TECHFREEDOM
LAW FOR A DYNAMIC FUTURE

Comments of

TechFreedom

James E. Dunstan[i]

In the Matter of

Non-Compete Clause Rulemaking

Matter No. P201200

Docket No. FTC-2023-0007

April 19, 2023

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INTRODUCTION

TechFreedom is a nonprofit, nonpartisan think tank based in Washington, D.C. It is dedicated to promoting technological progress that improves the human condition. It seeks to advance public policy that makes experimentation, entrepreneurship, and investment possible and thus unleashes the ultimate resource: human ingenuity.

TechFreedom submits three comments in response to the above-referenced docket. Our comments address three related but distinct aspects of the proposed rulemaking, namely:

1) Why the Commission lacks authority to make substantive rules with the force of law governing Unfair Methods of Competition under Section 6(g) of the FTC Act (cited internally as *TechFreedom I*);
2) How the proposed rule would affect intellectual property, if enacted (internally, *TechFreedom II*); and
3) A more limited rulemaking that would be consistent with the Commission's current understanding of its authority to prohibit, and enact rules with respect to, unfair or deceptive acts and practices (internally, *TechFreedom III*).

The present comment, *TechFreedom II,* addresses the second point offered above.

TechFreedom [1] welcomes the Federal Trade Commission's ("Commission") request for comment on its proposed rule prohibiting non-compete clauses as an unfair method of competition. [2] We submit this comment to specifically discuss the impact of a blanket ban on non-compete agreements within the tech sector of the U.S. economy. The impact of the tech sector on the overall economy of the United States is huge:

> Computing, data storage and processing, IT components, information services, semiconductors, and software are just a few examples of the industries that make up the U.S. IT industry, sometimes known as the "tech sector" by some. In 2020, the industry employed 5.9 million people or 4.4% of all private sector jobs in the United States. These workers made more than twice what the

[1] Our recent submissions to the Commission include Comments of TechFreedom (James E. Dunstan and Berin Szóka) on Petition for Rulemaking to Prohibit the Use on Children of Design Features that Maximize for Engagement (Jan. 18, 2023), https://techfreedom.org/wp-content/uploads/2023/01/TechFreedom-Comment-on-CDD-Engagement-Petition.pdf, and Comments of TechFreedom (Bilal Sayyed) on Request for Information on Merger Enforcement (Apr. 21, 2022), https://techfreedom.org/wp-content/uploads/2022/04/TechFreedom-Comments-Merger-Guidelines-April-21-2022.docx.pdf.

[2] Non-Compete Clause Rule, Notice of Proposed Rulemaking, 88 Fed. Reg. 3482 (proposed Jan. 19, 2023) (to be codified at 16 C.F.R. 910), https://www.federalregister.gov/documents/2023/01/19/2023-00414/non-compete-clause-rule.

> typical American worker made. When the multiplier effect is taken into consideration, the industry supports 19% of all jobs in the United States.
>
> Between 2010 and 2020, value added in the IT sector increased by $600 billion (109%) with data processing, Internet publishing, and other information services experiencing the highest growth at 215.1%. The gross domestic product (GDP) of the United States increased overall by 39% over that time. According to the Department of Commerce, the value added by the digital economy to the U.S. GDP in 2020 was 10.2% ($2.14 trillion).[3]

Because of the impact of technology companies on U.S. productivity and GDP, we discuss here the impact of a blanket ban on that part of the economy.

I. A Blanket Ban on Non-Competes Would Significantly Harm the Tech Sector: Trade Secret Law Is an Insufficient and Costly Alternative

Chair Lina Khan has made her position clear—employees should be free to switch jobs:

> The freedom to change jobs is core to economic liberty and to a competitive, thriving economy. Noncompetes block workers from freely switching jobs, depriving them of higher wages and better working conditions, and depriving businesses of a talent pool that they need to build and expand. By ending this practice, the FTC's proposed rule would promote greater dynamism, innovation, and healthy competition.[4]

The Majority say virtually the same thing in their statement accompanying the NPRM:[5]

> By design, noncompetes often close off a worker's most natural alternative employment options: jobs in the same geographic area and professional field.

