



UNITED STATES COUNCIL FOR INTERNATIONAL BUSINESS

April 19, 2023

Re: U.S. Council for International Business Comments on the U.S. Federal Trade Commission Non-Compete Clause Rulemaking, Matter No. P201200 (88 CFR 3482)

The United States Council for International Business (“USCIB”) is pleased to submit these comments on the U.S. Federal Trade Commission (“FTC”) Non-Compete Clause Rulemaking, Matter No. P201200 announced on January 5, 2023, and posted on January 19, 2023.¹ While USCIB generally shares the Biden-Harris Administration’s goal of preventing anticompetitive employment practices, we believe this rulemaking overreaches both in terms of the breadth of the ban and scope of FTC rulemaking authority.

USCIB is a member-driven association that promotes open markets, competitiveness and innovation, sustainable development, and corporate responsibility, supported by international engagement and regulatory coherence. Its members include U.S.-based global companies and professional services firms from every sector of the economy, with operations in every region of the world, generating \$5 trillion in annual revenues and employing over 11 million people worldwide. As the U.S. affiliate of the International Chamber of Commerce (ICC), the International Organization of Employers (IOE), and Business at OECD (known as BIAC), USCIB helps to provide business views to policy makers and regulatory authorities worldwide and works to facilitate international trade and investment.²

USCIB challenges the lack of evidence and methodologies used to support the FTC’s proposed rulemaking on non-competes clauses and is alarmed about the deleterious impacts the proposal will have on U.S. innovative industries. Not only does it break with longstanding legal precedent such as the consumer welfare standard and fact-specific inquiry, but it will irreparably harm U.S. companies that rely on non-competes to safeguard intellectual property rights and trade secrets. We also challenge the legal authority under which the FTC is issuing a binding regulation relating to unfair methods of competition. In no instance do we see FTC rulemaking authority explicitly provided by Congress, and there are significant and legitimate questions of any exercise of such authority based on the major questions and non-delegation doctrines, for example.

We respectfully offer the following analysis to support the concerns highlighted in the preceding paragraphs.

¹ Press Release, FTC Proposes Rule to Ban Noncompete Clauses, Which Hurt Workers and Harm Competition (Jan. 5, 2023) <https://www.ftc.gov/news-events/news/press-releases/2023/01/ftc-proposes-rule-ban-noncompete-clauses-which-hurt-workers-harm-competition>; Federal Register Notice at <https://www.govinfo.gov/content/pkg/FR-2023-01-19/pdf/2023-00414.pdf>.

² USCIB at a Glance, <https://www.uscib.org/uscib-at-a-glance-ud-2410/>.

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I. The FTC Has No Competition Rulemaking Authority

The FTC Act’s text, structure, and history, as well as recent guidance from the U.S. Supreme Court, all point in the same direction: the FTC lacks statutory authority to promulgate a rule banning or severely restricting non-compete clauses or any other practice. Section 5 of the FTC Act prohibits “unfair methods of competition” (UMC), and Section 6(g) states that the Commission “shall have power . . . [f]rom time to time to classify corporations and . . . to make rules or regulations for the purpose of carrying out the [Act’s] provisions.” 15 U.S.C. §§ 45, 46(g). Nothing in the Act’s text expressly or impliedly gives the FTC rulemaking authority to prohibit competitive methods that the FTC deems unfair. Nowhere, for example, does the Act state that the FTC shall or may promulgate rules to determine whether certain types of competitive methods are fair or unfair, to supplant state law, or to invalidate entire categories of business and employment contracts on competitive grounds.

The FTC Act’s structure confirms that the FTC lacks unfair methods of competition (“UMC”) rulemaking authority. In sharp contrast to the silence of the Act’s text on such authority, Congress expressly granted the FTC authority to promulgate other rules. For example, statutes such as the Children’s Online Privacy Protection Act and Telemarketing and Consumer Fraud and Abuse Prevention Act expressly grant the FTC the authority to engage in notice and comment rulemaking to enforce their provisions. Congress also provided the FTC explicit rulemaking authority for unfair and deceptive acts and practices through the Magnuson-Moss Warranty – Federal Trade Commission Improvement Act of 1975. In these statutes, Congress clearly defined the scope of its delegation to the FTC, either in terms of a proposed rule’s substantive scope or its procedural path, or both.

Moreover, the FTC Act fails to provide for any sanctions for violations of rules promulgated pursuant to Section 6. Again, this omission strongly suggests that Congress never intended to give the FTC substantive, binding UMC rulemaking authority at all. As the American Bar Association (“ABA”) explained, the Act’s “fail[ure] to provide any sanctions for violating any rule adopted pursuant to Section 6(g) . . . strongly suggest[s] that Congress did not intend to give the agency substantive rulemaking powers when it passed the Federal Trade Commission Act.”³

Recognizing its lack of authority, the FTC has hesitated to assert that it has UMC rulemaking authority. Until 1962, and for more than half a century since the enactment of Magnuson-Moss in 1975, the FTC never attempted to promulgate a UMC rule. Indeed, even prior to 1975, only once had the FTC’s authority to conduct rulemaking under Section 6(g) been tested in court. See *National Petroleum Refiners Association v. FTC*, 482 F.2d 672 (D.C. Cir. 1973). That silence speaks volumes.

