

## Three Limitations of Twombly: Antitrust Conspiracy Inferences in a Context of Historical Monopoly

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## SYMPOSIUM

# THREE LIMITATIONS OF *TWOMBLY*: ANTITRUST CONSPIRACY INFERENCES IN A CONTEXT OF HISTORICAL MONOPOLY

J. DOUGLAS RICHARDS†

### INTRODUCTION

In *Bell Atlantic Corp. v. Twombly*,<sup>1</sup> the Supreme Court has thrown litigants and lower courts into confusion by consigning to the dustbin key phraseology<sup>2</sup> that has served as a guiding light on motions to dismiss for half a century: that a motion to dismiss should be denied “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.”<sup>3</sup> Because that venerable phrase was an old friend to attorneys who actively litigate, the Supreme Court’s rejection of it has led many to sense a cataclysmic change in the legal landscape.<sup>4</sup> Other decisions rendered by the Court

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<sup>1</sup> 127 S. Ct. 1955 (2007).

<sup>2</sup> See *id.* at 1969 (“*Conley*’s ‘no set of facts’ language has been questioned, criticized, and explained away long enough. . . . [T]his famous observation has earned its retirement.”).

<sup>3</sup> *Conley v. Gibson*, 355 U.S. 41, 45–46 (1957), *overruled in part by Bell Atl. Corp. v. Twombly*, 127 S. Ct. 1955 (2007).

<sup>4</sup> See Keith Bradley, *Pleading Standards Should Not Change After Bell Atlantic v. Twombly*, 102 NW. U. L. REV. COLLOQUY 117, 117 (2007), <http://www.law.northwestern.edu/lawreview/colloquy/2007/31/LRColl2007n31Bradley.pdf> (noting that many view the *Twombly* decision as “a sweeping revision of the standards for civil pleadings and dismissals in general” and acknowledging that this view “seems to have prevailed”); Scott Dodson, *Pleading Standards After Bell Atlantic Corp. v. Twombly*, 93 VA. L. REV. IN BRIEF 135, 138 (2007), <http://www.virginialawreview.org/inbrief/2007/07/09/dodson.pdf> (“[T]he Court’s opinion presages more expansive application. . . . The best reading of *Bell Atlantic* is that the new standard is

since *Twombly* indicate, however, that fears of a major legal earthquake are overblown. In particular, in *Erickson v. Pardus*,<sup>5</sup> the Court strongly reaffirms key elements of historical pleading standards, stating that pleading “[s]pecific facts” is not necessary and that all factual allegations made in a complaint must be accepted as true<sup>6</sup>—neither of which, on first reading, the Court would seem to have applied in *Twombly*. Clearly, therefore, a close reading of the *Twombly* opinion is in order, to discern which ground rules have and have not been changed.

Although *Twombly* is the first Supreme Court decision to reference a “plausibility” requirement in connection with antitrust allegations on a motion to dismiss, it is significant that the Second Circuit’s reversed opinion in *Twombly*—which was generally perceived to be largely consistent with *Conley v. Gibson*<sup>7</sup>—also had held that “plausibility” is necessary to satisfy governing pleading standards in an antitrust conspiracy case.<sup>8</sup> The Second Circuit stated, in *Twombly*, that an antitrust conspiracy complaint must “include conspiracy among the realm of plausible possibilities,” and found that the allegations of conspiracy that were made in the case comfortably did so.<sup>9</sup> Because the Second Circuit professed to harmonize its own “plausibility” requirement with the any “set of facts” formulation of *Conley*,<sup>10</sup> its opinion was not perceived to effect major changes comparable to those feared from the Supreme Court’s opinion. In fact, the relative complacency that attended the Second Circuit’s decision was well-founded, since, as a matter of common usage, it is obvious that a requirement that an antitrust conspiracy complaint be merely “plausible” is not intended to raise pleading requirements very high. That is clear from principles strongly reaffirmed in *Twombly* itself, such as that a complaint that satisfies the Court’s new “plausibility” standard must be sustained “even if it strikes a savvy judge that actual proof of those facts alleged is

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absolute, that mere notice pleading is dead for all cases and causes of action.”).

