April 19, 2023

VIA ELECTRONIC SUBMISSION

April J. Tabor
Secretary of the Federal Trade Commission
600 Pennsylvania Avenue NW
Washington, D.C. 20580

Re: Non-Compete Clause Rule (16 CFR Part 910)

Dear Ms. Tabor:

The American Investment Council (the "AIC") appreciates the opportunity to submit this letter to the Federal Trade Commission (the "FTC" or the "Commission") on the Notice of Proposed Rulemaking concerning the "Non-Compete Clause Rule," published on the Federal Register on January 19, 2023 (hereinafter, the "NPRM"). The AIC submits this letter on behalf of our members, which include private equity and private credit firms.[1] Our members are united by their commitment to growing and strengthening the companies in which, or on whose behalf, they invest; and to helping secure the retirement of millions of pension holders and the financial security of America's educational institutions.

The AIC supports the FTC's use of its legal authority to address unfair methods of competition, including certain instances of noncompete clauses between employers and employees.[2] This comment letter will not address the question of the Commission's authority to promulgate regulations concerning "unfair methods of competition" under Section 6(g) of the Federal Trade Commission Act ("FTC Act").[3] We submit it to answer several questions posed by the NPRM, and to emphasize how (i) the noncompete arrangements most commonly used by our members comport with the antitrust and state contract law cited in the NPRM; and (ii) the empirical evidence the NPRM describes does not suffice to support a rule that would ban those arrangements. The use of noncompete clauses identified as examples of unfair methods of competition in the NPRM are categorically distinct from the ones with which our members are involved. Under law and in fact, they are materially different from noncompete clauses binding low-wage employees like the "cashier at a burger place" described by President Biden

[1] For purposes of this letter, we generally use the term "private equity" to encompass private equity funds, private credit funds, and other private investment vehicles.

[2] *See, e.g.*, Fed. Trade Comm'n, Complaint, *In re Prudential Sec., Inc. et al.*, Matter No. 221 0026 ¶¶ 12–13 (Dec. 28, 2022).

[3] Solely for purposes of this letter, the AIC takes no position on that authority, or specifically the rule proposed in the NPRM. The AIC notes that numerous statutory, constitutional, and other legal questions have been raised with respect to both, and reserves the right to raise those issues, or to support legal challenges to a final rule based on them, at a later date.

during his State of the Union address—or the "fast-food workers, arborist and manual laborers" described by FTC Chair Khan in a recent essay.[4]

The noncompete clauses in our members' industry are mutual agreements among sophisticated actors in multiple capacities; typically involving private equity firms, the companies in which they invest, selling equity owners, senior management and other highly compensated employees, not rank-and-file workers. They are not exploitative and do not lessen competition. In fact, they support investment and competition by, for example, enabling the combination of capital and management that helps companies thrive. In the private equity industry, noncompete clauses protect investors and incentivize firms to invest heavily in their people—developing and sharing investment ideas that improve the intellectual capital (and job prospects) of employees and the financial well-being of investors. In a real sense, equity holders, senior executives, and highly-paid and highly-skilled employees in private equity firms and portfolio companies receive important consideration for including these noncompete clauses within their agreements. These arrangements are not unfair methods of competition under Section 5 of the FTC Act—indeed, the NPRM cites not one case in which a noncompete clause in our industry has been adjudged illegal under the antitrust laws, or even the subject of antitrust enforcement—and thus are not appropriate subjects for rulemaking.

As detailed below, there are reasonable ways for the FTC to address the concerning practices that are the focus of the NPRM while still permitting pro-competitive noncompete clauses to be used to address the legitimate concerns and business realities that the law today permits, including in the context of investments of the sort that private equity firms typically make. The AIC appreciates the opportunity to address these issues and respond to questions identified in the NPRM.

The AIC and Private Equity

The AIC is an advocacy, communications, and research organization established to advance access to capital, job creation, retirement security, innovation, and economic growth by promoting responsible long-term investment. In this effort, the AIC develops, analyzes, and distributes information about the private equity industry and its contributions to the U.S. and global economy. Established in 2007, and formerly known as the Private Equity Growth Capital Council, the AIC is based in Washington, D.C.[5]

Private equity firms partner with their investors—including public pension funds, insurance companies and college endowments—to invest in companies and improve their performance, creating jobs and long-term value in the process. The returns from these ventures go directly to investors, including more than 34 million schoolteachers, first-

[4] Lina Khan, *Noncompetes Depress Wages and Kill Innovation*, N.Y. Times (Jan. 9, 2023).

[5] For further information about the AIC and its members, please visit our website at http://www.investmentcouncil.org.

responders, and other public servants who depend on pension returns for their retirements.

Over 5,000 private equity firms invested more than $4.5 trillion in American companies over the past five years.[6] More than 60% of that goes to support some 5,205 small businesses.[7] That tremendous investment in the American economy supports competition and jobs. In 2020, private equity-backed companies directly employed more than 11 million workers in all 50 states.[8] These are good jobs. Workers employed by private equity-backed companies earn higher salaries than the average American, which provides crucial support as historic inflation makes it more difficult for families to afford everyday goods.[9]

The investments AIC's members make in companies support competition, providing long-term stability even (and especially) in turbulent economic times. Take the Great Recession of 2008. A study by scholars at the Kellogg School of Management at Northwestern University and the Harvard Business School found that "*companies backed by private equity firms were more resilient in the face of the financial crisis compared to their counterparts*."[10] Investment capital, which our members provide, is an important driver of the United States economy, enabling companies to grow, hire, build, innovate and serve customer needs. It is the fuel of competition.

Those investments also bear fruit for investors. Year after year, private equity delivers the strongest returns of any asset class for investors across America—helping fuel public pension funds and strengthen retirements for American workers across all industries. In 2022, private equity investments delivered a median annualized return of 11.4% for state pension plans over a 22-year period, exceeding the median annualized return of public equity by 5.6%.[11] As public markets grow more volatile, private equity serves as an increasingly important tool for diversified pension funds looking for reliable investments.

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[6] Ernst & Young, *Economic Contribution of the US Private Equity Sector in 2020* (May 2021), available at: https://www.investmentcouncil.org/wp-content/uploads/ey-aic-pe-economic-contribution-report-final-05-13-2021.pdf.

[7] *Id*.

[8] In submitting this letter, the AIC does not purport to comment on behalf of each of the private equity-backed companies.

[9] *Id*.

[10] Shai Bernstein, Josh Lerner & Filippo Mezzanotti, *Private Equity Helped Firms Weather the Great Recession* (Jan. 4, 2018), available at: https://insight.kellogg.northwestern.edu/article/private-equity-helped-firms-weather-the-great-recession. Recent research has made similar findings as it relates to the COVID-19 pandemic. *See* Paul Lavery & Nick Wilson, *The Performance of Private Equity Portfolio Companies During the COVID-19 Pandemic* (Dec. 12, 2022), available at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4301174.

