Kluwer Competition Law Blog

UK Proposes Stricter Approach to Non-Compete Clauses

Nicholas Greenacre, Michael Engel (White & Case) and Peter Citron (Editor) (White & Case, Belgium) · Monday, May 29th, 2023

In a policy paper on "Smarter Regulation to Grow the Economy", the UK government has announced proposals to limit the duration of non-compete clauses in employment contracts to three months.

This proposal reflects the growing concern worldwide concerning the use of non-competes. Earlier this year, the FTC in the US took even more extreme action than the UK, by publishing a proposal to ban non-compete clauses completely.

What is the approach to non-competes in the UK?

There are currently no statutory restrictions on non-compete provisions in the UK. Under case law, non-competes will only be enforceable if they are no wider than reasonably necessary to protect a legitimate interest (e.g. protection of confidential information or customer contacts) and are not contrary to the public interest.

The UK courts have in the past enforced up to 12-month non-competes in employment contracts in certain sectors, particularly in case of non-competes imposed on founders or senior management. In other contexts, including partnership agreements and shareholder agreements, non-competes that apply for a longer duration have been enforced by the UK courts.

What are the proposals?

The UK government proposes to limit the duration of post-termination non-compete clauses in employment contracts to three months.

The three-month limit will only apply to non-competes in contracts of employment and the contracts of certain other workers who benefit from certain protections under UK employment law. The UK government does not propose to apply the limit to wider workplace contracts, such as partnership or shareholder agreements. This is on the basis that there are fundamental differences in the balance of bargaining power with these wider workplace contracts. Based on the consultation document, it appears that equity incentive documents, such as employee share option

agreements, would be considered a wider workplace contract as well.

There are carve-outs. The proposal will not limit or interfere with the employer's use of:

- Non-solicitation clauses;
- Paid notice periods or gardening leave; or
- Confidentiality clauses.

The proposal also will not affect the restrictions on former UK public sector employees under the UK business appointment rules. The proposal follows a consultation period between 4 December 2020 and 26 February 2021 that explored and ultimately rejected the following two alternatives:

- The complete prohibition of post-termination non-compete clauses; and
- Making post-termination non-compete clauses permissible only when the employer provides compensation for the period of restraint.

What are the drivers behind the UK reform?

The UK government estimates that there are around 5 million employees subject to non-compete clauses in Great Britain and that a typical duration is around 6 months.

Whilst recognising that non-compete clauses "*can play an important role in protecting businesses who invest in their staff*", the proposal claims that, "*unnecessarily burdensome clauses have become a default part of too many employment contracts, including where they fulfil no purpose*". The proposal states that non-compete clauses "*can inhibit workers from looking for better paying roles, and limit the ability of businesses to compete and innovate*".

The proposal's stated aims are to give "*UK workers greater freedom to switch jobs, apply their skills elsewhere and even earn a pay rise*". They also aim to "*provide a boost to the wider UK economy, supporting employers to grow their businesses and increase productivity by widening the talent pool, and improving the quality of candidates they can hire*".

Why no complete ban on non-competes?

In contrast to the US FTC's proposals, the UK government has ruled out a complete ban on non-competes. Following a review of "*available evidence, research, and literature*", the UK government considers that the risks and potential for unintended consequences could outweigh the potential benefits of a complete ban. While the UK government recognises that a complete ban could have "*a positive effect on competition and innovation*", it considers that "*there is some evidence to suggest that in certain circumstances, non-compete clauses can act as a mechanism to align incentives between workers and employers, and enable investments*".

What should employers do?

Employers should start to consider other ways they can protect their business interests once the

proposed limit comes into force.

In the UK, the most robust way of protecting an employer's business interests in an employment contract of a senior employee who holds valuable trade secrets is a long notice period combined with an express garden leave clause. A 12-month notice period is fairly typical for a C-suite executive.

Where a long notice period is not appropriate or cannot be agreed, then employers may consider including non-competes in wider workplace contracts. In particular, if equity incentive documents will ultimately be considered a "wider workplace contract" under the final legislation, then granting an option or other equity interest which includes a carefully drafted (and longer) non-compete in its terms might well be a sensible and enforceable alternative.

What is the proposed timetable?

The proposal states that the UK government intends to legislate "*when parliamentary time allows*". There is currently no clarity as to whether, if legislation does pass in this area, it will apply retroactively to existing employment contracts and contracts with workers and if so, whether pre-existing non-competes that apply for longer than 3 months will only be enforceable for 3 months after termination, or whether such non-competes will be unenforceable and void in their entirety.

To make sure you do not miss out on regular updates from the Kluwer Competition Law Blog, please subscribe here.

This entry was posted on Monday, May 29th, 2023 at 9:00 am and is filed under Labour market, United Kingdom
You can follow any responses to this entry through the Comments (RSS) feed. You can leave a response, or trackback from your own site.