<sup>5</sup> 127 S. Ct. 2197 (2007).

<sup>6</sup> *Id.* at 2200.

<sup>7</sup> 355 U.S. at 45–46 (1957).

<sup>8</sup> See *Twombly v. Bell Atl. Corp.*, 425 F.3d 99, 111 (2d Cir. 2005) (quoting *Asahi Glass Co. v. Pentech Pharm., Inc.*, 289 F. Supp. 2d 986, 995 (N.D. Ill. 2003) (Posner, J., sitting by designation)), *rev'd*, 127 S. Ct. 1955 (2007).

<sup>9</sup> *Id.* at 111–12.

<sup>10</sup> See *id.* at 111, 114.

improbable, and ‘that a recovery is very remote and unlikely.’”<sup>11</sup> In addition, the Court makes clear in *Twombly* that it is “not impos[ing] a probability requirement” for any facts that are alleged.<sup>12</sup>

The *Twombly* opinion confines itself narrowly to the specific question and context presented, and does little to explain whether or how broadly the standards that it articulates for the case at hand should be applied in other contexts. The contention of this Paper is that to the extent that *Twombly* raises the bar for pleadings, it does so only in the very narrow context of (1) antitrust conspiracy complaints; (2) only when those complaints explicitly rest allegations of conspiracy on pleaded inferences rather than factual allegations; and (3) in the unique historical context of the telecommunications industry. Lower courts should not assume that *Twombly* supports or portends significant changes in other contexts, unless and until the Supreme Court so states in a future case. It certainly has not so stated in *Twombly*.<sup>13</sup>

#### I. LIMITATION TO ANTITRUST CONSPIRACY

All of the references in *Twombly* to a “plausibility” requirement are couched in relation to allegations of antitrust conspiracy, and not to the pleading of claims generally.<sup>14</sup> Thus, the introductory section of the Court’s analysis takes pains to place the decision in the limited context of unique antitrust rules that are designed to guard, in the antitrust conspiracy context, against possible “false inferences from identical

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<sup>11</sup> *Twombly*, 127 S. Ct. at 1965.

<sup>12</sup> *Id.*

<sup>13</sup> At the time of publication, the only United States Court of Appeals that appears to have considered in detail whether *Twombly* is limited in ways analogous to those suggested here is the Second Circuit, principally in *Iqbal v. Hasty*, 490 F.3d 143 (2d Cir. 2007). Although the court in *Iqbal* did not embrace such limitations, it did discuss at length the language in *Twombly* that supports limiting it “only to section 1 allegations based on competitors’ parallel conduct or, slightly more broadly, only to antitrust cases.” *Id.* at 157–58. A dissent in the case suggests that *Twombly* is “less than crystal clear and fully deserve[s] reconsideration by the Supreme Court at the earliest opportunity” with regard to such questions. *Id.* at 178.

<sup>14</sup> See, e.g., *id.* at 1964 (“This case presents the antecedent question of what a plaintiff must plead in order to state a claim under § 1 of the Sherman Act.”); *id.* at 1965–66 (“In identifying facts that are suggestive enough to render a § 1 conspiracy plausible, we have the benefit of the prior rulings and considered views of leading commentators . . .”).

behavior at a number of points in the trial sequence.”<sup>15</sup> After a summary of conventional pleading standards in general, the opinion expresses the requirement of “plausibility” only in the course of “applying these general standards to a § 1 claim”<sup>16</sup>—i.e., in stating standards specifically applicable to antitrust conspiracy claims. The Court then makes plain that its limited purpose in granting certiorari was “to address the proper standard for pleading an antitrust conspiracy through allegations of parallel conduct.”<sup>17</sup> Importantly, nowhere in the entire *Twombly* opinion is the “plausibility” requirement said to be applicable outside the context of antitrust conspiracy. Instead, the structure and content of the *Twombly* opinion indicate that the “plausibility” requirement that *Twombly* articulates is a narrow standard, specially tailored for limited use only in the specific context of antitrust conspiracy allegations.

