⁶ Evan Starr, Justin Frake, & Rajshree Agarwal, *Mobility Constraint Externalities*, 30 *Org. Sci.* 961, 6 (2019).

⁷⁷ *Id.* at 11.

calls into question the causal relationship outlined in the study, the authors employ tests to increase confidence in the causal interpretation; however, the tests rely on what data the authors have available, and therefore cannot rule out explanations outside of the scope of their data. This study also analyzes the effect of non-compete clause use for certain workers on workers in a different firm, meaning that factors simultaneously driving non-compete clause use and outcomes within a certain firm will not break the causal chain identified in the study.

Starr, Frake, and Agarwal show the reduction in earnings (and mobility, discussed below) is due to a reduction in the rate of the arrival of job offers. Individuals in state/industry combinations which use non-compete clauses at a high rate do not receive job offers as frequently as individuals in state/industry combinations where non-compete clauses are not frequently used.⁷⁸ The authors also demonstrate decreased mobility and earnings are *not* due to increased job satisfaction (*i.e.*, if workers are more satisfied with their jobs, they may be less likely to change jobs, and more likely to accept lower pay).⁷⁹ Finally, they show that decreased mobility and earnings are not because workers are searching for jobs less frequently, suggesting that job openings and firm behavior matter more to the underlying mechanism.⁸⁰

The second study, conducted by Johnson, Lavetti, and Lipsitz, isolates the impact of a state's enforceability policy on workers not directly affected by that policy to demonstrate non-compete clauses affect not just the workers subject to those non-compete clauses, but the broader labor market as well. In particular, the study finds that

⁷⁸ *Id.* at 10.

⁷⁹ *Id.* at 13.

⁸⁰ *Id.*

increases in non-compete clause enforceability in one state have negative impacts on workers' earnings in bordering states, and the effects are nearly as large as the effects in the state in which enforceability changed. Johnson, Lavetti, and Lipsitz estimate that the impact on earnings of a law change in one state on workers just across that state's border is 87% as great as for workers in the state in which the law was changed (the effect tapers off as the distance to the bordering state increases).⁸¹ When a law change in one state decreases workers' earnings in that state by 4%, that would therefore mean that workers just across the border (*i.e.*, workers who share a commuting zone—a delineation of a local economy⁸²—but who live in another state) would experience decreased earnings of 3.5%. The authors conclude that, since the workers across the border are not *directly* affected by the law change (*i.e.*, contracts that they have signed do not become more or less enforceable), this effect must be due to changes in the local labor market.⁸³

d. Earnings – Distributional Effects

There is evidence that non-compete clauses increase racial and gender wage gaps by disproportionately reducing the wages of women and non-white workers. This may be, for example, because firms use the monopsony power which results from use of non-compete clauses as a means by which to wage discriminate. The study by Johnson, Lavetti, and Lipsitz finds that while earnings of white men would increase by about 3.2% if a state's enforceability moved from the fifth-strictest to the fifth most lax, the comparable earnings increase for workers in other demographic groups would be 3.7-

⁸¹ Johnson, Lavetti, & Lipsitz, *supra* note 63 at 51. Eighty seven percent is calculated as the coefficient on the donor state NCA score (-.181) divided by the coefficient on own state NCA score (-.207).

⁸² See U.S. Econ. Rsch. Serv., Commuting Zones and Labor Market Areas, <https://www.ers.usda.gov/data-products/commuting-zones-and-labor-market-areas/>.

⁸³ Johnson, Lavetti, & Lipsitz, *supra* note 63 at 30.

7.7%, depending on the characteristics of the group (though it is not clear from the study whether or not the differences are statistically significant).⁸⁴ The authors estimate that banning non-compete clauses nationwide would close racial and gender wage gaps by 3.6-9.1%.⁸⁵

e. Job Creation

While non-compete clauses may theoretically incentivize firms to create jobs by increasing the value associated with any given worker covered by a non-compete clause, the evidence is inconclusive. One study, by Gerald Carlino, estimates the job creation rate at startups increased by 7.8% when Michigan increased non-compete clause enforceability.⁸⁶ However, the job creation rate calculated in this study is the ratio of jobs created by startups to overall employment in the state: therefore, the job creation rate at startups may rise either because the number of jobs created by startups rose, or because employment overall fell. The study does not investigate which of these two factors drives the increase in the job creation rate at startups.

Another study finds that several increases in non-compete clause enforceability were associated with a 1.4% increase in average per-firm employment at new firms (though not necessarily total employment).⁸⁷ In this study, the authors attribute the increase in average employment to a change in the composition of newly founded firms. The increases in non-compete clause enforceability prevented the entry of relatively small startups which would otherwise have existed. Therefore, the firms which entered in

⁸⁴ *Id.* at 38.

⁸⁵ *Id.*

⁸⁶ Gerald A. Carlino, *Do Non-Compete Covenants Influence State Startup Activity? Evidence from the Michigan Experiment* at 16 (Fed. Reserve Bank of Phila. Working Paper 21-26, 2021).

⁸⁷ Evan Starr, Natarajan Balasubramanian, & Mariko Sakakibara, *Screening Spinouts? How Noncompete Enforceability Affects the Creation, Growth, and Survival of New Firms*, 64 *Mgmt. Sci.* 552, 561 (2018).

spite of increases in non-compete clause enforceability had more workers on average: this increased the average job creation rate at new firms, because the average entering firm was relatively larger. However, if the mechanism identified by the authors is correct, increases in enforceability generate fewer total jobs, because the same number of large firms may enter (regardless of non-compete clause enforceability), but fewer small firms enter.

A similar mechanism may explain the results in both studies above. If that is indeed the case, then an increase in average per-firm employment among startups is not a positive effect of non-compete clause enforceability: instead, it could actually represent a negative effect, since non-compete clauses prevent small firms from existing in the first place, and overall job creation may decrease. The Commission therefore believes, with respect to job creation rates, the evidence is inconclusive.

2. Product and Service Markets

In addition to analyzing how non-compete clauses affect competition in labor markets, researchers have also analyzed whether non-compete clauses affect competition in markets for products and services. The available evidence indicates the use of non-compete clauses interferes with competitive conditions in product and service markets as well.

The adverse effects of non-compete clauses on product and service markets likely result from reduced voluntary labor mobility. Non-compete clauses directly impede voluntary labor mobility by restricting workers subject to non-compete clauses from moving to new jobs covered by their non-compete clause. Since non-compete clauses prevent some job openings from occurring (by keeping workers in their jobs), they also

prevent workers who are not subject to non-compete clauses from finding new jobs (since the new jobs are already occupied by workers with non-compete clauses).

Influenced by Ronald Gilson's research positing that high-tech clusters in California may have been aided by increased labor mobility because non-compete clauses are generally unenforceable in that state,⁸⁸ many studies have examined how non-compete clauses affect labor mobility. Even literature primarily focused on other outcomes has examined labor mobility as a secondary outcome. Across the board, all studies have found decreased rates of mobility, measured by job separations, hiring rates, job-to-job mobility, implicit mobility defined by job tenure, and within- and between-industry mobility. We briefly describe each of these studies in turn.

A 2006 study conducted by Fallick, Fleischman, and Rebitzer supported Gilson's hypothesis by showing that labor mobility in information technology industries in metropolitan statistical areas (MSAs) in California was 56% higher than in comparison MSAs outside California. They note, however, the estimates may not be fully (or at all) attributable to non-compete clause enforceability. Although the Commission therefore does not find this particular study to be sufficiently probative of the relationship between non-compete clauses and labor mobility, its qualitative findings are in line with the rest of the literature.⁸⁹

To estimate the impacts of non-compete clause enforceability in a fashion that may more plausibly attribute causality to the relationship, in 2009, Marx, Strumsky, and

⁸⁸ Ronald J. Gilson, *The Legal Infrastructure of High Technology Industrial Districts: Silicon Valley, Route 128, and Non-Compete Clauses*, 74 N.Y.U. L. Rev. 575 (1999).

⁸⁹ Bruce Fallick, Charles A. Fleischman, & James B. Rebitzer, *Job-Hopping in Silicon Valley: Some Evidence Concerning the Microfoundations of a High-Technology Cluster*, 88 Rev. Econ. & Statistics 472, 477 (2006).

Fleming examined the impact on labor mobility of Michigan's switch to enforcing non-compete clauses. They found that Michigan's increase in enforceability led to an 8.1% decline in the mobility of inventors.⁹⁰

In 2011, Mark Garmaise examined how a suite of changes in non-compete clause enforceability affected labor mobility. Garmaise found executives made within-industry job changes 47% more often, between-industry job changes 25% more often (though this result was not statistically significant), and any job change 35% more often when non-compete clauses were less enforceable.⁹¹

A 2019 study by Jessica Jeffers uses several legal changes to analyze the impact of non-compete clauses on workers' mobility, finding that decreases in non-compete clause enforceability were associated with an 8.6% increase in departure rates of workers, and a 15.4% increase in within-industry departure rates of workers.⁹²

Evan Starr's 2019 study comparing workers in occupations which use non-compete clauses at a high versus low rate found that a state moving from mean enforceability to no enforceability would cause a decrease in employee tenure for workers in high-use occupations of 8.2%, compared with those in low-use occupations. Here, tenure serves as a proxy for mobility, since tenure is the absence of prior mobility.⁹³

⁹⁰ Matt Marx, Deborah Strumsky, & Lee Fleming, *Mobility, Skills, and the Michigan Non-Compete Experiment*, 55 *Mgmt. Sci.* 875, 884 (2009).

⁹¹ Garmaise, *supra* note 69 at 398.

⁹² Jessica Jeffers, *The Impact of Restricting Labor Mobility on Corporate Investment and Entrepreneurship* 22 (2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3040393.

⁹³ Starr, *supra* note 66 at 798. The value is calculated as $8.2\% = 0.56/6.46$, where 0.56 is the reported impact on tenure and 6.46 is mean tenure in the sample.

Returning to an examination of executives, Liyan Shi's 2020 paper qualitatively confirmed Garmaise's results, showing that executives with enforceable non-compete clauses were 1.8 percentage points less likely to separate from their employers, compared with executives without enforceable non-compete clauses.⁹⁴

Starr, Prescott, and Bishara's 2020 study found that having a non-compete clause was associated with a 35% decrease in the likelihood a worker would leave for a competitor.⁹⁵ However, they also found enforceability does not impact this prediction, in contrast with prior studies. Digging deeper into the mechanism, they find that what matters is the worker's belief about the likelihood their employer would seek to enforce a non-compete clause in court. Workers who did not believe employers would enforce non-compete clauses in court were more likely to report they would be willing to leave for a competitor.⁹⁶ This result confirms the need to ensure that workers are aware of the proposed rule, though it suffers from the same limitations as do previously discussed studies of the impacts of non-compete clause use, rather than enforceability: that studies of use are not causally interpretable, since they may conflate the effects of factors which cause use for the effects of use itself.

Two recent studies examined subgroups of the population affected by state law changes. Balasubramanian et al., in 2022, focused on high-tech workers whose non-compete clauses were banned in Hawaii, and Lipsitz and Starr, in 2022, focused on hourly workers whose non-compete clauses were banned in Oregon. The former found

⁹⁴ Shi, *supra* note 51 at 26.

⁹⁵ Evan Starr, J.J. Prescott, & Norm Bishara, *The Behavioral Effects of (Unenforceable) Contracts*, 36 J. L., Econ., & Org. 633, 652 (2020).

⁹⁶ *Id.* at 664.

that the ban increased mobility by 12.5% in the high-tech sector,⁹⁷ while the latter found that mobility of hourly workers increased by 17.3%.⁹⁸

Finally, a 2022 study by Johnson, Lavetti, and Lipsitz examined the impact on labor mobility of all legal changes after 1991 across the entire labor force. They found moving from the enforceability level of the fifth strictest state to that of the fifth most lax state causes a 6.0% increase in job-to-job mobility in industries using non-compete clauses at a high rate.⁹⁹ Furthermore, they found when a state changes its non-compete clause enforceability in that fashion, workers in neighboring states experience 4.8% increases in mobility as measured by job separations, and 3.9% increases as measured by hiring rates, though neither result was statistically significant.¹⁰⁰

As described below in Part IV.A.1.a.ii, the Commission does not view reduced labor mobility from non-compete clauses—in and of itself—as evidence non-compete clauses negatively affect competition in product and service markets. Instead, reduced labor mobility is best understood as the primary driver of effects in product and service markets that the Commission is concerned about. These effects are described below.

a. Consumer Prices and Concentration

There is evidence that non-compete clauses increase consumer prices and concentration in the health care sector. There is also evidence non-compete clauses increase industrial concentration more broadly. Non-compete clauses may have these effects by inhibiting entrepreneurial ventures (which could otherwise enhance

⁹⁷ Balasubramanian et al., *supra* note 68 at S351.

⁹⁸ Lipsitz & Starr, *supra* note 46 at 157.

⁹⁹ Johnson, Lavetti, & Lipsitz, *supra* note 63 at 21.

¹⁰⁰ *Id.* at 76.

competition in goods and service markets) or by foreclosing competitors' access to talented workers.

One study, by Naomi Hausman and Kurt Lavetti, finds increased concentration, as measured by the Herfindahl-Hirschman Index (HHI), at the firm level¹⁰¹ and increased final goods prices¹⁰² as the enforceability of non-compete clauses increases. Hausman and Lavetti's study focuses on physician markets, showing that while non-compete clauses allow physician practices to allocate clients more efficiently across physicians, this comes at the cost of greater concentration and prices for consumers. Generally, greater concentration may or may not lead to greater prices in all situations and may arise for reasons which simultaneously cause higher prices (indicating, therefore, a noncausal relationship between concentration and prices). In this case, the authors claim that researching the direct link between changes in law governing non-compete clauses and changes in concentration allows them to identify a causal chain starting with greater enforceability of non-compete clauses, which leads to greater concentration, and higher consumer prices.

While there is no additional direct evidence on the link between non-compete clauses and consumer prices, another study, by Michael Lipsitz and Mark Tremblay, shows increased enforceability of non-compete clauses at the state level increases

¹⁰¹ Naomi Hausman & Kurt Lavetti, *Physician Practice Organization and Negotiated Prices: Evidence from State Law Changes*, 13 Am. Econ. J. Applied Econ. 258, 284 (2021). Note that Hausman and Lavetti find decreased HHI at the establishment level (where an establishment is a physical location, and a firm is a company which may own multiple establishments). For the purposes of consumer outcomes such as a price or product quality, the relevant measure of concentration is at the firm level, since firms are unlikely to compete against themselves on price or quality.

¹⁰² *Id.* at 280.

concentration, as measured by an employment-based HHI.¹⁰³ Lipsitz and Tremblay theorize non-compete clauses inhibit entrepreneurial ventures which could otherwise enhance competition in goods and service markets, and show that the potential for harm is greatest in exactly those industries in which non-compete clauses are likely to be used at the highest rate.¹⁰⁴ If the general causal link governing the relationship between enforceability of non-compete clauses, concentration, and consumer prices acts similarly to that identified in the study by Hausman and Lavetti, then it is plausible that increases in concentration identified by Lipsitz and Tremblay would lead to higher prices in a broader set of industries.

In many settings, it is also theoretically plausible that increases in worker earnings from restricting non-compete clauses may increase consumer prices by raising firms' costs (though there is countervailing evidence, especially in goods manufacturing¹⁰⁵). However, we are not aware of empirical evidence that this occurs, and there are also countervailing forces—such as the impacts on concentration described above and positive impacts on innovation¹⁰⁶—that would tend to decrease consumer prices. Additionally, the greater wages observed for workers where non-compete clauses are less enforceable may be due to better worker-firm matching, which could simultaneously increase wages and increase productivity, which could lead to lower prices.

In addition, the only study of how non-compete clauses affect prices—the Hausman and Lavetti study described above—finds decreased non-compete clause

¹⁰³ Michael Lipsitz & Mark Tremblay, *Noncompete Agreements and the Welfare of Consumers* 6 (2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3975864.

¹⁰⁴ *Id.* at 3.

¹⁰⁵ Sebastian Heise, Fatih Karahan, & Ayşegül Şahin *The Missing Inflation Puzzle: The Role of the Wage-Price Pass-Through*, 54 *J. Money, Credit & Banking* 7 (2022).

¹⁰⁶ *See infra* Part II.B.2.d.

enforceability decreases prices in the healthcare market, rather than increasing them. The study notes that, in theory, changes in non-compete clause enforceability could impact physicians' earnings, which could subsequently pass through to prices in healthcare markets. However, the authors show that, where prices decrease due to decreased non-compete clause enforceability, labor cost pass-through is not driving price decreases. As the authors note, if price decreases associated with non-compete clause enforceability decreases were due to pass-through of decreases in physicians' earnings, then the most labor-intensive procedures would likely experience the greatest price decreases when enforceability decreased. However, they find the opposite: there is little to no effect on prices for the most labor-intensive procedures, in contrast with procedures which use relatively less labor. As the authors explain, this shows that decreases in healthcare prices associated with decreases in non-compete clause enforceability are not due to pass-through of lower labor costs.¹⁰⁷

b. Foreclosing Competitors' Ability to Access Talent

There is evidence that non-compete clauses foreclose the ability of competitors to access talent by effectively forcing future employers to buy out workers from their non-compete clauses if they want to hire them. Firms must either make inefficiently high payments to buy workers out of non-compete clauses with a former employer, which leads to deadweight economic loss, or forego the payment—and, consequently, the access to the talent the firm seeks. Whatever choice a firm makes, its economic outcomes in the market are harmed, relative to a scenario in which no workers are bound by non-compete clauses.

¹⁰⁷ Hausman & Lavetti, *supra* note 101 at 278.

Liyan Shi studies this effect in a 2022 paper. This paper finds non-compete clauses are used to ensure that potential new employers of executives make a buyout payment to the executive's current employer.¹⁰⁸ Such a mechanism could be tempered by the ability of a labor market to provide viable alternative workers for new or competing businesses. However, when a particular type of labor is somewhat scarce, when on-the-job experience matters significantly, or when frictions prevent workers from moving to new jobs, there is no way for the market to fill the gap created by non-compete clauses. By studying CEOs, who are difficult to replace and relatively scarce, Shi's paper shows that non-compete clauses foreclose the ability of competitors to access talent by effectively forcing them to make inefficiently high buyout payments. Shi ultimately concludes that "imposing a complete ban on noncompete clauses would be close to implementing the social optimum."¹⁰⁹

c. New Business Formation

The weight of the evidence indicates non-compete clauses likely have a negative impact on new business formation. Three studies show that non-compete clauses and increased enforceability of non-compete clauses reduce entrepreneurship, new business formation, or both. A fourth study also finds that non-compete clauses reduce the rate at which men and women found new startups, though the result is not statistically significant for men. A fifth study finds mixed effects which likely support the theory that non-compete clauses reduce new business formation, and a sixth study finds no effect.

¹⁰⁸ Shi, *supra* note 51.

¹⁰⁹ *Id.* at 35.

New business formation may refer to entrepreneurs creating new businesses from scratch or to businesses being spun off from existing businesses. New business formation increases competition first by bringing new ideas to market, and second, by forcing incumbent firms to respond to new firms' ideas instead of stagnating. New businesses disproportionately create new jobs and are, as a group, more resilient to economic downturns.¹¹⁰ Recent evidence that new business formation is trending downward has led to concerns that productivity and technological innovation are not as strong as they would have been had new business formation remained at higher levels.¹¹¹ Non-compete clauses restrain new business formation by preventing workers subject to non-compete clauses from starting their own businesses. In addition, firms are more willing to enter markets in which they know there are potential sources of skilled and experienced labor, unhampered by non-compete clauses.

Three studies show that non-compete clauses and increased enforceability of non-compete clauses reduce entrepreneurship and new business formation. First, Sampsa Samila and Olav Sorenson, in a 2011 study, examined the differential impacts of venture capital on business formation, patenting, and employment growth. They found when non-compete clauses are more enforceable, rates of entrepreneurship, patenting, and employment growth slow. They find that a 1% increase in venture capital funding increased the number of new firms by 0.8% when non-compete clauses were enforceable,

¹¹⁰ See, e.g., *The Importance of Young Firms for Economic Growth*, Policy Brief, Ewing Marion Kauffman Foundation (Sept. 24, 2015).

¹¹¹ See, e.g., Cong. Budget Off., *Federal Policies in Response to Declining Entrepreneurship* (December 2020).

and by 2.3% when non-compete clauses were not enforceable.¹¹² Similarly, a 1% increase in the rate of venture capital funding increased employment by 0.6% when non-compete clauses were enforceable, versus 2.5% where non-compete clauses were not enforceable.¹¹³

The second study, conducted by Jessica Jeffers in 2019, uses several state law changes to show a decline in new firm entry when non-compete clauses are more enforceable. When non-compete clause enforceability is made stricter (based on the relatively meaningful changes examined in her study), the entry rate of new firms decreased by 10% in the technology sector and the professional, scientific, and technical services sector.¹¹⁴

The third study, conducted by Evan Starr, Natarajan Balasubramanian, and Mariko Sakakibara in 2018, finds that the rate of within-industry spinouts (WSOs) decreases by 0.13 percentage points (against a mean of 0.4%) when non-compete clause enforceability increases by one standard deviation.¹¹⁵ The study's measured impact on the entry rate of non-WSOs (*i.e.*, spinoffs into other industries) is statistically indistinguishable from zero (0.07 percentage point increase associated with a one standard deviation increase in enforceability).¹¹⁶ WSOs have been shown to be highly successful, on average, when compared with typical entrepreneurial ventures.¹¹⁷ By

¹¹² Sampsa Samila & Olav Sorenson, *Noncompete Covenants: Incentives to Innovate or Impediments to Growth*, 57 *Mgmt. Sci.* 425, 432 (2011). The values are calculated as $0.8\% = e^{0.00755} - 1$ and $2.3\% = e^{0.00755 + 0.0155} - 1$, respectively.

¹¹³ *Id.* at 433. The values are calculated as $0.6\% = e^{0.00562} - 1$ and $2.3\% = e^{0.00562 + 0.0192} - 1$, respectively.

¹¹⁴ Jeffers, *supra* note 92 at 32.

¹¹⁵ Starr, Balasubramanian, & Sakakibara, *supra* note 87 at 561.

¹¹⁶ *Id.* at 561.

¹¹⁷ For reviews of the literature, *see, e.g.*, Steven Klepper, *Spinoffs: A Review and Synthesis*, 6 *European Mgmt. Rev.* 159–71 (2009) and April Franco, *Employee Entrepreneurship: Recent Research and Future Directions*, in *Handbook of Entrepreneurship Research* (2005) 81–96.

reducing intra-industry spinoff activity, non-compete clauses prevent entrepreneurial activity that is likely to be highly successful.

The fourth study, published by Matt Marx in 2021, examines the impact of several changes in non-compete clause enforceability between 1991 and 2014.¹¹⁸ Marx finds that, when non-compete clauses are more enforceable, men are 46% less likely to found a rival startup after leaving their employer (though this result is statistically insignificant), that women are 69% less likely to do so, and that the difference in the effect of non-compete clause enforceability on founding rates between men and women is statistically significant.¹¹⁹ This study therefore supports both the theory that non-compete clauses inhibit new business formation and that non-compete clauses tend to have more negative impacts for women than for men.

A fifth study finds mixed effects of non-compete clause enforceability on the entry of businesses into the State of Florida. Hyo Kang and Lee Fleming, in a 2020 study, examine a legal change in Florida which made non-compete clauses more enforceable. This study finds that larger businesses entered the state more frequently (by 8.5%), but smaller businesses entered less frequently (by 5.6%) following the change.¹²⁰ Similarly, Kang and Fleming found that employment at large businesses rose by 15.8% following the change, while employment at smaller businesses effectively did not change.¹²¹

In the Commission's view, however, the results of this study do not necessarily show how non-compete clauses affect new business formation. This study does not

¹¹⁸ Matt Marx, *Employee Non-compete Agreements, Gender, and Entrepreneurship*, Org. Sci. (Online ahead of print) (2021).

¹¹⁹ *Id.* at 9.

¹²⁰ Hyo Kang & Lee Fleming, *Non-Competes, Business Dynamism, and Concentration: Evidence From a Florida Case Study*, 29 J. Econ. & Mgmt. Strategy 663, 673 (2020).

¹²¹ *Id.* at 674. The value is calculated as $15.8\% = e^{0.1468} - 1$.

examine new business formation specifically; instead, it assesses the number of “business entries” into the state. As the authors acknowledge, many of these business entries are not new businesses being formed in Florida (*i.e.*, startups), but existing businesses that are moving to the state.¹²² Because startups are almost never large businesses, the authors’ finding that larger businesses entered the state more frequently is much more likely to reflect businesses moving to the state, rather than new businesses being formed in the state. (While a business’s relocation to Florida may benefit Florida, it is not net beneficial from a national perspective, since the business is simply moving from somewhere else.) The authors’ finding that increased non-compete clause enforceability decreased the entry of smaller businesses is more likely to reflect an effect of non-compete clause enforceability on new business formation, since smaller businesses are relatively more likely than larger businesses to be startups.

A sixth study finds no effect of non-compete clauses on new business formation. A 2021 study by Gerald Carlino analyzes the impact of a legal change in Michigan that allowed the courts to enforce non-compete clauses. This study finds no significant impact on new business formation.¹²³

d. Innovation

The weight of the evidence indicates non-compete clauses decrease innovation. Innovation may directly improve economic outcomes by increasing product quality or decreasing prices, or may promote competition because successful new products and services force competing firms to improve their own products and services. Non-compete

¹²² *Id.* at 668.

¹²³ Carlino, *supra* note 86 at 36.

clauses affect innovation by reducing the movement of workers between firms, which decreases knowledge flow between firms. Non-compete clauses also prevent workers from starting businesses in which they can pursue innovative new ideas.

One study shows increased enforceability of non-compete clauses decreases the value of patenting, using a variety of legal changes. Another study shows that increased non-compete clause enforceability decreases the rate at which venture capital funding increases patenting. Finally, using a legal change in Michigan which increased enforceability, one study shows there were mixed effects on patenting in terms of both quantity and quality, but mechanical patenting (a large part of patenting in Michigan) increased.

The first study, a 2021 study by Zhaozhao He, finds the value of patents, relative to the assets of the firm, increase by about 31% when non-compete clause enforceability decreases.¹²⁴ In contrast to the other two studies of innovation, the study uses the value of patents, rather than the number of patents, to mitigate concerns that patenting activity may not represent innovation, but rather substitutions of protections (in other words, that when non-compete clauses are made less enforceable, firms may use patents instead of non-compete clauses to seek to protect sensitive information).¹²⁵ The study also analyzes the impact of several legal changes to non-compete clause enforceability, which means that the results may be most broadly applicable.

The second study, by Samila and Sorensen, found that, when non-compete clauses are enforceable, venture capital induced less patenting, by 6.6 percentage points.¹²⁶

¹²⁴ Zhaozhao He, *Motivating Inventors: Non-Competes, Innovation Value and Efficiency* 21 (2021), <https://ssrn.com/abstract=3846964>. Thirty one percent is calculated as $e^{0.272}-1$.

¹²⁵ *Id.* at 17.

¹²⁶ Samila & Sorensen, *supra* note 112 at 432. The value is calculated as $6.6\%=e^{0.0208+0.0630}-e^{0.0208}$.

However, as explained above, the authors note patenting may or may not reflect the true level of innovation, as firms may use patenting as a substitute for non-compete clauses where they seek to protect sensitive information.¹²⁷ The final study of innovation, a 2021 study by Gerald Carlino, examined how patenting activity in Michigan was affected by an increase in non-compete enforceability. The study finds that mechanical patenting increased following the law change, but drug patenting fell, and the quality of computer patents fell (as measured by citations).¹²⁸ The increase in mechanical patenting appears to have primarily occurred approximately 14 years after non-compete clause enforceability changed, however, suggesting some other mechanism may have led to the increase in patenting activity.¹²⁹ We place relatively greater weight on studies focused on multiple legal changes to non-compete clause enforceability (such as the above referenced study by He), in which factors unrelated to the legal changes at issue are less likely to drive the results. The Carlino study also does not discuss whether patenting activity is an appropriate measure of innovation, though the other two studies suggest that it may be an unreliable measure at best. The study by Samila and Sorensen examines the enforceability of non-compete clauses across all states but does not consider changes in enforceability: they are therefore unable to rule out that their results could be due to underlying differences in the states rather than non-compete clause enforceability.

The Commission therefore places greatest weight on the study by He, which suggests innovation is largely harmed by non-compete clause enforceability. Though the

¹²⁷ *Id.*

¹²⁸ Carlino, *supra* note 86 at 40.

¹²⁹ *Id.* at 48.

results from Carlino countervail this finding, those results are subject to criticism (as is the corroborating evidence found in Samila and Sorensen).

Two additional studies address firm strategies related to innovation. The first, by Raffaele Conti, uses two changes in non-compete clause enforceability (in Texas and Florida), and indicates that firms engage in riskier strategies with respect to research and development when non-compete clause enforceability is greater.¹³⁰ Riskier research and development strategies lead to more breakthrough innovations, but also lead to more failures, leaving the net impact unclear. The paper does not quantify the total impact on innovation.

The second, by Fenglong Xiao, found increases in non-compete clause enforceability led to increases in exploitative innovation (*i.e.*, innovation which stays within the bounds of the innovating firm's existing competences), and decreases in exploratory innovation (*i.e.*, innovation which moves outside those bounds) in medical devices.¹³¹ Overall, this leads to an increase in the quantity of innovation as measured by the introduction of new medical devices. This increase in quantity, however, is the net result of an increase in exploitative innovation and a decrease in explorative innovation, where the latter is the mode of innovation which the empirical literature has found to be associated with high growth firms.¹³²

¹³⁰ Raffaele Conti, *Do Non-Competition Agreements Lead Firms to Pursue Riskier R&D Strategies?*, 35 Strategic Mgmt. J. 1230 (2014).

¹³¹ Fenglong Xiao, *Non-Competes and Innovation: Evidence from Medical Devices*, 51 Rsch. Pol'y 1 (2022).

¹³² Alessandra Colombelli, Jackie Krafft & Francesco Quatraro, *High-Growth Firms and Technical Knowledge: Do Gazelles Follow Exploration or Exploitation Strategies?*, 23.1 Industrial and Corporate Change 262 (2014).

While these two additional studies bring nuance to the changes in the types of innovation pursued by firms when non-compete clause enforceability changes, neither undermines the weight of the evidence described above: that increased non-compete clause enforceability broadly diminishes the rate of innovation.

e. Training and Other Investment

There is evidence that non-compete clauses increase employee training and other forms of investment. Four studies have examined investment outcomes: two examine the effects of non-compete clause enforceability on investment (both of which find positive impacts on investment), while two examine the relationship between non-compete clause use and investment (only one of which finds positive impacts on investment).

Of the two studies that examine the effects of non-compete clause enforceability on investment, one looks at employee training, and one looks at firm capital expenditures (e.g., investment in physical assets, such as machines). The first study, a 2020 study by Evan Starr, finds that moving from mean non-compete clause enforceability to no non-compete clause enforceability would decrease the number of workers receiving training by 14.7% in occupations that use non-compete clauses at a high rate (relative to a control group of occupations that use non-compete clauses at a low rate).¹³³ The study further finds changes in training are primarily due to changes in firm-sponsored, rather than employee-sponsored, training.¹³⁴ Firm-sponsored training is the type of training non-compete clauses are often theorized to protect, as the firm may be unwilling to make an unprotected investment.

¹³³ Starr, *supra* note 66 at 796–97.

¹³⁴ *Id.* at 797.

The second study, a 2021 study by Jessica Jeffers, finds knowledge-intensive firms invest 32% less in capital equipment following decreases in the enforceability of non-compete clauses.¹³⁵ While firms may invest in capital equipment for many different reasons, Jeffers examines this outcome (as opposed to labor-focused outcomes) to avoid looking at research and development expenditure as a whole, which is in large part composed of labor expenses. This allows the study to isolate the effects of non-compete clause enforceability on investment from other effects of non-compete clauses, such as reduced worker earnings. Jeffers finds that there are likely two mechanisms driving these effects: first, that firms may be more likely to invest in capital when they train their workers because worker training and capital expenditure are complementary (*i.e.*, the return on investment in capital equipment is greater when workers are more highly trained); and second, that non-compete clauses reduce competition, and firms' returns to capital expenditure are greater when competition is lower, incentivizing firms to invest more in capital.¹³⁶

The first study that examines the impact of non-compete clause use on investment is a 2021 study by Starr et. al. using their 2014 survey of non-compete clause use. They find no statistically significant impact on either training or the sharing of trade secrets (after inclusion of control variables) but cannot examine other investment outcomes.¹³⁷ The second study, a 2021 study by Johnson and Lipsitz, examines investment in the hair salon industry. It finds that firms that use non-compete clauses train their employees at a higher rate and invest in customer attraction through the use of digital coupons (on so-

¹³⁵ Jeffers, *supra* note 92 at 28.

¹³⁶ *Id.* at 29.

¹³⁷ Starr, Prescott, & Bishara, *supra* note 42 at 76.

called “deal sites”) to attract customers at a higher rate, both by 11 percentage points.¹³⁸ However, the authors of both studies caution that these results do not necessarily represent a causal relationship.¹³⁹ In each study, the use of non-compete clauses and the decision to invest may be jointly determined by other characteristics of the firms, labor markets, or product markets. For this reason, the Commission places relatively minimal weight on these studies in terms of how they inform the relationship between the proposed rule and future potential firm investment.

Overall, the additional incentive to invest (in assets like physical capital, human capital, or customer attraction, or in the sharing of trade secrets and confidential commercial information) is the primary justification for use of non-compete clauses. Any investment which is lost due to the inability of firms to use non-compete clauses would likely represent the greatest cost of the proposed rule. Indeed, one study, by Kenneth Younge and Matt Marx, finds that the value of publicly traded firms increased by 9% due to an increase in non-compete clause enforceability.¹⁴⁰ However, they attribute this increase to the value of retaining employees, which comes with the negative effects to parties other than the firm (employees, competitors, and consumers) described in this Part II.B. In particular, if benefits to the firm arise primarily from reductions in labor costs, then the increase in the value of firms is in part a transfer from workers to firms, and is therefore not necessarily a procompetitive benefit of non-compete clauses. However, the authors do not explore the extent to which increases in firm value arise from decreases in labor costs. The authors additionally note that since the time frame used in the study is

¹³⁸ Johnson & Lipsitz, *supra* note 54 at 711.

¹³⁹ Starr, Prescott, & Bishara, *supra* note 42 at 73; Johnson & Lipsitz, *supra* note 54 at 711.

¹⁴⁰ Kenneth A. Younge & Matt Marx, *The value of employee retention: evidence from a natural experiment*, 25 J. Econ. & Mgmt. Strategy 652 (2016).

short, “there may be deleterious effects of non-competes in the long run” which are absent in their findings.¹⁴¹

The Commission requests comment on all aspects of its description, in this Part II.B, of the empirical evidence relating to non-compete clauses and their effects on competition. In particular, the Commission seeks submissions of additional data that could inform the Commission’s understanding of these effects.

C. Current Law Governing Non-Compete Clauses

The states have always placed a variety of restrictions on the ability of employers to enforce non-compete clauses. These restrictions are based on public policy concerns American courts—and English courts before them—have recognized for centuries. For example, in the English opinion *Mitchel v. Reynolds* (1711), which provided the foundation for the American common law on non-compete clauses,¹⁴² the court expressed concerns that workers were vulnerable to exploitation under non-compete clauses and these clauses threatened workers’ ability to practice their trades and earn a living.¹⁴³

Today, while the enforceability of non-compete clauses varies between states, all fifty states restrict non-compete clauses between employers and workers to some degree.¹⁴⁴ Non-compete clauses between employers and workers are generally subject to

¹⁴¹ *Id.* at 674.

¹⁴² Harlan Blake, *Employment Agreements Not to Compete*, 73 Harv. L. Rev. 625, 630–31 (1960).

¹⁴³ *Mitchel v. Reynolds*, 1 P. Wms. 181, 190 (Q.B. 1711) (expressing concern that non-compete clauses threaten “the loss of [the worker’s] livelihood, and the subsistence of his family,” and also “the great abuses these voluntary restraints are liable to,” for example, “from masters, who are apt to give their apprentices much vexation” by using “many indirect practices to procure such bonds from them, lest they should prejudice them in their custom, when they come to set up for themselves.”).

¹⁴⁴ Cynthia Estlund, *Between Rights and Contract: Arbitration Agreements and Non-Compete Covenants as a Hybrid Form of Employment Law*, 155 U. Pa. L. Rev. 379, 391 (2006).

greater scrutiny under state common law than other employment terms, due to “the employee’s disadvantageous bargaining position at the time of contracting and hardship at the time of enforcement.”¹⁴⁵ For these reasons, state courts often characterize non-compete clauses as “disfavored.”¹⁴⁶

In addition to state common law, non-compete clauses have always been considered proper subjects for scrutiny under the nation’s antitrust laws.¹⁴⁷

1. State Law on Non-Compete Clauses

The question of whether or under what conditions an employer can enforce a particular non-compete clause depends on the applicable state law. Three states—California, North Dakota, and Oklahoma—have adopted statutes rendering non-compete clauses void for nearly all workers.¹⁴⁸ Among the 47 states where non-compete clauses may be enforced under certain circumstances, 11 states and the District of Columbia have enacted statutes making non-compete clauses void or unenforceable—or have banned

¹⁴⁵ *Id.* See also Restatement (Second) of Contracts sec. 188, cmt. g (1981) (“Postemployment restraints are scrutinized with particular care because they are often the product of unequal bargaining power and because the employee is likely to give scant attention to the hardship he may later suffer through loss of his livelihood.”).