[11] Cliffwater, *Long-Term Private Equity Performance: 2000-2022* (Feb. 28. 2023), available at: https://www.investmentcouncil.org/wp-content/uploads/2023/03/Cliffwater-Long-Term-PE-Performance46.pdf.

1. Responding to the NPRM's Questions.

The AIC welcomes the opportunity to respond to the questions posed by the NPRM, and to provide additional information as to how noncompete clauses typically are used in the private equity industry and the companies in which our members invest—all in ways that are fair to workers, consistent with governing law, protective of confidential and sensitive information, and value-enhancing for workers, portfolio companies and investors alike. The NPRM poses questions about three categories of noncompete clauses typically used in the private equity industry and our portfolio companies: those with the sellers of an acquired business; those with senior executives; and those with highly paid and/or highly skilled workers. For each of these categories, there are significant competitive advantages and benefits to the company; to our members' investors, who in turn invest in the company; and to the employees subject to the noncompete clauses, who themselves are often equity owners of the company. Not only does the NPRM fail to provide a sufficient basis for a rule banning noncompete clauses, doing so would undermine the benefits that companies, investors, and their employees presently derive from them. Should the Commission propose a final rule, these categories of noncompete clauses should not be included.

The NPRM lacks a basis for barring the vague category of "*de facto* noncompete clauses," a regulation that would inevitably be unworkable. Finally, the NPRM's conclusory identification of purported alternatives to noncompete clauses fails to provide adequate protection for sensitive company information and trade secrets.

A. Exception for Sale of Business

The Proposed Rule provides an exception to the ban for noncompete clauses entered into by a person selling a business or otherwise disposing all of their interest in the business, or by a person selling all or substantially all of the operating assets of the business, where the person restricted has a "substantial" interest in the business, defined in turn as an equity interest of 25% or more.[12] The NPRM seeks comment on this exception, including whether to apply any ownership threshold.[13] Our members have substantial experience with noncompete clauses binding sellers of a business, and neither their experience nor the NPRM offers any basis to conclude that such contractual clauses (at any level of ownership) constitute unfair methods of competition. Consistent with state laws across the country, these types of noncompete clauses should be categorically excluded from any ban the Commission might propose.

As a threshold matter, noncompete clauses such as these do not bind "workers"—they bind equity owners, whether they be majority or minority. They apply to capital, not

[12] NPRM at 114, 128.

[13] *Id*. at 130-31. The AIC notes that the NPRM fails to explain which forms of equity should be considered in calculating the threshold.

labor. Including such noncompete clauses within a ban targeting worker noncompete clauses is simply a category error.

Noncompete clauses such as these are not unfair methods of competition. The NPRM cites no case or even enforcement action in which such a noncompete clause, standing alone, has been found to violate the law, whether it be state contract law or antitrust law, including Section 5. The AIC is also unaware of any.

Under the Commission's Policy Statement Regarding the Scope of Unfair Methods of Competition Under Section 5 of the Federal Trade Commission Act (the "Section 5 Policy Statement"), it asks two questions in determining whether conduct constitutes an unfair method of competition. The first is whether "the conduct may be coercive, exploitative, collusive, abusive, deceptive, predatory, or involve the use of economic power of a similar nature."[14] Noncompete clauses binding selling equity owners of a business are no such thing. They are a result of careful negotiations between sophisticated and separately represented parties with legitimate goals, each seeking to maximize value. They are an expressly bargained-for exchange in the context of a broader transaction, and typically supported by vital and value-enhancing business reasons for both buyer and seller.[15]

From the perspective of the entity purchasing a business, such agreements are critical to realizing the value of the business being acquired and thus fundamental to the value proposition of the transaction. They are also critical to preserving the competitiveness of a company, *i.e.*, competition. That is why the FTC has previously approved divestiture orders that include noncompete clauses.[16] The NPRM takes the position that contractual terms the FTC itself has repeatedly imposed on companies are in fact illegal unfair methods of competition.

Noncompete clauses are essential to preserving the value—and competitiveness—of purchased companies. Without them, sellers of a business could profit immediately, then turn around, leave the business, and damage the goodwill in which the seller invested. As the NPRM recognizes, "restricting these types of non-compete clauses could potentially affect business acquisitions, including the incentives of various market actors to start, sell, or buy businesses."[17] That is to say, without these noncompete clauses, buyers would pay less for companies, hurting anyone with equity from majority owners to founders to workers with a stake. Where employees hold equity, their financial well-being is related to that of the company. An FTC rule that destroys the value of businesses,

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[14] Section 5 Policy Statement at 5.

[15] In any event, a final rule should exclude noncompete clauses that are paired with specific, bargained-for consideration.

[16] *See* Fed. Trade Comm'n, Decision and Order, *In re Polypore International, Inc.*, Matter No. 081 0131 at 14, 24-25 (Nov. 5, 2010).

[17] NPRM at 129-30.

including in particular smaller, family-owned businesses that are most likely to be subject to seller noncompete clauses, can hardly be considered pro-competition.

From the perspective of the individuals bound by the noncompete clause, the provisions are subject to substantial negotiation, with the individuals often represented by their own counsel, and often involve economic value. These individuals gain when they trade away narrowly tailored ownership and employment restrictions for substantial financial upside. There is no discrepancy of bargaining power, and no risk of exploitation or coercion. These noncompete clauses are also narrower than in the labor context, as state law generally requires that they be limited to the business, including its geographic scope as it existed at the time the transaction takes place, and are therefore well tailored to their purposes of protecting the buyer's investment and justifying the substantial consideration provided to the owners.

The FTC's Section 5 Policy Statement also asks about the impact of the business conduct on competitive conditions. The NPRM cites no legal basis and no empirical support for the proposition that noncompete clauses incident to the sale of a business negatively affect competitive conditions. Quite the contrary, these provisions are not (like labor noncompete clauses) subject to higher scrutiny under state law precisely because they enable investors in the company to get the benefit of what they are buying and avoid the unfair scenario in which an equity owner gains from selling a business and then turns around and erodes the value for the buyer. Courts recognize the value of these noncompete clauses: the sale of business exception "serves an important commercial purpose by protecting the value of the business acquired by the buyer. In the case of the sale of the goodwill of a business it is 'unfair' for the seller to engage in competition which diminishes the value of the asset he sold."[18] The "seller" in this context is the individual bound by the noncompete clause. *Banning* these noncompete clauses would be unfair, not *enforcing* them. The net result from barring such noncompete clauses will be less investment in companies with promise, less money for founders and entrepreneurs to build, less value realized by willing sellers, and the lessening of competition that comes with all of them.

