

EPI comment on the FTC's noncompete clause rule

Public Comments • By Heidi Shierholz, John Schmitt, and Samantha Sanders • April 19, 2023

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Federal Trade Commission
Office of the Secretary
600 Pennsylvania Avenue NW
Suite CC-5610 (Annex C)
Washington, DC 20580

Re: **Non-Compete Clause Rule** (RIN 3084-AB74)

To Whom It May Concern:

The Economic Policy Institute (EPI) is a nonprofit, nonpartisan think tank created in 1986 to include the needs of low- and middle-income workers in economic policy discussions. EPI conducts research and analysis on the economic status of working America, proposes public policies that protect and improve the economic conditions of low- and middle-income workers, and assesses policies with respect to how well they further those goals.

EPI strongly supports the Federal Trade Commission's proposed rulemaking to ban the use of noncompete agreements as conditions of employment, under the Commission's authority under Section 5 of the FTC Act. Noncompete agreements are employment provisions that ban workers at one company from going to work for, or starting, a competing business within a certain period of time after leaving a job. As EPI affirmed in a 2019 analysis of the prevalence of noncompete agreements, policymakers can and should prohibit the use of noncompetes due to the harm they inflict on workers and competition.

Under the FTC's proposed rule, employers would be barred from requiring workers to sign noncompetes, regardless of the worker's status as an employee or independent contractor, and would rescind existing noncompetes. This aligns with policy approaches already undertaken by some states, which have passed laws limiting employers' ability to impose noncompete agreements on their employees. In this comment,

we will discuss the ubiquity of noncompete agreements and describe the effect these agreements have on depressing wages, limiting worker freedom, and artificially reducing fair market competition. Given these arguments, the Federal Trade Commission should proceed in implementing a strong final rule to ban noncompete clauses and put an end to this anticompetitive, restrictive practice.

Noncompetes are widely used

Noncompete agreements are widespread, even among low-wage workers.

- A 2014 survey designed and administered by Evan Starr, J.J. Prescott, and Norman Bishara (2020) of over 11,000 labor force participants found that almost one in five workers (18%) are bound by noncompete agreements and almost two in five (38%) report having signed a noncompete agreement sometime in their career.¹
- Using a 2017 survey of a random sample of private-sector businesses with 50 or more employees, Alexander J. S. Colvin and Heidi Shierholz (2019) report that almost half (49.4%) of their sample required at least some employees to sign a noncompete agreement and almost one-third (31.8%) indicated that all employees were required to accede to a noncompete as a condition of employment. Based on their data, Colvin and Shierholz estimate that between 27.8% and 46.5% (36 million to 60 million workers at the time of their analysis) were subject to noncompete agreements.² The higher share subject to a noncompete found in this survey compared with the other surveys cited here could be due to the fact that this was a survey of business establishments, while the other are surveys of individual workers. While businesses know whether their workers are subject to noncompete agreements, workers may not know or remember they are covered by a noncompete, and thus may underreport being subject to them.
- An analysis by Natarajan Balasubramanian, Evan Starr, and Shotaro Yamaguchi (2023) of data from a 2017 survey of over 33,000 individuals who visited Payscale.com, a U.S. compensation firm, found that 22.1% of private-sector workers were covered by a noncompete agreement.³
- An analysis of the National Longitudinal Survey of Youth by Donna Rothstein and Evan Starr (2021) looking at private-sector workers in 2017–2018 who were between the ages of 32 and 38 estimated that 18% were bound by a noncompete agreement at their current job.⁴

Noncompete agreements are not limited to high-wage workers in knowledge-sensitive occupations and industries.

