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Restraint of Trade in North Carolina

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RESTRAINT OF TRADE IN NORTH CAROLINA

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PART I

Restraint of Trade is an expression loosely used concerning a wide range of business arrangements from giant trusts and combinations down to the simple covenants of small merchants not to compete with those who buy them out.[1]

The legality of these various arrangements has frequently been called in question and has often been a matter of great public concern, especially where the effect of the arrangement is either to force down the price paid to the producer of farm and other elemental products or to advance the cost of staples to the consumer.[2]

It is proposed here to examine the state of the North Carolina law on certain types of restraints against a background of selected cases elsewhere.

CONTRACTS NOT TO COMPETE

Superficially it would seem that a man might as well bind himself for a good consideration not to sell cigarettes as not to smoke them and that he might do so without regard to whether or not he had previously dealt in those articles.

But in the formative period of the law when a man could change occupations only with difficulty and when, if he changed towns, he was pointed at suspiciously by the new-village dames and sniffed at suspiciously by the new-village dogs, there was a decided policy against upholding a covenant by worker or tradesman not to engage in his accustomed business in his home town even if he was paid something for it. The aptest and most cited illustration of that policy on the bench is the tirade of a fifteenth century judge against a plaintiff seeking to recover the penalty for breach of a covenant binding a dyer not to practice his craft in one town for six months.[3] Out of that antagonistic attitude toward all restraint on trade later

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[1] See Holmes, J., dissenting in Northern Securities Co. v. U. S., 193 U. S. 197, 404, 24 Sup. Ct. 436, 469 (1904) distinguishing "contracts in restraint of trade" from "combinations in restraint of trade" at Common Law.

[2] See Clark, C. J., in Morehead City Sea Food Co., Inc. v. Way, 169 N. C. 679, 86 S. E. 603 (1915)—coast fisheries.

[3] Hull, J., in Anonymous Case, Y. B. Hen. V, fol. 5, pl. 26 (1415). And see The Blacksmith's Case, 2 Leo. 210 (1587, C. P.).

grew the modified rule that, while restraining contracts were *prima facie* bad, it might be shown that they were reasonable, and, if so, they were enforceable. This rule has been otherwise phrased as follows: that the restraint must be "such only as to afford a fair protection to the interests of the party in favour of whom it is given, and not so large as to interfere with the interests of the public."[4]

The types of restraint to which the latter part of the rule is directed—those which are thought to violate the public interest—are chiefly of these sorts:

(1) Creation of monopoly.

(2) Disabling public utilities from serving the public.

(3) Buying off of threatened competition.

Creating Monopoly

Monopolies were opposed to the common law and have been condemned in the United States by statutes both state and federal.[5] It can of course be no justification for such organizations that they are created by means of an otherwise justifiable agreement not to compete instead of by pool, trust, or conspiracy. The detailed consideration of that matter is reserved for a separate topic, but it is here noted that the question of monopolistic control was involved in several of the North Carolina cases considered in this paper and that in one or

[4] Language of Tindal, C. J., in Horner v. Graves, 7 Bing. 735 (1831, C. P.); Merriman v. Cover, 104 Va. 428, 57 S. E. 817, 819 (1905); Mar-Hof Co. v. Rosenbacher, 176 N. C. 330, 97 S. E. 169 (1918). The doctrine which also prevailed in England for some time that the restraint to be valid must not be general, i.e., cover the entire jurisdiction [Mitchell v. Reynolds, *infra*, note 9, McAuliffe v. Vaughan, 135 Ga. 852, 70 S. E. 322, 324 (1911); Brown v. Williams, 144 S. E. 256 (Ga. 1928), under code; cf. Fry, J., in Rousillon v. Rousillon, 14 Ch. Div. 351, 366 (1880)] will not be discussed herein since aside from some recitals of the rule in that form, [Mar-Hof Co. v. Rosenbacher, *supra;* Shute v. Heath, 131 N. C. 281, 42 S. E. 704 (1902)] the doctrine seems never to have had any place in North Carolina law, [see Cowan v. Fairbrother, 118 N. C. 406, 24 S. E. 212 (1896); Morehead City Case, *supra* note 2]. Though it has been tenaciously adhered to in some American jurisdictions since its abandonment in England. See, e.g., Lufkin Rule Co. v. Fringelli, 57 Ohio St. 596, 49 N. E. 1030 (1898). The reason which might justify the rule in England, i.e., that a covenantor would have to expatriate himself in order to pursue his accustomed line of business, has little pertinance when applied to people in the various states of this country. But see Taylor v. Blanchard, 13 Allen 370, 375 (Mass., 1866). Occasionally when a covenant is unlimited as to space only because of an apparent oversight of the parties, a liberal court will uphold the covenant as far as it would have been clearly proper to stipulate. See illiterate unlimited covenant in Fox v. Barbee, 146 Pac. 364 (Kans., 1915).

[5] C. S. N. C. §§2559-2574; U. S. C. A. Tit. 15, §1.

two instances the final result depended more upon that factor than on the question of how the restraint affected the covenantor.[6]

Restraining Public Utilities

It has been recognized in North Carolina as elsewhere that a covenant by a public utility not to engage in the business for which it has been established is unenforceable.[7] Some effort was made by counsel to use this doctrine in a later case to overthrow the covenant of a livery stable proprietor who sold out and then competed contrary to his agreement, the argument apparently being that the livery business was of a public character like a street car line or bus system. The court missed the point entirely and so ruled against the construction. But the argument was unsound anyway since, first, the livery in question was probably not a public service business and, second, if it were such, it would not be one of the type which owes any franchise duty to the public to continue operations and a self-imposed restraint would therefore not run afoul of the public interest.[8]

Forestalling Competition

Buying off threatened competition, that is, paying a man not to engage in a business in which he is not then engaged, has always been regarded as illegal.[9] Whether under changed economic conditions there is any need for this check on freedom of contract or not has sometimes been doubted. Perhaps less economic loss to a community

[6] In Shute v. Shute, 176 N. C. 462, 97 S. E. 392, 393 (1918), point is made of the fact that the parties "ginned at least 80% of the cotton ginned in Monroe."

