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Implications of the Federal Antitrust Laws On Franchising

Opposing a Franchisor's Motion for Summary Judgment In Federal Court

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This article explains how a franchisee who files a federal court action alleging violations of federal antitrust laws should respond to a franchisor's motion for summary judgment.

Franchisor's Violations of Federal Antitrust Laws

In *Siegel v. Chicken Delight Inc.*, 448 F.2d 43 (9th Cir. 1971), the 9th U.S. Circuit Court of Appeals held that:

> Under the per se theory of illegality, plaintiffs are required to establish not only the existence of a tying arrangement but also that the tying product possesses sufficient economic power to appreciably restrain free competition in the tied product markets. *N. Pac. R.R. Co. v. United States. supra.*
>
> Chicken Delight notes that while it was an early pioneer in the fast-food-franchising field, the record establishes that recently there has been a dramatic expansion in this area, with the advent of numerous firms, including many chicken franchising systems, all vigorously competing with each other.
>
> Under the circumstances, the franchisor contended that the existence of the requisite market dominance was a jury question.

The District Court ruled, however, that Chicken Delight's unique registered trademark, in combination with its demonstrated power to impose a tie-in, established as matter of law the existence of sufficient market power to evaluate the case under the Sherman Act.

We agree. In *Fortner Enterprises Inc. v. United States Steel Corp.,* 394 U.S. 495 (1969), the court said: "The standard of 'sufficient economic power' does not, as the District Court held, require that the defendant have a monopoly or even a dominant position throughout the market for the tying product. Our tie-in cases have made unmistakably clear that the economic power over the tying product can be sufficient even though the power falls far short of dominance and even though the power exists only with respect to some of the buyers in the market."

Later, the court said: "Accordingly, the proper focus of concern is whether the seller has the power to raise prices or impose other burdensome terms such as a tie-in, with respect to any appreciable number of buyers within the market." 448 F.2d at 49-50.

The 9th Circuit went on to hold that:

> One cannot immunize a tie-in from the antitrust laws by simply stamping a trademark symbol on the tied product, at least where the tied product is not itself the product represented by the mark. 448 F.2d at 52.

Finally, the 9th Circuit cited *United States v. Loew's Inc.*, 371 U.S. 38 (1962), in which the U.S. Supreme Court held that:

> Even absent a showing of market dominance, the crucial economic power may be inferred from the tying product's desirability to consumers or from uniqueness in its attributes. 448 F.2d at 50.

The plaintiff franchisee should show that this ties in with the unique services (specified in great detail in the complaint as to what makes this franchisor's products and services different from those offered by other companies) provided by the defendant franchisor, and demonstrates the validity and applicability of the plaintiff franchisee's antitrust claims to a franchisor-franchisee relationship.

The plaintiff franchisee should demonstrate how the antitrust counts (Sherman Antitrust Act, Clayton Act and Robinson-Patman Act) have been pleaded in great detail and contain all the elements required to proceed to trial.

Details should show the defendant franchisor's specific violations of the Sherman Antitrust, Clayton and Robinson-Patman Acts.

The plaintiff franchisee should show that the defendant franchisor's status as the only company providing its unique services and having control of 100 percent (or as high a percentage as possible that can be justifiably computed) of the market for the unique services.

The plaintiff franchisee should demonstrate:

- The defendant franchisor's improper pricing as to the plaintiff franchisee, the defendant franchisor's franchisees and the public;
- Restrictions on the purchases and sales by franchisees and the plaintiff franchisee; and
- Restrictions on the method by which franchisees and the plaintiff franchisee must conduct business have resulted in the defendant franchisor's creating a monopoly.

The plaintiff franchisee should show that the defendant franchisor's interstate presence affects a substantial amount of interstate commerce and that its monopoly power extends in interstate commerce.

The plaintiff franchisee also should show that the defendant franchisor's having monopoly power in the market concerning its pricing policies to franchisees and the public, franchise matters, and all other aspects regarding its operations in the state in which it is located and in interstate commerce.

