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Know Your Limits: Understanding State-Imposed Restrictions on Noncompetes

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An estimated 30 million workers in the United States, roughly 18 percent of the American workforce, are subject to a noncompete agreement, according to the US Treasury Department and Federal Trade Commission. Noncompete agreements, which prohibit employees or contractors from providing services to competitive companies for a period of time after the end of their employment, have always been subject to judicial, legislative and agency scrutiny.

Currently, there is no federal statute or agency rule that provides a unified approach to noncompetes. In the absence of such a controlling federal noncompete statute or final executive agency rule, states have increasingly imposed a patchwork of regulations limiting which employees may be subject to noncompete agreements.

However, on January 5, 2023, the Federal Trade Commission (FTC) proposed a rule with a sweeping ban of noncompete agreements, which resulted in more than 25,000 public comments through the close of the comment period on April 19, 2023. Considering the FTC's proposed rule, it is prudent for employers to have a complete understanding of the categories of employees *already* protected from noncompetes by state law.

Understanding the current state laws, and particularly the areas where the states find common ground on these issues, may provide a fertile opportunity for employers to consider adopting broad policies on using noncompetes. This can help employers to avoid the potential adverse impacts (i.e., imposition of a federal ban that aligns with current state restrictions) of any final agency rulemaking and to "futureproof" their business interests.

Even if (as is likely) the FTC's authority to promulgate its proposed rule is challenged under the Federal Trade Commission Act or "major questions doctrine," state laws will still provide the prevailing regulation of noncompetes that employers must follow.

A thorough analysis of nationwide noncompete laws identifies several distinct categories of employees that states often protect from the use of noncompetes. These protections come in the form of limits, or outright prohibitions, on the use of noncompetes. Similarly, there are many other categories of employees whom the states permit to be bound by a noncompete.

Who Is Protected?

The primary purposes of recent state laws limiting the use of noncompetes are:

1. Protecting low-wage employees;
2. Industry carve-outs;
3. Ensuring public access to critical services such as lawyers and doctors; and
4. Ensuring public access to critical information.

Protecting Low-Wage Employees

One of the most common limitations on the use of noncompetes, and a growing trend across the country, draws from the legislative philosophy of protecting “low wage” employees.

The 2018 Massachusetts Noncompetition Agreement Act (MNAA) was a turning point in the push by states to define and articulate classes of workers who may not be subject to noncompetes. In addition to several other provisions, the MNAA prohibited employers from entering into noncompete agreements with hourly employees and those working in temporary or entry-level jobs. This group of protected employees included:

- Employees classified as nonexempt/overtime-eligible under the Fair Labor Standards Act;
- Employees under 18;
- Undergraduate or graduate students working as interns or in other short-term employment; and
- Those terminated “without cause” or laid off.

These limits on noncompetes for low-wage employees kicked off a groundswell of regulation across the country, including in Maine, Maryland, New Hampshire, Rhode Island and Washington in 2019; Virginia in 2020; and Nevada in 2021. Now, a dozen states (including the District of Columbia) impose some degree of restriction on using noncompetes with low-wage workers.

Industry Carve-Outs

The most interesting and dynamic groups of employees whom state statutes protect from noncompetes are those who receive their protected status due to the impact of lobbying and state protectionism.

In contrast to the limits on noncompetes for employees earning at or below certain wage thresholds, there are restrictions in several states that beg the question, “Who fought to make this law?” The answer is not always apparent from the legislative record, but lobbying efforts are one reasonable inference.

Examples of these unique restrictions include:

- Security guards in Connecticut;
- Automobile salespeople in Louisiana;
- Motor vehicle dealers and franchisees in Maine; and
- Barbers and cosmetologists in Vermont.

Another notable group of protected employees is technology workers in Hawaii. In Hawaii, the state’s legislature banned and rendered void the use of noncompete and nonsolicit provisions in employment agreements with "employee[s] of a technology business," where a *technology business* is defined as "a trade or business that derives the majority of its gross income from the sale or license of products or services resulting from its software development or information technology development, or both."

The legislature was clear that it intended this measure to increase employment competition within the state and “stimulate Hawaii’s economy by preserving and providing jobs for employees in this sector and by providing opportunities for those technology employees to establish new technology companies and new job opportunities in the State.”

Public Access to Critical Services

Every state has adopted some form of the American Bar Association's Model Rules of Professional Conduct 5.6, which prohibits any "agreement that restricts the right of a lawyer to practice" law.

After lawyers, the group of professionals most guarded from the use of noncompetes is medical and healthcare professionals. Nearly half of the states have adopted, via legislation or common law, some form of limit on the ability to bind healthcare workers to noncompete agreements.

These restrictions come in a variety of forms.