All of that is why state laws treat noncompete clauses incident to the sale of a business as categorically different from other kinds of noncompete clauses. As the NPRM makes clear: "all states permit non-compete clauses between buyers and sellers."[19] In California, a state touted by the NPRM for its low level of noncompete enforceability[20] and economic vitality,[21] noncompete clauses may be applied in the

[18] *Strategix, Ltd. v. Infocrossing West, Inc.*, 142 Cal. App. 4th 1068, 1072-73 (2006) (citations omitted).
[19] *Id*. at 130.
[20] *Id*. at 56.
[21] *Id*. at 30, 100-01.

context of a sale of business transaction.[22] And California's statutory sale-of-business exception provides no minimum threshold for the amount of ownership in question.[23]

There is absolutely no legal basis, or competition policy basis, to condemn noncompete clauses entered into as part of the sale of a business. Nor is there an empirical one, as the NPRM also makes clear. The evidentiary record it lays out concerns noncompete clauses "that arise solely out of employment."[24] The NPRM concedes that "there has been little empirical research" concerning noncompete clauses entered into as part of a sale of a business,[25] and it cites none at all. The NPRM goes on, stating that the Commission is "not aware of empirical research on the economic effects of applying additional legal restrictions to these types of non-compete clauses."[26] The NPRM thus offers no empirical—or, again, legal—basis to condemn noncompete clauses entered into as part of a sale of a business.

The NPRM's limitation of the exception to majority sales and only for "substantial owner[s]" of 25% of the business is arbitrary and also has no legal or factual basis.[27] It is not based on any law or legal decision; and the NPRM cites no empirical (or any other) evidence to support the 25% threshold.[28] The number is apparently cut from whole cloth and not even justified.[29] In most real-world situations, such a threshold is far too high and would produce absurd results: the practical implication is that a business owned in equal shares by five individual founders could not bind any or all of them not to walk out the door the day after closing and start a directly competing business (or businesses). The threshold also fails to distinguish, for example, between passive investors, who may hold a significant stake in a company but do not necessarily have the information or skills necessary to compete and erode the value of the business, and those who do have such information and skills and stand to receive substantial consideration in a sale, but hold a percentage ownership interest that falls below the threshold. Consider a closely held business with a passive 80% equity owner and an active manager with a 20%

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[22] *See* Cal. Bus. & Prof. Code § 16601.

[21] *Id*.

[24] NPRM at 116.

[25] *Id*. at 130.

[26] *Id*.

[27] *Id*. at 106.

[28] Courts including in California have enforced noncompete clauses against sellers of far less than 25% of a business. *See, e.g.*, *Vacco Indus. Inc. v. Van Den Berg*, 5 Cal. App. 4th 34 (1992) (enforcing noncompete clause against seller with 3% ownership interest).

[29] The NPRM effectively acknowledges that it has little basis for the substantial owner line drawing exercise it performs. NPRM at 113 ("The Commission is proposing a threshold of 25% ownership interest because the Commission believes the exception should be available where, for example, a few entrepreneurs sharing ownership interest in a startup sell their firm."); *id.* at 114 ("The Commission believes a 25% threshold strikes the appropriate balance between a threshold that may be too high (and would exclude many scenarios in which a non-compete clause may be necessary to protect the value of the business acquired by the buyer) and a threshold that may be too low (and would allow the exception to apply more broadly than is needed to protect such an interest).").

equity stake.[30] Moreover, while many founders might own more than 25% of an enterprise at its early stages, each new round of investment typically would dilute founders to increasingly smaller percentages. The arbitrary threshold also fails to adequately address the pro-competitive concerns addressed above, reflected in the NPRM and state law.

Allowing owners to profit twice—first from sale of a business and then by eroding the value of the business—serves no one's interests, or any competition goal. Should the Commission propose a final rule, noncompete clauses with the selling shareholders of a business should be categorically excluded.

B. Senior Executives and Founders

The NPRM evaluates the application of the proposed ban on senior executives and seeks comment on this application.[31] Our members have substantial experience with noncompete clauses for senior executives, both within their firms and at portfolio companies in which they invest. For some senior executives,[32] these clauses are the subject of careful negotiation by resourced and sophisticated parties, often with the executives retaining separate counsel. And even where the noncompete clause is not negotiated, it is part of a package that involves considerable cash and equity compensation and protects critical competitive interests, like incentivizing training, and maintaining trade secrets and relationships with investors and key business partners.[33] These senior executives can become partners of the funds that they manage. Noncompete clauses in the context of limited liability companies and general partnerships are procompetitive, and thus explicitly protected by state law.[34]

The benefit to the executive is not limited to compensation. Trying to protect intellectual property without noncompete obligations can impose costs and inefficiency, inhibiting the sharing of ideas, preventing executives and others from critical professional growth, and ultimately hurting investors. Enabling noncompete clauses reduces these

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[30] The NPRM's discussion of and questions regarding noncompete clauses adopted in the context of business sales do not address any number of similar business transactions that may involve noncompete clauses including, for example, capital infusions where the continued participation of key personnel is required.

[31] NPRM at 150-52.

[32] The NPRM declines to define "senior executive" and instead seeks comment on an appropriate definition. NPRM at 150-51. Senior executive has no consensus meaning and our members' experience cautions against any attempt for a one-size-fits-all definition. Nevertheless, the analysis herein with respect to senior executives is applicable to those employees who exercise managerial responsibility, oversee business units, direct firm strategy and/or exercise budgetary authority with respect to any operating unit of a business enterprise. It also includes partners in professional or investment partnerships. *Accord infra* at 15.

[33] *See Am. Fin. Res., Inc. v. Money Source, Inc.*, No. 14-1651, 2014 WL 1705617, at *9 (D.N.J. Apr. 29, 2014).

[34] *See, e.g.*, Cal. Bus. & Prof. Code § 16602 (permitting noncompete clauses with partners in a partnership); *id.* § 16602.5 (permitting noncompete clauses for members in a limited liability company).

costs, making for a better workplace with more opportunity for professional growth, including that stemming from professional success.

Noncompete clauses work to enhance the mobility of senior executives in a manner the NPRM ignores entirely. Such employees have legal duties of confidentiality and fiduciary obligations to the firms they run (and own). Those duties do not terminate when employment ends, but rather carry on, creating legal risk to them and their future employers. As a practical matter, the term of noncompete clauses (which, under the law, must be reasonable in duration) gives a fixed end date to this uncertainty. There is a recognition in the marketplace that once the noncompete period has expired, former employers are more comfortable with former employees abiding by the continuing confidentiality obligations. The employees supposed by the NPRM to be prevented from moving on to new jobs by noncompete clauses are in fact freed by them to do just that.

There is no exploitation involved where senior executives agree to be bound by noncompete clauses. There is also nothing to suggest that such arrangements negatively impact competitive conditions. These types of noncompete clauses are not unfair methods of competition, and they should be excluded from any ban the Commission might propose.

