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13 UNITED STATES DISTRICT COURT
14 NORTHERN DISTRICT OF CALIFORNIA
15 OAKLAND DIVISION

17 IN RE ONLINE DVD RENTAL
18 ANTITRUST LITIGATION

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Hon. Phyllis J. Hamilton

19 This document relates to:

**NETFLIX'S REPLY IN SUPPORT OF
20 ITS RENEWED MOTION TO
21 DECERTIFY THE NETFLIX
22 SUBSCRIBER LITIGATION CLASS**

21 All Actions

Date: September 28, 2011
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1 **I. INTRODUCTION**

2 Plaintiffs admit that several months ago a conflict arose in Lead Class Counsel's
3 concurrent representation of both the plaintiff class and defendant Walmart. *See* Opp. at 8.
4 Plaintiffs also admit that Lead Class Counsel should have disclosed this conflict to the Court.
5 *See id.* Instead, class counsel remained silent about the conflict. Consequently, as soon as
6 Netflix learned of the conflict, it was compelled to bring it to the attention of the Court. As a
7 class action defendant, Netflix has a direct interest in seeing that potential defects in
8 representation of the certified class are adequately vetted by the Court so that any judgment will
9 be binding on absent class members and preclude absent class members from raising identical
10 claims in subsequent lawsuits.

11 While Lead Class Counsel claims to have obtained conflict waivers from the named class
12 representatives purporting to waive the direct conflict between the plaintiff class and defendant
13 Walmart, such waivers, which Plaintiffs have not produced to Netflix, are ineffective. Direct
14 conflicts cannot be waived on behalf of absent class members where the class has been certified
15 and where the waivers are obtained from interested class representatives on the verge of
16 collecting thousands of dollars in incentive payments under the settlement. Even if the conflict
17 could have been waived by the named class representatives, the very appearance of divided
18 loyalties renders Lead Class Counsel inadequate to represent the class, regardless of whether the
19 conflict has actually had negative effects on counsel's representation of the class. The class
20 should therefore be decertified, at least until new Class Counsel can be appointed who satisfy the
21 requirements of Rule 23(g).

22 **II. NETFLIX WAS COMPELLED TO RAISE LEAD CLASS COUNSEL'S**
23 **CONFLICTED REPRESENTATION TO PROTECT NETFLIX FROM FUTURE**
24 **CHALLENGES TO THE VALIDITY OF THIS CLASS ACTION**

25 Contrary to Plaintiffs' arguments that Lead Class Counsel's direct conflict with the
26 plaintiff class "does not touch Netflix," Opp. at 1, Netflix in fact has a strong interest in ensuring
27 that all significant defects in representation of the certified class are adequately vetted by the
28 Court so that any judgment will be binding on absent class members.

1 A class action defendant has a direct interest in ensuring that all members of a certified
2 class are bound by res judicata. *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 805 (1985)
3 (class action defendant has “a distinct and personal interest in seeing the entire plaintiff class
4 bound by res judicata”). Class members may later challenge the res judicata effect of a judgment
5 in a class action where they did not have adequate representation. *Hanlon v. Chrysler Corp.*, 150
6 F.3d 1011, 1020 (9th Cir. 1998) (“To satisfy constitutional due process concerns, absent class
7 members must be afforded adequate representation before entry of a judgment which binds
8 them.”); *Pelt v. Utah*, 539 F.3d 1271, 1285 (10th Cir. 2008) (“a court determining the res
9 judicata effect of a prior class judgment on an absent class member must evaluate the adequacy
10 of representation in terms of both the first court’s initial inquiry, as well as in light of whether the
11 representation was adequate after the termination of the lawsuit”); *Gonzales v. Cassidy*, 474 F.2d
12 67, 74 (5th Cir. 1973) (“Due process of law would be violated for the judgment in a class suit to
13 be res judicata to the absent members of a class unless the court applying res judicata can
14 conclude that the class was adequately represented in the first suit.”). Consequently, a class
15 action defendant seeking to protect its interest in a binding judgment must have the ability to
16 raise any defects in adequacy of representation to the court.

