Nos. 22-2333 & 22-2334

IN THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

LEINANI DESLANDES AND STEPHANIE TURNER,	)	On Appeal from the United States District Court for the Northern District of Illinois, Eastern Division
Plaintiffs-Appellants,	)	
v.	)	Case Nos. 1:17-cv-04857, 1:19-cv-05524
MCDONALD'S USA LLC, MCDONALD'S CORPORATION, DOES 1-10,	)	The Honorable Jorge L. Alonso, District Court Judge
Defendants-Appellees.	)	

BRIEF OF *AMICI CURIAE* THE RESTAURANT LAW CENTER AND INTERNATIONAL FRANCHISE ASSOCIATION IN SUPPORT OF DEFENDANTS-APPELLEES AND AFFIRMANCE

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CIRCUIT RULE 26.1 DISCLOSURE STATEMENT

Appellate Court No. 22-2333, 22-2334

Short Caption: Leinani Deslandes v. McDonald's USA LLC et al.

To enable the judges to determine whether recusal is necessary or appropriate, an attorney for a non-governmental party or amicus curiae, or a private attorney representing a government party, must furnish a disclosure statement providing the following information in compliance with Circuit Rule 26.1 and Fed. R. App. P. 26.1.

The Court prefers that the disclosure statement be filed immediately following docketing; but, the disclosure statement must be filed within 21 days of docketing or upon the filing of a motion, response, petition, or answer in this court, whichever occurs first. Attorneys are required to file an amended statement to reflect any material changes in the required information. The text of the statement must also be included in front of the table of contents of the party's main brief. **Counsel is required to complete the entire statement and to use N/A for any information that is not applicable if this form is used.**

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Restaurant Law Center, International Franchise Association

(2) The names of all law firms whose partners or associates have appeared for the party in the case (including proceedings in the District Court or before an administrative agency) or are expected to appear for the party in this court:

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(3) If the party or amicus is a corporation:

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None

ii) list any publicly held company that owns 10% or more of the party's or amicus' stock:

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4) Provide information required by FRAP 26.1(b) – Organizational Victims in Criminal Cases:

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(5) Provide Debtor information required by FRAP 26.1 (c) 1 & 2:

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Attorney's Signature /s/ Gabriel K. Gillett Date: January 10, 2023 (new)

Attorney's Printed Name: Gabriel K. Gillett

Please indicate if you are *Counsel of Record* for the above listed parties pursuant to Circuit Rule 3(d). **Yes** X **No** ____

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N/A

Attorney's Signature /s/ Angelo I. Amador Date: January 10, 2023

Attorney's Printed Name: Angelo I. Amador

Please indicate if you are *Counsel of Record* for the above listed parties pursuant to Circuit Rule 3(d). **Yes** | **No** X

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INTEREST OF *AMICI CURIAE*[1]

The Restaurant Law Center is the only independent public policy organization created specifically to represent the interests of the food-service industry in the courts. This labor-intensive industry is comprised of over one million restaurants and other foodservice outlets employing over 15 million people—approximately ten percent of the U.S. workforce, making it the second-largest private-sector employers in the United States. Through regular participation in *amicus* briefs on behalf of the industry, the Restaurant Law Center provides courts with the industry's perspective on legal issues significantly impacting its members and highlights the potential impact of pending cases like this one.

The International Franchise Association ("IFA") is the world's oldest and largest organization representing franchising as a method of distribution, whose worldwide membership includes franchisors, franchisees and suppliers in all 50 states. Since 1960, IFA has educated franchisors and franchisees on beneficial methods and business practices to improve the operation of their businesses through franchising. IFA also advocates on behalf of franchisors and franchisees. Through its educational, public-policy, and government-relations programs, it protects, enhances and promotes franchising on behalf of more than 1,400 brands in more than 300 different industries, including

[1] All parties consent to the filing of this brief. No party's counsel authored this brief in whole or in part, and no money intended to fund preparing or submitting this brief was contributed by a party or party's counsel or anyone other than *amicus*, its members, or its counsel. *See* Fed. R. App. P. 29.

restaurants. Franchising includes over 733,000 franchise establishments, supports nearly 7.6 million jobs and contributes more than $674 billion to the U.S. economy.

Amici and their members have a significant interest in two important antitrust issues raised by this case—how to properly define a relevant product and geographic market for restaurant industry labor and how to evaluate ancillary restraints in the intrabrand context (*i.e.*, within franchise agreements). *Amici* therefore write to provide this Court with important industry-specific context related to those issues and to offer practical perspectives for why the decision below should be affirmed. *See Prairie Rivers Network v. Dynegy Midwest Generation, LLC*, 976 F.3d 761, 762-64 (7th Cir. 2020) (Scudder, J., in chambers).[2]

SUMMARY OF ARGUMENT

I. In the district court, Plaintiffs' claims were dismissed because they failed to plausibly plead a core element of a Section 1 claim premised on the rule of reason: defining a relevant product and geographic market in a way that comports with industry realities. This Court should affirm that decision and emphasize that, consistent with the Supreme Court's teachings, antitrust plaintiffs cannot flout that key requirement of their claim and proceed to discovery—which is famously burdensome in antitrust cases, which may

[2] Unless stated otherwise, internal quotation marks and citations are omitted and quotations are "cleaned up" to remove extraneous material and enhance readability without materially changing the text. *See* Jack Metzler, *Cleaning Up Quotations,* 18 J. App. Prac. & Process 143 (2017).

unfairly pressure defendants to settle baseless claims, and which may risk inviting even more meritless claims.

