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TRADE REGULATIONS: CUSTOMER AND TERRITORIAL RESTRICTIONS

A number of legal problems have arisen through manufacturers efforts to restrict competition within their distribution system by regulating the territories in which their distributors may sell, and the types of customers to whom they may sell. The purpose of this article is to analyze the present status of customer and protected territory distribution restrictions and to inquire into the future of these regulations.

A discussion on customer and territorial restrictions must commence with the case of *White Motor Co. v. United States*.[1] White Motor Company manufactured and sold trucks directly to dealers. White's agreement with its distributors included a clause whereby the dealers agreed to sell only within a certain defined territory, and also agreed not to sell any trucks to individuals, firms, or corporations which did not have a place of business and/or a purchasing headquarters in the territory. In addition, the dealers were prohibited from selling the trucks to any federal or state government, or any department or political subdivision thereof, unless the right to do so was specifically granted by White Motor Company in writing. The district court granted summary judgment for the Government, holding that both the territorial restrictions and the customer restrictions were *per se* illegal.[2] However, the United States Supreme Court reversed and remanded the case to the district court for trial. The Government had argued before the Supreme Court that a vertical arrangement by a manufacturer which restricted the territory of his dealer was akin to a horizontal arrangement among competitors to divide territories. In answer to this the Court said:

> We are asked to extend the holding in *Timken Roller Bearing Co. v. United States,* 341 U.S. 593, 95 L. Ed. 1199, 79 S. Ct. 971, *supra* (which banned *horizontal* arrangement among competitors to divide territory), to a *vertical* arrangement by one manufacturer restricting the territory of his distributors or dealers. We intimate no view one way or the other on the legality of such an arrangement, for we believe that the applicable rule of law should be designed after a trial.[3]

The Court further stated:

> This is the first case involving a territorial restriction in a *vertical* arrangement; and we know too little of the actual impact both of that restriction and the one respecting customers to reach a conclusion on the bare bones of the documentary evidence before us.[4]

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[1] White Motor Co. v. United States, 372 U.S. 253 (1963).
[2] White Motor Co. v. United States, 194 F. Supp. 562 (N.D. Ohio 1961).
[3] White Motor Co. v. United States, *supra* note 1, at 261.
[4] *Ibid.*

Thus, the *White Motor* case falls far short of laying down any definitive rules concerning customer or territorial restraints. The Court intimated no view as to whether these restrictions are *per se* illegal or whether they are to be governed by the rule of reason. In actuality, all the Court decided was that they did not want to decide this issue on an appeal from a summary judgment.

Only one case has reached the courts since the Supreme Court decided the *White* case. In *Snap-On Tools Corporation v. Federal Trade Commission,*[5] the complaint brought against this manufacturer of hand tools and related equipment charged the company with unfair acts and practices and unfair methods of competition in violation of section 5 of the Federal Trade Commission Act[6] on the ground that Snap-On Tool dealership contracts limited and suppressed competition by fixing resale prices, geographically restricting markets, limiting customers, and restricting dealer's right to compete after ceasing to be dealers.[7] The hearing examiner dismissed the complaint for failure to establish a prima facie case. On appeal the Commission reversed the examiner and issued an order requiring the petitioner to cease and desist from engaging in each of the challenged practices.[8] The Commission did not strike down each of these practices individually, but rather ruled that they were illegal because they formed a part of a general plan or scheme which was unlawful. On appeal, the Commission's ruling was reversed, and the examiner's decision reinstated.[9] In holding that Snap-On Tools did not violate the anti-trust laws, the circuit court refused to treat the violations as part of a general scheme, but considered each violation separately. Although the court upheld both the territorial and customer restrictions, these restrictions factually differed from those in the *White Motor* case. Under the territorial restrictions, the dealers were allowed to sell only in certain specified territories. However, as was pointed out by the court, the dealers were free even under this provision to sell to any customer, regardless of the customer's permanent location, who wished to come to the dealer's assigned territory. These territorial restrictions were upheld on the basis that they were prompted by reasonable business expectations and were beneficial both to the manufacturer and the public because of their promotion of interbrand competition.

