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Trademarks in Tying and Exclusive Dealing Agreements: The opinion of the Federal Trade Commission in *Carvel Corporation*\(^1\) raises two issues for consideration in this article: a) whether a trademark can be a tying product, and b) whether all exclusive dealing agreements shall be subject to the qualitative analysis test.

The action was brought against *Carvel* under Section 5 ("unfair methods of competition") of the Federal Trade Commission Act\(^2\) and necessarily concerns principles and decisions resulting from applications of Section 1 ("restraint of trade") of the Sherman Act\(^3\) and Section 3 ("to substantially lessen competition") of the Clayton Act.\(^4\) There is a large amount of interchangeability among these three sections, but general distinctions may be noted: a) the Clayton Act and the FTC Act were enacted to supplement the Sherman Act;\(^5\) b) the Sherman Act requires actual restraints of trade, while the Clayton Act and the FTC Act require only a reasonable probability thereof;\(^6\) c) the Clayton Act requires specific violations, while the Sherman Act and FTC Act are couched in general terms; d) exclusive arrangements are charged under the FTC Act only when the Clayton Act does not apply.\(^7\)

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3. "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal . . . ." 26 Stat. 209 (1890), as amended, 15 U.S.C. §1 (1964).
4. "It shall be unlawful for any person engaged in commerce, in the course of such commerce, to lease or make a sale or contract for sale of goods, wares, merchandise, machinery, supplies, or other commodities, whether patented or unpatented, for use, consumption, or resale within the United States or any Territory thereof or the District of Columbia or any insular possession or other place under the jurisdiction of the United States, or fix a price charged therefor, or discount from, or rebate upon, such price on the condition, agreement, or understanding that the lessee or purchaser thereof shall not use or deal in the goods, wares, merchandise, machinery, supplies, or other commodities of a competitor or competitors of the lessor or seller, where the effect of such lease, sale, or contract for sale or such condition, agreement, or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce." 38 Stat. 731 (1914), 15 U.S.C. §14 (1964).
However, it is the substance of the violation, rather than the act violated which is the more determinative factor in antitrust law. In the area of exclusive arrangements, which is the subject of this article, there are three basic types: the tying agreement, the exclusive dealing agreement, and the requirements agreement. The tying agreement is one whereby a vendee or lessee is required, as a condition to the sale or lease of a desired product (the "tying product"), to purchase or lease some other product (the "tied product") of the seller or lessor. The vendee or lessee is forced to take one or more other products to get the tying product. An exclusive dealing agreement is one whereby the vendee or lessee is required, as a condition to the sale or lease of a product, not to use or deal in the product of a competitor. A requirements agreement is one whereby a vendee or lessee is required, as a condition to the sale or lease of a product, to buy or lease all or part of his subsequent needs of that product from that seller or lessor. As can be seen, an agreement requiring a vendee to purchase all of his subsequent needs of a product from a particular seller is, in all practical effects, the same as an exclusive dealing agreement.

In 1962, at the commencement of suit, the Carvel Corporation had approximately 340 franchised dealers located in eight states, including Wisconsin. The vast majority of these were located within a one-hundred mile radius of New York City. In 1959, Carvel's sales in a five state eastern area totalled $5 million, of which seventy per cent was accounted for in New York State. For purposes of this opinion, the New York area was used as a test market. In this area, Carvel had 37.7 per cent of the soft ice cream market and 4.5 per cent of the combination soft and hard ice cream market.

Carvel was charged with violating Section 5 of the FTC Act because of conditions in its agreements with its franchisees. These conditions were alleged to be illegal insofar as they required each dealer: 1) to purchase his entire supply of ice cream mix and associated products from Carvel or from sources designated by Carvel, 2) to refrain from selling any products not authorized by Carvel, 3) to purchase various items of equipment from Carvel, 4) to adhere to these contract provisions under the eye of a rigorous policing system involving threats and coercion directed at dealers and non-approved suppliers, and 5) to refrain from entering into a similar business within three years after termination of the franchise period.

This article will center on the first charge.

9 See 1 TRADE REG. REP. ¶¶2910, 2920, 2930 (1965).
10 The theory of injury in the complaint was the foreclosure of the Carvel dealer market to the dairies which were not selected by Carvel. Although Carvel operates in interstate commerce, the markets in which the various dairies effectively compete is local.
11 The other four charges were given scant space in the opinion. All were ruled in favor of Carvel.
I. THE TRADEMARK AS A TYING PRODUCT

The FTC examiner found the Carvel franchise agreements to be tying agreements. As a condition to the leasing of the Carvel trademark (the tying product), the franchisees were required to purchase ice cream mix, equipment, and commissary items (the tied products) from Carvel or from sources designated by Carvel. The mix was to be bought from authorized dairies in the dealers' area, which produced the mix under contract with Carvel and in accordance with specifications furnished them by Carvel and at prices set by Carvel. The examiner found these agreements to be illegal under the *Northern Pacific* test, because Carvel had sufficient economic power with respect to the tying product to appreciably restrain free competition in the market for the tied product and a "not insubstantial amount" of interstate commerce was affected.\(^2\)