[7] Cowan v. Fairbrother, *supra* note 4; Nat. Benefit Co. v. Union Hospital Co., 45 Minn. 272, 47 N. W. 806 (1891).

[8] So held as to hotels in Wittenberg v. Mollyneaux, 60 Nebr. 583, 83 N. W. 842 (1900); but cf. Clemons v. Meadows, 123 Ky. 178, 94 S. W. 13 (1906). Ginning—the business with which the case of Shute v. Shute, *supra* note 6, was concerned seems to be a public utility in respect of rate regulation in some states; see e.g., II Comp. Stat. Okla. (1921), §§3712 and 1114, but not in respect of compulsory service.

[9] "All contracts, where there is a bare restraint of trade and no more, must be void." Mitchell v. Reynolds, 1 P. Wms. 181, 192 (1711, K. B.); Gross-Kelly Co. v. Bibo, 19 N. M. 495, 145 Pac. 480 (1914). There is language in the pleadings reported in two cases suggesting otherwise but the cases do not bear out the language. Pierce v. Fuller, 8 Mass. 223, 5 Am. Dec. 102 (1811); Leslie v. Lorillard, 110 N. Y. 519, 18 N. E. 363 (1888). A bare covenant to retire from business without a sale of good will to the covenantee has likewise been treated as unenforceable. Shute v. Shute, *supra* note 6. But in the language of Mr. Justice Holmes, "The covenant makes the sale." Cinti. P., B. S. & P. Pkt. Co. v. Bay, 200 U. S. 179, 26 Sup. Ct. 208 (1906). See also Brett v. Ebel, 51 N. Y. Supp. 593, 29 App. Div. 256 (1898).

would come of letting one dry goods merchant buy off a newcomer before he opened a competing shop than of forcing the former to wait till the competitor had put his money into a lease, fixtures and a stock which might become useless, and had hired people who might then be suddenly thrown out of work when the deal was finally made. There is something to be said for keeping business running smoothly rather than legally contributing to unnecessary expansions and unsettling contractions. The dangers of extortion and other bogeys loom up, however, when any such views are expressed, and in the absence of a direct pronouncement by North Carolina authority, the law is probably to be understood as orthodox in this particular.

But if the covenant is an incident to some other valid transaction, the law may not be so hostile. The various kinds of contracts in chief to which the covenant in restraint of trade may attach itself for support will now be considered.

Covenants Accompanying the Sale of a Business or Profession

If the law were what it once seemed to be, that no one could covenant himself out of any trade for any time or place or reason,[10] it is evident that the owner of a small business might be embarrassed about selling it at a fair going-concern price, simply because he might later without legal restraint return to the neighborhood and regain his old customers.[11] And the better the man and the more successful the business, the worse off he would be as to a sale on that very account. In the light of these facts, the dismal pictures of idle tradesmen and their mendicant offspring which the courts had painted in early cases gave way to statements of the doctrine that a man might guarantee not thereafter to injure what he sold and that since the business consisted not only of goods but of good will he might covenant not to do acts which would injure the buyer's enjoyment of the good will.[12] A seller's covenant not to compete, assuming no public

[10] "This condition is against law, to prohibit or restrain any to use a lawful trade at any time or in any place." Colgate v. Bachelor, Cro. Eliz. 872 (1596), (K. B.)

[11] Kramer v. Old, 119 N. C. 1, 25 S. E. 813 (1896); Trenton Potteries v. Olyphant, 58 N. J. Eq. 307, 43 Atl. 723 (1899).

[12] Some courts have indicated a willingness to imply a covenant where none was given in such cases. Dwight v. Hamilton, 113 Mass. 175, 178 (1873); Hall v. Western Steel & Iron Wks., 227 Fed. 588, 594 (C. C. A. 7, 1915), per Baker, Cir. J. And there is much business justice in such a view since the buyer has very little to show for his expense in purchasing "good will" if he must try to sustain it against the competition of the person with whom the

interest to be involved as by the creation of a monopoly, may therefore lawfully be made an incident of the sale of a going business. The law is thoroughly established today on that point in North Carolina[13] and elsewhere.[14] And a similar rule obtains in the professions[15] though it has not had universal acceptance.[16] But since the theory of this rule was protection of the good will transferred, it followed that a covenant restraining the seller in a larger area than that covered by his good will was not warranted and would be unreasonable and illegal.

Extent of Good Will Conveyed

What then determines the extent of the good will which is being protected? Geographically speaking, a business has good will in the places where it has made sales. A few sporadic sales, however, out at a considerable distance beyond the normal sales territory ought not to justify the inclusion of that area and all the space between. The question is eminently practical. In a business sense what was

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good will is associated in the mind of the buying public. But the general rule is contra, subject only to the very ineffective restriction on the seller against singling out and soliciting old customers directly. Trego v. Hunt, L. R. [1896] App. Cas. 7 (H. of L.); Von Bremen v. Mac Monnies, 200 N. Y. 41, 93 N. E. 186 (1910); Meyers v. Kalamazoo Buggy Co., 54 Mich. 215, 20 N. W. 545, 548 (1884); Faust v. Rohr, 166 N. C. 187, 189, 81 S. E. 1096, 1099 (1914), *semble.* And where the contract of sale is in writing parole evidence has been held inadmissible to establish an accompanying covenant not to compete. Diller v. Schindler, 263 Pac. 277 (Cal. App., 1928); though seemingly it would be to explain an ambiguity. Faust v. Rohr, *supra,* and in the absence of a written contract in chief there is no requirement of common law that the agreement not to compete be in writing. Wooten v. Harris, 153 N. C. 43, 68 S. E. 898 (1910). Since 1913, however, there has been such a requirement by statute in North Carolina. C. S. §2562.

