Franchise Law Journal

STATEMENT OF IDENTIFICATION

Franchise Law Journal (ISSN: 8756-7962 (print); 2163-2154 (online)) is published quarterly, by season, by the American Bar Association Forum on Franchising, 321 North Clark Street, Chicago, Illinois 60654-7598. *Franchise Law Journal* seeks to inform and educate members of the bar by publishing articles, columns, and reviews concerning legal developments relevant to franchising as a method of distributing products and services. *Franchise Law Journal* is indexed in the *Current Law Index* under the citation Franchising.

Franchise Law Journal

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From the Editor-in-Chief

John M. Doroghazi*

Mr. Doroghazi

Welcome to the Doroghazi Era of the *Franchise Law Journal*.[1] My predecessor Dan Oates[2] left me a well-oiled machine, and I will certainly succeed as Editor-in-Chief if I can run the *Journal* half as well as he did for the last three years. I would also like to thank our departing editors Marlén Cortez Morris and Larry Weinberg for their many years of service and to welcome new Article & Topics Editors Maisa Frank, Jared Miller, Aaron-Michael Sapp, and Vanessa Wheeler.

We have a great slate of articles for you this edition. First up is a thorough argument by Thomas J. Collin why no-hire clauses in franchise related

1. My first idea for this column was to revolve the editorial around the Ship of Theseus paradox and how even though the *Journal*'s editorial board and the Editor-in-Chief change over time, the *Journal* remains. *See, e.g.*, G. Robert Blakely, *Time-Bars: RICO Criminal and Civil-Federal State*, 88 Notre Dame L. Rev. 1581, 1627 n.65 (2013) (providing detailed background of this philosophical question); *see also WandaVision: The Series Finale* (Disney+ 2021) (where two versions of the android Vision have a conversation about the Ship of Theseus and what it means for their identity). But attempting to frame my introductory editorial around a philosophical concept is both pretentious and, more importantly, would have been received like Dennis Miller on Monday Night Football. *See* Mike Thomas, *Why Did Monday Night Football Have Comedian Dennis Miller in the Booth for Two Years*, Sportscasting (Dec. 21, 2020), https://www.sportscasting.com/why-did-monday-night-football-have-comedian-dennis-miller-in-the-booth-for-two-years (explaining how the Dennis Miller era saw some of the lowest ratings ever for Monday Night Football).

2. Dan had incredibly kind words for me in his parting editorial. *See* Dan Oates, *From the Editor-in-Chief*, 41 Franchise L.J. iv, vi (2021). Aside from already serving as a sounding board and resource during the peaceful transition of power between Editors-in-Chief, Dan is my oldest friend in the Forum. I have another former captain of the *Journal*, Bethany Appleby, to thank for that. She knew that two lanky guys from opposite sides of the country with a shared love of many things that some would consider to be nerdy (i.e., *Star Wars*, *Lord of the Rings*, and comic books movies) would get along exceptional well, and she introduced us at the Forum on Franchising held in Seattle. I am also guessing that some of you are wondering why I am putting my tribute to Dan in a footnote. Two reasons. First, I didn't think that you all wanted to read an opening editorial that was a Dan Oates love-fest. Second, Dan loves footnotes much more than any person really should. So it is only fitting that my comments about him appear in a footnote.

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employment contracts do not violate the Sherman Act in his article entitled *No-Hire Clauses—Ancillary Restraints for Protection of Brand Goodwill*.

Next up is an article by two *Journal* veterans. Former Editor-in-Chief Chris Bussert and current Topic & Article Editor Bill Bryner have teamed up to write a timely article on recent trademark decisions from the United States Supreme Court entitled *The Sleeping Giant Awakens: Three 2020 Trademark Decisions from the United States Supreme Court, and How They May Affect Franchising*.

While the restaurant industry was moving towards ordering food for delivery by Internet or app before March 2020, the COVID-19 pandemic caused greatly accelerated this shift. Now, seemingly every restaurant offers a way to order food electronically. James Egle and Isaac Brodkey have offered a thoughtful examination of the interplay between this paradigm shift and franchise territorial relationships in *Encroachment in the Era of Digital Delivery Platforms: Impact of Delivery Apps on Brick and Motor Exclusive Territories*.

Our next two articles touch on trademark related issues, with Tom Vanderbloemen and Vincent Frantz telling us *The Untold Story of the Concurrent Use Trademark Registration*, and Jeff Wolf and Amy Heiserman providing an update on the current state of the law for proving post-termination harm to goodwill in their article *Goodwill Hunting: The Challenges in Proving Harm to Franchisor Goodwill in Termination-Related Disputes*.

Finally, Alan Adcock and a cadre of his colleagues from the Tilleke & Gibbins firm have written an informative and useful overview of franchise law issues in Cambodia, Laos, Myanmar, Thailand, and Vietnam in the article *An Overview of Franchising Law in Southeast Asia*.

Rounding out the slate is a great set of Currents from Matthew Gruenberg, David Harford, and Vanessa Wheeler, the 2021 Edward Wood Dunham Rising Scholar Award Winner.

Knowing what is in this edition, the real question you are probably asking yourself is why should anyone devote their time to reading these articles? Or studying franchising in general? There are the obvious answers. Anything from a love of the almost myriad issues that spring from a seemingly simple business and legal structure to "I needed the CLE credits" to "it pays the bills." But I propose another, much more practical answer: trivia night "fortune and glory."[3] On September 16, 2021, I attended the "Rated-R Trivia Night"[4] at the Kinsmen Brewing Company in Milldale, Connecticut[5] with my wife and another couple. Rated-R Trivia is a popular event, so we prepared to face off against almost twenty teams. After settling on our team name (the St. Lunatics,)[6] the contest began and we were off to a hot start. The St. Lunatics were in sole possession of first place after the first two rounds.

3. Henry Jones, Jr., Indiana Jones and The Temple of Doom (Paramount Pictures 1984).

4. Rated-R Trivia, Facebook (Sept. 16, 2021), https://www.facebook.com/RatedRCT/?fref=tag. It appeared to be Rated R because the host is named Ryan and he swore a lot. All of the trivia questions themselves were quite PG.

5. Kinsmen Brewing, https://kinsmenbrewing.com/newsite.

6. I grew up Missouri and attended law school in St. Louis. For those who are not immersed in mid-2000's popular culture, "St. Lunatics" is the name of a rap group from St. Louis

The next round required us to name as many items in a certain category as we could in one minute. The category was national pizza chains. Our team earned the most points, aided by my ability to think of every franchised pizza brand I have come across in my many years of franchise case law research, reading *Journal* and *Franchise Lawyer* articles, and attending the Annual Forum on Franchising. The next round was not for points. Instead, the winning team in that round took home a set of Tito's Vodka bandanas and Kinsmen pint glasses. The sole question in the round was to guess, without going over, how many Domino's Pizza locations there are in the United States. Everyone at the table turned to me. Working backwards and relying on my franchise knowledge, I explained that Subway had over 20,000 U.S. locations and that it was the largest restaurant chain by location count.[7] I then explained that I had read various articles over the years saying that there were more Subway locations in the country than many of the other top franchise chains combined.[8] My wife then told me that this wasn't a test where I needed to show my work and the clock was ticking, so I needed to just give an answer. I said, my guess was that there are approximately 5,500 Domino's in the country, but that we should guess low at 3,500, just to be safe. We submitted our answer, and a few minutes later, Ryan, our "Rated R" host, came back on the microphone. He explained that all but one team had gone over and that the correct answer is that there are 6,355 Domino's locations in the United States.[9] The triumphant St. Lunatics were handed free bandanas and pint glasses.[10] So if the traditional answers to "why study franchising" don't pique your interest, read the *Journal* to prepare yourself for earning sweet trivia night swag!

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comprised of Nelly, Ali, Murphy Lee, Kyjuan, and City Spud. *See* Kevin C. Johnson, *St. Lunatics Feud Signals an End to St. Louis' Original Hip-Hop Dynasty*, St. Louis Post Dispatch (Feb. 8, 2021), https://www.stltoday.com/entertainment/music/kevin-johnson/st-lunatics-feud-signals-an-end-to-st-louis-original-hip-hop-dynasty/article_ddbaff17-c0c5-5368-aca8-5c398f07c2cb.html (providing general overview of group's history and explaining current social media dispute over who founded the group).

7. To be precise, there are 22,201 Subway restaurants in the United States. *See The QSR Big List*, QSR, https://www.qsrmagazine.com/content/qsr50-2021-top-50-chart (last visited Sept. 15, 2021) [hereinafter Big List].

8. Chris Morran, *Subway Now Outnubmers 30 of the 50 Largest Fast Food Chains . . . Combined*, Consumerist (Aug. 21, 2013), https://consumerist.com/2013/08/21/subway-now-outnumbers-30-of-the-50-largest-fast-food-chains-combined.

9. Big List, *supra* note 7.

10. You might be wondering how the St. Lunatics fared in their quest for overall Rated R Trivia glory. Sadly, we struggled in the penultimate round (identifying household items from extreme closeup pictures), then whiffed when asked to identify the largest breed of dog in the final round (which is evidently the Irish Wolfhound), leading to a third-place finish.

No-Hire Clauses—Ancillary Restraints for Protection of Brand Goodwill

*Thomas J. Collin**

Mr. Collin

No-hire clauses in franchise agreements, often referred to as no-poaching clauses, are the subject of class actions directed against a number of franchise systems, from McDonald's, to Papa John's Pizza, to Jiffy Lube. Long in common use within the franchise industry, no-hire clauses prohibit a franchisee from soliciting or hiring employees (a) of another franchisee or (b) from a restaurant or store operated by the franchisor. Plaintiffs, who are current or former franchisee employees, claim in a series of recent lawsuits that enforcement of the clauses violates Section 1 of the Sherman Act. This article shows that the clauses, while incrementally limiting employee mobility, serve significant procompetitive purposes and that courts have been unwarrantedly indulgent in denying motions to dismiss. As restraints ancillary to business format franchise agreements, no-hire clauses prevent franchisee free riding and are reasonably necessary for achievement of the objectives of the franchise agreement, including protection of brand goodwill for the collective benefit of independent businesses operating under a common trademark.

The recent frontal assault on no-hire clauses in franchise agreements may advance state or federal labor policy, but it has no support in antitrust law. The absence of an antitrust predicate would not matter, except for the

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awkward fact that all federal court litigation challenging no-hire clauses to date stands on claimed violations of Section 1 of the Sherman Act.[1] A franchisee's promise not to hire employees from the franchisor or from franchisees operating under the franchisor's trademark does not violate Section 1 when the statute is properly applied. It is not per se illegal as the product of a conspiracy among franchisees, and it is not a violation under the rule of reason, whether using truncated or full analysis.

This article will show that courts have failed to address the unique context in which no-hire clauses arise—the business format franchise—and that, when correctly analyzed, a no-hire clause is valid and enforceable against the franchisee as a restraint ancillary to the franchise agreement, the core component of which is a trademark license.

In a product franchise or conventional dealership or distributorship, the trademark licensee is engaged in reselling a product manufactured by the owner of the trademark, and quality is under the direct control of the manufacturer. In a business format franchise, in contrast, goodwill associated with the franchisor's trademark is created by independent businesses selling goods or services under the franchisor's mark. The difference is crucial, because it means that the business format franchisor must regulate all aspects of a franchisee's operation to ensure sale of goods or services of uniform quality from one retail outlet to the next. The no-hire clause guards against franchisee free riding that could otherwise vitiate brand goodwill.

This article examines the no-hire clause which is the subject of all of the reported cases—a promise by the franchisee that it will not, during the term of the franchise, hire or solicit for employment an employee of the franchisor or another franchisee.[2] The clause previously found in the McDonald's standard franchise agreement is representative:

1. 15 U.S.C. § 1. Section 1 declares illegal "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations . . . . "

2. For reported cases, see Arrington v. Burger King Worldwide, Inc., 448 F. Supp. 3d 1322, 1326-27 (S.D. Fla. 2020) (franchisee shall not induce a franchisor employee or an employee of another franchisee to leave employment and shall not employ any such person for six months after he or she has left such employment); Ogden v. Little Caesar Enters., 393 F. Supp. 3d 622, 628 (E.D. Mich. 2019) (franchise shall not employ or seek to employ any person in a managerial capacity who in the last six months has been employed by franchisor or another franchisee); Fuentes v. Royal Dutch Shell PLC, No. 18-5174, 2019 U.S. Dist. LEXIS 224708, at *2 (E.D. Pa. Nov. 25, 2019) (franchisee shall not hire another Jiffy Lube franchisee's employee); Robinson v. Jackson Hewitt, Inc., No. 19-9066 (SDW) (LDW), 2019 U.S. Dist. LEXIS 188962, at *3 (D.N.J. Oct. 31, 2019) (franchisee shall not during the term of the franchise agreement and for two years thereafter solicit for employment or hire any person who in the immediate past year was employed by franchisor or another franchisee); *In re* Papa John's Emp. & Franchisee Emp. Antitrust Litig., No. 3:18-CV-00825-JHM, 2019 WL 5386484, at *1 (W.D. Ky. Oct. 21, 2019) (franchisee shall not employ during the term of the franchise agreement or for one year thereafter any person employed by franchisor or another franchisee); Blanton v. Domino's Pizza Franchising LLC, No. 18-13207, 2019 U.S. Dist. LEXIS 87737, at *3 (E.D. Mich. May 24, 2019) (franchisee shall not solicit or employ any person who is employed by franchisor or another franchisee); Butler v. Jimmy John's Franchise, LLC, 331 F. Supp.3d 786, 790 (S.D. Ill. 2018) (franchisee may not solicit for employment or hire a person who has been employed in the last twelve months by franchisor or another franchisee); Yi v. SK Bakeries, LLC, No.

> *Interference With Employment Relations of Others.* During the term of this Franchise, Franchisee shall not employ or seek to employ any person who is at the time employed by McDonalds, any of its subsidiaries, or by any person who is at the time operating a McDonald's restaurant or otherwise induce, directly or indirectly, such person to leave such employment. This paragraph [] shall not be violated if such person has left the employ of any of the foregoing parties for a period in excess of six (6) months.[3]

To the extent the clause bars franchisee solicitation or employment of the franchisor's employees, it is assumed that the goal is the same as it is for franchisee employees—to prevent a franchisee from hiring operating personnel away from other store locations in the franchise, whether franchisor-owned or franchisee-owned.[4]

Courts have so far failed to recognize that such restraints have no exact counterpart in case law addressing either vertical or horizontal restraints, and, before the current litigation, no federal court had ever considered the competitive effects under Section 1 of a no-hire clause in a franchise agreement.[5] In the total absence of any judicial experience, the legality of the clause must be evaluated under the rule of reason. For simplicity, this article assumes that the agreement between a franchisor and its franchisee satisfies the joint conduct requirement of Section 1.[6]

This article will outline in Part I the use of the Sherman Act to challenge restraints on employee hiring, leading up to the present class-action litigation. In Part II, it will describe the business format franchise and explain why no-hire clauses must be understood as restraints ancillary to trademark license agreements. Part III will show why the restraints are not per se

18-5627 RJB, 2018 U.S. Dist. LEXIS 220966, at *3 (W.D. Wash. Nov. 13, 2018) (franchisee shall not employ or seek to employ any person who is employed by franchisor (Cinnabon) or another franchisee); Deslandes v. McDonald's USA, LLC, No. 17 C 4857, 2018 U.S. Dist. LEXIS 105260, at *5 (N.D. Ill. June 25, 2018) (franchisee shall not employ or seek to employ any person who has been employed in the last six months by franchisor or another franchisee).

3. *Deslandes*, 2018 U.S. Dist. LEXIS 105260, at *5 (italics in original). McDonald's discontinued use of the clause in 2017, but it remains in franchise agreements applicable to some 13,000 McDonald's brand restaurants. *Id.*

4. This article does not consider the antitrust implications of a provision, appearing in the Jimmy John's franchise agreement, making franchisees third-party beneficiaries of a no-hire clause and giving them an independent right to enforce it against other franchisees. *See Butler*, 331 F. Supp. 3d at 790.

5. The legality of a no-switching clause, as it was called, in a Jack-in-the-Box franchise agreement was at issue in *Williams v. I.B. Fischer Nevada*, 794 F. Supp. 1026 (D. Nev. 1992), *aff'd*, 999 F.2d 445 (9th Cir. 1993), a case brought by an employee seeking to move from one franchisee to another in the Jack-in-the-Box system. Holding that the franchisor and employee's franchisee were part of a unitary economic enterprise and, as such, could not conspire for purposes of § 1 of the Sherman Act, the court had no need to consider whether the no-switching clause violated § 1. *See id.* at 1331–32.

6. In *Arrington v. Burger King Worldwide, Inc.*, 448 F. Supp. 3d 1322, 1332 (S.D. Fla. 2020), *appeal pending*, No. 20-13561 (11th Cir.), the court held that a franchise is a unitary enterprise and that a franchisor and its franchisees are therefore incapable of conspiring for purposes of § 1. Relying on *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752 (1984), the court held that plaintiffs had failed to state a claim that Burger King Corporation had conspired with its franchisees to prevent them from hiring employees of it or of other franchisees in violation of § 1. *Arrington*, 448 F. Supp. 3d at 1332.

unlawful under Section 1, and Part IV will explain why they do not violate Section 1 under the rule of reason. Finally, Part V demonstrates why a truncated rule-of-reason analysis cannot be used.

I. Labor Market Antitrust—Litigation and Enforcement Landscape

Antitrust law has a role to play in labor markets, and the normal rules apply. Employees have invoked Section 1 in repeated challenges to enforcement of noncompetition covenants. These challenges have been futile, however, because the legality of the covenants is tested under the rule of reason.[7] As restraints ancillary to employment contracts, noncompetition covenants have no market effects. No matter how the relevant market is defined, a restraint impacting only a single employee has no anticompetitive effect on any market (other than the employee's own personal market).[8]

The situation changes dramatically when an agreement between two employers is the subject of a Section 1 challenge. A firm's promise that it will not solicit or hire a competitor's employees is a horizontal market allocation,[9] and a division of markets between competitors is presumptively illegal unless in furtherance of a joint venture or other procompetitive integration.[10] The Department of Justice (DOJ), beginning in 2010, initiated a series of civil

7. *See, e.g.*, Bradford v. N.Y. Times Co., 501 F.2d 51, 60 (2d Cir. 1974) (rejecting per se illegality under § 1 and holding that "rule of reason considerations continue to apply" to employee noncompetition covenants).

8. *See, e.g.*, Lektro-Vend Corp. v. Vendo Co., 660 F.2d 255, 269 (7th Cir. 1981) (holding that former employee had to prove more "than mere injury to a competitor" to establish that enforcement of noncompetition covenant had an adverse effect on a relevant market); Coleman v. Gen. Elec. Co., 643 F. Supp. 1229, 1243 (E.D. Tenn. 1986) (holding that covenant incident to sale of business division barring seller from soliciting division employees did not violate rule of reason, because "there is no more than a de minimis impact on the employment market and the anti-competitive impact, if any, is incidental to the effective transition of ownership from 3M to GE"), *aff'd per curiam*, 822 F.2d 59 (6th Cir. 1987). The fact that enforcement of an employee noncompetition covenant can have no measurable market impact means, in the blunt assessment of one recent commentator, that "antitrust law is a nullity for employment noncompetes." Eric A. Posner, *The Antitrust Challenge to Covenants not to Compete in Employment Contracts*, 83 Antitrust L.J. 165, 175 (2020).

9. *See, e.g.*, Markson v. CRST Int'l, Inc., No. 5:17-cv-01261-SB-SP, 2021 U.S. Dist. LEXIS 60368, at *13–14 (C.D. Cal. Feb. 10, 2021) (holding that agreement among rivals to divide markets by not hiring each's employees was a per se violation of § 1); *In re* Ry. Indus. Emp. No-Poach Antitrust Litig., 395 F. Supp. 3d 464, 480–85 (W.D. Pa. 2019) (holding that no-hire agreements among competitors constituted a market allocation that may be per se illegal under § 1 and collecting cases on same); United States v. Kemp & Assocs., No. 2:16CR403 DS, 2019 U.S. Dist. LEXIS 28231, at *6–9 (D. Utah Feb. 21, 2019) (holding that customer allocation agreement between competitors was per se illegal under § 1); United States v. eBay, Inc., 968 F. Supp. 2d 1030, 1038–40 (N.D. Cal. 2013) (acknowledging that no-hire agreement between defendants was a market allocation, but deferring until completion of discovery any ruling as to whether it should be deemed per se illegal under § 1).

10. *See, e.g.*, Rothery Storage & Van Co. v. Atlas Van Lines, Inc., 792 F.2d 210, 229 (D.C. Cir. 1986) ("[A] naked horizontal restraint, one that does not accompany a contract integration, can have no purpose other than restricting output and raising prices, and so is illegal per se; an ancillary horizontal restraint, one that is part of an integration of economic activities of the a parties and appears capable of enhancing the group's efficiency, is to be judged according to its purpose and effect.").

enforcement actions against technology companies challenging such no-hire agreements.[11] In conjunction with the Federal Trade Commission (FTC), the DOJ released in October 2016 a guide on enforcement policy on hiring agreements between rivals,[12] announcing that it would proceed criminally against parties to such agreements, which it deems per se illegal.[13] No such agreements between competing employers are at issue in the franchise litigation that is the subject of this article.

Economic reports on the impact of noncompetition agreements on wages and mobility of hourly workers brought attention to the use of no-hire clauses in franchise agreements,[14] and enforcement initiatives were launched against the franchising industry by early 2018. The Attorney General for the State of Washington began a program in early 2018 "to eliminate no-poach clauses in franchise agreements nationwide,"[15] and it had concluded commitments with over 225 franchisors by early 2020.[16] Other attorneys general subsequently initiated separate investigations into the use of no-hire clauses by franchisors.[17]

No-hire clauses in franchise agreements attracted the interest of Senators Cory Booker and Elizabeth Warren in the U.S. Senate at about the same time, and they sent letters in July 2018 to some ninety franchisors requesting information about their use of "no-poach clauses" in franchise

11. *See* Press Release, U. S. Dep't of Justice, Justice Department Requires Six High Tech Companies to Stop Entering into Anticompetitive Employee Solicitation Agreements (Sept. 24, 2010) (announcing consent decree with Adobe Systems Inc., Apple Inc., Google Inc., Intel Corp., Intuit Inc., and Pixar), https://www.justice.gov/opa/pr/justice-department-requires-six-high-tech-companies-stop-entering-anticompetitive-employee; U.S. Dep't of Justice, Press Release, Justice Department Requires Lucasfilm to Stop Entering into Anticompetitive Employee Solicitation Agreements (Dec. 21, 2010) (announcing consent decree with Lucasfilm Ltd. to discontinue agreement with Pixar not to cold call each other's employees), https://www.justice.gov/opa/pr/justice-department-requires-lucasfilm-stop-entering-anticompetitive-employee-solicitation. The Department of Justice filed an action against eBay, Inc. in 2012 challenging its agreement with Intuit not to hire each other's employees. *See eBay, Inc.*, 968 F. Supp. 2d at 1034.

12. U. S. Dep't of Justice & Fed. Trade Comm'n, Antitrust Guidance for Human Resource Professionals (Oct. 2016), https://www.justice.gov/atr/file/903511/download [hereinafter Antitrust Guidance].

13. *Id.* at 3–4.

14. *See, e.g.*, Council of Econ. Advisors, Labor Market Monopsony: Trends, Consequences, and Policy Responses (Oct. 2016), https://obamawhitehouse.archives.gov/sites/default/files/page/files/20161025_monoposony_labor_mrkt_cea.pdf. For an influential study of the franchise industry, see Alan B. Krueger & Orley Ashenfelter, *Theory and Evidence on Employer Collusion in the Franchise Sector* (Princeton Univ., Indus. Relations Section, Working Paper No. 614, 2017), https://dataspace.princeton.edu/bitstream/88435/dsp014f16c547g/3/614.pdf. For an overview of empirical studies and economic analyses of restraints on employee mobility, see generally Ioana Marinescu & Eric A. Posner, *Why Has Antitrust Law Failed Workers?* 105 Cornell L. Rev. 1343, 1349–62 (2020).

15. *See* Attorney Gen. of Wash., Labor and Antitrust (2021), https://www.atg.wa.gov/print/13119.

16. *Id.*

17. *See* John M. Piper & Erik Ruda, *Employee "No-Poaching" Clauses in Franchise Agreements: An Assessment in Light of Recent Developments*, 38 Franchise L.J. 185, 201 (2018).

agreements.[18] Referencing the FTC/DOJ's *Antitrust Guidance for Human Resource Professionals*,[19] the senators made no distinction between competitor no-hire agreements and no-hire clauses in franchise agreements. They urged the addressees to remove no-hire clauses from franchise agreements because doing so would, in their words, "rectify a violation of federal antitrust law" and increase employee wages. In his July 9, 2021, executive order on promoting competition, President Biden directed the Chair of the FTC to consider working with the rest of the Commission to exercise its rulemaking authority "to curtail the unfair use of non-compete clauses . . . that may unfairly limit worker mobility."[20]

The first federal court employee class action alleging Sherman Act violations by franchisors was filed in June 2017.[21] Despite subsequent discontinuance of the use of no-hire clauses by major franchisors, either as a result of settlements with state attorneys general or voluntarily, litigation has continued, as plaintiffs seek damages for past conduct.[22] District courts have denied motions for class certification in two of the actions[23] and, in the process, have begun to clear away some of the errors embedded in earlier orders denying motions to dismiss. Most of the cases remain active, however, and appeals from district court judgments are a certainty.

II. Architecture of the Business Format Franchise

Courts have struggled with how to evaluate claims that no-hire clauses violate Section 1 and, in the process, have largely ignored the commercial context in which they are used. Without exception, the cases challenge no-hire clauses in business format franchises, and this context matters. A business format franchise agreement imposes an array of obligations calculated to advance and protect the goodwill of the franchisor's trademark, and the success of the entire franchise system depends upon the reputation of the brand.

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18. The form of letter can be found on Senator Elizabeth Warren's website, https://www.warren.senate.gov/imo/media/doc/No%20poach%20letter%20generic.pdf.

19. Antitrust Guidance, *supra* note 12.

20. Exec. Order No. 14036, 86 C.F.R. 36987 (July 9, 2021).

21. Deslandes v. McDonald's USA, LLC, No. 17 C 4857 (N.D. Ill. June 28, 2017). For a chronology of enforcement actions and litigation, see generally Brian Forgas & Rahul Rao, *Anti-Poaching Issues in Franchising*, Am. Bar Ass'n, 42nd Annual Forum on Franchising, W-18, at 9–12 (Oct. 2019).

22. McDonald's USA, LLC, for example, agreed with the State of Washington in an Assurance of Discontinuance filed in King County, Washington Superior Court on July 12, 2018, that it would not enforce the no-hire clause, Paragraph 14 in its standard-form franchise agreement, in any of its existing franchise agreements nationwide (Assurance §3.1.2) and that it would not include any such provision in any future franchise agreement nationwide (Assurance § 3.1.1). *See In re:* Franchise No Poaching Provisions, McDonald's USA, LLC Assurance of Discontinuance, No. 18-2-17229-2 SEA (Wash. Super. Ct. July 12, 2018), https://agportal-s3bucket.s3.amazonaws.com/uploadedfiles/Another/News/Press_Releases/20180712_McDonalds_SignedFiled_AOD%20%281%29.pdf.

23. *See* Conrad v. Jimmy John's Franchise, LLC, No. 18-CV-00133-NJR, 2021 U.S. Dist. LEXIS 142272 (S.D. Ill. July 23, 2021); Deslandes v. McDonald's USA, LLC, No. 17 C 4857, 2021 U.S. Dist. LEXIS 140735 (N.D. Ill. July 28, 2021).

In return for the grant of a trademark license and participation in the franchise, the licensee must conform its conduct to the franchisor's requirements for use of the mark, one of which is compliance with a no-hire clause.

Plaintiffs have alleged that inclusion of a no-hire clause in a franchise agreement is either per se illegal or facially illegal when evaluated using a quick-look analysis under the rule of reason, or both.[24] In two cases, plaintiffs have also alleged a violation of Section 1 under the rule of reason.[25] In every case, plaintiffs are employees of franchisees who have never themselves been party to a franchise agreement.

Most courts have deferred deciding on the correct Section 1 test until discovery has been concluded. In the process of postponing any determination, they have offered views, however, as to whether the per se rule should apply or whether no-hire clauses can be invalidated using a truncated rule of reason. Judicial analysis has fixated on labels—i.e., whether a franchise agreement with a no-hire clause is a "vertical" agreement or whether no-hire clauses are the product of a "horizontal" agreement between franchisees.[26] They are neither. Until courts recognize that no-hire clauses are restraints ancillary to license agreements establishing business format franchises, to which the label "horizontal" has no application and the adjective "vertical" is misplaced, proper Section 1 analysis is impossible. This issue is unexamined antitrust terrain.

Applying conventional vertical/horizontal taxonomy to weigh the competitive effects of no-hire clauses leads to an analytical dead end. Rule of reason treatment for "vertical" restraints has emerged out of dealer litigation involving restraints on how, where, and to whom a downstream buyer can resell goods.[27] There is no vertical relationship in this sense, however,

24. *See* Ogden v. Little Caesar Enters., 393 F. Supp. 3d 622, 631–36 (E.D. Mich. 2019) (granting motion to dismiss complaint for failure to state a claim for violation of § 1 under either per se rule or quick-look rule of reason); 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) (holding that complaint stated claim for violation of § 1 under per se rule and quick-look rule of reason); Butler v. Jimmy John's Franchise, LLC, 331 F. Supp. 3d 786, 795–97 (S.D. Ill. 2018) (same); Yi v. SK Bakeries, LLC, No. 18-5627 RJB, 2018 U.S. Dist. LEXIS 220966, at *14–15 (W.D. Wash. Nov. 13, 2018) (holding that complaint stated claim for violation of § 1 under quick-look rule of reason; motion to dismiss granted as to per se claim); Deslandes v. McDonald's USA, LLC, No. 17 C 4857, 2018 U.S. Dist. LEXIS 105260, at *20–23 (N.D. Ill. June 25, 2018) (same).

25. *See* Robinson v. Jackson Hewitt, Inc., No. 19-9066 (SDW) (LDW), 2019 U.S. Dist. LEXIS 188962, at *16 (D.N.J. Oct. 31, 2019); *In re* Papa John's Emp. & Franchisee Emp. Antitrust Litig., No. 3:18-CV-00825-JHM, 2019 WL 5386484, at *8 (W.D. Ky. Oct. 21, 2019).

26. *See, e.g.*, *Deslandes*, 2018 U.S. Dist. LEXIS 105260, at *15–16 ("The Court agrees that the restraint [in the McDonald's franchise agreement] has vertical elements, but the agreement is also a horizontal restraint.").

27. *See, e.g.*, Leegin Creative Leather Prods. v. PSKS, Inc., 551 U.S. 877, 907 (2007) (holding that vertical price restraints are subject to rule of reason, in case involving restrictions on resale of women's fashion accessories); NYNEX Corp. v. Discon, Inc., 525 U.S. 128, 136 (1998) ("[T]he case before us concerns only a vertical agreement and a vertical restraint, a restraint that takes the form of depriving a supplier of a potential customer," in a case involving providing removal services for obsolete telephone equipment); State Oil Co. v. Khan, 522 U.S. 3, 22 (1997) (holding that vertical maximum price fixing is subject to the rule of reason, in case involving retail sale of gasoline); Bus. Elecs. Corp. v. Sharp Elecs. Corp., 485 U.S. 717, 735–36

between a franchisor and franchisee because, in a business format franchise, the franchisor is not selling goods to a franchisee for resale. The franchisee makes the first sale of the trademarked goods or services, selling to the ultimate consumer. A business format franchise agreement creates a licensor-licensee relationship, not a buy-sell relationship in which the parties' respective rights and duties are subject to the Uniform Commercial Code.[28] Trademarked goods in a business format franchise do not originate with the franchisor; they are produced by the franchisee.

Calling restraints incident to a trademark license "vertical" does not, thus, align with use of the term *vertical* in the case law. In the case law, vertical restraints are those imposed by agreement between firms at different levels of distribution,[29] and they promote interbrand competition except in the rare case where they serve to further entrench a firm with market power.[30]

(1988) (holding that termination of dealer agreement for electronic calculators was subject to evaluation under rule of reason in absence of proof that it was pursuant to a price-fixing agreement between manufacturer and competing dealer); Cont'l T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 46, 59 (1977) (holding that restraint on location from which a dealer could resell television sets was subject to the rule of reason and noting that such restrictions, identical to that which the Court had earlier held per se illegal in *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365 (1967), "allowed Schwinn and Sylvania to regulate the amount of competition among their retailers by preventing a franchisee from selling franchised products from outlets other than the one covered by the franchise agreement"); White Motor Co. v. United States, 372 U.S.253, 263–64 (1963) (reversing summary judgment for the government on claim that vertical territorial restraints imposed by truck manufacturer on its dealers were per se illegal and noting that "[w]e need to know more than we do about the actual impact of these arrangements on competition to decide whether they have such a 'pernicious effect on competition and lack . . . any redeeming virtue' . . . and therefore should be classified as *per se* violations of the Sherman Act." (citation omitted; italics in original)). Confinement of "vertical" terminology to the product distribution context, in which a manufacturer or other supplier sells goods to a dealer or distributor for resale, is evident in the commentary, as well. *See, e.g.*, Frank H. Easterbrook, *Vertical Arrangements and the Rule of Reason*, 53 Antitrust L. J. 135 (1984) (proposing filters for rule of reason analysis of restricted distribution practices); Herbert J. Hovenkamp, *The Rule of Reason*, 70 Fla. L. Rev. 81, 161 (2018) ("Vertical nonprice restraints generally involve such things as assignment of dealer locations or territories and rules forbidding these dealers from making sales outside their appointed area. . . . Vertical nonprice restraints have been addressed under the rule of reason for most of the life of the antitrust laws.").

28. Under the great weight of authority, the relationship between a manufacturer and a dealership or distributorship is subject to Article 2 of the Uniform Commercial Code. *See, e.g.*, Specialty Beverages, L.L.C. v. Pabst Brewing Co., 537 F.3d 1165, 1173–74 (10th Cir. 2008) (holding that parties' rights under a beverage distributorship were subject, under Oklahoma law, to Article 2 governing transactions in goods and collecting cases supporting this conclusion); Sally Beauty Co. v. Nexxus Prods. Co., 801 F.2d 1001, 1005–06 (7th Cir. 1986) (holding that parties' rights under a distributor agreement for hair care products were subject, under Texas law, to Article 2 governing transactions in goods and collecting cases supporting this conclusion).

29. *E.g.*, Ohio v. Am. Express Co., 138 S. Ct. 2274, 2284 (2018) (vertical restraints are those "imposed by agreement between firms at different levels of distribution" (quoting Bus. Elecs. Corp. v. Sharp Elecs. Corp., 485 U.S. 717, 730 (1988))).

30. *See* Graphic Prods. Distribs. v. Itek Corp., 717 F.2d 1560, 1576–78 (11th Cir. 1983) (affirming judgment for terminated distributor claiming that manufacturer's imposition of exclusive territories violated § 1 under rule of reason where manufacturer controlled seventy percent of the national market for offset platemaking machines). In a survey of cases decided under the rule of reason between February 1999 and May 2009, many of which addressed vertical restraints, it was found that "plaintiffs almost never win" and that almost all cases were decided by finding that the plaintiff had failed to show any anticompetitive effect from the alleged restraint. *See*

Because vertical restraints are, in the usual case, intended to promote interbrand competition and have promotion of interbrand competition as their effect, they are subject to the rule of reason.[31]

Application of the "horizontal" label to licensing needed to create a business format franchise is similarly misplaced, because it obscures the fact that the franchisor determines the terms and content of a licensing agreement, not franchisees. Unless in furtherance of a legitimate joint venture or other procompetitive integration, restraints imposed by agreement between competitors—horizontal restraints—do not promote interbrand competition. They curtail it and are therefore per se illegal.[32] For the term *horizontal* to apply, there must be agreement between direct competitors on a restraint, and not even the most inventive drafters have alleged in any of the complaints that no-hire clauses are the product of a conspiracy among rival franchisees.[33]

To understand why conventional vertical/horizontal labeling fails to conform to the facts in the various cases, it is essential to examine the commercial context in which no-hire clauses are used (i.e., the business format franchise). The franchise systems at issue in the litigated cases are all business format franchises.[34] The business format franchise combines a trademark license with an array of goodwill protections intended to facilitate the success of a network of independent businesses operating under a single brand.

In a business format franchise, retail locations display uniform trade dress and signage, and all goods and services offered at the locations are associated exclusively with the franchisor's trademark. The FTC has described this type of franchise, which it called a "package franchise," as follows:

> In package franchising, the franchisee is licensed to do business under a prepackaged business format established by the franchisor and identified with the franchisor's trademark. While the franchisee is an independent businessman, *the franchisor usually controls the franchisee's method of operation to insure that the goods or services being sold meet the uniform quality standards imposed by the franchisor on all of its franchisees*. Additionally, the franchisor usually gives direct assistance to the franchisee in areas such as training, management technique, and promotional

Michael A. Carrier, *The Rule of Reason: An Empirical Update for the 21st Century*, 21 Geo. Mason L. Rev. 827, 829 (2009).

31. *E.g.*, *Cont'l T.V., Inc.*, 433 U.S. at 54 ("Vertical restrictions promote interbrand competition by allowing the manufacturer to achieve certain efficiencies in the distribution of his products. . . . Economists have identified a number of ways in which manufacturers can use such restrictions to compete more effectively against other manufacturers.").

32. *E.g.*, Rothery Storage & Van Co. v. Atlas Van Lines, Inc., 792 F.2d 210, 229 (D.C. Cir. 1986) ("[A] naked horizontal restraint, one that does not accompany a contract integration, can have no purpose other than restricting output and raising prices, and so is illegal per se . . . .").

33. Plaintiffs alleged in *Butler v. Jimmy John's Franchise, LLC*, 331 F. Supp. 3d 786, 795–96 (S.D. Ill. 2018), that Jimmy John's franchisees could, pursuant to the terms of the franchise agreement, enforce the no-hire clause against noncompliant franchisees and that there was, to this extent, tacit agreement among franchisees to enforce the clause. As indicated *supra* note 4, this provision is beyond the scope of this article.

34. Burger King, Cinnabon, Domino's Pizza, Jackson Hewitt, Jiffy Lube, Jimmy John's, Little Caesar, McDonald's, Papa John's.

> campaigns. The franchisee thus gets the benefit of the franchisor's established reputation, expertise, and superior resources; in return, he pays the franchisor for the privilege to operate the franchise.[35]

In a business format franchise, the franchisor sells a way of doing business to its franchisees.[36] The franchise includes "not only the product, service, and trademark, but the entire business format itself—a marketing strategy and plan, operating manuals and standards, quality control, and continuing two-way communication."[37] The franchise agreement creates an ongoing relationship between franchisor and franchisee regulating, among other matters, supplies, inspections, and quality standards in furtherance of maintaining the franchise's goodwill.[38]

The trademark is the "cornerstone" of a franchise system.[39] In licensing a trademark, the franchisor has a legal duty to maintain the goodwill inhering in it and to ensure the quality of goods or services associated with it.[40] Indeed, without effective control over licensee trademark use, the licensor may lose its exclusive rights in the mark.[41] The imperative for quality control was aptly explained nearly sixty years ago in an early business format franchise case, *Susser v. Carvel Corp.*:[42]

> . . . [A franchisor licensing a mark] must do so in a way that he maintains sufficient control over the nature and quality of the finished product, over the activities of the licensee, as will enable the licensor to sustain his original position of guarantor to the public that the goods now bearing the trademark are of the same nature and quality as were the goods bearing the trademark before the licensing, or, that the mark now has the same meaning as far as the public is concerned as it did before the licensing.[43]

35. Fed. Trade Comm'n, Statement of Basis and Purpose Relating to Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures, 43 Fed. Reg. 59,613, 59,697 (Dec. 21, 1978) (footnotes omitted; emphasis added).

36. *See* Roger D. Blair & Francine Lafontaine, The Economics of Franchising 6 (2005).

37. *Id.* (citation omitted).

38. *See, e.g.*, Queen City Pizza v. Domino's Pizza, 124 F.3d 430, 440 (3d Cir. 1997) ("[A] franchise agreement regulating supplies, inspections, and quality standards structures an ongoing relationship between franchisor and franchisee designed to maintain good will.").

39. Susser v. Carvel Corp., 206 F. Supp. 636, 640 (S.D.N.Y. 1962), *aff'd*, 332 F.2d 505 (2d Cir. 1964).

40. *See, e.g.*, Ky. Fried Chicken Corp. v. Diversified Packaging Corp., 549 F.2d 368, 387 (5th Cir. 1977) ("Courts have long imposed upon trademark licensors a duty to oversee the quality of licensees' products. . . . The rationale for this requirement is that marks are treated by purchasers as an indication that the trademark owner is associated with the product. Customers rely upon the owner's reputation when they select the trademarked goods." (citation omitted)).

41. *See, e.g.*, Sheila's Shine Prods. v. Sheila Shine, Inc., 486 F.2d 114, 123–24 (5th Cir. 1973) ("The owner of a trademark has not only a right to license the use of his trademark to others, but also a concurrent duty to exercise control and supervision over the licensee's use of the mark . . . . Failure to exercise such control and supervision for a significant period of time may estop the trademark owner from challenging the use of the mark and business which the licensee has developed during the period of such unsupervised use.").

42. Susser v. Carvel Corp., 206 F. Supp. 636 (S.D.N.Y. 1962), *aff'd*, 332 F.2d 505 (2d Cir. 1964).

43. *Id.* at 641 (quoting Morse-Starrett Prods. Co. v. Steccone, 86 F. Supp. 796, 805 (N.D. Cal. 1949)).

The strength and goodwill of a trademark provide a key inducement for a prospective franchisee to invest in a franchise, because, as a franchisee, the investor will "operate[] his outlet under a name that 'trades off' the franchisor's trademark."[44] A trademark license is an element of the definition of a franchise in the FTC's Franchise Rule,[45] and it is an element of the definition of a franchise in every state statute of general application regulating the sale, operation, or termination of franchises.[46]

The business format franchise is not the only type of franchise. The other major type is the product franchise, in which "the franchisor has already produced the goods and the franchisee merely provides an outlet for them."[47] Automobile and gasoline station dealerships are common examples of product franchises, and the franchisor "usually exercises significant control over the franchisee's operation to ensure proper marketing of the product, or gives the franchisee significant assistance in his business operation."[48] In the absence of such significant control or assistance, there is no franchise arrangement.[49] Most dealerships and distributorships are, for this and other reasons, not a *franchise* as the term is defined in state franchise protection statutes of general application,[50] even though a manufacturer may

44. Fed. Trade Comm'n, Statement of Basis and Purpose Relating to Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures, 43 Fed. Reg. 59,613, 59,701 (Dec. 21, 1978) (footnote omitted).

45. According to the Federal Trade Commission's franchise disclosure rule, a "franchise" means a continuing commercial relationship or arrangement (1) in which the "franchisee will obtain the right to operate a business that is identified or associated with the franchisor's trademark," (2) as to which the franchisor will exercise a significant degree of control over the franchisee's method of operation, and (3) for which the franchisee is required to make a payment to the franchisor or its affiliate. *See* 16 C.F.R. § 436.1(h)(1)–(3).

46. *See*, *e.g.*, Franchise Practices Act, Ark. Code Ann. § 4-72-202(1)(A); Franchise Relations Act, Cal. Bus. & Prof. Code § 20001(b); Franchise Act, Conn. Gen. Stat. Ann. § 42-133e(b)(2); Franchise Investment Law, Haw. Rev. Stat. Ann. § 482E-2; Franchise Disclosure Act, 815 Ill. Comp. Stat. 705/3(1)(b); Deceptive Franchise Practices Act, Ind. Code Ann. § 23-2-2.5-1(a)(2); Franchise Act, Iowa Code Ann. § 537A.10(1)(c)(1)(a)(iii); Franchise Registration & Disclosure Law, Md. Code Ann., Bus. Reg. § 14-201(e); Franchise Investment Law, Mich. Comp. Laws Ann. § 445.1502(3)(b); Franchise Law, Minn. Stat. Ann. § 80C.01(4)(a); Franchise Act, Miss. Code Ann. § 75-24-51(6); Franchise Act, Mo. Ann. Stat. § 407.400(1); Franchise Practices Act, Neb. Rev. Stat. § 87-402(1); Franchise Practices Act, N.J. Stat. Ann. § 56:10-3(a); N.Y. Gen. Bus. Law § 681(3); Franchise Investment Law, N.D. Cent. Code § 51-19-02(5.a); Franchise Investment Act, R.I. Gen. Laws § 19-28.1-3(7); Retail Franchising Act, Va. Code Ann. § 13.1-559(A)(b); Franchise Investment Protection Act, Wash. Rev. Code Ann. § 19.100.010(4)(a)(2); Franchise Investment Law, Wis. Stat. Ann. § 553.03(4)(a).

47. Statement of Basis and Purpose Relating to Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures, 43 Fed. Reg. at 59,697 (footnote omitted).

48. *Id.* at 59,698.

49. *Id.*

50. To qualify as a franchise under most state franchise statutes of general application, a product supply relationship must also entail a requirement that the buyer pay a franchise fee to the supplier. A franchise fee is defined variously under the statutes, but it does not include a payment made by the buyer to the supplier for the purchase of goods at a bona fide wholesale price. *See*, *e.g.*, Franchise Relations Act, Cal. Bus. & Prof. Code § 20007(a); Franchise Investment Law, Haw. Rev. Stat. Ann. § 482E-2; Franchise Disclosure Act, 815 Ill. Comp. Stat. 705/3(14(c); Ind. Code Ann. § 23-2-2.5-1(i)(3); Iowa Code Ann. § 537A.10(1)(d)(3); Franchise Investment Law, Mich. Comp. Laws Ann. § 445.1503(1)(a); Minn. Stat. Ann.

have granted the dealer or distributor a license to use its trademark to signify affiliation or sponsorship.

Because of the nature of the business format franchise, the restraints needed to ensure uniformity of goods and services and quality control among franchisees are necessarily more extensive than those incident to a product franchise or to a simple trademark license in a dealer or distributor agreement. In a product franchise, the trademark identifies a product,[51] and it is typically affixed during manufacture by the licensor. The manufacturer controls product quality and resulting goodwill. In a business format franchise, the trademark identifies an enterprise.[52] Goodwill inhering in the mark identifying a business format franchise comes from operation of individual retail outlets by franchisees and depends upon uniformity of operation and delivery of goods and services of consistent quality. The franchise agreement in a business format franchise confers a constellation of rights and obligations on the franchisee, all of which are anchored in protection of trademark value and goodwill.

The competitive effects of restraints incident to a trademark license agreement establishing a business format franchise are indistinguishable from those of restraints incident to a dealer or distributor agreement. While there is not perfect equivalence between the two types of agreement, intrabrand restraints incident to either have the same economic significance: they strengthen the marketing and sale of goods or services against interbrand competitors. At least one court has observed that, because intrabrand restrictions incident to a franchise could potentially increase interbrand competition, they should be deemed "vertical."[53] This view is incorrect, as they are not restraints imposed on a downstream reseller, and they are not, thus, "vertical."[54] Despite this fundamental distinction, the legality under Section 1 of

§ 80C.01(9)(a); Franchise Practices Act, Neb. Rev. Stat. § 87-402(5); Retail Franchising Act, Va. Code Ann. § 13.1-559(A)(3); Franchise Investment Protection Act, Wash. Rev. Code Ann. § 19.100.010(8)(a). In the typical product dealership or distributorship, the manufacturer does not exact a franchise fee, however it may be statutorily defined, from the dealer or distributor.

51. *See, e.g.*, Krehl v. Baskin-Robbins Ice Cream Co., 664 F.2d 1348, 1354 (9th Cir. 1982) (noting that the trademark "serves merely as a representation of the end product" marketed in what the court referred to as a distribution franchise system).

52. *See, e.g.*, *id.* at 1353 ("the trade-mark simply reflects the goodwill and quality standards of the enterprise it identifies" (quoting Siegel v. Chicken Delight, Inc., 448 F.2d 43, 49 (9th Cir. 1971))).

53. *See* St. Martin v. KFC Corp., 935 F. Supp. 898, 905 (W.D. Ky. 1996) ("KFCC's restrictions could potentially increase interbrand competition and thus should be considered vertical in nature.").

54. The Department of Justice has taken the position that no-hire restraints are vertical because a franchisor and franchisee "normally conduct business at different levels of the market structure." *See* Corrected Statement of Interest of the United States of America, at 11, Stigar v. Dough Dough, Inc., No. 2:18-cv-00247-SAB (E.D. Wash. Mar. 8, 2019), Dkt. No. 34, https://www.justice.gov/atr/case-document/file/1141731/download. The statement is based on a false premise. There are not two levels of marketing in a business format franchise. *All* of the marketing occurs through the franchisee and at the franchisee's level. To the extent a franchisor may be deemed to be marketing licenses, as opposed to branded goods or services, any analogy to downstream distribution restraints fails, because franchisees are not in the business of selling licenses.

restrictions incident to a franchise agreement is properly subject to the same rule-of-reason test as vertical distribution restraints, because both promote interbrand competition.

III. No-Hire Clauses Are Not Per Se Violations of Section 1

Plaintiffs allege in several cases that the no-hire restriction is per se illegal under Section 1.[55] This core claim has been variously formulated. One case alleged that, by signing the franchise agreement, franchisees "tacitly agreed not to hire one another's employees."[56] It is alleged in another case that the no-hire clause is per se illegal as a "market allocation agreement."[57] Another set of plaintiffs alleged that the franchisor "orchestrated an agreement amongst the franchisees not to hire each other's employees," the effects of which were felt "strictly at the horizontal level" between franchisees.[58] Some courts have declined to grant motions to dismiss the claim of per se illegality.[59] The motions should have been granted, however, because the claim has no support in the law.

Since the Supreme Court's holding in *Leegin Creative Leather Products v. PSKS, Inc.*[60] that resale price maintenance agreements are not per se illegal, only horizontal restraints "qualify as unreasonable *per se*."[61] The rule of reason is the accepted standard for testing whether a practice restrains trade in violation of Section 1,[62] and not even horizontal restraints will be deemed per se unlawful "until we have amassed 'considerable experience with the type of restraint at issue' and 'can predict with confidence that it would be invalidated in all or almost all circumstances.'"[63] The per se test should not apply to no-hire clauses. They are not the product of agreement among horizontal competitors, and the fact that they have horizontal effects is irrelevant.

55. *See* Ogden v. Little Caesar Enters., 393 F. Supp. 3d 622, 631–36 (E.D. Mich. 2019) (granting motion to dismiss complaint for failure to state a claim for violation of § 1 under either per se rule or quick-look rule of reason); 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) (holding that complaint stated claim for violation of § 1 under per se rule and quick-look rule of reason); Butler v. Jimmy John's Franchise, LLC, 331 F. Supp. 3d 786, 795–97 (S.D. Ill. 2018) (same); Yi v. SK Bakeries, LLC, No. 18-5627 RJB, 2018 U.S. Dist. LEXIS 220966, at *14–15 (W.D. Wash. Nov. 13, 2018) (holding that complaint stated claim for violation of § 1 under quick-look rule of reason; motion to dismiss granted as to *per se* claim); Deslandes v. McDonald's USA, LLC, No. 17 C 4857, 2018 U.S. Dist. LEXIS 105260, at *20–23 (N.D. Ill. June 25, 2018) (same).

56. *Blanton*, 2019 U.S. Dist. LEXIS 87737, at *12.

57. *In re* Papa John's Emp. & Franchisee Emp. Antitrust Litig., No. 3:18-CV-00825-JHM, 2019 WL 5386484, at *8 (W.D. Ky. Oct. 21, 2019).

58. *Butler*, 331 F. Supp. 3d at 795.

59. *See Blanton*, 2019 U.S. Dist. LEXIS 87737, at *12; *Butler*, 331 F. Supp. 3d at 797; *In re Papa John's*, 2019 WL 5386484, at *9; Robinson v. Jackson Hewitt, Inc., No. 19-9066 (SDW) (LDW), 2019 U.S. Dist. LEXIS 188962, at *17 (D.N.J. Oct. 31, 2019).

60. Leegin Creative Leather Prods. v. PSKS, Inc., 551 U.S. 877 (2007).

61. Ohio v. Am. Express Co., 138 S. Ct. 2274, 2284 (2018) (italics in original).

62. *Leegin*, 551 U.S. at 885.

63. NCAA v. Alston, 141 S. Ct. 2141, 2156 (2021) (quoting *Leegin*, 551 U.S. at 886–87).

No horizontal conspiracy. Nothing about a promise by a franchisee not to solicit or hire another franchisee's employees could be characterized as the product of a horizontal agreement. There is no agreement between competing independent entities.[64] There is, instead, a separate agreement between the franchisor and each franchisee. To date, no one has argued, nor could they realistically argue, that a no-hire clause was included in a franchise agreement pursuant to a separate conspiracy between the franchisor and one or more franchisees. The no-hire clause in a franchise agreement is uniform from one franchisee to the next, as one would expect in a document unilaterally formulated by the franchisor for regional or national application,[65] filed with multiple state regulators, and delivered to all prospective franchisees. Any claim that the franchisor sits at the center of a hub-and-spoke conspiracy[66] fails, because there is no agreement between any of the spokes.[67] There is no claim in any of the pending cases that franchisees in any local market agreed among themselves not to hire each other's employees.

No exclusion of the possibility of independent action. Plaintiffs allege in some of the cases that franchisees conspired among themselves not to compete for labor,[68] but, to survive summary judgment and reach a jury, evidence of an agreement or conspiracy under Section 1 must tend to exclude the possibility of independent action.[69] Evidence of franchisees executing identical franchise agreements does not exclude the possibility of independent

64. This is to be distinguished from agreements between competitors not to solicit or hire each other's employees. *See supra* notes 9–13 and accompanying text.

65. A franchise agreement is the product of the franchisor, and provisions in the agreement restricting franchisee activity are unilaterally imposed. They are not the product of negotiation between an individual franchisee and the franchisor. *See, e.g.*, St. Martin v. KFC Corp., 935 F. Supp. 898, 906 (W.D. Ky. 1996) ("KFCC's company town policy and non-KFC clause were unilaterally formulated and implemented by KFCC itself.").

66. For such a claim, see *Butler v. Jimmy John's Franchise, LLC*, 331 F. Supp. 3d 786, 795 (S.D. Ill. 2018) ("Jimmy John's headquarters orchestrated an agreement amongst the franchisees not to hire each other's employees, and while the contract in question may have been vertical, the *effects* are felt strictly at the horizontal level: Between the franchisees, not between any given franchisee and Jimmy John's corporate. . . . Some circuits refer to this as a 'hub-and-spoke' conspiracy. . . ." (italics in original)).

67. *See, e.g.*, PSKS, Inc. v. Leegin Creative Leather Prods., 615 F.3d 412, 420 (5th Cir. 2010) (no hub-and-spoke conspiracy, because plaintiff had not alleged agreement among retailers to implement resale price maintenance (RPM). "In the absence of an assertion that retailers agreed to RPM among themselves, there was no wheel and therefore no hub-and-spoke conspiracy . . .".)

