

Three Out of Four Economists Recommend Raising the  
Minimum Wage! A Closer Look at the Debate  
Surrounding Seattle’s Minimum Wage Ordinance

*Erica Bergmann\**

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\* J.D. Candidate at Seattle University School of Law. I want to sincerely thank the 2014–15 and 2015–16 members of *Seattle University Law Review*. Without their dedicated effort helping me draft and edit this Note, publication would not have been possible.

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#### INTRODUCTION

Minimum wage laws in the United States had a rocky start at the beginning of the twentieth century.<sup>1</sup> States were the first to enact these laws, which were met with a series of constitutional challenges under the Fifth Amendment.<sup>2</sup> Initially, the U.S. Supreme Court consistently struck down minimum wage laws as impinging on freedom of contract.<sup>3</sup> It wasn't until 1937 that the Court reversed these rulings, determining that freedom of contract was not in fact protected by the Constitution.<sup>4</sup> The next year, Congress adopted a national minimum wage standard by passing the Fair Labor Standards Act.<sup>5</sup> Ever since, all fifty states have been bound to enforce, at a minimum, the federal minimum wage standard.<sup>6</sup>

As of early 2015, the federal minimum wage was \$7.25 per hour,<sup>7</sup> but twenty-nine states, and Washington D.C., have enacted statutes setting the minimum wage higher than this required minimum standard.<sup>8</sup> Washington State's minimum wage of \$9.47 per hour is currently the highest of any state in the nation.<sup>9</sup> Current trends show cities enacting

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1. See Clifford F. Thies, *The First Minimum Wage Laws*, 10 CATO J. 715 (1991). The first hint of a minimum wage law was in Massachusetts in 1912 but was virtually unenforced. As other states adopted laws, they too had weak or nonexistent enforcement measures or were struck down by the U.S. Supreme Court as well as states' own supreme courts. *Id.* at 716–19.

2. *Id.* at 716–17.

3. *E.g.*, *Adkins v. Children's Hosp. of D.C.*, 261 U.S. 525, 545 (1923). The Due Process Clause of the Fifth Amendment was said to protect freedom of contract, which included the freedom to negotiate wages. *Id.*

4. Thies, *supra* note 1, at 720; see also *West Coast Hotel Co. v. Parrish*, 300 U.S. 379 (1937) (ruling that a Washington State minimum wage law was constitutional in a 5–4 decision).

5. 29 U.S.C. § 206 (2012); Thies, *supra* note 1, at 720.

6. 29 U.S.C. § 206 (2012).

7. *Minimum Wage Laws in the States – January 1, 2015*, U.S. DEP'T LAB. WAGE & HOUR DIVISION, <http://www.dol.gov/whd/minwage/america.htm> (last visited Mar. 18, 2015).

8. *Id.*

9. *Id.* But Washington D.C. has a higher minimum wage of \$9.50 per hour. *Id.*

local ordinances establishing a city-wide minimum wage.<sup>10</sup> The Seattle City Council, by a unanimous vote in June 2014, enacted an ordinance implementing a plan to gradually increase the city minimum wage to \$15 per hour,<sup>11</sup> an increase of over 60%.<sup>12</sup> The Minimum Wage Ordinance (Seattle Ordinance) went into effect April 1, 2015.<sup>13</sup> Almost as soon as the legislation was passed, there was backlash<sup>14</sup> from a group of local independent businesses and the International Franchise Association (IFA), leading to the IFA filing a lawsuit objecting to the implementation schedule.<sup>15</sup>

This Note will discuss the implications of a high minimum wage by examining the debate around the Seattle Ordinance with a particular focus on the IFA lawsuit. To analyze the possible impacts of the Seattle Ordinance, current and historical arguments both in support of and in opposition to minimum wage laws are considered. This Note ultimately concludes that the U.S. District Court rightly denied the IFA's motion for a preliminary injunction, which would have frustrated Seattle's experiment before it began.<sup>16</sup> Seattle's plan to implement a \$15 minimum wage, and similar experiments, should be permitted to proceed because the problem of income inequality is sufficiently troubling, and attempts to find a solution must be afforded some latitude.

This Note also acknowledges, however, that there are dangers to raising the minimum wage. Opponents of the minimum wage increase

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10. See *City Minimum Wage Laws: Recent Trends and Economic Evidence*, NAT'L EMP'T LAW PROJECT, <http://www.nelp.org/publication/city-minimum-wage-laws-recent-trends-and-economic-evidence-on-local-minimum-wages/> (last updated Sept. 18, 2015) [hereinafter *City Minimum Wage Laws*]. Several other cities are planning to raise their local minimum wages above those of their states. San Francisco, for example, passed an ordinance in 2014 to raise the minimum wage to \$15 an hour by 2018. *Id.*

11. Seattle, Wash., Ordinance 124490 (June 2, 2014) [hereinafter Ordinance 124490], available at [http://www.seattle.gov/council/issues/minimumwage/attachments/Ord\\_124490.pdf](http://www.seattle.gov/council/issues/minimumwage/attachments/Ord_124490.pdf) (codified at SEATTLE, WASH., MUN. CODE § 14.19 (2014)).

12. Hector Barreto, *The Real Reason for the Seattle Minimum Wage Fight*, FORBES (July 24, 2014, 1:44 PM), <http://www.forbes.com/sites/realspin/2014/07/24/the-real-reason-for-the-seattle-minimum-wage-fight>.

13. See SEATTLE, WASH., MUN. CODE § 14.19.030(A) (2014).

14. While supporters of the Seattle Ordinance celebrated the City Council's vote, the response of Steve Caldeira was "Game on." John Bacon, *Seattle Raises Minimum Wage to \$15 an Hour*, USA TODAY (June 3, 2014, 3:23 PM), <http://www.usatoday.com/story/money/business/2014/06/02/seattle-minimum-wage-vote/9863061/> (showing Caldeira and his colleagues in menacing business suits, contrasting with the bright orange of the minimum wage supporters). See FORWARD SEATTLE, <http://forwardseattle.wordpress.com> (last visited Apr. 15, 2015).

15. Matt Driscoll, *Challengers Line Up to Thwart Seattle Minimum-Wage Bill, Including Tim Eymann*, SEATTLE WEEKLY (June 5, 2014, 3:23 PM), <http://www.seattleweekly.com/home/952983-129/challengers-line-up-to-thwart-seattle>.

16. Int'l Franchise Ass'n, Inc. v. City of Seattle, 97 F. Supp. 3d 1256, 1263 (2015).

suggest that possible consequences include job loss and failed businesses.<sup>17</sup> Thus, Part I of this Note provides an overview of the historic controversy over minimum wage laws, taking into consideration concerns about employment, economic impact, and social justice.

Part II explains the new Seattle Ordinance and discusses some of the arguments specific to this Ordinance and the IFA lawsuit. Part III discusses the franchise structure. Part IV analyzes the predictions of the minimum wage hike effects and critiques the arguments of those who oppose both the Seattle Ordinance and the raising of the minimum wage in general. The Note concludes, reasserting a recommendation that, because the problem of income inequality requires urgent attention, efforts to address the issue must be treated with greater deference while the debate continues.

#### I. DEBATING THE HARMS OF A MINIMUM WAGE

Although the Supreme Court has concluded that the government has the power to regulate wages,<sup>18</sup> the debate among economists over the merits of a minimum wage rages on.<sup>19</sup> This debate has manifested in the arguments surrounding the Seattle Ordinance.<sup>20</sup> Much of the debate focuses on the effect that a minimum wage has on job loss.<sup>21</sup> Other relevant considerations include the right to a living wage,<sup>22</sup> the effect on the economy at large,<sup>23</sup> and the burdens placed on public assistance programs.<sup>24</sup> There are a number of factors and impacts to consider, but a recent study reported that three out of four economists agree that the benefits of raising the minimum wage outweigh any drawbacks.<sup>25</sup>

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17. See, e.g., Debra Burke et al., *Minimum Wage and Unemployment Rates: A Study of Contiguous Counties*, 46 GONZ. L. REV. 661, 672–76 (2011).

18. *West Coast Hotel Co. v. Parrish*, 300 U.S. 379, 398–99 (1937).