[13] Kramer v. Old, *supra* note 11. C. S. §2563, par. 6, dealing with certain illegal restraints adds the following proviso:

"That nothing herein shall be construed to prevent a person, firm or corporation from selling his or its business and good will to a competitor, and agreeing in writing not to enter the business in competition with the purchaser in a limited territory, as is now allowed under the common law: Provided, such agreement shall not violate the principles of the common law against trusts and shall not violate the provisions of this chapter."

Even before this proviso was added to the law, the court had interpreted the statute as not applicable to an ordinary sale-of-business covenant not to compete. Wooten v. Harris, 153 N. C. 43, 68 S. E. 898 (1910).

[14] Kochenrath v. Christman, 180 Ky. 799, 203 S. W. 738 (1918); Mapes v. Metcalf, 10 N. D. 601, 88 N. W. 713 (1901) and citations.

[15] Cowan v. Fairbrother, *supra* note 4, *semble;* Hauser v. Harding, 126 N. C. 295, 35 S. E. 586 (1900); Ryan v. Hamilton, 205 Ill. 191, 68 N. E. 781 (1903); McClurg's Appeal, 58 Pa. 51 (1868), cited with approval in Kramer v. Old, *supra* note 11.

[16] See Rakestraw v. Lanier, 104 Ga. 188, 30 S. E. 735 (1898), where restraint was unlimited as to time.

the extent of the seller's sales territory? Over what area has he created an appreciable inclination on the part of the public to patronize him? This question suggests that good will created by advertising in areas not yet sold may be pertinent and there is excellent authority for that view,[17] though the question does not seem to have been presented in this state. But mere general favorable reputation, unsupported by actual business transactions, does not supply the element of good will.[18] Otherwise such stores as those of Marshall Field & Co. and John Wanamaker would have worldwide good will.[19]

One other point in connection with the geographic extent of good will seems frequently to be overlooked. Good will necessarily arises from contact with the public; hence it is most often an asset of the sales force.[20] A manufacturer who sells out occasionally gives a contract not again to *manufacture* similar wares in the area covered by the good will he has sold.[21] This covenant is not exactly phrased. What is desired to prevent is sales in the territory delineated and not the manufacture in that area of goods for sale in some distant new market—a matter of no proper concern to the covenantee. Some point was made of this distinction in a famous Massachusetts case which raised the issue, so to speak, the other way around. Here a manufacturer who had contracted his entire output to one concern and who in consequence was not known to the public, sold his business and gave a covenant which restrained him from manufacturing *and selling*. Of course such a manufacturer would have a sort of inchoate good will with the trade which would become operative

[17] Hall v. Western, *supra* note 12. See also Western Oil Ref'g. Co. v. Jones, 27 F. (2d) 205 (C. C. A. 6, 1928), a trade name case in which it was said: "Those limitations, in our opinion, do not exclude territory which may be reasonably expected to be within the normal expansions of the business." Cf. Nat. Gro. Co. v. Nat. Stores Corp., 123 Atl. 740 (N. J. Ch., 1924), also a trade name case.

[18] See article on Good Will by Prof. Floyd A. Wright, to appear in (May, 1929) 23 ILL. L. REV. ———.

[19] There can of course be worldwide good will in a business of international character. Nordenfelt v. Maxim Nordenfelt Guns & Amm. Co., Ltd. [1894], A. C. 535 (Eng. H. of L.).

[20] It may be associated with purchases also. In the Morehead City case, supra note 2, the middlemen in the fisheries industry would have good will of both types through purchases from the fishermen and sales to the trade. But either way, dealing with the public is necessary.

[21] See covenant quoted in Trenton Potteries v. Olyphant, *supra* note 11; also Western Woodenware Assn. v. Starkey, 84 Mich. 76, 47 N. W. 604 (1890). Literally the restraint in Cowan v. Fairbrother, *supra* note 4, would prevent the seller of a newspaper from doing the *printing* for a magazine for circulation in other parts of the United States, but its obvious purpose was otherwise made clear.

when his then existing entire-output contract terminated. He might even have good will indirectly with the public if his selling agency marketed the product under his, the manufacturer's name. But the court treated him as a seller of plant only and not of a business and good will and accordingly refused on this ground, among others, to uphold the restraint.[22]

The next proposition is that the restraint must not cover lines of business other than those sold, since the seller's good will measures the restraint. A local shoe dealer in Chapel Hill, conveying to a clothing store, can legally covenant to restraint himself from selling shoes, but not clothing or groceries. His good will no more extends to these matters than it extends geographically to Kalamazoo. There would seem to be a good deal of sound sense, however, in relaxing this rule slightly where the restraining covenant covers in addition only closely related lines such as perhaps the public might have expected to obtain from the business whose good will was transferred, and there is an American decision of high authority for doing so.[23]

In view of the observations first made, however, a covenant restraining the seller "from competing with the buyer" is likely to be held unreasonable inasmuch as the buyer may be a dealer already engaged in much broader operations than the seller or he may expand into new lines and territory during the period of the covenant and the seller would in consequence be prevented from engaging in business of a character or in a location where he had no previous good will.[24] As to these restraints the deal would amount to buying off

[22] Gamewell Fire-Alarm Tel. Co. v. Crane, 160 Mass. 50, 35 N. E. 98 (1893).