Noncompete clauses that bind senior executives also protect another class of individuals, institutional investors, whose beneficiaries include a diverse array of teachers, firefighters, municipal workers, students, and professors. In the context of private equity, the capital used to make investments and run the business comes from pension plans, university endowments, and others similarly situated. As discussed in Section 1.A, *supra*, in the context of portfolio companies, noncompete clauses help protect the value of the company after a purchase. That value is ultimately value to the institutional investors and beneficiaries. For private equity firms themselves, investor capital creates the investment opportunity that drives returns. It funds the operations of the company, critically helping professionals identify the best uses for that capital. Noncompete clauses for senior executives ensure that the training, experience, and benefits to which those executives gain access, generated using investment capital, are directed to benefit institutional investors and beneficiaries. But this is a win-win, generating on the job learning and professional relationships for those executives.

The NPRM cites no legal authority for the proposition that noncompete clauses binding senior executives violate the law. It cites not one case in which any one such clause has been held to violate Section 5, or even state law on noncompete clauses. And while it certainly is plausible that some court held some clause involving a given individual at a particular company to be unreasonable, even a number of those would be a far cry from the systematic condemnation of clauses that might support a rulemaking that

such agreements were subject to a *per se* ban under antitrust law.[35] The NPRM offers no legal support for the proposition that noncompete clauses governing senior executives are unfair methods of competition.

Based on the substantial experience of its members, the AIC agrees with the NPRM's finding that noncompete clauses for senior executives are not exploitative or coercive.[36] This answers the Section 5 Policy Statement's first inquiry in the negative.

According to the Section 5 Policy Statement, where, as in the context of noncompete clauses for senior executives, the conduct is not "facially unfair", "more information about the nature of the commercial setting may be necessary to determine whether there is a tendency to negatively affect competitive conditions," including "[t]he size, power, and purpose of the" firm and "the current and potential future effects of the conduct."[37] This analysis "examines whether the [firm's] conduct has a tendency to generate negative consequences: for instance, raising prices, reducing output, limiting choice, lowering quality, reducing innovation, impairing other market participants, or reducing the likelihood of potential or nascent competition."[38] The evidence marshalled in the NPRM fails to satisfy this standard.

The FTC's recent enforcement actions in the *O-I Glass* and *Ardagh* matters provide a telling contrast. In those cases, the industry in question (glass-blowing) was concentrated; and the public record, including statements from the Commissioners, makes clear that the noncompete clauses functioned as barriers to entry, preventing firms that would compete from doing so because they could not get access to specialized technical skills.[39] The NPRM proposes to bar noncompete clauses in all industries, regardless of whether they are competitive to begin with or whether the noncompete clauses function as barriers to entry. Contrary to the Section 5 Policy Statement, the NPRM does not screen for "size," "power," or "purpose" of the firm, simply assuming that noncompete clauses produce the same effect no matter the realities of the market in question. Nor does the NPRM identify effects of the conduct with remotely the level of rigor, consistency, and confidence necessary to support a blanket economy-wide ban.

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[35] As the NPRM makes clear, antitrust and state contract law both subject noncompete clauses such as these to a reasonableness analysis. NPRM at 51-52. The AIC is aware of no authority for the proposition in the NPRM that a *per se* ban should apply.

[36] *Id*. at 69-72, 86.

[37] Section 5 Policy Statement at 9.

[38] *Id*. at 10. Courts have found that Section 5 bars mere invitations to collude, which standing alone do not violate the Sherman Act and, by definition, do not generate anticompetitive effects. *See FTC v. Motion Picture Advertising Serv. Co.,* 344 U.S. 392 (1953). But the "tendency" of such invitations to result in collusion, which does, is clear. Unlike invitations to collude, noncompete clauses are not incipient violations; and it is not clear precisely what "tendency" the NPRM contemplates.

[39] Fed. Trade Comm'n, Decision and Order, *In re O-I Glass, Inc.*, Matter No. 211 0182 (Feb. 21, 2023); Fed. Trade Comm'n, Decision and Order, *In re Ardagh Group S.A., et al.*, Matter No. 211 0182 (Feb. 21, 2023).

The NPRM purports to make preliminary findings about the effects of noncompete clauses for senior executives on labor and product markets, but these findings do not suffice for several reasons. *First*, the NPRM fails to define senior executives, a term that varies across industries and companies within industries.[40] Where the NPRM points to studies, they either do not concern senior executives or are limited to Chief Executive Officers, which are but a subset of senior executives. The attempt to ascertain effects of noncompete clauses—across myriad companies and industries—based on (very few) studies that are either over- or under-inclusive is simply not sufficient.

Second, the NPRM presents no support for the effects of conduct the FTC's Section 5 Policy Statement requires a "tendency" to generate. It asserts that "non-compete clauses for senior executives may harm competition in product markets in unique ways."[41] But the NPRM cites nothing for this claim—there are no footnotes—and instead speculates about the potential to block new entrants, to curb new business formation, or depress innovation due to senior executives' noncompete obligations.[42]

The experience of AIC's members is completely to the contrary. Noncompete clauses, often with (not immaterial) consideration specifically tied to them, have been used for senior executives in our industry since it began in the 1970s. Since that time, the number and success of firms has blossomed, with the number of private equity firms now exceeding the number of publicly traded firms in the U.S. and considerable ongoing mobility of talent, and there is robust competition on many fronts, including for hiring. There is no evidence of blocked entry, curbed business formation, lack of access to talent, depressed innovation, or any other evidence of negative impacts on competitive conditions. And that is just our industry. The NPRM makes its claims about noncompete clauses that bind senior executives for the whole economy. As a literature review conducted by an FTC economist in 2019 found, "[t]here is little evidence on the likely effects of broad prohibitions of non-compete agreements."[43] Put differently, *according to the FTC*, the state of the academic literature does not reflect the "tendency to generate negative consequences" that Section 5, *according to the FTC*, requires.[44]

In light of the NPRM's claim that noncompete clauses negatively impact business formation, the AIC also wishes to address the specific case of business founders who seek early-stage private equity financing to enable their businesses to grow and compete. The U.S. early growth capital environment has been responsible for countless innovations

[40] NPRM at 150-51. *See supra* n. 32.
[41] NPRM at 80.
[42] *Id*.
[43] John McAdams, *Non-Compete Agreements: A Review of the Literature* 4-20 (Dec. 31, 2019).
[44] For purposes of this comment letter only, the AIC adopts the legal framework declared by the Commission in the Section 5 Policy Statement and applied in the NPRM. The AIC notes that the Section 5 Policy Statement has been subjected to substantial criticism, and reserves the right to raise issues with the framework at a later date.

that have enhanced competition and generated substantial benefits to consumers.[45] The use of noncompete clauses in this environment is extraordinarily important. Competition is fierce in this financing market, and founders have the ability to negotiate noncompete clause terms as part of financing rounds. Founders use this financing to support the growth of companies, in particular in early stages where the absence of that financing can mean going out of business. Noncompete clauses are part of that package. The NPRM discounts (or ignores) the enhanced competition that this financing supports and fails to cite evidence in support of its conclusion that banning founder noncompete clauses negatively affects business formation and innovation. Our experience and the competitive marketplace say the opposite.

