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Legal Alerts

Texas Court's Preliminary Ruling Delays FTC Noncompete Ban, but Ruling Affects Only Parties to Lawsuit

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On April 23, 2024, the Federal Trade Commission (FTC) announced a final rule that would prohibit entering into noncompete agreements and render most existing noncompetes unenforceable. The FTC final rule prohibits entering into or enforcing a noncompete agreement unless entered into with a "senior executive" (a worker in a "policy-making" position who received a total compensation of $151,164 in the preceding year). However, the final rule does not prohibit non-disclosure agreements, training repayment agreements or non-solicitation agreements. The final rule requires employers to provide clear and conspicuous notice to workers who are subject to potentially prohibited noncompete clauses that such clauses are not legally enforceable.

However, on July 3, the US District Court for the Northern District of Texas issued a preliminary injunction that paused the implementation of the final rule. The judge found that the plaintiffs (tax preparation company Ryan LLC and the U.S. Chamber of Commerce) in *Ryan LLC v. Federal Trade Commission* are "substantially likely" to prevail on the merits of their challenge to the final rule.

The court found that the "text, structure, and history of the [statute creating the FTC] reveal that the FTC lacks substantive rulemaking authority" to address noncompetes. The court also noted that the final rule may be invalid under the Administrative Procedure Act (5 U.S.C. § 706(2)(A)), as the final rule is "unreasonably overbroad without a reasonable explanation" and "is based on inconsistent and flawed empirical evidence." According to the court, the FTC failed to consider the positive benefits of noncompete agreements and disregarded a substantial body of evidence supporting noncompetes.

Importantly, the ruling only applies to the two parties who filed the Texas lawsuit, and the judge declined to issue a nationwide stay of the Rule's effective date. Because 46 states have varied statutory and common law rules addressing noncompetes, the court found that the Ryan case would not "merit nationwide relief."

Another challenge to the FTC's final rule is pending in the US District Court for the Eastern District of Pennsylvania. The judge in that case, *ATS Tree Services, LLC v. Federal Trade Commission*, will issue a ruling by July 23. That ruling may be limited to those plaintiffs or may be nationwide in scope.

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Barring an unexpected change in the Texas case, or a broader ruling in the Pennsylvania case, the final rule will take effect on September 4, 2024, for all employers who were not parties to these lawsuits. Employers must continue to comply with applicable state requirements governing noncompetes and be prepared to implement the final rule. Employers should carefully draft new employment, confidentiality and other agreements that contain post-employment restrictions, and review similar existing agreements, to ensure compliance with the final rule and applicable state laws.

If you have questions about managing compliance with these noncompete laws or any other employment or labor issues, please contact any member of the Foster Garvey Labor, Employment & Immigration Group.

Authored by

Steven R. Peltin

Principal|Seattle

206.447.6215 steve.peltin@foster.com

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