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CONTRACTS - RESTRAINT OF TRADE - LEGALITY OF COVENANT RESTRICTING USE OF LAND BY THE PURCHASER WHERE NO GOODWILL TRANSFERRED

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CONTRACTS — RESTRAINT OF TRADE — LEGALITY OF COVENANT RESTRICTING USE OF LAND BY THE PURCHASER WHERE NO GOODWILL TRANSFERRED — Defendants' intestate, who owned large interests in two lime companies operating in Washington and California, entered into a contract for the sale of a tract of land to plaintiff's predecessor in title. The contract contained a restrictive covenant to the effect that the grantee, or those claiming under him, would not use any of the limerock in said land for the purpose of making lime. Subsequently the grantor died, and the conveyance and execution of a deed, which included within its provisions the restrictive covenant, were made by the administrator of grantor's estate, pursuant to court order. Plaintiff brought an action to cancel the restrictive covenant. *Held*, that such a restriction was a reasonable one for the grantor to make for the protection of his interest in the lime business, that it was not materially in restraint of trade, and therefore would stand as against plaintiff.¹ *Messett v. Cowell*, (Wash. 1938) 79 P. (2d) 337.

With an established exception where businesses of a public character are subject to state regulation, the prevailing legal attitude posits a free competitive system. It is with this entrenched doctrine that covenants restricting competition must struggle to maintain their validity.² To resolve this conflict and to determine whether such a covenant is valid, the courts now apply a test involving two elements: first, does the covenantee have a sufficient interest connected with the contract relationship of the parties to deserve the protection afforded by the covenant; second, is the covenant reasonable in its application to the facts of the particular situation so as not to unduly interfere with the public's interest?³ In the extreme case where *A* secures from *B* a promise, giving consideration therefor, not to continue in business, the courts almost uniformly invalidate such

¹ No consideration is given herein to the question whether assignees of the covenantor are bound by the restrictive covenant. For a discussion of this problem, see Giddings, "Restrictions Upon the Use of Land," 5 HARV. L. REV. 274 (1892); Keasbey, "Restrictions Upon the Use of Land," 6 HARV. L. REV. 280 (1893).

² For a further elaboration of this conflict, see GARE, COVENANTS IN RESTRAINT OF TRADE 3 (1935); 5 WILLISTON, CONTRACTS, rev. ed. § 1635 (1937).

³ *Horner v. Graves*, 7 Bing. 735, 131 Eng. Rep. 284 (1831); *Nordenfelt v. Maxim Nordenfelt Guns & Ammunition Co.*, [1894] A. C. 535; *Diamond Match Co. v. Roeber*, 106 N. Y. 473, 13 N. E. 419 (1887); *United States v. Addyston Pipe & Steel Co.*, (C. C. A. 6th, 1898) 85 F. 271; ANSON, CONTRACTS 316 (1930). That the common law originally held all restraints of trade invalid, and later determined the validity of such covenants by mechanical rules as to time and spatial limitations, and finally evolved the test of reasonableness, is familiar history to all students of the subject.

a covenant.⁴ In this case *A* is not seeking protection for an interest growing out of the subject matter of the contract; moreover, the public's interest is unduly threatened by this clear fostering of monopoly. But where *A* sells his business and goodwill to *B*, covenanting not to engage in said business, the provision is upheld if the protection assured to the interest of *B* under the contract (realization of the value of the goodwill and business) is no more than reasonably necessary.⁵ Likewise, where a partner in a firm sells out to a co-partner, there is an interest in the latter under the contract deserving protection, and if the limitations on the seller are only those reasonably required to secure the purchaser in his newly acquired interest, the courts validate such a covenant.⁶ However, in cases involving a covenant in an employment contract restricting the employee from exploiting, to his own advantage, the goodwill of his employer's business, or knowledge of trade secrets gained during his employment; or a covenant, as in the instant case, restricting the purchaser of land in his use thereof, we have different premises to consider. In these two situations the covenant is ancillary to an independent, valid contract, but no interest to be protected passes to the covenantee under the contract. Yet if the restrictions on the covenantors are reasonable,⁷ the courts find no difficulty in upholding them.⁸

⁴ 2 CONTRACTS RESTATEMENT, § 515 (e) (1932); *Clemons v. Meadows*, 123 Ky. 178, 94 S. W. 13 (1906); *Arctic Ice Co. v. Franklin Electric & Ice Co.*, 145 Ky. 32, 139 S. W. 1080 (1911); *Shapard v. Lesser*, 127 Ark. 590, 193 S. W. 262 (1917); *Santa Clara Valley Hill & Lumber Co. v. Hayes*, 76 Cal. 387 (1888); 5 WILLISTON, CONTRACTS, rev. ed., § 1636, p. 4582 (1937); and extensive note in 3 A. L. R. 250 (1919), supplemented in 91 A. L. R. 980 (1934). But see to the contrary, *Robey v. Plain City Theatre Co.*, 126 Iowa St. 473, 186 N. W. 1 (1933); *Horany v. Treese*, 91 Okla. 264, 217 P. 396 (1923); 47 HARV. L. REV. 140 (1933).

