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Agreements in Restraint of Trade

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THESIS.

AGREEMENTS IN RESTRAINT of TRADE.

by

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AGREEMENTS in RESTRAINT of TRADE:

Origin and History:

The rule that contracts or covenants in restraint of trade are void originated at an early day in the English law. The social condition of the country was woful. "Trade and the mechanic arts were in their infancy"; the artisans limited in number; merchants with capital by no means overabundant. The population was small, and the country sparsely settled. The nation desired no pauperism, but demanded that every citizen be free to engage himself in that department of labor in which his personal efforts would aid most to the aggregate possessions of the country. Hence it was deemed a matter of greatest public importance to prohibit contracts which in any way bound any man from the exercise or use of his trade or business in any place for any time. This rule was enunciated as early as the reign of Henry V, and Judge Hull is reported to have gone off in a passion at the sight of a contract by a buyer engaging to abstain himself from his craft for two years, and to have condemned the contract in language more forcible than elegant. The great fear of those early times was that such contracts would restrict competition in trade and tend to encourage monopolies.
It was said that the Roman law partially recognized the rule; but it is doubtful if it exists in the jurisprudence of other countries than those of England and her colonies and America.

An eminent authority states that if the cases are examined in connection with, and in view of, contemporaneous rules of law and usages in trade, much reason will be found for believing that the law in relation to these contracts grew out of the English law of apprenticeship. "By this law in its original severity", says Mr. Parsons, "no person could exercise any regular trade or handicraft, except after a long apprenticeship; and, generally, a formal admission to the proper guild or company. If he had a trade he must continue in that trade, or have none. To relinquish it therefore, was to throw himself out of employment, to fall a burden upon the community, to become a pauper." As, however, the severity of the law of apprenticeship relaxed, less antagonism was shown to contracts in restraint of trade (II Parsons on Contracts, p.257.)

For two hundred years after the case reported in the
Year Books, the rule remained unchanged, and without exception. The first attempt made to avoid the rule was by placing the covenant under seal, but this distinction between sealed instruments and simple contracts could not be sustained. Then the distinction between contracts in general restraint of trade and those in which the restraint was limited or partial, was set up and found favor with the Courts, and has remained, nominally, the rule to the present day. This qualification of the rule was reported in the case of Rogers v. Parrey, (2 Bulstr, 136), and again in Broad vs. Jollyffe, (1 Cro. Jac. 596), in the eighteenth year of James I, A.D. 1621. In the later case, a contract not to use a certain trade in a particular place was held an exception to the rule, and not void. It was said that it was usual in London for one to let the shop and wares to his servant when he was out of his apprenticeship and to covenant, for a valuable consideration, not to use that trade in such a shop, or in such a street. In 1711 was decided the great case of Mitchell vs. Reynolds (I Pr. Wms) All the authorities were carefully collected and reviewed by Park, J., and the rule, as declared in the opinion, has been followed up to
nearly the present day. The distinction between contracts under seal and those not under seal, was finally exploded, and the distinction between limited and general restraints fully established. Since that decision, the doctrine of the early cases was no longer vigorously insisted upon. The population had increased and there was greater competition in all useful pursuits; the laws of trade became better understood; the commercial and social system became developed and altered, so that the necessities for the stringent rule which before prevailed had, in a measure, ceased. The rule, consequently, was relaxed and modified, so that both in England and the United States a person may contract for a valuable consideration, not to pursue his occupation or calling within certain reasonable, restricted limits, and it will not be considered as contrary to public policy, and therefore void. It is not that such contracts are any more legal or enforcible, now, than they were at any former period, but that the Courts look differently at the question.
Principles underlying the Rule:

The reasons given by the Court in holding that contracts in restraint of trade are void are many. Every citizen should be free to engage himself "in that department of labor, in which his personal efforts will be likely to aid most to the aggregate production of the country", and, that public convenience requires "that all the various trades and employments of society should be pursued, each in its due proportion--a result with which the exclusion of any individual from his accustomed pursuits has a tendency to interfere." (Selden, J., in Lawrence v. Kidder, 10 Barb.). The Courts have said that since the products of man's labor belong immediately to the state, that he cannot, by contract, release his right to pursue that trade or calling by which he can aid most to the aggregate wealth of the state, and thereby compel himself to labor in some other occupation less advantageous to the state, or lead a life of idleness.

