Exclusive Foreign Distributor Agreements—Are They Illegal?

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INTRODUCTION

A DISTRIBUTOR'S agreement, like any other contract between two or more parties, is of primary importance to the contracting parties only and rarely concerns third parties. The "exclusive" clause of a distributor agreement, however, can be of great interest to a competitor in the territory as well as to the Department of Justice or to the Federal Trade Commission.

There is a dichotomy in the antitrust statutes which is only rarely pointed out in the vast literature concerning them: certain of them are applicable to foreign trade agreements made between American exporters or manufacturers for export and foreign distributors; others are inapplicable to such agreements but apply to identical agreements made between American manufacturers and domestic distributors. The frequent use of exclusive distributor agreements in the domestic trade is demonstrated by the litigation involving Section 3 of the Clayton Act, which specifically proscribes such clauses where their effect "may be to substantially lessen competition or tend to create a monopoly in any line of commerce." Since the Clayton Act is inapplicable to contracts between American manufacturers and foreign distributors, only the general provisions of the Sherman Act are applicable to determine the legality of a foreign distributor's agreement. To date no attempt has been made to test the legality of such an agreement in the field of foreign trade. However, many exporters and manufacturers for export believe that the domestic doctrine may soon be transposed into the foreign field where exclusivity clauses are almost universally used. This article attempts a "first reflection" on the possibility of such a transposition.

Most manufacturers for export have one or perhaps two distributors in each country where their products are exported, and the territory covered by the agreement is often the entire country in which the distributor is located. The agreement with each distributor is substantially identical. The purpose of the exclusivity clause in the distribution agreement is not primarily to suppress competition but rather to insure to the American manufacturer, who may be thousands of miles distant, that the distributor will promote his interests in the assigned territory, and to protect the distributor by preventing the manufacturer from putting another distributor into the

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business of selling his goods in the same territory. The restriction is among distributors and its purpose does not embrace prices or otherwise affect consumers. Under an "exclusive dealers agreement" with a manufacturer, a merchant agrees to refrain from handling competing lines of goods in consideration for his being supplied with the former's products. Under an "exclusive representation agreement," on the other hand, the manufacturer, in consideration of his products being stocked or solicited by the merchant, agrees to refrain from selling his products to competing dealers in a designated territory.[1] The twofold agreement is usually set forth in words similar to the following:

> Manufacturer hereby appoints Distributor and Distributor hereby accepts appointment as exclusive reseller of the Products in the Territory with the right also to solicit orders for sale of the Products directly by Manufacturer to consumers and other resellers in the Territory. Manufacturer shall not appoint any one other than Distributor as its Distributor of the Products in the Territory and Distributor shall not sell or deal in commodities in the Territory which are competitive with the Products.

Occasionally the clause is not entered directly in the body of the contract but rather it is entered in the schedule of products attached to the contract. Often the relationship is nowhere expressed but is simply "understood" by the parties. However, only rarely is it not written into the distributor agreement itself.[2]

POSITION OF AMERICAN EXPORTERS ON EXCLUSIVE DISTRIBUTORSHIPS

Most American exporters believe that the agreements with their foreign distributors must be exclusive for several reasons. (1) To remove the exclusive representation clause assuring the foreign distributor that he is the sole representative in his country for the American manufacturer would, in large measure, destroy the stimulus a distributor has to promote a line of products. This is usually the distributor's strongest inducement to enter the distribution agreement. (2) A similar result may be accomplished by removing the exclusivity clause but granting the distributor, in addition to his commission, special discounts or rebates on all sales to his territory

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[1] See WATKINS, PUBLIC REGULATION OF COMPETITIVE PRACTICE (1940).

[2] The clause may read: "*Appointment of Distributor.* The Company hereby appoints ....(hereinafter called the 'Distributor'), an authorized Distributor of the following products for the territory defined below . . . ." The restriction of the appointment "for the territory defined" must refer to a territorial allocation of some sort or the clause would be devoid of meaning.

Thus, it is seen that all large manufacturers for export to foreign countries try to allocate markets according to a territory. For the most part this is done in a fairly direct manner by an exclusive agreement allocating a territory to a foreign distributor. Occasionally some of these contracts do not explicitly prohibit the distributor from dealing in competitive products.

amounting, for example, to 3 per cent. The distributor would still be, in effect, the exclusive distributor in the territory. A "gentleman's agreement" that no other person will be appointed would hardly be necessary since either the manufacturer or such other person would be at an immediate 3 per cent disadvantage as compared with the first distributor. Sometimes these benefits are coupled with the exclusive contract. However, it is to be noted that such methods may be subject to attack by the Sherman Act and, secondly, the exclusive distributorship is less expensive to the manufacturer. (3) The commitment on the part of the distributor neither to distribute the products outside the territory nor to handle products of other manufacturers that may in any way compete with the contract products, assures the manufacturer that the distributor will not divide his time with competing products every time their market price is a bit lower than the manufacturer's products.

