Although a substantial part of the dollar volume of manufacturers is accounted for by sales made directly to commercial or consumer users, a more significant source of federal antitrust lore is the area of distribution systems in which manufacturers sell (typically, "consumer products") either to resellers, or through business entities designated as consignees or agents. The scope and application of antitrust doctrines relating to vertical restrictions in such distribution are unclear and require frequent review. To date Supreme Court opinions in this field have tended to contract the area of permitted use of such restrictions, but have always left open substantial questions for the future.

There are many types of restrictions which are agreed to by, or are imposed on, those downstream in the vertical distribution pattern (i.e., distributors, dealers, consignees and agents) who sell to the ultimate consumer.\(^1\) The restrictions discussed here are those most frequently dealt with in the cases: restrictions on (1) the prices at which the marketer sells the goods, (2) the geographic area in which he sells or solicits sales of the goods and (3) the categories of customers to whom he sells or of whom he solicits sales of the goods. Cases involving the latter two categories almost invariably have involved some element of the first category—restrictions affecting price.

Resale price maintenance was one of the earliest issues considered by the Supreme Court under the Sherman Act, whereas restrictions on territory and customer were not squarely treated by the Court until the 1960's. Yet even in the area of resale price maintenance, despite many decisions, intervening legislation and abundant literature dealing with the subject in the half century since the *Dr. Miles* decision in 1911,\(^2\) there is considerable uncertainty with respect to the scope and application of the resale

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price maintenance principles enunciated in the leading cases.

The antitrust history of vertical resale restrictions is tiresome to those who have been through it, and perhaps depressing to many manufacturers concerned with orderly marketing of their goods. But any discussion of the subject of vertical restrictions necessarily requires a brief recitation of this history. Ten leading cases demonstrate the long legal history of efforts to justify such restrictions and of the persistent tightening of the limitations on their use by the Supreme Court after 1919.

(1) The Dr. Miles case grew out of an action by a manufacturer (Dr. Miles) against a price-cutting wholesaler seeking to enjoin the latter from inducing other wholesalers or retailers to breach their written agreements with Dr. Miles not to sell to any reseller other than "designated Retail Agents." The Dr. Miles system of distribution was designed "to maintain certain prices fixed by it for all the sales of its products both at wholesale and retail." Dr. Miles argued that the agreements were consignment or agency contracts under which it properly controlled prices at which wholesalers and retailers sold as its agents. The Supreme Court construed the bill of complaint as attacking purchases by defendant from purchasers from the consignees or agents, and thereby held the distribution system invalid under common law and Sherman Act principles. After noting that the resale price maintenance provisions of the agreements were not analogous to those permitted in the case of a sale of good will because the manufacturer had not parted with any interest in its business, the Court mentioned the asserted justification for the restriction—that confusion and damage result where sales at less than standard retail prices are made. The Court reasoned that the advantage of such a standard retail price primarily concerned the dealers, not the manufacturer. Since agreements between or among dealers to maintain the price would be illegal, thought the court, "the com-

3 Dr. Miles Medical Co. v. John D. Park & Sons Co., 220 U.S. 373 (1911).
4 Id. at 394. Although technically the case presented an issue of the validity of contractual restrictions on the categories of resellers to whom the wholesalers or retailers could sell, the real thrust of the case was the resale price maintenance system.
5 Under the wholesale consignment contract, "Said Consignee agrees to confine the sale of all goods and products of the said Proprietor [Dr. Miles] strictly to and to sell only to the designated Retail Agents of said Proprietor as specified in lists of such Retail Agents furnished by said Proprietor . . ." and "at not less than the following prices." Id. at 376, 378. Under the Retail Agency Contract the drugstore agreed not to sell "to wholesale or Retail dealers not accredited agents of" Dr. Miles and agreed "in no case to sell or furnish the said Proprietary Medicines to any person, firm or corporation whatsoever, at less than the full retail price as printed on the packages." Id. at 380.
plaintant [Dr. Miles] can fare no better." The sweeping language of the Court was not limited to the facts before it:

Where commodities have passed into the channels of trade and are owned by dealers, the validity of agreements to prevent competition and to maintain prices is not to be determined by the circumstance whether they were produced by several manufacturers or by one, or whether they were previously owned by one or by many. The complainant having sold its product at prices satisfactory to itself, the public is entitled to whatever advantage may be derived from competition in the subsequent traffic.7

(2) The Colgate case8 turned on the construction of an indictment. The trial court construed it as not charging that the manufacturer had entered into agreements with its wholesale and retail customers, but rather as charging a combination of the manufacturer and its wholesale and retail customers. Thus the indictment was construed as charging that "The retailer, after buying, could, if he chose, give away his purchase; or sell it at any price he saw fit, or not sell it at all; his course in these respects being affected only by the fact that he might by his action incur the displeasure of the manufacturer, who could refuse to make further sales to him, as he had the undoubted right to do."9 In affirming the judgment sustaining a demurrer to the indictment, the Court set forth its famous statement:

In the absence of any purpose to create or maintain a monopoly, the Act does not restrict the long recognized right of trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal. And, of course, he may announce in advance the circumstances under which he will refuse to sell.10

(3) One year later in the Schrader's case11 the Court struck down a resale price maintenance system and affirmed the distinction between the Dr. Miles and Colgate opinions:

It seems unnecessary to dwell upon the obvious difference12

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6 Id. at 408.
7 Id. at 408-09. The Court accordingly affirmed an appellate judgment affirming a dismissal of the bill on demurrer for want of equity.
9 Id. at 305-06.
10 Id. at 307. Pertinent to later cases were the averments in the bill of complaint in Colgate that the defendant had engaged in many enforcement activities including "requests to offending dealers for assurances and promises of future adherence to prices, which were often given." Id. at 303.
between the situation presented when a manufacturer merely indicates his wishes concerning prices and declines further dealings with all who fail to observe them, and one where he enters into agreements — whether express or implied from a course of dealing or other circumstances — with all customers throughout the different States which undertake to bind them to observe fixed resale prices. (Emphasis added.)

(4) In the Old Dutch Cleanser case, decided the year after the Schrader’s decision, the Court noted that the opinion of the Court in Schrader’s “distinctly stated that the essential agreement, combination or conspiracy might be implied from a course of dealing or other circumstances,” and held that this issue was a question of fact for determination by the jury.

(5) The fourth of these consecutive year cases, the Beech-Nut case, became the source of great discussion in the journals for the next generation. That case, reversing a judgment based on the Colgate case, upheld as modified an FTC order to cease and desist issued under section 5 of the Federal Trade Commission Act. Beech-Nut had not entered into resale price agreements, but it had used elaborate cooperative and coercive tactics to enforce its program (reporting names of noncomplying dealers, causing dealers' names to be placed on lists of undesirable purchasers, reinstating customers previously cut off for cutting prices upon assurances to sell at suggested prices and to refuse to sell to price cutters, using numbers and symbols to trace noncomplying dealer sales, etc.). These practices were said to suppress freedom of competition by methods “which are quite as effectual as agreements express or implied intended to accomplish the same purpose” and were held to be unfair methods of competition.

13 United States v. A. Schrader's Son, Inc., 252 U.S. 85, 99 (1920). The Court reversed a judgment sustaining a demurrer to the indictment; the district court had sustained the demurrer reluctantly, forestating a problem of much subsequent litigation: “Personally, and with all due respect . . . I can see no real difference upon the facts between [Dr. Miles and Colgate]. The only difference is that in the former the arrangement for marketing its product was put in writing, whereas in the latter the wholesale and retail dealers observed the prices fixed by the vendor. This is a distinction without a difference. The tacit acquiescence of the wholesalers and retailers in the prices thus fixed is the equivalent for all practical purposes of an express agreement . . . .” Id. at 97.


15 Id. at 210.


17 Id. at 455. Commenting on the Dr. Miles-Colgate-Beech-Nut line of cases, Professor Chaffee concluded forty years ago that “It may be conjectured that the present legal confusion is not really due to an absence of clear thinking but only corresponds to the complicated interlacing of economic factors in a field where definite rules are
(6) The Bausch & Lomb case in 1944 held invalid a plan whereby, according to the Court, the wholesalers in question "accepted Soft-Lite's proffer of a plan of distribution by cooperating in prices, limitation of sales to, and approval of, retail licensees . . . ." The Court, after holding that Soft-Lite had conspired and combined with some of the wholesalers "by designating selected wholesalers as sub-distributors of Soft-Lite products, by fixing resale prices and by limiting the customers of the wholesalers to those recommended by the wholesalers and approved by Soft-Lite . . . ." vaguely opined that "[w]hether this conspiracy and combination was achieved by agreement or by acquiescence of the wholesalers coupled with assistance in effectuating its purpose is immaterial." Two other aspects of the Bausch & Lomb case had very significant influences on later developments: first, the Court upheld in a 4-4 decision the manufacturer's agreement not to sell to Soft-Lite's competitors; second, the Court included a statement in the opinion relating to Soft-Lite's marketing system—that apart from fair trade a seller "may not lawfully limit by agreement, express or implied, the price at which or the persons to whom its purchaser may resell . . . ." Two other aspects of the Bausch & Lomb case had very significant influences on later developments: first, the Court upheld in a 4-4 decision the manufacturer's agreement not to sell to Soft-Lite's competitors; second, the Court included a statement in the opinion relating to Soft-Lite's marketing system—that apart from fair trade a seller "may not lawfully limit by agreement, express or implied, the price at which or the persons to whom its purchaser may resell . . . ."