It is entirely plausible that a distinct procedural rule might be applicable only in antitrust conspiracy cases, which have been the subject of various distinct procedural rules at least since *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*<sup>18</sup> Indeed, one of the issues that was heavily contested by the parties in the briefs in *Twombly* was whether the sufficiency of allegations of antitrust conspiracy under Federal Rule of Civil Procedure 12(b)(6) should properly be controlled by general pleading standards, as the respondents contended, or whether substantive antitrust law required a higher standard in the particular context of antitrust conspiracy allegations, as was advocated by both the petitioners and the Solicitor General.<sup>19</sup> The Supreme Court’s adoption of a “plausibility” requirement for antitrust conspiracy cases clearly reflects an acceptance of the point of view advocated by petitioners and the Solicitor General, that substantive antitrust law requires that a unique “plausibility” standard be satisfied in the specific context of antitrust conspiracy allegations. Thus, there would be no more justification for applying *Twombly*’s “plausibility” requirement

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<sup>15</sup> *Id.* at 1964.

<sup>16</sup> *Id.* at 1965.

<sup>17</sup> *Id.* at 1963 (emphasis added).

<sup>18</sup> 475 U.S. 574 (1986).

<sup>19</sup> See Reply Brief of Petitioner at 8–16, *Twombly*, 127 S. Ct. 1955 (No. 05-1126), 2006 WL 3265610.

than *Matsushita's* unique summary judgment standards,<sup>20</sup> in cases that assert claims not based on antitrust conspiracy. Just as courts generally have not applied *Matsushita* outside the context of antitrust conspiracy,<sup>21</sup> they should not apply *Twombly's* "plausibility" standard in other contexts absent further opinions from the Supreme Court suggesting that to do so would be appropriate.

## II. LIMITATION TO PLEADED INFERENCES

Even in the context of antitrust conspiracy cases, the *Twombly* opinion makes very clear that its analysis is applicable only to those antitrust complaints that rest their conspiracy allegations solely on allegations of inferences from "descriptions of parallel conduct and not on any independent allegation of actual agreement."<sup>22</sup> This characterization of the allegations in *Twombly* is consistent throughout the Supreme Court's opinion. For example, the opinion's second sentence states that the limited question presented is "whether a § 1 complaint can survive a motion to dismiss when it alleges that major telecommunications providers engaged in certain parallel conduct unfavorable to competition, absent some factual context suggesting agreement, as distinct from identical, independent action."<sup>23</sup> The Court does observe that the complaint contained "a few stray statements" that "speak directly of agreement," but concludes, "on fair reading these are merely legal conclusions resting on the prior allegations."<sup>24</sup>

Importantly, to the extent that a complaint for antitrust conspiracy alleges any facts suggestive of conspiracy, nothing in *Twombly* invites a court to determine whether those factual allegations are themselves "plausible." On the contrary, the

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<sup>20</sup> See *Matsushita*, 475 U.S. at 588 ("To survive a motion for summary judgment or for a directed verdict, a plaintiff seeking damages for a violation of § 1 must present evidence 'that tends to exclude the possibility' that the alleged conspirators acted independently.").

<sup>21</sup> See Thomas A. Piraino, Jr., *Regulating Oligopoly Conduct Under the Antitrust Laws*, 89 MINN. L. REV. 9, 28–29 (2004); Spencer Weber Waller, *Matsushita at Twenty: A Conference Introduction*, 38 LOY. U. CHI. L.J. 399, 401–02 (2007); see also Herbert Hovenkamp, *The Rationalization of Antitrust*, 116 HARV. L. REV. 917, 926, 935 (2003) (reviewing RICHARD A. POSNER, *ANTITRUST LAW* (2001)).

<sup>22</sup> *Twombly*, 127 S. Ct. at 1970.

<sup>23</sup> *Id.* at 1961.

<sup>24</sup> *Id.* at 1970.