There are arguments that much the same result could be accomplished were the "antitrust conscious" commitments on both sides withdrawn. First, a clause may be put into the agreement spelling out the distributor's duties in some detail. For example, in the case of a distributor who purchases goods for resale the clause could read: "Distributor agrees to maintain a suitable place of business, to establish and maintain a sufficient stock of such products, to provide adequate facilities for the installation, replacement, service, and repair of such products, sold by Distributor, and adequately and diligently to promote the general distribution and sale of such products within the area set forth." Thus, in theory at least, the distributor will not have time and will have less inclination to concern himself with competing products to the detriment of the manufacturer.

Secondly, an inclination to deal with competing products can always be held within bounds by use of a thirty or sixty-day notice-of-termination clause which is commonly found in both exclusive and non-exclusive foreign distributor agreements. A distributor so bound should be less likely to take on a competing line for fear that he will be accused of lack of attention to the manufacturer's product and will thereby lose his account. The thirty or sixty-day clause is a whip which, according to many exporters, makes most of the rest of the agreement of less importance. The manufacturer relies upon it to take the place of the promotional clause set forth above. A distributor who values his manufacturer's account is not going to do anything to jeopardize the chances of keeping this account. Large manufacturers in particular think of the relationship in these terms. However, it is obvious that the manufacturer would not like to use the clause except as a last resort since it is, after all, a termination clause and not an operational clause.

Of the most important antitrust laws affecting or which might affect exclusivity agreements, only the Sherman Act[3] and the Federal Trade Commission Act[4] are capable of affecting exclusive foreign distributorships. However, a glance at other enactments, such as the Wilson Tariff Act of 1894,[5] the Clayton Act,[6] and the Webb-Pomerene Act,[7] may be of aid in

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[3] 26 STAT. 209 (1890), as amended, 50 STAT. 693 (1937), 15 U.S.C. § 1 (1946). This provides: "Every contract . . . in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal . . . ."

[4] Section 5 empowers the Commission to prevent corporations from using "unfair methods of competition in commerce, and unfair or deceptive acts or practices in commerce." 38 STAT. 719 (1914), as amended, 52 STAT. 1028 (1938), 15 U.S.C. § 45 (1946). "Commerce" includes trade between the United States and foreign nations and foreign competitors have been held to be within the protection of the statute. Eastman Kodak Co. v. Fed. Trade Comm., 7 F.2d 994 (2d Cir. 1925), *aff'd.*, Fed. Trade Comm. v. Eastman Kodak Co., 274 U.S. 619 (1927).

[5] 28 STAT. 570 (1894), as amended, 37 STAT. 667 (1913), 15 U.S.C. § 8 (1946). Any agreement "intended to operate in restraint of lawful trade, or free competition in lawful trade or commerce, or to increase the market price in any part of the United States of any article or articles imported or intended to be imported into the United States, or of any manufacture into which such imported article enters or is intended to enter" is illegal. Obviously, this statute has little direct effect upon foreign distribution agreements. However, cases interpreting this Act may be of value by analogy inasmuch as the Sherman Act clearly imposes liability of a similar nature with regard to the export trade.

[6] 38 STAT. 730 (1914), 15 U.S.C. §§ 13, 14 (1946). This is limited to goods sold for use, consumption, or resale within the United States. Section 3 provides: "It shall be unlawful for any person engaged in commerce ["Commerce" is defined in Section 1 to include trade with foreign nations], in the course of such commerce, to . . . make a sale or contract for sale of goods . . . whether patented or unpatented, *for use, consumption, or resale within the United States* . . . or fix a price charged therefore, or discount from . . . such price, on the condition . . . that . . . the purchaser thereof shall not use or deal in the goods . . . of a competitor . . . of the . . seller where the effect of such . . . sale, or contract for sale or such condition . . . may be to substantially lessen competition or tend to create a monopoly in any line of commerce" (italics added). 15 U.S.C. § 14 (1946).

The effect of this provision has been greately diminished with respect to foreign producers with the enactment of the Act of September 8, 1916, 39 STAT. 799 (1916), 15 U.S.C. § 73 (1946), which concerns exclusive agency agreements in favor of imported goods. This law states that: "If any article produced in a foreign country is imported into the United States under any agreement . . . that the importer thereof or any other person in the United States shall not use . . . the articles of any other person, there shall be levied . . . in addition to the duty otherwise imposed by law, a special duty equal to double the amount of such duty: *Provided, that the above shall not be interpreted to prevent the establishing in this country on the part of a foreign producer of an exclusive agency for the sale in the United States* of the products of said foreign producer or merchant, nor to prevent *such exclusive agent from agreeing not to use, purchase, or deal in* the article of any other person . . . ." (italics added).

In effect, the quoted provision, while specifically referring to tariffs, appears to sanction exclusive importing agreements according to which a distributor shall not handle products competing with those of his foreign supplier.

[7] 40 STAT. 516, 517 (1918), 15 U.S.C. §§ 61-65 (1946). Nothing contained in the Sherman Antitrust Act [or § 7 of the Clayton Act] "shall be construed as declaring to be illegal an association entered into for the sole purpose of engaging in export trade and actually engaged solely in such export trade, or an agreement made or act done in the course of export trade by such association, provided such association, agreement, or act is not in restraint of trade within the United States . . . ." 15 U.S.C. § 62 (1946). The Webb-Pomerene Act was enacted to permit American exporters to combine so as to compete more successfully with European exporters. Apparently it does not apply to an American manufacturing corporation exporting alone. Such a

determining judicial attitude by way of analogy should our courts have occasion to consider the legality of exclusivity agreements in foreign trade.

