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# The Pleading Problem in Antitrust Cases and Beyond

Herbert Hovenkamp\*

In *Bell Atlantic Corp. v. Twombly*, the Supreme Court held that a complaint alleging an anticompetitive agreement failed to state a claim because its allegations did not include enough “factual matter” to justify proceeding to discovery.<sup>1</sup> Two years later, the Supreme Court clarified that the new pleading standard set forth in *Twombly* was not limited to antitrust claims but applied to civil litigation generally.<sup>2</sup>

*Twombly* involved an allegation of anticompetitive conduct in violation of section 1 of the Sherman Act. Specifically, the prosecution alleged a nationwide geographic market-division agreement—a cartel in which members eliminate competition among themselves not by fixing the price, but rather by dividing the market into exclusive territories.<sup>3</sup> The prosecution alleged the following facts in support of this agreement: (1) the four dominant telephone companies, or Incumbent Local Exchange Carriers (“ILECs”), did not expand into one another’s geographic territories even though they were legally entitled to do so;<sup>4</sup> (2) each of the defendants vigorously excluded or limited the growth of competing telephone companies in their respective territories; and (3) the CEO of Qwest Communications, one of the four defendants, had once stated that competing in the territory of another defendant ““might be a good way to

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1. *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 556 (2007) (to the extent it is relevant, the author was consulted by a defendant).

2. *Ashcroft v. Iqbal*, 129 S. Ct. 1937 (2009).

3. *Twombly*, 550 U.S. at 551 (noting allegations that the defendants conspired to avoid competing with one another by not expanding into contiguous territories).

4. The seven original ILECs came into existence as a result of an antitrust consent decree that broke up the old telephone monopoly. See *Maryland v. United States*, 460 U.S. 1001 (1983); *United States v. AT&T Co. (Modification of Final Judgment)*, 552 F. Supp. 131 (D.D.C. 1982), *aff’d mem. sub nom.* Under the decree, these “Baby Bells” were forbidden from competing in one another’s territories. The territorial restriction was removed in the Telecommunications Act of 1996, Pub. Law No. 104-104, 110 Stat. 56 (codified at 47 U.S.C. § 271 (2006)). By the time of this litigation, some of the original ILECs had merged, and only four independent firms remained. See *Twombly*, 550 U.S. at 550 n.1 (describing the 1984 dissolution of AT&T’s monopoly).

turn a quick dollar but that doesn't make it right.”<sup>5</sup> Both allegations (1) and (2) were alleged to be “parallel” conduct, meaning that all the defendants engaged in the activities. The only evidence of any “mental state” suggesting an agreement, however, was the statement set forth in allegation (3). The agreement allegedly spanned many years during a time when the telecommunications industry underwent major changes. Discovery would have been very costly for the defendants and was further complicated by the nature of the telecommunications market—it is a network industry in which inter-firm communication is essential to maintaining network interoperability. As a result, the fact finder would have had to sort out harmful from harmless or beneficial communications to ascertain whether an actionable anticompetitive agreement in fact existed.

Kevin Clermont and Stephen C. Yeazell make a strong case that *Twombly*'s effect, coupled with the Supreme Court's subsequent *Iqbal* decision, is far reaching. They argue that the two decisions operate to deny judicial access to worthy litigants and that the effect of their broad reach and lack of clarity has “destabilized the entire system of civil litigation.”<sup>6</sup> A plaintiff must now “plead facts and even some evidence.”<sup>7</sup> Further, the pleading of facts must be “particularized” in the sense that the pleading is sufficient to “make plausible an inference of liability.”<sup>8</sup> As a result, they conclude, “the plaintiff who needs discovery to learn the required factual particulars is the person whom the Court has newly put in jeopardy.”<sup>9</sup> The two Supreme Court decisions “ask whether inferring liability is ‘plausible’ in light of the facts nonconclusorily pled—that is, whether it is a ‘reasonable inference.’”<sup>10</sup> This “appears equivalent to the standard of decision for summary judgment . . . .”<sup>11</sup> Indeed, they conclude that “the most startling aspect of *Twombly* and *Iqbal* is that they call for a judge to weigh likelihood without any evidential basis and with scant procedural protections, effectively creating a civil procedure hitherto foreign to our fundamental procedural principles . . . .”<sup>12</sup>

The Court could have avoided these startling consequences, which result from its discussion about the detail that plaintiffs must provide in federal complaints generally. As *Iqbal* illustrates, *Twombly*'s approach leads to a great deal of confusion and—in antitrust at least—has produced prolix

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5. *Twombly*, 550 U.S. at 550 (quoting Richard Notebaert, ILEC Qwest's CEO).