17 Here, Lead Class Counsel’s failure to disclose its direct conflict with the class placed the
18 binding nature and res judicata effect of this class action in jeopardy. If the conflict issue had not
19 been raised by Netflix so that it could be considered by the Court, Netflix would have been
20 exposed to the potential for subsequent lawsuits from absent class members raising identical
21 claims. In such a lawsuit, the plaintiffs would seek to rebut a res judicata defense by asserting
22 that the Court here had never considered the conflict in determining the adequacy of Lead Class
23 Counsel, such that the judgment should not be binding on them. Netflix thus has “a distinct and
24 personal interest” in raising the issue of Lead Class Counsel’s direct conflict with the class to
25 ensure that a judgment in this action will be binding on absent class members.

1 **III. LEAD CLASS COUNSEL’S DIRECT CONFLICT BETWEEN THE PLAINTIFF**
 2 **CLASS AND DEFENDANT WALMART CANNOT BE WAIVED WITHOUT**
 3 **CONSENT FROM ALL MEMBERS OF THE CERTIFIED CLASS**

4 As explained in Netflix’s opening brief (“Mot.”), while Lead Class Counsel claims to
 5 have obtained conflict waivers from the named class representatives purporting to waive Lead
 6 Class Counsel’s direct conflict between the plaintiff class and defendant Walmart, such waivers
 7 are ineffective. Mot. at 6-8. Direct conflicts cannot be waived on behalf of absent class
 8 members where the class has been certified and where the waivers are obtained from interested
 9 class representatives on the verge of collecting thousands of dollars in incentive payments under
 10 the settlement with Walmart.¹ *Id.*

11 In responding to Netflix’s motion, Plaintiffs incorrectly tell the Court that “Netflix relies
 12 on a single case in arguing that class representatives cannot waive conflicts on behalf of absent
 13 class members.” Opp. at 7. In fact, Netflix cited half a dozen cases recognizing that direct
 14 conflicts with the interests of the class cannot be waived on behalf of absent class members. *See*
 15 Mot. at 6-7 (citing *Baas v. Dollar Tree Stores, Inc.*, No. 07-03108, 2008 WL 906496, at *3-4
 16 (N.D. Cal. Apr. 1, 2008) (recognizing need to obtain informed written consent from absent class
 17 members if class is certified); *Moreno v. Autozone, Inc.*, No. 05-4432, 2007 WL 4287517, at *7
 18 (N.D. Cal. Dec. 6, 2007); *Palumbo v. Tele-Communications, Inc.*, 157 F.R.D. 129, 133 (D.D.C.
 19 1994); *McCauley v. Family Dollar, Inc.*, No. 10-0363, slip op. at 6 (W.D. Ky. Nov. 1, 2010)
 20 (copy submitted in this action as ECF No. 330-6); *Davis v. Kraft Foods N. Am.*, No. 03-6060,
 21 2006 WL 237512, at *13 (E.D. Pa. Jan. 31, 2006); *All Star Carts & Vehicles, Inc. v. BFI Can.*
 22 *Income Fund*, No. 08-1816, 2010 WL 2243351, at *7 (E.D.N.Y. June 1, 2010)).

23 Plaintiffs also incorrectly tell the Court that “Netflix does not cite or discuss California
 24 Rule of Professional Conduct 3-310(C)(3).” Opp. at 1. In fact, Netflix did cite and quote that
 25 rule. *See* Mot. at 7 (“Here, even to try to obtain an effective waiver, Class Counsel would have

26 ¹ Because Plaintiffs will not produce the waiver letters at issue to Netflix, Netflix is unable to
 27 determine whether the letters provided adequate information to obtain informed consent even
 28 from the class representatives.

