

11-1934

Contracts-Arbitration-Sherman Act

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Recommended Citation

(1934) "Contracts-Arbitration-Sherman Act," *Indiana Law Journal*: Vol. 10 : Iss. 2 , Article 12.

Available at: <https://www.repository.law.indiana.edu/ilj/vol10/iss2/12>

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Contracts—Arbitration—Sherman Act—Plaintiff Distributing Corporation sued the Defendant Theater Company for damages for breach of contract in which contract the defendant agreed to pay a fixed sum for the privilege of exhibiting certain pictures in defendant theater. The alleged breach of contract consisted of defendant's refusal to accept, play, or pay for the motion picture productions for which it had contracted. Defendant contended that the clause of the contract which required that the plaintiff should have pursued a course of arbitration before resorting to court action had not been complied with and also that the contract sued on was in restraint of trade and a violation of the Sherman Anti-Trust Law. Plaintiff obtained judgment in the trial court. Held: on appeal, affirmed, the court declaring that the clause requiring arbitration was void as in violation of the Sherman Act. but that the contract was divisible and thus the remainder could be sued upon.¹

The first attack on the validity of the Standard Exhibition Contract in the motion picture industry was made by the federal government in 1929. As a result of such attack, the United States Supreme Court in the case of *Paramount Famous Lasky Corporation v. United States*² found that the activities of the defendant producers and distributors, including the agreement to adopt and to use the Standard Form Contract, with its compulsory arbitration clause, constituted a conspiracy in restraint of trade and thus in violation of the Sherman Act.³ As a result of this decree, the question arose as to what effect the decision must have on the thousands of contracts made in the standard form by distributors and exhibitors throughout the country.

Before proceeding with the discussion, let it be said that the court's finding that the arbitration clause is invalid, yet the contract is divisible and the remaining portions are enforceable is not without respectable authority.⁴ But there is, also, equally as strong authority to the contrary.⁵

¹⁴ (1868) 29 Ind. 409.

¹ *Walker Theater Co. v. R. K. O. Distributing Corporation* (Ind. 1934), 189 N. E. 162.

² (1930), 282 U. S. 30, 51 S. Ct. 45.

³ 26 Stat. 209 (1891); 15 U. S. C. Nos. 1-7, 15 (1927).

⁴ *Metro-Goldwyn-Mayer Distributing Corporation v. Cocks* (Texas 1933), 56 S. W. (2d) 489; *Paramount Famous Lasky Corporation v. National Theater Corporation* (C. C. A. 1931), 49 Fed. (2d) 64; *Fox Film Corporation v. Buchanan* (1931), 17 La. App. 285, 136 So. 197; *Fox Film Corporation v. Bailly* (S. Dak. 1932), 246 N. W. 111; *Fox Film Corporation v. Ogden Theater Company* (Utah 1932), 17 Pac. (2d) 294; *Columbia Pictures Corporation v. Bi-Metallic Inv. Co.* (1930), 42 Fed. (2d) 873.

⁵ *United Artist Corporation v. Odeon Bldg.* (Wis. 1933), 248 N. W. 784; *Fox Film Corporation v. C. & M. Amusement Co.* (1932), 58 Fed. (2d) 337; *United Artists Corporation v. Piller* (N. Dak. 1932), 244 N. W. 20; *Universal Film Exchanges v. West* (Miss. 1932), 141 So. 293; *Fox Film Corporation v. Tri-State Theaters* (Idaho 1931), 6 Pac. (2d) 135; *Vitagraph Inc. v. Theatre Realty Co.* (1931), 50 Fed. (2d) 907; see *Majestic Theater Co. v. United Artist Corporation* (1930), 43 Fed. (2d) 991.

Insomuch as all the cases are based on the Paramount decision, it is best to make a careful analysis of it. Here, the action was brought by the United States government against the distributors to prevent further violation of the Sherman Act through a combination and conspiracy to restrain interstate commerce in motion picture films. The court enjoined them from operating under the contract in restraint of trade, but did not say nor undertake to say, that certain parts of the contract were invalid and certain parts valid.⁶ In the opinion appears the following passage, "It may be that arbitration is well adapted to the needs of the motion picture industry; but when under the guise of arbitration, parties enter into unusual arrangements which unreasonably suppress normal competition, their action becomes illegal."⁷ This language does not mean that the parties could in no case arbitrate, but that they might arbitrate as long as it was voluntary and without coercion. The case merely enjoined the combination of the distributors in restraint of trade which was to be carried out through the Standard Exhibition Contract. The enforceability of the contract against the exhibitor was not involved, he was not a party to the contract and his rights under it could not be determined.