19. E.g., Burke et al., *supra* note 17, at 670–76 (providing an overview of arguments on both sides of the debate).

20. See, e.g., Bacon, *supra* note 14; Barreto, *supra* note 12.

21. Barreto, *supra* note 12.

22. See *infra* Part I.C.

23. See sources cited *infra* notes 78–82 and accompanying text.

24. See sources cited *infra* notes 83–90 and accompanying text.

25. *Minimum Wage*, IGM CHICAGO BOOTH (Feb. 26, 2013, 10:56 AM), [http://www.igmchicago.org/igm-economic-experts-panel/poll-results?SurveyID=SV\\_br0IEq5a9E77NMV](http://www.igmchicago.org/igm-economic-experts-panel/poll-results?SurveyID=SV_br0IEq5a9E77NMV); see also *The Job Loss Myth, RAISE THE MINIMUM WAGE*, <http://www.raisetheminimumwage.com/pages/job-loss> (last visited Oct. 4, 2015).

A. *The Effect on Employment is Not Compelling Evidence in the Debate*

The supposed adverse effect on employment is one of the key criticisms of minimum wage laws.<sup>26</sup> Nevertheless, in light of substantial evidence to the contrary, courts should not give much weight to the argument that the adverse impact on employment should obstruct implementation of legislation seeking to raise the minimum wage.

Somewhat ironically, given that effects on employment are frequently raised in objections to minimum wage laws, wage regulation in the United States finds its origins in strategies aiming to reduce unemployment.<sup>27</sup> The original movement to increase the minimum wage developed in response to unemployment during the Great Depression.<sup>28</sup> In an effort to improve employment, President Franklin D. Roosevelt proposed the “President’s Reemployment Agreement” (Agreement) as part of the 1933 National Industrial Recovery Act (Act), which was ultimately struck down by the Supreme Court.<sup>29</sup> The Agreement operated as an opt-in program where businesses would cut workweeks, hire more workers to make up the lost hours, and increase the hourly wages so that workers would earn the same weekly income for fewer hours worked.<sup>30</sup> In advocating for this program, Roosevelt reasoned that no business would suffer a competitive disadvantage because all employers would be making this accommodation.<sup>31</sup> Employers who voluntarily participated in the program were granted the right to display a Blue Eagle for customers and the world to see.<sup>32</sup> Although the Act was eventually determined to be

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26. See *The Gist: Does the Minimum Wage Create or Kill Jobs?*, SLATE (June 19, 2014, 5:22 PM), [http://www.slate.com/articles/podcasts/gist/2014/06/the\\_gist\\_on\\_raising\\_the\\_minimum\\_wage\\_and\\_gop\\_chances\\_of\\_winning\\_the\\_senate.html](http://www.slate.com/articles/podcasts/gist/2014/06/the_gist_on_raising_the_minimum_wage_and_gop_chances_of_winning_the_senate.html) [hereinafter *The Gist*].

27. *Planet Money: The Birth of the Minimum Wage*, NAT’L PUB. RADIO 4:40 (Jan. 17, 2014), <http://www.npr.org/blogs/money/2014/01/17/263487421/episode-510-the-birth-of-the-minimum-wage>.

28. *Id.*

29. *Id.* at 13:03. The Supreme Court declared the National Industrial Recovery Act to be unconstitutional in *A.L.A. Schechter Poultry Corp. v. United States*, 295 U.S. 495 (1935), commonly referred to as the “sick chickens” case. The Court found that the Act did not bear a sufficiently direct relationship to “interstate commerce,” and exceeded the scope of Congress’s power. *Id.* at 544–50. Further, the Court found that the Act unconstitutionally delegated legislative powers to the executive branch. *Id.* at 530–37. “We are of the opinion that the attempt through the provisions of the code to fix the hours and wages of employees of defendants in their intrastate business was not a valid exercise of federal power.” *Id.* at 550.

30. *Planet Money: Birth of the Minimum Wage*, *supra* note 26, at 4:40.

31. *Id.* at 6:40. Compare Roosevelt’s logic to one of the arguments made by the IFA that franchisees will suffer from competitive disadvantage due to the separate schedules. Complaint at 13, *Int’l Franchise Ass’n. v. City of Seattle*, 97 F. Supp. 3d 1256 (2015) [hereinafter IFA Complaint].

32. *Planet Money: Birth of the Minimum Wage*, *supra* note 26, at 7:15.

unconstitutional, the Blue Eagle Program illustrates the historic link between unemployment and a minimum wage.

Whether a mandatory minimum wage actually harms or impacts jobs at all has been the subject of heated debate over the years.<sup>33</sup> Essentially, there are two schools of thought on the subject: one school contends that a minimum wage exacerbates unemployment, while the other argues that a minimum wage has no effect on employment, or even improves employment rates.<sup>34</sup> The first school of thought, which is based on neoclassical economic theory, reasons that a minimum wage negatively impacts employment because setting the price of labor creates a market distortion.<sup>35</sup> Economic theory dictates that, as a result of the price of labor being set higher than its value, employers will be unwilling to pay for the “commodity” of some workers’ labor, resulting in fewer people being employed.<sup>36</sup> In the context of the Seattle Ordinance, this means that, according to economic theory, many people whose work hour is valued at less than \$15 per hour will find themselves unable to obtain employment.<sup>37</sup>

As proponents of the second, more recent, school of thought observe, the problem with relying purely on economic theory is that human labor cannot be classified merely as a commodity but is something rather unique in the market<sup>38</sup> because it can be viewed as simultaneously belonging to the employer and the employee. While the employer is buying

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33. *Planet Money: Money, Work and TV*, NAT’L PUB. RADIO 14:10 (Mar. 28, 2014), <http://www.npr.org/blogs/money/2014/03/27/295341895/episode-528-money-work-and-tv>.

34. *The Gist*, *supra* note 26 at 11:30.

35. *Id.*

36. *But see* INEQUALITY FOR ALL 23:45 (The Weinstein Company 2013) [hereinafter INEQUALITY FOR ALL] (pointing out that the government sets all sorts of rules and regulations in order to create a free market, minimum wage included). Reich points out that in the last thirty years, the rules have started to change to benefit. *Id.*

37. *See* Thomas Sowell, *Minimum-Wage Madness*, NAT’L REV. (Sept. 17, 2013, 12:04 AM), <http://www.nationalreview.com/article/358640/minimum-wage-madness-thomas-sowell> (explaining how minimum wage causes young people and minorities to be priced out of jobs).

38. *See, e.g.*, Bruce E. Kaufman, *The Theoretical Foundation of Industrial Relations and Its Implications for Labor Economics and Human Resource Management*, 64 INDUS. & LAB. REL. REV. 74 (2010) (comparing neoclassical labor economics and human resource management). “The machine which yields its services to man is itself a commodity, and is only a means to an end, while the laborer who parts with labor is no longer a commodity in civilized lands, but is an end in himself, for man is the beginning and termination of all economic life.” *Id.* at 79 (quoting RICHARD ELY, *THE LABOR MOVEMENT IN AMERICA* 99 (1886)); *see also* Edwin E. Witte, *The Doctrine That Labor is a Commodity*, 69 ANNALS AM. ACAD. POL. & SOC. SCI. 133, 135 (1917) (explaining that the property rights and the right to do business are not absolute rights and an employer has no right to an employee’s labor, even if it should do harm to the business). “Though an employer [as a result of an employee quitting their employment] suffers loss of profits, he has no legal ground for complaint.” *Id.*

the employee's time and energy, the employee retains the right to quit at any time, withdrawing his or her labor from the employer's ownership.<sup>39</sup>

This alternate view of human labor makes it less surprising that, in contrast to the theoretical analysis, economic data tends to show that minimum wage does not have a substantial adverse effect on employment.<sup>40</sup> It has only been within the last fifteen years that studies have even bothered asking whether the minimum wage has an adverse effect on employment.<sup>41</sup> These studies have produced evidence that a minimum wage does not harm employment.<sup>42</sup> In light of this new evidence, some economists are changing their position.<sup>43</sup> Ultimately, there are studies that can support both camps,<sup>44</sup> but the weight of the evidence shows little to no negative impact of "modest increases in the minimum wage."<sup>45</sup> Moreover, meta-studies (studies of studies) corroborate this conclusion.<sup>46</sup>

The incongruity between theory and evidence is partially owing to the human aspect to labor, which makes wages resistant to market fluctuation.<sup>47</sup> "The human essence of labor also means that labor demand and supply curves are not independent functions, wages are likely to have a large degree of rigidity, and labor markets are no longer self-regulating."<sup>48</sup> Employers may be reluctant to lower wages because of the adverse effect on morale and productivity.<sup>49</sup> Similarly, employers may hesitate to raise wages—or hire new workers—for fear of the consequence, should they have to lower them again.<sup>50</sup> Wages do not, and should not, fluctuate with the value of labor. "Persistent unemployment may therefore result, not due to minimum wage laws, unions or other

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39. See, e.g., Kaufman, *supra* note 38, at 92.

