Updates
July 05, 2022
Antitrust Challenge to McDonald’s No-Poach Restriction Evaluated Under the Rule of Reason

A federal judge in the U.S. District Court for the Northern District of Illinois has held that an antitrust challenge to a "hiring restriction [that] prevented" plaintiff employees "from taking a better-paying position with a rival McDonald's outlet" must be evaluated under the full rule of reason. In declining to apply per se treatment to the McDonald's hiring restriction, Judge Jorge L. Alfonso relied on the ancillary restraint doctrine, which states that "where the horizontal restraint is necessary in order for the product to exist at all, a restraint will not be judged per se unlawful but rather will be judged under the rule of reason." Here, the judge noted, "[e]ach time McDonald's entered a franchise agreement, it increased output of burgers and fries, which is to say the agreement was output enhancing and thus procompetitive."

Judge Alfonso also discussed three reasons why the restriction should be evaluated under the rule of reason, as opposed to the middle-ground "quick look" analysis, which the U.S. Supreme Court adopted in *California Dental Association v. Federal Trade Commission (FTC)*. The quick look standard generally applies to restraints where "an observer with even a rudimentary understanding of economics could conclude that the arrangements in question would have an anticompetitive effect on customers and markets." The three reasons are as follows:

- First, the court lacked "enough experience with no-hire provisions of franchise agreements to predict with confidence that they must always be condemned."
- Second, Judge Alfonso found that McDonald's had proffered sufficient procompetitive effects "to warrant full rule of reason analysis" including "the benefits of a franchise business model and the free-rider problem that can be expected with such a model." The defendant's expert opined that "the hiring restriction encourages franchisees to train their employees without fear that other outlets will free-ride on this training by hiring away employees."
- Third, he characterized "a provision of the franchise agreement that prohibited franchisees from hiring McDonald's Corp. employees within six months" as partly a vertical agreement between franchisor and franchisee because McDonald's Corp. does not own franchises in approximately 20 states. Vertical restraints are often (though not always) evaluated under the rule of reason following the Supreme Court's decision in *Leegin Creative Leather Products v. PSKS*.

The standard of review that should apply when no-poach arrangements are made as part of franchise agreements has been a subject of recent debate, even among various government antitrust enforcers. This decision can be seen as a victory for the approach that the U.S. Department of Justice (DOJ) Antitrust Division (the Division) advocated in amicus briefs filed in three class actions in the U.S. District Court for the Eastern District of Washington. There, the Division analogized no-poach commitments in franchise agreements to vertical territorial allocation agreements between manufacturers and distributors, which are governed by the rule of reason and not the per se rule. Where the Division finds no poach or wage-fixing agreements that are not reasonably related to a franchise or other legitimate venture, it applies the per se rule and prosecutes such agreements as criminal violations.

Businesses should implement trainings and review best practices to avoid even the appearance of improper discussions with competitors about labor and employment issues. Enforcers provide useful resources for businesses seeking to ensure that their employment practices follow the law, including the FTC's Antitrust Red Flags for Employment Practices. Even if compliance programs are able to deter the type of per se unlawful behavior that is subject to criminal penalties, the risk of expensive civil litigation in a rule of reason case should cause businesses to be cautious before imposing no-poach arrangements or similar labor market restraints even in franchisee or other agreements.

Authors

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