Arbitration agreements in contracts are almost as old as Anglo-American law itself. At first, in England, such agreements met the disapproval of the courts since the courts at that time were jealous of anything which would deprive them of any control over the action.¹ But in England today, the parties apparently may make all rights under a contract conditional an arbitration by using language appropriate for the purpose.⁹ In many of the United States a doctrine similar to that adopted by the English courts seem to prevail.¹⁰ However, in many states, a distinction is made between an agreement to arbitrate the whole question of liability which is held ineffectual even though expressed in the form of a condition precedent, and an agreement which merely provides for the determination of a particular fact as for the valuation of loss or injury.¹¹ Of course, it has always been against the theory of the common law to uphold agreements ousting the courts of their jurisdiction,¹² but where the courts have control over the case as by a condition precedent or statutory arbitration the courts are not ousted of their jurisdiction and agreements which go no further than this are now held to be legal.¹³

⁶ *United Artist Corporation v. Piller* (N. Dak. 1932), 244 N. W. 20.

⁷ *Paramount Famous Lasky Corporation v. United States* (1930), 282 U. S. 30, 43.

⁸ *Scott v. Avery*, 5 H. L. Cas. 811; see also *U. S. Asphalt Refining Co. v. Trinidad Lake Petroleum Co.* (1915), 222 Fed. 1006.

⁹ *Scott v. Avery*, 5 H. L. C. 811; *Viney v. Bignold*, 29 Q. B. D. 172; *Manchester Ship Canal Co. v. Pearson* (1900), 2 Q. B. 606; *Spurrier v. La Cloche* (1902), A. C. 446; *Woodall v. Pearl Assurance Co.* (1919), 1 K. B. 593.

¹⁰ *Hamilton v. Home Ins. Co.* (1890), 137 U. S. 370, 11 S. Ct. 133; *Birmingham Ins. Co. v. Pulver* (1888), 126 Ill. 329, 18 N. E. 804; *Seward v. Rochester* (1888), 109 N. Y. 164, 16 N. E. 348.

¹¹ *Bauer v. Samson Lodge* (1885), 102 Ind. 262, 1 N. E. 571; *Supreme Council v. Garrigus* (1885), 104 Ind. 133, 3 N. E. 818; *Louisville, etc. Ry. Co. v. Donnegan* (1887), 111 Ind. 179, 12 N. E. 153; *Supreme Council v. Forsinger* (1890), 125 Ind. 52, 25 N. E. 129; *McCoy v. Able* (1891), 131 Ind. 417, 30 N. E. 528; *Miles v. Schmidt* (1897), 168 Mass. 339, 47 N. E. 115; *Meyers v. Jenkins* (1900), 63 Ohio State 224, 57 N. E. 1089; *Wyckoff v. Woarms* (1907), 118 N. Y. App. Div. 699, 103 N. Y. S. 650; *Maitland v. Reed* (1906), 37 Ind. App. 469, 77 N. E. 290; *Ditton v. Hart* (1911), 175 Ind. 181, 93 N. E. 961.

¹² *Kistler v. Indianapolis & St. L. R. R. Co.* (1882), 88 Ind. 460, 464; *The Supreme Council of the Order of Chosen Friends v. Forsinger* (1890), 125 Ind. 52, 55; *Meyers v. Jenkins* (1900), 63 Ohio State 224, 57 N. E. 1089.

¹³ H. E. Willis, *Indiana Annotations to the Restatement of the Law of Contracts* (1933), sec. 550; *Restatement to the Law of Contracts*, sec. 550; E. M. S. Steers, *Arbitration at Common Law in Indiana* (1929), 5 Ind. L. J. 175; *Hardware Dealers Mutual*

As arbitration clauses generally have been upheld as legal, it is extremely difficult to comprehend how they are illegal in this instance, unless such agreement is one of the provisions of a contract which is illegal because in restraint of trade. In other words, how can the arbitration stipulation be invalid while the contract is deemed valid? To defeat a contract as illegal because of it being in restraint of trade, it must appear that the contract is directly connected with the unlawful purpose and not merely collateral thereto.¹⁴ And contracts lawful on their face are illegal if in furtherance of a combination in itself illegal.¹⁵ In the instant case, it is obvious that the whole contract was in furtherance of the illegal combination of distributors and producers, it was the means to carry out the conspiracy. As far as the defendant is concerned, the vice is the contract and not merely the stipulation for arbitration since he was deprived of the freedom of contract which the law contemplates. The distributor is suing on the identical contract which was the evidence of the conspiracy and the object of the restraining decree in the Paramount case. The enforcement of the very instrumentality of the conspiracy itself, as done in this case, falls within the interdictum of the Supreme Court that an action cannot be maintained on a contract which is part of an unlawful conspiracy.¹⁶