The NPRM cherry picks a few academic papers to support arguments about the aggregate negative effects of noncompete clauses generally. As the NPRM concedes, there are other papers with contrary conclusions.[46] The NPRM simply dismisses those. The NPRM's literature review is also materially incomplete, among other things ignoring the one study of which the AIC is aware of employees in the financial services industry. That is surprising, because the study was presented at an FTC conference, is included in the aforementioned literature review published by an FTC economist, and can today be found on the FTC website.[47] The study found substantial negative effects, for companies and consumers, from *reducing* the enforcement of noncompete clauses: more employee misconduct and higher fees for end customers.[48] Here, the tendency of noncompete clauses was to generate positive consequences. Taken together, the empirical record is mixed at best and in any event insufficient to support a broad ban on noncompete clauses.

But even if you ignore the studies cutting against the NPRM's findings and credit wholly the few upon which it relies, the latter are simply gruel too thin on which to predicate a national regulation. The empirical method is a process through which consensus emerges after a long period of testing and retesting propositions against evidence. For the impact of noncompete clauses across the economy, in particular with respect to senior executives (however defined), we are just not there. As the FTC economist's literature review concluded, the "[d]ata on non-compete use in the U.S. are

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[45] *See* Samuel Kortum & Josh Lerner, *Assessing the Contribution of Venture Capital to Innovation* (Winter 2000), RAND Journal of Economics Vol. 31, No. 4, found at: https://www.jstor.org/stable/2696354.

[46] NPRM at 22-24; *see* McAdams, *supra* n. 43.

[47] Umit G. Gurun, Noah Stoffman & Scott E. Yonker, *Unlocking Clients: Non-Compete Agreements in the Financial Advisory Industry* (May 30, 2019), found at: https://www.ftc.gov/system/files/documents/public_events/1494697/gurunstoffmanyonker.pdf; *see* McAdams, *supra* n. 43, at 14, 15, 19; @FTC, Twitter (Nov. 14, 2019, 1:52 PM), https://twitter.com/ftc/status/1195052000758640640 (referring to Gurun et al., *supra*).

[48] Gurun et al., *supra* n. 47; McAdams, *supra* n. 43, at 14, 15, 19.

sparse;" and "further work is needed."[49] (The NPRM also makes no mention of this FTC-produced work product.[50])

In short, the NPRM fails to identify sufficient evidence of the negative impacts on competitive conditions resulting from noncompete clauses for senior executives per the sliding scale approach to conduct that is not facially unfair.[51] In the long experience of AIC members, the existence of noncompete clauses for senior executives does not inhibit competition or mobility.[52]

Third, the NPRM ignores entirely benefits to noncompete enforcement that are prevalent in the private equity industry, both at portfolio companies and private equity firms.

- Senior executives at private equity-backed portfolio companies are often compensated with a combination of cash and equity. These individuals are responsible for managing the growth of the companies for all stakeholders, among other things. Their incentives help ensure that the companies are strong market competitors and that the senior executives' interests are aligned with investors in the company, which include private equity fund investors like pensions. The noncompete clauses that typically apply to these senior executives are tied to equity grants, and there is nothing unfair tying these grants to reasonable noncompete obligations. The NPRM's claim that noncompete clauses are not bargained for is simply not correct when such clauses are linked specifically to continuing equity ownership in a business or to receipt of equity compensation.

- The NPRM also fails to address the competitive benefit to companies of having and keeping the right management. Part of what investors do when they buy companies is ensure, through a variety of incentives and contractual means (including noncompete clauses), that the right people are in place to run them. That is a key mechanism for maintaining and improving competitiveness, a benefit to competition. It protects all owners, including workers, who lose when the business loses. The NPRM also fails to address

[49] McAdams, *supra* n. 43, at 3-4.

[50] The NPRM claims that "[a]s evidence mounted regarding the anticompetitive effects of non-compete clauses, the Commission's focus on this issue increased" and refers to its January 9, 2020, public workshop on noncompete clauses. NPRM at 62. This public workshop, purportedly the culmination of the allegedly mounting evidence, was hosted nine days after the McAdams paper was published *by the FTC*. Nor was the testimony at the workshop remotely as uniform and confident as the narrative the NPRM presents. *See* Jackson Lewis P.C., *Against the Evidence*: *How the FTC Cast Aside the Input of Experts at Its Own Non-Compete Workshop*, J.D. Supra (Feb. 8, 2023); Daniel Gilman & Brian Albrecht, *FTC Proposal Jumps the Gun on Banning Noncompetes*, Law360 (Jan. 19, 2023).

[51] Section 5 Policy Statement at 9.

[52] New employers will often agree to buy out the noncompete obligations, either by making the senior executive whole or by indemnifying any future legal action.

the unique talents that senior executives at portfolio companies may bring to their firm in particular. Private equity investment often entails keeping incumbent management in place, precisely because the people who know a company best are those who run it. While managerial success is sometimes transferable, often a person's skill is optimally applied at a particular firm. The NPRM's assumption that senior executives will be equally or more effective at a company with which they are not familiar[53] is not supported.

- Senior executives at private equity firms are typically compensated through a combination of cash, equity and profit interests, in both the firm and its funds and/or portfolio companies. For similar reasons as apply to noncompete clauses incident to the purchase of a business, it is appropriate for a company to ask senior executives not to compete with it within reasonable bounds; and unfair to require a company to continue to grant ownership and make payouts to individuals who choose to leave that company and compete against it. The interests of private equity professionals should be aligned with fund investors, whom they serve.

- Senior executives at private equity firms may be responsible for leading long-term investment strategy for funds, which creates an investor interest in the continuity of talent.[54] Investors like pensions are willing to put their money at risk because the people managing it have the requisite experience, acumen, skills, and relationships. Their departures can cause disruption, particularly where a senior executive has the ability to take fund strategy or confidential information and repurpose them at a competing firm, for other investors. Just like firms, investors have an interest in protecting the intellectual property they pay to develop and share with senior executives, which interest would be undermined without noncompete clauses. The NPRM does not address this fund investor demand for continuity.

- Finally, some senior executives in private equity are responsible for raising capital, for example from pension funds and insurance companies. Protecting a company's investment in client lists, which are analogous, is a classic justification for enforcing noncompete clauses.[55] Non-solicit clauses are not an adequate substitute in these situations, especially given the NPRM's vague

[53] NPRM at 32.

[54] Indeed, some institutional investors in private equity funds may insist on contractual provisions aimed at retaining key persons responsible for governing the investments, with potentially severe consequences for the fund if the designated key persons leave, the severity of which is often materially enhanced in the case of small- and medium-sized funds. This reflects the importance of continuity in personnel for fund investors and presents an opportunity for the impacted individuals to demand consideration for their agreement to be subject to a noncompete clause.

[55] *See Money Source, Inc.*, 2014 WL 1705617, at *9; *see also* Gurun *et al.*, *supra* n. 47 at 12.

prohibition of "*de facto* non-competes." The NPRM fails to address these justifications.

