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Administrative Law & Regulatory Practice Update July 5, 2024

Northern District of Texas Preliminarily Enjoins the Federal Trade Commission's Non-Compete Rule

In *Ryan, LLC v. Federal Trade Commission*, the Northern District of Texas concluded "*The role of an administrative agency is to do as told by Congress, not to do what the agency think[s] it should do.*"

On July 3, 2024, the United States District Court for the Northern District of Texas concluded that the Federal Trade Commission's Non-Compete Rule, which would retroactively invalidate over 30 million employment contracts and preempt the laws of 46 states, exceeds the FTC's statutory authority and is arbitrary and capricious in violation of the Administrative Procedure Act. The court preliminarily enjoined enforcement of the Rule and stayed its effective date, but limited the scope of relief to the parties to the case. The court did not issue a nationwide preliminary injunction.

Background

Section 5 of the FTC Act authorizes the FTC "to prevent" the use of "unfair methods of competition" through case-by-case adjudication. Section 6(g) of the Act grants the FTC ancillary powers to support administrative adjudication, including the powers to make recommendations, publish reports, classify corporations, and "make rules and regulations for the purposes of carrying out the provisions of this subchapter."

On April 23, the FTC promulgated the Non-Compete Rule by a 3-2 vote. The Rule invokes the FTC's purported authority under Sections 5 and 6 and declares that nearly all non-compete agreements between employers and employees are "unfair methods of competition." The Rule accordingly prohibits businesses from entering into new non-competes except for those associated with the sale of certain business interests and bans the enforcement of nearly all non-competes (with narrow exceptions for the sale of certain business interests and for agreements with certain senior executives). The Rule also expressly preempted the laws of the 46 states that allow non-compete agreements.

Ryan, LLC, is a global tax-consulting firm headquartered in Dallas. Its principals and other workers are sought-after tax experts, many of whom agree to temporally limited non-compete agreements.

Represented by Gibson Dunn, Ryan filed suit against the FTC in the Northern District of Texas, alleging that the Non-Compete Rule exceeds the FTC's statutory authority, violates the Administrative Procedure Act, and defies the major questions doctrine, which instructs that federal agencies cannot regulate questions of deep economic and political significance absent clear authority from Congress. A group of trade associations led by the United States Chamber of Commerce intervened in the case to challenge the Rule as well.

The Court's Opinion

- The court determined that the Non-Compete Rule exceeds the scope of the FTC's statutory authority. "By a plain reading, Section 6(g) of the Act does not expressly grant the Commission authority to promulgate substantive rules regarding unfair methods of competition." The court emphasized that, unlike Section 5, Section 6(g) "contains no penalty provision—which indicates a lack of substantive force." Further, the court noted that "the location of the alleged substantive rulemaking authority is suspect . . . . Section 6(g) is the seventh in a list of twelve almost entirely investigative powers."
- The court further concluded that the Non-Compete Rule is arbitrary and capricious in violation of the Administrative Procedure Act. First, the Rule "is unreasonably overbroad without a reasonable explanation." The FTC "lack[ed] . . . evidence as to why they chose to impose such a sweeping prohibition—that prohibits entering or enforcing virtually all non-competes—instead of targeting specific, harmful non-competes." Second, "the FTC insufficiently addressed alternatives to issuing the Rule." It "dismissed any possible alternatives, merely concluding that either the pro-competitive justifications outweighed the harms, or that employers had other avenues to protect their interests."
- The court did not address the major questions doctrine.
- The court determined that Ryan and the intervenors would suffer irreparable harm if the Rule takes effect because they would face "financial injury" and expend "nonrecoverable costs [when] complying with the Rule."
- The court declined to enter a nationwide preliminary injunction. The preliminary injunction and stay are limited to Ryan and the intervenors, and do not extend to intervenors' member companies or other nonparties.

What It Means:

- The Non-Compete Rule was scheduled to take effect on September 4. As long as the preliminary injunction and stay are in place, the FTC cannot enforce the Rule against Ryan or the intervenors. Their existing non-compete agreements remain enforceable under federal law, and they are free to enter into new non-compete agreements.
- In the absence of nationwide relief, the Rule will go into effect on September 4 as to all other employers, meaning that state non-compete laws will be preempted, existing non-compete agreements will be retroactively invalidated, and businesses will be unable to enter into new non-compete agreements unrelated to certain sales of businesses.
- The decision is not binding precedent on other courts.
- Proceedings before the district court will continue. The court indicated that it would enter a final ruling on the merits by August 30.

Gibson Dunn attorneys Eugene Scalia, Allyson N. Ho, Amir C. Tayrani, Andrew Kilberg, Elizabeth A. Kiernan, Aaron Hauptman, and Josh Zuckerman represent Ryan, LLC.

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Gibson Dunn's lawyers are available to assist in addressing any questions you may have regarding the issues discussed in this update. Please contact the Gibson Dunn lawyer with whom you usually work, the authors, or any leader or member of the firm's Appellate & Constitutional Law, Labor & Employment, Administrative Law & Regulatory, or Antitrust & Competition practice groups:

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