Court takes pains in *Twombly* to make clear that it is not inviting lower courts to determine whether they believe or disbelieve facts alleged in an antitrust conspiracy complaint, stating that it is "not impos[ing] a probability requirement" for any facts that are alleged.<sup>25</sup> For example, if a complaint were to allege outright that particular individuals conspired with one another, or that a particular trade organization coordinated conspiratorial communications among antitrust defendants, those facts must be accepted as true for purposes of a motion to dismiss. Instead, the "plausibility" requirement of *Twombly* is carefully made applicable by the opinion only to pleaded inferences of conspiracy, and not to factual allegations of conspiracy, when such allegations are made in a complaint.<sup>26</sup> This consideration is likely to limit the scope of *Twombly*'s "plausibility" requirement considerably, since relatively few antitrust conspiracy complaints will rest, as the complaint did in *Twombly*, exclusively on pleaded inferences from parallel conduct and mere general market structure.

### III. LIMITATION TO THE TELECOMMUNICATIONS CONTEXT

Even in those relatively few cases that make allegations of antitrust conspiracy based entirely on proposed inferences from parallel conduct and market structure, *Twombly* should have limited impact since its fundamental rationale will have little application outside the telecommunications industry. The *Twombly* opinion begins by reciting some basic history of that industry,<sup>27</sup> which ultimately plays a pivotal role in its analysis. Before focusing closely on that later analysis, some additional background about the telecommunications industry is

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<sup>25</sup> *Id.* at 1965.

<sup>26</sup> The meaning of this distinction may be elucidated by the assertion of Justice Souter at oral argument in *Twombly*, that the plaintiffs had "by their pleadings, in effect, affirmatively indicated that they don't have enough facts to support a general allegation." Transcript of Oral Argument at 9-10, *Twombly*, 127 S. Ct. 1955 (No. 05-1126). In other words, even if a complaint were simply to allege outright that a conspiracy existed, the complaint would state a claim. The problem that the Court found in the *Twombly* complaint stemmed from the fact that it purported only to draw an inference of conspiracy from allegations of marketplace conduct that the Supreme Court believed could not reasonably give rise to such an inference, for reasons discussed in Part III *infra*.

<sup>27</sup> See *Twombly*, 127 S. Ct. at 1961-62, 1962 n.1.

appropriate in order to put the factual context of *Twombly* into clearer focus.

Prior to the divestiture of AT&T's local telephone business in 1984, telephone service was considered to be the textbook example of a so-called "natural monopoly" in which, due largely to enormous fixed costs of installing telephone wires into individual homes, the "natural outcome" of an unregulated environment was monopoly rather than a competitive industry.<sup>28</sup> Long-distance telephone service was separated from local service in connection with the 1984 divestiture, and was made competitive on the premise that it did not require the same massive investment to install wires into individual homes that was required for local telephone service.<sup>29</sup> The business of local telephone service continued to function as a monopoly, however, until the Telecommunications Act of 1996 ("1996 Act"),<sup>30</sup> a primary object of which was to make local telephone service competitive.<sup>31</sup>

To overcome basic hindrances that had made local service a "natural monopoly," the 1996 Act imposed certain legal obligations on the regional service monopolies that were somewhat "socialist" in their character, and that many perceived to be at odds with traditional competitive principles of the American economy.<sup>32</sup> Specifically, as the *Twombly* opinion points out, the 1996 Act effectively required each of the regional service monopolists to share its network with competitors.<sup>33</sup> In *Verizon Communications, Inc. v. Law Offices of Curtis V. Trinko*,<sup>34</sup> the quasi-socialist character of this obligation to share wires with competitors seems to have played an important role

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<sup>28</sup> *Id.* at 1972; *Verizon Commc'ns, Inc. v. F.C.C.*, 535 U.S. 467, 477-78 (2002); PETER W. HUBER, MICHAEL K. KELLOGG & JOHN THORNE, *THE TELECOMMUNICATIONS ACT OF 1996: SPECIAL REPORT 3* (1996).

<sup>29</sup> *See Twombly*, 127 S. Ct. at 1961; HUBER ET AL., *supra* note 28, at 17 (discussing incumbent local exchange carriers' obligation to house competitive local exchange carriers' network transmission equipment).

<sup>30</sup> Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (codified in scattered sections of 47 U.S.C.).

<sup>31</sup> *Twombly*, 127 S. Ct. at 1961; 74 AM. JUR. 2D *Telecommunications* § 16 (2007).

