Twombly and the Need to Plead Facts:

The Antitrust Decision Every Litigator Needs to Know

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The foundation of any litigation is the complaint, and more specifically, the allegations made to support the plaintiff's claims. Last month, the Supreme Court held in *Bell Atlantic Corp. v. Twombly* that bare assertions of conspiracy supported only by allegations of parallel conduct are not sufficient to state a claim that the major regional telephone companies illegally conspired not to compete with each other in violation of Section 1 of the Sherman Act. The Court fashioned a "plausibility standard" and held that a Section 1 claim requires a complaint with enough factual matter to suggest that an unlawful agreement was made and to inform the defendants of the challenged conduct in question. Beyond simply raising the bar on a particular type of antitrust claim under Section 1, *Twombly* undoubtedly will be used by defendants in many non-antitrust cases to challenge the sufficiency of pleadings under the Federal Rules.

In *Twombly*, plaintiffs filed a class action complaint on behalf of themselves and all individuals who purchased local telephone or high speed internet services within the United States between 1996 and the present. Plaintiffs alleged that the country's major providers of local telephone service had conspired not to compete with each other in their legacy markets and to prevent competitive entry into those markets. Because of the history of the telephone business in this country, the case had a heavy regulatory overlay.

As part of an extensive state and federal regulation scheme following the break-up of AT&T in 1984, defendants were effectively given monopoly power over local telephone services in their respective regions, but were restricted from competing in the long distance market and were required to provide exchange access to long distance carriers. The Telecommunications Act of 1996 was designed to replace the heavy regulatory structure of local telephone markets with competition. Under this law, the defendants were required to facilitate the entry of competitors into their respective local telephone markets in return for the opportunity to compete in the long distance telephone market.

In their complaint, the plaintiffs alleged that the defendants not only failed to comply with the Telecommunications Act, but that they did so pursuant to illegal agreements not to compete in the territories of the other defendants and to thwart the efforts of other new competitors. Plaintiffs alleged that the defendants' conspiracy was reflected in "parallel conduct" of not competing against each other in their respective local telephone markets. Plaintiffs alleged that this failure to compete was particularly telling because many of the territories serviced by defendants were non-contiguous and sometimes looped around territories served by one or more other defendants in ways that clearly invited entry in order to rationalize the service areas. Accordingly, Plaintiffs alleged that the defendants' collective failure to compete against each other was unlikely in the absence of an anticompetitive agreement between the defendants. In support of these allegations, plaintiffs pointed to a public statement by the CEO of Qwest that competing against the other defendants in their own territories "might be a good way to turn a quick dollar but that doesn't make it right." Plaintiffs argued that such a statement showed that competing against the other defendants in their markets would have been in the defendants' economic interests absent an agreement not to compete. Plaintiffs also alleged that the defendants frequently communicated with one another through industry organizations, and that the nature and structure of the market was such that a market allocation agreement could be maintained without frequent communications because any deviation from the alleged illegal agreement would be quickly discovered.

In a long, careful, and scholarly opinion, the district court concluded that plaintiffs failed to allege sufficient facts from which a conspiracy could be inferred and granted defendants' motion to dismiss. The opinion relies heavily on well-developed case law concerning the proof necessary for an antitrust plaintiff to survive summary judgment on a claim of conspiracy in a heavily concentrated market. In such markets, economic theory teaches that companies are likely to engage in parallel conduct without any actual

conspiracy. Therefore, under the Supreme Court's *Monsanto* and *Matsushita* decisions, proof of a Section 1 conspiracy must include evidence tending to exclude the possibility of independent action; thus, proof of parallel conduct is by itself insufficient to establish a Section 1 antitrust violation. In reaching its decision, the district court relied on the Second Circuit's related case law regarding Sherman Act claims at the summary judgment stage, requiring the plaintiff to establish at least one "plus factor" that tends to exclude independent self-interested conduct as an explanation for defendants' parallel behavior.

The district court noted that such plus factors include evidence that the parallel behavior would have been against the individual defendant's economic interest absent an illegal agreement or evidence that defendants possessed a strong motive to conspire. Although the district court noted that Rule 8 of the Federal Rules of Civil Procedure requires only a "short and plain statement of the claim," it held that plaintiffs' complaint was insufficient because (1) parallel behavior by competing companies is not itself illegal absent some agreement to restrain trade; and (2) allegations of plus factors are necessary to give defendants notice of plaintiffs' theory of conspiracy so that they can adequately prepare a defense. In essence, the district court found that the facts on which plaintiffs relied were consistent with independent action by these companies that had long enjoyed regulated monopolies and therefore would naturally be reluctant to disrupt the status quo by entering other territories.

