EXCLUSIVE DISTRIBUTORSHIP AGREEMENTS IN THE PETROL INDUSTRY

EXCLUSIVE dealing agreements between oil companies and operators of filling stations, by which the garage owner agrees to sell only the petrol of a particular oil company, now cover about 95 per cent. of all retail petrol outlets. Although the exact terms of a " solus " agreement vary from company to company, the essential feature of solus trading consists of an undertaking by the retailer to sell a particular supplier's brand or brands of motor fuels exclusively, in consideration of a solus rebate to be allowed by the supplier on all the motor fuels purchased (" the tying covenant "). Such agreements also provide for some measure of support to be given to the products of the petrol companies other than motor fuels, particularly lubricating oils. Invariably, the retailer also agrees that he will procure the acceptance of existing solus obligations by a purchaser on the sale or transfer of his business (" the continuity covenant "), and that in some cases the retailer will give the petrol company the first refusal to purchase. All petrol companies further stipulate that the retailer must keep open at reasonable hours and provide an efficient service (" the compulsory trading covenant ").

The solus system of marketing has recently been considered by both the Monopolies Commission and the Court of Appeal. The Monopolies Commission, which reported in July 1965, came to the conclusion that the solus system, in principle, does not operate against the public interest.[1] The three principal reasons for this conclusion were first, that the solus trading system reduces delivery costs for petrol, because oil companies can deliver to a smaller number of petrol stations, and make deliveries of a greater average size than would be the case under multi-brand trading. Secondly, that the financial assistance provided by the petrol companies had enabled garage owners to improve their sites,[2] and finally, that the solus system had neither led to an over-proliferation of petrol stations or had any appreciable effect in restricting the motorists' freedom to buy the petrol of his choice.[3] Professor Barna dissented from the conclusions of the Commission, and indeed the reasoning of the Commission is questionable. For example, the principal argument advanced by the Commission for holding that solus trading did not operate against the public interest, was that solus marketing

[1] The Monopolies Commission: Report on the Supply of Petrol to Retailers in the United Kingdom, July 1965 (hereinafter the Monopolies Commission Report), paras. 359–379.
[2] *Ibid.* para. 376.
[3] *Ibid.* paras. 377 and 378.

reduced the costs of distribution. However, it is apparent from the Report that these cost-savings were probably absorbed by the retailer and not passed on to the public,[4] and that any such savings could have equally well been achieved by quantity allowances on the size of the delivery to the solus site owner.[5] The Commission having come to the conclusion that it was possible to have a system of solus trading which did not operate against the public interest, nevertheless believed that certain features of solus marketing did in fact do so, and it accordingly made recommendations relating to them. Three of the most important of these recommendations were, first, that petrol companies should not impose any restrictions on solus retailers in relation to the sale of lubricating oils [6]; secondly, that solus agreements should not exceed five years or where a loan is granted for a period exceeding five years, the solus tie could extend to, but not beyond, the latest date for repayment [7]; and finally, to prevent the spread of company-owned stations, that petrol companies whose deliveries to company-owned sites exceed 15 per cent. of their total deliveries to petrol stations, should not acquire any further garages, provided that the total deliveries of the supplier exceed ten million gallons.[8] This would certainly seem to be the most radical recommendation in a Report which does not effectively answer many of the cogent points made by Professor Barna in his note of dissent.[9]

The Court of Appeal in *Petrofina (Gt. Britain) Ltd.* v. *Martin* [10] and *Esso Petroleum Co. Ltd.* v. *Harper's Garage (Stourport) Ltd.*[11] had to consider the extent to which the common law doctrine of restraint of trade was applicable to solus agreements.[12] The solus agreement in *Petrofina* included a " tying " covenant, a compulsory trading covenant and a continuity covenant. The agreement also stipulated that the defendant would sell at the retail prices fixed by the plaintiffs, that only Petrofina lubricating oil would be advertised at the site and used in the lubricating bay, and that the agreement would last for twelve years or until 600,000 gallons of the plaintiff's petrol had been sold by the defendant. The " break-even " point

4 *Ibid.* para. 374.
5 *Ibid.* paras. 242–251 and 425.
6 *Ibid.* para. 397.
7 *Ibid.* paras. 384–388.
8 *Ibid.* para. 415. The undertaking obtained from the petrol companies allows the acquisition of new company-owned stations provided existing stations are disposed of.
9 For example, that the oil companies could have utilised a system of quantity allowances to reduce distribution costs and that the retailing of petrol is inefficient in this country both in physical and financial terms.
10 [1966] 2 W.L.R. 318; [1966] 1 All E.R. 126.
11 [1966] 2 W.L.R. 1043; [1966] 1 All E.R. 725.
12 Solus agreements have also been considered by the Court of Appeal in *Regent Oil Co.* v. *Aldon Motors* [1965] 1 W.L.R. 956, and by Stamp J. in *Regent Oil Co. Ltd.* v. *J. T. Leavesley (Lichfield) Ltd.* [1966] 2 All E.R. 454; both cases related to interlocutory matters. For a discussion of *Petrofina* and *Esso* at first instance see Whiteman, " Agreements in Restraint of Trade " (1966) 29 M.L.R. 77.

for petrol sales was 50,000 gallons a year, but the defendant found after seven weeks' trading that he was selling petrol at the rate of 30,000 gallons a year, and therefore decided to sell another brand of petrol.