However, the Commission, in reviewing these findings, held that a trademark\(^3\) could not be a tying product, as it cannot be viewed separately from its product.\(^4\) The name "Carvel" and the subject Carvel ice cream cannot be viewed as distinct. Actually, though the opinion does not cite the case, this is a reversion to the old *Macmahon* doctrine that a trademark is not by itself such property as can be transferred, and the right to use it cannot be assigned except as incidental to the transfer of the business or property with which it has been used.\(^5\) Thus, reasoned the Commission, it would be conceptually impossible for a trade-

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\(^2\) As defined by the Lanham Act, the term "trademark" includes any "word, name, symbol, or device or any combination thereof adopted and used by a manufacturer or merchant to identify his goods and distinguish them from those manufactured or sold by others." 00 Stat. 443 (1946), 15 U.S.C. §1127 (1964).

\(^3\) *Carvel Corporation*, 3 TRADE REG. REP. ¶17298 at 22430-431 (1965).

mark to be a tying product, because a tying agreement must necessarily concern two separate and distinct products.¹⁶

Twenty years ago this position would have been valid, as prior to the Lanham Act¹⁷ a trademark was used to indicate the source or origin of the goods to which it was affixed. By this theory, the owner of a trademark could license it to another to use only if the licensor actively participated (e.g., by supplying some essential ingredient) in the production of the goods. If he did not, and disassociated himself from the production of whatever goods the licensee was putting out under his trademark, he would be held to have abandoned that trademark, since it no longer would indicate a uniform source and/or origin. As the case of United Drug v. Rectanus Co.,¹⁸ one of those cited by the FTC as authority for its holding, explained the trademark, "its function is simply to designate the goods as the product of a particular trader and to protect his good will against the sale of another's product as his; and it is not the subject of property except in connection with an existing business."¹⁹

However, today and ever since the Lanham Act, trademark licensing is based no longer upon the source theory but on a "guaranty" theory. A trademark now signifies only the quality of the goods. When the consumer purchases goods under a certain mark, that mark tells him not where the goods originated, but that they have been produced under uniform standards of quality, as were the goods, past and present, sold under that name. The licensor is released from any duty to actively participate in the production or preparation of the goods, being required only to control the quality of the goods produced under his trademark.²⁰ As a 1963 Yale Law Journal article summed it up:

Under the older view that trademarks indicated the source of goods, permissible licensing occurred only where the licensor so actively participated in the preparation of the final product through the supply of an essential ingredient or service that customer attribution of origin to the licensor was reasonably accurate. Thus, permissible trademark licensing was generally limited to such arrangements as manufacturer—further processor relationships where some major part of the finished product

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¹⁸ 248 U.S. 90 (1918).
¹⁹ Id. at 97.
²⁰ "Where a registered mark or a mark sought to be registered is or may be used legitimately by related companies, such use shall inure to the benefit of the registrant or applicant for registration, and such use shall not affect the validity of such mark or of its registration, provided such mark is not used in such manner as to deceive the public." 60 Stat. 429 (1946), 15 U.S.C. §1055 (1964). The term "related company" is defined 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." 60 Stat. 443 (1946), 15 U.S.C. §1127 (1964).
was supplied by the licensor. The guaranty theory removed this burden of active participation, substituting for it the lesser obligation of licensor control over the quality of goods emanating from different sources.\textsuperscript{21}

In \textit{Dazn Donut Co. v. Hart's Food Stores, Inc.},\textsuperscript{22} the court observed that, prior to the Lanham Act, trademarks could be transferred only in connection with goods. However, since the Lanham Act, "controlled licensing does not work an abandonment of the licensor's registration, while a system of naked licensing [i.e., without any control] does."\textsuperscript{23} Likewise, the case of \textit{Alligator Co. v. Robert Bruce, Inc.}\textsuperscript{24} held that the licensor does not have to participate in the final product in any other way than to control its quality. The above article noted that these two cases,

with their reading of the Lanham Act to extend the scope of permissible licensing beyond the strictness of the source theory, recognize the irrelevance of actual source . . . [and, the author concludes] the assurance of uniform quality may be the only safeguard from confusion and deception the consumer can expect.\textsuperscript{25}

It seems the majority viewpoint would be that a trademark is separable from that to which it is affixed. A case particularly in point is the 1964 case of \textit{Susser v. Carvel Corp.},\textsuperscript{26} a private suit by a dealer against Carvel on grounds almost identical to those of the FTC in this opinion. There it was said that "it seems clear in compelling circumstances the protection of good will, as embodied for example in a valuable trademark, may justify an otherwise invalid tying agreement."\textsuperscript{27} Also,

The true tying item was rather the Carvel trade-mark . . . . There may, of course, be cases where a trade-mark has acquired such prominence that the coupling of some further item to its license would constitute a \textit{per se} violation; but such a trademark would satisfy the market dominance test of \textit{Times-Picayune} and \textit{Northern Pacific}. The figures show that Carvel is not such a mark.\textsuperscript{28}

A trademark also has been viewed in the role of the tied product.\textsuperscript{29}

Of the three cases the Commission cited for authority in \textit{Carvel}, two were pre-Lanham\textsuperscript{30} and the third was a 1962 case from the fifth

\textsuperscript{21} Note, 72 Yale L.J. 1171 (1963). One of the earliest cases supporting this line of reasoning is E. I. Du Pont de Nemours & Co. v. Celanese Corp., 167 F. 2d 484, 489-90 (C.C.P.A. 1948).