In any event, Plaintiffs here do not come close to meeting their burden to plead or prove the relevant market they now posit. Plaintiffs' attempt to define a single-brand product market for labor in the restaurant industry is inconsistent with well-established caselaw, divorced from practical realities, and has the potential to subject restaurant businesses to expensive and unwarranted litigation. Plaintiffs fail to recognize that, while there are distinctions between jobs at various types of franchised businesses such as quick-service restaurants and retail outlets, the positions are reasonably interchangeable for purposes of the antitrust laws. Plaintiffs also seek to define a national market for labor at McDonald's restaurants, but common sense, practical experience, and the evidence in the record make clear that the proper geographic market is local and limited to a reasonable commuting distance—as the Court recognized from the outset. Plaintiffs thus have neither pleaded nor proved a viable relevant market, which provides an independent basis for this Court to affirm.

II. A key issue underpinning this case is the standard that applies to ancillary restraints in agreements within a franchise system. Courts have recognized franchising as a positive economic force, including in the restaurant industry. In addition to contributing to the nation's economic output, franchised restaurants employ large swaths of Americans and are especially

notable for providing opportunities for upward mobility, including for women and historically disadvantaged groups.

The success of the franchising model depends in significant part on intrabrand ancillary restraints. Such restraints enable cooperation that, in turn, promotes interbrand competition. This Court and others have long recognized the importance of ancillary restraints that reduce overall costs and ensure the quality and consistency of the franchised brand. That consistency is critical to the success of all franchisees, as trust is often the reason customers choose to patronize franchises over unknown establishments. Labor-related ancillary restraints may also incentivize investment in employee training and discourage free-riding between franchisees who otherwise could be tempted to hire already trained employees from another location. This investment leads to a better product and better positions franchisees, franchisors, and employees for interbrand competition in a vibrant market. Plaintiffs' misguided attempt to undermine the viability of ancillary restraints—no matter how fair, reasonable, and pro-competitive—would hurt franchised restaurants and in turn harm competition and the U.S. economy.

ARGUMENT

I. Plaintiffs' Failure To Plead Or Prove A Relevant Market That Fits Restaurant Industry Realities Is An Additional Reason To Affirm.

A. This Court Should Emphasize That Pleading A Plausible Relevant Market Is Required To State A Section 1 Claim.

Under this Court's well-established case law, ancillary restraints are evaluated under the rule of reason framework, which requires the plaintiff to

show that an agreement "has an anticompetitive effect on a given market within a given geographic area." *Agnew v. NCAA*, 683 F.3d 328, 335 (7th Cir. 2012); *see Polk Bros., Inc. v. Forest City Enters., Inc.*, 776 F.2d 185, 188-89 (7th Cir. 1985). Defining a relevant market in which the defendant's behavior had an allegedly anticompetitive effect is essential: it "is the existence of a commercial market that implicates the Sherman Act in the first instance." *Agnew*, 683 F.3d at 337.

"Without a definition of the market there is no way to measure the defendant's ability to lessen or destroy competition." *Ohio v. Am. Express Co.*, 138 S. Ct. 2274, 2285 (2018). Without a relevant market, there is no basis to determine whether the defendant exercised the requisite market power necessary for a cognizable claim under Section 1 of the Sherman Act. *See, e.g.*, *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877, 885-87 (2007); *Marion Diagnostic Ctr., LLC v. Becton Dickinson & Co.*, 29 F.4th 337, 348 & n.11 (7th Cir. 2022) (noting rule of reason equates with "an inquiry into market power and market structure designed to assess a restraint's actual effect").

A relevant market has both a geographic and a product component. To determine the boundaries of the "product market," one determines "the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it." *Sharif Pharmacy, Inc. v. Prime Therapeutics, LLC*, 950 F.3d 911, 918 (7th Cir. 2020). To determine the boundaries of the "geographic market," one examines the market area "to which the purchaser can practicably turn for supplies." *Republic Tobacco Co. v.*

N. Atl. Trading Co., 381 F.3d 717, 738 (7th Cir. 2004). In making these market determinations, the "antitrust statutes require a 'pragmatic' and 'factual' approach" because the "market must 'correspond to the commercial realities of the industry.'" *Sharif*, 950 F.3d at 917. Accordingly, "[a] properly defined market excludes other potential suppliers (1) whose product is too different (product dimension) or too far away (geographic dimension) and (2) who are not likely to shift promptly to offer defendant's customers a suitably proximate (in both product and geographic terms) alternative." *Id.* (citing Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law: An Analysis of Antitrust Principles and Their Application* ¶ 530a (4th ed. 2019)).