In *Chicken Delight* the franchisor specified from whom supplies had to be purchased regardless of performance because of kickbacks/rebates, which amount to the same thing as the premium charged by Chicken Delight.

The 9th Circuit shows that the franchisor-franchisee relationship does not immunize the franchisor from antitrust violations and in fact actually can contribute to violations of the antitrust statutes.

The plaintiff franchisee should show that the defendant franchisor causes franchisees and the plaintiff franchisee to pay higher prices for goods and services from the defendant franchisor and its suppliers. It also should show how the defendant franchisor harmed the plaintiff franchisee and the public.

The franchisee should show how the defendant franchisor's actions force its franchisees to charge higher prices to the public, engage in improper pricing of the delivery and providing of goods and services to its franchisees, the plaintiff franchisee and the public.

The franchisee also should show that the requirement that franchisees use architects, suppliers, uniforms and contractors specified by the defendant franchisor results in higher costs without a corresponding increase in quality.

In addition the franchisee should show that the defendant franchisor prohibits the franchisees from selling products at wholesale or for resale.

Finally, the franchisee should show that the defendant franchisor's illegal "tying arrangement" exploit its control over a "tying product" (the franchise) to force the plaintiff franchisee to accept the tied products (the defendant franchisor's products and services).

In *Alan's of Atlanta Inc. v. Minolta Corp.*, 903 F .2d 1414 (11th Cir . 1990), the 11th Circuit reversed the lower court's grant of summary judgment to the defendant franchisor, finding a genuine issue of material fact about whether an antitrust injury was inflicted upon the appellant.

In *Midwestern Waffles Inc. v. Waffle House Inc.,* 734 F.2d 705 (11th Cir. 1984), the case turned on the fact that the

plaintiff franchisee did not have standing to bring an antitrust claim. The 11th Circuit, however, held that:

> Antitrust cases by their very nature often are poorly suited for disposition by summary judgment motion since antitrust cases often raise questions of motive, credibility and conspiracy. C. Wright & A. Miller, Federal Practice & Procedure, § 2732, at 608-10 (1973). *See Poller v. Columbia Broadcasting System Inc.,* 386 U.S. 464, 82 S. Ct. 486, 7 L. Ed. 2d 458 (1962). 734 F.2d at 717.

In *Kypta v. McDonald's Corp.,* 671 F.2d 1282 (11th Cir. 1982), *cert. denied,* 459 U.S. 857 (1982), the court noted that the franchisor:

> Required all prospective franchisees to purchase from it a number of cookers, fryers, packing supplies and mixes as a condition of obtaining a license to use the Chicken Delight trademark. The trial judge found that all the elements of a tying arrangement, including actual injury, were reflected in this requirement. 671 F.2d at 1285.

The plaintiff franchisee should show that it was required to purchase its goods and services from the defendant franchisor and its suppliers and contractors.

It also should show that it was required to sell certain products and services.

These actions should help demonstrate the defendant franchisor's *per se* violation of the Sherman Antitrust Act (forced purchases, sales and prohibitions) and violation of Section 1 of the Sherman Antitrust Act due to the defendant franchisor's illegal tying arrangement, actions affecting the plaintiff franchisee, the consumers of the states in which the defendant franchisor conducted business and interstate commerce.

The relevant market for the franchisor's operations should be defined. This also should show the defendant franchisor's violation of the "rule of reason" and the defendant franchisor's willful maintenance of its monopoly power.

Marts v. Xerox Inc., 77 F.3d 1109 (8th Cir. 1996), held that "[e]ven if the products are available separately, an illegal tying arrangement can exist if purchasing the items together is the only viable economic option." 77 F.3d at 1113.

The plaintiff franchisee should show that this is what occurs with the purchase of a franchise. In this case the products are sold as a unit by the defendant franchisor in its sale of its franchise by virtue of the requirement of using the defendant franchisor's approved suppliers.