¹⁴⁶ See, e.g., *Navarre Chevrolet, Inc. v. Begnaud*, 205 So. 3d 973, 975 (La. Ct. App. 3d 2016); *Eastman Kodak Co. v. Carmosino*, 77 A.D.3d 1434, 1435 (N.Y. App. Div. 4th 2010); *Access Organics, Inc. v. Hernandez*, 175 P.3d 899, 904 (Mont. 2008); *Bybee v. Isaac*, 178 P.3d 616, 621 (Idaho 2008); *Softchoice, Inc. v. Schmidt*, 763 N.W.2d 660, 666 (Minn. Ct. App. 2009).

¹⁴⁷ See, e.g., *Am. Tobacco Co.*, 221 U.S. at 181–83 (holding several tobacco companies violated Sections 1 and 2 of the Sherman Act due to the collective effect of six of the companies’ practices, one of which was the “constantly recurring” use of non-compete clauses); *Newburger, Loeb & Co., Inc.*, 563 F.2d at 1082 (“Although such issues have not often been raised in the federal courts, employee agreements not to compete are proper subjects for scrutiny under section 1 of the Sherman Act. When a company interferes with free competition for one of its former employee’s services, the market’s ability to achieve the most economically efficient allocation of labor is impaired. Moreover, employee-noncompetition clauses can tie up industry expertise and experience and thereby forestall new entry.”) (internal citation omitted).

¹⁴⁸ See Cal. Bus. & Prof. Code sec. 16600; N.D. Cent. Code sec. 9-08-06; Okla. Stat. Ann. tit. 15, sec. 219A. While California law permits non-compete clauses if they are necessary to protect an employer’s trade secrets, see *Muggill v. Reuben H. Donnelley Corp.*, 62 Cal. 2d 239, 242 (Cal. 1965), the scope of this exception is unclear. In a recent case, the California Supreme Court declined to address the issue. *Edwards v. Arthur Andersen LLP*, 189 P.3d 285, 289 n.4 (Cal. 2008).

employers from entering into non-compete clauses—based on the worker’s earnings or a similar factor.¹⁴⁹ In addition, the majority of these 47 states have statutory provisions that ban or limit the enforceability of non-compete clauses for workers in certain specified occupations. In most states, those limits apply to just one or two occupations (most commonly, physicians).¹⁵⁰

States have been particularly active in restricting non-compete clauses in recent years. Of the twelve state statutes restricting non-compete clauses based on a worker’s earnings or a similar factor (including the D.C. statute), eleven were enacted in the past ten years.¹⁵¹ States have also recently passed legislation limiting the use of non-compete

¹⁴⁹ Colorado, Colo. Rev. Stat. Ann. sec. 8-2-113(2)(a)–(b), as amended by H.B. 22-1317 (effective Aug. 10, 2022) (non-compete clauses are void except where they apply to a “highly compensated worker,” currently defined as a worker earning at least \$101,250 annually, *see* Colo. Code Regs. sec. 1103-14:1.2); District of Columbia, D.C. Code sec. 32-581.02(a)(1) (effective Oct. 1, 2022) (where the employee’s compensation is less than \$150,000, or less than \$250,000 if the employee is a medical specialist, employers may not require or request that the employee sign an agreement or comply with a workplace policy that includes a non-compete clause); Illinois, 820 Ill. Comp. Stat. 90/10(a) (effective Jan. 1, 2017) (no employer shall enter into a non-compete clause unless the worker’s actual or expected earnings exceed \$75,000/year); Maine, Me. Rev. Stat. Ann. tit. 26, sec. 599-A(3) (effective Sep. 19, 2019) (an employer may not require or permit an employee earning wages at or below 400% of the federal poverty level to enter into a non-compete clause with the employer); Maryland, Md. Code Ann., Lab. & Empl. sec. 3-716(a)(1)(i) (effective Oct. 1, 2019) (non-compete clauses are void where an employee earns equal to or less than \$15 per hour or \$31,200 per year); Massachusetts, Mass. Gen. Laws Ann. ch. 149, sec. 24L(c) (effective Jan. 14, 2021) (non-compete clauses shall not be enforceable against workers classified as nonexempt under the Fair Labor Standards Act (“FLSA”)); Nevada, Nev. Rev. Stat. sec. 613.195(3) (effective Oct. 1, 2021) (non-compete clauses may not apply to hourly workers); New Hampshire, N.H. Rev. Stat. Ann. sec. 275:70-a(II) (effective Sept. 8, 2019) (employers shall not require a worker who earns an hourly rate less than or equal to 200% of the federal minimum wage to enter into a non-compete clause, and non-compete clauses with such workers are void and unenforceable); Oregon, Or. Rev. Stat. sec. 653.295(1)(e) (effective Jan. 1, 2022) (non-compete clauses are void and unenforceable except where the worker’s annualized gross salary and commissions at the time of the worker’s termination exceed \$100,533); Rhode Island, R.I. Gen. Laws sec. 28-59-3(a)(1) (effective Jan. 15, 2020) (non-compete clauses shall not be enforceable against workers classified as nonexempt under the FLSA); Virginia, Va. Code Ann. sec. 40.1-28.7:8(B) (effective July 1, 2020) (no employer shall enter into, enforce, or threaten to enforce a non-compete clause with an employee whose average weekly earnings are less than the Commonwealth’s average weekly wage); Washington, Wash. Rev. Code Ann. sec. 49.62.020(1)(b) and 49.62.030(1) (effective Jan. 1, 2020) (non-compete clause is void and unenforceable unless worker’s annualized earnings exceed \$100,000 for employees and \$250,000 for independent contractors, to be adjusted for inflation).

¹⁵⁰ *See* Russell Beck, Beck Reed Riden LLP, *Employee Noncompetes: A State-by-State Survey* (August 17, 2022), (hereinafter “Beck Reed Riden Chart”).

¹⁵¹ *See supra* note 149.

clauses for certain occupations.¹⁵² Other recent state legislation has imposed additional requirements on employers that use non-compete clauses. For example, Oregon, Maine, Massachusetts, New Hampshire, and Washington have enacted laws requiring employers to provide prior notice that a non-compete clause will be required as a condition of employment.¹⁵³ Massachusetts and Oregon have enacted “garden leave” provisions, which require employers to compensate workers during the post-employment period in which the workers are bound by the non-compete clause.¹⁵⁴ Washington limited the permissible duration of non-compete clauses to 18 months,¹⁵⁵ and Massachusetts and Oregon limited it to one year.¹⁵⁶

For workers not covered by these statutory restrictions, the question of whether or under what conditions a non-compete clause may be enforced against them depends on state common law.

In the 47 states where at least some non-compete clauses may be enforced, courts use a reasonableness inquiry to determine whether to enforce a non-compete clause, in addition to whatever statutory limits they are bound to apply. While the precise language

¹⁵² See, e.g., Connecticut, Conn. Gen. Stat. Ann. sec. 20-681 (effective June 26, 2019) (home health care workers); Florida, Fla. Stat. Ann. sec. 542.336 (effective June 25, 2019) (certain physicians in certain counties); Hawaii, Haw. Rev. Stat. sec. 480-4(d) (effective July 1, 2015) (technology workers); Indiana, Ind. Code sec. 25-22.5-5.5-2 (effective July 1, 2020) (physicians); Utah, Utah Code Ann. sec. 34-51-201 (effective May 18, 2018) (broadcasting employees).

¹⁵³ Oregon, Or. Rev. Stat. sec. 653.295(1)(a)(A) (effective Jan. 1, 2008); Maine, Me. Rev. Stat. Ann. tit. 26, sec. 599-A(4) (effective Sep. 19, 2019); Massachusetts, Mass. Gen. Laws Ann. ch. 149, sec. 24L(b)(i) (effective Jan. 14, 2021); New Hampshire, N.H. Rev. Stat. Ann. sec. 275:70 (effective July 28, 2014); Washington, Wash. Rev. Code Ann. sec. 49.62.020(1)(a)(i) (effective Jan. 1, 2020).

¹⁵⁴ Massachusetts, Mass. Gen. Laws Ann. ch. 149, sec. 24L(b)(vii) (effective Jan. 14, 2021); Oregon, Or. Rev. Stat. sec. 653.295(7) (effective Jan. 1, 2022).

¹⁵⁵ Washington, Wash. Rev. Code Ann. sec. 49.62.020(2) (effective Jan. 1, 2020).

¹⁵⁶ Massachusetts, Mass. Gen. Laws Ann. ch. 149, sec. 24L(b)(iv) (effective Jan. 14, 2021); Oregon, Or. Rev. Stat. sec. 653.295(3) (effective Jan. 1, 2022).

of the test differs from state to state, states typically use a test similar to the test in the Restatement (Second) of Contracts:

A promise to refrain from competition that imposes a restraint that is ancillary to an otherwise valid transaction or relationship is unreasonably in restraint of trade if (a) the restraint is greater than is needed to protect the promisee's legitimate interest, or (b) the promisee's need is outweighed by the hardship to the promisor and the likely injury to the public.¹⁵⁷

The first basis on which a non-compete clause can be found unreasonable is where the restraint is greater than needed to protect the employer's legitimate interest. Nearly all states recognize the protection of an employer's trade secrets as a legitimate interest.¹⁵⁸ Some states also recognize an interest in protecting confidential information that is not a trade secret.¹⁵⁹ Some states also recognize an interest in protecting the employer's investment in training, although many of these states define the interest as protecting specialized training.¹⁶⁰ A few states recognize an interest in preventing an worker who provides "unique" services from working for a competitor.¹⁶¹ Courts do not recognize protection from ordinary competition as a legitimate business interest.¹⁶²

If the employer can demonstrate a legitimate interest, the employer must then show the non-compete clause is tailored to that interest. This analysis typically considers

¹⁵⁷ Restatement (Second) of Contracts sec. 188 (1981).

¹⁵⁸ See, e.g., *Reed, Roberts Assocs. v. Strauman*, 40 N.Y.2d 303, 308–09 (N.Y. 1976); see Beck Reed Riden Chart, *supra* note 150 (listing each state's approach).

¹⁵⁹ See, e.g., *Proudfoot Consulting Co. v. Gordon*, 576 F.3d 1223, 1233–34 (11th Cir. 2009); see Beck Reed Riden Chart, *supra* note 150 (listing each state's approach).

¹⁶⁰ See, e.g., *IDMWORKS LLC v. Pophaly*, 192 F. Supp. 3d 1335, 1342 (S.D. Fla. 2016); see Beck Reed Riden Chart, *supra* note 150 (listing each state's approach).

¹⁶¹ See, e.g., *Ticor Title Ins. v. Cohen*, 173 F.3d 63, 70 (2d Cir. 1999); see Beck Reed Riden Chart, *supra* note 150 (listing each state's approach).

¹⁶² See, e.g., *Valley Med. Specialists v. Farber*, 982 P.2d 1277, 1281 (Ariz. 1999).

whether the non-compete clause prohibits a greater scope of activity than necessary to protect the employer's legitimate interests;¹⁶³ covers a geographic area more extensive than necessary to protect those interests;¹⁶⁴ or lasts longer than needed to protect those interests.¹⁶⁵

The second basis under which a non-compete clause can be found unreasonable is where the employer's need for the non-compete clause is outweighed by the hardship to the worker and the likely injury to the public. When assessing the "hardship to the worker" prong, courts typically consider whether the non-compete clause would be unreasonable in light of the worker's personal circumstances. For example, courts have invalidated non-compete clauses where they would destroy a worker's sole means of support.¹⁶⁶

When assessing the "likely injury to the public" prong, the factor most frequently considered by courts is whether enforcing the non-compete clause against the worker would deprive the community of essential goods and services.¹⁶⁷ Because these cases arise in the context of individual litigation, courts focus the "likely injury to the public" inquiry on the loss of the individual worker's services and not on the aggregate effects of non-compete clauses on competition in the relevant market.

State law also differs with respect to the steps courts take when they conclude that a non-compete clause is unenforceable as drafted. The majority of states have adopted the "reformation" or "equitable reform" doctrine, which allows courts to revise the text of an

¹⁶³ See, e.g., *Diversified Hum. Res. Grp., Inc. v. Levinson-Polakoff*, 752 S.W.2d 8, 11 (Tex. Ct. App. 1988).

¹⁶⁴ See, e.g., *Orkin Exterm. Co., Inc. v. Girardeau*, 301 So. 2d 38, 39 (Fla. Ct. App. 1st 1974).

¹⁶⁵ See, e.g., *Jorgensen v. Coppedge*, 181 P.3d 450, 454 (Idaho 2008).

¹⁶⁶ See, e.g., *Chavers v. Copy Prods. Co. of Mobile*, 519 So. 2d 942, 945 (Ala. 1988).

¹⁶⁷ See, e.g., *Dick v. Geist*, 693 P.2d 1133, 1136-37 (Idaho Ct. App. 1985).

unenforceable non-compete clause to make it enforceable.¹⁶⁸ Some states have adopted the “blue pencil” doctrine, under which courts may remove any defective provisions and may enforce the non-compete clause if the remaining provisions constitute a valid non-compete clause.¹⁶⁹ A few states have adopted the “red pencil” doctrine, under which courts declare an entire non-compete clause void if one or more of its provisions are found to be defective.¹⁷⁰

As noted above, the general language of the test for whether a non-compete clause is reasonable is fairly consistent from state to state. However, the specifics of non-compete clause law differ from state to state. For example, states vary in how narrowly or broadly they define legitimate interests for using a non-compete clause and the extent to which courts are permitted to modify an unenforceable non-compete clause to render it enforceable. As a result, among the 47 states where non-compete clauses may be enforced, variation exists with respect to the enforceability of non-compete clauses.¹⁷¹

Because the enforceability of non-compete clauses varies from state to state, the question of which state’s law applies in a legal dispute between an employer and a worker can determine the outcome of the case. Non-compete clauses often contain choice-of-law provisions designating a particular state’s law for resolution of any future dispute.¹⁷² Some non-compete clauses include forum-selection provisions specifying the

¹⁶⁸ See, e.g., *Butler v. Arrow Mirror & Glass, Inc.*, 51 S.W.3d 787, 794 (Tex. Ct. App. 2001). See also Beck Reed Riden Chart, supra note 150 (listing each state’s approach).

¹⁶⁹ See, e.g., *Compass Bank v. Hartley*, 430 F. Supp. 2d 973, 980 (D. Ariz. 2006). See also Beck Reed Riden Chart, supra note 150 (listing each state’s approach).

¹⁷⁰ See, e.g., *Hassler v. Circle C Res.*, 505 P.3d 169, 178 (Wyo. 2022). See also Beck Reed Riden Chart, supra note 150 (listing each state’s approach).

¹⁷¹ Norman D. Bishara, *Fifty Ways to Leave Your Employer: Relative Enforcement of Non-Compete Clauses, Trends, and Implications for Employee Mobility Policy*, 13 U. Pa. J. Bus. L. 751, 778–79 (2011).

¹⁷² Gillian Lester & Elizabeth Ryan, *Choice of Law and Employee Restrictive Covenants: An American Perspective*, 31 Comp. Lab. & Pol’y J. 389, 396–402 (2010).

court and location where any dispute will be heard.¹⁷³ The default rule under conflict-of-laws principles is that the court honors the parties' choice of law, meaning the burden is typically on the worker to argue that the law of a different forum should apply.¹⁷⁴

In addition, there is significant variation in how courts apply choice of law rules in disputes over non-compete clauses.¹⁷⁵ As a result, it can be difficult for employers and workers to predict how disputes over choice of law will be resolved.¹⁷⁶ Additionally—aside from the question of which state's law should apply—employers and workers may be uncertain about whether the non-compete clause is enforceable under the state's law. Furthermore, state non-compete law may change; as described above in Part II.C.1, there have been many changes in state non-compete law in recent years. The result is that employers and workers may face considerable uncertainty as to whether a particular non-compete clause may be enforced.

Workers may also be subject to arbitration clauses, which require that legal disputes with the employer—including disputes related to non-compete clauses—be resolved through binding arbitration rather than in court. Where such clauses are valid, the Federal Arbitration Act requires that courts enforce them.¹⁷⁷

¹⁷³ *Id.* at 402–04.

¹⁷⁴ Lester & Ryan, *supra* note 172 at 394. *Cf.* Cal. Lab. Code § 925(a) (stating that employers shall not require an employee who primarily resides and works in California, as a condition of employment, to agree to a provision that would either (1) require the employee to adjudicate outside of California a claim arising in California or (2) deprive the employee of the substantive protection of California law with respect to a controversy arising in California).

¹⁷⁵ *Id.*

¹⁷⁶ *Id.* at 394–95 (“The state of the law is perhaps characterized more by inconsistency than anything else, so much so that commentators lament the ‘disarray’ and ‘mish-mash’ of the law, and criticize courts for their ‘post-hoc rationalizing of intuitions’ or their use of a ‘hodgepodge of factors, often with insignificant explanation of how they decide what weight to give each.’”) (internal citations omitted).

¹⁷⁷ *See, e.g., Nitro-Lift Techs. v. Howard*, 568 U.S. 17, 21–22 (2012).

Most state courts apply different rules to non-compete clauses when they are entered into between the seller and buyer of a business, compared with non-compete clauses that arise solely out of the employment relationship.¹⁷⁸ The three states in which non-compete clauses are void in nearly all instances—California, North Dakota, and Oklahoma—permit enforcement when non-compete clauses are entered into between the seller and buyer of a business.¹⁷⁹ In most of the other states, non-compete clauses between the seller and buyer of a business are either exempted from the state’s non-compete clause statute, subject to a more lenient test under the statute, or subject to more lenient standard under the state’s case law.¹⁸⁰ Courts cite several different reasons for why they accord different treatment to non-compete clauses between the seller and buyer of a business. These reasons include the relatively equal bargaining power of both parties in the context of a business sale, relative to the employer-worker context, where there is more likely to be unequal bargaining power; the need to protect the buyer’s right to the goodwill for which it has paid; and the fact that the proceeds from the sale will ensure that the seller of the business will not experience undue hardship.¹⁸¹

2. Non-Compete Clauses and Antitrust Law

¹⁷⁸ Based on a review of the state cases in Malsberger (2017), *supra* note 62 and Fenwick & West LLC, *Summary of Non-Compete Clauses: A Global Perspective*, https://assets.fenwick.com/legacy/FenwickDocuments/RS_Summary-of-Covenants.pdf.

¹⁷⁹ Cal. Bus. & Prof. Code sec. 16601; N.D. Cent. Code sec. 9-08-06; Okla. Stat. Ann. tit. 15, sec. 218.

¹⁸⁰ *See, e.g.*, Colo. Rev. Stat. Ann. sec. 8-2-113(3)(c) (statutory exemption); Ga. Code Ann. sec. 13-8-57(d) (more lenient statutory test); *Jiffy Lube Int’l, Inc. v. Weiss Bros., Inc.*, 834 F. Supp. 683, 691 (D.N.J. 1993) (more lenient standard under case law).

¹⁸¹ *See, e.g.*, *Woodward v. Cadillac Overall Supply Co.*, 240 N.W. 2d 710, 715 (Mich. 1976) (bargaining power); *Bybee*, 178 P.3d at 622 (Idaho 2008) (goodwill); *Centorr-Vacuum Indus., Inc. v. Lavoie*, 609 A.2d 1213, 1215 (N.H. 1992) (undue hardship).

Non-compete clauses are “contract[s] . . . in restraint of trade.” Therefore, they are subject to Section 1 of the Sherman Act.¹⁸² The Commission has identified 17 cases in cases in which private plaintiffs or the federal government have challenged a non-compete clause between an employer and a worker under either Section 1 or an analogous provision in a state antitrust statute.¹⁸³ (Three of these 17 cases concerned non-compete clauses between the seller and buyer of a business,¹⁸⁴ and two of these 17 cases were brought under state antitrust statutes.¹⁸⁵)

In two of these 17 cases, the parties challenging the non-compete clause were successful to some degree. In the early antitrust case of *United States v. American Tobacco Co.*, the Supreme Court held that several tobacco companies violated both Section 1 and Section 2 of the Sherman Act because of the collective effect of six of the companies’ practices, one of which was the “constantly recurring” use of non-compete

¹⁸² See, e.g., *Newburger, Loeb & Co., Inc.*, 563 F.2d at 1082.

¹⁸³ *U.S. v. Am. Tobacco Co.*, 221 U.S. 106 (1911); *Alders v. AFA Corp. of Fla.*, 353 F. Supp. 654 (S.D. Fla. 1973) (non-compete clause between seller and buyer of a business); *Bradford v. N.Y. Times Co.*, 501 F.2d 51 (2d Cir. 1974); *Golden v. Kentile Floors, Inc.*, 512 F.2d 838 (5th Cir. 1975); *U.S. v. Empire Gas Corp.*, 537 F.2d 296 (8th Cir. 1976); *Newburger, Loeb & Co., Inc. v. Gross*, 563 F.2d 1057 (2d Cir. 1977); *Lektro-Vend Corp. v. Vendo Co.*, 660 F.2d 255 (7th Cir. 1981) (non-compete clause between seller and buyer of a business); *Aydin Corp. v. Loral Corp.*, 718 F.2d 897 (9th Cir. 1983); *Consultants & Designers, Inc. v. Butler Serv. Grp., Inc.*, 720 F.2d 1553 (11th Cir. 1983); *Caremark Homecare, Inc. v. New England Critical Care, Inc.*, 700 F. Supp. 1033 (D. Minn. 1988); *GTE Data Servs., Inc. v. Elec. Data Sys. Corp.*, 717 F. Supp. 1487 (M.D. Fla. 1989); *DeSantis v. Wackenhut Corp.*, 793 S.W.2d 670 (Tex. 1990) (state antitrust law case); *Borg-Warner Protective Servs. Corp. v. Guardsmark, Inc.*, 946 F. Supp. 495 (E.D. Ky. 1996); *Caudill v. Lancaster Bingo Co., Inc.*, 2005 WL 2738930 (S.D. Ohio Oct. 24, 2005); *Dallas South Mill, Inc. v. Kaolin Mushroom Farms, Inc.*, 2007 WL 9712116 (N.D. Tex. Feb. 23, 2007); *Cole v. Champion Enters., Inc.*, 496 F. Supp. 2d 613 (M.D.N.C. 2007) (non-compete clause between seller and buyer of a business) (state antitrust law case); *Signature MD, Inc. v. MDVIP, Inc.*, 2015 WL 3988959 (C.D. Cal. Apr. 21, 2015). There are also several opinions addressing whether non-compete clauses between businesses violate Section 1. Courts generally apply a less restrictive legal standard to non-compete clauses between businesses. See, e.g., *Lumber Liquidators, Inc.*, 415 F. Supp. 3d at 715–16.

¹⁸⁴ *Alders*, 353 F. Supp. 654; *Lektro-Vend*, 660 F.2d 255; *Cole*, 496 F. Supp. 2d 613.

¹⁸⁵ *DeSantis*, 793 S.W.2d 670; *Cole*, 496 F. Supp. 2d 613.

clauses.¹⁸⁶ This is the only case the Commission has identified in which a court analyzed the collective, rather than isolated, use of non-compete clauses.

More recently, a federal district court denied a motion to dismiss a plaintiff's claim that a non-compete clause between a concierge medicine firm and physicians violated Section 1. The court held that while the reasonableness of the non-compete clause ultimately would be a factual determination, the plaintiff stated a valid claim under Section 1 where it alleged the firm "includes post-contract non-compete clauses with an unreasonably large liquidated damage provision in its employment contracts," in addition to other practices.¹⁸⁷

In the other 15 Sherman Act cases, the challenge to the individual non-compete clause was unsuccessful. These claims failed for three main reasons. First, in several of these cases, the parties challenging the non-compete clause argued solely that the non-compete clause they were challenging should be *per se* unlawful under Section 1. Courts rejected these arguments, reasoning that non-compete clauses may serve legitimate business interests in some instances¹⁸⁸ and that courts have had insufficient experience with non-compete clauses to warrant a *per se* categorization under Section 1.¹⁸⁹

The second main reason these challenges have been unsuccessful is that, in the vast majority of these 15 cases, the party challenging the non-compete clause did not allege the non-compete clause adversely affected competition, which is an essential element of a Section 1 claim in rule of reason cases.¹⁹⁰ In only one case did the plaintiff

¹⁸⁶ *Am. Tobacco Co.*, 221 U.S. at 181–83. Section 2 of the Sherman Act, 15 U.S.C. 2, prohibits monopolization or attempted monopolization.

¹⁸⁷ *Signature MD, Inc.*, 2015 WL 3988959 at *7.

¹⁸⁸ *See, e.g., Lektro-Vend*, 660 F.2d at 265.

¹⁸⁹ *See, e.g., Aydin*, 718 F.2d at 900.

¹⁹⁰ *See, e.g., Ohio v. Am. Express Co.*, — U.S. —, 138 S. Ct. 2274, 2284 (2018).

appear to allege facts related to anticompetitive effect beyond the effect on the person bound by the non-compete clause. In that case, the court dismissed the plaintiff’s claim because the plaintiff did not sufficiently allege “the amount of competition foreclosed by defendant.”¹⁹¹

Third, courts have also rejected challenges to non-compete clauses based on reasoning that a corporation is not capable of conspiring with its employees as a matter of law.¹⁹²

Plaintiffs have also challenged non-compete clauses between employers and workers under Section 2 of the Sherman Act, which prohibits monopolization or attempted monopolization.¹⁹³ The Commission is not aware of a case in which a Section 2 claim relating to an employer’s use of a non-compete clause has been successful.

3. Federal and State Enforcement Activity Related to Non-Compete Clauses

In recent years, state attorneys general in Illinois, New York, and Washington have sued companies for unlawfully using non-compete clauses. As of January 2020, state attorneys general have publicly announced settlements with seven companies regarding the use of non-compete clauses.¹⁹⁴ In February 2022, the Antitrust Division filed a statement of interest in a state non-compete clause case brought by private plaintiffs.¹⁹⁵

¹⁹¹ *GTE Data Servs.*, 717 F. Supp. at 1492.

¹⁹² See, e.g., *Borg-Warner*, 946 F. Supp. 499; *Dallas South Mill*, 2007 WL 9712116 at *3.

¹⁹³ 15 U.S.C. 2. See, e.g., *BRFHH Shreveport, LLC v. Willis Knighton Med. Ctr.*, 176 F. Supp. 3d 606, 616–26 (W.D. La. 2016).

¹⁹⁴ See Public Comments of 19 State Attorneys General in Response to the Federal Trade Commission’s January 9, 2020 Workshop on Non-Compete Clauses in the Workplace at 6 n.23 (listing the settlements).

¹⁹⁵ Statement of Interest of the United States, *Beck v. Pickert Med. Grp.*, No. CV21-02092 (Nev. Dist. Ct. Feb. 25, 2022).

The Antitrust Division and the Commission have also taken steps in recent years to address other types of contractual provisions that restrict competition in labor markets. The Antitrust Division has brought civil enforcement actions under Section 1 against several technology companies for entering into no-poach agreements with competitors. These enforcement actions ended with consent judgments against the companies.¹⁹⁶ In addition, the Antitrust Division has brought criminal charges for wage-fixing and no-poach agreements against companies and individuals.¹⁹⁷ The Commission too has brought civil enforcement actions against companies related to competition for employment, which ended in consent judgments against the companies.¹⁹⁸ In addition, the attorney general of the State of Washington has entered into settlement agreements with over 200 companies in which the companies have agreed to stop using no-poach clauses.¹⁹⁹

The Commission seeks comment on all aspects of its description, in this Part II.C, of the law currently governing non-compete clauses. The Commission specifically seeks comment on the extent to which employers use choice-of-law provisions to evade the

¹⁹⁶ See Antitrust Guidance for Human Resource Professionals, *supra* note 37 at 3–4 (citing cases).

¹⁹⁷ *U.S. v. Neeraj Jindal and John Rodgers*, No. 4:20-cr-358-ALM-KPJ (E.D. Tex. Dec. 9, 2020); *U.S. v. Surgical Care Affiliates, LLC and SCAI Holdings, LLC*, No. 3:21-cr-011-L (N.D. Tex. Jan. 5, 2021); *U.S. v. Ryan Hee and VDA OC, LLC*, formerly ADVANTAGE ON CALL, LLC, No. 2:21-cr-00098-RFB-BNW (D. Nev. Mar. 26, 2021); *U.S. v. DaVita, Inc. and Kent Thiry*, No. 21-cr-00229-RBJ (D. Colo. Nov. 3, 2021); *U.S. v. Patel, et al.*, 3:21-cr-220-VHB-RAR (D. Conn. Dec. 15, 2021); *U.S. v. Manaha, et al.*, 2:22-cr-00013-JAW (D. Me. Jan. 27, 2022). The defendants in the *Jindal* case were found not guilty of the wage-fixing charge, and the defendants in the *DaVita* cases were found not guilty of all charges. *Jindal*, Jury Verdict (E.D. Tex. Apr. 14, 2022); *DaVita*, Verdict (D. Colo. Apr. 15, 2022). However, both courts found that the conduct alleged in the indictment properly fell within the confines of the *per se* rule. *Jindal*, Memorandum Opinion and Order, 2021 WL 5578687 (E.D. Tex. Nov. 29, 2021) at *4–*8; *DaVita*, Order Denying Defendants’ Motion to Dismiss, 2022 WL 266759 (D. Colo. Jan. 28, 2022) at *4–*8. The court in *Manaha* likewise recently denied a motion to dismiss, holding the indictment charged a recognized form of *per se* illegal conduct. 2022 WL 3161781, at **7, 9 (D. Me. Aug. 8, 2022).

¹⁹⁸ See Antitrust Guidance for Human Resource Professionals, *supra* note 37 at 4 (citing cases).

¹⁹⁹ Office of the Att’y Gen. of the State of Wash., Press Release, *AG Report: Ferguson’s Initiative Ends No-Poach Practices Nationally at 237 Corporate Franchise Chains* (June 16, 2020).

laws of states where non-compete clauses are relatively less enforceable. The Commission also seeks comment on the extent to which a uniform federal standard for non-compete clauses would promote certainty for employers and workers.

D. The Commission’s Work on Non-Compete Clauses

This rulemaking represents the culmination of several years of activity by the Commission related to non-compete clauses and their effects on competition. This activity has included extensive public outreach and fact-gathering related to non-compete clauses, other restrictive employment covenants that may harm competition, and competition in labor markets generally. The Commission has also analyzed non-compete clauses in connection with its enforcement, research, and merger review work.

The Commission first began focusing on non-compete clauses in the mid-2010s, as a growing body of empirical research raised concerns about the anticompetitive effects of non-compete clauses. In 2018 and 2019, the Commission held several “Hearings on Competition and Consumer Protection in the 21st Century.”²⁰⁰ The Commission invited public comment on a wide range of topics, including “the use of non-competition agreements and the conditions under which their use may be inconsistent with the antitrust laws.”²⁰¹ Participants addressed non-compete clauses at two of the hearings.²⁰²

²⁰⁰ Fed. Trade Comm’n, *Hearings on Competition and Consumer Protection in the 21st Century*, <https://www.ftc.gov/enforcement-policy/hearings-competition-consumer-protection>.

²⁰¹ Fed. Trade Comm’n, Notice, *Hearings on Competition and Consumer Protection in the 21st Century*, 83 FR 38307, 38309 (Aug. 6, 2018).

²⁰² Fed. Trade Comm’n, Transcript, *Competition and Consumer Protection in the 21st Century* (Oct. 16, 2018), https://www.ftc.gov/system/files/documents/public_events/1413712/ftc_hearings_session_3_transcript_day_2_10-16-18_1.pdf; Fed. Trade Comm’n, Transcript, *Competition and Consumer Protection in the 21st Century* (June 12, 2019), https://www.ftc.gov/system/files/documents/public_events/1519667/ftc_hearings_session_14_transcript_6-12-19_0.pdf.

Also in 2019, the Open Markets Institute, 19 labor and public interest organizations, and 46 individual advocates and scholars petitioned the Commission to initiate a rulemaking to prohibit non-compete clauses.²⁰³

As evidence mounted regarding the anticompetitive effects of non-compete clauses, the Commission's focus on this issue increased. On January 9, 2020, the Commission held a public workshop on non-compete clauses. At the workshop, speakers and panelists addressed topics including statutory and judicial treatment of non-compete clauses; the Commission's authority to address non-compete clauses; the economic literature regarding the effects of non-compete clauses; and whether the Commission should initiate a rulemaking on non-compete clauses.²⁰⁴ In connection with the workshop, the Commission sought public comment on a wide range of topics related to a potential rulemaking on non-compete clauses. The Commission received 328 comments addressing these topics from researchers, advocates for workers, employers, trade associations, attorneys, members of Congress, state and local officials, unions, other organizations, and individual members of the public.²⁰⁵

In addition, on August 5, 2021, the Commission issued a solicitation for public comment on contract terms that may harm competition, including “non-compete clauses that prevent workers from seeking employment with other firms.” The Commission

²⁰³ Open Markets Inst. et al., *Petition for Rulemaking to Prohibit Worker Non-Compete Clauses* (March 20, 2019).

²⁰⁴ Fed. Trade Comm'n, *Non-Competes in the Workplace: Examining Antitrust and Consumer Protection Issues*, <https://www.ftc.gov/news-events/events/2020/01/non-compete-clauses-workplace-examining-antitrust-consumer-protection-issues>.

²⁰⁵ Fed. Trade Comm'n, Docket FTC-2019-0093, *Workshop on Non-Compete Clauses Used in Employment Contracts*, <https://www.regulations.gov/document/FTC-2019-0093-0001/comment>.

received 280 comments on this solicitation from a wide range of stakeholders.²⁰⁶ On December 6-7, 2021, the Commission and the Antitrust Division held a workshop entitled “Making Competition Work: Promoting Competition in Labor Markets.” The Commission sought comment from the public in connection with this event and received 27 comments.²⁰⁷

As it has developed this proposed rule, the Commission has closely considered the views expressed at these forums and the public comments it has received through these engagement efforts. The comments have informed the Commission’s understanding of the evidence regarding the effects of non-compete clauses; the law currently governing non-compete clauses; and the options for how the Commission may seek to restrict the unfair use of non-compete clauses through rulemaking, among other topics.

The Commission has also focused on non-compete clauses in connection with its enforcement, merger review, and research work. With respect to enforcement, in 2021, the Commission initiated investigations into the use of non-compete clauses by manufacturers of glass containers used for food and beverage packaging. On December 28, 2022, the Commission accepted, subject to final approval, consent agreements with two manufacturers in the industry.²⁰⁸ The glass container industry is highly concentrated and is characterized by substantial barriers to entry and expansion. Among these barriers,

²⁰⁶ Fed. Trade Comm’n, *Solicitation for Public Comments on Contract Terms that May Harm Competition* (Aug 5, 2021), <https://www.regulations.gov/document/FTC-2021-0036-0022>.

²⁰⁷ Fed. Trade Comm’n, Docket FTC-2021-0057, *Making Competition Work: Promoting Competition in Labor Markets*, <https://www.regulations.gov/docket/FTC-2021-0057/comments>.

²⁰⁸ Fed. Trade Comm’n, Decision and Order, *In re O-I Glass, Inc. et al*, Matter No. 211 0182 (December 28, 2022); Fed. Trade Comm’n, Decision and Order, *In re Ardaugh Group S.A. et al*, Matter No. 211 0182 (December 28, 2022).

it is difficult to identify and employ personnel with skills and experience in glass container manufacturing.²⁰⁹

The complaints allege the manufacturers required employees across a variety of positions—including employees who work with the glass plants’ furnaces and forming equipment and in other glass production, engineering, and quality assurance roles—to enter into non-compete clauses. The complaints allege this conduct has a tendency or likelihood to impede rivals’ access to the restricted employees’ labor, to limit workers’ mobility, and thus to harm workers, consumers, competition, and the competitive process. As such, the complaints allege each company has engaged in an unfair method of competition in violation of Section 5 of the FTC Act.²¹⁰ The proposed consent orders would prohibit each manufacturer from “entering or attempting to enter, maintaining or attempting to maintain, or enforcing or attempting to enforce a Non-Compete Restriction with an Employee, or communicating to an Employee or a prospective or current employer of that Employee that the Employee is subject to a Non-Compete Restriction.”²¹¹

In 2021, the Commission also initiated investigations into the use of non-compete clauses in the security guard services industry. On December 28, 2022, the Commission accepted, subject to final approval, a consent agreement with Prudential Security, Inc., Prudential Command Inc., and the firms’ co-owners (collectively “Prudential Respondents”). Prudential Security, Inc. and Prudential Command Inc. provided security guard services to clients in several states.

²⁰⁹ Fed. Trade Comm’n, Analysis of Agreements Containing Consent Order to Aid Public Comment, *In re O-I Glass Inc. et al., In re Ardaugh Group S.A. et al.*, Matter No. 211 0182 (December 28, 2022) at 2.

²¹⁰ *Id.* at 1-2.

²¹¹ *Id.* at 7.

The Commission’s complaint alleges the Prudential Respondents’ use of non-compete clauses is an unfair method of competition under Section 5 because it is restrictive, coercive, and exploitative and negatively affects competitive conditions.²¹² The complaint further alleges the Prudential Respondents’ imposition of non-compete clauses took advantage of the unequal bargaining power between Prudential Respondents and their employees, particularly low-wage security guard employees, and thus reduced workers’ job mobility, limited competition for workers’ services, and ultimately deprived workers of higher wages and more favorable working conditions.²¹³ Under the terms of the proposed order, Prudential Respondents—including any companies the co-owners may control in the future—must cease and desist from entering, maintaining, enforcing, or attempting to enforce any non-compete clause.²¹⁴

These consent orders have been placed on the public record for 30 days in order to receive comments from interested persons. After 30 days, the Commission will again review the consent agreements and the comments received and will decide whether it should make the proposed orders final or take other appropriate action.²¹⁵

In addition, as part of a 2020 settlement with the Commission, three national rent-to-own companies agreed to refrain from enforcing non-compete clauses that were entered into in connection with reciprocal purchase agreements.²¹⁶

²¹² Fed. Trade Comm’n, Analysis of Agreement Containing Consent Order to Aid Public Comment, *In re Prudential Sec., Inc. et al.*, Matter No. 211 0026 at 1, 5–7 (December 28, 2022).

²¹³ *Id.* at 1.

