Legal Update Article

Texas Court Preliminarily Enjoins FTC from Enforcing Its Non-Compete Ban, but Refuses (for Now) to Extend Order to All Employers

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July 9, 2024

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On July 3, 2024, as anticipated, U.S. District Judge Ada Brown of the U.S. District Court for the Northern District of Texas granted Plaintiffs' and Plaintiff-Intervenors' motion to stay and preliminarily enjoin the effective date of the Federal Trade Commission's (FTC) final rule banning non-competition restrictions. By this Order, the Sept. 4, 2024, effective date of the FTC's non-compete ban is stayed, and the FTC is enjoined from implementing or enforcing the ban. However, at least for now, the Order applies only to the named Plaintiffs in the pending litigation: Ryan LLC, the U.S. Chamber of Commerce, Business Roundtable, Texas Association of Business, and Longview Chamber of Commerce. The Order specifically does not apply to any other employers or even to the members of the Chamber of Commerce and other association Plaintiffs.

In a 33-page decision, the Court found the Plaintiffs proved a likelihood of success on the merits of their claims that the FTC lacks the statutory authority to issue substantive (rather than housekeeping) rulemaking regarding unfair methods of competition, and that the proposed Final Rule is arbitrary and capricious by, among other things, imposing a "one-size-fits-all" approach with no end date.

The Court stated it would issue a merits disposition (akin to a final decision) on or before Aug. 30, 2024, and indications are that the final decision will continue to enjoin the FTC from instituting the non-compete ban. However, because the current preliminary injunction applies only to the named Plaintiffs, there remains uncertainty with respect to the FTC's ability to move forward with the non-compete ban as to those employers who are not Plaintiffs (or members of the association Plaintiffs) in the pending litigation.

In light of Judge Brown's July 3 Order and the resulting uncertainty regarding the non-compete ban's potential impact on employers not linked to the current litigation, there likely will be substantial litigation activity in the coming weeks in advance of the September 4, 2024, proposed effective date of the non-compete ban. While it is difficult to predict exactly how these issues will play out, there are several important points to consider when evaluating potential outcomes.

As an initial matter, it is possible that Judge Brown's final decision (expected on or before Aug. 30, 2024) will differ from the July 3 Order as it relates to non-parties to the litigation. There are several reasons to believe this may occur. First, among the relief sought by lead Plaintiff Ryan is an order vacating and setting aside the proposed non-compete ban. Under Fifth Circuit precedent, such relief, if granted, would extend not only to the Plaintiffs in the Ryan litigation but to non-parties as well. Second, while a preliminary injunction is a limited and "extraordinary" remedy, the merits disposition is a final order and is not held to the same standards. Third, the Order invited the parties to further brief certain issues that Judge Brown found were not sufficiently addressed in

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the previous filings, including the basis for associational standing and nationwide or universal application of any potential Court order striking down the non-compete ban. Perhaps after reviewing this additional briefing, Judge Brown will reverse course and extend the final order to cover non-parties as well.

Further, there are practical reasons why the expected Court order vacating the FTC's non-compete ban may apply universally, including:

1. On May 3, 2024, in the lawsuit originally commenced by the U.S. Chamber of Commerce against the FTC in the Eastern District of Texas (the "Eastern District litigation") the day after Ryan filed its lawsuit in the Northern District, Judge J. Campbell Barker entered an order staying that litigation pending the outcome of the previously filed Ryan lawsuit. In that stay order, Judge Barker noted that because both lawsuits against the FTC are seeking the remedy of vacating the proposed non-compete ban, if the Plaintiffs prevailed the FTC would not be able to enforce the ban against anyone, regardless of whether or not they were a party to any pending litigation. Therefore, even if any final order vacating the non-compete ban by Judge Brown in the Ryan lawsuit does not specifically state that it applies universally, it is possible that other courts, including the Eastern District litigation, will enter an order adopting such a ruling on a nationwide basis.

2. If there is an order vacating the ban, having it not apply universally likely would result in multiple additional lawsuits and motion practice in pending lawsuits brought by other employers seeking to have the relief granted by Judge Brown's order apply to them, as well. This is the type of inefficient, unnecessary, and duplicative litigation that courts usually try to avoid (see, e.g., F.R.C.P. Rule 1), thus providing an additional reason for any order vacating the ban to apply universally.

3. The likely basis for any decision vacating the non-compete ban is not specific to any of the plaintiffs in the pending litigations or their businesses. Rather, all indications are that the non-compete ban will be struck down based on the global actions of the FTC, such as the FTC's lack of authority to promulgate such a rule and the arbitrary and capricious nature of the ban itself.

4. Granting relief to the association intervening plaintiffs as entities is essentially meaningless; the whole purpose of such parties filing suit and seeking injunctive relief was to benefit their members.

Judge Brown's July 3 Order, while expected and a significant initial defeat for the FTC, leaves open the possibility that a final order vacating the non-compete ban for all employers may not be entered prior to the Sept. 4, 2024, effective date. While it may be likely that the FTC ultimately will not be permitted to enforce the ban against any employer, the uncertainty of when such an order will be entered leaves employers who use non-competes with tough choices in the coming weeks. Some employers might assume there will be clarity on this issue well in advance of Sept. 4 and not bother to take steps to prepare for the possibility that the ban may be in place, at least temporarily. Other employers might prudently plan for the ban if it goes into effect, and if it does not, any plans for compliance can be scrapped.

In planning to comply with the FTC's final rule banning non-competes, if the final rule

ever becomes effective, employers should consider the following steps:

- Inventory the restrictive covenants in use to determine if they include true non-competes, provisions that function as non-competes, or provisions that penalize workers for taking employment elsewhere.
- Determine whether such agreements have been signed by "senior executives" within the meaning of the FTC's final rule.
- Prepare and prepare to issue the required notice to non-"senior executives" who are subject to prohibited non-competes.
- Revise agreements for possible future use without prohibited non-competes, focusing on non-solicitation and other permitted restrictions.
- Revise stock grant, deferred compensation, and similar plans or arrangements to eliminate forfeiture for competition provisions.
- Inventory the company's trade secrets and develop or update a robust trade secret protection plan.

Deciding which approach to take is a function of several factors, including the employer's appetite for risk and the agility of its human resources and legal teams to the extent they need to quickly pivot to compliance actions. Regardless of which approach an employer chooses, Jackson Lewis will continue to monitor any changes in the status of the efforts to fight the FTC's non-compete ban, and the firm's attorneys are available to assist with any related strategy issues.