6. Kevin M. Clermont & Stephen C. Yeazell, *Inventing Tests, Destabilizing Systems*, 95 IOWA L. REV. 821, 821, 823 (2010); see also Adam N. Steinman, *The Pleading Problem*, 62 STAN. L. REV. (forthcoming 2010) (describing *Twombly*'s potential harm to litigants in civil litigation).

7. Clermont & Yeazell, *supra* note 6, at 830.

8. *Id.*

9. *Id.*

10. *Id.* at 833 (quoting *Ashcroft v. Iqbal*, 129 S. Ct. 1937, 1949 (2009)).

11. *Id.*

12. Clermont & Yeazell, *supra* note 6, at 834.

complaints sometimes running to more than one-hundred pages. What pleading reform requires is not so much an increase in “factual matter” as much as a closer correlation between the legal elements that plaintiffs must prove and the allegations in a complaint.

*Twombly* would have been much less unsettling had it focused less on pleading standards and more on the nature of proof required to establish antitrust conspiracies. The Court almost certainly would have reached the same result that it did<sup>13</sup> and would not have done the damage to the notice pleading system that Clermont and Yeazell lament.<sup>14</sup>

The pleading requirements articulated in *Twombly* contrast sharply with sample pleadings in the Appendix of Forms that accompany the Federal Rules of Civil Procedure. For example, Form 11 provides that the following is a sufficient allegation: that on a given date and street “defendant negligently drove a motor vehicle against plaintiff who was then crossing said highway”; as a result, “plaintiff was . . . injured . . .”<sup>15</sup> While the Form 11 pleading alleges a specific date and place, it is starkly conclusory with respect to the legal violation. In tort law, the term “negligence” refers to specific acts or omissions that a reasonable person would not do.<sup>16</sup> In this negligent driving example, the specific act could be speeding, failure to yield, failure to have an unobstructed view, failure to have headlights turned on after dark or windshield wiper blades running, and the like. The drafters of Form 11 were apparently satisfied with a generalized allegation of “negligence,” even if the plaintiff knew what the particular act of negligence was and could have set this out in the pleading. Allowing generalized allegations can yield strategic pleadings in situations where the plaintiff deliberately fails to plead what it knows. But requiring only a generalized allegation can also yield a reasonable balance between allegation and fact finding in cases where the defendant knows the particular acts but the plaintiff does not. The plaintiff who was knocked unconscious by the collision, for example, knows that she was walking lawfully with the light and that the defendant could have hit her for a number of different reasons, one of which will come out in discovery. Requiring the plaintiff to plead the specific act of negligence, rather than a

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13. Clermont and Yeazell express some doubts on this proposition. *See id.* at 836 (suggesting that the *Twombly* complaint may have been sufficient to state a section 1 agreement).

14. *See id.* (explaining that such an alternative regime would reduce the current frequency of weakly founded suits).

15. FED. R. CIV. P. FORM 11, available at <http://www.uscourts.gov/rules/cvforms2.htm>.

16. Under some doctrines, such as *res ipsa loquitur*, negligence can be inferred from other circumstances, but *res ipsa* would not govern a claim of driver negligence and, in any event, is not being alleged in Form 11. *See Byrne v. Boadle*, (1863) 159 Eng. Rep. 299 (Exch.) (a plaintiff struck by barrel of flour that fell from window ledge need not show a specific act of negligence; one could reasonably infer that flour would not have fallen in the absence of negligence); *see also* RICHARD A. EPSTEIN, TORTS §§ 7.3–7.5 (1999) (discussing the historical development of *res ipsa loquitur* and related issues in proving negligence).

generalized allegation is problematic, as this example demonstrates, where the plaintiff is unable to discover the specific unlawful conduct until later.