Recent U.S. Supreme Court decisions confirm that the FTC cannot assert broad authority without an express grant from Congress. In *AMG Capital Management v. FTC*, 141 S. Ct. 1341 (2021), the U.S. Supreme Court unanimously rejected the FTC’s claim that it could assert broad remedial powers without an express grant of authority from Congress. Likewise, the nondelegation doctrine requires Congress to provide “an intelligible principle” to assist the agency to which it has delegated legislative discretion. *J. W. Hampton, Jr., & Co. v. United States*, 276 U.S. 394, 409 (1928); *Gundy v. United States*, 139 S. Ct. 2116 (2019). Finally, the major-questions doctrine also requires Congress to “speak clearly if it wishes to assign to an agency decisions of vast economic and political significance.”⁴ That principle recognizes that

³ ABA, *Comments of the Antitrust Law Section of the American Bar Association in Connection with the Federal Trade Commission Workshop on “Non-Competes in the Workplace: Examining Antitrust and Consumer Protection Issues”* at 54

⁴ *Utility Air Reg. Grp.*, 573 U.S. at 324; see also *Nat’l Fed. of Indep. Bus. v. Occupational Health & Saf. Admin.*, 142 S. Ct. 661, 665 (2022).

“extraordinary grants of regulatory authority are rarely accomplished through modest words, vague terms, or subtle devices,” even when there is a “colorable textual basis” for the agency’s position.⁵ Pursuant to the reasoning of *AMG* and both the non-delegation and major question doctrines, Congress has not given the FTC the authority to promulgate such a vast rule.

II. Applicability for Non-competes Should Remain Case Dependent

Critical to the success of companies at the forefront of innovation is the ability to make significant long-term investments. This includes, but is not limited to, basic and applied research and development focused on emerging fields, products, and services – as well as investments in human capital, i.e., people. Non-competes are a critical tool to safeguard these investments from illegitimate access or misappropriation and ensure they remain a driver of economic growth and America’s competitive success.

Despite this, the FTC’s proposed rule is a near-complete ban on the use of employer-worker non-compete agreements without exceptions which ignores commercial risk concerns. The rule does not contain exceptions for high income workers/workers with access to confidential information. And while there is criticism of non-competes for low-wage employees (or employees in roles where there is no or limited exposure to sensitive nonpublic proprietary information), there are instances where they are an essential tool for companies to protect intellectual property, trade secrets and other confidential information.

III. State Law Versus Federal Blanket Ban

A number of states have legislated and passed tailored laws with respect to non-competes clauses that are not outright bans. These include the following means:

- Setting salary thresholds (and not all states do this for “highly compensated” employees). For example, the Illinois Freedom to Work Act prohibits non-competes on employees earning less than \$75,000 per year;
- Carving out forfeiture for competition agreements and non-solicitation covenants. The FTC’s proposed rule does not currently include an exception for these and other important employer protections, and thus arguably are included as “de facto” non-competes;
- Providing a requisite notice period prior to effective date (e.g., 14 days); and
- Advising employees to consult with counsel.

It is also important to note that states have not chosen to provide exceptions for discretionary terms or conditions such as job description or title because of ambiguity across sectors and industries. Similarly, they have not chosen to provide exceptions for a top pay percentage of employees since that would also be difficult to consistently determine.

IV. The FTC’s Proposed Rule Provides No Reliable Evidence that the Near-Complete Bans on Non-Compete Clauses in Three States Lead to Increased Economic Activity

The FTC’s proposed rule identifies only three states – California, North Dakota, and Oklahoma – that supposedly “have adopted statutes rendering non-compete clauses void for nearly all workers.”⁶ Despite what the FTC’s proposed rule characterizes as near-complete bans, the FTC’s proposed rule concludes that “California has become the global center of the technology sector,” and “the energy industry has thrived”

⁵ *West Virginia v. Env’tl Protec. Agency*, 142 S. Ct. 2587, 2609 (2022).

⁶ FTC’s proposed rule at 49.

in North Dakota and Oklahoma.⁷ But the FTC’s proposed rule’s characterization of California law is incomplete, and the energy industry’s success in North Dakota and Oklahoma has far more to do with the location of oil reserves and other natural resources than with employment contracts.

California’s ban on non-compete agreements is not as comprehensive as the FTC’s proposed rule suggests. California has long allowed non-compete clauses if they are necessary to protect trade secrets.⁸ While the California Supreme Court has not yet addressed the scope of this exception,⁹ its existence weighs against adopting a non-compete rule that offers no protection for trade secrets and other confidential information.¹⁰

Nor is it clear that these three states’ non-compete laws have furthered innovation, and the opposite may well be true. For example, Silicon Valley’s emergence as a technology epicenter is largely because many universities focused on science-based research, such as Stanford, are in California, along with a plethora of venture-capital firms.¹¹ As for Oklahoma’s and North Dakota’s energy industries, the success of those states’ industries stems from where natural resources are located – not the lack of non-compete clauses – and both states lag in the type of innovation that non-compete clauses seek to further.¹² A 2022 study ranked “North Dakota 49th among the 50 states and District of Columbia in innovation based on a score drawn from 22 key indicators, including the share of STEM professionals – those working in science, technology, engineering and math – as well as per-capita research and development spending.”¹³ Oklahoma similarly lags most jurisdictions, ranked as 39th out of 50 states and District of Columbia in innovation.¹⁴

The FTC’s proposed rule also fails to compare the alleged California, North Dakota, and Oklahoma data with that of the 47 States who do not have similar restrictions on non-competes. Such a comparison is crucial empirical data in this context.

The near-universal acceptance of trade secrets as a legitimate business interest should not be overridden based on these three outlier state laws and scant evidence that their so-called “near-complete bans” caused certain industries to flourish.

⁷ FTC’s proposed rule at 100-01.