\textsuperscript{22} 267 F. 2d 358 (2d Cir. 1959).

\textsuperscript{23} Id. at 367.


\textsuperscript{25} Note, supra note 21 at 1188.

\textsuperscript{26} 332 F. 2d 505 (2d Cir. 1964).

\textsuperscript{27} Id. at 512. See also Krayer, \textit{Domestic Trademark Licensing}, 43 J. Pat. Off. Soc'y 574, 585 (1961).

\textsuperscript{28} 332 F. 2d at 519.

\textsuperscript{29} Switzer Bros., Inc. v. Locklin, 297 F. 2d 39, 44 (7th Cir. 1961).

\textsuperscript{30} Trademark Cases, 100 U.S. 82 (1879); United Drug Co. v. Rectanus Co., 248...
circuit. The Commission referred to the court's statement in the latter case that "a trademark cannot travel to places where there is no article to bear it and no trader to supply the article." This is true, but it does not say that the licensor must supply the article. The statement of the court was in part answer to a licensee's objection to a provision of the license agreement, restricting him to an assigned sales area. The court approved of the territory limitation as a valid exercise of the licensor's duty to control his mark; for if there were no such restrictions, the mark could be said to exist everywhere. And yet, this is impossible, because it can exist only with an article or business (no matter by whom produced), and so could be held to be abandoned by the licensor.

Thus, conceptually, a trademark may be a tying product. Once the involved trademark agreement is held to be a tying agreement, it must be resolved whether it is substantial enough to be subject to the antitrust laws. In this area it has been said:

Tying agreements serve hardly any purpose beyond the suppression of competition. The justification most often advanced in their defense—the protection of the good will of the manufacturer of the tying device—fails in the usual situation because specification of the type and quality of the product to be used in connection with the tying device is protection enough.

However, in certain situations, even though technically violative of the antitrust laws, tying agreements are justifiable. In the case of Baker v. Simmons, it was held that:

business arrangements which conceptually could be styled 'tie-ins' might be excused from the reach of the antitrust laws if the arrangement was actuated by or could be explained on the basis of a legitimate business justification as opposed to an improper motive, e.g., desire to increase market control through the economic leverage supplied by the tying agreement.

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32 If the trademark is so widespread that the licensor cannot control its quality, it will either be held to have ceased to exist or will become public.
33 As later discussion will show, the Commission stated that even if it had held the agreement to be a tying agreement, Carvel lacked sufficient economic power to make the agreement subject to the antitrust laws.
35 307 F. 2d 458 (1st Cir. 1962).
In trademark situations, a plausible business justification is that under the Lanham Act a lessor necessarily must control the quality of the goods produced under his mark, else he will be held to have abandoned his mark. And, the lessor may argue, the tying agreement is the only sufficient means to meet that requirement of quality control. So the question is whether Carvel could have fulfilled its duty to control the quality of the ice cream by simply supplying its dealers with specifications and standards for the ice cream mix. If such means would not be sufficient the tying agreement would have been necessary and, thus, legitimate in fulfilling Carvel's duty of quality control.

The Commission discussed this point of justification in a slightly different context. Having held there could be no agreement, the Commission held that trademark agreements are still subject to the anti-trust laws. The test of the restrictions within the agreement is whether their main purpose is lawful and whether it can be said that any resulting restraint of trade is merely ancillary to this lawful purpose. The Commission found the lawful purpose to be Carvel's duty to control quality and that the tying agreement was its only way of maintaining such control. This same argument made to justify the trademark agreement is applicable to justify the trademark tying agreement.

The Commission argued that by the Lanham Act a lessor must control the quality of his lessee's dealings under his trademark to insure that they will apply the mark to either the same product or to one of substantially the same quality with which the public in the past has associated the product. If he does not retain such control, he will be held to have abandoned such trademark. Ordinarily, such control can be maintained by supplying the dealers with specifications; however, the Commission held that this is not true with a product as distinctive as food. The opinion cites the holding of Susser v. Carvel:

Such cases [i.e., those holding specifications are possible for manufacturing mechanical products] are scarcely relevant to

641 (7th Cir. 1935). It seems that even tying agreements involving patents (and thus copyrights also) can be justified. That a patent is only prima facie proof of monopoly over the tying product, see Standard Oil v. United States, 337 U.S. 293, 307 (1949); Northern Pac. Ry. v. United States, 356 U.S. 1, 10 n.8 (1958). But cf. United States v. Loew's, Inc., 371 U.S. 38, 45-46 (1962); But see Susser v. Carvel Corp., supra, at 520-21. Not only is there the danger of the licensor losing his trademark, but there is the onus of possible tort liability. RESTATEMENT (SECOND), TORTS §§402A-402B (1965).

