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BELL ATLANTIC v. TWOMBLY: **HIGH COURT SHOULD REVERSE** **IN ANTITRUST CLASS ACTION**

by

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On November 27th, the U.S. Supreme Court will hear oral argument in *Bell Atlantic Corp. v. Twombly*. On its face, *Twombly* is merely another in a long line of cases seeking to define what, precisely, the Federal Rules of Civil Procedure mean when they say that a pleading must “set[] forth a ... short and plain statement of the claim showing that the pleader is entitled to relief.” In fact, however, the case raises three important and potentially far-reaching issues.

First, the case could enhance the plaintiffs’ bar’s ability to hijack federal courts and extort what the Solicitor General described in his brief supporting the petitioners as “*in terrorem* settlements.” The U.S. Court of Appeals for the Second Circuit held that a complaint must survive a motion to dismiss unless there exists “*no set of facts*” that would entitle the plaintiff to relief. The Supreme Court should correct this misreading of the Federal Rules of Civil Procedure and help return federal courts to the business of resolving real disputes brought by real people who have suffered real grievances.

Second, *Twombly* could relax the pleading standards for Sherman Act Section 1 cases, giving further ammunition to the plaintiffs’ bar. Supreme Court jurisprudence clearly requires something more than mere parallel conduct among competitors to find a Section 1 violation. The Second Circuit, however, held that an antitrust claim could in essence be based on parallel conduct and still survive dismissal. If not reversed by the Supreme Court, this holding would open the floodgates for additional extortionate lawsuits by the plaintiff’s bar.

Third, taken to its logical conclusion, this case could force companies to enter unprofitable markets. A decision regarding whether to invest resources in a particular opportunity or market is a complex one that involves the weighing of long-term costs and benefits. If the Second Circuit’s decision is affirmed, this calculus will be disrupted by increased exposure to antitrust claims should the company decide not to embark on a risky new venture. The antitrust laws were not designed to interfere with independent business judgments such as these.

Background. The telecommunications industry was a fertile ground for litigation even before the Department of Justice initiated its lawsuit against AT&T in the 1970s. Congress sought to increase competition in the telecommunications industry by passing the Telecommunications Act of 1996. The Act permitted the

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largest providers of local telephone services to offer long-distance services, but only after they demonstrated to the Federal Communications Commission (“FCC”) that they had opened their local markets to competition. One by-product of this requirement was that it stanching the decades-long flow of litigation by transferring regulatory control of telecommunications markets from the United States District Court for the District of Columbia back to the FCC. The plaintiffs’ bar, unhappy with that aspect of the Act, has been trying to re-inject the federal courts into the industry ever since.

The plaintiffs’ bar suffered a major defeat two years ago in *Law Offices of Curtis V. Trinko v. Bell Atlantic Corp.* In *Trinko*, plaintiffs alleged that defendants’ failure to open their local and high-speed Internet networks constituted “exclusionary conduct” and therefore violated Section 2 of the Sherman Act. This “exclusion” purportedly involved twelve categories of conduct in which the phone companies allegedly avoided their obligations to share their local and high-speed Internet networks with competitors. Following another unfortunate Second Circuit decision, *Trinko* reached the Supreme Court. The Supreme Court reversed, holding that the antitrust laws do not require one competitor to provide assistance to another, absent extraordinary circumstances. See *Trinko*, 540 U.S. 398, 409 (2004).

Before the Supreme Court’s ruling in *Trinko*, Milberg Weiss Bershad Hynes & Lerach LLP filed a copycat case. After the Supreme Court issued its opinion in *Trinko*, Milberg withdrew the complaint, recognizing that *Trinko* spelled doom for its claims. Milberg Weiss then re-filed the complaint on behalf of the same plaintiff, challenging precisely the same twelve categories of “exclusionary conduct” that the Supreme Court had found insufficient to state a claim under Section 2 in *Trinko*. In the new complaint, however, Milberg Weiss also claimed that the defendants had failed to enter each others’ local markets pursuant to a conspiracy in violation of Sherman Act Section 1. The complaint did not contain any specific allegations of misconduct. Rather, it asserted that the apparent absence of local market competition contemplated by the Telecommunications Act “would be anomalous in the absence of an agreement.”

The District Court dismissed the new *Twombly* complaint. The court found that the plaintiffs’ allegations of parallel conduct, together with the simple conclusion that the conduct was the result of a conspiracy, did not state a claim under Section 1. The court explained that the alleged facts, even if proven, would not entitle the plaintiffs to substantive relief under the Sherman Act. 313 F. Supp. 2d 174 (S.D.N.Y. 2003). To survive a motion to dismiss under Rule 8(a), the court held, a plaintiff must plead facts demonstrating that the parallel conduct was the result of something other than the defendants’ individual self-interest.