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[3] *How the Tech Industry is Reinforcing the US Economy in 2023?*, ANALYTICS INSIGHT (Mar. 6, 2023), https://www.analyticsinsight.net/how-the-tech-industry-is-reinforcing-the-us-economy-in-2023/#:~:text=The%20gross%20domestic%20product%20(GDP,10.2%25%20(%242.14%20trillion).

[4] Press Release, Fed. Trade Comm'n, FTC Proposes Rule to Ban Noncompete Clauses, Which Hurt Workers and Harm Competition, (Jan. 5, 2023), https://www.ftc.gov/news-events/news/press-releases/2023/01/ftc-proposes-rule-ban-noncompete-clauses-which-hurt-workers-harm-competition.

[5] Non-Compete Clause Rule, Notice of Proposed Rulemaking, 88 Fed. Reg. 3482, 3536 (proposed Jan. 19, 2023) (to be codified at 16 C.F.R. 910), [hereinafter NPRM], https://www.govinfo.gov/content/pkg/FR-2023-01-19/pdf/2023-00414.pdf.

> These restrictions can undermine core economic liberties, burdening Americans' ability to freely switch jobs.[6]

No caveats. No limitations. The right of employees to freely leave their employment and compete directly with their former employers is paramount, including taking what they've learned from their former employer and putting it to use in their new job or business.[7] In the view of some, this employee mobility right should supersede any rights an employer may have in protecting its intellectual property:

> There is still time to better describe practices that effectively are noncompete agreements covered by the FTC rule. The agency, on January 8, invited comments and indicated that no poach rings, no hire agreements, nondisclosure, trade secret, proprietary, and confidential information clauses can also be used to threaten and block workers from gaining a different job at a competing firm.[8]

By elevating employee rights in this manner, however, the NPRM fails to consider the rights of employers to protect their intellectual property, a right enshrined in the U.S. Constitution,[9] and described by the Congressional Research Service as "perhaps the longest-running element of U.S. innovation policy."[10] If U.S. companies are unable to protect their intellectual property, they will be under threat not only from former employees, but also from foreign adversaries who will pick off employees from the U.S. tech sector and extract from them the intellectual property of their former employers.

It is not until 23 pages into the NPRM that an astute reader will find that the FTC will still allow limitations on the rights of employees to leverage the knowledge gained from their

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[6] Statement of Chair Lina M. Khan, Joined by Commissioner Rebecca Kelly Slaughter and Commissioner Alvaro M. Bedoya Regarding the Notice of Proposed Rulemaking to Restrict Employers' Use of Noncompete Clauses, Commission File No. P201200, 1 (Jan. 5, 2023), https://www.ftc.gov/system/files/ftc_gov/pdf/statement-of-chair-lina-m-khan-joined-by-commrs-slaughter-and-bedoya-on-noncompete-nprm.pdf.

[7] NPRM, *supra* note 5, at 3521 ("The proposed rule is targeted at increasing competition in labor markets by allowing workers to move more freely between jobs and increasing competition in product markets by ensuring firms are able to hire talented workers and workers are able to found entrepreneurial ventures.").

[8] Peter Norlander, *Fair Competition In The U.S. Labor Market Is Threatened By More Than The Noncompete Clauses Targeted By New Federal Trade Commission Rule*, WASHINGTON CENTER FOR EQUITABLE GROWTH (Feb. 23, 2023), https://equitablegrowth.org/fair-competition-in-the-u-s-labor-market-is-threatened-by-more-than-the-noncompete-clauses-targeted-by-new-federal-trade-commission-rule/.

[9] U.S. CONST. art I, § 8, cl. 8 ("To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries").