[5] Snap-On Tools Corporation v. Federal Trade Commission, 321 F. 2d 825 (7th Cir. 1963). See also In Sandura Co., FTC Docket No. 7042, 3 CCH Trade Reg. Rep. ¶16,095 (1962).

[6] 38 Stat. 719 (1914), 15 U.S.C. 45 (1958).

[7] The fact that Snap-On Tools Company was prosecuted under §5 of the Federal Trade Commission Act, while White Motors was prosecuted under §1 and §3 of the Sherman Act creates no important difference. The courts have generally given a broader interpretation to the Federal Trade Commission Act, holding that many violations of the Sherman Act are also violations of the Federal Trade Commission Act.

[8] Snap-On Tools Corp., FTC Docket No. 7116, 3 CCH Trade Reg. Rep. ¶15,546 (1961).

[9] Snap-On Tools Corporation v. Federal Trade Commission, *supra* note 5.

The court felt this justified the minimum curtailment of intrabrand competition. The customer restrictions also differed from *White* in that there were only a few occasional oral understandings between a branch manager and dealer that large industrial accounts would be reserved for the company's salesmen. The court felt that at most this was a *de minimus* restrain on competition; in actuality the accounts were too large or complex for a normally trained dealer with his limited inventory to handle properly. Thus, in the first case decided by the courts since the *White Motor* case, the court refused to adopt a rule of *per se* illegality, and felt that in applying the rule of reason, the restraints were not unreasonable.

TERRITORIAL RESTRICTIONS

The circuit court in the *Snap-On Tools* case used language which implied that the United States Supreme Court had held in the *White* case that territorial restricts were not *per se* illegal. Eventually, these territorial restrictions may be declared not to be *per se* illegal and instead subject to the rule of reason. But, such a conclusion cannot be reached on the basis of the Supreme Court's decision in *White,* since the Supreme Court merely postponed its decision on the legality of territorial restrictions until a trial could be had on the issues.

Thus, since there is still a possibility that these clauses may be declared illegal *per se,* the question of what makes a restraint of trade *per se* illegal is important. The Supreme Court has stated that the restraints which fall into the class of *per se* illegality are made up of:

> Agreements or practices which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable and, therefore, illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use.[10]

Among the practices which the Court has deemed to be unlawful in and of themselves are: price fixing, both vertical (*United States v. Parke, Davis & Co*)[11] and horizontal *(United States v. Socony-Vacuum Oil Co. Inc.),*[12] division of markets among competitors *(Timken Roller Bearing Co. v. United States),*[13] group boycotts *(Fashion Originators Guild of America, Inc. v. Federal Trade Commission),*[14] and tying arrangements *(International Salt Co. Inc. v. United States).*[15] It seems

[10] Northern Pacific Railway Co. v. United States, 356 U.S. 1, 5 (1958).
[11] United States v. Parke, Davis & Co., 362 U.S. 29 (1960).
[12] United States v. Socony-Vacuum Oil Co., Inc., 310 U.S. 150 (1940).
[13] Timken Roller Bearing Co. v. United States, 341 U.S. 593 (1951).
[14] Fashion Originators' Guild of America, Inc. v. Federal Trade Commission, 312 U.S. 457 (1941).
[15] International Salt Co., Inc. v. United States, 332 U.S. 392 (1947). Even where the Court has created a rule of *per se* illegality, certain practices may not fall into that category. For example, in the area of tie-in sales, there is no illegality if the seller has no control over the tying product, since he really has no way to pressure the buyer into taking the tied product.

readily apparent that all of these practices have the pernicious effect of restraining competition, while being of no benefit to anyone other than the companies entering into such restraints. But can the same be said about territorial confinement clauses? It appears that to answer this question the Court must analyze three points: the manufacturer's purpose for entering into these restrictions; the effect of these restrictions on interbrand competition; and alternate arrangements between the suppliers and distributors which might satisfy the same business purposes as territorial confinement, and yet interfere less with competition.

