

Spring 1969

Designing Distribution Systems: Anti-Trust Problems in Franchising and Marketing

Landon H. Rowland

Follow this and additional works at: <https://scholarship.law.missouri.edu/mlr>



Part of the [Law Commons](#)

Recommended Citation

Landon H. Rowland, *Designing Distribution Systems: Anti-Trust Problems in Franchising and Marketing*, 34 MO. L. REV. (1969)

Available at: <https://scholarship.law.missouri.edu/mlr/vol34/iss2/2>

This Article is brought to you for free and open access by the Law Journals at University of Missouri School of Law Scholarship Repository. It has been accepted for inclusion in Missouri Law Review by an authorized editor of University of Missouri School of Law Scholarship Repository. For more information, please contact bassettcw@missouri.edu.

DESIGNING DISTRIBUTION SYSTEMS: ANTI-TRUST PROBLEMS IN FRANCHISING AND MARKETING*

LONDON H. ROWLAND**

I. INTRODUCTION

There are fads in commerce and in the law of commerce as there are fads in fashion and entertainment. Franchising seems to be such a fad. As a result, unprecedented attention is being given to the anti-trust aspects of the distribution techniques employed in all franchising programs. The problems of the "franchising industry," however, are common to all systems of distribution and marketing. It so happens that "franchising" comes along as both a cause and effect of the examination of many anti-trust questions which some thought were not questions at all, or at most, questions to which there were satisfactory answers.¹

This article will discuss the courts' current attitudes toward the most frequently encountered techniques for insuring the integrity and effectiveness of marketing programs.² The purpose of this discussion is to alert the reader to the dangers which such distribution techniques often create under the present law. For the sake of simplicity, the observations here will be directed to two kinds of somewhat arbitrarily defined marketing arrangements. The first is the dealer-distributor arrangement, in which a manufacturer-supplier enters into a contract with a dealer or distributor simply for the sale and resale of his merchandise. The second type of arrangement is the franchise, which for the purposes of this discussion

*This article is based on a speech given by the author at an Anti-Trust Seminar presented at the Missouri Bar Association meeting, September 6, 1968, in St. Louis, Missouri, and at a Franchising Seminar presented by the Kansas City Bar Association, February 6, 1969.

**Member of the Missouri Bar; the author practices with the firm of Watson, Ess, Marshall & Enggas, Kansas City, Missouri.

1. One observer recently commented that so much has happened to the anti-trust law during the last twelve years that if anyone were to practice law today according to what was taught in the 1940's, he might well be regarded as a legal "Dennis the Menace." Handler, *The Twentieth Annual Anti-Trust Review* 1967, 53 VA. L. REV. 1667 (1967). This judgment is perhaps more true of the law of distribution and marketing than any others in the anti-trust field.

2. For a discussion of the business and economic considerations which justify or lead to use of such techniques, see AREEDA, *ANTI-TRUST ANALYSIS* 338-509 (1967); Note, 75 HARV. L. REV. 795 (1962).

involves the processing and sale of merchandise or services to the ultimate consumer through a franchisee operating under various trademark and tradename licenses and operating regulations, promulgated by the franchisor and designed to protect and enhance the quality and good will associated with the franchisor's enterprise. This article will focus on five areas commonly regarded as most important in designing a distribution system. These five areas are marked by significant recent changes in the law where change has been made most pronounced. These areas are: (a) resale price maintenance; (b) territorial or location limitations; (c) customer limitations; (d) purchase or operating limitations; and (e) rights of termination and cancellation.³

II. THE MARKET SETTING

The specific control techniques discussed herein cannot be discussed in a vacuum. They must be evaluated in the setting in which they function. This setting has two separate but connected aspects, both of which depend upon the relationship between the parties in the given economic situation. The first of these aspects has to do with the freedom of economic opportunity available to the parties, particularly to the franchisee or distributor; the second has to do with the range of collective action available to the parties in solving their economic problems.

A. *Relative Economic Power*

Two recent cases⁴ appear to stand for the proposition that where the distribution arrangement is part and parcel of a series of inter-

3. For an admirable discussion of the so-called common law of such restrictions, see Chafee, *Equitable Servitudes on Chattels*, 41 HARV. L. REV. 945 (1928), and Chafee, *The Music Goes Round and Round, Equitable Servitudes and Chattels*, 69 HARV. L. REV., 1250 (1956). Of the various anti-trust laws, the following will be referred to: 15 U.S.C. §§ 1 and 2 (1964) [hereafter § 1 or § 2 of the Sherman Act]; 15 U.S.C. § 14 (1964) [hereafter § 3 of the Clayton Act]; 15 U.S.C. § 13a (1964) [hereafter § 2a of The Robinson-Patman Act]; and 15 U.S.C. § 45(a)(1) (1964) [hereafter § 5 of the Federal Trade Commission Act]. The last of these statutes is the broadest of the federal statutes affecting antitrust policy and is aimed at incipient violations or conduct which might amount to an "unfair method of competition." As the Supreme Court has said, "It has long been recognized that there are many unfair methods of competition that do not assume the proportions of antitrust violations. *Atlantic Refining v. FTC*, 381 U.S. 357, 369 (1965). What this means is that the FTC may consider such methods to be antitrust violations, but that the Justice Department or private litigants may not.

Franchise licenses would not appear to be subject to the price discrimination provisions of the Robinson-Patman Act. See *LaSalle Street Press, Inc. v. McCormick & Henderson, Inc.* 293 F.Supp. 1004 (N.D.Ill. 1968).

4. *Permalife Mufflers, Inc. v. International Parts Corp.*, 392 U.S. 194 (1968); *Simpson v. Union Oil Co. of California*, 377 U.S. 13 (1964).

related agreements affecting and controlling a multitude of businesses and is "inherently" coercive so far as the franchisee or distributor is concerned, the arrangement itself may constitute a violation of the anti-trust laws. Hence the franchisee or distributor, may not be barred by his participation in the arrangement from suing the franchisor or seller for treble damages. The emphasis is shifted to an evaluation of the relative economic power of the participants, and away from an evaluation of the agreement between the participants and its effect on the market as a "restraint of trade." To this extent, the analysis becomes, for want of a better term, personalized.⁵

The recent decision in *FTC v. Texaco, Inc.*⁶ confirms this development in the Supreme Court's analysis of distribution arrangements. There, the Supreme Court found that Texaco's dominant economic control over its dealers was inherent in the structure and economics of petroleum distribution. Thus, Texaco's program providing for the sale of Goodrich Tires, batteries and accessories by Texaco dealers was held an unfair method of competition under section 5 of the Federal Trade Commission Act, although there was no evidence of overt coercion on the part of Texaco. This kind of decision is overcompensation for the dealer-franchisee's "lack of bargaining power" with a vengeance. It represents a barely articulated revolt against what are regarded as serious structural imperfections in distribution and marketing arrangements. Unfortunately, there is no way to foresee the consequences of heavy handed attempts to eliminate such imperfections or to balance the parties' "bargaining power" in a manner consistent with some myopic notions of the more perfect marketplace.

B. Collective Action

The second aspect of the market setting concerns the regulation of that special kind of economic power generated by varieties of collective action. Agreements between competitors, or so-called horizontal arrangements, are said to be illegal per se whether they involve prices, customers or territories.⁷ Similarly, if competing "franchisees" or "licensees" agree among themselves or with the seller or franchisor on any number of matters, including distribution techniques, their acts will be illegal,

5. See *The Supreme Court, 1967 Term*, 82 HARV. L. REV. 63, 262-263 (1968).

6. 37 U.S.L.W. 4059 (1968).

7. See, e.g., *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940); *United States v. Addyston Pipe & Steel Co.*, 85 Fed. 271 (6th Cir. 1898), *aff'd*, 175 U.S. 211 (1899).

whether or not a particular technique, considered alone, would be illegal.⁸ In *United States v. Sealy*,⁹ the licensees of Sealy's trademark agreed to restrict the manufacture and sale of mattresses to the territories described in their license agreements. The Supreme Court held that because the licensees owned the trademarks involved; the restraints were not vertically imposed and the licensees' agreements effected an unlawful horizontal territorial allocation.¹⁰ The Court also pointed out that the territorial allocation was a part of a program of trade restraints (including price fixing) and thus no inquiry as to the business purpose or reasonableness of the arrangement was required.¹¹

"Pseudo-horizontal" restraints—restraints not ordinarily regarded as involving competitors¹²—frequently arise in the context of franchise arrangements. For example, all franchisees may have agreed to spend a certain minimum amount on advertising. The maverick franchisee chooses not to make the necessary expenditure. Because reduced advertising reduces the goodwill and value of his trade name, and because of pressure from the other franchisees, the franchisor terminates the maverick's franchise. This hypothetical case resembles the situation in *Miller Motors, Inc. v. Ford Motor Co.*¹³ where Ford had collected from the Lincoln-Mercury dealers assessments made by the Lincoln-Mercury Dealers Association for a co-operative advertising program. It was held that the agreement by Ford to collect for the Association did not violate the anti-trust laws, but the court's scrutiny of the agreement for elements of trade restraint illustrates the potential dangers of such programs.¹⁴

Distinctions must be observed between devices imposed and enforced by the unilateral act of the manufacturer-seller or franchisor, on the one hand, and by concerted action between him and a host of other parties, on the other. The former are presumably legal; the latter are pre-

8. *United States v. General Motors Corp.*, 384 U.S. 127 (1966); *United States v. Sealy, Inc.*, 388 U.S. 350 (1967).

9. 388 U.S. 350 (1967).

10. *Id.* at 354.

11. *Id.* at 357-358.

12. *But see* *United States v. Sealy, Inc.*, 388 U.S. 350 (1967); *United States v. General Motors*, 384 U.S. 127 (1966).

13. 149 F. Supp. 790 (M.D.N.C. 1957), *aff'd.*, 252 F.2d 441 (4th Cir. 1958).

14. Joint advertising programs where references to prices are made are subject to special scrutiny. *See* FTC Advisory Opinion, March 28, 1963, 91 BNA ANTI-TRUST & TRADE REG. REP. X-1, holding that a proposed group publication of an advertisement containing any selling prices raised the questions whether members of the group—in this case, retail drugstores located throughout Iowa—had agreed to sell at such prices. This advisory opinion raised serious doubts about the advisability of any co-operative advertising plan where price information was to be included.

sumably illegal. There is no question in the anti-trust law of distribution which presents as many pitfalls as the question of whether an act is "unilateral" (and hence outside the strictures of section 1 of the Sherman Act) or "concerted." Of course, since section 1 of the Sherman Act is directed only to unreasonable restraints of trade and thus only to contracts and combinations which *unreasonably* restrain competition, an act that is concerted is not necessarily illegal.¹⁵ The usually complicated inquiry into the "reasonableness" of an arrangement, however, has led several courts to focus on the threshold question of whether there exists the requisite agreement,¹⁶ and to hold many acts unilateral which the Supreme Court's current tests of "contract, combination or conspiracy" would probably not justify.

III. SPECIFIC CONTROL TECHNIQUES

A. Resale Price Maintenance

Surprisingly enough, resale price maintenance provisions are commonly found in so-called franchise agreements.¹⁷ In some cases, the agreement may expressly provide that the goods or services to be marketed will be sold or distributed at prices established by the franchisor. In other cases, the agreement may provide that prices will be set by the franchisee, subject to the approval of the franchisor. In still others, the contract will provide nothing about pricing, but the practice of the parties will be to permit, indeed, require the approval of the franchisor as to the prices for the goods and services involved. Such price restrictions are increasingly rare in distributor situations where there is only a sale for resale.

1. The *Albrecht* case—Unilateral v. Concerted Action

Price-fixing agreements between competitors are per se illegal under section 1 of the Sherman Act.¹⁸ Like horizontal price-fixing, vertical price-

15. See *Northern Pacific Ry. v. United States*, 356 U.S. 1, 4-5 (1958); *Appalachian Coals, Inc. v. United States*, 288 U.S. 344, 360-361 (1933); *Chicago Board of Trade v. United States*, 246 U.S. 231, 238 (1918). See also *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365, 374 (1967).

16. See *Carbon Steel Products Corp. v. Alan Wood Steel Co.*, 289 F. Supp. 584, 587-588 (S.D.N.Y. 1968).

17. Resale price maintenance agreements are intended to prevent price cutting by the distributor or franchisee or sales to "discounters." They are also employed to prevent sales at prices above levels which the manufacturer or franchisor thinks his product must be sold in order to remain competitive.