The reasons for the rule were given in the great case of Mitchell vs. Reynolds in detail. They are given in substance in the well considered case of Alger v. Thatcher, (19 Pick., 57) by Morton, J., as follows:
(1) "Such contracts injure the parties making them, because they diminish their means of procuring livelihoods and a competency for their families. They tempt improvident persons, for the sake of present gain, to deprive themselves of the power to make future acquisition. And they expose such persons to imposition and oppression."

(2) "They tend to deprive the public of the services of men in the employments and capacities in which they may be most useful to the community, as well as to themselves."

(3) "They discourage industry and enterprise, and diminish the products of ingenuity and skill."

(4) "They prevent competition and enhance prices."

(5) "They expose the public to all the evils of monopoly."

Greater weight and emphasis has been given by the Courts to the reasons in paragraphs 2, 3, and 4, but we shall see later that the Courts during the last few years, have, owing to the great advancements in all things commercial and industrial, looked upon these facts, which governed the earlier Courts in their decisions, as no longer of special weight or force, since these dangers do not now exist to any
appreciable extent.

The reasons enumerated by the Massachusetts Court may be divided into two classes: (1) Such contracts are void because they injuriously affect the citizen and (2) because they are a detriment to the state. That the interests of the individual enter into the question at all, is denied by some Courts. Selden, J., in Lawrence v. Kidder, (10 Barb. 641,) ridicules the idea that the effect upon the individual has anything to do with it. "The principles of public policy which lie at the foundation of this rule," he says, "would seem to be plain and obvious, and yet we find it urged in many of the cases, as an objection to the contract, that it tended to deprive the person bound of the means of obtaining a livelihood, as though the personal interests of the contracting parties had something to do with the doctrine...... It is nevertheless clear that the validity of the contract does not depend in the slightest degree upon the question whether it is beneficial or otherwise, to the party, bound. The interests of the public alone were considered in the adoption of this rule."

Contracts held void, where ample territory was left to the obligee to carry on his business, or, where the re-
striction covered more territory than the obligee could reasonably be expected to extend his business over, are made to turn, by the New York Judge, entirely upon the questions affecting the public alone, without thought of private interest, because, in the one case, the public convenience demands, that the pursuit of the various arts and trades should be distributed throughout the different sections of the country, so that every locality should have its appropriate accommodation, and, in the other case, because the public is cut off from the benefit of having such art or trade carried on in that territory. But, notwithstanding, that the courts have considered most the protection of public interests in establishing this doctrine, the better opinion, at least, in the later cases, is that the doctrine is founded upon two principal grounds. One is the injury to the public by being deprived of the advantages of competition in skilled labor, the other is the injury to the party himself by being restricted from following his trade or business, and thus being prevented from supporting himself and family. (Oregon Steam Navigation Co. vs. Winsor, 20 Wall, 67)
Essential Requisites of the Rule:

A: Restraint must be partial:

It is a well settled rule of law that an agreement in general restraint of trade is illegal and void, but an agreement which operates only as a partial restraint is valid, if it possesses the other essential features. The term "general" is not synonymous with universal. Agreements covering only part of the territory of the kingdom or state have been held to be too general and therefore, void. The criterion whether an agreement is partial and valid, or too general and void, is the Unreasonableness of the restraint. (II Pomeroy Equity Jurisprudence, sec.934) What restrictions of territory have been held partial will more fully be explained in a subsequent paragraph. It is sufficient for the present head to state that the general rule is that an agreement is valid which merely operates in restraining trade over part of the state or kingdom, and one operating as a restraint over the entire kingdom or country, is void.
B:  Consideration.