⁸ See *Muggill v. Reuben H. Donnelley Corp.*, 62 Cal. 2d 239, 242 (Cal. 1965) (stating the California Business Code “invalidates provisions in employment contracts prohibiting an employee from working for a competitor after completion of his employment or imposing a penalty if he does so unless they are necessary to protect the employer’s trade secrets” (internal citations omitted)).

⁹ *Edwards v. Arthur Andersen LLP*, 189 P.3d 285, 289 n.4 (Cal. 2008).

¹⁰ Similarly, Oklahoma has an exception to its non-compete ban when the non-compete is narrowly construed to bar solicitation of “goods or services from the employer’s established customers.” *Howard v. Nitro-Lift Techs., LLC*, 2011 OK 98, ¶ 21.

¹¹ Manuel Castells, *The Rise of the Network Society* at 52 (2nd ed., Wiley-Blackwell 2011).

¹² See *Six U.S. States Accounted for Over Half of the Primary Energy Produced in 2019*, U.S. Energy Information Admin. (Aug. 31, 2021), <https://www.eia.gov/todayinenergy/detail.php?id=49356>.

¹³ Patrick Springer, *North Dakota Lags Near Bottom of States in Innovation Rankings*, The Dickinson Press (Mar. 28, 2021), <https://www.thedickinsonpress.com/business/north-dakota-lags-near-bottom-of-states-in-innovation-rankings>.

¹⁴ *Id.*

V. Using Non-Compete Clauses to Protect Trade Secrets and Other Confidential Information Is a Legitimate Business Interest

As the ABA has emphasized, the “[p]rotection of trade secrets enjoys the most universal recognition as a legitimate business justification for non-competes.”¹⁵ Indeed, the FTC’s proposed rule acknowledges that “[n]early all states recognize the protection of an employer’s trade secrets as a legitimate interest.”¹⁶ This justification is so well established that it is the model approach in the Restatement (Second) of Contracts,¹⁷ codified by many states,¹⁸ and enforced by courts across the country.¹⁹

When the FTC held a workshop to address the use of non-competes in January 2020, every contributor that addressed the subject recognized that protecting trade secrets and other confidential information with a non-compete clause is a legitimate business interest. *See, e.g.,* FTC Workshop, *Non-Competes in the Workplace: Examining Antitrust and Consumer Protection Issues*, Tr. 12:23-13:1 (Professor Orly Lobel: “So the legitimate business interest, I mentioned already trade secrets. Those are, I think, the best case for protectable interests that the employer might claim”); 122:17-19 (Economist Ryan Nunn: “The potential explanations that emphasize social benefits are typically – and in my view most importantly – trade secrets”); 134:13-16 (Nunn: “You can try to limit non-competes to jobs that have trade secrets. That sort of aligns them with what I think is the most powerful social justification for the non-competes.”).

¹⁵ Comments of the Antitrust Law Section of the American Bar Association in Connection with the Federal Trade Commission, at 14 (Apr. 24, 2020); *see also* U.S. Chambers of Commerce’s Comment Regarding Non-Compete Clauses Used in Employment Contracts at 2 (Mar. 10, 2020) (“State legislatures and courts nationwide recognize that an employer has a legitimate interest in protecting against a competitor’s acquisition of its sensitive business information through engaging a former employee.”).

¹⁶ Federal Trade Commission, Non-Compete Clause Rule at 52 (Jan. 5, 2023) (to be codified at 16 C.F.R. § 910), <https://www.ftc.gov/legal-library/browse/federal-register-notice/non-compete-clause-rulemaking>.

¹⁷ Restatement (Second) of Contracts § 188 cmt. f (1981) (“[An] employer has a legitimate interest in restraining the employee from appropriating valuable trade information”).

¹⁸ *See, e.g.,* Ark. Code Ann. § 4-75-101(b)(1); Colo. Rev. Stat. Ann. § 8-2-113(3); Fla. Stat. § 542.335(1)(e); Idaho Code § 44-2702(2); 820 Ill. Comp. Stat. 90/5; Mass. Gen. Laws ch. 149, § 24L(b)(iii).

¹⁹ *See, e.g., Biesse Am., Inc. v. Dominici*, 2019 NCBC LEXIS 50, at *27 (N.C. Super. Ct. Aug. 19, 2019) (“Our courts have recognized that protection of confidential information and trade secrets is a legitimate purpose of a non-compete.” (citing *United Lab., Inc. v. Kuykendall*, 322 N.C. 643, 650 (1988))); *Saturn Wireless Consulting, LLC v. Aversa*, 2017 U.S. Dist. LEXIS 65371, at *32 (D.N.J. Apr. 26, 2017) (“New Jersey courts considering restrictive covenants ‘recognize as legitimate the employer’s interest in protecting trade secrets, confidential information, and customer relations.’” (citation omitted)); *Whelan Sec. Co. v. Kennebrew*, 379 S.W.3d 835, 842 (Mo. 2012) (a non-compete is enforceable “to the extent that the restrictions protect the employer’s trade secrets or customer contacts”); *Mattern & Assocs., LLC v. Seidel*, 678 F. Supp. 2d 256, 267 (D. Del. 2010) (“The legitimate business interests present in the record before the court include, among other commercially sensitive information and trade secrets”); *Syncom Indus. v. Wood*, 155 N.H. 73, 79 (2007) (“Legitimate interests of an employer that may be protected from competition include: the employer’s trade secrets that have been communicated to the employee during the course of employment”); *Bryceland v. Northey*, 160 Ariz. 213, 216 (Ct. App. 1989) (“[A post-employment restraint] must usually be justified on the ground that the employer has a legitimate interest in restraining the employee from appropriating valuable trade information and customer relationships to which he has had access in the course of his employment.”); *Data Mgmt. v. Greene*, 757 P.2d 62, 65 (Alaska 1988) (“Among the factors properly to be considered are whether the employee is possessed with confidential information or trade secrets”); *Hasty v. Rent-A-Driver, Inc.*, 671 S.W.2d 471, 473 (Tenn. 1984) (“Such legitimate business interests include trade or business secrets or other confidential information”); *Sys. Concepts v. Dixon*, 669 P.2d 421, 426 (Utah Sup. Ct. 1983) (“We hold that a covenant is valid which protects good will as well as trade secrets”); *Reddy v. Cmty. Health Found. of Man*, 171 W. Va. 368, 378-79, 298 (1982) (“The situations most likely to give rise to such an injury [to their business] are those where the employer stands to lose his investment in employee training, have his trade secrets or customer lists converted by the employee.”).