THE DOMESTIC DOCTRINE

With the exception of the Wilson Tariff Act, which relates exclusively to imports, the Webb-Pomerene Act, which concerns only associations among exporters and manufacturers for export, and parts of the Clayton Act, the antitrust laws couple the concepts of trade or commerce "among the several states" with those of trade or commerce "with foreign nations." Therefore, in view of the present dearth of cases concerned with foreign exclusive distributor agreements and the great volume of domestic exclusive distributorship decisions, a discussion of some of the latter may be of value. Because of the general wording of Section 1 of the Sherman Act, declaring illegal every contract in restraint of trade, whether foreign or domestic, it appears that the principles of these domestic cases may be extended to the foreign field at any time. This possibility is a sword of Damocles to foreign traders, particularly American manufacturers with large, well-developed foreign markets.

Although the Clayton Act is limited in its application to sales of goods consumed or resold within the United States, cases interpreting Sections 2 and 3 of this statute offer the most useful analogies, since most domestic suits involving exclusive distributorships are brought under these sections. The principles derived therefrom may be applied to the foreign field by means of the Sherman Act. The only other distinction between these statutes is that the Sherman Act refers to all agreements "in restraint of trade or commerce" whereas the Clayton Act specifically refers to exclusive dealer agreements which may "substantially lessen competition or tend to create a monopoly in any line of commerce." Clearly agreements which are held to be substantially lessening competition or tending to create a monopoly may, without too much difficulty on the part of the court, also be held to be agreements which are in restraint of trade within the Sherman Act.

The congressional debates on Section 3 of the Clayton Act are illuminating. The House version of the Bill (later modified by the Senate to become the Clayton Act) prohibited both exclusive dealing and tying arrangements.[8] The Senate struck out the prohibition against exclusive dealing and

corporation can only be attacked through an export association of which it is a member. Under this Act, two corporations may be members of the same export association and jointly fix prices, without antitrust fears if care is taken to avoid interfering with the export trade of nonmember American competitors, or intentionally or artificially enhancing or depressing prices in the United States. See Statement of A. C. Phelps, Ch., Division of Export Trade, Bureau of Anti-Monopoly, Fed. Trade Comm., Meeting N.Y.C. Bar Association, January 24, 1951.

[8] 51 CONG. REC. 9911 (1914), H.R. 15657, 63rd Cong., 2d Sess. (1914). A supplier in a "tying" arrangement furnishes a controlled product on condition that the dealer or user also purchase a tied product that would otherwise be available from the supplier's competitors.

substituted a narrow bar on tying agreements on patented articles alone,[9] but the final form of the Act prohibited both such agreements which "substantially lessen competition or tend to create a monopoly in any line of commerce." Because of this qualifying clause, the so-called "rule of reason" must be applied to determine the legality of each competitive practice.[10]

Distributors who are "an integral part of the organization"

A single exclusive agreement between an American manufacturer and a domestic distributor is generally considered valid per se, assuming the termination clause contains a definite fixed time equal in extent and duration for both sides.[11] On the other hand, where several such contracts are a part of a general system to suppress competition, each exclusive agreement may be held illegal under the Clayton Act.

When distributors are an integral part of a producer's organization, a part built up by the producer as an outlet for his products, competitors cannot use the antitrust laws as a vehicle for launching their own products with the aid of that organization. In 1917 the Supreme Court held in *Pictorial Review Co. v. Curtis Publishing Co.*[12] that Section 2 of the Clayton Act was not violated by the refusal of the publisher of the *Ladies Home Journal* to allow its district agents to furnish retail dealers and newsboys with a magazine published by a competitor without first obtaining the former's approval. But the prohibition was contained in contracts between the company and its agents who, although purchasers of its magazines, were part of an elaborate sales force conceived, organized, trained and capitalized by the company.[13] Furthermore, even where such agencies are created by a producer, the recent decision in *United States v. Richfield Oil Corp.*[14] held that non-competitive dealer contracts are illegal if such agency does not remain in effect a branch office of the producer. There the Supreme Court decided that oral exclusive sales agreements between the interstate oil company and its local dealers violated the Sherman and Clayton Acts even though the company exercised extensive controls over the lessees of

[9] 51 CONG. REC. 14276 (1914).

[10] See Chicago Board of Trade v. United States, 246 U.S. 231, 238 (1918).

[11] RESTATEMENT, CONTRACTS § 516, comment g (1932); WILLISTON, CONTRACTS, §§ 1027A, 1645 (1936); Comment, 27 COL. L. REV. 838 (1927).

[12] 255 Fed. 206 (S.D.N.Y. 1917).