Here, there is no doubt that Plaintiffs have failed to allege or otherwise establish a relevant market under the rule of reason framework. Plaintiffs did not even attempt to plead a rule of reason claim much less undertake the necessary effort to marshal factual evidence to demonstrate the relevant product or geographic market for their labor. Plaintiffs' unsupported references to "worker pay nationwide" or "practical indicia" about training (App. Dkt. 47, Pls.' Opening Br. 31, 33-34), plainly do not satisfy the "pragmatic" and "factual" approach that the "antitrust statutes require," or demonstrate that a purported nationwide market for labor at McDonald's restaurants "correspond[s] to the commercial realities of the industry" at issue. *Sharif*, 950 F.3d at 917; *see also Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210, 219 (D.C. Cir. 1986) (rejecting single-brand market premised on supposed uniqueness); *Pastore v. Bell Tel. Co. of Pennsylvania*, 993 WL 664548, at *6 (W.D. Pa. Sept.

22, 1993), *aff'd*, 24 F.3d 508 (3d Cir. 1994) (rejecting single-brand market based on "technological uniqueness of the … product").

This Court should not allow plaintiffs to flout this Court's established framework for evaluating Section 1 claims under the rule of reason. Instead, this Court should follow its own well-established precedent, which holds that plaintiffs asserting Section 1 claims under the rule of reason framework must plead a plausible relevant market to survive a motion to dismiss.

Allowing improperly pleaded antitrust claims to survive a motion to dismiss has real and substantial negative consequences. "Under the rule of reason, the factfinder weighs all of the circumstances of a case in deciding whether a restrictive practice should be prohibited as imposing an unreasonable restraint on competition." *Marion Diagnostic*, 29 F.4th at 348. As a result, rule of reason cases may involve "an unbounded inquiry under antitrust law, with … famously burdensome discovery." *F.T.C. v. Actavis, Inc.*, 570 U.S. 136, 176-77 (2013) (Roberts, J., dissenting); *see also, e.g.*, *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 558-59 (2007) (collecting authorities "discussing the unusually high cost" and "extensive scope of discovery in antitrust cases"); *Polygram Holding, Inc. v. FTC*, 416 F.3d 29, 34 (D.C. Cir. 2005) ("Litigation costs are the product of vague rules combined with high stakes, and nowhere is that combination more deadly than in antitrust litigation under the Rule of Reason." (quoting Frank H. Easterbrook, *The Limits of Antitrust*, 63 Tex. L. Rev. 1, 12-13 (1984))). Meaningfully scrutinizing an antitrust complaint at the outset to ensure the plaintiff's proposed market is

plausible—and if so that it is appropriately circumscribed—is the best way to prevent that burden from being unfairly foisted on defendants. *See, e.g.*, *Twombly*, 550 U.S. at 558-59 ("Some threshold of plausibility must be crossed at the outset before a patent antitrust case should be permitted to go into its inevitably costly and protracted discovery phase.").

When combined with the prospect of treble damages, the potential for subjecting defendants to costly and unpredictable litigation may attract frivolous claims by plaintiffs' lawyers seeking to leverage the *in terrorem* effect into a settlement. *See* Maurice E. Stucke, *Does the Rule of Reason Violate the Rule of Law?*, 42 U.C. Davis L. Rev. 1375, 1384 & n.35 (June 2009). Indeed, it was in the context of a Section 1 case that the Supreme Court first held that pleadings must render the claim "plausible," rather than merely "conceivable," after noting that "the threat of discovery expense will push cost-conscious defendants to settle even anemic cases before reaching those proceedings," *Twombly*, 550 U.S. at 559, 570-71.

These important concerns can be substantially mitigated, however, if this Court affirms the decision below and makes clear that a Section 1 claim under the rule of reason will be dismissed if the complaint fails to plead a relevant market and power in that market, as Plaintiffs have failed to plead here.

B. Restaurant Industry Employers Compete For Workers Across Brands And Across Industries.

Plaintiffs have suggested that the relevant market for their labor is limited to McDonald's stores. *See* Pls.' Opening Br. 33-34. The assertion of an exceedingly narrow market for labor has no basis in either law or fact.

As a matter of law, plaintiffs cannot establish that a single restaurant brand's locations constitute a relevant market for labor. *See, e.g.*, *Sheridan v. Marathon Petroleum Co.*, 530 F.3d 590, 595 (7th Cir. 2008) (rejecting assertion that single-brand franchise system was a market); *Queen City Pizza, Inc. v. Domino's Pizza, Inc.*, 124 F.3d 430, 430 (3d Cir. 1997) (same); *Domed Stadium Hotel, Inc. v. Holiday Inns, Inc.*, 732 F.2d 480, 488 (5th Cir. 1984) (same). "It is an understatement to say that single-brand markets are disfavored," one court explained, noting that from "nearly the inception of modern antitrust law, the Supreme Court has expressed skepticism of single-brand markets." *In re Am. Express Anti-Steering Rules Antitrust Litig.*, 361 F. Supp. 3d 324, 343 (E.D.N.Y. 2019) (citing *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 393 (1956) and collecting cases).

