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ISSUE ALERTS

FTC'S PROPOSED BAN ON NONCOMPETE AGREEMENTS AND THE IMPACT ON HEALTHCARE ORGANIZATIONS

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For decades, the validity of an employment agreement noncompete provision has been determined under State law. On Jan. 5, 2023, the Federal Trade Commission proposed a new rule intended to preempt State law and generally ban employment noncompete clauses, including voiding those currently in effect. The FTC contends that such clauses constitute unfair competition prohibited by Section 5 of the Federal Trade Commission Act. This has generated considerable discussion, including a prior Issue Alert from this firm. The potential application of the proposed FTC rule to healthcare organizations deserves special mention.

Kansas courts have long ruled that a noncompete clause in an employment agreement is enforceable if it is reasonable in the circumstances and not adverse to the public welfare. Reported Kansas case law contains recent examples in which noncompete provisions in physician agreements have been enforced. The proposed FTC rule would expressly preempt State law to the extent inconsistent with its total ban on noncompete clauses.

However, the rule would not apply to all organizations. The FTC recognized this in a single paragraph buried in its lengthy discussion of noncompete clauses and their impact on employment and wages. It stated that "[s]ome entities that would otherwise be employers may not be subject to the Rule to the extent they are exempted from coverage under the FTC Act." The FTC noted that this would encompass various banks and financial institutions, common carriers, and meatpacking plants as well as an entity that is not "organized to carry on business for its own profit or that of its members."

The quoted language ties back to Section 4 of the FTC Act that makes the unfair competition provision of Section 5 applicable to corporations and other entities "organized to carry on business for [their] own profit or that of [their] members." Consequently, an organization is generally not subject to Section 5 of the Act if it is organized and operates for a public purpose and any surplus revenues are devoted to public, rather than private, interests. The common understanding is thus that the FTC lacks jurisdiction under Section 5 over nonprofit organizations such as

nonprofit hospitals. Whether this exemption extends to governmental hospitals — which also generally operate for a public purpose and do not distribute revenues to owners or members — is unclear but would seem arguable.

This somewhat suggests that nonprofit hospitals and other nonprofit organizations may continue to evaluate and enforce noncompete provisions in employment contracts under State law even if the proposed FTC rule is adopted. But the structure and operations of some organizations may require careful review to determine whether the applicable rules are those based in State law or whether the FTC rule applies if it is adopted.

For-profit organizations should be aware that the action of the FTC is not confined to proposing a rule. On Jan. 4, 2023, it announced enforcement actions against three companies and two individuals, forcing them to stop use of noncompete clauses. None of these were in health care and all of the enforcement actions involved somewhat unusual facts. But they clearly indicate that the FTC may take action without awaiting final adoption of the proposed rule.

In addition, attempts to enforce a physician noncompete when the result may be to materially impact patient access or care in concentrated markets may be challenged under other statutes. The FTC has in the past (as far back as 2012) asserted in particular circumstances that noncompete clauses in physician contracts should not be enforceable. As also noted by the FTC, alternatives to noncompete clauses may include nondisclosure and confidentiality clauses and a nonsolicitation clause so long as such clauses are not so broad and restrictive as to effectively equate to a noncompete.

Clearly, use of noncompete clauses is under attack. Healthcare organizations should be aware of this and should carefully evaluate the necessity and rationale for use of such clauses in each circumstance, and consider whether nondisclosure and confidentiality clauses and/or nonsolicitation clauses may be utilized to best protect the organization.

FOR MORE INFORMATION

If you have questions or want more information regarding the proposed noncompete law, contact your legal counsel. If you do not have regular counsel for such matters, Foulston Siefkin LLP would welcome the opportunity to work with you to meet your specific business needs. Foulston's healthcare lawyers maintain a high level of knowledge regarding federal and state regulations affecting the healthcare industry. At the same time, our healthcare practice group's relationship with Foulston's other practice groups, including the taxation, general business, labor and employment, and commercial litigation groups, enhances our ability to consider the legal ramifications of any situation or strategy. For more information, contact **Dick Hay** at 785.354.9413 or dhay@foulston.com, or **Brooke Bennett Aziere** at 316.291.9768 or baziere@foulston.com. For more information on the firm, please visit our website at www.foulston.com.

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