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Non-Compete & Trade SecretsAlert

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Protecting proprietary information after the FTC's new ban on non-competes

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The FTC's nationwide non-compete ban is already the subject of a court challenge. While the ban is being litigated, employers can act now to guard their proprietary information.

What's the impact?

- The FTC's new rule does not displace state or federal trade-secret protections.
- The FTC's new rule does not prohibit employers from entering into non-disclosure or non-solicitation agreements with their workers.
- The FTC's new rule does not prohibit employers from using the "inevitable-disclosure doctrine" to enjoin former workers from working for competitors.

The FTC's newly adopted rule banning non-compete agreements could have far-reaching implications for businesses across the country. By the agency's own estimate, approximately 18 percent of the US workforce is covered by non-compete agreements. That's roughly 30 million workers.

Although the FTC's non-compete ban is currently being challenged in federal court in Texas, employers planning for an uncertain future should act conservatively, assume the rule will be upheld, and be ready to comply with its requirements. During this uncertainty, the good news for employers is that the rule does not foreclose the possibility of entering into agreements that protect proprietary information, including agreements that help employers invoke the inevitable-disclosure doctrine to enjoin former workers from working for a competitor where there is a substantial risk that the workers will use or disclose trade secrets.

A recap of the FTC's non-compete Rule

On April 23, 2024, the FTC voted 3-2 to issue a final rule banning non-compete agreements nationwide. The rule is scheduled to go into effect on August 21, 2024.

With a small number of limited exceptions, the rule prohibits virtually all non-compete agreements, including for senior executives and independent contractors. It also prohibits enforcing most preexisting non-compete agreements. In addition, it requires employers to notify workers that their non-compete agreements cannot and will not be enforced.

Protecting proprietary information

An element of nearly all non-competes is protecting competitively sensitive information from immediate use by departing workers. The FTC's new rule leaves room for employers to continue safeguarding this information, including as follows.

NON-DISCLOSURE AGREEMENTS

Employers may continue using non-disclosure agreements as long as the agreements are not so broad that they prevent workers from working for other employers in the industry. As the FTC has noted, non-disclosure agreements are not affected by the non-compete ban unless they "span such a large scope of information that they function to prevent workers from seeking or accepting other work or starting a business after they leave their job." For example, a non-disclosure agreement is prohibited if it bars workers from using or disclosing any information that is "usable in" or "relates to" the industry in which they work.

NON-SOLICITATION AGREEMENTS

Employers may continue prohibiting workers from soliciting clients or other workers, as long the workers' non-solicitation obligations are not so broad as to functionally prevent them from seeking or accepting other work or starting a business after their employment ends.

INEVITABLE-DISCLOSURE DOCTRINE

In passing the rule, the FTC indicated that it also does not prevent employers from invoking the "inevitable-disclosure doctrine," which allows a court to enjoin a former worker from working at a competitor where there is a substantial risk that the worker will use or disclose the employer's trade secrets in the worker's new position. Courts in roughly one-third of the states currently recognize the inevitable-disclosure doctrine.

How can employers protect trade secrets?

Moving forward, employers will need to ensure that they have strong, well-tailored non-disclosure and non-solicitation agreements in place. In addition, if there is a substantial threat that a former worker hired by a competitor will use or disclose trade secrets, employers will need to position themselves to invoke the inevitable-disclosure doctrine. This includes implementing policies and procedures that help prove a substantial risk of use or disclosure and drafting agreements specifically designed to help employers rely on inevitable-disclosure principles.

Properly structured employment agreements, including agreements containing non-disclosure, non-solicitation, and inevitable-disclosure provisions, could strike a balance between complying with the FTC's non-compete ban and protecting proprietary information, since the ban does not prohibit non-disclosure or non-solicitation agreements or displace trade-secret protections. Newly adopted agreements are likely to be tested in litigation, and courts are likely to have competing views about the extent to which the agreements are enforceable. Carefully drafted, properly tailored restrictions on workers' future use of proprietary information, as well as agreements making it easier for employers to invoke the inevitable-disclosure doctrine, could offer some certainty in an uncertain legal environment.

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