CORNERSTONE NEWS

NON-COMPETE AGREEMENTS

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FTC Attacks Non-Compete Agreements as Unenforceable

As you likely have heard, the Federal Trade Commission (FTC) has recently attacked existing non-compete agreements.

The FTC ruled that such agreements are anti-competitive, and therefore generally unenforceable. This ruling covers all agreements existing as of or after September 4, 2024.

Exceptions include such agreements that relate to the most senior executives in a company, and those entered into as part of a bona fide "sale of business."

The ruling by the FTC is currently being challenged in some Federal courts. Regardless of the outcome of these challenges, we believe that it is important to better understand the potential retention role that Non-Qualified compensation arrangements can play in your organization.

Non-Qualified Plans – as a Substitute for Non-Compete Agreements

While companies appear to be able to enforce non-solicitation and confidentiality provisions, the loss of non-compete powers constitutes a large concern for many companies.

We have been asked for our thoughts on what other tools can be used to help protect companies. We believe that non-qualified compensation arrangements with cliff vesting provisions can fill some of the void created by the FTC ruling.

What is Non-Qualified Compensation?

Non-qualified compensation arrangements are those that typically establish an obligation to pay an employee or service provider future compensation based on the attainment of specified goals or metrics.

The recipient of such compensation is taxed for federal income taxes upon receipt, at which time the employer is entitled to a tax deduction for such amounts. Since amounts under such a plan can be quite large, companies generally pay these amounts out over time.

Cliff Vesting – as an Incentive to Stay With the Company!

Cliff vesting means that the recipient earns the right to receive this compensation immediately after a specified period of time, with 5 years being a very common period. If the recipient leaves before the vesting period has elapsed, they receive no right to the compensation specified in the plan. Companies will often make overlapping grants so that there would always be some compensation forfeited by the employee for their early departure.

Benefits to the Company:

These plans are particularly effective in both securing top-notch talent and retaining such talent for the future. They help dissuade individuals from leaving the company, and when care is given to the plan design, it can align employee performance to the company's strategic initiatives.

While these arrangements are limited in the scope of their application within a company, senior managers and those possessing specialized knowledge and skills can generally be accommodated.

***If you would like to learn more about this strategy, please contact us. Also, stay tuned for an additional strategy to address this situation*.**

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