*Twombly*'s facts pose concerns analogous to the negligent driving example above. Naked market-division conspiracies must be kept secret by the parties to the agreement because antitrust enforcers will prosecute them when they are detected—potentially producing criminal liability.<sup>17</sup> This inherent secrecy, which the *Twombly* opinion did not discuss, has dire consequences for plaintiffs under a standard that requires them to plead all essential facts with specificity. Indeed, such secrecy can close the door to prosecution in cases where the defendant's behavior demonstrates a possible or likely conspiracy, but all specific supporting evidence has not already been uncovered by other means.

Prior to *Twombly*, the Supreme Court as well as lower courts had frequently recognized and addressed the problem that secrecy poses from a pleading standpoint. They permitted the inference of antitrust conspiracies from acts falling short of explicit communication of an unlawful agreement. The *Twombly* majority, however, said this about the plaintiff's complaint:

Apart from identifying a seven-year span in which the § 1 violations were supposed to have occurred (i.e., “[b]eginning at least as early as February 6, 1996, and continuing to the present,”), . . . *the pleadings mentioned no specific time, place, or person involved in the alleged conspiracies*. This lack of notice contrasts sharply with the model form for pleading negligence, Form 9 . . . .<sup>18</sup> Whereas the model form alleges that the defendant struck the plaintiff with his car while plaintiff was crossing a particular highway at a specified date and time, *the complaint here furnishes no clue as to which of the four ILECs (much less which of their employees) supposedly agreed, or when and where the illicit agreement took place*. A defendant wishing to prepare an answer in the simple fact pattern laid out in Form 9 would know what to answer; a defendant seeking to respond to plaintiffs' conclusory allegations in the § 1 context would have little idea where to begin.<sup>19</sup>

The Court's discussion of perceived deficiencies in the complaint suggests a narrower view of the evidence that plaintiffs can use to establish an antitrust conspiracy under the Sherman Act.<sup>20</sup> In the paradigm cartel

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17. 12 HERBERT HOVENKAMP, ANTITRUST LAW ¶¶ 2030–31 (2d ed. 2005).

18. Here, the Court refers to Form 9. It is important to note that subsequent to *Twombly*, the Court enlarged and renumbered the list of forms. Form 9 is now Form 11. *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 565 n.10 (2007).

19. *Id.* (emphasis added).

20. On this point, see William H. Page, *Twombly and Communication: The Emerging Definition of Agreement Under the New Pleading Standards*, 5 COMPETITION L. & ECON. 439, 444–46 (2009) (suggesting that the impact of *Twombly* is to require plaintiffs to show actual communications among alleged conspirators). Section 5 of the Federal Trade Commission Act,

case, the defendants meet secretly in a hotel room and plot prices or output. Alleging this conduct in a pleading likely fits within the narrower evidence *Twombly* requires to prove a conspiracy. But antitrust conspiracies often do not involve such explicit agreements, and liability for unlawful agreements has not typically hinged upon pleading the paradigmatic cartel case. Rather, antitrust agreements can ordinarily be proven by other evidence, including evidence of interdependence, parallel behavior, and actions contrary to independent self-interest.<sup>21</sup> By indicating that the complaint failed because it did not state “which of their employees” may have conspired and “when” or “where” the agreement took place, the *Twombly* Court required the plaintiff to plead something in its claim that existing law did not require it to show in order to avoid summary judgment or judgment as a matter of law at trial. In altering the pleading standards, the Court concurrently changed the substantive conspiracy doctrine as well.