Probably the main reason why manufacturers insert clauses restricting the territory in which a dealer may sell is that the manufacturer feels that such a restriction is necessary for the orderly marketing of his products, so that he may compete more effectively. A manufacturer is anxious for his distributor to devote his full time and effort to developing sales in his own territory; the assumption being that a dealer who raids the territory of another is not fully developing his own territory. Moreover, when a dealer's territory has been invaded by another dealer, he very likely will retaliate in the same manner and with the result of dealer competing against dealer. And since the product is the same, the only way one can compete against the other is to cut prices. More important, when the dealers are actively competing against each other, the overall effect may be to decrease interbrand competition.

A second reason why manufacturers claim they must restrict the territories in which their dealers may sell is that, by so doing, their dealers are assured a sufficient market. In certain industries where a dealer requires a very large initial investment, the dealer himself wants an added protection for this investment, or else he may not take the risk involved. Thus, merely to obtain a suitable dealership force, the manufacturer might be required to include territorial restrictions in all of his dealership agreements.

By assuring the dealer a sufficient market for his product through the use of territorial restrictions, the manufacturer is also in a better position to obtain certain concessions for which he is unable to contract by law. For example, by assuring a dealer a sufficient market, he may be discouraged from handling competing lines, though a manufacturer could not legally impose such a restriction on his dealer under section 3 of the Clayton Act.[16]

The main question which still remains unanswered is whether these business purposes should be allowed to overcome the effect of territorial restrictions, *i.e.*, a restraint on intrabrand competition. No one can say how the Supreme Court will ultimately decide this issue, but it is this writer's opinion that if the choice is merely between an orderly marketing of goods without intrabrand competition or disorderly competition,

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[16] Clayton Anti-Trust Act §3, 38 Stat. 731 (1914), 15 U.S.C. 14 (1958).

the latter should prevail. But, if it can be shown that though these restraints limit intrabrand competition, they are nonetheless necessary in order to have effective interbrand competition, territory restrictions should be upheld. The impetus to interbrand competition must be stressed by proponents of territorial restrictions to stay clear of the rule of *per se* illegality.[17]

The question of alternative arrangements which are less likely to violate the anti-trust laws is important in two respects. If the Supreme Court feels there are less restrictive alternative arrangements, they could use this as a basis for declaring territorial restrictions *per se* illegal on the ground that the device adopted should be no more restrictive than necessary to fulfill the purpose. And even if they are not declared *per se* illegal, the fact that there is an agreement which restricts competition makes such a clause subject to the rule of reason under sections 1 and 3 of the Sherman Act.[18]

The manufacturer's safest alternative would be to integrate into the distribution phase of his own business, *i.e.* to act as manufacturer, wholesaler and retailer. This should raise no anti-trust problems, unless the company would come within the monopoly restriction of section 2 of the Sherman Act.[19] However, numerous economic and legal difficulties are created in areas such as taxation, doing business requirements, increased supervision, etc. Additionally, this is such a large undertaking that most manufacturers could not afford this extreme.[20]

The manufacturer could set up agency agreements with the dealers, and then impose territorial restraints on the dealers.[21] Agency arrangements would probably remove the danger of the anti-trust laws, but they create new problems in and of themselves.

> To have valid territorial restrictions in an agency contract, care must be taken to have true agency relationship between the supplier and its distributor. Extremely important to the validity of the agency agreement is the retention in the supplier of title

[17] The Commission in the *Snap-On Tools* case stated that even if the exclusive territorial agreements were necessary for the orderly marketing of its products, the public is entitled to the benefit of competition on the dealer level. Some strength was given to this statement by Dr. Miles Medical Company v. John D. Park & Sons Company, 220 U.S. 373 (1911) where it was stated: "The complainant having sold its product at prices satisfactory to itself, the public is entitled to whatever advantage may be derived from competition in the subsequent traffic." The circuit court answered this by saying that the public was also entitled to keen competition among differing brands of products such as was sought to be promoted by Snap-On Tools.

