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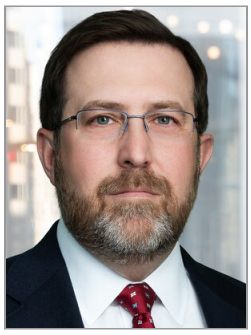
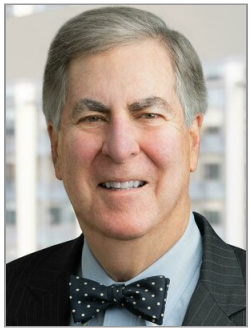
Noncompete Report Misinterpreted Critique Of FTC Proposal

By **Erik Weibust and Stuart Gerson** (January 8, 2024, 2:28 PM EST)



Erik Weibust



Stuart Gerson

In October 2023, Evan Starr, a labor economist and professor at the Robert H. Smith School of Business at the University of Maryland,[1] published a report on behalf of the Economic Innovation Group.

The report is titled "Noncompete Clauses: A Policymaker's Guide through the Key Questions and Evidence,"[2] and in it Starr refers to and critiques our January 2023 Law360 **guest article**, titled "FTC's Noncompete Proposal Is Based On Misrepresentations."

In our experience, Starr is very thoughtful, honest and open-minded, and has no preconceived notions about noncompetes. Nevertheless, we take issue with a few of Starr's critiques of our article and its basic thrust, which we will address here in a friendly effort to continue the important debate over the use and enforcement of noncompetes.

In our article we discussed the Federal Trade Commission's various purported bases for its **proposed rule** that would ban noncompetes nationwide, specifically its claims that:

1. "Noncompetes are regularly enforced against low-wage workers, such as fast-food workers, arborists and manual laborers";

2. "Noncompete clauses systemically drive down wages, even for workers who aren't bound by one";

3. "Noncompete clauses tend to make markets less competitive" and "reduce entrepreneurship and start-up formation"; and

4. "Noncompetes lead to higher prices for consumers by reducing competition."[3]

Starr's critique of our commentary focuses on claims 1 and 4, in particular.

Early in his report, Starr says, "Weibust and Gerson (2023) argue that because noncompetes are required to be narrowly tailored to be enforceable and because they must protect ... legitimate business interests (e.g., trade secrets), the use of noncompetes among low-wage workers or workers without any business justification are outliers."

We are in good company, as Starr's report goes on to cite former FTC Commissioner Christine Wilson for the same proposition.[4] He then concludes: "A growing body of empirical evidence suggests that we should be skeptical that status quo state enforcement policies sufficiently address the potential harms of noncompetes, or that noncompetes are associated with the many benefits that advocates suggest." He later refers to such advocates as "pro-noncompete advocates."

Starr's report gets a few things wrong here.

First, to imply that we are pro-noncompete advocates misconstrues our article and our stated views. To be clear, we are agnostic as to whether noncompetes should be enforceable; the fact is, they are in most states, and have been for generations.

Although we believe that noncompetes can be a valuable tool when used appropriately to protect a company's legitimate business interests, we would still have plenty of work to do if they were banned

nationally. We have stated this publicly many times. Indeed, we made this clear in our article.[5]

In other words, we simply suggested that the FTC should be truthful and transparent with the American public when attempting to promulgate a rule to alter a substantial part of the U.S. economy and upend hundreds of years of state law — especially when employing questionable, recently claimed powers that have never before been used in this manner.

Which brings us to the second mistake in Starr's critique of our article. He misinterprets what we wrote concerning the use and enforcement of noncompetes with low-wage workers, insinuating that we overstated the benefits and downplayed the potential harms of noncompetes. We did not do so.

Indeed, we believe that protections for low-wage workers are appropriate. We simply wrote that there is no conclusive evidence that the use of noncompetes with low-wage workers is the norm.[6]

Starr's own report demonstrates this point. He provides examples of a "temporarily employed Amazon packer making $13," a "volunteer at a non-profit that focuses on exercise among young girls," and "firms who are unwilling to hire a junior worker, even when they know the noncompete is likely unenforceable." Later he points to unpaid interns and janitors who are required to sign noncompetes. These are anecdotes. And Starr's report cites media stories to support these anecdotes.