Petrofina therefore brought an action against Martin claiming an injunction to prevent him selling any petrol other than Petrofina.

There were two agreements to be considered in the *Esso* case, both relating to garages owned by the defendants. In relation to one garage (the Mustow Green Garage), the important terms of the agreement were similar to those in *Petrofina* except for two significant differences: first, the defendant merely had to give preference to the sale of Esso motor fuels and second, the term of the agreement was four years and five months; the duration of the agreement was due to the fact that this was the period unexpired under a previous solus agreement when the defendant acquired the garage. On the other garage (the Corner Garage) Esso had a mortgage to secure a principal sum of £7,000 lent to the defendants, as well as a similar solus agreement. The mortgage money was repayable by instalments over a twenty-one year period, which was also the duration of the solus agreement. The mortgage charged the Corner Garage by way of legal mortgage with repayment and payment of interest, and contained covenants by the defendants to observe certain stipulations. The stipulations included a tying covenant and a compulsory trading covenant, and a provision that the mortgage should not be redeemed otherwise than in accordance with the covenant for repayment, *viz.*, for repayment by instalments over twenty-one years. As a result of a difference over Esso's decision to remove resale price maintenance clauses from all their solus agreements, the defendants began to sell low priced petrol other than Esso's at both garages. The defendants offered to redeem the mortgage and later gave formal notice to do so. Esso therefore claimed an injunction to restrain the defendants from selling any other petrol at their garage.

The consideration of solus agreements in the context of the common law doctrine of restraint of trade raises four distinct problems. First, is such an agreement within the purview and subject to the tests applicable to covenants in restraint of trade, that is, the *Nordenfelt* doctrine? Secondly, what interest is the oil company seeking to protect by the ordinary solus agreement, and whether this is an interest they are entitled to have protected? Thirdly, does the doctrine apply to covenants in a mortgage? Finally, is the restraint imposed reasonable in the circumstances?

The first issue was, therefore, the applicability of the *Nordenfelt* doctrine to "solus" agreements. Counsel submitted that the doctrine against restraint of trade has no application to a restriction imposed on the *trading use* to be made of a *particular piece of land,* as opposed to a restriction on a *person or corporation.* Although this contention was rejected by the Court of Appeal, Diplock L.J.

in *Petrofina* described it as " the formidable argument advanced on behalf of Petrofina." [13] Indeed, Mocatta J. had accepted the validity of this distinction in *Esso* at first instance [14] and as considerable stress will no doubt be placed on it in the House of Lords, it is a submission which merits the closest consideration. In restraint of trade cases the area covered by the restraint is very often the decisive consideration, and, by analogy, its relevance can be seen in the distinction propounded. With this qualification accepted, it is submitted that the Court of Appeal was quite right to reject this arbitrary distinction. The distinction is as meaningful and logical as a different distinction of which it is reminiscent: the unjustifiable nineteenth-century distinction between general and partial restraints.

This latter idea was finally rejected in 1918, on the obvious ground that it was inconsistent with commercial realities.[15] It may be argued with considerable cogency, what is the economic justification for the similar but different proposition now alleged?

It is submitted that the distinction propounded may not be meaningful for two distinct reasons. First, there is the preliminary, but fundamental, difficulty of distinguishing between a restraint which has been imposed on a person and one which has been imposed on a particular piece of land. *McEllistrim* v. *Ballymacelligott Co-operative Agricultural and Dairy Society* [16] illustrates this contention. In that case the members of a society in Ireland agreed to sell all the produce of their dairy herd kept *within a defined area* to the defendant's creamery. Under the rules of the society it was very difficult for a member to cease to be a member. The House of Lords held that the rules of the society imposed a greater restraint than was reasonably required for the protection of the society. Mocatta J. in *Esso* stated that the restraint in *McEllistrim's* case was one imposed on an individual,[17] whilst Lord Denning M.R.[18] and Diplock L.J.[19] in *Petrofina* took the opposite view of the restriction. This latter interpretation of *McEllistrim's* case must lead to the conclusion that the distinction submitted was ill-founded for the doctrine against restraint of trade had thus been applied in a case relating to a restraint on the use to be made of a particular plot of land.