37 It is uncertain, at this point, whether the Commission is viewing the agreement simply as a trademark agreement; as a semi-tying agreement like that in Atlantic Ref. Co. v. F.T.C., 381 U.S. 357, 369-70 (1965); or, as the agreement is later held to be, an exclusive dealing agreement, Carvel Corp., 3 TRADE REG. REP. ¶17298 at 22430 (1965).

38 See p. and note 20 supra.
the problem of controlling something so insusceptible of precise verbalization as the desired texture and taste of an ice cream cone or sundae; that Carvel was able to specify this to its source of supply, whose product it regularly checked, does not show that administration could be confided to 400 dealers.\textsuperscript{42}

If each Carvel dealer could purchase from whom he pleased, the Commission reasoned that Carvel would not be able to meet its obligation of quality control, as the inspection burdens would be too great. However, this line of reasoning could be made by any trademark licensor having substantial size. That inspection problems might be burdensome would seem to stem from the fact of its size rather than its system of quality control. The Commission's second argument is more cogent. It was contended that the public has come to expect more from Carvel than just quality. It has come to expect the distinctive taste of a Carvel ice cream cone. To insure Carvel's good will and avoid consumer deception,\textsuperscript{43} the restrictions on the purchase of the mix were held to be necessary for uniformity control; else the taste of a Carvel cone, no matter what its quality, could vary from state to state. The Commission concluded that the duty to control under trademark law is twofold—quality and uniformity.\textsuperscript{44} With a product as "imprecise" as food, while quality might be achievable by specifications, uniformity would not be.

In its final analysis of the point, the Commission ruled that Carvel, by its restrictions, had a primary and reasonable purpose of protecting

\textsuperscript{42} 332 F. 2d 505, 520 (2d Cir. 1964). Also, the fact that Carvel had a secret process for its mix is probably relevant. Dr. Miles Medical Co. v. Park & Sons Co., 220 U.S. 373, 402 (1911).

\textsuperscript{43} On the duty to prevent consumer deception, see Baker v. Simmons Co., 307 F. 2d 458, 469 (1st Cir. 1962): "In short, where the clear import of the sign program was to convey the message that a Beautyrest awaited the traveler inside, the Simmons Co. had ample justification in seeking to insure that the realization met this expectation. Simmons had a right, indeed a duty, to insure the truthfulness of its advertising and to exclude the possibility that a careless or capricious innkeeper might shortchange his guests with a different mattress."

\textsuperscript{44} The most difficult aspect of the opinion is the Commission's use of the principle of duty to control. The Commission uses it as part of its argument that a trademark cannot be a tying product: "[S]ince 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 trademarked product or its ingredient." Carvel Corp., 3 Trade Reg. Rep. 217298 at 22436 (1965). However, the Commission states, the trademark agreements are still subject to antitrust laws; and the restrictions within the agreements are illegal unless their primary purpose is to protect the trademark, any restraint of trade being ancillary. The duty to control is then used to validate the restrictions as having a primary purpose that is lawful.

It is the writer's position that a trademark can be a tying product and viewed as separate from the tied product to which the trademark is affixed. \textit{As the Commission states}, "There is no case which has held that a trademark licensor must itself manufacturer the trademarked products or their ingredients in order to retain control over the quality and uniformity of such products." Carvel Corp., supra, at 22437. Once established as a tying agreement, then the duty to control is used to justify it, if possible.
its mark and insuring the quality and uniformity of its product. Any restraint of trade (here, the foreclosure of non-authorized dairies in the area) was held to be merely ancillary to this valid purpose. Thus, Carvel was not liable under the general antitrust laws.\footnote{Carvel Corp., \textit{id.} at 22428.}

As noted earlier, this same line of reasoning, on quality and uniformity control, would have justified the trademark agreement even though it was a tying agreement. Therefore, whether it was a tying agreement or not made no practical difference in this case. However, this might not be true in other cases. When viewed as a tying agreement, a trademark agreement faces a more stringent test than when viewed as an exclusive dealing agreement. The necessary sufficient economic power is more easily found, and it should not have the benefit of the harder to prove market analysis test applicable to exclusive dealing agreements.\footnote{Northern Pac. Ry. v. United States, 356 U.S. 1, 5-8 (1958); Insto Gas Corp., 51 F.T.C. 363, 364 (1954).} As such, it is easier to prove illegal and harder to justify.