Although Starr's report goes on to say that "[s]urveys of workers and firms suggest that these stories are not anomalies," there can be no dispute that a suggestion is not conclusive evidence. This is especially true when the surveys that suggest these stories are not anomalies are very limited in scope, rely largely on self-reporting prone to errors, and have other admitted shortcomings.

For example, those surveyed may confuse noncompetes with other forms of restrictions, including nondisclosure and nonsolicitation covenants, claiming to be bound by noncompetes when they, in fact, are not. Similarly, the surveys do not isolate noncompetes from these other types of restrictions. Indeed, Starr, himself, has previously recognized this.[7]

To be clear, we did not argue in our article, and have not argued elsewhere, that there is conclusive evidence that noncompetes are never or even infrequently abused. We simply do not have the evidence of how widespread they actually are beyond the headlines. Nor have we argued that noncompetes benefit all workers. That is clearly not the case.

Perhaps our statement, "Indeed, they are not [the norm]" went too far, in that it could arguably be interpreted to mean that there are conclusive studies to this effect — although that was not our intent.

What we intended to get across was that — in our experience and that of many of the leading noncompete lawyers in the country who we know well — while noncompete abuse certainly occurs, cases where noncompetes are used with warehouse workers, volunteers, janitors, unpaid interns and other low-wage workers are outliers, not the norm.[8]

Is this anecdotal as well? It sure is, but if anyone were to encounter these abuses on a regular basis in the real world, it would be the attorneys advising employers on the use and enforcement of noncompetes, helping employers and employees navigate these issues when hiring from or joining a competitor, and litigating these types of cases nationwide.

In any event, our purpose was simply to point out that there is likewise no conclusive evidence that noncompetes are regularly abused or are harmful to most employees, which is what the FTC strongly implies, if not outright asserts, in support of its proposed rule. It was this lack of transparency, and the FTC's implication that there are conclusive studies to this effect, that we took issue with.

There is simply not conclusive evidence in either direction, so the FTC should not suggest otherwise to advance a political agenda. As Commissioner Wilson accurately pointed out in her dissent to the proposed rule, "the current record shows that studies in this area are scant, contain mixed results, and provide insufficient support for the scope of the proposed rule."[9]

This brings us to Starr's next critique of our article: that our interpretation of the studies referenced

in the FTC's rule — in particular one that he authored — are incorrect and "confus[e] correlation for causation."[10] But that assigns a conclusion to our statements that we did not reach.

Specifically, citing Starr's 2020 study, we wrote: "There are, in fact, reputable studies showing exactly the opposite of what the FTC claims — i.e., that workers who are presented with noncompetes before accepting job offers receive higher wages and more training, and are more satisfied in their jobs than those who are not bound by noncompetes."

Nowhere do we conclude, or even suggest, that the noncompetes caused the higher wages, additional training or increased satisfaction. We merely commented on the fact that Starr's study correlates the two. Perhaps he does not want his study being used to make this point, but what we wrote is exactly what Starr found in his 2020 study.[11]

We are not labor economists or social scientists, and have never claimed to be. Nevertheless, while Starr 's report claims that our reference to his study "confus[es] correlation with causation," virtually all the surveys and studies in this space look at correlation, not causation.

This is true whether it is Starr's survey that suggests workers who are presented with noncompetes before accepting job offers typically receive higher wages, more training, greater access to information, and are more satisfied in their jobs; or others that show certain types of workers including physicians, financial advisers and executives benefit from noncompetes irrespective of when they are notified.[12]

Or still, it could be other surveys, like those cited by the FTC, that purport to show detrimental effects on workers. That was precisely our point: There is no conclusive evidence either way, in part because virtually all the studies are merely correlational.

There is only so much that can be gleaned from these studies and surveys, however thoughtful, thorough and well-intentioned they might be, and the FTC's cherry-picking of some studies and surveys to support its policy goals as though they show causation and are "conclusive evidence" is misleading and misrepresents the state of the literature as we understand it.