This well-recognized justification should not be disturbed. Trade secrets and other confidential information are a positive sum aspect of the American economy: employers make costly investments to innovate and create trade secrets, which then help increase macroeconomic output.²⁰ As the U.S. Department of Treasury has recognized, additional economic activity and broader information sharing are spurred by non-competes.²¹ For example, a 2016 report by the U.S. Department of Treasury observes that non-competes solve an economic holdup problem in which “worker and firm have an interest in sharing vital information, as this raises the worker’s productivity.”²² The holdup problem is particularly acute when innovation is implicated. The FTC’s proposed non-compete rule risks limiting employer-employee information exchanges on trade secrets, production processes, and other proprietary or confidential information.

The holdup problem also extends to worker training and other investments because many businesses are reluctant to invest without assurance that employees will maintain their employment for a reasonable period after the investment.²³ The FTC’s proposed rule also acknowledges that two other studies demonstrate a positive relationship between non-compete enforceability and investment.²⁴ One of these studies found that knowledge-intensive firms, which are likely to produce trade secrets, invested 32 percent less in capital equipment following decreases in the enforceability of non-compete clauses.²⁵ Although the FTC’s proposed rule “places relatively minimal weight on these studies” because other factors “may” influence such investments, that does not mean that these studies should simply be dismissed or that the use of non-competes is not a critical factor.²⁶

Notably, by including a narrow exception to the FTC’s proposed non-compete ban for the sale of a business, the FTC’s proposed rule recognizes that the non-competes are necessary to “protect the value of a business acquired by a buyer.”²⁷ The FTC’s proposed rule recognizes that restricting non-compete clauses in this circumstance could reduce “incentives of various market actors to start, sell, or buy businesses.”²⁸ This narrow proposition conflicts with other rationale for the FTC’s proposed rule, such as statements that non-

²⁰ Ryan Nunn, *Fellow in Economic Studies at the Brookings Institution, Remarks at the Federal Trade Commission’s Workshop on Non-Competes in the Workplace: Examining Antitrust and Consumer Protection Issues* at 123, 125 (Jan. 9, 2020) (transcript available at https://www.ftc.gov/system/files/documents/public_events/1556256/non-compete-workshop-transcript-full.pdf).

²¹ OFFICE OF ECON. POLICY, U.S. DEP’T OF THE TREASURY, NON-COMPETE CONTRACTS: ECONOMIC EFFECTS AND POLICY IMPLICATIONS at 9-10 (2016), https://home.treasury.gov/system/files/226/Non_Compete_Contracts_Economic_Effects_and_Policy_Implications_MAR2016.pdf.

²² *Id.* at 7.

²³ *Id.* at 7.

²⁴ FTC’s proposed rule at 45-48 (citing Evan Starr, *Consider This: Training, Wages, and the Enforceability of Non-Compete Clause*, 72 I.L.R. Rev. 783, 796-97 (2019) and Jessica Jeffers, *The Impact of Restricting Labor Mobility on Corporate Investment and Entrepreneurship* 22, 28 (2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3040393).

²⁵ *Id.* at 46 (citing Jessica Jeffers, *The Impact of Restricting Labor Mobility on Corporate Investment and Entrepreneurship* at 22 (2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3040393).

²⁶ *Id.* at 22-23 (citing Evan P. Starr, James J. Prescott, & Norman D. Bishara, *Noncompete Agreements in the U.S. Labor Force*, 64 J. L. & Econ. 53, 75 (2021)); *id.* at 28-29 (citing Evan Starr, Natarajan Balasubramanian, & Mariko Sakakibara, *Screening Spinouts? How Noncompete Enforceability Affects the Creation, Growth, and Survival of New Firms*, 64 Mgmt. Sci. 552, 561 (2018)).

²⁷ FTC’s proposed rule at 106; *see also* Dissenting Statement of Commissioner Christine S. Wilson Regarding the Notice of Proposed Rulemaking for the Non-Compete Clause Rule, Commission File No. P201200-1 at 9 (Jan. 5, 2023), https://www.ftc.gov/system/files/ftc_gov/pdf/p201000noncompetewilsondissent.pdf (“Wilson Dissent”).