Two reasons could be asserted as a basis for distinguishing *McEllistrim's* case as one imposing a restraint on an individual whereas the solus agreement in *Petrofina* imposed a restraint on the trading use of land. First, that the agreement in *Petrofina* prohibited the covenantor from parting with possession of the land to

[13] [1966] 1 All E.R. 126 at p. 141.
[14] [1966] 3 W.L.R. 469; [1965] 2 All E.R. 933.
[15] *Mason* v. *Provident Clothing and Supply Co.* [1913] A.C. 724.
[16] [1919] A.C. 548.
[17] [1965] 3 W.L.R. 469 at p. 492.
[18] [1966] 1 W.L.R. 126 at pp. 131–132.
[19] *Ibid.* at pp. 141–142.

any person who did not enter into a similar covenant with the covenantee. This conclusion not only illustrates that the distinction propounded has little merit, but also that the doctrine could be evaded in every case by imposing a restriction on the liberty of the covenantee to dispose of his property. A second possible distinction between the two cases, is that in *McEllistrim's* case the restriction related to the produce of particular farms in the defined area, whereas the restriction in *Petrofina* concerned the goods sold at a particular filling station. However, this would seem to be an illogical ground for distinguishing the two cases, for if it were accepted, a garage proprietor who " tied " all his filling stations in a defined area would be in a different position from the owner who made a " solus " agreement relating to his only station. Indeed, if this were the correct basis for distinguishing between *Petrofina* and *McEllistrim's* case, or by implication, in a wider context between a restraint imposed on a person and one limited to land, the *Nordenfelt* doctrine could be evaded by making the " defined area " the whole of the United Kingdom.

The second principal reason for asserting that the distinction propounded has little substance, relates to the justification for this approach. Mocatta J. in *Esso* succinctly gave the reason for the distinction as follows: " the mischief against which the *Nordenfelt* doctrine is directed is that of taking a man wholly or partly out of trade; it does not apply to taking a particular plot of land out of trade." [20] However, it is submitted that a restraint on the trading use of a plot of land may be so onerous, that its effect will approximate to that of a restriction on an individual, and thus " take a man out of trade." Two dicta of Lord Birkenhead L.C. in *McEllistrim's* case illustrate this proposition [21]:

> " It is to be observed that in a sparsely inhabited agricultural neighbourhood, with scanty means of communication, a prohibition of trade in every township within a radius of ten miles, might have precisely the same effect upon the business of a small trader as if the preclusion extended to the remotest corners of Donegal."

And again [22]:

> " The result is that an unwilling member is likely to find himself precluded for life from disposing of the raw materials of his trade to anyone but the respondents within a radius which may easily include every neighbouring centre of population which affords him the slightest prospect of a valuable market. It is no answer to such a man to say ' You can go elsewhere.' He may be owner in fee of a small holding which has been in his family for generations. The fact that his integrity is known amongst his neighbours may be no small

[20] [1965] 3 W.L.R. 469 at pp. 485–486.
[21] [1919] A.C. 548 at p. 562.
[22] *Ibid.* at p. 565.

element in his stock-in-trade. Further, the power of migrating to a part of Ireland in which he may never have lived, cannot be considered to be *any allevation of the severity or unreasonableness of the rule.*" [23]

Indeed, the *Petrofina* case itself illustrates that if the alleged distinction were accepted, the effect of a restriction on the trading use of a piece of land could be as onerous as that on an individual. Buckley J. at first instance in *Petrofina* admirably summarised the position:

> " When Martin bought the business it was running at a loss. It is by no means fanciful to suppose that Martin might have experienced great difficulty in finding any purchaser of the property shackled by the solus agreement. In such circumstances the effect of the solus agreement would have been to interfere seriously with his ability to realise his interest in this particular venture and to use his capital resources in some other business elsewhere." [24]

Thus, a restraint of the trading use to be made of a particular piece of *land* may, nevertheless, take an *individual* " out of trade." Indeed, the very feature of the agreement in *Petrofina* (" the continuity covenant ") that was responsible for this onerous effect, was the sole clause of the agreement which counsel relied on as placing the agreement in the category of restraints relating to land. Thus, in many cases, if counsel were right, the only feature of an agreement which could justify that restriction being treated as relating to land, and thus exempt it from the *Nordenfelt* doctrine, would also be primarily responsible for the effect of that agreement being substantially as onerous as that on an individual. This curious conclusion emphasises the meaningless nature of the distinction propounded.