Private antitrust actions, such as this, are the only means by which injured individuals or businesses can recover their damages under the antitrust laws. *See Hanover Shoe v. United Shoe Mach. Corp.,* 392 U.S. 481, 494 (1968); *Perma Life Mufflers v. Int'l Parts Corp.,* 392 U.S. 134, 139 (1968). *See also Zenith Radio Corp. v. Hazeltine Research,* 395 U.S. 100, 131 (1969); *Minn. Mining & Mfg. Co. v. N.J. Wood Finishing Co.,* 381 U.S. 311, 318 (1965). *Accord Kelco Disposal v. Browning-Ferris Indus.*, 845 F.2d 404, 411 (2d Cir. 1988), *aff'd,* 492 U.S. 257 (1989); *Monarch Life Ins. Co. v. Loval Protective Life Ins. Co.,* 326 F.2d 841, 845 (2d Cir. 1963), *cert. denied,* 376 U.S. 952 (1964).

As to the pleading of an antitrust claim, as the 2nd Circuit held in *Nagler v. Admiral Corp.,* 248 F.2d 319 (2d Cir. 1957), an antitrust complaint need not spell out detailed facts and need only satisfy the liberal notice pleading requirements of Rule 8(a). *Accord, e.g., Barr v. Dramatists Guild,* 573 F. Supp. 555, 559 (S.D.N.Y. 1983) (the plaintiff franchisee "is not required to provide detailed allegations"); *Broadcast Music v. Hearst/ABC Viacom Entm't Servs.,* 746 F. Supp. 320, 326 (S.D.N.Y. 1990) ("[a]ntitrust allegations, however, are governed by the 'short and plain statement' requirement of Rule 8(a)"); *Newburger Loeb & Co. v. Gross,* 365 F. Supp. 1364, 1367-68 (S.D.N.Y. 1973) ("skeletal" allegations survive a motion to dismiss).

The courts have gone so far as to say that an antitrust complaint need only furnish "some clue as to what conduct by the defendant franchisor is claimed to constitute an illegal contract combination and conspiracy." *Klebanow v. N.Y. Produce Exch.,* 344 F.2d 294, 299 (2d Cir. 1965). *See* also, *Radovich v. Nat'l Football League,* 352 U.S. 445, 453 (1957) (dismissal of an antitrust claim is appropriate only if it is "wholly frivolous"); *United States v. Employing Plasterers Ass'n of Chicago,* 347 U.S. 186, 189 (1954); *Three Crown Partners v. Caxton Corp.,* 817 F. Supp. 1033, 1047 (S.D.N.Y. 1993).

In *Levine v. Central Florida Medical Affiliates,* 72 F.3d 1538 (11th Cir. 1996), a case involving a motion for summary judgment, the 11th Circuit said:

> The District Court had granted a motion for a directed verdict "before (the plaintiff franchisee) reached that part of his case involving restraint on competition." *Id.* at 829. We criticized the District Court's premature ruling and stated that "the better course would have been to defer ruling on the motions for directed verdict until after (the plaintiff franchisee) had presented his entire Section 1 case." *Id.* at 828. 72 F.3d at 1555. [Emphasis added].
>
> A claim for conspiracy to monopolize, on the other hand, does not require a showing of monopoly power. 72 F.3d at 1556.

In *Collins v. International Dairy Queen Inc.,* 980 F. Supp. 1252 (M.D. Ga. 1997), the defendant franchisor sought summary judgment against the franchisees' claims that the franchisor had violated the Sherman Antitrust Act. The court denied the defendant franchisor's motion for summary judgment, saying it failed to prove that there was no genuine issue of material fact. In *Collins*, as in the instant case, franchisees were prohibited from purchasing supplies from anyone not approved by the franchisor. The court held that:

> Because the restrictions imposed by the defendant franchisor prevent franchisees from being able to react to higher prices by purchasing competing products elsewhere, it is reasonable to conclude that there is a lack of interchangeability or cross-elasticity of demand between approved Dairy Queen products and similar non-approved products. 980 F. Supp. at 1259.