<sup>32</sup> *See Twombly*, 127 S. Ct. at 1961-62; HUBER ET AL., *supra* note 28, at 11-12 (listing the obligations imposed upon the incumbent local telephone service providers and the competitors).

<sup>33</sup> *Twombly*, 127 S. Ct. at 1961 (quoting *Verizon Commc'ns, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398, 402 (2004)).

<sup>34</sup> 540 U.S. 398 (2004).

in the Court's decision, which limited the application of antitrust law to the telecommunications industry in the different context of a monopolization claim. Thus, the Supreme Court, in *Trinko*, observed as follows:

Compelling such firms to share the source of their advantage is in some tension with the underlying purpose of antitrust law, since it may lessen the incentive for the monopolist, the rival, or both . . . . Enforced sharing also requires antitrust courts to act as central planners, identifying the proper price, quantity, and other terms of dealing—a role for which they are ill suited.<sup>35</sup>

In light of this quasi-socialist “central planning” character of the sharing obligation under the 1996 Act, the Supreme Court, in *Trinko*, evidently viewed unilateral conduct calculated to defeat that sharing obligation as being uniquely forgivable as a matter of antitrust policy, stating that because the 1996 Act seeks to “eliminate” monopolies while antitrust policy merely seeks to prevent the creation of them by unlawful conduct, “[t]he 1996 Act is, in an important respect, much more ambitious than the antitrust laws.”<sup>36</sup>

Echoes of those views from *Trinko* survive in the following passage of the *Twombly* opinion, in which the Court expresses its evident strong conviction that an alternative explanation, and not conspiracy, explains the stark absence of competition among the incumbent local telephone service providers (“ILECs”) as competitors (“CLECs”) in one another's territories, upon which the complaint in *Twombly* was fundamentally premised:

[The ILECs' non-competition with one another as CLECs] was not suggestive of conspiracy, not if history teaches anything. In a traditionally unregulated industry with low barriers to entry, sparse competition among large firms dominating separate geographical segments of the market could very well signify illegal agreement, but here we have an obvious alternative explanation. In the decade preceding the 1996 Act and well before that, monopoly was the norm in telecommunications, not the exception. The ILECs were born in that world, doubtless liked the world the way it was, and surely knew the adage about him who lives by the sword. Hence, a natural explanation for the noncompetition alleged is that the former Government-

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<sup>35</sup> *Id.* at 407–08.

<sup>36</sup> *Id.* at 415.

sanctioned monopolists were sitting tight, expecting their neighbors to do the same thing.<sup>37</sup>

This is the most pivotal text in the *Twombly* opinion. Significantly, the Court itself hypothesizes a mutually interdependent state of mind as the “natural” explanation of the ILECs’ non-competition with one another as CLECs. In the ordinary sense of the word “plausible,” it would certainly seem “plausible” to suggest that such a mutually interdependent state of mind may have been supported by unlawful communications between the ILECs, at a time when the ILECs clearly were regularly working together intensely to attempt to effect a legislative repeal of the sharing obligation itself. The Court, however, seems to have viewed such a mutually interdependent plan of the ILECs to avoid competition with one another to be uniquely “natural” and benign, in light of the “history” of the ILECs as government-sanctioned monopolies.<sup>38</sup> Similarly, the Court’s opinion seems dismissive of the expectations of Congress that the ILECs would compete with one another as CLECs, stating that “Congress may have expected some ILECs to become CLECs in the legacy territories of other ILECs, but the disappointment does not make conspiracy plausible.”<sup>39</sup>

In sum, the Court’s reasoning in *Twombly* seems to be based largely on a belief that the fundamental expectation embodied in the 1996 Act—that the ILECs acting in their own economic self-interests would seek to compete as CLECs in one another’s territories—was unrealistic from the outset and was contrary to natural competitive impulses that antitrust policy in a competitive economy generally seeks to nurture. Indeed, that

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<sup>37</sup> *Twombly*, 127 S. Ct. at 1972 (citation omitted).

<sup>38</sup> *Id.* at 1975 (Stevens, J., dissenting).