Finally, Starr's report cites our article in support of his statement that "[s]everal commentators have argued that if noncompetes are banned then prices will rise for consumers; some rely on the assumption that if wages rise then firms will pass on the wage increases to consumers." That is a fair characterization of what we wrote, and we stand by it.[13]

Starr's report suggests we are incorrect, and that our "concerns that wage increases that result from allowing workers to move across firms would translate into price increases are likely misplaced," because the enforcement of noncompetes leads to "less innovation and lower quality innovation," increased concentration resulting, in part, from "reduc[ed] new firm formation" and in part by increased M&A activity, which in turn can all lead to higher prices.

Again, the findings Starr's report cites are from surveys and studies like those discussed above, and the conclusion downplays what businesses actually do in the real world.

Indeed, we are seeing this before our very eyes right now, where the higher costs of inputs, at least in part, are leading to the increased cost of goods and services.[14] Wages are such an input. One does not need studies to confirm that companies engage in this rational business behavior. Nevertheless, there are myriad studies demonstrating that wage increases are passed along to customers through price increases.[15]

In sum, we stand squarely behind our article and our conclusions that:

- "The FTC made numerous misrepresentations about the use and effects of noncompetes, presumably for purposes of garnering public support for a move of the sort that no state

legislature [other than Minnesota in the summer of 2023, after publication of our article], has taken since the 1800s, despite repeated attempts over the years by opponents of noncompetes in some of the most employee-friendly states and cities in the country,"[16] and

- "The lack of conclusive evidence that [banning noncompetes] is warranted would render any such action arbitrary and capricious, and otherwise unlawful."

Only time will tell if the U.S. Supreme Court agrees with us, of course, but we are confident our view is the correct one.

We thank Starr for citing our work in his report and look forward to continuing this important conversation with him.

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[1] https://www.rhsmith.umd.edu/directory/evan-starr.

[2] https://eig.org/wp-content/uploads/2023/10/Noncompete-Clauses-A-Policymakers-Guide.pdf. EIG describes itself as "a bipartisan public policy organization dedicated to forging a more dynamic and inclusive American economy" that "produces nationally-recognized research and works with policymakers to develop ideas that empower workers, entrepreneurs, and communities." https://eig.org/about-us/.

[3] We have also written about the subjects at the following links: https://www.law360.com/articles/1511340/ftc-authority-to-ban-noncompetes-shaky-after-epa-ruling; https://www.wlf.org/2023/01/11/publishing/after-200-years-under-state-law-ftc-proposes-to-sweep-away-all-noncompetes-in-unauthorized-federal-power-grab/; https://www.tradesecretsandemployeemobility.com/ftc-signals-new-action-on-noncompetes-but-is-that-the-will-of-the-people.

We also discussed it at length during an episode of Spilling Secrets, Epstein Becker & Green, P.C.'s monthly podcast on all things trade secrets and noncompetes, available here: https://www.tradesecretsandemployeemobility.com/spilling-secrets-podcast-ftc-proposes-ban-on-non-competes.

[4] See https://www.ftc.gov/system/files/ftc_gov/pdf/p201000noncompetewilsondissent.pdf ("I am dubious that three unelected technocrats have somehow hit upon the right way to think about non-competes, and that all the preceding legal minds to examine this issue have gotten it wrong.").

[5] We wrote, "Regardless of whether one favors or disfavors the use and enforcement of noncompetes, the FTC should be forthright in its communications so that the public can make informed decisions about whether to support its actions — and thus the administration on whose behalf they are acting."

[6] We wrote, "[FTC Chair] Khan asserted that noncompetes are regularly enforced against low-wage workers, such as fast-food workers, arborists and manual laborers. This is a common refrain that the media uses to draw viewers and clicks, but it is misleading at best. While there are always outlier cases, the FTC cites no conclusive evidence that they are the norm. Indeed, they are not. Anecdotes

are not evidence of a systemic issue."

