Top Job Markets Show Noncompetes May Not Squash Growth

By **Leiza Dolghih**

Leiza Dolghih

In 2016, the White House issued a report concluding that noncompete agreements suppressed wages and deterred employee mobility, and calling the states to limit the use of such agreements around the country. However, The Wall Street Journal's recently published list of hot job markets, which mostly contains cities located in the jurisdictions where noncompetes are frequently enforced, throws into doubt the arguments that such contracts negatively affect wage growth and job mobility.

For example, Austin, Texas, which was ranked as the hottest job market for the second year in a row by The Wall Street Journal, is in the middle of the state that has a strong culture of noncompete enforcement. Yet, Austin beat San Jose, California, where noncompete agreements are banned, in wage and labor force growth.

In fact, Texas landed two cities on the top-10 list of hot job markets, despite the prevalence of noncompete agreements in that state. Eight out of the top 10 cities on The Wall Street Journal’s list are in the jurisdictions that enforce noncompete agreements, suggesting that such contracts are not as bad for business or employees as the proponents of noncompete bans have been arguing.

The anti-noncompete movement argues noncompetes are bad for wage growth and job mobility.

In 2014, HuffPost published an article exposing Jimmy John's Franchise LLC as requiring its low-wage sandwich makers to sign two-year noncompete agreements that prohibited them from working for any company that made sandwiches within three miles of any Jimmy John’s locations.[1] The spotlight on the issue of noncompete abuse and the ensuing public furor caused various government agencies and the executive branch to take a closer look at this issue.

In March 2016, the U.S. Department of the Treasury issued a report titled "Non-Compete Contracts: Economic Effects and Policy Implications," which cited several academic articles and limited case studies concluding that stricter noncompete enforcement reduced employee mobility, and caused both lower wage growth and lower initial wages, and negatively related to employment growth and entrepreneurship.[2]

In May 2016, the White House issued a report titled "Non-Compete Agreements: Analysis of the Usage, Potential Issues, and State Responses," which heavily relied on the Treasury Department’s report and concluded that noncompete contracts "hamper the efficiency of the economy as a whole by depressing wages, limiting mobility, and inhibiting innovation."[3]

In October 2016, the White House followed up with issuing a state call to action on noncompete agreements, asking the state legislators to ban noncompete clauses for certain categories of workers, improve transparency and fairness of noncompete agreements, and incentivize employers to write enforceable contracts.[4]

The state legislatures did not wait long before acting. In 2017 and 2018, California, Colorado, Idaho, Illinois, Nevada, New Mexico, Massachusetts, Oregon and Utah amended their noncompete statutes to provide more protections to employees. In 2019, New Hampshire, Maine, Oregon, Florida, Maryland, Washington and Rhode Island followed with their own amendments that limited the enforcement of noncompete agreements to certain types of workers or imposed additional requirements on employers in order to make their noncompete agreements enforceable.

Additionally, on the federal level, in 2015, various senators introduced the Mobility and Opportunity for Vulnerable Employees Act,[5] the Limiting the Ability to Demand Detrimental Employment Restrictions Act,[6] and the Freedom for Workers to Seek Opportunity Act,[7] which sought to ban noncompete agreements for low-wage workers or certain types of such workers. In 2018 and 2019, three more versions of bills banning or limiting noncompete agreements were introduced without success.

Despite the various states taking action, in 2019, the use of noncompete agreements nationwide came under an attack again; this time, before the Federal Trade Commission. In early 2019, the Open Markets Institute, American Federation of Labor and Congress of Industrial Organizations and various other entities filed a petition for rulemaking to prohibit worker noncompete clauses before the FTC.[8]

The petition relied heavily on academic studies in arguing that noncompete clauses deprived workers of labor market mobility and had a negative effect on employee's wages, presenting, perhaps, the most comprehensive case against noncompete agreements to date. The petition urged the FTC to initiate a rulemaking to prohibit employers from presenting noncompete clauses as a condition of employment, and find such agreements as an unfair method of competition and per se violation of Section 5 of the FTC Act.

In July and November 2019, attorneys general from various states filed two letters with the FTC urging it to use its Section 5 enforcement authority to stop the use of noncompete, nonsolicitation and no-poach agreements and declare noncompete agreements per se illegal.[9]

On Jan. 9, 2020, the FTC held a public workshop at which legal scholars, economists and policy experts reviewed the current state of the law and economic literature on noncompete clauses in contracts between employers and employees.[10] Following the workshop, the FTC announced that it will take public comments on the issue until March 11.

Reports on the hottest job markets suggest noncompetes do not have a large effect on wage growth or employee mobility.

The Wall Street Journal recently published a list of the hottest U.S. job markets in 2019.[11] The journal worked with Moody's Analytics to assess the labor markets, ranking them according to the unemployment rate, labor force participation rate, job growth, labor force growth and wage growth.

Eight of out 10 cities on The Wall Street Journal's list are located in those states that enforce noncompete agreements. Three out of the eight cities are located in Texas and Florida, both of which have a strong legal culture of enforcing the agreements.