(7) Then came the infusion of perhaps the greatest confusion sixteen years later with the decision of the Court in Parke, Davis. There the Court reversed the dismissal of the complaint on two grounds. First, the Court concluded that Parke, Davis had exceeded the permissible bounds of Colgate because it had not merely announced its policy regarding retail prices and followed this with a "simple" refusal to deal with any retailers who disregarded the policy. Rather, it had refused to deal with wholesalers "in order to elicit their willingness to deny Parke, Davis products to retailers and thereby help gain the retailers' adherence to its suggested minimum retail prices." The Court found that the wholesalers cut off price-cutting retailers when Parke, Davis furnished the names of the offenders. This course of conduct the Court said went beyond a mere Colgate-authorized announcement of policy and refusal to deal and perhaps impossible. Whatever solution of the price-control problem is adopted, it seems pretty sure to be unsatisfactory." Chaffee, *Equitable Servitudes on Chattels*, 41 Harv. L. Rev. 945, 992 (1928).


19 Id. at 723. Much reliance was later placed on this language of the opinion by the government in attacking customer restrictions. But, as indicated, the heart of the case was the Court's conclusion that there was present "an agreement between the seller and purchaser to maintain resale prices," Id. at 721; the price fixing was "an integral part of the whole distribution system," Id. at 720.

20 Id. at 721.

VERTICAL RESTRICTIONS

resulted in a combination of Parke, Davis with the retailers and wholesalers to maintain retail prices in violation of the Act. Second, the Court condemned the course of conduct engaged in by Parke, Davis with respect to suspension of price advertising. The Court concluded that Parke, Davis had been advised by Dart Drug, a retailer which had been advertising cut prices, that Dart would be willing to "go along," and that Parke, Davis had then approached other retailers and "Dart's apparent willingness to cooperate was used as the lever to gain their acquiescence in the program." Parke, Davis, "having secured those acquiescences," so reported to Dart and the advertising was suspended. The Court characterized this as concerted action induced by Parke, Davis and stated that under such circumstances "The manufacturer is thus the organizer of a price-maintenance combination or conspiracy in violation of the Sherman Act."\(^2\)

(8) Even more revolutionary in the sweep of some of its language was Mr. Justice Douglas' opinion for the Court in Simpson v. Union Oil Co.\(^23\) There the Court in effect granted summary judgment to the treble damage plaintiff on the question of violation on the ground that the price setting provisions of Union Oil's one year consignment contracts, used in conjunction with its one-year leases with its service station dealer-lessees amounted to unlawful resale price maintenance. Although the case has been distinguished on a number of grounds, the language of the opinion was unrestrained:

When . . . a "consignment" device is used to cover a vast gasoline distribution system, fixing prices through many retail outlets, the antitrust laws prevent calling the "consignment" an agency, for then the end result of [the Socony Vacuum case\(^24\) making horizontal price-fixing arrangements per se unlawful] would be avoided merely by clever manipulation of words, not by differences in substance. The present, coercive "consignment" device, if successful against challenge under the antitrust laws, furnishes a wooden formula for administering prices on a vast scale.\(^25\)

The Court did not follow its decision upholding price control clauses in consignment agreements in the General Electric case.\(^26\)

\(^{22}\) Id. at 46-47.

\(^{23}\) 377 U.S. 13 (1964).

\(^{24}\) Socony-Vacuum Oil Co. v. United States, 310 U.S. 150 (1940).

\(^{25}\) Simpson v. Union Oil Co., 377 U.S. 13, 21-22 (1964) (emphasis supplied.)

The *General Electric* case was apparently distinguished on the ground that it involved products covered by patents.

All of the foregoing cases essentially involved restrictions on prices at which persons at the retail level would sell to the public. The only Supreme Court decisions dealing at any length with vertical restrictions on geographical territories or classes of customers were relatively recent—*White Motor* in 1963 and *Schwinn* in 1967.

(9) *White Motor* involved what Mr. Justice Clark in dissent characterized as "one of the most brazen violations of the Sherman Act that I have experienced in a quarter of a century."20 The government contended that contract provisions that a distributor would not sell trucks, except to persons having a place of business and/or purchasing headquarters in a defined territory, and would not sell or authorize its dealers to sell trucks to any governmental body, were per se violations of the Sherman Act. The defendant asserted a number of reasons why the territory and customer clauses were necessary and proper. The Court, reversing a summary judgment for the government and sending the case back for trial, reasoned that since this was the first case "involving a territorial restriction in a vertical arrangement,"30 it knew "too little of the actual impact,"31 of the two types of restrictions, or of the "economic and business stuff out of which these arrangements emerge,"32 to decide whether they should be classified as per se restraints, even though the district court had found that the contracts also fixed resale prices, a ruling from which the defendant did not appeal.