As the experience of our members illustrates, the NPRM fails to adduce sufficient evidence to support applying a ban on noncompete clauses to senior executives. Should the Commission propose a final rule, noncompete clauses applied to senior executives should be excluded from it. The term "senior executives" should be interpreted broadly to include, at a minimum, those employees who exercise managerial responsibility, oversee business units, direct firm strategy and/or exercise budgetary authority with respect to any operating unit of a business enterprise. Partners in professional or investment partnerships should be included.

C. Highly Paid and/or Highly Skilled Workers

The NPRM evaluates the application of the proposed ban on highly paid and/or highly skilled[56] employees and seeks comment on this application.[57] Our members have substantial experience with noncompete clauses for such employees, both in our firms and at our portfolio companies; and the NPRM does not sufficiently establish that noncompete clauses for these workers are "unfair" under the Section 5 Policy Statement's framework. These types of noncompete clauses, applied to the workers most likely to have valuable trade secrets that noncompete clauses today protect, should be excluded from any ban the Commission might propose.

Highly paid workers are not likely to be exploited or coerced into signing a noncompete clause. Indeed, the NPRM acknowledges that the concern over worker exploitation and coercion is less strong where the workers are well compensated, sophisticated and/or highly skilled.[58] These employees are often also equity owners, like senior executives. Recently adopted state laws recognize that noncompete clauses binding such workers are not *per se* unfair. As the NPRM explains, many states limit enforceability of noncompete clauses based on income or occupation—permitting enforcement for more highly paid employees.[59]

This increasingly prevalent state law approach reflects the practical realities for highly paid employees. In our members' experience, these individuals are well compensated and savvy market actors. They are more likely to negotiate their noncompete clauses and to have the advice of counsel than the low-wage workers who are the focus of the NPRM. They also typically have more power and more options, short

[56] Many of the noncompete clauses at portfolio companies and private equity firms involving highly paid employees also involve highly skilled workers. This letter uses "highly paid" as a shorthand for both "highly paid" and "highly skilled" below.

[57] NPRM at 72.

[58] *Id*. at 81, 122. Nor is there any basis to believe that these workers are subject to any cognitive bias that would prevent them from understanding the noncompete clause within the employment agreement. *Id*. at 84.

[59] *Id*. at 49-51.

and long term, in the job market. With noncompete clauses often tied to grants of equity or severance, this class of employees has a choice to keep the additional compensation or forgo it and compete sooner. They can compete, but they have to forfeit something. Or they can get more compensation. And they are the group for whom the justifications for noncompete clauses—protecting trade secrets, for example—ring most true. Imposing noncompete clauses on such employees is hardly unfair, and not a unfair method of competition. This class of employee has similar characteristics to senior executives[60] and the same reasons support excepting them from to the proposed ban.

Noncompete clauses also facilitate the professional development and increase the marketability of highly paid employees. Losing this important tool will diminish firms' incentives to invest in and train employees, and to share valuable know-how with them, which ultimately reduces the value of human capital and productivity. In the absence of noncompete clauses, firms will unproductively divert time and manpower into creative workarounds to protect their trade secrets, intellectual property and confidential material; and may resort to siloing and insulating employees to minimize the harm from individual departures. The net result will be worse for these employees.

Empirical evidence suggests an absence of anticompetitive effects from noncompete clauses that bind highly paid workers—or at the very least a mixed bag. The NPRM concedes that one study upon which it relies heavily finds that noncompete clauses increase wages for the impacted workers, physicians.[61] As one of the study's authors testified at the FTC's 2020 workshop on noncompete clauses, the increased wages—which the NPRM cites as a *negative* competitive effect—are the result of an efficient system of referral by doctors within practices, which results in more revenue per hour worked by the impacted physicians.[62] And the study of financial service workers ignored by the NPRM shows that decreased noncompete enforcement had negative impacts on quality of services performed for customers and prices charged to customers.[63]

The NPRM argues that noncompete clauses for highly paid workers "negatively affect new business formation, innovation and the ability of competitors to hire skilled workers" based on the studies referred to above.[64] The NPRM goes even further than the studies to speculate that prohibiting noncompete clauses for highly paid workers "may have relatively greater benefits for consumers than prohibiting non-compete clauses for other workers."[65] As the NPRM reflects, the existing empirical work on highly paid and

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[60] *Id*. at 71-72.

[61] *Id*. at 76 n.248. The physicians in question may be employees, but may also be partners or other types of practice co-owners. *See supra* §§ 1.A, 1.B.

[62] Testimony of Kurt Lavetti, Non-Competes in the Workplace: Examining Antitrust and Consumer Protection Issues 146 (Jan. 9, 2020), available at: https://www.ftc.gov/system/files/documents/public_events/1556256/non-compete-workshop-transcript-full.pdf.

[63] Gurun et al., *supra* n. 47.

[64] NPRM at 123.

[65] *Id*.

highly skilled workers does not suggest a negative impact upon competition, still less the "greater benefits for consumers" that the NPRM imagines.[66] At best, again, it is a mixed bag. And in any event, as the FTC economist wrote, the empirical record is thin generally.[67] The NPRM thus fails to justify a ban on noncompete clauses for highly paid workers.

As an illustrative example, the experience of the private equity industry suggests the absence of negative effects. Our industry is not concentrated—there are more than 5,000 firms (more than the number of publicly traded companies in the US)—and is extremely competitive.[68] The NPRM acknowledges that workers subject to noncompete clauses individually have a marginal effect on competition, stating: "The effect of an individual worker's non-compete clause on competition in a particular labor market may be marginal or may be impossible to discern statistically."[69] Further, in our members' experience, there is steady turnover and worker mobility is not materially hampered by the use of noncompete clauses for this class of workers. Anecdotally, the net impact of noncompete clauses for this class of employee is, at most, to ensure relatively brief "cooling off" periods or buyouts of forfeited equity by new employers as private equity professionals switch firms, which they do regularly.

The NPRM lacks an adequate evidentiary basis to ban noncompete clauses binding highly paid employees, and the experience of the private equity industry is a good example of why there is no sound basis to do so. Should the Commission propose a final rule, noncompete clauses applied to highly paid employees should be excluded from it. While the NPRM includes no research support for a particular income threshold, the Commission can look to the various state law approaches for defining exclusion from the proposed ban, which largely fall under $150,000 in annual income.