[18] Sherman Anti-Trust Act §1 and §3, 26 Stat. 209 (1890), 15 U.S.C. 1, 3 (1958).

[19] Sherman Anti-Trust Act §2, 26 Stat. 209 (1890), 15 U.S.C. 2 (1958).

[20] It seems rather paradoxical to say that this is a safe alternative. The anti-trust laws were created to increase free competition, but when the manufacturer takes over the distribution of his own product, this result is stultified since there is a complete elimination of intra-brand competition.

[21] See United States v. General Electric Company, 272 U.S. 476 (1926) and Federal Trade Commission v. Curtis Publishing Company, 260 U.S. 568 (1923).

> to the product. In this respect, mere designation of title is not enough. The economic burdens of ownership must remain on the supplier. For example, payment by the supplier of casualty insurance premiums and property taxes on the goods; payment by the agent to the supplier for the goods only after sale to the ultimate consumer; the right of the distributor to return unsold goods; shipment by the supplier of goods sold by the agent directly to the purchaser; and the absence of competition between agent and principal all point toward a true agency relationship. On the other hand, failure to police agents properly; failure of the agent to account to the principal for its products; and payment by the agent for the product prior to delivery to the ultimate consumer may give an argument that no true agency agreement exists.
>
> Use of an agency method of distribution thus shifts substantial economic burdens from the distributor to the supplier. The entire cost of inventory maintenance and substantial accounting and policing costs are put on the supplier.
>
> In addition to economic burdens, the agency system of distribution shifts to the supplier certain legal burdens. Thus, the supplier may be liable in tort or contract to the ultimate consumer for the material misrepresentations of its agent-distributor concerning warranties or suitability of the product. Or, having avoided the Sherman Act limitations on territorial restrictions, the supplier may find that the use of agents in itself may create problems under the Robinson-Patman Act. If, for example, the supplier has given its agents some discretion as to price and if these agents should differ as to the price at which they sell to competing customers, the supplier may find that by virtue of establishing a unitary organization for purposes of being able to regulate intrabrand competition, he has by that very unity created customer price differentials in violation of the Robinson-Patman Act.[22] (Citations omitted.)

A manufacturer could also use an exclusive distributorship agreement alone, *i.e.*, not combining the exclusive distributorship with a territory restriction. This type of agreement appears to be valid, as long as the seller is not dominant in the market and the agreement is limited in terms of scope and duration.[23] This arrangement gives the dealer a certain measure of protection, and should result in a dealer giving more time and effort to developing his own territory.[24]

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[22] Stewart, *Exclusive Franchises and Territorial Confinement of Distributors*, 22 A.B.A. ANTITRUST SECTION 39, 40 (1963).

[23] See White Motor Co. v. United States, *supra* note 1, at note 11 to Justice Brennan's concurring opinion; Schwing Motor Co. v. Hudson Sales Corp., 138 F. Supp. 899 (D. Md.), *aff'd per curium*, 239 F. 2d 176 (4th Cir. 1956), *cert. denied*, 355 U.S. 823 (1957); Packard Motor Car Co. v. Webster Motor Co., 243 F. 2d 418 (D.C. Cir.), *cert. denied*, 355 U.S. 822 (1957); Robinson, *Restraints on Trade and the Orderly Marketing of Goods*, 45 CORNELL L. Q. 254, 255-261 (1960).

[24] If the manufacturer's article is a small, everyday household item, this seems to be an entirely satisfactory arrangement, since purchasers generally do not leave their community to buy such products. But if the item is a costly one

The restriction used in the *Snap-On Tools* case brings up an interesting question. In *White Motor Company,* the agreement not only prohibited a dealer from selling outside his territory, but also prohibited him from selling to anyone not having a place of business and/or a purchasing headquarters in his territory. However, the restriction in *Snap-On Tools,* although prohibiting the dealer from selling outside his territory, did not prohibit the dealer from selling to customers who came to him, even though they may have been located outside his territory. This type of provision is less restrictive than that used by White Motor Company since the dealer is allowed to sell to people living outside his territory. The question still remains, however, whether or not this makes the restriction valid since the dealer is still restrained from actively seeking sales in an area beyond his territorial limits.

