Docket No. FTC-2023-0007

COMMENT

of

WASHINGTON LEGAL FOUNDATION

to the

FEDERAL TRADE COMMISION

Concerning

NON-COMPETE CLAUSE RULE

IN RESPONSE TO THE PUBLIC NOTICE PUBLISHED AT 88 FED. REG. 3,482 (JAN. 19, 2022)

John M. Masslon II
Cory L. Andrews
WASHINGTON LEGAL FOUNDATION
2009 Massachusetts Ave., NW
Washington, DC 20036
(202) 588-0302

March 17, 2023

WASHINGTON LEGAL FOUNDATION
2009 Massachusetts Avenue, NW
Washington, DC 20036
(202) 588-0302

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Submitted Electronically (http://www.regulations.gov)
Honorable Lina M. Khan
c/o Office of the Secretary
Federal Trade Commission
600 Pennsylvania Avenue Northwest, Suite CC-5610
Washington, District of Columbia 20580

Re: Non-Compete Clause Rule, Docket No. FTC-2023-0007

Chairman Khan:

On behalf of Washington Legal Foundation, please consider this comment responding to the invitation for comments at 88 Fed. Reg. 3,482 (Jan. 19. 2023). WLF appreciates the opportunity to weigh in on whether the Federal Trade Commission should ban almost all noncompete clauses nationwide. As explained below, banning noncompete agreements violates the fundamental right to contract, exceeds the FTC's statutory authority, and will stop workers from living the American dream. The FTC should thus withdraw the Proposed Rule.

I. Interests of WLF

WLF is a nonprofit, public-interest law firm and policy center based in Washington, DC, with supporters nationwide. WLF devotes much of its resources to defending free enterprise, individual rights, limited government, and the rule of law. To that end, WLF often submits comments to the FTC about proposed rulemaking. *See, e.g.*, WLF Comment, *In re Draft FTC Strategic Plan for FY2022-2026* (Nov. 29, 2021); WLF Comment, *In re Rescission of 2015 FTC Statement on Unfair Methods of Competition* (July 1, 2021); WLF Comment, *In re FTC Investigation of Artificial Intelligence* (Nov. 14, 2018).

WLF's Legal Studies Division, its publishing arm, often produces and distributes articles on a wide array of legal issues related to the FTC's recent illegal power grabs. *See, e.g.,* Erik W. Weibust et al., *After 200+ Years Under State Law FTC Proposes to Sweep Away All Noncompetes in Unauthorized*

Federal Power Grab, WLF Legal Backgrounder (Jan. 11, 2023); Steven Cernak, *FTC's Challenge to Altria-JUUL Transaction: Antitrust and Constitutional Issues Hiding in Plain Sight*, WLF Legal Backgrounder (Sept. 7, 2022).

II. The Proposed Rule Violates The Fundamental Right to Contract.

Modern contract law "arose in both England and America as a reaction to and criticism of the medieval tradition of substantive justice." Morton J. Horowitz, *The Historical Foundations of Modern Contract Law*, 87 Harv. L. Rev. 917, 917 (1974). It rejects the medieval notion that "the justification of contractual obligation is derived from the inherent justice or fairness of an exchange." *Id.* Instead, "the source of the obligation of contract is the convergence of the wills of the contracting parties." *Id.* Contracts thus let people "order their personal and business affairs according to their particular needs and interests. Once arranged, those rights and obligations are binding under the law, and the parties [can] rely on them." *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234, 245 (1978).

While the feudal system fixed parties' rights and duties based on their status at birth, modern contract law presumes that individuals are mostly free and equal. The industrial revolution saw "a movement from Status to Contract." Henry Maine, *Ancient Law: Its Connections with the Early History of Society and Its Relation to Modern Ideas* 101 (J.J. Morgan ed., J.M. Dent & Sons Ltd. 1917) (1861). By enabling private parties to negotiate agreements that benefit all parties, contracts "made the modern world possible." Edward Peter Stringham, *How Private Governance Made the Modern World Possible* (Oct. 5, 2015), https://perma.cc/2AZN-JCAP. In other words, "Contract law does not require parties to behave altruistically toward each other; it does not proceed on the philosophy that I am my brother's keeper." *Original Great Am. Choc. Chip Cookie Co. v. River Valley Cookies Ltd.*, 970 F.2d 273, 280 (7th Cir. 1992). Rather, it simply requires parties to uphold their end of the contractual bargain.