- Michael Lipsitz and Evan Starr (2021) note that “while [noncompete agreements] are frequently assumed to occur only in high-wage jobs...we find that the modal worker bound by a [noncompete agreement] is paid by the hour, with median wages of \$14.”⁵
- Colvin and Shierholz (2019) report that more than a quarter (29.0%) of private workplaces they surveyed that had an average wage of less than \$13.00 per hour used noncompete agreements for all their workers.⁶

- In their analysis of private-sector workers in 2017–2018, Rothstein and Starr (2021) reported that 14.4% of workers who earned less than the equivalent of \$20 per hour and 14.7% of workers with less than a college degree had signed a noncompete agreement (compared with 21.7% for those earning more than \$20 per hour and 24.3% of college graduates).⁷
- Starr, Prescott, and Bishara (2020, Table 5) found that 13.3% of labor force participants who earned less than \$40,000 per year in 2017 reported that they were subject to a noncompete agreement and 33.0% had been subject to a noncompete at their current or an earlier employer.⁸
- Matthew Johnson and Michael Lipsitz’s (2022) email-based survey of hair salon owners who were members of the Professional Beauty Association, a trade organization of salon professionals, concluded that noncompete agreements “are widely used,” with 30% of hair salon owners reporting that they required their most recently hired stylist to sign a noncompete agreement.⁹

As Starr, Prescott, and Bishara (2020) note, “the frequency of noncompetes among low-wage employees without access to trade secrets and the lack of negotiation in the contracting process hint at more anticompetitive rationales for the use of noncompetes by employers.”¹⁰

Noncompetes lower wages

A growing body of research establishes that noncompete agreements lower the wages of workers who sign them relative to similar workers not subject to noncompetes.

- An analysis by Michael Lipsitz and Evan Starr (2021) of wage trends in Oregon after the state banned noncompete agreements found that wages for all hourly workers increased by 2–3% on average. When the researchers adjust the average change to reflect that only a share of low-wage workers have signed a noncompete agreement, their estimate of the direct negative wage effect on workers subject to a noncompete rises to 14–21%, “though the true effect is likely lower due to labor market spillovers onto those not bound by [noncompete agreements].” Lipsitz and Starr report even larger reductions in wages for nonhourly wage workers.¹¹
- In their analysis on the effects of noncompete agreements, Matthew Johnson, Kurt Lavetti, and Michael Lipsitz (2020) conclude that “[a] back of the envelope calculation using an out-of-sample extrapolation implies that rendering [noncompete agreements] unenforceable nationwide would increase average earnings among all workers by 3.3% to 13.9%” with the midpoint of the interval at 8.6%.¹²
- Using data from the Survey of Income and Program Participation, Evan Starr (2019) finds that an increase in enforcement of state noncompete laws (from nonenforcement to average state’s level of enforceability) is associated with a 4% decrease in hourly wages.¹³

Evidence suggests that noncompetes also lower wages of workers who are not subject to noncompete agreements. Matthew Johnson, Kurt Lavetti, and Michael Lipsitz (2020)

suggest that the negative wage impact on workers directly bound by these noncompetes can spill over to workers who have not signed agreements. Enforceable noncompete agreements “can increase recruitment costs for all firms,” they state, because hiring firms generally can’t observe whether a job applicant is subject to a noncompete agreement. Noncompetes “can also decrease the number of search firms...decrease entrepreneurship and new firm entry,” all of which “would increase local labor market concentration” and “depress wages” (p. 10). In general, they argue, noncompetes make labor markets “thinner,” reducing the likelihood of a successful “match,” and thereby “driv[ing] down equilibrium wages” (p. 9).¹⁴

An analysis of data of the Noncompete Survey Project by Evan Starr, Justin Frake, and Rajshree Agarwal (2019) presents evidence confirming Johnson, Lavetti, and Lipsitz’s logic. Starr, Frake, and Agarwal “find that in state-industry combinations with a higher incidence and enforceability of noncompetes, workers—including those unconstrained by noncompetes—receive relatively fewer job offers, have reduced mobility, and experience lower wages” (emphasis added).¹⁵

Noncompetes are often bundled with other anti-competitive employer practices that harm workers