Given the arguments advanced by the opponents of noncompete agreements, one would not expect to see any Texas or Florida cities on the list of top cities that is partially based on wage growth. Moreover, one would expect California to dominate the list of the hottest job markets given its historic ban on noncompete contracts.

Instead, only two California cities make the list — San Francisco and San Jose. And while San Francisco has the highest wage growth of 7.1% on that list, its fellow California city, San Jose, shows only 2.7% wage growth, lower than Austin, Dallas and Orlando, Florida, which are all located within strong noncompete states. The fact that there is a big difference in wage growth between San Francisco and San Jose, although noncompetes are banned in both of them, suggests that factors other than noncompete enforcement have a large effect on employees' wage growth.

Other reports also tend to support that the link between noncompete enforcement and wage growth or employee mobility is negligible. Last month, the Milken Institute, a nonprofit, nonpartisan think tank issued a report titled "Best-Performing Cities 2020: Where America's Jobs Are Created and Sustained," which ranked large metropolitan areas based on the long-term and short-term job growth, long-term and short-term wage growth, and high-tech gross domestic product growth.[12]

According to the report, employment and wage and salary growth were heavily weighted because of their critical importance to community vitality and because those metrics signaled the quality of the jobs being created and retained.

Consistent with The Wall Street Journal's list, San Francisco (where noncompete agreements are banned) and Austin and Orlando (where noncompete agreements are frequently enforced) appeared on the Milken Institute's list of the top 10 performing cities, in part based on the wage growth in each of such cities. If the argument that noncompete agreements suppress wage growth held true, one would not expect to see Austin or Orlando on the list of the top-performing cities.

The findings in both The Wall Street Journal and the Milliken report tend to disprove the common arguments against noncompete agreements causing wage suppression or negatively affecting job mobility and entrepreneurship — arguments first advanced in the 2016 White House report.

Conclusion

The recent independent reports regarding the top-performing cities around the country suggest that factors other than noncompete enforcement have a far greater effect on employee mobility and wage growth. Many employees may be drawn to Texas and Florida despite their noncompete policies because of the high demand for skilled workers, the low cost of living, and the absence of state income tax.

Employees may be willing to give up some of the freedom with respect to post-employment restrictions in exchange for economic benefits that come from living in cities with low cost of living and no state income tax. In such jurisdictions, as the demand for skilled workers increases, so do the wages, driven by employers' competition for talent.

Contrary to the arguments made by the opponents of noncompete agreements, most such contracts do not require employees to change the industry in which they are employed due to post-employment restrictions. For example, both Texas and Florida, require that the noncompete agreements be reasonable in their geographic scope, and will not enforce agreements that constitute an industry-wide ban. Thus, while employees in those states may be subject to some restrictions in terms of what they can do after they leave their employers, those restrictions are not so broad as to deprive employees from earning a living in their chosen profession.

Another reason as to why noncompete agreements may not affect employees' wages or mobility is because a lot of skilled employees can now work remotely, which means that they can easily find a job that allows them to continue living in the geographic area where they lived while working for their former employer, while working for a company that is outside the geographic area subject to the noncompete requirements.

Finally, while noncompete agreements do affect job mobility in that they restrict employees from taking certain types of jobs, such restraints are justified by businesses' needs to protect their intellectual property and confidential information from ending up in competitors' hands, which, in turn, allows companies to grow without the danger of being undercut by unfair competition, resulting in them hiring more employees.

In conclusion, while some reforms are needed for lower-wage employees with respect to noncompete agreements, a wholesale ban on such contracts because they negatively affect wage growth and employee mobility, is not supported by evidence and is not justified.

Leiza Dolghih is a partner and co-chair of the trade secrets and noncompete disputes practice at Lewis Brisbois Bisgaard & Smith LLP.

[1] https://www.huffpost.com/entry/jimmy-johns-non-compete_n_5978180?1413230622=.

[2] https://www.treasury.gov/resource-center/economic-policy/Documents/UST%20Non-competes%20Report.pdf.

[3] https://obamawhitehouse.archives.gov/sites/default/files/non-competes_report_final2.pdf.

[4] https://obamawhitehouse.archives.gov/sites/default/files/competition/noncompetes-calltoaction-final.pdf.

[5] https://www.congress.gov/bill/114th-congress/senate-bill/1504/text.

[6] https://www.congress.gov/bill/114th-congress/house-bill/2873/text.

[7] https://www.congress.gov/bill/114th-congress/house-bill/2873/text.

[8] https://openmarketsinstitute.org/wp-content/uploads/2019/03/Petition-for-Rulemaking-to-Prohibit-Worker-Non-Compete-Clauses.pdf.

[9] https://oag.ca.gov/system/files/attachments/press-docs/11%2015%2019%20Multistate%20FTC%20Non-Compete%20Letter%20FINAL.pdf.

[10] https://www.ftc.gov/system/files/documents/public_events/1556256/non-compete-workshop-transcript-full.pdf.

[11] https://www.wsj.com/articles/austin-nashville-rank-at-top-of-hottest-u-s-job-markets-

11582545600.

[12] https://milkeninstitute.org/sites/default/files/reports-pdf/BPC-2020%20Report.pdf.