The Second Circuit reversed. According to the Second Circuit, the pleading standard permits dismissal only where “there is no set of facts that would permit a plaintiff to demonstrate that the particular parallelism asserted was the product of collusion rather than coincidence.” 425 F.3d 99, 114 (2d Cir. 2005). The Second Circuit held that if a conspiracy is “among the realm of plausible possibilities” presented by the allegations, then the complaint can survive a motion to dismiss. *Id.*

Issue Before the Court. The incumbent local exchange carriers petitioned for *certiorari*. The Supreme Court granted the petition to decide whether a plaintiff satisfies the standard under Rule 8 by baldly asserting the existence of an illegal conspiracy. The Supreme Court should reverse. The Second Circuit’s decision that such an assertion does satisfy Rule 8 contradicts basic principles underlying the Federal Rules of Civil Procedure, well-established Supreme Court precedent governing the pleading standard required by Rule 8, and substantive principles of antitrust law. The Second Circuit confused the notion of a “heightened” pleading standard, which the Rules do not require, with the requirement that the complaint allege facts that, if proven true, would entitle the plaintiff to relief.

The Supreme Court consistently has held that a plaintiff must allege actual facts in order to present a justiciable claim.¹ The Court also has made clear that the plaintiffs’ allegations must be judged against the

¹See, e.g., *Dura Pharmaceuticals, Inc. v. Broudo*, 544 U.S. 336 (2005) (allegation of the causation element – necessary under the substantive law governing private securities fraud claims – lacked sufficient factual detail to survive dismissal under Rule 8); *Verizon Comm’ns, Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398 (2004) (bare allegation of anticompetitive exclusion insufficient to state a claim because it failed to allege facts establishing a refusal to deal, as required under the substantive law governing Section 2 claims);

backdrop of the law that governs the claim. Thus, the inquiry under Rule 12(b)(6) is whether, if the facts alleged in the complaint were true, they would entitle the plaintiff to relief under the substantive law. If so, the complaint satisfies Rule 8(a). If not, it must be dismissed for failure to state a claim. *See* Wright & Miller § 1218, at 273 (“[T]he appropriate generality for a pleading depends on the particular issue in question or the substantive context of the case before the court.”).

The Court’s opinion in *Swierkiewicz v. Sorema N.A.*, 534 U.S. 506 (2002), upon which the Second Circuit relied heavily, does not suggest otherwise. *Swierkiewicz* asked whether a plaintiff bringing federal employment discrimination claims was required to establish a “prima facie case of discrimination” at the pleading stage. In *Swierkiewicz*, the Supreme Court concluded that the plaintiff did not face such a burden. As the Court explained, however, the “prima facie case” construct is not an element of a claim of discrimination but a burden-shifting evidentiary construct created by the Court in *McDonnell Douglas Corp. v. Green*, 411 U.S. 792 (1973), 534 U.S. at 508. The Court’s decision not to import a mere *evidentiary* standard into a pleading-stage analysis is entirely consistent with its practice of analyzing the sufficiency of a complaint in light of the *substantive* requirements of the applicable law. *See Swierkiewicz*, 534 U.S. at 510 (the “prima facie case” is only “an evidentiary standard, not a pleading requirement”); *supra* note 1.

Twombly simply did not allege sufficient facts to state a claim. The Supreme Court’s antitrust jurisprudence makes clear that a plaintiff cannot recover damages for an unlawful conspiracy under Section 1 of the Sherman Act without affirmatively refuting that the allegedly conspiratorial conduct was the product of rational, self-interested behavior. In other words, to be successful, a plaintiff must do more than allege rationally based parallel conduct. The Second Circuit acknowledged as much in *Twombly*:

In a case brought under Section 1 of the Sherman Act . . . “the range of permissible inferences from ambiguous evidence” is limited[], because antitrust laws prohibit only contracts, combinations, or conspiracies – and not independent parallel conduct – that operate unreasonably to restrain trade Although “[p]arallel conduct can be probative evidence bearing on the issue of whether there is an antitrust conspiracy,” . . . it may also, as the district court in the instant case pointed out, “simply [be] the result of similar decisions by competitors who have the same information and the same basic economic interests.” Accordingly, in a Section 1 case where there is no “direct, ‘smoking gun’ evidence,” conduct as consistent with permissible competition as with illegal conspiracy does not, standing alone, support an inference of antitrust conspiracy. 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.

425 F.3d at 113-14 (quoting *Matsushita*, 475 U.S. 574, 588 (1986); *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 764 (1984); *Twombly*, 313 F. Supp. 2d at 181) (other citations and quotations omitted). *Accord* Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 1410a, at 59-61 (2d ed. 2002).