Restaurant industry work does not come close to satisfying the limited circumstances in which a single-brand market may exist. *See Eastman Kodak Co. v. Image Tech. Servs., Inc.*, 504 U.S. 451, 481 (1992) (involving aftermarket for replacement parts for a specific brand's products). Employees at a particular chain of restaurants are not proverbially "locked in to purchasing a subsequent product or service," even if they have a particular affinity for

working for one employer over another. *See Right Field Rooftops, LLC v. Chicago Baseball Holdings, LLC*, 87 F. Supp. 3d 874, 887-88 (N.D. Ill. 2015) ("While … there are some die-hard Cubs fans that would never attend a White Sox game, that does not mean that Cubs games constitute their own market.").

Nor can Plaintiffs here establish as a matter of fact that employment at a single brand's locations qualify as a relevant market for purposes of the antitrust laws. Plaintiffs cannot credibly claim that there are "no interchangeable substitutes" for their jobs at McDonald's. *Id.* To the contrary, Plaintiffs' jobs at a restaurant chain like McDonald's can be considered a reasonable substitute for a job at another restaurant chain or at other retail establishments where workers engage in the same core job duties.

Even if those jobs are not identical, they are sufficiently similar to be reasonably interchangeable for purposes of determining the relevant market for labor under the antitrust laws. *See Brown Shoe Co. v. United States*, 370 U.S. 294, 325-28 (1962) (rejecting attempt to define shoe markets based on "price/quality" and "age/sex" distinctions). As the Second Circuit explained in rejecting an attempt to define a relevant market as "labor services provided by nonmanagerial Hotel employees working or seeking work in Marriott-managed hotels in New York City," that definition "cannot plausibly be said to encompass all interchangeable substitute products." *Madison 92nd St. Assocs., LLC v. Courtyard Mgmt. Corp.*, 624 F. App'x 23, 29 (2d Cir. 2015). "If other, non-Marriott-managed hotels in New York City suddenly doubled the wages

they paid to their employees," the court noted, "it is beyond doubt that Marriott hotels would have to increase their wages to retain any employees." *Id.*

The same is true in the restaurant industry. There are over three million fast food and counter service jobs in the United States alone,[3] and many more positions as servers, managers, cleaners, delivery drivers, and other positions that are similar to jobs available at other retail establishments.[4] Competition among restaurant employers to fill those positions is fierce. At one point in 2021, Pizza Hut had 22,000 vacancies, Starbucks, had over 18,000 vacancies, and McDonald's had over 12,000 vacancies.[5] At the same time, restaurant businesses were competing with businesses in other industries for employees. *See* App. Dkt. 67, Defs.' Response Br. 54-55 (citing record evidence showing competition for workers between McDonald's, "Burger King, Arby's, Taco Bell, Culver's, Wendy's, Chipotle, Walmart, Amazon, Target, and the like").[6] This prompted many restaurants to raise wages—pay for hourly workers in leisure and hospitality jumped 13% from a year earlier—offer signing bonuses, and

[3] Bureau of Labor Statistics, Occupational Employment and Wage Statistics (May 2021), https://www.bls.gov/oes/current/oes353023.htm#nat.

[4] *See* Nat'l Restaurant Ass'n, *Summer Hiring Likely to be Challenged by a Tight Labor Market* (May 25, 2022), https://restaurant.org/research-and-media/research/economists-notebook/analysis-commentary/summer-hiring-likely-to-be-challenged-by-a-tight-labor-market/.

[5] Andrew Hunter, *How the Restaurant Industry Is Competing for Talent*, HR Daily Advisory (July 6, 2021), https://hrdailyadvisor.blr.com/2021/07/01/competing-for-talent/.

[6] *See* Samantha Masunaga, *These Five Workers Left Restaurant Jobs in the Pandemic. Where are They Now?,* LA Times (May 23, 2022), https://www.latimes.com/business/story/2022-05-23/restaurant-industry-year-on-from-great-resignation; Andrew Chamberlain, *Restaurant Workers Explore Careers in New Industries During COVID-19*, Glassdoor (May 27, 2020) https://www.glassdoor.com/research/restaurant-server-new-jobs/.

increase "access to wider employment perks" such as "health insurance, money toward education, and better and more flexible hours."[7] Such moves were necessary for restaurants, including franchised chains, to attract and maintain employees when many similar positions were available to those same individuals from other employers.[8]

Of course, different brands and businesses differentiate themselves in the marketplace. For example, companies may have somewhat different products, training programs, operating methods, and human resources policies and procedures. But the lion's share of the training and experience gained by employees in one brand's system is largely transferable to another brand's system. The core job functions—such as taking orders, providing good customer service, operating a cash register, maintaining a clean work area, collaborating effectively with colleagues, and so forth—are similar across the restaurant industry and much of the retail sector. *See* Defs.' Response Br. 55 (citing testimony that plaintiffs were able to "leverag[e] their McDonald's experience to seek or obtain other jobs"). Those similarities reinforce that a single brand's locations do not qualify as a relevant market for purposes of the antitrust laws.