The second principal issue was the interest which the oil company is seeking to protect under the simple solus agreement and whether that interest is one that the oil company is reasonably entitled to have protected. In *Petrofina*, as there was for example no legal charge on the land in favour of the petrol company or any advance of rebate allowed to the defendants on their sales of petrol (two fairly common provisions of solus agreements), quite clearly the plaintiffs were merely seeking to protect their competitive position in the petrol market. The Court of Appeal rather surprisingly held that this was an interest which *Petrofina* were entitled to have protected, but all three judgments dismiss this crucial aspect of the case in a most confused and brief fashion. For example, Harman L.J. who, by implication, must have found that Petrofina could protect their competitive position, at one point states " what (the covenantee) is in fact protecting is his competitive position and

[23] My italics.
[24] [1965] 2 W.L.R. 1299 at p. 1317.

I doubt whether that is a legitimate subject for protection." [25] Again, Diplock L.J. stated that Petrofina were entitled to protect their interest of " selling as great a quantity of their petroleum products as they can, as profitably as they can," [26] as though this was an interest quite distinct from their competitive interest.[27]

The conclusion of the Court of Appeal should be contrasted with an oft-quoted dictum of Lord Birkenhead L.C. in *McEllistrim's* case [28]:

> " The respondents were not entitled to be protected against mere competition. No excellence of motive on their part, no record of efficient public service, can for this purpose place them in a different position from that occupied by any contracting party, who is called upon to justify his restraint. And it has been laid down by your Lordships over and over again that in this class of case the covenantee is not entitled to be protected against competition *per se*."

An illustration of this approach is to be found in *Vancouver Malt and Sake Brewing Company Ltd.* v. *Vancouver Breweries Ltd.*[29] where Lord Birkenhead's dictum was applied. In that case, the appellants covenanted to sell to the respondents for $15,000 all the goodwill of their brewer's licence and that for fifteen years they would not engage in the trade or business of manufacturing or selling beer. The only business in which the vendors were engaged was the brewing of sake, and as the goodwill of their licence so far as it related to sake was expressly excluded from the sale, they had no goodwill to sell. The Privy Council, therefore, held, that in reality the covenant was a bare covenant against competition and therefore the agreement was unenforceable.

Although the conclusion of the Court of Appeal that Petrofina was entitled to protect its competitive position, is thus contrary to previous authority and is, indeed, inconsistent with the approach of the courts in all categories of contracts falling within the restraint of trade doctrine,[30] it is submitted that the approach of the court was logical. It would seem to be quite reasonable for a company to wish to protect its competitive position by an agreement which has been negotiated at arm's length. In the sphere of combinations for the regulation of trade relations, the courts have been most unsympathetic to a trader, who having freely entered into an arrangement with other traders, seeks to be released from his obligation on the ground that he has imposed an unreasonable burden upon himself. Such an approach is equally applicable to

[25] [1966] 1 All E.R. 126 at p. 137.
[26] *Ibid.* at p. 143.
[27] Compare however Stamp J. in *Regent Oil Co. Ltd.* v. *J. T. Leavesley (Lichfield) Ltd.* [1966] 2 All E.R. 454 at p. 456.
[28] [1919] A.C. 548 at pp. 563–564.
[29] [1934] A.C. 181.
[30] For example, *Bowler* v. *Lovegrove* [1921] 1 Ch. 642; *Routh* v. *Jones* [1947] 1 All E.R. 758 at p. 761; *Morris Ltd.* v. *Saxelby* [1916] 1 A.C. 688 at p. 708.

a freely negotiated contract between a supplier and dealer in a particular commodity.

It would appear from the judgments of Lord Denning M.R.[31] and Diplock L.J.[32] that it would not be in all market situations, that a supplier would be entitled to protect his competitive interest. Lord Denning M.R. elucidated his reasoning by stating:

> "Now, if these solus agreements had been challenged ten or twelve years ago, when they were first introduced into this country, and were few in number, I think the early ones might well have been held unreasonable because the company which introduced them was really seeking to protect itself from competition from its rivals and nothing else. But the solus agreements were not challenged then and they have become so numerous that the picture is reversed. If a comparatively small company like Petrofina is to obtain entry into the trade, it must be able to protect its own outlet for petrol lest it be swallowed up by its giant rivals; and a reasonable way of protecting its outlet is by a solus agreement." [33]

Thus, although Lord Denning M.R. and similarly Diplock L.J. believed that Petrofina could protect their competitive interest, because in a market situation where a system of restrictive agreements prevails it is not contrary to the public interest for *new small* firms to utilise them, it seems that the conclusion will be used to justify *any* oil company protecting its competitive position. For example, the Court of Appeal in *Esso* treated *Petrofina* as establishing that proposition, with the result that a qualified conclusion reached on the basis of a special situation is to be treated as of general application. However, the approach of Lord Denning M.R. and, to a lesser extent, Diplock L.J.[34] is realistic and indeed, indicates a way in which the *Nordenfelt* doctrine could be made economically purposeful. This heterodox approach would be that where a company is seeking to protect its competitive interest, and has no other interest which it is entitled to have protected, it would have to be established to the satisfaction of the court that the agreement, which has imposed a restriction in one sphere (on the covenantor), has the general effect of promoting competition. In this way, the doctrine against restraint of trade might become a useful weapon dealing with the effect on competition of restrictive agreements outside the scope of the Restrictive Trade Practices Act 1956.