As Evan Starr (2020) has testified before the Federal Trade Commission: “Non-competes are just maybe the tip of the iceberg, maybe the most restrictive tip, but just the tip of the iceberg” (p. 172).¹⁶ In a similar vein, Colvin and Shierholz (2019) note that “employers who require their workers to enter into one type of restrictive contract are more likely to require their workers to sign additional restrictive contracts” (pp. 8–9).¹⁷

- Balasubramanian, Starr, and Yamaguchi (2023, Table 2) analyzed data from the 2017 version of Payscale.com’s annual firm-level survey of HR professionals and other leaders at 1,855 private or publicly traded firms located in the United States. Almost one in four (22.7%) firms used noncompete agreements together with nondisclosure agreements (NDAs), nonsolicitation agreements (NSAs), and nonrecruitment agreements (NRAs) for all employees; more than half (55.2%) used all four types of agreements for at least some of their employees. Their firm-level results were consistent with findings from a separate employee-level survey they analyzed, in which 18% of workers said they were bound by a noncompete as well as an NDA, NSA, and NRA.¹⁸
- Starr, Prescott, and Bishara’s (2020, Table 4) 2017 survey of over 11,000 labor market participants found that among those who were bound by a noncompete agreement, 75% were also subject to a nondisclosure agreement, 18% to a nonpoaching agreement, 35% to a nonsolicitation agreement, and 19% to an arbitration agreement.¹⁹
- Colvin and Shierholz’s (2019, Table 6) analysis of firm data showed that over half (53.7%) of firms that required noncompetes for at least some of their employees also required at least some employees to agree to mandatory arbitration, rather than the court system to resolve disputes with their employers.²⁰

As the American Enterprise Institute’s John Lettieri has argued, workers often enter into noncompete agreements after little or no bargaining with their employer and without full information about the rights they are signing away:

The vast majority of noncompete agreements are not subject to any negotiation between the employer and employee, suggesting that the employee is unlikely to receive any benefits in return for their signature. A large share of these agreements are presented for signature only after the employee has already accepted the job offer—often on the first day of work. Employers frequently exploit workers’ lack of knowledge and resources when crafting noncompetes. For example, employers commonly request that workers sign noncompetes even in states where they are completely unenforceable—and workers nevertheless sign the agreements assuming they are valid. Likewise, employers often craft extremely broad provisions knowing that employees generally lack both an understanding of what is enforceable and the wherewithal to challenge the terms in court. (Lettieri 2020, p. 3)²¹

In their discussion of noncompetes in the context of a comprehensive review of a range of government and employer policies that suppress wages, Lawrence Mishel and Josh Bivens (2021) conclude that the bundling of noncompetes with nondisclosure, nonsolicitation, nonpoaching, and intellectual property assignment agreements “provides further evidence that [noncompetes’] purpose is to restrict employee options rather than to protect beneficial investments in and information held by employees.”²²

Banning noncompetes will help to reduce inflation

While eliminating noncompete agreements will raise wages, the net effect will be to *reduce* prices paid by consumers. Most directly, noncompete agreements increase concentration in the markets for goods and services by preventing workers from leaving their employers to create new businesses or join other firms that can increase the market supply and intensify competition. Banning noncompete agreements will reduce market concentration, thereby reducing market prices.

Noncompete agreements also reduce productivity growth by blocking the efficient reallocation of labor from less productive to more productive job matches. Eliminating noncompete agreements will allow workers to find firms, and firms to hire workers, that yield the most productive matches. The increased firm and economywide productivity will reduce, not increase, consumer prices.

Conclusion

Noncompete agreements are widespread, harmful to workers' wages, and limit competition among businesses. By banning the use of noncompete agreements for workers, the Federal Trade Commission's proposed rule would help raise wages for workers and allow for fair market competition. EPI strongly supports the proposed rule and urges the Federal Trade Commission to swiftly promulgate a final rule.

Sincerely,

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1. Evan P. Starr, J.J. Prescott, and Norman D. Bishara, "Noncompete Agreements in the U.S. Labor Force," *Journal of Law and Economics* 64, no. 1 (October 2020): 53–84, <http://dx.doi.org/10.2139/ssrn.2625714>.

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