[23] Holmes, J., in Anchor Elec. Co. v. Hawkes, 178 Mass. 101, 50 N. E. 509, 511 (1898) where the selling companies consolidated into a new company whose type of business was slightly broader than that of the separate companies. In Cowan v. Fairbrother, *supra* note 4, the seller transferred a newspaper business. The covenant given was that he "shall not edit, print, or conduct a newspaper or magazine . . . in the state," but no point was made of this. Likewise in Bradshaw v. Millikin where the covenant given by a retiring barber was not to engage "in the same or *any similar business*" in Hamlet, N. C. Might this language not cover a beauty or hairdressing parlor? Again resorting to the analogy of trade name protection (note 17, *supra*) and its broadening policy first along closely related lines, see Aunt Jemima Mills Co. v. Rigney & Co., 247 F. 407, 159 C. C. A. 461 (2d Cir., 1917), certiorari denied, 245 U. S. 672, 38 Sup. Ct. 222 (1917); (1927) 75 U. PA. L. REV. 197; Goble, *Where and What a Trade Mark Protects*, 22 ILL. L. R. 379 (1927).

[24] See Samuel Stores, Inc., v. Abrams, 108 Atl. 541 (Conn., 1919), although this was an employer-employee contract as to which the rules are more strict. "Appellant contends that such contracts were reasonably required to protect it, not only in the areas in which the business it purchased of respondents had been carried on, but also in other states to which it might extend that business. But this contention I deem to be inadmissible." Magie, C. J., in Trenton Potteries Case, *supra* note 11.

his threatened competition, the vice of which has already been mentioned.

Finally, the question of whether a restraining covenant is reasonable or not is held to be one of law for the court[25] and under that rule the Supreme Court of North Carolina has passed upon the validity of a large number of different agreements which will be summarized in the margin.[26]

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[25] Wiley v. Baumgardner, 97 Ind. 66 (1884); Shute v. Heath, 131 N. C. 281, 42 S. E. 704 (1902). Since most of the complaints are for equitable relief, there is little occasion to try out the mechanics of this rule in actual practice and no opportunity to see whether all it means is that the court will leave it to the jury to say whether the restraint provided did in fact reach spacially beyond the good will area of the business. New Jersey has phrased the rule differently. "If a contract having the scope suggested does not impose an unreasonable restraint upon trade, it would seem that the question whether the area which was embraced in a given contract was greater than was required for the full protection of the vendee must ordinarily be one of fact to be determined by the jury." Fleckenstein Bros. v. Fleckenstein, 76 N. J. Law 613, 616, 71 Atl. 265, 267 (1908). It is believed, however, that the two apparently differing rules will work out to the same result in actual operation.

[26] In the following cases the restraint was limited to one town and was treated as valid by the court: Baumgarten v. Broadaway, 77 N. C. 8 (1877), photography, Charlotte—10 years; Baker v. Cordon, 86 N. C. 116 (1882), drugs, Tarboro—while plaintiff is in the business; Jefferson Reeves & Co. v. Sprague, 114 N. C. 647, 19 S. E. 707 (1894), drugs, Waynesville—3 years; King v. Fountain, 126 N. C. 196, 35 S. E. 427 (1900), livery, Greenville—3 years; Disosway v. Edwards, 134 N. C. 254, 46 S. E. 501 (1904), sale of liquor, New Bern—20 years; Anders v. Gardner, 151 N. C. 604, 66 S. E. 665 (1910), livery, Gastonia—no time limit; Faust v. Rohr, 166 N. C. 187, 81 S. E. 1096 (1914), barber, Monroe—so long as plaintiff carried on business; Finch Bros. v. Michael, 167 N. C. 322, 83 S. E. 458 (1914), grocery, Lexington—1½ years; Bradshaw v. Millikin, 173 N. C. 432, 92 S. E. 161 (1917), barber, Hamlet—2 years. In the following cases the restraint was over a broader area. The holding is indicated: Kramer v. Old, 119 N. C. 1, 25 S. E. 813 (1896), milling, "in the vicinity of Elizabeth City"—no time limit, valid and restraining order proper over whole named territory; Wooten v. Harris, 153 N. C. 43, 68 S. E. 898 (1910), merchandising, "in the town of Falkland or near enough there to interfere with plaintiff's business"—no time limit, held good as to Falkland at least, that being all that was necessary to enjoin defendant; Hauser v. Harding, 126 N. C. 295, 35 S. E. 586 (1900), physician, "territory surrounding Yadkinville"—forever, good as to Yadkinville, remaining area too indefinite, not too broad; Shute v. Shute, 176 N. C. 462, 97 S. E. 392 (1918), ginning, part of Monroe County—10 years, invalid, declared by Clark, C. J., to be too large and too long, though case seems to have been decided on other grounds, see note 6, *supra;* Cowan v. Fairbrother, 118 N. C. 406, 24 S. E. 212 (1896), newspaper, State of N. C. as to one defendant, Durham County as to the other—10 years, held good; Morehead City Sea Food Co. v. Way, 169 N. C. 679, 86 S. E. 603 (1915), fish buying at coast, 100 miles of Morehead City—10 years, valid, Clark, C. J., dissenting on account of "great space" but chiefly on the ground that a monopoly was created. See also Shute v. Heath, note 27 *infra,* and Teague v. Schaub, note 29 *infra.* In the above summary of cases both the time and space limitations are stated. The time limitations are unimportant in North Carolina and covenants which are unlimited in this particular will be upheld for the lifetime of the covenantor. Shute v. Heath, note 27 *infra.* In only one case does the court seem to suggest that any period of time would be

RESTRAINTS OF INDEFINITE EXTENT

A covenant restraining the seller "from competing with the buyer" was shown above to be open to the objection of being too extensive; hence unreasonable. It might be open to another charge, that of being too indefinite to secure judicial approval, and such was the decision in North Carolina where the agreement was not again to engage in the business sold "in any territory now occupied by them or from which they secure their patronage, so as to compete with them or injure their business. . . ."[27] And to its condemnation of this limitation as incapable of ascertainment, the court added the unnecessarily strict requirement "that the limitation as to space shall be so definitely set out in the contract as that the bounds must be determined by the same rules as apply to the description of real estate in deeds."

