

## NEWS & INSIGHTS

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# How abolishment of non-compete agreements would impact the franchise model

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The U.S. Federal Trade Commission has proposed a ground-breaking rule with the potential to upend the franchise model. Non-compete agreements, which prohibit a franchisee from operating a competing business during the term of the franchise agreement and for a period of time after the end of the franchise agreement, are common practice in franchising but if the FTC rule goes into effect, they may soon be a thing of the past. The proposed rule could ban franchisors from entering into non-compete agreements with their franchisees and retroactively nullify existing non-

competes within six months.

Some courts have considered non-compete agreements to be unfavored restraints on trade and have scrutinized them to ensure they are narrowly tailored and reasonable in duration and geographical scope.

The [FTC's proposed rule](#), however, would be a blanket prohibition and would only provide a single exception for those who hold at least a 25% ownership interest in a business entity and who enter into a non-compete agreement for the sale of that business. This exception recognizes that those who hold a significant ownership interest in a business are likely to be privy to the business' proprietary information and know-how. As it stands, there is no exception recognizing that to operate a franchise, franchisees are similarly privy to a franchisor's trade secrets, customer lists and other proprietary information.

Non-compete agreements protect not only franchisors, but also preserve the goodwill and well-being of each individual franchisee of that system. Franchisees themselves are often advised by independent legal counsel to scrutinize franchise agreements that do not contain a form of non-compete obligation, as this could signal that other franchisees in the same system may directly compete with that franchisee either during the term of the franchise agreement or upon its expiration or termination.

With non-compete agreements possibly about to be abolished, franchisors do have other options to replace non-compete agreements. Franchisors should consult legal counsel to strengthen the confidentiality and non-solicitation provisions of their franchise agreements in an attempt to offset the impact that the FTC's proposed rule could have across the franchise community. Saxton and Stump attorney [Thomas J. Kent Jr.](#) and any member of the firm's [Franchising, Licensing and Distribution Group](#) are available to further discuss how to best protect the goodwill of the franchise model in light of this proposed rule.

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