²¹⁴ *Id.*

²¹⁵ *Id.* at 1–2; Glass Container Analysis to Aid Public Comment, *supra* note 209 at 1.

²¹⁶ Fed. Trade Comm’n, Press Release, *Rent-to-Own Operators Settle Charges that They Restrained Competition through Reciprocal Purchase Agreements* (Feb. 21, 2020), <https://www.ftc.gov/news-events/news/press-releases/2020/02/rent-own-operators-settle-charges-they-restrained-competition-through-reciprocal-purchase-agreements>.

With respect to merger review, on August 11, 2015, the Commission approved a final order settling charges that Zimmer Holdings, Inc.’s acquisition of Biomet, Inc. would have eliminated competition between the companies in the markets for certain orthopedic medical products. Among other things, the order requires Zimmer to “remove any impediments or incentives” that may deter workers from accepting employment with the divested businesses, including non-compete clauses.²¹⁷

On November 10, 2021, the Commission approved a final order settling charges that 7-Eleven’s acquisition of Marathon Petroleum Corporation’s Speedway subsidiary violated federal antitrust laws. Among other things, the order prohibits 7-Eleven from enforcing any non-compete clauses against any franchisees or employees working at or doing business with the divested assets.²¹⁸

On January 10, 2022, the Commission approved a final order settling charges that dialysis service provider DaVita, Inc.’s acquisition of University of Utah Health’s dialysis clinics would reduce competition in vital outpatient dialysis services in the Provo, Utah market. As part of the order, DaVita was required to remove certain non-compete clauses and prohibited from enforcing or entering into non-compete clauses with certain parties.²¹⁹ And on August 9, 2022, the Commission issued a final consent order in

²¹⁷ Fed. Trade Comm’n, *In the Matter of Zimmer Holdings, Inc. et al.*, No. C-4534, Decision and Order (Aug. 11, 2015), <https://www.ftc.gov/system/files/documents/cases/150820zimmerdo.pdf>.

²¹⁸ Fed. Trade Comm’n, Press Release, *FTC Approves Final Order Requiring Divestitures of Hundreds of Retail Gas and Diesel Fuel Stations Owned by 7-Eleven, Inc.* (Nov. 10, 2021), <https://www.ftc.gov/news-events/news/press-releases/2021/11/ftc-approves-final-order-requiring-divestitures-hundreds-retail-gas-diesel-fuel-stations-owned-7>.

²¹⁹ Fed. Trade Comm’n, *In the Matter of Davita Inc. and Total Renal Care, Inc.*, No. C-4752, Decision and Order (Jan. 10, 2022) at 12–14, https://www.ftc.gov/system/files/documents/cases/211_0056_c4752_davita_utah_health_order.pdf.

which ARKO Corp. and its subsidiary GPM agreed to roll back a sweeping non-compete clause they imposed on a company to which they sold 60 gas stations.²²⁰

With respect to research, in September 2021, the Commission issued a study analyzing acquisitions by five large technology companies that were not reported to the Commission and the U.S. Department of Justice under the Hart-Scott-Rodino Act.²²¹ The study found 76.7% of transactions included non-compete clauses for founders and key employees of the acquired entities. The study also found that higher-value transactions were more likely to use non-compete clauses.²²² The study does not explain why the companies used non-compete clauses or analyze the effects of these particular non-compete clauses on competition.

The Commission seeks comment on its description, in this Part II.D, of the Commission's work on non-compete clauses prior to this NPRM.

III. Legal Authority

Section 5 of the FTC Act declares “unfair methods of competition” to be unlawful.²²³ Section 5 further directs the Commission “to prevent persons, partnerships, or corporations . . . from using unfair methods of competition in or affecting commerce.”²²⁴ Section 6(g) of the FTC Act authorizes the Commission to “make rules and regulations for the purpose of carrying out the provisions of” the FTC Act, including

²²⁰ Fed. Trade Comm'n, Press Release, *FTC Approves Final Order Restoring Competitive Markets for Gasoline and Diesel in Michigan and Ohio* (Aug. 9, 2022), <https://www.ftc.gov/news-events/news/press-releases/2022/08/ftc-approves-final-order-restoring-competitive-markets-gasoline-diesel-michigan-ohio>.

²²¹ Fed. Trade Comm'n, *Non-HSR Reported Acquisitions by Select Technology Platforms, 2010–2019: An FTC Study* (September 2021) at 1.

²²² *Id.* at 21–22. The table states that the figure is 77.3%. The reason for this discrepancy is not clear.

²²³ 15 U.S.C. 45(a)(1).

²²⁴ 15 U.S.C. 45(a)(2).

the Act’s prohibition of unfair methods of competition.²²⁵ Taken together, Sections 5 and 6(g) provide the Commission with the authority to issue regulations declaring practices to be unfair methods of competition.²²⁶

Courts have made clear Section 5’s prohibition of unfair methods of competition encompasses all practices that violate either the Sherman or Clayton Acts.²²⁷ However, courts have long held the scope of Section 5 is not confined to the conduct that is prohibited under the Sherman Act, Clayton Act, or common law.²²⁸ Section 5 reaches incipient violations of the antitrust laws—conduct that, if left unrestrained, would grow into an antitrust violation in the foreseeable future.²²⁹ Additionally, Section 5 reaches conduct that, while not prohibited by the Sherman or Clayton Acts, violates the spirit or policies underlying those statutes.²³⁰

²²⁵ 15 U.S.C. 46(g).

²²⁶ *Nat’l Petroleum Refiners Ass’n v. Fed. Trade Comm’n*, 482 F.2d 672, 697–98 (D.C. Cir. 1973).

²²⁷ *See, e.g., Fed. Trade Comm’n v. Cement Inst.*, 333 U.S. 683, 693 (1948) (holding practices that violate the Sherman Act are unfair methods of competition); *Fashion Originators’ Guild of Am. v. Fed. Trade Comm’n*, 312 U.S. 457, 464 (1941) (holding practices that violate the Clayton Act are unfair methods of competition).

²²⁸ *See, e.g., Fed. Trade Comm’n v. Motion Picture Advert. Serv. Co.*, 344 U.S. 392, 394–95 (1953) (“The ‘Unfair methods of competition’, which are condemned by [Section] 5(a) of the [FTC] Act, are not confined to those that were illegal at common law or that were condemned by the Sherman Act. Congress advisedly left the concept flexible to be defined with particularity by the myriad of cases from the field of business.”) (internal citations omitted).

²²⁹ *See, e.g., Cement Inst.*, 333 U.S. at 708 (“A major purpose of [the FTC] Act was to enable the Commission to restrain practices as ‘unfair’ which, although not yet having grown into Sherman Act dimensions would most likely do so if left unrestrained.”); *Fashion Originators’ Guild*, 312 U.S. at 466; *Triangle Conduit & Cable Co. v. Fed. Trade Comm’n*, 168 F.2d 175, 176 (7th Cir. 1948).

²³⁰ *See, e.g., Fashion Originators’ Guild*, 312 U.S. at 463 (stating that “[i]f the purpose and practice of the combination of garment manufacturers and their affiliates runs counter to the public policy declared in the Sherman and Clayton Acts, the Federal Trade Commission has the power to suppress it as an unfair method of competition”); *E.I. du Pont de Nemours & Co. v. Fed. Trade Comm’n (Ethyl)*, 729 F.2d 128, 136–37 (2d Cir. 1984) (finding that the Commission may bar “conduct which, although not a violation of the letter of the antitrust laws, is close to a violation or is contrary to their spirit”). On November 10, 2022, the Commission issued a policy statement describing the key principles of general applicability concerning whether conduct is an unfair method of competition under Section 5. Fed. Trade Comm’n, *Policy Statement Regarding the Scope of Unfair Methods of Competition Under Section 5 of the Federal Trade Commission Act* (Nov. 10, 2022).

IV. The Commission’s Preliminary Determination that Non-Compete Clauses Are an Unfair Method of Competition

The Commission preliminarily determines 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 the worker is subject to an enforceable non-compete clause.²³¹ This preliminary determination is the basis for this proposed rule, which would provide that each of these practices is an unfair method of competition under Section 5.²³² This Part IV sets forth a series of preliminary findings that provide the basis for this preliminary determination. The Commission’s preliminary determination and each of these preliminary findings are subject to further consideration in light of the comments received and the Commission’s additional analysis. The Commission seeks comment on all aspects of this Part IV.²³³

A. Non-Compete Clauses Are an Unfair Method of Competition Under Section 5

1. Non-Compete Clauses Are Unfair

Courts have held conduct is an “unfair method of competition” under Section 5 where the conduct is facially unfair. In *Atlantic Refining Co. v. FTC* and *FTC v. Texaco, Inc.*, the Court held the Commission established an unfair method of competition where an oil company used its economic power over its gas stations to coerce them into buying certain tires, batteries, or accessories only from firms that paid the oil company a

²³¹ For ease of reference, this Part IV employs the term “use of non-compete clauses” as a shorthand to refer to this conduct.

²³² See proposed § 910.2(a).

²³³ The Commission intends for this Part IV to satisfy the requirements in Section 22 of the FTC Act that, in an NPRM, the Commission issue a preliminary regulatory analysis that contains “a concise statement of the need for, and the objectives of, the proposed rule.” 15 U.S.C. 57b-3.

commission.²³⁴ In *Texaco*, the Court held the conduct was an unfair method of competition even though Texaco’s conduct was not overtly coercive, reasoning that Texaco’s conduct was “inherently coercive” because its “dominant economic power was used in a manner which tended to foreclose competition.”²³⁵ In *FTC v. R.F. Keppel & Bro.*, the Court held the Commission established an unfair method of competition where a manufacturer exploited the inability of children to protect themselves in the marketplace by marketing inferior goods to them through use of a gambling scheme.²³⁶ In *E.I. du Pont de Nemours & Co. v. FTC (Ethyl)*, the U.S. Court of Appeals for the Second Circuit reaffirmed that coercive conduct is quintessentially covered by Section 5’s prohibition of unfair methods of competition.²³⁷

The Court has also held that, for coercive conduct to constitute unfair method of competition, it must burden commerce. In *Atlantic Refining*, the Court determined “a full-scale economic analysis of competitive effect” was not required; due to the nature of the conduct at issue, the Commission merely needed to show the conduct burdened “a not insubstantial portion of commerce.”²³⁸

In the cases described above, courts condemned conduct under Section 5 based on the facial unfairness of the conduct. In other cases, however, courts have condemned

²³⁴ *Atl. Refin. Co.*, 381 U.S. at 369–70; *Texaco, Inc.*, 393 U.S. at 228–29.

²³⁵ 393 U.S. 223 at 228–29 (1968). *See also Shell Oil Co. v. Fed. Trade Comm’n*, 360 F.2d 470, 487 (5th Cir. 1966) (“A man operating a gas station is bound to be overawed by the great corporation that is his supplier, his banker, and his landlord.”).

²³⁶ 291 U.S. 304, 313 (1934).

²³⁷ 729 F.2d 128, 140 (2d Cir. 1984) (“In short, in the absence of proof of a violation of the antitrust laws or evidence of collusive, coercive, predatory, or exclusionary conduct, business practices are not “unfair” in violation of § 5 unless those practices either have an anticompetitive purpose or cannot be supported by an independent legitimate reason.”).

²³⁸ 381 U.S. at 370–71. *See also Texaco, Inc.*, 393 U.S. at 230 (finding that the practice unfairly burdened competition for a not insignificant volume of commerce); *R.F. Keppel & Bro.*, 291 U.S. at 309 (“A practice so widespread and so far reaching in its consequences is of public concern if in other respects within the purview of the statute.”).

restrictive or exclusionary conduct under Section 5 based not on the facial unfairness of the conduct, but on the impact of the conduct on competition. For example, in *FTC v. Motion Picture Advertising Service Co.*, the Court held an exclusive dealing arrangement violated Section 5 where there was “substantial evidence” the contracts “unreasonably restrain competition.”²³⁹ Similarly, in *L.G. Balfour Co. v. FTC*, the U.S. Court of Appeals for the Seventh Circuit held a firm’s exclusive dealing contracts violated Section 5 where such contracts were “anti-competitive.”²⁴⁰ As the U.S. Court of Appeals for the Sixth Circuit stated in *Hastings Manufacturing Co. v. FTC*, the Section 5 jurisprudence has established that “acts [that are] not in themselves illegal or criminal, or even immoral, may, when repeated and continued and their impact upon commerce is fully revealed, constitute an unfair method of competition within the scope of the Commission’s authority to regulate and forbid.”²⁴¹

For the reasons described below, the Commission preliminarily finds the use by employers of non-compete clauses is an “unfair” method of competition under Section 5. The Commission’s preliminary findings differ based on whether the worker is a senior executive. For workers who are not senior executives, the Commission preliminarily finds the use by employers of non-compete clauses is “unfair” under Section 5 in three independent ways. First, non-compete clauses are restrictive conduct that negatively affects competitive conditions. Second, non-compete clauses are exploitative and coercive at the time of contracting while burdening a not insignificant volume of commerce. Third, non-compete clauses are exploitative and coercive at the time of the

²³⁹ 344 U.S. 392, 395–96 (1953).

²⁴⁰ 442 F.2d 1, 14 (7th Cir. 1971).

²⁴¹ 153 F.2d 253, 257 (6th Cir. 1946).

worker’s potential departure from the employer while burdening a not insignificant volume of commerce.

For workers who are senior executives, the Commission preliminarily finds the use by employers of non-compete clauses is “unfair” under Section 5 because such non-compete clauses are restrictive conduct that negatively affects competitive conditions. As described below in Part IV.A.1.a.ii, the Commission preliminarily concludes non-compete clauses for senior executives may harm competition in product markets in unique ways. The second and third preliminary findings described above—that non-compete clauses are exploitative and coercive at the time of contracting and at the time of a worker’s potential departure—do not apply to workers who are senior executives.²⁴²

The Commission seeks comment on whether this different unfairness analysis should apply to other highly paid or highly skilled workers who are not senior executives. Furthermore, in Part VI.C below, the Commission seeks comment on how this category of workers—whether “senior executives” or a broader category of highly paid or highly skilled workers—should be defined, and whether different regulatory standards should apply to this category of workers.

The Commission seeks comment on its preliminary finding that non-compete clauses are an “unfair” method of competition under Section 5.

a. Non-Compete Clauses are Restrictive Conduct that Negatively Affects

Competitive Conditions

²⁴² As described below in Part VII.B.1.a.iv, the Commission estimates that, when non-compete clauses are more enforceable, CEO earnings are reduced. This may result from the negative effects on competitive conditions that non-compete clauses have on labor markets (discussed in greater detail below in Part IV.A.1.a.i) rather than from exploitation or coercion.

First, the Commission preliminarily finds non-compete clauses are an “unfair” method of competition under Section 5 because they are restrictive conduct that negatively affects competitive conditions.

As noted above, courts have condemned restrictive or exclusionary conduct under Section 5 based not on the facial unfairness of the conduct, but on the impact of the conduct on competition.²⁴³ Non-compete clauses are restrictive conduct. By their express terms, non-compete clauses restrict a worker’s ability to work for a competitor of the employer—for example, by accepting a job with a competitor or starting a business that would compete against the employer. Non-compete clauses also restrict rivals from competing against the employer to attract their workers. Because non-compete clauses facially restrain competition in the labor market, courts have long held they are restraints of trade and proper subjects for scrutiny under the antitrust laws.²⁴⁴ Furthermore, as described in detail in this NPRM, there is considerable empirical evidence showing non-compete clauses negatively affect competition in labor markets and product and service markets.²⁴⁵ This evidence is summarized below.

i. Non-Compete Clauses Negatively Affect Competitive Conditions in Labor Markets

²⁴³ See *supra* Part IV.A.1.

²⁴⁴ See, e.g., *Am. Tobacco Co.*, 221 U.S. at 181–83 (holding several tobacco companies violated Sections 1 and 2 of the Sherman Act due to the collective effect of six of the companies’ practices, one of which was the “constantly recurring” use of non-compete clauses); *Newburger, Loeb & Co., Inc.*, 563 F.2d at 1082 (“Although such issues have not often been raised in the federal courts, employee agreements not to compete are proper subjects for scrutiny under section 1 of the Sherman Act. When a company interferes with free competition for one of its former employee’s services, the market’s ability to achieve the most economically efficient allocation of labor is impaired. Moreover, employee-noncompetition clauses can tie up industry expertise and experience and thereby forestall new entry.”)

²⁴⁵ See *supra* Part II.B.

As described in greater detail above in Part II.B.1, non-compete clauses negatively affect competitive conditions in labor markets by obstructing the sorting of workers and employers into the strongest possible matches. Labor markets function by matching workers and employers. In a well-functioning labor market, a worker who is seeking a better job—more pay, better working conditions, more enjoyable work, or whatever the worker may be seeking—can enter the labor market by looking for work. Employers who have positions available compete for the worker’s services. The worker’s current employer may also compete with these prospective employers by seeking to retain the worker—for example, by offering to raise the worker’s pay or promote the worker. Ultimately, the worker chooses the job that best meets their objectives. In general, the more jobs available—*i.e.*, the more options the worker has—the greater the possibility the worker will find a strong match.

Just as employers compete for workers in a well-functioning labor market, workers compete for jobs. In general, the more workers who are available—*i.e.*, the more options the employer has—the stronger the match the employer will find. Through these processes—employers competing for workers, workers competing for jobs, and employers and workers matching with one another—competition in the labor market leads to higher earnings for workers, greater productivity for employers, and better economic conditions.

In a perfectly competitive labor market, if a job that a worker would prefer more—for example, because it has higher pay or is in a better location—were to become available, the worker could switch to it quickly and easily. However, this perfectly competitive labor market exists only in theory. In practice, labor markets substantially

deviate from perfect competition. Non-compete clauses, in particular, impair competition in labor markets by restricting a worker's ability to change jobs. If a worker is bound by a non-compete clause, and the worker wants a better job, the non-compete clause will prevent the worker from accepting a new job within the scope of the non-compete clause. These will often be the most natural alternative employment options for a worker: jobs in the same geographic area and in the worker's field of expertise. The result is less competition among employers for the worker's services. Since the worker is prevented from taking these jobs, the worker may decide not to enter the labor market at all, or the worker may enter the labor market but take a job outside of their field of expertise in which they are less productive.

Non-compete clauses affect competition in labor markets through their use in the aggregate. The effect of an individual worker's non-compete clause on competition in a particular labor market may be marginal or may be impossible to discern statistically. However, the use of a large number of non-compete clauses across a labor market demonstrably affects the opportunities of all workers in that market. By making it more difficult for many workers in a labor market to switch to new jobs, non-compete clauses inhibit optimal matches from being made between employers and workers across the labor force. As a result, where non-compete clauses are prevalent in a market, workers are more likely to remain in jobs that are less optimal with respect to the worker's ability to maximize their productive capacity. This materially reduces wages for workers—not only for workers who are subject to non-compete clauses, but other workers in a labor market as well, since jobs that would otherwise be better matches for an unconstrained worker are filled by workers subject to non-compete clauses.

The Section 5 analysis as to whether conduct negatively affects competitive conditions does not require a showing that the conduct caused actual harm.²⁴⁶ However, whether conduct causes actual harm can be relevant to whether it is an unfair method of competition.²⁴⁷ There is significant empirical evidence that non-compete clauses cause actual harm to competition in labor markets, and that these harms are substantial.

As described above in Part II.B.1.a, the Commission estimates at least one in five American workers—or approximately 30 million workers—is bound by a non-compete clause. The proliferation of non-compete clauses is restraining competition in labor markets to such a degree that it is materially impacting workers’ earnings—both across the labor force in general, and also specifically for workers who are not subject to non-compete clauses. The available evidence indicates increased enforceability of non-compete clauses substantially reduces workers’ earnings, on average, across the labor market generally or for specific types of workers.²⁴⁸ The Commission estimates the proposed rule, which would prohibit employers from using non-compete clauses, would increase workers’ total earnings by \$250 to \$296 billion per year.²⁴⁹

In addition to the evidence showing non-compete clauses reduce earnings for workers across the labor force, there is also evidence non-compete clauses reduce

²⁴⁶ See *Fed. Trade Comm’n v. Sperry & Hutchinson Co.*, 405 U.S. 233, 244 (1972) (explaining that “unfair competitive practices [are] not limited to those likely to have anticompetitive consequences after the manner of the antitrust laws”); *In re Coca-Cola Co.*, 117 F.T.C. 795, 915 (FTC 1994) (rejecting argument that Section 5 violation requires showing “anticompetitive effects”).

²⁴⁷ See *Ethyl*, 729 F.2d at 138 (evidence of actual harm can be “a relevant factor in determining whether the challenged conduct is unfair”).

²⁴⁸ See *supra* Part II.B.1. While there is evidence that increased enforceability of non-compete clauses increases the rate of earnings growth for physicians, Lavetti, Simon, & White, *supra* note 53 at 1051, the Commission estimates that the proposed rule may increase physicians’ earnings, although the study does not allow for a precise calculation. See *infra* Part VII.B.1.a.ii.

²⁴⁹ See *infra* Part VII.B.1 (describing the Commission’s assessment of the benefits of the proposed rule).

earnings specifically for workers who are *not* subject to non-compete clauses.²⁵⁰ One study finds when the use of non-compete clauses by employers increases, that drives down wages for workers who do not have non-compete clauses but who work in the same state and industry. This study also finds this effect is stronger where non-compete clauses are more enforceable. This study shows the reduction in earnings (and also reduced labor mobility) is due to a reduction in the rate of the arrival of job offers.²⁵¹ Another study finds similarly that changes in non-compete clause enforceability in one state have negative impacts on workers' earnings in bordering states and that the effects are nearly as large as the effects in the state in which enforceability changed (though the effect tapers off as the distance to the bordering state increases).²⁵² The authors conclude that, since the workers across the border are not directly affected by the law change—because contracts that they have signed do not become more or less enforceable—this effect must be due to changes in the local labor market.²⁵³

The Commission preliminarily concludes non-compete clauses negatively affect competitive conditions in labor markets regardless of the worker's income or job function. Whether a worker is a senior executive or a security guard, non-compete clauses block the worker from switching to a job in which they would be better paid and more productive—restricting that worker's opportunities as well as the opportunities of other workers in the relevant labor market. The available data do not allow the Commission to estimate earnings effects for every occupation. However, the evidentiary

²⁵⁰ See *supra* Part II.B.1.c.

²⁵¹ Starr, Frake, & Agarwal, *supra* note 76 at 4.

²⁵² Johnson, Lavetti, & Lipsitz, *supra* note 63 at 51.

²⁵³ *Id.* at 30.

record indicates non-compete clauses depress wages for a wide range of subgroups of workers across the spectrum of income and job function. The Commission therefore estimates the proposed rule would increase earnings for workers in all of the subgroups of the labor force for which sufficient data is available.²⁵⁴

The Commission seeks comment on its preliminary finding that non-compete clauses negatively affect competitive conditions in labor markets.

ii. Non-Compete Clauses Negatively Affect Competitive Conditions in Markets for Products and Services

The adverse effects of non-compete clauses on product and service markets largely result from reduced labor mobility. Several studies show the use of non-compete clauses by employers reduces labor mobility. All of these studies have found decreased rates of labor mobility, as measured by job separations, hiring rates, job-to-job mobility, implicit mobility defined by job tenure, and within- and between-industry mobility.²⁵⁵ The Commission does not view reduced labor mobility from non-compete clauses—in and of itself—as evidence that non-compete clauses negatively affect competition in product and service markets. Instead, reduced labor mobility is best understood as the primary driver of the effects in product and service markets the Commission is concerned about.

Reduced labor mobility from non-compete clauses negatively affects competitive conditions in product and service markets in several respects. First, there is evidence non-compete clauses increase consumer prices and concentration in the health care sector.

²⁵⁴ See *infra* Part VII.B.1.a.

²⁵⁵ See *supra* Part II.B.2.

There is also evidence non-compete clauses increase industrial concentration more broadly. Non-compete clauses may have these effects by inhibiting entrepreneurial ventures (which could otherwise enhance competition in goods and service markets) or by foreclosing competitors' access to talented workers.²⁵⁶

Second, non-compete clauses foreclose the ability of competitors to access talent by effectively forcing future employers to buy out workers from their non-compete clauses if they want to hire them. Firms must either make inefficiently high payments to buy workers out of non-compete clauses with a former employer, which leads to deadweight economic loss, or forego the payment—and, consequently, the access to the talent the firm seeks. Whatever choice a firm makes, its economic outcomes in the market are harmed, relative to a scenario in which no workers are bound by non-compete clauses. There is evidence of this mechanism in the market for CEOs.²⁵⁷

Third, the weight of the evidence indicates non-compete clauses have a negative impact on new business formation. New business formation increases competition first by bringing new ideas to market, and second, by forcing incumbent firms to respond to new firms' ideas instead of stagnating. Non-compete clauses restrain new business formation by preventing workers subject to non-compete clauses from starting their own businesses. In addition, firms are more willing to enter markets in which they know there are potential sources of skilled and experienced labor, unhampered by non-compete clauses.²⁵⁸

²⁵⁶ See *supra* Part II.B.2.a.

²⁵⁷ See *supra* Part II.B.2.b.

²⁵⁸ See *supra* Part II.B.2.c.

Fourth, the weight of the evidence indicates non-compete clauses decrease innovation. Innovation may directly improve economic outcomes by increasing product quality or decreasing prices, or may promote competition because successful new products and services force competing firms to improve their own products and services. Non-compete clauses affect innovation by reducing the movement of workers between firms, which decreases knowledge flow between firms. Non-compete clauses also prevent workers from starting businesses in which they can pursue innovative new ideas.²⁵⁹

As noted above in Part II.B.2.e, there is also evidence non-compete clauses increase employee training and other forms of investment. The Commission considers this evidence below in Part IV.B as part of its analysis of the justifications for non-compete clauses.

The Commission believes non-compete clauses for senior executives may harm competition in product markets in unique ways, to the extent that senior executives may be likely to start competing businesses, be hired by potential entrants or competitors, or lead the development of innovative products and services. Non-compete clauses for senior executives may also block potential entrants, or raise their costs, to a high degree, because such workers are likely to be in high demand by potential entrants. As a result, prohibiting non-compete clauses for senior executives may have relatively greater benefits for consumers than prohibiting non-compete clauses for other workers. The Commission seeks comment on this analysis as well as whether this reasoning may apply to highly paid and highly skilled workers who are not senior executives.

²⁵⁹ See *supra* Part II.B.2.d.

The Commission seeks comment on its preliminary finding that non-compete clauses negatively affect competitive conditions in markets for products and services.

b. Non-Compete Clauses Are Exploitative and Coercive at the Time of Contracting

The Commission preliminarily finds non-compete clauses for workers other than senior executives are exploitative and coercive because they take advantage of unequal bargaining power between employers and workers at the time the employer and worker enter into the non-compete clause.

As noted above, courts have held conduct that is exploitative and coercive can violate Section 5 where it burdens a not insignificant volume of commerce.²⁶⁰ Courts have long recognized bargaining power between employers and workers is unequal and, as a result, workers are vulnerable to exploitation and coercion through the use of non-compete clauses at the time of contracting. Courts have expressed this concern since at least the early eighteenth century. In the foundational English case *Mitchel v. Reynolds*, the court cited “the great abuses these voluntary restraints are liable to . . . from masters, who are apt to give their apprentices much vexation” by using “many indirect practices to procure such bonds from them, lest they should prejudice them in their custom, when they come to set up for themselves.”²⁶¹ As another court stated, more recently:

The average, individual employee has little but his labor to sell or to use to make a living. He is often in urgent need of selling it and in no position to object to boiler plate restrictive covenants placed before him to sign. To him, the right to

²⁶⁰ See *supra* Part IV.A.1.

²⁶¹ 1 P. Wms. at 190.

work and support his family is the most important right he possesses. His individual bargaining power is seldom equal to that of his employer. . . . Under pressure of need and with little opportunity for choice, he is more likely than the seller to make a rash, improvident promise that, for the sake of present gain, may tend to impair his power to earn a living, impoverish him, render him a public charge or deprive the community of his skill and training.²⁶²

Indeed, courts have cited the imbalance of bargaining power between workers and employers as a central reason for imposing stricter scrutiny on non-compete clauses between employers and workers than on non-compete clauses between businesses or between the seller and buyer of a business.²⁶³

The imbalance of bargaining power between employers and workers results from several factors. Many of these factors relate to the nature of the employer-worker relationship in the United States generally. Most workers depend on income from their jobs to get by—to pay their rent or mortgage, pay their bills, and keep food on the table. For these workers, particularly the many workers who live paycheck to paycheck, loss of a job or a job opportunity can severely damage their finances.²⁶⁴ For these reasons, the

²⁶² *Arthur Murray Dance Studios of Cleveland v. Witter*, 105 N.E.2d 685, 703–04 (Ohio Ct. Com. Pl. 1952). *See also* Restatement (Second) of Contracts (1981) sec. 188 cmt. g (“Postemployment restraints are scrutinized with particular care because they are often the product of unequal bargaining power and because the employee is likely to give scant attention to the hardship he may later suffer through loss of his livelihood.”).

²⁶³ *See, e.g., Alexander & Alexander, Inc. v. Danahy*, 488 N.E.2d 22, 29 (Mass. App. Ct. 1986); *Diepholz v. Rutledge*, 659 N.E. 989, 991 (Ill. Ct. App. 1995); *Palmetto Mortuary Transp., Inc. v. Knight Sys., Inc.*, 818 S.E.2d 724, 731 (S.C. 2018).

²⁶⁴ *See, e.g.,* Jennie E. Brand, *The Far-Reaching Impact of Job Loss and Unemployment*, 41 Ann. Rev. of Socio. 359 (2015); CareerBuilder, *Living Paycheck to Paycheck is a Way of Life for Majority of U.S. Workers, According to New CareerBuilder Survey* (Aug. 24, 2017), <https://press.careerbuilder.com/2017-08-24-Living-Paycheck-to-Paycheck-is-a-Way-of-Life-for-Majority-of-U-S-Workers-According-to-New-CareerBuilder-Survey> (reporting that 78% of American workers live paycheck to paycheck); Jeff Ostrowski, Bankrate, *Survey: Fewer than 4 in 10 Americans could pay a surprise \$1,000 bill from savings* (Jan. 11, 2021), <https://www.bankrate.com/banking/savings/financial-security-january-2021/>.

loss of a job or an employment opportunity is far more likely to have serious financial consequences for a worker than the loss of a worker or a job candidate would have for most employers. In addition, employers generally have considerable labor market power, due to factors such as concentration and the difficulty of searching for a job.²⁶⁵ The considerable labor market power of employers has significantly diminished the bargaining power of U.S. workers.²⁶⁶

Several additional factors contribute to the imbalance of bargaining power between employers and workers generally. These include the decline in union membership, which forces more workers to negotiate with their employers individually;²⁶⁷ increased reliance by employers on various forms of outsourcing, which allows employers to fill persistent vacancies without having to raise wages or improve conditions for incumbent workers;²⁶⁸ and the proliferation of no-poaching agreements, which limit the mobility of workers and, as a result, their bargaining power.²⁶⁹

While the employer-worker relationship is defined by an imbalance of bargaining power generally, the imbalance of bargaining power is particularly acute in the context of negotiating employment terms such as non-compete clauses, for several reasons. First, as courts have long recognized, employers are repeat players who are likely to have greater experience and skill at bargaining, in the context of negotiating employment terms, than

²⁶⁵ Treasury Labor Market Competition Report, *supra* note 41 at i–ii.

²⁶⁶ *Id.* at ii (“As this report highlights, a careful review of the credible academic studies places the decrease in wages at roughly 20 percent relative to the level in a fully competitive market”).

²⁶⁷ See, e.g., Alan Krueger, *Luncheon Address: Reflections on Dwindling Worker Bargaining Power and Monetary Policy* at 272 (Aug. 24, 2018), https://www.kansascityfed.org/Jackson%20Hole/documents/6984/Lunch_JH2018.pdf.

²⁶⁸ *Id.*

²⁶⁹ *Id.* at 273.

individual workers.²⁷⁰ Second, and relatedly, workers are not likely to seek the assistance of counsel in reviewing employment terms,²⁷¹ while employers are more likely to seek the assistance of counsel in drafting them.

Third, research indicates consumers exhibit cognitive biases in the way they consider contractual terms,²⁷² and the same may be true of workers. Consumers rarely read standard-form contracts.²⁷³ Consumers also tend to focus their attention on a few salient terms of the transaction, such as price and quantity, and tend to disregard other terms, particularly terms that are relatively obscure.²⁷⁴ Consumers are particularly likely to disregard contingent terms—terms concerning scenarios that may or may not come to pass—or to be unable to assess what the impact of those terms may be.²⁷⁵ Consumers also tend to disregard onerous terms or terms that involve difficult trade-offs, such as giving up legal rights or future opportunities.²⁷⁶ Workers likely display similar cognitive biases in the way they consider employment terms. These reasons explain why the imbalance of bargaining power between workers and employers is particularly high in the context of negotiating employment terms such as non-compete clauses.

²⁷⁰ See, e.g., *Samuel Stores, Inc. v. Abrams*, 108 A. 541, 543 (Conn. 1919).

²⁷¹ In one survey, only 7.9% of workers with non-compete clauses reported consulting a lawyer in connection with the non-compete clause. Starr, Prescott, & Bishara, *supra* note 42, at 72.

²⁷² See, e.g., Arnow-Richman (2006), *supra* note 56 at 981; Russell Korobkin, *Bounded Rationality, Standard Form Contracts, and Unconscionability*, 70 U. Chi. L. Rev. 1203, 1206 (2003); Robert Hillman & Jeffrey Rachlinski, *Standard-Form Contracting in the Electronic Age*, 77 N.Y.U. L. Rev. 429, 450–54 (2002).

²⁷³ Korobkin, *supra* note 272 at 1206.

²⁷⁴ Arnow-Richman (2006), *supra* note 56 at 981; Hillman & Rachlinski, *supra* note 272 at 452.

²⁷⁵ See, e.g., Estlund, *supra* note 144 at 413 (2006). See also Fed. Trade Comm'n, *Credit Practices Rule*, 49 FR 7740, 7744 (Mar. 1, 1984) (noting that consumers tend to disregard contingent provisions and concentrate their search on factors such as interest rates and payment terms).

²⁷⁶ Arnow-Richman (2006), *supra* note 56 at 981; Korobkin, *supra* note 272 at 1203–31.

There is considerable evidence employers are exploiting this imbalance of bargaining power through the use of non-compete clauses. Non-compete clauses are typically standard-form contracts,²⁷⁷ which, as noted above, workers are not likely to read. The evidence shows workers rarely bargain over non-compete clauses²⁷⁸ and rarely seek the assistance of counsel in reviewing non-compete clauses.²⁷⁹ Furthermore, research indicates that, in states where non-compete clauses are unenforceable, workers are covered by non-compete clauses at roughly the same rate as workers in other states,²⁸⁰ suggesting that employers may believe workers are unaware of their legal rights, or that employers may be seeking to take advantage of workers' lack of knowledge of their legal rights. In addition, there is evidence employers often provide workers with non-compete clauses after they have accepted the job offer—in some cases, on or after their first day of work—when the worker's negotiating power is at its weakest, since the worker may have turned down other job offers or left their previous job.²⁸¹

Because there is a considerable imbalance of bargaining power between workers and employers in the context of negotiating employment terms, and because employers take advantage of this imbalance of bargaining power through the use of non-compete clauses, the Commission preliminarily finds non-compete clauses are exploitative and coercive at the time of contracting.

As noted above, for coercive conduct to constitute unfair method of competition, it must also burden a not insignificant volume of commerce. The Commission

²⁷⁷ Starr, Prescott, & Bishara, *supra* note 42 at 72 (“Taken together, the evidence in this section indicates that employers present (or employees receive) noncompete proposals as take-it-or-leave-it propositions.”).

²⁷⁸ *Id.*

²⁷⁹ *Id.*

²⁸⁰ *Id.* at 81.

²⁸¹ Marx (2011), *supra* note 55 at 706.

preliminarily finds non-compete clauses burden a not insignificant volume of commerce due to their negative effects on competitive conditions in labor markets and product and service markets, which are described above.²⁸²

This preliminary finding does not apply to workers who are senior executives. Non-compete clauses for senior executives are unlikely to be exploitative or coercive at the time of contracting, because senior executives are likely to negotiate the terms of their employment and may often do so with the assistance of counsel. The Commission seeks comment on whether there are other categories of highly paid or highly skilled workers (*i.e.*, other than senior executives) to whom this preliminary finding should not apply.

The Commission seeks comment on all aspects of its preliminary finding that non-compete clauses are exploitative and coercive at the time of contracting.

c. Non-Compete Clauses Are Exploitative and Coercive at the Time of the Worker's Potential Departure From the Employer

The Commission preliminarily finds non-compete clauses for workers other than senior executives are exploitative and coercive at the time of the worker's potential departure from the employer, because they force a worker to either stay in a job they want to leave or choose an alternative that likely impacts their livelihood.

For most workers who want to leave their jobs, the most natural employment options will be work in the same field and in the same geographic area. However, where a worker is bound by a non-compete clause, the worker's employment options are significantly limited. A worker who is subject to a non-compete clause, and who wants to leave their job, faces an undesirable choice that will likely affect their livelihood: either

²⁸² See *supra* Part IV.A.1.a.i-ii.

move out of the area; leave the workforce for a period of time; leave their field for period of time; pay the employer a sum of money to waive the non-compete clause; or violate the non-compete clause and risk a lawsuit from the employer. By forcing a worker who wants to leave their job to either stay in their job or take an action that will likely negatively affect their livelihood, non-compete clauses coerce workers into remaining in their current jobs. Courts have long expressed concern about this coercive effect of non-compete clauses—that non-compete clauses may threaten a worker’s livelihood if they leave their job.²⁸³

Workers have an inalienable right to quit their jobs.²⁸⁴ The Supreme Court has described this “right to change employers” as a critical “defense against oppressive hours, pay, working conditions, or treatment.”²⁸⁵ Strictly speaking, non-compete clauses do not prevent workers from quitting their jobs. However, non-compete clauses “burden the ability to quit, and with it the ability to demand better wages and working conditions and to resist oppressive conditions in the current job.”²⁸⁶ Non-compete clauses burden the ability to quit by forcing workers to either remain in their current job or, as described above, take an action—such as leaving the labor force for a period of time or taking a job in a different field—that would likely affect their livelihood. For this reason, the Commission finds non-compete clauses are exploitative and coercive at the time of the worker’s potential departure.