⁵ 2 CONTRACTS RESTATEMENT, § 516 (a) (1932); *Diamond Match Co. v. Roeber*, 106 N. Y. 473, 13 N. E. 419 (1887); 5 WILLISTON, CONTRACTS, rev. ed., § 1641 (1937); *Carpenter*, "Validity of Contracts Not to Compete," 76 UNIV. PA. L. REV. 244 (1928); *Langlois*, "Contracts in Restraint of Trade," 10 MICH. S. B. J. 155 (1931).

⁶ 2 CONTRACTS RESTATEMENT, § 516 (d) (1932); *Prame v. Ferrell*, 92 C. C. A. (6th) 374, 166 F. 702 (1909); *GARE, COVENANTS IN RESTRAINT OF TRADE* 89 (1935); *Angier v. Webber*, 14 Allen (96 Mass.) 211, 92 Am. Dec. 748 at 751 (1867); *O'Neal v. Hines*, 145 Ind. 32, 43 N. E. 946 (1896); *Storer v. Brock*, 351 Ill. 643, 184 N. E. 868 (1933).

⁷ It should be noted that a covenant restricting the purchaser of land in his use thereof is limited spatially, thereby fulfilling even the strict "partial restraint" test of the old common-law courts. Restrictions on the use of property by the purchaser which restrain competition beyond the degree allowed under the modern test are exemplified by *Burdell v. Grandi*, 152 Cal. 376, 92 P. 1022 (1907); *Chippewa Lumber Co. v. Tremper*, 75 Mich. 36, 42 N. W. 532 (1889).

⁸ Employer-employee relationship: 2 CONTRACTS RESTATEMENT, § 516 (f) (1932); *KALES, CONTRACTS AND COMBINATIONS IN RESTRAINT OF TRADE*, § 2 (1918); *Thum Co. v. Tloczynski*, 114 Mich. 149, 72 N. W. 140 (1897); *Eastman Co. v. Reichenbach*, 47 St. Rep. 435, 20 N. Y. S. 110 (1892); *Axelson v. Columbine Laundry Co.*, 81 Colo. 254, 254 P. 990 (1927).

Vendor-purchaser relationship: *Hodge v. Sloan*, 107 N. Y. 244, 17 N. E. 335 (1887); *Seeck v. Jakel*, 71 Ore. 35, 141 P. 211 (1914); *Natural Products Co. v.*

Seemingly then, the important factor to weigh in determining the validity of such covenants is whether there exists somewhere in the covenantees a sufficient interest deserving of protection which is related to the other provisions of the contract. In the employment cases, such a sufficient and related interest of the covenantee-employer is said to be present in his right to be free from unfair competitive acts on the part of the covenantor-employee which are made possible only by the contract of employment.⁹ A sufficient and related interest in the vendor of land is more difficult to lay hold of. If it is found to be the right to free alienation of land,¹⁰ the interest is a tenuous one. For such an explanation is completely oblivious of the doctrine of free competition. Moreover, we find this supposed interest limited in other branches of the law.¹¹ If the interest is the right to protect one's means of livelihood against destruction by the purchaser's use of the land conveyed,¹² then the explanation is similar to that sustaining an interest in the employer. However, the analogy is not a satisfactory one. In the case of the employee, it may be justifiable to hold that the employer has a right to restrain the employee in order to prevent his taking away the goodwill and trade secrets acquired as a result of the employment, which after all, rightfully belong to the employer. On the other hand, the purchaser of land gains through the contract of purchase no advantage in competing with the vendor that would not equally accrue to him through the purchase of any other tract of land having the same natural resources. The fact of the matter is that the courts have sustained such covenants more because the restraint involved is usually negligible in its net effect than because the restraint can be justified in accordance with the generally accepted principles.¹³

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Dolese & Shepard Co., 309 Ill. 230, 140 N. E. 840 (1923); American Strawboard Co. v. Haldeman Paper Co., (C. C. A. 6th, 1897) 83 F. 619; Robbins v. Webb, 68 Ala. 393 (1880); Dick v. Sears-Roebuck Co., 115 Conn. 122, 160 A. 432 (1932); Magee v. Osborne, 144 Misc. 449, 258 N. Y. S. 819 (1932).

⁹ See extensive annotation of cases dealing with this subject in 9 A. L. R. 1456 (1920).

¹⁰ As suggested by the court in *Morris & Morris v. Tuskalooza Mfg. Co.*, 83 Ala. 565 at 573 (1887). In sustaining the validity of these covenants, the courts not infrequently use as precedents decisions upholding restrictions on the purchaser where such restrictions are in connection with a land development plan (e.g., the land to be used for residential purposes only). Clearly, this is a misapplication of a rule of law unrelated to the case under discussion. See citations in the cases in note 8, second paragraph, *supra*.

¹¹ The taxing power of the state, the rule against perpetuities, the widow's right to dower, are all common examples of accepted legal restrictions upon the power of an owner of land in fee to alienate it according to his pleasure.

¹² This is the usual explanation given to justify the validity of this type of restrictive covenant. See *KALES, CONTRACTS AND COMBINATIONS IN RESTRAINT OF TRADE* 21 (1918).

¹³ It is interesting to notice the attitude of several state legislatures toward contracts restraining trade. All such contracts and covenants are held void except where a business and its goodwill are sold to the covenantor, or where one partner sells out his interest to another partner. *N. D. Comp. Laws Ann.* (1913), §§ 5928-5930; *Okla. Stat.* (1931), §§ 9492-9494.