The third principal issue, considered only in *Esso* was whether the doctrine of restraint of trade applies to covenants contained in a mortgage. The Court of Appeal had no hesitation in holding such covenants to be within the doctrine, and far from deciding the matter on technical grounds, the judgments clearly show that the

[31] [1966] 1 All E.R. 126 at p. 134.
[32] *Ibid.* at pp. 142–143.
[33] *Ibid.* at p. 134.
[34] *Ibid.* at p. 143.

Court of Appeal was determined that its decision in *Petrofina* (condemning the tie) should not be so easily evaded. The determination to make the *Nordenfelt* doctrine really effective is admirably illustrated by the judgment of Diplock L.J.:

> " Despite counsel for Esso's learned and ingenious argument, I am not persuaded that mortgages of land are condemned today to linger in a jurisprudential cul-de-sac built by the Court of Chancery before the Judicature Acts, from which the robust doctrines of the common law are barred. True it is that there is no reported case in which the doctrine against unreasonable restraint of trade has been applied to a mortgage of land, but it is also true that there is no reported case in which such long and onerous covenants in restraint of trade have been incorporated in a mortgage of land. . . . I think therefore, that we must decide the present case as a matter of principle. What magic is there in a mortgage of land to exclude it from the ambit of the general principle of public policy that no one can lawfully interfere with another in the free exercise of his trade or business unless there exists some just cause or excuse for such interference? " [35]

The conclusion of the Court of Appeal casts considerable doubt on the nineteenth century cases which established that a brewer could tie innkeepers to sell only the beer of that particular brewer at his public-house.[36] Lord Denning M.R. in *Petrofina* recognised that public-house ties, where the covenant was " in gross," were subject to the doctrine,[37] and his Lordship pointed out, quite rightly, that all the old cases were decided before it was held that partial restraints were no different to general restraints as far as the applicability of the doctrine was concerned. Again, as a result of the *Esso* decision, and as there are no material differences between the two types of exclusive dealing arrangement, even where the public-house tie is contained in a mortgage, it will be within the *Nordenfelt* doctrine and subject to the test of reasonableness embodied therein.[38]

The final issue in both cases was, therefore, whether the agreement imposed a restraint which was reasonable. In *Petrofina* Lord Denning M.R. and Diplock L.J. found the agreement to be unreasonable for three reasons: first, the tie was for too long; secondly, the restriction on lubricating oils was too great, and finally the " continuity covenant " imposed an unreasonable burden on

[35] [1966] 1 All E.R. 725 at p. 738.

[36] *e.g.*, *Clegg* v. *Hands* (1890) 44 Ch.D. 503 and *Catt* v. *Tourle* (1869) L.R. 4 Ch.App. 654.

[37] [1966] 1 All E.R. 126 at p. 133.

[38] The Government has announced that the supply of beer to licensed premises is to be investigated by the Monopolies Commission: *The Times*, June 15, 1966. The Board of Trade have since stated that the intention is to permit a full inquiry into the tied house system to see if it is operating against the public interest: *The Times*, July 28, 1966.

the trader. This last ground was the only one stated by Harman L.J. for holding the agreement to be unreasonable.

The exact ambit of the *Petrofina* decision is a matter of some doubt. The most unusual, and striking, feature of the agreement in *Petrofina* was that the garage owner *had to* operate his filling station for as long as the " tying " agreement subsisted, and it is the interaction of this stipulation with the continuity covenant and the term of the tie which provides the real *ratio* of the case. This submission can be illustrated by the judgment of Diplock L.J.[39]:

> " If [the respondent's] trade in the appellant's products does in fact involve him in a loss, he may find it impossible to find a purchaser for his business at all and so may be compelled to trade there at a loss for a period of at least twelve years and for some period of unpredictable duration thereafter. The greater the loss, the longer the period will be."

The unusual clause requiring the garage owner to operate the filling station for the duration of the tying agreement has indeed provided a basis for distinguishing the case: Lord Denning M.R. himself distinguished the decision of Buckley J. in the *Petrofina* case,[40] which was to the same effect, in *Regent Oil Co.* v. *Aldon Motors Ltd.*[41] on the ground, *inter alia*, that " the Petrofina company were seeking to make the defendant company operate, and continue to operate, at a loss." [42] In *Regent* the Court of Appeal had held that a solus agreement for seventeen and a half years coupled with a legal charge on land was sufficiently prima facie legal to found an interlocutory injunction. As their Lordships in that case entirely reserved the question whether the *Petrofina* case was correctly decided, and as it was only dealing with an interlocutory matter, it is submitted that the decision does not affect the validity of the two later decisions.