²⁸³ See, e.g., *Mitchel*, 1 P. Wms. at 190 (citing “the mischief which may arise from [non-compete clauses] . . . to the party, by the loss of his livelihood”).

²⁸⁴ *Bailey v. Alabama*, 219 U.S. 219, 242 (1911).

²⁸⁵ *Pollock v. Williams*, 322 U.S. 4, 17–18 (1944).

²⁸⁶ See Estlund, *supra* note 144 at 407.

As noted above, for coercive conduct to constitute unfair method of competition, it must also burden a not insignificant volume of commerce. The Commission preliminarily finds non-compete clauses burden a not insignificant volume of commerce due to their negative effects on competitive conditions in labor markets and product and service markets, which are described above.²⁸⁷

This preliminary finding does not apply to workers who are senior executives. Non-compete clauses for senior executives are unlikely to be exploitative or coercive at the time of the executive's departure. Because many senior executives negotiate their non-compete clauses with the assistance of expert counsel, they are likely to have bargained for a higher wage or more generous severance package in exchange for agreeing to the non-compete clause.²⁸⁸ The Commission seeks comment on whether there are other categories of highly paid or highly skilled workers (*i.e.*, other than senior executives) to whom this preliminary finding should not apply.

The Commission seeks comment on all aspects of its preliminary finding that non-compete clauses are exploitative and coercive at the time of the worker's potential departure from the employer.

2. Non-Compete Clauses Are a Method of Competition

For conduct to be an "unfair method of competition" under Section 5, it must be both "unfair" and a "method of competition." In *Ethyl*, the court distinguished between a "condition" of a marketplace, such as an oligopolistic market structure, and a "method"

²⁸⁷ See *supra* Part IV.A.1.a.i–ii.

²⁸⁸ See, e.g., Stewart J. Schwab & Randall S. Thomas, *An Empirical Analysis of CEO Employment Contracts: What Do Top Executives Bargain For?*, 63 Wash. & Lee L. Rev. 231, 256–57 (2006) (noting that 84% of CEO employment contracts that included both a non-compete clause and a severance payment have a severance payment that is equal to or greater than the length of the non-competition period).

of competition, which it described as “specific conduct which promotes” an anticompetitive result.²⁸⁹ When an employer uses a non-compete clause, it undertakes conduct in a marketplace. This conduct implicates competition; indeed, it has demonstrable effects on competition in both labor markets and markets for products and services.²⁹⁰ For these reasons, the Commission preliminarily finds non-compete clauses are a method of competition under Section 5. The Commission seeks comment on this preliminary finding.

B. The Justifications for Non-Compete Clauses Do Not Alter the Commission’s Preliminary Determination

For the reasons described above in Part IV.A, the Commission preliminarily determines non-compete clauses are an unfair method of competition under Section 5. In this Part IV.B, the Commission preliminarily finds the justifications for non-compete clauses do not alter the Commission’s preliminary determination that non-compete clauses are an unfair method of competition.

The circumstances under which a business justification can overcome a finding that conduct is an unfair method of competition are narrow. In *Fashion Originators’ Guild of America v. FTC*, the Court held that, in light of “the purpose and object of this combination, its potential power, its tendency to monopoly, [and] the coercion it could and did practice upon a rival method of competition,” the Commission did not err by refusing to hear evidence related to justifications, “for the reasonableness of the methods pursued by the combination to accomplish its unlawful object is no more material than

²⁸⁹ 729 F.2d at 139.

²⁹⁰ See *supra* Part II.B.

would be the reasonableness of the prices fixed by unlawful combination.”²⁹¹ In *Atlantic Refining*, the Court similarly held the Commission did not err by refusing to consider “evidence of economic justification for the program,” because, while the arrangements at issue “may well provide Atlantic with an economical method of assuring efficient product distribution among its dealers . . . the Commission was clearly justified in refusing the participants an opportunity to offset these evils by a showing of economic benefit to themselves.”²⁹²

Similarly, in *L.G. Balfour Co.*, the Commission challenged as an unfair method of competition the use of exclusive dealing contracts by a firm that manufactured and sold jewelry and other items bearing the insignia of fraternities and high schools. The firm argued the contracts were justified, in part because the fraternities and schools benefitted from uniformity in the design and workmanship of the items. The court reasoned “[w]hile it is relevant to consider the advantages of a trade practice on individual companies in the market, this cannot excuse an otherwise illegal business practice.”²⁹³ The court found the exclusive contracts were not justified, because the fraternities and schools had other means for accomplishing the goal of maintaining high quality for their jewelry and because the firm did not establish that its competitors could not satisfy its customers’ needs.²⁹⁴

In this Part IV.B, the Commission considers the commonly cited business justifications for non-compete clauses but preliminarily finds they do not alter the

²⁹¹ 312 U.S. at 467–68.

²⁹² 381 U.S. at 371.

²⁹³ 442 F.2d at 15, citing *Motion Picture Advert. Serv. Co.*, 344 U.S. 392.

²⁹⁴ *Id.* at 14–15.

Commission’s preliminary determination that non-compete clauses are an unfair method of competition, for two reasons. First, employers have alternatives to non-compete clauses that reasonably achieve the same purposes while burdening competition to a less significant degree. Second, the asserted benefits from these commonly cited justifications do not outweigh the considerable harm from non-compete clauses.

1. Commonly Cited Justifications for Non-Compete Clauses

The most cited justifications for non-compete clauses are that they increase employers’ incentive to make productive investments, including in worker training, client attraction, or in creating or sharing trade secrets with workers. According to these justifications, without non-compete clauses, employment relationships are subject to an investment hold-up problem. Investment hold-up occurs where an employer—faced with the possibility a worker may depart after receiving some sort of valuable investment—opts not to make that investment in the first place, thereby decreasing the firm’s productivity and overall social welfare. For example, according to these justifications, an employer may be more reticent to invest in trade secrets or other confidential information; to share this information with its workers; or to train its workers if it knows the worker may depart for or may establish a competing firm. Courts have cited these justifications when upholding non-compete clauses under state common law or antitrust law.²⁹⁵

As described above in Part II.B.2.e, there is evidence non-compete clauses increase worker training and capital investment (*e.g.*, investment in physical assets, such as machines). Non-compete clauses may increase an employer’s incentive to train their

²⁹⁵ See, *e.g.*, *U.S. v. Addyston Pipe & Steel Co.*, 85 F. 271, 281 (6th Cir. 1898); *Polk Bros., Inc. v. Forest City Enters.*, 776 F.2d 185, 189 (7th Cir. 1985).

workers or invest in capital equipment because workers bound by non-compete clauses are less likely to leave their jobs for competitors. The author of the study assessing effects on capital investment finds there are likely two mechanisms driving these effects. First, firms may be more likely to invest in capital when they train their workers because worker training and capital expenditure are complementary (*i.e.*, the return on investment in capital equipment is greater when workers are more highly trained). Second, non-compete clauses reduce competition, and firms' returns to capital expenditure are greater when competition is lower, incentivizing firms to invest more in capital.²⁹⁶

The Commission is not aware of any evidence of a relationship between the enforceability of non-compete clauses and the rate at which companies make other types of productive investments, such as investments in creating or sharing trade secrets. Similarly, the Commission is not aware of any evidence non-compete clauses reduce trade secret misappropriation or the loss of other types of confidential information. The Commission's understanding is there is little reliable empirical data on trade secret theft and firm investment in trade secrets in general, and no reliable data on how non-compete clauses affect these practices. The Commission understands these are difficult areas for researchers to study, due to, for example, the lack of a governmental registration requirement for trade secrets and the unwillingness of firms to disclose information about their practices related to trade secrets.²⁹⁷

The Commission is also not aware of any evidence that increased investment due to non-compete clauses leads to reduced prices for consumers. Indeed, the only empirical

²⁹⁶ Jeffers, *supra* note 92 at 29.

²⁹⁷ See, e.g., David S. Levine & Christopher B. Seaman, *The DTSA at One: An Empirical Study of the First Year of Litigation Under the Defend Trade Secrets Act*, 53 Wake Forest L. Rev. 105, 120–22 (2018).

study of the effects of non-compete clauses on consumer prices—in the health care sector—finds increased final goods prices as the enforceability of non-compete clauses increases.²⁹⁸

2. Employers Have Alternatives to Non-Compete Clauses for Protecting Valuable Investments

There are two reasons why the business justifications for non-compete clauses do not alter the Commission’s preliminary determination non-compete clauses are an unfair method of competition. The first is employers have alternatives to non-compete clauses for protecting valuable investments. These alternatives may not be as protective as employers would like, but they reasonably accomplish the same purposes as non-compete clauses while burdening competition to a less significant degree.

As noted above, the most commonly cited justifications for non-compete clauses are that they increase an employer’s incentive to make productive investments—such as investing in trade secrets or other confidential information, sharing this information with its workers, or training its workers—because employers may be more likely to make such investments if they know workers are not going to depart for or establish a competing firm. However, non-compete clauses restrict considerably more activity than necessary to achieve these benefits. Rather than restraining a broad scope of beneficial competitive activity—by barring workers altogether from leaving work with the employer for a competitor and starting a business that would compete with the employer—employers have alternatives for protecting valuable investments that are much more narrowly tailored to limit impacts on competitive conditions. These alternatives restrict a

²⁹⁸ See *supra* Part II.B.2.a.

considerably smaller scope of beneficial competitive activity than non-compete clauses because—while they may restrict an employee’s ability to use or disclose certain information—they generally do not prevent workers from working for a competitor or starting their own business altogether.²⁹⁹

a. Trade Secret Law

Trade secret law provides employers with an alternative means of protecting their investments in trade secrets. Trade secret law is a form of intellectual property law that protects confidential business information.³⁰⁰ It also serves as an alternative to the patent system, “granting proprietary rights to particular technologies, processes, designs, or formulae that may not be able to satisfy the rigorous standards for patentability.”³⁰¹ Even where information meets standards for patentability, companies may choose to rely on trade secret law and not obtain a patent, because they wish to keep information out of the public domain.³⁰²

Trade secret law has developed significantly in recent decades. Prior to the late 1970s, trade secret law across the states was inconsistent, leading to significant uncertainty regarding the scope of trade secret protections and the appropriate remedies for misappropriation.³⁰³ Recognizing the need for more uniform laws, the American Bar Association approved the Uniform Trade Secrets Act (“UTSA”) in 1979.³⁰⁴ Forty-seven

²⁹⁹ See, e.g., *MAI Basic Four, Inc. v. Basis, Inc.*, 880 F.2d 286, 287–88 (10th Cir. 1989) (stating that workers subject to NDAs—unlike workers subject to non-compete clauses—“remain free to work for whomever they wish, wherever they wish, and at whatever they wish,” subject only to the terms that prohibit them from disclosing or using certain information.”).

³⁰⁰ Brian T. Yeh, Protection of Trade Secrets: Overview of Current Law and Legislation, Cong. Rsch. Serv. Report R43714 (April 22, 2016) at 4.

³⁰¹ *Id.*

³⁰² *Id.* at 4–5.

³⁰³ Uniform Trade Secrets Act With 1985 Amendments (Feb. 11, 1986), Prefatory Note at 1.

³⁰⁴ *Id.* Prefatory Note at 3.

states and the District of Columbia have adopted the UTSA.³⁰⁵ The three states that have not adopted the UTSA offer protection to trade secrets under a different statute or under common law.³⁰⁶

The UTSA provides a civil cause of action for trade secret misappropriation, which refers to disclosure or use of a trade secret by a former employee without express or implied consent.³⁰⁷ The UTSA also provides for injunctive and monetary relief, including compensatory damages, punitive damages, and attorney's fees.³⁰⁸ In some states, under the "inevitable disclosure doctrine," courts may enjoin a worker from working for a competitor of the worker's employer where it is inevitable the worker will disclose trade secrets in the performance of the worker's job duties.³⁰⁹ The inevitable disclosure doctrine is highly controversial. Several states have declined to adopt it altogether, citing the doctrine's harsh effects on worker mobility.³¹⁰ Other states have required employers to meet high evidentiary burdens related to inevitability, irreparable harm, and bad faith before issuing an injunction pursuant to the doctrine.³¹¹

In addition, in 2016, Congress enacted the Defend Trade Secrets Act of 2016 ("DTSA"), which established a civil cause of action under federal law for trade secret misappropriation.³¹² The DTSA brought the rights of trade secret owners "into alignment

³⁰⁵ See Levine & Seaman, *supra* note 297 at 113.

³⁰⁶ Yeh, *supra* note 300 at 6 n.37.

³⁰⁷ UTSA, *supra* note 303 at sec. 1(2).

³⁰⁸ *Id.* at secs. 2–4.

³⁰⁹ See, e.g., *PepsiCo, Inc. v. Redmond*, 54 F.3d 1262 (7th Cir. 1995) (affirming the district court's order enjoining an employee from assuming his responsibilities at a competing employer for six months).

³¹⁰ See *Bayer Corp. v. Roche Molecular Sys., Inc.*, 72 F. Supp. 2d 1111, 1120 (N.D. Cal. 1999); *LeJeune v. Coin Acceptors, Inc.*, 849 A.2d 451, 471 (Md. 2004).

³¹¹ See, e.g., Eleanore R. Godfrey, *Inevitable Disclosure of Trade Secrets: Employee Mobility v. Employer Rights*, 3 J. High Tech. L. 161 (2004).

³¹² Defend Trade Secrets Act of 2016, Pub. L. No. 114-153, 130 Stat. 376 (May 11, 2016).

with those long enjoyed by owners of other forms of intellectual property, including copyrights, patents, and trademarks.”³¹³ Similar to state laws modeled on the UTSA, the DTSA authorizes civil remedies for trade secret misappropriation, including injunctive relief, damages (including punitive damages), and attorney’s fees.³¹⁴ The DTSA also authorizes a court, in “extraordinary circumstances,” to issue civil *ex parte* orders for the “seizure of property necessary to prevent the propagation or dissemination of the trade secret that is the subject of the action.”³¹⁵

Furthermore, trade secret theft is a federal crime. The Economic Espionage Act of 1996 (“EEA”) makes it a federal crime to steal a trade secret for either (1) the benefit of a foreign entity (“economic espionage”) or (2) the economic benefit of anyone other than the owner (“theft of trade secrets”).³¹⁶ The EEA authorizes substantial criminal fines and penalties for these crimes.³¹⁷ The EEA further authorizes criminal or civil forfeiture, including of “any property constituting, or derived from, any proceeds obtained directly or indirectly as a result of” an EEA offense.³¹⁸ The EEA also requires offenders to pay restitution to victims of trade secret theft.³¹⁹

Under these laws, the term “trade secret” is defined expansively and includes a wide range of confidential information. The UTSA generally defines a “trade secret” as information that (1) derives independent economic value from not being generally known to other persons who can obtain economic value from its disclosure or use and (2) is the

³¹³ U.S. Senate, Report to Accompany S. 1890, the Defend Trade Secrets Act of 2016, S. Rept. 114-220 at 3.

³¹⁴ 18 U.S.C. 1836(b)(3).

³¹⁵ 18 U.S.C. 1836(b)(2).

³¹⁶ 18 U.S.C. 1831 (economic espionage); 18 U.S.C. 1832 (theft of trade secrets).

³¹⁷ 18 U.S.C. 1831–1832.

³¹⁸ 18 U.S.C. 1834, 2323.

³¹⁹ 18 U.S.C. 1834, 2323.

subject of reasonable efforts to maintain its secrecy.³²⁰ The DTSA and EEA use a similar definition.³²¹ The Supreme Court has held “some novelty” is required for information to be a trade secret, because “that which does not possess novelty is usually known.”³²² Overall, the definition of “trade secret” covers a wide range of information employers seek to protect from disclosure. As the high court of one state noted, “[t]here is virtually no category of information that cannot, as long as the information is protected from disclosure to the public, constitute a trade secret.”³²³

The viability of trade secret law as a means for redressing trade secret theft is illustrated by the fact that firms regularly bring claims under trade secret law. A recent analysis by the legal analytics firm Lex Machina finds 1,382 trade secret lawsuits were filed in federal court in 2021.³²⁴ Perhaps due to the enactment of the DTSA, the number of cases filed increased 30% from 2015 to 2017—from 1,075 to 1,396 cases—and has remained steady ever since.³²⁵ In addition, an analysis by the law firm Morrison Foerster finds 1,103 trade secret cases were filed in state courts in 2019.³²⁶ The number of cases filed in state court has held steady since 2015, when 1,161 cases were filed.³²⁷ The fact that a considerable number of trade secret lawsuits are filed in federal and state court—approximately 2,500 cases per year—and the fact that this number has held steady for

³²⁰ UTSA, *supra* note 303 at sec. 1(4).

³²¹ 18 U.S.C. 1839(3).

³²² *Kewanee Oil Co. v. Bicron Corp.*, 416 U.S. 470, 476 (1974).

³²³ *U.S. West Commc'ns, Inc. v. Off. of Consumer Advoc.*, 498 N.W.2d 711, 714 (Iowa 1993). *See also Confold Pac., Inc. v. Polaris Indus., Inc.*, 433 F.3d 952 (7th Cir. 2006) (Posner, J.).

³²⁴ Lex Machina, Infographic, *Trade Secret Litigation Report 2021*, <https://lexmachina.com/resources/infographic-trade-secret-report/>.

³²⁵ Kenneth A. Kuwayti, John R. Lanham, & Candice F. Heinze, Morrison Foerster, Client Alert, *Happy Anniversary, DTSA: The Defend Trade Secrets Act at Five* (May 25, 2021).

³²⁶ *Id.*

³²⁷ *Id.*

several years suggests employers view trade secret law as a viable means of obtaining redress for trade secret theft.

In sum, intellectual property law already provides significant legal protections for an employer's trade secrets. Trade secret law may not be as protective as some firms might like, but overall, it provides employers with a viable means of protecting their investments in trade secrets.

b. Non-Disclosure Agreements

Employers that seek to protect valuable investments also have the ability to enter into NDAs with their workers.³²⁸ NDAs, which are also commonly known as confidentiality agreements, are contracts in which a party agrees not to disclose information the contract designates as confidential. NDAs may also prohibit workers from using information that is designated as confidential. If a worker violates an NDA, the worker may be liable for breach of contract.

Employers regularly use NDAs to protect trade secrets and other confidential business information. Researchers estimate between 33% and 57% of U.S. workers are subject to at least one NDA.³²⁹ In most states, NDAs are more enforceable than non-compete clauses.³³⁰

³²⁸ In this NPRM, we use the term “NDA” to refer to contractual provisions that are designed to protect trade secrets or other business information that has economic value. Employers may also seek to use NDAs to protect other kinds of information, such as information about discrimination, harassment, sexual assault, corporate wrongdoing, or information that may disparage the company or its executives or employees. These types of NDAs have been widely criticized for, among other things, their pernicious effects on workers. See, e.g., Rachel Arnow-Richman et al., *Supporting Market Accountability, Workplace Equity, and Fair Competition by Reining In Non-Disclosure Agreements*, UC-Hastings Research Paper Forthcoming at 2–6 (January 2022), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4022812.

³²⁹ *Id.*

³³⁰ See Chris Montville, *Reforming the Law of Proprietary Information*, 56 Duke L.J. 1159, 1179–83 (2007).

The widespread use of NDAs by firms has raised concerns that NDAs may inhibit innovation and worker mobility.³³¹ Scholars have also raised concerns that overbroad NDAs can function as *de facto* non-compete clauses.³³² However, the protection of trade secrets and other limited confidential business information is widely recognized as a legitimate use of NDAs.³³³

NDAs that are unusually broad in scope may function as *de facto* non-compete clauses, hence falling within the scope of the proposed rule.³³⁴ However, appropriately tailored NDAs, which would fall outside the scope of the proposed rule,³³⁵ burden competition to a lesser degree than non-compete clauses. Such NDAs may prevent workers from disclosing or using certain information, but they generally do not prevent workers from working for a competitor or starting their own business altogether. As the U.S. Court of Appeals for the Tenth Circuit has stated, workers subject to NDAs—unlike workers subject to non-compete clauses—“remain free to work for whomever they wish, wherever they wish, and at whatever they wish,” subject only to the terms that prohibit them from disclosing or using certain information.³³⁶

c. Other Means of Protecting Valuable Investments

In addition to trade secret law and NDAs, employers have additional means of protecting valuable investments. For example, if an employer wants to prevent a worker from leaving right after receiving valuable training, the employer can sign the worker to

³³¹ See Rex N. Alley, *Business Information and Non-Disclosure Agreements: A Public Policy Framework*, 116 Nw. L. Rev. 817, 832 (2022).

³³² See, e.g., Arnov-Richman et al., *supra* note 328 at 5. See also *Brown*, 57 Cal. App. 5th at 319.

³³³ See *Montville*, *supra* note 330 at 1179–83.

³³⁴ See proposed § 910.1(b)(2) (describing the functional test for whether a contractual term is a non-compete clause) and *infra* Part V (in the section-by-section analysis for proposed § 910.1(b)).

³³⁵ *Id.*

³³⁶ *MAI Basic Four, Inc.*, 880 F.2d at 287–88.

an employment contract with a fixed duration. An employer can establish a term of employment long enough for the employer to recoup its training investment without restricting a worker's ability to compete with the employer after the worker's employment ends. Employers that wish to retain their workers can also pay the worker more, offer them better hours or better working conditions, or otherwise improve the conditions of their employment. These are all viable alternatives for protecting training investments, and other investments an employer may make, that do not restrict a worker's ability to work for a competitor of the employer or a rival's ability to compete against the worker's employer to attract the worker.

Proponents of non-compete clauses sometimes assert that, without non-compete clauses, firms will be unable to protect their trade secrets or other valuable investments. However, there are three states in which non-compete clauses are generally unavailable to employers today: California, North Dakota, and Oklahoma. In these three states, employers generally cannot enforce non-compete clauses, so they must protect their investments using one or more of the alternatives described above. The experiences of these states suggest the alternatives described above are fundamentally viable for protecting valuable firm investments.

Non-compete clauses have been void in California since 1872, in North Dakota since 1877, and in Oklahoma since 1890.³³⁷ California is a state where large companies have succeeded—it is home to four of the world's ten largest companies by market

³³⁷ Gilson, *supra* note 88 at 616 (California); *Werlinger v. Mutual Service Casualty Ins. Co.*, 496 N.W.2d 26, 30 (N.D. 1993) (North Dakota); Brandon Kemp, *Noncompetes in Oklahoma Mergers and Acquisitions*, 88 Okla. Bar J. 128 (Jan. 21, 2017) (Oklahoma).

capitalization—and it also maintains a vibrant startup culture.³³⁸ Since the 1980s, California has become the global center of the technology sector, and technology firms are highly dependent on protecting trade secrets and other confidential information.³³⁹ (Indeed, researchers have posited that high-tech clusters in California may have been aided by increased labor mobility due to the unenforceability of non-compete clauses.³⁴⁰) In North Dakota and Oklahoma, the energy industry has thrived, and firms in the energy industry depend on the ability to protect trade secrets and other confidential information.

The economic success in these three states of industries highly dependent on trade secrets and other confidential information illustrates that companies have viable alternatives to non-compete clauses for protecting valuable investments. Relative to non-compete clauses, these alternatives are more narrowly tailored to limit impacts on competitive conditions.

The Commission seeks comment on its preliminary finding that employers have reasonable alternatives to non-compete clauses for protecting their investments.

3. The Asserted Benefits from These Justifications Do Not Outweigh the Harms from Non-Compete Clauses

The second reason why the commonly cited business justifications for non-compete clauses do not alter the Commission’s preliminary determination that non-compete clauses are an unfair method of competition is that, overall, the asserted benefits from these justifications do not outweigh the harms from non-compete clauses.

³³⁸ Josh Dylan, *What Is Market Cap In Stocks?*, Nasdaq.com (Aug, 12, 2022); Ewing Marion Kauffman Found., *State Entrepreneurship Rankings*, https://www.realclearpublicaffairs.com/public_affairs/2019/02/25/kauffman_foundation_state_entrepreneurship_rankings.html.

³³⁹ See, e.g., Gilson, *supra* note 88 at 594–95.

³⁴⁰ *Id.*; Fallick, Fleischman, & Rebitzer, *supra* note 89.

As described above, the Commission preliminarily finds that, for some workers, non-compete clauses are exploitative and coercive because they take advantage of unequal bargaining power between employers and workers at the time of contracting.³⁴¹ The Commission also preliminarily finds that, for some workers, non-compete clauses are exploitative and coercive at the time of the worker’s potential departure from the employer because they force a worker to either stay in a job they want to leave or choose an alternative that likely impacts their livelihood.³⁴² For these workers, for whom non-competes are facially unfair, the justifications for non-compete clauses must overcome a high bar to alter the Commission’s preliminary determination that non-compete clauses are an unfair method of competition.³⁴³

In addition, non-compete clauses cause considerable harm to competition in labor markets and product and service markets. There is evidence non-compete clauses harm both workers and consumers. Non-compete clauses obstruct competition in labor markets because they inhibit optimal matches from being made between employers and workers across the labor force. The available evidence indicates increased enforceability of non-compete clauses substantially reduces workers’ earnings, on average, across the labor force generally and for specific types of workers.³⁴⁴

In addition to the evidence showing non-compete clauses reduce earnings for workers across the labor force, there is also evidence non-compete clauses reduce earnings specifically for workers who are not subject to non-compete clauses.³⁴⁵ These

³⁴¹ See *supra* Part IV.A.1.b.

³⁴² See *supra* Part IV.A.1.c.

³⁴³ See, e.g., *Fashion Originators’ Guild*, 312 U.S. at 467–68; *Atl. Refining Co.*, 381 U.S. at 371.

³⁴⁴ See *supra* Part II.B.1.b.

³⁴⁵ See *supra* Part II.B.1.c.

workers are harmed by non-compete clauses, because their wages are depressed, but they do not necessarily benefit from any incentives for increased training that non-compete clauses may provide.

Overall, these harms to workers are significant. The Commission estimates that the proposed rule, which would prohibit employers from using non-compete clauses, would increase workers' total earnings by \$250 to \$296 billion per year.³⁴⁶

The available evidence also indicates non-compete clauses negatively affect competition in product and service markets. There is evidence non-compete clauses increase consumer prices and concentration in the health care sector.³⁴⁷ There is also evidence non-compete clauses foreclose the ability of competitors to access talent by effectively forcing future employers to buy out workers from their non-compete clauses if they want to hire them.³⁴⁸ The weight of the evidence also indicates non-compete clauses have a negative impact on new business formation and innovation.³⁴⁹ These harms are significant. For example, with respect to consumer prices in the health care sector alone, the Commission estimates health spending would decrease by \$148 billion annually due to the proposed rule.³⁵⁰

In the Commission's preliminary view, the asserted benefits from non-compete clauses do not outweigh these harms. In short, while there is considerable evidence non-compete clauses harm both workers and consumers, the evidence that non-compete clauses benefit workers or consumers is scant.

³⁴⁶ See *infra* Part VII.B.1.a.

³⁴⁷ See *supra* Part II.B.2.a.

³⁴⁸ See *supra* Part II.B.2.b.

³⁴⁹ See *supra* Part II.B.2.c–d.

³⁵⁰ See *infra* Part VII.B.2.c.

As described above, the most common justification for non-compete clauses is they increase employers' incentive to make productive investments in, for example, trade secrets, customer lists, worker training, and capital investment. There is evidence non-compete clauses increase employee training and capital investment, as noted above.³⁵¹ However, the considerable harms to workers and consumers are not outweighed because an employer has some marginally greater ability to protect trade secrets, customer lists, and other firm investments, or because the worker is receiving increased training, or because the firm has increased capital investments. If they were, workers would have higher earnings when non-compete clauses are more readily available to firms (*i.e.*, when legal enforceability of non-compete clauses increases) or prices for consumers would be lower. However, the empirical economic literature shows workers generally have lower, not higher, earnings when non-compete clause enforceability increases.

Moreover, the Commission is also not aware of any evidence these potential benefits of non-compete clauses lead to reduced prices for consumers. Indeed, the only empirical study of the effects of non-compete clauses on consumer prices—in the health care sector—finds increased final goods prices as the enforceability of non-compete clauses increases.³⁵² Furthermore, the Commission is not aware of any evidence non-compete clauses reduce trade secret misappropriation or the loss of other types of confidential information. The Commission's understanding is there is little reliable empirical data on trade secret theft and firm investment in trade secrets in general, and no reliable data on how non-compete clauses affect these practices. The Commission is also

³⁵¹ See *supra* Part II.B.2.e.

³⁵² See *supra* Part II.B.2.a.

not aware of evidence that, in the three states in which non-compete clauses are generally void, the inability to enforce non-compete clauses has materially harmed workers or consumers in those states.

As a result, the Commission preliminarily finds the asserted benefits from non-compete clauses do not outweigh the harms. The Commission seeks comment on this preliminary finding.

V. Section-by-Section Analysis

The Commission is proposing to create a new Subchapter J in Chapter 16 of the Code of Federal Regulations. Subchapter J would be titled “Rules Concerning Unfair Methods of Competition.” Within Subchapter J, the Commission is proposing to create 16 CFR part 910—the Non-Compete Clause Rule.³⁵³ The Commission describes each section of the proposed rule below.

Section 910.1 Definitions

Proposed § 910.1 would contain definitions of terms that would be used in the Rule.

1(a) Business Entity

Proposed § 910.1(a) would define the term business entity. This term would be used in proposed § 910.3, which would contain an exception for certain non-compete clauses. Under the exception, the Rule would not apply to a non-compete clause entered into by a person who is selling a business entity or otherwise disposing of all of the person’s ownership interest in the business entity, or by a person who is selling all or substantially all of a business entity’s operating assets, when the person restricted by the

³⁵³ For ease of reference, this Part V refers to proposed 16 CFR part 910 as “the Rule.”

non-compete clause is a substantial owner of, or substantial member or substantial partner in, the business entity at the time the person enters into the non-compete clause. The proposed rule would also use the term business entity in proposed § 910.1(e), which would define substantial owner, substantial member, or substantial partner as an owner, member, or partner holding at least a 25% ownership interest in a business entity.

Proposed § 910.1(a) would define the term business entity as a partnership, corporation, association, limited liability company, or other legal entity, or a division or subsidiary thereof. The Commission is proposing to include divisions and subsidiaries in the definition because it believes the exception in proposed § 910.3 should apply where a person is selling a division or subsidiary of a business entity. The primary rationale for the sale-of-a-business exception in proposed § 910.3—that the exception may help to protect the value of a business acquired by a buyer—would also apply where a person is selling a division or subsidiary of a business entity. Applying the sale-of-a-business exception where a person is selling a division or subsidiary of a business entity would also be consistent with many state laws that exempt non-compete clauses from certain requirements when they are between the seller and buyer of a business, including a division or subsidiary of the business.³⁵⁴

The Commission seeks comment on proposed § 910.1(a).

1(b) Non-Compete Clause

Proposed § 910.1(b)(1) would define non-compete clause as a contractual term between an employer and a worker that prevents the worker from seeking or accepting employment with a person or operating a business after the conclusion of the worker's

³⁵⁴ See, e.g., Cal. Bus. & Prof. Code sec. 16601; Mass. Gen. Laws Ann. ch. 149, sec. 24L (definition of “noncompetition agreement”); R.I. Gen. Laws sec. 28-59-2(8)(iii).

employment with the employer. The Commission believes this is a generally accepted definition of the term non-compete clause.

Proposed § 910.1(b)(1) would limit the coverage of the Rule to non-compete clauses between employers and workers. The Rule would not apply to other types of non-compete clauses—for example, non-compete clauses between two businesses, where neither is a worker pursuant to the Rule’s definition of “worker.”³⁵⁵ While such non-compete clauses would not be covered by the Rule, they would still be subject to federal antitrust law and all other applicable law.

Furthermore, pursuant to proposed § 910.1(b)(1), the Rule would apply only to post-employment restraints—*i.e.*, restrictions on what the worker may do after the conclusion of the worker’s employment with the employer. The Rule would not apply to concurrent-employment restraints—*i.e.*, restrictions on what the worker may do during the worker’s employment.

Some non-compete clauses do not use language that expressly prohibits a worker from competing against their employer, but instead effect the same restriction by requiring workers to pay damages if they compete against their employer. State courts generally view these contractual terms as non-compete clauses.³⁵⁶ These contractual terms would also be non-compete clauses under proposed § 910.1(b)(1), because they prevent a worker from seeking or accepting work with a person or operating a business after the conclusion of the worker’s employment with the employer (unless the damages specified in the contract are paid).

³⁵⁵ See proposed § 910.1(f).

³⁵⁶ See, e.g., *Wichita Clinic, P.A. v. Louis*, 185 P.3d 946, 951 (Kan. Ct. App. 2008); *Intermountain Eye & Laser Ctrs.*, 127 P.3d 121, 127 (Idaho 2005); *BDO Seidman v. Hirshberg*, 712 N.E.2d 1220, 1222–23 (N.Y. 1999).

Proposed § 910.1(b)(2) would clarify the definition of non-compete clause in proposed § 910.1(b)(1) by explaining that whether a contractual term is a non-compete clause for purposes of the Rule would depend on a functional test. In other words, whether a contractual term is a non-compete clause would depend not on what the term is called, but how the term functions.

In addition to non-compete clauses, employers and workers enter into many other types of covenants that restrict what a worker may do after the worker leaves their job, including, among others, NDAs; non-solicitation agreements; and TRAs.³⁵⁷ The definition of non-compete clause would generally not include these types of covenants, because these covenants generally do not prevent a worker from seeking or accepting work with a person or operating a business after the conclusion of the worker's employment with the employer. These other types of covenants may affect the way a worker competes with their former employer after the worker leaves their job. However, they do not generally prevent a worker from competing with their former employer altogether; and they do not generally prevent other employers from competing for that worker's labor. For example, if a worker leaves their job with their employer and goes to work for a competitor, an NDA the worker signed with their employer may prevent the worker from disclosing certain information to the competitor. However, a standard NDA would not prevent the worker from seeking or accepting work with the competitor.

The Commission is concerned, however, that some employers may seek to evade the requirements of the Rule by implementing restrictive employment covenants other than non-compete clauses that restrain such an unusually large scope of activity that they

³⁵⁷ See *supra* Part II.A.

are *de facto* non-compete clauses. Under proposed § 910.1(b)(2), such functional equivalents would be non-compete clauses for purposes of the Rule, whether drafted for purposes of evasion or not.

Courts have taken this approach when analyzing whether a contractual term is a non-compete clause under state law. For example, in *Brown v. TGS Mgmt. Co., LLC*, a California state court held an NDA that defined confidential information “so broadly as to prevent [the plaintiff] from ever working again in securities trading” operated as a *de facto* non-compete clause and therefore could not be enforced under California law, which generally prohibits enforcement of non-compete clauses. The NDA in this case restrained a far broader scope of activity than a typical NDA. For example, it defined “confidential information” as any information that is “usable in” or “relates to” the securities industry. As a result, the court concluded it effectively prevented the worker from working in the securities industry after his employment ended and was therefore a *de facto* non-compete clause.³⁵⁸ Similarly, in *Wegmann v. London*, the U.S. Court of Appeals for the Fifth Circuit concluded liquidated damages provisions in a partnership agreement were *de facto* non-compete clauses “given the prohibitive magnitudes of liquidated damages they specify.”³⁵⁹

The purpose of § 910.1(b)(2) is to clarify that, if an employer implements a restrictive covenant not called a “non-compete clause” but so unusually broad in scope it functions as such, the covenant would be within the definition of non-compete clause in proposed § 910.1(b)(1). Proposed § 910.1(b)(2) would state that the term non-compete

³⁵⁸ 57 Cal. App. 5th 303, 306, 316–319 (Cal. Ct. App. 2020).

³⁵⁹ 648 F.2d 1072, 1073 (5th Cir. 1981).

clause includes a contractual term that is a *de facto* non-compete clause because it has the effect of prohibiting the worker from seeking or accepting work with a person or operating a business after the conclusion of the worker's employment with the employer.

Proposed § 910.1(b)(2) would also provide two examples of contractual terms that may be *de facto* non-compete clauses. The first example, based on *Brown v. TGS Mgmt. Co., LLC*, would be a non-disclosure agreement between an employer and a worker written so broadly it effectively precludes the worker from working in the same field after the conclusion of the worker's employment with the employer. The second example, based on *Wegmann v. London*, would be a covenant between an employer and a worker that requires the worker to pay the employer or a third-party entity for training costs if the worker's employment terminates within a specified time period, where the required payment is not reasonably related to the costs the employer incurred for training the worker.

The Commission stresses this list of examples would be a non-exclusive list. Restrictive employment covenants other than NDAs and TRAs may also constitute *de facto* non-compete clauses, depending on the facts. In addition, NDAs and TRAs may constitute *de facto* non-compete clauses under factual scenarios other than the scenarios outlined in these examples.

The Commission seeks comment on proposed § 910.1(b)(1) and (2). In addition, the Commission is concerned that workplace policies similar to non-compete clauses—such as a term in an employee handbook stating workers are prohibited from working for competitors after their employment ends—could potentially have negative effects similar to non-compete clauses if workers believe they are binding, even if they do not impose a

contractual obligation. Therefore, the Commission also seeks comment on whether non-compete clause should be defined not only as a “contractual term” between an employer and a worker, but also as a provision in a workplace policy.³⁶⁰

1(c) Employer

The Rule would apply only to non-compete clauses between employers and workers.³⁶¹ Proposed § 910.1(c) would define employer as a person, as defined in 15 U.S.C. 57b-1(a)(6), that hires or contracts with a worker to work for the person. 15 U.S.C. 57b-1(a)(6) defines person as any natural person, partnership, corporation, association, or other legal entity, including any person acting under color or authority of state law. Thus, proposed § 910.1(c) would effectively define employer as any natural person, partnership, corporation, association, or other legal entity, including any person acting under color or authority of state law, that hires or contracts with a worker to work for the person.