40. See, e.g., JOHN SCHMITT, CTR. FOR ECON. & POLICY RESEARCH, WHY DOES THE MINIMUM WAGE HAVE NO DISCERNIBLE EFFECT ON EMPLOYMENT? (2013), available at <http://www.cepr.net/documents/publications/min-wage-2013-02.pdf> (describing and appraising key minimum wage studies in the last fifteen years); David Card & Alan B. Krueger, *Minimum Wages and Employment: A Case Study of the Fast Food Industry in New Jersey and Pennsylvania*, (Nat'l Bureau of Econ. Research, Working Paper No. 4509, 1993), available at <http://www.nber.org/papers/w4509.pdf>; see also *Planet Money: Money, Work and TV*, *supra* note 33.

41. See *Planet Money: Money, Work and TV*, *supra* note 33.

42. See *id.*

43. See *id.*

44. *Id.* at 14:15.

45. SCHMITT, *supra* note 40, at 1. Schmitt discusses a meta-study concluding that there are significant negative effects on employment, but dismisses the study as "considerably more subjective and arguably less relevant to the United States." *Id.* at 6.

46. *Id.* at 4–5. Studies about minimum wage impacts often focus on teens and fast-food workers. *Id.* at 5, 10.

47. See generally Kaufman, *supra* note 38.

48. *Id.* at 88.

49. *Id.*

50. See *id.*

such institutional impediments . . . but from the hard-wired though analytically inconvenient facts of human nature.”<sup>51</sup>

Further explaining the results of minimum wage studies, where there is a minimum wage increase, there are so-called alternative “channels of adjustment” that can accommodate the increased cost of labor besides eliminating jobs.<sup>52</sup> Because labor markets are not perfectly competitive,<sup>53</sup> employers have a number of options to maintain profitability.<sup>54</sup> In addition to raising prices or cutting expenses such as nonwage benefits, “a minimum-wage increase gives new incentives to employers to undertake additional productivity-improving practices.”<sup>55</sup> Furthermore, evidence shows that higher paid workers are more productive and less likely to take advantage of their employers.<sup>56</sup> The various secondary effects of raising wages,<sup>57</sup> as well as strategies employers may adopt,<sup>58</sup> reduce any impact on employment nearly to zero.<sup>59</sup> Considering the evidence, and logical explanations backing up that evidence, citing the adverse effect on unemployment in the minimum wage debate is less than persuasive.

### *B. Technological Innovation Gives Regulating Wages Even Greater Importance*

Advances in technology are almost guaranteed to impact the job market. Not only does technology threaten to eliminate low-skill or unskilled jobs,<sup>60</sup> it drops the value of human labor.<sup>61</sup> Technology increases the economic divide between skilled and unskilled laborers, and, im-

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51. *See id.*

52. SCHMITT, *supra* note 40, at 10, 11.

53. *See id.* at 12; *supra* text accompanying notes 48–51. *See generally* Kaufman, *supra* note 38.

54. *See* SCHMITT, *supra* note 40.

55. *Id.* at 12.

56. *The Gist*, *supra* note 26 at 13:55.

57. SCHMITT, *supra* note 40, at 13. “Turnover has been one of the more troublesome problems to manage in the foodservice industry. In 2013, franchised establishments experienced a turnover rate of 93 percent.” *Study: Raising Wages to \$15 an Hour for Limited-Service Restaurant Employees Would Raise Prices 4.3 Percent*, PURDUE UNIV. NEWS (July 27, 2015), <https://www.purdue.edu/newsroom/releases/2015/Q3/study-raising-wages-to-15-an-hour-for-limited-service-restaurant-employees-would-raise-prices-4.3-percent.html> (quoting Richard Ghiselli, the coauthor of the study).

58. SCHMITT, *supra* note 41, at 12.

59. *Id.* at 12–13.

60. Derek Thompson, *A World Without Work*, ATLANTIC, Jul.–Aug. 2015, at 54 (citing a 2013 prediction by Oxford researchers that “machines might be able to perform half of all U.S. jobs in the next two decades”).

61. *Id.* at 53 (predicting that “technology could exert a slow but continual downward pressure on the value and availability of work”). Some economists estimate that nearly half of the decline in paid wages in the United States can be attributed to technology replacing workers. *Id.*

portantly, between capital owners and laborers.<sup>62</sup> “Even when technological progress increases productivity and overall wealth, it can also affect the division of rewards, potentially making some people worse off than they were before the innovation.”<sup>63</sup> In the event that a high minimum wage does adversely impact unemployment of unskilled (or teenage) workers,<sup>64</sup> the jobs of these workers are still not safe; the increased use of technology will cause the value of unskilled labor to drop below the point where compensation for that labor is enough to sustain an individual, let alone a family.<sup>65</sup>

Viewed from a different angle, the use of technology can make it affordable for employers to pay their employees a living wage.<sup>66</sup> Yet, outside pressures such as regulation or public opinion are probably necessary to get employers to pay these higher wages. The combination of a higher minimum wage and the use of advanced technology could improve working conditions, increase wages, and lead to more opportunities for fulfilling employment.

### *C. Economic Rights, Human Rights, and the Right to a Living Wage*

In addition to more practical considerations, moral considerations must be incorporated into the analysis. In President Roosevelt’s 1944 State of the Union Address he stated, “We cannot be content, no matter how high that general standard of living may be, if some fraction of our people—whether it be one-third or one-fifth or one-tenth—is ill-fed, ill-clothed, ill-housed, and insecure.”<sup>67</sup> He proposed a Second Bill of Rights, an economic bill of rights, and called for Congress to recognize and establish laws protecting “the right to a useful and remunerative job”; “the

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62. ERIK BRYNJOLFSSON & ANDREW MCAFEE, RACE AGAINST THE MACHINE: HOW THE DIGITAL REVOLUTION IS ACCELERATING INNOVATION, DRIVING PRODUCTIVITY, AND IRREVERSIBLY TRANSFORMING EMPLOYMENT AND THE ECONOMY 45, 47 (2011).

63. *See id.* at 39.

64. For a discussion of the changing demographics of minimum wage workers, see *infra* notes 73–74 and accompanying text.

65. Thompson, *supra* note 60, at 53.

66. Lydia DePillis, *Minimum-Wage Offensive Could Speed Arrival of Robot-Powered Restaurants*, WASH. POST (Aug. 16, 2013), [http://www.washingtonpost.com/business/capitalbusiness/minimum-wage-offensive-could-speed-arrival-of-robot-powered-restaurants/2015/08/16/35f284ea-3f6f-11e5-8d45-d815146f81fa\\_story.html](http://www.washingtonpost.com/business/capitalbusiness/minimum-wage-offensive-could-speed-arrival-of-robot-powered-restaurants/2015/08/16/35f284ea-3f6f-11e5-8d45-d815146f81fa_story.html).

67. Franklin Delano Roosevelt, Message to Congress on the State of the Union (Jan. 11, 1944), available at <http://www.heritage.org/initiatives/first-principles/primary-sources/fdrs-second-bill-of-rights>.

right to earn enough to provide adequate food and clothing and recreation”; and the rights to a home, medical care, and a good education.<sup>68</sup>

Even before the genesis of the federal minimum wage, social justice concerns motivated discussion of a “living wage.”<sup>69</sup> Some of this debate is premised on the idea that individuals do not truly enter freely into contracts if they are driven by a need to secure the bare necessities.<sup>70</sup> A living wage is defined as “(1) a subsistence wage; [and] (2) a wage sufficient to provide the necessities and comforts essential to an acceptable standard of living.”<sup>71</sup> Consider that a minimum wage that is merely sufficient to allow workers to subsist does not address the concern of income inequality. Mere subsistence wages do not allow for upward mobility or address the growing concern of income inequality in the United States.

One consideration that is relevant to the ultimate conclusions of this Note is the changing demographics of minimum wage workers. The argument is often asserted that raising the minimum wage will disadvantage teenagers trying to get a first job.<sup>72</sup> It may be true that employers would be unwilling to pay employees \$15 per hour for their first job. But the belief that sixteen or seventeen year olds represent the vast majority of people in minimum wage positions is inaccurate.<sup>73</sup> Primary breadwinners, such as single parents, often hold minimum wage jobs.<sup>74</sup> Considering whether the minimum wage provides sufficient income requires a look at a living wage calculation for a family.