[10] EMILY G. BLEVINS, CONG. RESEARCH SERV., R47267, PATENTS AND INNOVATION POLICY (2022), https://sgp.fas.org/crs/misc/R47267.pdf. The report also identifies the other key protections afforded inventors under U.S. law, including copyrights, trademarks, and trade secrets. *Id.* at 2 n.11.

former employer—but only if former employers are willing to engage in costly trade secret or other IP litigation against their former employees.[11] The NPRM cites the Defend Trade Secrets Act of 2016 (DTSA) as allegedly a narrower alternative to protecting intellectual property. In effect, then, the FTC wishes to supplant hundreds of years of state law interpretation of the proper metes and bounds on non-compete agreements with a relatively new area of the law which "has developed significantly in recent decades."[12] The NPRM further notes, apparently with approval, that the standard for obtaining an injunction barring a former employee from disclosing the confidential information and trade secrets she received via her former employment involves "high evidentiary burdens related to inevitability, irreparable harm, and bad faith."[13] This is in direct contrast to the ability of an employer, according to the NPRM, to enjoin a former employee from joining a rival company based on a non-compete agreement.[14]

Commenters, and especially legal practitioners familiar with both non-compete and trade secret law, note the difficulty employers will have proceeding under a trade secret theory.[15] They find that employers will be forced to pursue costly and time-consuming litigation in order to protect their intellectual property. The NPRM responds by assuming, improbably, that there will be no increase in such litigation:

> The number of cases filed in state court has held steady since 2015, when 1,161 cases were filed. The fact that a considerable number of trade secret lawsuits are filed in federal and state court—approximately 2,500 cases per

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[11] NPRM, *supra* note 5, at 3505-07.

[12] *Id.* at 3506.

[13] *Id.*

[14] *Id.* at 3483 ("If a worker violates a non-compete clause, the employer may sue the worker for breach of contract. An employer may be able to obtain a preliminary injunction ordering the worker, for the duration of the lawsuit, to stop the conduct that allegedly violates the non-compete clause. If the employer wins the lawsuit, the employer may be able to obtain a permanent injunction ordering the worker to stop the conduct that violates the non-compete clause; a payment of monetary damages from the worker; or both.").

[15] *See, e.g.,* Thomas Hubert, et al., *FTC Hosts Public Forum on Proposed Rule Banning Non-Compete Clauses*, TRADE SECRET INSIDER (Mar. 14, 2023), https://www.tradesecretsinsider.com/ftc-hosts-public-forum-on-proposed-rule-banning-non-compete-clauses/ ("However, those opposed to the rule stated that trade secret law does not sufficiently protect companies because the information has already been revealed by the time the law is triggered. Non-competes help to circumvent this problem by getting ahead of trade secret or confidential information being shared."); Stefania Palma, *US Companies mount resistance to proposed ban on non-compete clauses*, FINANCIAL TIMES (Feb. 9, 2023), https://www.ft.com/content/6602eda5-70ac-416f-a78b-f29e44af1768 ("But Russell Beck, founding partner at Beck Reed Riden, argued that scrapping non-competes 'would eliminate one of the two critical tools in protecting trade secrets', with NDAs being the less effective alternative as 'oftentimes companies will never find out' about a leak 'until it's too late'. Eliminating non-competes would lead to a jump in complex trade secret claims, increasing costs and legal uncertainty for businesses, Beck added.").

> year—and the fact that this number has held steady for several years suggests employers view trade secret law as a viable means of obtaining redress for trade secret theft.[16]

Unfortunately, that is the complete opposite of what will occur if the FTC adopts a blanket ban on non-competes, and instead forces companies to protect their intellectual property rights through trade secret litigation. As two veteran labor litigators explain:

> Without non-competes, we should expect an increase in trade secret misappropriation claims under Texas and federal law. In addition, shifting focus from pre-employment negotiation of non-compete agreements to post-employment enforcement will add a layer of complexity and unpredictability to the process and could also dilute valuable intellectual property.[17]

But even employers' ability to protect their IP rights under trade secrets and the DTSA may be severely limited under the proposed new rule. That is because in addition to banning non-competes, the NPRM suggests that the FTC may also move to ban non-disclosure agreements (NDAs) that "function as de facto non-compete clauses."[18] The NPRM submits that between 33% and 57% of U.S. workers are subject to NDAs.[19] That means that there are some 50 to 91 *million* NDAs in force today that are instantly brought into question by the NPRM.[20] And rather than deciding the reasonableness of a non-compete under centuries-old theories[21] of time, geographic distance, and definition of industry,[22] courts will now have to delve into the reasonableness of NDAs in determining whether the information sought to be protected

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[16] NPRM, *supra* note 5, at 3506.