The court distinguished *Kramer v. Old*,[28] wherein the limitation upheld was "in or in the vicinity of Elizabeth City," on the ground that the point had not there been raised.

The question of indefiniteness had been presented in one previous case by the language of a covenant not to practice medicine "in the territory sorrounding Yadkinville," which was held inoperative on that ground as to all but the named town.[29]

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so long as to affect the validity of a restraining covenant. Shute v. Shute, *supra*. And this was not the principal reason, nor even seemingly an important one, for the adverse decision in that case. In some other jurisdictions, however, the time element is considered, and if regarded as too extensive, becomes the deciding factor against the covenant. See note 16, *supra*.

[27] Shute v. Heath, 131 N. C. 281, 42 S. E. 704 (1902); cf. Boggs v. Friend, 77 W. Va. 531, 87 S. E. 873 (1916).

[28] *Supra* note 11.

[29] Hauser v. Harding, *supra* note 26. In Teague v. Schaub, 133 N. C. 458, 45 S. E. 762 (1903), the parties being partners in the practice of medicine "at Roxboro and the territory adjacent thereto" agreed *inter alia* that at a fixed date *S* would locate elsewhere "if the field is not larger than now." The trial judge being of opinion that "the contract . . . was indefinite as to territory and could not be aided by extrinsic evidence," gave judgment for defendant who had not located elsewhere as agreed. Held, no error. The following arguments could be advanced: (1) That "territory adjacent" is too indefinite. This contention is sustainable. Hauser v. Harding, *supra*. (2) That "Roxboro" is too indefinite, if as contended, it is an unincorporated town. (See dissenting opinion, 133 N. C. 465, 45 S. E. 764.) This would be an incomprehensible refinement. (3) That the condition on which he was to depart, i.e., "if the field is not larger than now," is too indefinite. This seems to be the real ground of the decision in the Supreme Court, though not the ground of the judgment at trial. Cf. Ryan v. Hamilton, *supra* note 15, wherein defendant agreed not to reënter practice "unless forced to do so by some unforseen circumstances."

SEVERABILITY

Assume a covenant clearly covering too broad an area but describing the territory in sections thus: "in the city or county of Durham or elsewhere in North Carolina." How will such a phrase be dealt with when the good will extends only to Durham? There are two obvious arguments for holding it bad entirely, i.e., that to do otherwise is to make a contract for the parties, and also to invite excessively large restraints and put the courts to a determination of the most that would be good on the fact disclosed. The answers, be they sufficient or not, are that the judically made (or modified) contract approximates the one made by the parties and is certainly more satisfactory to one whose protection is in question than entire loss of protection would be, and the other party ought not to object to a lawful restraint which is less than he agreed upon voluntarily and for which he has been paid.[30]

North Carolina seems distinctly to have adopted this doctrine and even extended it to a case where the language was not clearly severable—"the territory surrounding Yadkinville" being held good as to Yadkinville.[31] Here is the insurance policy for the uncertain lawyer. Can he safely stipulate for a little added protection for his client? Let him subdivide the fringes with care and the doctrine of severability comes in to produce a variable limit adjustable to the views of any future court.

CONTRACTS APPORTIONING TRADE

Assuming a contract in restraint of trade to be properly limited in all the respects mentioned above, is it the worse because it effects an apportionment of certain business between the two parties. Thus, suppose *A* and *B* each operates a grocery and meat market in Durham and *A* conveys to *B* his meat business in exchange for *B's* grocery business, each taking from the other a properly limited covenant not to engage further in the line of business he had sold. The effect is that the grocery and meat business which they had together done in Durham is apportioned between them so that each is specialized in his future trade. Should that result make the covenants unenforce-

[30] For examples of opposite and technical extremes in opinion on this subject, Cf. Trenton Potteries Case, *supra* note 11, with More v. Bonnett, 40 Cal. 251 (1870). See also 2 EDDY, COMBINATIONS, §789.

[31] Hauser v. Harding, *supra* note 26; accord Wooten v. Harris, *supra* note 26. In both of these cases the covenant was severed so as to drop an indefinite excess area, but nothing appears properly to turn on that fact.

able? Certainly the covenants are reasonable as to the parties themselves. It is here that a different element is introduced, *i.e.*, reasonableness as to the public welfare, which has heretofore been mentioned briefly. In the case of a single sale to a stranger the same number of shops are usually continued in operation. The present device reduces the number by one in each class of trade. But in the absence of creating a monopoly, there seems to be no public harm from that fact, and so certain courts seem to have viewed the matter.[32] The same result would lawfully follow if one shop bought out another, consolidated the stocks under one roof and then closed up the vacant establishment.[33] But there is language in one North Carolina case and a decision in another to be reckoned with, at least where necessaries of life are concerned. Although the facts are not entirely disclosed in the first of these,[34] it appears that two brokers dealing competitively in flour and meats entered into an agreement whereby one relinquished the flour business and the other did likewise as to his trade in meats in a designated area. What this obviously amounts to is a sale by each of a portion of his business to the other. As an apportionment of trade, it is hard to see why this arrangement is unreasonable. True the court speaks of the deal as if it enabled the remaining party to charge the public his own price for the product of which he was given the sale, but there seems to have been no evidence that there were not plenty of other dealers, either selling that territory or willing to enter if the price were raised,[35] and in the absence of evidence that a monopoly is created, or likely to result from such an exchange, the public advantage may lie in specialization and its resulting economies, and the public interest may be best served by seeing a square deal between the parties. The real illegality of the reciprocal covenants under consideration and the sound ground for the decision of the court was not the apportionment but the fact that these brokers were agents of certain competitive millers and

[32] Wickens v. Evans, 3 Younge & J. 318 (Exch., 1829), apportionment of territory; Nat. Benefit Co. v. Union Hosp. Co., *supra* note 7, apportionment of lines of business.