The objectives of minimum wage laws vary. As described above, the minimum wage has been historically linked to the consistent concern of unemployment.<sup>75</sup> The Seattle Ordinance purportedly aims to address income inequality, remedy gender wage gaps, and meet the needs of low-wage workers as city living becomes increasingly expensive.<sup>76</sup> Notably, the City of Seattle is concerned with remedying income inequali-

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68. *Id.*; Stephanie Wagner, Note, *Big Box Living Wage Ordinances: Upholding Our Constitutive Commitment to a Remunerative Job*, 15 GEO. J. ON POVERTY L. & POL’Y 359, 359–60 (2008).

69. Thies, *supra* note 1, at 722.

70. *Id.* at 720.

71. *Living Wage*, MERRIAM-WEBSTER, <http://www.merriam-webster.com/dictionary/living%20wage> (last visited Apr. 15, 2015).

72. See, e.g., *The Gist*, *supra* note 26.

73. The inference being that if 52% of fast-food workers are on public assistance, they have families to support, or at least have no family supporting them. See KEN JACOBS ET AL., *THE HIGH PUBLIC COST OF LOW WAGES* (2015), available at <http://laborcenter.berkeley.edu/pdf/2015/the-high-public-cost-of-low-wages.pdf>.

74. *The Gist*, *supra* note 26, at 18:00.

75. See *supra* text accompanying notes 21–34.

76. Ordinance 124490, *supra* note 11.

ty.<sup>77</sup> The Seattle Ordinance recognized that “President Barack Obama has called addressing income inequality . . . ‘the defining issue of our time’.”<sup>78</sup> As a stated goal of the Ordinance, the minimum wage should aim to accommodate a living wage that is defined by quality of life, not mere subsistence, and provides the opportunity for upward mobility.

*D. Higher Wages Support the Economy and Relieve the Burden on Public Assistance Programs*

Humanitarian reasons aside, there are additional practical justifications for raising wages. A higher minimum wage could support the economy and get people off public assistance programs. Where raising the minimum wage is typically measured to simply catch up with inflation, the Seattle Ordinance is designed to actually stimulate the economy.<sup>79</sup> Economist and former Secretary of Labor Robert Reich has argued for reducing income inequality by increasing worker pay, explaining that distributing money to the low-income sector of society does more to stimulate the economy than putting that money into the hands of the super rich.<sup>80</sup> The wealthy have no need to spend their millions and will simply invest in hedge funds so their vast wealth makes them even richer.<sup>81</sup> Conversely, out of necessity, low- and middle-class citizens buy and spend, rather than invest and save.<sup>82</sup> Even when basic needs are covered, people at the lower end of the income spectrum will pay for things that are not necessities, but are key to upward mobility.<sup>83</sup> Similarly, a subsistence wage may not include provisions for the future or for unforeseen expenses, such as medical emergencies. Eventually, much of the low-

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77. *Id.*

78. *Id.*

79. See Dana Milbank, *Raising the Minimum Wage Without Raising Havoc*, WASH. POST (Sept. 5, 2014), [http://www.washingtonpost.com/opinions/dana-milbank-no-calamity-yet-as-seatac-wash-adjusts-to-15-minimum-wage/2014/09/05/d12ba922-3503-11e4-9e92-0899b306bba\\_story.html](http://www.washingtonpost.com/opinions/dana-milbank-no-calamity-yet-as-seatac-wash-adjusts-to-15-minimum-wage/2014/09/05/d12ba922-3503-11e4-9e92-0899b306bba_story.html) (explaining that, despite fears that local businesses will suffer, proprietors continue to expand). Examples cited include Tom Douglas, owner of several Seattle restaurants, who has continued to announce plans to open new restaurants in Seattle. *Id.*

80. INEQUALITY FOR ALL *supra* note 36, at 17:00; SCHMITT, *supra* note 40, at 12.

81. INEQUALITY FOR ALL, *supra* note 36, at 17:00.

82. *Id.* (noting that “consumer spending is seventy percent of the United States economy”). Middle and lower class spending also helps explain the conflict between theory and data with regard to a minimum wage’s effect on employment discussed *supra* in Part I.A. “Human beings are not just a supply, they also create their own demand.” *The Gist*, *supra* note 26, at 13:06; see also INEQUALITY FOR ALL, *supra* note 36, at 18:50 (explaining that customers and workers, not the super-rich, are job creators).

83. Education is one example of a commodity that appears to be treated as a luxury in the United States.

income population will have to avail itself of government-funded public assistance programs.<sup>84</sup>

Thus, a further consideration of the minimum and living wage analysis is presented: the burden on taxpayers due to low-income sector reliance on governmental assistance. In fact, a recent study by the Berkeley Labor Center indicated that 52% of fast-food workers—many of whom are employed by fast-food franchises—rely on public assistance.<sup>85</sup> Public assistance programs such as Medicaid, Children's Health Insurance Program (CHIP), Temporary Aid to Needy Families (TANF), and the Supplemental Nutrition Assistance Program (SNAP)<sup>86</sup> generally provide support to families, not single teenagers working their first jobs.

Public assistance programs amount to no small cost to the government. Between 2009 and 2011, the government—including federal and state contributions—paid \$152.8 billion annually toward public assistance programs.<sup>87</sup> Over half of this assistance went to working families.<sup>88</sup> Particularly relevant to this Note is the McDonald's franchise, whose U.S. workforce is over 700,000 and is estimated to cost taxpayers \$1.2 billion per year.<sup>89</sup> McDonald's profits in 2012 were \$5.46 billion.<sup>90</sup> Through providing public assistance to the employees of franchises such as McDonald's, the government and taxpayers are effectively subsidizing McDonald's profits.<sup>91</sup> In this regard, a higher minimum wage would shift

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84. Low-income earners may not be able to wait until old age or a medical emergency before requiring governmental assistance. The McDonald's franchise was featured in the news after a minimum wage worker called the employee hotline ("McResources") seeking to improve her situation and was referred to government assistance programs such as food stamps and Medicaid. Haley Peterson, *McDonald's Hotline Caught Urging Employee to Get Food Stamps*, BUS. INSIDER (Oct. 24, 2013, 4:00 PM), <http://www.businessinsider.com/mcdonalds-mcresources-hotline-tells-nancy-salgado-to-get-on-food-stamps-2013-10>. This circumstance highlights how the government subsidizes businesses that pay at the minimum wage, further distorting the market. In other words, setting the minimum wage is not the only market distortion. Employers might have to pay higher than the minimum wage in a truly fair market, where governmental assistance programs were unavailable.

85. JACOBS ET AL., *supra* note 73, at 3.

86. *Id.* at 1–2.

87. *Id.* at 2.

88. *Id.*

89. NAT'L EMP'T LAW PROJECT, SUPER-SIZING PUBLIC COSTS: HOW LOW WAGES AT TOP FAST-FOOD CHAINS LEAVE TAXPAYERS FOOTING THE BILL 1–2 (2013), available at <http://nelp.org/content/uploads/2015/03/NELP-Super-Sizing-Public-Costs-Fast-Food-Report.pdf>. NELP estimated that the total cost to tax payers to provide assistance to employees of the top ten fast-food companies was \$3.8 billion per year. *Id.* Employees of the Subway franchise receive \$436 million in public benefits. *Id.*

90. *Id.* at 3; see also Patricia Cohen, *Working, but Needing Public Assistance Anyway*, N.Y. TIMES, Apr. 13, 2015, at B1, <http://www.nytimes.com/2015/04/13/business/economy/working-but-needing-public-assistance-anyway.html>.

91. NAT'L EMP'T LAW PROJECT, *supra* note 89, at 3. Other major fast-food franchises include Subway and Dairy Queen. *Id.*

some of the burden of ensuring that franchise employees could live sustainably from the shoulders of the government to those of the franchise itself.

While the merits of the minimum wage continue to be debated,<sup>92</sup> the philosophies at the foundation for each school of thought inform opinions about what to do with the minimum wage. Those who support the minimum wage in general argue that it should reflect a living wage. Those who oppose minimum wage laws want to see the minimum wage stay low. The fact of the matter is that the minimum wage has been a part of our econo-employment system for more than three-quarters of a century and is here to stay. So, the question becomes how to address the minimum wage when income inequality is becoming an increasingly troubling problem. The following Part explains the Seattle Ordinance—one city’s approach to resolving the income inequality question with minimum wage laws.

## II. SEATTLE’S GRAND EXPERIMENT: THE LAW AND THE CONTROVERSY

Although there have been a variety of objections to Seattle’s minimum wage increase, it is the implementation schedule that is at issue in the IFA lawsuit.<sup>93</sup> This Part explains the particulars of the implementation schedule, the IFA’s allegations, and the City’s response.