To illustrate, in *High Fructose* the Seventh Circuit, speaking through Judge Posner, denied summary judgment after finding a conspiracy plausible on the basis of structural evidence and regression analysis examining prices and fluctuations in market share.<sup>22</sup> Similarly, several lower court decisions have permitted conspiracy claims to go forward on the basis of statistical evidence of “incumbency” rates.<sup>23</sup> The theory behind permitting this evidence to establish a conspiracy is that customers in a competitive market for a fungible product routinely shop among sellers. As a result, in the absence of long-term contracts, one would expect to see fairly unstable and shifting seller-customer pairings. By contrast, cartels typically “assign” customers to cartel members, creating relationships that are much more stable.<sup>24</sup> So one would expect to see incumbency rates (stable buyer-seller

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which prohibits unfair methods of competition, arguably reaches more broadly. See Herbert Hovenkamp, *The Federal Trade Commission and the Sherman Act*, 62 FLA. L. REV. (forthcoming 2010) (manuscript at 8), available at [http://papers.ssrn.com/so13/papers.cfm?abstract\\_id=1531136](http://papers.ssrn.com/so13/papers.cfm?abstract_id=1531136).

21. On the various approaches, see 6 PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW (forthcoming 2010) (manuscript ¶¶ 1431–36, on file with author).

22. *In re High Fructose Corn Syrup Antitrust Litig.*, 295 F.3d 651 (7th Cir. 2002) (discussing the problem of multicollinearity in regression analyses).

23. See, e.g., *City of Tuscaloosa v. Harcros Chems., Inc.*, 158 F.3d 548, 570–73 (11th Cir. 1998) (discussing that the high incumbency rate on new contracts is inconsistent with independent action); *State ex rel. Montgomery v. Louis Trauth Dairy, Inc.*, No. C-1-93-553, 1996 WL 343440 (S.D. Ohio Apr. 26, 1996) (same); see Gregory J. Werden, *Economic Evidence on the Existence of Collusion: Reconciling Antitrust Law with Oligopoly Theory*, 71 ANTITRUST L.J. 719, 759–65 (2004) (arguing that the present state of the law is unsatisfactory because neither courts nor many economists have grounded their analysis in modern oligopoly theory).

24. See AREEDA & HOVENKAMP, *supra* note 21, ¶ 1420(b) (discussing that a cartel or market division scheme typically “reserves” customers for specific cartel members and how this relationship can demonstrate or provide evidence of a conspiracy).

pairings) increase when a cartel is formed and decrease when the cartel falls apart and competition breaks out.<sup>25</sup>

None of this should be taken as a defense for any particular method of proving a conspiracy as the validity of these alternative methodologies for proving a conspiracy were not an issue before the Court. It is only an observation that the Court in *Twombly* was drawing some pretty substantive conclusions about what must go into a complaint to prove a conspiracy.

*Twombly* style proof-of-agreement cases are common in antitrust litigation. Importantly, the Court did not purport to overrule older decisions that found conspiracies yet lacked the elements required by *Twombly*.<sup>26</sup> Proof of agreement in an antitrust case can proceed along several routes. The typical cartel case in which proof of agreement becomes an issue is price-fixing. In many of these cases, prices move together in a suspiciously parallel fashion, or the firms simultaneously introduce or withdraw product offerings or abandon markets,<sup>27</sup> but there is no real evidence, or only inconclusive evidence, of explicit communications among the parties. The cases are pled against a legal background saying that “conscious parallelism” is not an agreement, mainly because firms can be expected to follow and match one another’s prices.<sup>28</sup> So one must have more. The question is: how much more must be alleged and eventually proven?

The most explicit evidence that a conspiracy exists is actual, observed communications among firms. For example, wiretaps or informants might produce evidence of actual discussions setting a price or reducing output.<sup>29</sup> When such communications are lacking—or more typically, when they are sufficiently thin that corroborating evidence is necessary—then agreements can be inferred from other circumstances. This requires interdependence plus some additional evidence of assent.

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25. That proposition can be tested empirically.

26. See, e.g., *Am. Tobacco Co. v. United States*, 328 U.S. 781, 809 (1946) (inferring agreement from price movements); *United States v. Masonite Corp.*, 316 U.S. 265, 275 (1942) (finding sufficient evidence of agreement in absence of any evidence of communication among the agreeing parties); *Interstate Circuit v. United States*, 306 U.S. 208, 474 (1939) (same); see also *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 574–76 (1986) (refusing to find a conspiracy from parallel behavior where other evidence suggested that the alleged conspiracy would have been implausible and granting summary judgment).