In the *Esso* case the Court of Appeal held the solus agreement relating to the Mustow Green Garage to be an unreasonable restraint of trade again for three reasons; first, while price maintenance was legal Esso (in contrast with the oil company in the *Petrofina* case) had the right to fix both the wholesale and retail prices so that they could squeeze the dealer's profit margin at their pleasure. Secondly, Esso were not under any restriction on their own sales to other persons, so that they could and indeed had, supplied petrol direct to other customers at less than their scheduled wholesale prices, who could then resell to the public at cut prices. Lord Denning M.R. stated that both clauses could have been valid if only imposed for a short term, so that the decision hinged on the third aspect of the agreement, whether the tie was too long. In this connection,

[39] [1966] 2 W.L.R. 318 at pp. 346–347.
[40] [1965] 2 W.L.R. 1299; [1965] 2 All E.R. 176.
[41] [1965] 1 W.L.R. 956; [1965] 2 All E.R. 644.
[42] *Ibid.* at p. 961.

the court paid considerable attention to the submission that if petrol companies are to sell motor fuel economically, they had to be able to rely on the continuity of outlets so that the most economical distribution of motor fuels could be achieved. Thus the question was whether the stipulated period was no longer than was reasonably necessary to give Esso time to find and obtain an alternative outlet in the same district on the termination of the solus agreement. As Denning M.R. and Diplock L.J. believed [43] that three years and two years respectively would be adequate for the protection of Esso's interest, it was therefore held that the agreement for four years and five months was unreasonable.

As far as the Corner Garage mortgage was concerned, the court held that the tie for twenty-one years, coupled with a proviso forbidding redemption for that period, was unreasonable. It was the combination of these two factors which was the vice of the mortgage.[44] Lord Denning M.R. stated *obiter* that the mortgage might have been reasonable if it had provided for a tie for five years and no right to redeem for that period,[45] and Diplock L.J. agreed that there might be cases where a tying covenant, which would not be reasonable if contained in an ordinary contract, would nevertheless be reasonably necessary to protect the mortgagee's interest in the land as security for his loan.[46] Thus although there is no magic in a mortgage to exclude the application of the doctrine, it may still be useful as a means of obtaining a slightly longer tie.

The *Esso* and *Petrofina* decisions leave little doubt that the vast majority of solus agreements would be condemned as an unreasonable restraint upon the solus retailer. The Court of Appeal not only condemned an agreement lasting for four years and five months, but also stated that normally only agreements for two to three years would be regarded as reasonable. As nearly all solus agreements are for a term in excess of such a period, and contain continuity and compulsory trading covenants and restrictions on the sale of lubricating oils on the Petrofina model,[47] the vice which affected the two decisions would occur in nearly every other solus agreement. However such potential judicial activity in this field has been limited by the fact that the Government has implemented the Monopolies Commission Report [48] (with certain modifications)

[43] [1966] 1 All E.R. 725 at pp. 729 and 737 respectively.
[44] See the comments of Diplock L.J., *ibid.* at p. 739.
[45] *Ibid.* at p. 731.
[46] *Ibid.* at p. 739.
[47] The restriction on the sale of lubricating oils in Esso was considered by Diplock L.J. to be unobjectionable: *ibid.* at p. 735.
[48] The Government's amendments to the Monopolies Commission Report certainly seem to favour the larger companies and discriminate against the smaller suppliers. The main modifications to the Report are: (1) that the limitation on company-owned stations where deliveries to company-owned sites exceed 15 per cent. of total deliveries to petrol stations only applies where the total deliveries of the supplier exceed 50 million gallons (not 10 million gallons as proposed by the Commission). (2) Companies which are thus prevented from

by obtaining voluntary undertakings from the oil companies which conform to the Commission's recommendations (as amended). Solus agreements in conformity with the voluntary undertakings might nevertheless still be condemned by the judiciary as unreasonable under the *Nordenfelt* doctrine. This possibility might occur because the voluntary undertaking as to the length of term of an agreement (five years) would probably be regarded as unduly long by the judiciary, and also because two features of the solus system that have been condemned by the judiciary, the continuity and compulsory trading covenants,[49] were not considered by the Commission to operate against the public interest and therefore it made no recommendations about them. Petrol companies will therefore, in future solus agreements, have to consider the voluntary undertakings and the two judicial decisions quite separately.

Finally, if the judiciary continues to condemn continuity covenants, a garage owner might at any time evade the obligations imposed on him by a solus agreement, by transferring the ownership of a garage to a limited company which he effectively owns or (if the court is prepared to lift the corporate veil) a company in which he is substantially interested.