68. *E.g.*, *In re* Papa John's Emp. & Franchisee Emp. Antitrust Litig., No. 3:18-CV-00825-JHM, 2019 WL 5386484, at *7 (W.D. Ky. Oct. 21, 2019) ("Plaintiffs allege that the Defendants conspired to not compete for labor among their franchisees" and that franchisees had opportunities to conspire at annual meetings.).

69. *E.g.*, Bell Atl. Corp. v. Twombly, 550 U.S. 544, 556–57 (2007) (explaining conspiracy pleading requirements under § 1 needed to survive motion to dismiss); Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 588 (1986) ("To survive a motion for summary judgment or for a directed verdict, a plaintiff seeking damages for a violation of § 1 must present evidence 'that tends to exclude the possibility' that the alleged conspirators acted independently." (citing Monsanto Co. v. Spray-Rite Serv. Corp., 465 U.S. 752, 764 (1984)); Quality Auto Painting Ctr. v. State Farm Indem. Co., 917 F.3d 1249, 1261–72 (11th Cir. 2019) (en banc) (noting that allegations of horizontal price fixing and group boycott did not exclude possibility of independent action by insurers).

action. The no-hire clause to which each franchisee has agreed is embodied in the franchise agreement that it received and potentially negotiated with its franchisor; it is not the product of franchisee collusion. Nor is it the result of collusion with a franchisor, which undoubtedly included the clause in the franchise agreement without attention to the needs or wants of any specific franchisee. Even if plaintiffs could point to evidence of agreement among franchisees to refrain from hiring each other's employees, that evidence would not tend to exclude the possibility that a franchisee acted independently in both executing a franchise agreement containing a no-hire clause and in deciding to comply with its provisions, including the no-hire clause.

The fact that a franchisor may be party to hundreds, or even thousands, of separate agreements with individual franchisees provides no evidence of any agreement between franchisees not to hire each other's employees. This is parallel conduct, not an agreement between franchisees.[70] Agreement between franchisees not to hire each other's employees would be superfluous, in any event, as it would add nothing to a franchisee's obligation to comply with the terms of its own franchise agreement.

Intrabrand restraints produce horizontal effects. The per se rule has no application to vertical agreements,[71] and it can have no application to a trademark license restraint having the same economic effect as a vertical restraint (i.e., enhancement of interbrand competition).[72] No-hire clauses have horizontal

70. On analogous facts, the Seventh Circuit affirmed dismissal of conspiracy claims against distributors that had entered into supply contracts with allegedly anticompetitive terms. The fact that individual distributors each agreed with their common supplier on identical contract terms evidenced parallel conduct, not a conspiracy among the distributors. *See* Marion Healthcare, LLC v. Becton Dickinson & Co., 952 F.3d 832, 843 (7th Cir. 2020) ("These allegations, whether taken alone or together, do not suffice to establish a hub-and-spokes conspiracy. All the Providers have alleged is that the distributors buy and sell the devices [manufactured by defendant, Becton Dickinson] in accordance with the terms of the contracts that the GPOs [group purchasing organizations] have negotiated [with Becton Dickinson]. They have made no argument that the distributors played any role in setting the anticompetitive pricing or that there was any *quid pro quo* according to which Becton compensated them for participating in the alleged antitrust conspiracy." (italics in original)). *Accord*, *e.g.*, *In re* Musical Instruments & Equip. Antitrust Litig., 798 F.3d 1186, 1198 (9th Cir. 2015) ("Plaintiffs have indeed provided a context for the manufacturers' adoption of [allegedly unlawful] MAP policies, but not one that plausibly suggests they entered into illegal horizontal agreements. Instead, the complaint tells a different story, one in which Guitar Center used its substantial market power [as a high-volume purchaser] to pressure each manufacturer to adopt similar policies, and each manufacturer adopted those policies as in its own interest.").

71. *See* Leegin Creative Leather Prods. v. PSKS, Inc., 551 U.S. 877, 893, 898–99 (2007) (rejecting per se illegality for resale price maintenance agreements while observing that a "horizontal cartel among competing manufacturers or competing retailers that decreases output or reduces competition in order to increase price is, and ought to be, *per se* unlawful" (italics in original)); Cont'l T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 58–59 (1977) (rejecting per se treatment for non-price vertical restraints).

72. The equivalence of economic effect has led to occasional description of franchise agreement restraints as "vertical." *See supra* note 53 and accompanying text; Randy M. Stutz, *The Evolving Antitrust Treatment of Labor-Market Restraints: From Theory to Practice* 18 Am. Antitrust Inst. (July 31, 2018), https://www.antitrustinstitute.org/wp-content/uploads/2018/09/AAI-Labor-Antitrust-White-Paper_0.pdf (noting that "franchisor/franchisee no-poaching

effects insofar as they reduce intrabrand competition between retailers, but this is equally true for purely benign vertical restraints. The very purpose of vertical restraints is to limit competition between downstream resellers, and the presence of horizontal effects provides no basis for applying the per se rule.[73] Only horizontal restraints are per se illegal,[74] and horizontal restraints involve agreements between rival firms not to compete.[75]

Horizontal effects incident to a vertical restraint are not evidence of any agreement between competitors to fix prices, rig bids, allocate territories or customers, or otherwise restrain trade. They are the intended consequence of a vertical restraint. A reduction in intrabrand competition by, for example, prohibiting out-of-territory sales may strengthen the manufacturer's position as against other brands. Economically, a no-hire clause serves the same purpose—to strengthen the franchisor's interbrand competitive standing—and it does so by reducing competition between franchisees for labor.

Dual distribution restraints are subject to the rule of reason. Nor is the per se rule applicable insofar as a no-hire clause bars a franchisee from soliciting or hiring workers employed at competing stores owned by the franchisor. The restraint is not implemented pursuant to agreement between franchisees. A trademark owner is free to control the scope of rights granted under a license, and there is no Sherman Act violation, for example, in confining a licensee to an exclusive territory.[76] Limiting a franchisee, pursuant to a license agreement, in the firms from which it can solicit and hire employees is, similarly, exercise of control over the scope of the license grant. Although such a no-hire restraint limits intrabrand competition between firms selling

agreements are vertical"). The Department of Justice applied the same label in a *Statement of Interest* filed in the no-hire clause litigation. *See supra* note 54.

73. *See, e.g.*, Bus. Elecs. Corp. v. Sharp Elecs. Corp., 485 U.S. 717, 730 n.4 (1988) (Even though vertical restraints have horizontal effects, they are not horizontal: "[A] restraint is horizontal not because it has horizontal effects, but because it is the product of a horizontal agreement."); *Cont'l T.V., Inc.*, 433 U.S. at 54 ("Vertical restrictions reduce intrabrand competition by limiting the number of sellers of a particular product competing for the business of a given group of buyers.").

74. *See, e.g.*, Ohio v. Am. Express Co., 138 S. Ct. 2274, 2283–84 (2018) ("Typically only 'horizontal' restraints—restraints 'imposed by agreement between competitors'—qualify as unreasonable *per se*." (citation omitted; italics in original)); NYNEX Corp. v. Discon, Inc., 525 U.S.128, 135 (1998) (noting that "precedent limits the *per se* rule in the boycott context to cases involving horizontal agreements between direct competitors" (italics in original)).

75. *E.g.*, *Am. Express Co.*, 138 S. Ct. at 2285 n.7 ("[H]orizontal restraints involve agreements between competitors not to compete in some way."); Bus. Elecs. Corp. v. Sharp Elecs. Corp., 485 U.S. 717, 730 (1988) ("Restraints imposed by agreement between competitors have traditionally been denominated as horizontal restraints . . . ."); Valley Liquors, Inc. v. Renfield Imps., Ltd., 678 F.2d 742, 744 (7th Cir. 1982) ("[A] horizontal conspiracy is one between two or more competing sellers.").

76. *See, e.g.*, Denison Mattress Factory v. Spring-Air Co., 308 F.2d 403, 409 (5th Cir. 1962) ("A trademark owner may extend the territory in which he has the right to exclusive use of his trademark, either by expanding his own operations, or he may introduce his trademark and create a demand for his variety of goods in new territory, by licenses subject to his control. . . . [S]pring-Air . . . had a right to license its trademark to exclusive dealers. . . . It is our opinion that the provision of the contract with respect to a division of trade territory in the circumstances of this case is not offensive to the antitrust laws.").

at the same distribution level, it is subject to the rule of reason as a dual distribution restraint. Dual distribution restraints imposed by a business format franchisor are subject to the rule of reason,[77] in common with dual distribution restraints imposed by manufacturers on independent dealers and distributors.[78] They limit intrabrand competition in furtherance of promotion of interbrand competition.

Trademark licensing agreements are subject to the rule of reason. Attempts to apply the per se rule to restraints in franchise agreements or other agreements licensing trademarks have repeatedly been rejected. The Fifth Circuit, for example, rejected a claim that an approved-source requirement in a Kentucky Fried Chicken franchise agreement was per se illegal.[79] It refused to apply the per se rule because, in the franchise context, such a requirement might be procompetitive:

> We are not prepared to say . . . that approved source requirements are so universally devoid of redeeming virtue that they warrant per se treatment. . . . [T]ies themselves are not as completely objectionable in the franchise context as in the contexts in which tying law originally developed. Moreover, franchise arrangements may sometimes create better competitive markets than would otherwise exist. A system under which an independent franchisee's choices are somewhat restricted may nevertheless prove superior to a system in which retail outlets are owned by the national firm. . . .
>
> . . . [T]he potential pro-competitive effects of franchising lead us to proceed cautiously lest we unduly shackle franchisors without achieving discernible competitive benefits. We must encourage business ingenuity so long as it is not competitively stifling.[80]

77. *See, e.g.*, Krehl v, Baskin-Robbins Ice Cream Co., 664 F.2d 1348, 1356–57 (9th Cir. 1982) (holding that territorial restraints imposed by trademark owner and franchisor on licensees (referred to as "area franchisors") were subject to rule of reason even though owner/franchisor competed at the same distribution level, through a wholly owned subsidiary, with the area franchisors); St. Martin v. KFC Corp., 935 F. Supp. 898, 904–06 (W.D. Ky. 1996) (holding that prohibition in franchise agreement against franchisee operation of a store in a geographic market served by a franchisor-owned store is a dual distribution restraint subject to the rule of reason).

78. *See, e.g.*, Jacobs v. Tempur-Pedic Int'l, 626 F.3d 1327, 1340 n.15 (11th Cir. 2010) (noting that the "recent trend" has been to view dual distribution restraints as vertical subject to the rule of reason); PSKS, Inc. v. Leegin Creative Leather Prods., 615 F.3d 412, 421 n.8 (5th Cir. 2010) (observing that "eight other circuits have applied the traditional rule of reason to dual distribution systems" (citations omitted)); AT&T Corp. v. JMC Telecom, LLC, 470 F.3d 525, 531 (3d Cir. 2006) ("Vertical restraints are generally not *per se* violations of the Sherman Act, even where a distributor and manufacturer also compete at the distribution level, *i.e.*, have some form of horizontal relationship (a/k/a dual distributor arrangement), as is the case here." (italics in original)); Elecs. Commc'ns Corp. v. Toshiba Am. Consumer Prods., 129 F.3d 240, 243 (2d Cir. 1997) (holding that dual distribution restraints are vertical and subject to the rule of reason); Smalley & Co. v. Emerson & Cuming, Inc., 13 F.3d 366, 368 (10th Cir. 1993) (holding that rule of reason was properly applied to a claim of horizontal market allocation because "dual distribution systems like that utilized by E & C are in fact vertical, not horizontal restraints on competition"); Ill. Corp. Travel, Inc. v. Am. Airlines, 889 F.2d 751, 753 (7th Cir. 1989) ("Dual distribution therefore does not subject to the per se ban a practice that would be lawful if the manufacturer were not selling direct to customers; antitrust laws encourage rather than forbid this extra competition.").

79. *See* Ky. Fried Chicken Corp. v. Diversified Packaging Corp., 549 F.2d 368 (5th Cir. 1977).

80. *Id.* at 379; *accord, e.g.*, *St. Martin*, 935 F. Supp. at 905 (rejecting per se treatment for provisions in franchise agreement prohibiting franchisee from operating a store in a market in

Challenging a requirement in a trademark license for mattresses that innersprings and other components be purchased from approved sources, a licensee of the Spring-Air trademark contended that the requirement was a per se illegal tying agreement.[81] The court refused to apply the per se test, because the licensor was not supplying any of the components. It noted that the sourcing requirement served a salutary purpose in protecting the value of the licensor's mark: "The trademark would be of no worth unless the public could be sure that every mattress which bore that mark was uniform both in exterior design and interior quality."[82]

Because no-hire clauses are not the product of a horizontal agreement among competing franchisees, their creation and enforcement are not per se illegal under Section 1. They have not previously been subjected to judicial scrutiny and, on this ground alone, should not be deemed per se illegal.[83] They must be evaluated under the rule of reason.

IV. Evaluating No-Hire Clauses Under the Rule of Reason

Employees bringing no-hire clause cases do not challenge the legality of the franchise agreements to which their employers are party. There is no hint that there is any antitrust violation in the fact that their employer executed a franchise agreement (nor could there be). The litigation is aimed, instead, at a specific provision in the agreement—the no-hire clause. As a restraint appurtenant to the main agreement between a franchisee and its franchisor, the legality under the Sherman Act of a no-hire clause is subject to the ancillary restraint doctrine.

An ancillary restraint is lawful, because it is subordinate to a legitimate transaction and "serves to make the main transaction more effective in accomplishing its purpose."[84] To be ancillary, the restraint must "contribute to the success of a cooperative venture that promises greater productivity and output"[85] and be related to "the efficiency sought to be achieved."[86]

which the franchisor operated a store and prohibiting a franchisee from having an interest in a fast food outlets other than KFC, since the restrictions "could potentially increase interbrand competition").

81. *See* Denison Mattress Factory v. Spring-Air Co., 308 F.2d 403 (5th Cir. 1962).

82. *Id.* at 410–11; *see also*, *e.g.*, Evans v. S.S. Kresge Co., 544 F.2d 1184, 1193 (3d Cir. 1976) (rejecting claim by licensee of K-Mart trade name that restriction against handling goods competitive with those sold by the licensor, S.S. Kresge Co., in K-Mart stores in which licensee sold groceries was per se illegal, since this and other license restraints "had as their purpose the stimulation of business and efficiency for both the department store and the supermarket" within a single K-Mart store).

83. *See*, *e.g.*, White Motor Co. v. United States, 372 U.S. 253, 263 (1963) ("We need to know more than we do about the actual impact of these arrangements on competition to decide whether they have such a 'pernicious effect on competition and lack . . . any redeeming virtue' . . . and therefore should be classified as *per se* violations of the Sherman Act." (citation omitted; italics in original)).

84. Rothery Storage & Van Co. v. Atlas Van Lines, Inc., 792 F.2d 210, 224 (D.C. Cir. 1986).

85. Polk Bros., Inc. v. Forest City Enters., 776 F.2d 185, 189 (7th Cir. 1985).

86. *Rothery Storage & Van Co.*, 792 F.2d at 224.

Agreements that would otherwise be per se illegal naked restraints between competitors are ancillary if, for example, they limit competition by members of a joint venture with the venture itself;[87] prevent free riding by a party to an agreement creating a jointly operated retail outlet;[88] prevent the seller of a business from hiring employees from the business after its sale to a third party;[89] prevent a party to an agreement for supplying traveling nurses to hospitals from soliciting the other party's employees;[90] restrict the sources from which a trademark licensee can buy components for the manufacture of finished goods to be sold under the licensor's mark;[91] or require members of a joint venture to authorize the joint venture to act as the exclusive licensor for all members' intellectual property rights.[92]

If a restraint is ancillary, it thereby escapes condemnation as a per se violation of Section 1.[93] Some case law suggests that an ancillary restraint is, *ipso*

87. *See*, *e.g.*, *id.* at 229–30 (approving rule adopted by joint venture prohibiting members from competing against it for their own account).

88. *See Polk Bros.*, *Inc.*, 776 F.2d at 190 (holding that agreement between competing firms to allocate products each could sell within a single retail outlet that they had agreed to build and jointly occupy was ancillary to the joint venture and therefore subject to rule of reason).

89. *See* Cesnik v. Chrysler Corp., 490 F. Supp. 859, 868 (M.D. Tenn. 1980) (noting that covenant prohibiting Chrysler from hiring employees from its Airtemp Division after selling the division to Fedders was "reasonably calculated to protect the legitimate interests of the purchaser in what he has purchased" (citation omitted)).

90. *See* Aya Healthcare Servs. v. AMN Healthcare, Inc., 2021 U.S. App. LEXIS 24794, at *13–14 (9th Cir. Aug. 19, 2021) ("We agree with the district court that the challenged restraint is reasonably necessary to the parties' procompetitive collaboration. The purpose of the parties' contract was to supply hospitals with traveling nurses. The non-solicitation agreement is necessary to achieving that end because it ensures that AMN will not lose its personnel during the collaboration.").

91. *See* Denison Mattress Factory v. Spring-Air Co., 308 F.2d 403, 410–11 (5th Cir. 1962) ("[I]t is our duty to determine whether the general primary purpose of the contract under consideration was to protect Spring-Air in its product, and then determine whether the provisions of the contract complained of here violate any antitrust law.").

92. *See* Major League Baseball Props., Inc. v. Salvino, Inc., 542 F.3d 290, 340 (2d Cir. 2008) (Sotomayor, J., concurring) ("In this case, the exclusivity and profit-sharing provisions of the MLBP [joint venture] agreement are reasonably necessary to achieve MLBP's efficiency-enhancing purposes because they eliminate several potential externalities that may otherwise distort the incentives of individual [baseball] Clubs and limit the potential efficiency gains of MLBP. . . . Most notable of these externalities is the so-called free-rider problem. . . . Under such circumstances, the challenged restraints must be viewed as ancillary to the joint venture and reviewed under the rule of reason in the context of the joint venture as a whole." (footnote omitted)).

93. *See*, *e.g.*, *Aya Healthcare Servs.*, 2021 U.S. App. LEXIS 24794, at *13 ("Accordingly, the restraint qualifies as an ancillary restraint, which triggers a rule-of-reason analysis." (footnote omitted)); Rothery Storage & Van Co. v. Atlas Van Lines, Inc., 792 F.2d 210, 224 (D.C. Cir. 1986) (holding that restraint was ancillary "and hence exempt from the per se rule"); *Polk Bros.*, *Inc.*, 776 F.2d at 190 ("The reason for discriminating between 'ancillary' and 'naked' restraints is to determine whether the agreement is part of a cooperative venture with prospects for increasing output. If it is, it should not be condemned *per se*. . . . The Rule of Reason therefore applies."); Staley v. Gilead Scis., Inc., 446 F. Supp. 3d 578, 594–98 (N.D. Cal. 2020) (holding that ancillary restraints are subject to evaluation under the rule of reason).

facto, lawful under Section 1,[94] but the fact that a restraint is ancillary is not enough. The restraint is still subject to evaluation under the rule of reason.[95]

The procedure for testing the legality of a restraint under the rule of reason is now largely settled,[96] and evaluation is a three-step process.[97] First, it must be determined whether the restraint has a substantial anticompetitive effect in a relevant market—that is, does it harm consumers by raising prices or limiting output? In a labor market, does it harm employees by depressing wages and benefits? This is the plaintiff's burden of proof. Without market power, a firm will not, in most cases, have the power to control prices or restrain output. In the case of a buyer-sided market such as hiring by franchisees, it must be determined whether the buyer has monopsony power.[98]

Preliminary, however, to any showing of market power or monopsony power, a plaintiff must prove the metes and bounds of the relevant product or service market and the relevant geographic market. Economic power cannot be measured until the relevant market is defined.[99] This first step—showing anticompetitive effects in a relevant market—operates as a filter, and there is no need to go to the second step in rule-of-reason analysis if a firm lacks market power or monopsony power.[100]

If a restraint does have substantial anticompetitive effects, the second step in rule-of-reason analysis is to determine whether there is a procompetitive justification for it—that is, does it strengthen the manufacturer's position

94. *See, e.g.*, Texaco Inc. v. Dagher, 547 U.S. 1, 7 (2006) ("Under the [ancillary restraints] doctrine, courts must determine whether the nonventure restriction is a naked restraint on trade, and thus invalid, or one that is ancillary to the legitimate and competitive purposes of the business association, and thus valid."); *Rothery Storage & Van Co.*, 792 F.2d at 224 ("If [Judge] Taft's formulation [in *United States v. Addyston Pipe & Steel Co.*, 85 F. 271 (6th Cir. 1898), *aff'd*, 175 U.S. 211 (1899)] is the law today, it is obvious that the Atlas agreements are legal, for *Addyston Pipe & Steel's* analysis of ancillary restraints fits this case exactly.").

95. *See, e.g.*, *Aya Healthcare Servs.*, 2021 U.S. App. LEXIS 24794, at *16 ("Given that the restraint is ancillary to the parties' broader agreement, the district court correctly subjected it to the rule-of-reason standard."); Princo Corp. v. ITC, 616 F.3d 1318, 1336 (Fed. Cir. 2010) (en banc) ("The 'ancillary restraints' that are often important to collaborative ventures, such as agreements between the collaborators not to compete against their joint venture, are also assessed under the rule of reason."); Polk Bros., Inc. v. Forest City Enters., 776 F.2d 185, 190 (7th Cir. 1985) (since restraint was ancillary, its legality was tested under the rule of reason).

96. The Supreme Court applied the rule of reason to vertical restraints in *Ohio v. Amercian Express Co.*, 138 S. Ct. 2274 (2018), using a "three-step, burden-shifting framework," *id.* at 2284. It followed the same framework in applying the rule of reason to restraints incident to a joint venture in *NCAA v. Alston*, 141 S. Ct. 2141, 2160–62 (2021).

97. *E.g.*, *Am. Express Co.*, 138 S. Ct. at 2284.

98. *See, e.g.*, Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co., 549 U.S. 312, 320 (2007) ("Monopsony power is market power on the buy side of the market.").

99. *See, e.g.*, *Am. Express Co.*, 138 S. Ct. at 2285 n.7 (noting that market power "cannot be evaluated unless the Court first defines the relevant market").

100. *E.g.*, SCFC ILC, Inc. v. Visa USA, Inc., 36 F.3d 958, 965 (10th Cir. 1994) ("Proof of market power, then, for many courts is a critical first step, or 'screen' or 'filter,' which is often dispositive of the case." (footnote omitted)); Valley Liquors, Inc. v. Renfield Imps., Ltd., 822 F.2d 656, 666 (7th Cir. 1987) ("A threshold inquiry in any Rule of Reason case is whether the defendant had market power, that is, the 'power to raise prices significantly above the competitive level without losing all of one's business.'" (citation omitted)).

in relation to competitors? This showing is the defendant's burden.[101] If the restraint does have a procompetitive justification, the third step is to determine whether the same benefits and efficiencies could be achieved through less restrictive means. This showing is the plaintiff's burden.[102] If the plaintiff shows that less restrictive means are available, the restraint violates Section 1.[103]

When no-hire clauses are tested under the rule of reason, there is no cognizable restraint of trade.

Economic power in a relevant market. Once a relevant market has been defined for purposes of measuring the competitive impact of a no-hire clause—as it must be for the first step in rule-of-reason analysis—it becomes apparent that none of the franchisors in the reported cases has monopsony power. The restriction on solicitation and hiring is limited to franchisees under a single trademark, and a single brand of goods or services cannot, with isolated exceptions not pertinent here, constitute a relevant market.[104]

The relevant product or service market for measuring franchisor monopsony power comprises companies that actively compete for the services of a specific employee (i.e., the universe of employers to which the employee can turn for work).[105] No-hire clauses prevent an employee from going to work for an employer operating under the same brand as his or her employer, but an employee is free to sell his or her services to any employer other than one operating under the trademark used by the current employer. The no-hire clause has no effect on the ability of an employee to seek work outside the franchise system. The relevant labor market for plaintiffs suing fast-food franchisors includes, thus, not merely hiring by franchisees or franchisor-owned stores operating under the same brand but also hiring by other quick-serve restaurants.[106]

101. *See Am. Express Co.*, 138 S. Ct. at 2284.

102. *See id.*

103. *See, e.g.*, NCAA v. Alston, 141 S. Ct. 2141, 2162 (2021) (affirming finding by district court that substantially less restrictive rules could have been implemented by the NCAA to regulate education-related benefits offered by colleges to student athletes).

104. *See, e.g.*, PSKS, Inc. v. Leegin Creative Leather Prods., 615 F.3d 412, 418 (5th Cir. 2010) (noting that district court "also correctly rejected the claim that Brighton products constitute their own market"); Todd v. Exxon Corp., 275 F.3d 191, 200 (2d Cir. 2001) (noting that dismissal for failure to allege a relevant market is appropriate when plaintiff has attempted "to limit a product market to a single brand, franchise, institution, or comparable entity that competes with potential substitutes" (footnote omitted)); Generac Corp. v. Caterpillar, Inc., 172 F.3d 971, 977 (7th Cir. 1999) ("Product markets are not defined in terms of one trademark or another; trademarks simply identify the origin of a product.").

105. *See, e.g.*, *Todd*, 275 F.3d at 202 (relevant market in labor monopsony case comprised employers that are seen by plaintiff employees as "reasonably good substitutes"); Eichorn v. AT&T Corp., 248 F.3d 131, 147–48 (3d Cir. 2001) ("We agree with the District Court that the relevant market is not limited to AT&T and its affiliates but rather includes all those technology companies and network services providers who actively compete for the employees with the skills and training possessed by plaintiffs.")

106. *See, e.g.*, Conrad v. Jimmy John's Franchise, LLC, No. 18-CV-00133-NJR, 2021 U.S. Dist. LEXIS 142272, at *39 (S.D. Ill. July 23, 2021) ("[T]he relevant labor market includes not merely Jimmy John's franchisees but also other quick-serve restaurants. . . .").

The boundaries of the other component of market definition, the relevant geographic market, will vary by franchisee, but they can be expected to correspond to a radius described by the distance that an employee will travel to a place of employment.[107] Within any such geographic market, an individual can turn to multiple potential employers, and the opportunities for employment can be expected to increase in proportion to an increase in the population density within the travel radius.

Without regard to any specific market, it is apparent that no franchisor could have monopsony power in a relevant market thus defined. Assuming, for example, a geographic market with twenty McDonald's restaurants, a no-hire clause restraining the movement of employees from one McDonald's restaurant to another would have no effect on their access to employment at other fast-food restaurants selling hamburgers (let alone fast-food restaurants generally) within the geographic market (e.g., Burger King, Wendy's, Arby's, Hardee's, Carl's, Big Boy). While the switching costs to an employee would be minimized by simply transferring to another employer within the same franchise system,[108] the skill sets of employees affected by no-hire clauses, whether managerial or hourly, are readily transferable to restaurants operating under competing brands, not to mention to other types of quick-service restaurants (e.g., Jimmy John's, Papa John's, Little Caesar, Domino's Pizza). Even if employees are categorized at the six-digit occupation level used in the Standard Occupational Classification Manual—like Cooks, Fast Food (35-2011); Fast Food and Counter Workers (35-3023)[109]—the employment alternatives within a geographic market will almost certainly greatly exceed the number of franchised locations affected by a no-hire clause.

The defendant's expert in the *Jimmy John's* case calculated that the vast majority of Jimmy John's branded restaurants have at least ten other quick-service restaurant brands within a ten-mile radius and that, on average, each store has 53 such nearby brands at 257 locations.[110] Given the number of employment alternatives within the relevant market, the no-hire clause would not, in the expert's judgment, produce any adverse competitive effects.[111] No matter which local geographic market were selected, it could be expected that the availability of out-of-franchise employers would be

107. It has been proposed that the geographic market should be defined by the employee's commuting zone. *See* Marinescu & Posner, *supra* note 14, at 1352–53, 1389. In denying class certification in the McDonald's litigation, the court observed that the evidence "bears out the intuition that the proposed class members sell their labor in local geographic markets, generally within easy commuting distance." Deslandes v. McDonald's USA, LLC, No. 17 C 4857, 2021 U.S. Dist. LEXIS 140735, at *34 (N.D. Ill. July 28, 2021).

108. For discussion of switching costs as a barrier to employee mobility, see Marinescu & Posner, *supra* note 14, at 1353–54.

109. U. S. Office of Mgmt. and Budget, Standard Occupational Classification Manual 123, 124 (2018), https://www.bls.gov/soc/2018/soc_2018_manual.pdf. For use of the SOC system in defining a labor market, see Marinescu & Posner, *supra* note 14, at 1352–53.

110. *See* Conrad v. Jimmy John's Franchise, LLC, No. 18-CV-00133-NJR, 2021 U.S. Dist. LEXIS 33933, at *23 (S.D. Ill. Feb. 16, 2021).

111. *Id.* at *23–24.

comparable. A franchisee would face competition from multiple employers outside the franchise in its efforts to hire workers.

In the absence of market power—here, monopsony power—there is no possibility that a restraint will have a substantial anticompetitive effect. Without it, there is no basis for advancing to the second step in rule-of-reason inquiry—that is, whether there is a procompetitive justification for the restraint. But considering that step supports this article's conclusion, because it demonstrates that, in a business format franchise, a no-hire clause is procompetitive.

Procompetitive justifications for no-hire clauses. Entirely separate from the fact that a franchisor could have no economic power in any relevant market, there are obvious procompetitive justifications for a no-hire clause. Even though a court should never advance to this second step in rule-of-reason analysis in a no-hire clause case, the procompetitive effects underscore the fallacy of Section 1 claims aimed at no-hire clauses in franchise agreements.

The justification for an ancillary restraint is measured at the time that it is entered, not at the time that it has competitive effects. Comparing a restraint ancillary to a joint venture agreement to an employee noncompetition covenant, the Seventh Circuit held in *Polk Bros., Inc. v. Forest City Enterprises*[112] that the legality of the restraint must be "viewed at the time it was adopted."[113] In reliance upon a noncompetition covenant, a firm will invest in and train an employee for its benefit.[114] When the employment is over, "there is nothing left but restraint—but the aftermath is the wrong focus" for measuring legality.[115]

When the restraint at issue in *Polk Bros.* was analyzed for effects as of the time that it was adopted, the court found it to be ancillary to a "productive cooperation."[116] There, an appliance retailer, Polk Brothers, and a building supplies retailer, Forest City, agreed to operate at a single retail location in the interest of providing a full range of goods for furnishing and maintaining a home. In furtherance of the collaboration, they negotiated a covenant restricting the type of goods that each could sell at the location. The legality of the covenant under Section 1 was subject to the rule of reason:

> Polk Bros. and Forest City were cooperating to produce, not to curtail output; the cooperation increased the amount of retail space available and was at least potentially beneficial to consumers; the restrictive covenant made the

112. Polk Bros., Inc. v. Forest City Enters., 776 F.2d 185, 189 (7th Cir. 1985).

113. *Id.*; *see also* Blackburn v. Sweeney, 53 F.3d 825, 828 (7th Cir. 1995) ("*Polk* teaches that courts must look to the time an agreement was adopted in assessing its potential for promoting enterprise and productivity . . . ."); *accord* Aya Healthcare Servs. v. AMN Healthcare, Inc., 2021 U.S. App. LEXIS 24794, at *15 (9th Cir. Aug. 19, 2021) (holding that restraint was ancillary because, among other reasons, it "was entered into at the same time the parties agreed to collaborate on a joint venture").

114. *Polk Bros., Inc.*, 776 F.2d at 189 ("Knowing that he is not cutting his own throat by doing so, the employer will train the employee, giving him skills, knowledge, and trade secrets that make the firm more productive.")

115. *Id.*

116. *Id.* at 190.

cooperation possible. The Rule of Reason therefore applies. Discriminating analysis is necessary.[117]

When the effects of a no-hire clause are viewed as of the time a firm or individual executes a franchise agreement, they are demonstrably procompetitive. In a business format franchise, the success of the enterprise depends upon elimination of the free rider—the franchisee that cuts its costs by exploiting the investment of other franchisees. The no-hire clause protects against a franchisee avoiding the cost of training by, instead, hiring trained workers away from other stores in the franchise. The cost savings enable a free rider to undercut pricing by its intrabrand competitors, thereby driving all pricing down within a market and leading to reduced profits for those franchisees that have incurred the cost of employee training. The prospect of losing employees to competing franchisees not only may deter franchisees from investing in training but also may discourage firms or individuals from even buying a franchise in the first place. Without confidence that its franchise opportunity will be safeguarded against predation from other franchisees, a firm or individual will have little incentive to make the investment.

The need for a no-hire clause and other restraints arises from the inherent economic tension between the interests of a franchisor and its individual franchisees. The incentives of a franchisee and the franchisor are not aligned, because the franchisee's interest in increased profits can lead to conduct that, in the absence of contractual restraints, may undermine the goodwill of the franchise itself.[118] The conduct can range from saving on food costs by sourcing from non-approved suppliers, to ignoring franchisor requirements for service of fresh products, to deviating from required menu offerings, to saving on labor costs by understaffing or scrimping on training.

117. *Id.* Judge Easterbrook's invocation of an employee noncompetition covenant as an ancillary restraint analogous to the joint venture restraint under review in *Polk Bros.* was not entirely apt, since enforcement of the former is subject to a range of equitable criteria not relevant to ancillary restraint analysis under § 1. Whether the covenant is necessary to protect the legitimate interests of the covenantee is the only common criterion. *See, e.g.*, Reliable Fire Equip. Co. v. Arredondo, 965 N.E.2d 393, 396 (Ill. 2011) ("A restrictive covenant, assuming it is ancillary to a valid employment relationship, is reasonable only if the covenant: (1) is no greater than is required for the protection of a legitimate business interest of the employer-promisee; (2) does not impose undue hardship on the employer-promisor; and (3) is not injurious to the public."); BDO Seidman v. Hirshberg, 93 N.Y.2d 382, 388–89 (N.Y. 1999) ("The modern, prevailing common-law standard of reasonableness for employee agreements no to compete applies a three-pronged test. A restraint is reasonable only if it: (1) is *no greater* than is necessary for the protection of the *legitimate interest* of the employer, (2) does not impose undue hardship on the employee, and (3) is not injurious to the public." (emphasis in original)); Raimonde v. Van Vlerah, 325 N.E.2d 544, 547 (Ohio 1975) ("A covenant restraining an employee from competing with his former employer upon termination of employment is reasonable if it is no greater than is required for the protection of the employer, does not impose undue hardship on the employee, and is not injurious to the public.").

118. For discussion of the tension between franchisor and franchisee incentives, see generally Blair & Lafontaine, *supra* note 36, at 118–21. "[T]he individual franchisee's incentives are not aligned with those of the franchisor: the profit-maximizing behavior of an individual franchisee can have adverse external effects on the franchisor and other franchisees as well." *Id.* at 118 (footnote omitted).

The damage to goodwill resulting from such profit-maximizing conduct is readily foreseeable:

> [I]t would be expected that in the absence of [intra]brand restrictions, franchisees would cut corners on investments in brand quality, for example by reducing food quality or customer service to reduce costs. For any individual franchisee, the short-run cost to the overall brand reputation of such deviations is small because the store is just one of many stores, while the benefit in profit can be significant. However, if all stores behave this way, then the overall quality of the brand will deteriorate in the long-run, which will harm all stores.[119]

Crediting the analysis of McDonald's expert economist in *Deslandes v. McDonald's USA, LLC*,[120] the court there described the benefits of a no-hire clause in limiting free riding by individual franchisees:

> [T]he hiring restriction encourages franchisees to train their employees without fear that other outlets will free-ride on this training by hiring away employees trained in the McDonald's way. It also encourages cooperation among franchisees. For example, franchisees are required to manage their restaurants personally and are required to complete significant training . . . before signing a franchisee agreement. That training sometimes involves on-the-job training at an existing franchise restaurant. Absent the hiring restriction, current franchisees would be reluctant to allow potential franchisees to train in their restaurants for fear they would use the opportunity to recruit employees.[121]

The no-hire clause contributes to increased output in the hamburger market, "because it encourages the very training that enhances the brand (by ensuring uniform food quality, customer service and building cleanliness)."[122] A strong brand leads, in turn, to additional franchise outlets. New outlets must be staffed, and new restaurants thus increase output in the labor market by increasing demand for labor.[123]

Case law bears out the procompetitive benefits of restraints, such as a no-hire clause, incident to trademark licensing. Such restraints in licenses granted by single-firm licensors have consistently been validated under the rule of reason.[124] Even though they may prevent a licensee from engaging

119. Conrad v. Jimmy John's Franchise, LLC, No. 18-CV-00133-NJR, 2021 U.S. Dist. LEXIS 33933, at *26–27 (S.D. Ill. Feb. 16, 2021).

120. Deslandes v. McDonald's USA, LLC, No. 17 C 4857, 2021 U.S. Dist. LEXIS 140735 (N.D. Ill. July 28, 2021).

121. *Id.* at *23–24.

122. *Id.* at *24.

123. *Id.* at *25.

124. The fact that licensing is by an entity existing independently of any licensees is crucial, because use of trademark licensing to allocate territories or customers among horizontal competitors has been deemed per se illegal where the trademark is owned by a licensor under control of the licensees. *See, e.g.*, United States v. Topco Assocs., 405 U.S. 596, 608–12 (1972) (purchasing association whose stock was owned by grocery store chain members violated § 1 by granting members exclusive territories in which to sell Topco-brand products and prohibiting members from selling Topco-brand products at wholesale); United States v. Sealy, Inc., 388 U.S. 350, 354 (1967) (noting that trademark owner licensed its stockholders to make and sell mattresses under the Sealy brand in exclusive territories in violation of § 1: "The territorial arrangements must be regarded as the creature of horizontal action by the licensees. It would violate reality to treat them as equivalent to territorial limitations imposed by a manufacturer upon independent dealers as incident to the sale of a trademarked product. Sealy, Inc., is an

in activity that would otherwise be available to it, there is no Sherman Act violation. In furtherance of a trademark license, a requirement, for example, that the franchisee refrain from selling goods under any mark other than that of the franchisor does not violate Section 1.[125] Nor is Section 1 violated by a prohibition against a franchisee operating a competing business in the territory in which it has been licensed to use a mark.[126] There is no violation in prohibiting a licensee from selling goods under brands competitive with that of the licensor.[127] For example, restraints on operation of grocery stores under the K-Mart trade name and service mark did not violate Section 1 where they were necessary for protection of the K-Mart image.[128] A restriction allocating geographic markets between the trademark owner and its licensee did not violate Section 1 where "both parties restricted their actions somewhat in the interest of more efficient promotion of the covered products and better sales."[129]

Trademarks are non-exclusionary, and agreements to protect trademark interests are "common, and favored, under the law."[130] If a licensee deems the restrictions of a license too onerous, it is free to end the license and market goods or services under another brand.[131] In the case of a business format franchise, a firm or individual is free to walk away from investing in

instrumentality of the licensees for purposes of the horizontal territorial allocation."); Timken Roller Bearing Co. v. United States, 341 U.S. 593, 597–99 (1951) (license of Timken trademark to British and French affiliates of license owner held to be subsidiary to main purpose of the parties' agreement to allocate territories in violation of § 1); *In re* Blue Cross Blue Shield Antitrust Litig., 308 F. Supp. 3d 1241, 1279 (N.D. Ala. 2018) (since licensor of Blue Cross and Blue Shield service marks was owned and controlled by licensees, licenses granting exclusive service areas to individual licensees effectuated a scheme of horizontal restraints in violation of § 1: "Defendants' aggregation of a market allocation scheme together with certain other output restrictions is due to be analyzed under the *per se* standard of review." (italics in original)).

125. *See* Susser v. Carvel Corp., 206 F. Supp. 636, 647–48 (S.D.N.Y. 1962) (approving exclusive dealing requirement), *aff'd*, 332 F.2d 505 (2d Cir. 1964).

126. *See* St. Martin v. KFC Corp., 935 F. Supp. 898, 902–04 (W.D. Ky. 1996) (approving a prohibition against a KFC franchisee operating a restaurant under another brand in the territory granted in the trademark license).

127. *See, e.g.*, Denison Mattress Factory v. Spring-Air Co., 308 F.2d 403, 412 (5th Cir. 1962) (rejecting claim by mattress manufacturer that trademark licensor's requirement that it refrain from selling mattresses under competing national brands was a per se violation of § 1).

128. *See* Evans v. S.S. Kresge Co., 394 F. Supp. 817, 846 (W.D. Pa. 1975) (rejecting per se treatment for restraints intended to ensure that licensee, an independent grocery store owner, operated stores under the K-Mart mark consistently with the trademark owner's objective of "attracting customers into the K-Mart stores by providing convenient one-stop shopping and quality merchandise at low prices"), *aff'd*, 544 F.2d 1184 (3d Cir. 1976).

129. Generac Corp. v. Caterpillar, Inc., 172 F.3d 971, 978 (7th Cir. 1990) (rejecting per se treatment for territorial allocation in trademark license pursuant to which plaintiff manufactured power generators under defendant's mark, sold part of the production to the licensor for resale in territories reserved to licensor, and sold the balance through dealers in territories reserved to licensee).

130. 1-800 Contacts, Inc. v. F.T.C., 1 F.4th 102, 119 (2d Cir. 2021) (quoting Clorox Co. v. Sterling Winthrop, Inc., 117 F.3d 50, 55, 57 (2d Cir. 1997)).

131. *See, e.g.*, *Clorox Co.*, 117 F.3d at 57 ("[A]ll that is required of a defendant in order to escape the clutches of an alleged trademark monopoly is to market his product under a different name." (quoting Seven-Up Co. v. No-Cal Corp., 183 U.S.P.Q. 165, 166 (E.D.N.Y. 1974)).

the franchise in the first place if the license restrictions are objectionable.[132] There is no compulsion to accept a trademark license, and protection of a trademark provides a procompetitive justification for restrictions incident to a trademark agreement.[133]

V. Resort to Quick-Look Analysis Under the Rule of Reason Is Foreclosed

Plaintiffs alleged in nearly all of the reported cases that quick-look rule of reason analysis is appropriate and that a no-hire clause violates Section 1 under this standard. Several courts agreed, denying motions to dismiss on this basis.[134] There is no basis for any such holding, as at least two courts have now acknowledged.[135]

The Supreme Court rejected in *Ohio v. American Express Co.* any departure from full rule of reason analysis for vertical restraints,[136] and quick-look analysis, which has been considered or applied by the Court only in cases involving horizontal conspiracies,[137] should have no application to no-hire

132. *See, e.g.*, Queen City Pizza v. Domino's Pizza, 124 F.3d 430, 441 (3d Cir. 1997) ("Plaintiffs need not have become Domino's franchisees. If the contractual restrictions in . . . the general franchise agreement were viewed as overly burdensome or risky at the time they were proposed, plaintiffs could have purchased a different form of restaurant, or made some alternative investment." (footnote omitted)).

133. *See, e.g.*, *1-800 Contacts*, 1 F.4th at 120 n.12 ("[W]e hold that protecting trademarks is a valid procompetitive justification for the restrictions" in a trademark infringement settlement agreement.).

134. *See* 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) (holding that complaint stated claim for violation of § 1 under per se rule and quick-look rule of reason); Butler v. Jimmy John's Franchise, LLC, 331 F. Supp. 3d 786, 795–97 (S.D. Ill. 2018) (same); Yi v. SK Bakeries, LLC, No. 18-5627 RJB, 2018 U.S. Dist. LEXIS 220966, at *14–15 (W.D. Wash. Nov. 13, 2018) (holding that complaint stated claim for violation of § 1 under quick-look rule of reason; motion to dismiss granted as to per se claim); Deslandes v. McDonald's USA, LLC, No. 17 C 4857, 2018 U.S. Dist. LEXIS 105260, at *20–23 (N.D. Ill. June 25, 2018) (same).

135. *See* Deslandes v. McDonald's USA, LLC, No. 17 C 4857, 2021 U.S. Dist. LEXIS 140735, at *18–19 (N.D. Ill. July 28, 2021) ("This Court cannot say that it has enough experience with no-hire provisions of franchise agreements to predict with confidence that they must always be condemned, which means, under [*NCAA* v.] *Alston* [141 S. Ct. 2141 (2021)], that the Court must apply rule of reason analysis to this case."); Conrad v. Jimmy John's Franchise, LLC, No. 18-CV-00133-NJR, 2021 U.S. Dist. LEXIS 142272, at *35 (S.D. Ill. July 23, 2021) ("*Alston* thus answers a question this Court punted at the motion-to-dismiss stage: The rule of reason applies in this monopsony case challenging a nationwide franchise's use of intrabrand restraints that were arguably 'designed to help (the company) more effectively compete with other brands by ensuring cooperation and collegiality among franchisees, and by encouraging investment in training.'" (citation omitted)).

136. *See* Ohio v. Am. Express Co., 138 S. Ct. 2274, 2285 n.7 (2018) (refusing to accept evidence of anticompetitive effects as a proxy for proof of the relevant market and market power in a case alleging an unlawful vertical restraint).

137. *See* NCAA v. Alston, 141 S. Ct. 2141, 2155–60 (2021) (rejecting quick look for review of horizontal price fixing by joint venture); Cal. Dental Ass'n v. F.T.C., 526 U.S. 756, 778 (1999) (application of quick look rejected); F.T.C. v. Ind. Fed'n of Dentists, 476 U.S. 447, 460–64 (1986) (quick look applied); NCAA v. Bd. of Regents, 468 U.S. 85, 109 (1984) (quick look applied).

clause cases, in which an intrabrand restraint has procompetitive effects comparable to those of vertical restraints.

The Court cleared away much of the analytical underbrush surrounding quick-look review in *NCAA v. Alston*,[138] holding that it is available only "for restraints at opposite ends of the competitive spectrum."[139] At one end of the spectrum are restraints "so obviously incapable of harming competition that they require little scrutiny."[140] At the other end are "agreements among competitors [that] so obviously threaten to reduce output and raise prices that they might be condemned as unlawful *per se* or rejected after only a quick look."[141] The Court noted that, as to the latter class of restraints, "we take special care not to deploy these condemnatory tools until we have amassed 'considerable experience with the type of restraint at issue' and 'can predict with confidence that it would be invalidated in all or almost all instances.'"[142] There is no such judicial experience with no-hire clauses in franchise agreements, as one court has already acknowledged.[143]

Because vertical restraints typically pose no risk to competition[144] and have procompetitive effects,[145] quick-look analysis of vertical restraints has been held to be improper.[146] Similarly, quick-look analysis of restraints incident to a trademark agreement has been rejected. The Second Circuit recently reversed the Federal Trade Commission's holding that such restraints are "inherently suspect" and therefore not requiring full rule-of-reason analysis.[147] Since trademarks are nonexclusionary and agreements to protect them should be presumed to be procompetitive, the appellate court rejected truncated rule-of-reason analysis for use restrictions incident to a trademark settlement agreement.[148]

138. *Alston*, 141 S. Ct. 2141.

139. *Id.* at 2155.

140. *Id.*

141. *Id.* at 2156 (italics in original).

142. *Id.* (quoting Leegin Creative Leather Prods. v. PSKS, Inc., 551 U.S. 877, 886–87 (2007)).

143. *See* Deslandes v. McDonald's USA, LLC, No. 17 C 4857, 2021 U.S. Dist. LEXIS 140735, at *18–19 (N.D. Ill. July 28, 2021) ("This Court cannot say that it has enough experience with no-hire provisions of franchise agreements to predict with confidence that they must always be condemned, which means, under *Alston*, that the Court must apply rule of reason analysis to this case.").

144. *See, e.g.*, Ohio v. Am. Express Co., 138 S. Ct. 2274, 2285 n.7 (2018) ("Vertical restraints often pose no risk to competition unless the entity imposing them has market power . . . .").

145. *See, e.g.*, Cont'l T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 54 (1977) ("Vertical restrictions promote interbrand competition by allowing the manufacturer to achieve certain efficiencies in the distribution of his products.").

146. *See, e.g.*, Physician Specialty Pharm. v. Therapeutics, No. 18-cv-1044 (MJD/TNL), 2019 U.S. Dist. LEXIS 53115, at *11–12 (D. Minn. Jan. 24, 2019) (magistrate's report and recommendation rejecting quick-look analysis for allegedly unlawful vertical restraints); Hannah's Boutique, Inc. v. Surdej, 112 F. Supp. 3d 758, 770 (N.D. Ill. 2015) (quick-look analysis rejected because "vertical restraints, including vertical agreements setting minimum resale prices, can have both pro-competitive and anti-competitive justifications" (citations omitted)).

147. *See* 1-800 Contacts, Inc. v. F.T.C., 1 F.4th 102, 116–17 (2d Cir. 2021).

148. *Id.* at 116 (rejecting truncated analysis for restraints incident to trademark infringement settlement agreement because trademarks are "by their nature non-exclusionary" and precedent "tells us instead to presume they are *procompetitive*" (citation omitted; emphasis in original)).

Truncated rule-of-reason analysis for no-hire clauses is barred, thus, not only because courts have had no experience analyzing the competitive effects of no-hire clauses in business format franchise systems but also because, as a trademark license, an agreement granting a business format franchise should be presumed to be procompetitive. A no-hire clause ancillary to the agreement must be evaluated under the full rule of reason.

VI. Conclusion

District court rulings on motions to dismiss in the no-hire litigation reflect an embarrassing mix of errors and naïveté, some of which may be laid at the feet of the requirement, under Federal Rule of Civil Procedure 12(b)(6), that a complaint is to be liberally construed in ruling on a motion to dismiss. Recent decisions denying motions for class certification[149] offer some promise that errors may be rectified in due course, but there is no certainty that other courts will get it right. Until it is recognized that no-hire clauses play a valuable role in protection of brand goodwill in the licensing of business format franchises, franchisors will continue to bear the cost and burden of defending against groundless Sherman Act claims advanced in a misguided effort to implement through the courts structural change in state and federal labor policy.

149. *See* Conrad v. Jimmy John's Franchise, LLC, No. 18-CV-00133-NJR, 2021 U.S. Dist. LEXIS 142272 (S.D. Ill. July 23, 2021); Deslandes v. McDonald's USA, LLC, No. 17 C 4857, 2021 U.S. Dist. LEXIS 140735 (N.D. Ill. July 28, 2021).

The Sleeping Giant Awakens: Three 2020 Trademark Decisions from the United States Supreme Court, and How They May Affect Franchising

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I. Introduction

The United States Supreme Court is the final arbiter of all matters involving federal law. Although a federal statute known as the Lanham Act governs many aspects of United States trademark law,[1] the Supreme Court typically has shown little interest in deciding trademark cases, at least in comparison to those involving other aspects of federal law. So, it was somewhat unusual when, in its term commencing in October 2019 and ending in June 2020, the Court decided three cases either interpreting the Lanham Act or arising from underlying trademark infringement litigation.[2]

This article summarizes those three decisions—*Romag Fasteners, Inc. v. Fossil, Inc.*,[3] *United States Patent & Trademark Office v. Booking.com B.V.*,[4] and *Lucky Brand*

1. *See* 15 U.S.C. § 1051 *et seq.*

2. Indeed, one of the authors of this year's International Trademark Association annual review began that work with the following observation:

> It is a time of great reckoning in United States trademark and unfair compensation law. For one thing the Supreme Court has continued to accept cases bearing on the subject of the Lanham Act at a rate that would have been unthinkable during the comparatively fallow years of the second half of the Twentieth Century.

Theodore H. Davis, Jr. & John L. Welch, *United States Annual Review: The Seventy-Third Year of Administration of the Lanham Act*, 111 Trademark Rep. 1 (2021).

3. Romag Fasteners, Inc. v. Fossil, Inc., 140 S. Ct. 1492 (2020), *on remand*, No. 3:10cv1827 (JBA), 2021 WL 1700695 (D. Conn. Apr. 29, 2021).

4. United States Patent & Trademark Office v. Booking.com B.V., 140 S. Ct. 2298 (2020), *vacated*, 141 S. Ct. 187 (2020), *on remand sub nom.* Booking.com, B.V. v. Hirshfeld, No. 1:16-cv-425 (LMB/IDD), 2021 WL 2277331 (E.D. Va. June 3, 2021).

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Dungarees, Inc. v. Marcel Fashions Group, Inc.[5]—explains the potential implications of those decisions generally, and identifies ways in which these decisions may affect the franchising community.

II. *Romag Fasteners, Inc. v. Fossil, Inc.*: The Court Addresses, but Perhaps Does Not Resolve, the Applicable Standards for an Accounting of Profits

Franchisors often have the occasion to bring litigation to enforce their trademark rights. Some of that litigation arises from "holdover" scenarios. These instances arise when the franchisee's franchise agreement and license to use the franchisor's trademarks has expired or has been terminated and the franchisee continues operating the franchised business, or one competitive to it, using the franchisor's trademarks or trademarks that are confusingly similar.[6] Because the franchisee is no longer licensed or otherwise authorized to use the franchisor's trademarks, any use of such trademarks post-termination or expiration constitutes trademark infringement.[7] Other trademark enforcement litigation involves franchisors pursuing other parties, including competitors, who may use trademarks identical or confusingly similar to those owned by the franchisors. In either case, if infringement is demonstrated, the Lanham Act provides franchisor trademark owners with seemingly robust monetary remedies, including the possible recovery of the defendant's profits attributable to the infringement.

Although judicial opinions often refer to the two interchangeably, the recovery of a defendant's profits, typically referred to as an "accounting" or "disgorgement," is a remedy that is separate from an award of the plaintiff's own actual damages.[8] Indeed, Section 35(a) of the Lanham Act expressly distinguishes between the two remedies by providing in relevant part:

> When a violation of any right of the registrant of a mark registered in the Patent and Trademark Office, that violation of Section 43(a) or (d), or a willful violation

5. Lucky Brand Dungarees, Inc. v. Marcel Fashions Grp., Inc., 140 S. Ct. 1589 (2020).

6. *See* Christopher P. Bussert & William M. Bryner, *A Practical Approach to Addressing Holdover Ex Franchisee Trademark Issues*, 27 Franchise L.J. 30 (2007).

7. *See, e.g.*, Burger King Corp. v. Mason, 710 F.2d 1480, 1492 (11th Cir. 1983) ("Common sense compels the conclusion that a strong risk of consumer confusion arises when a terminated franchisee continues to use the former franchisor's trademarks."); *see also* Tim Horton's USA, Inc. v. Tims Milner LLC., Bus. Franchise Guide (CCH) ¶ 16,442, No. 18-cv-24152-GAYLES/MCALILEY, 2019 WL 2515006 (S.D. Fla. June 17, 2019); New Horizons Educ. Corp. v. Krolak Tech. Mgmt. of Syracuse, LLC, Bus. Franchise Guide (CCH) ¶ 16,291, No. 5:18-cv-01223 (BKS/DEP), 2018 WL 5253070 (N.D.N.Y. Oct. 22, 2018); Mitsubishi Motors N. Am., Inc. v. Grand Auto., Inc., Bus. Franchise Guide (CCH) ¶ 16,181, No. CV 18-814 (SJF) (SIL), 2018 WL 2012875 (E.D.N.Y. Apr. 30, 2018); Peterbrooke Franchising of Am., LLC v. Mia. Chocolates, LLC, 312 F. Supp. 3d 1325 (S.D. Fla. 2018).

