

U.S. Supreme Court Rejects “Parallel Conduct” Pleading Under Section 1 of the Sherman Act, Retires “No Set of Facts” Pleading Standard

In a much anticipated decision, the Supreme Court tightened the standards for pleading an actionable violation of Section 1 of the Sherman Act. In the process, the Court also jettisoned a long-standing principle guiding sufficiency of allegations in a complaint.

Section 1 of the Sherman Act forbids “[e]very contract, combination . . . , or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations.” In *Bell Atlantic Corp. v. Twombly*, 550 U.S. (May 21, 2007), the Supreme Court held that a pleading should be dismissed where it merely alleges that competitors engaged in parallel conduct unfavorable to competition but does not otherwise allege facts implying an actual agreement. The Court also “retired” the oft-quoted standard 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,” requiring instead that a plaintiff plead “enough facts to state a claim to relief that is plausible on its face.”

The plaintiffs in *Twombly* sought to represent a nationwide class of all “subscribers of local telephone and/or high speed internet services . . . from February 8, 1996 to present.” They sued four local telephone companies, known as incumbent local exchange carriers (ILECs), alleging Section 1 violations and seeking treble damages and declaratory and injunctive relief. The Telecommunications Act of 1996 required ILECs to share their networks with competitors, known as competitive local exchange carriers (CLECs).

The plaintiffs alleged “parallel conduct” in the defendants’ respective services areas designed to inhibit the growth of CLECs and avoid competition with one another. The complaint alleged, upon information and belief, that the ILECs had “entered into a contract, combination or conspiracy to prevent competitive entry in their respective local telephone and/or high speed internet services markets and [had] agreed not to compete with one another and otherwise allocated customers and markets to one another.” The plaintiffs did not include any independent averment of an actual agreement among the ILECs.

In an earlier line of cases, the Supreme Court had held that evidence of parallel conduct or interdependence, without more, cannot establish Section 1 liability even though it may provide circumstantial evidence of an agreement. See *Matsushita Elec. Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986) (evidence offered by plaintiff in response to motion for summary judgment in Section 1 case must tend to rule out the possibility that the defendants were acting independently); *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752 (1984) (proof of Section 1 conspiracy requires evidence that tends to exclude the possibility of independent action); *Theatre Enterprises, Inc. v. Paramount Film Distributing Corp.*, 346 U.S. 537 (1954) (parallel conduct is admissible circumstantial evidence from which a fact finder may infer agreement, although it does not conclusively establish illegal agreement). In view of these precedents, the Court held that Section 1 plaintiffs must plead “enough factual matter (taken as true) to suggest that an agreement was made.” The Court explained:

[L]awful parallel conduct fails to bespeak unlawful agreement. It makes sense to say, therefore, that an allegation of parallel conduct and a bare assertion of conspiracy will not suffice. Without more, parallel conduct does not suggest conspiracy, and a conclusory allegation of agreement at some unidentified point does not supply facts adequate to show illegality. Hence, when allegations of parallel conduct are set out in order to make a § 1 claim, they must be placed in a context that raises a suggestion of a preceding agreement, not merely parallel conduct that could just as well be independent action.

In support of its conclusion, the Court noted the “massive” potential discovery costs, and the practical inability of the district courts to manage such costs without some degree of specificity in pleading. The potential discovery costs were particularly large in *Twombly*, where the plaintiffs sought to represent a class of at least 90 percent of all subscribers to local telephone or high speed internet service in the continental United States, and asserted Section 1 violations over a seven year period. The Court determined that the only practical way to avoid the potentially enormous expense of discovery in cases with no reasonable probability of success is to require specific factual allegations that plausibly suggest conspiracy.

The plaintiffs relied on the frequently-quoted passage from *Conley v. Gibson*, 355 U.S. 41 (1957), 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.” *Id.* at 45-46. The Court noted that “a good many judges and commentators have balked at taking the literal terms of the *Conley* passage as a pleading standard” inasmuch as they “would dispense with any showing of a ‘reasonably founded hope’ that a plaintiff would be able to make a case.” In view of the confusion generated by the “no set of facts” statement, the Court held that “this famous observation has earned its retirement.”

In place of the *Conley* standard, the Court held that plaintiffs must plead “enough facts to state a claim to relief that is plausible on its face.” Under this new standard, the plaintiffs’ allegations came up short. The references to an agreement in the complaint were merely legal conclusions resting on allegations of parallel conduct. “[N]othing contained in the complaint invests either the action or inaction alleged with a plausible suggestion of conspiracy.” Moreover, the “obvious” explanation for the ILECs’ reluctance to compete against one another was that “the former Government-sanctioned monopolists were sitting tight, expecting their neighbors to do the same thing.” “Because the plaintiffs here have not nudged their claims across the line from conceivable to plausible,” the Court held, “their complaint must be dismissed.”

Justice Stevens wrote a stinging dissent, observing that the Court’s holding marked “a fundamental—and unjustified—change in the character of pretrial practice.” He argued that the Court’s new “plausibility” standard “is irreconcilable with Rule 8 and with [the Court’s] governing precedents,” noting that the Court had relied on the “no set of facts” standard numerous times over the years. While he acknowledged that the ILECs might have engaged in parallel conduct in the absence of an unlawful agreement, he noted that such conduct “is also entirely consistent with the *presence* of the illegal agreement alleged in the complaint,” and thus the complaint should not have been dismissed.

Whether *Twombly* marks a fundamental change in the character of pretrial practice, as the dissent contends, remains to be seen. At a minimum, it is clear that Section 1 plaintiffs may not rely on generalized allegations of parallel conduct without pleading “enough factual matter (taken as true) to suggest that an agreement was made.”

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