[17] G. Scott Fiddler & Michael Drab, *Imagine There's No Non-Competes*, ALM GLOBAL (Feb. 14, 2023, 11:30 AM), https://www.law.com/texaslawyer/2023/02/14/imagine-theres-no-non-competes/?slreturn=20230312083526.

[18] NPRM, *supra* note 5, at 3507.

[19] *Id.*

[20] According to the U.S. Bureau of Labor Statistics, there are 160,892 U.S. employees as of March 2023. *Table A-1. Employment status of the civilian population by sex and age*, U.S. BUREAU OF LABOR STATISTICS (last modified Apr. 07, 2023), https://www.bls.gov/news.release/empsit.t01.htm.

[21] The first litigated non-compete agreement may well date back over 600 years. John Dyer's Case, 2 Hen. V, fol. 5, pl. 26 (C.P. 1414). *See also A Current Look at The Noncompete Agreement, One of the World's Oldest Business Practices*, THE ALEXANDER GROUP (June 19, 2019), https://tagsearch.com/insights/articles/a-current-look-at-the-noncompete-agreement-one-of-the-worlds-oldest-business-practices. Early U.S. non-compete jurisprudence (and antitrust cases in general) relied heavily on English precedent. *See, e.g.*, Addyson Pipe & Steel Co. v. United States, 85 F. 271 (6th Cir. 1898), *aff'd*, 175 U.S. 211 (1898) (relying heavily on Mitchel v. Reynolds, 1 P. Wms. 181, 24 E.R. 347 (Q.B. 1711)).

[22] For a good discussion of the development of non-compete law and the various approaches to "reasonableness," *see* Michael J. Garrison & John T. Wendt, *The Evolving Law of Employee Noncompete Agreements: Recent Trends and an Alternative Policy Approach*, 45 AM. BUS. L.J. 107 (2008).

qualifies as a trade secret, an analysis that will require extensive expert opinion. Or, as one commentator laments,

> Where the line between an "appropriately tailored" NDA and an NDA that surreptitiously functions as a prohibited non-compete is not at all explained by the FTC. . . Consequently, we are left with vague platitudes that "good" NDAs merely limit the way that a worker competes with their former employer while "bad" NDAs prevent a worker from competing altogether.[23]

The article quoted above goes on to posit that this restriction on the enforceability of NDAs may act as a restriction of IP holder rights under the DTSA. Any action brought under the DTSA could be dismissed if a court (or the FTC) finds that an NDA entered into by the employee was not "appropriately tailored."[24] Win or lose, the result of both a blanket ban on non-compete agreements and a ban on NDAs that are not "appropriately tailored" will lead to decades of costly litigation, and require courts to delve into highly technical examinations of whether certain information is a trade secret, and whether prohibiting former employees from using that information is "appropriate," whatever that means.

Yes, non-compete agreements are blunt instruments. But they are understandable, even by the layperson. How many months or years am I restricted? How many miles away must my new employment be? What is the nature of the industry in which I compete? These are all discernable factors. Eliminate those tests, and employers will have to revert to claims under trade secret law. Was the particular line of computer code I memorized in my old job and reused in my new job a trade secret? Were the internal equations on the spreadsheet I worked on to determine what price to quote for a kitchen renovation at my new job a trade secret? The complexity of this type of future litigation (versus determining the reasonableness of a non-compete agreement) will take up FTC time and court resources for decades to come.

II. Evidence Remains Lacking as to Any Overall Harm Caused by Non-Competes

While the NPRM adopts without question various studies buttressing its conclusion that non-competes are bad, the FTC has undertaken little, if any, analysis of the negative impacts such a ban would have on workers. The lack of empirical study of the impact of non-competes (especially banning them completely) has been noted by commentators in the field:

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[23] Aaron M. Levine & Matt A. Todd, *The FTC's Proposed Ban on Non-Compete Agreements and Conflict with the Defend Trade Secrets Act*, POLSINELLI PUBLICATIONS (Feb. 6, 2023), https://www.polsinelli.com/publications/the-ftcs-proposed-ban-on-non-compete-agreements-and-conflict-with-the-defend-trade-secrets-act.