The plaintiff franchisee should show that there are genuine issues concerning whether the franchisor's anti-competitive actions and the limited choices available to the franchisees had destroyed the interchangeability or cross-elasticity of demand between products approved by franchisers and other similar products.

Tominaga v. Shepherd, 682 F. Supp. 1489 (C.D. Cal. 1988), held that:

> Tying arrangements, therefore, receive per se condemnation only when "the seller has some special ability, usually called "market power," to force a purchaser to do something that he would not do in a competitive market." *Hyde*, 466 U.S. at 13-14, 104 S. Ct. at 1558-1559. 682 F. Supp. at 1493.

The plaintiff franchise should show that the defendant franchisor has this "special ability" as a result of the franchisor-franchisee relationship it had with the plaintiff franchisee. It also should show that the defendant franchisor specifically prohibited and provided negative inducements for the plaintiff franchisee to purchase products on the open market. *Tominaga* went on to hold that:

> Courts have identified three sources of market power: (1) when the government has granted the seller "a patent or similar monopoly over a product," (2) when the seller's share of the market is high and (3) when the seller offers a "unique" product that competitors are not able to offer. *Mozart*, 833 F.2d at 1345-1346.

The District Court in *In Re Mercedes-Benz Antitrust Litigation,* 157 F. Supp. 2d 355 (D.N.J. 2001), said:

> The defendant franchisor complains that the plaintiff franchisees have made no attempt to define either a geographic or product market in which the defendant franchisor is alleged to have wrongfully conspired to interfere with competition. The defendant franchisor argues that this lack dooms the complaint. The plaintiff franchisee responds that their allegations state a *per se* violation of the Sherman Act. The plaintiff franchisee submits that where a *per se* violation is pled, as distinct from a violation subject to "rule of reason" analysis, no market definition is required. The plaintiff franchisee [is] correct on both points. 157 F. Supp. 2d at 359 [emphasis added].

The plaintiff franchisee should show that the defendant franchisor's unique services cannot be exchanged for similar services provided by others because of the contractual restraints provided by the franchise agreement. This analysis that must be used to determine cross-elasticity of demand, which is at the core of the issue.

Standards for a Motion for Summary Judgment

The Supreme Court held in *Associated Press v. United States,* 326 U.S. 1 (1945); 326 U.S. 802, *reh'g denied* (1945); and 326 U.S. 803, *reh'g denied* (1945), that:

> Rule 56 [of the Federal Rules of Civil Procedure] should be cautiously invoked to the end that parties may always be afforded a trial where there is a bona fide dispute of facts between them. *Sartor v. Ark. Natural Gas Corp.,* 321 U.S. 620. 326 U.S. at 6.

Summary judgment is a tool to be used sparingly, and trial judges should be slow in disposing of a case of any complexity on a motion for summary judgment. *S.J. Groves & Sons Co. v. Ohio Turnpike Comm'n,* 315 F.2d 235 (6th Cir. 1963); 375 U.S. 824, *cert. denied* (1963); *Tee-Pak Inc. v. St. Regis Paper Co.,* 491 F.2d 1193 (6th Cir.).

Summary judgment is a lethal weapon. Courts must be mindful of its aims and targets and beware of overkill in its use. *Brunswick Corp. v. Vineberg*, 370 F.2d 605 (5th Cir. 1967).

Summary judgment pursuant to Federal Rule of Civil Procedure 56 ordinarily is not a proper vehicle for resolution of disputes concerning state of mind and interpretations of perceived events. *Schmidt v. McKay*, 555 F.2d 30 (2d Cir. 1977).

The plaintiff franchisee should show that the facts presented thus far do not meet the standard for summary

judgment and that there are numerous material and disputed-facts issues.

Testimony by the defendant franchisor during their depositions can provide very convincing proof as to the factual conflicts in the case.

Summary and Conclusion

By taking a step-by-step approach, a plaintiff franchisee should be able to demonstrate enough facts to show that the defendant franchisor's motion for summary judgment concerning its alleged violations of federal antitrust laws should not be granted.

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