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[7] Hunter, *supra* note 5; Jane Black, *How to Make an Unloved Job More Attractive? Restaurants Tinker with Wages*, N.Y. Times (Sept. 20, 2021), https://www.nytimes.com/2021/09/20/dining/restaurant-wages.html.

[8] *See* Heather Haddon, *Restaurants Serve Up Signing Bonuses, Higher Pay to Win Back Workers,* Wall St. J. (Apr. 25, 2021), https://www.wsj.com/articles/restaurants-serve-up-signing-bonuses-higher-pay-to-win-back-workers-11619359201.

C. The Geographic Market For Restaurant Industry Workers Is Small And Local, Not Large Or National.

While Plaintiffs' proposed product market is too narrow, their proposed geographic market is far too broad. As the district court recognized: The notion that Plaintiffs "sell their labor in a national market . . . defies logic." Dkt. 372 at 20. The geographic area to which the "purchaser" (or, here, prospective employee) "can practicably turn for supplies" (or, here, jobs) is far more limited than the entire nation. *See Republic Tobacco*, 381 F.3d at 738. Instead, both case law and common sense limit the geographic market to a reasonable commuting distance. Therefore, there are "hundreds or thousands of local relevant [labor] markets" across the country in which McDonald's restaurants compete for labor against any number of other employers. Dkt. 372 at 21.

At least for the types of jobs at issue here, the evidence demonstrates that prospective employees look locally. Notably, "92% of McDonald's employees work within ten miles of home." Defs.' Response Br. 56. There is no reason to doubt that similar numbers hold for similar employers given the abundance of reasonably interchangeable positions they offer.

As the district court found—and this Court has previously recognized—it therefore "defies logic to suppose" that Plaintiffs "sell their labor in a national market." Dkt. 372 at 20; *see Sharif*, 950 F.3d at 917 (explaining that geographic markets can be "small" where local "convenience is important"). If a prospective employee can choose to work at a nearby McDonald's, Burger King, Arby's, Taco Bell, Culver's, Wendy's, Chipotle, Walmart, Amazon, or Target (*see*

Defs.' Response Br. 54-55), then she need not consider whether to look for a job farther away at any one of those employers. And even a prospective employee's strong feelings about wanting to work for a particular company over another would not transform a fundamentally local market for labor into something broader. *See, e.g.*, *Right Field Rooftops*, 87 F. Supp. 3d at 887-88.

At bottom, the geographic market for labor in the restaurant industry is far smaller than Plaintiffs suggest, and certainly does not encompass the entire country, an entire state, or all the locations of a national chain. That provides yet another reason to affirm the decision below, and to reiterate that a plaintiff's Section 1 claim premised on the rule of reason should be dismissed when she fails to adequately plead or prove a relevant geographic market as required.

II. Ancillary Restraints In Franchise Arrangements Are Important To The Restaurant Industry, Particularly For Quick Service And Fast Casual Chains.

A. Franchising Is Essential To The U.S. Economy, The Restaurant Industry, And A Diverse Group Of Individual Entrepreneurs.

Franchising involves a "franchisor, who establishes the brand's trademark or trade name and a business system, and a franchisee, who pays a royalty and often an initial fee for the right to do business under the franchisor's name and system."[9] This model works well because the franchisee has the performance incentives associated with individual ownership while

[9] Int'l Franchise Ass'n, *What is a Franchise?* (last accessed Jan. 10, 2023), https://www.franchise.org/faqs/basics/what-is-a-franchise.

being able to capitalize on existing brand recognition, infrastructure, and resources of the franchisor, who also provides ongoing support.

As evidenced by their prevalence across the American landscape, franchising has proven to be a successful business model and has become a "bedrock" of the nation's economy. *Queen City Pizza*, 124 F.3d at 440-41; *see also, e.g.*, *Susser v. Carvel Corp.*, 206 F. Supp. 636, 640 (S.D.N.Y. 1962) (explaining how franchises creates a "class of independent businessmen" by enabling "individuals with small capital to become entrepreneurs," which is "good for the economy"). Approximately 775,000 franchise establishments provide Americans with 8.2 million jobs and contribute $474.2B to the economy.[10] This success may reflect a basic collaborative bargain between franchisors and franchisees. The latter is able to operate a business with a well-known brand or proven business model, which is often less intimidating and risky than starting from scratch, while the former is able to monetize its brand and experience while utilizing outside investments by franchisees to facilitate quickly scaling and achieving national reach.

The success of franchising is apparent in the restaurant industry. As of 2021, franchises accounted for approximately 40% of "domestic foodservice sales."[11] Collectively, in 2021 there were an estimated 220,429 franchised

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[10] *See* Int'l Franchise Ass'n, *National Economic Impact of Franchising* (last accessed Jan. 10, 2023), https://franchiseeconomy.com/reports/national-report.pdf.