[24] *Id.*

> In fact, we know surprisingly little about the frequency, scope, and strength of noncompetition agreements in this country. We know even less about how differences across jurisdictions in the law of noncompetes and in enforcement behavior relate to the prevalence and content of such agreements. Notwithstanding this dearth of basic information, there has been a near explosion in the attention being paid to noncompetes and their effects. Policymakers and commentators have been engrossed. Researchers, for their part, have published many provocative, but ultimately limited, exploratory studies about the many roles that noncompetes play in employment relationships and the economy. Much of this chorus has been fueled by unsupported assumptions and by high-profile anecdotal evidence of purportedly abusive practices involving noncompetes.[25]

In addressing the state of scholarship buttressing those who would ban non-competes, the authors continue: "Nevertheless, it is clear that—for the most part—this literature comprises unconnected, piecemeal, and often abstract articles. These articles do not have a basic, foundational understanding of noncompete contracting behavior 'on the ground' or even a full sense of state-by-state noncompete enforcement realities."[26] Finally, these authors question whether a nationwide ban on non-competes would actually change the labor markets. "Curiously, we find little credible evidence of any relationship between the strength of enforcement at the state level and employer noncompete use by state, raising questions about the practical significance of standard reform efforts."[27]

The FTC attempted to "close the knowledge gap" concerning non-competes by seeking comments and holding a workshop in 2020.[28] Yet the presentations at that workshop did little to provide an adequate evidentiary record sufficient to warrant the FTC to take action immediately. Ryan Nunn, for example, pointed to the lack of empirical studies on the impact of non-competes on the labor market,[29] especially given the decline of union membership in

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[25] James J. Prescott, et. al., *Understanding Noncompetition Agreements: The 2014 Noncompete Survey Project*, 2016 MICH. ST. L. REV. 369, 372 (2016).

[26] *Id.* at 373.

[27] *Id.* at 377.

[28] *Non-Competes in the Workplace: Examining Antitrust and Consumer Protection Issues*, FEDERAL TRADE COMMISSION (Jan. 9, 2020), https://www.ftc.gov/news-events/events/2020/01/non-competes-workplace-examining-antitrust-consumer-protection-issues.

[29] Ryan Nunn, *Noncompete Contracts: Potential Justifications and the Relevant Evidence*, The Brookings Institution (Feb. 4, 2020), https://www.brookings.edu/testimonies/non-compete-contracts-potential-justifications-and-the-relevant-evidence/; FED. TRADE COMM'N, PRESENTATION SLIDES FOR THE NON-COMPETE CLAUSES IN THE WORKPLACE WORKSHOP: EXAMINING ANTITRUST AND CONSUMER PROTECTION ISSUES 40 (2020) [hereinafter NON-COMPETE WORKSHOP SLIDES],

the private sector from 24 percent 50 years ago to less than six percent today.[30] He also noted that non-compete agreements can serve as a valuable tool to protect trade secrets:

> The trade secret justification starts with this premise that trade secrets litigation is protracted, it's costly, it's difficult for employers to win. Non-competes may be a more effective or at least lower cost way to prevent the theft of trade secrets than would a more narrowly targeted law that simply sanctions the exposure of the secrets themselves. I think the underlying idea here is that it's necessary to prevent those trade secrets from being divulged in order to induce the employer to share that information in the first place, the idea being that the employer shares the trade secrets with their worker, it facilitates their joint production and contributes to social welfare, because the employer knows that that information won't be divulged outside the firm.[31]

Mr. Nunn indicated that there is "limited evidence," but it appears that non-compete agreements correlate at least loosely to labor impacts that cut in both directions.[32]

Professor Kurt Lavetti of Ohio State University similarly reported that evidence is still lacking, with the current study conclusions "[s]till far from reaching a scientific standard for concluding NCAs are bad for overall welfare," and we "[a]lso don't yet fully understand the distribution of effects on workers."[33] He noted "in some contexts there is evidence they systematically increase earnings."[34] His ultimate conclusions is that "[m]ore empirical

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https://www.ftc.gov/system/files/documents/public_events/1556256/non-compete-workshop-slides.pdf; FED. TRADE COMM'N, TRANSCRIPT OF THE NON-COMPETE CLAUSES IN THE WORKPLACE WORKSHOP: EXAMINING ANTITRUST AND CONSUMER PROTECTION ISSUES 122-23 (Jan. 9, 2020) [hereinafter NON-COMPETE WORKSHOP TRANSCRIPT], https://www.ftc.gov/system/files/documents/public_events/1556256/non-compete-workshop-transcript-full.pdf.