8. *See, e.g.*, WMS Gaming Inc. v. WPC Prods. Ltd., 542 F.3d 601, 605 (7th Cir. 2008) (reversing district court's conflation of accountings of profits and awards of actual damages and explaining that "[b]oth types of relief are available under the Lanham Act to redress trademark infringement, and they are distinct remedies with different legal standards and burdens of proof" (citation omitted), *as amended* (Sept. 16, 2008)).

> under Section 43(c), have been established in a civil action arising under this Act, the plaintiff shall be entitled, . . . subject to the principals of equity, to recover (1) [the] defendant's profits [and] (2) any damages sustained by the plaintiff . . . .[9]

Although Section 35(a) expressly contemplates the recovery of a defendant's profits, courts have struggled with articulating and balancing the factors properly considered as part of the "principles of equity" analysis. As a result, many different tests emerged among the circuits for assessing the appropriateness of an accounting of defendants' profits. Up until 2020, perhaps the greatest point of disagreement in the various circuits was whether franchisor trademark owners must demonstrate that a defendant's infringement was willful or intentional as a prerequisite for an accounting of profits.[10]

In that regard, the First, Second, Eighth, and Ninth Circuits had required trademark owners to establish willful infringement as a prerequisite to recover a defendant's profits.[11] As of 2020, the Sixth Circuit had not expressly ruled on this issue,[12] although at least one district court in that circuit had embraced the willfulness requirement.[13] The Tenth and Eleventh Circuits had held that, although willful infringement was not a prerequisite to an award of a defendant's profits, it was either an alternative basis or justification for an accounting of profits.[14] Other circuits, namely, the Third, Fourth, Fifth, and Seventh Circuits, had held willfulness was not a prerequisite; rather, it was a factor to be considered, along with others, in assessing the "principles of equity" as to whether an infringer's profits can be recovered.[15] Some of

9. 15 U.S.C. § 1117(a).

10. *See generally* Christopher P. Bussert, *Trademark Law and Franchising: Five of the Most Significant Developments*, 40 Franchise L.J. 127, 143–47 (2020).

11. Merck Eprova A.G. v. Gnosis S.p.A., 760 F.3d 247, 261–62 (2d Cir. 2014) ("[U]nder any theory, a finding of defendant's willful deceptiveness is a prerequisite for awarding profits."); Fishman Transducers, Inc. v. Paul, 684 F.3d 187, 191 (1st Cir. 2012) ("[O]ur cases usually require willfulness . . . to allow . . . a recovery of the defendant's profits."); Spin Master, Ltd. v. Zobmondo Entm't, LLC, 944 F. Supp. 2d 830, 846 (C.D. Cal. 2012) ("In the Ninth Circuit, willfulness is required to disgorge an infringer of its illgotten profits."); *see also* Masters v. UHS of Del., Inc., 631 F.3d 464, 471 n.2 (8th Cir. 2011) ("[W]e assume, without deciding, that willful infringement is a prerequisite of monetary relief.").

12. Wynn Oil Co. v. Am. Way Serv. Corp., 943 F.2d 595, 607 (6th Cir. 1991).

13. *See* Wm. R. Hague, Inc. v. Sandburg, No. 2:06-cv-00363, 2009 WL 10679676 (S.D. Ohio Sept. 24, 2009).

14. PlayNation Play Sys., Inc. v. Velex Corp., 924 F.3d 1159, 1170 (11th Cir. 2019) ("An accounting of a defendant's profits is appropriate where: (1) the defendant's conduct was willful and deliberate, (2) the defendant was unjustly enriched, or (3) it is necessary to deter future conduct."), *aff'd*, 939 F.3d 1205 (11th Cir. 2019), *on remand*, No. 1:14-CV-1046-RWS, 2019 WL 11239152 (N.D. Ga. Oct. 11, 2019), *and on remand*, No. 1:14-CV-1046-RWS, 2020 WL 6895302 (N.D. Ga. July 9, 2020); KleinBoslker, USA, LLC v. Englert, 711 F.3d 1153, 1161 (10th Cir. 2013) ("[U]nder the Lanham Act, plaintiffs must show either actual damages or willful action on the part of the defendant as a prerequisite to recover disgorgement of profits.").

15. Retractable Techs, Inc. v. Becton Dickinson & Co., 919 F.3d 869, 883 (5th Cir. 2019) (citation omitted) (holding willful infringement an important factor for consideration when determining whether an accounting of profits is appropriate); Synergistic Int'l, LLC v. Korman, 470 F.3d 162, 175 n.13 (4th Cir. 2006) ("[W]e agree that willfulness is not an essential prerequisite for a damages [sic] award, but that it remains a highly pertinent factor."); Banjo Buddies, Inc. v. Renosky, 399 F.3d 168, 177–78 (3d Cir. 2005) (stating willfulness is only a factor, not an indispensable prerequisite to a recovery of profits); Roulo v. Russ Berrie & Co., 886

these circuits had adopted lists of nonexclusive factors (including willfulness) that courts should consider in determining whether an accounting of profits is warranted. For example, the Fifth Circuit in *Retractable Technologies, Inc. v. Becton Dickinson & Company*[16] articulated the following six non-exclusive factors in determining whether an award of profits was appropriate:

> (1) whether the defendant had the intent to confuse or deceive, (2) whether sales have been diverted, (3) the availability of other remedies, (4) any unreasonable delay by the plaintiff in asserting his rights, (5) the public interest in making the misconduct unprofitable, and (6) whether it is a case of palming off.[17]

Although over the years there have been several attempts to secure United States Supreme Court review of this issue, the Supreme Court only agreed in 2020 to address the matter in *Romag Fasteners, Inc. v. Fossil, Inc.*[18] Romag and Fossil were well acquainted, having been parties to an agreement under which Fossil could use Romag's fasteners in connection with Fossil's leather goods. After Romag discovered Fossil was having products bearing imitations of Romag's fasteners made in China, Romag sued Fossil under the Lanham Act for trademark infringement. Despite finding in Romag's favor on its trademark infringement claim, as well as that Fossil had acted in "callous disregard" of Romag's rights, the jury declined to find that Fossil had acted willfully as the trial court had defined that term in its instructions.[19] The Federal Circuit affirmed, holding that Romag's failure to prove willful infringement was fatal to its claim for profits.[20]

In an opinion authored by Justice Gorsuch, the Supreme Court reversed that outcome and remanded the case, holding that Section 35(a) of the Lanham Act does not impose a "willfulness" requirement for accountings of profits in trademark infringement actions. At the outset, the Court examined the language of Section 35(c) and determined that a showing of willfulness was expressly required only as a precondition to an accounting in actions for trademark dilution under Section 35(a).[21] The Court observed that Section 35(a)'s express language "had never required a showing of willfulness to win

F.2d 931, 941 (7th Cir. 1989) ("[T]here is no express requirement [in the Lanham Act] that the infringer . . . willfully infringe . . . to justify an award of profits."). The authors were counsel for Synergistic International, LLC.

16. Retractable Technologies, Inc. v. Becton Dickinson & Co., 919 F.3d 869 (5th Cir. 2019).

17. *Id.* at 876 (first quoting Pebble Beach Co. v. Tour 18 I Ltd., 155 F.3d 526, 554 (5th Cir. 1998), and then citing Quick Techs., Inc. v. Sage Grp. PLC, 313 F.3d 338, 349 (5th Cir. 2002)).

18. Romag Fasteners, Inc. v. Fossil, Inc., 140 S. Ct. 1492 (2020).

19. *See* Romag Fasteners, Inc. v. Fossil, Inc., 29 F. Supp. 3d 85, 107 (D. Conn. 2014) ("[U]nder existing Second Circuit precedent, a plaintiff must establish willful infringement in order to recover an award of the defendant's profits in a trademark action."), *vacated in part*, 686 F. App'x 889 (2017). The jury, however, did make an advisory accounting of $90,759.36 of Fossil's profits attributable to the infringement and $6,704.046 of Fossil's profits under a deterrence theory. This issue is discussed further below, as the district court addressed it on remand from the Supreme Court's decision.

20. Romag Fasteners, Inc. v. Fossil, Inc., 817 F.3d 782, 784–91 (Fed. Cir. 2016), *vacated*, 137 S. Ct. 1373 (2017).

21. *Romag Fasteners*, 140 S. Ct. at 1494–95.

a defendants' profits" and that it was not inclined to "read into the statutes words that aren't there," particularly when the term "willfulness" was used elsewhere in the same statutory provision.[22]

The Court next addressed Fossil's argument that the "principles of equity" qualification of Section 35(a) contemplated a willfulness requirement for profits. The Court rejected Fossil's reliance on the "principles of equity" language for two reasons.[23] First, it held such a reading was inconsistent with the express "*mens rea*" language in other sections of the Lanham Act, which expressly set forth whether certain actions were undertaken "intentionally," or with "knowledge," or were otherwise "willful."[24] According to the Court, Fossil's interpretation was not "an obvious construction of the statute."[25] Second, the Court rejected Fossil's contention that past precedent had consistently required a showing of willfulness before allowing a profits remedy, finding instead that Fossil's premise was "far from clear."[26] In that regard, the Court observed that, although some courts had treated willfulness as a prerequisite for an accounting, other courts had expressly rejected this rule.[27] Moreover, this analysis was further complicated by the fact that several leading commentators had expressed disagreement about the relationship between willfulness and accountings of profits in trademark cases.[28] At the end of the day, the Court concluded only that the defendant's mental state should be considered in determining the propriety of an accounting of profits,[29] but should not be an inflexible precondition to that relief.[30]

So what impact will *Romag* have on the pursuit of accountings under Section 35(a)? The short answer is that the issue is currently up for debate. In the authors' view, the answer is that the impact will likely depend on the forum hearing the case. For actions brought in the Third, Fourth, and Fifth Circuits, which already have multi-factor tests that include the consideration of a defendant's mental state, nothing will likely change because *Romag* seemingly endorsed that approach. As to circuits—such as the First, Second, Eighth, and Ninth—that required proof of willfulness as a prerequisite to recover an infringer's profits, those courts' precedents are no longer good law, and they will likely end up formulating their own multi-factor tests for assessing the accounting of profits remedy that include the defendant's mental state as one factor. Finally, for circuits like the Tenth and Eleventh, which have either identified willfulness as an alternative basis or separate justification for an accounting of profits, any basis or justification *not* arguably

22. *Id.* at 1495.
23. *Id.*
24. *Id.* at 1495 (emphasis omitted) (first citing 15 U.S.C. §§ 1117(b), 1117(c), 1118, and then citing §§ 1125(d)(1)(A)(i)–(B)(i)).
25. *Id.* at 1496.
26. *Id.*
27. *Id.*
28. *Id.* at 1496–97.
29. *Id.*
30. *Id.*

predicated on a finding of willfulness alone on the behalf of the defendant is probably still good law.[31]

However, some in the trademark bar have been critical of *Romag* and warned that its application could potentially lead to dire consequences. For example, some have suggested the following adverse effects:

- More opportunistic trademark lawsuits will be filed;
- More aggressive and inflexible positions by trademark plaintiffs may stymie efforts to settle trademark disputes;
- Litigation funding companies will have a renewed interest in funding trademark owner plaintiffs who pursue accountings of profits; and
- Innocent or inadvertent infringers face an increased likelihood of being required to disgorge profits.[32]

The source of the last potential effect is likely Justice Sotomayor's concurring opinion in *Romag*, in which she expressed concerns about how the majority's decision might affect innocent infringers. Indeed, at one point she accused the majority of being "agnostic about awarding profits for both 'willful' and innocent infringement."[33]

Others have pointed out that *Romag* does not resolve all issues associated with whether an accounting of profits is appropriate, such as whether the trademark plaintiff must demonstrate the existence of actual confusion.[34]

One important data point that the trademark bar's *Romag* critics seem not to have included in their analyses is the established track record of pre-*Romag* authority on this subject. A number of circuits pre-*Romag* did not require willfulness as a prerequisite to accountings. Accepting the concerns articulated above as valid, a reasonable assumption would be that circuits in which a finding of willfulness was not required would already order accountings of profits in a far higher percentage than circuits in which willfulness

31. Bussert, *supra* note 10, at 146.

32. *See* W. Drew Castner, *Practical Implications of Supreme Court's* Romag v. Fossil *Decision: Avoiding Forfeiture of Hard-Earned Profits in Trademark Infringement Lawsuits*, JDSupra (May 22, 2020), https://www.jdsupra.com/legalnews/practical-implications-of-supreme-court-86119; Melanie J. Howard & Douglas N. Masters, *Supreme Court Holds Trademark Infringement Does Not Require a Finding of "Willful" Infringement to Recover an Award of Profits*, Loeb & Loeb (May 2020); David Ervin et al., *Raising the Stakes for Trademark Damages:* Romag Fasteners, Inc. v. Fossil, Inc., Crowell Moring (Apr. 29, 2020), https://www.crowell.com/NewsEvents/AlertsNewsletters/all/Raising-the-Stakes-for-Trademark-Damages-Romag-Fasteners-Inc-v-Fossil-Inc; Matthew S. DeAntonio, *Trademark Law Trends to Follow in 2021* Law 360 (Jan. 3, 2021), https://www.law360.com/articles/1338890/trademark-law-trends-to-follow-in-2021; Tim Lince, Romag v. Fossil*: No Intent Required in Trademark Dispute to Secure Profit Awards, U.S. Supreme Court Rules*, World Trademark Rev. (Apr. 23, 2020), https://www.worldtrademarkreview.com/brand-management/romag-v-fossil-no-intent-required-in-trademark-disputes-secure-profits-awards; Bill Donahue, *Will High Court's Trademark Ruling Spark Litigation Wave?*, Law360 (Apr. 24, 2020), https://www.law360.com/articles/1267186.

33. Romag Fasteners, Inc. v. Fossil, Inc., 140 S. Ct. 1492, 1498 (2020) (Sotomayor, J., concurring).

34. Davis & Welch, *supra* note 2, at 406 (noting a current split on that issue between the Second and Eighth Circuits).

was required, as well as the existence of reported decisions requiring innocent or inadvertent infringers to disgorge their profits.

To test this assumption, the authors undertook a circuit-by-circuit survey of reported federal court decisions since 2005 in which a prevailing trademark plaintiff pursued an accounting of profits. Surprisingly, the percentage of those opinions ordering accountings was, on balance, remarkably close from circuit to circuit *irrespective* of whether or not willfulness was required as shown in the chart below:[35]

Circuit	**Number of Cases**	**Willfulness Finding Required**	**Cases Granting an Accounting**
1st	8	Yes	62.5%
2nd	70	Yes	61.4%
3rd	19	No	57.9%
4th	19	No	63.2%
5th	18	No	61.1%
6th	6	N/A	50%
7th	7	No	57.1%
8th	8	Yes	50%
9th	27	Yes	66.7%
10th	8	No	62.5%
11th	7	No	71.4%
DC	2	Yes	100%

What explains the reason for the apparent statistical consistency in accountings of profits in trademark cases? A number of factors are likely at play, the most significant of which is that the defendant's state of mind appears *always* to be an important factor to courts in evaluating the "principles of equity" for purposes of determining whether an accounting of profits is justified. Indeed, in those circuits not requiring willfulness, defendant's state of mind and culpability remained important considerations in ordering accountings, as well as other factors touching on that state of mind and culpability, including whether there was evidence of palming off or an intent to confuse or deceive, the need for deterrence, and the public interest in making the misconduct unprofitable.[36]

As to innocent or inadvertent infringers being required to disgorge profits, even Justice Sotomayor recognized that the weight of authority the

35. The authors greatly appreciate the assistance of Kilpatrick Townsend & Stockton associate Emily Yates in compiling these opinions.

36. *See, e.g.*, Retractable Techs., Inc. v. Becton Dickinson & Co., 842 F.3d 883, 900–01 (5th Cir. 2016); Optimum Techs., Inc. v. Home Depot U.S.A., Inc., 217 F. App'x 899, 902 (11th Cir. 2007); Banjo Buddies, Inc. v. Renosky, 399 F.3d 168, 177–78 (3d Cir. 2005).

parties in *Romag* provided in their briefs demonstrated "profits were hardly, if ever, awarded for innocent infringement."[37]

How have courts reacted since *Romag* in considering accountings of profits in trademark cases? Despite the lack of reported decisions, those opinions that have issued signal that courts intend to continue to consider willfulness as an important factor in assessing whether the principles of equity favor an accounting. Two recent cases bear this out. The first, *PlayNation Play Systems, Inc. v. Velex Corp.*,[38] involved a dispute between playground equipment manufacturers. After a bench trial in which the court concluded infringement had occurred, the court issued a preliminary order finding that an accounting of profits was justified. At the request of the parties, however, the court reserved its final ruling on the issue pending the Supreme Court's decision in *Romag*, which is reflected in this decision.

At the outset, the court observed that pre-*Romag* a trademark owner plaintiff was entitled to a defendant's profits in the Eleventh Circuit if one of three circumstances exists: "(1) the defendant's conduct was willful and deliberate, (2) the defendant was unjustly enriched, or (3) it is necessary to deter future conduct."[39] In this case, the court appeared to hold that all three circumstances justified the accounting of profits. As to unjust enrichment, the court noted that the plaintiff had established its mark was strong and that actual confusion existed at the retail level.[40] Although the court did not separately discuss the willfulness consideration, its deterrence analysis was heavily steeped in a discussion of the defendant's state of mind. According to the court, there was a strong need for deterrence in light of defendant's failure to accept responsibility for its conduct and its obfuscation of facts throughout the litigation in an effort to explain away its conduct.[41]

The second case, *Vitamins Online, Inc. v. Heartwise, Inc.*,[42] was a false advertising matter under Section 43(a) of the Lanham Act between two retailers of dietary supplements. After finding that defendant had engaged in false advertising based on its manipulation of Amazon.com's customer review system and disseminating false and misleading information regarding the content and characteristics of its products, the court examined whether an accounting of the defendant's profits was appropriate.

37. *Romag Fasteners*, 140 S. Ct. at 1498 (Sotomayor, J., concurring).

38. PlayNation Play Systems, Inc. v. Velex Corp., No. 1:14-CV-1046-RWS, 2020 WL 6895302 (N.D. Ga. July 9, 2020), *aff'd*, No. 20-12978, 2021 WL 2209096 (11th Cir. June 1, 2021).

39. *Id*. at *2 (quoting Optimum Techs., Inc. v. Henkel Consumer Adhesives, Inc., 496 F.3d 1231, 1241 (11th Cir. 2007)). Interestingly, in its analysis of *Romag*, the court suggested that "Romag Fasteners does not appear to have narrowed the instances in which an accounting of profits is appropriate." *Id*. Although not relevant to its ultimate decision in *PlayNation*, the court seemed to miss that *Romag* did in fact narrow the instances in which an accounting of profits was appropriate as it could no longer be predicated solely on a finding of "willful and deliberate" conduct. *Id*.

40. *PlayNation*, 2020 WL 6895302, at *2.

41. *Id*.

42. Vitamins Online, Inc. v. Heartwise, Inc., No. 2:13-cv-00982-DAK, 2020 WL 6581050 (D. Utah Nov. 10, 2020), *appeal filed*, No. 20-4126 (10th Cir. Dec. 4, 2020).

The court began its analysis by noting that, prior to *Romag*, the Tenth Circuit had held an accounting of profits was appropriate if the plaintiff could show actual damages or willful conduct by the defendant.[43] However, in view of *Romag*, the court found that an accounting could no longer be predicated solely on a finding of willful infringement. Instead, it was now proper to consider willfulness only as one of a number of equitable considerations, including (1) the degree of certainty that the defendant had benefited from the unlawful conduct; (2) the availability and accuracy of other remedies; (3) the role of a particular defendant in effectuating the infringement; (4) any laches by the plaintiff; and (5) any unclean hands by the plaintiff.[44] After analyzing each of these equitable considerations, the court concluded that a disgorgement of defendant's profits was an appropriate remedy. As to willfulness, the court found that defendant's actions were willful for the following reasons:

- defendant's representatives made willfully false representations relating to defendant's products and artificially altered reviews to make defendant more profitable;
- defendant had knowledge that certain lots of its products did not match their label claims yet continued to sell those products; and
- defendant had engaged in discovery improprieties during the course of litigation.[45]

Based on the track record of accountings in circuits in which a finding a willfulness was not required pre-*Romag*, as well as early post-*Romag* case returns, it seems unlikely that the "sky is falling" consequences that some have predicted will materialize. In particular, because a defendant's state of mind continues to appear to be a key consideration in the profits justification analysis, it seems that innocent or inadvertent infringers will rarely face being subjected to accountings.

Even if there were circumstances in which a court found that less culpable defendants, (*i.e.*, innocent or inadvertent infringers) should be required to disgorge profits, the Lanham Act includes an additional guardrail to help ensure that the amount awarded is not exorbitant. In addition to providing courts great discretion as to whether an accounting of profits is appropriate, consistent with the principles of equity, courts also have discretion as to the amount awarded.[46] In that regard, 15 U.S.C. § 1117 provides that "[i]f the court shall find that the amount of the recovery based on profits is either inadequate or excessive the court may in its discretion enter judgment for such sum as the court shall find to be just, according to the circumstances of the case."

43. *Id*. at *21 (citing Klein-Becker USA, LLC v. Englert, 711 F.3d 1153, 1161 (10th Cir. 2013)).

44. *Vitamins Online*, 2020 WL 6581050, at *21 (citing Gen. Steel Domestic Sales, LLC v. Chumley, No. 10-cv-01398-PAB-KLM, 2013 WL 1900562 (D. Colo. May 7, 2013)).

45. *Vitamins Online*, 2020 WL 6581050, at *22.

46. *See* Christopher P. Bussert & Theodore H. Davis, Jr., *Calculating Profits Under Section 35 of the Lanham Act: A Practitioners Guide*, 82 Trademark Rep. 182 (1992).

This additional discretion recently proved to be very helpful to Fossil upon remand of *Romag* to the trial court.[47] Although the court noted that the jury had made a pre-*Romag* advisory recommendation of a disgorgement of $90,759.36 of Fossil's profits attributable to its trademark infringement under an unjust enrichment theory[48] and $6,704,046.00 of Fossil's profits for trademark infringement under a deterrence theory,[49] the court awarded only the $90,759.36 amount. In so holding, the court held that an accounting based on deterrence was not justified because of the following factors:

- Fossil had been negligent but had not acted in reckless disregard or willful blindness;
- Romag engaged in chicanery in litigating the case by delaying commencement of this lawsuit to maximize its leverage over Fossil and made misrepresentations to the court during the course of the litigation; and
- Romag chose to gamble and pursue "a more uncertain, but potentially higher, disgorgement award" rather than a statutory damages award that was available and "would have adequately compensated it."[50]

The court added that Romag should not be rewarded for its unsuccessful gamble.

Romag's importance to franchising will be felt in actions franchisors may bring that assert Lanham Act claims either against franchisees or third parties. Pursuit of accountings will remain an attractive option to franchisors. And, although establishing willfulness is no longer a prerequisite to obtaining an accounting, franchisors should not ignore the importance of developing and presenting evidence of the defendant's state of mind in connection with its infringement, as such evidence will continue to be important to courts in their evaluation of the principles of equity in determining whether a profits award is justified.

III. *United States Patent & Trademark Office v. Booking.com B.V.*: Adding .com to a Generic Word Can, Under the Right Circumstances, Result in a Protectable Mark

A foundational principal of trademark law is that generic terms, such as the names of classes of products or services, are ineligible for trademark protection. But what happens when two admittedly generic elements are combined? Is the resulting combination generic as well? According to the U.S. Supreme Court in *United States Patent & Trademark Office v. Booking.com B.V.*,

47. Romag Fasteners, Inc. v. Fossil, Inc., Civ. No. 3:10cv1827 (JBA), 2021 WL 1700695 (D. Conn. Apr. 29, 2021).

48. *Id.* at *1. Significantly, the jury also determined that only one percent of Fossil's profits was attributable to its infringement of Romag's mark.

49. *Id.*

50. *Id.* at *7.

at least in the case of a mark consisting of the combination of a generic term and the top-level domain ".com," the answer is "it depends."[51]

Booking.com involved a many years' long battle between Booking.com and the U.S. Patent and Trademark Office (USPTO) regarding the registrability of the Booking.com mark. Booking.com had filed four separate applications to register the Booking.com mark. Each of the applications contained the term "Booking.com" but included different design elements. Both the examining attorney to whom the applications were assigned and the Trademark Trial and Appeal Board concluded that Booking.com was generic for the travel reservation-related services covered by the applications, which resulted in the refusal of each registration. According to the Board, the term "booking" meant making travel registrations and ".com" was well recognized as signifying a website.[52] The Board added that "customers would understand the term Booking.com primarily to refer to an online reservation service for travel, tours, and lodgings."[53]

Undeterred by these refusals, Booking.com sought a *de novo* review of the Board's refusal in the U.S. District Court for the Eastern District of Virginia.[54] In the district court, Booking.com introduced new evidence including a "Teflon" survey which showed that 74.8% of the respondents identified BOOKING.COM as a brand name.[55] Relying in significant part on Book ing.com's survey evidence, the district court concluded that, unlike "booking" standing alone, Booking.com was not generic. In so holding, the court found that the relevant consuming public "primarily understands that booking.com

51. U.S. Pat. & Trademark Off. v. Booking.com B.V., 140 S. Ct. 2298 (2020). The authors' firm participated in this case as counsel for several *amicus curiae*, including the America Intellectual Property Law Association, in support of Booking.com.

52. *Id.* at 2303.

53. *Id.*

54. Booking.com B.V. v. Matal, 278 F. Supp. 3d 891 (E.D. Va. 2017), *order amended*, No. 1:16-cv-425 (LMB/IDD), 2017 WL 4853755 (E.D. Va. Oct. 26, 2017), *vacated*, 141 S. Ct. 187 (2020), *and on remand*, No. 1:16-cv-425 (LMB/IDD), 2021 WL 2277331 (E.D. Va. June 3, 2021).

55. *Booking.com B.V.*, 278 F. Supp. 3d at 915–16. *Teflon* surveys have become the predominate survey format to resolve a genericness challenge and are recognized as having arisen from the survey introduced in *E.I. DuPont de Nemours & Co. v. Yoshida International, Inc.*, 393 F. Supp. 502 (E.D.N.Y. 1975). A *Teflon* survey begins by providing respondents with an explanation of the distinction between generic and common names and trademark or brand names and then presents respondents with a series of names, which they are asked to classify as common or brand names. *See Booking.com*, 278 F. Supp. 3d at 915. In this case, the list of terms shown to respondents were:

- The term at issue:
  - "BOOKING.COM"
- Three brand names:
  - "ETRADE.COM"
  - "PEPSI"
  - "SHUTTERFLY"
- Three common names:
  - "SPORTINGGOODS"
  - "WASHINGMACHINE.COM"
  - "SUPERMARKET"

does not refer to a genus, rather it is descriptive of services involving 'booking' available at that domain name."[56]

The USPTO appealed the district court's determination that booking.com was not generic to the Fourth Circuit. Finding no error in the district court's assessment of how the relevant consuming public perceived the term "booking.com," the Fourth Circuit affirmed. Because the Fourth Circuit's affirmance arguably created a split with earlier decisions from the Federal and Ninth Circuits on the treatment of the genericness issue,[57] the Supreme Court granted *certiorari*.

The precise question before the Court was whether a generic.com term (i.e., the combination of a generic top-level domain (".com") with an otherwise generic term) could result a protectable mark.[58] In an opinion authored by Justice Ginsburg,[59] the Supreme Court declined to hold as a matter of law that what it referred to as "generic.com" marks such as BOOKING.COM were generic and therefore ineligible for federal registration. At the outset, the Court reviewed several "guiding principles" on which the parties had agreed:

- A "generic" term names a "class" of goods or services, rather than any particular feature or exemplification of the class.
- For a compound term, the inquiry on protectability focuses on the term's meaning as a whole rather than its parts in isolation.
- The relevant meaning of a term is its meaning to consumers.
- Eligibility for registration turns on whether the mark is capable of distinguishing goods or services in commerce.[60]

In holding that booking.com was not generic for travel-related services, the Court articulated the following standard for assessing whether a "generic.com" term was generic:

> [W]hether "Booking.com" is generic turns on whether that term, taken as a whole, signifies to consumers the class of online hotel-reservation services. Thus, if "Booking.com" were generic, we might expect consumers to understand Travelocity—another such service—to be a "Booking.com." We might similarly expect that a consumer, searching for a trusted source of online hotel-reservation services, could ask a frequent traveler to name her booking "Booking.com" provider.[61]

The Court added that the evidence submitted by Booking.com before the district court established that consumers did not perceive "Booking.com" as generic but instead viewed it as a brand and that alone should resolve the case.

56. *Id.* at 918.
57. *See* Advertise.com v. AOL Advertising, Inc., 616 F.3d 974 (9th Cir. 2010); *In re* Hotels.com, L.P., 573 F.3d 1300 (Fed. Cir. 2009).
58. U.S. Pat. & Trademark Off. v. Booking.com B.V., 140 S. Ct. 2298 (2020).
59. *Booking.com* was Justice Ginsburg's final opinion as a Supreme Court Justice.
60. *Id.* at 2304.
61. *Id.* at 2304–05.

The USPTO opposed this conclusion and instead argued that "Booking.com" was ineligible for registration *regardless* of evidence of consumer perception. In doing so, it advanced a nearly *per se* rule that when a generic term is combined with ".com" the resulting combination is generic.[62] The Court found the USPTO's *per se* rule and analysis to be faulty for a number of reasons. First, the Court noted that the USPTO's past practice in assessing "generic.com" terms as trademarks was inconsistent at best. Among other things, the Court noted the existence in the record of registrations of Art.com on the Principal Register for, inter alia, "[o]nline retail store services" offering "art prints, original art, [and] art reproductions; and Dating.com on the Supplemental Register for "dating services."[63] Adoption of the rule the USPTO advanced, according to the Court, would result in these and other existing registrations inconsistent with this rule to be at risk for cancellation.[64]

Second, the Court noted the USPTO's *per se* rule was based on its reading of *Goodyear's India Rubber Glove Manufacturing Company v. Goodyear Rubber Company*.[65] In *Goodyear*, the Court had held that a generic corporate designation (i.e., Company) added to a generic term does not confer trademark eligibility.[66] According to the USPTO, a "generic.com" term was like a "generic company" and therefore was ineligible for trademark protection, let alone federal registration, because adding ".com" to a generic term conveyed no additional meaning that would distinguish one's goods or services from others.[67]

The Court found the USPTO's premise to this argument to be without merit, observing that a "generic.com" might also convey to consumers a "source-identifying characteristic" such as an association with a particular website. The Court added:

> [O]nly one entity can occupy a particular Internet domain name at a time, so "[a] consumer who is familiar with that aspect of the domain-name system can infer that BOOKING.COM refers to some specific entity. Thus, consumers could understand a given "generic.com" term to describe the corresponding website or to identify the website's proprietor.[68]

Third, and more fundamentally, the Court found that the USPTO's reliance on *Goodyear* was flawed to the extent the agency argued that "generic company" terms were ineligible for trademark protection *as a matter of law*, regardless of how "consumers would understand" the term.[69] Because a decision on whether a term is generic depends on its meaning to consumers, the Court reasoned that an unyielding legal rule entirely disregarding consumer

62. *Id*. at 2305.
63. *Id*.
64. *Id.*
65. Goodyear's India Rubber Glove Mfg. Co. v. Goodyear Rubber Co., 128 U.S. 598 (1888).
66. *Id*. at 602–03.
67. *Booking.com B.V.*, 140 S. Ct. at 2305–06.
68. *Id.* at 2306.
69. *Id.*

perception would be incompatible with the Lanham Act. The Court added that, although it was rejecting the inflexible rule proffered by the USPTO, it was also not simultaneously embracing a rule automatically classifying generic.com terms as nongeneric. Rather, whether any given "generic.com" term is generic "depends on whether consumers in fact perceive that term as the name of a class or, instead, as a term capable of distinguishing among members of the class."[70]

The Court then rejected several policy arguments advanced by the USPTO. The Court noted the USPTO's concern that extending trademark protection for a term like "Booking.com" would hinder competition. According to the USPTO, recognizing the protectability of Booking.com as a mark might result in excluding or inhibiting competitors from using the term "booking" or adopting domain names like "ebooking.com" or "hotel-booking.com."[71] The Court found these concerns to be largely overblown and attended any descriptive mark, particularly a weak one, and that existing trademark doctrines guarded against these perceived anticompetitive efforts. For example, descriptive marks generally receive far narrower protection than their non-descriptive counterparts, and the descriptive components even of registered marks could also be used fairly by competitors to describe accurately their own goods and services. Indeed, the Court noted that Booking.com had conceded that (1) the Booking.com mark would be weak, making it more difficult to establish likely confusion with close variations; and (2) federal registration of Booking.com would not prevent competitors from using the term "booking" descriptively to indicate that they also provided booking services.[72]

The Court also rejected the USPTO's suggestion that protection of generic.com brands was unnecessary because they enjoy "competitive advantages" including that the owner had already "seized" the domain name and that the websites were easy for consumers to find.[73] Rather, the Court observed:

> Those competitive advantages, however, do not inevitably disqualify a mark from federal registration. All descriptive marks are intuitively linked to the product or service and thus might be easy for consumers to find using a search engine or telephone directory. . . . And the PTO fails to explain how the exclusive connection between a domain name and its owner makes the domain name a generic term, all should be free to use. That connection makes trademark protection more appropriate, not less.[74]

Consistent with its holding in *Romag*, the Court again declined to adopt an inflexible bright-line rule, in this case that a "generic.com" term must be generic, and instead advocated a flexible standard for assessing

70. *Id.* at 2307.
71. *Id.*
72. *Id.*
73. *Id.*
74. *Id.*

protectability and registrability, which would be governed by evidence of consumer perception.

The trademark bar's reaction to *Booking.com* has been generally positive. Although some have warned that the USPTO will be deluged with generic.com mark filings and that litigation involving such marks will become more plentiful,[75] others have expressed a more measured view that the decision offers a roadmap to possibly securing protection of a generic.com mark and, in particular, the sources of evidence on which a mark owner may rely to establish a favorable consumer perception.[76] In that regard, although Booking.com's *Teflon* survey[77] was key to its success, Justice Sotomayor's concurring opinion warned against parties relying on flawed survey evidence, and added that, in any event, surveys were not the "be-all and end-all" to establish consumer perception.[78] She added that many other sources are available as well including "dictionaries, usage by consumers and competitors, and any other source of evidence bearing on how consumers perceive a term's meaning.[79]

Still others have suggested that *Booking.com* may find purchase in evaluation of marks consisting of other combinations of generic elements such as a generic term combined with a hashtag (#) symbol[80] or a telephone area code. Most, however, seem to agree that pursuing protection and registration of generic.com marks will be an expensive and time-consuming process.[81] And because the protection ultimately obtained will be limited, owners of

75. DeAntonio, *supra* note 32; Megan Bannigan & Jared Kagan, *Looking Back at the Highest Impact Trademark Cases of 2020*, IP Watchdog (Dec. 22, 2020), https://www.ipwatchdog.com/2020/12/22/looking-back-highest-impact-trademark-cases-2020/id=128462; Kyle Jahner & Blake Brittain, *Supreme Court Affirms Validity of "Booking.com" Trademark*, Bloomberg L. (June 30, 2020), https://www.bloomberglaw.com/bloomberglawnews/ip-law/X6JJ5NMG000000?bna_news_filter=ip-law#jcite. *But see* John Strand & Amanda Slade, *Supreme Court's Booking.com Ruling Signals Uptick in Registration of "Generic.com" Marks*, IP Watchdog (July 5, 2020), https://www.ipwatchdog.com/2020/07/05/supreme-courts-booking-com-ruling-signals-uptick-registration-generic-com-marks/id=123072 ("The decision will not necessarily open the floodgates to a countless number of 'generic.com' terms on the Trademark Register.").

76. Martha Allard, *Impact of Supreme Court Trademark Decision in Booking.com Case*, JDSupra (July 13, 2020), https://www.jdsupra.com/legalnews/impact-of-supreme-court-trademark-91400; Victoria J. B. Doyle & Theodore H. Davis, Jr., *Strategies for Cultivating Protectable Rights in, and Registering, Generic.com Marks After United States Patent and Trademark Office v. Booking.Com B.V.*, JDSupra (July 23, 2020), https://www.jdsupra.com/legalnews/strategies-for-cultivating-protectable-91688.

77. For a more detailed discussion of the *Teflon* and alternative survey formats, see Doyle & Davis, *supra* note 76.

78. U.S. Patent & Trademark Office v. Booking.com B.V., 140 S. Ct. 2298, 2309 (2020).

79. *Id.* For a more detailed discussion of the types of evidence deemed probative of consumer perception, see David Bernstein & Jared Kagan, *Consumer Perception Is King After Booking.com Decision*, Law360 (July 7, 2020), https://www.law360.com/articles/1289985/consumer-perception-is-king-after-booking-com-decision.

80. *See* Patricia Cotton & Paul E. Thomas, *Is the "Booking.com" Mark Registerable? SCOTUS Says Booking.com*-pletely!, Pillsburylaw.com (July 1, 2020), https://www.pillsburylaw.com/en/news-and-insights/booking-com-scotus-trademark.html.

81. Strand & Slade, *supra* note 75; Allard, *supra* note 76.

generic.com terms will need to evaluate whether that protection (assuming success) is worth the cost.[82]

For its part, the USPTO has reacted quickly to the decision in *Booking .com*. Perhaps in response to the Court's criticism that USPTO practice has resulted in disparate treatment of generic.com terms, the USPTO has sought to clarify its practice and in October 2020 issued a new "Examination Guide."[83] That Examination Guide informs the Examining Division of the holding in *Booking.com* and provides detailed guidance on the proper examination of generic.com marks, the relevant evidence to be considered, and procedures for issuing refusals.[84]

In its first reported decision post-*Booking.com*, the Trademark Trial and Appeal Board has signaled that owners of generic.com terms will continue to be severely tested as to their protectability and registerability. In *In re The Consumer Protection Firm PLLC*,[85] the applicant sought to register "The Consumer Protection Firm" and "The Consumer Protection Firm.com & Design" on the Supplemental Register for legal services. The examining attorney refused registration of both applications on the grounds that the subject marks were generic.[86] The Board affirmed the examining attorney's refusal as to "The Consumer Protection Firm" mark.[87] With respect to "The Consumer Protection Firm.com & Design" mark, the Board affirmed the refusal to register in the absence of a disclaimer of "The Consumer Protection Firm.com" wording apart from the design.[88]

Although the parties agreed that the decision as to genericness of both marks depended on consumer perception, the crux of the disagreement was the quantity and pertinence of the evidence on which each party relied. The examining attorney relied on definitions of the term "consumer protection," allegedly generic use of "consumer protection cases" on the applicant's website, numerous examples of third-party law firm use of the phrase "the consumer protection firm," and three different legal services websites on which the term "consumer protection" was a recognized search term. The applicant relied on a definition of the term "firm," numerous third-party registrations including the term "firm" for legal services, the results of a Google search, the first two dozen results of which referred to applicant and its lawyers, and copies of articles featuring interviews with applicant's lawyers.[89]

After carefully weighing the parties' evidentiary submissions, the Board found the examining attorney's evidence far more probative of consumer

82. *See* Cotton & Thomas, *supra* note 80 ("The *Booking.com* decision is clearly a 'win' for brand owners, but a federal registration for a [generic].com mark should not be viewed as *carte blanche* to enforce what may be otherwise be a very weak mark.").

83. *See* U.S. Pat. & Trademark Off., Examination Guide 3-20, Generic.com Terms After USPTO v. Booking.com (USPTO-T-9) (Oct. 2020).

84. *Id.*

85. 2021 U.S.P.Q.2d 238 (T.T.A.B. 2021).

86. *Id.* at *2.

87. *Id.* at *23

88. *Id.* at *26.

89. *Id.* at *13–15.

perception of the marks at issue. The Board noted applicant's principal argument as to the examining attorney's evidence was that it showed use of only the phrase "Consumer Protection Firm," rather than "*The* Consumer Protection Firm."[90] The Board rejected this argument, noting that well established precedent established that the addition of the term "The" did not add any source-identifying significance or otherwise affect a phrase's genericness.[91] By contrast, the Board found the examining attorney's evidence of the use by three different legal services organizations of the term "consumer protection" as a category of law filter was the most direct evidence of the understanding of ordinary consumers.[92] The Board also observed that the fact that references to applicant appeared "higher" in a list of Google search results was not probative of trademark significance.[93] Finally, as the applicant's registration evidence, the Board noted that the subject marks presented dissimilar circumstances.[94]

Turning to "The Consumer Protection Firm.com & Design" mark, the Board noted that, although its decision must be informed by *Booking.com*, the examining attorney's conclusion of genericness in the present case was proper.[95] In so holding, it noted that the examining attorney had established the relevant public understood "The Consumer Protection Firm" to refer to legal services concerning the laws relating to consumer protection.[96] Moreover, the applicant had accepted a disclaimer of the generic matter "Firm.com" and did not preserve any question as to the disclaimer for appeal.[97] Accordingly, that "Firm.com" was generic in connection with the applicant's services was no longer in question. As a result, "The Consumer Protection Firm.com & Design" mark could only be registered with a disclaimer of the wording "The Consumer Protection Firm.com."[98]

What will *Booking.com* mean for the franchise industry? It certainly opens up possibilities for franchisors as to the adoption of new marks and provides guidance as to the evidence that should be marshalled to establish consumer perception. Among other things, franchisors may reexamine whether more attention should be devoted to protecting the .com names of their websites (assuming they are used in a trademark manner) and the advisability of pursuing protection and registration of telephone number and hashtag marks embodying arguably generic terms. Again, whether to pursue this path will likely depend on the amount of time and resources that franchisors can reasonably devote to this effort. Building consumers' perception so that they recognize generic combinations as a brand will likely be a long and arduous

90. *Id.* at *17–18.
91. *Id.*
92. *Id.* at *21.
93. *Id.* at *19.
94. *Id.*
95. *Id.* at *25.
96. *Id.*
97. *Id.* at *25–26.
98. *Id.* at *27.

process. Indeed, the cost to brand owners in establishing favorable consumer perception by surveys and other means may easily run into expenditures of six figures or more, which would likely create a cost barrier for many brand owners.[99] And even if a brand owner successfully demonstrates its generic .com mark is descriptive as opposed to generic, that alone is insufficient to result in a protectable mark.[100]

IV. *Lucky Brand Dungarees, Inc. v. Marcel Fashions Group, Inc.*: When Does "Defensive Preclusion" Apply, and When Does It Not?

Trademark disputes, as well as franchising disputes, regularly spawn litigation. Often these disputes trigger multiple rounds of multi-year litigation between the same parties. This was one such case and raised for the Court the question of whether one party's failure to litigate one of its defenses in an earlier lawsuit prevented that party from asserting that defense in a subsequent, related lawsuit.[101] The Court held that, although the traditional doctrine of claim preclusion *could* prevent a party from relying on the previously unlitigated defense under appropriate circumstances, this case at hand did not require that outcome.

The case involves three rounds of litigation between the same adversaries. In 2001, Marcel Fashions Group, Inc. (Marcel) sued Lucky Brand Dungarees, Inc. (Lucky Brand), alleging that Lucky Brand's use of the phrase "Get Lucky" in advertising Lucky Brand's clothing infringed Marcel's federally registered GET LUCKY mark. In 2003, the parties settled the lawsuit by a written settlement agreement. In that agreement, Lucky Brand agreed to cease using the phrase "Get Lucky," while Marcel released Lucky Brand of any claims regarding Lucky Brand's use of Lucky Brand's *other* trademarks that incorporated the word "Lucky."[102]

Subsequently, in 2005, Lucky Brand sued Marcel alleging that, in launching a new clothing line, Marcel and a licensee had infringed Lucky Brand's trademarks by copying Lucky Brand's designs and logos.[103] Marcel counterclaimed, alleging that (a) Lucky Brand had breached the 2003 settlement agreement by continuing to use the "Get Lucky" phrase; and (b) Lucky Brand's use of the phrases "Get Lucky" and "Lucky Brands" together infringed Marcel's GET LUCKY mark. Marcel did *not* allege that Lucky Brand's use of Lucky Brand own marks alone—apart from uses of the phrase

99. *See* Strand & Slade, *supra* note 75.

100. *See In re* Sausser Summers, PC, 2021 U.S.P.Q.2d 618 (T.T.A.B. 2021) (finding ONLINE TRADEMARKATTORNEYS.COM mark descriptive of "legal services" but denying registration for want of acquired distinctiveness); *In re* GJ & AM, LLC, 2021 U.S.P.Q.2d 617 (T.T.A.B. 2021) (reversing examining attorney's genericness refusal as to the mark COOKINPELLETS.COM in light of *Booking.com*, but affirming refusal denying registration on the grounds that the mark was merely descriptive and had not acquired distinctiveness).

101. Lucky Brand Dungarees, Inc. v. Marcel Fashion Grp., Inc., 140 S. Ct. 1589 (2020).

102. *Id.* at 1592.

103. *Id.*

"Get Lucky"—infringed Marcel's GET LUCKY mark.[104] Relying on the 2003 settlement agreement's release, Lucky Brand moved to dismiss the counterclaims.[105] The district court denied Lucky Brand's motion without prejudice and, thereafter, Lucky Brand referenced the release defense in its reply to Marcel's counterclaims.[106] But, as the 2005 lawsuit moved forward, Lucky Brand never again relied on the release defense.[107]

Ultimately, Lucky Brand lost the 2005 litigation. As a discovery sanction, the district court permanently enjoined Lucky Brand from copying or imitating Marcel's GET LUCKY mark.[108] That injunction, however, did not prohibit, "or even mention," Lucky Brand's use of any other marks or phrases containing the word "Lucky."[109] Subsequently, the jury found in Marcel's favor on Marcel's counterclaims that Lucky Brand's use of the "Get Lucky" phrase together with Lucky Brand's other marks infringed Marcel's GET LUCKY mark.[110]

A third round of litigation ensued: In April 2011, Marcel sued Lucky Brand again.[111] This time, Marcel alleged that Lucky Brand's post-2010 use of Lucky Brand's own marks—some of which contained the word "Lucky"—infringed Marcel's GET LUCKY mark. Marcel requested the district court to enjoin Lucky Brand from using any of Lucky Brand's marks containing the word "Lucky."[112]

After an interim appeal of a summary judgment order, and a remand by the Second Circuit, Lucky Brand moved to dismiss, arguing that the 2003 settlement agreement released Lucky Brand of the claims that Marcel was now asserting in the 2011 lawsuit.[113] Marcel responded that Lucky Brand was precluded from relying on the release because Lucky Brand could have, but did not, pursue its release defense in the 2005 litigation.[114] The district court agreed with Lucky Brand and dismissed the action on the basis of the 2003 release.[115] The Second Circuit, however, disagreed, holding that "defense preclusion" barred Lucky Brand from now raising the release defense.[116] The Supreme Court granted *certiorari* "to resolve differences among the Circuits regarding when, if ever, claim preclusion applies to defenses raised in a later suit."[117]

104. *Id.*
105. *Id.* at 1593.
106. *Id.*
107. *Id.*
108. *Id.*
109. *Id.*
110. *Id.*
111. *Id.*
112. *Id.*
113. *Id.* at 1593–94.
114. *Id.* at 1594.
115. *Id.*
116. *Id.*
117. *Id.*

In a unanimous opinion written by Justice Sotomayor, the Court held Lucky Brand was entitled to assert the 2003 release defense. After discussing general guideposts of the preclusion doctrine—including those of claim preclusion and issue preclusion—the Court held that its precedents require that "any . . . preclusion of defenses must, at a minimum, satisfy the strictures of issue preclusion or claim preclusion."[118] The parties agreed that issue preclusion was inapplicable, and the Court therefore focused its analysis on whether claim preclusion barred Lucky Brand's assertion of its defense.[119]

Claim preclusion can only apply "if the 'causes of action are the same' in the two suits— that is, where they share a 'common nucleus of operative fact[s].'"[120] Here, the Court reasoned, the two suits in question "were grounded on different conduct, involving different marks, occurring at different times."[121] In particular, unlike the earlier actions, the 2011 suit did not involve allegations about Lucky Brand's use of the "Get Lucky" phrase, which were central to the earlier two actions and, specifically, to the 2005 litigation.[122] As a result, the Court concluded that different marks were involved.[123] Additionally, the Court relied on the fact that the conduct alleged in the 2011 lawsuit commenced after the conclusion of the 2005 litigation, so different timeframes were involved as well. [124] At the end of the day, the Court held that the cases were simply too different for traditional claim preclusion principles to apply.[125]

Although *Lucky Brand* is not a trademark case *per se*—in the sense that the Court applied generally applicable preclusion doctrines, rather than interpreting provisions of the Lanham Act or other specific aspects of trademark law—the decision's underlying trademark background did play a role in the Court's decision. In particular, the Court noted that "[t]his principle [that later conduct often gives rise to new material facts and, therefore, to a new 'claim'] takes on particular force in the trademark context, where the enforceability of a mark and likelihood of confusion between marks often turns on extrinsic facts that change over time."[126] Indeed, the Court credited Lucky Brand's assertion that "liability for trademark infringement turns on marketplace realities that can change dramatically from year to year."[127]

In addition, trademark law incorporates a number of affirmative defenses that, pursuant to *Lucky Brand*, may be susceptible to "defense preclusion" principles in appropriate circumstances. For instance, Section 33(b) of the Lanham Act[128] enumerates nine "defenses or defects" to claims of trademark

118. *Id.* at 1595.
119. *Id.*
120. *Id.*
121. *Id.*
122. *Id.* at 1596.
123. *Id.*
124. *Id.*
125. *Id.*
126. *Id.*
127. *Id.*
128. 15 U.S.C. § 1115(b).

infringement. This list includes such items as fraud,[129] abandonment,[130] classic fair use,[131] functionality,[132] and other equitable defenses.[133] Case law has recognized additional trademark infringement defenses, such as nominative fair use.[134] Each of these defenses, at least theoretically, could be subject to *Lucky Brand*'s "defense preclusion" principles if they arise from a previously litigated "common nucleus of operative facts."

The lessons of *Lucky Brand* for the franchising community are similar to those for the litigation community more generally: once a litigant has asserted a defense in an action, if it chooses not to litigate that defense during that action, there is an identifiable risk that the litigant might not be allowed to pursue the pleaded-but-unlitigated defense in a later lawsuit. In many ways, Lucky Brand was "fortunate" that the Court deemed Marcel's 2011 lawsuit to involve different claims from the 2005 action, in which Lucky Brand failed to pursue its release defense. With this Court decision as precedent, however, future parties in similar circumstances may not be so "lucky."

V. Conclusion

It is unclear whether the Supreme Court's recent interest in trademark cases is an aberration or whether it instead signals a more lasting phenomenon. Will the sleeping giant stay awake and roam the land? Or will he return to its prior slumber? Only time will tell. . . .

129. *Id.* § 1115(b)(1).
130. *Id.* § 1115(b)(2).
131. *Id.* § 1115(b)(4).
132. *Id.* § 1115(b)(8).
133. *Id.* § 1115(b)(9).
134. *See, e.g.*, New Kids on the Block v. News Am. Publ'g, Inc., 971 F.2d 302 (9th Cir. 1992).

Encroachment in the Era of Digital Delivery Platforms: Impact of Delivery Apps on Brick and Mortar Exclusive Territories

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Over the past several years, the use of online food delivery services has exploded,[1] with millions of Americans accessing these services through apps on their smart phone or computer.[2] The COVID-19 pandemic accelerated the use of these services and opened new market segments.[3] Consumers dealt with lockdowns and other restrictions on food businesses by turning to these services to provide them with meals, instead of buying food at the grocery store

1. *See*, *e.g.*, Jack Collison, The Impact of Online Food Delivery Services on Restaurant Sales 1 (2020), https://web.stanford.edu/~leinav/teaching/Collison.pdf ("A flood of new food delivery firms has caused rapid growth in the total number of transaction and revenue for the nascent industry."); Sarwant Singh, *The Soon to Be $200B Online Food Delivery Is Rapidly Changing the Global Food Industry*, Forbes (Sept. 9, 2019), https://www.forbes.com/sites/sarwantsingh/2019/09/09/the-soon-to-be-200b-online-food-delivery-is-rapidly-changing-the-global-food-industry/?sh=7d789de8b1bc (explaining that over the past decade "a slew of companies across the world appear to have zeroed in on a new (and now not so secret) magic formula; where earlier versions of online food delivery service were limited to a single restaurant or menu, it is now a veritable buffet, allowing customers access to thousands of restaurants and millions of dishes."); Derek Thompson, *The Booming, Ethically Dubious Business of Food Delivery*, Atlantic (Aug. 2, 2019), https://www.theatlantic.com/ideas/archive/2019/08/all-food-will-be-delivered/595222 (explaining that no segment of the restaurant industry is growing faster than online delivery).

2. Levi Sumagaysay, *The Pandemic Has More Than Doubled Food-Delivery Apps' Business. Now What?*, MarketWatch (Nov. 27, 2020), https://www.marketwatch.com/story/the-pandemic-has-more-than-doubled-americans-use-of-food-delivery-apps-but-that-doesnt-mean-the-companies-are-making-money-11606340169.

3. Ryan Young, *The Impact of COVID-19 on U.S. Food Delivery Services*, Towards Data Science (Jan. 18, 2021), https://towardsdatascience.com/the-impact-of-covid-19-on-food-delivery-services-in-the-u-s-47eae04655c8.

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or dining out.[4] As a result, companies like Grubhub, Postmates, and DoorDash have earned record revenues during recent months.[5]

These developments in the restaurant industry raise two franchisee territory encroachment concerns. First, online food delivery services may deliver *within* the territory of one franchisee, even though the purchase is from a franchisee *outside* the territory, violating the exclusivity inherent in the franchisor's grant of a territory to the franchisee. Depending on the delivery service's algorithm and absent a contrary agreement, certain franchisees may benefit at the expense of other franchisees in the same system. Second, an unaffiliated online food delivery service may advertise the availability of franchised restaurant's products and place orders with a franchised restaurant on behalf of the delivery service's customers, without first obtaining permission from the franchisee to make such representations to the public and to place such orders. In these instances, the franchisee often has little ability to combat the encroachment, because the franchisor usually controls all enforcement actions regarding its trademarks. A franchisee could face serious economic and reputational harm from its inability to combat these third-party delivery services.

This article reviews encroachment issues in the restaurant franchise industry that arise out of consumers' use of online food delivery services and discusses how a franchisee may be able to combat potential lost sales that may result from online food delivery services. First, the article provides a background on online food delivery services and how they function, differentiating the two types of online food delivery services: aggregators and third-party logistics services. Next, the article examines the current state of the law as applied to the encroachment resulting from consumers' use of online food delivery services, considering the potential harm to franchisees from these services and the limited remedies available to franchisees. Finally, the article looks toward the future, concluding that delivery services are here to stay, and, in the absence of legislation and developments in the case law, some franchisees may bear a significant burden with few routes for recourse.

