

Publications

July 5, 2024 • Updates

Impact of the Texas Federal Judge Partially Blocking FTC Ban on Non-Competes for Franchisors and Franchisees

As reported on July 3 by the Polsinelli Labor & Employment practice group alert, by order dated July 3, 2024, the Northern District of Texas granted a preliminary injunction preventing the Federal Trade Commission (FTC) from enforcing its ban on non-competition clauses against tax preparation company Ryan LLC. On April 23, 2024, the FTC passed a final rule banning most non-compete clauses in employment agreements on the purported basis of the unfair impact on competition (see the prior Polsinelli Labor & Employment alert for additional detail generally on the rule). Several lawsuits are pending challenging the new rule.

The court in *Ryan LLC v. Federal Trade Commission*, case number 3:24-cv-00986, is the first court to render a ruling on a challenge to the new FTC rule. The Northern District of Texas ordered a preliminary injunction preventing the FTC from enforcing its rule against the plaintiff in that case, Ryan LLC. But the court declined to issue a broader preliminary injunction against the rule nationally. Thus, the rule would still be effective as to other parties on the effective date of September 4, 2024, notwithstanding Wednesday's Order, unless a broader injunction is entered between now and then, either in that case or another of the several pending cases.

We anticipate a final decision from the Northern District of Texas in the Ryan case by August 30 and a ruling from Pennsylvania in the case of *TS Tree Services, LLC v. The Federal Trade Commission* in the interim. That court may offer a national preliminary injunction, and further, the Texas court's decision suggests that court may enter a national ruling. In granting this preliminary injunction, the Texas Court tipped its hand to how it likely will rule on its final decision, which it stated will be released before August 30. In its preliminary ruling, the court reasoned that the FTC likely exceeded its statutory authority for lack of substantive rule-making authority and that the categorical ban on nearly all employee non-competes would likely be found to be overly broad and without substantial basis. The rule-making process is a check and balance placed on federal agencies issuing regulations and is a high standard because of the effective circumvention of the legislative branch. As a result, agencies cannot issue regulations in the same method or to the same broad effect as Congress and are bound by the limitations of power of the executive

Related People

- Leonard (Len) MacPhee
- Joyce Mazero
- Jess A. Dance
- Jarina Duffy

Related Capabilities

- Global Franchise & Supply Network

branch.

Although the Rule does *not* prohibit non-compete clauses in franchise agreements *between* franchisors and franchisees, unless enjoined nationally, the rule would impact companies in franchising in several ways. Under the terms, the rule would ban non-compete agreements signed by employees of franchisees and by employees of franchisors and require companies to remove non-competes from their employment-related agreements and notify employees with current non-compete agreements that the clause will not be enforced. Further, to the extent franchisors have required franchisees to use agreements with non-compete clauses with certain of the franchisee's employees, franchisors will need to remove that requirement and ensure franchisees are aware the obligation is removed (see the Polsinelli Global Franchise & Supply Network alert for additional detail on the franchise implications of the rule). Further, for franchisors who have required owners or principals of franchisees to sign separate agreements or guarantees containing non-compete agreements with the franchisor, there is a risk that the carve-out for franchise agreements will not extend to such ancillary agreements, and each arrangement would need to be evaluated on a case-by-case basis.

Polsinelli attorneys will keep you updated on the developments to the challenges to the rule. We are also available to assist with the implementation of policies as you prepare your franchise business operations for the potential of the FTC rule and navigate the issues pending the above-mentioned rulings.