[11] Danny Klein, *Restaurant Franchising After COVID: A Story of Resiliency and Rebound*, QSR Magazine (Sept. 2022), https://www.qsrmagazine.com/reports/restaurant-franchising-after-covid-story-resiliency-and-rebound.

quick-service and full-service restaurants, which employed more than 4.7 million people (58% of employees of franchised businesses) and generated $334 billion in economic output.[12] Franchisors and franchisees in the restaurant industry come in all sizes—some have only a few locations, some operate on a regional level, and some operate globally, generating millions or even billions of dollars in revenue.

The restaurant industry, which features a number of companies that utilize the franchise business model, is a shining example of upward mobility. Eight in ten restaurant owners say their first industry job was an entry-level position.[13] Nine in ten restaurant managers say the same.[14] Indeed, as reflected in the record here, some McDonald's senior management started as crew members. *See, e.g.,* Dkt. 381-3 at 33, Dkt. 382-9. Restaurants also provide opportunities for historically disadvantaged communities. "Restaurants employ more minority managers than any other industry," and "41% of restaurant firms are owned by minorities – compared to 30% of businesses in the overall private sector." And restaurants provide immigrants with opportunities to work and own their own businesses.[15] This holds true in the franchise-restaurant context too, as people of varying backgrounds—including

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[12] Int'l Franchise Ass'n, 2022 Franchising Economic Outlook at 4, 5, 7, https://www.franchise.org/sites/default/files/2022-02/2022-Franchising-Economic-Outlook.pdf.

[13] Nat'l Restaurant Ass'n, National Statistics (last accessed Jan. 10, 2023), https://restaurant.org/research-and-media/research/industry-statistics/national-statistics/.

[14] *Id.*

[15] Americas Soc'y et al., *Bringing Vitality to Main Street: How Immigrant Small Businesses Help Local Economies Grow* (Jan. 2015).

women, immigrants, and historically underrepresented groups—use franchising as their first opportunity to set up their own business and claim their own piece of the American Dream.[16] The opportunities franchised restaurants provide are also particularly important during difficult economic times: franchised restaurants provided entry-level workers with "the highest wage growth during the pandemic," and the "number of unemployed people without a high school diploma is now the lowest in recorded history."[17]

For example, the history of Mister Softee ice cream trucks generally tracks the country's immigration patterns: the earliest franchisees in the 1960s largely consisted of immigrants from Ireland, Italy, and Greece; by the late 1990s "persons of Hispanic descent, particularly those from Puerto Rico, became some of the biggest franchise owners"; and today Mister Softee franchisees are increasingly from the Middle East.[18] And to highlight just one of many success stories: The Halal Guys started in 1990 as a "food cart on the

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[16] Dana Hatic, *Franchising a Restaurant, Explained,* EATER (May 8, 2017), https://www.eater.com/2017/5/8/14936008/how-to-franchise-restaurant-mcdonalds-arbys-subway ("Franchising also has a track record of providing an entry into business ownership for individuals who have immigrated to the United States"); Press Release, *McDonald's Announces Global Effort to Increase Demographic Representation of Franchisee Base* (Dec. 8, 2021), https://corporate.mcdonalds.com/corpmcd/our-stories/article/franchisee-diversity.html ("As of 2020, individuals from historically underrepresented groups, including those that identify as Asian, Black or Hispanic, accounted for 29.6% of all U.S. franchisees. Women also accounted for 28.9% of all U.S. franchisees."); *see also* Int'l Franchise Ass'n, *Immigrants Redefining the American Dream Through Franchising.*, (last accessed Jan. 10, 2023), https://www.franchise.org/blog/immigrants-redefining-the-american-dream-through-franchising.

[17] 2022 Franchising Economic Outlook, *supra* note 12, at 6.

[18] Daniela Galarza, *A Brief History of Mister Softee,* EATER (July 17, 2015), https://www.eater.com/2015/7/17/8956663/mister-softee.

corner of 53rd Street and Sixth Avenue in Manhattan" founded and operated by three men from Egypt who came to the United States and "quickly identified a demand in the area for quick and inexpensive halal meals on the go for Muslim taxi drivers."[19] The brand grew in popularity over the years, took its first steps towards franchising in 2014, and surpassed more than 100 stores worldwide in 2022.[20]

B. A Franchisor's Ability To Manage Its Brand—Including Through Ancillary Restraints—Is Critical To The Success Of The Business Model.

As noted above, the franchise business model utilized by a significant portion of the restaurant industry operates through a series of contractual relationships in which the franchisor licenses its trademark and business system to independent franchisees, who own and operate retail locations featuring the franchisor's name. Under this arrangement, each entity has its own role that capitalizes on its own skills and opportunities. Franchisees direct the day-to-day operations of their restaurants—for example, who to hire, and setting wages and schedules—while franchisors set standards to maintain brand uniformity and consistency—such as what food the restaurant serves and how it is prepared.[21]

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[19] Fiona Simpson, *From Food Cart To Global Franchise: The Halal Guys Continue Rapid Expansion Plans*, Forbes (Nov. 9, 2022), https://www.forbes.com/sites/fionasimpson1/2022/11/09/from-food-cart-to-global-franchise-the-halal-guys-continue-rapid-expansion-plans/.