In the \textit{Carvel} fact situation it appears obvious that the commissary items were tied to the trademark. Had they been found to constitute a substantial amount of trade rather than "de minimis," this part of the franchisee's agreement also would have been subject to the antitrust laws. It is doubtful whether the argument of quality and uniformity control would have justified the dealers being forced to buy the nuts, toppings and like items from Carvel. Here, specifications and standards set by Carvel would have worked as well. It is submitted that the trademark tying agreement would have been found to be illegal.\footnote{This is so although the courts have been liberal in recent decisions concerning tying restrictions in trademark agreements. Note 72 \textit{YALE L. J.} 1171, 1173 (1963).}

After having decided the agreement was not violative of the antitrust laws, the Commission did deal with the agreement as a tying agreement. However, it did so only partially and, even then, in a hypothetical sense.

The Commission, probably with an eye toward further litigation, stated that even if the subject agreement were a tying agreement, neither the law nor the evidence in this case was sufficient to justify a finding of illegality.\footnote{Carvel Corp., 3 \textit{TRADE REG. REP.} ¶17298 at 22429 (1965).} The illegality of a tying agreement turns upon whether a party has sufficient economic power with respect to the tying product and "a not 'insubstantial amount' of interstate commerce is affected."\footnote{356 U.S. at 11.} The Commission ruled that, upon the record, the examiner was incorrect in finding that Carvel had met the first require-
ment of "sufficient economic power" or "dominance." A trademark, by itself, does not confer monopoly power on its owner, as is the case with a patent or copyright; nor, argues the Commission, was the fact that Carvel controlled 37.7 per cent of the soft ice cream market conclusive, in itself, of sufficient economic power.

The Commission was unable to conclude from the record that Carvel had the requisite power in the trademark and, thus, in the soft ice cream business to pressure dealers and prospective dealers into purchasing its tied products. The position was indicated that the business was not difficult to enter; the capital requirements were not extensive; and there were many competitors, both chain and independent, within the business. It is important to note that these statements are not posi-

50 "Dominance," as the term was used in the past, is no longer necessary for tying agreements to be violative of antitrust laws. As Northern Pacific, ibid, states, only "sufficient economic power" is needed. Such dominance, in the term of monoplistic position, was originally the test.

In construing a tying agreement under Section 3 of the Clayton Act, it was held that if a company with a "dominating position" had such restrictive and tying agreements, they must necessarily restrict competition. United Shoe Mach. Co. v. United States, 258 U.S. 451, 457-58 (1922). Then the swing was to emphasize being upon the amount of commerce affected. International Salt Co. v. United States, 322 U.S. 392, 396 (1947), held that "it is unreasonable, per se, to foreclose competitors from any substantial market." The test was one of pure quantum, here the salt company tied $500,000 worth of salt to its sales of salt depositing machines. Then Times-Picayune v. United States, 345 U.S. 594 (1953), purported to make either test applicable under the Clayton Act and a combination of the two applicable under the Sherman Act. The Court noted (345 U.S. at 608-09):

From the 'tying' cases a perceptible pattern of illegality emerges: When the seller enjoys a monopolistic position in the market for the 'tying' product, or if a substantial volume of commerce in the 'tied' product is restrained, a tying arrangement violates the narrower standards expressed in §3 of the Clayton Act because from either factor the requisite potential lessening of competition is inferred. And because for even a lawful monopolist it is 'unreasonable, per se, to foreclose competitors from any substantial market,' a tying agreement is banned by §1 of the Sherman Act whenever both conditions are met. In either case the arrangement transgresses §5 of the Federal Trade Commission Act, since minimally that section registers violations of the Clayton and Sherman Acts.

The decision (345 U.S. at 612) makes it clear that when dealing in terms of a substantial volume of commerce, more proof is needed than the mere showing of a percentage (Standard Oil) or a dollar volume (International Salt).

The last definitive case in this area has been Northern Pacific, which does away with dominance. Practically, if one can prove the second part of its test, i.e., a "not insubstantial amount," the first "sufficient economic power," would seem to follow as a matter of course, since the second could not be achieved without the first. See Turner, The Validity of Tying Arrangements under the Antitrust Laws, 72 HARV. L. REV. 50, 61-62 (1958); Lockhart and Sacks, The Relevance of Economic Factors in Determining whether Exclusive Arrangements Violate Section 3 of the Clayton Act, 65 HARV. L. REV. 913, 945 (1952).

51 Carvel Corp., 3 TRADE REG. REP. ¶17298 at 22429 (1965). It is the very essence of a patent or copyright that its subject is one of a kind and unique in itself. The courts have been reluctant to allow a licensor to extend his patent or copyright monopoly by its use in a tying agreement. United States v. Loew's Inc., 371 U.S. 38, 45-46 (1962). But that it may be justified in certain instances, see note 34 supra.
tive assertions. The Commission simply stated that there is nothing in the record to prove their contrary to be true.52

The Commission next extended its hypothetical of the tying agreement one step further. It stated that even if Carvel's share of the market were enough to establish the element of sufficient economic power; there was still a failure of proof as to a showing of a not "insubstantial amount" of commerce being affected. In this later sense the Commission held it to be irrelevant whether the foreclosure of the market be viewed as 4.5 per cent of the hard and soft ice cream market or 37.7 per cent of the soft ice cream market.53 Before entering into this second point, the Commission dropped the hypothesis of the tying agreement.54

II. THE TRADEMARK AGREEMENT AS FORCING EXCLUSIVE DEALING

The Commission stated that the trademark agreement involved was actually an exclusive dealing agreement. As such, the Commission argued, the test of its effect on commerce must be judged according to the rigor of the market or qualitative test of Tampa Electric Co. v. Nashville Coal Co.55 In this manner the Commission entered into the qualitative (rule of reason, market analysis) versus quantitative (dollar volume or percentage) controversy in exclusive dealing agreement decisions and opinions.