18. *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940).

fixing or "resale price maintenance," as it is usually called, is for all practical purposes similarly illegal.¹⁹ No case better illustrates the almost certain illegality of vertical price-fixing arrangements than the Supreme Court's decision in *Albrecht v. The Herald Company*.²⁰ The Court applied the rule that maximum resale price maintenance was illegal per se, and that a seller cannot combine with others to refuse to deal as a means of insuring adherence of such resale prices. *Albrecht* was a treble damage case brought by a newspaper carrier against the owner of a newspaper, the *St. Louis Globe Democrat*. The *Globe-Democrat* was delivered to customers in the St. Louis area each morning through a system of 172 routes. The carriers on these routes were designated independent contractors, purchasing the papers at wholesale and selling them at retail. Plaintiff's route had approximately 1,200 customers. The carriers were subject to termination of contract for charging more than the *Globe Democrat's* suggested retail price.²¹ Plaintiff began "overcharging" in 1961, and was subsequently informed of customer complaints concerning his prices. The *Globe-Democrat* in 1964 told him that it would allow competition on his route by another carrier who would sell at the lower prices. Solicitation letters were sent to plaintiff's customers in behalf of the new carrier, and the letters were followed by house-to-house solicitations. The campaign resulted in a customer list of 314 persons which was taken over by the substitute carrier with the understanding he might be required to return it to plaintiff. The *Globe-Democrat* continued to sell papers to the plaintiff for resale, the paper again warning plaintiff that under the con-

19. See *United States v. Parke, Davis & Co.*, 362 U.S. 29 (1960); *United States v. General Motors*, 384 U.S. 127 (1966). Historically, resale price maintenance was thought to be possible where there was a genuine agency or consignment relationship between the manufacturer or supplier and the dealer. See *United States v. General Electric Co.*, 272 U.S. 476 (1926). However, this idea is of doubtful validity today. *Simpson v. Union Oil Co. of California*, 377 U.S. 13 (1964), appears to put the "G.E. doctrine" to rest in the case of consignment agreements where the manufacturer-supplier exercised "coercive" control over the dealer. But see *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365 (1967), which appears to hold out some hope for "genuine" agency or consignment arrangements if resale price maintenance is not a part of them. On consignment selling generally, see *Sun Oil Co. v. FTC*, 350 F.2d 624 (7th Cir. 1965).

20. 390 U.S. 145 (1968), *rev'g* 367 F.2d 517 (8th Cir. 1966).

21. The contract with the carriers provided:

The right of each carrier whose appointment is effective to sell the *St. Louis Globe-Democrat* by home delivery in his territory, will be maintained exclusively to him under the terms of his appointment so long as the price at which such sales are made in his territory shall not be higher than the price therefor suggested by the publisher for such sales in the City or County in which such territory is located.

Albrecht v. The Herald Company, 367 F.2d 517, 519 (8th Cir. 1966).

tract it was not required to continue to do business with him. After plaintiff had instituted suit, the *Globe-Democrat* notified him of the termination of his carrier contract. The Supreme Court found a "combination" between the *Globe-Democrat*, the solicitor of plaintiff's customers, and the substitute carrier, all of whom "knew" that plaintiff's customers would be returned to him if he complied with the newspaper's price demands. An important footnote to Mr. Justice White's opinion indicates that the "combination" between the *Globe-Democrat* and plaintiff's former customers might also have been illegal, and that a combination between the newspaper and other carriers might have existed because "the firmly enforced price policy applied to all carriers, most of whom acquiesced in it."²²

At one time, it was thought that so long as the seller enforced his resale price maintenance policy by unilateral action, his conduct was not illegal.²³ *Albrecht* shows that such "unilateral" acts are almost non-existent under the current Supreme Court standards for an illegal agreement.²⁴

A recent case illustrating the difficulties of applying the *Albrecht* decision is *Carbon Steel Products Corp. v. Allen Wood Steel Co.*,²⁵ where a steel supplier refused to deal with his former customer-distributor because the customer was allegedly selling cheap imported steel as well as higher priced domestic steel. The former distributor claimed the refusal to deal was intended to eliminate the competition from the imported steel. He attempted to sue the supplier under one of the theories suggested in *Albrecht*—that an illegal combination or conspiracy could be found in

22. 390 U.S. 145, 150 n.6. See also *Sahm v. V-1 Oil Co.*, 5 TRADE REG. REP. (1968 Trade Cas.) ¶ 72,604 (10th Cir. 1968), holding an illegal combination may exist between a terminated dealer or his supplier "at least as of the day he unwillingly complied" with the supplier's price maintenance policy; *Stanton v. Texaco, Inc.*, 289 F. Supp. 884 (D. R.I. 1968).

23. See *United States v. Colgate & Co.*, 250 U.S. 300 (1919); *United States v. A. Schrader's Son, Inc.*, 252 U.S. 85, 99-100 (1920).

24. The range of possibilities for a conspiracy theory which were opened up by the *Albrecht* case have been explored by others. See, e.g., *The Supreme Court, 1967 Term*, 82 HARV. L. REV. 63, 257-260 (1968). There it is suggested that the finding of conspiracy between the newspaper and its corporate agents was not justifiable. The implication is that any vertical re-sale price maintenance scheme is likely to be conspiratorial wherever outside corporate agents are employed in any way to assist the corporate defendant. As noted there, the Court's theory of conspiracy may put a premium on size because the functions performed by the outside agents could, under certain conditions, be performed by the corporate defendant itself. *Id.* at 257-258.

25. 289 F. Supp. 584 (S.D.N.Y. 1968).

a unilateral refusal to deal with a customer failing to comply with the supplier's demands. The court held that theory was unavailable since the plaintiff had never discontinued the sale of imported steel.²⁶

As the immediate discussion shows, the *Albrecht* case is as important for what it says about the law of illegal combinations and conspiracies under section 1 of the Sherman Act as it is for its pronouncement on maximum resale price maintenance. Indeed, no act or course of conduct in the field of marketing and distribution can be evaluated for its anti-trust implications without attention to the possible "contracts, combinations or conspiracies" which may arise in a given business situation. Thus, techniques and limitations which are otherwise lawful, may be used in a business setting which makes them improper, coercive and illegal.²⁷

2. Resale Price Maintenance Under State Law

Vertical price-fixing provisions of distribution and franchise agreements may be illegal under state statutes as well as federal anti-trust laws. Thus, a Dairy Queen franchise which required adherence to suggested retail prices established by the franchisor was held illegal and void under the governing Missouri anti-trust statutes.²⁸ The party to that franchise agreement agreed in writing that all retail selling prices might be set by the franchisor and that the franchisee would not deviate from those prices.²⁹

3. Alternative to Vertical Price Fixing

Decisions condemning resale price maintenance mean that such agreements may be challenged by a whole host of parties, including wholesale or retail customers who are cut off for failure to follow either suggested minimum or maximum resale prices, by wholesalers or distributors who are canceled because they have resold to price-cutters or discounters, or by persons complaining of excessive prices resulting from this so-called ver-

26. Apparently, plaintiff would have to establish a combination or conspiracy between defendant and its other customers who complained about plaintiff's sales of imported steel. The court also considered this approach and held that mere complaints to the defendant by the plaintiff's competitors were not sufficient to establish a conspiracy under section 1. *Id.* at 588.

27. *Cf.* *Advance Business Systems & Supply Co. v. SCM Corp.*, 287 F. Supp. 143, 157 (D. Md. 1968).

28. §§ 416.010-416.050, RSMo 1959.

29. *Temperato v. Horstman*, 321 S.W.2d 657, 662-663 (Mo. 1959). *See also* *State v. Miles Laboratories*, 282 S.W.2d 564 (Mo. En Banc 1955), involving vertical price-fixing practices. *Contra*, *Vess v. Fred Astaire Dance Studios Corp.*, 229 F.2d 892, 894 (5th Cir. 1956), applying Texas law and holding that minimum rates for dance lessons were not prohibited by Texas anti-trust laws.

tical price-fixing. Moreover, maximum resale price maintenance may be challenged by competitors of the party who established the maximum resale price on the ground that such maximum resale prices were part of a scheme to monopolize a particular market since the maximum resale price tended to operate as a barrier to entry of new competition in that particular field.

All this talk about resale price maintenance does not prevent the manufacturer from fair-trading his merchandise or suggesting retail prices.³⁰ Nonetheless, there are substantial difficulties with programs based on fair-trading and "pre-ticketing." First, many states are not "fair-trade" states; and even in fair-trade states,³¹ such programs must be rigorously policed or the seller will lose the right to resale price maintenance.³² Second, if suggested price or pre-ticketing programs are to be legal, compliance may not be compelled and the danger is always present that a suggested resale price program may become what Justice Fortas has identified as a "silent combination or understanding."³³

A form of "pre-ticketing" may be found in many franchising programs. Thus the franchisor may suggest a retail price through widespread price advertising or by supplying pre-priced merchandise or promotional literature to the franchisee.³⁴ A subtle use of illegal resale price maintenance may be encountered in the promotion of programs such as one requiring the dealer or franchisee to feature prices which are acceptable to the supplier as a prerequisite to the receipt of advertising allowances.³⁵ Questions may also be raised by the practice of requiring that the fran-

30. See, e.g., *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365 (1967).

31. Among the fair-trade states are, e.g.: Arkansas, Colorado, Florida, Iowa, Oklahoma, and Pennsylvania. On the other hand, Missouri, Kansas, Nebraska, and Texas are among the non fair-trade states.

32. If the resale price maintenance agreement is between competitors or parties operating at the same "functional level," fair trade does not immunize it. See *United States v. McKesson & Robbins*, 351 U.S. 305 (1956); *Esso Standard Oil Co. v. Secatore's, Inc.*, 246 F.2d 17 (1st Cir.), cert. denied, 355 U.S. 834 (1957).

33. *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365, 382 (1967).

34. Compare *Plymouth Dealers' Ass'n. of No. Cal. v. United States*, 279 F.2d 128, 132 (9th Cir. 1960), with *United States v. Nationwide Trailer Rental System*, 156 F. Supp. 800 (D. Kan.), aff'd., 355 U.S. 10 (1957).

35. See 16 C.F.R. § 240.9 (1968), in which the FTC states that such an arrangement is illegal. Compare FTC Advisory Opinion No. 309, 3 TRADE REG. REP. ¶ 18,594 (1968), dealing with the question of whether an allowance program could be conditioned on an agreement not to advertise prices below cost with FTC Advisory Opinion No. 163, 3 TRADE REG. REP. ¶ 18,174 (1968), dealing with a proposed policy of selling only to those who do not use such terms as "sale" or "closeout" in their advertising. See also *Lessig v. Tidewater Oil Co.*, 327 F.2d 459 (9th Cir.), cert. denied, 377 U.S. 993 (1964).

chisee contribute, for example, 3% of his gross sales to a national advertising program, and also that the franchisee use only approved advertising copy featuring prices.³⁶

B. Territorial or Location Limitations

Territorial or location limitations are also very common in the typical dealership or franchise agreement. There are two kinds of territorial limitations, both of which produce somewhat different anti-trust problems. The first is an agreement by the manufacturer or franchisor that he will not authorize anyone else in a territory or at a location to deal in his product or service. The second is an agreement by the dealer or franchisee that he will confine his activities to a particular territory or location.

1. Exclusive Dealership Agreements

The first type of territorial limitation is governed by the "rule of reason." That is to say there must be a full factual record regarding the economic effect of the territorial limitation and the court must determine, on that record, whether the limitation amounts to an unreasonable restraint of trade.³⁷

[A] manufacturer of a product other and equivalent brands of which are readily available in the market may select his customers, and for this purpose he may 'franchise' certain dealers to whom, alone, he will sell his goods. [Citation omitted] If the restraint stops at that point—if nothing more is involved than vertical 'confinement' of the manufacturer's own sales of the merchandise to selected dealers, and if competitive products are readily available to others, the restriction, on these facts alone, would not violate the Sherman Act . . .³⁸

36. See *United States v. Serta Associates*, 5 TRADE REG. REP. (1968 Trade Cas.) ¶ 72,543 (N.D. Ill. 1968), in which the use of "suggested list prices" contained in national advertising and combined with interference with local advertising showed a violation of section 1 of the Sherman Act. See also *United States v. Container Corporation of America*, 5 TRADE REG. REP. (1969 Trade Cas.) ¶ 72,675 (U.S. 1969).

37. Such restrictions on the seller's freedom to sell are not violative of section 1 if the seller is not dominant in the market. See *Bascom Launder Corp. v. Telecoin Corp.*, 204 F.2d 331, 335 (2d Cir.), cert. denied, 345 U.S. 994 (1953); *Packard Mtr. Car. Co. v. Webster Mtr. Car. Co.*, 243 F.2d 418, 420 (D.C. Cir.), cert. denied, 355 U.S. 822 (1957), dealing with agreements by a seller to sell its entire output to one buyer.

38. *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365, 376 (1967). The Court cited *United States v. Colgate & Co.*, 250 U.S. 300 (1919), in support of its statement.

This pronouncement should be taken to permit continuation of the rule allowing contracts whereby the manufacturer or franchisor merely grants the dealer or franchisee an exclusive territory and agrees not to compete with the dealer or franchisee or to locate another dealer or franchisee in the assigned area.³⁹

2. Territorial Confinement Agreements

Territorial limitations of the second type presently raise the greatest number of anti-trust problems. Until the *Schwinn*⁴⁰ case, the conventional wisdom was that, absent horizontal features, such a location or territorial confinement arrangement was legal so long as it satisfied the rule of reason.⁴¹ The legality or illegality of such restrictions was tested by an analysis of the facts peculiar to the particular business, including the relevant market for the goods and services involved and the market power of the parties.