Plaintiffs appealed to the Second Circuit, arguing that the district court incorrectly applied a standard of proof ordinarily applicable only at the summary judgment and trial stage. In addition, plaintiffs argued that even if there was a heightened pleading requirement, the district court erred by not accepting all of plaintiffs' allegations as true and by not drawing all inferences in plaintiffs' favor. The Second Circuit agreed with plaintiffs, finding that the Federal Rules did not require a heightened pleading standard for antitrust claims and that plaintiffs' allegations met the notice pleading standard.

The Supreme Court reversed the Second Circuit, largely adopting the district court's reasoning and analysis to require more than conclusory allegations that simply recite the claim elements. This decision is obviously important for antitrust, but the Court's reasoning led it to overrule a long-standing precedent that was important for all cases in the federal courts.

Rule 8(a)(2) of the Federal Rules requires that a complaint contain a "short and plain statement of the claim showing that the pleader is entitled to relief." It generally has been understood that under the Federal Rules, notice pleading replaced fact pleading and the merits of a claim were to be resolved during a flexible pretrial process and trial, if necessary. *Conley v. Gibson*, 355 U.S. 41 (1957), had long been the standard for determining the sufficiency of a pleading on a motion to dismiss and was frequently cited for the proposition that "a complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." Not surprisingly, the plaintiffs in *Twombly* placed heavy reliance on *Conley*, because "one set of facts" consistent with parallel conduct is that the defendants had entered into an illegal conspiracy. In *Twombly*, however, the Court stated: ". . . [T]his famous ["no set of facts"] observation has earned its retirement. The phrase is best forgotten as an incomplete, negative gloss on an accepted pleading standard." Rejecting Justice Steven's strong dissent in defense of *Conley* and the policy of notice pleading as established by the Federal Rules, the majority found that the passage from *Conley* should be interpreted in light of the plaintiffs' concrete allegations, which the Court found sufficiently stated a claim for relief: "*Conley* described the breadth of opportunity to prove what an adequate complaint claims, not the minimum standard of adequate pleading to govern a complaint's survival."

To overcome a motion to dismiss post-*Twombly*, there must now not only exist at least one set of facts in support of the plaintiff's claim, but plaintiff must also plead those facts in sufficient detail to make it "plausible" that a violation has occurred. The Court repeatedly stated that parallel conduct alone does not suggest conspiracy and "a conclusory allegation of agreement at some unidentified point does not supply facts adequate to show illegality." Indeed, the Court noted that apart from identifying the seven-year span during which the antitrust violations by defendants were alleged to have occurred, the plaintiffs' pleading "mentioned no specific time, place or person involved in the alleged conspiracies." As a result, the Court held that Plaintiffs'

complaint resulted in a lack of notice which would leave defendants "with little idea where to begin" in preparing their answer to the complaint.

The Court's "plausibility standard" in *Twombly* arises out of antitrust precedents which have recognized that certain business behavior is consistent not only with the existence of an illegal conspiracy, but also with rational and competitive business strategy independently driven by common perceptions of the market. Because of this acknowledged ambiguity of parallel conduct, the Court in *Twombly* therefore stated that a plaintiff's factual allegations must be enough to raise a right to relief "beyond a speculative level." For the purposes of stating a Section 1 claim, this means that allegations of parallel conduct must be placed in a context "that raises the suggestion of a preceding agreement, not merely parallel conduct that could just as well be independent action."

In reviewing the plausibility of the complaint in *Twombly*, the Court engaged in the same type of aggressive analysis done by the district court in concluding that plaintiffs' allegations were insufficient. For example, the Court went beyond the plaintiffs' allegations and conclusions on the face of the complaint to repeatedly characterize the defendants' conduct as "natural." This is somewhat puzzling as a court considering a motion to dismiss is required to assume all inferences in plaintiffs' favor. It seems at least equally natural for defendants' parallel behavior to be the result of an illegal agreement, especially considering that the defendants had long operated as state-sanctioned monopolists and no doubt preferred that life. Indeed, viewing the allegations most favorably to the plaintiffs, it would not be completely unreasonable to infer an illegal agreement between the defendants based upon the statement by Qwest's CEO and the defendants' opportunity to engage in discussions at trade association meetings, as alleged by plaintiffs. For example, in disputing the Court's finding that any inference of illegal agreement from defendants' parallel conduct is "implausible," Justice Stevens' dissent quoted Adam Smith for the perceptive observation that "people of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices."