[30] NON-COMPETE WORKSHOP SLIDES, *supra* note 29, at 38; NON-COMPETE WORKSHOP TRANSCRIPT, *supra* note 29, at 120-22.

[31] NON-COMPETE WORKSHOP TRANSCRIPT, *supra* note 29, at 123. The flip side of these findings is the fact that "[s]everal studies have shown NCAs to be common among workers with low pay and/or educational attainment, for whom [trade secrets] are often not relevant." NON-COMPETE WORKSHOP SLIDES, *supra* note 29, at 42.

[32] NON-COMPETE WORKSHOP SLIDES, *supra* note 29, at 48. Non-competes correlate to more worker training and more company investment, but also diminished firm entry and lower age-wage profiles. NON-COMPETE WORKSHOP TRANSCRIPT, *supra* note 29, at 131-32.

[33] NON-COMPETE WORKSHOP SLIDES, *supra* note 29, at 55; NON-COMPETE WORKSHOP TRANSCRIPT, *supra* note 29, at 138-39.

[34] NON-COMPETE WORKSHOP SLIDES, *supra* note 29, at 59 (studies of corporate executives and physicians); NON-COMPETE WORKSHOP TRANSCRIPT, *supra* note 29, at 144-45, 147-49; *see also* NON-COMPETE WORKSHOP SLIDES, *supra* note 29, at 61 (study of financial advisors showed that in states where non-competes are banned or not enforced, because of the threat of an advisor leaving and taking valuable clients with them, firms are forced to put up with higher misconduct, including higher fees charged to clients).

evidence is necessary before comprehensive curtailing of NCAs in all contexts."[35] He also went on to argue that, while some argue that wage depression can be linked to non-competes, such an attempted correlation "is oversimplification—many factors have contributed to this."[36] He pushed back further on the current momentum toward an outright ban on non-competes, noting that non-compete agreements "have been used for centuries, and empirical evidence on effects is relatively nascent."[37]

Questions regarding the impact of non-competes remain to this day. In its 2021 report on "NonHSR Reported Acquisitions by Select Technology Platforms, 2010-2019: An FTC Study,"[38] FTC staff found:

> More than 75% of transactions included non-compete clauses for founders and key employees of the acquired entities, with relatively small variation in the percentage of transactions that had non-compete clauses across the five respondents. Higher value transactions were more likely to use non-compete clauses.[39]

Note that this study found that, in these transactions, non-competes applied to "founders and key employees," and that, as those founders and key employees received more money from the transaction, they were more likely to agree to non-compete agreements. This is not evidence of a draconian misuse of non-competes; rather it's that the transaction market takes into account the value of non-competes and fully compensates those that agree to enter into such agreements with higher transaction payments, often by millions of dollars, as discussed below.

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[35] NON-COMPETE WORKSHOP SLIDES, *supra* note 29, at 66; NON-COMPETE WORKSHOP TRANSCRIPT, *supra* note 29, at 151-52.

[36] NON-COMPETE WORKSHOP SLIDES, *supra* note 29, at 67 (concluding that "[e]mpirical evidence is even more sparse on the firm and consumer sides."); NON-COMPETE WORKSHOP TRANSCRIPT, *supra* note 29, at 152-53.

[37] NON-COMPETE WORKSHOP SLIDES, *supra* note 29, at 68; NON-COMPETE WORKSHOP TRANSCRIPT, *supra* note 29, at 153-54.

[38] FED. TRADE COMM'N, NON-HSR REPORTED ACQUISITIONS BY SELECT TECHNOLOGY PLATFORMS, 2010–2019: AN FTC STUDY (September 15, 2021), https://www.ftc.gov/system/files/documents/reports/non-hsr-reported-acquisitions-select-technology-platforms-2010-2019-ftc-study/p201201technologyplatformstudy2021.pdf.