The *Schwinn* case changed all this. Justice Fortas' analysis is summed up in the following sentence:

Once the manufacturer has parted with title and risk, he has parted with dominion over the product, and his effort thereafter to restrict territory or persons to whom the product may be transferred—whether by explicit agreement or by silent combination or understanding with his vendee—is a *per se* violation of section 1 of the Sherman Act.⁴²

39. *White Motor Co. v. United States*, 372 U.S. 253, 271 n. 11 (1963); *Schwinn Motor Co. v. Hudson Sales Corp.*, 138 F. Supp. 899 (D. Md.), *aff'd*, 239 F.2d 176 (4th Cir. 1956), *cert. denied*, 355 U.S. 823 (1957); *Packard Motor Car Co. v. Webster Motor Car Co.*, 243 F.2d 418 (D.C. Cir.), *cert. denied*, 355 U.S. 822 (1957). In *United States v. Bausch & Lomb Optical Co.*, 45 F. Supp. 387, 398-399 (S.D.N.Y. 1942), *aff'd* (by equally divided court), 321 U.S. 707 (1944), the court upheld an agreement whereby Bausch & Lomb agreed to manufacture certain glass only for Soft-Lite and not to compete with it in the sale of lenses made from such glass. The business reasons for sustaining such a restriction on competition by the manufacturer-franchisor are explained in the *Bausch & Lomb* case and in Note, *Restricted Channels of Distribution Under The Sherman Act*, 75 HARV. L. REV. 795, 824-827 (1962). See *United States v. Imperial Chemical Industries*, 105 F. Supp. 215, 244-245 (S.D.N.Y. 1952), also upholding such an arrangement; *United States v. American Type Founders Co.*, TRADE REG. REP. (1958 Trade Cas.) ¶ 69,065 (D.N.J. 1958); *United States v. Pitney-Bowes, Inc.*, 5 TRADE REG. REP. (1959 Trade Cas.) ¶ 69,235 (D.Conn. 1959), involving consent decrees permitting exclusive distributorship arrangements.

40. *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365 (1967).

41. *United States v. White Motor Co.*, 372 U.S. 253, 263 (1963).

42. *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365, 382 (1967). This language could mean that a passage of title test may be applied to determine the legality or illegality of territorial or location restrictions. If the manufacturer or franchisor is selling its products and merchandise to the dealer or franchisee for resale, territorial or location restrictions are illegal. If, on the other hand, the products of

The *Schwinn* case involved two general kinds of distribution devices. Roughly 25% of Schwinn's output was marketed to distributors under outright sales. The rest of its output was sold under the "Schwinn Plan," where the distributor acted as an order taker and the sale was made directly by Schwinn to the retail account. The legality of the 25% sales for resale was governed by the language quoted above; the 75% of Schwinn's volume sold under the Schwinn Plan was to be tested under the rule of reason, looking "to the specifics of the challenged practices and their impact upon the marketplace in order to make a judgment as to whether the restraint is or is not reasonable"⁴³

Following the decision in *Schwinn*, Donald L. Turner, the then assistant Attorney General for the Justice Department's Anti-Trust Division was asked whether there would have to be a showing of justification or reasonableness of territorial limitations if a true agency were involved and the distributor was no more than a selling arm of the manufacturer. He responded:

I would certainly contemplate that there are situations in which the distributor is performing no more than a straight selling function and where he is doing it for this competitor only (because if he is doing it for all of them, or if he is a general distributor of many lines, then you get into problems), and where for all practical purposes he is just the selling representative of the manufacturer, an employee, then the manufacturer may properly be entitled to tell him what to do, price, who he can sell to, the territory in which he can sell⁴⁴

It is apparent from Turner's other remarks that he preferred to focus the inquiry on the nature of the function the distributor is performing and that where the distributor assumes certain responsibilities and risks, then restrictions as to price, customer and territory may be illegal. He indicated that such additional functions and responsibilities included ware-

the franchisor or manufacturer are provided to the franchisee or dealer on a consignment or agency basis, such restrictions may be proper.

In view of *Schwinn*, reliance on such cases as *Snap-On-Tools Corp. v. FTC*, 321 F.2d 825 (7th Cir. 1963), to justify territorial restrictions is unwise. The opinion of the court of appeals in *Sandura Co. v. FTC*, 339 F.2d 847 (6th Cir. 1965) may stand on somewhat different footing. In that case, closed territories were approved, principally because of its small market share (4.8% of the floor covering industry's sales). Justice Fortas' opinion in *Schwinn* may be said to tolerate territorial and location limitations under such circumstances. *Id.* at 374.

43. *Ibid.*

44. N.Y. State Bar Association Anti-Trust Symposium 39 (1968).

housing, the possession of goods, and the handling of transportation—"anything significant beyond simply order taking and selling."⁴⁵ A simple "passage of title" test thus would not suffice to determine the legality of a distribution arrangement.

A recent case illustrates the host of problems which *Schwinn* may spawn in this area. A terminated distributor sued its manufacturer-supplier for treble damages under the Clayton Act. Plaintiff moved for summary judgment based on the territorial resale limitations of the distributorship agreement. Each of the defendant's distributors was supplied with the defendant's products for resale to dentists on the distributor's own account subject to certain conditions, including the following:

To provide after-sales service in a satisfactory manner dealers are forbidden to make shipments beyond the normal range of their service facilities. . . .

The Company or the dealer may terminate relations at any time.

In the face of these restrictions, plaintiff made sales "beyond the range of its service facilities" and defendant, after repeated warnings to plaintiff that it was violating the distributorship agreement, cancelled their relationship.⁴⁶

The question before the court on plaintiff's motion for summary judgment was whether the condition banning sales beyond the range of the dealers' service facilities was illegal under *Schwinn*. Passing over the business purpose for a territorial restriction tied to service, the court indicated that if only a sale of the products were involved, with no strings attached, a per se violation of the Sherman Act resulted from any territorial restraint on resale; whereas, if the distributor's role was indistinguishable from that of an agent or salesman of the manufacturer, "no violation of the Sherman Act occurs unless the restriction is an unreasonable one."⁴⁷ The court denied plaintiff's motion for summary judgment, holding that it could not decide whether the territorial restrictions were illegal, even under *Schwinn*, until the nature of the relationship between the distributor and the manufacturer-supplier could be determined. The implica-

45. *Id.* at 44.

46. *Sherman v. Weber Dental Mfg. Co.*, 285 F. Supp. 114, 115 (E.D. Pa. 1968).

47. *Id.* at 116.

tion is clear that if the plaintiff was an agent or salesman only, the territorial restriction would not be illegal.

Valid territorial restrictions even in an agency arrangement may be difficult to achieve. The reasoning of the *Simpson*⁴⁸ case, which outlawed consignment agreements used coercively to maintain resale prices, may suggest the illegality of agency agreements used coercively to achieve territorial limitations. And, if the distributor or franchisee is viewed as a competitor,⁴⁹ the manufacturer or franchisor's designation of him as an agent may result in a ruling that the purpose of the agreement was to end competition between the manufacturer-franchisor and the agent-franchisee in violation of section 1 of the Sherman Act.

Still a different rule is to be applied where a franchise or license arrangement provides for territorial limitations in connection with the licensing of a trademark or service mark, and the sale of ingredients or parts, for combination into a product which is sold under that trademark or service mark. Traditionally, such arrangements have been viewed as requiring ancillary restraints to protect the trade or service mark and the licensor or franchisor's interest in the mark. So long as those restraints were reasonable and necessary to protect the mark, they were viewed as proper.⁵⁰

The Carvel Ice Cream litigation⁵¹ illustrates the rationale of those cases. While not expressly dealing with territorial restraints, Commissioner

48. *Simpson v. Union Oil Co.*, 377 U.S. 13 (1964). See *Advance Business Systems & Supply Co. v. SCM Corp.*, 287 F. Supp. 143, 157 (D.Md. 1968).

49. See *United States v. Masonite Corp.*, 316 U.S. 265 (1942).

50. See *Denison Mattress Factory v. Spring-Air Co.*, 308 F.2d 403, 409 (5th Cir. 1962); *Huber Baking Co. v. Stroehmann Bros. Co.*, 252 F.2d 945, 956 (2d Cir.), cert. denied, 358 U.S. 829 (1958); *E. F. Pritchard Co. v. Consumers Brewing Co.*, 136 F.2d 512 (6th Cir. 1943), cert. denied, 321 U.S. 763 (1944). See also *Parkway Baking Co. v. Freihofer Baking Co.*, 255 F.2d 641 (3d Cir. 1958), where plaintiff licensee had the exclusive right to bake and sell bread under the licensed mark and brought an action for damages and an injunction against defendant, an "exclusive licensee" in another territory, on the ground that defendant was selling to a distributor within his (defendant's) territory for ultimate distribution in plaintiff's territory. Plaintiff was granted the requested relief by the trial court. On appeal of the injunction issue only, the Court of Appeals for the Third Circuit reversed because defendant had discontinued the practice complained of. The court stated in dictum that plaintiff had recovered his damages because he was a third party beneficiary of the contract between defendant and the licensor; i.e., the agreement that defendant was an exclusive licensee restricted defendant's sales activity to a particular area.

51. *Carvel Corp.*, [1965-67 Transfer Binder] TRADE REG. REP. ¶ 17,298 (FTC 1965); *Susser v. Carvel Corp.*, 206 F. Supp. 636 (S.D.N.Y. 1962), aff'd., 332 F.2d 505 (2d Cir. 1964), cert. granted, 379 U.S. 885 (1965), cert. denied, 381 U.S. 125 (1966).

Jones' opinion in Carvel's FTC proceedings applying section 5 of the Federal Trade Commission Act is particularly illuminating. The case involved comprehensive provisions of a franchise program which restricted the locations of the dealers' outlets, the sources from which the dealers could purchase supplies, and the standards which the finished product must meet. In essence, the arrangements were held by the FTC to be reasonably ancillary to the trademark and its license to the various dealers.

Returning to territorial restrictions, it seems perfectly clear from the *Schwinn* decision that in the resale of finished articles of commerce, without more, territorial restrictions are not available to the established and successful manufacturer.⁵² On the other hand, Justice Fortas' opinion leaves it open to the newcomer or the failing company to adopt territorial restrictions in order to acquire business or stay in business.⁵³ Moreover, the Justice Department has recognized the practical problems of the manufacturer or franchisor in securing conscientious distributors or franchisees. In the final judgment in the *Schwinn* case, the Justice Department and Schwinn agreed to provisions which prohibited the company from limiting distributors and retailers as to where and to whom they may resell products. But Schwinn retained the right to impose territorial and customer restraints where it still owned the bicycles under consignment and agency agreements.

52. Rufus E. Wilson, Chief of the F.T.C.'s Division of General Trade Restraints, recently stated that a franchisor who sold extracts and reagents to a soft drink bottler and then attempted to restrict the sale of the soft drink to a specific territory might be going far beyond what was attempted and held to be illegal in *Schwinn*. Wilson pointed out that a franchisor was attempting, under those circumstances, to restrict the transfer or "alienation" of a product manufactured from an ingredient he had already sold and that this seemed to present a situation one step beyond the illegal restraint in *Schwinn*, which only involved a restraint on the actual product sold. Wilson, "Antitrust Policy in Franchising," presented before the California and Nevada Soft Drink Association, February 11, 1969, page 7. Wilson did not mention the special interest of the trade mark licensor in imposing such restraints.

53. 388 U.S. 364, 374 (1967). Former anti-trust division chief Donald Turner appears to believe that so long as territorial limitations in trademark licenses are not indefinite in duration and are reasonably designed to enable the licensee to recoup startup costs or investments in developing the mark in a particular territory, such vertically imposed territorial restrictions may be proper. N.Y. State Bar Association Anti-Trust Symposium 12 (1968). See also *Snap-On-Tools Corp. v. FTC*, 321 F.2d 825, 829-833 (1963), outlining the business reasons for the use of such restrictions. The Supreme Court's most recent opinion in this area, *Perma-Life Mufflers v. International Auto Parts*, 392 U.S. 134 (1968), expressly left this matter open. In footnote 4 to his opinion, Mr. Justice Black referred to defendant's argument that the restraints in question were permissible as a reasonable means to protect the registered trade and service marks. He also referred to the fact that because they had failed to answer interrogatories pertinent to this defense the district judge ordered it stricken without prejudice to renewal if defendants answered the relevant interrogatories.