27. See, e.g., *Interstate Circuit*, 306 U.S. at 215–17 (exhibiting a simultaneous increase in admission prices and abandonment of double features). For a recent application of *Interstate Circuit*, see generally *Toys “R” Us, Inc. v. FTC*, 221 F.3d 928 (7th Cir. 2000) (applying *Interstate Circuit* to an agreement among toy manufacturers to sell to discount clubs only in large packages).

28. See AREEDA & HOVENKAMP, *supra* note 21, ¶¶ 1428–31 (analyzing parallel behavior).

29. See, e.g., *United States v. Andreas*, 216 F.3d 645, 652–53 (7th Cir. 2000) (involving use of both wiretap evidence and informant to establish price fixing).

“Interdependence” is a critical first step in inferring an agreement from parallel behavior where evidence of explicit communication is lacking.<sup>30</sup> Importantly, interdependence is not the same thing as parallel conduct, although one passage in the *Twombly* opinion seems to presume otherwise.<sup>31</sup> “Interdependence” refers to a subset of conduct that is parallel because it results from one firm’s observation of other firms’ behavior and anticipations about those firms’ reactions. For example, if market prices are publicly known, the product is fairly fungible, and customers can quickly switch among brands, then prices are likely to move in parallel fashion. This is true of retail gasoline, where the stores post their price on a sign visible not only to passing motorists but also to nearby rivals. It is also true of the airlines, where prices are posted on websites, and both travel agents and consumers have virtually instant access to them. This “conscious parallelism” is not the same thing as an agreement, however, because there is no offer and acceptance. When the prices of four nearby gasoline stations or four airlines move up and down in tandem, the most we can infer is that one firm changed its price and the others individually decided to go along.

Moreover, conduct might be parallel for no other reason than that the firms are responding to the same external stimulus. In such cases, they may behave in parallel fashion without reacting to what their rivals are doing or, indeed, without even knowing what their rivals are up to. For example, upon reading or hearing a report of an early frost, thousands of farmers might decide to harvest a crop early. Or upon hearing a prediction of a recession, many manufacturers might decide not to increase their output for the coming year. That is to say, the mere fact that firms are rational profit maximizers in the same market implies that they will do a fair number of things in parallel fashion. Farmers switched from horses to tractors and airlines from propeller to jet aircraft not because of cartels, but because differences in performance justified those changes, and firms that did not switch would have lost out.

Most instances of “parallel” conduct are best described in this way. Why do most automobile manufacturers permit their dealers to sell only a single brand? Why do most computer manufacturers sell computers with hard drives preinstalled? Why do most fast-food franchises offer soft drinks as well as food? In all of these cases, the first inference to be drawn is not that the firms are conspiring with each other, but that competition, consumer preference, or market conditions have forced them to behave in a similar way. In that case, the new computer manufacturer who decides that its

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30. See AREEDA & HOVENKAMP, *supra* note 21, ¶ 1411 (discussing the relationship of interdependence to agreement).

31. See *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 554 (2007) (“The inadequacy of showing parallel conduct or interdependence, without more, mirrors the ambiguity of the behavior: consistent with conspiracy, but just as much in line with a wide swath of rational and competitive business strategy unilaterally prompted by common perceptions of the market.”).

product will be most appealing to consumers if hard drives are preinstalled is not “conspiring” with rival computer makers. Rather, the manufacturer is acting in its independent best interest given the state of consumer preference in that market.

The conduct alleged in the *Twombly* complaint was parallel, but not interdependent. Indeed, one important fact about *Twombly* is that, while it was a proof-of-agreement case, the claim was geographic market division rather than parallel pricing. For all of its lengthy discussion about the facts essential to a good complaint, the Supreme Court paid little attention to the difference between price fixing and market division.