[7] Evan Starr and Norman D. Bishara, "The Incomplete Noncompete Picture," 20 Lewis & Clark L. Rev. 497, 497 — 546 (2016), Robert H. Smith School Research Paper No. RHS 2782137, available at https://ssrn.com/abstract= 2782137 ("[T]he empirical studies of the impacts of noncompete enforceability, which make up the bulk of the literature, suffer from numerous shortcomings related to the lack of data on who signs noncompetes... . Given the lack of empirical work using actual data on noncompete usage, it is safe to say that we know relatively little about the uses and consequences of noncompetes.").

Evan Starr, Natarajan Balasubramanian, and Shotaro Yamaguchi, "Bundling Postemployment Restrictive Covenants: When, Why, and How It Matters" (2021), available at https://extranet.sioe.org/uploads/sioe2021/balasubramanian_starr_yamaguchi.pdf (noting how "examining a single [post-employment restrictive covenant, such as a noncompete] without considering the bundle [of all post-employment restrictive covenants, including nondisclosure and non-solicitation covenants] can be misleading").

Final Transcript of January 9, 2020 FTC Workshop ("FTC Workshop Tr.") — "Non-competes in the Workplace: Examining Antitrust and Consumer Protection Issues," p. 158-59, available at https://www.ftc.gov/system/files/documents/public_events/1556256/non-compete-workshoptranscript-full.pdf ("[W]hen you compare workers who have signed a non-compete to those who haven't, you have to worry that there are other differences between those workers, not just whether they have signed the non-compete, which could be driving any outcomes you observe ... . And it makes it really tricky, and I don't think we really have any great studies so far that really isolate random variation in the use of non-competes ... .").

See also Russell Beck, et al., "Written Submission of Practicing Attorneys Concerning Potential Federal Regulation of Noncompetition Agreements" ("Practicing Attorney Letter"), at p. 30, available at https://faircompetitionlaw.com/wp-content/uploads/2021/07/White-House-and-FTC-20210714-Joint-Submission-of-Trade-Secret-Lawyers-Beck-et-al.pdf ("Most of the studies that ask employees whether they are bound by a noncompete have no meaningful way to know whether the employee actually understands the difference between a noncompete, a nonsolicitation agreement, or even a nondisclosure agreement. Many employees do not know the difference.").

[8] See Practicing Attorney Letter, at pp. 25-27 ("As explained above, contrary to much of the colloquial commentary, noncompete agreements cannot (lawfully) be used to prevent an employee from broadly using his or her general skills and knowledge (or otherwise working). Yet, we often see the abuses captured in the headlines, and it can drive an overreaction that could potentially eliminate an important tool for some businesses to maintain control of critical information assets.").

Again, Professor Starr has previously acknowledged this as well. See James Prescott, Evan Starr, and Norman D. Bishara, "Understanding Noncompetition Agreements: The 2014 Noncompete Survey Project," Mich. St. L. Rev. 2016, no. 2 (2016): 369-464, available at https://repository.law.umich.edu/articles/1796/ ("Recent media reports have cataloged a number of egregious sounding noncompete practices. These disclosures appear to have influenced public perception, generating speculative conclusions that noncompete use is on the rise. News that employers have used noncompete restrictions with hair stylists, yoga instructors, lawn sprayers, teenage camp counselors, low-wage fast-food workers, and temporary warehouse workers, to cite just a few examples, strikes many as both surprising and inexplicable. These sorts of revelations draw ire and condemnation both from the public and from politicians... . However, many observers ignore pivotal questions about these stories... . [W]e do not know if these agreements — especially for low-wage employees, but even for more educated, skilled, and highly paid workers — are truly commonplace.").

[9] See footnote 5, supra.

[10] We again find ourselves good company with the other commentators he targets with this critique. See Herbert Hovenkamp, "Noncompete Agreements and Antitrust's Rule of Reason," The Regulatory Review (2023), available at https://www.theregreview.org/2023/01/16/hovenkamp-noncompetes-and-rule-of-reason/ ("Workers who sign such agreements often receive higher wages than those who do not.").