[20] *Id.*

[21] *See generally What is a Franchise?*, *supra* note 9.

This arrangement is fundamental to the franchise business model. Indeed, under the federal Lanham Act and the Federal Trade Commission's Franchise Rule, a franchise must be identified or associated with the franchisor's trademark, and trademark licensors must maintain control over the use of their trademarks. *See* 15 U.S.C. § 1127; *see also Barcamerica Int'l USA Tr. v. Tyfield Importers, Inc.*, 289 F.3d 589, 598 (9th Cir. 2002) (explaining that "where a trademark owner engages in naked licensing, without any control over the quality of goods produced by the licensee," they risk abandoning their rights to that trademark).

Accordingly, "[c]ourts and legal commentators have long recognized" the importance of ancillary restraints, such as those incorporated in franchise agreements. *Queen City Pizza*, 124 F.3d at 440. These ancillary restraints govern many aspects of the franchisees' business operations, including where they can operate, the products they can sell, and their obligation to cooperate with each through, for example, joint advertising campaigns. As the Third Circuit explained, such restraints serve as "an essential and important aspect of the franchise form of business organization because they reduce agency costs and prevent franchisees from freeriding—offering products of sub-standard quality insufficient to maintain the reputational value of the franchise product while benefitting from the quality control efforts of other actors in the franchise system." *Id.* at 440-41.

The Seventh Circuit recognizes restraints as ancillary when they may "contribute to the success of a cooperative venture that promises greater productivity and output," acknowledging that "cooperation is the basis of productivity," that "is necessary for people to cooperate in some respects before they may compete in others," and that "cooperation facilitates efficient production." *Polk Bros.*, 776 F.2d at 188-89. Other circuits have adopted this standard. *See, e.g.*, *Aya Healthcare Servs., Inc. v. AMN Healthcare, Inc.*, 9 F.4th 1102, 1110-11 (9th Cir. 2021) (holding that an ancillary restraint allows businesses to "collaborate . . . for the benefit of [their customers] without cutting [their] own throat[s]"); *Rothery Storage*, 792 F.2d at 224 (finding "the challenged agreements are ancillary in that they enhance the efficiency of that union by eliminating the problem of the free ride"); *see Med. Ctr. at Elizabeth Place, LLC v. Atrium Health Sys.*, 922 F.3d 713, 726-27 (6th Cir. 2019) (surveying cases); *Phillips v. Vandygriff*, 711 F.2d 1217, 1229 (5th Cir. 1983).

This standard is easily satisfied when it comes to restraints in franchise agreements in the restaurant industry. As a contractual and practical matter, franchisees must follow standards implemented by the franchisor to ensure uniformity and consistency of the goods, services, and methods of operation—which in turn is necessary to sustain a uniform customer experience and protect the brand value for the benefit of both the franchisor and franchisees. Such consistency, loyalty, trust, and efficiency are hallmarks of franchises and

critical to their success.[22] Customers who patronize franchised outlets expect that their experience—including the food preparation and safety, customer service, and overall experience—will be consistent. Indeed, "[u]niformity of product and control of its quality cause the public to turn to franchise restaurants," *Burger King Corp. v. Stephens*, 1989 WL 147557, at *10 (E.D. Pa. Dec. 6, 1989), and therefore the value of the brand a franchisee chooses to affiliate with is directly impacted by a franchisor's ability to maintain consistency and quality. A bad experience at one location can be attributed to the franchise system as a whole and standards are therefore necessary to protect the business. Ancillary restraints within a franchise agreement thus not only protect a particular brand but also benefit interbrand competition by improving overall quality and customer service.[23]

In the restaurant industry, ancillary restraints in franchise agreements may also provide pro-competitive benefits by fostering intrabrand cooperation. One major benefit to being a franchisee is the built-in support network of other franchisee operators, who can provide important advice, best practices, and

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[22] *See National Economic Impact of Franchising, supra* note 10.

[23] *See* Roger D. Blair & Francine Lafontaine, *The Economics of Franchising* 117 (Cambridge University Press, 2011) (noting that "it's the consistency of the system's operation, service, and product quality that attracts customers and induces loyalty: customers become loyal if the experiences they enjoy at diverse units of these chains routinely meet their expectations"); Benjamin Klein, *Transaction Cost Determinants of 'Unfair' Contractual Arrangements*, The American Economic Review, Vol. 70, No. 2, at 356-63, 358-59 (1980) (noting that "there is an incentive for an individual opportunistic franchisee to cheat the franchisor by supplying a lower quality of product than contracted for" and that "depreciates the reputation and hence the future profit stream of the franchisor"); *see generally* Defendant-Appellees' SA 131-34.

other assistance.[24] The franchisee also benefits from the franchisor, which provides the franchisee with "an entire system for operating the business" and may provide "site selection and development support, operating manuals, training, brand standards, quality control, a marketing strategy and business advisory support."[25] Ancillary restraints in franchise agreements can facilitate this pro-competitive collaboration by laying the foundation for trust between franchisees as well as between franchisees and franchisors.[26] In turn, that benefits franchisees, franchisors, their employees and customers, and the U.S. economy.