1 been required to obtain informed written consent from ‘each’ of the tens of millions of absent
2 class members before continuing to represent the class when the conflict arose. Cal. R. Prof.
3 Conduct 3-310(C) (attorneys must obtain ‘the informed written consent of each client’ before
4 even accepting representation of clients that are adverse to other clients’’). As Netflix explained
5 in its opening papers, the express language of Rule California Rule of Professional Conduct 3-
6 310(C) required Plaintiffs to obtain informed written consent from “each” client affected by the
7 conflict before continuing to represent the class. *Id.* Lead Class Counsel violated the rule by
8 continuing to represent the class after the conflict arose without first obtaining the required
9 informed written consent from absent class members, or even seeking approval from the Court to
10 proceed without obtaining consent from absent class members.

11 In arguing that it was not necessary to obtain informed written consent from absent class
12 members, Plaintiffs cite *Sharp v. Next Entm’t, Inc.*, 163 Cal. App. 4th 410 (2008), in which the
13 California Court of Appeal for the Second District held, on a motion for *disqualification* (not
14 decertification), that it was not necessary for plaintiffs’ counsel to obtain a conflict waiver from
15 unnamed putative class members where no attempt had even been made to certify the class. The
16 rule obtained in *Sharp* expressly applied only to conflicts that arise “before class certification is
17 sought.” *Id.* at 435 (emphasis added). The court did not consider the effect of conflicts that arise
18 after the class has been certified. The distinction is critical because, under California law, the
19 attorney-client relationship between class counsel and absent class members does not form until
20 after the class has been certified. See *Kullar v. Foot Locker Retail, Inc.*, 191 Cal. App. 4th 1201,
21 1205 (2011) (“since no class has yet been certified . . . no attorney-client relationship has yet
22 arisen between [counsel] and the members of the putative class”). Once the class is certified,
23 absent class members of the certified class are parties represented by class counsel for purposes
24 of applying the rules of professional conduct. *Hernandez v. Vitamin Shoppe Indus., Inc.*, 174
25 Cal. App. 4th 1441, 1460-61 (2009) (attorney violated rules of professional conduct with respect
26 to absent members of certified class).

27 Thus, the holding in *Sharp*, which only concerned a putative class that the plaintiffs had
28 not yet even sought to certify, is inapposite here because the Court has already certified the class

1 of Netflix subscribers and appointed Lead Class Counsel to represent the certified class. Indeed,
2 as the *Sharp* court acknowledged, the adequacy of representation requirement during the
3 eventual class certification proceedings would operate to protect against conflicted
4 representation, because the court “[would] not permit certification” if it found that the named
5 representatives “[were] incapable of providing informed written conflict waivers.” 163 Cal.
6 App. 4th at 433. But prior to any class certification proceedings, that inquiry was premature
7 under the facts presented in *Sharp*.

8 Moreover, unlike Lead Class Counsel’s direct conflict with the plaintiff class and
9 defendant Walmart, the conflict in *Sharp* was not a direct conflict between concurrent
10 representations of adverse parties by class counsel. Rather, in *Sharp*, before any attempt had
11 been made to certify the putative class, the defendants brought a motion to disqualify plaintiffs’
12 counsel, arguing that plaintiffs’ counsel was conflicted because the nonparty guild to which the
13 named plaintiffs belonged was paying the attorney fees. *Id.* at 421. The only concern was that
14 the plaintiffs’ attorneys may have been tempted to pursue the agenda of the guild instead of
15 maximizing the monetary recovery for the class. *See id.* The court recognized that
16 disqualification would have been appropriate if it were “not reasonably likely that the lawyer will
17 be able to provide adequate representation to one or more clients.” *Id.* at 436.

18 Here, unlike *Sharp*, it is not reasonably likely that Lead Class Counsel can provide
19 adequate representation because any win for the class in settlement is a direct loss for its other
20 client, Walmart, and because Lead Class Counsel will have to drag its client Walmart through
21 the mud in any zealous attempt to prevail on Plaintiffs’ claims against Netflix.² *See Mot.* at 5-6.
22 As discussed at the hearing on summary judgment, Plaintiffs’ case against Netflix here requires
23 the jury find that every witness from Walmart lied under oath. “The spectacle of an attorney
24

25
26 ² Plaintiffs argue that that the procedural posture of their case *against Walmart* means that
27 the conflict is not serious, noting that the case against Walmart was stayed and that a settlement
28 with Walmart has been agreed to. *Opp.* at 8. These points are irrelevant: Walmart is a crucial
witness in Plaintiffs’ case *against Netflix*, regardless of the status of their case against Walmart.