More importantly, paragraph VI of the judgment stated that Schwinn was *not* prevented from:

maintaining and creating or eliminating areas or territories of prime responsibility for its distributors; from choosing and selecting its distributors and retailers or designating geographic areas in which such distributors shall respectively be primarily responsible for distributing Schwinn products, or from terminating such distributorships of distributors who do not adequately represent Schwinn and promote the sale of Schwinn products in areas so designated as their primary responsibility; from designating in its retailer franchise agreements the location of the place or places of business for which the franchise is issued.⁵⁴

“Location clauses” authorizing the dealer or franchisee to operate at a given location, and agreeing not to appoint another dealer or franchisee in the area contiguous to that location also appear to be proper, at least at this time.⁵⁵

Other methods may be employed to insure dealer or franchisee concentration on business in a particular location or in a particular territory. Justice Brennan alluded to one such method in his concurring opinion in *White Motor Company v. United States*.⁵⁶ There he was speaking of the sanctions which may be imposed by the franchisor or franchisees who “raid” or sell across territorial boundaries. He said:

If, for example, such a cross-sale incurs only an obligation to share (or “pass over”) the profit with the dealer whose territory has been invaded—as is most often, and apparently here, the case—then the practical effect upon competition of a territorial limitation may be no more harmful than that of the typical exclusive franchise—the lawfulness of which the government does not dispute here. If, on the other hand, the dealer who cross-sells runs the risk under the agreement of losing his franchise altogether, intrabrand competition across territorial boundaries involves serious hazards which might well deter any effort to compete.⁵⁷

While one may or may not take Mr. Justice Brennan’s passing reference to the “typical exclusive franchise” as an indication of his views on that sub-

54. 5 TRADE REG. REP. (1968 Trade Cas.) ¶ 72,480 at 85,569 (N.D. Ill. 1968). The FTC apparently feels that designation of areas of prime responsibility is permissible. Snap-On-Tools Corp., TRADE REG. REP. (1961 Trade Cas.) ¶ 15,546 at 20, 413-414 (FTC 1961).

55. In *United States v. General Motors Corp.*, 384 U.S. 127 (1964), the Justice Department disclaimed any attack on General Motors’ location clauses. See also *Boro Hall Corp. v. General Motors*, 124 F.2d 822 (2d Cir. 1942).

56. 372 U.S. 253 (1963).

57. *Id.* at 270-271.

ject, it is at least clear that royalty adjustments may thus be employed to secure adherence to territorial restrictions.⁵⁸ Establishment of sales quotas, inventory requirements, or standards of performance may also serve the same purpose.⁵⁹

This statement from *White Motor* is a reminder of the important fact that the response of the manufacturer or franchisor to violations of the dealer or franchise agreement must be carefully examined. One response may have anti-trust consequences; another may not.⁶⁰

Despite the use of location clauses, areas of primary responsibility, and "pay over" provisions, the difficulties of territorial restrictions in franchise and dealership agreements persist. Are the territorial limitations designed by and for the benefit of the dealers and distributors, or are they designed to serve exclusively the manufacturer or franchisors' interest?⁶¹ If the franchisees and dealers are responsible for the territorial limitations and restrictions, then they would be illegal even though the restrictions were formally and ostensibly imposed by the manufacturer through his franchise agreement rather than through an inter-dealer agreement.⁶² Moreover, if it appears that territorial restrictions are ancillary to a price-fixing or price stabilization program, they may be struck down regardless of what the arrangement is called on paper.⁶³

C. Customer Limitations

Restraints as to the customers with whom a dealer or franchisee may deal are also common. As in the case of vertically imposed territorial limitations, the conventional wisdom prior to the *Schwinn* decision was that cus-

58. See Brief for United States at 18, 20-21, *United States v. Sealy, Inc.*, 388 U.S. 350 (1967).

59. See *Victory Motors of Savannah, Inc. v. Chrysler Motors Corp.*, 357 F.2d 429, 430-432 (5th Cir. 1966); *Kotula v. Ford Motor Co.*, 338 F.2d 732, 735-738 (8th Cir. 1964), cert. denied, 380 U.S. 979 (1965); *Pick Mfg. Co. v. General Motors Corp.*, 80 F.2d 641, 642, 644 (7th Cir. 1935), aff'd per curiam, 299 U.S. 3 (1936); *Hammond Ford, Inc. v. Ford Motor Co.*, TRADE REG. REP. (1967 Trade Cas. ¶ 71,689 (S.D.N.Y. 1966)).

60. *Snap-On-Tools v. FTC*, 321 F.2d 825 (7th Cir. 1963). These responses are more fully discussed later in this article in the discussion of termination of distributorships and franchises.

61. See *White Motor Co. v. United States*, 372 U.S. 253, 267 (1963).

62. *United States v. Sealy, Inc.*, 388 U.S. 350 (1967).

63. *Albrecht v. The Herald Co.*, 389 U.S. 805 (1968); *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365, 373 (1967); *United States v. Sealy, Inc.*, 388 U.S. 350 (1967); *United States v. Bausch & Lomb Optical Co.*, 321 U.S. 707, 720 (1944).

tomers limitations were to be tested by the rule of reason.⁶⁴ In *White Motor*⁶⁵ case, involving the imposition of extensive customer and territorial restrictions upon White's dealers, the Supreme Court held that the legality or illegality of White's distribution program could be determined only after a trial and a rule of reason inquiry.

The *Schwinn* case made it clear that if the manufacturer or franchisor has sold the merchandise to the dealer or franchisee, customer restrictions which confine the "wholesaler" to approved "retailers" are per se illegal under section 1 of the Sherman Act. In *White Motor*, the customer restrictions provided not only for controlled reselling, as in *Schwinn*, but also for reserving certain customers and classes of ultimate customers to the manufacturer. Distributors and dealers agreed not to sell trucks to any federal or state government or to any department or political subdivision unless White Motor granted them the right.⁶⁶ Such reservations of customers are presumably still governed by *White Motor* and not by *Schwinn*.⁶⁷ Mr. Justice Brennan's concurring opinion in the *White Motor* case,⁶⁸ where he deals at length with the problem of customer restrictions, should be carefully studied, however. His opinion provides antecedents and amplification for much of what Mr. Justice Fortas says in *Schwinn*. There is some strong language by

64. When, however, customer restrictions were used to achieve resale price maintenance, there was no question of their illegality. *United States v. Bausch & Lomb Optical Co.*, 321 U.S. 707 (1944); *Ethyl Gasoline Corp. v. United States*, 309 U.S. 436 (1940).

65. *White Motor Co. v. United States*, 372 U.S. 253 (1963). White Motor argued to the trial court that the purpose of the customer restrictions was to assure the company "that 'national accounts,' 'fleet accounts' and Federal and State governments and departments and political subdivisions thereof, which are classes of customers with respect to which the defendant is in especially severe competition with the manufacturers of other makes of trucks and which are likely to have a continuing volume of orders to place, shall not be deprived of their appropriate discounts on their purchases of repair parts and accessories from any distributor or dealer, with the result of becoming discontented with The White Motor Company and the treatment they received with reference to the prices of repair parts and accessories for White trucks." *Id.* at 257. White also argued that a manufacturer may properly enter into agreements which restrict his distributors to sales of one class of customer leaving sales to other classes of customers to the manufacturer. *Id.* at 258-259.

66. *White Motor Co. v. United States*, 372 U.S. 253, 256 (1963).

67. Similar customer restrictions were involved in *Roux Distrib. Co.*, 55 FTC 1386 (1959), where the manufacturer restricted each distributor to a particular class of customers which it was best able to serve. Because there was no showing that the restrictions substantially lessened competition, the FTC dismissed the complaint against Roux. The *Roux* case raises the question of whether an absolute prohibition against resale of a dangerous product to the public would be tested by the rule of reason or by a per se rule. See *Chicago Sugar Co. v. American Sugar Ref. Co.*, 176 F.2d 1, 8-9 (7th Cir. 1949), cert. denied, 338 U.S. 948 (1950).

68. 372 U.S. 253, 272-275.

Mr. Justice Brennan indicating that under certain circumstances a "dual distribution" system involving this second type of customer restriction may also be illegal per se:

The second justification White offers (for customer restrictions) is that 'the only sure way to make certain that something really important is done right, is to do it for oneself.' This argument seems to me to prove too much, for if the distributors truly cannot be counted on to solicit and service the governmental and fleet accounts—not all of which are, in fact, large or demanding,—then this suggests that the only adequate solution may be vertical integration, the elimination of all independent or franchised distribution. But that White is either unwilling or unable to do. Instead, it seeks the best of both worlds—to retain a distribution system for the general run of its customers, while skimming off the cream of the trade for its own direct sales. That, it seems to me, the anti-trust laws would not permit . . . if in fact the distributors could compete for the reserved accounts without the restrictions.⁶⁹

No court has gone so far as Mr. Justice Brennan's remarks would seem to lead. Many anti-trust observers believe that a manufacturer or franchisor is still entitled to develop and maintain house accounts or to grant franchises which reserve certain fields or classes of business to the franchisor so long as the restriction does not have the effect of stifling price competition.⁷⁰ One may sense in the *Schwinn* opinion, however, a general abhorrence of all customer restrictions. While the distinction between restrictions which confine a dealer's sales to certain specific customers, on the one hand, and restrictions by which he may sell to all but certain customers reserved to the manufacturer, on the other, may have practical importance, it may also be without legal significance.⁷¹

D. *Limitations on Purchases, Supplies, Products and Services*

1. Purpose of the Restrictions

Limitations on the kinds and sources of products or ingredients which

69. *Id.* at 274.

70. *Cf. Reines Distributors, Inc. v. Admiral Corp.*, 257 F. Supp. 619 (S.D. N.Y. 1965), which held that a seller's "division" and "wholly owned subsidiary" were not purchasers so as to allow a proceeding against the seller under the price discrimination provisions of section 2a of the Robinson-Patman Act.

71. *See Interphoto Corp. v. Minolta Corp.*, 5 TRADE REG. REP. (1969 Trade Cas.) ¶ 72,694 (S.D.N.Y. 1969). The problem again appears of what means other than termination or cancellation of the franchise can be used to achieve adherence to customer restrictions. While cross royalty agreements may be adopted they may prove to be unenforceable.

the franchisee or dealer may buy or use or limitations on the manner in which he may operate (apart from the specific areas already discussed) are the last important kind of restriction to be discussed in this article. These limitations are very important to the seller or franchisor because it is by limiting the products and services used by his customer or franchisee that he insures integrity of his business and the consistency of the quality of his products as they reach the ultimate consumer. They are also important because they insure the distribution and sale of the products on which the seller or franchisor profits. This fact is self-evident where the distribution problem involves the seller and his dealer, but it is also true in the case of the franchisor and the franchisee. In such cases, the franchisor may earn a substantial amount on the sale of supplies or merchandise which, under the terms of the franchise agreement, the franchisee is obligated to use. In such cases, the franchisor may earn considerably more for the sale of such items than he does from the royalties for the use of a trade-name, trademark or business method.

These restrictions are also important to the franchisee or dealer. The benefits of such limitations are in management control and marketing know-how. More important, they also insure uniformity of product or service and thus an entry into an established market. There are also disadvantages to the franchisee or dealer. Frequently, he wishes to use sources of supply other than those approved by the seller or franchisor. He may also find that he wishes to expand into lines of goods and services which may not be compatible with those approved by the seller or franchisor.

2. Exclusive Dealership Agreements and Requirements Contracts

A variety of anti-trust questions are raised by these restrictions. These questions are usually analyzed in terms of "traditional" categories such as exclusive dealing and tying arrangements and requirements contracts. Some such product and supply limitations result in exclusive dealing arrangements. The dealer or franchisee agrees to sell only the products of the seller or franchisor and he agrees not to sell similar products of any other manufacturer.⁷² One effect of such an arrangement may be the foreclosure of the

72. The Dairy Queen franchise at issue in *Engbrecht v. Dairy Queen Co.*, 203 F. Supp. 714 (D. Kan. 1962), provided that the licensees agreed to use "their best efforts to develop the Dairy Queen business within the franchise area involved, and to maintain the high standards of appearance, public approval and acceptance previously established for the Dairy Queen business," "to sell no product other than Dairy Queen products without defendants approval," to use the trade name "Dairy

seller or franchisor's competitors from the market represented by the buyer or franchisee. This arrangement is the kind which the FTC attacked in the *Brown Shoe Company* proceedings.⁷³ That case involved Brown Shoe's plan under which some 650 franchised dealers of Brown, the second largest shoe manufacturer, received various benefits in return for a promise to purchase shoes, primarily from Brown. The FTC and the Supreme Court concluded that an exclusive dealing which effectively foreclosed competitors, from a "significant number" of outlets was illegal as an "unfair method of competition" under the very liberal requirements of section 5 even though such dealing might not violate the Sherman and Clayton Acts.

As the opinion in *Brown Shoe* indicated, an entirely different approach must be taken in suits brought under section 1 of the Sherman Act or section 3 of the Clayton Act.⁷⁴ There must be a weighing of the "probable effect of the contract on the relevant area of effective competition . . . and the probable immediate and future effects which pre-emption of that share of the market might have on effective competition therein."⁷⁵ There must be, in other words, a "rule of reason" inquiry as to whether there has been or is likely to be a substantial lessening of competition.