D. *De Facto* Noncompete Clauses

The NPRM proposes that certain other provisions may amount to a "*de facto* noncompete clause" and seeks comment as to this proposal. We are concerned that the NPRM's vague description of potential "*de facto* noncompete clauses" brings a significant amount of uncertainty to existing relationships between our members and their own employees and those of the portfolio companies.[70] These types of agreements, including ones endemic to the U.S. economy (and the federal workforce) that effectively encourage employees to stay in their jobs should be excluded from any ban the

[66] *Id*.
[67] McAdams, *supra* n. 43, at 3-4.
[68] *See, e.g.*, Committee on Capital Markets Regulation, *A Competitive Analysis of the U.S. Private Equity Fund Market* (April 2023), found at: https://capmktsreg.org/wp-content/uploads/2023/04/CCMR-Private-Equity-Funds-Competition-Analysis-04.11.20231.pdf.
[69] NPRM at 75.
[70] That uncertainty is a legal problem as well as a business implementation problem, as a rule banning "de facto" noncompete clauses may be constitutionally void for vagueness. *See FCC v. Fox Television Stations, Inc.*, 567 U.S. 239 (2012).

Commission might propose and addressed in individual court proceedings should the need arise.

The lack of clarity surrounding "*de facto* noncompete clauses" compounds a similarly broad and unclear feature in the proposed rule. The proposed rule applies to "a contractual term ... that prevents the worker from ... operating a business."[71] It does not define what "a business" is. One's business might very well be something that a legitimate post-employment restriction might bar. Federal ethics rules bar former government officials operating a business from petitioning their former agency for a time. Non-solicitation rules bar former employees from operating a business they wish to, potentially with the best target clients.

The Section 5 Policy Statement's framework also cannot be applied. As a threshold matter, the lack of clarity in the definition of "*de facto* non-compete clause" will make both business implementation and rule enforcement impossible. For example, if the definition is unclear, then analyzing "facial unfairness" or effects is impossible. Even if one were to limit the scope of a "*de facto* noncompete clause" to the two examples provided (which the NPRM expressly disclaims is the correct interpretation), it is clear that the NPRM lacks sufficient evidence to demonstrate that these terms are globally unfair.

As the NPRM recognizes in defending its proposal of an outright ban on noncompete clauses, there is a cost to uncertainty, including costs associated with litigating both existing employment terms and prospective employment terms designed to account for the NPRM's proposed ban.[72] The NPRM's vague description of its "functional test" makes it difficult for companies to follow the rule and all but ensures a cottage industry of litigation surrounding the proper scope of non-disclosure agreements and other employment terms that could potentially be characterized by creative counsel as having the requisite effect. The NPRM encourages this case-by-case approach to interpreting employment terms. However, the costs associated with such uncertainty and litigation are borne by both firm and employee and could ultimately have a more chilling effect on job mobility (and hiring) than the noncompete clauses the NPRM purports to address.

The NPRM's treatment of *de facto* noncompete clauses also undermines the very alternative the NPRM identifies for firms seeking to protect sensitive company materials and trade secrets. The NPRM relies on non-disclosure agreements as both a "reasonable alternative" to a noncompete clause,[73] and a potential source of uncertainty as to satisfaction of the functional test for *de facto* noncompete clauses.[74] This internal contradiction is untenable for both firms and workers seeking to come to an agreement

[71] *See, e.g.*, NPRM at 106.
[72] *Id*. at 190-91.
[73] *Id*. at 98-99, 109.
[74] *Id*. at 99.

that can be relied upon into the future that protects both parties' interests. To get trade secret protection, a company is obligated to take "reasonable measures" to protect that information.[75] One such measure is a non-disclosure agreement.[76] To the extent such agreements constitute "*de facto* noncompete clauses," the inability to use them strips trade secret protection. The broad category destroys the mechanism touted by the NPRM as an alternative to noncompete clauses.

There is no legal or factual basis supporting the "functional test" set forth in the NPRM or the need for regulation on so-called *de facto* noncompete clauses outside of the existing framework. The NPRM identifies no other jurisdiction or regulatory regime that has purported to regulate employment terms of the nature described in the NPRM as *de facto* noncompete clauses. It cites no empirical work establishing that such *de facto* clauses impede competition or lead to other negative effects that might suggest a failure of competition. As research from the financial services industry reflects, decreased enforcement of noncompete clauses can increase employee misconduct.[77] And were a potential ban to prevent companies from using tools to prevent misconduct, like forfeiture of equity awards under certain conditions, that impact would be materially exacerbated. To the extent that there are situations in which firms purport to enforce overly prohibitive contractual provisions against their workers, the record indicates that courts are well positioned to address the issue on a situational basis, as they do now. The NPRM's "functional test" would not alleviate that practice, and instead, as discussed above, would be likely to increase the need for court evaluation and case-by-case analysis.

Should the Commission put forth a final rule, the definition of noncompete clause in Section 910.1(b) should not include any reference to *de facto* noncompete clauses or the proposed "functional test."

E. Protecting Trade Secrets and Sensitive Company Materials

The NPRM identifies certain alternatives to noncompete clauses as means of protecting company trade secrets and other sensitive materials and "seeks comment on its preliminary finding that employers have reasonable alternatives to noncompete clauses for protecting their investments."[78]

First, in the experience of our members, noncompete clauses are essential to protecting sensitive company information, know-how and trade secrets, permitting firms to better compete. Senior executives and highly paid employees receive substantial confidential and often competitively sensitive information regarding, among other things, strategy and intellectual property, not just of the company they work for, but of that

[75] *See, e.g.*, 18 U.S.C. § 1839(3)(A) (requiring the owner of a trade secret to have "taken reasonable measures to keep such information secret").
[76] *See Altavion, Inc. v. Konica Minolta Sys. Lab'y Inc.*, 226 Cal. App. 4th 26 (2014).
[77] Gurun et al., *supra* n. 47.
[78] NPRM at 101.

company's clients, vendors and other partners. No one disputes that protecting such information is vital to a company's success and competitiveness, but proving that a departed executive misused confidential information to the benefit of a new employer is notoriously difficult.[79] Indeed, tenured employees, beyond just senior executives, may retain opinions, insight and other information that influence their behavior and decision-making after they leave a firm, even where they do not intend to misappropriate confidential information. As the NPRM concedes, protecting against this kind of information sharing by enforcing the "inevitable disclosure doctrine" is not always possible and, in any event, is subject to high evidentiary burdens.[80] (It is also very expensive.) Noncompete clauses therefore often serve as a prophylactic measure, not to punish the executive and prevent him or her from working, but to ensure they cannot take confidential or proprietary information with them to a competitive business until it has become at least somewhat stale. This prophylaxis helps protect competition, in a manner the NPRM also misses. Among the most sensitive information that employees have is pricing information, fund strategy, and terms, the recency of which is a critical facet of its value. Noncompete clauses work to slow—marginally—the exit process. Preventing recent prices from reaching competitors protects competition; it does not hinder it.

Second, the NPRM does not support a contrary conclusion. It acknowledges that "there is little reliable empirical data on trade secret theft and firm investment in trade secrets in general."[81] The NPRM relies on the "considerable" number of lawsuits alleging trade secret misappropriation filed each year as the sole basis for its claim that trade secret law is a "viable means of obtaining redress for trade secret theft."[82] That firms feel compelled to sue is not suggestive that the remedy is adequate—it may indeed suggest that trade secret theft is undeterred. Nor does it suggest that the remedies received in court adequately place the aggrieved party in the position it was before the trade secrets were disclosed. The NPRM does no analysis about the lawsuits to which it refers.