After the justice department took its stand against the legality of territorial restrictions, many consent judgments were entered into by various companies which, though prohibiting a company from restricting a territory beyond which a distributor could sell, allowed the seller to designate a geographical area within which a distributor could agree to devote his best efforts, or to designate a geographical area in which a distributor would be primarily responsible for selling the company's products.[25] This "area of primary responsibility" doctrine allows the supplier to promise that he will appoint no one else in a particular territory, and to terminate the franchise agreement with any dealer who doesn't devote his best efforts in the area or adequately represent the supplier.

The legality of agreements based on this doctrine may eventually depend on the outcome of the *White* case, *i.e.* if territory distribution agreements are eventually struck down, the primary responsibility agreements could also fall. But, it is this writer's opinion that these agreements could be sustained on their own, because they temper the conflict

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such as a truck (or a number of trucks) the buyer is more likely to "shop around" in other territories.

[25] See United States v. Bastitch, Inc., TRADE REG. REP. (1958 Trade Cas.) ¶69, 207 (D.R.I. 1958); United States v. American Type Founders Co., TRADE REG. REP. (1958 Trade Cas.) ¶69,065 (D.N.J. 1958); United States v. Philco Corp., TRADE REG. REP. (1956 Trade Cas.) ¶68,409 (E.D. Pa. 1956); United States v. Rudolph Wurlitzer Co., TRADE REG. REP. (1958 Trade Cas.) ¶69,011 (W.D.N.Y. 1958).

The *Wurlitzer* consent judgment contains a typical primary responsibility provision:

> "Subject to the above subsections of this section IV, Wurlitzer may exercise its rights from time to time to choose and select its distributors and customers and to designate geographical areas within which a distributor may agree to devote his best efforts to the sale of coin-operated phonographs and may terminate the contract of any distributor who may fail to devote his best efforts to the sale in the area so designated of coin-operated phonographs manufactured by Wurlitzer or to represent Wurlitzer adequately in said area, and the designation of geographical areas for such specified purposes only shall not be considered a violation of this section IV."

between a manufacturer's business reasons for imposing territorial restrictions and the resultant decrease in intrabrand competition by allowing a dealer to compete beyond his assigned territory, but only if he has properly developed his own territory.

An interesting and fairly persuasive argument can also be advanced to uphold the "area of primary responsibility" doctrine on the basis of *United States v. Colgate & Company.*[26] In this case, the manufacturer sent lists of uniform prices to his dealers, and informed them that if they failed to adhere to the stated prices, no further sales would be made to them. In holding that this policy was not illegal the Court stated:

> The purpose of the Sherman Act is to prohibit monopolies, contracts and combinations which probably would unduly interfere with free exercise of their rights by those engaged, or who wish to engage, in trade and commerce—in a word to preserve the right of freedom to trade. In the absence of any purpose to create or maintain a monopoly, the act does not restrict the long recognized right of trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal. And, of course, he may announce in advance the circumstances under which he will refuse to sell.[27]

However, since the *Colgate* case was handed down, numerous decisions have narrowly limited its scope. See *Federal Trade Commission v. Beech-Nut Packing Company,*[28] *United States v. Bausch & Lomb Optical Co.,*[29] and the recent case of *United States v. Parke, Davis & Co.*[30]

In this latter case, the Court struck down the practice whereby a manufacturer announced the price at which his product was to be sold, told dealers that if they refused to abide by this price, he would no longer deal with them, induced wholesalers to stop selling to retailers who disregarded the stated price, and set up other methods of gathering information on those who did not abide by the stated practice. The Court acknowledged the existence of the *Colgate* doctrine, but confined its immunity to a mere announcement of the policy and a simple refusal to deal. The Court stated:

> Thus, whatever uncertainty previously existed as to the scope of the *Colgate* doctrine, *Bausch & Lomb* and *Beech-Nut* plainly fashioned its dimensions as meaning no more than that a simple refusal to sell to customers who will not resell at prices suggested by the seller is permissible under the Sherman Act. In other words, an unlawful combination is not just such as arises from a price maintenance *agreement,* express or implied; such a combination is also organized if the producer secures adherence

[26] United States v. Colgate & Company, 250 U.S. 300 (1919).
[27] *Id.* at 307.
[28] Federal Trade Commission v. Beech-Nut Packing Company, 257 U.S. 441 (1922).
[29] United States v. Bausch & Lomb Optical Co., 321 U.S. 707 (1944).
[30] United States v. Parke, Davis & Co., 362 U.S. 29 (1960).

