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SPOTLIGHT ON

Preserving the Responsible Use of Non-Compete Agreements

Policymakers should shift from full blanket bans to a middle-ground approach that protects both middle/low wage workers and employee mobility while enabling companies to safeguard American innovation and competitive advantage.

By Ani Huang

About this Series

HR Policy Association (HRPA) represents nearly 400 of the largest companies worldwide. Members employ more than 10 million individuals in the U.S. This report articulates the perspectives of our members regarding the trajectory of work in the U.S. and the need for specific changes in both corporate and public policies to effectively advance the future of the American workforce.

HR Policy Association's "Advancing the American Workforce" series equips policymakers and business leaders with insights from Chief Human Resource Officers (CHROs) of major companies. The profound changes employers and society have experienced over the past five years have transformed the way large employers and their employees think about work, the workforce, and the workplace and how each needs to be structured for long-term success. HR Policy provides the perspective, not only from employers, but from CHROs who bridge the goals of their companies with the talents and needs of its greatest asset: employees.

New technologies, evolving demographics, and shifting political winds demand a strategic approach to HR. Chief Human Resource Officers are at the forefront of navigating these changes, and their perspective provides invaluable insights for policymakers. This multi-part series offers practical experiences and perspectives on the critical trends shaping the future of work, and suggests policy approaches to ensure the American workforce remains at the vanguard of global excellence in the years to come.

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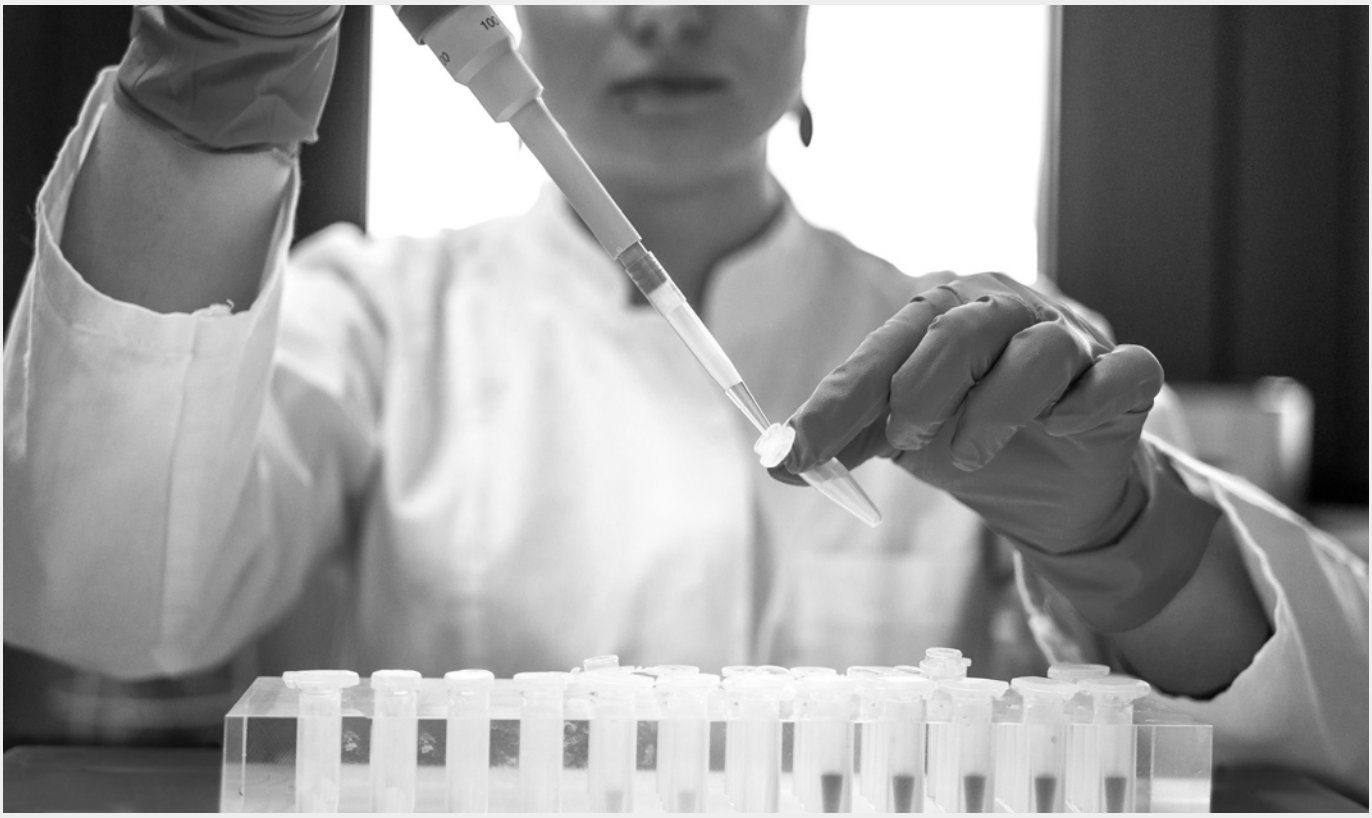

