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FTC TURNS UP THE HEAT FOR NONCOMPETE ENFORCEMENT: 5 STEPS FOR EMPLOYERS TO STAY COMPLIANT IN A NEW REGULATORY ERA

Insights
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The Federal Trade Commission just launched a new era of oversight when it comes to noncompete agreements between employers and employees, and the aggressive moves from the agency are turning some heads. On Thursday, it announced the first enforcement action by its newly created task force created to root out anticompetitive contracts that affect the labor market. The agency's Chairman also released a statement explaining the factors and circumstances it would be keeping an eye out for with noncompetes as the "cop on the beat." The FTC then called on employees – and even competitors – to turn over information to the agency about employers' use of noncompete agreements in an effort to find new targets. Finally, on Friday, it essentially put the final nail in the coffin on the Biden-era attempted noncompete ban. What should employers do in the wake of this aggressive new stance from the federal government?

Most Significant Takeaways For Employers

We dive into each one in more detail below, but this list provides a quick overview of the main developments.

1. The FTC Joint Labor Task Force on competition in the labor market is officially active, with the first of possibly many enforcement actions publicly announced yesterday.

2. The legal standard by which the FTC will assess noncompetes under federal law is much like the common-law rule of reasonableness in the enforcement context.

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Jonathan Crook
Partner
704.334.9313

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3. The FTC is not just going after "true" noncompete provisions. It is also scrutinizing customer nonsolicitation provisions that have the effect of excluding employees from an industry.

4. The noncompete ban of the Biden-era FTC is dead. The FTC announced on Friday that will not continue defending it in litigation. Instead, the agency will enforce the law through individual enforcement actions on a case-by-case basis.

5. The FTC is giving the public 60 days to provide information on the use of noncompete agreements. The FTC invites companies to share information about their competitors' use of such agreements, and it is particularly concerned with the use of noncompetes in the healthcare industry.

FP Analysis of Main Developments

First Enforcement Action of the Joint Labor Task Force

In February of this year, FTC Chairman Andrew N. Ferguson directed the FTC to form a Joint Labor Task Force, with an aim of "rooting out and prosecuting deceptive, unfair, and anticompetitive labor-market practices that harm American workers."

The FTC has now announced its first enforcement action over the use of noncompete agreements after the Joint Labor Task Force's creation. The FTC took action against a large pet cremation company, whom the FTC accused of using noncompetes with "all newly hired employees, regardless of their position or responsibilities."

Under the proposed Consent Order:

- The company is prohibited from entering into, maintaining, or enforcing noncompete agreements, with limited exceptions for certain high-ranking employees and equity holders;
- The company must provide notice to applicable employees that they are no longer subject to a noncompete agreement; and
- The company cannot prohibit employees in any employment agreement from soliciting any prospective, current, or former customers, except with respect to those

current or prospective customers with whom the employee had direct contact or personally provided service in the last 12 months of their employment with the company.

Commissioners Explain Legal Standard for Analyzing Noncompete Agreements Under Federal Law

In a separate statement issued with the enforcement action announcement, Chairman Ferguson (joined by Commissioner Melissa Holyoak) set out the "fact-specific approach and considerations that govern the Commission's evaluation of noncompete agreements."

The FTC will continue to "apply a case-specific approach to assessing the lawfulness of noncompete agreements." Among the factors relevant to the FTC's finding of unlawfulness here included:

- The size of the company, both in terms of employees and business;
- Whether the company required noncompetes of all employees or a subset of employees;
- The behavioral, temporal, and geographic scope of the noncompete provisions; and
- Whether the employees with noncompetes had job duties that might justify noncompete restrictions.

Chairman Ferguson noted that the FTC's analysis is similar to the common law standard of assessing the reasonableness of a noncompete in the enforcement context, which "asks whether the restriction is no greater than necessary to protect the employer's legitimate interests, and balances those interests against the hardship inflicted on the employee and any potential injury to the public."

That similarity is "not a coincidence," Chairman Ferguson said, since the first time a court ever deployed the "rule of reason" to assess a restraint on trade was in a case involving a noncompete agreement.

Chairman Ferguson noted that the proposed Consent Order excluded noncompetes entered in the context of the sale of a business, and those entered with "equity holders, their families, very senior managers, those with outside business

relationships with [the company], [and] those who otherwise have more unique access to competitively sensitive information."

These exceptions are "consistent with the general common-law rule that noncompete agreements are justified when they go no further than necessary to protect specific, identifiable, and valid interests of the employer that could not be protected without the noncompete agreement."

Customer Nonsolicitation Provisions Are Also Subject to Federal Scrutiny

Chairman Ferguson discussed the remedies to which the company agreed in the proposed Consent Order, including the limitation on customer nonsolicitation provisions.

The proposed Consent Order restricts nonsolicitation agreements to customers with whom the employee "had direct contact or personally provided service" in the previous 12 months of their service.