²⁸ FTC’s proposed rule at 129-30.

competes “limit entrepreneurship and new business formation” by “decreasing the flow of information and knowledge among firms.”²⁹ While the FTC’s proposed rule claims that protecting the value of a business is unique to a non-compete between the buyer and seller of a business,³⁰ there is no principled basis to exclude protections of trade-secret and other confidential information under the proposed non-compete rule, which is similarly necessary to maintain incentives for any market actor to continue to innovate and increase economic output.³¹

Finally, not only do non-competes enhance innovation and output, but evidence also shows that non-competes do not systematically reduce employee welfare. The FTC’s proposed rule recognizes that non-compete clauses have been linked to higher earnings and increased job creation, along with the increase in worker training and other investments described above.³² In fact, senior executives who, as a general matter have access to competitively sensitive, confidential information, are an example of the types of employees for which it would be reasonable for an employer to seek a non-compete, and who are well-positioned to negotiate benefits – such as long-term incentives and other compensation – in exchange for their willingness to agree to noncompete provisions. Despite this evidence, the FTC’s proposed rule questions the “probative” value of such data because other factors “may” be an influencing factor.³³ But even if that is true in certain circumstances, no basis exists to disregard these studies altogether or ignore that employees subject to non-competes who handle trade secrets are highly educated and should expect large salaries. Indeed, as a 2019 FTC publication analyzing non-competes acknowledges, “to the extent that non-compete agreements mitigate holdup, we should expect to see wages rise over a worker’s tenure, all else equal.”³⁴

In short, a sweeping ban on non-competes that does not provide an exception for the protection of trade secrets and other confidential information unjustifiably risks a reduction in productivity and incentives to innovate and invest in workers.³⁵

VI. The FTC’s Proposed Rule Incorrectly Concludes That There Is a Lack of Evidence Showing that Non-Compete Clauses Reduce Trade-Secret Misappropriation

The FTC’s proposed rule also seeks to justify a near-complete ban on non-compete clauses because the FTC “is not aware of any evidence non-compete clauses reduce trade secret misappropriation or the loss of other types of confidential information.”³⁶ But evidence does, in fact, suggest that non-compete clauses reduce trade secret and other confidential information misappropriation.

²⁹ Statement of Chair Lina M. Khan Regarding Joined by Commissioner Rebecca Kelly Slaughter and Commissioner Alvaro M. Bedoya Regarding the Notice of Proposed Rulemaking to Restrict Employers’ Use of Noncompete Clauses at 1, Commission File No. P201200 (Jan. 5, 2023), https://www.ftc.gov/system/files/ftc_gov/pdf/statement-of-chair-lina-m-khan-joined-by-commrs-slaughter-and-bedoya-on-noncompete-nprm.pdf.

³⁰ FTC’s proposed rule at 129.

³¹ See Global Antitrust Institute, Comment Letter In Connection With the Federal Trade Commission Workshop on Non-Compete Clauses Used in Employment Contracts at 3 (Feb. 10, 2020), <https://www.regulations.gov/comment/FTC-2019-0093-0243>.

³² FTC’s proposed rule at 22-23, 28-29, 45-47.

³³ *Id.* at 23-24, 29.

³⁴ John M. McAdams, *Non-Compete Agreements: A Review of the Literature*, Federal Trade Commission Bureau of Economics at 3, 6 (Dec. 31, 2019).

³⁵ See Global Antitrust Institute, Comment Letter In Connection With the Federal Trade Commission Workshop on Non-Compete Clauses Used in Employment Contracts at 3 (Feb. 10, 2020), <https://www.regulations.gov/comment/FTC-2019-0093-0243>.

³⁶ FTC’s proposed rule at 92.

For example, many sources cited in the FTC’s December 2019 publication, *Non-Compete Agreements: A Review of the Literature*, acknowledge that the unenforceability of most non-compete clauses in California is a perceived *benefit* to competitors who are able to acquire confidential information.³⁷ Citing an article by Professor Ronald Gilson on the effects of limited non-compete enforcement in the development of Silicon Valley, the FTC’s *Review of the Literature* observes that:

[G]reater worker mobility may lead to knowledge spillovers that spread information to other firms, enhancing their productivity..... On the other hand, firms may be reluctant to invest in risky R&D when departing workers can transfer proprietary information to competitors.³⁸

And a 2016 empirical study of Silicon Valley’s development, cited in the FTC’s *Review of the Literature*, further observes that:

[T]he costs of knowledge spillovers can be substantial even when all human capital is general and when firms retain full control over their trade secrets and technology. As a contractual form, non-compete agreements are well-suited to inhibiting both these sorts of knowledge spillovers.³⁹

As noted, sweeping claims that a prohibition on most non-compete clauses is a primary factor in the growth of Silicon Valley have been challenged both as a mischaracterization of California law and as a failure to recognize similar growth in jurisdictions with greater enforcement of non-compete clauses.⁴⁰

Ignoring this evidence from the FTC’s *Review of the Literature*, the FTC’s proposed rule also asserts that “there is little reliable empirical data on trade secret theft and firm investment in trade secrets in general, and no reliable data on how non-compete clauses affect these practices.”⁴¹ According to the FTC’s proposed rule, “these are difficult areas for researchers to study, due to, for example, the lack of a governmental registration requirement for trade secrets and the unwillingness of firms to disclose information about their practices related to trade secrets.”⁴² But the FTC’s proposed rule also fails to consider that the lack of relevant data is likely because non-compete clauses in the trade-secret context are usually the subject of fact-specific circumstances and analyzed at a level of granularity that is difficult, if not impossible, to replicate in broad academic surveys.

Ultimately, if the FTC considers the availability of relevant data to be insufficient, this uncertainty counsels against adopting a broad non-compete ban that fails to protect trade secrets. Aside from the many questions concerning the overall legal authority, a cautious, incremental approach to regulation is more appropriate.⁴³

³⁷ McAdams, *supra* note 36, at 8.

³⁸ *Id.* at 8 (citing Robert J. Gilson, *The Legal Infrastructure of High Technology Industrial Districts: Silicon Valley, Route 128, and Covenants not to Compete*, 74 N.Y.U.L. REV. 575 (1999)).