I. Background: Online Food Delivery Services

The public's desire to have food delivered is nothing new. In an often-told and likely apocryphal tale, the first pizza delivery occurred in 1889, when Neapolitan chef Raffaele Espositio brought a pizza to King Umberto.[6] Today, there are three principal arrangements for restaurants to provide their food to customers away from the brick-and-mortar premises of the restaurant:

4. *Id.*

5. Sumagaysay, *supra* note 2; *see also* Janine Perri, *Which Company Is Winning the Restaurant Food Delivery War?*, Second Measure (Sept. 14, 2021), https://secondmeasure.com/datapoints/food-delivery-services-grubhub-uber-eats-doordash-postmates.

6. *See, e.g.*, Alexander Lee, *The Historian's Cookbook: Pizza*, History Today, July 1, 2018, at 87.

(1) the restaurant sells directly to the customer, and its in-house delivery staff delivers the product;

(2) the customer orders through a third-party entity that processes the transaction, places an order with the restaurant, and delivers the food to the customer; or

(3) the customer orders through a third-party entity that processes the transaction, but in-house delivery staff delivers the product.

The first arrangement has been around for over seventy years and originally provided a competitive advantage in the marketplace for early adopters, most notably pizzerias and Chinese restaurants.[7] The popularity of these arrangements has dropped off for reasons discussed later, yet some businesses—such as Domino's—have expanded their in-house delivery programming.[8]

The second means of delivery—through a third-party entity (like DoorDash, Uber Eats, or Postmates)—allows restaurant franchisees to easily offer delivery services for those brands that had not historically delivered.[9] As to restaurants that have historically offered delivery services, using these third-party delivery services may reduce the restaurant's labor cost for delivery drivers, outsource delivery complications, and take advantage of the delivery service's brand name and point-of-sale technology.[10]

Under the third arrangement, the third-party entity solicits orders for the restaurant in exchange for a negotiated fee, but the restaurant uses its own personnel to make deliveries. The restaurant benefits from being listed on the third-party app as well as efficiencies in processing orders realized by utilizing the point-of-sale technology provided by the vendor, while retaining control of deliveries (and thus the quality of the consumer's experience).[11]

Notwithstanding its meteoric rise in the last few years, online food delivery service has existed since the early days of the Internet.[12] Early on, these services were limited to grocery deliveries. Companies like HomeGrocer and Peapod laid the groundwork for today's food delivery services.[13] Soon

7. Emelyn Rude, *What Take-Out Food Can Teach You About American History*, Time (Apr. 14, 2016), https://time.com/4291197/take-out-delivery-food-history.

8. Heather Haddon, *Domino's Pizza Goes It Alone on Delivery*, Wall St. J. (Aug. 19, 2019), https://www.wsj.com/articles/dominos-goes-it-alone-on-delivery-11566219685?mod=article_inline.

9. These success stories are heralded by the food delivery services. *See, e.g.*, *Merchant Success Stories*, DoorDash, https://get.doordash.com/en-us/success-stories (last visited Aug. 30, 2021); *Restaurant Stories from Around the World*, Uber Eats for Merchants, https://restaurants.ubereats.com/us/en/restaurant-stories/ (last visited Aug. 30, 2021).

10. Kara K. Martin, *Disruptive New Technologies and Franchising*, IBA/Int'l Franchise Assoc. 34th Ann. Joint Conference 4 (May 2018).

11. Lindsey Christians, *How to Think Smarter About Ordering Takeout and Deliv*ery, Cap. Times (Feb. 20, 2021), https://madison.com/ct/entertainment/dining/how-to-think-smarter-about-ordering-takeout-and-delivery/article_b04844d6-2324-5c8b-b493-839405e63d4a.html. Because these relationships are contractual in nature, they do not raise issues relating to unauthorized distribution, although encroachment of another franchisee's territory is possible.

12. Christopher Mueller, *Deliverying Food to the Front Door: A New, Or Very Old, Convenience?*, Boston Hosp. Rev. (Feb. 1, 2015), https://www.bu.edu/bhr/2015/02/01/780.

13. Scott Austin, *10 Years Ago Today: When Online Groceries Were All the Rage*, Wall St. J. (Nov. 2, 2009), https://www.wsj.com/articles/BL-VCDB-3817.

after, in 1994, Pizza Hut became the first major restaurant franchise system to offer customers the ability to order online.[14] Within a year, World Wide Waiter launched the country's first online food delivery service.[15]

Originally founded as a means for restaurants to eliminate paper menus, Grubhub transformed itself into the country's first major online food delivery service.[16] After a 2011 merger with Seamless—a different online food delivery service—Grubhub expanded its services and soon became available in nearly every major American city. Within a handful of years, Uber Eats, Postmates, DoorDash and EatStreet were launched to compete with Grubhub in the online food delivery space.[17] Now, these services collectively cover almost all metropolitan areas across the country.[18] The COVID-19 pandemic only fueled their growth, as these delivery services provided a badly needed means for restaurants to supplement sales when faced with government-imposed limitations on in-person dining.[19]

From the customer's perspective the process is simple:

(1) The customer logins onto the service's website or smartphone app;

(2) The customer is provided with a list of restaurants to order from, reviews the menu, and places an order using the app or website;

(3) The customer pays for the order using a credit card or other electronic means of payment on the service's app or website;

(4) The restaurant receives the order from the online service and then prepares the food; and

(5) A courier picks up the order and delivers it to the customer.

Behind the scenes, however, the business is more complicated. These major food delivery services fall into two broad categories: aggregators and third-party logistics services.

The primary difference between the types of businesses is how the transactions are structured.[20] Aggregators like Grubhub charge the restaurant a

14. Michael Schrage, *On-Line Pizza Idea Is Clever but Only Half-Baked*, L.A. Times (Aug. 25, 1994), https://www.latimes.com/archives/la-xpm-1994-08-25-fi-31168-story.html.

15. Erik Lorenzsonn, *Delivering on Its Potential: How Eatstreet Is Changing the Way Madison Gets Dinner*, Capitol Times (Sept. 26, 2018), https://madison.com/ct/business/technology/delivering-on-its-potential-how-eatstreet-is-changing-the-way-madison-gets-dinner/article_e806c59f-9d3b-59e5-9333-f9c6dbe409ba.html. Rebranded as Waiter.com, this food delivery service is still around today, although it is much more limited than the major players in the industry. *See Our Story: Happiness Through Food*, Waiter.com, https://www.waiter.com/our-story (last visited Aug. 30, 2021).

16. *Grubhub History*, Grubhub, https://about.grubhub.com/about-us/company-timeline/default.aspx (last visited Aug. 30, 2021).

17. Mike Isaac, *One Surprise Standout for Uber: Food Delivery*, N.Y. Times (Sept. 23, 2017), https://www.nytimes.com/2017/09/23/technology/ubereats-food-delivery.html.

18. Perri, *supra* note 5, at 2.

19. Kate Conger, *A Pandemic Lifeline for Restaurants, Delivery Is 'Here to Stay'*, N.Y. Times (July 2, 2021), https://www.nytimes.com/2021/07/02/technology/restaurant-delivery-takeout-orders-covid-coronavirus.html.

20. Andraya Frith et al., *Food Delivery Service Issues: The Last Mile—Navigating the Restaurant Food Delivery Paradigm Shift*, Int'l Franchise Assoc. 52nd Ann. Legal Symposium (2019).

commission fee ranging from five percent to thirty percent to permit customers to order from the aggregator's app or website, with aggregators sometimes providing a higher placement in their app search results for higher commissions.[21] In addition, aggregators generally charge a separate delivery fee.[22] The aggregator may also impose an additional "small order fee" on the customer if the order does not meet a certain price threshold.[23] Because delivery fees and small order fees are costs are built into the customer order price, the customer ultimately pays substantially more than he or she otherwise would have paid in-store. Commissions can also cut significantly into the restaurant's profit margin, especially if the delivery services' terms limit a restaurant's increases in online menu prices. In some instances, for an additional fee, aggregators will work with restaurants to provide marketing and advertising assistance.[24] Each of these additional expenses may result in little to no profit for restaurants.[25]

Conversely, third-party logistics services act as "a pick-up service representing the customer . . . not a delivery service representing the restaurant."[26] These services only charge a delivery fee to the customer and do not charge the restaurant a commission or service fee. For the most part, third-party logistics services appear to be fading, with former standouts such as Postmates[27] operating more like aggregators since launching partnership programs like Postmates' Merchant Program.[28] There are also occasions where an aggregator initially behaves like a third-party logistics service to get a foothold with a restaurant's customers, only to approach the restaurant and

21. *Id.* at 12–15; *see also* Bobby Allyn, *Restaurants Are Desperate—But You May Not Be Helping When You Use Delivery Apps*, NPR (May 14, 2020), https://www.npr.org/2020/05/14/856444431/cities-crack-down-on-food-delivery-app-fees-as-restaurants-struggle-to-survive; Noah Licentstein, *The Hidden Cost of Food Delivery*, Techcrunch (Mar. 16, 2020), https://techcrunch.com/2020/03/16/the-hidden-cost-of-food-delivery. These high rates have caused cities like Seattle, New York City, and San Francisco to impose rate caps. Biz Carson, *Delivery Companies Are Fighting City Commission Caps. Does Anybody Win?*, Protocol (May 20, 2020), https://www.protocol.com/delivery-commission-caps-uber-eats-grubhub.

22. Frith, *supra* note 20, at 12–15.

23. Brian X. Chen, *Up to 91% More Expensive: How Delivery Apps Eat Up Your Budget*, N.Y. Times (Feb. 26, 2020), https://www.nytimes.com/2020/02/26/technology/personaltech/ubereats-doordash-postmates-grubhub-review.html.

24. Frith, *supra* note 20, at 12 (citing Kanika Gupta, *Case Study: The Three Biggest Food Delivery Services and What They Mean for You*, Bikky Inc. (June 26, 2018)); *see also Restaurant Survival Guide for the 2020s*, Nation's Restaurant News (May 4, 2020), https://www.nrn.com/node/393062 (detailing how Grubhub can assist in marketing, promotions, customer loyalty programs, and consulting services).

25. Gene Marks, *Restaurant Owners May Not Like Delivery Services—but Can They Do Without Them?*, Guardian, (Dec. 2, 2020), https://www.theguardian.com/business/2020/dec/02/restaurant-owners-delivery-services-grubhub-doordash-fees-pandemic.

26. Sara Jones, *The Postmates Problem: Why Some Restaurants Are Forced to Fight the Delivery App*, Eater (July 31, 2015), https://www.eater.com/2015/7/31/9074491/postmates-delivery-problems (quoting Postmates' then-director of business development Anand Dass).

27. Uber acquired Postmates in late 2020 to improve growth in its Uber Eats division. Mike Isaac, Erin Griffith & Adam Satariano, *Uber Buys Postmates for $2.65 Billion*, N.Y. Times (July 5, 2020), https://www.nytimes.com/2020/07/05/technology/uber-postmates-deal.html.

28. Frith, *supra* note 20, at 12.

negotiate some formal arrangement.[29] That said, restaurants dealing with a true third-party logistics service may realize a higher profit margin on a sale than it would under an arrangement with an aggregator due to the absence of commissions and the customer footing the cost of the delivery.

For the purposes of this article, aggregators are online food delivery services that have formal agreements to provide services on behalf of a restaurant, and third-party logistics services are those service providers that do not have a contractual relationship with a restaurant.

Some restaurant franchisors have entered into formal arrangements with online delivery services.[30] Most prominently, Grubhub had a formal relationship with Yum! Brands, the parent company of Taco Bell and KFC.[31] Although things have since turned sour between Yum! Brands and Grubhub,[32] many other restaurants are partnering with aggregators and third-party logistics services.[33] Generally, franchisees are not required by their franchise agreements to utilize these services, but franchisees may nevertheless be subjected to the agreement of a franchisor and service.[34] If a franchisor enters an agreement with an aggregator, in circumstances where the franchise agreement does not expressly authorize that change but includes provisions under which the franchisor can modify its "system" without consent of the franchisee, the franchisee may want to assert that change is not permitted or is perhaps a violation of good faith and fair dealing.[35] Those issues are beyond the scope of this article.

Because both aggregators and third-party logistics services function as intermediaries between the customer and the franchisor's product sold through the franchisee, two potential encroachment issues may arise. First, the online food delivery service may pick-up an order *within* the territory of one franchisee and deliver to a customer located *outside* the franchisee's

29. *See* Nait Garun, *Grubhub's New Growth Hack Is Listing Restaurants That Didn't Agree to Be Listed*, Verge (Jan. 20, 2020), https://www.theverge.com/2020/1/29/21113876/grubhub-seamless-fake-restaurant-listings-no-permission-postmates-doordash.

30. Perri, *supra* note 5, at 2.

31. *Yum! Brands and Grubhub Announce New U.S. Growth Partnership*, Yum! (Feb. 8, 2018), https://www.yum.com/wps/portal/yumbrands/Yumbrands/news/press-releases/yum%21+brands+and+grubhub+announce+new+u.s.+growth+partnership.

32. Amelia Lucas, *Taco Bell Owner Sues Grubhub, Claiming It Violated Distribution Agreement*, CNBC (June 11, 2020), https://www.cnbc.com/2020/06/11/taco-bell-owner-sues-grubhub-claiming-it-violated-distribution-agreement.html.

33. *See, e.g.*, Perri, *supra* note 5, at 2 (identifying delivery arrangements with Starbucks, Popeyes, and Wendys); Heather Haddon, *Little Caesars Teams Up with DoorDash on Delivery*, Wall St. J. (Jan. 6, 2020), https://www.wsj.com/articles/little-caesars-teams-up-with-doordash-on-delivery-11578286860. KFC and Taco Bell have also recently negotiated deals with DoorDash. Alicia Kelso, *Taco Bell Adds DoorDash as a Delivery Partner*, RestaurantDive (Oct. 14, 2020), https://www.restaurantdive.com/news/taco-bell-partners-with-doordash-after-ending-exclusive-grubhub-deal/586959.

34. Jennifer Dolman & Dominic Mochrie, *Driving Sales Without Driving You Crazy—The Unique Challenges of Delivery Aggregators in Franchise Systems*, Whos Who Legal (Nov. 14, 2019), https://whoswholegal.com/features/driving-sales-without-driving-you-crazy--the-unique-challenges-of-delivery-aggregators-in-franchise-systems (explaining what franchisors must consider their current franchisee contracts before entering into delivery arrangements).

35. *Id.*; Frith, *supra* note 20, at 17.

territory. The restaurant from where the order is placed and delivered is often determined by the customer's physical location and not by the contracted-for exclusive territory.[36] Second, a franchisee may not wish to utilize third-party delivery services for a number of reasons, but finds that third parties are doing so anyway without its consent.[37] That franchisee, however, may find its ability to prevent an unaffiliated online food delivery service from delivering the franchisee's products to be constrained by its franchisor's control of enforcement actions as to the system's trademarks and intellectual property.

II. Encroachment Arising out of Online Food Delivery Services

Since the 1950s, franchising has become a distinctive feature of our economy with hundreds of thousands of active franchises across the country.[38] As franchises have grown and developed, encroachment—or the fear of encroachment—has surfaced as a significant problem in the franchising world. Encroachment usually occurs when a franchisor violates its franchisee's contracted-for exclusive territory.[39] Although franchisors offer exclusive territories less often today than in the past, many franchisees have some form of exclusive territory.[40] Most commonly, the territory is set forth in the parties' contract; however, in some states, statutory law provides additional protection.[41]

Because traditional franchise agreements usually define exclusive territory in terms of radius, maps, population density, and the like,[42] e-commerce has created issues when a franchise agreement is silent on how online sales may affect the franchisee's brick-and-mortar territory. Questions arise regarding the extent of the franchisee's exclusive territory, the franchisor's responsibilities to prevent the online sale of its products into a franchisee's territory, and where the "sale" occurs. If a franchisee elects not to participate in an online delivery service, it begs the question whether the franchisor may

36. Frith, *supra*, note 20, at 21. It is unclear whether franchisors have the ability to affect the specific algorithms used by online food delivery services.

37. These reasons include (1) retaining control of the quality of delivery services rendered and food safety practices; (2) avoiding potential liability problems that could arise out of the acts of a third party whom the customer may view as the agent of the restaurant; and (3) staying clear of questions relating to the collection of sales tax for services rendered by the third party.

38. Daniel J. Oates, Vanessa L. Wheeler, & Katie Loberstein, *A State's Reach Cannot Exceed Its Grasp: Territorial Limitations on State Franchise Statutes*, 37 Franchise L.J. 185 (2017).

39. Lori J. Parker, 22 Causes of Action 2d 91 (2021) (collecting cases). Encroachment finally became a cause of action soon after the U.S. Supreme Court found that territorial restrictions did not violate the Sherman Antitrust Act. *See* Cont'l T.V. Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977).

40. Robert W. Emerson, *Franchise Territories: A Community Standard*, 45 Wake Forest L. Rev. 779, 786 (2010).

41. *Id.* at 787-88 (citing Haw. Rev. Stat. § 482E-(6)(2)(e) (2008); Ind. Code §§ 23-2-2, 7-1(2), -2(4) (1999); Iowa Code § 523 H.6 (2007); Wash. Rev. Code § 19.100.180(2)(F) (1999); Minn. R. § 2860.4400(C) (2009)).

42. Emily I. Bridges, *Keep off My (Virtual) Lawn: Encroachment in the Age of the Internet*, 36 Franchise L.J. 415, 418 (2017).

direct online orders from customers located with that franchisee's territory to another franchisee that is participating in the program.

When a franchisor offers its products or services online, individuals from across the country may purchase the product from anywhere, including a franchisee's exclusive territory.[43] If the franchisor has reserved the right to distribute its products and services through "alternative distribution channels" under its franchise agreement, it may have reserved the right to permit third-party delivery services to make deliveries within a franchisee's territory—if the reservation of rights is broad enough to permit such practices.

With a continuing shift from brick-and-mortar locations to online shopping, online encroachment issues in the franchise context have only been exacerbated by the COVID-19 pandemic.[44] According to the International Franchise Association (IFA), 21,834 restaurant franchises have permanently closed due to the pandemic, and an estimated 36,000 are at serious risk of failing without additional government assistance.[45] In a more recent report, the IFA optimistically projected that the industry will recover most of these losses and identifies that franchises with significant drive-through and delivery businesses have "weathered the storm better than [full-service restaurants]."[46] It remains to be seen how franchisors will approach the post-pandemic environment with nearly every indicator pointing toward a more delivery-based system.[47]

Courts have taken different approaches in dealing with the online encroachment issues. In some decisions, courts have relied on the existence or absence of the franchise agreement's express terms. For instance, in *Stillwell v. Radio-Shack Corp.*,[48] the United States District Court for the Southern District of California found that because the franchise agreement did not expressly prohibit online sales, there was no encroachment by the franchisor for selling products within the franchisee's exclusive territory.[49]

In a similar situation, a federal district court in Michigan rejected a golf product franchisee's motion for summary judgment given the factual question as to whether actual sales occurred within the franchisee's territory.[50]

43. *Id.* at 417.

44. Harold Brown et al., Franchising: Realities and Remedies § 1.01 (Law Journal Press rev. ed. 2021).

45. *Id.* (citing *Six-Month COVID-19 Impact Analysis on Franchising Market*, FranData (Sept. 2020), https://www.franchise.org/sites/default/files/2020-10/SixMonth%20COVID%20Impact%20on%20Franchising_Final.pdf).

46. *Business Outlook for 2021*, FranData (Feb. 4, 2021), https://www.franchise.org/sites/default/files/2021-02/Economic%20Outlook%202021_web2.pdf (prepared for International Franchise Association).

47. Jackie Davalos, *DoorDash Falls amid Steep Costs to Sustain Pandemic Growth*, Bloomberg (Aug. 12, 2021), https://www.bloomberg.com/news/articles/2021-08-12/doordash-beats-sales-estimates-on-sustained-food-delivery-demand; *see also* Conger, *supra* note 19, (discussing adjustments made by businesses to account for heightened delivery demand).

48. Stillwell v. Radio-Shack Corp., 676 F. Supp. 2d 962 (S.D. Cal. 2009).

49. *Id.* at 971.

50. Pro Golf of Fla., Inc. v. Pro Golf of Am., Inc., No. 05-71380, 2006 WL 1556211 (E.D. Mich. June 6, 2006).

Because the franchise agreement was silent on the issue of Internet sales, the court found that "where" the title to the purchased items transferred was a factual question requiring determination by the fact finder to assess whether the sale violated the exclusive territory provision.[51] If carried forward, this recognition could foreclose online encroachment actions.[52]

With these issues on the horizon, some franchisors have ceased granting exclusive territory altogether or explicitly qualifying that the franchisee may face competition from other franchisees and the franchisor through alternate distribution channels.[53] Effective as of July 1, 2007, the FTC Franchise Rule required disclosures in Item 12 of a franchisor's Franchise Disclosure Document (FDD) regarding whether restrictions are placed on the solicitation and acceptance of orders within the franchisee's exclusive territory through the Internet or alternative distribution channels, in addition to disclosure regarding whether the franchisor grants exclusive territories.[54]

Newpaper, LLC v. Party City Corp. provides an example of how courts likely will treat claims arising under franchise agreements reserving the franchisor's right to sell online.[55] There, the United States District Court for the District of Minnesota rejected a franchisee's breach of contract claim premised on the franchisor's sale of products online in violation of the franchise agreement's exclusive territory grant because the franchisor expressly reserved the right to sell products to customers located within the exclusive territory through "any channel of distribution, including whole sales and sales by or through the internet."[56]

Today, almost invariably, franchisors reserve the right to sell products or services to customers within franchisees' exclusive territories through any channel of distribution, including wholesale and sales by or through the Internet.[57] Most of these agreements include language specifically reserving the right of both the franchisor and sister franchisees to sell within the franchisee's territory through alternative distribution channels, including the Internet. Many FDDs explicitly state that the franchisee may experience competition from the franchisor and sister franchisees through these alternative distribution channels.

51. *Id.* at *7.

52. Robert W. Emerson, *Franchise Encroachment*, 47 Am. Bus. L.J. 191 (2010) ("[The *Pro Golf of Florida* decision] could signal the death knell for internet encroachment claims based on exclusivity provisions restricting franchisor sales occurring within a franchisee's territory.").

53. Bridges, *supra* note 42, at 425–26.

54. 16 C.F.R. § 436.5(l)(6).

55. Newpaper, LLC v. Party City Corp., No. CIV. 13-1735 ADM/LIB, 2013 WL 5406722 (D. Minn. Sept. 25, 2013).

56. *Id.* at *4.

57. The authors pulled from the Wisconsin Department of Financial Institutions dozens of recent financial disclosure documents of restaurant franchise systems. These systems ranged from fast food to fast causal to traditional sit-down restaurants. The disclosure documents nearly uniformly reserved the franchisor's right to distribute within the franchisee's territory through alternate distribution channels and explicitly advised that the franchisee may face such competition.

A. *Delivery Services Delivering Goods from One Franchisee's Territory into Another Franchisee's Territory*

Although other factors might come into play, when a customer orders from an online food delivery service, his or her geospatial position is the primary determinant for which restaurants are available for delivery.[58] If an online food delivery service negotiates a "territory" with a franchisor, that territory might not match the delineation of territories for brick-and-mortar stores. Consequently, a franchisee closer to the individual may complete the sale, and the food may be delivered within another franchisee's exclusive territory.

These online delivery sales can substantially affect the bottom line of the encroached-upon franchisee. It has often been said that location is everything and franchising is no exception to that rule. A desirable territory is often a deciding factor for prospective franchisees, and it is crucial to the franchisee's financial success.[59] The franchisee, however, faces difficulty in maintaining exclusive rights to this territory. As a general matter, in absence of an express condition in a franchise agreement that addresses intra-system competition, the franchisee faces a difficult challenge in convincing a court to find the franchisor responsible to prevent such competition.[60]

The franchisor is in the best position to prevent intra-system encroachment caused by online food delivery services, and it may also have an obligation to do so. Ultimately, whether a franchisor must protect its franchisee from intra-system competition turns on (1) the language of the franchise agreement; and (2) whether the franchisor's action (or inaction) rises to the level of violating the express or implied covenant of good faith and fair dealing. In the first instance, if the franchise agreement unequivocally states that franchisees will be protected from intra-system competition, then the franchisor has a legal obligation to police its franchisees. Conversely, if the franchise agreement states that franchisees will experience intra-system competition, then courts are unwilling to read in an obligation contrary to the agreement's text.[61] When a franchisor has disclosed the risks and burdens of the franchise agreement, only in an "extreme abuse case[]" may a franchisee assert a violation of good faith and fair dealing.[62] In absence of express language in the franchise agreement addressing a franchisor's obligation (or lack thereof) to police encroachment by and among its franchisees,

58. Frith, *supra* note 20, at 16.

59. *See* H.G. Parsa et al., *Why Restaurants Fail? Part IV: The Relationship Between Restaurant Failures and Demographic Factors*, 56 Cornell Hosp. Q. 80–90 (2015) (finding that location makes significant difference in restaurant failure—which is consistent with earlier studies).

60. Craig Tractenberg et al., *The Franchisor's Duty to Police the Franchise System*, 36 Franchise L.J. 87, 89–92 (2016) (explaining that few courts have imposed a duty to police a franchise system and those that do generally base it on protecting the public from being misled regarding the quality of products under the franchisor's trademark).

61. Joel Iglesias, *Applying the Implied Covenant of Good Faith and Fair Dealing to Franchises*, 40 Hous. L. Rev. 1423, 1438 (2004).

62. *Id.*

the case law leans in favor of the franchisor and depends heavily on the facts at hand.[63]

The most obvious instance in which the franchisor does have an affirmative duty to protect its franchisees from intra-system encroachment would be where the franchise agreement includes a contractual obligation to do so. In other instances, an obligation may be inferred from the circumstances at hand based on the implied covenant of good faith and fair dealing.[64]

Pepsi-Cola Bottling Co. of Pittsburg, Inc. v. PepsiCo, Inc. provides an illustration of the interplay between a franchisor's express and implied obligations to enforce territorial agreements between franchisees.[65] There, in reversing summary judgment in the franchisee's favor, the Tenth Circuit found that PepsiCo—as grantor—had a duty to "take reasonable steps to prevent competing bottlers from encroaching on Pittsburg Pepsi's exclusive territory."[66] The court found that exclusive bottling appointment (EBA), a "vigorous no-fault transshipment enforcement program," and the implied duty of good faith and fair dealing obligated PepsiCo to protect its franchisee from intra-system encroachment.[67] While there were still unresolved facts as to whether PepsiCo breached the EBA's exclusivity clause, the court held that (a) franchisors, under certain circumstances, are obligated to protect their franchisee's exclusive territory granted in the franchise agreement; (b) even if not expressly provided for in the franchise agreement, the franchisor may still be obligated to protect its franchisee's territory under an implied good faith and fair dealing theory; and (c) a jury could conclude that PepsiCo's knowledge of the intra-system poaching was a meaningful consideration with respect to its failure to enforce its transshipment enforcement program.[68]

Most franchise agreements do not require franchisors to enforce their franchisees' territorial boundaries. Yet, even in the absence of a separate territorial enforcement program, constructive notice may be sufficient to obligate the franchisor to take action against the encroachment. For example, if the franchisor receives multiple complaints from franchisee A that an online food delivery service is delivering franchisee B's food within franchisee A's territory, the franchisor's notice and response to the complaints may implicate its implied duty of good faith and fair dealing. This obligation is buttressed by the franchisor's positioning as the grantor of both franchises.[69]

63. Gary R. Duvall, *Using the Web More Effectively*, 24 Franchise L.J. 173, 176 (2005) (analyzing several court and arbitration decisions before concluding that "contract language will normally determine the outcome" and if that language is ambiguous, then "the facts of each case will determine how the implied covenant of good faith and fair dealing will be applied").

64. *See also* Rochelle Spandorf et al., *Implications of the Covenant of Good Faith: Its Extension to Franchising*, 5 Franchise L.J. 5 (1986).

65. Pepsi-Cola Bottling Co. of Pittsburg, Inc. v. PepsiCo, Inc., 431 F.3d 1241 (10th Cir. 2005).

66. *Id.* at 1259.

67. *Id.*

68. *Id.* at 1259–60.

69. Duvall, *supra* note 63, at 176 ("All is not lost, however, if the existing franchise agreements do not reserve the right of the franchisor to market via alternative channels such as the Internet. Franchisors can develop an Internet strategy that avoids the franchisees' exclusive territories.").

Fundamentally, franchisee A's exclusivity provision would be toothless if the franchisor neglected to act in these circumstances. In *Scheck v. Burger King Corp.*,[70] the court found that the covenant of good faith and fair dealing protected a franchisee from Burger King placing competing franchises near the franchisee, despite there being no express grant of exclusive territory.[71] In the aftermath of that 1992 decision, however, many franchisors now regularly include provisions that explicitly allow for intra-system competition.

Most courts reject arguments that a franchisor has an affirmative duty to protect a franchisee from deliveries made by a fellow franchisee within the exclusive territory of the first franchisee. For example, in *Cottage Inn Carryout & Delivery, Inc. v. True Freedom, Investments, LLC*, a franchisee claimed that its franchisor breached the franchise agreement by failing to prevent another franchisee from delivering pizzas within the agreed-upon exclusive territory.[72] The United States District Court for the Eastern District of Michigan dismissed this claim because the contract did not state that the franchisor had a duty to police the franchisee's exclusive territory, and the court was unwilling to read in an obligation to do so.[73] Further, there was no violation of the implied covenant of good faith and fair dealing because Michigan law does not recognize it as a separate cause of action apart from a breach of contract.[74]

In another recent decision, *Mailing & Shipping Systems, Inc. v. Neopost USA*, the United States District Court for the Western District of Texas held that, absent an express contractual provision, a distributor was not required to protect its dealer from intra-system encroachment.[75] The court found that even if with a general duty of good faith and fair dealing,[76] the parties' agreement did not explicitly obligate the grantor to protect against intra-system encroachment.[77]

Relatedly, absent a provision in the franchise agreement to the contrary, franchisors are not obligated to negotiate contracts with online delivery services. However, if a franchisor were to establish such a delivery arrangement, then the franchisor's failure to properly ensure compliance with exclusivity agreements with its franchisees during the implementation of the online delivery arrangement could be considered to be a critical fact in finding a breach of good faith and fair dealing.

70. Scheck v. Burger King Corp., 798 F. Supp. 692 (S.D. Fla. 1992).

71. *Id.*

72. Cottage Inn Carryout & Delivery, Inc. v. True Freedom Invs. LLC, No. CIV. 10-12833, 2010 WL 4188311 (E.D. Mich. Oct. 20, 2010).

73. *Id.* at *4.

74. *Id.*

75. Mailing & Shipping Sys., Inc. v. Neopost USA, Inc., 937 F. Supp. 2d 879 (W.D. Tex. 2013).

76. Texas law, unlike most states, does not impose a duty of good faith and fair dealing in every contract. Houle v. Casillas, 594 S.W.3d 524, 544 (Tex. Ct. App. 2019) ("[U]nder Texas law not all contracts contain an implied covenant of good faith and fair dealing.").

77. *Mailing & Shipping Systems, Inc.*, 937 F. Supp. 2d at 888.

Further, as discussed later, franchisors generally reserve all rights to enforce trademark rights and can prevent unassociated online food delivery services from engaging with a franchisee. For example, a harmed franchisee may be unable to resolve the actual issue without the assistance of the franchisor. The harmed franchisee cannot pursue a claim against the benefitting sister franchisee because the harmed franchisee lacks trademark policing rights. Additionally, a franchisor may negotiate arrangements with the online food delivery services at a system level—something that franchisees are unable to do at all.[78]

In the absence of an explicit obligation to police the system and protect aggrieved franchisees, franchisees will likely struggle to force their franchisor to take action. Franchisees, in turn, likely will need to rely on strong franchisee associations to lobby the franchisor to monitor online sales practices and take decisive action as necessary. If the franchisor requires franchisees to use an aggregator, for example, the franchisor arguably should have an increased obligation to protect franchisees from having their franchise rights diluted.

B. *Delivery App Services Who Have Not Obtained Permission to Sell Franchisee's Products*

The lack of a formal agreement between a restaurant and a third-party logistics service leads to several concerns regarding brand reputation. For example, in Madison, Wisconsin, several restaurant owners expressed concerns regarding a third-party logistic service failing to provide up-to-date menus, slow delivery, spoliation, and a general lack of control over the delivery process.[79] Naturally, the restaurants were concerned with the association between the poor delivery service and the actual restaurant itself. The Old Fashioned—a popular Madison restaurant—eliminated to-go ordering entirely due to negative reception from customers regarding their famed cheese curds being delivered cold or late.[80]

This problem is not unique to Madison, Wisconsin. In October 2020, a plaintiff filed a putative action seeking to represent 150,000 restaurants that alleged Grubhub violated the Lanham Act by using the putative classes' trademarks without permission.[81] The plaintiff alleged that Grubhub listing its and the putative class members' restaurants without permission had: (1) disrupted normal operations; (2) overburdened staff; (3) created quality issues; (4) affected the classes' ability to control customer service; (5) caused

78. Frith, *supra* note 20, at 15 (discussing trademark limitations imposed by aggregator agreements).

79. Lindsay Christians, *Grubhub Hubbub: Restaurants Fire Back at Delivery Companies That Post Menus Without Consent*, Cap Times (Feb. 22, 2020), https://madison.com/ct/entertainment/dining/grubhub-hubbub-restaurants-fire-back-at-delivery-companies-that-post-menus-without-consent/article_6e709111-900a-57f7-8998-e462e9e5db5a.html

80. *Id.*

81. Lynn Scott, LLC v. Grubhub Inc., 1:20-CV-06334 (N.D. Ill Oct. 26, 2020). This case settled out of court in April 2021. Julie Littman, *Grubhub Settles Lawsuit over Non-Partnered Listings*, RestaurantDive (Apr. 21, 2021), https://www.restaurantdive.com/news/grubhub-settles-lawsuit-over-non-partnered-listings/598780.

unnecessary and increased order refunds; (6) affected the classes' catered method of enjoyment; (7) altered the tip distribution; (8) affected relationships with contracted delivery services; and (9) overcharged orders.

To demonstrate these harms even further, consider a company that prides itself on guaranteeing a level of service. Although "30 minutes or free pizza" promotions have gone by the wayside, similar guarantees are prevalent. Jimmy John's was originally at the forefront of the fight against online food delivery services in part because of their "freaky fast" delivery guarantee.[82] Recently, the company decided to partner with DoorDash on the condition that Jimmy John's own delivery drivers would continue to handle the deliveries.[83] Another example is in the nearly ubiquitous "100% satisfaction guaranteed" statements. Placing customer orders in the hands of unaffiliated delivery services can and has created serious problems.

Moreover, there is a growing trend in which customers submit fraudulent refund requests after receiving their food.[84] These scams play on the high volume of restaurant sales, the disconnect from the delivery app to the restaurant, and the "customer is always right" mantra.[85] Despite online food delivery service providers' efforts, this modern "dine and dash" scam has forced several restaurants to close and has affected countless other restaurants.[86]

Most non-franchised restaurants are capable of fending off unaffiliated delivery services, albeit at a cost of legal expenses. As owners of their own trademarks, non-franchised restaurants can file or participate in lawsuits like the putative class action against Grubhub. But because franchisors typically retain control over enforcement of their trademarks, an affected franchisee must rely on the franchisor filing lawsuits or joining such class actions.

Recent legislative efforts have provided some help to restaurants against unaffiliated delivery services. Effective January 1, 2021, California has prohibited food delivery services from arranging for the delivery of an order from a restaurant without first obtaining an agreement with the food facility expressly authorizing the food delivery service to take orders and deliver meals prepared by the restaurant.[87] New York has introduced similar legislation.[88]

82. Amelia Lucas, *Jimmy John's Partners with DoorDash but Will Still Deliver Its Own Sandwiches*, CNBC (Dec. 2, 2020), https://www.cnbc.com/2020/12/02/jimmy-johns-partners-with-doordash-but-will-still-deliver-its-own-sandwiches.html.

83. *Id.*

84. Amarelle Wenkert, *The Dark Side of Delicious: Decoding Food Delivery Fraud on the Dark Web*, Riskified Blog, (Aug. 17, 2020), https://www.riskified.com/blog/the-dark-side-of-delicious-the-dark-web-can-teach-us-about-food-delivery-fraud.

85. *Id.*

86. Alex Lockie, *Delivery App Fraud: The New Dine-and-Dash Hurting Restaurants*, 1851 Franchise (Mar. 1, 2021), https://1851franchise.com/delivery-app-fraud-the-new-dine-and-dash-hurting-restaurants-2715121#stories.

87. Cal. Bus. & Prof. Code § 22599.

88. Kelly McCarthy, *New Law Requires Delivery Platforms to Partner with Restaurants Directly*, ABC News (Jan. 7, 2021), https://abc7ny.com/new-law-requires-delivery-platforms-to-partner-with-restaurants-directly/9413711; *see* New York State Assembly Bill A784 (2021).

Laws like California's delivery law may protect franchisees from the harms created by unaffiliated delivery services. However, franchisees that lack meaningful trademark rights still face an uphill battle. These franchisees are essentially unable to prevent the third-party logistics services from listing the franchisee on their apps and websites without their franchisor taking action.

While most courts have found that the franchisor is not required to actively police the franchise system, a franchisor's duty to police its trademark and contractual duty to police system standards may require action against unaffiliated delivery services.[89] This duty would presumably stem from franchise agreement provisions that require the franchisee to report any potential infringement issues and reserve to the franchisor the exclusive right to enforce the trademarks through litigation.[90]

When a franchisor fails to adequately police its trademark, it runs the risk of abandonment of the mark.[91] Naked licensing occurs when a licensor grants permission to use a mark without sufficient control over the licensee's goods or services.[92] The Lanham Act requires that trademark holders, including franchisors, adequately maintain certain quality standards.[93] This requirement reflects the core purpose of trademark law: to eliminate transaction costs to allow the consumer to make quicker, more informed choices.[94] Or, as the Seventh Circuit stated:

> A person who visits one Kentucky Fried Chicken outlet finds that it has much the same ambiance and menu as any other. A visitor to any Burger King likewise enjoys a comforting familiarity and knows that the place will not be remotely like a Kentucky Fried Chicken outlet (and is sure to differ from Hardee's, Wendy's, and Applebee's too). The trademark's function is to tell shoppers what to expect—and whom to blame if a given outlet falls short. The licensor's reputation is at stake in every outlet, so it invests to the extent required to keep the consumer satisfied by ensuring a repeatable experience.[95]

Accordingly, failure to exercise control over the goods and services obviates the fundamental purpose of trademark law, and courts regularly find that the licensor has abandoned the mark in such circumstances.[96]

Applied here, a franchisor runs the risk of abandoning its trademark if the franchisor makes no effort to control the quality of the franchisee's food delivery. As noted earlier, third-party food delivery services often fail to

89. Tractenberg, *supra* note 60, at 87–92 .

90. Of the agreements that the authors obtained, all contained a provision providing for policing.

91. Christopher Kelly & Vincent Frantz, *Basics Track: Franchisor's Intellectual Property and How to Protect It*, Int'l Franchise Assoc. 52nd Ann. Legal Symposium (2019).

92. *Id.* at 32; *see also* Luke S. Curran, *NSFW: Naked Licensing and Uncontrolled Trademark Use*, 51 Les Nouvelles 266 (2016).

93. 2 Gilson on Trademarks § 6.04 (2020).

94. *Id.*; *see also* William M. Landes & Richard A. Posner, *Trademark Law: An Economic Perspective*, 30 J. L. & Econ. 265 (1987).

95. Eva's Bridal, Ltd. v. Halanick Enters., 639 F.3d 788, 790 (7th Cir. 2011).

96. *See*, *e.g.*, FreecycleSunnyvale v. Freecycle Network, 626 F.3d 509 (9th Cir. 2010).

live up to quality standards. According to a recent report from the Service Management Group, forty-two percent of 47,383 unique respondents have experienced an issue with an online food delivery services.[97] Inaccuracy, followed by freshness concerns, are the two most common complaints.[98] These concerns directly implicate the consumer's consistency and predictability expectations. And, more often than not, the consumer connects the poor experience with the restaurant instead of the delivery service.[99]

As of the date of this article, the authors are aware of no case law touching on policing an online food delivery service's unauthorized relationship of a franchisee's likeness (such as its store front). The primary driver of the franchisor's actions should be to protect the franchise system as a whole and avoid trademark abandonment. Additionally, given that the general trend in favor of finding for the franchisor,[100] the franchisee will likely need to rely on express contract language to force a franchisor to take action or to recover from damages incurred through the franchisor's inaction. This, of course, requires a case-by-case, contract-by-contract evaluation.

C. *Statutory Remedies*

Franchisees may find it difficult to protect their exclusive territory rights against delivery service-facilitated encroachment through lawsuits based on breach of contract or the implied covenant of good faith and fair dealing. State franchise relationship laws and other applicable state laws might provide an alternative avenue to a remedy. The Wisconsin Fair Dealership Law, for example, provides that a franchisor may not take an action which "substantially change[s] the competitive circumstances . . . without good cause."[101] If a franchisor were to implement a system-wide third-party online delivery service program that adversely affects a franchisee's profit margins, such action could be deemed a violation of the statute unless the franchisor could demonstrate good cause, a fact specific inquiry.

Likewise, the Indiana Franchise Act may provide relief for aggrieved franchisees.[102] It states that franchisees are protected from competition within a "reasonable area" of the franchisee's location. Notably, this right extends beyond the language of the franchise agreement.

Iowa goes a step further and provides a cause of action for monetary damages for a franchisee's lost sales on account of a franchisor developing a new

97. Serv. Mgmt. Grp., *Take Control of Third-party Delivery to Protect Your Brand*, 25 (3d ed.), https://www.smg.com/docs/default-source/default-document-library/Resources/smg_take-control-of-third-party-delivery-to-protect-your-brand (last visited Oct. 8, 2021).

98. *Id.*

99. *Id.*; Caroline B. Fichter et al., *Don't Tread on Me: A Defense of State Franchise Regulation*, 38 Franchise L.J. 23, 36 (2018).

100. Peter C. Lagarias & Robert S. Boulter, *The Modern Reality of the Controlling Franchisor: The Case for More, Not Less, Franchisee Protections*, 29 Franchise L.J. 139 (2010). *But see* William L. Killion, *The Modern Myth of the Vulnerable Franchisee: The Case for A More Balanced View of the Franchisor-Franchisee Relationship*, 28 Franchise L.J. 23 (2008).

101. Wis. Stat. § 135.03.

102. Ind. Code Ann. § 23-2-2.7-1.

"outlet or location which sells essentially the same goods or services under the same trademark, service mark, trade name, logotype, or other commercial symbol as an existing franchisee."[103] This cause of action is not available if any of the following are applicable: (1) the franchisor offered the new outlet or location to the existing franchisee on the same basic terms and conditions available to the other potential franchise; (2) the adverse impact is determined to have been less than five percent of gross sales during the first twelve months of operation of the new outlet or location; and (3) the existing franchisee is not in compliance with the franchisor's then reasonable criteria for eligibility for a new franchisee.[104] Other state franchise relationship laws, including those in Minnesota and Washington, might also provide a remedy in encroachment type matters.[105]

Various deceptive trade practices laws are another potential means of recourse for franchisees.[106] Every state has enacted a deceptive trade practices act meant to protect the public from predatory commercial behavior.[107] A franchisee, however, may run into standing or other threshold issues pursuing claims under these laws. For instance, it is an open question in Wisconsin law as to whether a non-party has standing under the Wisconsin Deceptive Trade Practices Act.[108] Without clear authority on this standing issue, a Wisconsin-based franchisee may be foreclosed from bringing such a claim against either a franchisor or a sister franchisee. Similarly, other states limit these causes of actions to consumers, not businesses. [109] As such, the strength of deceptive trade practice claims will be very state dependent.

Finally, as explained earlier, the recently enacted California Business and Professional Code §§ 22598–22599 requires food delivery services to receive a restaurant's express authorization in order to deliver from said restaurant. This statute provides:

> For purposes of this chapter, the following definitions shall apply:
>
> (a) "Food delivery platform" means an online business that acts as an intermediary between consumers and multiple food facilities to submit food orders

103. Iowa Code § 523H.6.

104. *Id.*

105. *See* Minn. R. § 2860.4400; Wash. Rev. Code §19.100.180(2)(F).

106. Dolman, *supra* note 34, at 5.

107. *Id.*; *see* Carolyn L. Carter, *Consumer Protection in the States: A 50-State Report on Unfair and Deceptive Acts and Practices Statutes*, Nat'l Consumer L. Ctr. (Feb. 2009), https://www.nclc.org/images/pdf/udap/report_50_states.pdf.

108. For several years, the Seventh Circuit assumed that only people defrauded by a false representation had standing to sue. *See In re* C2R Global Mfg., Inc., 617 B.R. 618, 624 (Bankr. E.D. Wis. 2020) ("Even though C2R and Verde have not offered, and the Court has not found, Wisconsin state case law directly addressing whether a competitor of defendant can be a plaintiff under sec. 100.18."). But, recently, the Wisconsin Court of Appeals differentiated these decisions. *See* Pagoudis v. Keidl, No. 2020AP225, 2021 WL 2945584, at *8 (Wis. Ct. App. July 14, 2021) (recommended for publication) (rejecting the notion that section 100.18 limits the ability of a party to bring a claim for a false or misleading representation made by the defendant to a third-party).

109. Dolman, *supra* note 34, at 6 (explaining that courts in some states have refused to recognize franchisees as consumers).

> from a consumer to a participating food facility, and to arrange for the delivery of the order from the food facility to the consumer.
>
> (b) "Food facility" means a food facility, as defined in Section 113789 of the Health and Safety Code.
>
> A food delivery platform shall not arrange for the delivery of an order from a food facility without first obtaining an agreement with the food facility expressly authorizing the food delivery platform to take orders and deliver meals prepared by the food facility.

Currently, no decisions interpret § 22599, but the plain language of the statute is clear. The definition for "food delivery platform" encompasses the above-mentioned aggregators and third-party logistics services. Further, the borrowed definition for food facility is broadly written, including any "operation that stores, prepares, packages, serves, vends, or otherwise provides food for human consumption at the retail level."[110] The law does not exclude franchised restaurants from its coverage or condition rights on ownership of trademark rights; accordingly, franchisees may sue for injunctive relief under § 22599. Although the statute does not provide a private right of action, a franchisee may have standing under California's unfair competition statute.[111]

With other state legislatures contemplating instituting similar measures, more franchisees might be able to avail themselves of protection against encroachment of their territories by online food delivery services, should such legislation be enacted. The authors also note that the evolution of the business model of third-party delivery services (perhaps altered somewhat by the threat of legal action for unauthorized delivery services and state regulation) might be what ultimately resolves the unauthorized delivery problem. In December 2020, the National Restaurant Association announced that it had reached agreement with several third-party delivery services, including Grubhub, DoorDash, UberEats and Postmates, on a set of "Public Policy Principles for Third-Party Delivery" to guide lawmakers in developing public policy for the industry.[112] Among these principles are the following:

- Restaurants have a right to know and determine when and if their food is delivered.
- Customers should expect the same degree of food safety from delivery as they do when dining in a restaurant.
- Sales tax collection responsibility must be clear in terms of which party is collecting and remitting the specific sales tax to the appropriate authority.

110. Cal. Health & Safety Code § 113789(a).

111. Korea Supply Co. v. Lockheed Martin Corp., 63 P.3d 937, 943 (Cal. 2003) (stating that Cal. Bus. & Prof. Code § 17200 "borrows violations from other laws by making them independently actionable as unfair competitive practices").

112. *Restaurants and Third-Party Delivery Companies Agree to Public Policy Principles*, Nat'l Rest. Ass'n (Dec. 16, 2020), https://restaurant.org/news/pressroom/press-releases/restaurants-and-delivery-companies-agree-to-policy.

- Third-party food delivery contracts need contractual transparency, and issues surrounding fees, costs, terms, policies, marketing practices involving the restaurant or its likeness, and insurance/indemnity should be clear.
- Restaurants deserve transparency on fees (including commissions, delivery fees, and promotional fees) charged by third-party delivery companies.[113]

III. Conclusion

Online food delivery services are here to stay. Franchisees face an uphill battle to prevent encroachment of their territory or to obtain a remedy when such encroachment occurs. Without legislative intervention or significant case-law developments favoring franchisees, these services may prove to be a serious threat to the exclusive territory provided to many brick-and-mortar franchise restaurants. Legislation like that enacted in California may prove helpful and expand protections beyond those provided under some state franchise relationship laws. Those franchisors who negotiate arrangements with online food delivery services, and then require franchisees to participate in the programs, grant permission to deliver food from their franchisees, and should be pushed to take actions protecting the reasonable expectations of their franchisees. It is also conceivable that high percentage commissions assessed by aggregators (and corresponding complaints from franchisees) will cause some franchisors to take exclusive control of online sale and delivery of their products by permitting online sales only through apps and websites controlled by the franchisor. Finally, market forces are likely to push third-party delivery and order solicitation services to work with restaurants in a more collaborative, mutually beneficial and transparent manner.

113. *Id.*

The Untold Story of the Concurrent Use Trademark Registration

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Usually buried in footnotes of textbooks and law review articles, the "concurrent use" trademark registration rarely is the topic of a thoughtful legal discussion among practitioners. Sure, it is in the Lanham Act, and yes, there might be more Bigfoot sightings than the number of concurrent use registrations.[1] However, are they plausible options for trademark owners? This article unveils that mystery and tells the untold story of the concurrent use registration.

To set the stage, consider the following hypothetical. For decades, a family has owned and operated the local MARCA's restaurant, which has developed a loyal following in its town. Tired of the weekly grind of running the restaurant, the parents want to step back and let their children take over the business. Although the children hope to carry on the MARCA's name in honor of their parents' blood, sweat, and tears in running the business, they lack interest in running the restaurant day-to-day and instead suggest franchising.

This proposal sounds like a great plan until the family discovers *another* MARCA's restaurant 2,000 miles away, operating on the other side of the country. Yes, the marks for each restaurant are identical. And yes, the marks both identify restaurants. However, neither the family nor the owners of the other MARCA's restaurant have federally registered the MARCA's mark in connection with restaurant services. The family now wonders whether it

1. To better understand the rarity of concurrent use registrations, see Barton Beebe & Jeanne C. Fromer, *Are We Running Out of Trademarks? An Empirical Study of Trademark Depletion and Congestion*, 131 Harv. L. Rev. 945 (2018) (explaining that, of the 5.9 million federal trademark applications for the Principal Register at the United States Patent and Trademark Office (USPTO) between 1985 and 2014, 604 applications resulted in concurrent use registrations). According to one website, there are that many Bigfoot sightings in Washington state alone. *See* Trevor Wheelwright, *States with the Most Bigfoot Sightings*, SatelliteInternet.com (July 20, 2020), https://www.satelliteinternet.com/resources/states-with-the-most-bigfoot-sightings.

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even has a trademark or whether it can register the MARCA's mark now that it knows of the other restaurant. The family not only questions whether franchising is still an option, but it also questions whether it can continue using the MARCA's name for its own restaurant.

Unfortunately for this hypothetical family, the actual answers—like all things in the law—will depend on many factors. This article strives to unpack these questions and concerns.

I. The Basics of Trademarks and Why to Register Them

A trademark is a word, name, design, symbol, slogan, sound, or smell (or some combination thereof) that (1) *identifies* a single source of certain goods or services; and (2) *distinguishes* those goods and services from others.[2] Trademarks in the United States are created from *use* of a mark in connection with specific goods and services. This reality—that use creates trademark rights—means that trademarks can exist even if not registered at the state or federal level. Without a federal registration, however, the trademark owner's rights are limited to the area where the trademark has been used and, depending on the case law, where the trademark owner's "zone of natural expansion" extends.[3]

When a trademark's "use" (or its intended use) comprises "use in commerce" falling within Congress's power under the Commerce Clause,[4] the trademark owner can apply to register the mark with the United States Patent and Trademark Office (USPTO) to protect its mark throughout the entirety of the United States.[5] The registration gives the trademark owner priority over others who adopt a confusingly similar mark after the application filing date, even if they are in other parts of the country where the trademark owner has not yet "used" the mark. Registrations are still subject to anyone else's common-law trademark rights that existed before the application filing date.[6]

In the context of franchising, franchisors should register their marks with the USPTO for several reasons. These reasons include that the franchisor (1) will increase its ability to expand use of the mark across the country; (2) will strengthen its enforcement capabilities against infringing third parties and holdover franchisees; (3) can mitigate the risk of its, and its franchisees', infringement of other parties' marks; (4) can take advantage of exemptions

2. 15 U.S.C. § 1127.

3. *See* 5 McCarthy on Trademarks and Unfair Competition § 26:20 (5th ed. 2017).

4. Larry Harmon Pictures Corp. v. Williams Rest. Corp., 929 F.2d 662, 664 (Fed. Cir. 1991) (citing U.S. Const. art. I, § 8).

5. The three forms of "commerce" captured by the Commerce Clause are (1) interstate commerce; (2) territorial commerce (i.e., commerce with a U.S. territory, such as Guam, Puerto Rico, American Samoa, or the U.S. Virgin Islands); or (3) commerce between the United States and a foreign country. *See, e.g.*, U.S. Patent & Trademark Office, U.S. Dep't of Commerce, Trademark Manual of Examining Procedure § 901.03 [hereinafter TMEP].

6. *See* 5 McCarthy on Trademarks and Unfair Competition, *supra* note 3, § 16:18.50.

from certain state business opportunity laws;[7] and (5) can avoid the need to include certain statutory language in Item 13 of the Franchise Disclosure Document (FDD), as required by the Federal Trade Commission's Franchise Rule.[8] In addition, and although not specific to franchisors, a federal registration will require the USPTO to block subsequent applications for confusingly similar marks, which further deters parties from using infringing marks. Just having a registration—which is easily locatable through the search function on the USPTO's website[9]—gives notice to others and may stop similar applications from even being filed.

Furthermore, trademarks registered on the USPTO's Principal Register receive certain benefits, such as the presumptions of validity, ownership, and exclusivity to the mark, along with the possibility of the mark becoming incontestable.[10] Registration on the Principal Register also helps with certain online enforcement activities, such as on the Amazon® Brand Registry,[11] and also with enforcement by U.S. Customs.[12] As is well known and reiterated in the franchise world, franchisors consistently point to their principal registered trademark or service mark as one of their most valuable assets.

Federal trademark registrations are aimed to grant exclusivity throughout the country to one owner of a particular mark for use with designated goods and services. Congress, however, also created a mechanism that affords multiple users of the same mark in completely separate geographic areas the chance of each obtaining a federal registration.[13] As a result, a "middle ground" took shape in the form of concurrent use trademark registrations granted to more than one owner.

7. Franchisors who offer franchises pursuant to a franchise disclosure document (FDD) that complies with the Federal Trade Commission's Franchise Rule will not be subject to a majority of state business opportunity laws; however, if a franchisor federally registers its trademark or service mark, the business opportunity laws of the following states may also be exempt: Connecticut (Conn. Gen. Stat. Ann. § 36b-61), Georgia (Ga. Code Ann. § 10-1-410), Louisiana (La. Stat. Ann. § 51:1821), Maine (Me. Rev. Stat. tit. 32, § 4691), North Carolina (N.C. Gen. Stat. Ann. § 66-94), and South Carolina (S.C. Code Ann. § 39-57-20).