[13] The court stated: "If nothing but a sale were involved, I might support complainant's contention that defendant has violated the Clayton Act by preventing its wholesale dealers from selling the Pictorial Review through subdealers and boys; but what complaintant evidently desires is, not merely to sell to these wholesalers . . . but to avail itself of the organization of the Curtis boys, built up by the ingenuity, labor, and capital of the defendant. The defendant, in insisting upon maintaining the integrity of its system, is not in my opinion guilty of unfair trade." *Id.* at pp, 208, 209.

[14] 99 F. Supp. 280 (S.D. Cal. 1951), *aff'd per curiam*, Richfield Oil Corp. v. United States, 343 U.S. 922, 958 (1952).

its service stations. The lessees were held to be independent of the company even though the company constructed and leased stations in order to "create" markets for its products. The court perhaps tried to distinguish the *Curtis* case when it stated that "No case will be found which supports the contention that the mere creation of an exclusive form of outlet is, in itself, sufficient to avoid the consequences of the antitrust laws."[15] The opinion cannot be understood as overruling the *Curtis* case, however, in view of the fact that the dealers were independent.[16]

One of the most important economic considerations in the field of foreign trade is the extent to which the exclusivity device is used by foreign manufacturers in their contracts with distributors in the region where American manufacturers are marketing their goods. To prohibit only American manufacturers from using exclusivity contracts in South America could hardly be considered fair, in view of European competition in the same area. Without an exclusive arrangement by the American producer, a European manufacturer could await the development of the South American market by the American's local distributors before making his own arrangements with the distributor for the handling of similar products. The argument of the *Curtis* case that the distributor is but an arm of the American manufacturer is unavailable because foreign distributors universally handle several product lines from different American and other foreign producers, and therefore they cannot be considered proteges of a single foreign manufacturer.

One argument often given in defense of the exclusivity device is that proscription of the device would lead to vertical integration of an industry. This reason has less force in the foreign trade field where the difficulties of establishing a local dealer on the payroll of the American producer corporation are often insurmountable. Although establishment of a branch is not contemplated, the American corporation may be subject to local taxation and registration. Recently, many exporters have been considering the tax cost of establishing foreign branches in connection with the exigencies of a Western Hemisphere Trade Corporation under Section 109 of the Internal Revenue Code. Even with the added incentive of 28 per cent credit on both normal and surtaxes as well as complete exemption from the excess profits tax, few manufacturers have been willing to establish branches in all the countries where their distributors are located, although they would not hesi-

[15] *Id.* at 291.

[16] *Cf.* Carter Carburetor Corp. v. The Federal Trade Commission, 112 F.2d 722 (8th Cir. 1940). Here a carburetor manufacturer made contracts granting discounts to retailers on the condition that they cease to deal in a new competing line. The court, sustaining a cease and desist order issued by the Federal Trade Commission, cited the *Curtis* case and distinguished it on the ground that in the instant case the thousands of service stations involved were established independent outlets where the public has been accustomed to go for service on all makes of carburetors and have never constituted an exclusive selling agency for Carter products.

tate to do so in a similarly important marketing area in the United States.[17]

Certainly the rare situation in the *Curtis* case is generally not attained in the field of foreign trade. Foreign distributors of most American manufacturers for export are not comparable to "Curtis boys" inasmuch as they are general distributors and handle products of many other companies. As a rule foreign distributors were not developed as distributors of a particular company's products, and therefore exporters and manufacturers for export can expect a little substantive help from such analogy.

The Supreme Court's Change from the Test of a "Dominating" to One of a "Substantial" Position in the Line of Commerce

The Supreme Court held in an early case, *Standard Fashion Co. v. Magrane-Houston Co.*,[18] that the fact that a manufacturer maintained a dominating position in the field can be of utmost importance. The Standard Fashion Company, a manufacturer of dress patterns, had an agreement with a Boston department store to handle the manufacturer's product exclusively during the term of the contract. In holding this agreement a violation of Section 3 of the Clayton Act, the Supreme Court noted that both lower courts "put special stress on the fact found that, of 52,000 so-called pattern agencies in the entire country, the Standard Fashion Company, or its holding company, controlling it and two other pattern companies approximately controlled two-fifths of such agencies."[19]

This "large-fraction-of-the-industry" test to determine whether the agreement violates the qualifying clause of Section 3 of the Clayton Act—generally taken to mean that the industry must maintain a dominating position in the field—was further reinforced recently in *Standard Oil Co. of California v. United States*[20] in which dealer-owned service stations were bound by an agreement to sell only Standard Oil products. In view of the defendant's small percentage (23 per cent) of the total Pacific Area gasoline business, the Supreme Court's holding that the defendant's exclusive supply contracts with independent dealers were illegal under the Clayton Act narrows the previous requirement of a "dominating" position. Under the new formulation of the "rule of reason," exclusive dealer agreements which may restrain a "substantial" amount of trade are invalidated. Previously dealers agreements which actually substantially lessened competi-

[17] This may be caused by exchange controls and other reasons, but it is certainly due in part to the American tradition of counting on the home market with the mental attitude toward foreign markets being that they are only to be serviced after the home market has been thoroughly satisfied. This attitude is changing as American manufacturers for export realize that where the market justifies the expense, there is little excuse for inadequate service.

