How A Federal Noncompete Law May Develop Under President Biden

Insights
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President-elect Joe Biden's campaign platform called for federal legislation to eliminate all employee noncompete agreements other than what it called "the very few that are absolutely necessary to protect a narrowly defined category of trade secrets." Noncompete agreements and other post-employment restrictive covenants have always been governed solely by state law in the U.S., with no nationwide federal legislation or regulatory scheme.

This allows states to take varying approaches based on sometimes very different views of what best serves the public interest in their location. But this also has posed challenges for multistate employers who must manage compliance with disparate state laws throughout the company's geographic footprint.

This has only gotten harder in recent years as legislatures enacted new statutes making the variance among state laws even greater. This raises a question of whether there could be some sort of national legislation governing noncompete agreements or other post-employment restrictive agreements.

Biden's platform proposal did not arise in a vacuum. In the past several years there have been a number of bills introduced on Capitol Hill designed to limit the use of noncompete agreements. Proponents have argued that such agreements can harm workers and the economy by limiting wage growth and restraining labor market competition.

Opponents of broad-based bans on noncompetes, on the other hand, assert that enforcing reasonable restrictions encourages companies to invest in operations and employees by allowing the company to protect itself from employees leaving and providing competitors with access to the company's confidential business information and key business relationships.

Although the bills proposed in recent years have all failed to pass even one house of Congress, the time may be ripe for national action on these issues. The new administration has promised to enact legislation limiting the use of noncompetes. There are representatives and senators on both sides of the aisle who have proposed legislation in recent years, sometimes on a bipartisan basis.

And with the profusion of new state statutes and bills promising to make it ever more difficult for national employers to manage the varying state law requirements, employers and business groups

might support national legislation, especially if it creates consistency and ease of compliance.

To succeed where others have failed, any proposal likely must account for both employee protection and company business needs, and must politically navigate prevailing philosophies ranging from California's long-standing statute banning nearly all noncompetes, to Florida's statute that was specifically designed to make noncompetes readily enforceable if they are reasonable.

Past Congressional Efforts At Noncompete Legislation

Beginning in 2015-2016, Democrats in the U.S. House of Representatives and U.S. Senate proposed three bills seeking to prohibit the use of noncompetes for low-wage employees and other specific categories of lower-skilled workers:

- The Mobility and Opportunity for Vulnerable Employees, or MOVE, Act, introduced by Sen. Chris Murphy, D-Conn., and co-sponsored by Sens. Richard Blumenthal, D-Conn., Elizabeth Warren, D-Mass., Sheldon Whitehouse, D-R.I., and former Sen. Al Franken, D-Minn.;
- The Freedom for Workers to Seek Opportunity Act, introduced by Rep. Derek Kilmer, D-Wash.; and
- The Limiting the Ability to Demand Detrimental Employment Restrictions, or LADDER, Act, introduced by former Rep. Joseph Crowley, D-N.Y.

While none of these initial bills gained much traction, Democratic efforts to curb the use of noncompetes continued. By 2018, Warren, Murphy and Sen. Ron Wyden, D-Ore., introduced the Workforce Mobility Act, or WMA, with the goal of imposing a total ban on virtually all noncompete agreements outside the sale of a business or dissolution of a partnership.

A companion bill was introduced in the House by Crowley, Reps. Linda Sanchez, D-Calif., Mark Pocan, D-Wis., Jerrold Nadler, D-N.Y., David Cicilline, D-R.I., and former Rep. Keith Ellison, D-Minn., who were later joined by Reps. Jan Schakowsky, D-Ill., and Alan Lowenthal, D-Calif. Those efforts failed when the session ended without action on either bill.

The WMA was reintroduced in October 2019 with new bipartisan support by Murphy and Sen. Todd Young, R-Ind. Like the original, the 2019 WMA generally prohibits any company from entering into, enforcing or threatening to enforce a noncompete agreement with any individual who works for the company. The bill defines a "noncompete agreement" as any agreement between a company and a worker that restricts the worker, after the termination of the working relationship, from:

- Working for another person;
- Working in a specified geographic area; and
- Working for another person in work that is similar to the individual's work for the company.

Interestingly, the proposal appears to have been drafted to leave room for it to be interpreted to ban lesser restrictions, such as covenants not to solicit clients. Unlike some recent state statutes limiting noncompetes, the WMA does not specifically state that it is not intended to impact other types of restrictions, even though it has a section saying it does not limit nondisclosure agreements.

Notably, California's statute banning noncompete agreements has been interpreted by its courts to also ban nonsolicit agreements, even though the statute does not mention them. Similar to California's statute, the WMA does allow for the use of noncompete agreements under limited circumstances. It would permit companies to enter noncompetes with individuals that sell a business and with senior executives in severance agreements executed as part of the sale of business, provided it includes at least 12 months' salary. Finally, the bill would permit noncompete agreements as part of the dissolution or disassociation of a partnership, and in business-to-business transactions.

Lessons From the Federal DTSA

Notably, the initial introduction of noncompete bills coincided with Congress passing the federal Defend Trade Secrets Act, or DTSA, which for the first time created a national law giving companies the opportunity to protect against and remedy the misappropriation of trade secrets. Historically, trade secret laws, like noncompete laws, have been the province of state common law and statutes.

The DTSA ultimately enjoyed wide bipartisan support leading up to its enactment, likely as a result of amendments to the original bill that resolved and accounted for specific state and party concerns. Moreover, while the DTSA created a federal cause of action, it did not fully federalize trade secrets law.