The American experiment relied on freedom of contract as the "legal underpinning of a dynamic and expanding free enterprise system." E. Allan Farnsworth, *Contracts* § 1.7 (4th ed. 2004). Legal historians have declared the country's early years to be "above all else, the years of contract." *Id.* (citation omitted). Those who gathered in Philadelphia in the Summer of 1787 were concerned about laws that relieved parties of their contractual obligations. So they included the Contracts Clause, which prohibits any State from "impairing the Obligation of Contracts." U.S. Const. art. I, § 10 cl. 1. The Constitution does

not hold citizens to a standard that the Framers were unwilling to abide by themselves. That is why the Constitution preserved "[a]ll debts contracted and engagements entered into, before the adoption of th[e] Constitution." *Id.* art. VI, § 1.

These constitutional provisions show that the founding generation believed that a party's right to enforce a valid contract was sacrosanct. "They took the view that treating existing contracts as 'inviolable' would benefit society by ensuring that all persons could count on the ability to enforce promises lawfully made to them—even if they or their agreements later prove unpopular with some passing majority." *Sveen v. Melin*, 138 S. Ct. 1815, 1827 (2018) (Gorsuch, J., dissenting) (citation omitted). As Madison observed, "impairing the obligation of contracts" is "contrary to the first principles of the social compact, and to every principle of sound legislation." The Federalist No. 44, 282 (James Madison) Clinton Rossiter ed. 1961). Freedom of contract is the general rule; "restraint the exception." *Charles Wolff Packing Co. v. Ct. of Indus. Rels. of State of Kansas*, 262 U.S. 522, 534 (1923).

True, the Contracts Clause does not apply to the Federal Government. *Peick v. Pension Benefit Guar. Corp.*, 724 F.2d 1247, 1253 (7th Cir. 1983); *see also* Erwin Chemerinsky, *Constitutional Law* 629 (3d ed. 2006). But that does not mean that the FTC should ignore the fundamental right to contract when deciding whether to ban most noncompetes nationwide. There are things the government may legally do that still violate individuals' fundamental rights. For example, eminent domain used for private development is legal after *Kelo v. City of New London*, 545 US 469 (2005). Yet it does not comply with fundamental principles of justice.

The same is true with impairing the rights of individuals and companies to voluntarily enter into noncompete agreements. The ability to contract is a fundamental right. *Jones v. Alfred H. Mayer Co.*, 392 U.S. 409, 432 (1968); *Erotic Serv. Provider Legal Educ. & Rsch. Project v. Gascon*, 880 F.3d 450, 459 (9th Cir. 2018); *United States v. Alabama*, 691 F.3d 1269, 1293 (11th Cir. 2012). The lack of a Contracts Clause violation does not mean that it is a good idea to violate the fundamental right to contract. Yet that is what the Proposed Rule does. This is reason enough to withdraw the Proposed Rule.

III. The Major-Questions Doctrine Deprives The FTC Of The Authority To Promulgate The Proposed Rule.

A. Only Congress May Resolve Major Questions.

Under the major-questions doctrine, the Court "presume[s] that 'Congress intends to make major policy decisions itself, not leave those decision to agencies.'" *West Virginia v. EPA*, 142 S. Ct. 2587, 2609 (2022) (quoting *U.S. Telecom Ass'n v. FCC*, 855 F.3d 381, 422-23 (D.C. Cir. 2019) (Kavanaugh, J., dissenting from denial of rehearing en banc))). This is especially true when, as here, an agency asserts regulatory authority "beyond what Congress could reasonably be understood to have granted." *Id.* Such "grants of regulatory authority are rarely accomplished through 'modest words,' 'vague terms,' or 'subtle device[s].'" *Id.* (quoting *Whitman v. Am. Trucking Ass'n*, 531 U.S. 457, 468 (2001)).

