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BLOG

Courts Unwilling to Condemn Franchise No-Poach Provisions Under the *Per Se* Rule

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More courts are declining to apply the *per se* rule to so-called "no-poach" or "no-hire" arrangements, at least at the pleading stage. In the franchise context, the recent decision involving Jiffy Lube in *Fuentes v. Royal Dutch Shell PLC*, is the latest data point. That court declined to commit to any standard of review pending discovery (an approach that seems to be trending), while other courts have rejected *per se* review, applying a quick look at the pleading stage instead (which allows some additional latitude in pleading relative to a full-blown rule of reason test). The difference is meaningful, including because a *per se* claim need not plead and prove power in a relevant market, nor does it allow the court to consider a defendant's countervailing procompetitive justifications.

Background

No-poach or no-hire arrangements are said to fix wages by restraining trade in the market for the supply of labor. In short, two or more companies competing *for labor talent* (even if they do not compete in end products or services) agree not to hire each other's employees, essentially restricting demand for labor and artificially limiting employee mobility and wages.

The DOJ and FTC's October 2016 Antitrust Guidance for Human Resource Professionals ("Guidance") provides that if such agreements are not "reasonably necessary to a larger legitimate collaboration between the employers," then they are "naked" restraints on wages or labor mobility and "deemed illegal without any inquiry into its competitive effects," *i.e.*, the DOJ and FTC consider it a *per se* violation. While the Guidance does not explicitly identify examples of naked restraints subject to *per se* review, it considers an agreement naked where it is unrelated to a legitimate collaboration and therefore not ancillary to joint procompetitive activity. By contrast, courts typically examine no-poach provisions that are ancillary to an agreement that creates otherwise non-existent trade (*e.g.*, joint ventures offering new products or services) or otherwise leads to efficient outcomes (*e.g.*, consulting) under a more probing standard (rule of reason or quick look).

Incidentally, the Guidance also announced that the DOJ will criminally prosecute new (e.g., beginning or continuing post-Guidance) naked no-poach conduct going forward. Although they have not yet publicly brought any such criminal charges, at least the DOJ remains very interested and involved in enforcement, including to intervene in

private actions. Meanwhile, state attorneys general and private plaintiffs have been active, particularly in the franchise context.

Recent No-Poach Decisions in the Franchise Context

No-poach provisions in the franchise context are particularly interesting because the provisions are contained in otherwise routine and lawful franchise agreements, typically restricting the ability of one franchisee to hire another franchisee's employees, while not restricting the ability of the employee to seek employment outside of the brand. Presumably, this protects the employing franchisee's training of and other investment in that employee so that another franchisee will not freeride. But, in somewhat of a twist, in most of the litigated examples, the franchisor itself owns and operates at least some of the franchise locations, meaning that the franchisor is not only vertical to its franchisees, but is also a direct horizontal competitor in the market for labor against its own franchisees.

For instance, *Ogden v. Little Caesar Enterprises* dismissed franchise no-poach claims and found *per se* review inappropriate because the plaintiff failed to allege any naked agreement to fix wages or divide the labor market. 393 F. Supp. 3d 622, 632-636 (E.D. Mich. 2019). The *Ogden* court held that merely alleging a horizontal restraint via a hub-and-spoke arrangement did not warrant *per se* treatment and it declined a quick look because that "framework still requires an equivalent amount of obviousness that is lacking here" especially "where the agreements display both vertical and horizontal components and therefore require a more in-depth analysis to determine unreasonableness." *Id.*

But other courts have found franchise no-poach restraints plausibly unlawful under a quick look approach even where they hold *per se* treatment inapplicable to the same claims because the arrangements cannot be described as lacking any procompetitive justification. *See Deslandes v. McDonald's USA, LLC*, No. 17 C 4857 2018 U.S. Dist. LEXIS 105260 at *18-20 (N.D. Ill. June 25, 2018) (holding *per se* treatment inappropriate because no-poach provision was ancillary to franchise agreement but finding alleged restraint plausibly unlawful under quick look analysis); *Yi v. SK Bakeries, LLC*, No. 18-cv-5627, 2018 U.S. Dist. LEXIS 220966, at *13 (W.D. Wash. Nov. 13, 2018) (finding plaintiff plausibly stated claim under quick look analysis but not under *per se* rule and noting that "[w]hile it may be easily ascertained that the agreement not to compete for employees has 'manifestly anticompetitive effects,' it is not clear that the Defendants' agreements 'lack any redeeming virtue'").

Still others have refused to eliminate any rules of decision at the pleadings stage, preferring for discovery to determine the appropriate resolution of the claims. For instance, in *Butler v. Jimmy John's Franchise, LLC*, the court declined at the pleadings stage to identify which rule applied but noted that if evidence shows franchisees are truly independent the quick look analysis is likely appropriate and, if the evidence of franchisee independence "is Herculean, then the *per se* rule might even apply." 331 F. Supp. 3d 786, 797 (S.D. Ill. 2018). A number of other courts adopted the same approach, including *Fuentes* where the court noted the alleged conspiracy "may, in part or in full, be characterized as 'horizontal,'" despite Jiffy Lube's arguments that it did not own any stores and the restraint was purely vertical in nature. *See also In re Papa John's Emple. & Franchisee Emple. Antitrust Litig.*, No. 3:18-CV-00825-JHM, 2019 U.S. Dist. LEXIS 181298, at *30 (W.D. Ky. Oct. 21, 2019) (declining to announce rule of analysis because plaintiffs did not tether viability of their claim to any one rule and noting "more factual development is necessary before a standard of review is selected"); *Blanton v. Domino's Pizza Franchising LLC*, No. 18-13207, 2019 U.S. Dist. LEXIS 87737, at *12-13 (E.D. Mich. May 24, 2019) (finding plaintiff plausibly alleged *per se* and quick look no-hire claims but requiring additional factual development).

Seemingly recognizing the confusion amongst litigants and various district courts, in March 2019, the DOJ filed a statement of interest in a number of civil federal fast food franchise no-poach actions, indicating that "[m]ost franchisor-franchisee restraints are subject to the rule of reason," and that "[w]hen no-poach restrictions within a franchise system warrant rule of reason analysis, they warrant full rule of reason analysis, not a 'quick look.'"

By contrast, three days later, the Washington attorney general argued in an amicus filing that such agreements are restraints among horizontal competitors and are subject to *per se* review. Amicus Curiae Brief by the Attorney General of Washington, No. 2:18-cv-00246-SAB, ECF No. 47 (E.D. Wa. Mar. 11, 2019).

Conclusion

There is heightened interest and litigation in the no-poach space. Given the uncertainty as to the appropriate antitrust standard in franchise cases—where a no-poach agreement is ancillary to an otherwise valid, procompetitive franchise agreement—complaints predominantly are surviving the motion to dismiss stage. As a result, defendants in such cases may be subjected to expensive and burdensome discovery, potentially impacting their settlement calculus while evaluating efforts to avoid protracted litigation.

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