

What is the Impact of the FTC's Final Non-Compete Rule on Franchisors and Franchisees?

As explained in Polsinelli's prior [alert](#) of April 24, 2024, the FTC announced its final rule on non-compete covenants (the "Rule") on April 23, 2024.

Critically, the Rule does *not* prohibit non-compete agreements *between* franchisors and franchisees. However, it does apply to non-compete agreements signed by employees of a franchisee or franchisor.

Franchise agreements often require franchisees to obtain non-compete agreements from their managers or other key employees. Unless a particular employee is a "Senior Executive" (a worker earning more than \$151,164 who is in a "policy-making position"), such non-compete agreements between a franchisee and its employee will be rendered unenforceable under the new Rule. In fact, since the Rule prohibits attempts to enter into non-compete agreements, franchisees will be precluded from even requesting that employees sign agreements containing non-compete language, even though such language would be unenforceable in any case. As a practical matter, if the rule is not enjoined, (1) franchisees cannot demand that their employees (aside from Senior Executives) execute non-compete agreements, and (2) franchisors will want to review and edit their form franchise agreements to remove any such requirements of franchisees.

Additionally, under the Rule, employers (including franchisees) must provide workers with existing non-competes (excluding Senior Executives) notice that such non-compete clauses are no longer enforceable. Such notice must be provided by the Rule's effective date, which is expected to be in late August 2024 (120 days following its forthcoming publication in the Federal Register). If the Rule is enjoined, depending on the scope of the injunction, this requirement may not apply.

As noted above, the Rule does not prohibit non-competes in a franchise agreement between a franchisor and a franchisee. Specifically, the Rule expressly states that the term "worker" "does not include a franchisee in the context of a franchisee-franchisor relationship." Accordingly, subject to state law (and absent a successful misclassification claim by a franchisee), the Rule will not impact franchisors' ability to obtain and enforce reasonable covenants restricting individual franchisees from competing after the expiration or termination of a franchise agreement or the sale of a franchised business.

The Rule applies only to work in the United States or operating a business in the United States. Accordingly, international franchisors should still be able to require that franchisees restrict post-employment work outside of the United States, subject to the legal regime of other implicated jurisdictions.

Finally, the Rule covers employees of the franchisor. Accordingly, like all other employers, franchisors should take care to omit any non-compete clauses from their own employment contracts moving forward, except where allowed for Senior Executives or in connection with the sale of the business, and to provide the necessary notice of unenforceability to all (non-Senior Executive) employees currently covered by such clauses. Importantly, the Senior Executive exemption will only apply to Senior Executives who are subject to non-competes prior to the Effective Date. That exemption will not apply (assuming the Rule is not enjoined) to Agreements entered into after the Effective Date.