Even when a statutory gap exists, an agency may fill that gap only when the "statutory circumstances" show that Congress intended to grant it gap-filling power. *United States v. Mead Corp.*, 533 U.S. 218, 229 (2001). Even if Congress gives an agency power to issue rules or adjudicate disputes, that does not—standing alone—show that Congress "delegate[d] its authority to settle or amend major social and economic policy decisions." William N. Eskridge Jr., *Interpreting Law: A Primer on How to Read Statutes and the Constitution* 288 (2016). Rather, Congress itself is "more likely to have focused upon, and answered, major questions." Stephen Breyer, *Judicial Review of Questions of Law and Policy*, 38 Admin. L. Rev. 363, 370 (1986). That is why the Supreme Court "expect[s] Congress to speak clearly if it wishes to assign to an agency decisions of vast 'economic and political significance.'" *Util. Air Regul. Grp. v. EPA*, 573 U.S. 302, 324 (2014) (quoting *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 160 (2000)).

The major-questions doctrine is based on "the strong presumption of continuity for major policies unless and until Congress has deliberated about and enacted a change in those major policies." Eskridge at 289. "Because a major policy change should be made by the most democratically accountable process—Article I, Section 7 legislation—this kind of continuity is consistent with democratic values." *Id.*

The Supreme Court has stepped up its enforcement of the major-questions doctrine. Most recently, in *West Virginia*, the Court rejected the Environmental Protection Agency's argument that it could essentially implement a cap-and-trade system for carbon emissions. As the Court

explained, it was "not plausible that Congress gave EPA authority to adopt on its own such a regulatory scheme." *West Virginia*, 142 S. Ct. at 2616. Such a major question "rests with Congress itself, or an agency acting pursuant to a clear delegation from that representative body." *Id.*

In holding that the cap-and-trade system exceeded EPA's authority, the Court emphasized that questions about "basic and consequential tradeoffs . . . are ones that Congress would likely have intended for itself." *West Virginia*, 142 S. Ct. at 2613. As discussed in § III.C, *infra*, banning noncompete agreements is also a major question. Thus, the FTC lacks authority to regulate noncompete agreements.

West Virginia just continued the Supreme Court's trend of rejecting administrative agencies' attempts at exceeding the power Congress gave them. Earlier in the term, the CDC argued that it had "broad authority to take whatever measures it deems necessary to control the spread of COVID-19, including issuing" an eviction moratorium. *Ala. Ass'n of Realtors v. Dep't of Health & Hum. Servs.*, 141 S. Ct. 2485, 2488 (2021) (per curiam). In rejecting the CDC's argument, the Court focused on the fact that the CDC's order affected between six and seventeen million people. *Id.* at 2489. This amounted to an economic impact of around $50 billion. *See id.* (citation omitted). This, the Court said, was the type of economic regulation that the major-questions doctrine prevents agencies from promulgating absent a clear statement from Congress.

Another in the line of cases rejecting agencies' exercise of non-delegated power was *NFIB v. OSHA*, 142 S. Ct. 661 (2022) (per curiam). Nearly the entire opinion focused on whether the statute included the clear-statement that the major-questions doctrine requires. There was very little focus on whether OSHA's vaccine mandate was a major question. Only one paragraph discussed that issue and easily concluded that the "significant encroachment into the lives—and health—of a vast number of employees" was a major question. *Id.* at 665.

B. There Is No Clear Statement Giving The FTC Power To Ban Noncompete Agreements.

Examining whether the FTC has express statutory authority to regulate noncompete agreements is trivial. The FTC relies on Section 5 of the Federal Trade Commission Act to support the Proposed Rule. 88 Fed. Reg. at 3,482. That statute bans "[u]nfair methods of competition." 15 U.S.C. § 45(a)(1). Nothing in the Federal Trade Commission Act suggests that the FTC's power

to ban unfair methods of competition includes the power to ban noncompete agreements. Section 6(g) of the Federal Trade Commission Act, which the FTC also cites to support the Proposed Rule, only allows the FTC to issue regulations. *See* 15 U.S.C. § 46(g).