> to his suggested prices by means which go beyond his mere declination to sell to a customer who will not observe his announced policy.[31]

The holding in this case caused Justice Harlan to state in his dissenting opinion: "I think that what the Court has really done here is to throw the *Colgate* doctrine into disgard."[32]

If there is any vitality remaining in the *Colgate* doctrine, a supplier may be able to validly state in advance that he will refuse to deal with his distributors unless they devote their best efforts to a certain area. As long as there is no conduct on the part of the manufacturer or distributor implying any agreement to restrict the latter's activities to the "area of primary responsibility," the manufacturer's unilateral refusal to deal should be protected.

However, it must be noted that there are two disadvantages in creating areas of primary responsibility. The first one encompasses the result which flows from a dealer selling beyond his territory when he has failed to properly develop his own territory. It is clear, both under the *Colgate* doctrine and under the consent decrees which the Government has allowed, that if a dealer invades the territory of others without properly developing his own, the only alternative for the manufacturer is to discontinue the franchise. If the manufacturer merely warns the dealer and gives him another chance, the manufacturer has then gone beyond a mere refusal to deal, and an agreement has arisen which may be violative of the Sherman Act.[33] The second disadvantage is that it tends to give a bonus to those dealers who can properly develop their own territory. If a dealer does properly develop his territory,

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[31] *Id.* at 43.

[32] United States v. Parke, Davis & Co., *supra* note 29, at 57 (dissenting opinion).

[33] *See* 60 MICH. L. REV. 1006, 1009 n. 14 (1962). The author makes the following suggestions to reduce the risk that distributor cooperation might evidence an agreement or conspiracy to allocate territories:

> "[T]he manufacturer should take the following precautions: (1) He should omit any reference to territorial restrictions as a condition of the continuance of the franchise. Any suggestion that distributors restrict their activities to a designated area should be contained in a clearly unilateral declaration of the manufacturer's general policy, but the distributor should be free to decide whether or not to acquiesce therein. In the Matter of Columbus Coated Fabrics Corp., 55 F.T.C. 1500 (1959). (2) He should refrain from soliciting any assurances from nonconforming distributors that they will adhere to the policy in the future, since such assurances may imply an agreement between the manufacturer and the distributor. United States v. Parke, Davis & Co., 362 U.S. 29, 46 (1960). (3) He should allow only his own employees and agents to investigate distributor activities, since any assistance by a distributor in determining whether any distributor is violating the manufacturer's policy is evidence of an implied agreement. United States v. Bausch & Lomb Co., 321 U.S. 707, 723 (1944); FTC v. Beech-Nut Co., 257 U.S. 441, 445-56 (1922.)"

The typical territorial restriction agreement avoids this problem by imposing the less drastic remedy of "profit pass over." Thus, if a dealer invades the territory of another he merely incurs an obligation to share the profit with the dealer whose territory has been invaded.

the manufacturer cannot complain if the dealer branches out into other territories. Naturally, this could tend to create dissension among those dealers who are being invaded. Notwithstanding these disadvantages, the "area of primary responsibility" doctrine can be a convenient and useful means of serving the legitimate business needs of a seller while evading the uncertainty of the legality of territorial restrictions. Moreover, the existence of this alternative could permit the Supreme Court to declare territorial restrictions illegal *per se.*

CUSTOMER RESTRICTIONS

In both the *White Motor* case and the *Snap-On Tools* case, restrictions were placed in the dealer agreements which precluded the dealers from selling to certain large accounts, mainly federal, state and municipal governments, unless permission was received from the manufacturer. The justice department has claimed for many years that this practice of restricting customers to whom a dealer can sell is also illegal *per se.*[34] There is no doubt that a manufacturer can reserve the right to sell to certain customers, but the main question which arises is whether he can go further and prohibit the dealer to sell to the customers. In *United States v. Bausch & Lomb Optical Co.,*[35] a price-fixing case, the Court used language which would prohibit a manufacturer from limiting the customers to whom a dealer may sell.