EXECUTIVE SUMMARY

Preserving the Responsible Use of Non-Compete Agreements

Non-compete agreements are an important tool that help companies protect vital investments in their employees, while ensuring the security of research and development, trade secrets, and institutional knowledge.

Increasingly, certain policymakers have focused on blanket bans on non-compete agreements, with the well-intentioned but misguided belief that these bans will protect employee mobility and promote labor market competitiveness.

The legislative and regulatory landscape around non-competes in the United States is complex and constantly evolving, with a mix of federal and state laws addressing the issue. As we look to 2030 and beyond, policymakers should take a middle-ground approach to non-compete legislation that protects both middle/low wage workers and employee mobility while also enabling companies to safeguard their intellectual property and competitive advantage.

Companies Rely on Non-Competes to Protect American Innovation

Large employers use non-compete agreements for executive-level employees or those with access to sensitive information; the agreements are limited in time and are often tied to specific benefits.

In a January 2023 survey of HR Policy Association members, 75% of respondents indicated that fewer than 10% of their employee population were subject to non-compete restrictions (28% of these respondents utilized non-compete agreements for fewer than 1% of their workforce). HRPA's survey also showed that member companies, in nearly all cases, used non-compete agreements solely for executive or leadership level employees or those employees with specific access to confidential and proprietary information.[1] Further, most companies reported that their non-compete agreements remain in effect for no more than one year after an employee's departure, and as little as six months for non-executive officers.

Large employers typically use non-compete agreements for executive-level employees or other employees with access to sensitive information. The agreements are limited in time and are most often included as consideration for equity awards or severance agreements (*i.e.*, tied to a specific benefit). These agreements are the result of negotiation between sophisticated parties often represented by legal counsel, not an imbalance in bargaining power between the employer and the employee. Finally, these agreements are entered into to protect trade secrets, intellectual property, and proprietary information and (to a lesser extent) the company's goodwill and reputation with its customer base. Each of these are reasonable justifications recognized under state law and by the courts.[2]

There has been a recent explosion of state and federal action to completely ban the use of non-compete agreements at all levels of a company. The FTC finalized its sweeping ban in 2024, while New York may join California and a number of other states with total non-compete bans, not to mention the existing patchwork of limited bans in a slew of other states.

A blanket ban on non-compete agreements, such as the FTC's rule, while intended to protect employee mobility and promote labor market competitiveness, would in fact present significant challenges for companies and the safeguarding of intellectual property.

75% of large employers report that fewer than 10% of their employee population is subject to non-compete agreements.

Most non-compete agreements remain in effect from 6 months to 1 year after an employee's departure.

SOURCE: HR POLICY ASSOCIATION'S CHRO SURVEY, 2023

The FTC's Blanket Ban is Not the Answer

While intended to protect employee mobility and promote labor market competitiveness, a blanket ban on non-compete agreements – such as the FTC's rule – would in fact present significant challenges for companies and the safeguarding of intellectual property.