Requirements contracts were involved in the *Tampa Electric* case,⁷⁶ where a coal producer had agreed to supply the coal requirements of a

Queen" with no other products, and to refrain from engaging "in a competitive business selling ice-cream or ice-milk or other frozen or semi-frozen dairy products" within a ten mile radius of the store, both during the term of the franchise and for a period of two years following termination of the franchise. See Findings of Fact, Nos. 15, 16 and 17, *Engbrecht v. Dairy Queen* (Civil No. W-1772) (unreported). In upholding these provisions, the court held that substantial market foreclosure had not been demonstrated.

73. *FTC v. Brown Shoe Co.*, 384 U.S. 316, 321 (1966). *Accord*, *Luria Bros. & Co. v. FTC*, 389 F.2d 847 (3rd Cir. 1968), *cert. denied*, 390 U.S. 946 (1968); *Mytinger & Casselberry, Inc.* 57 FTC 717 (1960), *aff'd.*, 301 F.2d 534 (D.C. Cir. 1962), involving section 3 of the Clayton Act.

74. Exclusive dealing arrangements involving "commodities" are usually tested by section 3 of the Clayton Act, 15 U.S.C. § 14 (1964), because it is easier for the prosecutor or plaintiff to show that an exclusive dealing arrangement may substantially lessen competition or have a tendency to create a monopoly under that section than it is to show that an exclusive dealing arrangement is an unreasonable restraint of trade under section 1 of the Sherman Act. However, where land or services are involved, section 1 must be applied because section 3 is limited by its terms to "goods."

75. *Tampa Elec. Co. v. Nashville Coal Co.*, 365 U.S. 320, 329 (1961).

76. *Tampa Elec. Co. v. Nashville Coal Co.*, *supra* note 74. A restrictive buyer's contract of the sort involved in *Tampa* is the converse of a "full" output contract under which the manufacturer agrees to sell its entire output to one buyer. Such a full output contract, which limits the freedom of the manufacturer to deal with other buyers, is not a violation of section 1 so long as the seller does not hold a dominant position in the market and the output contract is limited in duration. See *Packard Motor Car Co. v. Webster Motor Car Co.*, 243 F.2d 418, 420 (D.C. Cir.), *cert. denied*, 355 U.S. 822 (1957); *Bascom Lauder Corp. v. Tele-Coin Corp.*,

power company for a twenty-year period. The contract covered less than one per cent of the coal produced and marketed on the Eastern Seaboard. In the power company's declaratory judgment suit, the court of appeals held that the contract was unenforceable because it violated the antitrust laws. The Supreme Court reversed. In upholding this requirements contract, it distinguished the exclusive dealing cases, pointing out that Nashville Coal Company was not a dominant seller and did not have substantial sales volume coupled with industry-wide reliance upon exclusive contracts or plainly restrictive tie-in agreements. In the Court's judgment, the percentage of market foreclosure to competitors of the seller by the arrangement in question was not sufficient to require condemnation under the anti-trust laws.

3. Tying Agreements

A similar test of market foreclosure is applied in the tying cases,⁷⁷ although the tendency has been to treat them more severely. Tying arrangements involve the sale of one product or service (the "tying" article) on the condition that the buyer will purchase some other product or service (the "tied" article). Dominance or foreclosure of the market for the tying product or service usually requires an analysis of the market in which it is sold, except that foreclosure or dominance may be presumed from a showing that the tying item is patented, copyrighted or otherwise unique.⁷⁸ In the case of a franchise program, it is sometimes difficult to say that there is a tying and a tied product or service. There is a franchise package, sold as a unit, and the elements are not marketed separately. In this situation the tying cases may not apply at all.⁷⁹

204 F.2d 331, 335 (2d Cir.), *cert. denied*, 345 U.S. 994 (1953). *Cf.* Hershey Chocolate Corp. v. FTC, 121 F.2d 968 (3rd Cir. 1941).

On the question of whether partial requirements contracts might not be proper, see Luria Bros. & Co. v. FTC, 389, F.2d 847 (3rd Cir. 1968) and Luria Bros., [1961-63 Transfer Binder] TRADE REG. REP. ¶ 16, 183 (FTC 1962).

77. See *United States v. Loew's, Inc.*, 371 U.S. 38 (1962); *Northern Pacific Ry. Co. v. United States*, 356 U.S. 1 (1958); *Times-Picayune v. United States*, 345 U.S. 594, 614 (1953).

78. See *Fortner Enterprises, Inc. v. United States Steel Corp.*, — U.S. —, 37 U.S.L.W. 4297 (April 7, 1969), 5 TRADE REG. REP. (1969 Trade Cas.) ¶ 72,757 (U.S. 1969), suggesting that such dominance might possibly be shown by the personal uniqueness of the tying product, in that case credit, to the supplier's customer. See also, *IBM v. United States*, 298 U.S. 131 (1936) (patent); *United States v. Loew's, Inc.*, 371 U.S. 38 (1962) (copyright).

79. *Times-Picayune v. United States*, 345 U.S. 594, 614 (1953); *Carvel Corp.*, [1965-67 Transfer Binder] TRADE REG. REP. ¶ 17,298 (FTC 1965). Such a "package" may raise questions of "full line forcing." See *Pick Mfg. Co. v. General Motors Corp.*, 80 F.2d 641 (7th Cir. 1935), *aff'd. per curiam*, 299 U.S. 3 (1936).

4. Trademarks and Product and Supply Limitations

To achieve the maximum benefits of restrictions on sources of supply or products to be sold, they must be economically necessary and they generally must be related to the good will, reputation and image of the supplier or franchisor.⁸⁰ Trademarks or service marks thus become the vehicles for these restrictions. Indeed, the legal effect of all such limitations may be very different if they appear in a franchise context involving trademark licenses rather than in a simple purchase and sale. A case which illustrates the importance of trademarks in restricting the franchisee to products and supplies approved by the franchisor is *Franchised Stores of New York, Inc. v. Winter*.⁸¹ Plaintiff in that case was a franchisor which had been granted a license of the Carvel trademark and trade-name in order to develop and operate a franchise system. Defendant was alleged to have sold certain products in his Carvel store which were neither manufactured nor authorized by the Carvel organization or the Carvel franchise contract.⁸²

The trial court had dismissed plaintiff's complaint for lack of federal jurisdiction since it felt the infringing acts occurred in intrastate commerce and were thus not within the coverage of the Lanham Act.⁸³ In reversing the trial court's dismissal, the court of appeals first satisfied itself that the Lanham Act protected against the kind of acts committed by defendant. The court said:

It would be totally illogical to provide protection to a trademark owner where someone uses a 'colorable imitation' of the mark but

80. See *Chicken Delight Eastern, Inc. v. Hunter Paper Co., Inc.*, 5 TRADE REG. REP. (1968 Trade Cas.) ¶ 72,448 (N.Y. Sup. Ct. 1968), where the court observed that it is lawful for a franchisor to contract with its franchisees for the use of packaging material that will assure quality of exclusively delivered food stuffs sold by them. That action involved a lawsuit by the franchisor to enjoin the defendant from selling paper packaging products to an operator of Chicken Delight stores in the New York Metropolitan area.

81. 394 F.2d 664 (2d Cir. 1968). Several of the same franchise agreement provisions that were at issue in the Federal Trade Commission and earlier Second Circuit proceedings were involved in the *Winter* case.

82. Defendant admitted using "Liberty" syrup on Carvel products dispensed in "Carvel" containers and also selling "Marchiony" ices in unmarked paper squeeze cups. The fourth clause of the franchise agreement provided that the franchisee would sell Carvel's frozen dairy products solely in accordance with the franchise manual and would sell no other product except as expressly provided in the agreement; in the sixth clause of the agreement the franchisee agreed, in order to protect the integrity of Carvel's trademarks to purchase from Carvel or from sources approved and designated by Carvel his entire requirements of Carvel's frozen dairy products, mixed toppings, flavorings and other ingredients, cones and any other item sold as a part of the "end product."

83. 15 U.S.C. § 1114 (1964), providing for federal registration of trademarks.

to deny protection where the owner's own mark is employed to palm off on the public the merchandise of someone else. . . . Though Winter in the instant case initially had permission to use the 'Carvel' mark, that consent did not cover the use of the mark on non-Carvel goods⁸⁴

The court found that the Carvel trademark was used in connection with the sale of unauthorized goods and that since the Carvel trademark covered not only the ice-cream but also the type of retail outlet at which the ice-cream was sold, the defendant's use of the Carvel mark in connection with the sale of other ices in plain cups also violated plaintiff's right. The court then reviewed the authorities holding that a trademark owner must, under applicable provisions of the Lanham Act,⁸⁵ control his licensee to prevent the mark from losing its significance as an indication of origin. Otherwise, the trademark owner might suffer cancellation of its federal registration.⁸⁶

The franchise agreements employed by the Carvel Corporation in the sale and distribution of soft ice-cream raise in a direct way many of the questions considered in this part of the article.⁸⁷ Those agreements show how the typical franchise scheme cuts across many traditional anti-trust categories, including exclusive dealing, tying arrangements and requirements contracts. Under Carvel's franchise agreement, Carvel licensed retail dealers to use its patents, copyrights and business methods and to operate roadside stands selling its trademarked ice-cream and related products. Carvel had originally developed a freezer and soft ice-cream mix and prior to 1949 was primarily engaged in the business of manufacturing and selling freezers for the production of soft ice-cream. Because of the unsuccessful operations of

84. *Franchised Stores of New York, Inc. v. Winter*, 394 F.2d 664, 668 (2d Cir. 1968).

85. 15 U.S.C. §§ 1064, 1127 (1964).

86. Having found that defendant infringed plaintiff's marks, the court rejected the trial court's holding that defendant's unauthorized sales of non-Carvel products in purely intrastate commerce were not sufficient to confer jurisdiction on the federal court because the alleged infringement did not actually occur in interstate commerce. In the court of appeals' view, defendant's unauthorized sales had a "substantial effect" on interstate commerce in that the sale of such products at individual Carvel stores had a potentially adverse effect on the entire Carvel system, and that effect was sufficient to confer jurisdiction on the federal courts to enjoin the infringement. 394 F.2d 664, 670 (2d Cir. 1968). *Cf. Temperato v. Horstman*, 321 S.W.2d 657 (Mo. 1959), discussed *infra* in pt. III D(6), which suggests that Carvel's restrictions on its franchisee's sources of supply would probably violate the Missouri anti-trust laws.

87. *Suser v. Carvel Corp.*, 206 F. Supp. 636 (S.D.N.Y. 1962), *aff'd*, 332 F.2d 505 (2d Cir. 1964), *cert. granted*, 379 U.S. 885 (1965), *cert. dismissed*, 381 U.S. 125 (1966). The related FTC proceedings are reported as Carvel Corp., [1965-67 Transfer Binder] TRADE REG. REP. ¶ 17,289 (FTC 1965).

many of the purchasers of these freezers, Carvel decided in 1949 not to install equipment unless it controlled the operation of the store, and to this end began the development of a system of franchised retail dealers. These retail dealers' premises, the paper cones and all the various products and items used in the sale of Carvel soft ice-cream carried the Carvel trade-name or trademark and were all of identical design in accordance with Carvel's design patents. Under the franchise agreement, the retailer-dealer was required to purchase from Carvel and from sources designated by Carvel, his entire requirements of mix, toppings, flavors and other ingredients, cones and any other items which constituted a part of the end product sold at retail to the consuming public. The dealers were also required to operate in strict accord with procedures prescribed by Carvel's Standard Operating Procedure Manual regulating the operation of the store and equipment, sanitation procedures, methods to be used as to flavoring, freezing and dispensing ice-cream mix as well as other products made from the mix. Among other things, the Manual described the products which the franchisees could sell, the advertising they could use, the color they could paint the store, the hours they could turn their lights on and off, the amount of insurance they were required to carry, and the kind and color of the uniforms worn by their employees. The dealers were permitted to manufacture or handle only those products specifically prescribed by Carvel.

The FTC complaint charged that the franchise agreements and Carvel's practices were illegal insofar as they required each franchise licensee-dealer: (1) to purchase its entire supply of ice-cream mix and associated products from Carvel or from persons designated by Carvel; (2) to refrain from selling products not authorized by Carvel; (3) to purchase various items of equipment from Carvel; (4) to adhere to those contract provisions through a rigorous policing system involving threats and coercion directed to dealers and to non-approved suppliers; (5) to refrain from entering into a similar business within three years after termination of the franchise. After extensive hearings, the trial examiner concluded that the Carvel franchise agreements were illegal "tying" agreements which tied the purchase of equipment, ice-cream mix and commissary items to licenses to use the Carvel name, copyrights, patents, products and techniques.⁸⁸

88. [1965-67 Transfer Binder] TRADE REG. REP. ¶ 17,298 at 22,423 (FTC 1965). It is interesting to speculate why the FTC complaint counsel chose to proceed with his case against Carvel on the theory of tying devices rather than exclusive dealing. The answer may be that he believed, based on *Northern Pacific Ry. v. United States*, 356 U.S. 1 (1958), that the former were illegal per se whereas the latter were to be tested under the rule of reason.