> A distributor of a trade-marked article may not lawfully limit by agreement, express or implied, the price at which or the persons to whom its purchaser may resell, except as the seller moves along the route which is marked by the Miller-Tydings Act.[36]

Though the language concerning the prohibition on restricting the customers to whom a dealer can sell was dictum in the case, the Government has used it for declaring these restrictions *per se* illegal. The manufacturer's major argument in favor of restricting dealer sales to large accounts such as federal and state governments is that since there are such large and lucrative accounts, the manufacturer cannot take a chance on the dealer servicing these accounts in an unsatisfactory manner. They claim these sales are so highly competitive, that to properly compete, the manufacturer must retain the right to make these sales himself. Nonetheless, it is this writer's feeling that these restrictions will ultimately be declared *per se* illegal. In a concurring opinion in the *White Motor* case, Justice Brennan stated:

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[34] See Letter of Lawrence E. Walsh, Deputy Attorney General, June 20, 1958, in *Automobile Distribution, Hearings Before the Senate Committee on Interstate and Foreign Commerce,* 85th Cong., 2d Sess. 65-66 (1958); Statement of Stanley N. Barnes, Assistant Attorney General in Charge of the Antitrust Division, *Automobile Marketing Legislation, Hearings Before a Subcommittee of the House Committee on Interstate and Foreign Commerce,* 84th Cong., 2d Sess. 359-365 (1956).

[35] United States v. Bausch & Lomb Optical Co., *supra* note 28.

[36] *Id.* at 721.

> The customer restraints would seem inherently the more dangerous of the two, for they serve to suppress all competition between manufacturer and distributors for the custom of the most desirable accounts. At the same time they seem to lack any of the countervailing tendencies to foster competition between brands which may accompany the territorial limitations. In short, there is far more difficulty in supposing that such customer restrictions can be justified.[37]

In Justice Brennan's opinion the only way this restraint could be upheld, is by showing that the dealers could not have effectively competed with the manufacturer anyway. Justice Brennan stated: "On trial, as I see it, the Government will necessarily prevail unless the proof warrants a finding that, even in the absence of the restrictions, the economics of trade are such that the distributors cannot compete for the reserved account."[38] The manufacturer is naturally in a much more favorable position to make the sales to these large accounts because the cost of the product is greater to the dealer. That this is not always the case, however, was seen in *United States v. Kearflax Linen Looms, Inc.*[39] In that case the manufacturer's dealer on two occasions underbid the manufacturer on sales to the Government. When the manufacturer forbade the dealer from bidding on these Government contracts, the district court held that the company violated section 2 of the Sherman Act[40] since the company had a complete monopoly on the particular product. This case clearly shows that there can be effective competition between a dealer and a manufacturer.

In addition to Justice Brennan's concurring opinion, three Justices speaking through Justice Clark dissented. In stating that the customer restrictions were *per se* illegal, Justice Clark declared:

> But the rule of reason is inapplicable to agreements made solely for the purpose of eliminating competition. . . . To admit, as does the petitioner, that competition is eliminated under its contract is, under our cases, to admit a violation of the Sherman Act. No justification, no matter how beneficial can save it from that interdiction.[41]

It is hard to see how these customer restrictions can be upheld. They prohibit all competition between the dealer and the manufacturer, and are not justified, as the territorial restraints might be, by the fact that they spur inter-competitive dealings. Even Justice Brennan's argument that these restrictions may be legal if the dealer could not in fact compete against the manufacturer seems to be without basis, since if a