Protection of Trade Secrets and Proprietary Information: Non-compete agreements serve as a critical tool for protecting trade secrets and proprietary information. Without them, companies face heightened risks of employees leaving to work for competitors and potentially taking sensitive information, leading to unauthorized use or disclosure of valuable intellectual property. Such agreements are often the only protection available to a company, since it can be virtually impossible to determine what proprietary information the former employee has shared with the new employer.

Innovation and Research & Development: Companies heavily invested in research and development, particularly in industries with long product development cycles, such as medical device development, rely on non-compete agreements to retain talent and protect their innovation. A blanket ban would enable employees critical to the development of the product, technology or research to take proprietary information to competitors, hindering innovation and impeding technological advancements in industries reliant on intellectual property.

Competitive Disadvantage: Companies may face a competitive disadvantage without the ability to limit employees' immediate entry into competing firms. This unrestricted mobility could allow competitors to poach key talent, benefiting from the knowledge and expertise gained from a former employer, thus eroding a company's market share or competitive edge.

Impact on Training and Investment: Companies invest significantly in training and development of employees. Without non-compete protections, there's a risk of employees leaving shortly after substantial investments in their skills and knowledge, leading to losses for the company.

Regional Competitiveness: In jurisdictions where non-competes are banned, local companies might struggle to compete against counterparts from regions with more favorable IP protection laws. This could result in talent drain and economic challenges for companies with facilities in these regions.

Non-competes are a vital tool

A full ban presents significant challenges for companies and the safeguarding of intellectual property

HRPA's Policy Recommendations

Properly tailored federal legislation could achieve the goals of both opponents and proponents of non-compete agreements.

A middle ground solution would prohibit their use for lower-wage, entry-level employees with little to no economic leverage, while retaining their use for more sophisticated, highly compensated employees. The latter group generally consists of employees with significant economic leverage and access to the types of information companies are seeking to protect.

A framework for potential model legislation should encompass the reforms below.

HR Policy Association Supports the Following Reforms:

1. **Reform non-compete agreements to apply to specific populations**
   Non-compete agreements would be presumed lawful for protection of specific business interests for all employees making more than the average wage in the state in which the agreement is operative.

2. **Eliminate non-compete agreements for lower-wage employees**
   Non-compete agreements would be prohibited for employees making below the average wage in the state in which the agreement is operative.

3. **Define lawful protectable business interests**
   Lawful protectable business interests would include trade secrets (broadly defined), ongoing client and customer relationships, as well as certain specific business sales or business creations.

4. **Narrowly tailor the geographical area and scope of the competition**
   For agreements to be lawful, they must be narrowly tailored in geographical area and type of work or services impacted to protect a lawful protectable business interest.

5. **Limit the time that agreements are in effect after work relationships end**
   For trade secrets and client and customer relationships, non-compete agreements cannot be in effect for more than one year after the work relationship ends.

6. **Extend the effective period for specific cases**
   For business creation and business sales, the period would be extended to five years.

Federal action is needed to responsibly preserve non-competes

Without reforms, American companies face significant challenges, stifled innovation, and reduced competitiveness in the global market

A Final Thought on Non-Compete Agreements

In the absence of federal action, replicating current, workable state laws (such as in Georgia) across different jurisdictions would be the most effective option to preventing a proliferation of more restrictive actions, including blanket bans. In any case, creating more uniformity and harmony across the states should be a priority.

Endnotes

[1] Nearly half of respondents also reported using non-compete agreements for equity recipients, as a condition of receiving such equity.

[2] *Noncompete Agreements and American Workers: Hearing Before the Subcomm. On Small Business and Entrepreneurship*, 116th Cong. 70-84 (2019) (Written Testimony of Russell Beck, Partner, Beck Reed Riden LLP).

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ABOUT

HR Policy Association

For more than 50 years, HR Policy Association has been the lead organization representing Chief Human Resource Officers of major employers. HRPA consists of nearly 400 of the largest corporations doing business in the United States and globally. These companies are represented in the organization by their most senior human resource executives. Collectively, HRPA member companies employ more than 10 million employees in the United States, over nine percent of the private sector workforce, and 20 million employees worldwide. These senior corporate officers participate in the Association because of their unwavering commitment to improving the direction of human resources policy. To learn more, visit hrpolicy.org.