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CLIENT ALERT: TEXAS FEDERAL COURT GRANTS LIMITED INJUNCTION OF FTC'S RULE BANNING NONCOMPETE CLAUSES

What It Means for Your Business

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On July 3, a federal court in Texas issued a narrow and preliminary injunction which delays, with regard to only a few named parties, the implementation of the FTC's final rule prohibiting many non-compete agreements. That court is expected to issue a further ruling by August 30, 2024. Meanwhile, a similar challenge in another court is set to be heard on July 10 and has the potential to result in a nationwide injunction. While employers seeking to enforce non-compete agreements may view the Texas decision as a provisional win, they should stay tuned for further updates from the courts and continue contingency planning. We expect to provide further alerts on this issue.

FTC Rule in April 2024

In April of this year, the Federal Trade Commission (FTC) approved a final Rule banning the use of most non-compete agreements between businesses and their employees and independent contractors. It would also require employers to notify workers subject to such agreements that their agreements are no longer enforceable. The Rule is scheduled to go into effect on September 4, 2024. In order to ensure compliance with the notification requirements of the Rule and to effectively continue to protect trade secrets, however, many businesses are already in the midst of preparing new strategies.

Texas Lawsuit

Several lawsuits have been filed challenging the validity of the Rule. Ryan, LLC, a Dallas-based tax services firm filed one such challenge in the federal court for the Northern District of Texas, and was joined by a group of organizations including the U.S. Chamber of Commerce, Business Roundtable, the Texas Association of Business, and the Longview [Texas] Chamber of Commerce.

July 3 Ruling

On Wednesday, July 3, the judge in the Texas case granted a preliminary injunction in favor of plaintiff Ryan LLC and the intervenor organizations, postponing the effective date of the Rule, but only as applied to the plaintiffs. The ruling does not extend to the member businesses of the Chamber of Commerce and other associational plaintiffs. Plaintiffs' request to enjoin the rule nationwide was denied, with Judge Ada Brown deciding it was not clear whether such an order was appropriate. The judge said she would issue a final ruling by August 30, a few days before the Rule is scheduled to go into effect.

Notably, the judge ruled that, "…after reviewing the text, structure, and history of the [FTC] Act, the Court concludes the FTC lacks the authority to create substantive rules" to preclude unfair methods of competition. She reasoned that the FTC is empowered to prescribe "interpretive rules and general statements of policy with respect to unfair or deceptive acts or practices in or affecting commerce" under the relevant statute, but that the FTC's authority was limited to "rules of agency organization procedure or practice"—e.g., "housekeeping."

What does this mean for other businesses in the U.S.?

The FTC is temporarily prohibited from taking any action to implement or enforce the Rule as against the plaintiffs in the Texas lawsuit. The FTC may appeal the preliminary injunction and, if necessary, any final decision on the merits to the United States Court of Appeals for the Fifth Circuit.

Businesses around the country are now wondering what effect the Texas ruling has on them. That ruling was limited to the parties in the case, and only 2 months remain before the FTC Rule goes into effect unless further enjoined in the interim. Therefore, it may be prudent for businesses to continue to work with their legal counsel to prepare alternate strategies in order to weather both the current uncertainties and any future outcome.

Other Relevant Cases

There are two other cases pending in which plaintiffs are challenging the validity of the FTC Rule: one in the federal court for the Eastern District of Pennsylvania, and one in the Eastern District of Texas which was put on hold to await the resolution of the *Ryan* case. The Pennsylvania court has scheduled a preliminary injunction hearing for July 10, 2024.

In addition, on June 28, 2024, the U.S. Supreme Court issued an opinion in the case of *Loper Bright v. Raimodo and Relentless, Inc. v. Department of Commerce* which overruled its 1984 decision in *Chevron U.S.A. v. Natural Resources Defense Council* granting deference to the reasonable interpretation of the federal agency administering a law if that law was deemed ambiguous—the so-called *Chevron* defense. This development is relevant to the FTC Rule because Judge Brown's July 3 decision explicitly cites and relies on the Supreme Court's decision in the *Loper Bright* case, and because other federal courts may be more likely to follow Judge Brown's reasoning in the wake of *Loper Bright* to grant additional or broader injunctions against the implementation and enforcement of the FTC Rule banning non-competes.

Employers should assess their current and anticipated use and enforcement of non-compete agreements and consider how the implementation of the proposed rule would affect their business and compliance obligations. For more information on relevant considerations for your business, please contact Leonard K. Samuels, Ruth Vafek, or any other member of Berger Singerman's Labor & Employment Practice.

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