A person, as defined in 15 U.S.C. 57b-1(a)(6), that hires or contracts with a worker to work for the person would be an employer under proposed § 910.1(c) regardless of whether the person meets another legal definition of employer, such as a definition in federal or state labor law.

Some entities that would otherwise be employers may not be subject to the Rule to the extent they are exempted from coverage under the FTC Act. These entities include certain banks, savings and loan institutions, federal credit unions, common carriers, air carriers and foreign air carriers, and persons subject to the Packers and Stockyards Act of

³⁶⁰ See, e.g., D.C. Code sec. 32-581.01(15).

³⁶¹ See proposed § 910.1(b)(1).

1921,³⁶² as well as an entity that is not “organized to carry on business for its own profit or that of its members.”³⁶³ Where an employer is exempt from coverage under the FTC Act, the employer would not be subject to the Rule.

Furthermore, state and local government entities—as well as some private entities—may not be subject to the Rule when engaging in action protected by the state action doctrine. States are subject to the antitrust laws.³⁶⁴ However, under the state action doctrine, federal statutes do not limit the sovereign states’ autonomous authority over their own officers, agents, and policies in the absence of clear congressional intent to do so.³⁶⁵ The key question is whether the conduct at issue is “compelled by direction of the state acting as a sovereign.”³⁶⁶ The state action doctrine may also be invoked by private entities in certain limited scenarios—specifically, where (1) the challenged restraint is clearly articulated as and affirmatively expressed as state policy, and (2) the policy is actively supervised by the state itself.³⁶⁷ Thus, some entities that would otherwise be employers under proposed § 910.1(c) may not be subject to the Rule when engaging in action protected by the state action doctrine. Where private entities are involved, this would likely require a highly fact-specific inquiry.

The Commission seeks comment on proposed § 910.1(c).

1(d) Employment

³⁶² 15 U.S.C. 45(a)(2).

³⁶³ 15 U.S.C. 44.

³⁶⁴ *Goldfarb v. Va. State Bar*, 421 U.S. 773, 791–92 (1975).

³⁶⁵ *Parker v. Brown*, 317 U.S. 341, 350–51 (1943) (construing the Sherman Act).

³⁶⁶ *Goldfarb*, 421 U.S. at 791.

³⁶⁷ *Cal. Retail Liquor Dealers Ass’n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 105 (1980).

The proposed rule would define the term non-compete clause as a contractual term between an employer and a worker that prevents the worker from seeking or accepting employment with a person, or operating a business, after the conclusion of the worker's employment with the employer. Proposed § 910.1(d) would define employment as work for an employer, as the term employer is defined in § 910.1(c). This proposed definition would clarify that an employment relationship exists, for purposes of the Rule, regardless of whether an employment relationship exists under another law, such as a federal or state labor law. The Commission seeks comment on proposed § 910.1(d).

1(e) Substantial Owner, Substantial Member, and Substantial Partner

The proposed rule would use the terms substantial owner, substantial member, and substantial partner in proposed § 910.3, which would exempt certain non-compete clauses from coverage under the Rule. This exception would only be available where the party restricted by the non-compete clause is a substantial owner of, or substantial member or substantial partner in, the business entity. Limiting the exception to substantial owners, substantial members, and substantial partners would ensure the exception is only available where the seller's stake in the business is large enough that a non-compete clause may be necessary to protect the value of the business acquired by the buyer.

Proposed § 910.1(e) would define substantial owner, substantial member, and substantial partner as an owner, member, or partner holding at least a 25% ownership interest in a business entity. The Commission is proposing a threshold of 25% ownership interest because the Commission believes the exception should be available where, for example, a few entrepreneurs sharing ownership interest in a startup sell their firm. In

such a scenario, a non-compete clause may be necessary to protect the value of the business acquired by the buyer. For this reason, a threshold of, for example, 51% may be too high.

However, the Commission believes the exception should not be available where the ownership interest in question is so small the transfer of ownership interest would not be necessary to protect the value of the business acquired by the buyer. For example, the exception should not be available where a worker with a small amount of company stock sells stock back to the company as part of a stock redemption agreement when the worker's employment ends. The Commission believes a 25% threshold strikes the appropriate balance between a threshold that may be too high (and would exclude many scenarios in which a non-compete clause may be necessary to protect the value of the business acquired by the buyer) and a threshold that may be too low (and would allow the exception to apply more broadly than is needed to protect such an interest).

Instead of establishing a threshold, the Rule could simply use the terms substantial owner, substantial member, and substantial partner in proposed § 910.3 and leave the interpretation of those terms to case-by-case adjudication. However, if the Rule does not define a threshold, sellers of businesses may be unsure whether or not they are substantial owners, substantial members, and substantial partners under proposed § 910.3. Defining a threshold would provide greater clarity to the public and facilitate compliance with the Rule.

The Commission seeks comment on proposed § 910.1(e).

1(f) Worker

The Rule would apply only to non-compete clauses between employers and workers.³⁶⁸ Proposed § 910.1(f) would define worker as a natural person who works, whether paid or unpaid, for an employer. Proposed § 910.1(f) would further state the term worker 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.

As this definition states, the term worker would include not only employees, but also individuals classified as independent contractors, as well as other kinds of workers. Under proposed § 910.1(f), the term worker would include any natural person who works, whether paid or unpaid, for an employer, without regard to whether the worker is classified as an “employee” under the Fair Labor Standards Act (FLSA) or any other statute that draws a distinction between “employees” and other types of workers. Thus, gig economy workers such as rideshare drivers would be considered workers for purposes of proposed § 910.1(f).

The Commission is concerned that, if the Rule were to define workers as “employees” according to, for example, the FLSA definition, employers may misclassify employees as independent contractors to evade the Rule’s requirements. Furthermore, the Commission has no reason to believe non-compete clauses that apply to workers such as independent contractors or interns negatively affect competitive conditions to a lesser degree than non-compete clauses that apply to employees. Such non-compete clauses may, in fact, be more harmful to competition, given that these other types of workers tend to have shorter employment relationships. In addition, the Commission does not believe

³⁶⁸ See proposed § 910.1(b)(1).

employers have stronger business justifications for applying non-compete clauses to independent contractors than they would to employees.

Proposed § 910.1(f) would also state the term worker does not include a franchisee in the context of a franchisee-franchisor relationship. The Commission believes that, in some cases, the relationship between a franchisor and franchisee may be more analogous to the relationship between two businesses than the relationship between an employer and a worker. In addition, the evidentiary record before the Commission relates primarily to non-compete clauses that arise solely out of employment. The Commission has surveyed the available evidence relating to non-compete clauses and is not aware of research on the effects of applying additional legal restrictions to non-compete clauses between franchisors and franchisees. Therefore, the Commission believes it would be appropriate to clarify that a franchisee—in the context of a franchisor-franchisee relationship—is not a worker for purposes of proposed § 910.1(f).

Proposed § 910.1(f) would further clarify, however, the term worker includes a natural person who works for the franchisee or franchisor. In addition, proposed § 910.1(f) would clarify non-compete clauses between franchisors and franchisees would remain subject to federal antitrust law as well as all other applicable law. These laws include state laws that apply to non-compete clauses in the franchise context. The Commission is not proposing to find that non-compete clauses between franchisors and franchisees are beneficial to competition.

The Commission seeks comment on proposed § 910.1(f).

Section 910.2 Unfair Methods of Competition

2(a) Unfair Methods of Competition

Proposed § 910.2(a) would state 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 the worker is subject to an enforceable non-compete clause. In effect, proposed § 910.2(a) would categorically ban employers from using non-compete clauses, because—as of the compliance date—employers would be prohibited from maintaining pre-existing non-compete clauses and entering into new non-compete clauses.³⁶⁹

Part IV above explains the legal basis for the Commission’s preliminary determination that the practices listed in proposed § 910.2(a) are unfair methods of competition. This section-by-section analysis for proposed § 910.2(a) describes how each of the three prongs of proposed § 910.2(a) would function and explains why the Commission is proposing a categorical ban on non-compete clauses.

How Proposed § 910.2(a) Would Function

Proposed § 910.2(a) would prohibit an employer from entering into or attempting to enter into a non-compete clause with a worker and maintaining with a worker a non-compete clause. Proposed § 910.2(a) would use both the term “enter into” and the term “maintain” to make clear it is an unfair method of competition for an employer to either (1) enter into or attempt to enter into new non-compete clauses as of the Rule’s compliance date or (2) maintain pre-existing non-compete clauses as of the compliance date. The Commission believes non-compete clauses entered into before the compliance date implicate the concerns described above in Part IV to the same degree as non-

³⁶⁹ However, employers could still use non-compete clauses where they qualify for the exception in proposed § 910.3 for non-compete clauses between the seller and buyer of a business.

compete clauses entered into as of the compliance date.³⁷⁰ As a result, the Commission believes it would be appropriate to require employers to rescind non-compete clauses entered into before the compliance date, as well as to refrain from entering into or attempting to enter into new non-compete clauses starting on the compliance date.

Furthermore, requiring employers to rescind existing non-compete clauses would not impose significant compliance costs, due to the safe harbor in proposed § 910.2(b)(3). Under this safe harbor, an employer could comply with the requirement to rescind existing non-compete clauses by providing notice to the affected workers. In addition, proposed § 910.2(b)(2)(C) would further reduce compliance costs by providing language that would presumptively meet this notice requirement.

Proposed § 910.2(a) would prohibit an employer from attempting to enter into a non-compete clause with a worker. An employer attempts to enter a non-compete clause with a worker where, for example, the employer provides the worker with the non-compete clause, but the worker does not sign it. The Commission is concerned that attempting to enter into a non-compete clause with a worker would have *in terrorem* effects because, in this situation, the worker may still believe they are subject to a non-compete clause even if they did not sign it. For example, the worker may not recall whether they signed the non-compete clause or may not realize they are not bound by the non-compete clause unless they signed it.

Proposed § 910.2(a) would also prohibit an employer from representing to a worker that the worker is covered by a non-compete clause where the employer has no good faith basis to believe the worker is subject to an enforceable non-compete clause.

³⁷⁰ See *supra* Part IV (describing the reasons for the Commission’s preliminary determination that non-compete clauses between employers and workers are an unfair method of competition).

Workers often lack knowledge of whether employers may enforce non-compete clauses.³⁷¹ In addition, the available evidence indicates that, in states where non-compete clause are void, workers are subject to non-compete clauses at approximately the same rate as workers in other states, suggesting that employers may believe workers are unaware of their legal rights.³⁷² Because many workers lack knowledge of whether their employer may enforce a non-compete clause under state law, they may also be unaware of any final rule issued by the Commission prohibiting employers from entering into or maintaining non-compete clauses. Employers may seek to exploit this lack of awareness by representing to workers that they are subject to a non-compete clause when they are not. This would likely have an *in terrorem* effect on workers, causing them to refrain from looking for work or taking another job, thereby furthering the adverse effects on competition motivating this proposed rule. As a result, the Commission believes it is appropriate for the Rule to prohibit employers from representing to workers that they are covered by a non-compete clause.

In addition, workers—particularly low-income workers—may lack resources to litigate against their employers. As a result, mere threats to enforce a non-compete clause may deter workers from looking for work with a competitor or starting their own business, which would result in the anticompetitive effects described above in Part IV.A.

Under this “representation” prong of proposed § 910.2(a), an employer would be prohibited from, among other things, threatening to enforce a non-compete clause against a worker; advising a worker that, due to a non-compete clause, they should not pursue a

³⁷¹ See Prescott & Starr, *supra* note 57 at 10–11.

³⁷² See Starr, Prescott, & Bishara, *supra* note 42 at 81.

particular job opportunity; or simply telling the worker that the worker is covered by a non-compete clause. However, under proposed § 910.2(a), this prohibition on representation would only apply where the employer has no good faith basis to believe the worker is subject to an enforceable non-compete clause. Proposed § 910.2(a) includes this “no good faith basis” exception to ensure the representation prong is consistent with the First Amendment. The Supreme Court has held “there can be no constitutional objection to the suppression of commercial messages that do not accurately inform the public about lawful activity.”³⁷³ Accordingly, “[t]he government may ban forms of communication more likely to deceive the public than to inform it, or commercial speech related to illegal activity.”³⁷⁴ A rule that prohibits an employer from representing 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—would meet this test because, under such circumstances, an employer would be making a false claim and asserting an illegal restraint on worker activity. An employer would have no good faith basis to believe that a worker is subject to an enforceable non-compete clause where non-compete clauses are not enforceable in the relevant state or where the validity of the Rule—which would prohibit employers from maintaining or entering into non-compete clauses—has been adjudicated and upheld.

Proposed § 910.2(a) would not apply retroactively. An employer would not violate proposed § 910.2(a) where—prior to the compliance date—it entered into or attempted to enter into a non-compete clause with a worker; maintained with a worker a

³⁷³ *Cent. Hudson Gas & Elec. v. Pub. Serv. Comm'n of N.Y.*, 447 U.S. 557, 563 (1980).

³⁷⁴ *Id.* at 563–64.

non-compete clause; or represented to a worker that the worker is subject to a non-compete clause. Instead, proposed § 910.2(a) would require employers to refrain from these practices starting on the compliance date.

Why the Commission Is Proposing A Categorical Ban on Non-Compete Clauses

Except for certain non-compete clauses between the seller and buyer of a business,³⁷⁵ the proposed rule would categorically ban employers from using non-compete clauses with workers. The proposed rule would prohibit an employer from using a non-compete clause with any of its workers, without regard to the worker's earnings or job function.

The Commission is proposing a categorical ban on non-compete clauses because, fundamentally, non-compete clauses obstruct labor market competition through a similar mechanism for all workers. Non-compete clauses block workers in a labor market from switching to jobs in which they would be better paid and more productive. This harms workers who are subject to non-compete clauses. This also harms other workers in the labor market, since jobs that may be better matches for those workers are filled by workers who are unable to leave their jobs due to non-compete clauses.³⁷⁶ And this harms other firms and potential entrants into the market, who have a more limited pool of workers from which to hire. Regardless of a worker's income or job status, non-compete clauses block workers from switching to jobs in which they would be better paid and more productive—restricting the opportunities of all workers in that labor market.

³⁷⁵ See proposed § 910.3.

³⁷⁶ See *supra* Part II.B.1.

The available data do not allow the Commission to estimate earnings effects for every occupation. However, the evidentiary record indicates non-compete clauses depress wages for a wide range of subgroups of workers across the spectrum of income and job function—from hourly workers to highly paid, highly skilled workers such as executives. The Commission therefore estimates the proposed rule would increase earnings for workers in all of the subgroups of the labor force for which sufficient data is available.³⁷⁷ Excluding these workers from the proposed rule would deny these workers the benefits of higher earnings through increased competition in the market for their labor.

The Commission recognizes there are compelling reasons for banning non-compete clauses that apply more strongly to lower-wage workers. Non-compete clauses for lower-wage workers—such as sandwich shop workers, warehouse workers, or security guards³⁷⁸—may be more likely than non-compete clauses for higher-wage workers to be exploitative and coercive at the time of contracting and at the time of the worker’s potential departure from the employer.³⁷⁹ In addition, the most commonly cited justifications for non-compete clauses appear particularly weak when applied to relatively lower-wage workers, to the extent such workers are less likely to have access to trade secrets or confidential information.³⁸⁰

The Commission believes there are also compelling reasons for banning non-compete clauses that apply more strongly to highly paid or highly skilled workers such as senior executives. As described above, the weight of the available evidence indicates

³⁷⁷ See *infra* Part VII.B.1.a.

³⁷⁸ See *supra* Part II.A (listing illustrative examples of non-compete clauses).

³⁷⁹ See *infra* Part IV.A.1.b–c.

³⁸⁰ See *supra* Part IV.B (describing the most commonly cited justifications for non-compete clauses).

non-compete clauses negatively affect new business formation, innovation, and the ability of competitors to hire skilled workers.³⁸¹ Non-compete clauses for highly paid or highly skilled workers such as senior executives may be contributing more to these harms than non-compete clauses for some other workers, to the extent such workers may be likely to start competing businesses, be hired by potential entrants or competitors, or develop innovative products and services. Non-compete clauses for highly paid or highly skilled workers such as senior executives may also block potential entrants, or raise their costs, to a high degree, because such workers are likely to be in high demand by potential entrants. As a result, prohibiting non-compete clauses for highly paid or highly skilled workers such as senior executives may have relatively greater benefits for consumers than prohibiting non-compete clauses for other workers.

For these reasons, the Commission preliminarily believes a categorical ban on non-compete clauses would best achieve the objective of the proposed rule, which is to remedy the adverse effects of non-compete clauses on competition in labor markets and product and service markets. However, the Commission also believes several alternatives to a categorical ban may also accomplish the objectives of the proposed rule to some degree, including different standards for senior executives. These alternatives are described in detail in Part VI.

The Commission seeks comment on proposed § 910.2(a).

2(b) Existing Non-Compete Clauses

³⁸¹ See *supra* Part II.B.2.b–d.

Proposed § 910.2(b) would clarify employers' obligations, and impose additional requirements, related to non-compete clauses entered into by the employer prior to the compliance date ("existing non-compete clauses").

2(b)(1) Rescission Requirement

Proposed § 910.2(b)(1) would state that, to comply with proposed § 910.2(a)—which states it is an unfair method of competition for an employer to maintain with a worker a non-compete clause—an employer that entered into a non-compete clause with a worker prior to the compliance date must rescind the non-compete clause no later than the compliance date. The reasons why the Commission is proposing this rescission requirement are described above in the section-by-section analysis for proposed § 910.2(a).

The requirements in § 910.2(b)(1)–(3) do not apply where a worker's obligation not to compete elapsed prior to the compliance date. This is because the requirements in § 910.2(b)(1)–(3) derive from § 910.2(a), which establishes it is an unfair method of competition to maintain with a worker a non-compete clause. An employer does not maintain with a worker a non-compete clause, in violation of the Rule, where the obligation not to compete elapsed prior to the compliance date. For example, if a worker left their job in 2019 and was subject to a two-year obligation not to compete, that obligation would have elapsed in 2021, and the employer would not violate the Rule by failing to rescind the non-compete clause.

The Commission seeks comment on proposed § 910.2(b)(1).

2(b)(2) Notice Requirement

Proposed § 910.2(b)(2) would require that the employer provide notice to a worker that the worker's non-compete clause has been rescinded. Proposed § 910.2(b)(2) would have three subparagraphs that would impose various requirements related to the notice.

First, proposed § 910.2(b)(2)(A) would state that an employer that rescinds a non-compete clause pursuant to § 910.2(b)(1) must provide notice to the worker that the worker's non-compete clause is no longer in effect and may not be enforced against the worker. Proposed § 910.2(b)(2)(A) would contain a notice requirement because the Commission believes the available evidence indicates that many workers are not aware of the applicable law governing non-compete clauses or their rights under those laws.³⁸² As a result, if the Commission were to issue a final Non-Compete Clause Rule, many workers who had entered into non-compete clauses may be unaware that, due to the Rule, their employer is no longer permitted to maintain the non-compete clause. As a result, these workers may continue to refrain from leaving their job to work for a competitor or start their own business. This would negatively affect competitive conditions in the same manner the Commission is concerned about.³⁸³ A notice requirement would help address this concern by ensuring workers are informed that their non-compete clause is no longer in effect and may not be enforced against them.

Proposed § 910.2(b)(2)(A) would state further that the employer must provide the notice to the worker in an individualized communication. As such, an employer could not satisfy the notice requirement by, for example, posting a notice at the employer's

³⁸² See Prescott & Starr, *supra* note 57 at 10–11.

³⁸³ See *supra* Part IV.A.1.a.

workplace that workers' non-compete clauses are no longer in effect. Proposed § 910.2(b)(2)(A) would also state that the employer must provide the notice on paper or in a digital format such as, for example, an email or text message. As such, a notice communicated orally would not meet the notice requirement. Allowing employers to provide the notice in a digital format would also reduce compliance costs for employers. Proposed § 910.2(b)(2)(A) would also require the employer to provide the notice to the worker within 45 days of rescinding the non-compete clause.

Second, proposed § 910.2(b)(2)(B) would state that the employer must provide the notice to a worker who currently works for the employer. The Commission believes that most employers have contact information available for their current workers and can use this contact information to provide the notice.

Proposed § 910.2(b)(2)(B) would also state that the employer must provide the notice to a worker who formerly worked for the employer, provided that the employer has the worker's contact information readily available. Providing the notice to former workers may be even more vital than providing the notice to current workers because former workers may be refraining actively from competitive activity because they believe they are subject to a non-compete clause. However, employers may not have contact information readily available for all former workers. Proposed § 910.2(b)(2)(B) would therefore require employers to provide the notice to former workers only where the employer has the worker's contact information readily available. The Commission believes that this requirement would strike the appropriate balance between providing notice to affected workers and minimizing compliance costs for employers.

Third, proposed § 910.2(b)(2)(C) would provide model language that would satisfy the requirement in proposed § 910.2(b)(2)(A) that the employer “provide notice to the worker that the worker’s non-compete clause is no longer in effect and may not be enforced against the worker.” The model language is designed to communicate the relevant information in a simple and straightforward manner. Proposed § 910.2(b)(2)(C) would also clarify that an employer may also use language that is different from the model language, provided that the language communicates to the worker that the worker’s non-compete clause is no longer in effect and may not be enforced against the worker. Proposed § 910.2(b)(2)(C) would reduce compliance costs and increase compliance certainty for employers by providing employers with model language they could use, while simultaneously providing employers with the flexibility to use other language that would communicate the required information.

The Commission seeks comment on proposed § 910.2(b)(2)(A)–(C).

2(b)(3) Safe Harbor

Proposed § 910.2(b)(3) would contain a safe harbor for compliance with the rescission requirement in proposed § 910.2(b)(1). Proposed § 910.2(b)(3) would state that an employer complies with the rescission requirement described in § 910.2(b)(1) where it provides notice to a worker pursuant to § 910.2(b)(2). Consequently, to comply with the rescission requirement for purposes of the Rule, an employer could simply send a notice to a worker that is compliant with proposed § 910.2(b)(2). An employer that does so would not need to take any other steps to comply with the rescission requirement in proposed § 910.2(b)(1). The Commission believes that this safe harbor would strike an

appropriate balance between ensuring that workers receive adequate notice of their rights under the Non-Compete Clause Rule and minimizing compliance costs for employers.

The Commission seeks comment on proposed § 910.2(b)(3).

Section 910.3 Exception

Proposed § 910.3 would exempt certain non-compete clauses between the seller and buyer of a business from coverage under the Rule. Proposed § 910.3 would state that the requirements of the Rule shall not apply to a non-compete clause that is entered into by a person who is selling a business entity or otherwise disposing of all of the person's ownership interest in the business entity, or by a person who is selling all or substantially all of a business entity's operating assets, when the person restricted by the non-compete clause is a substantial owner of, or substantial member or substantial partner in, the business entity at the time the person enters into the non-compete clause. Proposed § 910.3 would also clarify that non-compete clauses covered by this exception would remain subject to federal antitrust law as well as all other applicable law.

The exception in proposed § 910.3 would apply only in a narrow set of circumstances. The Rule, as a whole, would only apply to non-compete clauses between employers and workers.³⁸⁴ As a result, the exception in proposed § 910.3 would apply only where the party restricted by the non-compete clause is a worker (for example, where the seller of a business is going to work for the acquiring business). Where the person restricted by the non-compete clause is not a worker, the Rule would not apply as an initial matter.

³⁸⁴ See proposed § 910.1(b).

The Commission is proposing the exception in § 910.3 because non-compete clauses between the seller and buyer of a business may be unique in certain respects from non-compete clauses arising solely out of employment. Specifically, non-compete clauses between the seller and buyer of a business may be distinct from non-compete clauses that arise solely out of employment because they may help protect the value of the business acquired by the buyer.

This view is consistent with the law of the majority of the states, under which non-compete clauses between the seller and buyer of a business are treated differently from non-compete clauses arising solely out of employment. For example, while non-compete clauses are generally void in California, North Dakota, and Oklahoma, each of these three states exempts non-compete clauses between the seller and buyer of a business from this general rule.³⁸⁵ In the majority of the 47 states that enforce non-compete clauses under some circumstances, non-compete clauses between sellers and buyers of businesses are reviewed under a more lenient standard than non-compete clauses that arise solely out of employment.³⁸⁶ A frequently cited reason for this difference in treatment is that such non-compete clauses implicate an additional interest relative to non-compete clauses that arise solely out of employment: they protect the value of the business acquired by the buyer.³⁸⁷ If non-compete clauses between the seller and buyer of a business help protect the value of the business acquired by the buyer, restricting these types of non-compete clauses could potentially affect business

³⁸⁵ Cal. Bus. & Prof. Code sec. 16601; N.D. Cent. Code sec. 9-08-06(1); Okla. Stat. Ann. tit. 15, secs. 218 (sale of a business) and 219 (dissolution of a partnership).

³⁸⁶ See, e.g., Fla. Stat. Ann. sec. 542.335(1)(d); *Hess Newmark Owens Wolf, Inc. v. Owens*, 415 F.3d 630, 634 (7th Cir. 2005); *Jiffy Lube Int'l, Inc. v. Weiss Bros., Inc.*, 834 F. Supp. 683, 691 (D.N.J. 1993).

³⁸⁷ See, e.g., *Strategix, Ltd. v. Infocrossing West, Inc.*, 142 Cal. App. 4th 1068, 1072–73 (Cal. Ct. App. 4th 2006); *Reed Mill & Lumber Co.*, 165 P.3d at 736; *Bybee*, 178 P.3d at 622.

acquisitions, including the incentives of various market actors to start, sell, or buy businesses.

The Commission further notes that the evidentiary record described above in Part II.B relates primarily to non-compete clauses that arise solely out of employment. Unlike non-compete clauses that arise solely out of employment, there has been little empirical research on the prevalence of non-compete clauses between the seller and buyer of a business. The Commission is also not aware of empirical research on the economic effects of applying additional legal restrictions to these types of non-compete clauses. In part, this is because all states permit non-compete clauses between buyers and sellers of businesses to some degree, and because the laws that apply to these types of non-compete clauses have seen fewer changes recently than the laws that apply to non-compete clauses that arise solely out of employment. As a result, there have been few natural experiments that allow researchers to assess how restricting these types of non-compete clauses may affect competition, including any effects on business acquisitions.

For these reasons, the Commission believes it may be appropriate to exempt non-compete clauses between the seller and buyer of a business from coverage under the Rule. Proposed § 910.3 would clarify, however, that these non-compete clauses would remain subject to federal antitrust law and all other applicable law, including state law requiring non-compete clauses to be tailored to protect a legitimate business interest and to be limited in duration, geographic area, and the scope of activity prohibited.

Exempting non-compete clauses between the seller and buyer of a business from coverage under the Rule would not represent a finding that such non-compete clauses are beneficial to competition. It would simply reflect the Commission's view that it would be

appropriate to tailor the Rule to non-compete clauses that arise solely out of employment—given that non-compete clauses between the seller and buyer of a business may implicate unique interests and have unique effects, and that the evidentiary record does not permit the Commission to assess these potential effects as thoroughly as the potential effects of restricting non-compete clauses that arise solely out of employment.

The exception in proposed § 910.3 would only apply where the seller of the business is a substantial owner of, or substantial member or substantial partner in, the business at the time the person enters into the non-compete clause. Proposed § 910.1(e) would define substantial owner, substantial member, or substantial partner as an owner, member, or partner holding at least a 25% ownership interest in a business entity. The exception would therefore not allow non-compete clauses to be applied to a business’s workers in connection with the sale of a business, where those workers are not substantial owners, members, or partners. The reasons for this proposed 25% threshold are described above in the section-by-section analysis for proposed § 910.1(e).

The Commission seeks comment on proposed § 910.3.

Section 910.4 Relation to State Laws

The Supremacy Clause of the U.S. Constitution provides that the Constitution, and the laws of the United States made pursuant to the Constitution, “shall be the supreme Law of the Land.”³⁸⁸ Hence, federal law preempts any state law that conflicts with the exercise of federal power.³⁸⁹ Such conflict preemption occurs either “where it is impossible for a private party to comply with both state and federal law” or where state

³⁸⁸ U.S. Const. art. VI, cl. 2.

³⁸⁹ *Fid. Fed. Sav. & Loan Ass’n v. de la Cuesta*, 458 U.S. 141, 153 (1982) (citing roots in the Supremacy Clause); *McCulloch v. Md.*, U.S. Supreme Court, 4 Wheat 159 (1819) (citing the Supremacy Clause and the Necessary and Proper Clause (Article I, Section 8, clause 18)).

law “stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.”³⁹⁰ Congressional intent to preempt state law can be expressed in the statutory language itself (express preemption) or implied in the structure and purpose of federal law (implied preemption).³⁹¹ Federal regulations “have no less pre-emptive effect than federal statutes,”³⁹² and agencies themselves, implementing federal statutes, can expressly preempt conflicting state laws and regulations.³⁹³

In some instances, a federal law may fully preempt contrary state laws. In others, federal law may impliedly or expressly respect the continuing and concurrent exercise of state power, thus setting a regulatory “floor” but not a “ceiling.”³⁹⁴ The Commission notes that “Congress intended the federal antitrust laws to supplement, not displace, state antitrust remedies.”³⁹⁵

The proposed rule would contain an express preemption provision. Proposed § 910.4 would provide that the Rule shall supersede any state statute, regulation, order, or interpretation to the extent that such statute, regulation, order, or interpretation is inconsistent with the Rule.³⁹⁶ Proposed § 910.4 would further provide that a state statute, regulation, order, or interpretation is not inconsistent with the provisions of the Rule if the protection such statute, regulation, order, or interpretation affords any worker is greater than the protection provided under the Rule.

³⁹⁰ *Crosby v. Nat’l Foreign Trade Council*, 530 U.S. 363, 372–73 (2000).

³⁹¹ *Cipollone v. Liggett Grp., Inc.*, 505 U.S. 504, 516 (1992); *Jones v. Rath Packing Co.*, 430 U.S. 519, 525 (1977).

³⁹² *Fid. Fed. Sav. & Loan Ass’n*, 458 U.S. at 153.

³⁹³ *Id.*; see also *U.S. v. Shimer*, 367 U.S. 374, 383 (1961).

³⁹⁴ See, e.g., *Oneok, Inc. v. Learjet, Inc.*, 575 U.S. 373, 384–85 (2015).

³⁹⁵ *Cal. v. ARC Am. Corp.*, 490 U.S. 93, 102 (1989).

³⁹⁶ In this Part V, we refer to state statutes, regulations, orders, or interpretations as “state laws” for ease of reference.

This preemption provision would reflect the Commission’s intent that the Non-Compete Clause Rule establish a regulatory floor, not a ceiling. Under the proposed preemption provision, state laws that are inconsistent with the Rule would be preempted. One example would be a state law providing that an employer may enforce a non-compete clause against a worker where the non-compete clause is tailored to a legitimate business interest and reasonably limited in duration, geographic area, and scope of activity prohibited. Such a law would be inconsistent with proposed § 910.2(a), which would state that it is an unfair method of competition—and therefore a violation of Section 5 of the FTC Act—for an employer to enter into, attempt to enter into, or maintain a non-compete clause with a worker. Under proposed § 910.4, proposed § 910.2(a) would preempt the contrary state law to the extent that it conflicts with proposed § 910.2(a).

However, under the second sentence of proposed § 910.4, a state law would not conflict with the provisions of the Rule if the state law afforded greater protection to the worker than the protection provided under the Rule. For example, as noted above, proposed § 910.3 would exempt certain non-compete clauses between the seller and buyer of a business from coverage under the Rule. If a state were to prohibit employers from entering into, attempting to enter into, or maintaining all non-compete clauses—including non-compete clauses between the seller and buyer of a business—an employer could comply with both the state law and the Rule by not entering into, attempting to enter into, or maintaining non-compete clauses between the seller and buyer of a business.

The Commission seeks comment on proposed § 910.4.

Section 910.5 Compliance Date

The proposed rule would establish a separate effective date and compliance date. Under proposed § 910.5, the proposed rule’s effective date would be the date that is 60 days after the final rule is published in the *Federal Register*. The proposed rule’s compliance date would be the date that is 180 days after the final rule is published in the *Federal Register*. In this NPRM, the Commission refers to the 180-day period between the publication of the final rule and the compliance date as the “compliance period.”

Compliance with § 910.2(a). The Commission expects that employers would need to undertake the following two types of tasks during the compliance period to be prepared to comply with § 910.2(a) starting on the compliance date. First, starting on the compliance date, employers would be prohibited from maintaining existing non-compete clauses (*i.e.*, non-compete clauses that the employer entered into with a worker prior to the compliance date).³⁹⁷ As a result, during the compliance period, an employer would need to assess whether to implement replacements for existing non-compete clauses, such as NDAs; draft those covenants; and then negotiate and enter into those covenants with the relevant workers. Second, an employer would be prohibited from entering into new non-compete clauses starting on the compliance date.³⁹⁸ As a result, during the compliance period, employers would need to, for example, remove any non-compete clauses from employment contracts that they provide to new workers. The Commission believes that 180 days—or approximately six months—would be enough time for employers to accomplish each of these two tasks.

³⁹⁷ See proposed § 910.2(a).

³⁹⁸ *Id.*

Compliance with § 910.2(b)(1)–(3). To comply with § 910.2(b)(1)–(3) starting on the compliance date, an employer would be required to rescind, no later than the compliance date, any non-compete clauses that it entered into prior to the compliance date.³⁹⁹ Where an employer rescinds a non-compete clause, the employer would be required to provide notice to the worker that the worker’s non-compete clause is no longer in effect and may not be enforced against the worker.⁴⁰⁰ This notice may be provided in a digital format, such as an email or text message.⁴⁰¹ The Rule would require the employer to provide the notice to the worker within 45 days of rescinding the non-compete clause.⁴⁰² Employers would be required to provide the notice to current workers, as well as former workers where the employer has the former worker’s contact information readily available.⁴⁰³ To reduce compliance costs, the Rule would provide model language that employers may use for the notice.⁴⁰⁴ However, employers would have the flexibility to use language other than the model language, provided that it communicates to the worker that the worker’s non-compete clause is no longer in effect and may not be enforced against the worker.⁴⁰⁵ The Rule would also provide a safe harbor that would allow an employer to comply with the Rule’s rescission requirement by providing a compliant notice.⁴⁰⁶ The Commission believes that this would significantly reduce compliance costs. The Commission believes that the 180-day compliance period

³⁹⁹ See proposed § 910.2(b)(1).

⁴⁰⁰ See proposed § 910.2(b)(2)(A)–(C).

⁴⁰¹ See proposed § 910.2(b)(2)(A).

⁴⁰² *Id.*

⁴⁰³ *Id.*

⁴⁰⁴ See proposed § 910.2(b)(2)(C).

⁴⁰⁵ *Id.*

⁴⁰⁶ See proposed § 910.2(b)(3).

would provide employers with sufficient time to prepare to rescind existing non-compete clauses no later than the compliance date.

The Commission is proposing an effective date of 60 days after publication of the final rule in the *Federal Register* because it expects that the final rule would likely be a major rule under the Congressional Review Act (CRA). Under the CRA, a “major rule” may not take effect fewer than 60 days after the rule is published in the *Federal Register*.⁴⁰⁷ The CRA further states that a rule is a “major rule” if it has an annual effect on the economy of \$100 million or more.⁴⁰⁸ The Commission believes that the impacts of the proposed rule, if finalized, would be large enough that the final rule would be a major rule under the CRA.⁴⁰⁹

The Commission seeks comment on proposed § 910.5.

VI. Alternatives to the Proposed Rule

In this Part VI, the Commission describes alternatives to the proposed rule.⁴¹⁰ This Part VI addresses the alternatives related to the rule’s fundamental design. These alternatives flow from two key questions: (1) whether the rule should impose a categorical ban on non-compete clauses or a rebuttable presumption of unlawfulness, and (2) whether the rule should apply uniformly to all workers or whether there should be exemptions or different standards for different categories of workers. The different

⁴⁰⁷ 5 U.S.C. 801(a)(3)(A).

⁴⁰⁸ 5 U.S.C. 804(2).

⁴⁰⁹ See *infra* Part VII (analyzing the costs and benefits of the proposed rule).

⁴¹⁰ The Commission intends for this Part VI to satisfy the requirements in Section 22 of the FTC Act that, in an NPRM, the Commission issue a preliminary regulatory analysis that shall contain “a description of any reasonable alternatives to the proposed rule which may accomplish the stated objective of the rule in a manner consistent with applicable law” and “a preliminary analysis of the effectiveness of the proposed rule and each alternative in meeting the stated objectives of the proposed rule.” 15 U.S.C. 57b-3(b)(1)(B)–(C).

permutations of the answers to each of these questions yield the different alternatives for the rule’s fundamental design.

This Part VI does not generally address alternatives related to the design of specific regulatory provisions. For example, proposed § 910.1(e) defines a substantial owner, substantial member, or substantial partner as an owner, member, or partner holding at least a 25% ownership interest in a business entity. In a final rule, the Commission could set this standard at a different percentage level—for example, 50% or 10%. The Commission seeks comment on these types of granular questions not in this Part VI, but in the section-by-section analysis for the relevant provision in Part V above.