The power to issue regulations to carry out an agency's mission does not give it unlimited power. That is shown by *West Virginia*, *Alabama Association of Realtors*, and *NFIB*. That the EPA, the CDC, and OSHA all have authority to issue regulations to carry out their mission is a given. Yet the Supreme Court found in each case that these general grants of authority did not permit them to regulate major questions because there was no clear statement from Congress that they could do so. The same is true here. Section 6(g) of the Federal Trade Commission Act is the furthest thing from a clear statement by Congress giving the FTC power to regulate noncompete agreements.

Nor do other statutes come close to making a clear statement that Congress meant to give such broad power to the FTC. So if the Proposed Rule is a major question, then the major-questions doctrine means that the FTC lacks the authority to promulgate the Proposed Rule.

C. Banning Noncompete Agreements Is A Major Question.

Because Congress has not made a clear statement that the FTC can bar noncompetes, the inquiry must focus on whether banning noncompete agreements nationwide is a major question. At bottom, the major-questions doctrine "supports a presumption of *non*delegation in the face of statutory ambiguity over major policy questions or questions of major political or economic significance." Abbe R. Gluck & Lisa Schultz Bressman, *Statutory Interpretation from the Inside—An Empirical Study of Congressional Drafting, Delegation, and the Canons: Part 1,* 65 Stan. L. Rev. 901, 1003 (2013). Whether noncompete agreements should be banned is surely a "major question."

The Proposed Rule "estimates that [it will affect] approximately one in five American workers—or approximately 30 million workers." 88 Fed. Reg. at 3,485 (citing Natarajan Balasubramanian et al., *Bundling Employment Restrictions and Value Appropriation from Employees*, 35 (2022), https://tinyurl.com/3jjtxf4h). As discussed above, just two years ago the Supreme Court held that a rule affecting, at most, sixteen million Americans was a major question reserved for Congress. *Ala. Ass'n of Realtors*, 141 S. Ct. at 2489. The number of people affected by the Proposed Rule is double the number that were affected by the CDC's eviction moratorium. Try as it might, the FTC cannot escape the reality that, under *Alabama Association of Realtors*,

the Proposed Rule is a major question reserved for Congress—not unelected bureaucrats. Thus, the FTC should withdraw the Proposed Rule because it lacks statutory authority to promulgate it.

IV. The Distributional Analysis Is Deeply Flawed, And The Proposed Rule Will Stop Upward Mobility For Low-Skill And Low-Income Workers.

Even if the FTC could issue the Proposed Rule, it should not do so because it is bad policy. Other commentors focus on the harm to national security and business interests. So this comment focuses on the harm that the Proposed Rule will do to workers—the group that the FTC claims that the Proposed Rule will help.

The FTC appears to believe that the Proposed Rule is beneficial because it "would close racial and gender wage gaps." *See* 88 Fed. Reg. at 3,488. This argument fails for at least two reasons.

First, the premise that closing the racial and gender pay gaps benefits women and non-white workers is factually wrong. An example shows the absurdity of the FTC's argument. Assume that workers and companies currently share $2 trillion—each receiving $1 trillion. But assume that after the Proposed Rule, the parties share only $1.5 trillion—the companies receiving $600 billion and workers receiving $900 billion.

This assumption of an overall reduction in output is reasonable. Despite the Proposed Rule's protestations to the contrary, it will lead to a 32% decrease in capital investment. *See* Jessica Jeffers, *The Impact of Restricting Labor Mobility on Corporate Investment and Entrepreneurship*, 28 (2019), https://tinyurl.com/ bddvrkw3. Private capital investment drives economic growth. *See* U.S. Bureau of Economic Analysis, *NIPA Handbook: Concepts and Methods of the U.S. National Income and Product Accounts*, 6-1 (Dec. 2022). If capital investment decreases, real growth also decreases.

The hypothetical may see the wage gap close as white male workers' pay decreases more than women and non-white workers. But no sane person would say that this "helps" women and racial minorities. Workers would see a 10% decrease in combined salaries and benefits. Yet the Proposed Rule argues that it may still be appropriate because of this distributional change. This understanding of distributional consequences turns cost-benefit analysis on its head. At a minimum, the FTC should start anew and properly consider the costs and benefits of the Proposed Rule viewed through the correct lens.

