

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

10 CIV 1733

BRANDON BRUNO on behalf of himself
and all others similarly situated,

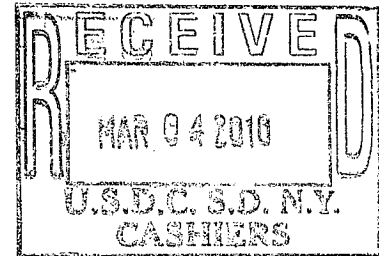
Plaintiff,

No.

v.

WARNER HOME VIDEO, WARNER
BROS. HOME ENTERTAINMENT INC.,
WARNER BROS. ENTERTAINMENT
INC. and NETFLIX, INC.,

Defendants.



CLASS ACTION COMPLAINT

Plaintiff Brandon Bruno ("Plaintiff"), individually and on behalf of all others similarly situated, allege the following based upon the investigation of counsel, except for those allegations pertaining to plaintiff, which are based on personal knowledge. The investigation of counsel is predicated upon, among other things, a review of court filings, press releases, media reports, and other publicly available information relating to the video sales and rental businesses.

I. NATURE OF THE ACTION

1. Plaintiff is a subscriber and customer of Netflix, Inc. ("Netflix"). Netflix is an internet-based video rental company that uses the U.S Postal Service to deliver DVD and Blu-ray titles (collectively referred to herein as "Videos") to its customers. Netflix is, by a substantial margin, the largest Video-by-mail rental business in the U.S.

2. Warner Home Video ("Warner Home Video"), a division of Warner Bros. Home Entertainment Inc. ("WBHE"), is the largest distributor of filmed entertainment in the world. Defendant Warner Bros. Entertainment Inc. ("WBE") is the parent company of WBHE. Warner

Home Video, WBHE, and WBE are referred to collectively herein as "Warner."

3. Plaintiff brings this lawsuit as a class action against defendants Warner and Netflix (collectively, "Defendants"), on behalf of all Netflix subscribers during the period from January 6, 2010 to the present (the "Class").

4. Plaintiff seeks damages and equitable relief from Defendants under Section 1 of the Sherman Antitrust Act, 15 U.S.C. § 1, on behalf of themselves and the Class. As detailed below, Plaintiff alleges that Warner entered into an agreement with Netflix to maintain and enforce a 28 day no-rental window for Video titles released and sold by Warner to the public (the "Agreement").

5. Pursuant to the Agreement, Netflix eliminated subscriber access to Warner's new-release¹ Video titles for a period of 28 days after the titles are first released for sale or rental to the public.

6. Prior to Netflix entering into the Agreement with Warner, Netflix customers had access to Warner's new-release Video titles as part of their subscription plans. Defendants took away that access through their scheme to restrain trade. As a result of the restrictions imposed through the Agreement, Netflix subscribers' subscription plans have materially declined in value: Netflix customers have lost the ability to access a substantial portion of the Videos available in the new-release Video market.

7. Consumer demand for a new-release Video is highest during the weekend immediately after its release and declines substantially thereafter. Accordingly, the value of each of Netflix's subscription packages has decreased. Plaintiff and the Class members have been, and are currently being, damaged in that they still pay the price Netflix previously charged for

¹ In this Complaint, a "new-release" Video refers to those Videos that are within 28 days of the day they are released for sale or rental to the public.

each of its subscription plans prior to the date of the Agreement.

8. Moreover, the Agreement is part and parcel of an anti-competitive scheme under which Warner leveraged its substantial market power and dominance to cut off access to Warner Video rentals for the first 28 days after the titles are released to the public. Through this scheme, Warner agreed with Netflix to fix Video rental prices, unreasonably restrain trade, and to illegally maintain and enhance Netflix's market power in the Video-by-mail business.

9. The Agreement was specifically intended to protect Warner from competition for its sales and rentals of newly releases Videos. Defendants accomplished this by cutting off the supply of Warner Video titles to Netflix for the first 28 days after the titles are released for sale to the public, in exchange for Netflix receiving discounted pricing on Warner Video titles after the conclusion of the 28-day period.