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[37] White Motor Co. v. United States, *supra* note 1 at 272 (concurring opinion).
[38] *Id.* at 275.
[39] United States v. Klearflax Linen Looms, Inc., 63 F. Supp. 32 (D. Minn. 1945).
[40] 26 Stat. 209 (1890), 15 U.S.C. 2 (1958).
[41] White Motor Co. v. United States, *supra* note 1, at 281 (dissenting opinion).

dealer cannot effectively compete against the manufacturer, there is absolutely no reason for including such a restriction.[42]

This discussion of territorial restraints and customer limitations has been confined to their effect as individual restraints. However, a warning must be noted based on *United States v. Bausch & Lomb Optical Co.*

> We think that where a distribution system exists, prior to the making of such price maintenance contracts, which is illegal because of unallowable price fixing contracts and where that illegality necessarily persists in part because a portion of the resales are not covered by the "fair trade" contracts, as just explained, subsequent price maintenance contracts, otherwise valid, should be cancelled, along with the invalid arrangements, in order that the ground may be cleansed essentially from the vice of the former illegality. Equity has power to eradicate the evils of a condemned scheme by prohibition of the use of admittedly valid parts of an invalid whole.[43]

Thus, even though a certain restriction, for example, a territorial restriction, would ultimately be held legal by itself, it may be illegal when combined with other restraints. The Supreme Court in the *White Motor* case specifically recognized this rule by stating:

> In any price-fixing case restrictive practices ancilliary to the price-fixing scheme are also quite properly restrained. Such was *United States v. Bausch & Lomb Optical Co.*, 321 U.S. 707, where price-fixing was an integral part of the whole distribution system (id. 720) including customer restrictions. No such finding was made in this case; and whether or not the facts would permit one we do not stop to inquire.[44]

Since the *White Motor* case also involved price-fixing, it is possible that the case might eventually be decided on the basis of *Bausch & Lomb.* The *Snap-On Tools* case also involved price-fixing. But while the order of the Commission was not based on the illegality of the individual restraints, but rather on the basis that as a whole they must be outlawed, the circuit court refused to treat the restraints *in toto,* but considered each one individually.

CONCLUSION

It would be an understatement to say that the *White Motor* case has left much confusion concerning the legality of territorial and customer restrictions. The Supreme Court has still reserved for itself the right to declare either or both of these restrictions illegal *per se.* And it is noteworthy that three Justices out of the eight who heard the case (Justice White did not take part in the case) felt that both of these

[42] It is possible that the Supreme Court could hold customer restrictions *per se* illegal, but recognize an exception when the evidence discloses that the dealers could not in fact compete against the manufacturer. See note 15 *supra.*

[43] United States v. Bausch & Lomb Optical Co., *supra* note 28, at 724.

[44] White Motor Co. v. United States, *supra* note 1, at 260.

restrictions were *per se* illegal, while Justice Brennan in his concurring opinion intimated that customer restrictions had little justification and were probably *per se* illegal. Customer restrictions do not appear to have any major favorable aspects. About the strongest argument against their being declared *per se* illegal is that, generally, these restrictions do not have the effect of restraining competition because dealers cannot effectively compete with the manufacturers anyway. But even this point is hard, if not impossible to prove, and appears to have little merit.

The territorial restraints stand on a somewhat different footing though. The Court could have declared these illegal *per se* by equating vertical territorial restraints with other cases which have held that both vertical price-fixing and horizontal divisions of markets are *per se* illegal. But the Court refused to go that far. If it can be shown that the legitimate objectives of territorial security agreements outweigh the concomitant restriction on intrabrand competition, the territorial restraints might survive a test of *per se* illegality, although they would still be subject to the rule of reason. The key in either respect will be to show that the intrabrand competition, which was lost, was not as beneficial as the vigorous interbrand competition which resulted from the distribution policy. However, until a final decision is rendered on this subject, companies wishing to initiate territorial restraints would be in a far safer position if they chose alternatives, such as, exclusive distributorships or the assignment of areas of primary responsibility.

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