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Texas Court Blocks FTC's Noncompete Ban

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On August 20, 2024, the US District Court for the Northern District of Texas in ***Ryan LLC v. Federal Trade Commission*** issued an order blocking the Federal Trade Commission (FTC) rule banning all post-employment noncompete agreements with workers from taking effect on September 4, 2024. Unlike the **court's preliminary injunction ruling in early July**, which enjoined the rule as to only the five plaintiffs in the case, Judge Ada Brown's most recent merits decision blocked the rule from taking effect on a nationwide basis. Therefore, all employers using noncompete agreements will not be subject to the ban on September 4, and will not need to comply with the rule's notice and other requirements (discussed in **this April 2024 Cooley client alert**).

Merits decision

Judge Brown granted summary judgment in favor of Ryan and the plaintiff-intervenors, concluding that:

1. The FTC exceeded its statutory authority in implementing the rule because the agency lacks substantive rulemaking authority with respect to unfair methods of competition.
2. The rule is arbitrary and capricious because it is unreasonably overbroad without a reasonable explanation.

In determining that the agency exceeded its authority, the court analyzed the text, structure and history of the agency, concluding that while the FTC has "some authority" to promulgate rules to preclude unfair methods of competition, it lacks the authority to create substantive rules. Among other things, Judge Brown confirmed that Section 6(g) of the Federal Trade Commission Act (the section the FTC relied upon as its authority to issue its rule) is indeed a "housekeeping statute," authorizing only rules of agency organization procedure or practices and not substantive rules. She found support for this conclusion by pointing to the lack of a penalty provision in Section 6(g), which indicates a lack of "substantive force," along with the fact that the FTC did not "promulgate a single *substantive* rule under Section 6(g)" until its noncompete rule. The court concluded that the FTC's arguments about its rulemaking authority constituted a "piecemeal attempt to confer rulemaking authority that Congress has not affirmatively granted to the FTC. The role of an administrative agency is to do as told by Congress, not to do what the agency thinks it should do."

Judge Brown also concluded that the rule violated the Administrative Procedure Act (APA) because it is arbitrary and capricious, noting that it is unreasonably overbroad without a reasonable explanation. Judge Brown held that, "the [rule] imposes a one-size-fits-all approach with no end date, which fails to establish a 'rational connection between the facts found and the choice made.'" Among other things, Judge Brown noted that the record does not support the rule, the agency provided "no evidence or reasoned basis" for imposing a categorical ban instead of "targeting specific, harmful non-competes," was based on "inconsistent and flawed empirical evidence," failed to "consider the positive benefits of non-compete agreements," and "disregard[ed] the substantial body of evidence supporting these agreements." In addition, the court found that the FTC failed to sufficiently address "less disruptive alternatives" to issuing the rule.

After concluding that the agency acted unlawfully in issuing its rule, the court held that the appropriate remedy under the APA was to set the rule aside. Specifically, the court rejected the FTC's argument that the relief should be limited to only the named plaintiffs in the case, determining that the APA "does not contemplate party-specific relief," and as a result, the rule cannot be enforced or otherwise take effect on September 4 as to all employers.

What's next?

The ruling is a significant victory for employers in favor of using reasonable and legitimate noncompete agreements with workers. As Ryan noted **in a press release following the court's decision**, the ruling "preserves the economic freedom of businesses and their employees to enter into non-compete agreements," and recognized the "vital role [of noncompetes] in safeguarding intellectual property and innovation, building trust within businesses, and investing in training their people." Thus, for the time being, employers using noncompetes may continue to utilize them, subject to applicable state laws.

However, uncertainty remains on the rule's ultimate future, as the agency is considering whether to appeal the court's ruling to the US Court of Appeals for the Fifth Circuit, and the outcome of that possible action could be further appealed to the US Supreme Court. Indeed, an **FTC spokesperson stated that the agency was disappointed by the decision** and would "keep fighting to stop noncompetes that restrict the economic liberty of hardworking Americans, hamper economic growth, limit innovation and depress wages." The agency added that it was "seriously considering a potential appeal, and [the] decision does not prevent the [agency] from addressing noncompetes through case-by-case enforcement actions."

Even if the FTC rule does not ultimately take effect at the federal level, employers should revisit their existing noncompete provisions to ensure compliance with state laws – including new rules passed in **Washington**, **California** and **Minnesota**.

Cooley's employment team will continue to follow developments relating to the FTC rule. Employers with questions about the use of restrictive covenants should contact their Cooley employment lawyers.

To learn more, check out Cooley's **FTC Noncompete Ban Resources** page and our **What to Know About the FTC's Noncompete Ban** on-demand webinar.

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