8. 16. C.F.R. § 436.5 (providing that, if the franchisor's trademark is not registered on the Principal Register of the USPTO, the FDD must include the following statement in Item 13: "We do not have a federal registration for our principal trademark. Therefore, our trademark does not have many legal benefits and rights as a federally registered trademark. If our right to use the trademark is challenged, you may have to change to an alternative trademark, which may increase your expenses.").

9. *See* United States Patent and Trademark Office, Trademark Electronic Search System, https://www.uspto.gov/trademarks/search [hereinafter TESS].

10. 15 U.S.C. §§ 1057(b), 1065, 1115(a), 1115(b).

11. Amazon has launched a service called the Amazon Brand Registry (https://brandservices.amazon.com/), which allows trademark owners to "register" their marks with Amazon to help mitigate infringing uses in Amazon's marketplace.

12. TMEP, *supra* note 5, § 801.02(a); *see also* U.S. Customs & Border Protection, *How to Obtain Border Enforcement of Trademarks and Copyrights*, https://iprr.cbp.gov (last visited Oct. 25, 2021).

13. *See* 15 U.S.C. §1052(d).

II. Procedural Aspects of Concurrent Use Trademark Registrations

15 U.S.C. §1052(d) codifies the USPTO's power to grant concurrent registrations for similar marks that are not likely to confuse the public, and it states:

> [I]f the [USPTO] Director determines that confusion, mistake, or deception is not likely to result from the continued use by more than one person of the same or similar marks under conditions and limitations as to the mode or place of use of the marks or the goods on or in connection with which such marks are used, concurrent registrations may be issued to such persons when they have become entitled to use such marks as to a result of their concurrent lawful use in commerce prior to (1) the earliest of the filing dates of the applications pending or of any registration issued under this chapter. . . .

The United States Trademark Trial and Appeal Board (TTAB) has since taken steps to set the standard for granting concurrent use registrations.[14] Under the TTAB's standard, two conditions precedent must exist: (1) the parties must be entitled to concurrent lawful use of the marks in commerce, and (2) there must be no likelihood of confusion, mistake, or deception in the marketplace as to the source of the goods or services resulting from the marks' concurrent use.[15] In practice, three primary routes lead to a concurrent use registration: (a) if the applicant raises the issue in an application; (b) if the issue arises in opposition or cancellation proceedings before the TTAB; or (c) when a court determines that more than one person is entitled to use the same or similar marks in commerce.[16]

For the first route, an applicant believing it is entitled to a concurrent use registration can raise the issue in its own trademark application with the USPTO. To do so, the applicant should provide (a) the geographic area, the goods or services, and the mode of use with respect to its desired registration; and (b) to applicant's knowledge, the details of others' concurrent lawful use, including the names and addresses of each, whether the others own any relevant applications or registrations, and where, and for how long, the others have used their marks.[17] These other users are the "excepted users."[18] The applicant could include the concurrent use request in the initial application or could amend an unrestricted application to one seeking a concurrent use registration.[19]

Unless the applicant relies on a court or TTAB decision, or on the consent of the other party holding a registration, the applicant must show that its "date of first use in commerce is before the filing date of the pending applications or of any registrations issued under the Trademark Act of

14. America's Best Franchising, Inc. v. Abbott, 2013 WL 3168104, at *8 (T.T.A.B. 2013).

15. *Id.* at *8 (citing *In re* Beatrice Foods Co., 429 F.2d 466, 473–74 (C.C.P.A. 1970)).

16. *See* U.S. Patent & Trademark Office, U.S. Dep't of Commerce, Trademark Trial and Appeal Board Manual of Procedure § 1102.02 (citing 15 U.S.C. § 1052(d)) [hereinafter TBMP].

17. *Id.* § 1102.02; *see also* TMEP, *supra* note 5, § 1207.04.

18. TMEP, *supra* note 5, § 1207.

19. *Id.* § 1207.04(b).

1946."[20] This includes the filing date of any federal application that may be filed by any excepted users.[21]

If the basic requirements for a concurrent use application are met and there are no other issues with the application, it is published for opposition with a qualifier that the bounds of any concurrent use remain subject to review. If no opposition is filed, or if any opposition that is filed is dismissed or withdrawn, the TTAB will institute the concurrent use proceeding and determine such available concurrent use rights.[22]

Applicants cannot rely on an intent-to-use filing basis under 15 U.S.C. § 1051(b) (a "Section 1(b) filing") or a foreign asset filing basis under 15 U.S.C. § 1126 (a "Section 44" filing) or 15 U.S.C. § 1141f(a) (a "Section 66(a)" filing) for concurrent use proceedings.[23] Only applicants that allege actual use under 15 U.S.C. § 1051(a) may proceed. This approach makes sense, because the applicant seeks a concurrent *use* registration, so it must already use the mark. In addition, applications for registration on the Supplemental Register cannot mature into concurrent use registrations.[24]

A second route to a concurrent use registration comes in opposition and cancellation proceedings among disputing trademark owners.[25] An opposition occurs where a third party opposes an applicant's registration on the Principal Register during the publication period in the USPTO's *Official Gazette*.[26] While similar to an opposition, a cancellation occurs after the mark has been federally registered, where a third party seeks to cancel the registration.[27] In both situations, the third party must claim that it believes it will be "damaged" by the registration.[28] If concurrent use issues arise in these cases, the opposition or cancellation proceeding is not converted into a concurrent use proceeding *per se*, but, rather, the instituted opposition or cancellation proceeding is terminated and a subsequent concurrent use proceeding is immediately instituted thereafter.[29]

The USPTO's *Trademark Manual of Examining Procedure* (TMEP) sets forth four common examples of concurrent use issues arising in opposition

20. *Id*. § 1207.04(c).

21. *Id*.

22. *Id*. § 1207.04(e)(1).

23. *Id*. § 1103.01(a); *see also* TBMP, *supra* note 16, § 1105.

24. TBMP, *supra* note 16, § 1105. The Supplemental Register is a secondary register that allows marks to become federally registered that have not yet proven their distinctiveness from other sources in the marketplace. *See* 15 U.S.C. §§ 1091–1096. For example, an applicant who applies for an otherwise descriptive mark on the Principal Register will often amend the application to be registered on the Supplemental Register until the applicant can prove that its mark has distinctively identified the applicant's goods or services from competitors. Often, and depending on the mark, the USPTO will accept five years of continuous use of the mark as *prima facie* evidence that the mark has acquired the necessary distinctiveness to be worthy of the Principal Register. *See* 15 U.S.C. § 1052(f).

25. TMEP, *supra* note 5, § 1113.01.

26. TBMP, *supra* note 16, § 301.01.

27. *Id.*

28. *Id.*

29. *Id*. § 1113.01–1113.02.

proceedings: (1) a specified party in the applicant's concurrent use application opposes the application;[30] (2) an unspecified party opposes the applicant's concurrent use application and files a concurrent use application in parallel, naming the applicant's use as an exception;[31] (3) an unspecified party opposes the applicant's concurrent use application, but does not file a concurrent use application, whereby the applicant amends its application to exclude the opposing party's use;[32] and (4) a party opposes the applicant's *unrestricted* application (i.e., not a concurrent use application) and the applicant moves to amend its application to a concurrent use application.[33]

Where concurrent use issues arise in cancellation proceedings, typically the third party files a concurrent use application and also petitions to cancel an existing registration in parallel, upon which the TTAB may defer to the concurrent use proceeding and terminate the cancellation proceeding.[34] However, if the cancellation proceeding is not terminated, and a decision in the cancellation proceeding is adverse to the respondent, the respondent may still be able to file a new application seeking a concurrent registration with the petitioner.[35] That said, a registrant may not file a request under 15 U.S.C. § 1057(e) (a "Section 7(e)" filing) to amend the territoriality of the existing registration, whether a cancellation proceeding has been filed or not.[36] Additionally, even "incontestable" registrations are subject to concurrent use registration proceedings.[37]

Through all these examples, the core factual disputes typically involve (1) whether a senior user only used its mark in one geographical area, while a junior user used the mark in a different one, such that there was no meaningful likelihood of confusion among the public; and (2) in which parts of the country each party is entitled to a registration. In some cases, the junior user may even receive a much larger territory than the senior user if the senior user has, "through its failure to expand over a long period of time," abandoned its right to use the mark throughout the entire United States.[38]

30. See *id.* § 1113.01 (explaining that an applicant who admits that it is not entitled to an unrestricted registration warrants a concurrent use proceeding rather than an opposition proceeding).

31. See *id.* § 1113.01 (explaining that the TTAB will suspend the opposition until the opposer's concurrent use application is published and there are no oppositions).

32. *Id.* § 1113.01.

33. *See id.* (providing that if the opposer consents to the amendment, the opposition will be dismissed without prejudice, and the concurrent use proceeding will be instituted).

34. *Id.* § 1113.02.

35. *Id.*

36. *Id.* § 1114.

37. *Id.* § 1105 (providing, however, that "any registration issued to the concurrent use applicant against the owner of an incontestable registration will be limited (even if applicant is the prior user) to applicant's area of actual use prior to actual or constructive notice of registrant's rights, unless the parties stipulate otherwise.").

38. *See id.* § 1103.01(d)(2).

A third route to concurrent use registrations is a judicial decision that "more than one person is entitled to use the same or similar marks in commerce."[39]

Regardless of the route, either the TTAB or a court will have to decide whether both parties are entitled to registration and whether consumers are unlikely to be confused, mistaken, or deceived as to the source of the goods or services resulting from the continued concurrent use of the marks. The case law, discussed in the next section, contains a number of important decisions that have fleshed out the law surrounding concurrent use applications and registrations.

III. The Relevant Case Law

A. *The Foundation: The* Weiner King *Case*

One of the foundational cases discussing concurrent use is *Weiner King, Inc. v. Wiener King Corp.* from the U.S. Court of Customs and Patent Appeals, a predecessor to the Federal Circuit.[40] The case has a detailed factual and procedural history, but provides a great discussion of basic concepts of concurrent use rights and is routinely cited by subsequent concurrent use cases.[41]

The "original" Weiner King began using its mark in 1962 for a restaurant in Flemington, New Jersey.[42] It opened additional restaurants in Flemington and had other locations in New Jersey.[43] However, it did not apply to register its trademark until 1975.[44]

Unaware of the "original" Weiner King, a different restaurant in North Carolina began using its own Wiener King mark in 1970.[45] That junior user, "Wiener King North Carolina" or "WKNC" (as the court labeled it), obtained three federal trademark registrations without opposition covering the WIENER KING marks.[46] By 1972, WKNC had eleven company-owned restaurants in operation using the marks.[47] After WKNC learned about the "senior" Weiner King, it nonetheless continued expanding and began offering franchises.[48] By 1975, WKNC's system had more than one hundred facilities in twenty states that were either open, under construction, or under site development.[49]

WKNC filed applications to register additional WIENER KING marks, later seeking to amend those applications to carve out certain counties in

39. *See id.* § 1102.02.
40. Weiner King, Inc. v. Wiener King Corp., 615 F.2d 512 (C.C.P.A. 1980).
41. *Id.* at 514–19.
42. *Id.* at 515.
43. *Id.*
44. *Id.*
45. *Id.*
46. *Id.* at 516.
47. *Id.*
48. *Id.*
49. *Id.*

New Jersey where the "original" Weiner King was located.[50] Soon thereafter, the "original" Weiner King petitioned to cancel WKNC's existing registrations, filed its own territorially unrestricted applications, and sued WKNC in the U.S. District Court for the District of New Jersey.[51] The USPTO declared concurrent use proceedings between the parties before the TTAB, which consolidated and stayed all the proceedings pending the outcome of the federal court litigation.[52]

The result of the civil litigation was to grant the "original" Weiner King an injunction against WKNC, but only in the areas of the "original" Weiner King's use.[53] The remaining issues concerning registration and concurrent use were left for the TTAB to decide.[54]

The TTAB then granted the "original" Weiner King's petitions to cancel to the extent that WKNC's registrations were restricted to exclude the "original" Weiner King's trading area in New Jersey (as determined by the TTAB).[55] The TTAB also granted WKNC's new applications, subject to an amendment restricting them to exclude that same "original" Weiner King's trading area.[56] In short, the TTAB determined that the application of the "original" Weiner King, although the senior user, was limited to its trading area in New Jersey.[57]

On appeal, the Court of Customs and Patent Appeals (in the role now held by the Federal Circuit) affirmed most of the TTAB's decision.[58] The court observed that, even though the "original" Weiner King was the "first to adopt and use its mark," WKNC "innocently adopt[ed] its mark . . . in a market area remote from that of [the 'original'] Weiner King's market area. Under such circumstances, it is settled law that each party has a right to use its mark in its own initial area of use."[59]

The court explained how trademark cases are based on equity, and equity, like nature, "abhors a vacuum."[60] In such a situation, the TTAB had the "task of balancing the equities between a prior user who remained content to operate a small, locally oriented business with no apparent desire to expand, and who, until recently, declined to seek the benefits of Lanham Act registration, and a subsequent user, whose expressed purpose has been, from its inception, to expand into a nationwide franchising operation, and who has fulfilled that purpose, taking advantage of registration under the Lanham Act in the process."[61] Also, notably, the court further explained that it was

50. *Id.*
51. *Id.*
52. *Id.*
53. *Id.* at 516–17.
54. *Id.* at 517.
55. *Id.* at 519.
56. *Id.*
57. *Id.*
58. *Id.* at 521–26.
59. *Id.* at 522.
60. *Id.*
61. *Id.*

not bad faith, under the specific facts of the case, for WKNC to expand after learning of the "original" Weiner King's trademarks, as "mere knowledge of the existence of the prior user should not, by itself, constitute bad faith."[62]

Against this backdrop, the court set out certain criteria relevant to "who gets what territory," explaining that "actual use in a territory was not necessary to establish rights in that territory."[63] The inquiry should focus on the following for each party:

(1) previous business activity;

(2) previous expansion or lack thereof;

(3) dominance of contiguous areas;

(4) presently planned expansion; and, where applicable,

(5) possible market penetration by means of products brought in from other areas.[64]

The court also emphasized that WKNC was the first to seek registration and confirmed that "there is a policy of encouraging prompt registration of marks by rewarding those who first seek registration under the Lanham Act."[65] The court also looked to the purpose of the Lanham Act, which is to prevent consumer confusion.[66] Considering this purpose, the court referred to the TTAB's finding that, outside of the "original" Weiner King's "little enclave," the Wiener King brand was identified with WKNC, which had expanded considerably to many other states.[67] Giving the "original" Weiner King rights beyond its "enclave" would risk creating confusion with WKNC, which is what the Lanham Act was intended to prevent.[68] The court did conclude that the "original" Weiner King had shown rights to its zones of reputation and natural expansion in portions of New Jersey, but otherwise found in favor of WKNC as to the rest of the United States, even though WKNC was the junior user.[69]

Weiner King may be an older case, but it lays out many important principles about concurrent use. It also describes a situation in which, depending on the equities, the junior user may end up with greater geographic rights than the senior user, which is significant.

62. *Id*. Additionally, in a footnote, the court further explained that "[w]hile it is clear that appropriation of a mark with knowledge that it is being used by another is not in good faith, it does not follow that a later user who has adopted in good faith must forego any further expansion after learning of the prior user." *Id*. at 522 n.6.

63. *Id*. at 523 (citing *In re* Beatrice Foods, 429 F.2d 466, 475 (C.C.P.A. 1970)).

64. Weiner King, Inc. v. Wiener King Corp., 615 F.2d 512, 523 (C.C.P.A. 1980).

65. *Id*.

66. *Id*. at 524.

67. *Id*.

68. *Id*.

69. *Id*. at 524–26.

B. *Taking* Weiner King *to Modern Media:* The Copy Club *and* Tribolite *Cases*

In 2006, in *CDS, Inc. v. I.C.E.D. Management, Inc.*, the TTAB relied on *Weiner King* in a concurrent use case involving THE COPY CLUB mark for use in connection with various document copying, processing, and publishing services.[70]

There, the junior user, CDS, filed a concurrent use application for THE COPY CLUB to cover the states of Utah, New Jersey, New York, Connecticut, Pennsylvania, Kansas, and Missouri.[71] The senior user, I.C.E.D. Management, Inc. (ICED), owned an unrestricted federal registration for COPY CLUB.[72] Nevertheless, and despite having a first use date in 1992, ICED did not apply for its registration until 2004.[73] In the meantime, CDS began using its mark in 1993, outside of ICED's area, satisfying the TTAB's requirement for jurisdiction in a concurrent use proceeding (i.e., the junior user began lawful use of its mark outside of the senior user's area before that senior user's application for registration).[74] ICED (the senior user) had not used its mark in any of the seven states that CDS claimed in its concurrent use application, and, by the time of the proceedings before the TTAB, CDS had stopped any use in areas overlapping with those of ICED.[75]

In its decision, the TTAB explained the general rule that ICED, "as the registrant and prior user is entitled to a registration covering the entire United States, including areas of its use and non-use, subject only to the exception of geographic areas where the junior user can prove prior use. The junior user is, in effect, frozen in its area of prior use."[76] However, and referring to *Weiner King*, the TTAB clarified that "the area of 'prior use' includes more than areas of actual use," because "actual use in a territory was not necessary to establish rights in that territory."[77] Analyzing the evidence in light of the five factors set forth in *Weiner King*, the TTAB concluded that CDS had not established its use in the states of Utah, New Jersey, New York, Connecticut, and Pennsylvania, but had established use across Kansas and parts of Missouri.[78]

However, the TTAB then considered the likelihood of confusion between the marks if the parties received registrations for these respective territories: Kansas and part of Missouri for CDS, and the rest of the United States for

70. CDS, Inc. v. I.C.E.D. Mgmt., Inc., 2006 WL 1968616 (T.T.A.B. 2006).
71. *Id.* at *1. CDS initially asked to include Texas and California, but later dropped those states. *Id.* at *1 n.2.
72. *Id.* at *1–2.
73. *Id.* at *3, *8.
74. *Id.* at *8.
75. *Id.* at *8–9.
76. *Id.* at *9 (quoting Enter. Rent-A-Car Co. v. Advantage Rent-A-Car, Inc., 330 F.3d 1333 (Fed. Cir. 2003)).
77. CDS, Inc. v. I.C.E.D. Mgmt., Inc., 2006 WL 1968616, at *9 (T.T.A.B. 2006) (quoting Weiner King, Inc. v. Wiener King Corp., 615 F.2d 512,523 (C.C.P.A. 1980)).
78. *CDS, Inc.*, 2006 WL 1968616, at *11.

ICED.[79] Both parties advertised on the Internet, and ICED believed that this fact could still lead to confusion.[80] The TTAB commented that it did not believe "that the creation of the Internet has rendered the concurrent use provision of the Trademark Act moot" and referred to pre-Internet cases in which marks could be used in different territories, even if advertising and customer solicitation occurred in overlapping areas.[81] The TTAB also noted a disclaimer on CDS's website explaining that it only did business in the seven states claimed in its application, states in which ICED had not done business.[82]

Based on the full record, the TTAB concluded that concurrent use registrations could issue, with CDS (the junior user) having rights in Kansas and parts of Missouri, and ICED (the senior user) having rights in the rest of the United States.[83]

Almost eight years later, the TTAB decided *Turdin v. Trilobite, Ltd.*, in which it relied on the principles set out in *Weiner King* to determine that concurrent use registrations were inappropriate for the mark TRILOBITE for use with audiovisual recording and production services, even in areas where the parties' actual use did not overlap.[84]

The senior user of the TRILOBITE mark was Trilobite, Ltd., formed in 1982 in Michigan.[85] It had used the TRILOBITE mark for videos regarding sporting events and news stories, fictional works, and animations, and had worked with companies that produced content for cable television shows, such as Food Network, "DIY," and "HDTV."[86] Based on its use, Trilobite Ltd. filed geographically unrestricted applications to register TRILOBITE in 2009.[87]

The junior user, Peter Turdin, started using TRILOBITE PICTURES in January 2000 in Connecticut.[88] He claimed to use the mark in the fictional film and media industry, including directing films, writing scripts, editing films, and film animation.[89] He sought a concurrent use registration giving him rights in Connecticut and New York City.[90]

Although Trilobite, the senior user, had not performed any work in or received any orders from Connecticut, it claimed its "products" had appeared in Connecticut and been consumed by customers there.[91] It also claimed to have "a lot" of clients in New York City, including NBC, ABC, CBS, and Fox.[92]

79. *Id*. at *12.
80. *Id*.
81. *Id*.
82. *Id*. at *13.
83. *Id*. at *15.
84. Turdin v. Trilobite, Ltd., 2014 WL 343270 (T.T.A.B. 2014).
85. *Id.* at *3.
86. *Id.*
87. *Id.* at *1 nn.2–3.
88. *Id.* at *3.
89. *Id.*
90. *Id.* at *2.
91. *Id.* at *3.
92. *Id.*

The TTAB determined that Turdin met the threshold requirement for a concurrent use proceeding because he had begun lawful use of his mark before the filing of Trilobite's application.[93] The TTAB then concluded that Trilobite had used its mark in various locations, including New York City, but not Connecticut, while Turdin had used his mark in Connecticut and New York City.[94] Therefore, there was territorial overlap in New York City, but not in Connecticut.[95]

After establishing the territories of use, the TTAB then discussed the likelihood of confusion if the parties used their marks in their respective territories.[96] The TTAB determined that there would be likely confusion in New York, especially given the overlapping territory.[97] As to Connecticut, Trilobite (the senior user) had no evidence of any previous business activity or planned expansion there, but the senior user testified about an overlap of people who live in Connecticut and work in New York, where it did use the TRILOBITE mark.[98] Under these facts, the TTAB felt that Turdin, the junior user, had not carried his burden and refused the concurrent use registration.[99]

The TTAB had noted the "well established" rule that, "where the trading territories of concurrent users overlap in actual use, that fact precludes the granting of concurrent use registrations."[100] Here, even though the territories of actual use did not completely overlap, and even though the junior user had used the mark in a distinct geographical area before the senior user's application to register, the TTAB found the junior user not entitled to a concurrent use registration at all.

C. *Concurrent Use in the Franchise World: The* America's Best Franchising *Case*

In 2013, the franchise legal community witnessed a practical example of concurrent use proceedings in action in *America's Best Franchising, Inc. v. Abbott*.[101] In that case, America's Best Franchising, Inc. (ABF), a franchisor of several hotel brands, filed three intent-to-use applications to register the 3 PALMS mark (and certain designs), initially without any geographic limitations.[102] Roger Abbott (Abbott), who owned a hotel through his "related company" that was also using a 3 PALMS mark in Scottsdale, Arizona, opposed ABF's applications based on his prior use of that mark.[103] In response to the oppositions, ABF moved to amend its applications to cover the entire United States

93. *Id.* at *5.
94. *Id.* at *5–9.
95. *Id.* at *9.
96. *Id.* at *9–13.
97. *Id.* at *12.
98. *Id.*
99. *Id.* at *13.
100. *Id.* at *5.
101. America's Best Franchising, Inc. v. Abbott, 2013 WL 3168104 (T.T.A.B. 2013).
102. *Id.* at *1.
103. *Id.* at *1 n.2, *3.

except the state of Arizona and conceded Abbott's prior use of the mark in Arizona.[104] The TTAB then instituted the concurrent use proceeding in light of ABF's amendment.[105]

Abbott argued that ABF was not entitled to concurrent use registration of the 3 PALMS mark, because, although Abbott only used the mark in connection with a Scottsdale hotel, "the Internet marketing, advertising and promotion of hotels by necessity has expanded [Abbott's] territory nationwide or to something significantly greater than the state of Arizona."[106] Further, Abbott claimed that approximately fifty percent of his hotel's customers came from outside of Arizona and "100 percent of [its] business [came] from online marketing."[107]

Citing to *Weiner King* and *CDS*, the TTAB held that the first condition precedent was met, because "ABF adopted its marks in good faith, in its own geographic area of Central Florida, and without knowledge of Abbott's prior use of 3 PALMS."[108] Additionally, the TTAB concluded that ABF began using the mark before the date that Abbott filed his own geographically unrestricted application.[109] However, the next step in the analysis led the TTAB to review what *registerable* rights the parties were entitled to receive.[110] The TTAB, quoting a Court of Customs and Patent Appeals decision, stated:

> We have concluded that in concurrent use proceedings in which neither party owns a registration for the mark, the starting point for any determination as to the extent to which the registrations are to be territorially restricted should be the conclusion that the prior user is prima facie entitled to a registration covering the entire United States. Such a prior user, who applies for a registration before registration is granted to another party, is entitled to a registration having nationwide effect no less than if there were no concurrent user having registrable rights. His rights and, therefore, his registration, should be limited only to the extent that any other subsequent user, who can establish the existence of rights earlier than the prior user's application for registration, can also prove a likelihood of confusion, mistake or deception.[111]

The TTAB then analyzed whether confusion was likely.[112] It found the services were identical and the literal elements of the marks were in part identical.[113] Although "consumers may very well be confused if the parties' marks were used in the same geographic area," that question was not before the TTAB.[114] The question, instead, was "whether a likelihood of confusion would be avoided by a geographic restriction."[115]

104. *Id.* at *1.
105. *Id.*
106. *Id.*
107. *Id.* at *4–5.
108. *Id.* at *9.
109. *Id.*
110. *Id.* at *10.
111. *Id.* (quoting *In re* Beatrice Foods, 429 F.2d 466, 474 (C.C.P.A. 1970)).
112. *Id.* at *10–11.
113. *Id.*
114. *Id.* at *11.
115. *Id.*

The TTAB held that, so long as the geographic restriction was appropriate, confusion was unlikely for several reasons.[116] First, many marks incorporating the term PALM identified hotel services across the Internet and other marketing channels and could co-exist on the Principal Register, proving Abbott's mark to be quite weak, which "significantly minimize[d] the likelihood of consumer confusion."[117] "Second, and perhaps more importantly, a geographic restriction would make confusion unlikely, especially where purchasers have been conditioned, when faced with hotel marks containing the terms PALM or PALMS, or designs comprised of palm trees, to consider other factors when choosing a hotel."[118] Consumers may see advertisements online for certain hotels, but the services that such mark owners provide are aligned with specific locations.[119] The mere "fact that both parties' services are promoted and offered online is not enough to result in a likelihood of confusion."[120] Lastly, despite certain overlap on the Internet for approximately four years, it did not purport to result in actual consumer confusion, and the TTAB held that to be "at least somewhat relevant."[121]

Having found confusion unlikely, the TTAB set out to define the parties' respective territories.[122] Citing to *Weiner King*, the TTAB explained that ABF should be rewarded with the greater territory, as it was the first party to file for registration and was actively expanding, while Abbott's use of the 3 PALMS mark had remained static in Scottsdale, Arizona.[123] As a result, the TTAB awarded ABF the entire United States except the state of Arizona, which remained with Abbott.[124]

IV. Practical Takeaways After Understanding the Landscape

Trademark cases are necessarily fact-dependent and not susceptible to bright-line rules. That said, these cases allow for a few observations.

Parties can have concurrent rights and can be entitled to concurrent use registrations. This reality means that junior users may have an option to seek such rights rather than re-branding their concept, so long as the junior party began lawful use of its mark in its own area before the senior user's application and if the parties' concurrent uses are unlikely to cause confusion. As in *Weiner King* and *America's Best Franchising*, the equities may favor a junior

116. *Id*.
117. *Id*. (citing, among other authority, King Candy Co. v. Eunice King's Kitchen, Inc., 496 F.2d 1400, 1401 (C.C.P.A. 1974)).
118. *Id.* at *12.
119. *Id.* ("Hotel services are by definition rendered in a particular geographic location, even if they are also offered, by the same ultimate source, in other geographic locations under the same mark. In fact, a hotel's physical location is among its most salient features. . . .")
120. *Id.* at *14.
121. *Id*. at *15.
122. *Id.* at *15–17.
123. *Id.* at *17.
124. *Id.* at *18.

user who applies first to register and has shown a more diligent effort to expand use nationwide, essentially "flipping the script" and giving greater territorial rights to the junior user, even if "actual use" has not occurred in all of the requested territory.

However, practitioners should know that the parties' goods and services, and the proximity of their respective territories will play a critical role. Sometimes, as in *CDS*, the parties' territories may be physically separate such that confusion is unlikely, even if consumers in both territories are exposed to both parties' advertising over the Internet.[125] In other cases, however, as in *Trilobite*, a junior user can start lawful use in its own territory, but may be so close to the senior user's territory that confusion is still likely, at least to the point that the junior party cannot show its entitlement to a concurrent use registration.

For franchisors (and potential franchisors), the cases provide another reminder of the benefits of seeking federal registration early in the process. Concurrent use issues can be messy, but could usually be avoided if the senior user had applied to register prior to the junior user's adoption of the mark. After all, for the TTAB to have jurisdiction to consider a concurrent use proceeding, the junior user must have begun lawful use of its mark outside of the senior user's area *before* that senior user's application for registration.[126] That said, the franchisor (or potential franchisor) may not always be the senior user. If that is the case, all may not be lost if the franchisor can still meet the concurrent use registration requirements. The franchisor, even if a junior user, may still be able to obtain the benefits of a federal registration, albeit one that is limited geographically.

V. What About the Family-Owned MARCA's Restaurant?

Returning to the hypothetical family looking to franchise the MARCA's restaurant, the family will need to understand the timing and scope of how and when the other MARCA's restaurant started using the mark, and whether the other MARCA's has registered, or filed an application to register, the mark with the USPTO. These datapoints will help the family determine the bounds and potential coverage of its MARCA's mark and its exclusivity, if any. Even if the other MARCA's started using the mark first, the family may not be out of luck if the other MARCA's has not applied to register the mark—or applied after the family started its use—and as long as the parties' territories are distinct so that confusion is unlikely. The family could consider filing a concurrent use application, listing the "other" MARCA's as an

125. For a more detailed analysis regarding the Internet's impact on the co-existence of marks, see Matthew Bender & Company, Inc., *Proving Ownership Online . . . And Keeping It: The Internet's Impact on Trademark Use and Coexistence* (2014), https://www.brinksgilson.com/files/gilson_on_trademarks_article_2014.pdf.

126. *See*, *e.g.*, CDS, Inc. v. I.C.E.D. Mgmt., Inc., 2006 WL 1968616, at *8 (T.T.A.B. 2006).

excepted user in a specific location, which, of course, can be tailored according to the facts and in the best light reasonably possible for the family. Then, the process can take its course; the family may ultimately still obtain a federal registration, at least for part of the country, and it may set the stage for a larger negotiation with the other MARCA's about trademark and franchise rights. Concurrent use trademark registrations, therefore, may still provide a way forward, even for junior trademark users.

Goodwill Hunting: The Challenges in Proving Harm to Franchisor Goodwill in Termination-Related Disputes

*Jeffrey H. Wolf & Amy Heiserman**

Mr. Wolf

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Trust is a crucial element of relationship building: "*Trust is the glue of life. It's the most essential ingredient in effective communication. It's the foundational principle that holds all relationships*."[1] Without trust in a relationship, leaders micromanage subordinates, spouses monitor each other, and faith in others is generally all but lost. In the context of business, trust is a fundamental precept that fosters growth and development. As a franchisor's business gains success, it typically considers expansion by opening more company-owned locations, selling franchises, or a combination of both. Deciding to utilize the franchise business model requires the franchisor to trust the franchisees to represent the brand well in the marketplace, particularly in a market that the franchisor might not yet have captured. To do so, the franchisor allows outsiders access to its "secret sauce," including its trademarks, brand, systems, manuals, processes, products, and other proprietary information.[2]

There is always a risk that franchisees will either fail to perform or otherwise not comply with system requirements, leading to the termination of the franchise relationship. From the franchisor's perspective, an all-important and immediate consideration when a terminated franchisee seeks to compete unfairly—either through the unauthorized use of the franchisor's trademarks or in violation of a restrictive

1. Stephen R. Covey (@StephenRCovey), Twitter (May 18, 2019, 9:01 AM), https://twitter.com/StephenRCovey/status/1129748909088235521 (emphasis added).

2. Keller Corp. v. Kelley, 187 P.3d 1133, 1138 (Colo. App. 2008) ("[T]he primary characteristic of a franchise is the license given to the franchisee to trade upon and exploit the franchisor's goodwill.").

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covenant—is to take the steps needed to protect its customer goodwill. This is no small or simple task, and, frequently, swift legal action is required. Should the matter reach litigation, injury to, or diversion of, goodwill is a primary component of damage for which a franchisor may seek compensation. But how is an intangible property right such as goodwill protected, proven, or quantified? This article will discuss, and to some extent evaluate, two very distinct questions of harm to franchisor goodwill given the current state of the law: (1) harm in trademark infringement cases; and (2) harm in non-trademark infringement cases. They are both related, but one is much easier to prove no matter the jurisdiction. As this article demonstrates, the clear takeaway is that franchisors must be prepared to come with specific evidence of harm to ensure that they can obtain redress for either trademark infringement or the breach of post-termination restrictive covenants.

I. Defining Franchisor Goodwill

The definition of *business-related goodwill* has taken different forms, from "that element of value which inheres in the fixed and favorable consideration of customers, arising from an established and well-known and well-conducted business"[3] and "probability that customers will continue their patronage"[4] to "a company's positive reputation in the eyes of its customers and potential customers" that "is generated by repeat business with existing customers . . . or referrals to potential customers."[5] In 1993, the U.S. Supreme Court endorsed the shorthand description of goodwill as "the expectancy of continued patronage."[6] That definition did not assist taxpayers in evaluating which of its intangible assets are subject to a depreciation allowance, so the U.S. Court of Claims in *Richard S. Miller & Sons, Inc. v. United States* elaborated on the definition:

> The term "goodwill" has a varying content, depending on its usage. Goodwill sometimes is used to describe the aggregate of all of the intangibles of a business, including such items as patents, trademarks, leases, contracts, and franchises. Since a normal rate of return usually is calculated on tangible assets only, goodwill has been used as a synonym for the return on all the intangibles of a business. In a more restricted sense, goodwill is the expectancy that the old customers will resort to the old place. It is the sum total of all the imponderable qualities that attract customers and bring patronage to the business without contractual compulsion. Another definition equates goodwill with a rate of return on investment which is above normal returns in the industry and limits it to the residual intangible asset that generates earnings in excess of a normal return on all other tangible and intangible assets.[7]

3. Des Moines Gas Co. v. Des Moines, 238 U.S. 153, 165 (1915).
4. *Goodwill*, Black's Law Dictionary (6th ed. 1990).
5. N. Am. Expositions Co. v. Corcoran, 898 N.E.2d 831, 846 (Mass. 2009).
6. Newark Morning Ledger Co. v. United States, 507 U.S. 546, 555 (1993) (citing Boe v. Comm'r, 307 F.2d 339, 343 (9th Cir. 1962)).
7. Richard S. Miller & Sons, Inc. v. United States, 537 F.2d 446, 450–54 (Ct. Cl. 1968).

Courts have formulated narrower definitions in the context of franchise law by focusing on how trademarks generate a franchisor's goodwill through "association with the franchisor and serv[ing] as a symbol of brand recognition,"[8] and noting that it is "goodwill for the [franchisor's] mark, not the specific [franchise]."[9] Legal lexica such as *Black's Law Dictionary* similarly recognize the interaction between goodwill and trademarks: "Because an established business's trademark or servicemark is a symbol of goodwill, trademark infringement is a form of theft of goodwill. By the same token, when a trademark is assigned, the goodwill that it carries is also assigned."[10] *Merriam-Webster* also recognizes that goodwill is favor garnered through a company's "brands and its good reputation."[11]

State legislatures also struggle to define goodwill, at least in any sort of uniform fashion. For example, California[12] and North Dakota[13] have adopted and codified definitions of goodwill that focus on client patronage, although North Dakota excludes from goodwill a right to use the name of any person from whom it was acquired.[14] Although the precise legal definition somewhat varies by source, the consensus is that goodwill reflects the intangibles of a business that make customers want to come back.[15] While injury to goodwill and reputation is a recoverable form of damage, it is "difficult to measure in dollars and cents."[16]

II. Proof of Harm to Goodwill Is Not Always Straightforward or Easy

A. *The Need for Injunctive Relief to Prevent Irreparable Harm*

When a business chooses franchising as a method of growth, it relies heavily on the goodwill of its brand to drive consumer traffic.[17] Although owned

8. Desert Subway, Inc. v. City of Tempe, 322 F. Supp. 2d 1036, 1041 (D. Ariz. 2003).

9. Pappan Enters., Inc. v. Hardee's Food Sys., Inc., 143 F.3d 800, 806 (3d Cir. 1998).

10. *Goodwill*, Black's Law Dictionary (11th ed. 2019); *see also id.* (defining *goodwill* as "[a] business's reputation, patronage, and other intangible assets that are considered when appraising the business, esp. for purchase; the ability to earn income in excess of the income that would be expected from the business viewed as a mere collection of assets").

11. *Goodwill*, Merriam-Webster Dictionary, https://www.merriam-webster.com/dictionary/goodwill (last visited Jan. 30, 2021).

12. Cal. Bus. & Prof. Code § 14100.

13. N.D. Cent. Code § 47-07-10.

14. *Id.*

15. Spicer v. Maxus Healthcare Partners, LLC, 616 S.W.3d 59, 111 (Tex. Ct. App. 2020) ("Business goodwill is an intangible asset based on reputation and the relationships that a company has developed with its customers and employees."); Walsh v. Walsh, 286 P.3d 1095, 1099 (Ariz. Ct. App. 2012) ("[R]eferred to as the most intangible of intangibles, goodwill is essentially reputation that will probably generate future business." (quoting Dugan v. Dugan, 457 A.2d 1, 3 (N.J. 1983))); Gaskill v. Robbins, 282 S.W.3d 306, 314 (Ky. 2009) ("Goodwill in a professional practice may be attributable to the business enterprise itself by virtue of its existing arrangements with suppliers, customers or others, and its anticipated future customer base due to factors attributable to the business." (quoting May v. May, 589 S.E.2d 536, 545 (W. Va. 2003)).

16. 5 J. Thomas McCarthy, McCarthy on Trademarks and Unfair Competition § 30:47 (4th ed. 1996).

17. Get in Shape Franchise, Inc. v. TFL Fishers, LLC, 167 F. Supp. 3d 173, 202–03 (D. Mass. 2016) (Customer goodwill is "a company's positive reputation in the eyes of its customers or

and operated by separate and distinct individuals or entities, the franchisees are, as a matter of course, required to operate their stores in a uniform manner to create brand consistency.[18] This consistency is achieved through the franchisee's implementation of the required practices and protocols of the franchised concept.[19] The franchisees receive access to manuals, systems, trademarks, and other confidential and proprietary information that combine to create a brand or brand image that is easily recognizable in the minds of consumers.[20]

If properly drafted, the franchise agreement will contain provisions designed to create strict guidelines by which the franchisee is authorized to use the system, including a license to utilize federal-registered trademarks and other intellectual property.[21] The franchise agreement typically also obligates the franchisees to maintain the confidentiality of certain types of sensitive business information, abide by in-term and post-termination restrictive covenants, and comply with other provisions that protect the franchisor from competition upon termination of the franchise relationship.[22] The underlying rationale for these protective measures is to ensure that the terminated franchisee does not damage or impermissibly use the franchisor's marks and proprietary information in a way that devalues them or brings a negative association to the franchisor's business.[23]

It is, of course, common for franchise relationships to end before their expiration, either voluntarily or involuntarily, which is the point at which franchisors must focus on the protection of its most valuable assets: its brand value and goodwill. This focus is also true when franchise agreements reach

potential customers" and "is generated by repeat business with existing customers or by referrals to potential customers.'" (quoting N. Am. Expositions Co. Ltd. P'Ship v. Corcoran, 898 N.E.2d 831, 846 (Mass. 2009)).

18. Int'l Franchise Ass'n Inc. v. City of Seattle, 97 F. Supp. 3d 1256, 1264 (W.D. Wash. 2015) ("Most franchise agreements heavily regulate the conduct of the franchisee and include statements about how the franchisee is expected to run the franchise, whether or not the franchisee has an exclusive territory, and when and where the franchisee may open another business. Franchise agreements also contain clauses that outline acceptable outlet 'appearance, hours of operation, location, and product quality' and typically allow franchisors to conduct 'inspections, audits, mystery shopper programs, and so on' of the franchisees.").

19. *Id.*

20. Anytime Fitness, LLC v. Edinburgh Fitness, Civil No. 14–348 (DWF/JJG), 2014 WL 1415081, at *1 (D. Minn. 2014) ("When a franchisee joins the AF system, it has access to [trademarks, trade names, service marks, logos, designs, commercial symbols], marketing and advertising systems, training programs, confidential proprietary materials, and other materials to assist in operating the fitness centers."); *see also* Jason M. Murray & Michael R. Gray, *The Enforcement of Covenants Against Competition*, ABA 28th Annual Forum on Franchising L6, at 1, 3–11 (2005) (identifying cases that have found that a franchisor's method and style of doing business, as well as the goodwill associated therewith, are legitimate business interests).

21. *See* TGI Friday's Inc. v. Great Nw. Rests., Inc., 652 F. Supp. 2d 763, 766 (N.D. Tex. 2009).

22. *See* 7-Eleven, Inc. v. Kapoor Bros. Inc., 977 F. Supp. 2d 1211, 1228–29 (M.D. Fla. 2013).

23. *Id.* at 1228 (franchisor arguing that restrictive covenants are reasonably necessary to protect its trademarks and goodwill; prevent franchisees' unauthorized use of confidential business information such as business operations manuals, specialized training material, associated advertising and sales material; and preserve and protect important customer relationships that associate franchisor's trademarks with franchisees).

their natural maturity. Whether the parting of ways is amicable and the parties are working together to disentangle themselves, or contentious as a result of a dispute requiring legal action, franchisors must take care to ensure that the goodwill of the business is adequately protected. Franchisors frequently must sue terminated franchisees for trademark infringement, unfair competition, breach of contract, and other causes of action if the franchisee continues to use the franchisor's trademarks or attempts to appropriate the business's goodwill. To prevent irreparable harm to its business, the franchisor often seeks a preliminary injunction, which requires proving a likelihood of success on the claims asserted.[24]

Injunctive relief is designed to prevent or stop irreparable harm from occurring by restraining the defendant's wrongful conduct. Under the Lanham Act,[25] an aggrieved party must establish that it owns a valid, protectable trademark, and that the offending party's use of the mark is likely to cause confusion among customers.[26] To obtain injunctive relief in federal court, the party bringing the lawsuit must establish (1) a likelihood of success on the merits; (2) likelihood of irreparable harm; (3) that the balance of the equities weighs in favor of granting the injunction; and (4) that an injunction is in the public interest.[27] State courts and arbitration panels do not always apply federal procedural requirements when injunctive relief is sought, so if there is a contractual obligation to arbitrate or the venue is state court, the franchisor should determine the applicable injunctive relief standard that will be applied under the governing state laws or arbitration rules.

1. The Presumption of Harm in Trademark Infringement Cases

Regarding the element of irreparable harm, or as sometimes styled, the absence of an adequate legal remedy, the most logical justification for a judicial restraint is the protection of brand or customer goodwill.[28] When seeking injunctive relief on a trademark infringement claim, there is a split in the case law regarding the quantum of proof required to demonstrate irreparable harm.[29] In some jurisdictions, courts presume harm to goodwill;[30] in others, the franchisor must show actual harm caused by the alleged

24. *See, e.g.*, Winter v. Natural Res. Def. Council, Inc., 555 U.S. 7, 20–21 (2008); *see also Kapoor Bros.*, 977 F. Supp. 2d at 1228–29; *TGI Friday's, Inc.*, 652 F. Supp. 2d at 767–68.

25. 15 U.S.C. § 1125(a).

26. Brookfield Commc'ns, Inc. v. W. Coast Entm't Corp., 174 F.3d 1036, 1047 (9th Cir. 1999).

27. *Winter*, 555 U.S. at 20.

28. *Id.* (outlining four-part test for motions for preliminary injunctive relief, one of which is that the plaintiff is likely to suffer irreparable harm in the absence of preliminary relief); *see also* Doran v. Salem Inn, Inc., 422 U.S. 922, 931 (1975) (explaining that the "traditional standard for granting a preliminary injunction requires the plaintiff to show that in the absence of its issuance he will suffer irreparable injury"); Stanley v. Univ. of S. Cal., 13 F.3d 1313, 1320 (9th Cir. 1994) (quoting Beacon Theaters, Inc. v. Westover, 359 U.S. 500, 506–07 n.8 (1959)) ("The basis of injunctive relief in the federal courts has always been irreparable harm and inadequacy of legal remedies.").

29. *Compare infra* Section II.1, *with infra* Section II.2.

30. Merck Eprova AG v. Gnosis S.p.A. 760 F.3d 247, 260 (2d Cir. 2014); N. Am. Med. Corp. v. Axiom Worldwide, Inc., 522 F.3d 1211, 1228 (11th Cir. 2008).

infringement, even if the franchisor has established a likelihood of confusion.[31] It is paramount to a party's success, in either prosecuting or defending an action, to know exactly what to prove and how courts evaluate whether such proof has been or can be shown.

The U.S. Supreme Court addressed the notion that irreparable harm should be presumed upon a showing of likelihood of confusion in *eBay v. MarcExchange, LLC*.[32] There, the Court considered whether the traditional four-factor test applied by courts of equity when considering whether to award permanent injunctive relief applies to disputes arising under the Patent Act.[33] At the district court level, MercExchange filed a patent infringement suit against eBay and Half.com.[34] The jury found that MercExchange's patent was valid, eBay and Half.com had infringed that patent, and an award of damages was appropriate.[35] After the verdict, MercExchange filed a motion for permanent injunction, which the district court denied.[36] The Federal Circuit reversed, applying the general rule that courts will issue permanent injunctions against patent infringement absent exceptional circumstances.[37]

The U.S. Supreme Court on appeal held that "the decision whether to grant or deny injunctive relief rests within the equitable discretion of the district courts, and that such discretion must be exercised consistent with traditional principles of equity, in patent disputes no less than in other cases governed by such standards."[38] The Court then explained that neither the district court nor the Federal Circuit fairly applied the traditional four-factor test for injunctive relief because both inappropriately applied categorical rules to the grant or denial of injunctive relief.[39] Although *eBay* did not expressly hold that irreparable harm should not be presumed, the Court's ruling called into question such a presumption by indicating that each factor should be evaluated in its own right.[40]

2. The Third and Ninth Circuits Require Proof of Harm to Goodwill

The Eleventh Circuit became the first court to evaluate whether *eBay* applied in trademark infringement cases by questioning whether a finding of likelihood of confusion was sufficient to establish irreparable harm.[41] There, the court vacated a preliminary injunction and noted that "[a]lthough *eBay* dealt with the Patent Act and with permanent injunctive relief, a strong case can be made that *eBay*'s holding necessarily extends to the grant of preliminary injunctions under the Lanham Act" because the language of the Lanham Act

31. *N. Am. Med. Corp.*, 522 F.3d at 1228.
32. eBay, Inc. v. MercExchange, LLC, 547 U.S. 388 (2006).
33. *Id.* at 391.
34. *Id.* at 390.
35. *Id.* at 390–91.
36. *Id.* at 391.
37. *Id.*
38. *Id.* at 394.
39. *Id.*
40. See *id.* at 393–94.
41. N. Am. Med. Corp. v. Axiom Worldwide, Inc., 522 F.3d 1211 (11th Cir. 2008).

"is so similar to the language of the Patent Act . . . ."[42] But the Eleventh Circuit did not go so far as to hold that *eBay* applied and instead remanded the issue for consideration by the district court. This decision laid the path for other courts to begin questioning whether and to what extent *eBay* applied to trademark cases.

The Ninth Circuit became the first federal circuit to reject the majority view of presuming irreparable harm once a likelihood of confusion is established.[43] The Third Circuit later joined the Ninth Circuit.[44] The Ninth and Third Circuits therefore extended the U.S. Supreme Court's rationale to trademark infringement claims.[45] Much like the Patent Act at issue in *eBay*, the injunctive relief provision of the Lanham Act is premised upon traditional principles of equity.[46] Moreover, the language of the Lanham Act makes clear that the legislature did not intend "a major departure from the long tradition of equity practice."[47] Under this rationale, because presuming irreparable harm deviates from the application of traditional principles of equity, no presumption of harm can be afforded to parties seeking injunctive relief in Lanham Act.[48]

3. The First, Fifth, and Tenth Circuits Have Doubts About a Presuming Harm

The First, Fifth, and Tenth Circuits have expressed reservations about the continuing validity of the irreparable harm presumption following *eBay*, but have declined to apply *eBay* in the trademark infringement context.[49] Lower

42. *Id.* at 1228.

43. Herb Reed Enters., LLC v. Fla. Entm't Mgmt., Inc., 736 F.3d 1239, 1250–51 (9th Cir. 2013) (holding that irreparable harm is not presumed after a showing of likelihood of confusion; those seeking injunctive relief must proffer evidence establishing the likelihood of irreparable harm).

44. Ferring Pharms., Inc. v. Watson Pharms., Inc., 765 F.3d 205, 211–16 (3d Cir. 2014) (finding that, in light of *eBay* and *Winter*, no presumption of irreparable harm is afforded to parties seeking injunctive relief in Lanham Act cases). *But see* Commodores Entm't v. McClary, 648 F. App'x 771, 774 (11th Cir. 2016) (finding that, in light of *eBay*, "a presumption of irreparable harm cannot survive," but noting that the holding in *eBay* permits a plaintiff to prove irreparable harm using the same evidence the plaintiff proffered to support a showing of a likelihood of success on the merits).

45. *Ferring*, 765 F.3d at 214; *Herb Reed Enters.*, 736 F.3d at 1250–51.

46. *Ferring*, 765 F.3d at 214 (quoting 15 U.S.C. § 1116(a) ("The several courts vested with jurisdiction of civil actions arising under this chapter shall have power to grant injunctions, according to the principles of equity and upon such terms as the court may deem reasonable. . . .").

47. *Id.* at 215.

48. *Id.* at 216.

49. Peoples Fed. Sav. Bank v. People's United Bank, 672 F.3d 1, 9 (1st Cir. 2012) (noting that a "looming question" exists as to whether the longstanding presumption of irreparable harm can co-exist with *eBay*, but declining to determine whether *eBay* precludes the presumption); Paulsson Geophysical Servs., Inc. v. Sigmar, 529 F.3d 303, 312 (5th Cir. 2008) (explaining that it has avoided "expressly adopting" the presumption of irreparable injury, but declining to decide whether a court may presume irreparable injury upon a finding of likelihood of confusion in a trademark case because it was a "difficult question" in light of *eBay*); Lorillard Tobacco Co. v. Engida, 213 F. App'x 654, 656–57 (10th Cir. 2007) (explaining that the Tenth Circuit has frequently presumed irreparable injury when a trademark is wrongfully appropriated, and declining to consider whether *eBay* applies in the trademark infringement context).

courts within these and other jurisdictions are also beginning to question the presumption.[50] Indeed, prior to *eBay*, most circuit courts, including the Second, Fourth, Sixth, Seventh, and Eighth Circuits, presumed irreparable harm if the plaintiff was able to prove a likelihood of confusion.[51] But the *eBay* decision has called the continuing authority or viability of these cases into question as well, leaving lower federal courts unsure as to what the correct approach is in trademark cases.[52]

4. Congress Amended the Lanham Act in 2020 to Clarify That Irreparable Harm Is Presumed

There were really only two ways to achieve clarity on whether or not there is a presumption of harm in trademark infringement cases: a ruling by the Supreme Court or action by Congress. The latter occurred first when President Trump signed the Trademark Modernization Act of 2020 (TMA) into law on December 27, 2020.[53] Included as part of Congress's COVID-19 relief package, the TMA made it easier for trademark registrants to obtain injunctive relief by restoring the presumption of irreparable harm when a trademark is infringed. In particular, Congress amended Section 34(a) of the Lanham Act by adding a rebuttable presumption of irreparable harm upon a

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50. *E.g.*, Pub. Impact, LLC v. Boston Consulting Grp., 169 F. Supp. 3d 278, 298 (D. Mass. 2016) (stating that the First Circuit has generally presumed harm in the trademark litigation context if a plaintiff demonstrates likelihood of success on the merits, but noting that whether the presumption still applies in light of *eBay* is an open question); NYP Holdings v. N.Y. Post Publ'g Inc., 63 F. Supp. 3d 328, 341 (S.D.N.Y. 2014) (finding that in light of *eBay*, irreparable harm is no longer presumed, but noting that the Second Circuit has not addressed whether *eBay* applies to preliminary injunctions in trademark infringement suits).

51. Scotts Co. v. United Indus. Corp., 315 F.3d 264, 273 (4th Cir. 2002) ("In Lanham Act cases involving trademark infringement, a presumption of irreparable injury is generally applied once the plaintiff has demonstrated a likelihood of confusion."); Fed. Express Corp. v. Fed. Espresso, Inc., 201 F.3d 168, 174 (2d Cir. 2000) ("[P]roof of a likelihood of confusion would create a presumption of irreparable harm."); Eli Lilly & Co. v. Nat. Answers, Inc., 233 F.3d 456, 469 (7th Cir. 2000) (noting that irreparable harm is generally presumed in trademark cases); Wynn Oil Co. v. Am. Way Serv. Corp., 943 F.2d 595, 608 (6th Cir. 1991) (stating that irreparable injury "ordinarily follows" when a likelihood of confusion is demonstrated and determining that it therefore did not need to make specific finding if irreparable harm); Mut. of Omaha Ins. Co. v. Novak, 836 F. 397, 403 n.11 (8th Cir. 1987) ("Injury is presumed once a likelihood of confusion has been established.").

52. Ronald T. Coleman Jr., Trishanda L. Treadwell & Elizabeth A. Loyd, *Applicability of the Presumption of Irreparable Harm After Ebay*, 32 Franchise L.J. 3, 5–7 (2012); Scott McIntosh & Jonathan Labukas, *To Presume, or Not to Presume, Irreparable Injury in Trademark Disputes Involving Franchises Following Ebay and Winter*, 36 Franchise L.J. 43, 61–68 (2016); Jeffrey M. Sanchez, *The Irreparably Harmed Presumption? Why the Presumption of Irreparable Harm in Trademark Law Will Survive Ebay and Winter*, 2011 BYU L. Rev. 535, 545–53 (2011); David H. Bernstein & Andrew Gilden, *No Trolls Barred: Trademark Injunctions After Ebay*, 99 Trademark Rep. 1037, 1045 (2009).

53. Pub. L. 116-260, § 226, 134 Stat. 2208 (2020) ("Section 34 of the Trademark Act of 1946 (15 U.S.C. 1116) is amended in subsection (a) by inserting after the first sentence the following new sentence: 'A plaintiff seeking any such injunction shall be entitled to a rebuttable presumption of irreparable harm upon a finding of a violation identified in this subsection in the case of a motion for a permanent injunction or upon a finding of likelihood of success on the merits for a violation identified in this subsection in the case of a motion for a preliminary injunction or temporary restraining order.'").

finding of infringement, or of likely success on the merits in the context of injunctive relief.[54]

Only two courts appear to have discussed the TMA in the context of a motion for preliminary injunction.[55] In *Vineyard House, LLC v. Constellation Brands U.S. Operations, Inc.*, the U.S. District Court for the Northern District of California held that the insertion of the irreparable harm language added via the TMA "only reinforces the appropriateness of a permanent injunction requested by [the trademark registrant]."[56] The U.S. District Court for the District of Oregon held in *Suzie's Brewery Co. v. Anheuser-Busch Cos.* that because the plaintiff had "shown a likelihood of success of the merits on its motion for a temporary restraining order . . . Plaintiff is entitled to the benefit of the rebuttable presumption provided in § 1116(a)."[57] It is significant that district courts within the Ninth Circuit, a circuit that was the first to reject the presumption of harm under *eBay*, are now applying this presumption in light of the TMA. These decisions demonstrate that the TMA was an important step toward uniformity in how courts evaluate requests for injunctive relief in trademark infringement cases.