### *A. The Nitty-Gritty Details of Seattle’s Minimum Wage Ordinance Phase-In Schedule*

In enacting this ordinance, the City of Seattle acknowledged the concern that smaller employers will have difficulty meeting the new requirements.<sup>94</sup> For this reason, the Income Inequality Advisory Committee (IIAC)—the task force charged with the job of coming up with a plan to address income inequality—developed two implementation schedules: a three-year schedule for large employers (Schedule 1), and a seven-year schedule for small employers (Schedule 2).<sup>95</sup>

Ultimately, all employers with workers in Seattle will be required to pay a \$15 minimum wage.<sup>96</sup> Large employers—those who employ

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92. See *supra* text accompanying notes 33–44.

93. IFA Complaint, *supra* note 31.

94. Ordinance 124490, *supra* note 11. The cost for some employers could be as much as \$20,000 per year.

95. CITY OF SEATTLE, INCOME INEQUALITY ADVISORY COMMITTEE (2014), available at <http://www.seattle.gov/Documents/Departments/IncomeInequalityAdvisoryCommittee/one-pager.pdf>.

96. SEATTLE, WASH., MUN. CODE § 14.19.030 (2014).

more than 500 employees—are on Schedule 1 and have until January 1, 2017 to implement the \$15 minimum wage through incremental increases.<sup>97</sup> Small employers—those with 500 or fewer employees—are on Schedule 2 and have until January 1, 2021<sup>98</sup> to increase their wages to \$15 per hour.<sup>99</sup> Once reaching \$15 per hour, the minimum wage will be indexed to increase annually with inflation.<sup>100</sup>

For purposes of determining whether an employer is Schedule 1 or Schedule 2, the number of employees is calculated based on the employer's total workforce, regardless of location.<sup>101</sup> Therefore, if a business employs 501 people, but only one within the City of Seattle, that employer must pay that employee based on the Seattle minimum wage for the time they spend working within the geographic boundaries of the city.<sup>102</sup> And, as was pointed out by the IFA in its complaint, “a non-franchise business that has 500 employees is treated as a ‘small’ employer whereas a small franchisee with only 5 employees is treated as a ‘large’ employer if, as is usually the case, the franchisee is part of a network that employs more than 500 workers.”<sup>103</sup>

In evaluating whether this classification is justified, it is necessary to discuss the justifications for the different schedules. Small business owners fear being unable to keep up with paying the increased wages to their employees and thus being forced to close.<sup>104</sup> The danger imposed on small businesses is more acute because, with generally lower profit margins, there is less flexibility to adjust wages.<sup>105</sup> In turn, employees of

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97. *Id.* § 14.19.040. But employers who pay into an employee's medical benefits plan have until 2018.

98. *Id.* § 14.19.050.

99. *Id.*

100. *Id.* § 14.19.030. Note that while the Seattle Ordinance provides for indexed increases once the \$15 minimum is reached, and Washington State's minimum wage has been increasing with inflation since 2001, the federal minimum wage only increases by congressional action. Several states, but not all, already have annual indexed increases, and several more have indexed increases scheduled to start within the next few years. *State Minimum Wages: 2015 Minimum Wage by State*, NAT'L CONF. ST. LEGISLATURES, <http://www.ncsl.org/research/labor-and-employment/state-minimum-wage-chart.aspx> (last updated Nov. 10, 2015).

101. SEATTLE, WASH., MUN. CODE § 14.19.010 (2014).

102. *Id.* § 14.19.020.

103. IFA Complaint, *supra* note 31, at 2.

104. Barreto, *supra* note 12; see also Andrew Friedman, *Your Favorite Indie Shop is Out of Business if \$15-an-Hour Happens*, THE STRANGER (Apr. 2, 2014), <http://www.thestranger.com/seattle/your-favorite-indie-shop-is-out-of-business-if-15-an-hour-happens/Content?oid=19182099> (noting that payroll is a large portion of the cost of running a small business and appealing to the independent-business lover to oppose this law to keep local small businesses from closing); FORWARD SEATTLE, <http://forwardseattle.wordpress.com> (last visited Apr. 15, 2015).

105. See Friedman, *supra* note 104.

small businesses fear losing their jobs over the Ordinance, instead preferring low-wage and steady employment to uncertain employment with higher pay.<sup>106</sup> In response, proponents of the Ordinance argue that increased wages will improve worker retention, productivity, and customer service.<sup>107</sup> There are undoubtedly growing pains associated with this type of action. The extended seven-year phase-in period small businesses have to implement the new minimum wage is meant to allow for an easier adjustment. Although franchisees are still bound by the shorter, three-year schedule, they are still permitted an adjustment period.

*B. The IFA's Position Regarding Franchises and the Ordinance*

One rapid, vehement response to the Seattle Ordinance was the IFA lawsuit.<sup>108</sup> On June 11, 2014, merely nine days after the Seattle Ordinance was passed, the IFA filed suit in U.S. District Court seeking preliminary and permanent injunctive relief.<sup>109</sup> The complaint alleged several violations, including violations of the federal and state constitutions as well as statutory law.<sup>110</sup> One key allegation stated that the Seattle Ordinance “unfairly and irrationally discriminates against interstate commerce generally, and small businesses that operate under the franchise business model specifically.”<sup>111</sup>

The complaint argued that not only are franchises subject to unconstitutional differential treatment, but they are also unfairly disadvantaged by the Seattle Ordinance.<sup>112</sup> The IFA asserted that “[small franchisees] will be forced to raise prices, reduce employees, or lower the quality of their goods and services to comply with the Ordinance to a substantially greater extent than their non-franchise counterparts.”<sup>113</sup> The IFA argued that the Seattle Ordinance is particularly discriminatory because, as a result of the disparity in minimum wage requirements between 2017 and 2021, small franchises will be subject to an unfairly competitive market-

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106. Barreto, *supra* note 12. Employees may criticize such a dramatic increase in minimum wage as unfairly increasing compensation for newly-hired employees while employees who have invested years working for a company may earn \$15 or less. This particular objection is from the author's own personal experience and conversation with former colleagues.

107. *See generally City Minimum Wage Laws supra* note 10; *see also supra* text accompanying note 56.

108. *See, e.g., Bacon, supra* note 14 and accompanying text.

109. IFA Complaint, *supra* note 31, at 1, 33.

110. *See generally id.* at 23–33; *Int'l Franchise Ass'n. Inc. v. City of Seattle*, 97 F. Supp. 3d 1256, 1266 (W.D. Wash. 2015).

111. IFA Complaint, *supra* note 31, at 2.

112. *Id.*

113. *Id.* at 3.

place.<sup>114</sup> During those four years, Schedule 1 employers—including applicable franchisees—must pay their employees a \$15 minimum wage, while Schedule 2 employers will still be incrementally increasing their wages. The IFA argued that the “perverse effect” of the Seattle Ordinance’s classifications—specifically, that an employer with 495 employees will be on a less strict schedule than a franchisee with a handful of employees—is that small franchise owners are harmed through disparate treatment.<sup>115</sup>

The IFA went so far as to claim that the higher minimum wage will destroy the franchise business model.<sup>116</sup> The IFA explained in a letter to Seattle Mayor Ed Murray that “[a]ccording to case law as well as state and federal statutes, franchisees are not the employees of franchisors. Likewise, franchisees’ employees are not the employees of franchisors.”<sup>117</sup> Rather, the letter asserts, “[i]t is the owner of an individual local franchise who is responsible for the hiring and wage decisions at his or her location.”<sup>118</sup> The Seattle Ordinance ignores this characteristic of franchisees, not franchisors, as employers.

The complaint carefully characterizes the plaintiffs as individuals putting it all on the line to embark on a business venture. In addition to the IFA, there are a number of franchisees located in Seattle that are plaintiffs in this case.<sup>119</sup> The franchisors are not actual parties to the lawsuit.<sup>120</sup> The complaint highlighted the substantial personal investment on the part of the plaintiffs.<sup>121</sup> Moreover, these franchises are strategically characterized as providing more specialized services than entry-level positions at McDonalds.<sup>122</sup> Appealing to America’s fixation on entrepreneurship and extolling the franchise model as creating opportunity for aspiring business owners evokes sympathy for the plaintiffs.

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114. *Id.*

115. Letter from Dean Heyl, Vice President, State Government Relations, Public Policy & Tax Counsel, International Franchise Association, to Ed Murray, Seattle City Mayor, and Members of the Seattle City Council (May 19, 2014), available at <http://emarket.franchise.org/SeattleMinimumWageLetter.pdf> [hereinafter Heyl Letter]; see also IFA Complaint, *supra* note 31, at 12.