[33] U. S. Chem. Co. v. Prov. Chem. Co., 64 Fed. 946 (E. D. Mo., 1894). Cf. Western Woodenware Assn. v. Starkey, 84 Mich. 76, 47 N. W. 604 (1890), *contra* because of some evidence of monopoly and also in support of home industries.

[34] Culp v. Love, 127 N. C. 457, 37 S. E. 476 (1900).

[35] See remark of Faircloth, C. J., in King v. Fountain, *supra* note 26, "The restriction applies to one individual only, and it is quite probable that, if the demands of that place require more extensive livery business, some other enterprising citizen will supply the demand, especially if it be profitable."

their secret deal between themselves constitutes a shameless fraud on the principal of one or both. Without resort to any question of restraint of trade or monopoly, therefore, the court could quite properly have refused to enforce such an agreement for one of the dishonest parties to it. It is true that apportionment cases require perhaps closer scrutiny than the ordinary type as they are more likely to result in monopoly, but where such is not shown to be the result, it would seem that they are well governed by the ordinary rules regarding contracts not to compete.

The other North Carolina case was as follows: Two brothers, each apparently operating a cotton ginning plant in Monroe, entered into reciprocal agreements substantially on these terms. *A* sold his plant to *B* and agreed not to operate thereafter for ten years in the part of the county south of Bear Skin Creek. *B*, instead of selling his plant in turn to *A*, agreed to dismantle and remove it and not to operate for a like period in the part of the county north of the creek. This arrangement apportions the territory between them. Suit was upon the second part of the contract to enjoin the erection by *B* of a new gin, contrary to his promise. It was held invalid.[36] If the first only of these agreements were considered, it would appear to be a rather narrowly limited restraint accompanying a sale of business.[37] Though good will was not specifically mentioned, it would seem to be properly regarded as transferred since the seller's agreement to withdraw and refrain from competition would leave the buyer the benefit of the seller's customers so far as he could get and keep them. In the language already quoted from Mr. Justice Holmes, "The covenant makes the sale."[38] Under the ordinary rules heretofore considered this single restraint probably would be held valid.

Looking now at the other side of the deal, we find that *B* sold no plant or tangible property to *A*, but closed it down for *A's* benefit and added a covenant that he would not for ten years engage in the business in a designated part of the county. An agreement to relinquish business in favor of another is not the less a transfer of the business because no property is delivered to the buyer.[39] He may not want the plant. And, of course, he could buy the plant, business, and good

[36] Shute v. Shute, *supra* note 6.

[37] Although Clark, C. J., remarked that the territory was "unnecessarily large" and "the period of ten years was also excessive."

[38] *Supra* note 9.

[39] Rowe v. Toon, 185 Ia. 848, 169 N. W. 38 (1918); Brett v. Ebel, *supra* note 9. And see discussion in Mapes v. Metcalf, *supra* note 14.

will, take a restraining covenant and then dismantle the plant and put it up at auction so as to conduct the operations more efficiently at his other establishment. Unless then there is something about the business of ginning cotton to call for rules different from those applied to drug stores or the milling business, it would seem that this individual contract, with its moderate restraints as far as the parties are concerned, could also properly be sustained. Clark, C. J., intimated that there was a difference. He said, "This is clearly against public interest, which is that these ginning plants shall be multiplied according to the needs of the public and shall not be restricted in number by agreement between parties in that line of business." And further on, "A restriction as to territory which would be reasonable in regard to issuing a newspaper which draws from a large territory would not apply to the prohibition of the erection of ginning plants in which business it is burdensome to the public to haul seed cotton any great distance to be ginned."[40]

The unreasonableness he has in mind is clearly from a public point of view. If that public risk actually exists, it would seem to be equal ground for invalidating a ten-year, half-county restraining covenant accompanying the bona fide sale of a single cotton gin business. But that the court will carry its view thus far may well be doubted. And it may be that the court would sustain such a single sale and covenant even if the area of the restraint were increased to the whole county.[41] If so, it is difficult to see that the mere apportionment of the county between two threatens any more serious injury to the citizens of the state. One is tempted to think of this case in the words of Priest, District Judge, that "It is a nervous and alarmed imagination which sees in every transaction involving large exchange of properties a monster threatening public interests."[42] But there are too many elements in *Shute v. Shute* to permit of an accurate appraisal of the case as authority for the future.[43] It behooves counsel in the light of that decision, however, to recite specifically the transfer of business and good will and to avoid apportionment, especially terri-

[40] 176 N. C. at p. 464, 97 S. E. at p. 393.

[41] Compare "in the vicinity of Elizabeth City," sustained as to milling business in Kramer v. Old, *supra* note 11.

[42] U. S. Chem. Co. v. Prov. Chem. Co., *supra* note 33, at p. 950.

[43] (1) No sale of business, mere agreement to quit, (2) no sale of property, (3) no sale of good will, (4) business of special public interest; so restraints must be specially limited. Cf. notes 8 and 9, *supra,* (5) monopoly—see note 6, *supra,* (6) division of territory.

torial apportionment wherever possible, for, whatever the argument, there can be no question that divisions of territory are not favored by the judges.