[39] *Id.* at 37. The study further found that in almost every transaction over $25 million, non-competes were involved.

III. A Blanket Ban on Non-Competes Will Take Money Out of the Pockets of Employees and Restrict Their Ability to Build Skills

Besides creating a completely unworkable system for preventing employees from walking out the door with valuable intellectual property, the result of banning all non-compete agreements will be that employees will suffer, as one veteran litigator explains:

> Businesses already take a big risk by investing a significant amount of money into projects that may not pan out, and to take the further risk that those employees can immediately take that know-how to a competitor may lead to businesses just opting not to take that risk and not want to throw the money at it. . . NDAs cannot make an employee forget what he's learned or allow an employer to monitor what's being disclosed. So those are not an adequate tool for the employer. Now, large businesses might be able to absorb that risk, but smaller ones will not. This will lead to fewer job opportunities for workers in the tech field, not more, as smaller businesses will exit the marketplace leaving fewer employers in the industry.[40]

Businesses know this and are willing to pay employees in exchange for protecting their intellectual property. "Employees can usually negotiate stronger compensation packages due to the restrictions posed by non-compete agreements. It's possible that a ban on non-competes may incentivize fewer perks for employees, especially if an employer thinks that their new executive hire can pack up and leave in a few short months after they've learned valuable secrets from their current company."[41]

Remove protections afforded by appropriate non-compete agreements, and employers will likely limit internal access to IP or skills training, for fear that an employee will simply leave to compete (especially if NDAs become non-enforceable as well). The NPRM downplays this possibility:

> The proposed rule may also impact the extent to which trade secrets are shared with workers. Non-compete clauses are commonly justified as a means by which firms are able to protect trade secrets, which may allow those trade secrets to be shared more freely with workers, positively impacting

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[40] FED. TRADE COMM'N, FTC FORUM EXAMINING PROPOSED RULE TO BAN NONCOMPETE CLAUSES, Comments of Eric Poggemiller 41 (Feb. 16, 2023), https://www.ftc.gov/system/files/ftc_gov/pdf/FTC-Forum-Examining-Proposed-Rule-to-Ban-Noncompete-Clauses-February-16-2023.pdf.

[41] Edward Segal, *How Biden's Proposed Ban On Non-Compete Agreements Would Impact Companies*, FORBES (July 9, 2021) (quoting Christopher Ghazarian, General Counsel at Dreamhost), https://www.forbes.com/sites/edwardsegal/2021/07/09/how-bidens-proposed-ban-on-non-compete-agreements-would-impact-companies/?sh=4bf0248874e0.

> productivity. However, to the best of our knowledge, there is no available evidence on this topic which would allow us to quantify or monetize the cost, or identify whether it exists in practice.[42]

Yet, as noted above, IP legal practitioners are already cautioning employers that they will have to restrict access to their prize IP if it can't be protected through non-competes or enforceable NDAs.[43]

IV. Limiting Non-Competes in Acquisition Transactions to 25% Owners Will Deprive Many Employees of the Benefits of an Acquisition

The final area where a blanket ban on non-competes will directly harm employees is in the case of company acquisitions (mergers and acquisitions, or M&A). The proposed rule would provide an exception to the ban on non-competes in the case of a company acquisition, but the exception is limited only to "substantial owners" of the business, defined as those owning 25 percent or more of the business.[44] In the tech sector especially, it is quite common for the acquiror to "tie up" senior management and key personnel with non-compete agreements as part of the acquisition, and pay those key personnel handsomely in exchange. This includes both owners of more than 25 percent of the equity in the business, and key personnel which the acquiror wishes to retain and reward who might not reach the 25 percent threshold. Banning non-competes in these instances literally will take money, possibly millions, out of the pockets of young entrepreneurs.

Without the ability to tie up personnel with reasonable non-competes, either deals will not get done, or the price of future deals will decline precipitously. "Such a restriction would," one practitioner notes, "limit the ability of buyers to prevent minority shareholders, who play a role in the business, from competing with the acquired business after the sale. This shift in dynamics could have implications across the deal-making arena, from valuations to

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[42] NPRM, *supra* note 5, at 3529.