Rather, it is very deferential to the states, explicitly restricting courts from granting any injunction under the DTSA that conflicts with an applicable state law prohibiting restraints on the practice of a lawful profession, trade or business. This clause clearly protects the interests of California and other states whose public policies would be offended by a DTSA order prohibiting an employee, on trade secrets grounds, from accepting a directly competitive position.

Legislators pushing for national noncompete legislation may be taking note of the compromises that made the DTSA possible. In 2019, Sen. Marco Rubio, R-Fla., introduced the Freedom to Compete Act to amend the Fair Labor Standards Act. Rubio's bill scales back on the sweeping legislation sought through the WMA by more narrowly focusing on protections for entry-level, low-wage workers.

Although less all-encompassing than the WMA, the Freedom to Compete Act suggests a potential level of bipartisan support for noncompete legislation that stops short of the WMA's mimicking of California's outright ban. This suggests the legislative environment may be ripe for passage of bills creating, for example, a wage threshold for noncompetes, as has been done in a number of state statutes.

On the other hand, it probably would be more difficult to implement a national law broadly governing noncompetes or other restrictive covenants. It is possible that employers and business groups might get behind the idea of truly federalizing restrictive covenant law if the federal law filled the field and displaced state laws, but without going so far as the WMA and California's outright bans.

It would be exceedingly challenging as a political matter, however, to enact a federal law that displaced California's long-standing statutory ban. This is both because California's large and powerful delegation would most likely strongly oppose it, and because the more progressive wing of the Democratic delegation would view this as a large step backward in light of their advocacy for a California-style approach nationally.

What The New Administration Might Do If Congress Doesn't Act

If Congress does not enact legislation, Biden might seek to act through regulatory changes or an executive order.

Regulation is an as-yet untested option, but prior administrations have been moving in that direction over the past five years. As recently as January, the Federal Trade Commission held a public workshop to examine whether there is "sufficient legal basis and empirical economic support" to promulgate a commission rule that would restrict the use of noncompete clauses in employment contracts.

At the workshop, the FTC discussed topics including the impact of noncompete clauses on labor market participants, the business justifications for noncompete clauses, whether state laws were adequate, whether employers routinely enforced them, whether they constituted unfair competition, and whether the FTC should consider using its rulemaking authority to address the potential harms of noncompetes. The FTC also solicited comments following the workshop.

Among the hundreds of comments received, on March 12, attorneys general from a minority of states submitted comments asserting that noncompetition agreements harm workers by suppressing wages and degrading benefits, harm consumers by reducing business' access to skilled and unskilled labor, and reduce innovation. The 17 attorneys general argued against some of the frequently asserted justifications for noncompetes — to protect trade secrets and investments in training workers — and further argued that noncompetes, particularly for low-wage workers, are usually not the result of free bargaining.

However, many commenters, including attorneys throughout the country, pointed out that noncompetition provisions provide benefits to both companies and the economy, and are an important tool in the protection of trade secrets and other valuable business assets. Some of those comments support limiting possible overreach of agreements but not prohibiting noncompetes altogether. Specific limits mentioned included banning noncompetes for low-wage workers, requiring employers to give notice of the restrictions in advance of hiring, limiting geographic scope of restrictions, and imposing maximum durations.

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Others, perhaps including some of the other 33 states' attorneys general, might argue that this issue is not properly one for the FTC to regulate at all. Indeed, there are serious questions about whether the FTC has the power to regulate noncompetes.

Nevertheless, if the new administration opts to make this a priority, it is possible that Biden's FTC could continue down the path toward rulemaking, setting up court challenges down the road as to the propriety of such regulation.

Finally, and less aggressively, the Biden administration could seek to effect change through an executive order, as President Barack Obama did during his second term. In 2016, in response to the administration's frustration with the lack of any sweeping federal legislation, Obama launched an initiative criticizing what his administration saw as the abuse of noncompete agreements in the U.S. and urging states to impose limitations on the use of such agreements.

A October 2016 White House report encouraged states to ban noncompetes for certain categories of workers — such as low-wage workers and those in occupations that promote public health and safety — discourage the use of overly restrictive noncompetes, and improve the transparency and fairness of noncompetes by disallowing noncompetes unless they are proposed before a job offer or in connection with a significant promotion.

In the intervening years, quite a few states have enacted new legislation along these lines, and many other bills have been and continue to be introduced in statehouses. This of course has led to the growing level of variation among states' laws that makes this issue so difficult for multistate employers to manage.

What Is Most Likely?

Given political realities, the most likely scenario may be enactment of a federal statute prohibiting noncompete agreements for low-wage workers, but specifically noting it does not prohibit the other restrictions such as nonsolicits, and does not prevent individual states from having laws providing greater protection for employees — such as, for instance, a higher definition of what constitutes a low wage worker. Given the extent of vested interests, both geographically and politically, a comprehensive fully federalized national law of noncompetes appears unlikely.

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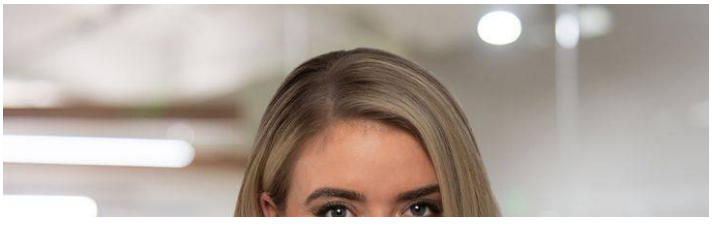

Gabrielle Giombetti
Partner
610.230.2186
Email

Susan M. Guerette
Partner
610.230.2133
Email

Christopher P. Stief
Regional Managing Partner
207.477.7007
Email

Abby H. Putzulu
Associate
415.490.9044
Email

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