5. Presumption of Harm to Goodwill Is Important in Trademark Infringement Cases

It makes perfect sense that Congress would build a presumption of harm into the Lanham Act for purposes of seeking injunctive relief. This conclusion is especially true in the context of a franchise relationship, where trademarks serve an outsized purpose and trademark infringement often comes into play. If a terminated franchisee continues using the franchisor's trademark, or one that is confusingly similar, the consuming public is likely to affiliate the terminated franchisee with the franchisor's business or concept even though the two are no longer associated and the franchisors is no longer providing any oversight over the quality, actions, and/or performance of the franchisee. Customers could become confused and attribute the poor service, quality, or misdeeds of the terminated franchisee to the franchisor.[58]

For example, assume that a franchise agreement for a "Buffy Burger" franchise has terminated, but the franchisee continues to display exterior or interior signage bearing the franchisor's marks for several weeks or months while the former franchisee transitions under a new business name. During that time, the former franchisee does not follow the franchise protocols and procedures to ensure the cleanliness of its restaurant. Customers complain

54. 15 U.S.C. § 1116(a).

55. Vineyard House, LLC v. Constellation Brands U.S. Ops., Inc., 515 F. Supp. 3d 1061, 1079 n.16 (N.D. Cal. Jan. 26, 2021); Suzie's Brewery Co. v. Anheuser-Busch Cos., LLC, 519 F. Supp. 3d 839, 851 (D. Or. Feb. 9, 2021).

56. *Vineyard House, LLC*, 515 F. Supp. 3d at 1081 n.16.

57. *Suzie's Brewery*, 519 F. Supp. 3d at 855.

58. Ledo Pizza Sys. Inc. v. Singh, 983 F. Supp. 2d 632, 637 (D. Md. 2013) (use of franchisor's décor, floor plan, and recipes after termination of franchise agreement caused customer confusion).

that the store has bugs, trash on the tables, and dirty bathrooms. It is not far-fetched, and indeed is likely, that a customer's experience at the rogue Buffy Burger will inform his or her view of other Buffy Burger stores. Further assume that other franchise owners comply with the quality assurance requirements of the Buffy Burger system and, therefore, do not have these same issues. Having a negative experience at one franchised location can result in a domino effect on other franchised locations and, ultimately, harm the overall Buffy Burger brand.

Many courts have thus presumed that, at the preliminary injunction stage, a likelihood of confusion from the infringement of a party's trademark amounts to irreparable harm. In the context of franchise law, the irreparable harm element of injunctive relief typically equates to harm to goodwill.[59]

If irreparable harm is not presumed, the franchisor must hunt for specific examples of how its goodwill is likely to be harmed by infringing conduct of a terminated franchisee.[60] A shift in customer perception of the business through negative reviews can serve as evidence of an impact on goodwill.[61] So can the testimony of confused customers (if a party can find them and convince them to testify). But that kind of hard evidence is not always easy to locate, especially on the compressed timetable that accompanies a motion for preliminary injunction. Without a presumption, generalities and assumptions likely will not suffice for a court to issue a preliminary injunction, especially if the alleged harm is speculative or not tied to specific actions of the franchisee or examples of potential damage to the brand.[62]

59. Get in Shape Franchise, Inc. v. TFL Fishers, LLC, 167 F. Supp. 3d 173, 202–03 (D. Mass. 2016) (concluding that irreparable harm was shown because "[t]he existence of a competing, small-group, women's fitness studio at the location of the former [franchisee's] studio will likely harm [the franchisor's] goodwill and impair its ability to establish another studio"); Buffalo Wild Wings Int'l, Inc. v. Grand Canyon Equity Partners, LLC, 829 F. Supp. 2d 836, 846 (D. Minn. 2011) (finding the potential loss of goodwill qualifies as irreparable harm because "a former franchisee's continued use of a franchisor's marks after termination of the franchise agreement poses a substantial risk to the franchisor's brand reputation and goodwill"); TGI Friday's Inc. v. Great Nw. Rests., Inc., 652 F. Supp. 2d 763, 771 (N.D. Tex. 2009) ("TGIF has shown that, through defendants' continued passing off of their restaurants as TGIF franchises after the termination of the franchise agreements, TGIF has lost control over its valuable trademarks and the quality of the restaurants operating under its name. This lost control poses a substantial threat of injury to TGIF's reputation and the goodwill it has built in its brand. Such injury is irreparable. . . ."); Desert Subway, Inc. v. City of Tempe, 322 F. Supp. 2d 1036, 1041 (D. Ariz. 2003) (finding irreparable harm to franchisor demonstrated by loss of goodwill).

60. *See*, *e.g.*, Jiffy Lube Int'l, Inc. v. Weiss Bros., Inc., 834 F. Supp. 683, 691–93 (D.N.J. 1993).

61. *See*, *e.g.* Life Alert Emergency Response, Inc. v. LifeWatch, Inc., 601 F. App'x 469, 474 (9th Cir. 2015) (finding that "numerous and persistent complaints from would-be customers" online constituted harm to reputation and goodwill); Home Comfort Heating & Air Conditioning, Inc. v. Ken Starr, Inc., 2018 WL 3816745, at *9 (C.D. Cal. July 24, 2018) (considering "negative online review and customer complaints . . . intended for Defendant" in analyzing irreparable harm).

62. *See*, *e.g.*, Gen. Motors LLC v. KAR Auto Grp. of Decorah, Inc., 2020 WL 4937119, at *2–3 (N.D. Iowa Aug. 24, 2020) (finding assumptions based on "experience," "belief[s]" and "hypotheticals that have no factual basis in the record" insufficient to show irreparable harm to goodwill).

Some courts view franchisees as having built up their own goodwill in their business. Because of the intangible nature of goodwill, it can be an arduous task for a court to evaluate whether the goodwill derives from the overall brand of the business versus the effort put in by the individual franchisee to build a positive reputation in the local community. This local goodwill can be accomplished in a variety of ways, such as providing top-quality customer service, supporting local non-profit organizations, or sponsoring community sports teams. The franchisee may also have his or her own specific style of leadership and training that sets that particular location apart from the rest. So when the franchise relationship terminates, franchisees many times argue that their personal efforts garnered the goodwill of the business and that goodwill does not belong to the franchisor.[63] This very fact-driven analysis leaves room for inconsistency by courts, so it is important for franchisors to differentiate between goodwill of the brand and goodwill of the specific franchise location.[64]

B. *Proving Actual Harm to Goodwill in the Context of Enforcing Post-Termination Restrictive Covenants*

Unlike in trademark infringement cases, disputes over the enforcement of post-termination contractual restrictions, such as covenants against competition, require the franchisor to demonstrate, both preliminarily and ultimately at trial, actual harm to its goodwill, thereby justifying the need for injunctive relief.[65] This proof may be accomplished through a showing that the former franchisee is engaged in competitive activities within its former franchise territory or otherwise is engaged in activity designed to divert customers.[66] Courts have acknowledged the difficulty of proving the value of

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63. Michael J. Boxerman & William K. Whitner, *Recent Trends in Litigating Non-Compete Agreements*, ABA 32nd Annual Forum on Franchising W22, at 1, 22 (2009); *see also* Robert W. Emerson, *Franchise Contract Clauses and the Franchisor's Duty of Care Towards its Franchisees*, 72 N.C. L. Rev. 905, 968 (1994) (discussing, generally, that former franchisees may argue that they have an ownership interest in the brand's goodwill based on expending time, energy, and funds to create customer relationships).

64. *See, e.g.*, LaGuardia Assocs. v. Holiday Hosp. Franchising, Inc., 92 F. Supp. 2d 119, 125 (E.D.N.Y. 2000) (explaining that the "hallmark" of a franchise relationship is an exchange of goodwill between the parties, where the franchisor lends its national goodwill to the franchisee who generates the local goodwill).

65. *See* Get in Shape Franchise, Inc. v. TFL Fishers, LLC, 167 F. Supp. 3d 173, 202–03 (D. Mass. 2016) (finding violation of non-competition agreement likely to harm goodwill because "one purpose of a non-compete clause in a franchise agreement is to protect the franchisor's goodwill"); MarbleLife, Inc. v. Stone Res., Inc., 759 F. Supp. 2d 552, 562–63 (E.D. Penn. 2010) (finding irreparable harm because ex-franchisee's breach of covenant not to compete harmed franchisor's goodwill).

66. *See, e.g.*, Soft Pretzel Franchise Sys., Inc. v. Taralli, Inc., 2013 WL 5525015, at *11 (E.D. Pa. Oct. 4, 2013) (irreparable harm shown by potential for customer confusion and damage to goodwill as a result of operating in former franchise territory); Outdoor Lighting Persps. Franchising, Inc. v. OLP-Pittsburgh, Inc., 2012 WL 1313251, at *4 (W.D.N.C. Apr. 17, 2012) (franchisor will suffer irreparable harm to goodwill if former franchisee is not enjoined from operating in former franchise territory).

goodwill.[67] Because there is not necessarily a presumption of harm to goodwill in non-infringement, unfair competition cases, courts usually require the aggrieved party to put forth some evidence of at least probable harm to goodwill.[68]

1. Non-Compete Provisions Protect the Franchise System

Because harm to goodwill can be not only difficult to prove but also detrimental to a business, franchisors can attempt to protect themselves by including post-termination restrictive covenants in their franchise agreements. By prohibiting a competing business for a reasonable period of time in a certain geographic location, the franchisor helps ensure that its goodwill will not be improperly traded upon by a former franchise and eliminates the uncertainty inherent in evaluating harm to goodwill calculation. This proactive measure is intended to prevent franchisees from misappropriating the franchisor's business assets, either during the franchise term or following its conclusion. Courts regularly acknowledge that properly tailored restrictive covenants are enforceable to prevent a former franchisee from using the franchisor's trademarks and other confidential and proprietary information.[69] To balance this consideration with public policy concerns, courts require restrictive covenants to be reasonable in time, geographic scope, and the extent of covered activities.[70] In other words, these clauses should not, and as a practical matter cannot, result in an unreasonable restraint of trade. This public policy means that the restraint cannot unreasonably limit competition or restrict the franchisee in the exercise of a gainful occupation.[71] Some states, however, go farther and prohibit restrictive covenants as a matter of course and view them as unreasonable restraints on trade in any circumstance. Thus, franchisors must be aware of whether states where franchises are located permit contractual non-compete clauses and should tailor their franchise agreements accordingly.

Sometimes franchisees deliberately ignore an enforceable covenant and continue or open a competing business. In those circumstances, the court

67. Sw. Stainless, LP v. Sappington, 582 F.3d 1176, 1192 (10th Cir. 2009) ("[I]t is so difficult to prove the value of goodwill.").

68. *See* Purugganan v. AFC Franchising, LLC, 2020 WL 6946558, at *5 (D. Conn. Nov. 25, 2020) (declining to grant injunctive relief because harm to goodwill from operating in former franchise territory was "entirely speculative"); Anago Franchising, Inc. v. CHMI, Inc., 2009 WL 5176548, at *12 (S.D. Fla. Dec. 21, 2009) (declining to grant injunctive relief because franchisor provided "no evidence" of harm to goodwill through business operations in the former franchise territory).

69. Jiffy Lube Int'l, Inc. v. Weiss Bros., Inc., 834 F. Supp. 683, 691 (D.N.J. 1993) (non-compete clause in franchise agreements "is necessary to protect the goodwill" of the franchisor); O.V. Mktg. Assocs., Inc. v. Carter, 766 F. Supp. 960, 966 (D. Kan. 1991) ("Courts have recognized certain interests attendant to a franchise that are protectable by restrictive covenants, such as good will, trade secrets, or the ability to secure a new franchise in the territory.").

70. *See, e.g.*, Soft Pretzel Franchise Sys., Inc. v. Taralli, Inc., 2013 WL 5525015, at *11 (E.D. Pa. Oct. 4, 2013) (covenant not to compete must be "reasonably limited in both time and territory" (quoting Piercing Pagoda, Inc. v. Hoffner, 351 A.2d 207, 210 (Pa. 1976)).

71. Restatement (Second) of Contracts § 186 (1981).

will examine whether a tangible harm to the franchisor's goodwill has or will occur by evaluating a variety of factors.

2. Factors Courts Consider in Determining Harm to Goodwill

There is no "standard" or pre-set list of factors that courts evaluate, but a review of case law suggests that evidence of at least some of the following may suffice to provide potential harm to goodwill: (1) loss of control over business reputation;[72] (2) negative customer reviews;[73] and (3) access to customer information and other proprietary materials.[74] Actual harm often is not required, only that harm would likely occur absent a temporary restraining order or preliminary injunction.[75]

In *Pom Wonderful LLC v. Pur Beverages LLC*, a federal district court found that, despite a declaration discussing the inconsistent product and advertising concerns surrounding the infringing use of Pom's marks, the declarations did not constitute evidence of harm.[76] In particular, Pom had not presented any evidence that its customers knew of the infringer's product or that they had a negative reaction to it or the infringer's advertising.[77] Nor was there any evidence of a negative impact to Pom's brand image.[78]

In *Tilden Recreational Vehicles v. Belair*, Belair signed an employment non-compete agreement stating he would not work in recreational vehicle sales within fifty miles of Boat-N-RV Superstore (BNRV) for one year after his employment.[79] When Belair left for BNRV's competitor, Chesaco, BNRV sued for breach of contract and sought a preliminary injunction.[80] Although BNRV did not present evidence that Belair had already caused harm to its interests, the Third Circuit upheld the district court's finding that BNRV would have suffered irreparable harm if Belair continued to work at Chesaco.[81] During his employment, Belair learned about BRNV's products, pricing strategy, and other information used to compete with BNRV.[82] By using its (or that) training, confidential information, and personal customer

72. Herb Reed Enters., LLC v. Fla. Entm't Mgmt., Inc., 736 F.3d 1239, 1250–51 (9th Cir. 2013).

73. JTH Tax LLC v. McHugh, 2020 WL 1689731, at *2 (W.D. Wash. Apr. 27, 2020) (negative customer reviews); 7-Eleven, Inc. v. Kapoor Bros., Inc., 977 F. Supp. 2d 1211, 1226–27 (M.D. Fla. Sept. 13, 2013) (customer complaints).

74. Basicomputer Corp. v. Scott, 973 F.2d 507, 512 (6th Cir. 1992) (employees had access to customer information and pricing information, which harmed employer's goodwill); Handel's Enters., Inc. v. Schulenburg, 765 F. App'x 117, 124–25 (6th Cir. 2019) (article published describing franchisee's ice cream as a "replication" of franchisor and that franchisee had "brought [franchisor's] winning formula" to franchisee's new location).

75. Tilden Recreational Vehicles, Inc. v. Belair, 786 F. App'x 335, 342 (3d Cir. 2019).

76. Pom Wonderful LLC v. Pur Beverages LLC, 2015 WL 10433693, at *7 (C.D. Cal. Aug. 6, 2015).

77. *Id.* at *11.

78. *Id.*

79. *Tilden*, 786 F. App'x at 337.

80. *Id.* at 337–38.

81. *Id.* at 342.

82. *Id.*

goodwill to attract sales and customer loyalty, the court found that Belair might harm BNRV's customer goodwill.[83]

3. Some Examples of Evidence of Harm

The majority of courts that have evaluated harm caused by a violation of a non-compete provision "have concluded that franchising companies suffer irreparable harm when their former franchisees are allowed to ignore reasonable covenants not to compete."[84] Said differently, evidence of the violation is evidence, without more, of the harm. For example, in *Quizno's Corp. v. Kampendah*,[85] the U.S. District Court for the Northern District of California granted an injunction against a former Quizno's franchisee who violated a covenant not to compete by opening a sandwich shop at the same location at which his Quizno's shop had been located for five years.[86] The court deemed the non-compete "essential to allow time for the public to stop associating [the new shop] with Quizno's."[87] The court also adopted Quizno's argument that it would "not be able to reenter the market as long as the [new shop] [was] in operation and w[ould] therefore lose sales, goodwill, and market presence it once had in the area."[88] Notably, the court observed that allowing the franchisee to *willfully* violate the covenant not to compete "sends a message to other franchisees that the Agreement does not protect Quizno's and may be disregarded at will,"[89] which other courts have adopted as well in franchise cases.[90]

Similarly, in *Bad Ass Coffee Company of Hawaii* (BACH), the U.S. District Court for the District of Utah found irreparable harm resulting from defendants' switch to a Java Cove in the same place where defendants had operated a BACH franchise for six years.[91] According to the court, customers might believe that BACH endorsed Java Cove or that defendants no longer stood by BACH.[92] The court held these messages could erode goodwill in the marketplace.[93] Additionally, BACH suffered harm by customers becoming Java Cove customers and by losing a potential franchisee if it had to compete with Java Cove.[94]

83. *Id.*
84. Bad Ass Coffee Co. of Hawaii, Inc. v. JH Nterprises, LLC, 636 F. Supp. 2d 1237, 1249 (D. Utah 2009).
85. Quizno's Corp. v. Kampendah, 2002 WL 1012997 (N.D. Ill. May 20, 2002).
86. *Id.* at *7.
87. *Id.*
88. *Id.*
89. *Id.*
90. *See, e.g.*, Flip Flop Shops Franchise Co. v. Neb, 2016 WL 9275403, at *8–9 (C.D. Cal. Dec. 5, 2016) (following *Quizno's* and finding irreparable harm because a contrary result would "embolden" future franchisee to violate the non-compete agreement and "jeopardize [franchisor's] entire business model"); *Bad Ass Coffee Co*., 636 F. Supp. 2d at 1249.
91. *Bad Ass Coffee Co.*, 636 F. Supp. 2d at 1249.
92. *Id.*
93. *Id.*
94. *Id.*

The cases cited in the previous section, as well as others cited in this article, illustrate the importance of putting forth actual evidence of likelihood of harm. Mere conclusory allegations of potential harm are not enough. Rather, courts will look for a specific aspect of the business that may be harmed, particular knowledge the infringer may have that can result in a loss of goodwill, or an example of how the infringement may cause the franchisor to lose control over its brand or reputation.[95] If harm has already taken place, it would be prudent to submit declarations identifying the specific examples of harm, such as negative customer reviews, customer surveys, or inquiries evidencing customer confusion. If harm is likely, but has not yet occurred, the franchisor should introduce evidence of what knowledge or confidential information the franchisee had access to and/or still retains. The franchisor also should have, at minimum, a credible and knowledgeable employee provide testimony that explains how a competitor's use of that information would be detrimental to the goodwill. Paint a clear picture, do not leave anything to chance, and, when in doubt, err on the side of submitting more evidence, not less.

III. Conclusion

The intangible nature of goodwill does not render it non-existent or incapable of proof. Although courts and legislatures continue to work toward developing a more concrete definition of this element of a business's success, franchisors need to take matters into their own hands when seeking injunctive relief to prevent harm to business reputation or brand. As an initial matter, the franchisor or its counsel should determine the applicable standards of proof required to succeed in obtaining injunctive relief. In cases involving trademark infringement, depending on the facts and applicable law, the franchisor may not need to prove irreparable harm if it can show a likelihood of confusion. Many courts, however, still require actual proof of irreparable harm, including specific damage to goodwill. In those jurisdictions, relying only on conclusory allegations that harm to goodwill is likely to occur is insufficient. Be as specific as possible and identify tangible examples of harm. Although there are no guarantees in life or litigation, preparation and thoroughness are a litigant's best friends.

95. *See, e.g.*, Purugganan v. AFC Franchising, LLC, 2020 WL 6946558, at *5 (D. Conn. Nov. 25, 2020) (declining to award injunctive relief because plaintiff "does not explain in any concrete fashion *how* these purchases will harm reputation or goodwill"); Pom Wonderful LLC v. Pur Beverages LLC, 2015 WL 10433693, at *5 (C.D. Cal. Aug. 6, 2015) ("A finding of reputational harm may not be based on pronouncements that are grounded in platitudes rather than evidence.") (citations, alterations, and quotation marks omitted).

An Overview of Franchising Law in Southeast Asia

*Alan Adcock, Chandavya Ing, Dino Santaniello, Jay Cohen, Mealtey Oeurn, David Mol, Sher Hann Chua, Thao Thu Bui, Tu Ngoc Trinh & Waewpen Piemwichai**

I. Introduction

Mr. Adcock

The popularity of the franchise business model has grown rapidly in mainland Southeast Asia in recent years, with some of the world's top brands becoming common sights in the commercial districts and shopping malls of major regional cities in Cambodia, Laos, Myanmar, Thailand, and Vietnam.

Although these countries have not yet enacted franchising-specific laws, certain features of each country's regulatory regime impact franchising. As such, well-prepared franchise business operations have comfortably adapted to each country's regulatory framework, and the growth is poised to continue even as the global retail sector redesigns and redoubles its efforts in the wake of the COVID-19 pandemic. In fact, the franchise business model, which is both global and local at the same time, may offer retail entrepreneurs a solution in their quest to meet the challenges of the new retail economic realities.

This article explains the legal frameworks that impact the franchise business model in Cambodia, Laos, Myanmar, Thailand, and Vietnam. For each country, this article discusses relevant regulatory considerations for franchise

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agreements, how to protect intellectual property rights, and judicial and arbitral procedures for resolving disputes that might arise between a franchisor and a franchisee.

II. Cambodia

By Jay Cohen, Chandavya Ing, Mealtey Oeurn, and David Mol

Cambodia's steady, robust economic growth continues to draw foreign direct investment (FDI), in addition to increasing the purchasing power of the country's population. The World Bank puts the growth rate of Cambodia's economy at eight percent between 1995 and 2018,[1] and, during that time, Cambodia transitioned from being classified as a low-income country to a lower-middle income country.[2] Along with economic growth, and a welcoming investment framework, Cambodia has witnessed the entrance of a number of international franchise brands, especially in the food and consumer goods sectors.

Domestic franchising typically consists of direct franchising, often involving home businesses such as laundry services, whereby the franchisee is given training and provided with systems to operate successfully and economically. Most international franchising in the country takes place through master franchise agreements. Master franchising can save a franchisor the expense and uncertainty of establishing its own local infrastructure.

Cambodia has not yet enacted a comprehensive franchising regulatory scheme similar to the United States. Franchising is governed primarily by the Civil Code;[3] the Law Concerning Marks, Trade Names and Acts of Unfair Competition, dated February 7, 2002 (Trademark Law);[4] the Sub-Decree on the Implementation of the Law Concerning Marks, Trade Names and Acts of Unfair Competition, dated July 12, 2006 (Trademark Implementation Law);[5] the Notification on the Recordal of License Contracts and Franchise Contracts, dated March 12, 2015;[6] and the Prakas on the Recordal of License Contract Over Mark and Franchise Contract, dated 13 January 2020.[7]

A. *Franchising in Cambodia*

An overseas franchisor is not required to use a separate entity to enter into a franchise agreement with a franchisee in Cambodia, but they are permitted to do so if they desire.

1. *Cambodia Overview*, Worldbank, https://www.worldbank.org/en/country/cambodia/overview.
2. *Cambodia*, Worldbank, https://ida.worldbank.org/results/cambodia.
3. Civil Code (2007) [Cambodia] [hereinafter Cambodia Civil Code].
4. Law Concerning Marks, Trade Names, and Acts of Unfair Competition (2002) [hereinafter Cambodia Trademark Law].
5. Sub-Decree on the Implementation of the Law Concerning Marks, Trade Names and Acts of Unfair Competition (2006) [hereinafter Cambodia Trademark Implementation Law].
6. Notification on the Recordal of License Contracts and Franchise Contracts (2015).
7. Prakas on the Recordal of License Contract over Mark and Franchise Contract (2020).

For franchise agreements originally prepared in a foreign jurisdiction and according to the law of a country other than Cambodia, franchisors should focus on adapting the following provisions in the franchise agreement to ensure they are enforceable in Cambodia: pre-disclosure and guaranty provisions; non-compete obligations; fees and tax-related clauses; termination and damages; intellectual property provisions; dispute resolution clauses; and real estate provisions.

The articles addresses a few of the important aspects of these provisions below, but franchisors should work with local counsel to ensure that their full agreement is sufficiently adapted to comply with Cambodian law.

B. *Pre-Disclosure & Guaranty*

While Cambodian law does not provide any requirements on pre-contract disclosure, all of the information provided in the franchise agreement must be accurate. If a party enters into a contract on the basis of another party's misrepresentation, the Civil Code stipulates that they are entitled to rescind the contract and make a claim for damages from the party who made the misrepresentation.[8]

Further, under the same legislation, a personal guaranty is invalid if the guarantor was not fully informed of all material information on the guaranteed obligation at the time that the guaranty was provided.[9] Accordingly, the franchisor must ensure that the proper material information is provided at the time of the signing of the guaranty and should ensure that the guaranty contains an agreement that all material information was provided.

C. *Non-Compete Obligations*

Cambodia does not currently have specific competition legislation. Although the Ministry of Commerce is working on a draft Competition Law, there is no timeline for its enactment. However, it is common for foreign companies to insert non-competition provisions in their franchise agreements to restrict franchisees from engaging in any activities that compete with the franchisor. In Cambodia, employees may not be restricted by their former employers in any way,[10] effectively prohibiting non-compete provisions in employment relationships. The franchise agreement should take into consideration this limitation when drafting a non-compete provision, as the clause may affect the mobility of employees post-employment with the franchisee.

D. *Fees and Taxes*

Initial fees, continuing fees (management charges or royalty fees), advertising contributions, required advertising spend, and other customary franchisee fees are common in franchise agreements in Cambodia. There is no restriction on the amount that can be charged for initial fees, continuing fees

8. Cambodia Civil Code, art. 345.
9. *Id.* art. 900.
10. Labor Law, art. 70.

or charges, advertising contributions, or required advertising spend. However, for tax purposes, advertising contributions and required advertising spend paid directly to the franchisor will generally be treated as royalties payable to the franchisor, according to the current practice of the General Department of Taxation.

Interest on overdue payments is allowed under the Civil Code, with a default interest rate of five percent per year unless specified otherwise.[11] There is no maximum interest rate that can be charged on overdue payments, except in the context of a loan.[12] If interest accrues unpaid for over one year despite payment being demanded of the franchisee, the franchisor can add the overdue interest to the principal amount.[13]

E. *Termination and Damages*

There are no specific statutory limitations on the right of a franchisor to terminate a franchise agreement. Termination rights (including compensation for early termination) are governed by the terms of the agreement, and breach of a contractual provision concerning termination may result in a civil action for damages.[14] Any contractual provision that purports to limit a defaulting party's liability for intentional non-performance, or non-performance resulting from gross negligence, is deemed to be void and unenforceable.[15]

In addition, a contractual provision providing for the payment of liquidated damages does not preclude a claim for additional damages arising from a breach or termination of the contract.[16] Typically, liquidated damages clauses are enforceable in Cambodia as long as the damages amount reasonably correlates to the anticipated losses resulting from a breach.[17] Liquidated damages fixed by the parties that are deemed punitive or grossly higher than the amount of damages actually suffered may be lowered by the court.[18] The court is likewise authorized to award additional damages if the actual damages exceed the liquidated damages provided under the contract.[19]

F. *Intellectual Property*

Intellectual property is another key part of franchise agreements, with franchisors typically granting franchisees the right to use trademarks, systems, logos, advertisements, patents and industrial designs, and know-how in connection with the franchised business.

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11. Civil Code, art. 318.
12. Prakas on Interest Rate Ceiling on Loan (2017), https://www.nbc.org.kh/download_files/legislation/prakas_eng/Prakas-on-Interest-Rate-Cap-Eng.pdf.
13. Cambodia Civil Code, art. 586.
14. *Id.* ch. IV (Remedies for Breach of Contract).
15. *Id.*, art. 403(2).
16. *Id.*, art. 403(4).
17. *Id.*, art. 403 (1).
18. *Id.*, art. 403 (3)
19. *Id.*, art. 403.

Trademark owners need to register their trademarks with the Department of Intellectual Property Rights (DIPR) to receive protection under local law for a renewable term of ten years.[20] Since Cambodia is a member of the Paris Convention for the Protection of Industrial Property, a trademark priority claim period of six months is applicable.[21] To maintain registration and avoid cancellation, the owner of the trademark must file an Affidavit of Use/Non-Use for the mark within one year following the fifth anniversary of the date of registration (or of the renewal date).[22] In 2015, Cambodia became a member of the Madrid System; thus, trademark registration applications initiated at a national or regional intellectual property office of another party to the system can also be designated for filing in Cambodia.[23]

Under Article 19 of the Trademark Law, any license agreement for trademarks, including a franchise agreement with provisions on trademark licenses, must impose the obligation on the licensor to effectively control the quality of the goods or services in connection with the mark used; otherwise, the contract will not be valid.[24]

In theory, trademark license agreements cannot be enforced against third parties if they have not been registered with the DIPR.[25] That means, in practice, it is only necessary to register a trademark license agreement, or a franchise agreement that contains trademark license provisions, if the licensor wants to allow the licensee the right to enforce the agreement against third parties (e.g., persons in Cambodia infringing on the licensor's trademarks). The official fee to record a franchise agreement is KHR 400,000 (approximately $100) per trademark.[26]

Similarly, patent and industrial design licenses should be registered with the Ministry of Industry and Handicrafts (MIH).[27] Cambodia is a member of the Paris Convention for the Protection of Industrial Property,[28] a contracting state of the Patent Cooperation Treaty (PCT),[29] and a contracting party to the Hague Agreement on the International Registration of Industrial

20. Cambodia Trademark Law, art. 12.

21. *Id.*, art. 6.

22. Cambodia Trademark Implementation Law, art. 21.

23. *See* Prakas on the Procedure for International Registration of Marks Under the Madrid Protocol (2016), https://wipolex.wipo.int/en/legislation/details/19479.

24. Cambodia Trademark Law, art. 19.

25. Prakas on the Recordal of License Contract Over Mark and Franchise Contract art. 14 (2020).

26. Inter-ministerial Prakas on the Provision of Public Services at the Ministry of Commerce (2017).

27. Law on Patents, Utility Model Certificates and Industrial Designs, art. 16 (2003).

28. Paris Convention for the Protection of Industrial Property, as last revised at the Stockholm Revision Conference, Mar. 20, 1883; Paris Notification No. 186, Paris Convention on the Protection of Industrial Property: Accession by the Kingdom of Cambodia, June 22, 1998, *available at* https://www.wipo.int/treaties/en/notifications/paris/treaty_paris_186.html.

29. PCT Notification No. 210, Patent Cooperation Treaty (PCT): Accession by the Kingdom of Cambodia, Sept. 8, 2016, *available at* https://www.wipo.int/treaties/en/notifications/pct/treaty_pct_210.html

Design.[30] Although Cambodia lacks the infrastructure to examine patent applications, the MIH has made it possible to obtain patent protection in Cambodia through a number of agreements with other governments that set out an accelerated process that can be completed in months, not years. These agreements have been made with the Intellectual Property Office of Singapore,[31] the Japan Patent Office,[32] the European Patent Office,[33] the China National Intellectual Property Administration,[34] and, more recently, the Korean Intellectual Property Office[35] and the United States Patent and Trademark Office.[36]

Cambodia ratified the Berne Convention in 2020, and the government was authorized to take the necessary steps to accede to the convention.[37] At the time of writing, Cambodia has not yet deposited the instrument of accession with the director general of the World Intellectual Property Organization (WIPO), and several legislative or regulatory updates may be introduced to bring the country's copyright law in line with the Berne Convention, including provisions relating to the automatic protection of foreign copyrights. Therefore, until Cambodia officially accedes to the Berne Convention, foreign copyrights are not protected in Cambodia unless the work is created by a person who is resident in Cambodia, created by a legal person with a registered office in Cambodia, or first published abroad and registered in Cambodia within thirty days of the first communication to the public.[38] This reality means that franchisors' manuals and other similar materials may not be protected in Cambodia through copyrights, and other means of protection (e.g., by keeping it as a trade secret or through the patent process) should be sought.

30. *Cambodia Joins the Hague System*, WIPO News (Nov. 25, 2016), wipo.int/hague/en/news/2016/news_0011.html.

31. Memorandum of Understanding (MOU) on the Co-operation in Industrial Property between the Ministry Industry and Handicraft and the Intellectual Property Office of Singapore, Jan. 20, 2015; Renewal of the MOU on the Co-operation in Industrial Property between the Ministry of Industry and Handicraft and the Intellectual Property Office of Singapore, Jan. 14, 2020.

32. Joint Statement of Intent on Cooperation for Facilitating Patent Grant of Cambodia-Related Patent Application (May 4, 2016).

33. Agreement Between the President of the European Patent Office and the Cambodian Ministry of Industry and Handicraft (Jan. 23, 2017).

34. Memorandum of Understanding (MOU) on Cooperation on Intellectual Property Between the Ministry of Industry and Handicraft and the State Intellectual Property Office of China (Sept. 21, 2017).

35. Memorandum of Understanding (MOU) on Patent Cooperation Between Ministry of Industry and Handicraft and the Korean Intellectual Property Office of the Republic of Korea (Aug. 16, 2019).

36. Memorandum of Understanding (MOU) on the Co-operation to expedite the issuance of patents in Cambodia Between the Minister of Industry, Science, Technology and Innovation and USPTO (Oct. 23, 2020).

37. Law on Ratification of Cambodia to Join the Berne Convention for the Protection of Literary and Artistic Works 1886 and its Amendment in 1979 (2020).

38. Law on Copyright and Related Rights, 2003, art. 3 [Cambodia].

Cambodia does not currently have any law governing trade secrets. Mostly, franchisors use non-disclosure clauses in their franchise agreements to secure and protect their know-how from third parties.

G. *Dispute Resolution*

Choosing a foreign country's law as the governing law for a franchise agreement does not contravene Cambodian law. However, in the authors' experience, local courts may be unwilling to apply foreign law to disputes before them. In addition, certain subject matter (such as advertisement approval requirements for certain services, like healthcare,[39] or the owning of land)[40] can only be governed by Cambodian law.

Foreign franchisors should carefully consider the dispute resolution mechanism provided in their franchise agreements. Under Cambodian law, foreign court judgments are not enforceable in Cambodia unless, among other requirements, there is a guarantee of reciprocity between Cambodia and the country in which the court is based.[41] Cambodia has only entered into such an agreement with Vietnam.[42]

Cambodia is, however, a member of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, so foreign arbitration awards are enforceable in Cambodia.[43] Further, Cambodia has its own domestic arbitration institution called the National Commercial Arbitration Center.[44] Foreign parties almost always include arbitration clauses in their franchise agreements, and they usually require arbitration to be conducted under the rules of an established foreign arbitration body such as the Singapore International Arbitration Centre (SIAC).[45] Nevertheless, most foreign parties tend to conclude their disputes with a Cambodian counter-party by arriving at a settlement.

H. *Real Estate*

In Cambodia, land ownership is limited to Cambodian nationals, or entities of Cambodian nationality, meaning that at least fifty-one percent of the company's shares are held by Cambodian nationals or other companies of Cambodian nationality.[46] Foreigners may, however, own up to seventy

39. Prakas No. 028 on Private Practice Advertisement in Medical, Paramedical and Medical Aid Practices, 2004.

40. Constitution of the Kingdom of Cambodia, Sept. 21, 1993, art. 44; Land Law (amended 2001), art. 9 [Cambodia].

41. Code of Civil Procedure, art.199 [Cambodia].

42. Agreement on Mutual Judicial Assistance in Civil Matters Between the Kingdom of Cambodia and the Socialist Republic of Vietnam (Jan. 21, 2013).

43. Law on the Ratification and Implementation of the UN Convention on Recognition of Foreign Arbitration Award (July 23, 2001).

44. Law on Commercial Arbitration (2006) [Cambodia].

45. Singapore Int'l Arb. Centre, https://www.siac.org.sg.

46. Constitution of the Kingdom of Cambodia, dated September 21, 1993, Article 44; Land Law (amended 2001), dated August 31, 2001, Article 9.

percent of the floor space on co-owned buildings (which are akin to condos and mixed used developments).[47] Any real estate related provisions in a franchise agreement should adhere to these limitations, and care should be taken to ensure that mechanisms are in place for any real estate related to the franchise.

III. Laos

By Dino Santaniello

Eclipsed by its more prominent neighbors that include China, Thailand, and Vietnam, Laos has often been overlooked by foreign investors seeking to capitalize on investment opportunities in the region. However, thanks to an increased commitment from the government to ease restrictions on FDI and efforts to create a more well-rounded economy that is less dependent on natural resources, Laos has witnessed a surge of new franchise operations over the past few years. From food and beverage operators to car rental providers and clothing retailers, these new franchises represent a variety of different industries and help to diversify the Lao economy.

While there are no specific franchising regulations in Laos, there are a number of other pieces of legislation that may govern franchises in the country.

The Decision on Wholesale and Retail Businesses 2015 No. 1005/MOIC.ITD, dated May 22, 2015, mentions the term *franchise* and stipulates that general wholesale and retail activities can be carried out under this type of business.[48] While there are no prohibitions on foreigners who wish to invest in a franchise business, there are specific requirements and restrictions on FDI. For example, the minimum registered capital imposed on foreign investors in the retail and wholesale business will depend on the share equity held in the company carrying out the franchise.[49] Depending on the business activities of the franchise, additional restrictions on the ratio of shares between foreigners and Lao nationals may apply.[50]

All franchise agreements are also governed by the common rules of the Civil Code No. 55/NA, dated December 6, 2018,[51] and the Law on Notary No. 11/NA, dated November 26, 2009 (Notary Law).[52] For contracts of a certain value, it is therefore strongly recommended to proceed with the notarization of the contract by the Notary Office of the Ministry of Justice or one of its related departments. This notarization proves that the contract is valid under existing Lao laws and thus fully enforceable against a third

47. Law on Providing Foreigners with Ownership Rights Over Private Part of Co-Owned Buildings, 2010.

48. Decision on Wholesale and Retail Businesses, art. 11 (2015) [Laos].

49. *Id.* art. 13.

50. As a matter of example, the Notification No.1327/MOIC.ER, 2015, includes a list of activities whose investment is restricted from foreign investors.

51. Civil Code No. 55/NA, 2018 [Laos] [hereinafter Laos Civil Code].

52. Law on Notary No. 11/NA, 2009 [hereinafter Laos Notary Law].

party.[53] There are no statutory pre-contract disclosure requirements in Laos. Regarding the protection of intellectual property of a franchise agreement, the applicable legislation is the Law on Intellectual Property No. 38/NA, dated November 15, 2017,[54] and the subsequent Decision on Trademarks and Trade Names No. 2822/MOST, dated December 17, 2019 (Decision on Trademarks.)[55]

A. *Franchise Agreements*

Typically, franchise agreements, or similar agreements relating to trademarks, would fall under the provision of the Decision on Trademarks, which regulates the "authorization to use a trademark," thus enabling trademark owners to contractually allow others to use their trademark.[56] The decision provides that the licensee or licensor must notify the Lao Department of Intellectual Property (DIP) of any agreement authorizing use of a trademark (e.g., a license agreement). While the Decision on Trademarks does not provide any sanctions for failing to register, the recordal can be used by the licensee as a proof of its rights to act on behalf of the trademark owner to carry out any legal actions, for instance.

The Civil Code requires good faith in the performance of contracts.[57] Though "good faith" is not legally defined or described, it can generally be construed as performing a contract without the intention to defraud the other party, or to act without malice.

Clauses that could be deemed anti-competitive also need to be treated very carefully. For instance, imposing different prices or terms for transactions involving the same goods or services is prohibited under a chapter dedicated to abuse of dominant market position, as is monopoly,[58] by the Law on Business Competition, No. 60/NA, dated July 14, 2015.[59] Similarly, Laos prohibits the imposition of terms and conditions through a sale or purchase agreement,[60] as well as the act of forcing the performance of obligations that are not required by contract.[61] This provision aims to protect franchisees from franchisors who may attempt to abuse their power during negotiations or during the performance of the contract. Finally, the Law on Business Competition expressly prohibits price fixing for operators in a position of market dominance. Franchisors are thus not permitted to impose a price

53. *Id.* art. 15.

54. Law on Intellectual Property No. 38/NA, 2017 [hereinafter Laos Law on Intellectual Property].

55. Decision on Trademarks and Trade Names No. 2822/MOST, 2019, art. 32 [hereinafter Laos Decision on Trademarks]. The Decision on Trademarks literally speaks of an agreement on "Authorization to Use a Trademark."

56. *Id.* art. 32.

57. Laos Civil Code art. 378.

58. Law on Business Competition, No. 60/NA, 2015, art. 36 [hereinafter Laos Law on Business Competition].

59. *See generally* Laos Law on Business Competition.

60. *Id.* art. 26.

61. *Id.*

related to their goods or services upon franchisees, except in very particular circumstances.

Non-compete clauses that amount to an absolute or excessive restraint of trade are not permitted. What is usually permissible is a reasonable restraint that is narrow in scope and specific to the circumstances. Despite the absence of case law defining a reasonable scope for a non-compete provision, provisions with a very narrow scope relating to specific circumstances would likely be enforceable. For these reasons, post-contractual non-compete clauses should be drafted carefully, identifying a reasonable and clearly defined scope.

B. *Intellectual Property*

Issues surrounding the protection of all forms of intellectual property are important in franchisor-franchisee relationships. There is no requirement to register trademarks under Lao law before circulating goods or services in the country; however, franchisors may benefit from doing so. Laos uses the first-to-file system for trademark registrations, meaning that the first person to file a trademark will hold exclusive rights over that mark. Registration of a trademark, which gives the registered owner the ability to protect its trademarks against infringement, will be necessary to initiate and conduct seizures against parties selling goods or services that infringe on the intellectual property rights of the registered trademark owner.[62] Accordingly, a franchisor or franchisee in Laos that has registered a trademark will be able to seek assistance from authorities to conduct seizures of counterfeit or imitation goods.

Copyrights do not need to be registered in order to be protected by law, as the rights arise automatically when a work is created.[63] However, an official notification claiming copyright ownership can be useful as evidence in case of a violation or dispute and may be filed with the DIP.

Trade secrets are expressly mentioned under the law on intellectual property and also do not require registration in order to be protected.[64] They will remain protected as long as the information (1) remains confidential, (2) has trade value, and (3) is not easily accessible. However, it would be prudent to set out contract provisions regarding the relationship of the franchisor and franchisee regarding trade secrets and their protection.

Similarly, it can also be beneficial to ensure that franchise employees (including third-party contractors) are contractually informed of intellectual property issues—for instance, through standard confidentiality and intellectual property acknowledgment and assignment, and contingency clauses in employment contracts.

62. Laos Law on Intellectual Property, art. 58.
63. *Id.* art. 97.
64. *Id.* art. 12.

C. *Taxation and Dispute Resolution*

Under the Law on Income Tax No. 67/NA, dated June 18, 2019, a ten percent withholding tax applies to payments made with respect to dividends,[65] and a five percent withholding tax applies to intellectual property royalty fees.[66]

Taxation rates may differ from those prescribed in the law if the recipient of the payment is from a country that has signed a double taxation agreement with Laos. Currently, this situation applies to Brunei, China, Luxembourg, Malaysia, Myanmar, North Korea, Russia, Singapore, South Korea, Thailand,[67] and Vietnam.

In Laos, there is no dispute resolution body with specific responsibility for handling franchise disputes. Generally, franchise operators in Laos prefer to remedy disputes by filing complaints with the relevant administrative bodies (determined by the nature of the dispute), instead of filing complaints with the Lao People's Court.[68] Mediation is often considered a prerequisite to filing a complaint with the Lao People's Court, which is an option if the administrative remedy of the mediation process fails.

Laos is a signatory to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards.[69] Accordingly, foreign arbitral awards are recognized and enforceable in Laos, as long as they do not affect the sovereignty of Laos, contradict the country's laws, or affect the "peace and orderliness" of Lao society.[70]

IV. Myanmar

By Sher Hann Chua

The relaxation of foreign investment restrictions and a growing, aspiring middle class have encouraged new players to enter Myanmar's franchising industry in recent years. Previously, both Western and Asian franchises in Myanmar predominantly operated in the food and beverage industry; however, in the last few years, the country has witnessed a growth spurt of franchise operations in the services and education sectors. Domestic franchising is still relatively uncommon. International franchise brands typically enter the Myanmar market by appointing a local master franchisee—which helps

65. Law on Income Tax No. 67/NA, 2019, art. 39 [Laos].

66. *Id.*

67. Double Tax Agreement Between the Government of Kingdom Thailand and Lao PDR (Dec. 23, 1997).

68. Administrative remedies are filed with the relevant administration (e.g., Ministry of Industry and Commerce if the nature of the dispute pertains to consumer protection) whereby the administration may serve as mediator and ultimately take sanction against one of the parties (e.g., warning, fine, withdrawal of license). The right to file a complaint with the Lao People's Court to force compliance with the rule is included in the Law on Civil Procedure, and the court has the ability to impose sanctions, including civil compensation.

69. Notification no.2454/PMO, 1998 [Laos].

70. Law on Civil Procedure, art. 362 [Laos].

in dealing with legal and regulatory restrictions applicable to foreign investors, as well as the challenges of understanding local business frameworks and infrastructure.

Myanmar does not currently have any specific legislation regulating franchise relationships, and there are no statutory, pre-sale disclosure requirements. Nevertheless, franchise relations are subject to other relevant legislation on contracts and business operations, such as the Competition Law of 2015,[71] the Consumer Protection Law of 2019,[72] the Contract Act of 1872,[73] the Myanmar Companies Law of 2017,[74] and the Trademark Law of 2019.[75]

A. *Franchise Agreements and Fees*

In drafting, negotiating, and executing franchise agreements, a franchisor should be careful to observe the existing laws. Abusing bargaining power or imposing conditions that interfere in the franchisee's business operations may violate provisions of local law.[76] For instance, charging different franchise fees to different franchisees may raise anti-competitive concerns, while requiring franchisees to buy products and services only from nominated suppliers may also be deemed a violation of the Competition Law of 2015 in certain cases.[77] In addition, restrictive covenants prohibiting franchisees from engaging in a similar business upon the expiration or termination of a franchise relationship need to contain carefully drafted limitations on the applicable term and geographical area.[78]

Parties are free to set the fee and payment requirements in a franchise agreement. Typically, franchisees pay the initial and continuing fees (or management charges), as well as advertising contributions, required advertising spend, training fees, and other customary franchisee fees.

Initial fees and ongoing royalty fees are subject to a withholding tax payable by a non-resident foreign franchisor at a rate of 15% and by a resident foreign or local franchisor at a rate of 10%.[79] For goods sold or services rendered as part of a franchise transaction by the franchisor, such as operational equipment and training fees, a withholding tax of 2.5% is applicable for a non-resident foreign franchisor; for a resident foreign or local franchisor, no withholding tax is payable.[80] If existing double-taxation agreements are in place, the withholding tax amount payable by non-resident foreigners may be reduced or exempted, subject to the discretion of the Ministry of

71. Competition Law (2015) [Myanmar] [hereinafter Myanmar Competition Law].
72. Consumer Protection Law (2019) [Myanmar].
73. Contract Act (1872) [Myanmar] [Myanmar Contract Act].
74. Myanmar Companies Law (2017).
75. Trademark Law (2019) [Myanmar] [hereinafter Myanmar Trademark Law].
76. Myanmar Competition Law, ch. VIII, XI.
77. *Id.* §§ 13, 15, 17.
78. Myanmar Contract Act § 27.
79. Myanmar Ministry of Planning and Finance, Notification No. 47/2018.
80. *Id.*

Planning and Finance and the Internal Revenue Department.[81] To date, Myanmar has entered into double-taxation agreements with India, Laos, Malaysia, Singapore, South Korea, Thailand, the United Kingdom, and Vietnam.[82] Double-taxation agreements with Bangladesh and Indonesia have also been concluded but have yet to be ratified.[83]

B. *Intellectual Property*

As in any jurisdiction, intellectual property should be a central concern in a franchise relationship in Myanmar. Many franchisors are rightly concerned that a former franchisee will utilize the knowledge and experience gained from running a franchise operation to open a competing business. To prevent this issue, it is vital for franchisors to protect themselves by using clear and comprehensive language in their franchise agreements. As part of this step, franchise agreements should contain robust provisions prohibiting the disclosure and use of information, knowledge, and trade secrets obtained from operation of the franchise. Disclosure of trade secrets is punishable under the Competition Law of 2015 by imprisonment for up to two years, a fine of up to MMK ten million (approximately $7,100), or both.[84]

In 2019, Myanmar enacted a suite of intellectual property legislation, comprising a Trademark Law,[85] Industrial Designs Law,[86] Patent Law,[87] and Copyright Law.[88] Under the new intellectual property system, trademarks, industrial designs, and patent licenses must be recorded with the intellectual property office to be deemed enforceable in Myanmar.[89] Similarly, under the Science, Technology, and Innovation Law of 2018, all agreements on technology transfers must comply with the terms set by the National Council for Science, Technology, and Innovation Development, and they must be registered with the designated registrar to be deemed enforceable.[90]

C. *Dispute Resolution*

It is common for foreign franchisors in Myanmar to opt for the franchise agreement to be governed by foreign laws, and for disputes to be settled via arbitration outside of Myanmar, such as in Singapore under the Singapore International Arbitration Centre rules. Under the Arbitration Law of 2016

81. *Avoidance of Double Taxation Agreements of Union of Myanmar*, Myanmar Internal Rev. Dept., https://www.ird.gov.mm/en/page/589.

82. *Id.*

83. *Myanmar: Individual-Foreign Tax Relief and Tax Treaties*, pwc.com, https://taxsummaries.pwc.com/myanmar/individual/foreign-tax-relief-and-tax-treaties.

84. Myanmar Competition Law, 2015, §§19, 41.

85. Myanmar Trademark Law.

86. Industrial Designs Law (2019) [Myanmar] [hereinafter Myanmar Industrial Designs Law].

87. Patent Law (2019) [Myanmar] [hereinafter Myanmar Patent Law].

88. Copyright Law (2019) [Myanmar].

89. Myanmar Trademark Law § 49; Myanmar Industrial Designs Law § 58; Myanmar Patent Law § 64.

90. Technology and Innovation Law, 2018, Ch. IX (Science) [Myanmar].

and the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (to which Myanmar is a signatory), foreign arbitral awards are recognized and enforceable by Myanmar courts, except in certain cases.[91] For example, Myanmar courts may refuse to recognize a foreign arbitral award if the party against whom it is invoked furnishes to the court proof that, among other reasons, the parties to the arbitration agreement referred was under some incapacity;[92] the agreement concerned is not valid under the law to which the parties have subjected to it;[93] or if the award has not yet become binding on the parties or has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made.[94] Enforcement of a foreign arbitral award may be refused if the Myanmar courts find that the subject matter of the dispute is not capable of settlement by arbitration under Myanmar laws,[95] or if the enforcement of the award would be contrary to the public policy of Myanmar.[96] Therefore, unless the dispute arising from a franchise agreement falls within one of the limited exceptions of the Arbitration Law of 2016, Myanmar courts are required to honor an election of international arbitration dispute resolution where an arbitration clause has been incorporated into the franchise agreement.[97]

A foreign civil court judgment is enforceable in Myanmar under the Civil Procedure Code if it was issued by a court of competent jurisdiction, was decided on merits, was not obtained by fraud, is not against the principles of natural justice, is in accordance with the principles of international law, and does not contradict any law in force in Myanmar.[98]

V. Thailand

By Sher Hann Chua

Industry research indicates that there are currently more than 350 franchisors (the majority of which are foreign-owned) and more than 15,000 franchisees in Thailand.[99] Some of the most popular franchise operations are in the food and restaurant sector, services, education, and retailing.[100]

While no specific statutes govern franchising in Thailand, the Trade Competition Commission of Thailand issued a set of guidelines in 2019 to regulate unfair trade practices in franchise businesses.[101] The government has

91. Arbitration Law § 46 (2016) [Myanmar] [hereinafter Myanmar Arbitration Law].
92. *Id.* § 46(b)(i).
93. *Id.* § 46(b)(ii).
94. *Id.* § 46(b)(vi).
95. *Id.* § 46(c)(i).
96. *Id.* § 46(c)(ii).
97. Myanmar Arbitration Law § 46.
98. Civil Procedure Code § 13 [Thai.].
99. Thai Franchise Center, https://www.thaifranchisecenter.com/stats/franchise_stats.php.
100. *Id.*
101. Notification of the Trade Competition Commission Re: Guidelines for the Consideration of Unfair Trade Practices in Franchise Businesses (2019) [Thai.] [hereinafter Thailand Franchise Guidelines].

also been contemplating the enactment of a Franchising Business Act, but no concrete steps have been taken to move it forward. It is widely considered that Thailand may follow the Chinese model as set out in the 2005 PRC Ministry of Commerce's Administrative Measures on Commercial Franchising[102] and the subsequent 2007 Franchise Regulations.[103] An important point to watch here will be whether Thailand follows the Chinese model by requiring a franchisor to prove the viability of its business model by showing a record of profitability at two or more outlets before selling a franchise contract to a franchisee.[104]

A. *Franchise Agreements*

The terms of a franchise agreement in Thailand will generally need to conform to the following laws:

- Civil and Commercial Code;[105]
- Trademark Act B.E. 2534 (1991), as amended by Trademark Act (No. 2) B.E. 2543 (2000) and Trademark Act (No. 3) B.E. 2559 (2016);[106]
- Patent Act B.E. 2522 (1979), as amended by Patent Act (No. 2) B.E. 2535 (1992) and Patent Act (No. 3) B.E. 2542 (1999);[107]
- Copyright Act B.E. 2537 (1994), as amended by Copyright Act (No. 2) B.E. 2558 (2015) and Copyright Act (No. 3) B.E. 2558 (2015);[108]
- Trade Secrets Act B.E. 2545 (2002), as amended by Trade Secrets Act (No. 2) B.E. 2558 (2015);[109]
- Unfair Contract Terms Act B.E. 2540 (1997);[110]
- Trade Competition Act B.E. 2560 (2017);[111]
- Act Relating to Price of Merchandise and Service B.E. 2542 (1999);[112] and
- Revenue Code B.E. 2481 (1938)[113]

102. Administrative Measures on Commercial Franchising, (promulgated by Ministry of Commerce, Dec. 30, 2004, effective Jan. 1, 2005) (China).

103. Regulations on the Administration of Commercial Franchise (promulgated by the State Council on Jan. 31, 2007 and effective May 1, 2007) (China).

104. Administrative Measures on Commercial Franchising, (promulgated by Ministry of Commerce, Dec. 30, 2004, effective Jan. 1, 2005), art. 7(4) (China).