116. Heyl Letter, *supra* note 115.

117. *Id.*

118. *Id.*

119. IFA Complaint, *supra* note 31, at 4–6.

120. See *id.* The franchisee-plaintiffs are Brightstar Care (homecare for children and elderly) and Alphaprint, Inc., of the AlphaGraphics franchise. *Id.* at 5.

121. *Id.* at 18. Charles Stempler, owner of Alphaprint, supposedly invested \$100,000 while the Lyons, owners and operators of Brightstar, purportedly invested more than \$435,000, over half of which was borrowed. *Id.* at 19.

122. *Id.* at 5–6.

C. *City of Seattle's Position Regarding Franchises and the Ordinance*

The City of Seattle's response to the IFA's arguments shows very little concern for the alleged hardship franchisees will face, instead painting a different picture of the franchise model. Mayor Murray responded to the IFA's statements, pointing out that "[f]ranchises have resources that . . . small business[es] . . . do not have."<sup>123</sup> The Mayor stated that, in determining classifications for Schedule 1 and Schedule 2 employers, the City considered the differences between a truly local business and a franchise: "Franchise restaurants have menus that are developed by a corporate national entity, a food supply and products that are provided by a corporate national entity, training provided by a corporate national entity, and advertising provided by a corporate national entity."<sup>124</sup> These additional support structures were deemed sufficient to offset any hardship caused by attaching franchises to the shorter, three-year schedule.

Significantly, franchises were deliberately considered in the City's analysis and plan: "The movement around wage equality in our nation began with fast food workers walking off the job. . . . That was the straw that broke wage disparity's back in this nation."<sup>125</sup> The IAC apparently found the interests of franchisees less compelling than the interests of low-wage workers in the city. After all, the Seattle Ordinance expressly includes franchises in the definition of "Schedule 1 Employer."<sup>126</sup>

Furthermore, the Mayor went so far as to say that the franchise business model is flawed, suggesting that franchisees should look to their corporate parents for support, not to the City.<sup>127</sup> The Mayor's statements subliminally evoke concern that any benefit to franchises derived from a low minimum wage is paid for by low-wage workers, the government, and even the middle class through taxation.<sup>128</sup>

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123. Seattle Mayor Ed Murray, Statement on International Franchise Association Lawsuit (June 11, 2014), *available at* <http://murray.seattle.gov/mayor-murray-statement-on-international-franchise-association-lawsuit/#sthash.OzAheAX1.dpbs> [hereinafter Mayor Murray Statement].

124. *Id.*

125. *Id.*; *see also* Answer at 5, Int'l Franchise Ass'n. v. City of Seattle, 97 F. Supp. 3d 1256 (W.D. Wash. 2015) [hereinafter Seattle Answer].

126. SEATTLE, WASH., MUN. CODE § 14.19.030 (2014).

127. Mayor Murray Statement, *supra* note 123. "There is a problem in the franchise business model and I believe this is a discussion franchise owners should be having with their corporate parents. I don't believe that the economic strain comes from a fairly slow phase in of a higher minimum wage, but on a business model that really does—in many cases—harm franchise owners. I don't doubt at all that franchise workers are operating under tight conditions, but I think it's a conversation to have with the people who have decided to spend oodles of money on lawyers to fight a higher minimum wage." *Id.*

128. *See supra* notes 84–91 and accompanying text.

Famously, McDonald's Corporation is consistently used as an example of a franchise: a massive corporation, whose executive made \$9.5 million in 2014.<sup>129</sup> The IFA prudently chose plaintiffs that defy the McDonald's stereotype.<sup>130</sup> While it is clear that franchises vary in size and, to some degree, method of operation, the question remains whether the City of Seattle has unjustly designated McDonald's Corporation (and its ilk) as representative of the franchise business model.

*D. The Courts' Conclusions Regarding Franchises and the Ordinance*

The IFA's motion for a preliminary injunction was filed on August 5, 2014.<sup>131</sup> In March 2015, the District Court for the Western District of Washington denied the IFA's motion,<sup>132</sup> and on September 25, 2015, the Court of Appeals for the Ninth Circuit denied the IFA's appeal.<sup>133</sup> The basis for the IFA's motion and the courts' decisions focused on the City of Seattle's alleged constitutional violations, which are not addressed in this Note.<sup>134</sup> The opinions from both the district court and the court of appeals also note the impact that a preliminary injunction would have on the City's workers.<sup>135</sup> Although the court of appeals concluded that "[t]he district court . . . erred in finding that IFA did not demonstrate that the *balance of hardships* tips in its favor," the court found that "the district court did not err in concluding that *the public interest* disfavors an injunction."<sup>136</sup> The Ninth Circuit's observation is interesting because in balancing hardships, the court compared hardships of the IFA and the City as entities. In contrast, when considering the public interest impact, the court considered the hardship of Seattle workers, finding that "[g]ranted a preliminary injunction would likely result in many workers receiving reduced wages."<sup>137</sup>

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129. *Editorial: Redefine Franchises Under Seattle's Minimum-Wage Proposal*, SEATTLE TIMES (June 2, 2014, 11:56 AM), [http://seattletimes.com/html/editorials/2023733816\\_editminimum\\_wage31.xml.html](http://seattletimes.com/html/editorials/2023733816_editminimum_wage31.xml.html).

130. *See supra* text accompanying notes 119–122.

131. Plaintiffs' Motion for a Limited Preliminary Injunction, *Int'l Franchise Ass'n. Inc. v. City of Seattle*, 97 F. Supp. 3d 1256 (W.D. Wash. 2015).

132. *See id.*; *Int'l Franchise Ass'n, Inc. v. City of Seattle*, 97 F. Supp. 3d 1256 (W.D. Wash. 2015).

133. *Int'l Franchise Ass'n, Inc. v. City of Seattle*, 803 F.3d 389 (9th Cir. 2015).

134. *See* Record of Oral Arguments, *Int'l Franchise Ass'n, Inc. v. City of Seattle*, 803 F.3d 389 (9th Cir. 2015), available at [http://www.ca9.uscourts.gov/media/view\\_video.php?pk\\_vid=0000008141](http://www.ca9.uscourts.gov/media/view_video.php?pk_vid=0000008141).

135. *Int'l Franchise Ass'n*, 97 F. Supp. 3d at 1286; *Int'l Franchise Ass'n*, 803 F.3d at 412.

136. *Int'l Franchise Ass'n*, 803 F.3d at 412 (emphasis added).

137. *Id.*

The court of appeals also concluded that the IFA did provide evidence that the Seattle Ordinance put them at a competitive disadvantage.<sup>138</sup> It was enough for the IFA to provide evidence that “franchisees will face higher minimum wage obligation compared to non-franchisees.” Nevertheless, the court concluded that the IFA failed to provide evidence to show they would suffer irreparable harm.<sup>139</sup> The following Parts examine the franchise business model<sup>140</sup> and evaluate the impacts of the minimum wage schedule on corporate franchise entities, franchisees, and employees of the franchise.<sup>141</sup>

### III. FRANCHISES

Franchises represent a significant sector of American business. The 2007 Economic Census reported that franchised businesses employed 7.9 million workers—5% of the total workforce—at 453,326 establishments.<sup>142</sup> The total annual sales of these businesses amounted to nearly \$1.3 trillion and annual payroll was around \$154 billion.<sup>143</sup> The majority of these establishments are in accommodation and food services, or retail trade.<sup>144</sup>

#### A. *What are Franchises?*

The franchisor–franchisee relationship is typically governed by the franchise agreement, but federal, state, and local laws do impose certain regulations upon franchises.<sup>145</sup> As defined by the Seattle Ordinance, a

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138. *Id.* at 411.

139. *Id.* The court noted:

The record does not discuss the costs and revenues of these businesses, the performance of non-franchisees, current or future labor costs, the proportion of employees earning more than the minimum, or the elasticity of demand for goods and services provided by franchisees. Thus, it is impossible to evaluate whether franchisees will need to raise prices or whether price changes will result in decreased demand. The chain of events suggested by IFA is speculation that does not rise beyond the mere “possibility” of harm.

*Id.* at 411–12.

140. *See infra* Part III.

141. *See infra* Part IV.

142. Ying Fan et al., *Financial Constraints and Moral Hazard: The Case of Franchising* (CESIFO, Working Paper No. 4474, 2013), available at <http://ssrn.com/abstract=2359409>.

143. U.S. CENSUS BUREAU, 2007 ECONOMIC CENSUS: FRANCHISE STATISTICS (2007), available at [http://www.census.gov/econ/census/pdf/franchise\\_flyer.pdf](http://www.census.gov/econ/census/pdf/franchise_flyer.pdf).

