THE UNCERTAIN VIABILITY OF THE FTC'S NONCOMPETE BAN

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Recent developments in Supreme Court jurisprudence pose a stiff challenge to the FTC's Noncompete Ban (the "**Noncompete Ban**"). Specifically, the United States Supreme Court's decision in *Loper Bright Enterprises v. Raimondo* ("**Loper**") and a federal injunction from a Texas court on July 3, 2024 both cast doubt on the legitimacy of the ban.

The key issue is that *Loper* stands for the idea that federal agencies – like the FTC – no longer deserve deference by courts when those agencies create new regulations and rules. As we will explore below, the Noncompete Ban could be viewed by a court as an overreach, as an instance of the FTC inappropriately acting to create and effect regulations beyond the agency's official remit.

The FTC's Noncompete Ban

Here is a brief overview of why the Noncompete Ban is under attack:

1. **Proposed Rule**: The FTC's rule aims to ban most noncompete clauses, arguing they restrict worker mobility and suppress wages. The FTC issued the Noncompete Ban because the agency believes that the restriction of worker mobility and the suppression of wages constitute a form of unfair competition, which the FTC is explicitly authorized to address pursuant to the Section 5 of FTC Act. The ban is scheduled to take effect on September 4, 2024.

2. **Existing Legal Challenges to Enforcing the Noncompete Ban**: A range of businesses and industry groups have claimed that the FTC overstepped its authority by introducing the ban. The core theme in these criticisms is that while the FTC does have the authority to address unfair competition, it does not have the authority to prohibit certain contractual agreements between employers and employees. In the wake of *Loper* – which overturns the Chevron Deference (as set forth below) – an injunction granted in *Ryan LLC v. Federal Trade Commission* has called into question whether the ban will be enforceable over the long term across all US jurisdictions. This injunction is the first example of business and industry groups convincing a court that *Loper* casts serious doubt on the FTC's wholesale ban of noncompete agreements.

What is Chevron Deference?

1. **The Supreme Court Standard**: In 1984, the Supreme Court ruled in *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc*. that lower courts must defer to reasonable agency interpretations of statutes such agencies administer, even if those statutes are ambiguous in material ways ("**Chevron Deference**"). This doctrine gave agencies like the FTC significant authority, as we will cover in greater detail below.

2. **How Does this Standard Support the Noncompete Ban?**: The customary legal thinking is that Chevon Deference supports the FTC's Noncompete Ban. Specifically, the FTC took the position that Sections 5 and 6 of the FTC Act, the federal law that provides the FTC with its regulatory remit, give the agency the authority to render unlawful "unfair methods of competition." Because the FTC Act does not define noncompete provisions in private contracts as unfair methods of competition, the FTC had to engage in rulemaking in order to prohibit these provisions.

3. **The Practical Impact of Chevron Deference**: Under Chevon Deference, agency rulemaking – including the creation of rules such as the Noncompete Ban – is very hard to challenge for one simple reason: agencies get to decide what ambiguous statutes mean as long as their interpretations of the statutes are "reasonable". Because what is "reasonable" is in the eye of the beholder, Chevron Deference historically provided agencies a robust defense against challenges to their interpretations of even the most ambiguous federal laws.

Loper: The End of Chevron Deference

1. **The New Supreme Court Standard**: On *June 28, 2024*, the Supreme Court effectively overruled Chevron Deference. The heart of the *Loper* holding is straightforward and simple: *Courts may not defer to an agency interpretation of the law simply because a statute is ambiguous.*

2. **How Does *Loper* Undermine the Noncompete Ban?**: *Loper* undermines the FTC's Noncompete Ban in two obvious ways:

> a. First, agencies like the FTC generally face a higher burden when justifying rulemaking that is based in statutes that give those agencies their regulatory authority and define the scope of such authority. In other words, the burden has shifted to agencies to justify new rulemaking, whereas Chevron Deference previously forced courts to meet the burden of establishing why an agency had clearly overstepped its bounds.
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> b. Second, *Loper* actually encourages courts to exercise their independent judgement when assessing agency rulemaking. In practical terms, this means that courts are empowered to look at how and why an agency passed a certain rule. This will undoubtedly translate into differences of opinion as to whether an agency should or should not have passed a certain rule. To take the Noncompete Ban as an example, a court could take the position that the data the FTC relied upon to justify the Noncompete Ban – data allegedly showing

that non-competes constitute "unfair competition" by suppressing wages or interfering with the efficient matching of employers and employees – is incomplete, misleading, or inaccurate. Alternatively, a court could also take the position that while the data the FTC relied upon was accurate and complete, the agency simply lacks the authority under the FTC Act to regulate matters of private contract.

The Impact of the *Ryan Foods* Case

1. **What Happened in *Ryan Foods*?**: In *Ryan LLC v. Federal Trade Commission*, Ryan Foods challenged the FTC's authority to enforce a nationwide ban on noncompete agreements. A federal judge issued an injunction on July 3, 2024, halting enforcement specifically against the plaintiffs, citing FTC overreach and the arbitrary and capricious nature of the unqualified ban on all noncompetes.

2. **Why Did the Court Grant an Injunction?**: The court enjoined the enforcement of the Noncompete Ban for two key reasons. First, in light of the Supreme Court's decision in *Loper*, the court concluded that there was a significant likelihood that the FTC had exceeded its authority to develop rules such as the Noncompete Ban to combat unfair methods of competition. Second, because the FTC decided to ban all noncompete provisions – regardless of scope and content of such provisions – the ban is probably arbitrary and capricious.

The Broad Impact of *Loper* and *Ryan Foods*

- **Increased Judicial Scrutiny in Federal District Courts**: In light of the limited injunction in the *Ryan Foods* case, it is likely that federal courts will continue to heavily scrutinize the impact of the Noncompete Ban in the near future. It is unclear whether all federal courts will focus on the same issues that played a role in *Ryan Foods* litigation, it is clear that federal judges have the legal authority to consider whether the Noncompete Ban is an appropriate exercise of the FTC's authority.
- **Diversity of Approaches Across the Federal Courts**: Federal district courts could take a wide variety of approaches to examining the Noncompete Ban after *Loper*. Because *Loper* only stands for the idea that courts are not compelled to defer to the FTC's interpretation of the FTC Act, federal judges are encouraged to exercise their own independent judgment when assessing whether the FTC has exceeded its authority. This could lead to a patchwork of different positions across the federal district courts when it comes to the enforceability of the Noncompete Ban.
- **Impact on Running and Governing a Business**: The *Ryan Foods* injunction, coupled with the *Loper* decision, creates uncertainty about the enforceability of the FTC's Noncompete Ban. In turn, this could lead business owners to take the position that noncompetes are still worth incorporating into private agreements with employees unless and until there is certainty with respect to the enforceability of noncompete provisions. As a result, disputes between employers and business owners could escalate, causing exactly the kind of legal

confusion that the FTC's blanket ban was designed to prevent.

- **Potential Legislative Change**: Even prior to the *Ryan Foods* injunction was granted in July of 2024, business leaders were making the case that the FTC exceeded its authority when it issued the Noncompete Ban. Their argument is based on a straightforward idea: The FTC Act was passed to provide the FTC with authority to issue rules to protect consumers in matters related to fraud, false advertising, and unfair competition, and that narrow mandate does not include authority to issue rules regulating competition in employment markets. Given the costs of allowing legal uncertainty about the Noncompete Ban to fester, it is possible Congress will craft legislation to further clarify the scope of the FTC's authority to issue partial or total bans on noncompete agreements.

BurgherGray LLP is at the forefront of advising companies on how to effect compliance with the FTC noncompete ban. Contact **Gopal Burgher** *(gburgher@burghergray.com) or* ***John Eden*** *(jeden@burghergray.com) to discuss how to address noncompete issues without running afoul of the FTC's new prohibition on these agreements.*

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