On review of the trial examiners' decision before the full Commission, all the charges were dismissed. The Commission concluded that Carvel's franchise agreements were not illegal tying agreements and that the steps taken to enforce those provisions were not violative of section 5 of the Federal Trade Commission Act. In reaching this result the Commission first decided Carvel's franchise agreements could not be considered tying arrangements because the trademark license conceptually could not constitute a tying product, and even if it could, it could not be regarded as a product separate from the mix and commissary items to which it was attached. The Commission said:

It seems clear that since no property right inheres in a trademark apart from the product or service to which it relates, and since trademarks may be licensed but only on condition that the trademark owner retains control over the licensee's use of the trademark, it is conceptually impossible, in our opinion, to view a license to use a trademark as separate and distinct from the sale of the trademark product or its ingredient. The Carvel franchise serves the single purpose of permitting the dealer to sell the trademarked products as trademarked, and cannot really be separated from the license. Both were necessary in combination to permit the dealer to exercise fully the license.

. . . .

Moreover, tie-in arrangements must involve two separable and distinct products and have been held not to exist where the courts concluded that the two products could not be disassociated from each other [citing cases]. Since Carvel's franchise for the sale of Carvel products and its license to use are part of a single package, we conclude that the examiner erred in holding that the Carvel franchise agreements were illegal tie-in arrangements.⁸⁹

The Commission completed its analysis of the Carvel system by concluding that Carvel's restrictions on its dealer's sources for mix and other supplies were reasonably related "to Carvel's right—and obligation—to con-

89. [1965-67 Transfer Binder] TRADE REG. REP. ¶ 17,298 at 22,426 (FTC 1965).

trol the quality of its trademarked product and identity and image of its tradename."⁹⁰

The Court of Appeals for the Second Circuit applied standards similar to those of the Federal Trade Commission in analyzing the Carvel franchise agreement in the context of treble damage actions in the case of *Susser v. Carvel Corp.*⁹¹ There Carvel's franchise agreement with the licensee-plaintiffs required them to purchase the ice-cream mix they used in the manufacture of the ice-cream from suppliers designated by Carvel, and further required them to purchase paper goods, napkins, cones, extracts, spoons and other related products from sources approved by Carvel. Carvel's co-defendants were two of the suppliers who had been "approved" or "designated" by Carvel as sources from which its licensees could purchase the ice-cream mix. Plaintiffs alleged that the requirements that they purchase the mix from a source of supply designated by Carvel was an unlawful tying arrangement under both section 3 of the Clayton Act and section 1 of the Sherman Act. Plaintiffs made no showing that other suppliers of ice-cream mix competing with "approved" suppliers were foreclosed from a substantial amount of the market for ice-cream mix.

The district court ruled the plaintiffs had failed to make a case either under section 3 of the Clayton Act or under section 1 of the Sherman Act, holding that the "requirement imposed by Carvel that the plaintiffs use the supplier defendants' product or products approved by Carvel was not illegal tie-in or a violation of the anti-trust laws in any respect." In reaching this conclusion, the district court emphasized (1) that there was no indication that Carvel "reaped any profit itself from any of the tie-ins" and (2) that it was clear that the purpose of the limitation on licensees as to their source of supply of ice-cream mix (and other accessories) was imposed upon the licensees solely for the purpose of protecting the good will and trademark of Carvel.⁹² The court also observed:

The plaintiffs made no showing, as ordinarily required under the cases, that Carvel occupies a dominant position as a franchisor of soft ice cream or seller of ice cream freezers, or even that a sub-

90. *Id.* at 22,427. See also *Crawford Transport Co. v. Chrysler Corp.*, 338 F.2d 934, 936 (6th Cir. 1964), *cert. denied*, 380 U.S. 964 (1965); *Denison Mattress Factory v. Spring-Air Co.*, 308 F.2d 403, 410-11 (5th Cir. 1962). A good discussion of controlled licensing and its indicia is found in *Heaton Distributing Co. v. Union Tank Car Co.*, 387 F.2d 477, 485 (8th Cir. 1967).

91. 332 F.2d 505 (2d Cir. 1964), *aff'g* 206 F. Supp. 636 (S.D.N.Y. 1962), *petition for cert. dismissed*, 381 U.S. 125.

92. *Suser v. Carvel Corp.*, 206 F. Supp. 636, 646 (S.D.N.Y. 1962).

stantial amount of commerce in the 'tied' products was foreclosed. In the absence of these facts there is no basis for recovery.⁹³

The Court of Appeals for the Second Circuit affirmed, holding that plaintiffs failed to establish Carvel's market dominance and that a substantial amount of commerce was affected by the arrangements in dispute.⁹⁴

The Carvel franchise arrangement and its evaluation by the courts and the FTC has been discussed in detail to suggest the difficult problem which faces counsel in evaluating restriction on sources of supply and exclusive dealing arrangements. In franchise, license and dealership arrangements, it takes no great imagination to see the need for an extensive inquiry into the reasonableness or business purpose of an arrangement or the market effect or market position of the parties before the legality of a program can be determined.⁹⁵ A more narrow inquiry is possible where the activities of the franchisee or licensee affect an asset of the franchisor or licensor, *i.e.*, his trademark, trade name or service mark, and good will.⁹⁶

5. A Broader Test: Freedom of Entry

The foregoing analysis may be somewhat over-simplified, however. One senses, in recent Supreme Court cases, that the emphasis on substantial market foreclosure as the test of illegality presages or is a part of a broader anti-trust policy favoring free access to markets by competing suppliers and sellers, freedom of choice by buyers and customers, and general equality of economic opportunity.⁹⁷ To the extent that vertical restrictions raise barriers

93. *Id.* at 646. (Emphasis added.)

94. *Susser v. Carvel*, 332 F.2d 505 at 512, 518 (2d Cir. 1964). The Federal Trade Commission's decision also considered this phase of the tying agreement. *Carvel Corp.* [1965-67 Transfer Binder] TRADE REG. REP. ¶ 17,298 at 22,429 (FTC 1965). In addition to holding that Carvel's restrictions on its franchisee's rights to secure products and supplies from third persons were necessary to protect its trademark, goodwill and business methods, and that the franchise package did not lend itself to treatment as a tying arrangement, the FTC concluded that even if it were to view the franchise as a tying arrangement, the facts of the case did not show there was the requisite economic power in the relevant market with respect to the tying product. *Id.* at 22,429-22,430. The Commission then pointed out that the record was barren of the kind of evidence required by the Supreme Court's decision in *Tampa Electric Co. v. National Coal Co.*, 365 U.S. 320 (1961).

95. There is some indication that exclusive dealing arrangements for no more than a year will not be illegal. See FTC Advisory Opinion No. 254 (5-30-68) approving an exclusive check cashing concession in grocery stores for one year.

96. *Cf. A & E Plastic Pak Co., Inc. v. Monsanto Co.*, 3 TRADE REG. REP. (1968 Trade Cas.) ¶ 72,487 (9th Cir. 1968), dealing with "sham" licensing apparently intended to avoid certain anti-trust prohibitions.

97. See Kauper, *The "Warren Court" and the Anti Trust Laws: of Economics, Populism and Cynicism*, 67 MICH. L. REV. 325, 331-333 (1968).

to entry and bar access to markets, they deprive the parties of opportunities which they need in order to do business and hence may be illegal. A highly significant case in developing this approach with respect to the kind of anti-trust problems considered in this article is *Silver v. New York Stock Exchange*.⁹⁸ The case revolved about the right of the New York Stock Exchange to terminate a securities dealer's private wire service for alleged violation of the Exchange's rules. The Supreme Court held the "boycott" was illegal per se because the plaintiffs had been deprived "of a valuable business service which they needed in order to compete effectively as broker-dealers in the over-the-counter securities market."⁹⁹ This result was reached, however, after an evaluation and balancing of the parties' conflicting interests.

The opinion in *Silver* is also significant because it appears to narrow the scope of the district court's broad prohibition against concerted action in this kind of situation.¹⁰⁰ As one commentator observed, the less sweeping rule had its origin in an amicus brief filed by the Solicitor General in the *Silver* case.¹⁰¹ There it was suggested that concerted refusals to deal would be deemed illegal where no price-fixing or monopolization was involved only if they prevented access to the market on an equitable and non-discriminatory basis by all those who were in, or seeking to enter, the market. The *Silver* case is thus especially important in evaluating conditions of access to "markets" such as the franchisees or distributors of a particular product or service.¹⁰²

Use of specifications or standards are occasionally suggested as a means of insuring such freedom of access to markets, customers, or suppliers and eliminating the need for exclusive dealing. The FTC considered this point in the *Carvel* case but concluded that specifications under the circumstances of that case were not enough to achieve the franchisor's business purposes and that Carvel was entitled to insist on purchases from approved suppliers.

98. 373 U.S. 341 (1963).

99. *Id.* at 347.

100. *Silver v. New York Stock Exchange*, 196 F. Supp. 209, 222-223 (S.D.N.Y. 1961).

101. See Groenke, *What's New In the Anti-Trust Aspects of Selecting and Terminating Distributors*, 13 ANTI-TRUST BULL. 131, 138 (Spring 1968).

102. Cf. Use of the Carter-Fone Device and Message Toll Telephone Service, FCC Docket No. 16942 (1967); *Carter v. A.T. & T. Co.*, FCC Docket No. 17073 (1968), in which the FCC refused to reconsider its decision striking down an A. T. & T. tariff prohibiting the use of any telephone-interconnection devices not furnished by the telephone company. The FCC held that a telephone company may prohibit the use of only those foreign attachments that adversely affect the telephone system and a tariff proscribing harmless and harmful devices alike is unreasonable if it assumes *a priori* that there will be harmful effects.

The hearing examiner took the view that Carvel could have prescribed specifications for the manufacture of ice-cream mix and that specification of the type and quality of the product to be used in connection with the franchise was protection enough to Carvel. The FTC rejected these conclusions and held that while quality might be achieved by specifications, uniformity of product probably would not be. Moreover, the FTC stated that it was the government's burden to present evidence sufficient to persuade the Commission that specifications would have produced the requisite uniformity and quality control.¹⁰³

6. State v. Federal Regulation of Product and Supplier Limitations

The conflict between state and federal regulation of the control devices discussed in this part of the article raises important questions of choice of law and federal "pre-emption." Sometimes state courts fail to give adequate consideration to the federal law which may be applicable in a given case.

In the *Temperato* case¹⁰⁴ the Missouri Supreme Court appeared to lump together contractual provisions that all materials used in the operation of the Dairy Queen Franchises must meet the franchisor's standards of quality and specifications with provisions that all supplies must be purchased from approved sources. The court said that while such quality control provisions may be proper and even necessary under federal law relating to trademark licensing, federal authorities did not control if they conflicted

103. Cf. *International Business Machines Corp. v. United States*, 298 U.S. 131 (1936); *International Salt Co. v. United States*, 332 U.S. 392 (1947); *Dehydrating Process Co. v. A. O. Smith Corp.*, 292 F.2d 653, 657 (1st Cir. 1961), *cert. denied*, 368 U.S. 931 (1962). A franchise or distribution system in which each member or participant is authorized to use a certification mark to identify his product as one meeting standard specifications raises related anti-trust problems. See *Structural Laminates, Inc. v. Douglas Fir Plywood Assoc.*, 261 F. Supp. 154 (D. Ore. 1966), *aff'd*, 399 F.2d 155 (9th Cir. 1968), *cert. denied*, 37 U.S.L.W. 3242 (1969), dismissing plaintiffs' treble damage claims against a trade association for promulgation of a trade standard which allegedly resulted in a boycott of one of the plaintiffs' products. FTC Commissioner Mary Gardiner Jones considered some of these problems in a recent speech on the adoption of voluntary standards before the USA Standards Institute in Washington, D. C. on December 10, 1968. See also letter of Edwin M. Zimmerman, Dept. of Justice, Anti-Trust Chief, to Malcolm W. Jensen, Chief of the Office of Weights and Measures, in which Zimmerman states that informal standardization of packaging undertaken by an industry group with the cooperation of the Department of Commerce in order to avoid the delay of formal proceedings under the Fair Packaging & Labeling Act will not immunize participants and adherents from procedures under the anti-trust laws. 387 A.T.R.R. (12-10-68) p. X-1.

104. *Temperato v. Horstman*, 321 S.W.2d 657 (Mo. 1959). See discussion pt. III, § A of this article.

with Missouri anti-trust law. The court held that restrictions giving the franchisor power to designate and change the sources for any and all supplies used in the operation of the franchise are illegal and void under Missouri statutes.¹⁰⁵ The court also implied there may be a question as to the legality of a requirement that no product other than Dairy Queen was to be sold on the premises of the franchisee.