Applying the standard pleading rules and the substantive antitrust law requires that a pleading include more than general allegations of an agreement or conspiracy based solely on parallel behavior.² Nevertheless, the Second Circuit concluded only that the “pleaded factual predicate must include conspiracy among the realm of ‘plausible’ possibilities in order to survive a motion to dismiss.”³ The Second Circuit standard therefore would

Sutton v. United Air Lines, Inc., 527 U.S. 471, 493 (1999) (dismissal warranted where complaint alleged that plaintiffs were “regarded as disabled” by a potential employer who refused to hire them because of correctible vision impairments, but “failed to allege adequately” a necessary element of a claim under the Americans With Disabilities Act—specifically, that the plaintiffs’ physical impairments were regarded as a substantial limitation on a major life activity).

²*Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 597 n. 21 (1986) (“[C]onduct that is as consistent with permissible competition as with illegal conspiracy does not, without more, support even an inference of conspiracy.”). *Id.* (quoting *Monsanto* that the plaintiff “must present evidence ‘that tends to exclude the possibility that the alleged conspirators acted independently.’”).

³*Twombly*, 425 F.3d at 114 (interpreting *Nagler v. Admiral Corp.*, 248 F.2d 319, 325 (2d Cir. 1957), to suggest that a pleading

allow the court to assume that the plaintiff will be able to prove facts that it has not alleged, directly contradicting Supreme Court jurisprudence.⁴

Because the *Twombly* complaint does not allege facts that, if proven true, would permit an inference of conspiracy under the Sherman Act, it does not establish a claim upon which relief may be granted. The Solicitor General agreed with this point in his brief to the Supreme Court, stating that the district court was correct to dismiss the complaint for failing to allege more than parallel conduct, with or without a conclusory allegation of an agreement.⁵ Under the Supreme Court's Rule 8(a) jurisprudence, *see supra* note 1, the Court should find that the *Twombly* complaint failed adequately to allege a conspiracy in violation of Section 1.

The Bottom Line. *Twombly* easily could be written off as just another case interpreting Rule 8 of the Federal Rules of Civil Procedure, but its impact should not be underestimated. First, the Second Circuit's decision invites plaintiffs to use the mechanism of civil discovery to fish for facts to support vaguely stated notions of harm and to use the asymmetrical nature of discovery in these types of cases to extract unjustified settlements.⁶ Second, the relaxed pleading standards established by the Second Circuit for Sherman Act Section 1 violations all but beg plaintiffs to file conspiracy claims based on nothing more than parallel, and likely efficient, conduct. Third, companies may even be pushed to make investments that do not satisfy minimum return-on-investment thresholds so as to avoid baseless market allocation claims that could result in *in terrorem* settlements.

If the Supreme Court lets this decision stand, companies across the country will find themselves increasingly subject to the massive disruption and expense associated with civil discovery. Moreover, consumers will suffer from the chilled competition resulting from these companies' need to avoid such unfair exposure. Let us hope that the Supreme Court reverses the Second Circuit's decision, preventing unmeritorious claims from wasting the time and resources of courts and litigants alike.

of facts indicating parallel conduct by the defendants can suffice to state a plausible claim of conspiracy).

⁴*See Associated Gen. Contractors of Cal. Inc. v. Cal. State Council of Carpenters*, 459 U.S. 519, 526 (1983) ("It is not, however, proper to assume that the Union [plaintiff] can prove facts that it has not alleged or that the defendants have violated the antitrust laws in ways that have not been alleged."); *see also Dura Pharms., Inc. v. Broudo*, 544 U.S. 336, 347 ("It would permit a plaintiff 'with a largely groundless claim to simply take up the time of a number of other people, with the right to do so representing an *in terrorem* increment of the settlement value, rather than a reasonably founded hope that the [discovery] process will reveal relevant evidence'" sufficient to establish a claim upon which relief could be granted) (quoting *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 741 (1975)).

⁵Brief for the United States as Amicus Curiae Supporting Petitioners, *Bell Atlantic Corp. v. Twombly*, No. 05-1126, 2006 WL 2482696, at 10 (filed Aug. 26, 2006).

⁶Civil discovery is extraordinarily costly and time-consuming, especially in antitrust actions, which tend to be disproportionately fact-intensive and complex. *See* Keith N. Hylton, AEI-Brookings Joint Center for Regulatory Studies, *When Should a Case be Dismissed? The Economics of Pleading and Summary Judgment Standards* at 14-15 (Apr. 2006) ("The discovery costs [in antitrust cases] are large enough to encourage defendants to settle claims even when the plaintiff's claim is highly likely to fail. In the case of a large class action for treble damages, high discovery costs coupled with only a one percent chance of victory at trial could force defendants to pay substantial settlements."); *see also* Douglas J. Ginsburg, *Comparing Antitrust Enforcement in the United States and Europe*, 1 J. COMP. L. & ECON. 427, 435-36 (2005).