A. Two Key Dimensions of Alternatives

In Part IV above, the Commission preliminarily finds that the use of non-compete clauses by employers is an “unfair” method of competition under Section 5. For workers who are not senior executives, the Commission preliminarily finds that non-compete clauses are “unfair” under Section 5 in three independent ways. First, the use by employers of non-compete clauses is restrictive conduct that negatively affects competitive conditions. Second, non-compete clauses are exploitative and coercive at the time of contracting while burdening a not insignificant volume of commerce. Third, non-compete clauses are exploitative and coercive at the time of the worker’s potential departure from the employer while burdening a not insignificant volume of commerce.⁴¹¹

For workers who are senior executives, the Commission preliminarily finds that the use by employers of non-compete clauses is “unfair” under Section 5 because such non-compete clauses are restrictive conduct that negatively affects competitive

⁴¹¹ See *supra* Part IV.A.1. The Commission also preliminarily finds that non-compete clauses are a “method of competition.” See *supra* Part IV.A.2.

conditions. Indeed, as described above in Part IV.A.1.a.ii, the Commission preliminarily believes that non-compete clauses for senior executives may harm competition in product markets in unique ways. (The second and third preliminary findings described above—that non-compete clauses are exploitative and coercive at the time of contracting and at the time of a worker’s potential departure—do not apply to senior executives.) In Part IV, the Commission seeks comment on whether this different unfairness analysis should also apply to highly paid or highly skilled workers who are not senior executives.

The objective of the proposed rule is to remedy these adverse effects from the use of non-compete clauses. The proposed rule would seek to accomplish this objective by prohibiting an employer from entering into or attempting to enter into a non-compete clause with a worker; maintaining with a worker a non-compete clause; and, under certain circumstances, representing to a worker that the worker is subject to a non-compete clause.⁴¹²

The proposed rule would ban non-compete clauses categorically, with a limited exception for certain non-compete clauses between the seller and buyer of a business.⁴¹³ In Part V, the Commission explains why it is proposing a categorical ban on non-compete clauses.⁴¹⁴

There are two key dimensions of alternatives related to the rule’s fundamental design. First, instead of a categorical ban, the Commission could adopt a rebuttable

⁴¹² See proposed § 910.2(a). For ease of reference, this Part VI employs the term “use of non-compete clauses” to refer to the specific conduct that the proposed rule would prohibit.

⁴¹³ See proposed § 910.3. As described in Part V (in the section-by-section analysis for proposed § 910.1(c)), the proposed rule would also not apply to employers to the extent they are exempt under Section 5(a)(2) of the FTC Act, and the proposed rule may not apply under certain circumstances due to the state action doctrine.

⁴¹⁴ See *supra* Part V, in the section-by-section analysis for proposed § 910.2(a).

presumption of unlawfulness. Under this approach, it would be presumptively unlawful for an employer to use a non-compete clause, but the use of a non-compete clause would be permitted if the employer could meet a certain evidentiary burden, based on a standard that would be articulated in the rule. Second, instead of applying to all workers uniformly, the Rule could include exemptions or different standards for different categories of workers. These exemptions or different standards could be based on a worker's job functions, earnings, another factor, or some combination of factors.

1. Categorical Ban vs. Rebuttable Presumption

The Commission could adopt a rebuttable presumption of unlawfulness instead of a categorical ban. Under this approach, it would be presumptively unlawful for an employer to use a non-compete clause. However, the use of a non-compete clause would be permitted if the employer could meet a certain evidentiary burden, based on a standard that would be articulated in the rule. The rationale behind this approach would be that prohibiting employers from using non-compete clauses is an appropriate default rule in light of the adverse effects on competition from their use in the aggregate; however, there may be specific sets of facts under which their use may be justified, so it would be appropriate to permit employers to use them in those cases.

Conceptually, the rebuttable presumption approach would be similar to “quick look” analysis under antitrust law. In antitrust cases, most restraints are analyzed under the rule of reason, which entails an intensive, fact-specific assessment of market power and market structure to determine a restraint's actual effect on competition.⁴¹⁵ However, where “the great likelihood of anticompetitive effects can be easily ascertained,” a court

⁴¹⁵ See, e.g., *Am. Express Co.*, 138 S. Ct. at 2284.

may also adopt a truncated, or “quick look,” rule of reason analysis.⁴¹⁶ Courts apply quick look analysis where, “based upon economic learning and the experience of the market, it is obvious that a restraint of trade likely impairs competition.”⁴¹⁷ In such cases, “the restraint is presumed unlawful and, in order to avoid liability, the defendant must either identify some reason the restraint is unlikely to harm consumers or identify some competitive benefit that plausibly offsets the apparent or anticipated harm.”⁴¹⁸ A rebuttable presumption in the Rule would mirror this approach. Non-compete clauses would be presumed unlawful, based on the “economic learning and experience of the market” summarized in Part IV above, but the use of a non-compete clause would be permitted if the employer could make a showing that satisfies a certain standard.

The rebuttable presumption approach would also be similar in many respects to the current common law governing non-compete clauses. In most states, non-compete clauses are disfavored, but are permitted if an employer can identify a legitimate business interest and if the non-compete clause is reasonable with respect to geographic area, duration, and the scope of activity prohibited.⁴¹⁹ Similarly, under the rebuttable presumption approach, non-compete clauses would be presumptively unlawful but would be permitted under certain circumstances.

One important question related to the rebuttable presumption approach is what the test for rebutting the presumption should be. The Commission preliminarily believes that, if it were to adopt a rebuttable presumption in a final rule, it would adopt a test that is

⁴¹⁶ See, e.g., *Calif. Dental Ass’n v. Fed. Trade Comm’n*, 526 U.S. 756, 770 (1999).

⁴¹⁷ *Polygram Holding, Inc. v. Fed. Trade Comm’n*, 416 F.3d 29, 36 (D.C. Cir. 2005).

⁴¹⁸ *Id.*

⁴¹⁹ See *supra* Part II.C.1.

more restrictive than the current common-law standard. Otherwise, the Rule would be no more restrictive than current law, and the objective of the Rule—to remedy the adverse effects to competition from employers’ use of non-compete clause—would not be achieved.

One option would be a test derived from the quick look test. For example, the rule could allow an employer to rebut the presumption where the employer “shows by clear and convincing evidence that the non-compete clause is unlikely to harm competition in labor markets or product or service markets, or identifies some competitive benefit that plausibly outweighs the apparent or anticipated harm.” Alternatively, the test could focus exclusively on either of these two prongs: unlikelihood of harm to competition, or presence of a competitive benefit that plausibly outweighs the apparent or anticipated harm to competition. A term other than “clear and convincing evidence,” such as “preponderance of the evidence,” could also be used.

Another option would be a test that piggybacks on state law. For example, the rule could allow an employer to rebut the presumption where the employer “shows by clear and convincing evidence that a non-compete clause is necessary to protect a legitimate business interest.” This would be a higher standard than the current common law test because it would require an employer to show not only that it has a “legitimate business interest” under state law, but that it cannot protect this interest in another way—for example, through the use of an NDA. The test could also use the term “reasonably necessary” instead of “necessary,” or a term other than “clear and convincing evidence, such as “preponderance of the evidence.” The Commission could also establish what “legitimate business interests” could justify a non-compete clause and which could not.

The Commission preliminarily believes the categorical ban in the proposed rule would advance the proposed rule’s objectives to a greater degree than the rebuttable presumption approach. The Commission is concerned that the rebuttable presumption approach could foster confusion among employers and workers because the question of whether an employer may use a non-compete clause would depend on an abstract legal test rather than a bright-line rule. Under a categorical ban, it would be clear non-compete clauses are prohibited. In contrast, under the rebuttable presumption approach, it may be difficult for both employers and workers to know whether a particular non-compete clause meets the abstract legal test articulated in the rule. For example, it may be difficult for an employer or worker to know whether a particular non-compete clause is “unlikely to harm competition in labor markets or product or service markets,” whether “there is some competitive benefit that plausibly outweighs the apparent or anticipated harm,” or whether a non-compete clause is “necessary” to protect a legitimate business interest. Furthermore, because only the Commission can enforce a rule issued under Section 6(g), the development of the law—and therefore clarity for employers—would be slow in coming.

However, the rebuttable presumption could also have some advantages over a categorical ban. If there were to be specific factual scenarios, unanticipated by the Commission, in which a particular non-compete clause did not implicate the anticompetitive concerns the Commission is concerned about, the rebuttable presumption would allow the clause to be used.

The Commission seeks comment on whether it should adopt a rebuttable presumption instead of a categorical ban and what the test for rebutting the presumption should be.

2. Uniform Rule vs. Differentiation

In addition to establishing a categorical ban on non-compete clauses, the proposed rule would apply uniformly to all workers. Employers covered by the rule—*i.e.*, employers other than those exempt from coverage under the FTC Act⁴²⁰—would be prohibited from using a non-compete clause with a worker, except in limited scenarios where the non-compete clause is between the seller and buyer of a business.⁴²¹

Rather than applying a rule uniformly to all workers, the Commission could apply different rules to different categories of workers based on a worker’s job function, occupation, earnings, another factor, or some combination of factors. For example, the rule could ban non-compete clauses for workers generally, but could apply a rebuttable presumption to non-compete clauses for workers whose earnings are above a certain threshold (or could exempt such workers altogether).

This Part VI uses the term “more-lenient standards” to refer to the more relaxed regulatory standards that would apply to certain categories of workers—such as the workers above the earnings threshold in the example above—under this approach. This Part VI also uses the term “more-stringent standards” to refer to the stricter standards that would apply to certain categories of workers, such as the workers below the earnings threshold in the second example above.

⁴²⁰ See *supra* Part V, in the section-by-section analysis for proposed § 910.1(c), for additional discussion of this issue.

⁴²¹ See proposed § 910.3.

As described above in Part II.C.1, the recent non-compete clause statutes many states have enacted have generally differentiated among categories of workers. Most of these states have restricted non-compete clauses only for workers below a threshold based on the worker's earnings or a similar factor, such as whether the worker is non-exempt under the FLSA or whether the worker is an hourly worker.⁴²²

There are three main ways a rule could differentiate among workers. First, a rule could apply different standards to workers based on the workers' job functions or occupations. For example, a rule could apply more-lenient standards to non-compete clauses for senior executives or could exempt them from coverage altogether.

Second, a rule could apply different standards to workers based on some combination of job functions/occupations and a worker's earnings. For example, the rule could apply more-lenient standards to workers who qualify for the FLSA exemptions for "executives" and "learned professionals."⁴²³ Workers qualify for these FLSA exemptions (which exempt the worker from minimum-wage and overtime-pay rules) if they earn above a certain amount and perform certain types of job duties.⁴²⁴ Another potential alternative could be to apply more-lenient standards to a worker who qualifies for any FLSA exemption.⁴²⁵

Third, like the recent state statutes described above, a rule could apply different standards based on the worker's earnings. An earnings threshold could be relatively high (as in, *e.g.*, the State of Washington, where a non-compete clause is void unless the

⁴²² See *supra* Part II.C.1.

⁴²³ See 29 CFR 541.100; 29 CFR 541.200.

⁴²⁴ See Dep't of Labor, *Fact Sheet #17A: Exemption for Executive, Administrative, Professional, Computer & Outside Sales Employees Under the Fair Labor Standards Act (FLSA)* (Sept. 2019).

⁴²⁵ See Dep't of Labor, *Handy Reference Guide to the Fair Labor Standards Act*, entry under Exemptions, <https://www.dol.gov/agencies/whd/compliance-assistance/handy-reference-guide-flsa#8>.

worker's annual earnings exceed \$100,000 for employees and \$250,000 for independent contractors); in the middle (as in, *e.g.*, Virginia, where employers may not enter into, enforce, or threaten to enforce a non-compete clause with a worker whose average weekly earnings are less than the Commonwealth's average weekly wage); or relatively low (as in, *e.g.*, Maryland, where non-compete clauses are void where a worker earns equal to or less than \$15 per hour or \$31,200 per year).⁴²⁶ The Commission also believes if it were to adopt a threshold based on earnings, it would be appropriate to index the earnings level to inflation, to ensure as well as possible that the threshold continues to correspond to the Commission's justification for it.

A rule could also differentiate among workers based on a different factor, or based on some combination of factors.

The Commission preliminarily concludes applying the rule uniformly to all workers would advance the proposed rule's objectives to a greater degree than differentiating among workers. As described in Part V above, non-compete clauses obstruct labor market competition in a similar way for all workers, regardless of a worker's income or job status.⁴²⁷ Whether a labor market includes high earners or low-wage workers, non-compete clauses block workers in that market from switching to jobs in which they would be better paid and more productive—restricting the opportunities of all workers in that labor market. The Commission estimates the proposed rule would increase earnings for workers across the labor force, as well as for workers in all of the subgroups of the labor force for which sufficient data are available—from hourly workers

⁴²⁶ See *supra* note 149 and accompanying text.

⁴²⁷ See *supra* Part V (in the section-by-section analysis for proposed § 910.2(a)).

to highly paid, highly skilled workers such as executives.⁴²⁸ Excluding these workers from the proposed rule would deny these workers the benefits of higher earnings through increased competition in the market for their labor.

The Commission also preliminarily concludes a rule that applies uniformly to all workers would better ensure workers are aware of their rights under the rule. For example, the Commission believes employers generally know whether a particular worker is exempt under the FLSA, but many workers may not know this themselves. Therefore, if the Rule were to prohibit non-compete clauses with FLSA non-exempt workers, and an employer were to enter into a non-compete clause with an FLSA non-exempt worker in violation of the Rule, the worker may not know whether the non-compete clause is valid.

If the Commission were to adopt a final rule differentiating among categories of workers, it may also adopt a severability clause indicating the Commission intends for the standards to be severable.⁴²⁹ If a regulatory provision is severable, and one part of the provision is invalidated by a court, the court may allow the other parts of the provision to remain in effect.⁴³⁰ When analyzing whether a provision is severable, courts consider both (a) the agency's intent and (b) whether severing the invalid parts of the provision would impair the function of the remaining parts.⁴³¹ Including a severability clause would clarify the Commission's intent that, if a court were to invalidate the standards for one category of workers, the other standards would remain in effect. The Commission

⁴²⁸ See *infra* Part VII.B.1.a.

⁴²⁹ The Commission may adopt a severability clause even if it did not apply different standards to the different categories of workers.

⁴³⁰ See, e.g., *Davis Cnty. Solid Waste Mgmt. v. EPA*, 108 F.3d 1454, 1459 (D.C. Cir. 1997).

⁴³¹ *Id.* at 1460.

also believes if it were to adopt a final rule differentiating between categories of workers, and a court were to strike down the rules for one category, that would not impair the function of the remaining provisions. If every worker falls into only one category, and one or more (but not all) of the standards were to be invalidated, an employer could simply comply with the standards that remain in effect.

The Commission seeks comment on whether it should differentiate between workers rather than adopting a rule that applies uniformly to all workers. In addition, the Commission seeks comment on what the specific threshold(s) should be.

B. Discrete Alternatives

As described above, there are two key dimensions of alternatives related to the fundamental design of the rule. The first is whether the rule should impose a categorical ban on non-compete clauses or a rebuttable presumption of unlawfulness. The second is whether the rule should apply uniformly to all workers or whether there should be exemptions or different standards for different categories of workers, using one or more thresholds based on a worker's job functions, earnings, some other factor, or some combination of factors. The different permutations of the answers to each of these questions yield the different alternatives for the rule's fundamental design. As a result, the number of potential alternatives to the proposed rule is nearly limitless. However, for the purpose of focusing public comment, this Part VI.B describes four discrete alternatives to the proposed rule. The Commission preliminarily believes each of these alternatives may further the objectives of the proposed rule, to some degree.

For each of the alternatives described below, the Commission could adopt a variety of different thresholds. As described above in Part VI.A.2, a threshold could be

based on job functions, the worker's occupation, earnings, some other factor, or some combination of factors. A threshold could be set relatively high, relatively low, or in the middle.

1. Alternative #1: Categorical Ban Below Threshold, Rebuttable Presumption Above

Under Alternative #1, the rule would categorically ban the use of non-compete clauses for some workers and apply a rebuttable presumption of unlawfulness to non-compete clauses for the other workers. For example, the rule could ban non-compete clauses generally, but apply a rebuttable presumption to workers who qualify for the FLSA exemptions for executives or learned professionals.⁴³² Or the rule could ban non-compete clauses but apply a rebuttable presumption to workers who earn more than \$100,000 per year.

The Commission is not proposing this approach due to the preliminary concerns, described above in Parts VI.A.1 and VI.A.2, about the rebuttable presumption approach and about differentiating among categories of workers. However, the Commission seeks comment on this alternative.

2. Alternative #2: Categorical Ban Below Threshold, No Requirements Above

Under Alternative #2, the rule would categorically ban the use of non-compete clauses for some workers and not apply any requirements to the other workers. In effect, the other workers would simply be exempt from coverage under the rule. This approach would be similar to the recent non-compete clause statutes many states have enacted.⁴³³ For example, like the recent State of Washington statute, the rule could prohibit the use

⁴³² See *supra* note 423–424 and accompanying text.

⁴³³ See *supra* note 149.

of non-compete clauses for employees earning \$100,000 or less per year and independent contractors earning less than \$250,000 or less per year. Or, like the recent Massachusetts and Rhode Island statutes, the rule could prohibit the use of non-compete clauses for workers who are non-exempt under the FLSA.

The Commission is not proposing this approach due to its preliminary concerns, described above in Part VI.A.2, about differentiating among categories of workers. However, the Commission seeks comment on this alternative.

3. Alternative #3: Rebuttable Presumption for All Workers

Under Alternative #3, the rule would apply a rebuttable presumption of unlawfulness to non-compete clauses for all workers. This approach would be similar to the proposed rule in that it would apply uniformly to all U.S. workers. However, instead of a categorical ban, the rule would apply a rebuttable presumption. The Commission is not proposing this approach due to its preliminary concerns with the rebuttable presumption approach, which are described above in Part VI.A.1. However, the Commission seeks comment on this alternative.

4. Alternative #4: Rebuttable Presumption Below Threshold, No Requirements Above

Under Alternative #4, the rule would apply a rebuttable presumption of unlawfulness to non-compete clauses for some workers and not apply any requirements to the other workers. This approach would be similar to Alternative #2, except that, instead of categorically banning non-compete clauses for workers below the threshold, the rule would apply a rebuttable presumption. The Commission is not proposing this approach due to the preliminary concerns, described above in Parts VI.A.1 and VI.A.2,

about the rebuttable presumption approach and about differentiating among categories of workers. However, the Commission seeks comment on this alternative.

The Commission seeks comment on each of these alternatives described in this Part VI.B, including whether the alternative would advance the objectives of the proposed rule to a greater or lesser degree than the proposed rule, and how the Commission should design the rule if it were to adopt the alternative.

C. Different Standards for Senior Executives

In addition to seeking comment generally on whether the rule should apply uniformly to all workers or differentiate between categories of workers,⁴³⁴ the Commission seeks comment specifically on whether it should adopt different standards for non-compete clauses with senior executives.⁴³⁵

The proposed rule would categorically ban non-compete clauses for all workers, including senior executives. However, the Commission recognizes non-compete clauses for senior executives may present distinct concerns. As described in Part IV, the Commission preliminarily finds that, like non-compete clauses for other workers, non-compete clauses for senior executives negatively affect competitive conditions in labor markets.⁴³⁶ The Commission also preliminarily finds non-compete clauses for senior executives negatively affect competitive conditions in product and service markets, and they may do so in unique ways.⁴³⁷ However, unlike non-compete clauses for other workers, the Commission does not preliminarily find non-compete clauses for senior

⁴³⁴ See *supra* Part VI.A.2.

⁴³⁵ The Commission could also define senior executives as a separate category, but apply the same standards to senior executives as to other workers.

⁴³⁶ See *supra* Part IV.A.1.a.i.

⁴³⁷ See *supra* Part IV.A.1.a.ii.

executives are exploitative and coercive at the time of contracting or at the time of the worker's potential departure.⁴³⁸

Given that non-compete clauses for senior executives may present distinct concerns, the Commission is interested in the public's views about whether different standards for senior executives would be appropriate. For example, the Commission could adopt a categorical ban on non-compete clauses for workers in general, but apply a rebuttable presumption of unlawfulness for senior executives or exempt senior executives altogether.

The Commission seeks comment on how, if the Commission were to adopt different standards for senior executives, this category of workers should be defined. The Commission is not aware of a generally accepted legal definition of "senior executive." This term may be challenging to define, given the variety of organizational structures used by employers. The Commission could cross-reference a definition in an existing federal regulation, such as the definition of "named executive officer" in Securities and Exchange Commission (SEC) Regulation S-K⁴³⁹ or the definition of "executive officers" in SEC Rule 3b-7;⁴⁴⁰ adopt a definition closely based on a definition in an existing federal regulation; adopt a new definition; define the category according to a worker's earnings; use some combination of these approaches; or use a different approach. The Commission seeks comment on what definition would draw the appropriate line—with respect to which workers should be covered by the different standards—while providing sufficient clarity to employers and workers.

⁴³⁸ See *supra* Part IV.A.1.b–c.

⁴³⁹ 17 CFR 229.402(a)(3).

⁴⁴⁰ 17 CFR 203.501(f).

In addition, the Commission seeks comment on whether these different standards should also be applied to other highly paid or highly skilled workers who are not senior executives, including specifically how such a category should be defined.

D. Coverage of Non-Compete Clauses Between Franchisors and Franchisees

The proposed rule would state the term “worker” does not include a franchisee in the context of a franchisee-franchisor relationship.⁴⁴¹ As a result, the proposed rule would not cover non-compete clauses between franchisors and franchisees.⁴⁴² As described above in Part V, the Commission believes that, in some cases, the relationship between a franchisor and franchisee may be more analogous to the relationship between two businesses than the relationship between an employer and a worker. In addition, the evidentiary record before the Commission relates primarily to non-compete clauses that arise solely out of employment; the Commission has surveyed the available evidence relating to non-compete clauses and is not aware of research on the effects of applying additional legal restrictions to non-compete clauses between franchisors and franchisees. Therefore, the Commission believes it is appropriate to clarify that a franchisee—in the context of a franchisor-franchisee relationship—is not a “worker” for purposes of proposed § 910.1(f).⁴⁴³ (Proposed § 910.1(f) would explain, however, the term “worker” includes a natural person who works for the franchisee or franchisor, and non-compete clauses between franchisors and franchisees would remain subject to federal antitrust law as well as all other applicable law.)

⁴⁴¹ See proposed § 910.1(f).

⁴⁴² For ease of reference, this Part VI refers to these types of non-compete clauses as “franchisor/franchisee non-compete clauses.”

⁴⁴³ See *supra* Part V (in the section-by-section analysis for proposed § 910.1(f)).

While the Commission is not currently proposing to cover franchisor/franchisee non-compete clauses for these reasons, the Commission recognizes that, in some cases, these non-compete clauses may present concerns under Section 5 similar to the concerns presented by non-compete clauses between employers and workers. Many franchise agreements may contain non-compete clauses.⁴⁴⁴ By restricting a franchisee's ability to start a new business, franchisor/franchisee non-compete clauses could potentially stifle new business formation and innovation, reduce the earnings of franchisees, and have other negative effects on competitive conditions similar to non-compete clauses between employers and workers. Franchisor/franchisee non-compete clauses could also potentially be exploitative and coercive in some cases, such as where there is an imbalance of bargaining power between the parties. While the relationship between franchisors and franchisees may, in some cases, be more analogous to a business-to-business relationship, many franchisees lack bargaining power in the context of their relationship with franchisors and may be susceptible to exploitation and coercion through the use of non-compete clauses.⁴⁴⁵

For these reasons, the Commission seeks comment on whether the Rule should cover franchisor/franchisee non-compete clauses and why. The Commission also seeks comment on whether, if the Rule were to cover franchisor/franchisee non-compete clauses, they should be categorically banned or subject to a rebuttable presumption of

⁴⁴⁴ See, e.g., Brian Callaci, Sergio Pinto, Marshall Steinbaum, & Matthew Walsh, *Vertical Restraints and Labor Markets in Franchised Industries* (July 6, 2022), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4155571 (finding that, in a sample of 530 franchising contracts, various types of vertical restraints were prevalent, while not specifically addressing non-compete clauses). The Commission has also frequently encountered non-compete clauses in franchise agreements. See *supra* Part II.D (describing consent orders that restricted a franchisor's ability to enforce non-compete clauses).

⁴⁴⁵ See, e.g., Brian Callaci & Sandeep Vaheesan, *Antitrust Remedies for Fissured Work*, Cornell L. Rev. (forthcoming), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4076274 at 21–22.

unlawfulness (and if the latter, what the standard for rebutting the presumption should be). The Commission further seeks comment on whether, if the rule were to cover franchisor/franchisee non-compete clauses, the rule should apply uniformly to all such non-compete clauses or whether certain categories of franchisor/franchisee non-compete clauses should be exempted or subject to different standards. The Commission encourages commenters to submit data or other evidence that could inform the Commission's consideration of this issue.

E. Other Alternatives

This Part VI.E describes two alternatives the Commission believes would likely not further the objectives of the proposed rule. However, this assessment is preliminary. Based on the public comments and the Commission's additional analysis, the Commission could potentially decide to adopt one or both of the alternatives described below in a final rule instead of, or in addition to, the proposed rule or one of the alternatives described above. The Commission seeks comment on each of the two alternatives described in this Part VI.E, as well as whether there are other alternatives not described in Part VI that the Commission should consider.

1. Disclosure Rule

The Commission could potentially adopt disclosure requirements related to non-compete clauses.⁴⁴⁶ For example, research suggests many workers often do not find out about non-compete clauses until after they have accepted an employment offer.⁴⁴⁷ This concern could be addressed by requiring an employer to disclose to a worker, before

⁴⁴⁶ The Commission's Franchise Rule requires non-compete clauses to be disclosed to a franchisee. 16 CFR 436(i); 436(q).

⁴⁴⁷ Marx (2011), *supra* note 55 at 706.

making the employment offer, that the worker will be subject to a non-compete clause. The employer could also potentially be required to explain the terms of the non-compete clause and how the worker would be affected by signing the non-compete clause.

While there is evidence disclosure of non-compete clauses to workers prior to acceptance of a job offer may increase earnings, increase rates of training, and increase job satisfaction for that worker,⁴⁴⁸ the Commission does not believe this alternative would achieve the objectives of the proposed rule. Merely ensuring workers are informed about non-compete clauses would not address one of the Commission’s central concerns: that, in the aggregate, they are negatively affecting competitive conditions in labor markets—including impacts on workers who are not bound by non-compete clauses—and in markets for products and services. Moreover, the benefits of a disclosure rule may be limited due to the differential in bargaining power between many workers and their employers, which would hamper those workers’ ability to negotiate for better employment terms.⁴⁴⁹

2. Reporting Rule

The Commission could also potentially require employers to report certain information to the Commission relating to their use of non-compete clauses. For example, employers that use non-compete clauses could be required to submit a copy of the non-compete clause to the Commission. This would enable the Commission to monitor the

⁴⁴⁸ Starr, Prescott, and Bishara, *supra* note 42 at 75.

⁴⁴⁹ See *supra* Part IV.A.1.b.

use of non-compete clauses. It would also potentially discourage employers from using non-compete clauses where they are clearly not justified under existing law.

However, the Commission does not believe a reporting rule would achieve the objectives of the proposed rule. Merely requiring employers to submit their non-compete clauses to the Commission may not meaningfully reduce the prevalence of non-compete clauses. As a result, it may not remedy the extent to which non-compete clauses adversely affect competitive conditions in labor markets and product and service markets. A reporting rule would also impose significant and recurring compliance costs on employers.

The Commission seeks comment on all aspects of this Part VI, including whether the Commission should adopt one of the alternatives described above, or a different alternative, instead of the proposed rule.

VII. Analysis of Benefits and Costs of the Proposed Rule and Alternatives

The proposed rule would provide it is an unfair method of competition—and thus a violation of Section 5 of the FTC Act—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 the worker is subject to an enforceable non-compete clause.⁴⁵⁰ The proposed rule is targeted at increasing competition in labor markets by allowing workers to move more freely between jobs and increasing competition in product markets by ensuring firms are able to hire talented workers and workers are able to found entrepreneurial ventures.

⁴⁵⁰ See proposed § 910.2(a).

The proposed rule is intended to alleviate two primary competitive problems. First, non-compete clauses anticompetitively interfere in the functioning of labor markets without generating compensating benefits. Non-compete clauses prevent firms from competing for workers' services and increase barriers to voluntary labor mobility, obstructing the smooth functioning of labor markets, resulting in lower wages and diminished worker and firm productivity.

The second competitive problem is non-compete clauses create negative spillovers in labor markets and in product and service markets. In labor markets, non-compete clauses negatively impact workers who are not themselves bound by non-compete clauses by preventing the opening of vacancies and thereby creating mismatches between labor and firms. In product and service markets, non-compete clauses prevent entrepreneurial growth, which negatively impacts consumers by reducing competition in those markets. Non-compete clauses also foreclose competitors' ability to access labor market talent, negatively affecting those competitors' ability to effectively compete in the marketplace. Additionally, non-compete clauses impede innovation, which may negatively impact technological growth rates.

Section 22 of the FTC Act requires the Commission to issue a preliminary regulatory analysis when publishing a proposed rule that would declare a practice to be an unfair method of competition under Section 5 of the FTC Act.⁴⁵¹ The preliminary regulatory analysis must contain (1) a concise description of the need for, and objectives of, the proposed rule; (2) a description of any reasonable alternatives to the proposed rule which may accomplish the stated objective of the rule in a manner consistent with

⁴⁵¹ 15 U.S.C. 57b-3.

applicable law; and (3) for the proposed rule, and for each of the alternatives described in the analysis, a preliminary analysis of the projected benefits and any adverse economic effects and any other effects.⁴⁵²

In the preliminary analysis below, we describe the anticipated impacts of the rule as proposed. Where possible, we quantify the benefits and costs. If a benefit or cost is quantified, we indicate the sources of the data relied upon. If an assumption is needed, the text makes clear which quantities are being assumed. We measure the benefits and costs of the rule against a baseline in which no rule regarding non-compete clauses has been promulgated by the Commission. The Commission solicits comments from the public to improve the assumptions used in this preliminary analysis before promulgation of any final rule.

This preliminary analysis attempts to include in its scope the broadest set of economic actors possible. The Commission invites submission of information pertaining to additional economic actors who would be affected by the proposed rule. Several of the benefits and costs described in this analysis are either quantifiable, but not monetizable (especially with respect to separation between transfers, benefits, and costs), or not quantifiable at all. The Commission therefore also invites submission of information which could be applied to quantify or monetize estimates contained in the analysis.

For some of the economic effects of non-compete clauses, conflicting evidence exists in the academic literature. We classify these effects under both benefits and costs, and discuss divergences in the evidence, as well as relative strengths and weaknesses of the evidence.

⁴⁵² 15 U.S.C. 57b-3(b)(1)(A)–(C).

The Commission seeks comment on all aspects of the preliminary analysis presented in this Part VII as well as submissions of additional data that could inform the Commission's analysis of the benefits, any adverse economic effects, and any other effects of the proposed rule.

A. Overview of the Effects of the Proposed Rule

In this preliminary regulatory analysis, we have quantified and monetized those costs and benefits for which we are able and described all other costs and benefits. The Commission finds substantial benefits of the proposed rule: workers' earnings would likely increase by \$250-\$296 billion annually (though some portion of this represents an economic transfer from firms to workers), new firm formation and competition would increase, health care prices would fall (and prices in other markets may fall), and innovation would increase, though several of these benefits overlap (*e.g.*, increases in competition may fully or in part drive decreases in prices and increases in innovation). The Commission also finds some costs of the proposed rule: direct compliance and contract updating would result in \$1.02 to \$1.77 billion in one-time costs, and firm investment in worker training and capital assets would fall.

The nature of the estimates, however, creates substantial difficulty in calculating a bottom-line present value of the net benefit to the economy of the proposed rule. The Commission believes the substantial labor and product market benefits of the proposed rule would exceed the costs, and additionally would persist over a substantially longer time horizon than some of the one-time costs of compliance and contract updating. However, we do not present here an estimate of the net benefit, as it would necessarily omit major components of both costs and benefits. In particular, the numbers reported

above are not comparable in order to estimate the net benefit of the rule: as noted, some portion of the earnings increase estimate represents transfers rather than benefits; several benefits and costs are unmonetized in this analysis; and several of the annualized benefits and costs (including the portion of the earnings increase attributable to benefit) may persist indefinitely, as compared with the one-time compliance and contract updating costs.

B. Estimated Benefits of the Proposed Rule

In this Part VII.B, we describe the beneficial impacts of the proposed rule; provide preliminary quantitative, monetized estimates where possible; and describe benefits we can only assess qualitatively. We enumerate benefits in two broad categories (further divided into subcategories): benefits related to labor markets and benefits related to goods and service markets.

Overall, the Commission estimates worker earnings would increase by \$250-\$296 billion annually as a result of the proposed rule. While the Commission believes some of this increase represents an economic benefit, some portion of this increase likely represents a transfer of income from firms to workers, or from consumers to workers if firms pass labor costs on to consumers. The Commission also finds, however, the proposed rule would increase the rate of new firm formation, the rate of innovation, and the extent of competition in product and service markets, which may lead to lower prices for consumers, though the sizes of these effects are not quantifiable based on the estimates in the economic literature (except in the case of healthcare).

1. Benefits Related to Labor Markets

By preventing workers from changing employers or embarking upon entrepreneurial ventures, non-compete clauses prevent beneficial labor market competition in two primary ways. First, non-compete clauses prevent workers from leaving their job for higher-paying jobs, or from leveraging such an offer to increase their earnings at their current employer. Second, non-compete clauses reduce voluntary churn in labor markets. While churn is not necessarily beneficial in and of itself, voluntary churn allows workers (who would otherwise be bound by non-compete clauses) and firms to sort into the best possible matches and opens vacancies, which allow workers who are not necessarily bound by non-compete clauses to find better matches. Both mechanisms exhibit, at least in part, as earnings losses for workers when non-compete clauses enforceability increases; however, the extent to which earnings gains associated with the proposed rule represent benefits versus transfers may depend on the mechanism. We describe in which cases we are and are not able to categorize, quantify, and monetize these estimates below.

a. Earnings

The primary impact of the proposed rule is an increase in earnings or earnings growth for workers, and more efficient functioning of labor markets. A full analysis of this benefit would seek to quantify the entire range of heterogeneity in the effect of the proposed rule on earnings. In other words, for any given worker, the likely impact on that worker's earnings is based on whether that worker has a non-compete clause, whether non-compete clauses are broadly used in their occupation/industry/local area, how much that worker earns, that worker's demographics, and much more. While some studies have sought to quantify heterogeneous impacts of non-compete clauses and their enforceability

on subgroups of workers, this accounting is limited to fairly small sectors of the population. For this reason, we focus primarily on estimates of average effects across the American labor force, though we provide details on what heterogeneity has been analyzed below.

The study containing the most direct estimate of the increase in workers’ earnings given a prohibition on non-compete clauses finds that earnings would increase across the labor force by an average of 3.3-13.9%.⁴⁵³ For several reasons, we primarily focus on the low end of this range: in addition to generating the most conservative estimate, this range represents an out-of-sample approximation and is furthermore based on enforceability in 2014. Since then, some states have passed legislation causing non-compete clauses to be more difficult to enforce for subsets of their workforces, therefore causing a prohibition on non-compete clauses today to have a slightly lesser effect than a prohibition would have had in 2014.⁴⁵⁴ Using total annual wage earnings in the United States for private employers in 2020 (the most recent year with finalized numbers) as a baseline,⁴⁵⁵ we estimate a total annual earnings increase of \$250.05 billion. We also report the total annual earnings increase that is associated with other levels of the percentage increase in earnings that fall within the range reported in the study in Table 1, in addition to 10-year discounted earnings increases using both 3% and 7% discount rates.

Table 1.

Percentage Increase in Earnings (%)	Total Annual Earnings Increase (\$ billion)	Total 10-Year Earnings Increase,	Total 10-Year Earnings Increase,
--------------------------------------------	----------------------------------------------------	-----------------------------------------	-----------------------------------------

⁴⁵³ Johnson, Lavetti, & Lipsitz, *supra* note 63 at 2.

⁴⁵⁴ See *supra* Part II.C.1.

⁴⁵⁵ National annual earnings are taken from Bureau of Labor Statistics, *Employment and Wages Data Viewer* (last visited Dec. 9, 2022), https://data.bls.gov/cew/apps/data_views/data_views.htm#tab=Tables.

		3% Discount Rate (\$ billion)	7% Discount Rate (\$ billion)
3.3	250.05	2,132.97	1,756.24
5.0	378.86	3,231.78	2,660.98
7.0	530.41	4,524.49	3,725.37
9.0	681.95	5,817.20	4,789.76
11.0	833.50	7,109.91	5,854.15
13.0	985.04	8,402.63	6,918.54
13.9	1,053.24	8,984.35	7,397.51

Another study estimates decreased non-compete clause enforceability would increase earnings by approximately 1%. This study uses, as a control group, occupations which use non-compete clauses at a low rate: the estimate therefore represents the differential effect on occupations which use non-compete clauses at a *high* rate, relative to the control group. While the study does estimate the separate impact of non-compete clause enforceability for each group, there is no way to disentangle this effect from state-specific effects (*e.g.*, that California does not typically enforce non-compete clauses, and also differs from other states in many ways).⁴⁵⁶ Since workers in occupations which use non-compete clauses at a low rate may also be affected by changes in non-compete clause enforceability, the reported increase in earnings likely underestimates the impact on the entire labor force. The change in enforceability which generates this estimate is a one standard deviation change, as measured using non-compete clause enforceability

⁴⁵⁶ Starr, *supra* note 66 at 792–93.

scores.⁴⁵⁷ for all 50 states and the District of Columbia in 1991. Applying the 1% earnings effect estimate to each state (based on the scores in 2009), we calculate that each state moving to non-enforceability (as would be the case under the proposed rule) would result in an overall annual earnings increase of \$295.9 billion.⁴⁵⁸

The Commission’s preliminary finding is therefore the proposed rule would increase workers’ earnings workforce-wide by \$250-\$296 billion annually. We discuss in Part VII.B.1.b the extent to which the Commission believes this increase represents a benefit of the proposed rule versus a transfer.