The reasoning in exclusive dealing decisions begins much the same as with tying agreements. In Standard Fashion Co. v. Magrane Houston Co.,56 the Court stated that the dominance of the seller would be all that is necessary to make the agreement violative of the Clayton Act. This test was modified by the leading case of Standard Oil v. United States.57 Standard was the largest seller of gasoline in a seven-state Western area. It had exclusive dealing contracts with 5937 independent stations or sixteen per cent of the retail gasoline outlets in the Western area selling 6.7 per cent of the gasoline and over $8.2 million worth of other products.

Justice Frankfurter, writing for the majority, held that even though the seller could not be said to have a dominant position (only 6.7 per cent of the market), "Section 3 of the Clayton Act is satisfied by proof that competition has been foreclosed in a substantial share of the line of commerce affected." The test was stated in terms of a quantitative market share rather than a strict dollar volume test as used in International Salt58 and strictly rejected any rule of reason.

52 Carvel Corp., ibid.
53 Id. at 22430.
54 Ibid.
57 337 U.S. 293, 314 (1949).
test. One need not prove the probable effects in the market, if he can show a substantial share of commerce affected.

However, the Tampa case, without overruling the Standard case, applied the rule of reason to the exclusive dealing arrangement between the Tampa Electric Company and National Coal Company. The public utility company contracted to buy all of its coal needs for the next twenty years from the coal company. This contract would amount to about $128 million over the years. Though this projected amount of coal would exceed the entire amount of coal otherwise used in the peninsular area of Florida during the same period, the court held the relevant market to be that within which the coal supplier effectively competed. This broadened it to a seven state area, wherein the particular contract would account for only .77 per cent of the total sales. Rather than applying any quantitative tests, the court held:

To determine substantiality in a given case, it is necessary to weigh the probable effect of the contract on the relevant area of effective competition, taking into account the relative strength of the parties, the proportion of volume of commerce involved in relation to the total volume of commerce in the relevant market area, and the probable immediate and future effects which pre-emption of that share of the market might have on effective competition therein. It follows that a mere showing that the contract itself involves a substantial number of dollars is ordinarily of little consequence.

The Commission in Carvel adopted the Tampa test:

The theory of injury in complaint counsel's case is principally the foreclosure of Carvel's dealers as possible market outlets for other manufacturers of soft ice cream mix. Reliance is placed solely on the percentage share of soft ice cream mix consumed by Carvel dealers. However, the Carvel franchise agreement, which is in fact an exclusive distributorship agreement, should be evaluated in terms of the criteria set down in Tampa... for viewing exclusive dealing arrangements, and that the alleged foreclosure of mix suppliers from the Carvel market should be determined in a broader economic context in an effort to determine 'the probable immediate and future effects which pre-emption of that share of the market might have on effective competition therein.'

The rule of reason test, as stated in an early case, held that "the court must ordinarily consider the facts peculiar to the business to which the restraint is applied; its condition before and after the restraint was imposed; the nature of the restraint and its effect, actual or probable. The history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, the purpose or end sought to be obtained, are all relevant facts." Chicago Bd. of Trade v. United States, 246 U.S. 231, 238 (1918). As simply stated, "the relative effect of percentage command of a market varies with the setting in which that factor is placed." United States v. Columbia Steel Co., 334 U.S. 495, 528 (1948).

The Commission then stated that the record was silent as to the operations of these other dairies; as to what percentage of these dairies' sales was accounted for by the sale of soft ice cream mix; and as to whether or not the soft ice cream mix market being foreclosed, the dairies could switch to other markets.62

Thus the FTC opinion adopted the qualitative test for exclusive dealing agreements, which test obviously supplies a more difficult standard of proof than the quantitative test, which merely involves proving a dollar volume or a market percentage. The question has been asked,63 and it is not fully clear, which standard the FTC will apply from one opinion to the next.

*Maico Company, Inc.*, in 195364 reviewed an examiner's findings on an exclusive dealing contract under Section 3 of the Clayton Act. The examiner cited the *Standard* case and held there must have been a substantial lessening of competition, because the defendant was one of the largest companies in the hearing aid field. The examiner excluded all evidence of actual competitive effect. However, the Commission reversed and, in effect, rejected *Standard* insofar as it held one need only show the foreclosing of a substantial share of commerce under Section 3 of the Clayton Act. The Commission stated that while this might be a proper test for the courts, it was not so for the Commission, which Congress created "with the avowed purpose of lodging the administrative functions committed to it in 'a body specially competent to deal with them by reason of information, experience, and careful study of the business and economic conditions of the industry affected. . ."65 In effect, it held that the FTC, due to its inherent expertise, would extend the full-searching qualitative test to every exclusive dealing agreement.