The complaint alleged that the defendants had conspired to exclude *all* new entrants from their historical territories by engaging in various activities such as making unfair agreements with new entrants, providing them with inferior network connections, overcharging them, and trying to sabotage them in other ways.<sup>32</sup> As the Court observed, however, *every* firm that is dominant in its own market has an incentive to try to exclude rivals.<sup>33</sup> As a result, the fact that each firm behaved this way hardly indicated a market-division conspiracy—the acts would have been profitable for each firm whether or not the others were doing them as well. The Court echoed the district court’s conclusion that “the behavior of each ILEC in resisting the incursion of CLECs is fully explained by the ILEC’s own interests in defending its individual territory.”<sup>34</sup>

Once we have concluded that parallel behavior is not merely a response to the same stimulus but also an *interdependent* response, we then must look for other factors creating an inference of agreement.<sup>35</sup> This analysis is objective, just as it typically is in the tort law of negligence. The question, therefore, is not so much whether a “meeting of the minds” in the common-law contract sense existed as whether these are types of behavior that the law should suppress. In the presence of interdependence, which is a potentially dangerous condition, communications among rivals about planned output changes increase the danger of collusion. Absent justifications, we condemn them by finding a Sherman Act agreement.

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32. *Id.* at 550–51; *see, e.g.*, *Verizon Comm’ns Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398, 403–05 (2004) (detailing some of ILEC Verizon’s efforts to limit the growth of an interconnecting rival).

33. *Twombly*, 550 U.S. at 566 (stating that “resisting competition is routine market conduct”).

34. *Id.* at 552 (quoting the district court in *Bell Atl. Corp. v. Twombly*, 313 F. Supp. 2d 174, 183 (S.D.N.Y. 2003)).

35. In reversing the district court and reinstating the complaint, the Second Circuit simply assumed that the conduct was interdependent and that “plus factors” were evidence and not essential to the pleadings. *Twombly v. Bell Atl. Corp.*, 425 F.3d 99, 114 (2d Cir. 2005) *rev’d*, 550 U.S. 544 (2007).

Parallel *pricing* raises an inference of interdependence and perhaps even a degree of implied cooperation among the firms.<sup>36</sup> While parallel pricing alone is not generally sufficient to prove an agreement,<sup>37</sup> it is enough to raise our antennae. This provokes a search for other things, inelegantly referred to as “plus factors,”<sup>38</sup> that enable the leap from merely parallel prices to *agreed* parallel prices. These plus factors can include explicit communications, but they can also include things like incumbency rates,<sup>39</sup> highly suspicious behavior, the use of “facilitating” practices that serve to make collusion easier, or other actions that are generally contrary to the self interest of the actors, except on the assumption that they are acting in concert.<sup>40</sup> Proving some of these factors requires an expert and the use of statistics. As a result, if *Twombly* requires that plus factors be pled, drafting of a good faith complaint may require engagement of an expert and at least a preliminary factual inquiry. In some cases, of course, the data that an expert needs can be obtained only in discovery.

A complaint alleging that the defendants moved their prices up and down sequentially in lockstep fashion and a market structure conducive to collusion, coupled with some observations of relevant communication among the parties, would remain sufficient under *Twombly*'s formulation.

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36. See AREEDA & HOVENKAMP, *supra* note 21, ¶¶ 1432 (describing interdependent pricing).

37. *But see* Am. Tobacco Co. v. United States, 328 U.S. 781, 804–08 (1946) (inferring agreement almost exclusively from price movements).

38. See AREEDA & HOVENKAMP, *supra* note 21, ¶¶ 1430–34; *see, e.g.*, Merck-Medco Managed Care v. Rite Aid Corp., No. 98-2847, 1999 WL 691840, at \*9 (4th Cir. Sept. 7, 1999). The court stated:

In order to infer a conspiracy, conscious parallelism must be accompanied by “plus factors.” While the Supreme Court has not recounted a list of plus factors, numerous plus factors, such as “motive to conspire,” “opportunity to conspire,” “high level of inter-firm communications,” irrational acts or acts contrary to a defendant’s economic interest, but rational if the alleged agreement existed, and departure from normal business practices, have been considered by other circuits.