1 skewering her own client on the witness stand in the interest of defending another client demeans
2 the integrity of the legal profession and undermines confidence in the attorney-client
3 relationship.” *Baas*, 2008 WL 906496, at *4 (quoting *Hernandez v. Paicius*, 109 Cal. App. 4th
4 452, 467 (2003)). Very different from the facts of *Sharp*, *Baas* is the only case cited by the
5 parties to consider whether class representatives can waive a conflict involving concurrent
6 representation of a plaintiff class and a party who class counsel would have to treat as an adverse
7 witness at trial in the class action. *Id.* The court in *Baas* recognized that in order to prevail on
8 the class claims, class counsel would “either have to cross-examine [the adverse witness client]
9 and impeach his credibility, or ‘soft-pedal’ their examination of [the adverse witness client] to
10 the detriment of their representation of the class members in this action.” *Id.* The court held that
11 such a conflict would violate the “duty of loyalty Plaintiffs’ counsel owe to all their clients.” *Id.*
12 at *3. Consequently, certification had to be denied. *Id.* at *4

13 Plaintiffs also incorrectly rely on a comment to the ABA Model Rules of Professional
14 Conduct that was cited by the court in *Sharp*:

15 When a lawyer represents or seeks to represent a class of plaintiffs or defendants
16 in a class-action lawsuit, unnamed members of the class are ordinarily not
17 considered to be clients of the lawyer for purposes of applying paragraph (a)(1) of
18 this Rule [that restricts representation when there are concurrent conflicts of
19 interest]. Thus the lawyer does not typically need to get the consent of such a
person before representing a client suing the person in an unrelated matter.
Similarly, a lawyer seeking to represent an opponent in a class action does not
typically need the consent of an unnamed member of the class whom the lawyer
represents in an unrelated matter.

20 *Sharp*, 163 Cal. App. 4th at 433-34 (quoting ABA Model Rules Prof'l Conduct, R. 1.7 cmt. 25)
21 (bracketed text in original) (emphasis added).

22 As Plaintiffs concede, this comment has not yet been adopted by the California Supreme
23 Court and is thus not a part of the California Rules of Professional Conduct that govern class
24 counsel’s conduct in this action. *See Opp.* at 6 n.2. Even so, as the underlined words
25 “ordinarily” and “typically” in the above quote demonstrate, the comment recognizes exceptions
26 to the proposed rule. Such exceptions are easily identified by looking at the “typical” situations
27 expressly described in the comment: first, the situation where a lawyer seeks to represent a
28 client who is suing one of the unnamed absent class members in an unrelated matter; and second,

1 the situation where a lawyer seeks to represent a client against a class where the lawyer already
2 represents one of the unnamed absent class members in an unrelated matter. *See* ABA Model
3 Rules Prof'l Conduct, R. 1.7 cmt. 25. As these two "typical" situations demonstrate, the
4 proposed rule (not yet enacted) to excuse counsel from obtaining informed written consent from
5 an absent class member would only apply to those conflicts that affect only a single absent
6 member of the class. It would not apply to the atypical situation where a lawyer, such as Lead
7 Class Counsel, seeks to represent both the entire class and the class adversary.