Second, the Proposed Rule's distributional analysis ignores the evidence showing that banning noncompete agreements will harm those lowest on the socio-economic ladder. As the Proposed Rule must admit, "non-compete clauses increase employee training and other forms of investment." 88 Fed. Reg. at 3,493. Banning noncompete agreements would decrease employee training by at least 14.7%. *See id.* (citing Evan Starr, *Consider This: Training, Wages, and the Enforceability of Non-Compete Clauses*, 72 I.L.R. Rev. 783, 796-97 (2019)). The "changes in training are primarily due to changes in firm-sponsored, rather than employee-sponsored, training." *Id.* (citing Starr, 72 I.L.R. Rev. at 797).

These empirical results track economic theory. *See* 88 Fed. Reg. at 3,493. Firms have incentive to invest in their workers when they know that those workers will be there for a long time. For example, firms may pay $10,000 to train individuals on how to use equipment because they know that if the employees stay for some time that they will make a profit from that training. What firms do not want is to spend $10,000 training an employee only to see that employee leave a week later for a competitor across town. This is why people must commit to five years of active duty and three years of reserve duty after attending a military academy. *See* 10 U.S.C. §§ 651, 7448, 8459, 9448. Uncle Sam doesn't want to train soldiers only to see them take the skills they learn to private industry a few months after graduation.

The Proposed Rule, however, would bar companies from using noncompete agreements to stop that from happening. Companies would thus have no incentive to train their own employees. Why pay $10,000 to train someone if you can offer someone working for your rival $1,000 more than they currently make if the competitor provided the training? You don't. As every firm has this same incentive, the result is training across the board plummets. This, of course, means that the employees don't receive the $10,000 in training.

True, doctors, lawyers, and other wealthy individuals are not harmed as much by the decrease in employer-sponsored investment. These professionals have received substantial schooling that provided most of the training necessary to make a living. But even if there is additional training needed to advance in one's career, richer Americans can afford to pay for that training out of pocket. For example, a lawyer can pay to attend a law and economics seminar at the Antonin Scalia Law School. (The current FTC commissioners may want to do so themselves.)

Low-wage employees, however, typically lack advanced schooling. They rely on training from their employers. With this training, low-skilled workers gain valuable skills that help to propel them up the socio-economic ladder. For example, when she was eighteen years old, Mary Barra started out on the assembly line at General Motors. Because GM provided her with significant training opportunities, she was able to climb the ladder and now serves as GM's chief executive officer. *See* Frank Olito, *10 CEOs that started in entry-level positions at the companies they now lead*, Business Insider (Aug. 2, 2019), https://tinyurl.com/5ya2efwv.

This upward mobility will disappear under the Proposed Rule. Low-wage employees lack the resources to pay for their own training. They also lack formal schooling. What they receive now, however, is training from their employers. This training is critical to these workers' living the American dream and advancing in their careers. But there will be no incentive for employers to provide this training if the Proposed Rule takes effect. Rather, the incentive will be not to provide worker training and poach from companies that provide training. Soon, there is a race to the bottom and no firm is providing the training necessary to help low-wage workers advance in their careers. So even if the FTC had the authority to promulgate the Proposed Rule, doing so would hurt the most vulnerable in our society. Besides violating the law, then, the Proposed Rule is bad policy.

* * *

The Proposed Rule tramples on Americans' fundamental right to contract. In doing so, it ignores both the Constitution and myriad federal statutes. The Proposed Rule will make labor attorneys rich and force the FTC to expend taxpayer dollars defending an illegal rule. But even if it were legally sound, it is not good policy. Companies will no longer have the incentive to provide on-the-job training to Americans who rely on that training to achieve the American dream. The FTC should realize the errors of its way and withdraw the Proposed Rule.

Respectfully submitted,

John M. Masslon II
SENIOR LITIGATION COUNSEL

Cory L. Andrews
GENERAL COUNSEL & VICE
PRESIDENT OF LITIGATION