A.J. Meese, "Don't Abolish Employee Noncompete Agreements," Wake Forest L. Rev., 57, p. 631 (2022), available at https://scholarship.law.wm.edu/cgi/viewcontent.cgi?article=3158&context=facpubs ("The employer's payment of premium wages that induce such an agreement thereby shares with employees the gains that such contracts make possible.").

[11] Evan Starr, J.J. Prescott, and Norman D. Bishara, "Noncompete Agreements in the U.S. Labor Force" (October 2020), Journal of Law and Economics 2021, available at https://ssrn.com/abstract=2625714 ("Focusing first on those who learn of their noncompete before they accept their job offer, our most saturated model indicates that these employees have 9.7% (e0.093) higher earnings, are 4.3 percentage points more likely to have information shared with them (a 7.8% increase relative to the sample average), are 5.5 percentage points more likely to have received training in the last year (an 11% increase), and are 4.5 percentage points more likely to be satisfied in their job (a 6.6% increase) relative to those employees without a noncompete... . In all specifications but one, within-model tests confirm that those who learn of their noncompete from their prospective employer before they accept that employer's offer do statistically significantly better (in terms of compensation, training, access to information, and satisfaction) relative to those who learn of and acquiesce to their noncompete only after they accept their employment offer.").

See also Ryan Nunn and Matt Marx, "The Chilling Effect of Non-Compete Agreements," available at https://econofact.org/the-chilling-effect-of-non-compete-agreements ("If it were the case that workers made fully informed decisions about signing a noncompete and could negotiate higher compensation in exchange for doing so, these agreements could be valuable for both workers and firms.").

[12] FTC Workshop Tr., at 144-51 (comments of Professor Kurt Lavetti) and at 175-79 (comments of Professor Ryan Williams, University of Arizona).

[13] We wrote, "Perhaps Khan's oddest claim is that 'noncompetes lead to higher prices for consumers by reducing competition.' Leaving aside that the FTC has no conclusive evidence for this assertion, and relies entirely on a single study of the health care industry, if it were true — as the FTC would have us believe — that noncompetes drive down wages, and that doing away with them will increase workers' earnings by hundreds of billions of dollars annually, then prices will naturally increase as employers attempt to recoup their lost profits. Assuming that increasing a company's costs will somehow lead to lower prices is illogical. Again, Wilson points out that the proposed rule 'omits studies showing that reducing the enforceability of non-compete restrictions leads to higher prices for consumers.'"

[14] "What is inflation?," McKinsey & Company (Aug. 17, 2022), available at https://www.mckinsey.com/featured-insights/mckinsey-explainers/what-is-inflation#/ ("Companies lose purchasing power, and risk seeing their margins decline, when prices increase for inputs used in production, such as raw materials like coal and crude oil, intermediate products such as flour and steel, and finished machinery. In response, companies typically raise the prices of their products or services to offset inflation, meaning consumers absorb these price increases.").

[15] See, e.g., James M. MacDonald and Daniel Aaronson, "How Do Retail Prices React to Minimum Wage Increases?" Federal Reserve Bank of Chicago Working Paper 00-20 (2000), available at https://www.chicagofed.org/ publications/working-papers/2000/2000-20 ("A textbook consequence of an industry-wide cost shock is that it will be passed on to consumers through an increase in prices. The minimum wage offers a compelling natural experiment of such a cost shock, particularly among industries that employ low wage labor. We assess the effect of recent minimum wage increases on restaurant prices, using specific item prices collected by the Bureau of Labor Statistics (BLS). We find that price responses follow textbook expectations in several dimensions.").

James Sherk, "$15 Minimum Wages Will Substantially Raise Prices," The Heritage Foundation (2017), available at https://www.heritage.org/jobs-and-labor/report/15-minimum-wages-will-substantially-raise-prices ("Economic research consistently finds that businesses pass minimum-wage costs on to their customers through price increases.").

[16] Michigan also banned noncompetes in 1905, although that ban was rescinded in 1985.

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