³⁹ Fallick, Bruce, Charles A. Fleischman, and James B. Rebitzer, *Job-Hopping in Silicon Valley: Some Evidence Concerning the Microfoundations of a High-Technology Cluster*, REVIEW OF ECONOMICS AND STATISTICS 88(3) at 475 n.14 (2006) (cited in McAdams, *Non-Compete Agreements: A Review of the Literature*, Federal Trade Commission Bureau of Economics at 11, 15 (Dec. 31, 2019)).

⁴⁰ See generally Jonathan M. Barnett & Ted Sichelman, *The Case for Noncompetes*, 87 U. CHI. L. REV. 953, 978-1009 (June 2020).

⁴¹ FTC’s proposed rule at 92.

⁴² *Id.*

⁴³ See, e.g., Paul Crampton, *Striking the Right Balance Between Competition and Regulation: The Key is Learning From Our Mistakes*, Org. for Eco. Co-Operation and Dev. (OECD) ¶ 8 (Oct. 2002) (explaining that studies

A more incremental solution would allow the FTC to gain valuable additional data and achieve the primary goals of the proposed rule without abruptly disrupting a pillar of trade-secret protection.

VII. NDAs and Trade Secret Law Do Not “Reasonably Accomplish the Same Purposes” as Non-Compete Clauses

The FTC’s proposed rule suggestion that non-disclosure agreements and trade-secret law “reasonably accomplish the same purposes” as non-compete clauses overlooks key limitations and market realities.⁴⁴

To begin with, an employer must overcome significant challenges when trying to determine whether an ex-employee has disclosed trade secrets or other confidential information to a rival employer. Without non-competes, employers would need to expend time and resources monitoring ex-employees and their competitors.⁴⁵ Trade-secret theft is also particularly challenging to discover and prosecute both because an ex-employee may simply rely on their knowledge of trade secrets or other confidential information while improving a rival’s production processes, without overtly transferring the secrets per se.⁴⁶ After all, a competitor rarely announces to the market that its internal and non-public activities relied on the use of a competitor’s trade secrets. And any resulting litigation is prone to unpredictability, as courts are hard-pressed to sort through conflicting testimony about where an idea or proprietary information originated.⁴⁷

In addition, non-disclosure agreements and trade-secret law offer limited remedies. For instance, while the Defend Trade Secrets Act of 2016 provides injunctive relief for successful claims of trade-secret misappropriation, it does not permit injunctions to “prevent a person from entering into an employment relationship” and requires that “conditions placed on such employment [be] based on evidence of threatened misappropriation and not merely on the information the person knows.”⁴⁸ Successful lawsuits may also prove wasteful and insufficient if an ex-employee is judgment proof. And this type of litigation is often burdensome, costly, and protracted.⁴⁹

More importantly, non-competes minimize the risk that trade secrets are revealed to a rival in the first place. Litigation is a disfavored remedy because it operates *ex-post* once a trade secret is disclosed and the damage likely cannot be undone. The value employers assign to trade-secret protection is not rooted in recovering damages. Businesses are concerned about ensuring that their direct competitors cannot freeride off the time, money, and labor invested in developing valuable trade secrets. Non-competes uniquely protect against these harms.

Indeed, courts have long recognized the difficulty of proving trade-secret or confidential information misappropriation and encourage the use of non-competes. For example, some courts have recognized a claim of threatened misappropriation based on the doctrine of inevitable disclosure. This doctrine assumes that

consistently show overregulation has inhibited “large price reductions to consumers and substantial improvements in quality and service”); *Changes in Latitudes, Changes in Attitudes: Enforcement Cooperation in Financial Markets*, U.S. Dep’t of Justice at 3 (June 22, 2020) (“[I]ntroducing or increasing regulatory burdens can impair competition by increasing costs which, in turn, can disproportionately affect smaller firms or reduce the likelihood of new entry.”).

⁴⁴ FTC’s proposed rule at 93 (emphasis added).

⁴⁵ See Alan J. Meese, *Don’t Abolish Employee Noncompete Agreements*, 57 WAKE FOREST L. REV. 631 (2022), 631, 694-695 (2022); Global Antitrust Institute, *supra* note 31, at 5.

⁴⁶ See Eric A. Posner, *The Antitrust Challenge to Covenants Not to Compete in Employment Contracts*, 83 ANTITRUST L. J. 165, 180 (2020).

⁴⁷ See Meese, *supra* note 47, at 695.

⁴⁸ Pub. L. No. 114-153, 130 Stat. 376, 379-380 (2016) (codified at 18 U.S.C. § 1836(b)(3)(A)(i)(I) (2018)).

⁴⁹ Nunn, *supra* note 20, at 125.

after an employee has gained knowledge of confidential information while working for a business, they “cannot possibly forget or refrain from relying on that knowledge during [their] employment with the competitor.”⁵⁰ Still, “[w]hile the inevitable disclosure doctrine may serve the salutary purpose of protecting a company’s investment in its trade secrets, its application is fraught with hazards,” and “a non-compete clause is the best way of promoting predictability during the employment relationship and afterwards.”⁵¹

It must also be noted that the FTC has signaled that NDAs, too, can be outlawed, so how can the FTC suggest they be used to accomplish the same thing as non-competes?