This decision clearly fails to take account of extensive protection given registered trademarks and service marks under federal law. First, the Lanham Act gives notice, effective throughout the nation, that a particular mark is owned by a particular person.¹⁰⁶ Such notice is sufficient to give nationwide protection to the mark owner. Second, the statute requires the mark owner to exercise such control over use of the mark as to insure that it does not lose its significance as an indication of origin.¹⁰⁷ The Lanham Act is thus read to require quality control of the sort which the Missouri Supreme Court indicated was per se illegal under Missouri anti-trust law.¹⁰⁸

The *Temperato* case raises the question of whether this kind of state regulation of an interstate concern doing business under registered trademarks can be tolerated. In other words, is not the state "policy" pre-empted by a federal policy and regulatory scheme developed under the Lanham Act and federal anti-trust laws?¹⁰⁹ Proper recognition and resolution of the pre-emption problem is suggested by *TNT Communications, Inc. v. Management Television Systems, Inc.*,¹¹⁰ where it was held, *inter alia*, that a coun-

105. 321 S.W.2d 657, 665. The Missouri law under which the *Temperato* case was decided does not apply to services as opposed to goods or commodities. See *Harelson v. Tyler*, 281 Mo. 383, 219 S.W. 908, 913 (1920); *State v. Green*, 344 Mo. 985, 988, 130 S.W.2d 475, 477 (1939); *Standard Monument Co. v. Mt. Hope Cemetery*, 369 S.W.2d 876, 880 (St. L. Mo. App. 1963).

106. 15 U.S.C. § 1072 (1964), known popularly as the Lanham Act, § 22.

107. 15 U.S.C. § 1055 (1964), dealing with use of the mark by related companies. "Related Company" is defined in 15 U.S.C. § 1127 (1964) as "any person who legitimately controls or is controlled by the registrant or applicant for registration in respect to the nature and quality of the goods or services in connection with which the mark is used."

108. See *Franchised Stores of N.Y. Inc. v. Winter*, 394 F.2d 664 (2d Cir. 1968).

109. Compare *Engelhardt v. Bell & Howell Co.*, 327 F.2d 30, 35 (8th Cir. 1964) and *International Railways of Central America v. United Fruit Co.*, 373 F.2d 408, 417 (2d Cir. 1967), with *Cream Top Creamery v. Dean Milk Co.*, 383 F.2d 358, 363-364 (6th Cir. 1967). See also *St. John v. State Farm Mut. Auto. Ins. Co.*, 225 F.Supp. 74 (W.D. Mo. 1964).

110. 5 TRADE REG. REP. (1968 Trade Cas.) ¶ 72,653 (N.Y. Sup. Ct. 1968). The complaint in that case was based on alleged wrongful acquisition and use of trade secrets by plaintiff's former employees now working for defendant. Defendant's answer, among other things, combined an affirmative defense with a counter-claim

ter-claim could not be sustained because state law was inapplicable in view of the interstate character of the subject matter, a multi-media network with no particular New York impact in its operations. The court pointed out that regardless of whether the network was regulated by the FCC, such networks were "inherently involved in interstate commerce and regulated by the Federal Anti-Trust Laws."¹¹¹ Hence, the New York Anti-Trust Act could not regulate that area. The courts did, however, permit the pleading of the defendants to stand as an affirmative defense.

The *TNT* court's focus on the interstate commerce aspects of plaintiff's business and the product involved indicate the importance of the commerce question in such cases. In cases where the effect on commerce is slight, there may be a place for regulation of the parties' conduct pursuant to state anti-trust statutes. On the other hand, where interstate commerce is the dominant element in the parties' relationship and the products and services involved, federal law should pre-empt the field.¹¹² Doubts should be resolved in favor of application of a uniform federal rule even though the state courts have "concurrent jurisdiction." Trademarks and service marks registered under the Lanham Act and the products and services which they identify certainly call for application of the pre-emption principle.¹¹³

Apart from the serious "Federal pre-emption" and choice of law questions raised by the Missouri Supreme Court's decision in the *Temperato* case, the case creates significant practical problems for a national franchising concern doing business in Missouri and states with similar notions. The

which asserted claims under the federal and state anti-trust laws. See *Denison Mattress Factory v. Spring-Air Co.*, 308 F.2d 403, (5th Cir. 1962); *Vendo Co. v. Stoner*, 5 Trade Reg. Rep. (1969 Trade Cas.) ¶ 72,747 (Ill. App. 1969). Compare *Sears, Roebuck and Co. v. Stiffel Co.*, 376 U.S. 225 (1964), holding that state law of unfair competition was pre-empted by the federal policy implicit in the patent laws and the anti-trust laws.

111. *Id.* at 86,331.

112. See *Burke v. Ford*, 389 U.S. 320 (1967), holding that an alleged conspiracy to divide territories and brands in the sale of liquor in Oklahoma affected commerce as a matter of law because such arrangements, if proved, "almost invariably" and "inevitably" affect commerce. This decision suggests that interstate commerce is the dominant element in almost every distribution plan.

113. See *Franchised Stores of N.Y., Inc. v. Winter*, 394 F.2d 664, 669-670 (2d Cir. 1968). On the question of whether there is a substantial or insubstantial effect on commerce, see *Sunbeam Corp. v. Wentling*, 185 F.2d 903, 907-908 (3d Cir. 1950), *vacated and remanded*, 341 U.S. 944 (1951), *on remand*, 192 F.2d 7 (3d Cir. 1951). Compare, *Dean Milk Co. v. FTC*, 5 TRADE REG. REP. (1968 Trade Cas.) ¶ 72,559 (9th Cir. 1968) *with* *Abramson v. Colonial Oil Co.*, 390 F.2d 873 (5th Cir. 1968), *cert. denied*, 37 U.S.L.W. 3133 (Oct. 15, 1968). *But see* *State v. Arkansas Lumber Co.*, 260 Mo. 212, 169 S.W. 145 (1913).

contracts in *Temperato* were held to be void because they were contrary to the declared public policy and public interest of the State of Missouri.¹¹⁴ The holding of the Missouri Supreme Court suggests that even if the franchise or dealership contract expressly provides that the law of some other state will govern, the anti-trust law of Missouri (or the state involved) must be examined to determine the legality of many of the agreement's provisions, especially those containing restrictions of the kind discussed here.

E. *Reprise: The General Problem of Discipline and Termination
of Dealerships and Franchises*

1. Generally

Earlier in this article some emphasis was placed on an analysis of the setting in which marketing control techniques are employed.¹¹⁵ Another aspect of this setting is the manner in which the manufacturer-seller or franchisor secures adherence to his distribution plan including price, territory, customer, supplier or product restriction. This disciplinary aspect is most commonly revealed in dealership or franchise termination cases. Many of the situations encountered by the lawyer involve the manufacturer-franchisor who wishes advice as to how to terminate a distribution relationship or the local dealer or franchisee whose contract or franchise has been cancelled. Therefore, this article will close with a brief discussion about the manner in which the four principal areas of restrictions affect the right to terminate business relations with dealers, franchisees, and otherwise to discipline them.

Mr. Justice Brennan's concurring opinion in the *White Motor* case¹¹⁶ shows how conduct apparently in breach of a franchise or dealership agreement can best be evaluated for anti-trust purposes by examining the response which the manufacturer, seller or franchisor makes to such conduct. The implication is that extreme measures which seem punitive to the court

114. *Temperato v. Horstman*, 321 S.W.2d 657, 665 (Mo. 1959). See *Order of United Comm'l Travelers v. Meinsen*, 131 F.2d 176 (8th Cir. 1942); *May v. Mulligan*, 36 F. Supp. 596 (W.D. Mich. 1939), *aff'd*, 117 F.2d 259 (6th Cir. 1940); *Holland Furnace Co. v. Connelly*, 48 F. Supp. 543 (E.D. Mo. 1942). Cf. Annot., 70 ALR2d 1297. See also *Asel v. Order of United Comm'l. Travelers*, 193 S.W.2d 74, 80 (K.C. Mo. App. 1946), *aff'd*, 355 Mo. 658, 197 S.W.2d 639 (1946); *Maxey v. Railey & Bros. Banking Co.*, 57 S.W.2d 1091 (K.C. Mo. App. 1933), holding that certain contracts valid where made could not be enforced in Missouri because they violated the law of that state.

115. Pt. II *supra*.

116. *White Motor Co. v. United States*, 372 U.S. 253, 264 (1963).

or regulatory agency suffice to convert otherwise lawful unilateral activity into conduct violative of the anti-trust laws.¹¹⁷

2. Discipline and Resale Price Maintenance

Thus, the *Albrecht* decision represented an attempt by a manufacturer-seller, the St. Louis *Globe-Democrat*, to cancel a dealer for failure to observe maximum resale prices which the manufacturer-seller suggested.¹¹⁸ To be sure, there were elements of conspiratorial conduct in the case in that the newspaper, a solicitor and substitute distributor, were involved in "coercing" the dealer to observe the resale price schedule. It was obvious to all concerned that if the terminated dealer got back into line on the observance of the resale prices suggested by the newspaper, his franchise would be returned to him. Perhaps if the newspaper had acted "unilaterally," its action would have been held legal, but occasions when action is truly unilateral are very infrequent.¹¹⁹ One can only conclude that policing and discipline which in any form are intended to achieve resale price maintenance are exceedingly dangerous.

3. Discipline and Restrictions on Territories, Customers, Products and Supplies

Absent a situation where the purpose of the discipline (including termination or cancellation) is to induce compliance with a resale price maintenance program,¹²⁰ the question is, can a manufacturer-seller or franchisor compel the observance and adherence to the other kinds of restrictions preciously discussed. *Amplex of Maryland v. Outboard Marine Corp.*,¹²¹ recently denied certiorari by the Supreme Court,¹²² demonstrates the seriousness of this question but hardly supplies its answer. There, Outboard Marine refused to renew Amplex's franchise for the sale of marine motors because it had not discontinued selling Mercury outboard motors, a competing product. Outboard Marine then awarded the franchise to another Mercury dealer, who ceased to carry Mercury motors and began selling Outboard's motors exclusively. Amplex's business allegedly failed as a result of the loss of the

117. See *Simpson v. Union Oil Co. of Calif.*, 377 U.S. 13 (1964).

118. 389 U.S. 805 (1968). See pt. III, § A *supra*.

119. See discussion in pt. III, § A *supra*.

120. See *Kay Instruments Sales Co. v. Haldex*, 3 TRADE REG. REP. (1968 Trade Cas.) ¶ 72,488 (S.D.N.Y. 1968)

121. 380 F.2d 112 (4th Cir. 1967).

122. 389 U.S. 1036 (1968).

franchise and Amplex sued for treble damages. The trial court and the Court of Appeals for the Fourth Circuit rejected Amplex's claims, holding that Outboard was legally entitled to take unilateral steps to enforce its exclusive dealing policy.¹²³

The *Amplex* case has significance principally because of the arguments made in the Justice Department's memorandum in support of the dealer's petition for certiorari. It was argued that Outboard was coercing adherence to exclusive dealing arrangements by terminating and threatening to terminate dealers who did not deal exclusively in its products. The Justice Department urged the Supreme Court to rule that a refusal to deal gave rise to treble damage liability when such refusal was "used to secure, or in an attempt to secure, agreement to a proposal, which, if acceded to, would (1) comprise one of a set of contracts in unreasonable restraint of trade, or (2) constitute one of a number of sales agreements made on condition or understanding of unlawful exclusive dealing."¹²⁴ The Supreme Court denied certiorari. For the moment then, unilateral refusals to deal may be employed to secure adherence to exclusive dealing arrangements. However, this conclusion is tentative, and radiations from *Albrecht* and *Schwinn* may call for re-evaluation of *Amplex* and similar cases.¹²⁵

Adoption of the rule proposed by the Justice Department in its *Amplex* amicus brief would undermine the integrity of the network of contracts and agreements which characterize most franchise and distribution systems. There are, for example, a great many cases which deal with situations where for good business purposes, including the increase of efficiency of a manufacturer's or a franchisor's operations, certain suppliers or dealers are eliminated or one is substituted for another. The *Crawford Transport* case¹²⁶ represents a situation where one supplier among many was eliminated by a franchisor in the course of a program designed to improve the overall effi-

123. *Accord*, *Timken Roller Bearing v. FTC*, 299 F.2d 839 (6th Cir. 1962), *cert. denied*, 371 U.S. 861 (1962).

124. Memorandum for the United States as Amicus Curiae in Support of the Petition for Writ of Certiorari, *Amplex of Maryland v. Outboard Marine Corp.*, No. 668, *cert. denied*, 389 U.S. 1036 (1968).

125. *See also* *Lessig v. Tidewater Oil Co.*, 327 F.2d 459 (9th Cir. 1964), *cert. denied*, 377 U.S. 993 (1963), a treble damage case brought by a terminated service station dealer. The court held that Tidewater, on a showing of specific intent to fix prices charged by its dealers or to exclude other suppliers from selling to its dealers, could be guilty of an attempt to monopolize a "part" of commerce, the "part" being the business of Tidewater's 2,500 dealers. *But see* *Walker Process Equipment, Inc. v. Food Machinery & Chemical Corp.*, 382 U.S. 172 (1965).