Four broad classes of workers merit specific attention, as researchers have generated empirical estimates of the effects of non-compete clause enforceability based specifically on those sectors. These classes are (a) high-tech workers; (b) physicians; (c) workers paid on an hourly basis; and (d) CEOs. We clarify that the effects we present on each of these specific classes of workers are contained within the broader estimates presented above: that is, the estimates above contain each of these classes of workers, plus the rest of the labor force. The specific estimates for each class of workers are therefore presented to indicate the range of effects observed in the labor market and to illustrate the scope of empirical work that has been performed on the topic.

i. High-Tech Workers

⁴⁵⁷ Non-compete clause enforceability scores, used for this estimate as well as several others, are calculated using various methods based on legal descriptions provided in various editions of “Non-Compete Clauses: A State-by-State Survey” by Brian M. Malsberger.

⁴⁵⁸ The total earnings increase is calculated as the sum over all states of:

$(e^{0.0099 * (\text{State's Enforceability Score} - \text{Lowest State Enforceability Score}) - 1}) * (\text{Total Annual Wages of the State})$

This calculation assumes that all workers benefit from the increase in earnings, as opposed to calculating the benefits to those in high-use occupations versus those in low-use occupations. The benefit of this approach is that it yields a total predicted earnings increase for the economy as a whole, rather than a comparison between different types of workers. However, it is likely an overestimate for workers in low-use occupations, and an underestimate for those in high-use occupations.

One study examines the impact of non-compete clause enforceability on high-tech workers in Hawaii.⁴⁵⁹ That study includes estimates for the entirety of the high-tech work force, as well as for newly hired workers. Since the ban in Hawaii did not void previously signed non-compete clauses, while the proposed rule would, we use the estimate for newly hired workers. This is because that estimate reflects the effects on those workers who were subject to a regime with no non-compete clause enforceability. Extrapolating from the estimates for Hawaii to the average impact on high-tech workers in each state, a prohibition such as the one in this proposed rule would increase earnings of high-tech workers in the average state by 4.8%.⁴⁶⁰ Caution is recommended in interpreting this extrapolation, however, since results from one sector within one state may not necessarily inform outcomes that would occur in the rest of the country.

ii. Physicians

One study reports the effects of non-compete clause use and enforceability on the earnings growth of physicians.⁴⁶¹

Due to the limitations of the study design, the main estimate concerns the impact of non-compete clause use on earnings growth, rather than the level of earnings.⁴⁶²

However, assuming physicians begin at an identical level of earnings, a physician with a non-compete clause would have an estimated 89% earnings growth over a ten-year

⁴⁵⁹ Balasubramanian et al., *supra* note 68 at S349.

⁴⁶⁰ The increase in earnings in each state is calculated as $e^{(0.0441 * (\text{State's Enforceability Score} - \text{Lowest State Enforceability Score}) / (\text{Hawaii's Enforceability Score} - \text{Lowest State's Enforceability Score}) - 1}$, where 0.0441 represents the impact of Hawaii's prohibition on log earnings for newly hired high-tech workers (Table 2, Panel A, Column 5).

⁴⁶¹ Lavetti, Simon, & White, *supra* note 53 at 1025.

⁴⁶² In Table 4 of the study, the table which reports earnings effects, the authors include a "job-match" fixed effect, which rules out several alternate explanations for the authors' findings but leaves the authors unable to estimate the base effect of having a non-compete clause on earnings.

period, versus an estimated 36% for a physician without a non-compete clause. In other words, the physician with a non-compete clause would have earnings approximately 39% greater than the physician without.⁴⁶³

This estimate, however, is based solely on non-compete clause use, and does not consider the impact of enforceability changing. Use of non-compete clauses is likely determined by several characteristics of an employer (*e.g.*, the value of trade secrets or client attraction, productivity gains associated with training, nearness of potential competitors), some of which may also cause changes in earnings levels or earnings growth. Taking the separate effect of non-compete clause enforceability into account, it is possible that the estimated effect on earnings growth would differ from the estimates reported above.

The combined effect of enforceability and use on earnings growth may separately be estimated using another model in the same study.⁴⁶⁴ We note that the authors state this model presents only “suggestive evidence.” Furthermore, while this model does estimate the effect of non-compete clause use on physicians’ earnings (in contrast to that reported above, which only examines earnings growth), as well as the interaction between use and enforceability, it does not report the baseline effect of non-compete clause enforceability, independent of use.⁴⁶⁵ Using those estimates, nonetheless, allows for estimation of the impact of simultaneously removing non-compete clause enforceability and non-compete clause use on earnings at various levels of experience (omitting the baseline effect of

⁴⁶³ Calculated as $1.89/1.36 - 1 = 39\%$.

⁴⁶⁴ The estimates are presented in Table 6, Column 2.

⁴⁶⁵ In Table 6 of the study, the authors use local market fixed effects: again, these fixed effects are necessary to rule out alternate explanations for their findings, but prevent estimation of the baseline impact of non-compete clause enforceability on earnings.

enforceability, which is not reported). For a physician with 10 years of experience in the state which enforces non-compete clauses most readily, the estimates suggest a prohibition on non-compete clauses and removing that physician's non-compete clause would lead to a 12.7% increase in earnings, in contrast with the results of the model reported above.⁴⁶⁶ For the identical situation for a physician with just 1 year of experience, the increase in earnings would be 37.4%. We emphasize, however, that if the baseline effect of enforceability (which the authors are unable to estimate) is large, it could qualitatively change the effect on earnings of a simultaneous change in enforceability and use that we report.

iii. Workers Paid on an Hourly Basis

One study analyzed how Oregon's 2008 prohibition on non-compete clauses for hourly workers impacted their wages.⁴⁶⁷ The study estimates Oregon's prohibition increased hourly workers' earnings by 2.3%, with twice the effect (4.6%) on workers in occupations which use non-compete clauses at a relatively high rate.⁴⁶⁸ Extrapolating from the estimates for Oregon to the average impact on hourly workers in each state, a prohibition such as the one in this proposed rule would increase earnings of hourly workers in the average state by 2.3%.⁴⁶⁹ Caution is recommended in interpreting this

⁴⁶⁶ The increase in earnings are calculated as $e^B - 1$, where B is the sum of each of the coefficients on NCA, NCA*Log Exp, Bishara Score*NCA, and Bishara Score*NCA*Log Exp, each multiplied by the relevant variable.

⁴⁶⁷ Lipsitz & Starr, *supra* note 46 at 143.

⁴⁶⁸ *Id.* at Table 3, columns 3 and 4, respectively; percent changes are calculated as $e^b - 1$, where b is the relevant reported coefficient.

⁴⁶⁹ The increase in earnings in each state is calculated as $e^{(0.023*(\text{State's Enforceability Score} - \text{Lowest State Enforceability Score})/(\text{Oregon's Enforceability Score} - \text{Lowest State's Enforceability Score}))} - 1$, where 0.023 represents the impact of Oregon's prohibition on log earnings for hourly workers (Table 3, Column 3).

extrapolation, however, since results from one segment of the workforce within one state may not necessarily inform outcomes that would occur in the rest of the country.

iv. CEOs

One estimate of the impact of non-compete clause enforceability finds that moving from full enforceability of non-compete clauses to a prohibition would increase earnings growth by 8.2% and the level of earnings by 12.7% for CEOs.⁴⁷⁰ Again ignoring heterogeneity and implementing a linear extrapolation using 2009 enforceability scores, the average CEO would experience a 9.4% increase in earnings due to the prohibition in the proposed rule.⁴⁷¹

Another study simultaneously examines the effect of *use* of a non-compete clause and the enforceability thereof.⁴⁷² This study finds that decreased enforceability of non-compete clauses led to lower earnings for CEOs when use of non-compete clauses is held constant. However, this study also finds that, when non-compete clause enforceability decreases (as it would under the proposed rule), non-compete clause use does not stay constant; it decreases.⁴⁷³ As a result, the Commission believes the appropriate way to extrapolate based on the findings of this study is to take into account both the impact of non-compete clause enforceability decreasing and the effect of non-compete clause use decreasing.

⁴⁷⁰ Garmaise, *supra* note 69 at 376–425. We assume the average level of in-state competition for the estimate of the effect on the level of earnings, as reported in Table 1.

⁴⁷¹ We first calculate the difference between each state’s score and the lowest score (which represents a full prohibition) after normalizing scores to a 0 to 1 scale. Then, we find the average of that difference (0.742) and multiply by the estimated change of 12.7% to arrive at 9.4%.

⁴⁷² Kini, Williams, & Yin, *supra* note 52 at 4701.

⁴⁷³ The study estimates that an increase in enforceability of 1 on a 0 to 12 scale increases CEO noncompete use by 10.2 percentage points in their sample. *Id.* at 4718.

When this relationship is taken into account, decreases in non-compete clause enforceability (as would occur under the proposed rule) result in greater earnings for CEOs. The study estimates an increase in enforceability of 1 on a 0 to 12 scale increases CEO noncompete use by 10.2 percentage points in their sample: therefore, a prohibition on non-compete clauses would affect CEOs' earnings via the effect the study attributes to enforceability alone, as well as by changing the use of non-compete clauses by CEOs, which has its own effect on earnings, according to the study.⁴⁷⁴

Assuming a baseline level of enforceability, it is possible to use the estimates from this study to calculate the impact on CEOs' earnings of simultaneously decreasing enforceability and non-compete clause use to zero (which would mirror the effect of the proposed rule). At the highest level of enforceability (9; Florida from 1997-2014), setting enforceability to zero and eliminating non-compete clauses from contracts would increase CEOs' earnings by 11.4%, based on this study. From a lower baseline level of enforceability (for example, 3, as in New York from 1992 to 2014), setting enforceability to zero and eliminating non-compete clauses from contracts would increase earnings by 14.1%.⁴⁷⁵

Based on the results of these two studies, the Commission therefore believes total compensation for CEOs would increase by 9.4% as a result of the proposed rule. This estimate is based on the first study discussed: while the results from the second study are qualitatively similar, the extent to which its results can be extrapolated are murkier due to the reliance on the secondary estimate of how non-compete clause use changes with non-

⁴⁷⁴ *Id.*

⁴⁷⁵ The estimated impact of an increase in enforceability on CEOs with non-compete clauses is calculated as the effect of the sum of the coefficients on CEO noncompete x HQ Enforce and HQ enforce (i.e., $0.4\% = e^{(0.047 - 0.043)} - 1$).

compete clause enforceability. Ultimately, this finding is in accordance with findings in other segments of the labor force. Similar to typical workers, non-compete clauses prevent employers from competing for the labor of CEOs, including by offering better remuneration. Therefore, CEOs, like other workers, are locked into jobs in ways that prevent them from taking advantage of positive changes in labor market conditions.

b. Discussion of Transfers Versus Benefits

It is difficult to determine the extent to which the earnings effects discussed above represent transfers versus benefits. In the context of this analysis, transfers refer to “monetary payments from one group to another that do not affect total resources available to society.”⁴⁷⁶ In other words, transfers do not represent a net benefit or cost to the economy as a whole.

Broad increases in earnings when non-compete clauses are prohibited may simply represent a transfer of income from firms to workers (or, if firms pass labor costs on to consumers, from consumers to workers). There may, however, be a related benefit if the earnings increase of workers is related to market power or efficiency in the labor market. In other words, if a prohibition on non-compete clauses leads to a more efficient allocation of labor in the market, perhaps due to a rebalancing of power between workers and employers which decreases monopsony power, then the resulting earnings increases may represent a net benefit to the economy.

Additionally, if earnings increases are due to higher quality matching which results from increased labor market churn, then increased pay reflects a benefit to the economy, since workers’ higher pay reflects higher productivity.

⁴⁷⁶ Off. of Mgmt. & Budget, *Circular A-4* (Sept. 17, 2003) at 38.

Several pieces of evidence support the idea that at least part of the increase in earnings represents a social benefit, rather than just a transfer. As described above in Part II.B.1.c, two studies have sought to estimate the external impact of non-compete clause use or enforceability: that is, the effect of use or enforceability on individuals other than those directly affected by use or enforceability.

First, one study demonstrates when the use of non-compete clauses by employers increases, that decreases wages for workers who do not have non-compete clauses but who work in the same state and industry. This study also finds this effect is stronger where non-compete clauses are more enforceable.⁴⁷⁷ Since the affected workers are not bound by non-compete clauses themselves, the differential in earnings does not completely represent a transfer due to a change in bargaining power between a worker bound by a non-compete clause and their employer, though available data does not allow for an estimate of the magnitude of transfers versus the total increase in economic benefit.

A second study directly estimates the external impact of a change in non-compete clause enforceability.⁴⁷⁸ While use of non-compete clauses is not observed in the study, the impacts of changes in a state's laws are assessed on outcomes in a neighboring state. Since the enforceability of the contracts of workers in neighboring states are not affected by these law changes, the effect must represent a change related to the labor market, which workers in both states share. The estimate suggests workers in the neighboring state experience impacts on their earnings that are 87% as large as workers in the state in

⁴⁷⁷ Starr, Frake, & Agarwal, *supra* note 76 at 961–80.

⁴⁷⁸ Johnson, Lavetti, & Lipsitz, *supra* note 63 at 26.

which enforceability changed.⁴⁷⁹ In other words, two workers who share a labor market would experience nearly the same increase in their earnings due to a prohibition on non-compete clauses, even if the prohibition only impacts one worker. While the study does not directly estimate the differential effects by use, the effects on workers unaffected by a change in enforceability may be similar to the effects on workers not bound by non-compete clauses.

Overall, these two studies suggest there are market-level dynamics governing the relationship between earnings and the enforceability of non-compete clauses: that restrictions on the enforceability of non-compete clauses impact competition in labor markets by alleviating frictions and allowing for more productive matching. Changes in enforceability or use of non-compete clauses affect earnings of workers who do not have non-compete clauses or who work in local labor markets near, but not in, locations which experience changes in enforceability. If non-compete clauses simply changed the relative bargaining power of workers and firms, without affecting market frictions or competition, then these patterns would not be observed.

With a full accounting of all other costs and benefits, one could perform a “sensitivity analysis” to estimate how much the percentage of earnings increases that represent benefits, rather than transfers, would affect the net impact of the proposed rule. However, as discussed, we are unable to fully monetize, or even quantify, several costs and benefits associated with the proposed rule. We present, instead, a partial sensitivity analysis which answers the question: for a given level of costs, what percentage of the earnings increases would offset those costs? The costs may be interpreted as the overall

⁴⁷⁹ Calculated as $-0.181/-0.207=87\%$. Coefficients taken from *id.* at Table 6, Column 2.

net cost of the rule, excluding benefits associated with earnings increases: that is, the costs listed in the table are the direct compliance and contract updating costs, plus the nonquantifiable and nonmonetizable costs, minus all benefits, excluding benefits associated with earnings increases.

The estimates are presented in Table 2. In order to present the most conservative estimates possible, we assume the earnings increase represents the lowest end of the range we estimate from the empirical literature (\$250.05 billion). We discount annually at the rate of 7% (which is more conservative than a 3% discount rate, given that the costs are more front-loaded than the benefits due to the upfront compliance costs and costs of contract updating), and assume that annualized benefits and costs persist for 10 years. The first estimate, for zero or negative net cost, demonstrates that, if the non-earnings-related benefits of the proposed rule outweigh the total costs of the proposed rule, then the costs are already offset, and no portion of the earnings increase must be a benefit. The next estimate for costs is the midpoint of the estimates presented for direct compliance and contract updating costs, as estimated in Part VII.C: if the costs of the proposed rule (excluding direct compliance and contract updating costs) exactly offset the benefits (excluding earnings-related benefits), then if 0.08% of the earnings increases are benefits, they would exactly offset the estimated \$1.394 billion costs of direct compliance and contract updating (where that estimate is the midpoint of the estimated range). While the Commission does not have detailed or complete enough quantifiable and monetizable estimates to determine whether net costs are positive or negative, the rest of Table 2 presents estimates for the portion of the earnings increase which would offset net costs greater than \$1.394 billion, should they exist.

Table 2.

Net Cost Estimate (\$ million)	Portion of Earnings Increase that Offsets the Cost Estimate
0 or Negative	0.00%
1,394	0.08%
5,000	0.28%
10,000	0.57%
15,000	0.85%
20,000	1.14%
25,000	1.42%
30,000	1.71%
35,000	1.99%
40,000	2.28%
45,000	2.56%
50,000	2.85%

2. Benefits Related to Product and Service Markets

There is evidence the proposed rule would positively impact the markets for products and services in multiple ways. Studies show that new firm formation would rise under a prohibition on non-compete clauses, for two primary reasons: first, workers would be free to form spin-offs which compete with their employers, contributing to increased competition and growth. Second, firms are more willing to enter markets in which they know there are potential sources of skilled and experienced labor, unhampered by non-compete clauses.

Another possible benefit of the proposed rule related to markets for products and services is that worker flows across employers contribute to knowledge sharing, resulting in increased levels of innovation.

We note that, to the extent productivity increases of firms may be shared with workers, some of the benefits outlined in this Part VII.B.2 may overlap with the earnings estimates outlined above in Part VII.B.1.a. Similarly, to the extent harms to incumbent firms (due to, *e.g.*, increased competition) may negatively impact workers, those would also be reflected in the earnings estimates.

a. Increased Firm Formation and Competition

Intra-industry employee spinoffs (*i.e.*, firms formed by entrepreneurs who previously worked for a firm against which they now compete—also known as within-industry spinouts or WSOs) have been shown to be highly successful, on average, when compared with typical entrepreneurial ventures.⁴⁸⁰ Non-compete clauses typically reduce the prevalence of intra-industry spinoffs, and therefore prevent entrepreneurial activity that is likely to be highly successful. One estimate implies that a one-standard-deviation increase in non-compete clause enforceability decreases the rate of WSOs by 0.13 percentage points (against a mean of 0.4%).⁴⁸¹ The proposed prohibition, by extrapolation, would result in an overall increase in the rate of WSOs by 0.56 percentage points, which would more than double the rate of WSOs. We note this is a linear approximation and cannot account for heterogeneous effects of enforceability across

⁴⁸⁰ For reviews of the literature, *see, e.g.*, Steven Klepper, *Spinoffs: A Review and Synthesis*, 6 *European Mgmt. Rev.* 159–71 (2009) and April Franco, *Employee Entrepreneurship: Recent Research and Future Directions*, in *Handbook of Entrepreneurship Research* (2005) 81–96.

⁴⁸¹ Starr, Balasubramanian, & Sakakibara, *supra* note 87 at 561.

states, nor can it account for nonlinearities in the impact of enforceability (as neither analysis is reported in the study).

The study also estimates the impact on the entry rate of non-WSOs (*i.e.*, spinoffs into other industries), and calculates a coefficient statistically indistinguishable from zero (0.07 percentage point increase associated with a one standard deviation increase in enforceability).⁴⁸²

Another study similarly estimates the impacts of non-compete clause enforceability on departures of employees to found new firms, as well as on all new firm entry.⁴⁸³ These outcomes differ slightly from the ones previously reported: for employee departures to found new firms, the target industry of the employee spinoff is not reported (so the effect encompasses both within-industry and out-of-industry spinoffs). The latter outcome encompasses all new firm entry, not just spinoffs. There are pros and cons of this approach, relative to studying only spinoffs. On the one hand, it examines an outcome less likely to be directly impacted by non-compete clauses. On the other hand, if firms are encouraged to enter when non-compete clauses are more easily enforceable (due to, *e.g.*, greater projected protection of knowledge assets), then this approach will likely identify effects that may appear only weakly when looking just at spinoffs.

For each outcome, the estimated effect of an increase in non-compete clause enforceability (which is, in this study, measured by a collection of discrete legal changes) is negative: an increase in non-compete clause enforceability decreases the rate at which employees leave to become founders of firms by 0.78 percentage points, against a mean

⁴⁸² *Id.* at 561.

⁴⁸³ Jeffers (2019), *supra* note 92 at 1.

in the sample of 5% (though the result is statistically indistinguishable from zero),⁴⁸⁴ and decreases the rate of new firm entry by 0.06 firms per million people (against a mean of 0.38) for firms in the knowledge sector, compared with firms in other sectors (for which there is no statistically significant effect). Due to the design of the study, the change in legal enforceability is not quantified, and therefore no extrapolation is possible to the country as a whole.

Three more estimates related to firm entry exist in the literature. One examines the differential impacts of venture capital (“VC”) funding on firm entry: it finds a 1% increase in VC funding increases business formation by 2.3% when non-compete clauses are not enforceable, and by 0.8% when non-compete clauses are enforceable.⁴⁸⁵ Another study examined the extent to which a legal enforceability increase in Michigan affected firm entry, and found that, among all sectors, there was no change in the entry rate of new firms (none of the estimated coefficients were statistically significant).⁴⁸⁶ Among high-tech firms, the increase in enforceability was associated with a 40.3% increase in entry when compared with states that did not enforce non-compete clauses. However, the study also notes that, compared with its neighbors, or using a statistical technique to match Michigan’s trend in firm entry (synthetic control method), the estimated effect was statistically indistinguishable from zero. Finally, a study examining the effect of an increase in enforceability in Florida found small firm (fewer than 50 employees) entry

⁴⁸⁴ The estimated effect is statistically significant at the 10% level, and nearly doubles to 0.014, when attention is focused on firms which employ at least 40% of workers in the state in which their headquarters resides. This is important because it ensures that a greater portion of the workforce is subject to the local non-compete clause policy regime: a broadly dispersed company has workers subject to many different legal policies surrounding non-compete clauses, and it is therefore not surprising that the estimate is unable to distinguish a large impact of the policy changes.

⁴⁸⁵ Samila & Sorenson, *supra* note 112 at 425–38.

⁴⁸⁶ Carlino, *supra* note 86.

fell by 5.6%, while large firm (greater than 1,000 employees) entry increased by 8.5%. Similarly, employment at large businesses rose by 15.8% following the change, while employment at smaller businesses effectively did not change.⁴⁸⁷ The net effect was a 4.4% increase in concentration, as measured by a Herfindahl-Hirschman Index, due to the overall increase in the size of firms. It is important to note that firm entry, in this study, is not necessarily new business formation. Indeed, the authors describe many business entries into Florida are existing businesses which are seeking to move or establish new franchises. The observed effects may therefore be due to relocations across state lines, which would likely not occur under the proposed rule.

For the previously mentioned three sets of estimates, it is again difficult to extrapolate to a population-wide measure of impact, since the “size” of the enforceability change is not quantified.

In Part II.B.2.c above, the Commission states the weight of the evidence demonstrates new firm formation would increase under the proposed rule; however, the Commission is unable to extrapolate from the studies which examine this outcome in order to quantify or monetize the effect.

b. Innovation

Scholars have posited that a lack of non-compete clause enforceability led Silicon Valley to become a hub of technological innovation. One paper theorizes that, as workers freely flowed between knowledge firms, those workers shared ideas and generated innovations greater than what a fixed set of workers, not interacting with outside workers,

⁴⁸⁷ Kang & Fleming, *supra* note 120 at 674.

could have generated.⁴⁸⁸ Studies have shown labor mobility is greater when non-compete clauses are more difficult to enforce.⁴⁸⁹ However, those same studies did not directly show innovation is aided by the free flow of knowledge workers.

If non-compete clauses inhibit innovation by creating barriers to knowledge-sharing, then a prohibition on non-compete clauses, by alleviating those barriers, would increase innovation. Studies have sought to directly quantify this effect, primarily focused on patenting activity.

One study examined the impact of non-compete clause enforceability on venture capital's relationship with innovation. The study found that, when non-compete clauses are enforceable, venture capital induced less patenting, by 6.6 percentage points.⁴⁹⁰ Two other studies directly focused on the relationship between non-compete clause enforceability and patenting. One, examining seven changes in non-compete clause enforceability, finds a 26.6% decline in the value of patents (as measured by changes in stock prices surrounding the date a patent is granted) associated with increases in non-compete clause enforceability.⁴⁹¹ The other, examining the impact of a legal change in enforceability in Michigan, finds an increase in non-compete clause enforceability leads to an increase in the number of patents per 10,000 residents of 0.054 (against a mean of 2.20 in Michigan prior to the legal change).⁴⁹² There is no clear reason for this discrepancy in findings. It may be due to the setting being studied: the study finding a 26.6% decline in patent value considers several legal changes in non-compete clause

⁴⁸⁸ Gilson, *supra* note 88.

⁴⁸⁹ See, e.g., Fallick, Fleischman, & Rebitzer, *supra* note 89 at 472–81; Johnson, Lavetti, & Lipsitz, *supra* note 42.

⁴⁹⁰ Samila & Sorenson, *supra* note 112 at 432.

⁴⁹¹ He, *supra* note 124 at 22.

⁴⁹² Carlino, *supra* note 86 at 40.

enforceability, rather than just using one (as in the Michigan study) or relying on cross-sectional differences (as in the study of venture capital).

While the Commission believes the strongest evidence (due to the robustness of the findings across several legal changes) indicates innovation would likely increase under the proposed rule, as described above in Part II.B.2.d, the Commission is unable to extrapolate from the relevant studies to quantify or monetize this benefit.

c. Prices

Several of the effects discussed above, as well as costs of the proposed rule on products and service markets, may possibly filter through to consumer prices. Prices, therefore, may act as a summary metric for the impacts on consumers. We note this metric is highly imperfect: for example, increased innovation due to the proposed rule could cause quality increases in products, which drives prices up. Consumers may be better off, even though prices increased. For this reason, as well as to avoid double-counting (since prices may take into account changes in innovation, investment, market structure, wages, and other outcomes), we consider evidence on prices to be corroborating evidence, rather than a unique cost or benefit on its own.

One study estimates the impact of non-compete clause enforceability on consumer prices in the market for physician services.⁴⁹³ The study estimates moving from the lowest observed non-compete clause enforceability score to the highest would increase prices by 53.3%. Extrapolating to the effect of the proposed prohibition nationwide (using 2009 enforceability scores), and applying percentage price decreases to state-level

⁴⁹³ Hausman & Lavetti, *supra* note 101 at 258.

physician spending,⁴⁹⁴ we estimate health spending would decrease by \$148.0 billion annually. We note, again, this is a large (linear) extrapolation from the estimate provided in the study. Furthermore, this amount is partially a transfer from physician practices to consumers, and additionally, we reiterate this estimate likely encompasses some of the prior estimates (*i.e.*, those regarding new firm formation or innovation), and we therefore do not count it as a standalone benefit of the proposed rule.

With respect to other industries, if the relationship between non-compete clause enforceability and prices observed in healthcare markets holds, the Commission believes prices would decrease, product and service quality would increase, or both under the proposed rule. Insofar as such effects may be driven by increases in competition (see Part VII.B.2.a), it is likely output would also increase. However, the evidence in the economic literature is solely based on healthcare markets (which do comprise a large portion of spending in the United States, but are far from all consumer spending), and while there is evidence that there are relationships between non-compete clause enforceability and concentration, innovation, new firm formation, and other product market outcomes, the Commission cannot say with certainty similar effects would be present for other products and services.

In many settings, it is theoretically plausible increases in worker earnings from restricting non-compete clauses may increase consumer prices by raising firms' costs

⁴⁹⁴ The latest available numbers are from 2014. See Ctrs. for Medicare & Medicaid Servs., *National Health Expenditure Data, Health Expenditures by State of Provider, 1980–2014* (last visited Dec. 9, 2022), <https://www.cms.gov/Research-Statistics-Data-and-Systems/Statistics-Trends-and-Reports/NationalHealthExpendData/NationalHealthAccountsStateHealthAccountsProvider>. We use physician and clinical spending in 2014 by state of provider.

(though there is countervailing evidence, especially in goods manufacturing).⁴⁹⁵ We note an absence of empirical evidence that this mechanism persists in practice, as well as countervailing forces, such as the impacts on concentration described above and positive impacts on innovation (see Part II.B.2.d). Additionally, greater wages for workers freed from non-compete clauses may be due to better worker-firm matching, which could simultaneously increase wages and increase productivity, which could lead to lower prices. Finally, as described in Part II.B.2.a, increases in healthcare prices are not due to pass-through of greater labor costs.

C. Estimated Costs of the Proposed Rule

In this Part VII.C, we describe the costs associated with the proposed rule; provide preliminary quantitative, monetized estimates where possible; and describe costs we can only assess qualitatively. We welcome public comment regarding the scope of the costs outlined in this Part VII.C, especially with respect to direct compliance costs and the costs of updating contractual practices.

The Commission estimates firms' direct compliance costs and the costs of firms updating their contractual practices would total \$1.02 to \$1.77 billion. The Commission also finds worker training and firm investment in capital assets would likely decrease under the proposed rule. Finally, the Commission finds inconclusive evidence that the job creation rate would diminish under the proposed rule. Given the evidence available, the Commission is unable to monetize the estimates of worker training, firm investment in capital assets, and job creation, however.

1. Direct Compliance Costs

⁴⁹⁵ Sebastian Heise, Fatih Karahan, & Ayşegül Şahin *The Missing Inflation Puzzle: The Role of the Wage-Price Pass-Through*, 54 *J. Money, Credit & Banking* 7 (2022).

In order to comply with the proposed rule, firms must remove non-compete clauses from workers' contracts in two ways. First, to comply with proposed § 910.2(a), which states it is an unfair method of competition to maintain with a worker a non-compete clause, firms would need to no longer include non-compete clauses in the contracts of incoming workers, which may include revising existing employment contracts. Second, to comply with proposed § 910.2(b)(1) and (2), firms would need to rescind existing non-compete clauses no later than the compliance date and provide notice to workers that the worker's non-compete clause is no longer in effect and may not be enforced against the worker.

In order to reduce compliance costs and increase compliance certainty, proposed § 910.2(b)(3) would provide that an employer complies with the rescission requirement in proposed § 910.2(b)(1) where it provides notice to a worker pursuant to § 910.2(b)(2). Furthermore, proposed § 910.2(b)(2)(C) includes model language which may be provided to the worker in order to inform the worker that their non-compete clause is no longer in effect. We estimate composing and sending this message in a digital format to all of a firm's workers and applicable former workers would take 20 minutes of a human resources specialist's time. According to the Bureau of Labor Statistics, the median wage for a human resources specialist was \$29.95 per hour in 2021.⁴⁹⁶ The cost of compliance for currently employed workers is therefore $\$29.95/3 = \9.98 per firm. According to the U.S. Census Bureau's Statistics of U.S. Businesses database, in 2019 (the most recent year with data available), there were 6.10 million firms and 7.96 million establishments

⁴⁹⁶ See Bureau of Lab. Stats., *Occupational Outlook Handbook, Human Resources Specialists*, <https://www.bls.gov/ooh/business-and-financial/human-resources-specialists.htm>.

in the United States.⁴⁹⁷ We estimate the percentage of firms using non-compete clauses in the U.S. at 49.4%. This estimate is based on Colvin and Shierholz's 2017 survey of business establishments. Colvin and Shierholz estimate 49% of establishments of more than 50 employees use non-compete clauses for at least some of their employees, and 32% of establishments use non-compete clauses for all of their employees.⁴⁹⁸

Conservatively assuming each establishment must engage in its own communication (*i.e.*, that a firm's headquarters does not have the ability to send a company-wide e-mail, for example), this means the total direct compliance cost for rescinding existing non-compete clauses and providing notice is $\$9.98 * 7.96$ million $* 0.494 = \$39.25$ million.

To ensure incoming workers' contracts do not include non-compete clauses and they fully comply with the proposed rule, firms may employ in-house counsel, outside counsel, or human resource specialists (depending on the complexity of the relevant non-compete clause). For many firms, this process would likely be straightforward (*i.e.*, simply not using non-compete clauses or removing one section from a boilerplate contract). For other firms, it may be more difficult and require more time. We assume that, on average, ensuring contracts for incoming workers do not have non-compete clauses would take the equivalent of one hour of a lawyer's time (valued at \$61.54),⁴⁹⁹ resulting in a total cost of $\$61.54 * 7.96$ million $* 0.494 = \$241.96$ million. We acknowledge there may be substantial heterogeneity in the costs for individual firms; however, we

⁴⁹⁷ The dataset is available at U.S. Census Bureau, *2019 SUSB Annual Data Tables by Establishment Industry*, <https://www.census.gov/data/tables/2019/econ/susb/2019-susb-annual.html> (last visited Dec. 9, 2022).

⁴⁹⁸ Alexander J.S. Colvin & Heidi Shierholz, Econ. Pol'y Inst., *Noncompete Agreements* (2019) at 1.

⁴⁹⁹ Bureau of Lab. Stats., *Occupational Outlook Handbook: Lawyers*, <https://www.bls.gov/ooh/legal/lawyers.htm>.

believe this number is conservative. For firms whose costs of removing non-compete clauses for incoming workers is greater, the work of ensuring contracts comply with the law would overlap substantially with the costs of updating contractual practices, described in the next section.

2. Costs of Updating Contractual Practices

Firms may seek to update their contractual practices by expanding the scope of non-disclosure agreements (NDAs) or other contractual provisions to ensure they are expansive enough to protect trade secrets and other valuable investments. To do so, firms may use in-house counsel or outside counsel to examine and amend current contracts or enter into new contracts with workers.

The Commission is not aware of empirical evidence on how much it costs firms to update their contractual practices when they can no longer use non-compete clauses. However, there is evidence indicating firms that use non-compete clauses are already using other types of restrictive employment provisions. Firms may be doing so because, among other things, they are uncertain whether a non-compete clause will be enforceable, or because they desire the additional protections NDAs and other types of restrictive employment provisions can offer. Balasubramanian et al. find that 97.5% of workers with non-compete clauses are also subject to a non-solicitation agreement, non-disclosure agreement, or a non-recruitment agreement, and 74.7% of workers with non-compete clauses are also subject to all three other types of provisions.⁵⁰⁰ Firms that are already

⁵⁰⁰ Balasubramanian, Starr, & Yamaguchi, supra note 40 at 35. We calculate 97.5% as $(1 - 0.6\% / 24.2\%)$, where 0.6% represents the proportion of workers with only a non-compete clause, and no other post-employment restriction, and 24.2% represents the proportion of workers with a non-compete clause, regardless of what other post-employment restrictions they have.

using multiple layers of protection may not need to expand the scope of existing restrictive employment provisions or enter into new ones.

Among the approximately one half of firms that use non-compete clauses,⁵⁰¹ we assume the average firm employs the equivalent of four to eight hours of a lawyer's time to update their contractual practices. We emphasize this is an average to underline the fact that there would likely be large differences in the extent to which firms update their contractual practices. Many firms, including those which use non-compete clauses only with workers who do not have access to sensitive information, or those which are already using other types of restrictive employment provisions to protect sensitive information, may opt to do nothing. Other firms may employ several hours or multiple days of lawyers' time to arrive at a new contract.⁵⁰² Our estimated range of four to eight hours represents an average taken across these different possibilities. For example, if two-thirds of firms that currently use non-compete clauses opt to make no changes to their contractual practices (for example, because they are one of the 97.5% of firms which already implement other post-employment restrictions, or because they will rely on trade secret law in the future, or because they are using non-compete clauses with workers who do not have access to sensitive information), and one-third of such firms spend (on average) the equivalent of 1.5 to 3 days of an attorney's time, this would result in the estimate of 4-8 hours on average reported above.

We further emphasize this estimate is an average across all employers that would be covered by the rule. There is likely substantial heterogeneity in the amount of time

⁵⁰¹ Colvin & Shierholz, *supra* note 498 at 1.

⁵⁰² These estimates are derived from outreach to employment attorneys active in assisting firms in writing their non-compete clauses.

firms would use to update contractual practices; very large firms that use non-compete clauses extensively would likely incur greater costs.

Under the assumption the average firm that uses a non-compete clause employs the equivalent of four to eight hours of a lawyer's time, we calculate the total expenditure on updating contractual practices to range from $\$61.54 \times 4 \times 49.4\% \times 6,102,412 = \742.07 million to $\$61.54 \times 8 \times 49.4\% \times 6,102,412 = \1.48 billion. Note that we assume decisions regarding protection of sensitive information and contract updating are made at the firm, rather than establishment, level, since sensitive information is likely shared across business establishments of a firm. The Commission seeks comment on this estimate.

3. Firm Investment

Non-compete clauses may impact investments made by firms in multiple ways.⁵⁰³ First, a firm may anticipate a greater return on investment in a worker with a non-compete clause—since the worker is unable to take the skills they attain to a competitor—and may therefore provide greater levels of training. Second, since non-compete clauses increase worker training, firms may increase investment that complements human capital when they are able to use non-compete clauses. Third, non-compete clauses decrease competition, which increases returns on investment at the firm level, inducing additional investment at the firm level. This increased investment at the firm level does not necessarily mean, however, investment would increase at the market level, since decreased competition may also decrease output, decreasing employed capital stock and investment in that capital stock.

⁵⁰³ For more discussion, see Jeffers (2019), *supra* note 92; Starr (2019), *supra* note 66 at 783–817.

Once again, the costs described in this section may overlap with estimates reported in preceding sections. For example, if increased enforceability of non-compete clauses increases training of workers, and increased training results in higher wages for workers, then the estimate of the wage decrease when enforceability increases already takes into account the extent to which increased training increases wages. That is, if training were held constant, the earnings increase associated with the proposed rule would likely be even larger.

With respect to worker training, one study finds that an increase in the non-compete clause enforceability index of one standard deviation (across states) results in an increase in the number of workers who reported receiving training of 14.7% for workers in occupations which use non-compete clauses at a high rate, relative to those in which non-compete clauses are used at a low rate.⁵⁰⁴ Extending this estimate to the U.S. workforce implies that, on average, 3.1% fewer workers would receive training in a given year, as a result of the proposed rule.⁵⁰⁵

An estimate of the impact of non-compete clause enforceability on firm investment in capital assets implies that an increase in enforceability leads to an increase in firms' net investment to asset ratio of 1.3 percentage points (against a mean of 3.5%). The magnitude of the enforceability increase which is associated with this change is not

⁵⁰⁴ Starr (2019), *supra* note 66 at 796. Estimates are taken from Table 4, Column 4.