[43] *See* Aaron Levine & Matt Todd, *FTC Noncompete Ban Could Erode Trade Secret Protections*, LAW360 (Feb. 28, 2023), https://www.law360.com/articles/1579186/ftc-noncompete-ban-could-erode-trade-secret-protections ("In addition, much greater emphasis needs to be placed on physical and information technology controls for important information because contractual terms—though reasonable measures under the Defend Trade Secrets Act—may not actually be reliable per the FTC's functional approach to effectively protect trade secrets after an incident. As a result, employees can likely expect tighter access controls, more surveillance in the workplace and most likely a much more thorough annual performance review, incorporate elements of trade secret access and management, and a much more detailed exit review. By not allowing employers the ability to use agreements to control trade secret misappropriation, the FTC will force employers to further visibly intrude on the privacy of employees at the workplace, or on their devices, which is a consequence that will have to be examined carefully in the time to come.").

[44] NPRM, *supra* note 5, at 3508.

closing conditions."[45] As another M&A practitioner put it, "Erosion of protections from competition will be factored into the purchase price by buyers evaluating the value of an entity and by sellers looking to maximize the value of their enterprise."[46] The value an employee brings to a business, and the ability of an employee to leave post-acquisition to compete, does not necessarily correlate to the equity position of the employee. Two veteran labor lawyers explain:

> And the amount of equity owned by an individual is not necessarily correlated to the value that individual brings to an organization, which may be based more on their level of involvement in the business or relationships they may maintain. Further, key employees often have significant institutional knowledge and relationships that drive the profitability of the organization, but they may not meet the ownership threshold of the proposed rule. In fact, in many instances, those key employees have no or nominal ownership interest. Locking key employees into employment agreements that include noncompete restrictions is often, from a buyer's perspective, critical to consummating the purchase. This is also critical from a seller's perspective as it helps justify a higher selling price. Permitting key employees with valuable information to compete with a buyer immediately after closing could significantly dilute the value the business, which could not just drive down the purchase price, but also deter some buyers.[47]

CONCLUSION

It is no secret that Chair Khan has a general loathing of mergers.[48] One way to wreck the economy, especially in the tech sector, is to constrain mergers by outlawing non-competes

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[45] *Proposed FTC Ban on Non-Competes: Consideration for M&A Transactions*, HUNTON ANDREWS KURTH (Jan. 18, 2023), https://www.huntonak.com/en/insights/proposed-ftc-ban-on-non-competes-considerations-for-manda-transactions.html.

[46] Adam Gersh & Mariel Giletto, *FTC Noncompete Ban Could Harm Buyers and Sellers in M&A*, FLASTER GREEENBERG (Feb. 10, 2023), https://www.flastergreenberg.com/newsroom-articles-ftc-noncompete-ban-could-harm-buyers-and-sellers-in-ma.html.

[47] *Id.*

[48] FED. TRADE COMM'N, REMARKS OF CHAIR LINA M. KHAN REGARDING THE REQUEST FOR INFORMATION ON MERGER ENFORCEMENT, DOCKET NO. FTC-2022-0003 (2022), https://www.ftc.gov/system/files/documents/public_statements/1599783/statement_of_chair_lina_m_khan_regarding_the_request_for_information_on_merger_enforcement_final.pdf ("Evidence suggests that decades of mergers have been a key driver of consolidation across industries, with this latest merger wave threatening to concentrate our markets further yet."); Lina Khan, *ESG Won't Stop the FTC*, THE WALL STREET JOURNAL (Dec. 21, 2022, 5:10 PM), https://www.wsj.com/articles/esg-wont-stop-the-ftc-competition-merger-lina-khan-social-economic-promises-court-11671637135; Sharron Bennet, *FTC Chair Lina Khan's 'illegal*

that would compensate employees as part of an acquisition through the use of such restrictive agreements. The FTC should reconsider its conclusion that non-competes may only be used in a limited situation in the merger context to reflect the realities of the marketplace.

Respectfully submitted,

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April 19, 2023

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