[18] 258 U.S. 346 (1922).

[19] *Id.* at 357.

[20] 337 U.S. 293 (1949).

tion were unlawful under the Sherman Act only if they were unreasonable or economically injurious to the public. However, in referring to several of the economic tests mentioned by Justice Brandeis in the *Chicago Board of Trade* case[21] as criteria which must be taken into consideration if the rule of reason is to be applied, Justice Frankfurter rejected most of them in a cavalier fashion by merely noting that "serious difficulties would attend the attempt to apply these tests."[22] Referring specifically to that case, Frankfurter stated that: "To insist upon such an investigation would be to stultify the force of Congress' declaration that requirements contracts are to be prohibited whenever their effect 'may be' to substantially lessen competition."[23] Therefore, the court held that the exclusive dealership contracts were per se violations of Section 3 of the Clayton Act solely because the court felt that "use of the contracts creates just such a potential clog on competition as it was the purpose of Section 3 to remove wherever, were it to become actual, it would impede a substantial amount of competitive activity."[24] The *Standard Oil* case thus eliminates from the qualifying clause of Section 3 of the Clayton Act the test of reasonableness and requires only that a substantial share of commerce be tied up by the exclusive arrangements—which arrangements may or may not presently imperil competition.

There was a strong dissent in the *Standard Oil* case from the "quantity approach" of the majority opinion to the effect that the requirements contract cannot be illegal per se and that the Government must establish that either the actual or probable effect of the arrangement is to substantially lessen competition; "proof of their [the contracts] quantity does not prove that they had this forbidden quality."[25] The minority opinion brought out the fact that logically the quantity or share of commerce affected is not by itself a guide to the effect of exclusive arrangements on competition.

During the four years since the *Standard Oil* decision, the majority opinion incorporating the principle of the per se violation when a substantial amount of trade may be affected has been quickly applied to many other industries, although the decision has been very strictly construed by most courts.[26]

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[21] *Supra* note 10.

[22] *Supra* note 20 at 308.

[23] *Id.* at 313.

[24] It is to be noted that the case was decided under the Clayton Act only, Justice Frankfurter stating that it was therefore unnecessary to apply the Sherman Act. *Id.* at 314.

[25] *Id.* at 322.

[26] *Electricity* (Sherman and Clayton Acts). In Pennsylvania W. & P. Co. v. Consolidated G.E.L.&P., 184 F.2d 552 (4th Cir.), *cert. denied,* 340 U.S. 906 (1950), an agreement between a Pennsylvania and a Maryland utility requiring the former to take all its supplemental electricity from the Maryland utility was held illegal under both the Sherman Act and the Clayton Act. Here the public suffered by the exclusive contract which was reinforced by the monopoly of the utility in the State of Pennsylvania.

Can Closing Machines (Sherman Act). In United States v. American Can Co., 87 F. Supp.

The foreign trader who has been following the decisions which concern domestic exclusive dealer agreements should remember that although the Supreme Court did not apply the Sherman Act, it indicated by inference that the Sherman Act can be applied where the Clayton Act is inapplicable.

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18 (N.D. Cal. 1949), the court held illegal per se an agreement between the American Can Company which controlled 54 per cent of all can-closing machines leased to canners, whereby the latter leased the closing machines with a tying clause not to purchase cans from any competing company. The agreement covered all the customer's American needs for certain types of cans for a term of five years. The court held that not only the agreement, but "the five-year term creates an unreasonable restraint in the light of all the facts . . . ." It then decided under Sections 1 and 2 of the Sherman Act (noting that the *Standard Oil* case was decided only under the Clayton Act) that "a reasonable period of time for said duration is one year." The court ruled out the Clayton Act by stating, without explanation, that "Defendants requirement contracts do not come within either the language or the intent of Section 3 of the Clayton Act." No relief was granted pending further hearings and thus, the contracts have not been declared void to our present knowledge.

Petroleum Products. The *Standard Oil* case has been strictly interpreted to the extent tbat recently one court refused to apply the Clayton Act without proof that a substantial amount of commerce may be effected. Thus, in Knight v. Hamilton, 313 Ky. 858, 233 S.W.2d 969 (Ky. App. 1950), the defendant was required to buy from plaintiff exclusively all the products used in the operation of the gasoline filling station under the terms of a contract referred to in defendant's lease for the station's property. In granting an injunction prohibiting defendants from breaching the contract, the court held that such contract was not in restraint of trade in violation of Section 3 of the Clayton Act. It refused to apply the doctrine of the *Standard Oil* case inasmuch as no proof was offered to show that the effect of this contract "may be to substantially lessen competition." It pointed out that the Standard Oil Company's sales amounted to 23 per cent of the total gallonage sold in the area whereas the instant case involved, according to the evidence, only one gasoline station.