⁵⁰⁵ The total training decrease is calculated as the weighted average (where weights are equal to employment in 2020, the latest year available, taken from https://data.bls.gov/cew/apps/table_maker/v4/table_maker.htm) over all states of: $(e^{-0.0077*(\text{State's Enforceability Score} - \text{Lowest State Enforceability Score})} - 1)$

This calculation assumes that all workers are subject to the decrease in training, as opposed to calculating the decrease to those in high-use occupations versus those in low-use occupations. The benefit of this approach is that it yields a total predicted training decrease for the economy as a whole, rather than a comparison between different types of workers. However, it is likely an overestimate for workers in low-use occupations, and an underestimate for those in high-use occupations. It is the same methodology used to calculate earnings increases in Part VII.B.1.a for the estimate drawn from the same study.

quantified according to the scale above, however, so it is not possible to extend this estimate to the population. Additionally, the estimate is constructed at the firm level, and it is not possible to extrapolate the estimate to the market level, given potential changes in the composition of the market associated with changes in non-compete clause enforceability.

The proposed rule may also impact the extent to which trade secrets are shared with workers. Non-compete clauses are commonly justified as a means by which firms are able to protect trade secrets, which may allow those trade secrets to be shared more freely with workers, positively impacting productivity. However, to the best of our knowledge, there is no available evidence on this topic which would allow us to quantify or monetize the cost, or identify whether it exists in practice.

4. Job Creation Rates

While non-compete clauses may, in theory, incentivize firms to create jobs by increasing the value associated with any given worker covered by a non-compete clause, the evidence is inconclusive. One estimate indicates the job creation rate at startups increased by 7.8% when Michigan increased non-compete clause enforceability.⁵⁰⁶ However, the job creation rate calculated in this study is the ratio of jobs created by startups to overall employment in the state: therefore, the job creation rate at startups may rise either because the number of jobs created by startups rose, or because employment overall fell. The study does not investigate which of these two factors drives the increase in the job creation rate at startups.

⁵⁰⁶ Carlino, *supra* note 86 at 16.

Another study finds that several increases in non-compete clause enforceability were associated with a 1.4% increase in average employment at new firms.⁵⁰⁷ However, the authors attribute the increase in average employment to a change in the composition of newly founded firms. The increases in enforceability prevented the entry of relatively small startups which would otherwise have existed. The remaining firms which entered were therefore larger on average: this increases the average job creation rate at new firms, because the average entering firm is relatively larger. However, in terms of total jobs created, it means that increases in enforceability generate fewer total jobs, if the mechanism identified by the authors is correct. A similar mechanism may explain the results in both studies above. If that is indeed the case, then an increased job creation rate among startups is not a cost of the proposed rule. Instead, it could actually be a benefit (albeit unquantifiable), since non-compete clauses prevent small firms from existing in the first place. The Commission therefore believes that, with respect to job creation rates, the evidence is inconclusive: it is unclear whether the negative results have causes which are actually benign, or even positive.

5. Litigation Costs

The proposed rule would likely reduce litigation costs associated with non-compete clauses, since there would be little to no uncertainty that the vast majority of those clauses are prohibited. However, it is also possible that costs associated with trade secret claims or other post-employment restrictions, such as non-disclosure agreements or non-solicitation agreements, would increase. The Commission is not aware of any evidence indicating the magnitude of the change in litigation costs associated with any of

⁵⁰⁷ Starr, Balasubramanian, & Sakakibara, *supra* note 87 at 561.

these claims, and it is therefore not clear whether the net impact on litigation costs would be a benefit or a cost of the proposed rule. The Commission seeks comment on the impact the rule would have on litigation costs.

D. Discussion of Alternatives

In Part VI of this NPRM, the Commission describes several alternatives to the proposed rule. Here, we discuss the extent to which implementation of each of these alternatives would change the analysis of benefits and costs presented above.

We treat Alternatives 1 and 3 first. Under Alternative 1, the rule would categorically ban the use of non-compete clauses for some workers and apply a rebuttable presumption of unlawfulness to non-compete clauses for other workers. For example, the rule could ban non-compete clauses generally, but apply the rebuttable presumption to workers who qualify for the FLSA exemptions for executives or learned professionals.⁵⁰⁸ Or the rule could ban non-compete clauses but apply the rebuttable presumption to workers who earn more than \$100,000 per year. Under Alternative 3, non-compete clauses for all workers would be subject to a rebuttable presumption of illegality.

There are two primary ways in which a rebuttable presumption of illegality, rather than a prohibition, could affect the benefits and costs associated with the proposed rule. First, a rebuttable presumption may decrease costs associated with the proposed rule by allowing employers to use non-compete clauses in situations in which the true benefits of non-compete clauses exceed the costs. In other words, the non-compete clauses which

⁵⁰⁸ See *supra* notes 423–424 and accompanying text.

survive a rebuttable presumption may contribute to economic efficiency to the extent a court is able to identify efficiency-enhancing non-compete clauses.

Second, a rebuttable presumption could increase costs by forcing cases involving non-compete clauses to be litigated more frequently, since the line defining a permissible non-compete clause would be less bright. Additionally, there may be situations in which the presumption would likely hold (*i.e.*, a given non-compete clause is likely prohibited under the presumption), but which are not fought by workers, fearing they might lose the case. In such cases, any costs and benefits associated with non-compete clauses (such as those outlined in the preceding sections) would accrue to the economy.

The two impacts of a change from a prohibition to a rebuttable presumption would likely be more drastic for workers above the threshold (for whom the presumption would be rebuttable under Alternative 1), as compared with those additional workers for whom the presumption would be rebuttable under Alternative 3. For the latter set of workers, there are fewer plausible cases in which the presumption would be rebutted, since higher-paid workers typically have access to greater levels of sensitive information. This means there is a smaller efficiency gain to be had from allowing non-compete clauses which could plausibly rebut the presumption; however, it also means there would likely be fewer litigated cases since there would be fewer marginal non-compete clauses. Therefore, the effect of moving from the proposed rule to Alternative 1 is likely more substantial than the effect of moving from Alternative 1 to Alternative 3.

The effects of Alternatives 2 and 4 may be analyzed similarly. Under Alternative 2, the rule would categorically ban the use of non-compete clauses for some workers and not apply any requirements to other workers. For example, like the recent State of

Washington statute, the rule could prohibit the use of non-compete clauses for employees earning \$100,000 or less per year and independent contractors earning less than \$250,000 or less per year. Or, like the recent Massachusetts and Rhode Island statutes, the rule could prohibit the use of non-compete clauses for workers who are non-exempt under the FLSA.⁵⁰⁹ Under Alternative 4, the rule would apply a rebuttable presumption of unlawfulness to non-compete clauses for some workers and not apply any requirements to other workers. Workers above the threshold are most likely to be those workers for whom firm investment and training are valuable, but they are also often uniquely positioned to found new firms, since they hold knowledge gained by working in their industry. Therefore, a large portion of the benefits associated with the proposed rule would be lost if workers above the threshold were not covered; however, a large portion of the costs would also be lost, since the need to restructure contracts to protect sensitive information would no longer be present for those workers, and firms would continue to train and invest in those workers in the same way they currently do. Additionally, the earnings effects for relatively lower-wage workers appear to be less, based on empirical work, though the legal changes analyzed were not perfectly comparable. This could indicate, again, there are more substantial benefits to be had from prohibiting non-compete clauses for workers above the threshold based on harms to labor markets, compared with workers below the threshold.

The alternative under which the rule would use a different standard for senior executives, discussed in Part VI.C, would yield similar effects to the analyses discussed above. If a rebuttable presumption were applied to senior executives, if there are some

⁵⁰⁹ See *supra* Part VI.B.2.

non-compete clauses that are efficient, and if courts are able to appropriately identify efficient non-compete clauses, then some non-compete clauses would likely be used (and may survive challenges) which are indeed efficient. On the other hand, costs associated with legal challenges would likely increase due to an increased frequency of legal challenges associated with a less bright line. If no requirement is applied to senior executives, then a large portion of the benefit of the proposed rule, as it applies to senior executives, would be lost: benefits associated with increased product market competition and benefits associated with increased labor market competition. The costs of restructuring contracts, however, would be lost, as well.

Another alternative, discussed in Part VI.D, concerns whether non-compete clauses between a franchisor and a franchisee would be covered by the proposed rule. As noted in Part VI.D, evidence concerning the impact of prohibiting non-compete clauses between franchisors and franchisees does not exist. The Commission is therefore unable to estimate the extent to which the costs and benefits which would result from the proposed rule covering those parties would be similar to those resulting from prohibiting worker non-compete clauses.

E. Other Major Effects

There are two substantial equity concerns associated with the proposed rule which are not captured above. The first relates to the economic outcomes of women and racial and ethnic minorities. Non-compete clauses may affect women and racial and ethnic minorities more negatively than other workers. For example, firms may use the monopsony power which results from use of non-compete clauses as a means by which to

wage discriminate, or women (who may exhibit greater risk aversion, in practice⁵¹⁰) may be more reluctant to start businesses when non-compete clauses are enforceable. One estimate indicates that gender and racial wage gaps would close by 3.6-9.1% under a nationwide prohibition on non-compete clauses.⁵¹¹ Another estimate indicates the negative impact of non-compete clause enforceability on within-industry entrepreneurship is 15% greater for women than for men.⁵¹²

The second equity concern related to non-compete clauses is that workers may not be willing to file lawsuits against deep-pocketed employers to challenge their non-compete clauses, even if they predict a high probability of success. The proposed rule would substantially mitigate this concern by enacting a bright-line prohibition, which the Commission could enforce. This would mitigate uncertainty for workers and would be especially helpful for relatively low-paid workers, for whom access to legal services may be prohibitively expensive.

VIII. Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA), as amended by the Small Business Regulatory Enforcement Fairness Act of 1996, requires an agency to either provide an Initial Regulatory Flexibility Analysis (IRFA) with a proposed rule or certify that the proposed rule would not have a significant impact on a substantial number of

⁵¹⁰ See, e.g., Catherine C. Eckel & Philip J. Grossman, *Men, Women and Risk Aversion: Experimental Evidence*, *Handbook of Experimental Economics Results* 1 (2008) 1061–073 and Gary Charness & Uri Gneezy, *Strong Evidence For Gender Differences in Risk Taking*, 83 *J. Econ. Behavior & Org.* 50–58 (2012).

⁵¹¹ Johnson, Lavetti, & Lipsitz, *supra* note 63 at 38.

⁵¹² Marx (2021), *supra* note 118 at 8.

small entities.⁵¹³ The Commission does not expect the proposed rule, if adopted, would have a significant impact on a substantial number of small entities.

Although small entities across all industrial classes—*i.e.*, all North American Industry Classification System (NAICS) codes—would be affected, the estimated impact on each entity would be relatively small. The Small Business Administration (SBA) states that, as a rule of thumb, the impact of a proposed rule could be significant if the cost of the proposed rule (a) eliminates more than 10% of the businesses' profits; (b) exceeds 1% of the gross revenues of the entities in a particular sector, or (c) exceeds 5% of the labor costs of the entities in the sector.⁵¹⁴ As calculated in Part VIII.D, the Commission estimates direct compliance costs and the costs of updating contractual practices would result in costs of \$317.68 to \$563.84 for single-establishment firms. These costs would only exceed these sample limits if the average profit of regulated entities is \$3,177 to \$5,638, average revenue is \$31,768 to \$56,384, or average labor costs are \$6,353 to \$11,276, respectively. Furthermore, while there are additional nonmonetizable costs associated with the proposed rule, there are also nonmonetizable benefits which would at least partially offset those costs, as explained above in Part VII.

Although the Commission certifies under the RFA that the proposed rule would not have a significant impact on a substantial number of small entities, and hereby provides notice of that certification to the SBA, the Commission has determined it is appropriate to publish an IRFA in order to describe the impact of the

⁵¹³ 5 U.S.C. 603–605.

⁵¹⁴ Small Bus. Admin., *A Guide for Government Agencies: How to Comply With the Regulatory Flexibility Act* (August 2017) (hereinafter RFA Compliance Guide) at 19.

proposed rule on small entities. The Commission seeks comment on all aspects of the IRFA in this Part VIII.

A. Reasons for the Proposed Rule

The Commission describes the reasons for the proposed rule above in Part IV.

B. Statement of Objectives and Legal Basis

The Commission describes the objectives and legal basis for the proposed rule above in Part IV and the legal authority for the rule above in Part III.

C. Description and Estimated Number of Small Entities to Which the Rule Would Apply

The proposed rule would impact all small businesses, across all industry classes, that use non-compete clauses. The Commission does not expect there are classes of businesses that would face disproportionate impacts from the proposed rule.

For the vast majority of industries, there is no granular data regarding the percentage of firms that use non-compete clauses (which could then be used to calculate the number of small entities in that industry using non-compete clauses). Due to this data limitation and given the relatively stable percentage of firms using non-compete clauses across the size distribution,⁵¹⁵ we estimate the total number of small firms across all industries in the U.S. economy. We then calculate the number of firms estimated to use non-compete clauses by applying an estimate of the percentage of firms using non-compete clauses to that total. Using the size standards set by the SBA,⁵¹⁶ we calculate

⁵¹⁵ See Colvin & Shierholz, *supra* note 498 at 5. We emphasize that, since smaller firms generally use non-compete clauses at a lower rate, based on the numbers reported in Table 1, our estimate of the number of affected small entities is likely larger than is true in practice.

⁵¹⁶ See Small Bus. Admin., *Table of Size Standards*, <https://www.sba.gov/document/support-table-size-standards>.

that there are 5.95 million small firms and 6.24 million small establishments in the U.S.⁵¹⁷ Assuming 49.4% of firms or establishments use non-compete clauses,⁵¹⁸ we estimate 2.94 million small firms, comprising 3.08 million small establishments, would be affected by the proposed rule. Since our estimate ignores differential use of non-compete clauses across industries (in the absence of more detailed data), these firms span all industries and various sizes below the standards set in the SBA’s size standards.

D. Projected Reporting, Recordkeeping, and Other Compliance Requirements

As calculated in Parts VIII.D.1 and VIII.D.2, the Commission estimates the direct compliance costs and the costs of updating contractual practices would total \$246.16 to \$492.32 for each small firm, plus an additional \$71.52 for each establishment owned by that firm. A single-establishment firm, for example, would bear estimated costs of \$317.68 to \$563.84, for example.

As described in greater detail in Part VII.C.3, the Commission also finds worker training and firm investment in capital assets would likely decrease under the proposed rule. Finally, as described in greater detail in Part VII.C.4, the Commission finds mixed evidence that the job creation rate would diminish under the proposed rule. Given the evidence available, the Commission is unable to monetize the estimates of worker training, firm investment in capital assets, and job creation, however.

⁵¹⁷ We use the latest data available from the U.S. Census Bureau’s Statistics of U.S. Businesses database, available based on firm revenue and firm size. U.S. Census Bureau, *Statistics of U.S. Businesses (SUSB)*, <https://www.census.gov/programs-surveys/susb.html> (last visited Dec. 9, 2022). We deflate to current dollars using Historical Table 10.1. Off. of Mgmt. & Budget, *Historical Tables*, <https://www.whitehouse.gov/omb/budget/historical-tables/> (last visited Dec. 9, 2022). As used in this analysis, per the U.S. Census Bureau, “a firm is a business organization consisting of one or more domestic establishments in the same geographic area and industry that were specified under common ownership or control.” On the other hand, “an establishment is a single physical location at which business is conducted or services or industrial operations are performed.” See U.S. Census Bureau, *Glossary*, <https://www.census.gov/programs-surveys/susb/about/glossary.html>.

⁵¹⁸ See Colvin & Shierholz, *supra* note 498 at 1.

1. Direct Compliance Costs

In order to comply with the proposed rule, small entities must remove non-compete clauses from workers' contracts in two ways. First, to comply with proposed § 910.2(a), which states it is an unfair method of competition to maintain with a worker a non-compete clause, small entities would need to no longer include non-compete clauses in the contracts of incoming workers, which may include revising existing employment contracts. Second, to comply with proposed § 910.2(b)(1) and (2), small entities would need to rescind existing non-compete clauses no later than the compliance date and provide notice to workers that the worker's non-compete clause is no longer in effect and may not be enforced against the worker.

In order to reduce compliance costs and increase compliance certainty, proposed § 910.2(b)(3) would provide that an employer complies with the rescission requirement in proposed § 910.2(b)(1) where it provides notice to a worker pursuant to § 910.2(b)(2). Furthermore, proposed § 910.2(b)(2)(C) includes model language which may be provided to the worker in order to inform the worker that their non-compete clause is no longer in effect. We estimate composing and sending this message in a digital format to all of a firm's workers and applicable former workers would take 20 minutes of a human resources specialist's time. According to the Bureau of Labor Statistics, the median wage for a human resources specialist was \$29.95 per hour in 2021.⁵¹⁹ The cost of compliance for currently employed workers is therefore $\$29.95/3=\9.98 per firm. As calculated in Part VIII.C, we estimate there are 2.94 million small firms, comprising 3.08 million small

⁵¹⁹ See U.S. Bureau of Lab. Stats., *Occupational Outlook Handbook, Human Resources Specialists*, <https://www.bls.gov/ooh/business-and-financial/human-resources-specialists.htm>.

establishments, in the United States which use non-compete clauses.⁵²⁰ Conservatively assuming that each establishment must engage in its own communication (*i.e.*, a firm's headquarters does not have the ability to send a company-wide e-mail, for example), this means the total direct compliance cost for workers who are already employed is $\$9.98 * 3.08 \text{ million} = \30.74 million .

To ensure incoming workers' contracts do not include non-compete clauses and they fully comply with the proposed rule, firms may employ in-house counsel, outside counsel, or human resource specialists (depending on the complexity of the relevant non-compete clause). For many firms, this process would likely be straightforward (*i.e.*, simply not using non-compete clauses or removing one section from a boilerplate contract). For other firms, it may be more difficult and require more time. We assume that, on average, ensuring contracts for incoming workers do not have non-compete clauses would take the equivalent of one hour of a lawyer's time (valued at \$61.54),⁵²¹ resulting in a total cost of $\$61.54 * 3.08 \text{ million} = \189.54 million . We acknowledge there may be substantial heterogeneity in the costs for individual firms; however, we believe this number is conservative. For firms whose costs of removing non-compete clauses for incoming workers is greater, the work of ensuring that contracts comply with the law would overlap substantially with the costs of updating contractual practices, described in the next section.

⁵²⁰ The dataset is available at U.S. Census Bureau, *2019 SUSB Annual Data Tables by Establishment Industry*, <https://www.census.gov/data/tables/2019/econ/susb/2019-susb-annual.html>, (last visited Dec. 9, 2022).

⁵²¹ U.S. Bureau of Lab. Stats., *Occupational Outlook Handbook, Lawyers*, <https://www.bls.gov/ooh/legal/lawyers.htm>.

For each establishment of each firm, we estimate direct compliance costs would total $\$9.98 + \$61.54 = \$71.52$.

2. Costs of Updating Contractual Practices

Firms may seek to update their contractual practices by expanding the scope of non-disclosure agreements (NDAs) or other contractual provisions to ensure they are expansive enough to protect trade secrets and other valuable investments. To do so, firms may use in-house counsel or outside counsel to examine and amend current contracts or enter into new contracts with workers.

The Commission is not aware of empirical evidence on how much it costs firms to update their contractual practices when they can no longer use non-compete clauses. However, there is evidence indicating firms that use non-compete clauses are already using other types of restrictive employment provisions. Firms may be doing so because, among other things, they are uncertain whether a non-compete clause will be enforceable, or because they desire the additional protections NDAs and other types of restrictive employment provisions can offer. Balasubramanian et al. find that 97.5% of workers with non-compete clauses are also subject to a non-solicitation agreement, non-disclosure agreement, or a non-recruitment agreement, and 74.7% of workers with non-compete clauses are also subject to all three other types of provisions.⁵²² Firms already using multiple layers of protection may not need to expand the scope of existing restrictive employment provisions or enter into new ones.

⁵²² Balasubramanian, Starr, & Yamaguchi, supra note 40 at 35. We calculate 97.5% as $(1 - 0.6\% / 24.2\%)$, where 0.6% represents the proportion of workers with only a non-compete clause, and no other post-employment restriction, and 24.2% represents the proportion of workers with a non-compete clause, regardless of what other post-employment restrictions they have.

Among the approximately one half of firms that use non-compete clauses,⁵²³ we assume the average firm employs the equivalent of four to eight hours of a lawyer's time to update their contractual practices. We emphasize this is an average to underline the likelihood of large differences in the extent to which firms update their contractual practices. Many firms, including those which use non-compete clauses only with workers who do not have access to sensitive information, or those which are already using other types of restrictive employment provisions to protect sensitive information, may opt to do nothing. Other firms may employ several hours or multiple days of lawyers' time to arrive at a new contract.⁵²⁴ Our estimated range of four to eight hours represents an average taken across these different possibilities. For example, if two-thirds of firms that currently use non-compete clauses opt to make no changes to their contractual practices (for example, because they are one of the 97.5% of firms which already implement other post-employment restrictions, or because they will rely on trade secret law in the future, or because they are using non-compete clauses with workers who do not have access to sensitive information), and one-third of such firms spend (on average) the equivalent of 1.5 to 3 days of an attorney's time, this would result in the estimate of 4-8 hours on average reported above.

We further emphasize this estimate is an average across all employers that would be covered by the rule. There is likely substantial heterogeneity in the amount of time firms would use to update contractual practices; very large firms that use non-compete clauses extensively would likely incur greater costs.

⁵²³ Colvin & Shierholz, *supra* note 498 at 1.

⁵²⁴ These estimates are derived from outreach to employment attorneys active in assisting firms in writing their non-compete clauses.

Under the assumption the average firm that uses a non-compete clause employs the equivalent of four to eight hours of a lawyer's time, we calculate the total expenditure on updating contractual practices to range from $\$61.54 \times 4 \times 2.94$ million = \$723.7 million to $\$61.54 \times 8 \times 2.94$ million = \$1.45 billion. Note that we assume decisions regarding protection of sensitive information and contract updating are made at the firm, rather than establishment, level, since sensitive information is likely shared across business establishments of a firm. The Commission seeks comment on this estimate.

For each firm, we estimate the cost of updating contractual practices would be $\$61.54 \times 4 = \246.16 to $\$61.54 \times 8 = \492.32 .

E. Identification of Duplicative, Overlapping, or Conflicting Federal Rules

The Commission is not aware of any duplicative, overlapping, or conflicting federal rules. As described above in Part II.C.1, the enforceability of a non-compete clause currently depends on state law. Non-compete clauses are also subject to federal antitrust law. However, the Commission is not aware of any federal regulations that would duplicate, overlap, or conflict with the proposed rule.

F. Discussion of Significant Alternatives

In Part VI above, the Commission discusses significant alternatives to the proposed rule. Part VI also includes a preliminary assessment of whether each of the significant alternatives would accomplish the objectives of the proposed rule. In addition, the Commission's analysis of benefits and costs in Part VII includes an assessment of the benefits and costs of various alternatives.⁵²⁵

⁵²⁵ See *supra* Part VII.D.

The Commission is not proposing an exemption for small entities or different regulatory requirements for small entities. The proposed rule would provide 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, under certain circumstances, to represent to a worker that the worker is subject to a non-compete clause.⁵²⁶ For the reasons described above in Part IV, the Commission is proposing to provide these practices are an unfair method of competition under Section 5. Based on the available evidence, the Commission does not believe the analysis in Part IV above is fundamentally different for non-compete clauses imposed by small entities. For this reason, the Commission is not proposing an exemption for small entities or different regulatory requirements for small entities. The Commission seeks comment on whether it should propose a small entity exemption or different requirements for small entities, including whether non-compete clauses used by small entities are less likely to have the anticompetitive effects described in Part IV.A above, and whether employers that are small entities are less likely than other employers to have alternatives available for protecting their investments, as described in Part IV.B above.

The Commission is also not proposing a delayed compliance date for small entities. Under proposed § 910.5, compliance with the proposed rule would be required as of the proposed compliance date, which would be 180 days after publication of the final rule in the *Federal Register*.⁵²⁷ In the Commission's preliminary view, this proposed

⁵²⁶ See proposed § 910.2(a).

⁵²⁷ See proposed § 910.5.

compliance period would afford small entities a sufficient period of time to comply with the proposed rule.⁵²⁸ The Commission seeks comment on whether this is the case.

IX. Paperwork Reduction Act

Under the Paperwork Reduction Act of 1995 (PRA),⁵²⁹ federal agencies must obtain approval from the Office of Management and Budget (OMB) for each collection of information they conduct or sponsor. The term “collection of information” includes any requirement or request for persons to obtain, maintain, retain, report, or publicly disclose information.⁵³⁰ Under the PRA, the Commission may not conduct or sponsor, and, notwithstanding any other provision of law, a person is not required to respond to, an information collection unless the information collection displays a valid control number assigned by OMB.⁵³¹

The Commission believes the proposed rule would contain a disclosure requirement that would constitute a collection of information requiring OMB approval under the PRA. Proposed § 910.2(a) would state 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, under certain circumstances, represent to a worker that the worker is subject to a non-compete clause. Proposed § 910.2(b)(1) would state that, to comply with § 910.2(a), an employer that entered into a non-compete clause with a worker prior to the compliance date must rescind the non-compete clause no later than the compliance date.

⁵²⁸ See *supra* Part V, in the section-by-section analysis for proposed § 910.5.

⁵²⁹ 44 U.S.C. 3501 *et seq.*

⁵³⁰ 44 U.S.C. 3502(3); 5 CFR 1320.3(c).

⁵³¹ 44 U.S.C. 3506(c)(1)(B); 5 CFR 1320.5(a)(3).

Proposed § 910.2(b)(2)—the provision that would contain the disclosure requirement that would require OMB approval—would require employers to provide a notice to workers in certain circumstances. Specifically, proposed § 910.2(b)(2)(A) would require an employer that rescinds a non-compete clause pursuant to § 910.2(b)(1) to provide notice to the worker that the worker’s non-compete clause is no longer in effect and may not be enforced against the worker. Proposed § 910.2(b)(2)(A) would also state the employer must provide the notice to the worker in an individualized communication and the employer must provide the notice on paper or in a digital format such as, for example, an email or text message. Proposed § 910.2(b)(2)(B) would state the employer must provide the notice to a worker who currently works for the employer. Proposed § 910.2(b)(2)(B) would also state that the employer must also provide the notice to a worker who formerly worked for the employer, provided the employer has the worker’s contact information readily available. Finally, proposed § 910.2(b)(2)(C) would provide model language that would satisfy the notice requirement. Proposed § 910.2(b)(2)(C) would also state that an employer may also use different language, provided the notice communicates to the worker that the worker’s non-compete clause is no longer in effect and may not be enforced against the worker.

The Commission estimates composing and sending this message in a digital format to all workers would take 20 minutes of a human resources specialist’s time. According to the Bureau of Labor Statistics, the median wage for a human resources specialist in 2021 was \$29.95 per hour.⁵³² The cost of compliance for currently employed workers is therefore $\$29.95 / 3 = \9.98 per firm. According to the U.S. Census Bureau’s

⁵³² U.S. Bureau of Lab. Stats., *Occupational Outlook Handbook: Human Resources Specialists*, <https://www.bls.gov/ooh/business-and-financial/human-resources-specialists.htm>.

Statistics of U.S. Businesses database, in 2019 (the most recent year for which data are available), there were 6.10 million firms and 7.96 million establishments in the United States.⁵³³ The Commission estimates the percentage of firms using non-compete clauses in the United States at 49.4%.⁵³⁴ This yields an estimated 3,932,240 covered establishments. Conservatively assuming that each establishment must engage in its own communication—*i.e.*, a firm’s headquarters does not have the ability to send a company-wide e-mail, for example—this means covered employers would incur an estimated labor cost burden of 1,310,747 hours to comply with this requirement (3,932,240 establishments × 20 minutes). The Commission estimates the associated labor cost for notifying affected workers who are already employed is $\$9.98 \times 7.96$ million × 0.494 = \$39,243,755.

The proposed rule would impose only *de minimis* capital and non-labor costs. The Commission anticipates covered employers already have in place existing systems to communicate with and provide employment-related disclosures to workers. While the proposed rule would require a one-time disclosure to some workers subject to a rescinded non-compete clause, the Commission anticipates this one-time disclosure would not require substantial investments in new systems or other non-labor costs. Moreover, many establishments are likely to provide the disclosure electronically, further reducing total costs.

The Commission invites comments on: (1) Whether the proposed collection of information is necessary for the proper performance of the functions of the agency,

⁵³³ U.S. Census Bureau, 2019 SUSB Annual Data Tables by Establishment Industry (February 2022), <https://www.census.gov/data/tables/2019/econ/susb/2019-susb-annual.html> (last visited Dec. 9, 2022).

⁵³⁴ See Colvin & Shierholz, *supra* note 498 at 4.

including whether the information would have practical utility; (2) the accuracy of the agency's estimate of the burden of the proposed collection of information, including the validity of the methodology and assumptions used; (3) ways to enhance the quality, utility, and clarity of the information to be collected; and (4) ways to minimize the burden of these information collections on respondents. The Commission seeks comment on all aspects of this Part IX.

Comments on the proposed reporting requirements subject to Paperwork Reduction Act review by OMB should additionally be submitted to www.reginfo.gov/public/do/PRAMain. Find this particular information collection by selecting "Currently under 30-day Review—Open for Public Comments" or by using the search function. The [reginfo.gov](http://www.reginfo.gov) web link is a United States Government website operated by OMB and the General Services Administration (GSA). Under PRA requirements, OMB's Office of Information and Regulatory Affairs (OIRA) reviews federal information collections.

X. Request for Comment

You can file a comment online or on paper. For the Commission to consider your comment, we must receive it on or before [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE *FEDERAL REGISTER*]. Write "Non-Compete Clause Rulemaking, Matter No. P201200" on your comment. Your comment—including your name and your state—will be placed on the public record of this proceeding, including the <https://www.regulations.gov> website.

Because of the public health emergency in response to the COVID-19 outbreak and the agency's heightened security screening, postal mail addressed to the Commission

will be subject to delay. We strongly encourage you to submit your comments online through the <https://www.regulations.gov> website. To ensure the Commission considers your online comment, please follow the instructions on the web-based form.

If you file your comment on paper, write “Non-Compete Clause Rulemaking, Matter No. P201200” on your comment and on the envelope, and mail your comment to the following address: Federal Trade Commission, Office of the Secretary, 600 Pennsylvania Avenue NW, Suite CC-5610 (Annex C), Washington, DC 20580.

Because your comment will be placed on the publicly accessible website at <https://www.regulations.gov>, you are solely responsible for making sure your comment does not include any sensitive or confidential information. In particular, your comment should not include any sensitive personal information, such as your or anyone else’s Social Security number; date of birth; driver’s license number or other state identification number, or foreign country equivalent; passport number; financial account number; or credit or debit card number. You are also solely responsible for making sure your comment does not include any sensitive health information, such as medical records or other individually identifiable health information. In addition, your comment should not include any “trade secret or any commercial or financial information which...is privileged or confidential”—as provided by 15 U.S.C. 46(f) and 16 CFR 4.10(a)(2)—including, in particular, competitively sensitive information such as costs, sales statistics, inventories, formulas, patterns, devices, manufacturing processes, or customer names.

Comments containing material for which confidential treatment is requested must be filed in paper form, must be clearly labeled “Confidential,” and must comply with 16 CFR 4.9(c). In particular, the written request for confidential treatment that accompanies

the comment must include the factual and legal basis for the request, and must identify the specific portions of the comment to be withheld from the public record. Your comment will be kept confidential only if the General Counsel grants your request in accordance with the law and the public interest. Once your comment has been posted publicly at <https://www.regulations.gov>—as legally required by 16 CFR 4.9(b)—we cannot redact or remove your comment, unless you submit a confidentiality request that meets the requirements for such treatment under FTC Rule 4.9(c) and the General Counsel grants that request.

Visit the Commission’s website, www.ftc.gov, to read this NPRM and the fact sheet describing it. The FTC Act and other laws the Commission administers permit the collection of public comments to consider and use in this proceeding as appropriate. The Commission will consider all timely and responsive public comments that it receives on or before [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE *FEDERAL REGISTER*]. For information on the Commission’s privacy policy, including routine uses permitted by the Privacy Act, see <https://www.ftc.gov/site-information/privacy-policy>.

XI. Communications by Outside Parties to Commissioners or Their Advisors

Written communications and summaries or transcripts of oral communications respecting the merits of this proceeding, from any outside party to any Commissioner or Commissioner’s advisor, will be placed on the public record, per 16 CFR 1.26(b)(5).

List of Subjects in 16 CFR Part 910

Antitrust.

For the reasons set forth above, the Federal Trade Commission proposes to add a new subchapter J, consisting of part 910, to chapter I in title 16 of the Code of Federal Regulations:

1. Add new subchapter J, consisting of part 910, to read as follows:

SUBCHAPTER J—RULES CONCERNING UNFAIR METHODS OF COMPETITION

PART 910—NON-COMPETE CLAUSES

Sec.

910.1. Definitions.

910.2. Unfair methods of competition.

910.3. Exception.

910.4. Greater protection under State law.

910.5. Effective date and compliance date.

Authority: 15 U.S.C. 45 and 46(g).

§ 910.1 Definitions.

(a) *Business entity* means a partnership, corporation, association, limited liability company, or other legal entity, or a division or subsidiary thereof.

(b) *Non-compete clause*.

(1) *Non-compete clause* means a contractual term between an employer and a worker that prevents the worker from seeking or accepting employment with a person, or operating a business, after the conclusion of the worker's employment with the employer.

(2) *Functional test for whether a contractual term is a non-compete clause.* The term non-compete clause includes a contractual term that is a *de facto* non-compete clause because it has the effect of prohibiting the worker from seeking or accepting employment with a person or operating a business after the conclusion of the worker's employment with the employer. For example, the following types of contractual terms, among others, may be *de facto* non-compete clauses:

i. A non-disclosure agreement between an employer and a worker that is written so broadly that it effectively precludes the worker from working in the same field after the conclusion of the worker's employment with the employer.

ii. A contractual term between an employer and a worker that requires the worker to pay the employer or a third-party entity for training costs if the worker's employment terminates within a specified time period, where the required payment is not reasonably related to the costs the employer incurred for training the worker.

(c) *Employer* means a person, as defined in 15 U.S.C. 57b-1(a)(6), that hires or contracts with a worker to work for the person.

(d) *Employment* means work for an employer, as the term employer is defined in paragraph (c) of this section.

(e) *Substantial owner, substantial member, and substantial partner* mean an owner, member, or partner holding at least a 25 percent ownership interest in a business entity.

(f) *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. The term worker does not include a franchisee in the context of a franchisee-franchisor relationship; however, the term worker includes a natural person who works for the franchisee or franchisor. Non-compete clauses between franchisors and franchisees would remain subject to Federal antitrust law as well as all other applicable law.

§ 910.2 Unfair methods of competition.

(a) *Unfair methods of competition.* 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.

(b) *Existing non-compete clauses.*

(1) *Rescission requirement.* To comply with paragraph (a) of this section, which states that it is an unfair method of competition for an employer to maintain with a worker a non-compete clause, an employer that entered into a non-compete clause with a worker prior to the compliance date must rescind the non-compete clause no later than the compliance date.

(2) *Notice requirement.*

(A) An employer that rescinds a non-compete clause pursuant to paragraph (b)(1) of this section must provide notice to the worker that the worker's non-compete clause is no longer in effect and may not be enforced against the worker. The employer must provide the notice to the worker in an individualized communication. The employer must provide the notice on paper or in a digital format such as, for example, an email or text

message. The employer must provide the notice to the worker within 45 days of rescinding the non-compete clause.

(B) The employer must provide the notice to a worker who currently works for the employer. The employer must also provide the notice to a worker who formerly worked for the employer, provided that the employer has the worker's contact information readily available.

(C) The following model language constitutes notice to the worker that the worker's non-compete clause is no longer in effect and may not be enforced against the worker, for purposes of paragraph (b)(2)(A) of this section. An employer may also use different language, provided that the notice communicates to the worker that the worker's non-compete clause is no longer in effect and may not be enforced against the worker.

A new rule enforced by the Federal Trade Commission makes it unlawful for us to maintain a non-compete clause in your employment contract. As of [DATE 180 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE], the non-compete clause in your contract is no longer in effect. This means that once you stop working for [EMPLOYER NAME]:

- You may seek or accept a job with any company or any person—even if they compete with [EMPLOYER NAME].
- You may run your own business—even if it competes with [EMPLOYER NAME].
- You may compete with [EMPLOYER NAME] at any time following your employment with [EMPLOYER NAME].

The FTC's new rule does not affect any other terms of your employment contract.

For more information about the rule, visit [*link to final rule landing page*].

(3) *Safe harbor*. An employer complies with the rescission requirement in paragraph (b)(1) of this section where it provides notice to a worker pursuant to paragraph (b)(2) of this section.

§ 910.3 Exception.

The requirements of this Part 910 shall not apply to a non-compete clause that is entered into by a person who is selling a business entity or otherwise disposing of all of the person's ownership interest in the business entity, or by a person who is selling all or substantially all of a business entity's operating assets, when the person restricted by the non-compete clause is a substantial owner of, or substantial member or substantial partner in, the business entity at the time the person enters into the non-compete clause. Non-compete clauses covered by this exception would remain subject to Federal antitrust law as well as all other applicable law.

§ 910.4 Relation to State laws.

This Part 910 shall supersede any State statute, regulation, order, or interpretation to the extent that such statute, regulation, order, or interpretation is inconsistent with this Part 910. A State statute, regulation, order, or interpretation is not inconsistent with the provisions of this Part 910 if the protection such statute, regulation, order, or interpretation affords any worker is greater than the protection provided under this Part 910.

§ 910.5 Compliance date.

Compliance with this Part 910 is required as of [INSERT DATE 180 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE].

By direction of the Commission, Commissioner Wilson dissenting.

April J. Tabor,

Secretary.