VIII. Any Final Rule Limiting Non-Competes, If Implemented, Should Contain An Express Exception Protecting Trade Secrets Based on Well-Established Factors

As discussed above, the FTC’s proposed rule should not be implemented in any form. However, if the FTC implements a final rule, it should contain an express exception for non-compete clauses that are reasonably tailored to protect confidential information and intellectual property like trade secrets. As discussed above, such an exception follows long-established precedent and limits unintended and perhaps severe consequences on businesses and state economies. This exception would also align with what other substantive comments submitted to the FTC have proposed.⁵²

IX. Lack of Clarity for Companies Regarding What Conduct Is Allowed/Disallowed

The proposed language attempts to apply a functional test that prohibits so-called “de facto” non-compete clauses that have the effect of actual non-compete clauses.

As drafted, the language adds a significant degree of uncertainty for stakeholders, because an endless number of clauses may be argued to indirectly have an effect on employment after the conclusion of the worker’s employment, while the proposed language only offers a few examples.

This is a completely unbound and undefined assertion of authority that we would like to see stricken. Alternatively, to provide clear guidance and transparency which are goals advanced by the FTC⁵³ and helpful for stakeholders’ compliance efforts, we recommend that a closed list of examples of de facto non-compete clauses be provided, so that companies will know clearly what clauses they should avoid.

⁵⁰ M. Claire Flowers, *Facing the Inevitable: The Inevitable Disclosure Doctrine and the Defend Trade Secrets Act of 2016*, 75 Wash. & Lee L. Rev. 2207, 2216 (2018); *see also* Antitrust Law Section of the American Bar Association, Comment Letter in connection with the Federal Trade Commission Workshop on Non-Compete Clauses Used in Employment Contracts at 27 n.95 (Apr. 24, 2020), <https://www.regulations.gov/comment/FTC-2019-0093-0243>.

⁵¹ *EarthWeb, Inc. v. Shlack*, 71 F. Supp. 2d 299, 311 (S.D.N.Y. 1999), *remanded for further explanation*, 205 F.3d 1322 (2d Cir. 2000), *subsequently aff’d*, No. 99-9302, 2000 WL 1093320 (2d Cir. 2000).

⁵² *See, e.g.*, Herbert Hovenkamp, Thoughts on FTC Policy on Employee/Independent Contractor Noncompete Agreements at 1 (Jan. 11, 2023), <https://www.regulations.gov/comment/FTC-2023-0007-0348> (recognizing that certain non-compete agreements “do server to protect legitimate employer concerns about . . . protection of confidential information”).

⁵³ *See* https://www.ftc.gov/system/files/documents/reports/2018-2022-strategic-plan/ftc_fy18-22_strategic_plan.pdf “Strategies.... Provide transparency in the decision-making process, through comment periods, press releases, policy guidance, and analyses to aid public comment, and ensure existing guidance is up-to-date.”; *See also* The 2019 OPEN Government Data Act, which recognizes the importance of government transparency and collaboration with its citizens <https://www.ftc.gov/policy-notice/open-government>.

X. The Alternatives in Part VI of the FTC’s Proposed Rule Are Not Workable

The FTC seeks comment on several alternative rules that are variations on (1) a rebuttable presumption of illegality instead of a blanket ban and (2) differentiation among different types of workers (based on job function, salary or other factors) instead of a blanket ban for all workers.⁵⁴ Neither dimension of these alternatives is workable; all, in one way or another, upend a century of established antitrust case law governing this issue.

First, the rebuttable presumption approach ignores established law and market realities.

- The FTC posits that this approach is similar to a “quick look” analysis “where, ‘based upon economic learning and the experience of the market, it is obvious that a restraint of trade likely impairs competition.’”⁵⁵ However, courts recognize that there are few situations that justify a “quick look” review, and none have applied it to a non-compete agreement.⁵⁶
- In addition, one need look no further than the state-by-state survey cited in the FTC’s proposed rule itself to see that the vast majority of states allow non-compete clauses and recognize – in caselaw, statutes, or both – a myriad of legitimate interests protectible by non-compete clauses, including trade secrets, confidential information, goodwill, and even the *prevention* of unfair competition.⁵⁷ This clearly contradicts the FTC’s position that it is “obvious” that all non-compete clauses impair competition such that the FTC can dispense in all cases with making a showing of actual harm to competition before the burden shifts to the employer.
- The use of a rebuttable presumption is also objectionable in that it shifts the burden of proof, a drastic change better reserved for the legislature. Even the state legislatures that have included rebuttable presumptions in their non-compete statutes have done so only to create presumptively legal safe harbors – e.g., a non-compete clause of 18 months or less is presumptively reasonable – rather than the presumptively illegal approach the FTC proposes.
- Finally, the rebuttable presumption approach is not workable for the reasons the FTC acknowledges in the FTC’s proposed rule.⁵⁸ Both businesses and workers need predictability and clarity, yet they would not know at the time a non-compete is entered into, and possibly for a long time thereafter, whether the FTC might eventually challenge it or whether it will be upheld. That does not make the bright-line of the proposed blanket ban the preferred alternative; such a ban is unauthorized and ill-conceived for the reasons stated above.

Second, differentiating among different categories of workers rather than imposing a blanket ban would be exceedingly difficult and unavoidably arbitrary. As noted previously, the institution of non-compete clauses to employees should be based solely on access to and handling of trade secrets and confidential information. Setting a threshold based on arbitrary lines – earnings, exempt status, or other factors – would not necessarily bear on whether the employee has access to trade secrets or other confidential information.

⁵⁴ As with the proposed blanket ban, the FTC lacks the authority to promulgate the alternative rules.

⁵⁵ FTC’s proposed rule at 140.