*Id.*

39. See *supra* notes 23–25 and accompanying text (discussing incumbency rates).

40. *Twombly* did not discuss plus factors except for a brief mention suggesting that it disagreed with the Second Circuit’s conclusion that plus factors need not be pled, although they might be necessary to avoid summary judgment. *See* Bell Atl. Corp. v. *Twombly*, 550 U.S. 544, 553, 569 (2007). The Second Circuit held:

On a motion for summary judgment in a case involving alleged violations of Section 1, “courts have held that a plaintiff must show the existence of additional circumstances, often referred to as ‘plus’ factors, which, when viewed in conjunction with the parallel acts, can serve to allow a fact-finder to infer a conspiracy.” These “plus factors” may include: “a common motive to conspire,” evidence that “shows that the parallel acts were against the apparent individual economic self-interest of the alleged conspirators,” and evidence of “a high level of interfirm communications . . . .”

*Twombly*, 425 F.3d at 114.

These would constitute facts “plausibly suggesting” an agreement or raising a “reasonable expectation”<sup>41</sup> that discovery would reveal more, as many post-*Twombly* decisions have held.<sup>42</sup> In such cases, the appropriate message to be taken from *Twombly* is that plaintiffs must research carefully and look at objective evidence drawn from market and firm structure and behavior as well as subjective evidence of statements, communications, and the like.

But *Twombly* was a market division case, and parallel failures to enter one another’s markets do not create the same set of suspicions as parallel pricing. If they did, the premise must be that absent agreements, everybody would be selling everything everywhere. When one walks down the street and sees a pet store that does not sell groceries and a grocery store that does not sell puppies, no inference of a market division agreement comes to mind. Nor is a cartel the likely explanation if Alpha owns a pizza place only on the west side of town and Beta only on the east side, or the fact that a lawyer does not practice medicine on the side while her neighbor, a physician, does not practice law. As the Supreme Court observed in *Twombly*,

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41. *Twombly*, 550 U.S. at 545.

42. For examples of such decisions, see generally *Starr v. Sony BMG Music Entm’t*, 592 F.3d 314 (2d Cir. 2010) (allegations of price fixing of digital music sufficed under *Twombly* when conduct was alleged to be irrational in the absence of an agreement); *Urethane Antitrust Litig.*, 663 F. Supp. 2d 1067 (D. Kan. 2009) (pleading of conspiracy sufficient under *Twombly* when market was prone to collusion; price increase announcements were made in interrelated fashion; and defendants participated in meetings at which prices were discussed); *Korkala v. Allpro Imaging, Inc.*, No. 08-2712, 2009 WL 2496506 (D.N.J. Aug. 10, 2009) (holding that the plaintiff adequately alleged price fixing by manufacturers of X-ray film based on parallel price increases and numerous meetings of sales managers at which the increases were discussed); *Standard Iron Works v. Arcelormittal USA, Inc.*, 639 F. Supp. 2d 877 (N.D. Ill. 2009) (*Twombly* permitted the claim that domestic steel producers fixed prices, based mainly on allegation that they simultaneously reduced output in the face of increasing demand—an act that would have been contrary to individual self interest); *Simon-Whelan v. Andy Warhol Found. for the Visual Arts, Inc.*, No. 07 Civ. 6423(LTS), 2009 WL 1457177 (S.D.N.Y. May 26, 2009) (the plaintiffs adequately alleged conspiracy among the only two entities authenticating Andy Warhol art works based on suspicious parallel behavior in certifying and then denying certification on various works, and inconsistent application of authentication policies); *Wanachek Mink Ranch v. Alaska Brokerage Int’l, Inc.*, No. C06-089RSM, 2009 WL 1342676 (W.D. Wash. May 5, 2009) (holding that mink ranchers adequately alleged conspiracy of fur buyers to suppress mink fur prices, including bid rotation and lot allocation); *Hackman v. Dickerson Realtors, Inc.*, 595 F. Supp. 2d 875 (N.D. Ill. 2009) (real estate broker adequately alleged group boycott against him with claims that discussions were held at a real estate association meeting pertaining to excluding him; and that representatives of a different agency told him about a boycott); *In re TFT-LCD (Flat Panel) Antitrust Litig.*, 586 F. Supp. 2d 1109 (N.D. Cal. 2008) (plaintiffs adequately alleged agreement with claims that defendants manipulated their plant production capacity in ways that did not make sense except on the premise of an agreement; that there were numerous invitations to conspire followed by some responsive assurance; and pretextual reasons given for price increases; however, complaint lacked sufficient allegations with respect to specific defendants). See also *In re TFT-LCD (Flat Panel) Antitrust Litig.*, No. M 07-1827 SI, 2009 WL 533130 (N.D. Cal. Mar. 3, 2009) (finding that allegations in amended complaint with respect to specific defendants were adequate); *In re Rail Freight Fuel Surcharge Antitrust Litig.*, 593 F. Supp. 2d 29 (D.D.C. 2008) (plaintiffs adequately alleged that railroads fixed price by manipulating fuel surcharges).