The same result was reached in Sunset Oil Co. v. Vertner, 34 Wash. 2d 268, 208 P.2d 906 (1949). In this case the Sunset Gas & Oil Company, a distributor for the plaintiff, entered a distributor's agreement with the defendant, according to which the latter agreed to purchase petroleum products exclusively from the Sunset Gas & Oil Company for resale within his territory. In August, 1946, Sunset Gas & Oil Company assigned its interest in the contract to tbe plaintiff. The defendant controlled five service stations. In October, 1946, he sold his business and ceased to purchase petroleum products from plaintiff as he was required to do under the contract. In granting judgment for the plaintiff, the court quoted from United States v. Standard Oil Co. of California, 78 F. Supp. 850, 877 (S.D. Cal. 1948), *aff'd.*, Standard Oil Co. v. United States, 337 U.S. 293 (1949), where it is pointed out that such an "exclusivity" contract is not illegal per se but "becomes illegal ony if it results in a substantial lessening of competition." 34 Wash. 2d at 279, 208 P.2d at 912. The contract in the instant case was not held to be illegal under the antitrust acts because no evidence was introduced concerning the lessing of competition.

Farm Machinery. In United States v. J. I. Case Co., 101 F. Supp. 856 (D. Minn. 1951), an exclusive dealership policy was held not to he unlawful within the Sherman and Clayton Anti-Trust Acts. In this case the dealers were retailers .

The J. I. Case Company, third largest American manufacturer of long line farm machinery, distributed through 3,738 independent owners and operators of farm machinery businesses, of whom 1,050 handled no competing lines. These dealers had a yearly contract with Case. The Government contended that Case maintained a policy of exclusivity which it foisted upon its dealers. However, Case showed that where a dealer was handling another full line, the Case merchandise was carried as a mere sideline with inadequate service facilities. In such instances, the dealer was given a choice between the two lines and where the competing line was chosen, Case looked for another dealer. The court noted that "Generally, the result in either situation would be that there became a Case dealer and the competitive dealer in the community. There-

This could be interpreted to mean that Section 3 of the Clayton Act, can be transposed into the field of foreign trade through the vehicle of the Sherman Act. In a roughly comparable manner, restrictions contained in the First Amendment to the United States Constitution, which is limited to

fore, not only did competition continue, but the free flow of farm machinery rather than being impeded was usually increased." The court pointed out that there was "no showing that any farm machinery manufacturer had difficulty in obtaining dealers as outlets for its particular line in such circumstances" and upheld the right of a manufacturer to select its customers.

The bulk of the agreements were held not to sustain an inference of an understanding that Case contracts were granted upon the condition that no competitive goods would be handled. The holding was based on the finding that the test set up in Standard Oil Co. of California v. United States, 337 U.S. 293, 311 (1949), was not met as there existed insufficient potential power to lessen competition which, were it to become actual, "would impede a substantial amount of competitive activity." The fact that almost one-third of Case's distributors were in fact exclusive was not deemed important inasmuch as there existed no covenant not to handle goods of a competitor as in the *Standard Oil* case. Moreover, it was not considered necessary to draw any percentage of exclusive dealerships compared with available dealers, in view of that fact.

The court allowed in evidence for the defendant a statistical report demonstrating that competition had not decreased during the period in question, although it stated that the conclusions reached would remain the same in its absence.

It is to be noted that contracts made with an illegal purpose are per se illegal regardless of the amount of trade affected. The case of Maryland & Virginia Milk Pro. Ass'n. v. United States, 193 F.2d 907, 911 (D.C. Cir. 1951), arose on an indictment under Section 3 of the Sherman Act, 15 U.S.C. §3 (1946), concerning "full supply" contracts between a cooperative milk producers' association and distributors. The producers' association brought about 80 per cent of the milk to the district area; however, only a few of the distributors continued on the "full supply" contract basis immediately prior to the indictment. The trial court dismissed the indictment and held that these contracts were not per se violations of the Sherman Act.

The Government appealed to the Supreme Court which remanded the case to the court of appeals. 335 U.S. 802 (1948). The latter court reversed the decision of the district court on the ground that where, as stated in the indictment, the full supply contracts are "made for the purpose of eliminating and suppressing competition," they are illegal per se. 179 F.2d 426 (D.C. Cir.), *cert. denied,* Maryland & Virginia Milk Pro. As'n. v. United States, 338 U.S. 831 (1949).

The defendants not parties to "full supply" contracts during the three-year period immediately preceding the filing of the indictment were acquitted. As to the remaining defendants, the proceeding was "limited and restricted to the subject of 'full supply' contracts embodying the classification plan." Thus, where only a few distributors continued the "full supply" contracts, the court was unable to hold the contracts illegal restraints because of the exclusivity feature alone. It was only in conjunction with the plan to fix prices that the contracts were in violation of the Sherman Act. 90 F. Supp. 681, 688 (D.C. 1950). On appeal, even these convictions were reversed because of insufficient proof of the existence of such illegal purpose. 193 F.2d 907 (D.C. Cir. 1951).

Thus, the principle of the *Standard Oil* case (brought under the Clayton Act), has been distinguished: where the contracts are made for a restraining purpose they are illegal even though less than a "substantial" amount of trade is affected.