(10) Four years later a somewhat similar case reached the Court; by this time the Court apparently felt that it did have the requisite knowledge to invalidate territorial and customer restrictions on resellers. In *Schwinn* the Court was presented with a distribution program in which, in essence, three methods were used: sales to distributors who resold to retailers, sales to retailers by means of

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The subsequent consent decree, reprinted at 1964 TRADE CAS. ¶ 71,195 (N.D. Ohio 1964) enjoined the defendant from entering into "any contract, combination, agreement or understanding, with any distributor, dealer, or any other person to limit, allocate or restrict the territories in which, or the persons or classes of persons to whom, any distributor, dealer or other person may sell trucks."
31 Id. at 263.
32 Id.
consignment or agency arrangements with distributors, and sales to retailers under the "Schwinn plan" under which Schwinn made direct shipments to retailers with Schwinn invoicing the retailer and extending credit and then paying a commission to the distributor who took the order. Schwinn assigned specific territories "which were allocated on an exclusive basis" to each distributor and instructed it to sell only to franchised Schwinn accounts and only in the assigned territory. The district court, after a lengthy trial, had prohibited Schwinn from requiring that distributors who purchased from Schwinn resell only in their assigned territories, but upheld the restriction where the consignment or agency or Schwinn plan method was used and upheld customer restrictions under all three methods of distribution. A major charge of the government—that Schwinn required retailers to adhere to retail prices designated by Schwinn—was rejected by the district court.

Only the government appealed. It did not appeal the part of the decision finding defendants innocent of price fixing. In its arguments on appeal the government sought to have the decree enlarged in two major respects—first, to prohibit territorial restrictions on distributors in consignment, agency and Schwinn plan transactions as well as resale transactions; and, second, to prohibit customer restrictions in arrangements with distributors or retailers regardless of the form of the transaction. The government prevailed in its attack on customer restrictions in resale transactions but otherwise lost the appeal.

The Supreme Court, acknowledging that it was concerned with a truly vertical arrangement, began its legal analysis by looking to the "specifics of the challenged practices and their impact upon the marketplace in order to make a judgment as to whether the restraint is or is not 'reasonable' . . . ." But somehow the Court concluded that "where a manufacturer sells products to his distributors subject to territorial restrictions upon resale, a per se violation of the Sherman Act results [and that] the same principle applies to restrictions of outlets with which the distributors may deal and to restraints

34 This injunctive relief was granted on the basis of the district court's holding that Schwinn and certain distributors had entered into a horizontal agreement to allocate the territories of those distributors. United States v. Arnold, Schwinn & Co., 237 F. Supp. 323, 342 (N.D. Ill. 1965).

35 "These are not horizontal restraints, in which the actors are distributors with or without the manufacturer's participation." United States v. Arnold, Schwinn & Co., 388 U.S. 365, 372 (1967). Here the Court cited United States v. General Motors Corp., 384 U.S. 127 (1966). The Court also emphasized that it did not have a case "of territorial or dealer restrictions accompanied by price fixing." Id. at 373.

upon retailers to whom the goods are sold." But where consignment, agency or Schwinn plan type restrictions were involved, the Court went on to hold that "it is only if the impact of the confinement is 'unreasonably' restrictive of competition that a violation of section 1 results...." The Court upheld the reasonableness of the restrictions in the latter types of transactions on the facts of the Schwinn record, noting that Schwinn had retained "all indicia of ownership, including title, dominion, and risk" and citing as "critical" four factors—other competitive bicycles were available in the marketplace, the distributors and retailers handled other brands as well as Schwinn, the vertical restraints were not improperly intermixed with price fixing and the net effect of the restrictions was to preserve and not to damage competition in the bicycle market.

One immediate observation about the foregoing line of cases is that they have been controversial, even at the Supreme Court level. In only one of the ten cases—Colgate—did nine Justices adhere to the opinion of the Court, and the average number of Justices joining in the majority opinion without concurring opinion in the other nine cases has been only 5.6. A second major consideration is that

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87 Id. at 379. (emphasis by the Court.) This was of course dictum, since Schwinn had not appealed from the district court's decision on this point.

88 Id. at 380.

89 Id. at 381-82, Schwinn was applied in Hensley Equip. Co. v. Esco Corp., 383 F.2d 252 (5th Cir. 1967), in such a manner as to make unenforceable a supplier's patents on grounds of patent misuse; the offending provision of the patentee's license agreement restricted the license "to the use of licensed products and/or sale of licensed products for original installation on ... equipment manufactured by or for Caterpillar and sold by ... Caterpillar dealers ... and to use as replacement parts sold by Caterpillar and Caterpillar dealers ... for such ... equipment." Id. at 263 n. 22.

40 Positions of the Justices may be tabulated as follows:

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** On procedural grounds
all of them involved charges of resale price maintenance—even in Schwinn the government, foreclosed by its appellate strategy from attacking the district court's finding of no price-fixing, argued that the customer restriction was "specifically designed to exclude . . . retailers likely to emphasize price competition" [i.e., discount houses]. While much sophisticated analysis has been utilized in the Court's handling of the precedents, fact situations and posture of legal questions presented to it in these cases, a basic consideration is the fundamental, if fading, distinction between interbrand and intrabrand competition. As Mr. Justice Holmes plaintively put it in dissent, "I cannot see how it is unfair competition to say to those to whom the respondent sells, and to the world, you can have my goods only on the terms that I propose, when the existence of any competition in dealing with them depends on the respondent's will." Today the dissent has an added social content, arising out of the advantages to the small retail merchant operating under a "franchise" in competition with "vertically integrated giants". "Through various forms of franchising, the manufacturer is assured qualified and effective outlets for his products, and the franchisee enjoys backing in the form of know-how and financial assistance." But, with the exception of the brief pause for White Motor, the Supreme Court has consistently insisted upon intrabrand competition among resellers in the cases it has considered.