Chairman Ferguson said, "[t]hese additional restrictions are necessary to ensure [the company] cannot circumvent the prohibition on noncompete agreements by enforcing onerous nonsolicitation terms that would effectively prohibit employees from starting a competing business. After all, a broad non-solicitation clause that bars employees from working directly with any current or potential [company] customer would severely inhibit the employee's ability to work in the industry during the term of the non-solicitation agreement, even in the absence of a noncompete agreement."

Commissioners Confirm the Biden-Era Noncompete Ban is Dead

Recall that the Biden-era FTC promulgated a near-complete ban on noncompete agreements in April 2024, but a Texas federal district court judge set aside the ban as unlawful in *Ryan v. FTC* last year. The FTC (under Democratic leadership) appealed to the 5th Circuit.

The FTC had a September 8 deadline to update the appellate court about whether it will continue to defend the noncompete ban. We discussed the lengthy extensions the FTC has sought in that case, which potentially suggested that the Trump FTC would continue litigating.

But the agency confirmed that it would stop pursuing the action. On Thursday, the FTC announced that the agency will not take up the fight, and the noncompete ban is officially dead. Chairman Ferguson said it was "indefensible" for the Biden FTC to throw "thousands of manhours into the rule," and the "rule was obviously unlawful." On Friday, the agency formally filed paperwork in court indicating it would drop the fight and kill off the attempted noncompete ban.

Rather than defending the rule, the FTC will address noncompete agreements "through enforcement actions against companies that misuse them in violation of the law." According to the Chairman, "[a] steady stream of enforcement actions against an unlawful practice provides the markets with transparency about what the agency believes the law requires[.]"

FTC Requests Information from the Public on the Use of Noncompete Agreements

The FTC also launched a public inquiry to "better understand the scope, prevalence, and effects of employer noncompete agreements, as well as to gather information to inform possible future enforcement actions."

The RFI itself "encourages members of the public, including current and former employees restricted by noncompete agreements, employers facing hiring difficulties due to a rival's noncompete agreements, and market participants in the healthcare sector in particular, to share information about the use of noncompete agreements."

The public has 60 days to respond. The RFI asks a number of detailed questions, such as:

- What is the name of any employer currently known to you to be using employee noncompete agreements?
- What reason, if any, has the employer given for using noncompete agreements?
- For what roles, positions, or job functions does the employer use noncompete agreements?
- What are the typical salary ranges of the roles or positions subject to noncompete agreements?
- What are the terms or limitations of the noncompete agreements (such as the duration or geographic scope)?

- Does the employer enforce the noncompete agreements? If so, how?

These are just a few of the 25+ questions and sub-questions in the RFI. Anticipating that it may be soliciting confidential information, the FTC also gives respondents the option of making a "confidential submission."

Conclusion and 5 Steps for Employers to Take Now

We are officially in a new era of federal regulation over noncompete agreements, and we expect the FTC's enforcement efforts will only ramp up from here.

Here are five steps you can take now to ensure you stay compliant.

1. Don't Abandon Your Restrictive Covenants Completely. While the FTC's new focus on noncompetes is a significant development, it is not a reason to eliminate your restrictive covenants entirely. Chairman Ferguson made clear in his statement that the FTC continues to recognize that the appropriate use of narrow noncompete and customer nonsolicitation provisions remains legal.

2. Take Stock of How You Use Noncompetes Throughout the Workforce. The FTC is focusing on employers who ask everyone to sign noncompetes, even employees whose duties do not justify such restrictions. Take stock of how you use these agreements. If you use noncompetes with all employees, regardless of job duties, contact your Fisher Phillips attorney to discuss ways you can tailor your covenants and reduce risk.

3. Reexamine the Scope of Your Noncompetes. Even if you only use noncompetes with employees whose duties justify them, you still need to ensure the substantive restrictions are no broader than necessary to protect a legitimate business interest. Work with your counsel to identify those interests and narrowly tailor the covenants to appropriate behavioral, temporal, and geographic scopes.

4. Don't Forget About State Law. The FTC's new scrutiny of noncompetes is far from the only legal hurdle for employers. Noncompete and nonsolicitation agreements are governed by a patchwork of state laws that change every year, with some states imposing steep civil penalties for noncompliance. Subscribe to Blue Pencil Box to stay up to

date on this ever-shifting legal landscape, and discuss with your Fisher Phillips attorney how you can make your multistate contracts compliant wherever you have employees.

5. Take Advantage of Other Protections. Noncompete agreements are just one arrow in the quiver when it comes to preventing unfair competition. Make sure you have a strong trade secrets protection program in place, along with appropriate company policies and confidentiality provisions for all levels of employees. Fisher Phillips attorneys can help you secure your trade secrets, confidential information, customer relationships, and other protectable interests, even if you choose not to use noncompete agreements.

Conclusion

We will continue to monitor developments that impact your workplace and provide updates as warranted. Make sure you are subscribed to Fisher Phillips' Insight System to get the most up-to-date information, and check out Blue Pencil Box updates on restrictive covenant law. If you have any questions, please contact your Fisher Phillips attorney, the authors of this Insight, or any member of our Employee Defection and Trade Secrets Practice Group.