144. *Id.*

145. *Franchise Agreement*, BLACK’S LAW DICTIONARY 773 (10th ed. 2014). “The contract between a franchisor and franchisee establishing the terms and conditions of the franchise relationship. State and federal laws regulate franchise agreements.” *Id.* The Federal Trade Commission regulates some franchise activity, *see* 16 C.F.R. pt. 436 (2015), but franchise agreements are typically governed by state law and vary greatly from state to state. Washington is one of seventeen states that have adopted franchise relationship laws. Thomas M. Pitegoff, *Franchise Relationship Laws: A*

franchise has three elements: (1) “[a] person is granted the right to engage in [a] business . . . under a marketing plan prescribed or suggested in substantial part by the grantor or its affiliate”; (2) “[t]he operation of the business is substantially associated with a trademark . . . owned by . . . the grantor or its affiliate”; and (3) the franchisee pays a fee for use of the trademark.<sup>146</sup> In other words, trademark owners license the use of their trademarks to others, who get the benefit of the trademark’s reputation and goodwill associated with that trade name.<sup>147</sup> The owner of the trademark maintains quality control over the goods and services provided.<sup>148</sup> In return, the franchisee—those who are granted license to use the trademark—turns over some of his or her profits to the trademark owner, the corporate franchise.<sup>149</sup>

Scholars have identified a number of benefits and drawbacks to structuring a business as a franchise. In choosing to franchise, a business owner is able to see significant returns on investment with relatively low risk because the franchisees take on the risk of losing an investment when a new business is unsuccessful.<sup>150</sup> The structure also incentivizes franchise owners, more than salaried or hourly employees, to work hard and make the business successful.<sup>151</sup> In this way the franchise model has been thought to diminish the risks of adverse selection<sup>152</sup> and moral hazard.<sup>153</sup> The drawbacks to franchising, however, require the franchisor to

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*Minefield for Franchisors*, in BUILDING FRANCHISE RELATIONSHIPS: A GUIDE TO ANTICIPATING PROBLEMS, RESOLVING CONFLICTS, AND REPRESENTING CLIENTS 140, 142 (Ann Hurwitz & Rochelle Buchsbaum Spandorf eds., 1996). A franchise agreement generally includes more than just a license to use the trademark; the franchisee also has the right to use the marketing and distribution system established by the franchisor. FUNDAMENTALS OF FRANCHISING 4 (Rupert M. Barkoff & Andres C. Selden eds., 2d ed. 2004). For example, in Washington the definitional requirements of a franchise include trademark license, marketing plan, fee, and part of disclosure law. Pitegoff, *supra* at 171–72. These elements also limit the scope in Washington of what is defined as a franchise in the state. *Id.* at 144.

146. SEATTLE, WASH., MUN. CODE § 14.19.010 (2014).

147. FUNDAMENTALS OF FRANCHISING, *supra* note 145.

148. *Id.*

149. *Id.*

150. Scott Shane, *The Pros and Cons of Franchising Your Business*, ENTREPRENEUR (May 7, 2013), <http://www.entrepreneur.com/article/226489>.

151. *Id.*

152. CASES AND MATERIALS ON BUSINESS ENTITIES 883 (Eric A. Chiappinelli ed., 3d ed. 2014) (defining the term as “[p]rincipals choosing suboptimal agents, or agents choosing suboptimal principals”).

153. *Id.* at 890 (defining the term as “[t]he risk that a party with discretion to act will choose an action that decreases the expected value of the transaction to the other party in a way that the other party cannot effectively prohibit”); *see also* Scott A. Shane, *Making New Franchise Systems Work*, 19 STRATEGIC MGMT. J. 697, 697 (1998).

relinquish some control.<sup>154</sup> In addition, the nature of a structure that offers greater incentives for each individual franchise to be successful can also put individual franchisees in competition with one another.<sup>155</sup>

### *B. The Significance to the Franchisor-Franchisee Relationship*

While franchises might appear to offer opportunities to people who might not otherwise be able to afford the expensive and risky venture of business ownership, the opportunities are not expansively available so as to mitigate income inequality. Franchise ownership is still too expensive to be a viable option for the lower class. McDonald's, for example, requires a significant amount of independent capital from a prospective franchisee in order to even be considered for a franchise agreement:<sup>156</sup> "Generally, [McDonald's] require[s] a minimum of \$750,000 of non-borrowed personal resources . . ." <sup>157</sup> McDonald's also requires a buyer to pay a 25% cash down payment toward the purchase of an existing restaurant, or 40% for a brand new restaurant.<sup>158</sup> In the case of McDonald's franchisees, while the franchise structure may help a prospective business owner, the cost of owning a franchise is still prohibitive to certain classes of Americans.<sup>159</sup>

The franchises that are party to the lawsuit show significant differences in size in comparison to McDonald's—the go-to example of a franchise in this debate; yet, they are not as different as one might think. The plaintiffs invested a substantial amount of independent capital in starting their franchise locations in addition to having borrowed substantial sums of money to start their businesses.<sup>160</sup> Although the support provided through the franchise model may facilitate business ownership in some circumstances, the significant sum of money required to purchase a

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154. Shane, *supra*, note 150.

155. *Id.*

156. *Acquiring a Franchise*, ABOUT MCDONALD'S, [http://www.aboutmcdonalds.com/mcd/franchising/us\\_franchising/acquiring\\_a\\_franchise.html](http://www.aboutmcdonalds.com/mcd/franchising/us_franchising/acquiring_a_franchise.html) (last visited Apr. 17, 2015).

157. *Id.*

158. *Id.*

159. "[T]he substantial financial resources required to open a fast-food franchise make entrepreneurship an unrealistic option for front-line fast food workers earning poverty-level wages." NAT'L EMP'T LAW PROJECT, GOING NOWHERE FAST: LIMITED OCCUPATIONAL MOBILITY IN THE FAST FOOD INDUSTRY (July 2013), available at [http://nelp.3cdn.net/84a67b124db45841d4\\_o0m6bq42h.pdf](http://nelp.3cdn.net/84a67b124db45841d4_o0m6bq42h.pdf) [hereinafter NEMP OCCUPATIONAL MOBILITY]. Professor Shane argues that when franchisees are required to make greater investments in purchasing a franchise, the businesses are more likely to be successful because of self-selection in prospective franchisees. Shane, *supra* note 153, at 598–99. If Professor Shane's hypothesis is correct, franchisors have more incentive to increase the start-up cost, further prohibiting low-income entrepreneurs from becoming franchise owners.

160. IFA Complaint, *supra* note 31, at 14; see also *supra* note 121.

franchise means that those who suffer from the effects of income inequality are still unlikely to be in the position to benefit from this opportunity. The business opportunities offered by the franchise model do not remedy income inequality. In fact, the same incentives that drive franchisees to run a successful business may also incentivize paying low-as-possible wages in order to maximize the franchise's profits. The next Part discusses the minimum wage in connection with franchises.

#### IV. AN ASSESSMENT OF THE EFFECTS OF THE MINIMUM WAGE AND A CRITIQUE OF ARGUMENTS

As mentioned above, Seattle's Ordinance is an experimental measure, intending to address a pervasive, troubling problem.<sup>161</sup> Seattle plans to closely monitor and study the effects of the Ordinance's implementation over the next few years.<sup>162</sup> While only time will tell the true effects of the minimum wage, some predictions warrant analysis.

##### *A. The Effect of the Minimum Wage on Franchises, Franchise Owners, and Franchise Employees*

In supporting their position, opponents of raising the minimum wage appeal to the fear that the high minimum wage will have a devastating effect on businesses,<sup>163</sup> but again, evidence shows otherwise.<sup>164</sup> For example, a recent study predicts that raising the minimum wage to \$15 per hour would only cause a 4.3% increase in prices at fast-food restaurants.<sup>165</sup> In addition, despite the plaintiffs' claim that franchises will be deterred from opening businesses in Seattle—and other areas where a high minimum wage imposes extra costs of operation<sup>166</sup>—at least some

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161. See *infra* p. 617. "Seattle's greatest social and economic experiment is about to begin." Bacon, *supra* note 14.

162. Faculty from the University of Washington's Schools of Public Affairs, Public Health and Social Work will embark on a five-year study regarding the effect of the minimum wage increase. The study will examine several impacts, including the impact on workers, the community, employment, consumer prices, quality of life, eligibility for public assistance programs, and nonprofit services. Peter Kelley, *UW Faculty Team for Five-Year Study of Seattle's Minimum Wage Increase*, UW TODAY (Mar. 30, 2015), <http://www.washington.edu/news/2015/03/30/uw-faculty-team-for-five-year-study-of-seattles-minimum-wage-increase/>.