Response to the articulated premises and reasoning of the Court in its expansions of the 1960's of antitrust strictures against restrictions on purchasers or consignees—Parke, Davis, Simpson and Schwinn—has been vocal and extended. Parke, Davis has been criticized roundly as crippling or making unintelligible the Colgate doctrine; Simpson has been scored as undermining settled principles of agency-antitrust law; and Schwinn has been condemned as badly misinterpreting its supposed legal foundation and as further un-

44 The only authorities relied on by the Court (other than a citation to the Dr. Miles case, which essentially involved price fixing) were the White Motor case and the ancient rule against restraints on alienation. In White Motor the Court expressly refused to hold that territorial and customer restrictions were per se unlawful, even where admittedly accompanied by price-fixing. The Court's scholarship with respect to, and the present-day relevance of, the law of restraints on alienation has been questioned. See dissenting opinion of Justice Stewart, Id. at 391-93; Handler, The Twentieth Annual Antitrust Review — 1967, 53 VA. L. REV. 1667, 1684-86 (1967).
justifiably upsetting the long-assumed and sensible principle that agency arrangements need not be tested by the "rule of reason" since they do not constitute "contracts, conspiracies or combinations in restraint of trade."45

But proceeding on the proposition that the law is what the Supreme Court says it is, what vertical restrictions may a manufacturer seek with respect to price, territory and/or customer? Some of the approaches to and arguments for permissible restrictions are discussed below.

Where sales are made to distributors, or direct to retailers, in contrast to transactions properly characterized as agency or consignment transactions, there is, obviously, considerably less latitude available to the manufacturer. As articulated in Schwinn, "proper application of section 1 of the Sherman Act to this problem requires differentiation between the situation where the manufacturer parts with title, dominion or risk with respect to the article, and where he completely retains ownership..."46

Resale price control is of course the area historically most trodden. Clearly, the manufacturer may unilaterally establish and publish suggested resale or list prices.47 Additionally, under Colgate he may, "without more," announce that he will refuse to deal with anyone who sells at or advertises prices other than the suggested prices, and cut off those who do not abide by the policy.48 He may control resale prices within specified limitations in states where fair trade laws are still in force. He probably may explain to purchasers the advantage of following specified resale price schedules, although this practice approaches the edge of the cliff overlooking "contract, conspiracy or combination." He may ordinarily control resale prices of goods for

45 "[B]efore Schwinn it was settled law that bona fide agency and consignment arrangements required no justification since they involved no restraints." Handler, The Twentieth Annual Antitrust Review — 1967, 53 VA. L. REV. 1667, 1686 (1967).

46 United States v. Arnold, Schwinn & Co., 388 U.S. 365, 378-79 (1967). The government did not argue on appeal that the restriction should be per se unlawful where a resale relationship existed, and the Court did not state why transfer of title should control the outcome. The Assistant Attorney General in charge of the Antitrust Division was later reported as suggesting in a panel discussion that "By and large [transfer of title] shouldn't make any difference. Beyond a certain point, a distributor is the same as a salesman, and he should be treated as one." 342 BNA ATTR A-20 (1968).

47 Absent decree provisions imposed as a remedial device or fictitious pricing or other deceptive acts.

export if there is no adverse effect on interstate or foreign commerce. He may control resale prices if so permitted under an established exemption from the antitrust laws.

Provisions affecting the distributor's territory are judged by less exacting strictures than those affecting resale price. Clearly, nothing in Schwinn should preclude a manufacturer from "assigning", in the sense of "designating", territories (the distributor retaining the right to sell outside the territory). Similarly, the manufacturer probably can agree not to appoint another distributor in each "assigned" territory. He may insist that the distributor use his best efforts to exploit the territory, which he frequently cannot effectively do if he expends his efforts in forays outside the territory. He may conceivably provide for pass-over of part of the distributor's gross margin in the case of sales outside the territory where the magnitude of the pass-over is not tantamount to a restriction on extending activity beyond the territorial boundary. This is particularly true where the prime purpose of the pass-over is to compensate the distributor in the "invaded" territory for installation and/or service obligations necessarily incurred. It should be that he can enforce location clauses

49 There is some authority "for concluding that the practice usually would not sufficiently affect United States foreign trade to come within the Sherman Act." FUGE, FOREIGN COMMERCE AND THE ANTITRUST LAWS 106 (1958).

50 See, e.g., Packard Motor Car Co. v. Webster Motor Car Co., 243 F.2d 418 (D.C. Cir.), cert. denied, 355 U.S. 822 (1957); Schwing Motor Co. v. Hudson Sales Corp., 138 F. Supp. 899 (D. Md.), aff'd per curiam, 239 F.2d 176 (4th Cir. 1956), cert. denied, 355 U.S. 823 (1957). (This freedom may be limited if the supplier is determined to be a monopolist. See Cherokee Laboratories, Inc. v. Rotary Drilling Services, Inc., 383 F.2d 97 (5th Cir. 1967).)