The Court, however, neutralized the arguably suspicious statement by Qwest's CEO by looking to the CEO's other statements regarding the business uncertainty of competing against the other defendants. Furthermore, the Court dismissed the defendants' participation in trade associations as advancing the suggestion of an illegal agreement. In response to Justice Stevens' reliance on Adam Smith, the Court quipped that the great economist would be surprised that his tongue-in-cheek comment about trade guilds "would be authority to force his famous pinmaker to devote financial and human capital to hire lawyers, prepare for depositions, and otherwise fend off allegations of conspiracy." Although the Court acknowledged that a "few stray statements speak directly of agreement," it concluded that on a "fair reading," these were merely legal conclusions resting on prior allegations, which the Court found insufficient.

It is clear that the decision in *Twombly* was heavily influenced by the Court's reluctance to impose the heavy cost of discovery on the defendants in the absence of something more than what was in the pleadings. This impulse is understandable, but arguably inconsistent with many years of precedent under the Federal Rules. Under the notice pleading standards of Federal Rules, it has been the norm that the merits of cases would be tested during the pretrial process, not at the pleading stage. The Court, however, clearly required more fact allegations at the pleading stage. For example, the Court noted that the *Twombly* plaintiffs represented a putative class of at least 90% of all subscribers of local telephone and Internet services in the United States in a case against the nation's largest telecommunications firms which have "gigabytes of business records." Finding that the threat of discovery expense will compel some defendants to settle even marginal claims before ever reaching the summary judgment stage, the Court stated that only by requiring more factual allegations at the pleading stage will the potentially enormous expense of discovery be avoided in cases where there is no "reasonably founded hope that the discovery process will reveal relevant evidence" in support of plaintiffs' claims. The Court expressly rejected the argument that this problem could be handled through effective judicial management. The Court did not dispute that such problems were the proper subject of judicial management. Rather, the Court was expressly skeptical of the ability of judges to manage such a large and complex case effectively.

Of course, antitrust cases are not alone in being large, expensive and difficult to manage, or being inviting targets for plaintiffs on fishing expeditions. It is unclear how far *Twombly* will be applied, but clearly defendants in many different types of cases will now argue that the expense of discovery should not be imposed unless the plaintiff shows that its claims are more plausible, not just possible. This may be especially true in cases such as securities litigation (or even trade secret misappropriation) where the behavior by the defendant may be subject to conflicting inferences and detailed facts in support of alleged wrongdoing is unavailable to the plaintiff before filing suit. It remains to be seen whether *Twombly* will serve generally as support for more aggressive court review of a plaintiff's pleading allegations and possible inferences. It is possible that the Court's probing analysis in *Twombly* will be confined specifically to antitrust cases, which are increasingly governed by economic analysis and invite – if not require – such review in light of their ambiguous facts.

Just two weeks after deciding *Twombly*, the Supreme Court issued a *per curiam* decision that provides additional information about the continuing role of notice pleading in the federal courts. *Erickson v. Pardus* involved the sufficiency under Rule 8 of a prisoner's pleading of constitutional violations by the prison officials who allegedly wrongfully terminated medical treatment of the prisoner's liver condition. The Tenth Circuit affirmed the dismissal of the complaint on the grounds that it was conclusory. The Supreme Court reversed. In holding that the pleading was sufficient, the Court remarked that compliance with Rule 8 does not require specific facts but only fair notice of what the claim is and the grounds upon which it rests, even citing *Twombly* for a quote from *Conley* in support. However, the Court in *Erickson* found that the plaintiff had alleged that the termination of the medical treatment endangered his life and "bolstered his claim by making more specific allegations in documents attached to the complaint and later filings." On these facts, the Court found that Rule 8 had been satisfied and held that the Tenth Circuit erred in finding the plaintiff's allegations too conclusory regarding the "substantial harm" caused by the defendants' actions. Moreover, *Erickson* is supported by the legal rule that documents filed by *pro se* litigants are to be liberally construed and must be held to less stringent standards than formal pleadings drafted by lawyers. In short *Erickson* is a very different kind of case from *Twombly*, and it remains to be seen what the impact of *Twombly* will be in the large commercial cases that more nearly resemble it.

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