Covenants Taken When Seller Is Corporation

In this class of cases, so far as the selling corporation is concerned, the rules are the same as those discussed above for individual sellers except that the courts view them with more indifference since an idle corporation does not lounge on a park bench, talk overthrow of the existing order, and leave at home a brood of wailing children suffering because daddy is out of work. But correspondingly the taking of a covenant from the corporate entity not to detract from the good will "it" has conveyed may not be a very durable protection to the buyer since the personnel of the corporation may appear in new name and dress at any moment. A wise buyer therefore seeks to obtain the endorsement of the important individuals in the corporation on the restraining covenant as a bank does upon the corporate note. In strict legal theory since the corporation is regarded as a distinct person from its stockholders, it is difficult to see how this individual restraint can be sustained. The individual, according to this argument, is selling no good will and he should not be bound by a covenant protecting the good will owned and conveyed by a third person, the corporation. But the law would certainly be askew, particularly in a court of equity, if it followed any such strict theory based on doctrines of artificial persons, and while the cases anywhere are not numerous, they do for the most part seemingly allow the individual officers at least to be bound where they have signed the covenant.[44]

Covenants by Seller of Corporate Stock

Closely related to the type of case just discussed is that wherein an individual sells shares in a corporation and simultaneously gives his covenant not to compete with the corporation in which the buyer now becomes interested. It might be argued that the stockholder by selling his shares conveys no good will and so canont bind himself by a trade restraining covenant. That view follows the corporate entity

[44] Barrows v. McMurtry Mfg. Co., 54 Colo. 432, 131 Pac. 430 (1913); Feenaughty v. Beall, 178 Pac. 600 (Or., 1919), semble; 2 Page, Contracts, 1370, §778. And see Hall's Safe Co. v. Herring-Hall-Marvin Safe Co., 146 Fed. 37 (C. C. A. 6, 1906); Donnell v. Herring-Hall-Marvin Safe Co., 208 U. S. 267, 28 Sup. Ct. 288 (1908).

theory strictly—a stockholder owning one-third of the shares owns none of the corporate property or good will, though a partner owning a one-third interest in a like business admittedly would have a pro rata interest in the partnership good will.[45] This line of reasoning has the apparent virtue of preciseness, and yet a North Carolina case,[46] in accord with the overwhelming weight of authority elsewhere,[47] disregarded the view entirely and upheld a covenant by the owner of ten shares (one-third of the capital stock) in a livery company not to engage in the livery business locally after he had sold his interest to another. Would the same result have been reached in case of a covenant by the seller of, say, ten shares of Southern Public Utilities stock to protect the transportation business of its subsidiary, the Carolina Coach Co.? That may well be doubted, and the probable extent of the rule is suggested by this extreme comparison. A stockholder's covenant not to compete with the corporation whose stock he sells ought to be upheld only when he is the holder of a large, if not controlling, interest, or when he occupies some office which makes the corporation good will appreciably dependent on him personally. No case has been found in which this specific point was raised, but it is believed that the decisions throughout the country are consistent with the view expressed and that the rule of *Anders v. Gardner* will be so limited when occasion arises.

Assignability; Effect of Later Contract

Whatever may have once been the rule, it is now well settled that lawful contracts in restraint of trade may be assigned,[48] and it seems also to have been held in one North Carolina case, not too clear on its facts, that such a contract survives subsequent joint business transactions of the parties where the originally imposed restraint is not specifically made the subject of a new agreement.[49]

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[45] Bradford & Carson v. Montgomery Furn. Co., 92 S. W. 1104 (Tenn., 1906).

[46] Anders v. Gardner, *supra* note 26.

[47] Up-River Ice Co. v. Denler, 114 Mich. 296, 72 N. W. 157 (1897); Buckhout v. Witwer, 157 Mich. 406, 122 N. W. 184 (1909); Kronschnabel-Smith & Co. v. Kronschnabel, 87 Minn. 230, 91 N. W. 892 (1902); Farmers State Bk. v. Petersburg State Bk., 187 N. W. 117 (Nebr., 1922); Kradwell v. Thiesen, 131 Wis. 97, 111 N. W. 233 (1907). *Contra*, under Code, Chamberlain v. Augustine, 172 Cal. 285, 156 Pac. 479 (1916). And see Brunswick v. Grossman, *infra* note 64.

[48] Cowan v. Fairbrother, *supra* note 4; Anders v. Gardner, *supra* note 26. Up-River Ice Co. v. Denler, *supra* note 47.

[49] Faust v. Rohr, *supra* note 26. Cf. Hall Safe cases, *supra* note 44.

WHAT CONSTITUTES BREACH

When one has lawfully covenanted not to engage in a business in a certain community, such shams as reëstablishing the business in the name of the wife or of a son or a friend will, of course, be stricken down.[50] And to enter a competitor's service as manager has also been properly disapproved.[51] It ought also to follow that one could not hold any other position in which his personality would materially detract from the good will he had sold.[52]

But if the defendant takes up some menial employment with a competing company or even a less humble employment which does not bring him into relations with the public in such a way as to detract from the good will he previously sold, it would seem that he should not be restrained.[53] Something might turn on the express language of his covenant. If it provided not only against his engaging in but against his aiding or assisting the conduct of a similar business to the one he had sold, his slightest service for a competitor would seem literally to be prohibited. It is believed, however, that in so far as the language might seek to reach such a situation, it would be invalid as too extensive and that the courts should interpret it narrowly as they have seemed to do.

To take up another angle of the matter, what if defendant's sole breach is becoming interested in a corporation which competes within the forbidden area? The answer may turn on the question of what importance he occupies in the new corporation and the kind of interest he takes. A gentleman who had sold and retired to California and who bought a few shares in some large competing corporation solely for investment would not be competing either in strict legal

[50] Baker v. Cordon, *supra* note 26, after previous competition by defendant in his own name had been enjoined; King v. Fountain, *supra* note 26.

[51] Baker v. Cordon, *supra;* Jefferson v. Markert, 112 Ga. 498, 37 S. E. 758 (1900); and see Stephens v. Pahl, 23 Ohio N. P. (N. S.), 377 (Cinti. Super. Ct., 1921).

[52] Anders v. Gardner, *supra* note 26; Alcock v. Alcock, 267 Ill. 422, 108 N. E. 671 (1915); cf. dictum in Baker v. Cordon, *supra* note 26, that becoming drug clerk would not have violated the restraining order which had been issued in that case.

