The Daily Dish

The FTC's Sweeping Noncompete Clause Rule

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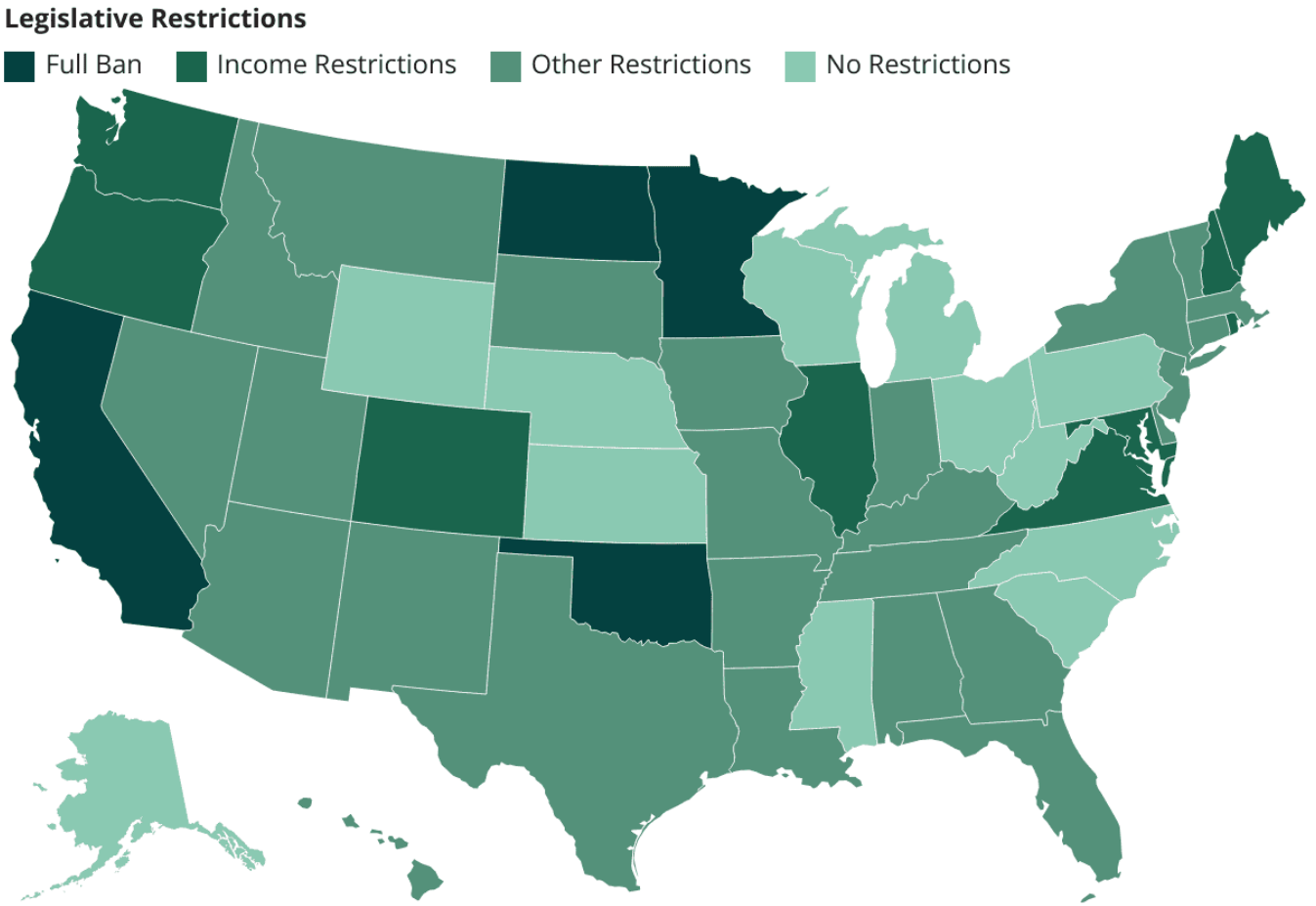
Yesterday the Federal Trade Commission (FTC) finalized its rule banning any future noncompete clauses in labor contracts. Specifically, the final rule "provides that it is an unfair method of competition—and therefore a violation of Section 5 of the FTC Act—for employers to enter into noncompetes with workers after the effective date." For existing noncompetes, the FTC will allow enforcement of those with senior executives (workers earning more than $151,164 annually who are in a "policy-making position") – estimated by the FTC to be 1 percent of workers. The rest go away.

The rule is spectacular, according to the FTC fact sheet. It will reduce health care costs, spur 8,500 more new businesses each year, enhance innovation, and raise worker earnings. It's evidently more powerful that eating your Wheaties.

Now, what should one think about this?

The first issue is whether the FTC has the authority to do this. That is, does this fall under its statutory authorities and is it not a "major question" that the courts think should be addressed by Congress? The legislation creating the FTC has been repeatedly revised over the years specifically because the agency is a serial over-stepper of its rulemaking authorities. And the "major questions doctrine" invoked in the recent Supreme Court ruling in *West Virginia v. EPA* would seem to apply to a nationwide intervention in all new labor contracts and an *ex post* revision of all existing contracts. Further, the more the FTC touts the impact of the rule, the more the major questions doctrine would seem to apply.

The second issue is whether the federal government needs to step in at all. Banning noncompetes is a classic one-size-fits-all, liberal strategy. In contrast, labor markets differ dramatically across the United States. As it turns out, the states have been quite active in differing approaches to NCAs:



If the states are keeping an eye on the best interests of labor market competition in their borders, why should the FTC override their efforts?

The third issue is the quality of the economic policy. (AAF has weighed in on this before.) At first blush, one would expect that a worker would not knowingly enter into a noncompete – forfeiting future options – without a compensating increase in current pay. Noncompetes made sense for certain C-suite executives and employees with knowledge of trade secrets, and concern only arose when noncompetes started being used with entry-level employees. And something does seem amiss when those employees are not informed of the noncompete clause until after they are hired and have left their previous job.

In short, while noncompetes have value but also a track record of misuse, does a blanket prohibition pass a benefit-cost test? Eakinomics has its doubts.