In Schwinn the Court seemingly acknowledged this principle, except where the supplier is a monopolist:

[a] manufacturer of a product other and equivalent brands of which are readily available in the market may select his customers, and for this purpose he may 'franchise' certain dealers to whom, alone, he will sell his goods. Cf. United States v. Colgate & Co., 250 U.S. 300 (1919). If the restraint stops at that point — if nothing more is involved than vertical "confinement" of the manufacturer's own sales of the merchandise to selected dealers, and if competitive products are readily available to others, the restriction, on these facts alone, would not violate the Sherman Act.


such as were upheld in the 1942 Boro Hall case,\(^5\) since they are essentially contractual arrangements ancillary to the manufacturer’s right to select dealers, and do not affect the right of the dealer to sell outside his territory.

Restrictions on the categories of customers to whom the distributor may sell were characterized by Mr. Justice Brennan in his concurring opinion in White Motor as being “inherently . . . more dangerous” than territory restrictions. He suggested that they might merely “codify the economically obvious” if as a practical matter the distributors could not sell the prohibited accounts.\(^6\) Presumably the manufacturer may restrict resale customer categories where safety or other requirements of law would otherwise be violated—e.g., the sale of certain drugs to persons other than those authorized by law to sell or dispense them.\(^7\) Certain sanctions might be provided—e.g., return of part of the discount where sales are made to retailers rather than jobbers, in order to avoid violation of the Robinson-Patman Act. And the Schwinn case does not really deal with the situation involved in the intriguing FTC decision in Roux Distrib. Co.,\(^8\) where a complaint attacking customer restrictions was dismissed in part on the ground that the two classes of purchasers, drug wholesalers (who were confined to selling to drug and department stores) and beauty supply dealers (who were confined to selling to beauty salons), were not engaged in substantial competition with each other.

The Schwinn case left open certain questions as to the situations in which the “per se violation” concept will be applied to vertical territorial and customer restrictions. First, although the Court did not emphasize the fact, the basis for its dictum that territorial restrictions on a reseller are invalid per se was a district court holding that such restrictions were invalid where they were imposed as part of a horizontal arrangement at the distributor level.\(^9\)

\(^5\) Boro Hall Corp. v. General Motors Corp., 124 F.2d 822 (2d Cir. 1942). “Location clauses may be necessary. It’s one thing if it’s a substitution for territorial restrictions, but if it’s ancillary to an exclusive distributorship that’s different. Manufacturers need some latitude but we should preclude restrictions that aren’t economically merited.” Reported remarks of Mr. Donald F. Turner, Assistant Attorney General in charge of the Antitrust Division, in panel discussion, 342 BNA ATTR A-19 (1968).


\(^7\) Consider whether the per se rule should apply where the purpose of a restriction is to permit equitable distribution during a period of shortage. Cf. Fosburgh v. California & Hawaiian Sugar Ref. Co., 291 F. 29 (9th Cir. 1923).

\(^8\) 55 F.T.C. 1886 (1959).

\(^9\) See United States v. Arnold, Schwinn & Co., 287 F. Supp. 823 (N.D. Ill. 1965). Thus the case might conceivably be read some day as being limited to such fact situa-
Another possible area of permissible use of either customer or territorial restrictions or both has been noted in the peculiar treatment by the Court in *Schwinn* of the situation of the "struggling company" or the "newcomer". In *White Motor* the Court, acknowledging that "We do not know enough of the economic and business stuff out of which [territorial limitations] emerge to be certain" that they are "naked restraints of trade with no purpose except stifling of competition," observed that such restrictions "may be allowable protections against aggressive competitors or the only practicable means a small company has for breaking into or staying in business . . ."57 The Court specifically observed in *Schwinn* that, in its view, the facts there did not come within these "specific illustrations" of the possible application of the rule of reason adverted to in *White Motor*.58 The fact that the Court did not even cite the *Sandura* and *Snap-On* cases9 lends additional weight to this interpretation. While it seems illogical and discriminatory to permit "small companies" to use contractual provisions and to deny their use to other competitors, there is no doubt that courts entertain favorably this type of argument, presumably on the premise that competition is increased, rather than restrained, in such situations. Assuming that such a limitation on the sweep of the *Schwinn* per se pronouncements is valid, the usual questions of how small is small, how long does a newcomer remain a newcomer, etc., will remain for case by case analysis or repronouncement by the courts.