163. The IFA, for example, alleges the harm to franchise businesses in its complaint, which the district court found unsupported by facts. *Int'l Franchise Ass'n, Inc. v. City of Seattle*, 97 F. Supp. 3d 1256, 1286 (W.D. Wash. 2015).

164. See, e.g., Roberto A. Ferdman, *What Paying Fast Food Workers a Living Wage Would Do to the Price of a Big Mac*, WASH. POST (July 30, 2014), <http://www.washingtonpost.com/news/wonkblog/wp/2015/07/30/what-doubling-the-minimum-wage-would-do-to-the-price-of-a-big-mac/>.

165. *Id.*

166. IFA Complaint, *supra* note 31, at 2–3.

franchise restaurants are still planning on opening new locations in Seattle.<sup>167</sup>

Significantly, the franchise structure also impacts the relationship between employee and employer, thus influencing how much external regulation may be required. The nature of franchise employees' position limits their bargaining power.<sup>168</sup> Employees of franchisees who have adopted the franchise structure are impeded from successfully protesting their low-wages because of the fragmented nature of this business model.<sup>169</sup> What franchise employees' protests can accomplish, however, is raising awareness of "the abysmal incomes of millions of hardworking Americans."<sup>170</sup> Where corporations have not always been adequately responsive, some city and state governments have taken action, raising the minimum wage.<sup>171</sup> As labor unions decline,<sup>172</sup> governments are stepping in to fill the role of protecting workers.

The origins of the minimum wage are associated with an effort to provide a disadvantaged class of people with equal pay.<sup>173</sup> That tradition of protecting disadvantaged workers continues today with the Seattle Ordinance.<sup>174</sup> For better or for worse,<sup>175</sup> our society has decided that an enforceable minimum wage is one means of continuing to protect the interests of disadvantaged workers. With various factors to consider, from unemployment to quality of life to reliance on public assistance, no one can accurately predict the effects of this "extreme" increase in the minimum wage. What most can agree on is that income inequality is a

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167. The Togo's sandwich chain planned to open eighteen stores in the Seattle-Tacoma area in early 2015, despite the ordinance. Togo's CEO says that franchisees, along with everyone else, will simply have to figure out ways to stay competitive, whether that means increasing prices, or finding other ways to save money. Rachel Lerman, *Fast-Food Eatery Togo's Will Expand to Seattle (Not Afraid of \$15 Wage)*, PUGET SOUND BUS. J. (June 11, 2014, 2:54 PM), <http://www.bizjournals.com/seattle/blog/2014/06/fast-food-eatery-togo-s-will-expand-to-seattle-not.html?page=all>.

168. "The hundreds of thousands of people who work for the [McDonald's] Company and its franchises are scattered among thousands of small outlets. It's hard to see how even a rising number of sporadic strikes by discrete groups of employees will bring McDonald's to the bargaining table anytime soon." Harold Meyerson, *How to Get a Raise at McDonald's*, WASH. POST (Sept. 3, 2014), [http://www.washingtonpost.com/opinions/harold-meyerson-minimum-wage-fights-mark-unions-adapting-to-change/2014/09/03/8f1eb71c-3397-11e4-9e92-0899b306bba\\_story.html](http://www.washingtonpost.com/opinions/harold-meyerson-minimum-wage-fights-mark-unions-adapting-to-change/2014/09/03/8f1eb71c-3397-11e4-9e92-0899b306bba_story.html).

169. *Id.*

170. *Id.*

171. *Id.*

172. For details regarding the history of labor unions, an explanation of their decline, and an analysis of their potential force in the future, see Abraham L. Gitlow, *Ebb and Flow in America's Trade Unions: The Present Prospect*, 63 LAB. L.J. 123 (2012).

173. See *West Coast Hotel Co. v. Parrish*, 300 U.S. 379 (1937).

174. Ordinance 124490, *supra* note 11, at 1-2.

175. For a discussion of the merits of minimum wage, see *supra* Part I.

troubling problem in this country.<sup>176</sup> Because income inequality is such an important concern, even legitimate interests in opposition to this Ordinance should not prevent the City of Seattle and other local governments from trying different solutions.

It is untenable to think that an employee would be prohibited from quitting his or her position because of the losses to the employer.<sup>177</sup> It should be similarly distasteful to allow an employer to influence legislation intending to benefit employees. This point is exactly what the IFA is arguing: franchises will suffer economic harm as a result of the Seattle Ordinance. But one of the City's goals in enacting the Ordinance is to improve the standard of living for Seattle workers.<sup>178</sup> The lawsuit is essentially claiming that franchise-businesses' property rights should extend to controlling the wages of their employees, impinging on workers' human rights. Although franchise employees are not compelled to enter into an employment contract with franchise owners, the lack of real choice and bargaining power in seeking employment puts employers at a significant advantage in setting wages. The power of labor unions has been declining<sup>179</sup>—and will likely continue to do so—thus, the government is stepping in to protect and benefit workers.<sup>180</sup>

### *B. Franchisors Have an Incentive to Help Franchisees Succeed*

Corporate franchises are not altruistic institutions; they have incentives to ensure franchisees survive. Franchisors profit from opening new franchise locations.<sup>181</sup> To return to the ubiquitous example of the McDonald's franchise,<sup>182</sup> McDonald's receives a percentage of its franchisees' monthly sales.<sup>183</sup> Thus, franchisors have an interest in seeing that their franchisees continue to be profitable. While individual franchise owners may bear the initial burden of the Schedule 1 wage hike, the franchisor corporations will be adversely impacted by franchisee failures. Because the franchisor has an interest in the franchisee's success, the argument that franchisees are unfairly disadvantaged is flawed—

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176. *But see Intelligence Squared U.S. Debates: Does Income Inequality Impair the American Dream?*, NAT'L PUB. RADIO (Oct. 29, 2014, 1:32 PM), <http://www.npr.org/player/v2/mediaPlayer.html?action=1&t=1&islist=false&id=359363643&m=359841625>.

177. Witte, *supra* note 38, at 139.

178. Ordinance 124490, *supra* note 11, § 1.

179. *See, e.g.*, Gitlow, *supra* note 172.

180. Kaufman, *supra* note 38.

181. FUNDAMENTALS OF FRANCHISING, *supra* note 145.

182. *Acquiring a Franchise*, *supra* note 156.

183. *Id.* This percentage includes a service fee of 4% of the monthly sales and "rent," which could include a monthly base rent or an additional percentage of monthly sales. *Id.*

franchisors will not allow their franchisees to fail unless they become unprofitable. Franchises are therefore more similar to big businesses than small businesses and the Seattle Ordinance rightly classified them as Schedule 1 employers.

#### CONCLUSION

Ultimately, the consequences of the Seattle Ordinance are uncertain. Nevertheless, theory and research can offer rather persuasive evidence that the outlook is not as dire as some—such as the IFA—would have policymakers and the public believe. Even if this were not the case, theoretical harms should not deter Seattle and other jurisdictions from seeking solutions to what is one of the defining social concerns of our time.

In the words of Franklin Delano Roosevelt, “We have come to a clear realization of the fact that true individual freedom cannot exist without economic security and independence. ‘Necessitous men are not free men.’”<sup>184</sup> It is the protection of our freedom that makes economic justice such a pressing concern. Franchise employees are some of the most vulnerable workers because they lack bargaining power and because many make minimum wage. Catering to the wishes of franchises would undercut the force of Seattle’s efforts. The courts have thus far denied the IFA’s motion, notably considering the impact to Seattle workers.<sup>185</sup> Other courts and local governments should follow this example and continue to put the interests of the low-income population in America above the interests of corporate franchises.

Although not thoroughly addressed in this Note, considering the future of the minimum wage is connected to the future availability of low-wage jobs. It has been predicted that in as little as a generation or two robotics and other technological advancements will take over most low-wage positions, eventually making unskilled labor redundant and unnecessary.<sup>186</sup> It is the opinion of this author that raising the minimum wage, while a valiant effort, will not resolve income inequality satisfactorily. Ultimately, to avoid mass unemployment, it will be necessary to invest in education and skilled job-training, thus avoiding the dangers of putting too high a price on unskilled labor (distorting the market) and the future problem of technology displacing huge portions of the labor force.

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184. Franklin Delano Roosevelt, *supra* note 67.

185. Int’l Franchise Ass’n, Inc. v. City of Seattle, 97 F. Supp. 3d 1256, 1287 (W.D. Wash. 2015); Int’l Franchise Ass’n, Inc. v. City of Seattle, 803 F.3d 389, 412 (9th Cir. 2015).

186. See *supra* notes 61–63 and accompanying text.