It is to be noted that in United States v. Yellow Cab Co., 332 U.S. 218 (1947), which is cited in the *Standard Oil* opinion, it was stated that the amount of interstate trade affected was immaterial. However, the Supreme Court followed "some rule of reason" and went on to show in detail how an "appreciable" amount of trade had been restrained by defendant company which controlled several operating cab companies and obliged these companies to purchase the cabs exclusively from a cab manufacturing corporation which the defendant also controlled: "The complaint in this case deals with interstate purchases of replacement of some 5,000 licensed taxicabs in four cities. That is an appreciable amount of commerce under any standard." 332 U.S. 218, 225 (1947).

acts on the part of the Federal government, have been transposed by the Federal courts through the vehicle of the Fourteenth Amendment so as to restrict state action.

If the narrow reasoning of the *Standard Oil* decision were applied to exclusivity contracts made with foreign distributors, it would be difficult to reach any conclusion other than one holding them to be illegal.[27]

The attack on exclusivity contracts by the Government could be made on a country-by-country basis, or by regions, although apparently only the latter would be feasible. For example, in order to establish a violation of the Sherman Act the Department of Justice need only ascertain that 23 per cent of a product or line of products entered South America through distributors, one per country or less, (in South America large distributors resell in several countries), each of whom has an exclusive dealing clause in his contract with one particular American manufacturer. In this example the *Standard Oil* decision would apparently be in point, the "Pacific Area" being simply replaced by the "Continent of South America" in the foreign trade case.

DECISIONS DEALING WITH FOREIGN EXCLUSIVE DISTRIBUTOR AGREEMENTS

Although there are apparently no judicial decisions entirely concerned with foreign exclusive distributor agreements, two very important decisions have recently dealt with the problem as a matter secondary to the principal issues with which they were concerned.

In *United States v. Minnesota Mining & Mfg. Co.*,[28] four domestic manufacturers, controlling four-fifths of the export trade in coated abrasives, formed an export association under the Webb-Pomerene exception to the Sherman Act which provides that the Sherman Act shall not apply to an association entered into for the sole purpose of engaging in export trade. All exports were directed through the export company which later formed foreign subsidiaries for the purpose of manufacturing abrasives abroad, and agreed not to export to the foreign countries served by the subsidiaries. The defendants claimed that due to the tremendous rise in trade barriers, it was more profitable to make abrasives abroad rather than export. The court held that the purpose of the combination was not within the terms of the Webb-Pomerene Act, because the export of capital to engage in local foreign trade is not "export trade," and, instead of promoting export trade,

[27] Lately, it has been strongly urged that the Supreme Court flatly overrule its decision. Lockhart and Sacks, *The Relevants of Economic Factors in Determining Whether Exclusive Arrangements Violate Section 3 of the Clayton Act*, 65 HARV. L. REV. 913, 941 (1952). Although the recent *Richfield Oil* holding expressed some doubt regarding the present court's feeling toward the *Standard Oil* decision the court in *Richfield Oil* refused to overrule the *Standard Oil* decision in the absence of a full court, two justices not having heard oral argument due to illness. See note 14 *supra*. Therefore, the reasoning of *Standard Oil* must be accepted as being the latest word of our highest tribunal.

[28] 92 F. Supp. 947 (D. Mass. 1950).

the arrangement violated the Sherman Act since it restricted American exports.

The Government further contended that the use of Minnesota of exclusive foreign distributorships was illegal. The export company used three different forms of distributor contracts, one of which made the distributor exclusive in his area; another provided for a fixed number of other distributors in his area; a third was non-exclusive. All distribution contracts made since February, 1947, required the distributor to carry stocks and solicit trade but provided that the arrangement was non-exclusive. The court held that trade was not necessarily restrained by the exclusivity because this limitation was not designed to effect a monopoly of channels of distribution. It found that the export company had fewer distributors than when the manufacturing defendants had exported separately and not through the export company. It further noted that there were an ample number of foreign distributors available and that the actual volume of abrasives shipped by competing American exporters had been constantly increasing. This was a singular holding on foreign exclusive distributor agreements and no authority could be cited therefore. However, because ample qualified distributors are not always available in every country and because in another case exports of competitors may happen to decrease shortly after the agreements are made, this case may be restricted to its facts in the future when a somewhat different situation is present to the courts.

In *Timken Roller Bearing Co. v. United States*[29] the American Timken Company, defendant, was charged with conspiring with its foreign affiliates to restrain trade under Sections 1, 3 and 4 of the Sherman Act and the Government sought a permanent injunction against such activity. Between 1941 and 1945, defendant manufactured between 71 and 78 per cent of American anti-friction bearings. The percentages of its partially-owned subsidiaries, British Timken and French Timken, were even higher in their respective countries.

Beginning in 1909, the American firm made agreements with the predecessor of British Timken granting it the exclusive license to "make, use, exercise, and vend" roller bearings in the United Kingdom pursuant to specifications of British patents owned by the defendant or to be acquired from him. Defendant was prohibited from licensing others in the territory, and the British Corporation was probibited from manufacturing or selling roller bearings except those made under the licensed patents.