[53] See dictum cited in note 52, *supra;* Mitchell v. Nat. Window Cleaning Co., 155 Ga. 245, 116 S. E. 532 (1923); also series of lower court decisions in Ohio relating to express and moving, and window cleaning business. Schroeder v. Schultze, 16 Ohio C. C. (N. S.), 303 (1908); Queen City Window Cleaning Co. v. Davis, 37 Ohio Cir. 474 (1916); Lichtenstein v. Silverman, 28 O. C. A. 126 (1914). The covenant in Faust v. Rohr, *supra* note 26, in terms prohibited defendant from "concerning himself in . . . conducting the business of a barber, either as principal, agent *or servant.*"

or practical business understanding and would consequently not be violating his covenant in that manner. Neither, it seems, would he be appreciably aiding such competition within the meaning of a covenant including the extra provision already mentioned, that he would neither directly nor indirectly engage in, or aid, or assist in the conduct of such business; though it would seem literally within the provision (often included) not to become interested in any such business. If, however, he became one of the chief stockholders or a minor stockholder and an active official of the new concern, it is believed he should be restrained, and the authority in this state accords with this view. "It was, therefore, a violation of the contract . . . to take stock in or help to organize or manage a corporation formed to compete with plaintiff."[54] But merely selling goods to third party competitors and taking a mortgage back for security does not constitute a breach of a covenant not to enter the drug business.[55] And, somewhat more doubtfully, neither does lending money to a competitor.[56]

The case might very well be otherwise if the loan was the chief financial backing for a newly organized concern, but there is no such suggestion in the opinion.

RELIEF

Upon breach of the restraining covenant, the covenantee may have, first of all, his action at law for actual damages sustained. It requires no extended illustration to show that such relief is unsatisfactory. What with the necessity of proving not only that customers were lost to the plaintiff but that they were lost because of defendant's competition, and the further necessity of establishing what profit would have come from their custom, the action promises to cost more than it yields.[57]

If he has stipulated for liquidated damages, plaintiff may fare better. According to one North Carolina decision, plaintiff must show in such a case "that some actual loss has been sustained, and that the amount of the bond is not unreasonable."[58] A more recent

[54] Kramer v. Old, *supra* note 26.

[55] Reeves v. Sprague, *supra* note 26.

[56] Finch Bros. v. Michael, *supra* note 26; and see Stephens v. Pahl, *supra* note 51.

[57] Plaintiff who had bought a garage, with defendant's covenant not to set up in Reading for five years, put in evidence of a falling off of his business and specific proof of the loss of one job. Held, insufficient to warrant jury's finding damages to plaintiff of $781. Satz v. Lamar, 14 Berks Co. L. J. 113 (Pa. Com. Pl., 1921). And see Finch Bros. v. Michael, *supra* note 26.

[58] Disosway v. Edwards, *supra* note 26, which also states that the requirement of proof may be met by admitted allegations.

case, however, lays down the rule as follows: "It has been the policy of the courts to construe such an agreement as liquidated damages rather than as a penalty, in the absence of any evidence to show that the amount of damages claimed is unjust or oppressive, or that the amount claimed is disproportionate to the damages that would result from the breach."[59] At most, this distinction seems to be one of presumptions or burden of proof, and the real substantive test of the validity would seem to be, not whether the damages after breach total up to the approximate amount stipulated, but whether in prospect at the date the contract was made they looked as if they might.[60] It would probably be impossible, however, in the application of this test for the judge or jury to avoid being influenced by what damages appear actually to have been inflicted.

There remains finally equitable relief to consider. Legal relief by way of damages being recognized as inadequate because of the speculative character of future losses, the courts have consistently issued injunctions against the violation of proper restraining covenants.[61] It is the rule furthermore both in North Carolina and elsewhere that a provision for liquidated damages does not bar injunctive relief, unless the language clearly shows that the covenant is in the alternative: to abstain from competition or to pay the agreed sum as the price for the privilege of resuming business.[62] And it seems that plaintiff may have both the injunction and compensation for losses actually suffered to that date,[63] this dual remedy corresponding to the injunction and accounting in jurisdictions not under the code.

Finally, in a case where the buyer has paid in part by giving notes to the seller conditioned upon his not reëngaging in the business in a certain area, the buyer may obtain indirect relief for breach of the

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[59] Bradshaw v. Millikin, *supra* note 26; accord Pendleton v. Elizabeth City Light Co., 121 N. C. 20, 27 S. E. 1003 (1897), not a restraint of trade case.

[60] See 2 WILLISTON, CONTRACTS, §§777-779.

[61] Baumgarten, King, Cowan, Hauser and Faust cases, all in note 26, *supra*. See also discussion in Jolley v. Brady, 127 N. C. 142, 37 S. E. 153 (1900), restraining covenant but not one accompanying sale of a going business.

[62] Bradshaw v. Millikin, *supra* note 26, and citations. See Busk v. F. Wolf & Co., 143 Ga. 18, 84 S. E. 63 (1915).

[63] *Ibid.* This holding invites a further argument. Liquidated damages are intended to cover the whole period of a possible breach by the covenantor. An injunction granted cuts short the breach so that the stipulated damages should not be given. On the other hand the actual damages suffered to the date of the injunction are difficult to prove and this part of the relief is incomplete if not inadequate. But prompt action by the covenantee will keep this injury to a minimum and for all practical purposes it would seem that the Bradshaw Case is correctly decided on this point.

condition by resisting the payment of the notes—a proposition so obvious that it would not be mentioned except for a very interesting extension of it in one outside case which relieved the maker from paying purchase money notes where the payee had violated a covenant for an unlimited and hence otherwise unenforceable restraint.[64] This decision has possibilities even more attractive than injunctions and damages to the lawyer who wishes to include in his client's contract of purchase a restraining covenant broader than he fears will survive a judicial test.

[64] Brunswick v. Grossman, 217 Ill. App. 108 (1920).