Employee "No-Poach" Agreements Draw Antitrust Attention and Debate

March 15, 2019

Since the fall of 2016, federal, state, and private enforcers have sharpened their focus on allegedly anticompetitive restrictions in labor markets: so-called "no-poach" and wage-fixing agreements. This remains a hotly debated topic, with the Department of Justice ("DOJ") and the Washington State Attorney General this month submitting consolidated amicus briefs in three proposed antitrust class actions filed in a Washington federal court dueling over the appropriate legal standard. Nevertheless, it is becoming clear that while certain restrictions—"naked"[1] agreements on hiring between competitors for employees—carry grave risk of both criminal penalties and treble civil damages, other restrictions on employee hiring may be permissible, at least under federal law, if properly structured.

Debevoise & Plimpton

Enforcers' sharpened focus. In October 2016, the DOJ and the Federal Trade Commission issued their landmark Antitrust Guidance for Human Resources Professionals ("2016 Guidance"), expounding the agencies' position that naked agreements between companies not to compete for each other's employees (a.k.a. "no-poach" agreements) and naked wage-fixing agreements among employers are *per se* illegal under the antitrust laws and that the DOJ would seek criminal penalties against companies using those agreements.

In January 2018, Principal Deputy Assistant Attorney General Andrew Finch announced that the DOJ would proceed criminally against any naked no-poach or wage-fixing agreement that began or continued after the 2016 Guidance was issued; by April, the DOJ disclosed that active investigations were underway. That same month, the DOJ filed a civil[2] settlement with competitors in the railway industry that allegedly had entered into naked no-poach agreements.

Since the DOJ's announcements, the states have begun their own enforcement activity. The Washington State Attorney General has been particularly aggressive, entering into agreements to eliminate no-poach provisions in franchise agreements with more than

---

1 Under the doctrine of ancillary restraints, an agreement is "naked" if it is not reasonably necessary to any separate, legitimate business collaboration between the parties.

2 Exercising its prosecutorial discretion, the DOJ treated these companies' conduct as a civil violation because the alleged agreements had terminated prior to the 2016 Guidance's issuance.

fifty companies and suing one—Jersey Mike's Subs—in state court after it refused to remove the provision. In July 2018, a coalition of attorneys general covering ten states and the District of Columbia opened an investigation into fast-food franchisors' use of no-poach provisions; on March 12, 2019, four of those franchisors—Dunkin', Arby's, Five Guys, and Little Caesars—entered into a settlement with 13 states and the District of Columbia, agreeing to stop including no-poach provisions in their franchise agreements, and to stop enforcing any already in place.

Following these governmental investigations, franchise employees have filed private class actions in federal courts nationwide. Lawsuits are now pending against fast-food restaurants, tax preparation services, car repair services, and other franchise-based businesses that have agreements barring franchisees from hiring each other's employees. These private actions typically allege that the no-poach provision in the franchise agreement violates Section 1 of the Sherman Act and call for *per se* treatment of the restraint.

Different analytical frameworks: DOJ vs. Washington State AG. During the last five weeks, the DOJ has weighed in repeatedly on which no-poach agreements should be subject to *per se* invalidity and which should be analyzed under the rule of reason, which balances a restraint's procompetitive and anticompetitive effects. The DOJ has filed three amicus briefs in five pending civil actions in federal courts in North Carolina, Pennsylvania, and Washington challenging no-poach agreements, and on March 1, 2019, Deputy Assistant Attorney General Michael Murray delivered remarks summarizing the agency's analytical framework on the issue. These sources have made clear the agency's position on the legal standards governing no-poach agreements, which can be summarized as follows:

- A no-poach agreement among employers that compete with each other for employees (even if their products or services do not compete):
  - is *per se* unlawful if "naked" and will be pursued criminally by the DOJ if the activity began or continued after October 2016; but
  - is analyzed under the rule of reason if the restraint is ancillary to and reasonably necessary for a separate legitimate transaction or collaboration, such as a joint venture, merger, or franchising agreement.
- A no-poach agreement among entities that do not compete for employees and are vertically related in their industry, such as most franchisors and franchisees, is analyzed under the rule of reason.

On March 11, 2019, the Washington State AG filed an amicus brief in the three civil actions pending in a Washington federal court advocating different legal standards governing no-poach agreements. AG Ferguson first noted that Washington State's and federal antitrust laws differ. Thus, a court applying state law could find that no-poach provisions in franchise agreements are *per se* unlawful notwithstanding their legality under the Sherman Act. Second, the AG argued that a franchisor and its franchisees can be in a horizontal relationship, such as when a franchisor owns and operates its own stores, and so any no-poach agreement between those entities should presumptively be analyzed as a *per se* restraint (consistent with the DOJ's approach). However, AG Ferguson advocated for "a heavy burden" on a franchisor to show that a no-poach provision satisfies the ancillary restraint doctrine, given Washington State's view, informed by its investigation, that these provisions are not reasonably necessary to legitimate franchising relationships.

How this might affect you. These dueling amicus briefs are merely statements of enforcement positions, and we must wait for the courts to establish the proper legal standard for analyzing hiring restrictions. Nonetheless, it is clear that entering into or continuing to engage in a naked no-poach or wage-restriction agreement carries a substantial risk of criminal penalties and civil treble damages. And under federal law, the rule of reason analysis should prevail in either of two circumstances: (1) the restriction is between parties that do not actually compete in the labor market, including between franchisees and a franchisor that does not own and operate stores; or (2) the restriction is between competitors for employees but that restriction is ancillary to and reasonably necessary for a separate, legitimate venture between the competitors, such as a joint venture or merger. An open issue that may be addressed in the pending cases is the legality of a hiring restriction between franchisees and a franchisor that also owns and operates stores. Washington State likely would advocate for *per se* treatment; the DOJ appears open to treating such restraints as ancillary and thus potentially lawful under the rule of reason. In all cases, parties considering entering into hiring restrictions must be prepared to justify their lack of competition in the labor market or the necessity of the restrictions and their procompetitive justifications.

How Debevoise can help. Debevoise lawyers are well versed in the evolving law in this area. We are available to advise parties regarding the legality of their proposed restrictions, as well as to guide clients through any government investigation and/or litigation related to preexisting ones.

* * *

Please do not hesitate to contact us with any questions.

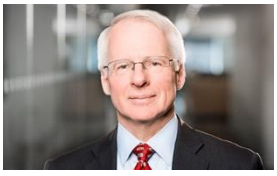
WASHINGTON, D.C.

Ted Hassi
thassi@debevoise.com

Leah Martin
lmartin@debevoise.com

NEW YORK

Daniel M. Abuhoff
dmabuhoff@debevoise.com



Gary W. Kubek
gwkubek@debevoise.com

Michael Schaper
mschaper@debevoise.com

Erica S. Weisgerber
eweisgerber@debevoise.com