In order that an agreement in restraint of trade be valid, there must be a consideration. The Courts at one time supposed that the consideration must be adequate (Mitchell v. Reynolds), but since the decision of Hitchcock v. Coker, (6 Ad. & E. 438), the notion that the consideration must be adequate to the restraint has no longer prevailed. The Courts will no longer require into the question whether the consideration for the restraint is, or is not, adequate. If the contract shows on its face a legal and valuable consideration, it is sufficient. The parties themselves, upon their own view of all the circumstances, surrounding the contract, must determine whether or not, the consideration is adequate or inadequate. (Guerrand vs. Daudelt, 32 Md. 561, Smith’s L.C. Part II, note, p. 773) To look into the adequacy of the consideration, the law would be practically making the bargain, instead of determining only what is a reasonable and proper bargain. (Hitchcock vs. Coker, supra) In Pierce vs. Fuller (8 Mass. 223) one dollar was held to be a sufficient consideration for a covenant not to run a stage coach between Providence and Boston in opposition to the
A consideration is necessary although the contract be under seal. At common law, this is probably the only exception to the rule that a contract under seal imports a consideration which a party is not permitted to deny. (Metcalf on Contracts sec. 233) The reason of this inconsistency is that "consideration is here required for a different reason than that whereon the ordinary law of contracts without consideration rests. The reason being that it would be unreasonable for a man to enter into such a stipulation without some consideration, though it must be left to a sense of his own interests to determine what should be the amount or nature of the consideration." (Hitchcock v. Coker, supra)

C: Restraint must be Reasonable.

The general rule is that contracts which impose an unreasonable restraint upon the exercise of a business, trade, or profession, are void, but contracts in reasonable restraint are valid. No precise boundary line can be laid down within which the restraint would be reasonable, and beyond which, excessive. One of the chief factors in determining the reasonableness of the restraint is the extent
of the territory from which the person is restricted. The Courts at the present time allow a much wider restraint than formerly. Commercial welfare and business exigencies demand it. The rule is becoming broader in its effect as will appear upon examination of the later decisions.

In determining what is a reasonable restraint the contract should be viewed in all its aspects. If it such only as to afford "fair protection to the interests of the party in favor of whom it is given, and not so large as to interfere with the interests of the public," it will be regarded, in the eye of the law, as reasonable. (Horner vs. Graves, 7 Bing. 735). The answer may depend upon the various circumstances brought to bear upon it. The situation or object of the parties; the trade or profession and the way in which it is conducted; the numbers of inhabitants in the district, are material facts in determining whether the restraint contracted for is reasonable for the protection of the interests of the party in whose favor it is imposed, and not specially injurious to the public. (Horner vs. Graves, supra, Hubbard vs. Miller, 27 Mich. 15)
The question of time in the restriction is unimportant in determining whether a contract is void, as being in restraint of trade. If the restraint is otherwise reasonable, the circumstance that it is indefinite in time will not affect its validity, and, on the other hand, if the contract be reasonable in other respects, a limitation as to time, will not cure the illegality. The reason of this is that the public are for the time being losers of the services of the individual and do not derive any benefit in return. However, Tindal C.J. (2 M. & G.20), said that the time element cannot be altogether left out in determining the question whether the restraint is unreasonable or not in point of space. That which would be unreasonable, were it to continue for any length of time may not be so when it is to last only for a few days.

Presumption:

The general presumption as given by text writers, and decisions of many Courts, especially the early ones, is against all contracts in restraint of trade, whether general
or limited. They are considered prima facie void, or are presumed to be void until it is shown that the circumstances under which the contract was made were such as to render it reasonable and also that there was a valuable consideration. (Chappel vs. Brockway, 21 Wend.,157) Contra to this view is the opinion of Christiaen in Hubbard v. Miller (25 Mich., 15), where it is said that "the rule to be drawn from a careful analysis of the adjudged cases and the reasons upon which they are founded, does not seem to us to involve any such presumption, in the accurate or legal sense of the term."

