Federal Court Sets Aside FTC Final Noncompete Rule Nationwide

August 22, 2024

On August 20, 2024, the United States District Court for the Northern District of Texas set aside the final rule promulgated by the Federal Trade Commission (the "FTC") that would ban nearly all post-employment noncompete agreements. As many anticipated, the Court granted summary judgment to the challengers in *Ryan LLC v. Federal Trade Commission* ("*Ryan*") and found that the final rule exceeds the FTC's statutory authority and is arbitrary and capricious. The Court therefore vacated the final rule with nationwide effect. The FTC may, of course, appeal this decision. But, for now, the final rule will not be going into effect on September 4 or at any time before a successful appeal.

The Texas Court's Ruling. The Texas court's decision in *Ryan* rested on two grounds. First, the Court found that the FTC exceeded its statutory authority in promulgating the final rule. The Court agreed with Plaintiffs that the FTC Act did not grant substantive rulemaking authority to the FTC. The Court noted that "the lack of statutory penalty for violating rules promulgated under Section 6(g) demonstrates [the FTC's] lack of substantive rulemaking power." The Court also found that the text and history of the Federal Trade Commission Act further establish that the FTC was only given authority to decide whether a practice is considered an "unfair method of competition" on a case-by-case basis.

Second, the Court concluded that the final rule is "arbitrary and capricious because it is unreasonably overbroad without a reasonable explanation. The final rule imposes a one-size-fits-all approach with no end date, which fails to establish a rational connection between the facts found and the choice made." The Court noted in particular that the final rule is "based on inconsistent and flawed empirical evidence, fails to consider the positive benefits of non-compete agreements, and disregards the substantial body of evidence supporting these agreements." Additionally, the FTC "failed to sufficiently address alternatives to issuing the Rule." Instead, the FTC "dismissed any possible alternatives, concluding that either the pro-competitive justifications outweighed the harms, or that employers had other avenues to protect their interests."

What Happens Next? Unless and until the FTC appeals this decision and wins the appeal, the final rule will not go into effect. If the FTC chooses to appeal, it must file a notice of appeal within 30 days (i.e., on or before September 19, 2024). The FTC may choose to file a motion to expedite appeal, but it will only be granted if the appellate court finds that there is good cause. In any event, it is unlikely that even an expedited appeal will yield any contrary decision before September 4.

There is also parallel litigation pending in the United States District Court for the Eastern District of Pennsylvania (*ATS Tree Services, LLC v. Federal Trade Commission*) and in the United States District Court for the Middle District of Florida (*Properties of the Villages, Inc. v. Federal Trade Commission*). Both courts have issued their rulings on the motions for a preliminary injunction, but neither court has received motions for summary judgment from the parties. Given the current status of those two cases as well as the decision from the Northern District of Texas, it is highly unlikely that any contrary decision will issue from either court prior to September 4, the original effective date of the final rule.

Advice for Employers. Given that the Texas court has set aside the FTC's final rule, there is no need for employers to send notices to current and former covered employees with noncompetes on September 4, which was the date that the rule would have become effective without judicial intervention.

As noted, the FTC may decide to appeal this decision, so employers should continue to monitor for developments. Equally importantly, however, employers should consider the state law landscape, which has been a source of significant change as more states find compelling local public policies in the areas of competition and worker mobility. These policy developments have to date only been in one direction—making noncompetes harder to enforce—and the invalidation of the FTC final rule can reasonably be expected to invigorate more action at the state level, including in the bellwether corporate jurisdictions of New York and Delaware, both of which have seen legislative and judicial activity recently.

Therefore, we continue to recommend that employers enhance trade secret protections beyond the use of noncompetes and consider compensation changes and alternative arrangements, including garden leave arrangements, repayment agreements, retention bonuses or longer vesting periods for long-term awards (e.g., cliff-vesting or back-loaded schedules).

Finally, even if the FTC's rulemaking efforts are blocked, we anticipate that the FTC will continue to pursue enforcement actions against companies that broadly use noncompete agreements, particularly for lower-wage workers, under Section 5 of the FTC Act. We recommend that employers before or soon to be before the FTC in other

contexts (e.g., merger review under the Hart-Scott-Rodino Act) be aware of, evaluate, and consider proactively modifying their use of noncompetes. If such employers are using noncompetes broadly, the FTC may hold up their mergers or subject them to separate post-closing investigations.

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