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VIA EMAIL

To Our Investment Adviser Clients and Other Friends:

Re: Federal Trade Commission ("**FTC**") Ban on Non-Compete Clauses

On April 23, 2024, the FTC issued a final rule (the "**Final Rule**") broadly banning post-employment non-competition clauses between employers and their workers. The Final Rule becomes effective on September 4, 2024 (the "**Effective Date**") and applies to all investment advisers.

The Final Rule: (1) bans entering into new non-compete agreements with workers after the Effective Date; (2) renders unenforceable all existing non-compete agreements with workers, except for restrictions in agreements with certain senior executives (employees with over $151,164 annual compensation and who are in policy-making positions); and (3) requires employers to notify, in an individualized, written communication, affected workers of the unenforceability of existing non-compete agreements. The Final Rule defines a prohibited "non-compete" clause as any contract term, workplace policy, or term or condition of employment that prohibits a worker from, penalizes a worker for or functions to prevent a worker from seeking work, accepting work or operating a business after the conclusion of the engagement that was subject to the term or condition. Workers covered under the Final Rule include employees, independent contractors, externs, interns, volunteers, apprentices or sole proprietors who provide a service to a client or a customer.

There are certain limited exceptions to the Final Rule, including non-competes entered into by a person pursuant to a bona fide sale of a business entity, of a person's ownership interest in a business entity or of all or substantially all of a business entity's operating assets. The non-compete clauses allowed by this bona fide sale exception will be governed by state law.

While the Final Rule does not explicitly ban non-disclosure agreements or non-solicitation agreements, it does ban restrictive covenants when they are overbroad and have the same anti-competitive functional effects as a non-compete clause. As a result, agreements can still use trade secrets law and non-disclosure clauses to protect confidential information, but care should be taken to properly define the scope of what information is protected.

There are a few pending lawsuits attempting to vacate the Final Rule, but it is unclear if any will be successful prior to the Effective Date. The U.S. District Court for the Northern District of Texas has indicated that the FTC likely exceeded its statutory authority and may vacate the Final Rule shortly before the Effective Date. However, a federal court in the Eastern District of Pennsylvania is inclined to hold the opposite, that the FTC did not exceed its authority. To date, no litigation has resulted in a nationwide injunction delaying compliance with the Final Rule, and any ruling that vacates the Final Rule will likely be appealed. In the absence of a court order vacating the Final Rule

or a nationwide injunction to stay the Effective Date, employers should prepare to comply with the ban by the Effective Date.

Compliance with the Final Rule includes: (1) identifying any non-compete clauses or overbroad restrictive covenants in contracts with workers; (2) providing the required notices to workers with prohibited non-compete clauses prior to the Effective Date; and (3) updating all applicable form agreements to remove any post-engagement non-compete clause and any other confidentiality clauses that may be overbroad or anti-competitive.

Even if the Final Rule is vacated, employers should update their agreements for this issue because certain states have also adopted bans on non-compete agreements (including California, Minnesota, North Dakota and Oklahoma), and many other states have introduced legal restrictions on non-compete agreements. Similar to the FTC's Final Rule, California has a non-compete ban that invalidates overly broad non-disclosure restrictions if the confidential information protected is so broadly defined that the agreement is anti-competitive. Investment advisers with employees in California or non-disclosure agreements with counterparties in California should review and update their form agreements regardless of the outcome of pending litigation on the FTC's Final Rule.

If you have any questions regarding compliance with the FTC non-compete ban or state non-compete restrictions, please contact one of the Shartsis Friese attorneys in the Investment Funds & Advisers Group.

Previous letters to our investment advisory clients and friends and discussions of other topics relevant to private fund managers, investment advisers and private investment funds can be found at our insights page: www.sflaw.com/blog/investment-funds-advisers-insights.

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