Labor-related ancillary restraints, in particular, can be pro-competitive. Achieving uniformity in a brand's system, methods, and standards requires investing significant resources in training employees, particularly for managers and supervisors. If a franchisee could avoid costs by hiring trained employees

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[24] *See, e.g.*, Defendants' Opposition to Plaintiffs' Motion for Class Certification at 4, *Conrad v. Jimmy John's Franchise LLC*, 2020 WL 5834961 (S.D. Ill. July 23, 2021), ECF No. 136 (citing evidence that "[f]ranchise owners view one another as partners with a shared interest in promoting and protecting the brand, and they work together to ensure customer expectations are met, which can include collaborating on local marketing events or large catering orders, sharing bread or chips with a franchisee running low, or sending one of their own employees to cover an open shift at a nearby franchisee's restaurant."); *see also* David Smith, *Iranian Immigrant Thrives as Franchisee*, Immigrant Business (July 12, 2016), https://www.immigrantbiz.org/iranian-immigrant-thrives-as-franchisee/; Hatic, *supra* note 16 (describing franchisees seeking advice from each other).

[25] *What is a Franchise?, supra* note 9.

[26] *See* Press Release, *McDonald's Announces Global Effort to Increase Demographic Representation of Franchisee Base, supra* note 16 ("McDonald's will significantly expand its franchisee recruiting and training efforts for all backgrounds, including for historically underrepresented groups, … to support newly recruited franchisees and the broader System. In the U.S., McDonald's also plans to harness the power of its System to support new franchisees through access to cross-functional resources and mentoring from experienced franchise owners, among other programs.").

away from a franchisor or other franchisees, such "free riding" would reduce all franchisees' incentives to invest in training. In turn, that may reduce the number of properly trained employees, detract from the customer experience, and lead customers to have negative associations with a brand. A franchisee's ability to find and keep well-trained employees thus benefits both the employing franchisee and other franchisees in the system by helping ensure customers have positive experiences in stores and positive associations with a brand. Likewise, restraints on employees—particularly skilled managerial and salaried employees who are critical to managing operations, supervising and training other employees, and maintaining high levels of service and customer satisfaction—can be important to the success of both franchisors and franchisees by incentivizing investment, limiting free-riding, and promoting cooperation and trust within the brand.

Finally, it is worth noting that existing rules and regulations require disclosures that permit employees to make informed decisions when choosing whether to work at franchised restaurants. For example, the Franchise Disclosure Document contains, among other things, the franchisor's obligations regarding the hiring and training of employees and the components of the franchisor's training program. *See* 16 C.F.R. §§ 436.5(k)(3)(v), (k)(7)(i). These disclosures allow for the market to provide an important check on impermissibly restrictive ancillary restraints, and permit individuals choosing among multiple possible employers to take any ancillary restraints into account. Meanwhile, in industries like restaurants where competition for labor

is fierce, ancillary restraints can encourage internal promotion, protect investments in training, and limit free-riding without unduly restricting employee mobility.

CONCLUSION

For the foregoing reasons, *amici curiae* respectfully urge this Court to affirm the judgment below.

Dated: January 10, 2023

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

I hereby certify that this document complies with the word limit of Federal Rule of Appellate Procedure 29(a)(5) and Circuit Rule 29 because, excluding the parts of the document exempted by Federal Rule of Appellate Procedure 32(f), this document contains 5,840 words. This document complies with the typeface requirements of Federal Rule of Appellate Procedure 32(a)(5) and the type-style requirements of Federal Rule of Appellate Procedure 32(a)(6) because this document has been prepared in a proportionally spaced typeface using Microsoft Office Word 365 in 12 point Bookman Old Style font for text and 11 point Bookman Old Style font for footnotes.

Dated: January 10, 2023

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CERTIFICATE OF SERVICE

I, Gabriel K. Gillett, an attorney, hereby certify that on January 10, 2023, I caused the **Brief Of *Amici Curiae* The Restaurant Law Center And International Franchise Association In Support Of Defendants-Appellees And Affirmance** to be electronically filed with the Clerk of the Court for the United States Court Of Appeals for the Seventh Circuit by using the CM/ECF system. I certify that all participants in this case are registered CM/ECF users and that service will be accomplished by the CM/ECF system.

Pursuant to ECF procedure (h)(2) and Circuit Rule 31(b), and upon notice of this Court's acceptance of the electronic brief for filing, I certify that I will cause fifteen copies of the above cited brief to be transmitted to the Court via UPS overnight delivery, delivery fee prepaid within five days of that date.

Dated: January 10, 2023

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