All Roads Lead to Dallas: FTC Non-Compete Rule Set to Face Its First Legal Test in the Northern District of Texas

Amir Tayrani is a partner at Gibson, Dunn & Crutcher LLP in Washington, D.C. Together with Eugene Scalia and Andrew Kilberg, he is representing Ryan, LLC in its challenge to the FTC's Non-Compete Rule.

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The sweeping prohibition on noncompete agreements promulgated by the Federal Trade Commision (FTC)—which would nullify 30 million contracts and preempt the laws of 46 states if it takes effect, as scheduled, on Sept. 4—is set for its first judicial test. In *Ryan, LLC v. FTC*, Judge Ada Brown of the U.S. District Court for the Northern District of Texas has indicated that she expects to rule on the plaintiffs' motions for a stay of the effective date and for a preliminary injunction by July 3. Expedited proceedings in the U.S. Court of Appeals for the 5th Circuit, and perhaps the U.S. Supreme Court, are likely to follow.

The FTC's Non-Compete Rule declares that it is an "unfair method of competition" for a person to enter into or attempt to enter into a noncompete agreement, to enforce or attempt to enforce a noncompete agreement, or to represent that a worker is subject to a noncompete clause. These expansive prohibitions not only apply prospectively but also render tens of millions of *existing* noncompete agreements unenforceable. The only exceptions are for noncompete agreements entered into pursuant to the sale of a business and for existing (but not future) noncompete agreements with "senior executives," narrowly defined as workers who earned more than $151,164 in the prior year and hold a "policy-making position."

Like countless other employers across the United States, Ryan, LLC—a global tax-services firm based in Dallas—uses noncompete agreements to prevent departing principals from poaching Ryan's clients and team members, and as one tool to protect its confidential business information. As Ryan's chairman and CEO Brint Ryan explained in a *Wall Street Journal* op-ed, the Non-Compete Rule "takes away a major tool businesses rely on to protect their intellectual property," while also "threaten[ing] employees' ability to launch and sustain careers" by "mak[ing] it riskier for companies to invest in the development of employees."

Motivated by these concerns, Ryan filed suit challenging the Non-Compete Rule on April 23, hours after the FTC released the rule. Ryan's complaint highlights multiples deficiencies in the Non-Compete Rule, including that it exceeds the FTC's statutory authority, is unconstitutional, and is the product of arbitrary and capricious decisionmaking.

As Ryan explained, the FTC lacks the authority to promulgate substantive rules defining unfair methods of competition—which the agency purported to do in its Non-Compete Rule—because the provision the agency invoked, Section 6(g) of the FTC Act, authorizes only *procedural* rules. That provision says the agency may "[f]rom time to time classify corporations and . . . make rules and regulations for the purpose of carrying out the provisions of this subchapter." It is unfathomable that Congress, in one half of one subsection of a provision addressing procedural matters, provided the FTC with the far-reaching power to issue substantive rules categorically condemning economic practices as unfair methods of competition on a nationwide basis.

Ryan further explained that, even if Congress did grant the FTC authority to promulgate *some* substantive unfair-competition rules, it did not invest the FTC with authority to decide the major question of whether noncompete agreements are categorically unfair and anticompetitive, a question with seismic consequences affecting tens of millions of workers, millions of employers, and billions of dollars in economic productivity. In the absence of clear authorization from Congress, that weighty question rests with the legislature, not unelected bureaucrats. Indeed, Congress could not constitutionally have conferred this authority on the FTC with the open-ended language to which the FTC points, because the statute does not provide an "intelligible principle" to guide a rulemaking defining unfair methods of competition, as required by the Constitution's non-delegation doctrine.

Finally, Ryan identified multiple analytical and evidentiary deficiencies in the Non-Compete Rule that render the rule arbitrary and capricious in violation of the Administrative Procedure Act. In particular, the FTC inconsistently weighed the evidence, using empirical studies in an opportunistic, inconsistent manner and giving logically inconsistent reasons for the rule; ignored numerous categories of costs that the rule will impose; and failed to give meaningful consideration to the many alternative approaches to its *per se* prohibition on noncompetes.

Ryan was not alone in acting swiftly to challenge the Non-Compete Rule. The day after Ryan filed suit in the Northern District of Texas, the U.S. Chamber of Commerce—joined by the Business Roundtable, Texas Association of Business, and Longview Chamber of Commerce—filed suit against the FTC in the U.S. District Court for the Eastern District of Texas. After initial proceedings in that court, the Chamber's case was stayed in order to permit the Chamber to intervene in the *Ryan* action. Judge Brown promptly granted the Chamber's motion to intervene in the case in the Northern District of Texas.

The validity of the FTC's Non-Compete Rule is thus squarely teed up for decision by Judge Brown. Both Ryan and the Chamber have filed motions for a stay and a preliminary injunction, supported by *amicus* briefs from an array of organizations that underscore the rule's breadth and significance, including the National Association of Manufacturers; the National Retail Federation, International Franchise Association, and Associated Builders and Contractors; and the Securities Industry and Financial Market Association. The FTC's opposition is due May 29, replies are due June 12, and a potential hearing is set for June 17. A ruling is expected by July 3, which will leave time for the losing side to seek expedited relief from the 5th Circuit in advance of the rule's Sept. 4 effective date.

Millions of employers across the nation are watching the case closely, as the Non-Compete Rule's Sept. 4 effective date approaches and, with it, the need to prepare FTC-mandated notices to current and former employees subject to noncompetes, examine and update existing employment agreements, and evaluate alternative measures to shield sensitive competitive information from public disclosure. The Northern District of Texas will have the first opportunity to decide whether the FTC has the authority to impose those burdens on employers—or whether, as has been the case for centuries, noncompete agreements will continue to be regulated primarily at the state level. The outcome will determine the continuing efficacy of the statutory and constitutional guardrails on FTC rulemaking and the viability of centuries' old principles of federalism and economic freedom.

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