<sup>39</sup> *Id.* at 1973 (majority opinion); see also *id.* at 1972 (characterizing the failure of the ILECs to compete with one another as having been merely “[c]ontrary to hope”). Additional indications of the Court’s idiosyncratically dim view of the expectations of Congress in the 1996 Act may be found in Justice Scalia’s statement at oral argument that “I used to work in the field of telecommunications and if the criterion is that happens which Congress expected to happen when it passed its law, your case is very weak.” Transcript of Oral Argument at 49, *Twombly*, 127 S. Ct. 1955 (No. 05-1126). The author’s recollection is that Justice Scalia said that his son had worked in the telecommunications industry, not that Justice Scalia himself had done so, as the transcript currently available on the Court’s website indicates. For present purposes, however, the significance of Justice Scalia’s statement is unaffected by this difference.

bias seems fundamentally to have slanted the Court's reading of the actual allegations made in *Twombly*, given that the Court states that the *Twombly* complaint "does not allege that competition as CLECs was potentially any more lucrative than other opportunities being pursued by the ILECs during the same period."<sup>40</sup> In fact, the complaint in *Twombly* plainly did allege that competition of the ILECs with one another as CLECs was "an especially attractive business opportunity."<sup>41</sup> Only remarkably finicky reasoning would draw a critical distinction between alleging that competition with one another as CLECs would have been "more lucrative than other opportunities,"<sup>42</sup> and the allegation, which clearly was made in *Twombly*, that it would have been "an especially attractive business opportunity."<sup>43</sup> The Supreme Court, in *Twombly*, seems to have premised its analysis on so microscopic a distinction only because, as is manifest in *Trinko*, the Justices idiosyncratically perceived the "sharing" obligations of the 1996 Act—notwithstanding their enactment by Congress in formal legislation—to have been unrealistic and fundamentally contrary to the economic self-interests of each of the ILECs.

Ordinary procedural norms would suggest that such judgments should be reserved until a later stage of the proceedings, so that a court would have the benefit of evidence from discovery and expert analyses before making them. That seems particularly true in view of the fact that even the Solicitor General's brief in *Twombly*, while advocating a heightened pleading standard, twice conceded that whether such a heightened standard would be satisfied by the allegations in *Twombly* was a "close question."<sup>44</sup> The Court in *Twombly*, however, seems to have felt that it knew enough to make that judgment without any assistance, in the specific context of the telecommunications industry.

It seems improbable that many future antitrust cases arising outside the telecommunications industry will provide such a basis for trumping inferences from evidently non-

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<sup>40</sup> *Twombly*, 127 S. Ct. at 1972.

<sup>41</sup> Consolidated Amended Class Action Complaint ¶ 40, *Twombly v. Bell Atl. Corp.*, 313 F. Supp. 2d 174 (S.D.N.Y. Apr. 14, 2003) (No. 02-CV-10220).

<sup>42</sup> *Twombly*, 127 S. Ct. at 1972.

<sup>43</sup> Consolidated Amended Class Action Complaint, *supra* note 41, ¶ 40.

<sup>44</sup> Brief for Solicitor General as Amicus Curiae Supporting Respondents at 26, *Twombly*, 127 S. Ct. 1955 (No. 05-1126).

competitive behavior, based on a prior history of government-sanctioned monopolies. Indeed, the Court, in *Twombly*, hastens to point out that the same pattern of behavior alleged in the *Twombly* complaint would in fact be suggestive of a “plausible” conspiracy in most other contexts.<sup>45</sup> Ultimately, therefore, *Twombly* is best perceived as stemming uniquely from this Court’s idiosyncratic skepticism concerning perceived economic unrealism of the “sharing” obligations contained in the 1996 Act. *Twombly* thus should have limited impact in future antitrust conspiracy cases, even when those cases are based solely on pleaded inferences from mere market behavior, as the Court concluded—rightly or wrongly—that the *Twombly* case was, rather than on facts or events indicative of conspiracy.

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<sup>45</sup> *Twombly*, 127 S. Ct. at 1972 (“In a traditionally unregulated industry with low barriers to entry, sparse competition among large firms dominating separate geographical segments of the market could very well signify illegal agreement.”).