8 Lead Class Counsel was, therefore, required to obtain informed written consent from
9 "each" absent member of the certified class before continuing to represent the entire class. If
10 obtaining the required consent is not practical because of the large size of the class, Lead Class
11 Counsel cannot be permitted to serve in that capacity. *See Baas*, 2008 WL 906496, at *4
12 ("Plaintiffs' counsel would need to obtain waivers from every class member, which, as a
13 practical matter, they cannot do from the absent class members. Therefore, the Court concludes
14 that Plaintiffs have not demonstrated their counsel would adequately represent the class as
15 required by Rule 23(a)(4)."); *Moreno*, 2007 WL 4287517, at *7 (disqualifying conflicted counsel
16 where "[a]s a practical matter, [class counsel] cannot obtain written waiver of the actual conflicts
17 of interest that exist from the absent class members").

18 **IV. EVEN IF A WAIVER FROM THE CLASS REPS COULD SATISFY CLASS**
19 **COUNSEL'S PROFESSIONAL OBLIGATIONS, THE APPEARANCE OF**
20 **DIVIDED LOYALTIES RENDERS LEAD CLASS COUNSEL INADEQUATE**

21 Even if obtaining conflict waivers only from the class representatives were effective to
22 fulfill Lead Class Counsel's professional responsibilities, the appearance of Lead Class
23 Counsel's divided loyalties has rendered its representation of the class inadequate.

24 The adequacy of class counsel -- and by extension the ability of the class action to bind
25 absent class members -- may be lost with even the mere "appearance of divided loyalties."
26 *Rodriguez v. West Publ'g Corp.*, 563 F.3d 948, 968 (9th Cir. 2009) (quoting *Kayes v. Pac.*
27 *Lumber Co.*, 51 F.3d 1449, 1465 (9th Cir. 1995) ("The responsibility of class counsel to absent
28 class members whose control over their attorneys is limited does not permit even the appearance
of divided loyalties of counsel.")); *accord Baas*, 2008 WL 906496, at *2. Where class counsel is

1 caught in the appearance of divided loyalties, it makes no difference whether the conflict has
2 actually affected class counsel's representation of the class or not. *Kayes*, 51 F.3d at 1465 ("The
3 'appearance' of divided loyalties refers to differing and potentially conflicting interests and is not
4 limited to instances manifesting such conflict.").

5 Plaintiffs incorrectly argue that *Rodriguez* supports a determination here that the Lead
6 Class Counsel's representation is adequate despite the appearance of divided loyalties because
7 the Ninth Circuit in *Rodriguez* chose not to overturn the district court's approval of a class
8 settlement despite class counsel's breach of the duty of loyalty to some class members. *See Opp.*
9 at 8-9 (citing *Rodriguez*, 563 F.3d at 961). But as Plaintiffs concede, "*Rodriguez* is factually
10 distinguishable." *Id.* at 9. There, five of the seven class representatives had entered into
11 agreements with their separate counsel that required class counsel to seek a predetermined value
12 of incentive awards for the class representatives. *Rodriguez*, 563 F.3d at 957. Class counsel
13 failed to disclose these agreements at the class certification stage. The Ninth Circuit held that
14 "[i]t was inappropriate not to disclose these agreements at the class certification stage, because
15 an ex ante incentive agreement is relevant to whether a named plaintiff who is party to one can
16 adequately represent the class." *Id.* at 968. "However, this impropriety did not require the
17 district court to reject the settlement negotiated in [the] case because two non-conflicted class
18 representatives with non-conflicted counsel participated." *Id.* Though it upheld the settlement,
19 the Ninth Circuit reversed the award of attorney's fees to class counsel and remanded for the
20 district court to reconsider whether class counsel was entitled to recover its fees in light of the
21 violation of the duty of loyalty. *Id.* at 969.

22 Here, like *Rodriguez*, Lead Class Counsel violated the duty of loyalty to the class and
23 duty of candor to the Court by failing to disclose a conflict that had an impact on the adequacy of
24 representation of the class. However, unlike *Rodriguez*, the conflict here is far more direct and
25 concerning because it involves concurrent representation of adverse parties and witnesses, not
26 merely an agreement to seek a slightly larger incentive payment for some class representatives.
27 Indeed, the present conflict is of the type that has been held to be impermissible and unwaivable
28 in the class action context. *See Baas*, 2008 WL 906496, at *4. In addition, unlike *Rodriguez*, the

1 direct conflict created by Lead Class Counsel’s representation of both the plaintiff class and
2 defendant Walmart does not merely affect settlement. Rather, the conflict is ongoing and will
3 continue throughout this litigation if the case proceeds to trial against Netflix. There is no reason
4 the Court cannot and should not, in light of the nature of the conflict and Lead Class Counsel’s
5 failure to disclose it, cure the impermissible “appearance of divided loyalties” by simply
6 decertifying the class until new lead class counsel can be appointed.