But the *Dictograph Products, Inc. v. F.T.C.* case66 appeared, in 1954, to revert back to the quantitative rule. The defendant did $2 million worth of business a year (again, in the hearing aid field) and controlled 22.7 per cent of the market. Without more the court found the company's exclusive dealing agreements violative of Section 3 of the Clayton Act. The court cited *Standard* as authority. Purporting to definitively construe that section of the Clayton Act, the Court

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62 There are ten different instances in the opinion where the Commission either finds the record silent or lacking sufficient evidence to substantiate a certain point. *Ibid.*


66 217 F. 2d 821 (2d Cir. 1954). See Anchor Serum Co. v. F.T.C., 217 F. 2d 867, 872 (7th Cir. 1954).
stated, "It is hardly likely that the insertion of the qualifying phrase, 'where the effect . . . may be to substantially lessen competition or tend to create a monopoly' was intended to reinstate the same Sherman Act test [i.e., the rule of reason] which had, at that very time [i.e., the time when the Clayton Act was created] been determined to be inadequate." 67

Since the collision of these two theories, there has appeared, on the surface at least, to be confusion and vacillation among the FTC opinions themselves and between the FTC opinions and the court decisions. 68 No distinctions are made as to whether the action is brought under Section 3 of the Clayton Act or Section 5 of the FTC Act; the issue is as to whether the qualitative or quantitative standard should be used under either. 69 One can look to the FTC in 1961 and find two opinions holding the quantitative standard should be applied to exclusive dealing agreements, 70 another holding out for the qualitative standard, 71 and another indiscriminately citing both Tampa and Standard as authorities. 72

To see that there is confusion in the courts, one need look no further than Susser v. Carvel: 73

We need not comment on whether the appellants [Susser] could sustain their allegations under the doctrine enunciated in Standard Oil, for it seems indisputable that in Tampa Electric the Court deviated from the more rigorous and inflexible rule it had established in Standard Oil and erected criteria which demand close scrutiny of the economic ramifications of an exclusive dealing in order to determine the probable anti-competitive effects of such a device. 74 (Emphasis added.)

In another case, Curly's Dairy, Inc. v. Dairy Cooperative Association, 75 the court held that the Tampa case narrowed the rule in the Standard case to the particular facts therein, and that "the court in Tampa made it perfectly clear that neither comparative quantitative substantiality [i.e., the market share foreclosed] nor absolute quantitative substantiality [i.e., the dollar volume foreclosed] should be the controlling factor." 76

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67 217 F. 2d at 827.
73 332 F. 2d 505 (2d Cir. 1964).
74 Id. at 516.
76 Curly's Dairy, Inc. v. Dairy Cooperative Assn., supra note 75 at 484-85.
However, the author feels that, in looking closer at the decisions and opinions, the better view would be that neither Standard nor Tampa applies to all exclusive dealing agreements in exclusion of the other. There is no firm and set rule, and the courts and Commission exercise a certain amount of discretion in construing all the factors within a particular fact situation. Judicial and administrative bodies would make their position clearer if they would not adopt the rule pertinent to their situation by a shorthand reference to Standard or Tampa as being exclusive of any other interpretation.

In the Tampa case itself, the court did not claim that the qualitative test shall be the sole test for illegality of exclusive dealing agreements. The court held that “in practical application, even though a contract is found to be an exclusive-dealing arrangement, it does not violate the section unless the court believes it probable that performance of the contract will foreclose competition in a substantial share of the line of commerce affected.” (Emphasis added.) Also, “the line of commerce...involved must be determined, where it is in controversy, on the basis of facts peculiar to the case.”

The court stated that there was not enough in that fact situation to show the probability of a substantial lessening of competition. Despite the money volume involved ($128 million over twenty years), the court would require more proof before inferring the necessary lessening of competition, as the contract covered only .77 per cent of the market in which defendant and his competitors effectively competed. Tampa, in construing the Standard case, stated:

There the impact of the requirements contracts was studied in the setting of the large number of gasoline stations—8,937 or 16.7% of the retail outlets in the relevant market—and the large number of contracts, over 8,000, together with the great volume of products involved. This combination dictated a finding that ‘Standard’s use of the contracts [created] just such a potential clog on competition as it was the purpose of §3 to remove’ where, as there, the effective proportion of retail sales was substantial. (Emphasis added.)

The court in Tampa did not consider any of the factors in the case strong enough to spring the case from a qualitative to a quantitative type test. It stated, “there is here neither a seller with a dominant position in the market as in Standard Fashion... nor myriad outlets with substantial sales volume, coupled with an industry-wide practice of relying upon exclusive contracts, as in Standard Oil... nor a plainly restrictive tying agreement, as in International Salt,...”