105. Civil and Commercial Code [Thai.].

106. Trademark Act B.E. 2534 (1991), as amended by Trademark Act (No. 2) B.E. 2543 (2000) and Trademark Act (No. 3) B.E. 2559 (2016) [Thai.] [hereinafter Thailand Trademark Act].

107. Patent Act B.E. 2522 (1979), as amended by Patent Act (No. 2) B.E. 2535 (1992) and Patent Act (No. 3) B.E. 2542 (1999) [Thai.] [hereinafter Thailand Patent Act].

108. Copyright Act B.E. 2537 (1994), as amended by Copyright Act (No. 2) B.E. 2558 (2015) and Copyright Act (No. 3) B.E. 2558 (2015) [Thai.].

109. Trade Secrets Act B.E. 2545 (2002), as amended by Trade Secrets Act (No. 2) B.E. 2558 (2015) [Thailand] [hereinafter Thailand Trade Secrets Act].

110. Unfair Contract Terms Act B.E. 2540 (1997) [Thai.].

111. Trade Competition Act B.E. 2560 (2017) [Thai.] [hereinafter Thailand Trade Competition Act].

112. Act Relating to Price of Merchandise and Service B.E. 2542 (1999) [Thai.].

113. Revenue Code B.E. 2481 (1938) [Thai.].

The parties must be well aware of all relevant local regulations when negotiating the terms of a given agreement. A deal between parties of equal bargaining power will generally not be disturbed by the Thai courts unless there is a clear public policy reason to do so.

A franchisor must be reasonable in setting terms, or the term may be held to be unenforceable as an unfair limitation on competition.[114] For example, in the context of a franchising arrangement involving use of technology, a "tying arrangement" in which the franchisor requires the franchisee to purchase materials from the franchisor, or his or her agent, for use in production of a particular item without justifiable reasons may be seen as anticompetitive and may be unenforceable.[115]

Empowered under the Trade Competition Act B.E. 2560 (2017), the Office of the Trade Competition Commission of Thailand recently issued its Guidelines for the Consideration of Unfair Trade Practices in Franchise Businesses in December 2019 (Franchise Guidelines), which are aimed at preventing franchisors from adopting overly restrictive and unfair contractual conditions that could cause damage to franchisees.[116] For example, franchisors are prohibited from stipulating unjustified restrictions on the franchisees, such as forcing the latter to exclusively buy products or services that are irrelevant to the operation of the franchise business from a source designated by the franchisors.[117] Franchisors are also not allowed to prevent franchisees from offering discounts on perishable items that are close to their expiration,[118] and franchisors cannot discriminate among its franchisees by stipulating different conditions without justifiable reasons.[119]

Notably, the Franchise Guidelines also impose pre-contractual disclosure requirements on the franchisor, specifying that franchisors must provide to the franchisee details on matters concerning franchise fee payments, intellectual property rights, renewal and termination terms, and the model of the franchising system.[120] Under the Franchise Guidelines, franchisors who wish to enter into the market by setting up a branch by their own are also required to offer to right of first refusal to the franchisee operating in that area.[121]

B. *Intellectual Property*

One of the most important components of a franchise system is the trademark portfolio of the franchisor. The proprietor of a registered trademark may grant a license to other persons to use it for any or all of the goods or services for which it was registered.

114. Thailand Trade Competition Act B.E. 2560.
115. Franchise Guidelines § 5 (2019) [Thai.] [hereinafter Thailand Franchise Guidelines].
116. *See generally* Thailand Franchise Guidelines.
117. *Id.* § 5.1.1.
118. *Id.* § 5.4.
119. *Id.* § 5.5.
120. *Id.* § 3.
121. *Id.* § 4.

A trademark license agreement, which is typically a separate stand-alone agreement, but may also be contained within the franchise agreement itself, must be registered with the Department of Intellectual Property (DIP).[122] The unrecorded use of a trademark by a franchisee or licensee will not be considered as proof of use of that trademark for the purposes of defending the franchisor or licensor's registered trademark from a third party trademark cancellation action based on alleged non-use of the trademark.[123] Both the franchisor/licensor and the franchisee/licensee may take action against infringers, although the franchisee's/licensee's ability to take action is restricted by the terms of the agreement. Because Thailand is a freedom-of-contract jurisdiction, the contracting parties can adopt any terms or conditions that they deem appropriate concerning the ability to act, as long as the terms and conditions are legal, possible, and not contrary to public order or good morals.[124]

Another important component of some franchises is the franchisor's patented technology. In Thailand, the law of patents is primarily enshrined in the Patent Act B.E. 2522 (1979). Section 41 of the current Patent Act requires that a patent license agreement be similarly registered with the DIP.[125]

A franchisor must be vigilant to identify and carefully control the use and disclosure of its proprietary trade secrets, such as secret know-how, formulas, recipes, inventions, client lists, and sales data. This can be done in a separate nondisclosure or confidentiality agreement or with an airtight confidentiality provision within the franchise agreement itself, or both. In Thailand, trade secrets are protected under the amended Trade Secrets Act B.E. 2545 (2002) (TSA). Provisions in this law protect against unauthorized disclosure of trade secrets and enable the court to issue injunctions against disclosure of trade secrets.[126]

The TSA provides for broad protection and severe penalties for trade secret infringement.[127] However, one can only resort to the TSA for enforcement purposes if careful, demonstrable steps have been taken to maintain the secrecy of whatever proprietary information is in dispute. The expansion of such protection should be viewed as a benefit for trade secret owners in seeking remedial action for unauthorized disclosure of secrets.

122. Thailand Trademark Act § 58.
123. Supreme Court Judgment 4440/2552 (2009) [Thai.].
124. Civil & Commercial Code § 150 [Thai.].
125. Thailand Patent Act § 41.
126. Thailand Trade Secrets Act § 18.
127. *See generally* Thailand Trade Secrets Act B.E. 2545.

VI. Vietnam

By Thao Thu Bui, Tu Ngoc Trinh, and Waewpen Piemwichai

Franchising has become increasingly commonplace in in Vietnam in recent years. International franchise brands are now commonly seen in Vietnam's major cities, with particular prominence in the fields of food and beverages, fashion, and convenience stores. In addition to foreign franchises, local restaurant groups have seen tremendous growth. By May 2019, the Ministry of Industry and Trade had granted over 230 franchise licenses.[128] With the franchise model now well established in restaurants and retail, areas such as services, entertainment, and technology are expected to develop in the near future.

Direct franchising is usually used in domestic franchises. Overseas franchisors expanding into Vietnam have used a variety of franchising models, ranging from direct franchising methods (for example, multi-unit or development agreements) to master franchise agreements. Based on our experience, single-unit franchising methods are uncommon.

No specific laws in Vietnam encourage franchising. Franchising is governed by the Commercial Law,[129] along with the following implementing legal instruments:

- Decree 35/2006/ND-CP, as amended by Decree 120/2011/ND-CP and Decree 08/2018/ND-CP Decree 35;[130]
- Decree 98/2020/ND-CP;[131] and
- Circular 09/2006/TT-BTM, as amended by Circular 04/2016/TT-BTC.[132]

The Commercial Law vests control of the business operations with the franchisor, and the financial obligation to perform such business operations with the franchisee.[133] This arrangement can create a significant financial burden for the franchisee if the franchisor decides to change the layout or design of the operation outlet, resulting in a substantial change to the franchisee's financial obligations. Regulations do require the franchisor to inform its franchisees of any potentially consequential changes, but they do not provide legal means for franchisees to refuse the changes or escape from the resulting obligations.[134]

128. *See* Viet. Ministry of Ind. & Trade, https://www.moit.gov.vn/nhuong-quyen-thuong-mai1.
129. Law on Commercial No. 36/2005/QH11 passed by the National Assembly of Vietnam on 14 June 2005 [hereinafter Vietnam Commercial Law].
130. Decree 35/2006/ND-CP, as amended by Decree 120/2011/ND-CP and Decree 08/2018/ND-CP Decree 35 (May 15, 2020) [Viet.] [hereinafter Decree 35].
131. Decree 98/2020/ND-CP (Aug. 26, 2020).
132. Circular 09/2006/TT-BTM, as amended by Circular 04/2016/TT-BTC [Viet.].
133. Vietnam Commercial Law, art. 284.
134. *Id.* art. 8.2; *see also* Decree 35.

The offer and sale of franchises is also likely to trigger Vietnam's rules relating to mergers and acquisitions. Because no single body of legislation governs mergers and acquisitions, several areas of law (such as investment, company, competition, securities, tax, and foreign exchange law) may apply.[135] The ongoing relationship between a franchisor and franchisee is also likely to be affected by several areas of law, including intellectual property and contract law.[136]

The most recent Law on Competition, which took effect on July 1, 2019, contains a number of provisions that could potentially restrict franchising activities. It is especially restrictive of agreements that restrain technical or technological development, or agreements barring trade with outside parties, and prohibits various price fixing, supply, exclusivity, and other potentially competition-lessening arrangements if such agreements "have or potentially have the effect of significantly restricting competition in the market."[137]

The primary regulatory authority responsible for enforcing franchising laws and requirements in Vietnam is the Ministry of Industry and Trade (MOIT).[138] All franchising activities from overseas into Vietnam must first be registered with the MOIT before they are carried out.[139]

A. *Franchise Agreements*

When preparing to enter into a franchising agreement, which franchising regulations require to be made in Vietnamese,[140] the general rule is that franchisors and franchisees have the right to freely negotiate the terms and conditions of the franchise agreement, including their rights and obligations toward one another.[141]

The franchisor must provide a copy of the franchise agreement form and a franchise disclosure document to the proposed franchisee at least fifteen

135. Law on Investment No. 61/2020/QH14 passed by the National Assembly of Vietnam on 17 June 2020 [hereinafter Vietnam LOI]; Law on Enterprises No. 59/2020/QH14 passed by the National Assembly of Vietnam on 17 June 2020 [hereinafter Vietnam LOE]; Law on Competition No. 23/2018/QH14 passed by the National Assembly of Vietnam on 12 June 2018 [hereinafter Vietnam Competition Law]; Law on Securities No. 54/2019/QH14 passed by the National Assembly of Vietnam on 26 November 2019 [hereinafter Vietnam Law on Securities]; Law on Enterprise Income Tax No. 14/2008/QH12 passed by the National Assembly of Vietnam on 3 June 2008, as amended by Law No. 32/2013/QH13 dated 19 May 2013, Law No. 71/2014/QH13 dated 26 November 2014 and the LOI [hereinafter Vietnam LEIT]; Ordinance on Foreign Exchange Control No. 28/2005/PL-UBTVQH11 adopted by the Standing Committee of the National Assembly on 13 December 2005, as amended by Ordinance No. 06/2013/UBTVQH13 dated 18 March 2013 [hereinafter Vietnam Ordinance on Foreign Exchange Control].

136. Law on Intellectual Property No. 50/2005/QH11 passed by the National Assembly of Vietnam on 29 November 2005, as amended by Law No. 36/2009/QH12 and Law No. 42/2019/QH 14 [hereinafter together Vietnam IP Law]; Civil Code No. 91/2015/QH13 adopted by the National Assembly of Vietnam on 24 November 2015 [hereinafter Vietnam Civil Code].

137. Vietnam Competition Law art. 12.

138. *Id.* art. 4.1; Decree 35.

139. Vietnam Competition Law arts. 17, 18; Decree 35.

140. Vietnam Competition Law, art. 12; Decree 35.

141. Vietnam Civil Code arts. 3.2, 117.1(b).

business days before the signing of the agreement.[142] The franchise disclosure document should include general information on the franchisor (such as incorporation details), initial costs to be paid by the franchisee, rights and obligations of the franchisor and the franchisee, and a description of the franchise system.[143] However, it does not include any information on the franchisee.[144] In addition, the proposed franchisee is responsible for providing all reasonably requested information to the franchisor.[145] As for local sub-franchising, only the local sub-franchisor will be under these various regulatory obligations, rather than the overseas franchisor and IP owner.[146]

Non-compete covenants are not expressly prohibited by law and are commonplace in franchise agreements. However, enforcement of these covenants is relatively untested.

A franchisor can restrict a franchisee's freedom to sell, transfer, assign, or otherwise dispose of the franchised business. It is key to ensure that franchisors have a broad discretion to reject the sale, transfer, or assignment of the franchised business. Vigilance and responsiveness are equally important because Vietnamese law presumes that the franchisor has given its approval if it does not give a written response to the franchisee within fifteen days of receipt of a request for an assignment.[147]

Parties may freely decide on the payment of fees, such as franchisee or initial fees, continuing fees, and advertising contributions. Interest can be charged on overdue payments, and, if the governing law of the franchise agreement is Vietnamese law, the amount of interest that can be charged may be limited.[148]

B. *Intellectual Property*

The assignment of intellectual property rights is part of the franchising agreement terms and can thus be decided freely by the parties. Licenses for trademarks, industrial design rights, and patent rights can be registered with the Intellectual Property Office of Vietnam (IP Office). Under the Intellectual Property Law, a trademark license agreement is binding on the involved parties as well as third parties, even without recordal at the IP Office.[149] However, licenses for other industrial property rights, such as patents, must still be recorded with the IP Office to be legally binding on a third party.[150]

Vietnamese law does not have any specific definitions of *know-how*, but generally, business secrets are protected by law and by nature are not registered.[151]

142. Vietnam Competition Law, art. 8.1; Decree 35.
143. Circular 09, app. III.
144. See Appendix III of Circular 9 for the standard form of franchise disclosure document.
145. Vietnam Competition Law, art. 8.2; Decree 35.
146. Vietnam Competition Law, art. 8.3; Decree 35.
147. Vietnam Competition Law, art. 15.2; Decree 35.
148. Vietnam Civil Code arts. 357.2, 468.1.
149. Intellectual Property Law, art. 148.2 [Vietnam].
150. *Id.* art. 148.3.
151. *Id.* art. 6.3(c).

C. *Dispute Resolution*

For the settlement of disputes that may arise in relation to franchising operations, the Civil Code allows for a transaction involving at least one foreign organization to be governed by the laws of a foreign country if the parties so agree.[152] However, the foreign law must not be contrary to the "basic principles of Vietnamese law"—and in the past this phrase has been interpreted very broadly.[153] Even seemingly minor inconsistencies could render contract terms unenforceable. Therefore, choosing foreign law as the governing law requires that the franchise agreement be closely reviewed to ensure compliance with Vietnamese law.[154]

Foreign arbitral awards and some foreign court judgments can be enforced in Vietnam. As Vietnam is a member of the New York Convention, dispute resolution by foreign arbitration can be enforced in Vietnam if it is recognized by a Vietnamese court.[155] However, a foreign court judgment may be enforced in Vietnam on a treaty or reciprocal basis.[156] The particular dispute resolution forum thus needs to be selected carefully, as the choice of forum can greatly impact the chances of successfully enforcing an award against a local franchisee.

VII. Conclusion

As mentioned above, the franchising environment in mainland Southeast Asia has been growing ever more active, with the latest from the COVID-19 pandemic looking like it will not seriously impede this trend. While the laws of the region may sometimes seem like a patchwork to outside franchisors, each jurisdiction in fact has a well-worn legal path supporting franchisors, franchisees, and their business operations. Developments in recent years have indicated that the legal and regulatory framework for franchising is becoming increasingly formalized; for instance, Thailand's early 2020 regulations emphasizing trade competition practices in relation to franchising businesses, which had essentially already been in place, but were formally laid out as rules for franchisors and franchisees.

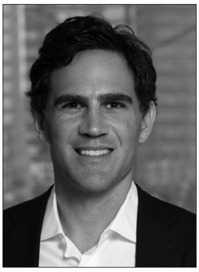
This trend seems likely to continue in Thailand and neighboring countries, as does the popularity of the franchising business model for doing business in mainland Southeast Asia.

152. Vietnam Civil Code art. 664.2.
153. *Id.* art. 670.1(a).
154. *Id.* arts. 664, 670.
155. Civil Procedure Code No. 92/2015/QH13, passed by the National Assembly of Vietnam on 25 Nov. 2015, as amended by Labor Code No. 45/2019/QH14 and Law on Enterprise No. 59/2020/QH14, art. 424.
156. *Id.* art. 423.

Franchising & Distribution Currents

*Matthew Gruenberg, David Harford & Vanessa Wheeler**

ARBITRATION



Mr. Gruenberg

Mr. Harford

Ms. Wheeler

***Jai Sai Baba LLC v. Choice Hotels International Inc.*, Bus. Franchise Guide (CCH) ¶ 16,837, 2021 WL 1049994 (E.D. Pa. Mar. 19, 2021)**

The U.S. District Court for the Eastern District of Pennsylvania granted a motion to compel arbitration and stay proceedings filed by a hotel franchisor and its related franchisee association, requiring that each franchisee plaintiff bring its claims in arbitration individually.

This case collectively involved the claims of ninety franchisees against a hotel franchisor, Choice Hotels, and its franchisee association. Each franchisee owned and operated one or more hotels under the Choice Hotels brand. The plaintiffs brought twenty-one claims for RICO, Sherman Act, and Civil Rights Act violations, breach of contract and fiduciary duty, common law fraud, and violations of various state franchise laws. Each plaintiff had entered into one or more franchise agreements with Choice Hotels, and all of the agreements included an identical binding arbitration clause that required arbitration in Maryland, and some of them also a class action waiver provision.

Defendants filed a joint motion to compel arbitration and stay proceedings based upon the mandatory arbitration provisions in each plaintiff's franchise agreement. Plaintiffs conceded the existence of the arbitration and class action waiver clauses, but argued that they were unenforceable because (1) plaintiffs could not vindicate their statutory claims with arbitrations' high fees and prehearing discovery limits; (2) the clauses were procedurally and substantially unconscionable

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where plaintiffs were in weaker bargaining positions and the clauses were offered on a take-it-or-leave-it basis; (3) the franchisee association had no right to enforce the arbitration clauses because it was a non-signatory and had duties to the franchisees that were independent of the franchise agreements; and (4) the class-action waiver was not in all the franchise agreements and its enforcement against all franchisees would prevent them from vindicating their claims.

Defendants argued that the arbitral discovery limits did not prevent plaintiffs from pursuing their claims and that the arbitration fees were not unreasonable. They further argued that arbitration clauses were not unconscionable where the franchisees were sophisticated business entities that had opportunity to negotiate the terms of the franchise agreement. As to the franchisee association, defendants acknowledged that it was not a signatory to the arbitration provisions, but asserted that it could enforce them nonetheless because of its close relationship with Choice Hotels, the fact that plaintiffs' claims against the association arose from the franchise agreements, and that the alleged conduct underlying plaintiffs' claims was the same for each defendant. Finally, defendants asked that the court require plaintiffs to arbitrate their claims individually because two thirds of the franchise agreements contained the class action waiver and the rest were silent on the issue.

The court sided with the defendants on each issue. Following the rulings of other courts, the court held that the claims were arbitrable and that the discovery limitations were mutual and did not completely foreclose discovery. It further held that plaintiffs had not shown any inability to pay the arbitration costs required. The court was also unpersuaded that the provisions were unconscionable, ruling that the plaintiffs were sophisticated businesses, had an opportunity to obtain legal advice, and were not prevented by the provisions from pursuing their claims. Having determined that the arbitration provisions were valid and enforceable, the court held that they applied to the claims against the franchise association as well under equitable estoppel principles because such claims arose from the franchise agreements. Finally, because plaintiffs had not shown that the arbitration or class waiver provisions were unconscionable, the court required that each plaintiff arbitrate its own claim separately.

***Sashital v. Seva Beauty, LLC*, Bus. Franchise Guide (CCH) ¶ 16,847, 2021 WL 1222895 (N.D. Ill. Mar. 31, 2021)**

This case is discussed under the topic heading "Injunctive Relief."

***Williams v. Planet Fitness, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,849, 2021 WL 1165101 (N.D. Ill. Mar. 26, 2021)**

The U.S. District Court for the Northern District of Illinois dismissed the claims of two Planet Fitness customers seeking to represent classes of gym members who were charged membership fees in March 2020, but then were barred from entry after the COVID-19 pandemic forced the gyms to shut down.

Jason Williams was a member of a Planet Fitness gym in Chicago. Gunnar Amos was a member of a Planet Fitness gym in Coeur d'Alene, Idaho. Each entered into a membership agreement with their local Planet Fitness franchisee and paid monthly dues of about $10 under those agreements. Williams's two-page membership agreement included a "dispute resolution provision" stating:

"(J) Dispute Resolution: In the unlikely event that Planet Fitness and/or PF Corporate is unable to resolve a complaint you may have to your satisfaction (or is unable to resolve a dispute with you after attempting to do so informally), we each agree to resolve such disputes through binding arbitration or small claims court rather than a court of general jurisdiction. For simplicity and fairness, arbitration will be conducted on an individual basis in accordance with the American Arbitration Association's rules for consumer arbitration. By signing this agreement, you acknowledge and agree that you, Planet Fitness, and PF Corporate are each waiving the right to a trial by jury and the right to participate in a class action, either in court or in arbitration. Nothing in this clause limits Planet Fitness and/or PF Corporate from seeking preliminary injunctive relief from a court in aid of arbitration. This Dispute Resolution provision shall apply to this contract unless, within thirty (30) days of signing this contract, you notify Planet Fitness in writing that you reject this provision."

Amos's membership agreement did not include an arbitration provision. Both plaintiffs paid their monthly fee on March 17, 2020. The next day, Planet Fitness temporarily closed all its corporate stores in response to the COVID-19 pandemic and encouraged all its franchisees to do the same. On March 30, 2020, Planet Fitness extended the closure of its facilities and indefinitely suspended operations of both franchise and corporate locations. Planet Fitness did not provide refunds; it offered to credit members' bills or to extend their existing memberships, if, and when, they reopened.

Williams sued Planet Fitness and the franchisee that owned his gym asserting claims on behalf of a putative Illinois sub-class for violations of the Illinois Consumer Fraud and Deceptive Business Practices Act and for violations of the Illinois Physical Fitness Services Act. Amos sued Planet Fitness on behalf of a putative Idaho sub-class for violations of the Idaho Consumer Protection Act. Both sued for breach of contract, unjust enrichment, conversion, and declaratory judgment. Amos, however, did not name the franchisee that owned his gym as a defendant. The defendants moved to compel arbitration and dismiss the claims of Williams for improper venue under Rule 12(b)(3); and to dismiss the claims of Amos for failure to join an indispensable party under Rule 12(b)(7).

Williams opposed the motion, arguing that the arbitration clause was unconscionable. Williams claimed the arbitration provision was procedurally unconscionable because it was inconspicuously "buried in fine print at the bottom of the membership contract." The court rejected this argument because the whole contract was only two pages, the arbitration clause appeared in the same font as the rest of the agreement, and the clause was located under the heading "Dispute Resolution." Williams argued the arbitration provision was substantively unconscionable because it required informal dispute resolution without specifying the informal procedure and because Planet Fitness did not attach the AAA's consumer arbitration rules to the agreement. The court disagreed, finding that the AAA rules are easy to locate on the Internet and that there is no legal requirement that an arbitration provision specify an informal dispute resolution procedure in order to make the requirement to arbitrate binding. Upon determining that the agreement was enforceable and covered the dispute, the court dismissed Williams's claims rather than staying them pending completion of arbitration.

The court granted the motion to dismiss Amos's claims because he had not named "the sole counter-party" to his agreement: the franchisee that owned the Planet Fitness franchise in Coeur d'Alene, Idaho. Analyzing the issue under Federal Rule of Civil Procedure 19, the court found that the franchisee was both a necessary and indispensable party. The franchisee was necessary because it had an interest in the outcome of the case, but the court could not join it as a party. Amos sought a judicial declaration that his membership agreement with the franchisee was "void or voidable." Joinder was not possible because the court had no grounds to assert personal jurisdiction over the franchisee. The franchisee was an Idaho based limited liability company. It did not conduct any business in Illinois, did not have any employees or maintain any real property in Illinois, and its interactions with Amos occurred only in Idaho.

The court held that the franchisee was an indispensable party. It found that a judgment rendered in the absence of the franchisee's participation could be prejudicial to it, and the court could not tailor its judgment in the case to alleviate that prejudice. The court found that a judgment rendered in the absence of the franchisee would be inadequate because Amos would have to file new case against the franchisee in Idaho order to enforce it. The court also found that Amos could pursue his claims in Idaho. Because the court concluded that all these factors weighed heavily in favor of refusing to proceed without the franchisee, it dismissed Amos's claims without prejudice.

CHOICE OF FORUM

Adventure Park Hamilton, LLC v. UATP Management, LLC, Bus. Franchise Guide (CCH) ¶ 16,845, 2021 WL 2396580 (N.J. Super. Ct. Mar. 25, 2021)

The Superior Court of New Jersey dismissed for lack of personal jurisdiction all of franchisees' claims against a franchisor and individual defendants based upon a valid forum selection clause in each franchise agreement and a failure to show that any alleged misconduct was linked to New Jersey.

This action arose out of franchisee agreements that three current franchisees and one former franchisee entered into with UATP Management, to operate Urban Air-branded indoor adventure parks in each of their respective territories. One franchise location was in New Jersey, but the franchisee never operated. The other three franchise locations were in other states. Each agreement contained a forum selection clause requiring any and all claims to be brought in Texas, the state in which UTAP Management maintained its principal place of business.

The plaintiffs filed suit in the Superior Court of New Jersey on October 20, 2020, alleging that UATP Management fraudulently induced each plaintiff to enter into the franchise agreements and then breached the franchise agreements with each respective plaintiff.

UATP Management and the three individual defendants moved to dismiss the claims for lack of personal jurisdiction. The defendants argued that the claims had to be brought in Texas pursuant to the forum selection clause in each of the relevant franchise agreements. The plaintiffs asserted that the forum selection clauses were invalid under the New Jersey Franchise Practices Act (NJFPA). The court held that the NJFPA did not apply because the franchises did not meet the three requirements for the NJFPA: (1) the franchise agreement contemplates or requires the establishment or maintenance of a place of business in New Jersey; (2) $35,000 or more in gross sale of products or services between the franchisor and franchisee in the twelve months preceding the action; and (3) more than twenty percent of the franchisees' gross sales are or are meant to be derived from the franchise.

The court found that the franchisees could not individually meet the requirements and could not combine their claims in a way that would allow them to meet the requirements together, so the forum selection clauses had to be enforced. The court also held that it had no personal jurisdiction over the individual defendants because the defendants resided in Texas and plaintiffs had not alleged sufficient facts to show that the defendants' alleged misrepresentations were in any way connected to New Jersey. The Court dismissed all claims.

***Universal Property Services, Inc. v. Lehigh Gas Wholesale Services, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,863, 2021 WL 1720866 (D.N.J. Apr. 30, 2021)**

The U.S. District Court for the District of New Jersey granted in part and denied in part motions to dismiss a gas station franchisee's statutory and common law claims for fraud and misrepresentation and violations of the Florida Deceptive and Unfair Trade Practices Act, the Florida Franchise Act, the Petroleum Marketing Practices Act, and Florida state law.

In 2018, plaintiffs entered into seventeen supply agreements and leases with Circle K, along with seventeen franchise agreements with TMC Franchise Corp., for franchised gas station and convenience store locations in Florida. In 2020, plaintiffs sued Circle K and TMC for thirteen claims related to violations of the Florida Deceptive and Unfair Trade Practices Act, the Florida Franchise Act, and common law fraud. Plaintiffs also sued

Lehigh Gas, which became involved after Circle K assigned it certain rights in 2019, for breach of contract, violation of the Petroleum Marketing Practices Act (PMPA), permanent injunction, and declaratory relief.

In response, the defendants filed three separate motions to dismiss. Lehigh Gas moved to dismiss based on lack of personal jurisdiction, improper venue, and failure to state a claim, relying heavily on a provision in the PMPA that authorizes a franchisee to file suit in either (1) the district of the franchisor's principal place of business, or (2) the district in which the franchisee conducts business. Circle K and TMC moved to dismiss the plaintiffs' common law fraud claims and Florida statutory claims, in part on the basis that the parties' supply and lease agreements contained a Pennsylvania choice of law provision. The court denied Lehigh Gas's motion to dismiss as to jurisdiction and determined that the Pennsylvania choice of law provision only applied to contract claims. However, the court requested supplemental briefing on whether Pennsylvania or New Jersey law should apply to the plaintiffs' tort claims based on an evaluation of which state had the most significant relationship.

On Circle K's motion, the court determined that New Jersey law governed the common law fraud and misrepresentation claims, as the parties agreed that New Jersey had the most significant relationship to the claims. The court dismissed the fraud, fraudulent concealment, and negligent misrepresentation claims, but granted plaintiffs' leave to file an amended complaint.

Lehigh Gas moved to dismiss the plaintiffs' claims on the basis that venue was improper, that the requests for injunctive and declaratory relief were duplicative and moot, and that the claim of punitive damages was not sufficiently pled. Because the plaintiffs had already voluntarily surrendered their franchised locations at the time of the ruling, the court dismissed the claims for declaratory and injunctive relief as moot. The court also dismiss plaintiffs' claim for punitive damages, finding that plaintiffs did not oppose the motion to dismiss on that ground. However, the court refused to dismiss plaintiffs' claims for improper venue, holding that the language of the venue provision in the PMPA was permissive rather than mandatory and that plaintiffs properly alleged that they did business in New Jersey.

CHOICE OF LAW

***Purugganan v. AFC Franchising, LLC*, Bus. Franchise Guide ¶ 16,824, 2021 WL 723916 (D. Conn. Feb. 24, 2021)**

This case is discussed under the topic heading "Definition of Franchise."

***Universal Property Services, Inc. v. Lehigh Gas Wholesale LLC*, Bus. Franchise Guide (CCH) ¶ 16,863, 2021 WL 1720886 (D.N.J. Apr. 30, 2021)**

This case is discussed under the topic heading "Choice of Forum."

CLASS ACTIONS

Caddick v. Tasty Baking Co., Bus. Franchise Guide (CCH) ¶ 16,854, 2021 WL 1374607 (E.D. Pa. Apr. 12, 2021)

The U.S. District Court for the Eastern District of Pennsylvania preliminarily approved a class-wide settlement of a wage and hour class action brought by distributors alleging that Tasty Baking had misclassified them as independent contractors under federal and state law and seeking unpaid overtime wages and reimbursement for deductions.

Tasty Baking is in the business of manufacturing, distributing, and selling baked goods. Plaintiffs each individually entered into distributor agreements with Tasty Baking in order to sell and distribute Tasty Baking products in Pennsylvania, New Jersey, and Maryland. Under the agreements, Tasty Baking sets product prices, negotiates retail pricing and merchandising, modifies orders, and dictates how distributors stock product and engage in marketing. Plaintiffs were each classified as an independent contractor by Tasty Baking, but they assert that they qualified as employees of Tasty Baking due to the amount of control Tasty Baking exercised over their businesses.

On May 15, 2019, plaintiffs filed claims for unpaid overtime under the Fair Labor Standards Act (FLSA) and reimbursement for improper pay deductions under Pennsylvania law, as well as for expenses on an unjust enrichment claim. The court dismissed the unjust enrichment claim shortly thereafter. On January 24, 2020, the court granted conditional certification of the class under the FLSA that consisted of any person who had entered performed work as a distributor under a distribution agreement with Tasty Baking in the three years prior to the filing of the action. A subsequent related action was filed by one of the plaintiffs in the U.S. District Court for the District of New Jersey, alleging similar claims against Tasty Baking under the New Jersey Wage and Payment Law, and the cases were consolidated.

After negotiations, the parties reached a settlement for a class including any person that worked under a Tasty Baking distributor agreement without an arbitration clause in a warehouse in Pennsylvania, New Jersey, or Maryland. The settlement would create a fund of $3,150,000 to cover payouts to class members and attorney fees. The settlement also provided for a payment to current distributors who entered into arbitration agreements with class action waiver provisions.

To attain preliminary approval of the settlement, the parties had to show that the class qualified for certification and that the settlement agreement was "fundamentally fair, reasonable, and adequate." The court agreed that the class qualified for certification because it (1) had over forty potential members in each state; (2) had two common questions related to whether distributors had been misclassified as independent contractors and whether Tasty Baking had violated labor laws; and (3) the class representatives were typical and adequate because they faced the same issues as all other class members, there were no unique defenses, and there was no evidence the class members were antagonistic to other members. The court also approved the settlement itself because it met all the relevant factors: namely, it was an arm's length negotiation in which the representatives expended significant time and effort; it balanced the settlement amounts with the risk to representatives, the ability of members to opt out, and a fair allocation of attorney fees; it provided a fair calculation for payments; the additional terms, such as an arbitration clause for the settlement agreement, were not oppressive; the case presented a bona fide dispute; and the settlement would not frustrate the purposes of the FLSA, so long as the confidentiality provision in it allows plaintiffs to discuss the terms of settlement with other Tasty Baking distributors. On those grounds and conditions, the court approved the settlement.

***Fleming v. Matco Tools Corp.*, Bus. Franchise Guide (CCH) ¶ 16,818, 2021 WL 673445 (N.D. Cal. Feb. 21, 2021)**

The U.S. District Court for the Northern District of California granted in part and denied in part a motion to certify a class in a wage and hour class action alleging that Matco Tools Corp. misclassified distributers as independent contractors when they were actually employees under California law.

The case involved claims made by John Fleming, who served as a Matco franchisee and distributor of Matco products from 2012 through 2018. Franchisees typically paid an initial franchise fee to Matco, agreed to operate pursuant to a distributorship agreement, and were granted the right to sell Matco tools through Matco's system. They were required to attend an intensive training program, lease or buy a Matco truck from which to sell Matco tools, license and use a Matco-approved software system, allow Matco to inspect their truck during business hours, wear Matco uniforms, comply with Matco sales and marketing programs, and attend at least eighty percent of Matco district sales meetings. Matco did not have any time tracking procedures or requirements, did not reimburse franchisees for business expenses, and classified them as independent contractors.

Fleming terminated his franchise and distributor agreement in 2018. He subsequently filed a lawsuit alleging that Matco misclassified him as an independent contractor to avoid a bevy of obligations, including the following: (1) reimbursing him for his business expenses; (2) paying overtime for working over forty hours a week or eight hours a day; (3) providing off-duty meal times; (4) authorizing paid breaks; (5) providing accurate wage statements; (6) paying all wages due on termination; and (7) recognizing unlawful collection of earned wages. Fleming sought class certification under Federal Rule of Civil Procedure 23(b)(3) for all signatories to franchise distributor agreements in California that personally operated a mobile store in the four years prior to the filing of the lawsuit.

Class certification requires satisfaction of four threshold requirements: (1) the joinder of all members is impractical due to the size of the class;

(2) common questions of law or fact exist; (3) representative parties' claims or defenses are typical of the class; and (4) the interests of the class will be adequately and fairly protected by the representative parties. The court determined that the first requirement was satisfied because Fleming showed there were 288 potential class members, and the Ninth Circuit generally accepts numerosity as being met for any proposed class with forty or more members. Matco did not dispute that the second requirement was met.

As to the third and fourth requirements, Matco argued that Fleming was neither typical nor adequate as a representative. Matco's argument stemmed largely from the fact that Fleming was a former franchisee, which some courts have held are not adequate representatives for current franchisees, that franchisees from 2019 and 2020 were subject to arbitration provisions, and that many of Matco's franchisees were happy with their status as independent contractors. However, the court determined that the most important question for these requirements was whether Fleming's claims were co-extensive with other class members', which Matco did not dispute. The court also held that additional questions, like those surrounding arbitration, were not significant enough to prevent certification.

Additionally, plaintiff must show that separate actions would create a substantial risk of prejudice, that it would be appropriate to grant declaratory or injunctive relief to the class as a whole, and/or that a class action would be the best method for adjudicating the claims and common questions of fact or law predominate. In determining that common questions of law and facts predominate, the court decided that the ABC test was proper when looking at whether franchisees were improperly classified as independent contractors. The ABC test states that an individual will be considered an employee unless the hiring party can meet three requirements: (1) the hiring party does not control or direct the individual under the terms of the contract or in fact; (2) the individual's work is outside of the hiring party's usual course of business; and (3) the individual is typically involved in an independent trade, career, or business similar to the one being done for the hiring party. Under the ABC test, the court determines that franchisees will likely be similarly situated and have common issues of fact and law because their franchise agreements, which govern their operation as franchisees, are substantially similar. Alternatively, the court found that common questions would also predominate under the *Borello* test, because it also focuses on questions of control that will be substantially similar for franchisees in connection with their franchise agreements.

Based on these findings, the court held that common questions predominated as to the misclassification claim, for which it granted class certification. The court similarly found that common questions predominated as to Fleming's expense reimbursement claim, because Matco has a global policy against reimbursing distributors' expenses; and as to the wage statement penalty and UCL claims (as to reimbursement for business expenses), because the parties agree that they largely derived from the misclassification issue.

Conversely, the court found that individual questions predominate on Fleming's overtime, meal and rest break, and waiting time claims, as well as Fleming's wage deduction claims. In evaluating the overtime, meal/rest break, and waiting time claims, the court focused primarily on Matco's affirmative defense that the claims are barred by the outside sales exemption, which relieves employers of the need to pay overtime or provide meal and rest breaks where the "employee" is an outside salesperson who spends the majority of his or her time working outside of the employer's place of business. The court found that Matco had a persuasive argument that at least some of its franchisees, who engage in both sales and non-sales activities, would be subject to the exemption. Because the exemption must be applied case-by-case under California law, the court held that individual questions, not common questions would predominate. The court found similarly for the wage deduction claims, but largely because Fleming had the burden of proof and barely addressed it.

Finally, the court considered whether a class action was the superior method of adjudicating the claims raised by Fleming and determined that it was. Matco argued that it was not the superior model because (1) franchisees' significant investment in their businesses gave them an interest in controlling their own cases; and (2) some class members might not want to join the class or bring claims at all because they are satisfied with the business model. The court was unpersuaded by these arguments, holding that disagreement among class members was an insufficient basis to deny certification and that class members were always able to opt out.

The court ultimately granted the motion to certify the class on the issues of misclassification and claims related to reimbursement of business expenses, wage statements, and the California Unfair Competition Law. It denied the motion as to claims related to overtime, breaks, waiting time, and wage deduction.

***Jai Sai Baba LLC v. Choice Hotels Int'l Inc.*, Bus. Franchise Guide (CCH) ¶ 16,837, 2021 WL 1049994 (E.D. Pa. Mar. 19, 2021)**
This case is discussed under the topic heading "Arbitration."

***Sashital v. Seva Beauty, LLC*, Bus. Franchise Guide (CCH) ¶ 16,847, 2021 WL 1222895 (N.D. Ill. Mar. 31, 2021)**
This case is discussed under the topic heading "Injunctive Relief."

CONTRACT ISSUES

***Casco, Inc. v. John Deere Construction & Forestry Co.*, Bus. Franchise Guide (CCH) ¶ 16,826, 990 F.3d 1 (1st Cir. Mar. 2, 2021)**
This case is discussed under the topic heading "Termination and Nonrenewal."

***Jai Sai Baba LLC v. Choice Hotels Int'l Inc.*, Bus. Franchise Guide (CCH) ¶ 16,837, 2021 WL 1049994 (E.D. Pa. Mar. 19, 2021)**
This case is discussed under the topic heading "Arbitration."

***Maaco Franchisor SPV, LLC v. Cruce*, Bus. Franchise Guide (CCH) ¶ 16,822, 2021 WL 706424 (W.D.N.C. Feb. 23, 2021)**

The U.S. District Court for the Western District of North Carolina entered an order for default and summary final judgment in favor of Maaco Franchisor SPV, LLC for over $1.5 million in damages, interest, attorneys' fees, costs, and expenses for breach of contract by a former franchisee and its two principals.

In August 2013, Cruco Production Auto Painting, Inc. (Cruco) entered into a franchise agreement with the plaintiff franchisor's predecessor-in-interest for the operation of a Maaco-branded automobile maintenance and repair center in Tucson, Arizona. Cruco entered into a second franchise agreement with the franchisor in May 2014. William and Marilyn Cruce, Cruco's principals, personally guaranteed all obligations under both the agreements. The second franchise agreement, as amended, included a fifteen-year term from July 7, 2014, to July 7, 2029.

In October 2013, the franchisor entered into two franchise agreements with Justin and Linda Vigil for franchise locations in Albuquerque, New Mexico. The Vigils assigned their rights and obligations under those franchise agreements to the Cruces in September 2014. All four of the franchise agreements required the defendants to continuously operate and to pay royalties and fees weekly. Between August 29, 2014, and August 6, 2015, the Cruces executed three promissory notes in connection with the franchise agreements in favor of the franchisor, in the principal amounts of $140,074.33, $137,779.61, and $162,074.24 respectively, as well as a security agreement.

The Cruces and Cruco failed to pay all of the weekly royalties and fees. They further closed all of their Maaco locations on or about April 4, 2017, with no intention of reopening. The franchisor sued Cruco, as well as the Cruces individually, for breach of the franchise agreements, the guaranties, the promissory notes, and the security agreement. Plaintiff properly served defendants, but they failed to respond or otherwise defend against the action, and the court entered an order of default against defendants. The franchisor sought unpaid royalties and fees during the operation period of each location, lost future royalties and fees for an additional three years for each location, attorneys' fees and cost, and prejudgment interest. Plaintiff then moved for default and summary final judgment on liability and its damages.

In connection with its motion, the franchisor provided the court with evidence of the agreements, as well as affidavits and exhibits related to the defendants' payment history to support the damages. The court found on the undisputed evidence that the franchisor was entitled to a default judgment on liability and that no separate hearing on damages was necessary. It held that the damages owed to the point of termination was liquidated and supported by uncontroverted evidence.

For the lost future profits, the court applied a three-part test: (1) whether there is reasonable certainty that the profits would have been obtained but for the breach; (2) whether there is reasonable certainty as to the amount of the profits; and (3) whether the profits were reasonably foreseeable at the time of contract as damages in the event of breach. Based on historical data showing the profits arising from defendants' operation of the locations pre-closure, the court determined that both the amount and the breach as the cause of the lost profits were reasonably certain. The court further found that the fifteen-year term, the exclusivity of the territories, and the binding nature of the agreement made the lost profits reasonably foreseeable. Finally, the court held that the plaintiff had provided sufficient evidence that it would take, on average, three years to re-franchise the locations to show that it had mitigated its damages under North Carolina law by limiting lost profits to three additional years.

***McNeel v. Kiddie Academy Domestic Franchising, LLC*, Bus. Franchise Guide (CCH) ¶ 16,830, 2021 WL 920108 (S.D. Tex. Mar. 10, 2021)**
This case is discussed under the topic heading "Vicarious Liability."

***Purugganan v. AFC Franchising, LLC*, Bus. Franchise Guide ¶ 16,824, 2021 WL 723916 (D. Conn. Feb. 24, 2021)**
This case is discussed under the topic heading "Definition of Franchise."

COVID-19

***Williams v. Planet Fitness, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,849, 2021 WL 1165101 (N.D. Ill. Mar. 26, 2021)**
This case is discussed under the topic heading "Arbitration."

***La Simple Co., Ltd. v. SLP Enterprises, LLC*, Bus. Franchise Guide (CCH) ¶ 16,864, 2021 WL 1648762 (D. Mass. Apr. 27, 2021)**
This case is discussed under the topic heading "Injunctive Relief."

DAMAGES

***Casco, Inc. v. John Deere Construction & Forestry Co.*, Bus. Franchise Guide (CCH) ¶ 16,826, 990 F.3d 1 (1st Cir. Mar. 2, 2021)**
This case is discussed under the topic heading "Termination and Nonrenewal."

***Maaco Franchisor SPV, LLC v. Cruce*, Bus. Franchise Guide (CCH) ¶ 16,822, 2021 WL 706424 (W.D.N.C. Feb. 23, 2021)**
This case is discussed under the topic heading "Contract Issues."

***Mount Holly Kickboxing, LLC v. FranChoice Inc.*, Bus. Franchise Guide (CCH) ¶ 16,839, 2021 WL 1117968 (D. Minn. Mar. 24, 2021)**
This case is discussed under the topic heading "Fraud."

DEFINITION OF FRANCHISE

***Adventure Park Hamilton, LLC v. UATP Management, LLC*, Bus. Franchise Guide (CCH) ¶ 16,845, 2021 WL 2396580 (N.J. Super. Ct. Mar. 25, 2021)**

This case is discussed under the topic heading "Choice of Forum."

***Purugganan v. AFC Franchising, LLC*, Bus. Franchise Guide ¶ 16,824, 2021 WL 723916 (D. Conn. Feb. 24, 2021)**

The U.S. District Court for the District of Connecticut denied a franchisor's motion to dismiss based on lack of Article III standing, but granted in full the franchisor's motion for partial judgment on the pleadings.

AFC Franchising, LLC's (AFC) and Danilo Purugganan (Plaintiff) were parties to a Master Development Agreement (MDA) pursuant to which AFC granted Plaintiff the right to (1) develop and operate Doctors Express Urgent Care Businesses in a specified territory; (2) assist AFC with the sale of franchises to third parties who would operate and/or manage Doctors Express Urgent Care Businesses in the territory; and (3) perform certain initial and ongoing support and assistance functions and monitor the performance of franchisees of in the territory. In response to AFC's pending purchase of certain urgent care franchises in Plaintiff's territory, Plaintiff brought a series of claims against AFC. In response, AFC filed a motion to dismiss based on lack of Article III standing and, alternatively, filed a motion for partial judgment of the pleadings.

As a preliminary matter, and in response to Plaintiff's allegation that he would suffer economic losses if AFC closed on the purchase of certain urgent care franchises in Plaintiff's territory, AFC first moved to dismiss Plaintiff's Sherman Act, tortious interference, Connecticut Franchise Act (CFA), Connecticut Unfair Trade Practice Act (CUPTA), and abuse of process claims for lack of subject matter jurisdiction. Specifically, AFC argued that Plaintiff's allegations of damages were too speculative and, therefore, Plaintiff lacked standing. However, the court determined that the harm that Plaintiff alleged was "sufficiently imminent" at the time that the complaint was filed. Although the closings had not occurred at the time that the suit was filed, the transactions were underway, providing standing to bring claims based on AFC's alleged breach of the MDA, and Plaintiff's anticipated losses. Therefore, the court denied AFC's motion to dismiss for Plaintiff's purported lack of Article III standing.

AFC alternatively moved for judgment on the pleadings on Plaintiff's Sherman Act, tortious interference, CFA, CUPTA, and abuse of process claims. As a threshold matter, the court next determined that Maryland law governed the dispute between AFC and Plaintiff. The court upheld the MDA's choice of law provision because Doctors Express Franchising, LLC (Doctors Express), AFC's predecessor in interest, was located in Maryland at the time that Doctors Express and Plaintiff executed the MDA. The court found Doctors Express's connection to Maryland sufficient to establish a substantial relationship between Maryland and one of the original contracting parties. As a result, the choice of law provision precluded Plaintiff from bringing a CUTPA claim under Connecticut law. The court rejected Plaintiff's argument that CUPTA is a public policy statute and, as such, could not be waived by the choice of law provision in the MDA due to Plaintiff's failure cite any authority in support of its proposition. Therefore, the court granted judgment in favor of AFC on Plaintiff's CUPTA claim.

In response to Plaintiff's allegation that AFC improperly terminated his rights under the MDA violating the CFA, AFC argued that "the CFA does not apply because [Plaintiff] is not a franchisee, but rather a master developer who assists in the identification of prospective franchisees and supervises those franchisees that AFC under its system." Agreeing with AFC, the court found that the MDA did not meet the first element of a "franchise" under Connecticut law because Plaintiff did not "have the right to offer, sell or distribute goods or services" under AFC's trademarks. The MDA did not grant Plaintiff the right to operate or grant other the right to operate Doctors Express Urgent Care Businesses or use or grant others the right to use AFC's trademark or system. Rather, Plaintiff was authorized to "solicit, evaluate, and screen individuals and entities to establish and operate Franchises within the Territory," subject to AFC's approval of prospective franchisees. The court concluded that Plaintiff acted more as an agent of the AFC, rather than a franchisee, and granted judgment on the pleadings in favor of AFC.

The also court granted judgment on the pleadings in favor of AFC on Plaintiff's Sherman Act claim, breach of the covenant of good faith and faith dealing, promissory estoppel, violation of the Uniform Commercial Code, tortious interference, and abuse of process claims, finding that the allegations generally did not meet the elements necessary for those causes of action.

EARNINGS CLAIMS

***Mount Holly Kickboxing, LLC v. FranChoice Inc.*, Bus. Franchise Guide (CCH) ¶ 16,839, 2021 WL 1117968 (D. Minn. Mar. 24, 2021)**

This case is discussed under the topic heading "Fraud."

FRAUD

***Mount Holly Kickboxing, LLC v. FranChoice Inc.*, Bus. Franchise Guide (CCH) ¶ 16,839, 2021 WL 1117968 (D. Minn. Mar. 24, 2021)**

The U.S. District Court for the District of Minnesota granted summary judgment in favor of franchise consultant, FranChoice, and one of its employees, on a franchisee's claims arising out FranChoice recommending that the franchisee consider investing in an iLoveKickboxing.com franchise.

The plaintiff, Dhyan Tarver, was a West Point graduate with an MBA degree. Since his honorable discharge from the Army in 2011, he had worked a full-time job in sales and operated his own real estate investment business. A friend referred him to FranChoice in August 2016 after Tarver expressed an interest in investing in a franchise. Tarver told one of FranChoice's consultants that he was looking for a franchise that worked on an absentee owner model and would not require his fulltime presence. He did not want to quit his full-time job to operate a franchise. The consultant identified three potential franchise systems to Tarver, told him about each one, and then had each of these franchisors contact Tarver directly. One of these potential opportunities was iLoveKickboxing.com.

Tarver claimed that FranChoice's consultant made numerous misrepresentations about iLoveKickboxing.com while recommending the franchise to him. He claimed the consultant said iLoveKickboxing.com franchises were suitable for absentee or semi-absentee ownership, which meant that Tarver would only have to work a few hours a week. Tarver claimed that FranChoice told him that the maximum cost to start the franchise was $275,000, that other franchisees made monthly profits ranging from $10,000 to $20,000, that there were no struggling franchisees, the plaintiff only needed 200 members to break even, and that franchise locations broke even before their grand openings. Tarver claimed FranChoice told him the franchisor handled all the marketing, the franchisor worked well with franchisees and is very responsive, and that no franchise locations had ever closed. Tarver also claimed that FranChoice's consultant recommended that he form a business entity to operate his franchise.

Before purchasing an iLoveKickboxing.com franchise, Tarver conducted his own investigation of the opportunity by reviewing iLoveKickboxing.com's franchise disclosure document, participating in a discovery day, and speaking to current franchisees. Contrary to what Tarver claims he heard from FranChoice, the disclosure document listed several iLoveKickboxing.com franchises that had closed.

Tarver nonetheless entered into a franchise agreement with iLoveKickboxing.com in October 2016. He opened his franchise in Charlotte, North Carolina in June 2017. After operating the studio for about a year and a half, Tarver closed the studio because he claimed that too few people had signed up for memberships and that the franchise was not suitable for absentee ownership.

Tarver and the entity he had formed to operate the franchise, Mount Holly Kickboxing (Mount Holly), sued FranChoice for fraud, negligent misrepresentation, violation of the New York Franchise Sales Act, and violation of the North California Unfair and Deceptive Trade Practices Act.

In its summary judgment motion, FranChoice first argued that Mount Holly had no standing to sue because FranChoice had not made any representations to the entity. The court rejected this argument because there was evidence that Tarver had informed FranChoice of his intent to form an LLC to operate his franchise.

FranChoice also attacked the merits of each claim. The court held that Tarver's claims for fraud, negligent misrepresentation, and violation of the

New York Franchise Sales Act failed because Tarver and Mount Holly had not presented evidence of an actionable misrepresentation or his reasonable reliance on such a representation. The court found that Tarver and Mount Holly had not provided any evidence that the majority of the alleged misrepresentations were false when FranChoice conveyed them to him in 2016.

The court found that FranChoice had made a misrepresentation when its consultant stated that no franchises had closed, but that the plaintiff could not have reasonably relied upon that statement because the disclosure document disclosed that several franchise locations had closed.

With respect to his claim for violation of the North California Unfair and Deceptive Practices Act, Tarver asserted his claim was not based upon representations about iLoveKickboxing.com. Instead, he argued that the claim relied upon claims made on the FranChoice website that led him to believe that FranChoice would only present him with franchise opportunities that passed FranChoice's "exacting standards." Specifically, Tarver pointed to statements on the website asserting that FranChoice would present him "only with franchises that were safe, stable, and high-quality" and that he would have "all of the information that [he] needed about a franchise, particularly with respect to litigation and potentially adverse information." The court rejected this theory because it found that the complaint did not provide fair notice of this theory of liability. The court also rejected this theory on the merits finding that each alleged representation was puffery, was a true statement, or both.

***MTR Capital, LLC v. LaVida Massage Franchise Development, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,861, 2021WL 1626353 (E.D. Mich. Apr. 27, 2021)**

Applying Florida law, the U.S. District Court for the Eastern District of Michigan denied the parties' cross motions to alter or amend the final judgment and the plaintiff's motion for attorney fees.

Plaintiff MTR Capital, LLC (MTR) sued LaVida Massage Franchise Development, Inc. (LaVida) and several individual employees over a failed franchise venture in which MTR claimed that LaVida fraudulently induced it to engage. The parties participated in a four-day bench trial, in which plaintiff argued that LaVida had engaged in several violations of the Florida Deceptive and Unfair Trade Practices Act (FDUPTA) and the Florida Franchise Act (FFA). MTR prevailed on a single claim: that the defendants' failure to provide MTR with an updated and accurate franchise disclosure document (FDD) constituted an unfair and deceptive act under the FDUTPA. The court awarded MTR $39,000 in damages, which was the amount it originally paid as a franchise fee.

Both parties filed motions to alter or amend the judgment. MTR argued that it should have prevailed on all of its claims, including that defendants had violated the FFA and had made other statements that constituted violations of the FFA and FDUTPA, and that it was entitled to greater damages, for which the individual defendants should be held jointly liable. Defendants conversely asserted that (1) the failure to provide an updated FDD was not an unfair or deceptive act; and (2) the damages award was too high, as the failure to provide an updated FDD had not rendered the franchise valueless. The defendants also argued that the court should not have awarded damages against all the defendants jointly, claiming that plaintiff did not submit sufficient evidence that the individual defendants had directly engaged in any misconduct.

The court denied both motions in their entirety. It found that neither party raised any issues of fraud, mistake, or new evidence under Rule 60(b) and that each party merely sought to improperly relitigate the case on the merits. The court declined to relitigate the claims and let the prior judgment stand. In addition, the court declined to grant MTR attorney fees, holding that it was not the prevailing party, having lost on most of its claims. The court nonetheless analyzed the seven factors considered in determining whether to award attorney fees under the FDUTPA: (1) scope and history of litigation; (2) ability of non-prevailing party to pay the fee award; (3) deterrent effect on other actors; (4) merits of each party's position; (5) whether claim was frivolous, unreasonable, or meritless; (6) whether defense was raised in bad faith; and (7) significance of the underlying legal question to FDUTPA law. In weighing these factors, the court found that only third factor favored MTR and declined to award fees on that basis as well.