Whether application of the per se violation doctrine stated in the *Schwinn* case will be applied in all reseller situations is thus not completely clear. It is probably accurate to state that until the *Simpson* and *Schwinn* cases most counsel proceeded on the premise that restrictions on price, territory and customer category were per se legal in true consignment or agency arrangements, with no "rule of reason" justification being necessary. There was always the question whether the agency or consignment was "bona fide," but the nearly universal understanding was that a true consignment or agency relationship made the consignee or agent an arm of the manufacturer

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58 In the *Sealy* case, decided on the same day as *Schwinn*, the Court even suggested that a horizontal allocation of territories among small grocers might be justifiable. *United States v. Sealy*, 388 U.S. 350, 357 (1967).
59 *Sandura Co. v. FTC*, 339 F.2d 847 (6th Cir. 1964); *Snap-On Tools Corp. v. FTC*, 321 F.2d 825 (7th Cir. 1963). In both cases territorial restrictions were upheld as reasonable restraints. Further, in *Snap-On* certain restrictions on customers were held to amount to at most a de minimis restraint on competition.
and thus no "contract, conspiracy or combination in restraint of
trade" was present. Now that the Court apparently has changed all
this in Schwinn, and has concluded that consignment or agency
arrangements which contain restrictions on territories or cus-
tomers may constitute "contracts, combinations or conspiracies in re-
straint of trade", the propriety of which is to be judged by applica-
tion of the rule of reason, what standards are available?60

First, there is doubt that the opinion can be read to permit
application of the rule of reason to price restriction clauses or in
monopoly contexts—the Court said that vertical restrictions are not
per se violations "absent price fixing and in the presence of ade-
quate sources of alternative products to meet the needs of the
unfranchised..."61 Second, presumably the manufacturer must act
unilaterally and without horizontal "agreement" at the manufacturer
or distributor level. Third, the kinds of business justifications ap-
propriate to establishing that territory and customer restrictions do
not "unreasonably" restrain trade are probably as many and varied
as are the rule of reason cases in the antitrust books. Those which
the Court mentioned as persuasive in Schwinn were: (1) Schwinn
adopted its program "in a competitive situation dominated by mass
merchandisers;" (2) Schwinn's practices did not result in "an
inadequate competitive situation;" and (3) Schwinn's program
did not exceed the limits reasonably necessary "to meet the
competitive problems posed by its more powerful competitors."62
A shorthand version of this might be to say that Schwinn faced

60 One observer has suggested that the bar has over-reached to Schwinn and
that the basic question in this type of case is whether the particular manufacturer
is "dominant": "If you have a dominant position, any kind of restraint, I think, is
going to be looked at very critically by the court. If you do not have a dominant
position the Court is much more likely to treat a greater restraint as one that comes
within exceptions to this per se rule, or is going to treat it differently under the
rule of reason. Therefore, I think, from a practical point of view, that the Schwinn
case really doesn't change very much." Cohen, remarks in panel discussion, 36 ABA
ANTITRUST L. J. 84, 90 (1967). One critical factor in any such approach of course is
the accordion-like expanse of the imprecise term "dominant."

point in the opinion the Court indicated that where the "function of the dealer in
question is, in fact, indistinguishable from that of an agent or salesman of the man-
ufacturer, it is only if the impact of the confinement is 'unreasonably' restrictive of
competition that a violation of § 1 results from such confinement, uncumbered by
culpable price fixing." Id. at 380. Of course this phrase adds only further confusion.
If the dealer is equivalent in function to a salesman, what conceivable wrong is there
in setting the price at which he may sell? And if price fixing in such circumstances
is bad only if it is "culpable," what is the content of that fighting term?

62 Id. at 380-81.
more powerful competitors, did not achieve dominance by its program and went no further than it had to in imposing restrictions. This is a customary rule of reason analysis, and permits justification in many factual situations. Fourth, it is possible that the form of the particular arrangement will be decisive. It is unfortunate perhaps that for purposes of legal analysis the Schwinn case involved a hodge-podge of programs of resale, agency and consignment, thus tending to suggest that the actual differences between them were minor; for example, the government relied in part on a provision in dealer franchise forms (which were signed by Schwinn, the distributor and the dealer) that the distributor would act "as an independent distributor and not as an agent."8 Thus a pattern of distribution limited entirely to persons who are indisputably agents might be argued to fall outside the bounds of the Schwinn principle. However, such a view must be characterized as sanguine except in the case of pure manufacturer's representatives or other agencies where neither title nor possession is transferred. Finally, a question might be raised if a manufacturer did not impose restrictions but simply announced that he would pay his agent commissions only on specified sales.64

Permissible areas of restrictive provisions in consignment arrangements are illustrated by selected facts of the Schwinn case itself. One year prior to the institution of the Schwinn marketing program it "had the largest single share of the United States bicycle market—22.5 percent,"65 and its dollar and unit sales rose substantially thereafter (although its market share fell to 12.8 percent). It had reduced the number of retail outlets on its mailing list by two-thirds and had instituted the practice of franchising approved retail outlets. Schwinn had been "firm and resolute" in insisting upon observance of territorial and customer limitations and its firmness "was grounded upon the communicated danger of termination."

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63 Brief for Petitioner, at 21, United States v. Arnold, Schwinn & Co., 388 U.S. 365 (1967). The Court in Simpson referred to "a so-called retail dealer 'consignment' agreement," Simpson v. Union Oil Co., 377 U.S. 13, 14 (1964) and said that there the dealers "have all or most of the indicia of entrepreneurs, except for price fixing." Id. at 20. However, the agreements there differed only in minor respects from those involved in United States v. General Elec. Co., 272 U.S. 476 (1926), after which many other agreements have been modelled.