Although certain conclusions about the solus system of marketing are common to both the Monopolies Commission Report and the judgments of the Court of Appeal the standpoint of each body is different. The Commission is concerned only with the public interest, while the judges, notwithstanding the dictum of Lord MacNaghten in *Nordenfelt* that both the parties in question *and* the public interest should be considered in applying the test of reasonableness [50] consider only whether *this* restraint imposed on *this* particular trader is unreasonable, and this is regarded as synonymous with a consideration of the public interest. The justification for equating the two is generally stated to be that the

acquiring additional company-owned stations, nonetheless, are able to build new stations provided existing stations are disposed of—an unjustifiable concession which will allow the larger companies to replace out-dated stations by large new garages. (3) Solus ties on motorway sites (all controlled by the majors) will not be subject to the five-year limit. (4) Companies can build their own stations immediately opposite existing ones.

The President of the Board of Trade announced on July 19, 1966, that all the petrol companies (except one) had given voluntary undertakings which conform to the Monopolies Commission Report as amended, and which, in the event, came into force on August 6, 1966. Total Oil Products (G.B.) Ltd. refused to give the undertaking because of the limitation on company-owned stations, which has the effect of freezing the larger companies' advantage in this field (see "Why Total is the Villain," *The Times*, July 25, 1966). A statutory order was therefore made on Total, in comparable terms to the voluntary undertaking. Mr. Jay had threatened that if he was forced to make statutory orders on all the companies "the order would be couched in more rigid, and therefore in some respects, less favourable terms than the present undertakings." See generally *The Times*, July 24, 1966. The undertakings will be reviewed in 18 months' time.

[49] Monopolies Commission Report, paras. 403 and 408-411.

[50] [1894] A.C. 535 at p. 565.

public has an interest in seeing that every individual can trade with whom he pleases in what manner he considers to be desirable.[51] However it seems somewhat illogical to allow a trader to come before the court and say that by a freely negotiated contract, which has conferred considerable benefits upon him, he has imposed an unreasonable burden upon himself.

In the analogous situation of contracts between traders to restrict output or maintain the selling price of certain commodities, the court looks with disfavour, indeed distaste, on a trader who alleges that, although the agreement was negotiated at arm's length on an equal footing, it has imposed an unreasonable restraint of trade on his trading activities. The courts have applied the test that in commercial agreements of this kind, the parties to the contract are the best judges of what is reasonable.[52] Indeed, a solus agreement confers considerable benefits on the garage proprietor, and it may only be reasonable that the oil company seeks equivalent advantages. The only justification for allowing a contracting party to come before the court should therefore be that the public interest has been adversely affected by this agreement, and therefore the judiciary should concentrate on the second aspect of Lord MacNaghten's test.

The House of Lords, when it comes to consider the *Petrofina* and *Esso* cases will have an opportunity to make the *Nordenfelt* doctrine more purposeful. The Court of Appeal has shown that the doctrine may be a flexible weapon in the judiciary armoury,[53] for what is reasonable in the interests of the parties and in the public interest, may alter as economic conditions or more particularly the attitude of the judiciary changes. The House of Lords could invigorate the doctrine in either or both of two ways: first, it could insist that where the oil company is seeking to protect its competitive interest only by a restriction on the solus site operator, it must be established that the agreement has the general effect of promoting competition in the retail petrol market. Secondly, and more important, the House of Lords could revitalise the doctrine merely by separating the two aspects of the test of reasonableness propounded by Lord MacNaghten, so that it would have to be clearly established that the agreement was reasonable in relation to the public interest, quite apart from its reasonableness between the parties. The judiciary could then insist that if it is to be established that the agreement does not operate contrary to the public interest

[51] See Diplock L.J. in *Petrofina* [1966] 1 All E.R. 126 at p. 138.

[52] *North Western Salt Co. Ltd.* v. *Electrolytic Alkali Co. Ltd.* [1914] A.C. 461 at p. 471, *per* Lord Haldane.

[53] Denning M.R. stated that the three kinds of restraint usually referred to in the textbooks (see, *e.g.*, Cheshire and Fifoot, *The Law of Contract*, 6th ed., 1964, p. 324) were not exhaustive: "The categories of restraint of trade are not closed. As methods of trading change, so do the areas of restraint expand. The law, if it is to fulfil its purpose, must keep pace with them." [1966] 1 All E.R. at p. 131.

the economic implications of the arrangement must be considered. It is surely quite anachronistic that the Court of Appeal paid no attention to the economic issues and whether, in fact, the agreement operated to the detriment of the public in the widest economic sense. Such a radical approach to the doctrine is certainly possible, for the judiciary has shown under the Restrictive Trade Practices Act of 1956 that it is most competent to handle such wide economic issues. Indeed, the actual decisions in the two cases could be the result of handing the issue of restrictive practices back to the judiciary in 1956, so that the judicial attitude towards anti-competitive agreements has undergone a fundamental change. The economic arguments of counsel before the Restrictive Practices Court and the judgments of that court are now starting to permeate the judiciary so that the refreshing breezes that so often blow through the Restrictive Practices Court are now likely to be encountered even in the Chancery Division.