The rule more correctly stated, he says, would be that all contracts in restraint of trade are void "considered only in the abstract". But if they are considered with the surrounding circumstances in view, and with reference to which they were made, and the restriction appears reasonable, and "the weight or effect to be given to these circumstances is not to be affected by any presumption, for or against the validity of the restriction."
Sale of Secret Arts or Patents:

Contracts for the exclusive use of a secret art or patent are not within the rule and will be upheld if they are in other respects valid. The reasoning, however, which underlies and governs the decision in both lines of cases, is the same. The rights of individuals and the interests of the public require it. If public policy requires that contracts be void which deprive the state of the benefit of the talent and labor of a citizen, it, on the other hand, demands that where a person has obtained legitimately something which he wants to sell, he should be allowed to sell in the way most advantageous to him, and to do this, it is often necessary that he should be able to bind himself to abstain from again entering into the business. This policy enables persons to enter into restrictive covenants and if, in the judgment of the Court, are not unreasonable, looking to the subject matter of the contract, they will be upheld. (Leather Cloth Co. vs. Lorsont, L.R.9 Eq., 345)

The excepting of patented inventions and secrets of art or trade, not patented, from the general rule is allowed, "for the purpose of stimulating inventive genius and of en-
couraging science and well-directed ingenuity." (Mackinnon Pen Co. v. Fountain Ink Co., 48 N.Y. Superior Ct., 442)

Judge Peckham, in the case of Good v. Tucker & Carter Cord-axe Co. considered this question carefully, and this exception to the rule may perhaps be left clear, and the reason for it expressed more accurately, if the language of the Court is given. A patentee in this case agreed to allow the defendants the exclusive use and sale on the western continent, of certain inventions patented by him, and to warrant and protect them in the manufacture and sale of them. "The owner of a patent," says Peckham, J., "may keep the right of introducing the invention to the public, or make the machinery or manufacture the patented article alone, or he may permit others to share such right with him, or he may allow them an exclusive right and retain none himself. It all follows and is founded upon the absolute and exclusive right which the owner of a patent has in the article patented, having such right he must plainly be permitted to sell to another the right itself, or, to agree with him that he will permit none other than such person to use it. Considera-
ations, which might obtain if the agreement were in regard to other articles, cannot be of any weight in the decision of a question arising upon an agreement as to patented articles."
Restraint as to Space:

The matter of space in the contracts of parties who bind themselves not to exercise their ordinary rights has been, and still is, a most important question in determining their invalidity or validity. In former times, if the restraint was general, nothing more need be ascertained, the covenant being void. It was an essential requisite that the contract should be partial as distinguished from general. The term general, however, was not used in the sense of universal. To-day, the contract will not fall to the ground, simply because it is unlimited as to territory. Still the subject of space is the guide-post looked to by the Courts in determining whether the stipulation is reasonable or unreasonable. That it may be seen exactly how the Courts have viewed the question what limitation will be considered partial and what general, it will be best, perhaps, to give a brief statement of facts from a few leading cases, and in nearly their chronological order, and with numerous quotations from the Opinions. In so doing, there will be an reiteration of much already given, but it is hoped this will
be compensated by arriving at a clearer and more exact understanding of the whole subject, both in its past and its present.

As has already been stated, the rule first enunciated was that any agreement whereby a person bound himself not to exercise his trade or business was void, notwithstanding it was limited as to a place certain and for a time certain; that also this rule did not long stand but was superseded by a more reasonable holding, and, that the doctrine was settled by the great case of Mitchell vs. Reynolds—if indeed, it was not settled before—that an agreement in restraint of trade, reasonable in its terms, supported by a valuable consideration, and limited as to space, is good and not contrary to public policy. This rule on its face has remained the same for nearly two hundred years, but the interpretation of it to-day is widely different than even a quarter century ago. What was once looked upon as a general restraint may now be considered as partial and in fact, may be no restraint at all. As an illustration, in the early part of the 18th century, a milkman sold his business and covenanted not to engage in it again upon certain streets,
(his old route), This was a partial restraint. To-day the merchant may sell his business, and bind himself from again exercising it within the entire kingdom.

A brief examination of a few cases will show the modifications that have taken place in applying the rule.

One of the earliest American cases was that of Pierce v Fuller, supra, which was adjudicated in Massachusetts in 1841. In this case, the obligation was not to run a stage between Boston and Providence, a distance of about forty miles, in opposition to the plaintiff's stage. The restriction was upheld, and the decision followed by several cases in that state.

In the case of Alger v. Thacher, supra, the condition was that the obligor should never carry on or be concerned in the business of founding iron. The bond was void, the restraint being general.

