

August 21, 2024

FTC Non-Compete Clause Rule Is Set Aside by Court

- A federal district court in Texas ruled on the merits that the FTC does not have statutory authority to promulgate the Non-Compete Clause Rule and that the rule is arbitrary and capricious.
- As a consequence, the court set aside the rule under the Administrative Procedure Act and ordered that it “shall not be enforced or otherwise take effect.” The order is nationwide in scope and not party-specific.
- Two other challenges to the rule are pending in other district courts. To the extent those actions produce inconsistent orders, it will be up to the courts of appeals and ultimately the United States Supreme Court to either maintain the district court’s order or allow the rule to go into effect.

The Court’s Order Setting Aside the Non-Compete Clause Rule

On August 20, 2024, Judge Ada E. Brown of the United States District Court for the Northern District of Texas issued a final order setting aside the Federal Trade Commission (FTC) [Non-Compete Clause Rule](#), which was to have taken effect on September 4, 2024. According to the court’s order, the rule “shall not be enforced or otherwise take effect on” that date “or thereafter.” As the court explained, the relief “has nationwide effect, is not party-restricted, and affects persons in all judicial districts equally.” The order is a consequence of the court finding that “the FTC lacks statutory authority to promulgate” the rule, and that the rule is “arbitrary and capricious.” Under the applicable provision of the Administrative Procedure Act, when a court reaches either of these conclusions, it must set aside the rule in question. The case is *Ryan LLC, et al. v. Federal Trade Commission*, No. 24-cv-986 (N.D. Tex. Aug. 8, 2024).

The FTC Lacks Unfair Methods of Competition Rulemaking Authority

The FTC argued that section 6(g) of the FTC Act, 15 U.S.C. §§ 41-58, granted it the power to promulgate substantive rules relating to unfair methods of competition, such as the Non-Compete Clause Rule. By its terms, section 6(g) gives the FTC the authority to “classify corporations and . . . to make rules and regulations for the purpose of carrying out the provisions of” certain parts of the FTC Act, including the provision prohibiting unfair methods of competition. The court, however, held that the FTC’s authority under section 6(g) “does not expressly grant the Commission authority to promulgate substantive rules regarding unfair methods of competition.” Rather, it is a “housekeeping statute” that authorizes “rules of agency organization procedure or practice as opposed to substantive rules.” The lack of a statutory penalty for violating rules promulgated under section 6(g)—in contrast to the penalty provided for violations of unfair or deceptive trade acts or practices rules, which are authorized by the FTC Act—further supported the court’s conclusion that section 6(g) does not confer substantive rulemaking authority.

The FTC’s Rule Is Arbitrary and Capricious

The court also found that the record of the FTC’s rulemaking proceeding “does not support” the rule. According to the court, the 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.” The court also found that the FTC unjustifiably “failed to sufficiently address alternatives to issuing” the rule.

Possible Scenarios Going Forward

Further Legal Proceedings Regarding the Rule

In a statement released shortly after the Texas court’s ruling, an FTC spokesperson said that the Commission is “seriously considering a potential appeal.” An appeal of the *Ryan* decision could introduce a number of uncertainties as to timing and the effect of interim relief, if any, pending appeal. In addition, two other actions challenging the rule are pending in district courts in two different circuits. This could potentially lead to a circuit split. In *ATS Tree Services, LLC v. Federal Trade Commission, et al.*, No. 24-cv-1743 (E.D. Pa. July 23, 2024), the court denied the plaintiff’s motion for stay of effective date and preliminary injunction. The parties to that action have requested that the court enter a summary judgment briefing schedule that would continue through October. More recently, on August 15, 2024, the court in *Properties of the Villages v. Federal Trade Commission*, No. 24-cv-316 (M.D. Fla. June 21, 2024), granted the plaintiff’s motion for stay and preliminary injunction, but limited this relief to the named plaintiff. That court has yet to order a schedule for further proceedings.

Enforcement Against Non-Competes Through Individual Adjudication

The FTC spokesperson said that the agency “will keep fighting to stop non-competes that restrict the economic liberty of hardworking Americans, hamper economic growth, limit innovation, and depress wages” and that the “decision does not prevent the FTC from addressing non-competes through case-by-case enforcement actions.” The FTC has asserted that non-competes are unfair methods of competition under section 5 of the FTC Act and that it is consequently empowered to “prevent” entities under its jurisdiction from “using” them. The FTC asserted this power in several adjudicative actions just prior to the promulgation of the Non-Compete Clause Rule, but these were resolved on consent and the FTC’s asserted authority in this area has not been tested by an adversarial proceeding on the merits. Notably, the court in the *ATS Tree Services* action in Pennsylvania, found “that the FTC acted within its authority under the [FTC] Act in designating all non-competes clauses as unfair methods of competition.” Also, under certain circumstances a non-competes agreement may be found to violate the rule of reason under section 1 of the Sherman Antitrust Act. There are also numerous state laws regulating non-competes.

We continue to monitor developments in these actions and the FTC’s treatment of non-competes clauses.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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