The radical approach propounded is certainly possible, and in the analogous sphere of restrictive trade agreements under the Restrictive Trade Practices Act 1956 the judiciary has shown its determination to make that Act really effective.[54] That determination has not only resulted in a revolutionary change in the judiciary's implementation of that Act, but also seems to show, quite clearly, that there is now an awareness on the part of the judiciary that strong legislation is needed to curb restrictive practices among businessmen. Indeed, the echoes of that attitude are apparent in the *Petrofina* and *Esso* cases, so that another " branch " of restrictive practices law could be made meaningful. For example, Diplock L.J. concluded his judgment by stating[55]:

> " [Petrofina] seek to create a new commercial serfdom from which the garage proprietor can obtain manumission only on finding a substitute serf. To this end the courts of *twentieth-century* England will not lend their aid." [56]

However, such a revitalisation of the *Nordenfelt* doctrine would still not provide the best judicial answer to the problem. A type of agreement may or may not be in the public interest depending on, *inter alia*, the market domination of the contracting party. Therefore legislative action is needed directing the courts' attention to the issue of competition, so that the judiciary could consider exclusive dealing agreements in a wider context. Moreover, the legislature by clearly making a policy choice (the promotion of competition), and embodying that principle with sufficient precision in appropriate legislation, will have created a justiciable issue, and, certainly, the courts are ideal places to effectuate generalised policies in individual cases. It is interesting in this context to contrast the American

[54] See R. B. Stevens and B. S. Yamey, *The Restrictive Practices Court: The Judicial Process and Economic Policy*, pp. 157–192, for an excellent account of this development.

[55] [1966] 1 All E.R. 126 at p. 144.

[56] My italics.

legislation on this topic. Section 3 of the Clayton Act deals specifically with, *inter alia*, exclusive dealing contracts, and provides that it is unlawful to sell or lease goods for resale on the condition that the purchaser or lessee must not deal in the goods of a competitor, where the effect of that agreement " may be to substantially lessen competition or tend to create a monopoly in any line of commerce." A crucial aspect of section 3 is that the lessening of competition must be substantial, so that in two cases, where the exclusive dealing contract was essentially the same, it was held in one, that the Clayton Act was violated where the manufacturer controlled 40 per cent. of the relevant market,[57] but not where a little more than 1 per cent. was controlled.[58]

Again, in *Standard Oil Company of California* v. *United States* [59] exclusive distributorship agreements relating to filling stations supplying 14 per cent. of the petrol sold by retail in the western states of America, were held to be within the condemnation of section 3.

Thus, legislation on the lines of the American model would represent a considerable advance over the common law doctrine of restraint of trade's consideration of single agreements, and then, at present, only in the light of legalistic concepts. However such a provision would have to be so drafted and implemented that, in contrast with section 3, the judiciary should be directed to consider evidence bearing on the economic usefulness of the exclusive arrangement, and its effect upon the competitive situation.

The legislature took a courageous step in 1956 in handing the issue of restrictive practices back to a judiciary which had previously not only intentionally abdicated any role in shaping the competitive nature of the economy, but had also shown itself to be anti-competitive, and ill-equipped to handle such issues. This act of faith has been justified by subsequent events,[60] and the judicial responsibility in the field of competition was enlarged by the Resale Prices Act of 1964. It is to be hoped that the House of Lords will acknowledge the faith that has been reposed in them by the legislature, and will readily respond to the challenge to make the *Nordenfelt* doctrine both purposeful and effective and, by so doing, accept an enlarged role in the sphere of restrictive practices and the enforcement of competition.[61]

PETER G. WHITEMAN.

[57] *Standard Fashion Co.* v. *Margrane-Houston Company*, 258 U.S. 346 (1922).
[58] *Pearsall Butter Company* v. *Federal Trade Commission*, 292 F. 720 (C.C.A. 7th, 1923).
[59] 337 U.S. 293 (1949).
[60] Consider the extremely realistic attitude adopted by the Restrictive Practices Court in its treatment of anti-competitive agreements under section 6 of the 1956 Act in *Re Mileage Conference Group of the Tyre Manufacturers' Conference, Ltd.'s Agreement* [1966] 2 All E.R. 849. See (1966) 29 M.L.R. 563.
[61] Thanks are due to Professor B. S. Yamey for reading a preliminary draft of this article and for making several valuable suggestions as to its content.