⁵⁶ *United States v. Booz Allen Hamilton Inc.*, 2022 WL 9976035, at *4 (D. Md. Oct. 17, 2022); *see also Nat’l Collegiate Athletic Ass’n v. Alston*, 141 S. Ct. 2141, 2156 (2021) (stating that “quick look” is proper only when courts have “amassed ‘considerable experience with the type of restraint at issue’ and ‘can predict with confidence that it would be invalidated in all or almost all instances.’” (quoting *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, 551 U.S. 877, 886-887 (2007))). Far from invalidating non-competes “in all or nearly all instances,” courts across the country have long upheld non-competes that are reasonable in time and scope.

⁵⁷ FTC’s proposed rule at 50, n.150.

⁵⁸ FTC’s proposed rule at 142.

Carving out Senior Executives, however defined, would likewise not address the need to protect trade secrets and confidential information held by lower-level employees.

XI. Other Concerns

National Security Concerns

U.S. companies' know-how and trade secrets play a key role in U.S. technological leadership. By effectively banning non-compete clauses and diluting trade secret protection, the draft would facilitate employees' ability to take with them valuable trade secrets and know-how to foreign companies. On January 5, 2023, the very same day the FTC issued this draft for public comments, President Biden signed the Protecting American Intellectual Property Act of 2022 into law (P.L. 117-336).⁵⁹ This law aims to deter the theft of U.S. intellectual property by non-U.S. individuals and entities.

Given the above, and in line with the Biden Administration's July 9, 2021, Executive Order on Prompting Competition in the American Economy⁶⁰ which highlighted the importance of a "Whole-of-Government Competition Policy" approach, we recommend that the FTC consult with the federal agencies tasked with securing U.S. technological leadership and security, seeking to ensure that the proposed rule is tailored in a way that does not threaten U.S. technological leadership. Such agencies may include the Department of Defense, Department of Commerce, Department of Justice National Security Division, National Economic Council, and others.

Persons Selling a Business Entity

Section 910.3 of the FTC's proposed rule recognizes that non-competes are necessary to "protect the value of a business acquired by a buyer."⁶¹ The FTC acknowledges that restricting non-compete clauses in this circumstance could reduce "incentives of various market actors to start, sell, or buy businesses."⁶² After all, if the seller had "the unlimited right to re-engage in a competitive business, he could attract his old customers to his new establishment and thereby destroy the value of the property right he has sold."⁶³

Despite these important justifications, the FTC narrowly limits this proposed sale-of-business exception to a "substantial owner, substantial member, and substantial partner as an owner, member, or partner holding at least a 25 percent ownership interest in a business entity."⁶⁴ In doing so, the FTC's proposed 25 percent threshold appears to be arbitrary and no legal authority or other source is cited in support of such.

By contrast, the FTC's proposed rule would effectively preempt at least 16 states that have sale-of-business exceptions to restrictions on non-compete agreements, which apply on a case-by-case basis.⁶⁵ For example,

⁵⁹ S. 1294 Protecting American Intellectual Property Act of 2022, <https://www.congress.gov/bill/117th-congress/senate-bill/1294/text>

⁶⁰ <https://www.whitehouse.gov/briefing-room/presidential-actions/2021/07/09/executive-order-on-promoting-competition-in-the-american-economy/>.

⁶¹ FTC's proposed rule at 106; *see also* Wilson Dissent, *supra* note 55, at 9.

⁶² FTC's proposed rule at 129-30.

⁶³ Alan B. Soclof, *The Sale of a Business—Restraints upon the Vendor's Right To Compete*, 13 W. Res. L. Rev. 161, 162 (1961).

⁶⁴ FTC's proposed rule at 113.

⁶⁵ *See* Ala. Code § 8-1-190; Ark. Code Ann. § 4-75- 101(h); Cal. Bus. & Prof. Code § 16601; Colo. Rev. Stat. § 8-2-113(3)(c); Fla. Stat. Ann. § 542.335(1)(d); Ga. Code Ann. § 13- 8-57(b); Haw. Rev. Stat. §480-4(c)(1); La. Rev. Stat. Ann. § 23:921(A)(2)(C); Mass. Gen. Laws ch. 149, §§ 24L(a), 24L(b)(iii); Mo. Stat. Ann. §431.202(2)(b); Mont. Code Ann. §§28-2- 704; N.D. Cent. Code §9- 08-06; Okla. Stat. tit. 15, § 218; S.D. Codified Laws §53-9-9; UT Code Ann. §§ 34-51- 101-301(2); Wash. Rev. Code §§ 49.62.010(5), 49.62.020(1).

in *Vacco Industries v. Van Den Berg*, 6 Cal. Rptr. 2d 602, 609 (Cal. Ct. App. 1992), the court enforced a sale-of-business non-compete agreement where the threshold was significantly below 25 percent. The court held that the defendant, who held less than 3 percent of the company’s stock, was a substantial shareholder against whom the non-compete was enforceable because he was the ninth largest shareholder and was one of the company’s principal officers.⁶⁶

As the FTC recognizes, “[i]nstead of establishing a threshold, the Rule could simply use the terms substantial owner, substantial member, and substantial partner in proposed § 910.3 and leave the interpretation of those terms to case-by-case adjudication.”⁶⁷ The FTC’s desire to “provide greater clarity to the public and facilitate compliance with the Rule” through a defined threshold can be accomplished by providing a safe harbor for at least a 25 percent ownership interest in a business entity. An ownership interest below 25 percent should continue to be assessed on a case-by-case basis.

XII. Conclusion

USCIB thanks the FTC in advance for giving careful consideration to our comments on such a transformative policy initiative. We stand ready to engage with the Administration to ensure best outcomes for all Americans, including our critical innovative industries.

⁶⁶ *Vacco Indus.*, 6 Cal. Rptr. 2d at 609.

⁶⁷ FTC’s proposed rule at 114.