In 1927, the chairman of English Timken, Dewar, made an agreement with American Timken to buy the English company, whereby each would purchase the stock of British Timken for 52,500 pounds and 47,500 pounds,

[29] 341 U.S. 593 (1951). The history of this case is thoroughly discussed in the District Court opinion. 83 F. Supp. 284 (N.D. Ohio 1949).

respectively, Dewar maintaining control. Each party agreed not to sell bearings either directly or to third parties for shipment into the other's territory. The following year, defendant and Dewar organized and divided the stock of French Timken, Dewar again given supervision, and a trade agreement between French Timken and British Timken was made similar to that between the British and American companies, the territory comprising France and her colonies. In 1938, the three companies entered a "tripartite agreement" to govern their conduct until 1965.

The exclusive territorial divisions were so well lived up to that the trial court found "that defendant entered the agreements . . . for the purpose of preventing competition in the sale of bearings"[30] in violation of the Sherman Act and this view was affirmed in the Supreme Court.[31]

Both the *Minnesota* and *Timken* cases were primarily concerned with the relations of foreign subsidiaries and American parent companies and only secondarily with the exclusivity feature, although the *Minnesota* case also contained a ruling on exclusive foreign independent distributorships while the holding in the *Timken* case was entirely confined to the subsidiary problem. However, a restrictive agreement between an Amercian manufacturing company and its foreign subsidiary may be compared with an exclusive foreign agency agreement. Both are agreements not to sell to third parties within a prescribed territory and where trade is restrained as a result of either agreement, it falls within the proscription of the Sherman Act.

The *Timken* holding was not as striking to American manufacturers in foreign trade as was the *Standard* case to domestic traders. The very purpose of the agreements between the American, British and French Timken companies was found to be that of suppressing competition. In the *Standard* case the court found no such purpose; the exclusivity agreements were only found to be potentially capable of suppressing competition.

The *Timken* case is also of interest because the Supreme Court rejected the argument that the use of restrictive agreements with foreign subsidiaries was excusable as a reasonable method of doing business in view of current foreign trade conditions including tariffs and quota restrictions. The argument was rejected on the ground that it "iguores the fact that the *provisions in the Sherman Act . . . are based on the assumption and reflect the policy that export and import trade in commodities is both possible and desirable*" (italics added).[32] Logically, the economic argument should be welcomed by the court, with respect to exclusive agency agreements where it may be shown that it bears on the success of the American import and

[30] United States v. Timken Roller Bearing Co., 83 F. Supp. at 315.
[31] 341 U.S. 593 (1951).
[32] *Id.* at 599.

export trade. This distinction was drawn in the *Minnesota* case and the court even noted that by the channeling of defendant's products through the export company, which in turn used exclusive foreign distributors, there were "an ample number of foreign distributors available" for competitors to use.

CONCLUSION

It is the opinion of this writer that the exclusive foreign distributorship is a business organizational device which greatly aids in the promotion of international trade without stifling competition to an appreciable extent.

The exclusivity feature of a distributorship set up abroad which is entirely devoted to the promotion and sale of the products of a single American corporation would undoubtedly have no adverse antitrust effects, even though the goods are actually purchased by the foreign agent.[33] An exclusive agency agreement for the purpose of importing goods has been sanctioned by statute solely on the basis of the economic necessity of such an arrangement.[34] Similarly, there is an economic necessity for exporting products manufactured in the United States through exclusive agencies located in marketing areas abroad. This is especially true where there is foreign competition in the territory which is unhampered by antitrust laws.

A prime distinction may be drawn between the decisions concerning foreign and domestic exclusive distributorships. Domestic manufacturers who have violated the antitrust laws have invariably attempted to have exclusive distributorships with all or a large percentage of the available distributors in a given area.[35] When no attempt is made to obtain exclusive agreement with a large number of the available distributors in a given area, the courts have generally refused to declare the agreements illegal.[36] While an exclusive distributorship is per se illegal if made "for the purpose of suppressing competition," such purpose will not be found to exist unless there is an attempt to monopolize available distributors in a given area. When only one distributor already is working in a given area, an American manufacturer ought not be sanctioned for seizing upon this agent's exclusive services. Foreign traders have always been satisfied with a minimum number of local distributors. It may well be hoped that the limited protection obtained by manufacturers in foreign markets through use of the exclusivity clause will not be eliminated by an extension of the domestic doctrine and especially of the *Standard Oil* decision into the foreign markets through the vehicle of the Sherman Act.

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33 Pictorial Review Co. v. Curtis Publishing Co., 255 Fed. 206 (S.D.N.Y. 1917); see note 12 *supra*.

34 15 U.S.C. § 73 (1946); see note 6 *supra*.

35 See Carter Carburetor Corp. v. Fed. Trade Comm., *supra* note 16; Standard Fashion Co. v. Magrane-Houston Co., *supra* note 18; Standard Oil Company of California v. United States, *supra* note 20; Pennsylvania W. & P. v. Consolidated G.E.L. & P. Co., *supra* note 26; United States v. Yellow Cab Co., 332 U.S. 218 (1947).

36 See Knight v. Hamilton, *supra* note 26; Sunset Oil Co. v. Vertner, *supra* note 26.