64 A pessimistic view that Schwinn may become a "laboratory specimen," at least with respect to situations such as that present in Schwinn where a desire of the manufacturer is to keep the product out of the hands of discounter, is set forth in Kittelle, Territorial and Customer Restrictions Through Consignment or Agency-Schwinn or Sin?, 12 ANTITRUST BULL. 1007 (1967).

With all of this, the Court upheld the restrictions.

The conclusions to be drawn from the Schwinn case will no doubt be various and many. Why the Court suddenly threw territorial and customer resale restrictions into the oblivion of per se violation doctrine, when a vast amount of literature and evidence suggested that reasonable justification for restraints exists in many situations, is a mystery. As stated by Professor Day in 1962, "A review of prior writings discloses that virtually every writer on the subject of exclusive territory arrangements believes that such distribution arrangements are valid if they do not constitute an attempt to monopolize or do not unreasonably lessen competition."60

There were good reasons for this view: (1) the analogies customarily relied on to attack vertical restrictions67—the analogy to resale price fixing and the Dr. Miles analogy to horizontal agreement at the distributor level to allocate territories—are not really appropriate in analyzing territory and customer restrictions. Vertical price restrictions are almost inevitably for the benefit of the distributors,68 and distributor conspiracies normally have as their main purpose elimination of competition at that level, whereas territory and customer restrictions frequently are designed for the benefit of the manufacturer to permit his product to compete more effectively with other brands. As to price maintenance, the restriction normally would have a tendency to hobble interbrand as well as intrabrand competition, whereas the principal purpose of territorial and customer restrictions is frequently to strengthen and promote interbrand competition. (2) There is a host of reasons why in particular circumstances vertical territory or customer restrictions would be entirely reasonable as restraints of trade, particularly where their net effect is to promote competition. Examples include the need of non-dominant firms to attract effective distributors, particularly where substantial capital commitment at the distributor level is required, the situation where service is a major or crucial element of marketing and interbrand competition and requires some element of control by the manufacturer, the need of newcomers and failing manu-


68 However, in Albrecht v. Herald Co., 36 U.S.L.W. 4171 (U.S., March 4, 1968), the Court held arrangements affecting maximum resale prices to be within the per se illegality principle.
facturing firms to strengthen their competitive positions vis-a-vis more substantial competitors, the need to keep the product out of the hands of distributors or dealers who handle it in such a way as to hurt the public, and the situation where the manufacturer's only practical alternative is vertical integration.

In the face of all this, the Court in *Schwinn* merely issued a flat pronouncement on the per se illegality of post-sale restrictions, opining that it is unreasonable "without more to seek to restrict and confine" areas or persons in such cases and that "such restraints are so obviously destructive of competition that their mere existence is enough." Under these circumstances, it can be predicted that if application of the flat pronouncements of the *Dr. Miles* case in 1911 with respect to resale price maintenance is still unclear in 1968 after a series of interpretative decisions in the interim, the same will be even more true in the case of vertical territory and customer restrictions. Questions as to whether a "contract, combination or conspiracy," is present, whether a restriction is present, whether the "per se" rule of *Schwinn* really is intended to apply to all such vertical restrictions, whether the manufacturer has given up the requisite indicia of ownership, etc., will remain. And in the area of agency and consignment arrangements, all the additional questions of whether the *Schwinn* case applies to particular transactions, and in any event what factors are appropriate in applying the rule of reason, will remain. Accordingly, even if ours is not to reason why the Supreme Court handled vertical restrictions in the way it did in the *Schwinn* case, we can look ahead to years of further uncertainty for lawyers and businessmen in dealing with the problems of vertical restrictions.

69 The government noted in arguing the *Schwinn* case that a manufacturer "has, we grant, an interest in keeping his product from retail dealers whose methods might damage the goodwill of the product and thereby hamper him in competing with other manufacturers. An example would be a retailer who refused to permit damaged merchandise to be returned." Brief for Petitioner at 43, 388 U.S. 365 (1967). In one old case an agreement of the purchaser of stale cigarettes not to resell them in the United States was upheld in light of the allegation that sale here would injure the seller's reputation. *P. Lorillard Co. v. Weingarden*, 280 F. 238 (W.D.N.Y. 1922).

70 Counsel for Schwinn has stated that "the plain effect of Justice Fortas' opinion is going to be to force manufacturers like Schwinn to vertically integrate. I'm sure that it will be no secret when it comes out that Schwinn will vertically integrate." Remarks of Robert C. Keck in panel discussion, 56 ABA ANTITRUST L. J. 95 (1967).

71 United States v. Arnold, Schwinn & Co., 388 U.S. 365, 379 (1967). The Court said that the effect of such restrictions in the agency and consignment arrangements before it "is to preserve and not to damage competition in the bicycle market." *Id.* at 382.