***Sashital v. Seva Beauty, LLC*, Bus. Franchise Guide (CCH) ¶ 16,847, 2021 WL 1222895 (N.D. Ill. Mar. 31, 2021)**
This case is discussed under the topic heading "Injunctive Relief."

***Universal Property Services, Inc. v. Lehigh Gas Wholesale LLC*, Bus. Franchise Guide (CCH) ¶ 16,863, 2021 WL 1720886 (D.N.J. Apr. 30, 2021)**
This case is discussed under the topic heading "Choice of Forum."

GOOD FAITH AND FAIR DEALING

***Purugganan v. AFC Franchising, LLC*, Bus. Franchise Guide ¶ 16,824, 2021 WL 723916 (D. Conn. Feb. 24, 2021)**
This case is discussed under the topic heading "Definition of Franchise."

INJUNCTIVE RELIEF

***Core Progression Franchise LLC v. O'Hare*, Bus. Franchise Guide (CCH) ¶ 16,850, 2021 WL 1222768 (D. Colo. Apr. 1, 2021)**
The U.S. District Court for the District of Colorado enjoined a former Core Progression franchisee from operating a competing business or using any of Core Progression's confidential business information, but did require, as a condition of receiving injunctive relief, that Core Progression post a bond of $156,000.

In September 2019, defendant Chris O'Hare (O'Hare) entered into a franchise agreement with Core Progression Franchise, LLC (Core Progression)—a fitness center franchisor. Over the course of the next eleven months, O'Hare went through a comprehensive training program with Core Progression and received assistance with finding, designing, and building out his location. Core Progression provided operations manuals, marketing materials, and access to Core Progression's customer management software, Zen Planner. These materials and information had all been created and developed over fourteen years of Core Progression's operations in the fitness industry.

In August 2020, O'Hare, through an entity, CAO Enterprises (CAO), opened a Core Progression franchise in Apex, North Carolina. In December 2020, O'Hare defaulted on his monetary obligations under the franchise agreement. On January 7, 2021, Core Progression received a notification from the Zen Planner customer management software system that O' Hare was attempting to copy the Core Progression customer database. On January 29, 2021, Core Progression terminated the franchise agreement. After terminating the agreement, Core Progression discovered that since December 2020, O'Hare had been taking steps to operate a competing fitness center, Altru Fitness, in the same location as his Core Progression franchise. O'Hare had manually copied numerous customer records from the Zen Planner customer database, had used his Core Progression email address to communicate with customers about his plan to create a competing gym, and created a new website bearing the Altru Fitness name but that essentially copied the content of the Core Progression website.

On March 3, 2021, Core Progression sued O'Hare and CAO for breach of contract and trademark infringement under the Lanham Act. Core Progression also sought a preliminary injunction against the defendants seeking to prevent them from operating the fitness center pending the outcome of the lawsuit. Core Progression argued that the operation of the fitness center at the same location violated a non-compete clause in the franchise agreement.

O'Hare and CAO argued in response that the court did not have authority to hear the dispute because it was subject to an arbitration clause in the franchise agreement, because Core Progression had fraudulently induced them to enter into the franchise agreement, and because there was nothing proprietary or unique about Core Progression's franchise system.

The court first addressed the appropriate standard applicable to Core Progression's request for relief. The court decided that, because Core Progression sought to "change the status quo" by enjoining defendants from continuing to operate a business, the court had to use a heightened standard applicable to disfavored preliminary injunctions.

The court also addressed its authority to hear the dispute notwithstanding the arbitration clause in the franchise agreement. The court found that the request for injunctive relief filed by Core Progression was outside the scope of the arbitration clause because there was an express exemption to the arbitration requirement for claims related to injunctive relief.

The court then turned to the merits of Core Progression's request for injunctive relief. The court found that Core Progression had shown a substantial likelihood of success on the merits of its claim for breach of the covenant not to compete in the franchise agreement. Despite the fact that Colorado law generally prohibits covenants not to compete, the court held that the covenant in the Core Progression franchise agreement fell within two exceptions to this rule: covenants governing trade secrets and covenants applying to management personnel. The court found that the defendants effectively conceded that they used Core Progression's confidential information to build their competing business. They did not dispute that they downloaded the Core Progression client relationship database with customer and membership information before leaving the Core Progression system; or that they wrote Core Progression customers from their @coreprogression.com e-mail accounts to say that they were transitioning to a competing software while they were still franchisees. The court rejected as unsubstantiated defendants' claims that the franchise agreement was unenforceable because of alleged fraud by Core Progression.

In determining that Core Progression had proven a likelihood of irreparable harm, the court relied upon testimony from Core Progression's CEO that the series of events made it look like Core Progression had tried and failed to open a successful franchise location in North Carolina. The court found that an injunction was necessary to preserve any remaining goodwill for the Core Progression brand in the North Carolina market.

The court held that the balance of the hardships favored Core Progression even if Altru Fitness is O'Hare's only source of income. The court, citing to other cases from the District of Colorado, held that protecting a defendant's sole source of income was not a sufficient basis to refuse to grant an injunction where a plaintiff had provided strong evidence of a loss of trade secrets and significant damage to its business.

The court found no harm to the public interest reasoning that the public has an interest in the enforcement of valid non-competition agreements.

The court issued the injunction on the condition that Core Progression post a bond sufficient to secure the potential damages that defendants might suffer if the injunction had been granted in error. The court rejected Core Progression's argument that the franchise agreement expressly permitted the court to enter an injunction without a bond. The court calculated the amount of the bond by multiplying defendant's gross sales by the twelve-month period of the non-compete agreement.

Denbra IP Holdings, LLC v. Thornton, Bus. Franchise Guide (CCH) ¶ 16,817, 2021 WL 674238 (E.D. Tex. Feb. 22, 2021)

This case is discussed under the topic heading "Trademark Infringement."

***La Simple Co., Ltd. v. SLP Enterprises, LLC*, Bus. Franchise Guide (CCH) ¶ 16,864, 2021 WL 1648762 (D. Mass. Apr. 27, 2021)**

The U.S. District Court for the District of Massachusetts denied a former exclusive distributor's motion for a preliminary injunction against a sunglasses manufacturer's termination of the exclusive distribution agreement.

In 2013, La Simple Co., Ltd. (La Simple) entered into a three-year exclusive distributor agreement with SLP Enterprises, LLC (SLP) for distribution of SLP's sunglasses in Hong Kong and China. The parties renewed their agreement for subsequent three-year terms commencing in 2016 and 2019. All the agreements had minimum purchase quotas, but the third agreement included an order schedule that required La Simple to order a certain percentage of its yearly quota by specific dates. The third agreement also permitted SLP to terminate the agreement on sixty days' notice in the event La Simple failed to meet the yearly quota or order schedule.

In 2019, La Simple failed to meet the order schedule, but the parties apparently agreed to extend the deadlines. In 2020, La Simple was impacted by COVID-19 and again failed to meet several of the deadlines. The parties disputed whether an oral agreement was reached modifying the schedule for 2020.

On November 23, 2020, SLP notified La Simple that it was terminating La Simple's agreement effective January 22, 2021, based on La Simple's failure to meet the purchase quota schedule. At approximately the same time, SLP entered into a new exclusive distributor agreement for Hong Kong and China with La Simple's competitor. La Simple then sued SLP, its CEO, and the competitor for breach of contract, breach of the covenant of good faith and fair dealing, fraudulent misrepresentation, promissory estoppel, intentional interference with business relationships, violation of Chapter 93A of the Massachusetts General Laws, and a request for declaratory relief and specific performance. At the time of filing, La Simple also filed a motion for injunctive relief. Injunctive relief requires the plaintiff to show (1) likelihood of success on the merits; (2) irreparable harm if the injunction is not granted; (3) balance of hardships between the parties; and (4) effect of an injunction on the public interest. However, the court considered only the first two factors to decide the injunction request, which it determined to be threshold issues.

First, the court found that La Simple was not likely to succeed on the merits of its claims. La Simple argued that it would success on its claims based on one of two theories: (1) SLP validly modified the purchase order schedule by oral agreement, such that La Simple had not breached its obligations; or (2) COVID-19 triggered the force majeure provision of the agreement, excusing La Simple from meeting its obligations under the schedule. The court found that La Simple could not prove either. The court held that La Simple had failed to establish its first theory because it could offer no contemporaneous evidence that any oral modification had ever been made. The court determined that La Simple was unlikely to succeed on its second theory because La Simple provided no evidence that COVID-19 caused it to fail in its obligations, as it was failing to perform the year before COVID-19 emerged.

Second, the court found that La Simple could not show irreparable harm because all of its claimed damages were either monetary—unsold products, prepaid shipping and related fees, lowered sales expectations, refund demands, business loan balances, lost revenue—or speculative. Having determined that La Simple could not satisfy either of the threshold factors, the court denied the motion for a preliminary injunction.

***Sashital v. Seva Beauty, LLC*, Bus. Franchise Guide (CCH) ¶ 16,847, 2021 WL 1222895 (N.D. Ill. Mar. 31, 2021)**

The U.S. District Court for the Northern District of Illinois denied three franchisees' request for a preliminary injunction prohibiting Seva Beauty, LLC (Seva Beauty), a franchisor of "fast casual" beauty spas, from terminating their franchise agreements.

In July 2020, three franchisees filed a putative class action against Seva Beauty seeking declaratory and injunctive relief. Each alleged that Seva Beauty fraudulently induced them to enter into a franchise agreement with Seva Beauty. Each of those agreements gave the franchisees the right to operate Seva Beauty salons and spas, which are typically located in Walmart stores. The agreement required each plaintiff to pay the greater of a six percent royalty or $250 per week. Two of the plaintiffs had defaulted on this royalty obligation because of business interruptions caused by the COVID-19 pandemic.

The plaintiffs asserted that Seva Beauty presented the franchise as a no-lose investment opportunity for significant passive income. The plaintiffs accused Seva Beauty of providing misleading financial information in its franchise disclosure document (FDD)—contending that the information in the FDD was based solely upon a handful of profitable franchises that use fraudulent labor practices to avoid paying employee benefits and overtime. The plaintiffs also alleged that Seva Beauty misrepresented the nature of its relationship with Walmart. According to the plaintiffs, the relationship with Walmart was the only value provided to franchisees compared to the value provided by competing salon franchisors. The plaintiffs contended Seva Beauty claimed that the relationship was strong when it was actually "falling apart" and Walmart was refusing to renew franchisees' leases.

The plaintiffs filed a motion for temporary restraining order and a preliminary injunction that sought to prohibit Seva Beauty from terminating their or any other franchise agreements for failure to pay the weekly royalty. The franchisor opposed the motion, arguing that the claims were subject to arbitration and the individual plaintiffs, who each operated their franchises through business entities, lacked standing to sue. The court held that the arbitration clause did not prohibit the plaintiffs from seeking provisional injunctive relief because the franchise agreement expressly carved out claims for injunctive relief from the scope of the arbitration agreement. The court also rejected the franchisor's standing argument because the plaintiffs each claimed that they had personally received the alleged fraudulent misrepresentations and decided to enter into the franchise agreements through their entities on that basis.

The court then denied the preliminary injunction because the plaintiffs failed to establish a risk of irreparable harm that could not be remedied with money damages. The plaintiffs had argued that, if the court did not issue an injunction, the franchisor would terminate their agreements and they would lose their franchised business. The court found this insufficient because the plaintiff had not offered evidence that their businesses had loyal customers, goodwill, or intangible value in the mere existence of their franchises. The court found, "to the contrary," that the plaintiffs' lawsuit was premised upon the assertion that their franchises were total failures that were doomed from the start. The court reasoned that because the lawsuit sought to terminate their relationship with Seva Beauty, there was little value in permitting the plaintiffs to continue to operate Seva Beauty franchises.

The court also addressed a motion to dismiss or stay pending arbitration. The franchisor had argued that the underlying suit was covered by the arbitration clause in the franchise agreement. It also argued that the claims were barred by a one-year contractual limitations period in the franchise agreement and that the plaintiffs lacked standing. The court struck the motion without prejudice to renewal and advised the parties that any renewed briefing need to address these "complicated" issues in detail.

JURISDICTION

***Adventure Park Hamilton, LLC v. UATP Management, LLC*, Bus. Franchise Guide (CCH) ¶ 16,845, 2021 WL 2396580 (N.J. Super. Ct. Mar. 25, 2021)**
This case is discussed under the topic heading "Choice of Forum."

***Universal Property Services, Inc. v. Lehigh Gas Wholesale LLC*, Bus. Franchise Guide (CCH) ¶ 16,863, 2021 WL 1720886 (D.N.J. Apr. 30, 2021)**
This case is discussed under the topic heading "Choice of Forum."

LABOR AND EMPLOYMENT

***Caddick v. Tasty Baking Co.*, Bus. Franchise Guide (CCH) ¶ 16,854, 2021 WL 1374607 (E.D. Pa. Apr. 12, 2021)**
This case is discussed under the topic heading "Class Actions."

***Conrad v. Jimmy John's Franchise, LLC*, Bus. Franchise Guide ¶ 16,821, 2021 WL 718320 (S.D. Ill. Feb. 24, 2021)**
The U.S. District Court for the Southern District of Illinois ruled on motions to exclude experts in connection with a class certification motion, finding that an expert who relied on an inaccurate premise must be excluded, while the challenges to the competing experts did not give rise to his exclusion.

Jimmy John's Franchise, LLC (Jimmy John's) included a no-poach provision in its Franchise Agreement from 2014 to 2018. Under the no-poach provision, franchisees agreed not to "recruit as a partner or investor/owner, or hire as an employee, any person then employed, or who was employed within the preceding twelve (12) months, by [Jimmy John's], any of [Jimmy John's] affiliates, or a franchisee . . . without obtaining the existing or former employer's prior written permission. . . ." Plaintiffs, a putative class of employees of Jimmy John's restaurants, alleged that the no-poach provision prohibited employees from gaining employment at other Jimmy John's locations with different owners, thereby suppressing wages and stifling worker mobility through the unlawful exercise of the monopsony power in violation of Section 1 of the Sherman Act.

In support of their Motion for Class Certification, Plaintiffs relied on the expert report of Dr. Hal Singer (Singer). Singer concluded that common methods and evidence demonstrated anticompetitive effects and common impact to the class, as well as aggregate damages attributable to the no-poach provision. In particular, Singer argued that the no-poach provision evidenced Jimmy John's monopsony power because it prohibited workers from bidding up worker wages among independently owned stores thereby suppressing labor mobility. To test his hypothesis, Singer first conducted a wage regression analysis comparing "(1) the wages paid to Class Members when the No-Poach Provision was in effect with (2) the wages paid to Class Members after the No-Poach Provision was officially halted in mid-2018." To create this model, he used hourly compensation data from Weekly Sales Reports (WSRs) submitted to Jimmy John's by franchisees. The WSRs included information such as daily hours workers and compensation for employees. According to Singer, based on the wage regression, between eighty-seven to ninety-one percent of class members suffered an anti-trust injury.

Singer next considered whether there was a class-wide compensation structure that artificially reduced compensation broadly across the class. He determined that there was, after performing additional regressions to measure, among other things, "the extent to which an increase in hourly compensation for Class Members generally [was] statistically associated with an increased [sic] in compensation for an individual Class Member." Based on this set of findings, Singer contended that *all* putative class members were injured by the no-poach provision.

Jimmy John's contested the reliability of Singer's report and offered two rebuttal reports from its own expert witnesses, Dr. Janusz Ordover (Ordover) and Dr. Justin McCrary (McCrary). In addition to pointing out conceptual and statistical flaws in Singer's approach, Ordover concluded that economic injury could not be shown for all or nearly all of the putative class members and that highly individualized investigations would be required to determine whether any individual class member suffered an antitrust injury. Similar to Singer, Ordover conducted regressions. However, Ordover unpooled "the WSR data for the job manager category into two separate manger job categories: (i) those who appear[ed] to be paid on an hourly basis; and (ii) those who appear[ed] to be paid a salary."

McCrary, on the other hand, suggested that Singer's conclusions conflict with Plaintiffs' monopsony theory. According to McCrary, Plaintiffs' theory was based on the idea "franchisees are independent horizontal competitors," a foundation which is "inconsistent with . . . the economics of franchising." Instead, according to McCrary, Jimmy John's and other franchisors have vertical restraints to ensure that no franchisee undermines the franchise or brand through freeriding, encroachment, or otherwise. McCrary contended that these restraints benefit employees because they "[increase] demand for the brand's products and [expand] the size of the franchise system, which in turn increases the total labor demand on the franchise system."

Jimmy John's and Plaintiffs each moved to exclude the other's expert reports. As a preliminary matter, the court noted that, while expert witnesses generally play a limited role in class certification hearings, courts will rule on a challenge to an expert's qualifications or submissions if the expert's report or testimony is critical to class certification. In this instance, the disputed expert testimony involved Rule 23(b)'s predominance requirement, so it was appropriate for the court to rule on the expert challenges.

Turning to the parties' substantive arguments, Jimmy John's first argued that Singer's testimony should be excluded because he used flawed data in his regression analysis. In making this argument, Jimmy John's relied on franchisee testimony that wages reflected in the WSRs are rarely accurate. Thus, according to Jimmy John's, the WSR data was an unreliable record of actual wages. The court disagreed, noting that reliance on faulty information does not go to admissibility, but rather should be explored on cross-examination.

Turning next to Singer's methodology, Jimmy John's asserted that Singer "grossly misinterpreted" the data contained in the WSRs because he incorrectly assumed all wages contained in the WSR data reflected hourly wages. Rather, the WSR data reflected hourly wages for some employees and per-shift wages for other employees. According to Jimmy John's, this mistake inflated Singer's results and caused them to be unreliable. The court agreed that the wage discrepancy was material, rendering Singer's testimony unreliable. Therefore, due to this methodological flaw, the court granted Jimmy's John's Motion to Exclude Singer's testimony.

The court next addressed Plaintiffs' Motion to Exclude Ordover's and McCrary's testimony. Beginning with Ordover, the court noted that while Plaintiffs raised several objections that went to the weight of the expert testimony, none of the objections justified the exclusion of Ordover's report. Plaintiffs first asserted that Ordover's approach suffered from an endogeneity bias. The court rejected this argument because Plaintiffs failed to point to any demonstrable evidence that Ordover's results were skewed. Next, Plaintiffs argued that Ordover improperly conducted regressions by state and by year, disregarding most relevant data. The court again disagreed, noting that while Ordover disregarded 34,000 data points out of millions, that was not sufficient to make his methodology unreliable. The court also rejected Plaintiffs' arguments that (1) Ordover's analysis suffered from endogenous sample selection; (2) Ordover erred by conducting separate regressions for each state and year; and (3) Ordover's false-positive analysis was faulty.

Turning to McCrary, Plaintiffs argued that McCrary's testimony must be excluded because, among other reasons, (1) McCrary failed to show Jimmy John's adopted the no-poach provision for procompetitive benefits; (2) McCrary's argument rested on insufficient facts; (3) McCrary's did not conduct a scientific analysis showing that the removal of the no-poach provision reduced the procompetitive benefit; (4) McCrary used unreliable facts, namely franchisee-declarations; (5) McCrary's graph showing a decrease in the use of certified managers was misleading due to graph's caption; and (6) McCrary did not control for the fact that use of certified managers was declining before Jimmy John's stopped enforcing its no-poach provision. The court was not persuaded by Plaintiffs' arguments. While none of Plaintiffs' arguments justified the exclusion of McCrary's report, the court did note that at least some of Plaintiffs' disputes went to the weight of the expert's testimony.

Plaintiffs also objected to McCrary's release analysis. As background, based on his review of relevant documents, McCrary asserted that requests for release from the no-poach restrictions were granted eighty-eight percent of the time. Plaintiffs first argued that enforcement of the no-poach provision was a question for the jury. The court rejected this argument noting that, when determining whether common questions predominate, its analysis may overlap with the merits during the class-certification stage. Plaintiffs next argued that McCrary's testimony should be excluded as "incomplete and unhelpful" because McCrary did not set an objective standard for what is means to enforce the no-poach provision and, therefore, his results could not be replicated. However, according to the court, Plaintiffs mischaracterized McCrary's statements and ignored his report which sufficiently laid out his release analysis methodology. Plaintiffs next argued the McCrary's analysis was incomplete because he failed to consider that Jimmy's John's and numerous franchisees had blanket policies for not granting releases. The court rejected this argument as Plaintiffs provided no evidence showing that a large proportion of stores had such a policy. Finally, Plaintiffs asserted that McCrary's economic principles were unreliable and that McCrary's testimony was "pure theoretical speculation" as he failed to study the extent to which revenues were reduced by the no-poach provision. The again court rejected both of these arguments.

Finding both Ordover's and McCrary's testimony reliable, the court denied Plaintiffs' Motion to Exclude.

***C.S. v. Wyndham Hotels & Resorts, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,851, 2021 WL 1264226 (M.D. Fla. Apr. 6, 2021)**

This case is discussed under the topic heading "Vicarious Liability."

***Fleming v. Matco Tools Corp.*, Bus. Franchise Guide (CCH) ¶ 16,818, 2021 WL 673445 (N.D. Cal. Feb. 21, 2021)**

This case is discussed under the topic heading "Class Actions."

Rivers v. International House of Pancakes, Bus. Franchise Guide (CCH) ¶ 16,843, 2021 WL 860590 (S.D.N.Y. Mar. 8, 2021)

The plaintiff, Nyjhia Rivers (Rivers) brought an action against International House of Pancakes (IHOP), Trihop 14th Street, LLC (Trihop) and Sylvia LNU (Sylvia), claiming that the defendants violated Title VII, the Americans with Disabilities Act (ADA), the New York State Human Rights Law (NYSHRL) and the New York City Human Rights Law (NYCHRL). Rivers alleged that the defendants discriminatorily reduced her hours and subsequently terminated her after she became pregnant. The U.S. District Court for the Southern District of New York granted a franchisor and its franchisees' motion to dismiss claims asserting various employment claims against them.

Rivers worked as a server at an IHOP franchise in Brooklyn between June 2015 and approximately May 2016. In June 2016, she was hired as a server at an IHOP franchise in Manhattan, which was under the management of a different franchisee, Trihop. At both locations, Rivers's job duties were governed by IHOP's Serving Protocol Handbook (Handbook). The Handbook explained "in great detail" various aspects of the server's role. IHOP ensured that the Brooklyn and Manhattan franchises implemented the Handbook's requirements by conducting detailed inspections on a semi-annual basis. At the end of each inspection, IHOP's inspector would inform the staff members of what they did wrong and needed to correct. Staff members whose performance did not improve after an inspection risked discipline, up to and including termination. Rivers was an "above-satisfactory employee" and was promoted while working at the Manhattan franchise. Several months after she was promoted, she learned that she was pregnant. She informed the general manager, Sylvia, and requested that her evening shifts be swapped for morning shifts to accommodate the pregnancy-induced nausea that she experienced in the evening. Rivers was removed from the work schedule for two weeks before Sylvia assigned her new shifts. Rivers protested but was never returned to a full workload. Eventually, Sylvia stopped assigning Rivers shifts altogether.

In July 2019, Rivers filed a charge of discrimination against IHOP and Sylvia (but not Trihop) with the Equal Employment Opportunities Commission (EEOC). Rivers received a Notice of Right to Sue in January 2020, and she commenced the case against IHOP and Sylvia in March 2020, later amending the complaint to name Trihop as a defendant.

In their motion to dismiss, the defendants argued that the claims against IHOP failed because (1) Trihop (not IHOP) was plaintiff's employer; (2) Rivers's EEOC charge of discrimination did not mention Trihop; and (3) the court need not exercise supplemental jurisdiction over Rivers's state and city claims.

To be held liable for employment discrimination under Title VII or the ADA, a defendant must have been the plaintiff's "employer." Rivers acknowledged that Trihop was her direct employer but contended that IHOP also may be considered an employer based on the control that it exercised over its franchises. The court explained that an entity that is not a plaintiff's direct employer may be liable under Title VII and the ADA as a "joint employer." The joint employer doctrine is triggered when "an employee, formally employed by one entity, . . . has been assigned to work in circumstances that justify the conclusion that the employee is at the same time constructively employed by another entity." To determine whether an entity is a "joint employer," courts look for evidence that the purported joint employer "had immediate control over the other company's employees."

A joint employer's control may be formal or functional in nature. Regarding formal control, the court considered whether IHOP (1) had the power to hire and fire Trihop employees; (2) supervised and controlled employee work schedules or conditions of employment; (3) determined rate and method of payment; and (4) maintained employment records. Rivers did not allege that IHOP played in a role in Trihop's hiring and firing decisions. Similarly, Rivers did not allege that IHOP controlled Trihop's work schedules or supervised work conditions beyond its semi-annual inspections. The court noted that infrequent inspections "for the purposes of quality control" have been recognized as "insufficient to establish joint employer status." The court also noted that Rivers failed to include any allegations in her complaint suggesting that IHOP influenced Trihop's wages or maintained Trihop's employment records. Thus, the court found that none of these factors demonstrated that IHOP had formal control over Trihop's employees.

To determine functional control, the court looked at several factors: (1) whether the alleged employer's premises and equipment were used for the plaintiff's work; (2) whether the direct employer had a business that could or did shift as a unit from one putative joint employer to another; (3) the extent to which the plaintiff performed a discrete line job that was integral to the alleged employer's process of production; (4) whether responsibility under the contracts could pass from one direct employer to another without material changes; (5) the degree to which the alleged employer or their agents supervised the plaintiff's work; and (6) whether the plaintiff worked exclusively or predominantly for the alleged employer. The court stated that many of these factors are difficult to translate into the franchisee-franchisor context, and thus did not deserve much weight in the court's analysis. The court found that these factors were of no more help to Rivers's case than the factors regarding formal control. For instance, Rivers did not allege that she used IHOP's, as opposed to Trihop's, premises or equipment. She also did not allege that the material aspects of her work environment would be unchanged if she were to gain employment with a different IHOP franchise. Further, she alleged only marginal supervision on behalf of IHOP. The court found that these factors were insufficient to plead IHOP's functional control over Trihop employees. The court was unwilling to allow the case to proceed to discovery, given that the allegations in the complaint regarding joint employer status were so sparse.

Under Title VII and the ADA, a claimant may bring suit in federal court only if she has filed a timely complaint with the EEOC and obtained a right to sue letter. This requirement applies to each defendant individually, to ensure that defendants have adequate notice of the claims and an opportunity to voluntarily comply. However, courts may make an "identify of interest" exception to permit an action to proceed against an unnamed party if the following circumstances apply: (1) the role of the unnamed party could not be ascertained at the time of the filing of the EEOC complaint; (2) the interests of a named party are so similar as the unnamed party's that it would be unnecessary to include the unnamed party in the EEOC proceedings for the purpose of obtaining voluntary conciliation and compliance; (3) the unnamed party's absence from the EEOC proceedings did not result in actual prejudice to its interests; or (4) the unnamed party has represented to the complainant that its relationship with the complainant is to be through the named party. The identity of interest exception is born from concerns regarding plaintiff's sophistication. As a result, courts in the Southern District of New York have imposed a threshold inquiry regarding a plaintiff's degree of representation before the EEOC and have often restricted the identity of interest exception to plaintiffs who filed their EEOC charges *pro se* or with a lawyer inexperienced in Title VII or ADA litigation.

Here, Rivers's charge of discrimination named IHOP and Sylvia but not Trihop. Rivers was represented by counsel when she filed the EEOC charges, and the complaint did not indicate that her counsel lacked experience litigating Title VII or ADA claims. Thus, the court held that the charges against Trihop should be dismissed because Rivers had adequate representation. Even if the court were to analyze the factors discussed above, relief would be precluded because Rivers and her counsel should have been able to determine the identity of her direct employer; IHOP and Trihop were not commonly controlled and did not share liability for the alleged discrimination; and Trihop never suggested that Rivers's relationship with Trihop should be channelled through IHOP.

Given the fact that the court dismissed Rivers's federal claims, the court had to determine whether to exercise supplemental jurisdiction over her NYSHRL and NYCHRL claims. The court explained that it could decline to exercise supplemental jurisdiction over state claims on various grounds, including the fact that the court had dismissed all the federal claims over which it had original jurisdiction. The court decided not to exercise supplemental jurisdiction, in part because the case was at an early stage of litigation. Thus, the court dismissed Rivers's NYSHRL and NYCHRL claims without prejudice.

NONCOMPETE AGREEMENTS

Core Progression Franchise LLC v. O' Hare, Bus. Franchise Guide (CCH) ¶ 16,850, 2021 WL 1222768 (D. Colo. Apr. 1, 2021)

This case is discussed under the topic heading "Injunctive Relief."

STATUTORY CLAIMS

***Caddick v. Tasty Baking Co.*, Bus. Franchise Guide (CCH) ¶ 16,854, 2021 WL 1374607 (E.D. Pa. Apr. 12, 2021)**
This case is discussed under the topic heading "Class Actions."

***C.S. v. Wyndham Hotels & Resorts, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,851, 2021 WL 1264226 (M.D. Fla. Apr. 6, 2021)**
This case is discussed under the topic heading "Vicarious Liability."

***Fleming v. Matco Tools Corp.*, Bus. Franchise Guide (CCH) ¶ 16,818, 2021 WL 673445 (N.D. Cal. Feb. 21, 2021)**
This case is discussed under the topic heading "Class Actions."

***MTR Capital, LLC v. LaVida Massage Franchise Development, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,861, 2021WL 1626353 (E.D. Mich. Apr. 27, 2021)**
This case is discussed under the topic heading "Fraud."

***Purugganan v. AFC Franchising, LLC*, Bus. Franchise Guide ¶ 16,824, 2021 WL 723916 (D. Conn. Feb. 24, 2021).**
This case is discussed under the topic heading "Definition of Franchise."

TERMINATION AND NONRENEWAL

***Casco, Inc. v. John Deere Construction & Forestry Co.*, Bus. Franchise Guide (CCH) ¶ 16,826, 990 F.3d 1 (1st Cir. Mar. 2, 2021)**
The First Circuit denied the parties' cross appeals in which the plaintiff dealer appealed the dismissal of one of its claims and judgment in favor of the defendant on its counterclaims, and defendant appealed the lower court's denial of its request for a new trial on the plaintiff's impairment claim and for dismissal of the plaintiff's wrongful termination claim.

In 1986, defendant John Deere Construction & Forestry Company (Deere) entered into an agreement with Casco, Inc. (Casco) that permitted Casco to resell Deere construction equipment in Puerto Rico. The agreement required Casco to comply with certain "Essential Obligations," including stocking certain inventory, maintaining service facilities and trained personnel, and actively promoting sales. Article 10 of the agreement allowed Deere to terminate if Casco failed in any of the Essential Obligations or failed to pay all indebtedness to Deere when it became due.

In 2009, Casco sued Deere, alleging Deere improperly modified payment terms. The parties settled and agreed to "mutually assist and cooperate with each other in the sale and distribution of the John Deere products." In September 2012, Casco failed to make timely payments under the agreement, but cured the deficiency. Nonetheless, Deere cancelled a purchase order from Casco for farm equipment that Casco had already sold to a construction company, citing Casco's failure to complete certain required training. In 2013, Casco again fell behind on payments, and Deere terminated the agreement under Article 10.

In April 2013, Casco sued Deere again, asserting unjust impairment of the agreement based on the December 2012 cancellation of Casco's order, the 2013 termination, and *dolus* (deceit) for fraudulent inducement under the settlement agreement. Deere filed a counterclaim for the amounts still owed by Casco.

The parties went to trial in March 2016. Deere moved to dismiss all counts and obtain judgment on the counterclaim at the end of Casco case-in-chief. The Court dismissed the *dolus* claim and granted judgment in favor of Deere on the counterclaim. The jury found in favor of Casco on both the impairment and termination claims, awarding it over $1.5 million in damages.

Casco then sought reinstatement of its *dolus* claim or certification of the issue to the Supreme Court of Puerto Rico and renewed its motion to dismiss Deere's counterclaim. Deere cross-filed a motion renewing its request to dismiss the termination charge, seeking a new trial as to the impairment charges or a remittitur of damages against it, and requesting an amended judgment increasing the amount of damages on the counterclaim. The Court denied Casco's motion, denied Deere's as to the request for a new trial, but granted it as to remitting the impairment damages to $58,000.00 and increasing the counterclaim award by several thousand dollars. Both parties appealed.

On appeal, Deere argued that there should be a new trial on the impairment claim, asserting that the evidence showed that it had just cause to cancel the equipment order because Casco had not complied with the required training. The Court disagreed, noting that the jury was presented evidence that Deere did not require strict compliance with the training requirements and that Casco's failure to comply was partly attributable to Deere's failure to provide it proper access to the training.

Deere further argued that the termination claim should be dismissed as a matter of law on the basis that it had just cause to terminate Casco because Casco failed to make timely payments and failed to fulfill several of its essential obligations. The Court again disagreed, holding that it was reasonable for the jury to conclude that there were abnormal circumstances excusing the failure to make timely payments and that Deere was responsible for any failure on the part of Casco to comply with certain essential obligations.

Casco argued that the court below improperly dismissed its *dolus* claim. The First Circuit agreed with the court below that the *dolus* claim relied on the possibility of Casco winning a constructive termination claim, which did not exist at law. Because there was no actual termination in 2009, the *dolus* claim was properly dismissed. The First Circuit similarly held that Casco was not entitled to dismissal of Deere's counterclaims, as the amounts owed were incurred before termination. As a result, Article 1077 of the Puerto Rico Civil Code, allowing a party to rescind its part of a mutual obligation if the other party failed to perform its own part, was not applicable.

Finally, the First Circuit ruled that Deere was not entitled to a new trial on damages. Although Deere argued that Casco's expert, whose evaluation the jury adopted, made methodological errors in his computation, Deere did not seek to have the testimony excluded. As a result, the jury was entitled to make its own evaluation of the credibility of each witness, and its damages award would stand.

***Core Progression Franchise LLC v. O' Hare*, Bus. Franchise Guide (CCH) ¶ 16,850, 2021 WL 1222768 (D. Colo. Apr. 1, 2021)**
This case is discussed under the topic heading "Injunctive Relief."

***La Simple Co., Ltd. v. SLP Enterprises, LLC*, Bus. Franchise Guide (CCH) ¶ 16,864, 2021 WL 1648762 (D. Mass. Apr. 27, 2021)**
This case is discussed under the topic heading "Injunctive Relief."

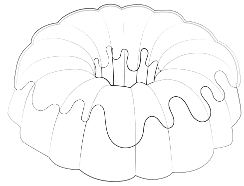
TORTIOUS INTERFERENCE

***Purugganan v. AFC Franchising, LLC*, Bus. Franchise Guide ¶ 16,824, 2021 WL 723916 (D. Conn. Feb. 24, 2021)**
This case is discussed under the topic heading "Definition of Franchise."

TRADEMARK INFRINGEMENT

***Denbra IP Holdings, LLC v. Thornton*, Bus. Franchise Guide (CCH) ¶ 16,817, 2021 WL 674238 (E.D. Tex. Feb. 22, 2021)**
The U.S. District Court for the Eastern District of Texas granted a preliminary injunction in favor the plaintiff, a franchisor whose system used the mark Nothing Bundt Cakes, finding that a competitor's use of Nothing Bundt Cake's trademark frosting pattern gave rise to the risk of irreparable harm to the plaintiff.

In mid-August 2020, plaintiff Denbra IP Holdings, LLC (Denbra) learned from several of its franchisees that an individual named Kerri Thornton (Thornton) was operating a business called "Anything Bundt Cakes" that sold bundt cakes in the Dallas-Fort Worth area. Thornton marketed bundt cakes to customers through a website and Facebook page. She also used the same tubular frosting pattern as the one, seen below, Denbra had registered with the U.S. Patent and Trademark office in 2008:

U.S. Reg. No.	First Use Date	Reg. Date	Mark
3,526.479	10/15/1998	11/4/2008	

Shortly after receiving notification of Thornton's activities, Denbra sent a letter demanding that Thornton cease using the frosting pattern and the name Anything Bundt Cakes. Thornton changed her business' name to "All About Bundt Cakes," but continued using the frosting pattern. Denbra sent another demand letter and then sued for trademark infringement. It also sought a preliminary injunction seeking to prohibit Thornton from continuing to use the frosting pattern.

Although Thornton did not respond or oppose the application, the court rigorously analyzed whether Denbra had proven a likelihood of success on the merits, the likelihood of irreparable harm, the balance of the equities, and that an injunction was in the public interest. First, the court analyzed Denbra's likelihood of success on the merits of its infringement claim. It found that Denbra had sufficiently established a likelihood of success on the merits because the frosting pattern was a legally protectable trademark owned by Denbra and because Thornton's use of the same frosting pattern was likely to cause confusion in the marketplace.

In determining whether Denbra owned a legally protectable trademark, the court held that the frosting pattern had a secondary meaning in the market in the minds of consumers purchasing bundt cakes. The court cited to the over two decades' worth of use of the frosting pattern by Denbra, the fact that its franchisees collectively earn over $100 million a year selling bundt cakes with the frosting pattern, and that a consumer survey found that eighty-three percent of consumers identified the frosting pattern with Nothing Bundt Cakes labelled products. The court also found that Denbra was the senior user of the mark.

The court analyzed eight factors to determine whether Denbra had proven a likelihood of confusion: (1) the type of mark allegedly infringed; (2) the similarity between the two marks; (3) the similarity of the products or services; (4) the identity of the retail outlets and purchasers; (5) the identity of the advertising media used; (6) the defendant's intent; (7) any evidence of actual confusion; and the degree of care exercised by potential purchasers.

The court held that most of the factors weighed in favor of Denbra. It found that the frosting pattern was a distinctive mark, that the frosting pattern used by Thornton was identical, and that it was selling a similar product to substantially overlapping customers in the Dallas-Fort Worth area. The court noted no direct evidence of intent, but the court found circumstantial evidence of intent based upon the fact that Thornton had been using a similar business name to sell similar products. The court also found that customers purchasing bundt cakes were unlikely to take particular care in selecting a bundt cake, thereby increasing the probability of confusion in the marketplace.

The court found that Denbra had proven a likelihood of irreparable harm because it had experienced a loss of control over the reputation of its products and a loss of goodwill. The evidence showed that Denbra had developed goodwill in the Dallas-Fort Worth community, that Thornton was operating in that same community, and that Denbra had no control over the goods and services offered by Thornton.

The court found that there was minimal or no harm in forcing Thornton to change her business's frosting pattern. It also found that Thornton had accepted the risk of harm by continuing to use the frosting pattern even after receiving notification from Denbra that she infringed its trademark rights. The court determined that an injunction did not disserve the public because enforcing compliance with the Lanham Act was in the public interest.

The court prohibited Thornton from using the Nothing Bundt Cakes frosting-pattern mark and all confusingly similar variations of it in any form of interstate commerce related to the food and beverage industry. The court also ordered Thornton to take down or remove any advertisement displaying the Nothing Bundt Cakes frosting pattern.

UNFAIR COMPETITION/ UNFAIR AND DECEPTIVE PRACTICES

***Conrad v. Jimmy John's Franchise, LLC*, Bus. Franchise Guide ¶ 16,821, 2021 WL 718320 (S.D. Ill. Feb. 24, 2021)**

This case is discussed under the topic heading "Labor and Employment."

***Purugganan v. AFC Franchising, LLC*, Bus. Franchise Guide ¶ 16,824, 2021 WL 723916 (D. Conn. Feb. 24, 2021)**

This case is discussed under the topic heading "Definition of Franchise".

VICARIOUS LIABILITY

***C.S. v. Wyndham Hotels & Resorts, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,851, 2021 WL 1264226 (M.D. Fla. April 6, 2021)**

The plaintiff (C.S.), an alleged victim of sex trafficking, filed a complaint alleging violation of the Trafficking Victims Protection Reauthorization Act of 2008 (TVPRA); violation of the Florida RICO statute; premise liability; and negligent hiring, supervision, and retention against Wyndham Hotels & Resorts Inc. (Wyndham), La Quinta Holdings Inc. (La Quinta Holdings), Corepoint Lodging Inc. (Corepoint), CPLG L.L.C. (CPLG), and CPLG FL Properties L.L.C. (CPLG FL). In addition, the plaintiff alleged negligent rescue and aiding, abetting, harboring, confining, coercion, and criminal enterprise against La Quinta Holdings, La Quinta Properties, Inc. (La Quinta Properties), Corepoint, CPLG, and CPLG FL. The U.S. District Court for the Middle District of Florida denied the defendants' motions to dismiss, which argued that the plaintiff had filed a shotgun pleading, that the plaintiff failed to state a claim, and that the premise liability claim was barred by the relevant statute of limitations.

C.S. alleged that she was a victim of continuous sex trafficking at a La Quinta Inn & Suites by Wyndham in Naples, Florida (the La Quinta Hotel) between 2015 and February 2016. The La Quinta Hotel was operated by La

Quinta Holdings, La Quinta Properties, Corepoint, CPLG, and CPLG FL as a franchisee of Wyndham.

The defendants argued that C.S.'s complaint should be dismissed for several reasons. First, they argued that the complaint was a shotgun pleading because the complaint identified the defendants collectively as the "La Quinta Defendants" and grouped all the defendants together. The court explained that one way in which a complaint may constitute an impermissible shotgun pleading is if it "assert[s] multiple claims against multiple defendants without specifying which of the defendants are responsible for which acts or omissions, or which of the defendants the claim is brought against." However, the failure to specify a particular defendant is not fatal when the complaint can be read to aver that all defendants are responsible for the alleged conduct. Thus, although the court noted that the complaint did repeatedly refer to the defendants collectively as the "La Quinta Defendants," the court also found that the complaint could be read to allege that each of the defendants was involved in the identified conduct attributed to the "La Quinta Defendants." Therefore, the court found that the complaint did not constitute a shotgun pleading.

Next, the defendants argued that certain claims should be dismissed due to C.S.'s failure to state a claim. The defendants' motions to dismiss challenged the sufficiency of the alleged violation of the TVPRA. To state a claim under Section 1595(a) of the TVPRA, a plaintiff must plausibly allege that she was a victim of a criminal offense under Section 1595(a) and that the defendant knowingly benefited financially or by receiving something of value, from participation in a venture engaged in sex trafficking. The motions to dismiss argued that the complaint's allegations were insufficient to state a claim under Section 1595(a). First, the motions argued that the complaint lacked well-pled allegations that the defendants participated in a "venture." Based on the definition of "venture" used in the criminal portion of the TVPRA, the motions asserted that a "venture" requires two or more individuals "associated in fact." Using the federal RICO definition of "enterprise," the motions argued that "associated in fact" requires that persons must operate as a "continuing unit that functions with a common purpose." The motions argued that, in the context of a TVPRA claim against a hotel operator, the complaint must, at a minimum, allege a "continuous business relationship between the trafficker and the hotels," such that it would appear that the trafficker and the hotels had established a pattern of conduct or a tacit agreement. The defendants also argued that "participation" in a venture required an allegation of an overt act and that failure to prevent sex trafficking was not an overt act.

C.S.'s complaint alleged that the defendants participated in a venture by engaging in a pattern of acts and omissions that were intended to support, facilitate, harbor, and otherwise further the traffickers' sale and victimization of C.S. by repeatedly renting rooms at the La Quinta Hotel to people that the defendants knew or should have known were engaged in sex trafficking.

The complaint also alleged that the defendants should have been on notice of the sex trafficking and that they failed to prevent it. The court found the allegations sufficient to allege participation in a venture and stated that the "overt act" argument was not convincing due to the defendants' lack of controlling authority in support of the argument.

The motions also argued that the complaint insufficiently alleged that the defendants knowingly benefitted *from* participation in a venture that committed TVPRA crimes, with knowledge of the causal relationship. The motions argued that the allegation that the defendants benefited from the operation of the La Quinta Hotel generally was insufficient. The complaint alleged that the defendants knowingly benefited from the sex trafficking of C.S. by receiving payment for the rooms rented for C.S. and her traffickers at the La Quinta Hotel and by receiving other financial benefits in the form of food and beverage sales and ATM fees from those persons who were engaged in sex trafficking. As to the franchisor, Wyndham, the complaint alleged that it received a significant franchise fee and continuous royalties on the La Quinta Hotel's gross revenue, while also exercising ongoing and systematic control over the La Quinta Hotel's operations. The court found these allegations sufficient to satisfy the "knowingly benefitted" element.

The motions further argued that the complaint failed to plausibly allege that the defendants knew or should have known that the "venture" was engaging in sex trafficking crimes. The motions argued that the complaint only alleged that the hotel staff did not interfere with witnessed indicia of commercial sex activity but that the allegations do not give rise to a reasonable inference that the defendants knew or should have known about any *forced* commercial sex activity. The court disagreed with this argument. First, the court stated that knowledge and other conditions of a person's mind "may be alleged generally." Second, the court noted that C.S. made sufficient allegations to reasonably infer the defendants knew or should have known of the sex trafficking venture.

In addition, the motions argued that C.S. insufficiently pled the enterprise element of her claim under Florida's civil RICO statute. Florida's RICO statute defines *enterprise* to include a "group of individuals associated in fact although not a legal entity." C.S. must allege that a group of persons shares a purpose, relationships among those associated with the enterprise, and longevity sufficient to permit these associates to pursue the enterprise's purpose. The motions argued that the complaint failed to sufficiently allege a "common purpose" among the defendants. The court found C.S.'s allegation that the defendants associated with each other and/or C.S.'s sex traffickers for the common purpose of profiting off an established sex trafficking scheme sufficient to allege the defendants constituted an enterprise under Florida's RICO statute. The motions also argued that the complaint failed to sufficiently plead the "pattern of criminal activity" element of the Florida RICO statute for the same reasons that C.S. failed to state a TVPRA claim. The court, however, determined that C.S.'s TVPRA claim was sufficiently pled and therefore also rejected the motions' argument as to the Florida RICO claim.

The motions next argued that C.S.'s premise liability claim was insufficient. A premise liability claim is a form of negligence action. In addition to the elements of negligence (duty, breach, harm, and proximate cause), premise liability also includes the defendant's possession or control of the premises and notice of the dangerous condition. The motions argued that the premise liability claim should be dismissed because it was barred by the relevant statute of limitations and was insufficiently pled.

Under Florida law, the statute of limitations for negligence claims is four years. C.S. alleged that the sex trafficking occurred at the La Quinta Hotel from approximately 2015 to February 2016; because the complaint was filed in August 2020, the defendants argued that the premise liability claim was time barred. The court found that C.S alleged she was a repeat victim of sex trafficking between 2015 and February 2016, such that her allegations were sufficient to invoke the continuing tort doctrine. Thus, the court found that C.S.'s premise liability claim did not accrue until February 2016 (when the continuing tort ended) and therefore that she had until February 2020 to file a complaint asserting premises liability. C.S. met this deadline, according to the court, by filing her first amended complaint against Wyndham on December 31, 2019. Although the court determined severance of the parties was appropriate in the original action, the court found that the December 2019 date was applicable for statute of limitations purposes under the relation-back provisions of Rule 15(c) of the Federal Rules of Civil Procedure. Under Rule 15, a claim in an amended complaint relates back to the filing date of the original complaint if it "asserts a claim or defense that arose out of the conduct, transaction, or occurrence set out—or attempted to be set out—in the original pleading." Since the court did not find it apparent from the face of the complaint that the claim against Wyndham was time-barred, the court found that dismissal on the statute of limitations affirmative defense was not appropriate. Although La Quinta Holdings, Corepoint, CPLG, and CPLG FL were not named in the December 2019 first amended complaint, C.S. requested that the court permit discovery to occur to determine whether Wyndham may have notified other defendants when the lawsuit was originally filed in December 2019, pursuant to the terms of the franchise agreement (as such notification could permit relation-back). The court agreed to permit this discovery and thus denied defendants' motion to dismiss on the statute of limitations grounds.

The motions to dismiss also argued the premise liability claim was insufficiently pled because it did not allege the defendants possessed or controlled the La Quinta Hotel. The court disagreed, noting that the complaint alleged that the defendants were the "owners, operators, managers, supervisors, controllers and innkeepers" of the La Quinta Hotel, and that Wyndham exercised control over the means and methods of the hotel's operations. In addition, the motions to dismiss argued the premise liability claim was insufficiently pled because the criminal conduct was not foreseeable, such that the defendants had no duty to protect C.S. from such conduct. The court found that the complaint contained sufficient allegations that sex trafficking was occurring at the La Quinta hotel and that the defendants knew or should have known it. Under Florida law, a business owes invitees a duty to use due care to maintain its premises in a reasonable safe condition, including to protect customers from criminal attacks that are reasonably foreseeable. Foreseeability can be established either by showing that a proprietor knew or should have known of a dangerous condition on its premises that would be likely to cause harm to a plaintiff or by showing that a proprietor knew or should have known of the dangerous propensities of a particular patron. Finally, the motions argued that the premise liability claim lacked any allegation supporting causation. The court noted that the complaint alleged that the defendants were on notice of the sex trafficking and not only failed to prevent it, but knowingly turned a blind eye to it in exchange for increased profits. The court found that the allegations of C.S.'s various injuries and damages were sufficient to allege proximate cause to defendants' willingness to turn a blind eye. Thus, the court found that the premise liability claim was sufficiently pled.

Defendants also argued that the negligent hiring, supervision, and retention claim was insufficiently pled. To state this claim under Florida law, the plaintiff must establish that the employer owed a legal duty to the plaintiff to exercise reasonable care in hiring and retaining safe and competent employees. Florida law also holds employers liable for reasonably foreseeable damages resulting from the negligent training of its employees and agents. The complaint alleged that each defendant was in control of the hiring, instructing, training, supervising, and terminating of hotel employees and that the defendants knew or should have known that the hotel employees were allowing criminals to rent rooms for prostitution and drug dealing, failing to identify and/or report sex trafficking, and failing to refuse lodging services to sex traffickers. The motions to dismiss argue that the claim fails because it lacks sufficient factual allegations that the defendants knew or should have known of any unfit employees and hired or employed any of the employees at issue. The court found that the complaint, which alleged facts suggesting sex trafficking was occurring at the hotel, that the employees knew of it and failed to prevent it, and that the defendants had control over the employees, contained sufficient allegations at this stage of the proceedings.

The defendants also argued that C.S. failed to sufficiently allege the negligent rescue claim. The complaint alleged the defendants, as the owners and operators of the La Quinta Hotel, had a duty to keep the premises safe and prevent foreseeable criminal activity, as well as a duty to make safe a dangerous condition at the La Quinta Hotel and to rescue their hotel guests, including C.S., from the peril they created. The complaint alleged that the defendants breached these duties by various acts and omissions and that the sex trafficking of C.S. was the direct and foreseeable result. The motions to dismiss argued that the negligent rescue was insufficiently pled under the "rescue doctrine." There is no common law duty to rescue a stranger. Under Florida law, the rescue doctrine holds a tortfeasor liable for injuries to a third party who is hurt in attempting to rescue the direct victim of the tortfeasor. The basic concept of the rescue doctrine "is that the person who has created a situation of peril for another will be held in law to have caused peril not only to the victim, but also to his rescuer, and thereby to have caused any injury suffered by the rescuer in the rescue attempt." The court found that the rescue doctrine was not implicated by C.S.'s negligent rescue claim because the rescue doctrine is related to, but separate from, the affirmative duty to rescue an imperilled party. Thus, the court denied the defendants' request for dismissal based on the rescue doctrine.

Finally, the defendants argued that C.S.'s claim for aiding and abetting was insufficiently pled because it failed to articulate a cognizable, independent cause of action, and purported to assert multiple claims in a single count. Under Florida law, the following elements must be alleged to state a claim for aiding and abetting a common law tort: (1) an underlying violation on the part of the primary wrongdoer; (2) knowledge of the underlying violation by the alleged aider and abettor; and (3) the rendering of substantial assistance in committing the wrongdoing by the alleged aider and abettor. The court found that C.S.'s allegations were not impermissibly vague and were sufficient to state a claim for aiding and abetting. Thus, the court denied the defendants' request for dismissal on these grounds.

***McNeel v. Kiddie Academy Domestic Franchising, LLC*, Bus. Franchise Guide (CCH) ¶ 16,830, 2021 WL 920108 (S.D. Tex. Mar. 10, 2021)**

Jared and Lindsey McNeel (McNeel), parents of a child who was found dead in her crib at a franchised Kiddie Academy location, filed a wrongful-death suit against the franchisor, Kiddie Academy Domestic Franchising, LLC (Kiddie Academy). Kiddie Academy moved for summary judgment, on the basis that it was not vicariously liable for the franchisee's negligence. The court disagreed and denied Kiddie Academy's motion for summary judgment.

The McNeels alleged multiple theories of vicarious liability, including contractual control—the notion that the franchise agreement afforded Kiddie Academy significant control over the franchisee, such that its negligence should be imputed to Kiddie Academy. The court determined that this was a question of law and therefore could not be properly resolved on summary judgment.

The court noted that, although the franchise agreement expressly designated the franchisee as an independent contractor (and employers generally have no duty to ensure that an independent contractor performs its work in a safe manner), employers "can be held vicariously liable for the actions of an independent contractor if the employer retains some control over the manner in which the contractor performs the work that causes the damage." A contract may spell out the level of control that one party has over another, thereby creating a duty of care. The duty of care is commensurate with the control retained over the contractor.

The parties disputed the level of control the franchise agreement gave Kiddie Academy. Kiddie Academy argued that the contract gave it merely supervisory control over the franchisee and, as a result, Kiddie Academy's duty was only to ensure that the procedures that it promulgated did not unreasonably increase the probability and severity of injury. The McNeels argued that the contract permitted Kiddie Academy to control the "operative details" of the franchisee's work. As a result, the McNeels argued that the franchisee's negligence should be imputed to Kiddie Academy. The Court agreed with the McNeels, stating that the franchise agreement (like many franchise agreements) allowed it a degree of control over the "big-picture operations" of the franchisee, including the right to inspect the facility, provide plans and specifications, train the franchisee's childcare directors, and require the franchisee to follow certain standards of practice and internal operating procedures (including the "Kiddie Academy Infant/Toddler Safe Sleep Policy").

The court acknowledged that merely retaining supervisory rights ordinarily would not rise to a degree of control high enough to impute liability. The court distinguished Kiddie Academy's level of control from the contractual provisions that appear in other franchisor's franchise agreements (which, other courts concluded, did not give rise to liability, as the right to control did not reach the "operative details" of the franchisee's work). Here, the court concluded that the franchise agreement provided that in the event of a default (e.g., if the franchisee operated in a dangerous manner or failed to follow Kiddie Academy's procedures), Kiddie Academy may enter the premises and exercise "complete authority" with respect to the operation of the franchised business until Kiddie Academy determined that the default had been cured. The court found that this right under the franchise agreement gave Kiddie Academy control over the "operative details" of a franchisee's work. Even though Kiddie Academy was not exercising this right of control at the time of the child's death, the court focused on the fact that Kiddie Academy had this right of control, not whether actual control was exercised. The fact that no actual control was exercised could not absolve the franchisor of liability. The right to exercise that control was sufficient to impart liability. Thus, the court held that Kiddie Academy exposed itself to vicarious liability for the franchisee's negligence and denied Kiddie Academy's motion for summary judgment.

***Rivers v. International House of Pancakes*, Bus. Franchise Guide (CCH) ¶ 16,843, 2021 WL 860590 (S.D.N.Y. Mar. 8, 2021)**

This case is discussed under the topic heading "Labor and Employment."