- Outright bans:
  - Delaware: A noncompete provision that "restricts the right of a physician to practice medicine in a particular locale and/or for a defined period of time" is void.
  - New Hampshire: Any agreement with a licensed physician that "includes any restriction to ... practice medicine in any geographic area for any period of time" is void.
- Formula-based restrictions:
  - Florida: A noncompete with a physician is enforceable only if there is another physician "who practices [the] medical specialty in [the] county" and is employed by a different entity.
  - Tennessee: A noncompete with a physician is "reasonable" if the restriction is included in an "employment agreement or other written document" and the duration and geographic scope comply with Tennessee-imposed limitations.
- Patient-focused directions:
  - New Jersey: Physicians may not enter into agreement "that interferes with or restricts the ability of a client to see or continue to see [their] therapist."

Public Access to Critical Information

Nine states limit the use of noncompetes for broadcast journalists. Many of these restrictions have been introduced or championed by SAG-AFTRA, the union that represents broadcast journalists, actors and other media professionals. According to the President of Seattle Local AFTRA, the purpose of these restrictions is clear: "[this bill] protects the future and the integrity of the principal vehicle by which your constituents receive the information they use to make their decisions about the kind of state they want."

When states impose noncompete restrictions on broadcasters, these are often outright bans:

- Arizona: It is unlawful for a "broadcast employer" to require a noncompete.
- Illinois: A "broadcasting industry employer" may not require a noncompete.
- Maine: A noncompete for a broadcast employee is "presumed to be unreasonable."

However, some states (e.g., Utah and Oregon) apply guardrails only on an employer's ability to use noncompetes with broadcast employees.

Who Isn't Protected?

It is as interesting and valuable to understand which groups the various state legislatures have deemed are *not* subject to noncompete agreement protections as it is to understand which are covered within their state's limits on the use of noncompetes.

Business Sellers

The original three anti-noncompete states are California, North Dakota and Oklahoma. In each of these states, the use of noncompetes is extremely limited, to the point of near impossibility – unless the restriction applies to someone who has sold their business. Those who sell their business, including its "goodwill," find themselves without protection from noncompetes, even in the states that are the most hostile to these restrictions.

Indeed, even in California – the longstanding anti-noncompete standard-bearer– the legislature explicitly exempted individuals who sell their business from the formidable protections of the state law prohibiting noncompetes. This exemption provides buyers with the confidence and protection to go through with significant business transactions.

High-Wage Earners

The opposite side of state legislatures' _ is their determination of the wage above which employees no longer need blanket protection from noncompetes. Mirroring the low-wage limits, the high-wage threshold varies significantly across jurisdictions. From Maryland, which allows noncompetes for employees earning more than $15 per hour or $31,200 per year (changing to 150 percent of the minimum wage rate effective October 1, 2023), to Washington, DC, which allows noncompetes only for employees earning more than $150,000 per year, and Washington state, which currently sets the threshold above roughly $115,000 per year for an employee and nearly $300,000 per year for an independent contractor.

Physicians

While many states explicitly protect physicians from noncompetes, Tennessee takes the opposite approach for a subset of its medical providers. Even though the state includes geographic and temporal restrictions on the use of noncompetes for most physicians, "physicians who specialize in the practice of emergency medicine" are not subject to such protections.

Broadcast Journalists

While roughly 20 percent of states include some form of protection for broadcast journalists, Hawaii excludes them from the state's noncompete protection, specifically legislating that the definition of a *technology business*, which is uniquely protected from noncompetes in Hawaii, "excludes any trade or business that is considered by standard practice as part of the broadcast industry or any telecommunications carrier."

Any Employee Subject to Reasonable and Necessary Restraints

Even the most hardline, anti-noncompete states will typically allow employees to sign on to some form of an agreement. For example, Colorado, which gained noncompete notoriety in 2022 for its imposition of criminal penalties for the use of improper noncompetes, will uphold a noncompete that "is for the protection of trade secrets and is no broader than is reasonably necessary to protect the employer's legitimate interest in protecting trade secrets."

Takeaways

The groups of employees across the nation captured within or excluded from state noncompete protections reflect an assortment of disparate legislative priorities. States have trended towards shielding employees who earn ‘low’ wages or who provide the public with access to critical services and information from the imposition of a noncompete agreement.

Looking ahead, although employers should remain vigilant and monitor local lobbying efforts and initiatives in their industry, it appears unlikely that one-off protections such as those codified for barbers in Vermont or automobile salespeople in Louisiana will sweep the nation.

Instead, any continued movement on a state-by-state level is likely to follow the prevailing trend of state laws and focus on shielding low-wage workers from the use of noncompetes. Conversely, states seem unlikely to impose limits on the use of noncompetes for individuals who earn significant wages – as determined by their state’s thresholds – or who have sold their businesses.

Ultimately, in every state, noncompetes are meant to serve a legitimate purpose: protecting the former employer’s business, standing and goodwill. Employers are best advised to consider what protections they really need rather than simply asking, “What is the longest noncompete that the state will allow?” As a practical matter, courts and opposing counsel in negotiations often care less about what is “permitted” than what is “needed” to accomplish an employer’s legitimate aims.

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