firms “do not expand without limit.”<sup>43</sup> Further, “none of them enters every market that an outside observer might regard as profitable, or even a small portion of such markets.”<sup>44</sup> A firm’s decision to expand involves many factors. First is the availability of capital and the question whether to expand at all. Second is the selection of an expansion market, looking at costs, risks, and expected payoffs given the anticipated responses from incumbents.

Chief Justice Roberts was on the right track in the oral argument when he asked this question:

[W]ould it state an antitrust violation if had you a grocery store on one corner of the block and a pet store on the other corner of the block and you say, well, the grocery store is not selling pet supplies and they could make money if they did, therefore that’s an antitrust violation?<sup>45</sup>

The all-important question about *Twombly* is whether the plaintiffs ever reached the first step in pleading an agreement. Did they allege that the failure of several incumbent telephone companies to move outside of their initially assigned geographic territories was interdependent conduct?<sup>46</sup> The plaintiffs alleged that the defendants individually had the know-how to expand and that expansion would have been profitable.<sup>47</sup> But those allegations could be made about almost any firm and hardly suggest interdependence. Consider a pizza restaurateur on the west side of town and another on the east side. Assuming that each one knows its business in its own location, a reasonable inference is that they would know the business on the other side of town as well. So they would have the know-how to enter. We might also observe that others are entering the business on both sides of town, as was the case in *Twombly*.<sup>48</sup> The fact that entry is easy for these other firms means that it must be easy for the two defendant firms as well. Further, they have the experience advantage in that they are already running pizza restaurants in their home locations.

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43. *Twombly*, 550 U.S. at 569 (quoting AREEDA & HOVENKAMP, *supra* note 21, ¶ 307d (Supp. 2006)).

44. *Id.*

45. Transcript of Oral Argument at 31, *Twombly*, 550 U.S. 544 (No. 05-1126), available at [http://www.supremecourtus.gov/oral\\_arguments/argument\\_transcripts/05-1126.pdf](http://www.supremecourtus.gov/oral_arguments/argument_transcripts/05-1126.pdf).

46. On the initial assignments under the antitrust consent decree, see *supra* note 4.

47. Actually, the complaint alleged that the ILECs had complained repeatedly that the Telecommunications Act required them to interconnect with CLECs at below cost, and that this entailed that competitive entry as a CLEC would have been profitable. See *Twombly v. Bell Atl. Corp.*, 425 F.3d 99, 118 (2d Cir. 2005) (discussing the Complaint ¶ 39). The allegation is a non-sequitur: the fact that a new entrant can purchase an input at below cost does not guarantee that it will be profitable.

48. See *Twombly*, 550 U.S. at 546 (noting that other firms were entering the markets as CLECs).

One might play this story on for a few more rounds, but the point should be clear: reasoning of this sort turns ordinary competitive business behavior into allegations of a conspiracy. And the world would contain millions of them, *provided* that we accept the premise, which must be something like “a firm will enter a different market any time it appears profitable to do so, unless it is conspiring with a rival in that new market.”

In sum, the complaint in *Twombly* attempted to manufacture something out of nothing. In the *Twombly* case even the injury must be inferred—that is, an expert would postulate that prices would have been lower had the two pizza restaurant owners built stores in one another’s territories. Indeed, entry into a new market virtually always lowers prices unless someone else reduces its output by an amount at least equal to the output of the new entrant.

*Twombly* clearly reached the correct conclusion, but it could have done less damage to the values of notice pleading stated in the Federal Rules had it focused more narrowly on the mechanisms by which anticompetitive agreements are proven.

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