

Noncompete agreements in employment contracts

Can regulation ensure that noncompete agreements benefit both workers and firms?

Keywords: noncompete agreements, employment law, wages, job mobility

ELEVATOR PITCH

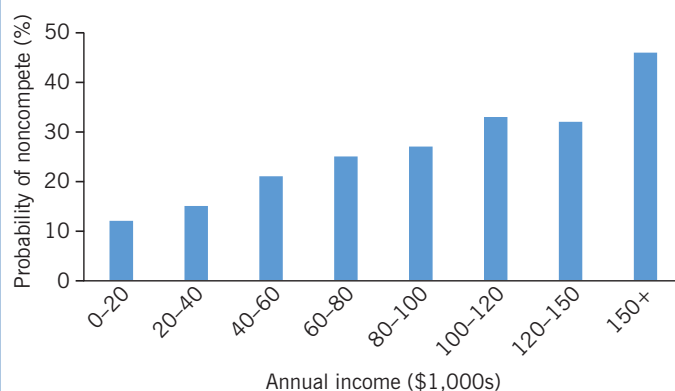
Labor market institutions that may weaken workers' bargaining leverage have received increased scrutiny in recent years. One example is noncompete agreements, which prevent workers from freely moving across employers, potentially weakening earnings growth. New data sources and empirical evidence have led policymakers to consider sharp restrictions on their use, especially among lower-income workers. These restrictions take many different forms, each of which has unique tradeoffs between the desire to protect workers while allowing firms to use noncompetes in cases where they may create social value.

KEY FINDINGS

Pros

- ⊕ Noncompete agreements can promote investments in intangible assets, such as research or worker training, that potentially benefit both employers and workers.
- ⊕ Empirical evidence supports the theory that noncompetes increase worker training and overall rates of corporate investment.
- ⊕ Noncompete agreements can help employers screen out job applicants who are more inclined to job-hop, reducing turnover and overall hiring costs.

Share of US workers with noncompete agreements



Source: Author's own compilation based on data reported in[1].

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Cons

- ⊖ By restricting workers' ability to change employers, noncompete agreements can shift bargaining power away from workers and hinder wage growth.
- ⊖ Most empirical studies show that the use and enforceability of noncompetes decrease wages, on average, with exceptions in some occupations.
- ⊖ Noncompete agreements can create spillover effects on workers and firms that do not sign them, and potentially reduce the overall competitiveness of labor markets.
- ⊖ Evidence suggests the negative wage impacts of noncompete agreements are disproportionately concentrated on more vulnerable and lower-income workers, including minorities and women.

AUTHOR'S MAIN MESSAGE

Economic theory suggests noncompete agreements have the potential to increase productive investments, but can also harm workers. Empirical evidence is similarly dichotomous, consistent with greater worker training and rates of corporate investment, but lower wages and job mobility on average. Though the harmful effects are often most salient, policymakers should aim to balance regulation that protects workers while still allowing the benefits of noncompetes in some contexts. Regulatory options include noncompete wage floors, transparent information requirements, and matching the timing of payments for noncompetes with the work restriction period.