7 **V. DECERTIFYING THE CLASS UNTIL ADEQUATE LEAD COUNSEL CAN BE**
8 **APPOINTED WILL BENEFIT, NOT HARM, THE CLASS**

9 Contrary to Plaintiffs’ arguments, decertifying the class to appoint adequate class counsel
10 will only benefit, not harm, the class.

11 While Plaintiffs argue that decertification at this stage will “harm the class by erasing a
12 hard-fought, arms-length settlement with Wal-Mart that provides millions of dollars in benefits
13 to the class,” Opp. at 9, the reality is that the settlement benefit to class members amounts to less
14 than 50 cents per class member (given the total cash settlement value of \$27.25 million minus
15 the costs and fees to be taken out, divided among an assumed class of 40 million subscribers).
16 Thus any actual harm to class members caused by a small delay in receiving their 50 cents is
17 minimal. Even so, decertification of the class need not derail the Walmart settlement. The Court
18 can take the motion for approval of the settlement under submission until new, adequate lead
19 class counsel has been appointed in the context of a motion to recertify the class. Assuming the
20 settlement is ratified by new lead class counsel, the Court can then approve the same settlement
21 if it otherwise determines that approval is appropriate.

22 In fact, an order outlining a similar course issued just this week in another large antitrust
23 class action where the court was forced to decertify another class represented by Lead Class
24 Counsel Robert Abrams due to a conflict that arose while approval of a class settlement was
25 pending:

26 [Decertifying the class now] does not mean, however, that the joint motion to
27 preliminarily approve the settlement agreement must be denied or that the
28 settlement cannot under any circumstances be finally approved. Since this matter
has been subject to the adversarial process and potential class members have been
afforded significant structural protections, except for representation by separate

1 counsel, it seems to the Court that the appropriate course is for the Court to take
2 the joint motion for preliminary approval of the settlement under advisement
3 pending appointment of separate counsel and class representatives for the DFA
4 subclass. After an appropriate opportunity for counsel to review the matter, it
5 may be possible for the Court to certify the DFA subclass for settlement purposes,
6 grant the motion to preliminary approve the settlement agreement, give notice of
7 the settlement and proceed with a fairness hearing where objections, if any, can be
8 heard and resolved.

9 *Sweetwater Farms, Inc. v. Dean Foods Co.*, No. 07-00208, ECF No. 1262, at *9-10 (E.D. Tenn.
10 Aug. 31. 2011) (Attachment A hereto). Notably, in the *Sweetwater Farms* action, Lead Class
11 Counsel Robert Abrams agreed with the court’s approach outlined above. *See id.*, ECF No. 1265
12 (Attachment B hereto).

13 In addition, contrary to Plaintiffs’ assertions, decertification to appoint new lead class
14 counsel need not cause the class to lose the benefit of counsel familiar with the case. Plaintiffs
15 have been simultaneously represented by several law firms that have substantively participated in
16 every aspect of this action. The Court may well be able to find an adequate, non-conflicted lead
17 class counsel among them, or at a minimum, their continued participation in the action as co-
18 counsel would confer the same benefits due to their longstanding involvement and familiarity
19 with the case.

20 **VI. CONCLUSION**

21 For the reasons set forth herein, the Court should decertify the class of Netflix subscribers
22 previously certified in this action until new lead class counsel can be appointed.

23 Dated: September 2, 2011

Respectfully submitted,

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26 By: /s/ Jonathan M. Jacobson
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