126. *Crawford Transport Co. v. Chrysler Corp.*, 338 F.2d 934 (6th Cir. 1964), *cert. denied*, 380 U.S. 954 (1965).

ciency of its operations. In that case Chrysler reacted to a particular market condition or problem in a manner which required the termination of business relationships with many suppliers of transportation service. Apparently Chrysler made no attempt to determine whether a particular supplier such as the plaintiff or group of suppliers was the source of the difficulty which Chrysler wanted to eliminate; it simply terminated its dealings with all of the suppliers and subsequently reappointed a selected group of suppliers to carry on the service in question. In this situation it would not appear that Chrysler or any other manufacturer or franchisor is required to personalize its reaction to market problems. It is enough that the franchisor or manufacturer adopt a plan or policy which is conceived and implemented on a reasonable and nondiscriminatory basis to achieve the desired business purposes. Uniformity on a national basis is the goal and the fact that some suppliers, distributors, franchisees or licensees must look elsewhere for business should not be a barrier to implementation of the program.¹²⁷

There are other cases which simply involve the substitution of one distributor for another and the cases are legion that support the manufacturer or franchisor's unilateral right to make such substitution in the event of disloyalty or unsatisfactory performance by the dealer or franchisor.¹²⁸

Concerted refusals to deal are treated altogether differently. They are sometimes called group boycotts and the latter term adequately demonstrates the opprobrium associated with such activity. The per se illegality of concerted refusals to deal is not limited to cases where they are used to achieve price fixing; it applies to any kind of boycott for almost any purpose.¹²⁹ As the Supreme Court has recognized, however, this doctrine does

127. See *Dehydrating Process Co. v. A. O. Smith Corp.*, 292 F.2d. 653, 656-657 (1st Cir. 1961), *cert. denied*, 386 U.S. 931 (1962).

128. See, e.g., *Scanlan v. Anheuser-Busch*, 388 F.2d 918 (9th Cir.), *cert. denied*, 391 U.S. 916 (1968); *Ace Beer Dist., Inc. v. Kohn*, 318 F.2d 283 (6th Cir.), *cert. denied*, 375 U.S. 922 (1963); *Packard Mtr. Car Co. v. Webster Motor Car Co.*, 243 F.2d 418 (D.C. Cir.), *cert. denied*, 355 U.S. 822 (1957); *Peerless Dental Supply Co. v. Weber Dental Mfg. Co.*, F. Supp. 288 (E.D. Pa. 1968), finding no illegal combination under § 1 of the Sherman Act in manufacturer's substitution of one exclusive distributor for another, even if it was done at the instigation of the new exclusive distributor, in the absence of joint horizontal action or price fixing. Cf. *Metropolitan Dry Cleaning Machinery Co. v. Washex Machinery Corp.*, 5 TRADE REG. REP. (1969 Trade Cas.), ¶ 72,686 (E.D.N.Y. 1968), dealing with a conspiracy to "substitute" distributors.

129. *Fashion Originators' Guild v. FTC*, 312 U.S. 457, 467-468 (1941); *Associated Press v. United States*, 326 U.S. 1, 15-16, 18-19 (1945); *Klor's v. Broadway-Hale Stores*, 359 U.S. 207, 212-213 (1959); *Silver v. New York Stock Exchange*, 373 U.S. 341, 347-349 (1963).

not apply to a single trader refusing to deal with another or to a manufacturer's agreement to grant a dealer an exclusive distributorship.¹³⁰

Other means of securing territorial, customer and product exclusivity include agreements to pay royalties on sales outside a given territory or class of customer, sales quotas and minimum royalties, inventory and usage requirements.¹³¹ Each may present special problems related to the context in which it is employed. Moreover, even the most carefully devised arrangements may founder on the practical problems of supervising such arrangements. For example, there must be fair and mutually satisfactory procedures to verify sales outside the approved territory or class of customers before the appropriate royalty can be ascertained and required to be paid. As the cases discussed in this article show, the risks to the franchisor or manufacturer-seller of overreaching or unfairness can be great. The possibility of government proceedings and treble damage actions under section 4 of the Clayton Act¹³² require that special attention be given to the form of discipline which particular conduct receives.

Nor are the consequences under federal rules the only ones to be considered. State law must also be taken into account. Missouri courts, for example, follow the rule that where an exclusive sales or distribution contract is terminated before the agent or distributor has been able to recover his investment, he is entitled to receive an award of damages equal to that portion of his investment which he has not recouped at the time of the franchise termination.¹³³ The language of the Missouri Supreme Court in the *Bardahl* case is to the point:

We think the evidence was sufficient for the jury to infer and find that, after respondent had in compliance with the terms of his agreement necessarily expended work, labor and money to promote appellant's products and in establishing distributors for appellant's products, the appellant cancelled respondent's franchise, terminated the relationship and retained and appropriated the benefit of respondent's work, labor and expense in promoting the sale of appellant's products and establishing distributorships before respondent had had a reasonable time within which to recoup his expenses and receive a reasonable value for his work and services. Under such circumstances the law would imply an obligation on the part of ap-

130. *Klor's v. Broadway-Hale Stores*, note 127 *supra*.

131. Territorial and location restrictions are discussed in pt. III, § B *supra*.

132. 15 U.S.C.A. § 15 (1964).

133. *Superior Concrete Accessories v. Kemper*, 284 S.W.2d 482, 491-492 (Mo. 1955); *Gibbs v. Bardahl Oil Co.*, 331 S.W.2d 614, 621-622 (Mo. 1960).

pellant to pay the reasonable value thereof to the extent mentioned and respondent would be entitled to recover accordingly.¹³⁴

Moreover, the effect of some state anti-trust laws such as Missouri's is to make void and unenforceable any contract in violation of that law.¹³⁵ Thus, if the agreement is terminated or cancelled with the dealer or franchisee owing substantial sums to the manufacturer or franchisor, the latter may never be able to collect those sums. The rule in such states as to the voidability of contracts varies significantly from the federal rules which require an analysis of the contract and the alleged restraint to determine whether the restraint is collateral to the parties' agreement.¹³⁶ The Supreme Court has repeatedly refused to treat illegal contract defenses as an anti-trust enforcement tool. The Court has indicated its preference for direct action to enforce anti-trust laws and its reluctance to hand a "windfall" to a buyer who does not want to pay for goods he has received.¹³⁷ Of course, if a contract, in and of itself, inherently violates the anti-trust laws it may not be enforced. However, there must be an analysis of the contract to determine whether it is an integral part of an anti-trust conspiracy and therefore illegal, on the one hand, or whether the contract is merely collateral to an illegal combination or conspiracy and is therefore enforceable by either party.¹³⁸

Even though a dealer or franchisee is notified that his distribution arrangement is to be terminated, he may, under some circumstances, be able to prevent the cessation of sales by the manufacturer or franchisor to him.¹³⁹ In a recent case the distributor of a taxi meter sued to enjoin the termina-

134. *Gibbs v. Bardahl Oil Co.*, *supra* note 131, at 621-622.

135. § 416.040, RSMo 1959. *See* *Temperato v. Horstman*, 321 S.W.2d 657 (Mo. 1959). If, however, the contract in question constitutes "interstate commerce" it is not governed by Missouri law and the contract would be unenforceable. *See* *J. R. Watkins v. Holloway*, 168 S.W. 290, 292-294 (Spr. Mo. App. 1914), and *First Nat'l Bank v. Missouri Glass*, 152 S.W. 378, 381-382 (St. L. Mo. App. 1912).

136. *See, e.g.*, the cases cited in Mr. Justice Harlan's Memorandum granting a stay in *American Mfrs. Mut. Ins. Co. v. American Broadcasting-Paramount Theatres*, TRADE REG. REP. (1966 Trade Cas.) ¶ 71,850 (U.S. 1966), including *Kelly v. Kosuga*, 358 U.S. 516 (1959).

137. *See also* *American Manufacturer's Ins. Co. v. American Broadcasting Paramount*, 388 F.2d 272, 279 n. 9 (2d Cir. 1967).

138. *See* *Bruce's Juices v. American Can Co.*, 330 U.S. 743 (1947).

139. *See* *Beverage Distributors, v. Olympia Brewing Co.*, 5 TRADE REG. REP. (1968 Trade Cas.) ¶ 72,530 (N.D. Cal. 1967); ¶ 75,531 (9th Cir. 1968), temporarily restraining a brewer from refusing to sell beer to a wholesaler because the wholesaler had allegedly sold the brewer's product at less than other wholesaler's prices and had sold outside its designated territory. *Cf.* *House of Materials, Inc. v. Simplicity Pattern Co.*, 298 F.2d 867 (2d Cir. 1962); *Bergen Drug Co. v. Parke, Davis & Co.*, 307 F.2d 725 (3rd Cir. 1962).

tion of his distributorship agreement with a manufacturer and supplier of taxi meters.¹⁴⁰ He alleged that the only reason he was being terminated was because he refused to adhere to a resale price maintenance scheme which had been adopted by his supplier and one of the supplier's competitors. The court granted a temporary injunction, holding that irreparable injury to the plaintiff was apparent since he had been a distributor for over twenty years, had collaborated in developing the new taxi meter as to which the alleged resale price maintenance agreement was directed, and the plaintiff-distributor's organization might be raided by the replacement distributor.¹⁴¹

IV. CONCLUSION

Other means of securing adherence to a distribution plan have not been as widely employed or litigated as the threat of termination of the relationship.¹⁴² Indeed, one might speculate that termination or cancellation is the only means of securing the distribution discipline which is required for successful marketing. However, the right to terminate a dealer or franchisee, as in the case of the right to regulate his resale prices, customers, territories, suppliers, products and services, is currently feeling the effect of a major re-

140. *Kay Instrument Sales Co. v. Haldex*, 5 TRADE REG. REP. (1968 Trade Cas.) ¶ 72,488 (S.D.N.Y. 1968).

141. *See also Costen v. Pauline's Sportswear, Inc.*, 391 F.2d 81 (9th Cir. 1968), a suit for treble damages and injunction by a franchisee continuing to operate under franchise agreement.

In this context, the matter of the *in pari delicto* defense must be considered. That is, can the disenfranchised dealer be barred from suing for damages because he was a participant in what he now claims to be an illegal arrangement? The answer appears to be no, unless he did so voluntarily. *Compare Simpson v. Union Oil Co.*, 377 U.S. 13 (1964); *see Perma-Life Mufflers v. International Auto Parts*, 392 U.S. 134 (1968), and *Albrecht v. The Herald Co.*, 390 U.S. 145 (1968) (especially footnote 6), with *Premier Electric Construction Co. v. Miller Davis Co.*, 5 TRADE REG. REP. (1968 Trade Cas.) ¶ 72,710 (N.D. Ill. 1968) and *Temperato v. Horstman*, 321 S.W.2d 657 (Mo. 1959).

142. Frequently, provisions of a franchise or dealership agreement impose restrictions on the former franchisee or distributor once the franchise or distributorship agreement has been terminated. Such a non-competition provision, if limited in time, geographic area and product line, may be upheld on the grounds that it is reasonably ancillary to the principal agreement. *See, e.g., Prentice v. Williams*, 324 S.W.2d 466, 469-471 (Spr. Mo. App. 1959); *Prentice v. Rowe*, 324 S.W.2d 457, 461-463 (Spr. Mo. App. 1959); and cases discussed and cited note 113 *supra*. However, such a rule of reason approach to evaluation of post-termination competition restrictions may also be rejected outright by the courts and regulatory agencies. *Cf. Snap-On-Tools*, TRADE REG. REP. (1961 Trade Cas.) ¶ 15,546 (FTC 1961), holding that a limitation on post-termination competition by a former franchisee was unlawful, with *Carvel Corp.* [1965-67 Transfer Binder] TRADE REG. REP. § 17,298 (FTC 1965), upholding the validity of a limitation on post-termination competition by the former franchisee.

evaluation of the goals of anti-trust policy. The right of cancellation must be described, therefore, as a qualified right.¹⁴³ Indeed, more qualifications should be anticipated. The lawyer who advises in this area must not only be able to read the law as it is; he must also be something of a forecaster—in the sense of one who predicts atmospheric changes or great climatic disasters but who has only an imperfect understanding of the system which links them all and makes them comprehensible.

143. Rufus E. Wilson, the FTC's Chief of the Division of General Trade Restraints, alluded to the need for such a re-evaluation in a recent speech before the California-Nevada Soft Drink Association. *See* Wilson, "Antitrust Policy and Franchising," Feb. 11, 1969, pp. 10-13. Many of his remarks were addressed to problems which arise in the termination of franchisees. He said that the failure of the franchise movement to evolve a doctrine of fairness with respect to terminated franchises could lead to the adoption of a policy against restricting transfers by dealers and distributors. He specifically said that compulsory reversion to the franchisor of all rights in the franchise without adequate compensation to the franchisee could possibly be considered an unfair trade practice or method of competition under section 5 of the Federal Trade Commission Act. He also indicated that the termination of franchises could be attacked as unconscionable and thus illegal under Section 5 of the Federal Trade Commission Act.