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77 365 U.S. at 327.
78 Ibid.
79 365 U.S. at 328-29.
80 Id. at 334.
In *Brown Shoe v. United States*, the court reiterated, though certainly not as explicitly as it could have, that both *Standard* and *Tampa* apply to exclusive dealing agreements, and that a lack of size is one of the factors that will take an agreement from without the *standard* test and place it under the *Tampa* test.

The FTC used this same rationale in *Carvel*, for it is in cases of large dealers enforcing exclusive dealing agreements that the quantitative test is used. Timken Roller Bearing Company was the nation’s largest manufacturer of tapered roller bearings. The International Staple & Machine Company controlled one-third of the market. Luria Bros., Inc. was the nation’s largest broker of iron and steel scrap.

In the leading *Dictograph* case, the court reasoned:

> It seems clear that whatever utility the elaborate economic inquiry contended for by petitioner may still have under Section 3 of the Clayton Act when applied to organizations not doing a substantial share of the business or not yet firmly established in a particular line of commerce, it has no place in a case such as this where the condemned contracts are being employed by a corporation which does almost $2,000,000 worth of business each year, is one of the industry’s three leaders, all or some of whom use this restrictive device, and which alone controls by such means over one-fifth of the nation’s prime retail outlets for products of this kind.

In the 1962 case of *Mytinger & Casselberry, Inc. v. F.T.C.*, where the Commission relied on the *Standard* case and the Company argued for the *Tampa* rule, the court flatly stated that *Tampa*, where only .77 per cent of the market was affected, did not apply. The Mytinger Company controlled 61.52 per cent, 34.6 per cent and 8.6 per cent of three lines of commerce dealing in multi-vitamin supplements.

The FTC opinion in *Rural Gas Service, Inc.* is very relevant. The Company controlled only three per cent of the sales in its total market area and less than four per cent in a two-state test market area. The Commission noted that the United States Supreme Court in *Standard* went all the way down to a 6.7 per cent market foreclosure in applying the quantitative test, but gave no indication as to just how low it will go. However, in the *Rural Gas* opinion, the Commission said that it was “not able to infer competitive injury solely from the market shares foreclosed. Where foreclosure is so small, further evidence of competitive effect is required.” The Commission cited *Tampa* and ruled

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82. 58 F.T.C. 98 (1961).
84. TRADE REG. REP. (1963 Transfer Binder) ¶16299 (1963).
85. 217 F. 2d 821, 828 (2d Cir. 1954).
86. 301 F. 2d 534, 539 (1962).
88. Id. at 918.
that, due to the lack of evidence, there was no violation of Section 3 of the Clayton Act, and that the same lack of evidence ruled out any violation of Section 5 of the FTC Act.

One of the best clues to understanding the confusion in the qualitative-quantitative struggle is supplied by Justice Frankfurter in his dissenting opinion in the 1953 case of *F.T.C. v. Motion Picture Advertising*. It is to be most importantly recalled that Justice Frankfurter wrote the majority opinion in *Standard Oil*. In the *Motion Picture* case, he lists all the factors that mitigated against applying a qualitative rule to the situation in the *Standard* case—Standard was the largest seller of gasoline in the market; it controlled 16.7 per cent of the retail outlets in the area purchasing $57 million worth of gas; it was involved in a business that was significant to the public; there was an obvious discrepancy of bargaining power between it and its dealers; the supplier, not the dealers, wanted and pressured for the exclusive dealing agreements; it was the central business of those affected; and competitors were absolutely excluded from the share of the market foreclosed. It is also to be recalled that there were some 5937 dealers affected and that the practice of exclusive dealing agreements was industry wide.

In final analysis, therefore, it appears that there are some factors, as mentioned above, which will dictate use of the quantitative substantiality test rather than that of qualitative substantiality. Certainly, the most important factor is market share. It appears that in the *Carvel* case the FTC ignored the importance of market share when it stated that it made no difference whether Carvel controlled 37.7 per cent or 4.5 per cent. If the reasoning suggested above had been accepted by the Commission, the quantitative substantiality rule would have been followed and might have induced a different result if the agreement was treated as an exclusive dealing agreement.

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91 That discrepancy in bargaining power could grow to be a more heavily weighted element in the future, see the Supreme Court's recent use of it in *Atlantic Ref. Co. v. F.T.C.*, 381 U.S. 357, 368 (1965).

92 However, the Court will always use the rule of reason test for vertical territorial limitations, not being sufficiently familiar with such arrangements to use a quantitative standard. *White Motor Co. v. United States*, 372 U.S. 253, 263 (1963); *Snap-On Tools Corp. v. F.T.C.*, 321 F. 2d 825, 828 (7th Cir. 1963).

93 Practically, the finding of the "not insubstantial amount" of commerce affected facilitates the finding of the first element of sufficient economic power. See note 50 *supra*. However, that the sufficient economic power is less easily found than in tying products, see note 46 *supra* and accompanying text.