In the case of Taylor v. Blanchard, (13 Allen, 370) the defendant agreed never to set up, exercise, or carry on the trade or business of manufacturing and selling shoe cutters at any place within the state. This was also void, as a too
general restraint.

In 1851, in New York, was decided the case of Lawrence v. Kidder, supra. The defendant here covenantcd not to carry on the business of manufacturing or trading in palm leaf beds or mattresses, directly or indirectly, in all the territory of the state of New York, west of Albany. This limitation was considered a general one.

The case of Murray v. Vanderbilt, (39 Barb., 140) decided that a covenant by an ocean steamship Co., with another not to run its boats between the continents of North and South America, was void, since it prevented competition in commerce, and would increase the rates for transportation.

In the case of Beal v. Chase, (31 Mich. 490), Chase covenanted not to engage, directly or indirectly, "in the business of printing or publishing in the state of Michigan. This was held to be only a partial and therefore valid restraint.

In the case of Oregon, etc. Navigation Co. v. Winsor, (20 Wall.), a covenant by the purchaser of a steamship not to employ the ship for ten years in the waters of the state of California, was upheld.
It is to be noticed that the early cases consider a limitation which extends throughout the state, or the greater portion thereof, as a total restraint, while in the later cases, a different view is held. The judgment in the early cases, it is said, were founded upon the reasons that each state is an entire jurisdiction and can protect its citizens only within its borders, and does not know what benefits they may enjoy in other states; and it is a duty to see that the freedom of its citizens is not restrained from all its territory; that it is not for the interests of an independent state that its citizens be allowed to sell their industrial freedom for a small present gain, and thereby be compelled to remain idle with danger of becoming a burden to the state, or else to seek other trades or climes. Instead of considering each state as only one of many in the Union, in which the person would be left free to act, where he was restrained by contract from one state, Selden, J., declared it to be "repugnant to the general frame and policy of our government, to regard the Union in respect to our ordinary internal and domestic interest, as one consolidated nation. For these purposes, each state is a separate com-
munity, with separate and independent public interests."

Lawrence v. Kidder, supra. This view it may safely be said is no longer entertained. In Oregon, etc. Co. v. Winsor, supra Judge Bradley said that "this country is substantially one country, especially in all matters of trade and business."

Again, and later, the position of Selden, J., is denounced by Christianity, J., in Beal v. Chase, supra. It is asked by the Judge if the necessary and probable consequence of a contract which binds a person not to engage in a particular business within the state, is to bring that person to idleness or immigration. In answer to this, he says, that in former times, it might have been so "but in this country, at this time, where merchants become manufacturers and lawyers farmers, and farmers tradees", simply because they believe that such changes will be for their advantage, and not because they receive a consideration. "Any rule of law, therefore, 'which should assume that one who for a consideration bargained not to follow his previous business, had thereby bound himself to idleness and penury, to the detriment of the state, would be a rule absurd in itself and contrary to general experience and observation." Nor does
the learned Judge consider it any objection to such a contract that it may possibly result in one party going beyond the state to engage anew in the business. The interests of a state he says are not so petty or exclusive and its policy so narrow and invidious that its rules are framed to keep people within the state, contrary to their inclination, or where it would be for their interests to go elsewhere.

From the last two cases cited, it is seen that a contract in restraint of trade may be reasonable and valid, even if the entire territory of a state is included in the restriction. Has the low-water mark of public policy forbearance been reached? This is best by an examination of the following cases: Diamond Match Co. v. Roeber (106 N.Y., 433); Rousillon v. Rousillon, (14 Ch.Div.351.); Leslie v. Lorillard, (110 N.Y., 519); and Watertown Thermometer Co., v. Poole, (51 Hun, 157)