Just looking at the source cited by the NPRM for its figures demonstrates the significant burdens reliance on trade secret lawsuits places on firms. Between the years 2016 and 2020, Lex Machina determined that:

- While courts granted the plaintiff a preliminary injunction in 54% of cases reaching judgment on the merits, plaintiffs ultimately secured permanent injunctions in 74% of the cases, meaning that 20% of plaintiffs failed to

[79] Even where it is possible to demonstrate improper sharing of confidential information, at that point the genie cannot be put back into the bottle and damages often cannot be reasonable calculated. Noncompete clauses seek to prevent the individual subject to it from being in a position where he or she could intentionally or unintentionally disclose confidential information. This is theoretically similar to the FTC's preference for structural remedies in merger cases. Keeping parties apart polices interaction better.

[80] NPRM at 95.

[81] *Id*. at 92.

[82] *Id*. at 97-98. It should be noted that this logic, referring simply to the availability of the courts, simultaneously could be used to support the current regime of enforcement of noncompete clauses to protect sensitive company information.

get timely, preemptive relief from the courts protecting their investments from misappropriation.[83]

- And the delay can be substantial: the median termination of a trade secret case was 8.5 months from the time of filing; the median summary judgment decision was more than 20 months; and the median trial was more than 26 months.[84] These periods are much longer than the typical noncompete clauses in our industry.

- Nearly $1.3 billion in damages were awarded in trade secret cases filed in federal court, including $77 million in prejudgment interest and $95 million in attorneys' fees and costs.[85] In 2020 alone, $591 million in damages were awarded.[86]

The NPRM undertakes no analysis (or even consideration) of the costs and difficulties in policing the use of trade secrets—something the state and federal trade secret laws take into account by adopting a generous three-year statute of limitations, triggered on the discovery of the misappropriation.[87] It ignores entirely the likelihood that a great deal more trade secret and other litigation may attend to weakening noncompete clauses. And while the NPRM claims that there is an expansive definition of trade secrets under existing law, the NPRM does not address protections for sensitive business information that may not fall within the scope of the trade secret laws, like negotiations with vendors.

Third, the NPRM points to different employment terms as potential means of protecting sensitive company information, including non-disclosure agreements, fixed-term employment contracts, and improving pay, benefits, and the general employee experience. The experience of our members is that none of these proposed alternatives is sufficient to satisfactorily protect sensitive company information. Once an employee has joined a competitor, policing the secrecy of trade secrets is nearly impossible, and enforcing rights involves potential litigation taking years and costing millions of dollars. As discussed above, the NPRM has also identified non-disclosure agreements as the type of agreement that could be considered a *de facto* noncompete agreement, which would further undermine a firm's confidence that it would be able to appropriately protect its information through the use of a non-disclosure agreement that could ultimately be invalidated based on an undefined standard.

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[83] Lex Machina, Infographic, *Trade Secret Litigation Report 2021*, https://lexmachina.com/resources/infographic-trade-secret-report/.
[84] *Id.*
[85] *Id.*
[86] *Id.*
[87] Uniform Trade Secrets Act With 1985 Amendments (Feb. 11, 1986); Defend Trade Secrets Act of 2016, Pub. L. No. 114-153, 130 Stat. 376 (May 11, 2016).

Fixed-term employment contracts, while useful in certain limited circumstances, require significant amounts of administration and upkeep and inject uncertainty on both firms and workers. A fixed-term employment contract alone does not suffice to protect the disclosure and use of sensitive company information. As noted above, the less able a company is to protect its sensitive information and trade secrets, the less likely it is to make people privy to this information, thus decreasing efficiency. The NPRM does not consider these elements of a fixed-term employment relationship in making its reasonableness finding.

The NPRM's assertion that firms "that wish to retain their workers can also pay the worker more, offer them better hours or better working conditions, or otherwise improve the conditions of their employment" fails to contend with practical realities and implicitly acknowledges that, in a world without noncompete clauses, a company's confidential information may routinely be auctioned off to the highest bidder.[88] As a threshold matter, our members pay their employees well, and offer substantial benefits. And our industry has a great deal of mobility. But there is still a need to protect sensitive company information on departure and negotiations about leaving (which noncompete clauses encourage) most efficiently resolve these issues. Noncompete clauses are not used to retain employees, but rather to protect investors and the value of the companies in which they invest; and that in turn benefits the employees of the company.

This collection of employment terms simply does not provide a reasonable alternative to the use of noncompete clauses. And in our member's experience, trade secret law is, standing alone, inadequate to protect the legitimate interests that firms have preventing trade secret theft.

2. Existing Noncompete Obligations

The NPRM purports to apply the proposed ban on noncompete clauses both prospectively and retroactively. Putting aside the substantive legal concerns, both constitutional and statutory, about the scope of the NPRM and the proposed ban, the retroactive application of the proposed ban would upend untold numbers of employment and other agreements between firms and employees, partners, shareholders, and others, as well as other contractual obligations based on the existence and validity of those agreements. It would create an unfairness, rewarding employees with expensive equity and compensation without consideration, and increasing ownership stakes in competitors (a traditional concern of antitrust). While the NPRM assesses the purportedly pro-competitive effects of the retroactive applicability of the proposed ban, the NPRM fails to assess the follow-on results of striking discrete portions of such a large number of agreements without an automatic or default mechanism in place to address the legitimate

[88] NPRM at 100.

concerns for sensitive business information, trade secrets and firm investment recognized as interests protected via existing noncompete clauses.

The discussion in the NPRM of the cost of rescinding existing noncompete clauses misses the mark. This is not simply a question of tearing up sheets of paper or drawing lines through text. The noncompete clauses in our industry are part of broader contracts, often tied to other things (like equity grants). Rescinding them, especially in the tens of millions of instances estimated by the NPRM, will involve difficult questions of contractual severability. If a rule is applied to ban existing noncompete clauses, those questions must be answered for each contract under varying state contract laws. The answers will vary, widely. The effect will, too. Former employees who get to keep equity or cash or health insurance will face questions about unjust enrichment, and possibly other legal claims. Will someone who forfeited equity as a result of joining a competitor now get that equity back? Will former senior executives getting compensated by their new employers for their noncompete clauses get paid twice? All these questions will need to be answered through time-consuming, distracting, and expensive negotiation, or even litigation. That will cost a great deal more than the NPRM supposes.

As such, should the Commission put forth a final rule, the proposed ban on noncompete clauses should be exclusively applied prospectively to agreements concluded after the effective date.

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The AIC appreciates the opportunity to comment on the NPRM and would be pleased to answer any questions that you might have concerning our comments.

Respectfully submitted,

//s// Rebekah Goshorn Jurata

Rebekah Goshorn Jurata
General Counsel
American Investment Council