In the first case the defendant, who was engaged in the manufacture in the state and sale throughout the states and territories, sold the manufactury and good will of the business, to the plaintiff, and covenanted not to engage in the manufacture or sale of friction matches for ninety-nine
years, except in Montana and Nevada. The restraint was held partial, reasonable, and valid. The opinion of the Court is given by Andrews, J., and the subject is carefully considered. "The tendency of recent adjudications", he says, "is marked in the direction of relaxing the rigor of the doctrine that all contracts in general restraint of trade are void, irrespective of special circumstances........When the restraint is general, but, at the same time, co-extensive only with the interests to be protected, and with the benefit meant to be conferred, there seems to be no good reason why, as between the parties, the contract is not as reasonable as when the restraint is partial, and there is a corresponding partial restraint." He also refutes the doctrine that a general restraint of trade depends on state lines. "The boundaries of the state," he says, "are not those of trade and commerce, and business is restrained within no such limit. Some trades and employments are from their nature, local, but manufacturing industries, in general, are not. It is only reasonable, that when a person has by industry and enterprise built up a business which extends over a continent, that he be allowed to accompany the sale with a stipulation
for a restraint co-extensive with the business he sells. He may, thereby, obtain a better price. Such a person is in no more danger of becoming a burden upon the state than one who sells a business, local in its nature.

In the case of Rousillon v. Rousillon, the defendant, in obtaining employment as a traveller for a wine merchant agrees not to carry on the wine business for two years after leaving his employment. The business extends throughout England and Scotland. The agreement is valid. Fry, J., in this case doubted if there had ever been, a "hard and fast rule" as to how great a restraint would render a contract void, and he refused to adhere to those cases in which an unlimited prohibition was void without regard to the circumstances and nature of the business.

In Leslie v. Lorillard, the defendant, a corporation, agreed not to run or be interested in running steamships in opposition to the plaintiff's line upon their route. The contract is valid. In deciding whether the contract is contrary to public policy and void, because in restraint of competition, and tending to create an monopoly, Gray, J., said "the tendency of modern thought and of the decisions, how-
over, has been no longer to uphold in its strictness, the
doctrine which formerly prevailed in respect of agreements
in restraint of trade." The rule became relaxed. "This
change was gradual and may be considered perhaps as due,
mainly to the growth and spread of industrial activities,
of the world, and to enlarged commercial facilities, which
render such agreements less dangerous, as tending to create
monopolies."

In the case of Watertown Thermometer Co. v. Poole, the
defendant, for a consideration, assigned, the Trade-Mark
used in the manufacture of thermometers and storm-glasses,
and also agreed, "not to engage in the manufacture of
thermometers or storm-glasses, at any place within the
United States, at any time within the period of ten years.
This restraint, though general, did not invalidate the con-
tract, for the learned Judge, who wrote the opinion, con-
sidered it only, "co-extensive only, with the interests to
be protected, and with the benefit meant to be conferred by
the agreement."
What then is the true rule at present? We have seen that a person may restrain himself from exercising a business anywhere within the United States, if it is reasonable, and co-extensive with the business sold, and the tineerests to be protected. The old rule can no longer be given as sound. The reasons which supported it are much less forcible now than when Mitchell v. Reynolds was decided. "Steam and electricity have, for the purpose of trade and commerce, almost annihilated distance, and the whole world is now a mart for the distribution of the products of industry. The great diffusion of wealth and the restless activity of mankind, striving to better their condition, has greatly enlarged the field of human enterprise, and created a vast number of new industries, which give scope to ingenuity and employment for capital and labor." (Diamond Match Co. v. Roeber, supra).

It is no longer feared that the public will suffer from want of competition, but rather from over-competition. It is true that when the contract prevents the vendor from carrying on the particular trade, it deprives the community of any benefit it might derive from his entering into competi-
tion. But the business is open to all others, and if it is profitable, capital will be at hand to enter it.

Neither do the contracts create monopolies "for they confer no exclusive privileges."

The law favors the greatest freedom to contract which is consistent with the interest of the individual and the public. It is contrary to this rule and absurd to hold a contract void, made in the sale of an extensive business, and with the good will of the same, and accompanied with a stipulation not to engage in competition, with the vendee, because the vendor, would be compelled to change his business. Such a rule would often prevent a profitable disposition of property and business.

It may therefore be stated that at the present time a contract will be upheld if reasonable and co-extensive only with the subject matter of the contract to be protected and that, too, although its operation extend to every foot of ground in the United States, provided that, thereby, the maker is not compelled to leave the country.

Carl Jay Seymour.