10. Absent Defendants' anti-competitive conduct, the value of Plaintiff's and the Class members' Netflix subscriptions would not have been diminished. Plaintiff thus seeks damages and equitable relief under Section 1 of the Sherman Antitrust Act, 15 U.S.C. § 1, and Clayton Act, 15 U.S.C. § 15.

II. JURISDICTION AND VENUE

11. Plaintiff brings this action pursuant to Sections 4 and 16 of the Clayton Act, 15 U.S.C. §§ 15(a) and 26, to recover treble damages, equitable relief, costs of suit and reasonable attorneys' fees for Defendants' violations of Section 1 of the Sherman Act, 15 U.S.C. § 1. Subject matter jurisdiction is proper pursuant to Section 4(a) of the Clayton Act, 15 U.S.C. § 15 (a), and 28 U.S.C. §§1331 and 1337, because the action arises under the laws of the United States.

12. Venue is proper in this federal judicial district under 15 U.S.C. § 15(a) because

Defendants reside, or are found, or have an agent here. Warner has a principal place of business located in this District. In addition, Netflix has several shipping centers located in New York. Alternatively, venue is proper in this judicial district pursuant to Section 12 of the Clayton Act, 15 U.S.C. § 22, and 28 U.S.C. §1391 (b) and (c), because during the Class Period Defendants resided, transacted business, were found, or had agents in this District, and because a substantial part of the events giving rise to Plaintiff's claims occurred, and a substantial portion of the affected interstate trade and commerce described below has been carried out, in this District.

13. The Court has personal jurisdiction over Defendants pursuant to Section 12 of the Clayton Act, 15 U.S.C. § 22.

III. PARTIES

14. Plaintiff Brandon Bruno, a resident of Cherry Hill, New Jersey, is a Netflix subscriber and was thus injured by Defendants' conduct.

15. Defendant Warner Home Video is a Delaware corporation with a principal place of business in New York, New York. Warner Home Video is a division of Warner Bros. Home Entertainment Inc. Warner Home Video distributes DVDs and Blu-ray discs containing filmed entertainment product produced or otherwise acquired by Time Warner, Inc.'s various content-producing subsidiaries and divisions, including Warner Bros. Pictures, Warner Bros. Television, New Line Cinema LLC, Home Box Office and Turner Broadcasting System, Inc., which together command approximately 20 percent of the U.S. and Canadian box office.

16. Defendant Warner Bros. Home Entertainment Inc. is a Delaware corporation with a principal place of business in New York, New York.

17. Defendant Warner Bros. Home Entertainment Inc. is a Delaware corporation with a principal place of business in New York, New York.

18. Netflix, Inc. is a Delaware corporation with its principal place of business located in Los Gatos, California. Netflix was formed in 1997 as one of the first Video rental companies to distribute Video titles to its customers through the U.S. Mail. Netflix features a subscription-based pricing model, with monthly prices currently ranging from \$4.99 to \$16.99.

19. Netflix has 100 shipping points nationwide, including numerous shipping points located in New York. More than 97% of Netflix's subscribers receive their Videos within approximately one business day of shipping. Near the end of 2002, Netflix served around 1 million subscribers. By the beginning of 2009, that number had grown to 10 million, and it currently has approximately 12.3 million subscribers. Every business day, Netflix ships an average of 2.2 million Videos to its subscribers nationwide. Netflix expects to end 2010 with between 15.5 million to 16.3 million subscribers, all of which will be damaged as they will be paying for subscriptions that would be much more valuable but for Defendants' wrongful conduct alleged herein. Netflix reported revenues of \$1.67 billion and net income of \$115.8 million for the year ending December 31, 2009.

IV. INTERSTATE TRADE AND COMMERCE

20. The activities of Defendants, as described in this Complaint, were within the flow of, and substantially affected, interstate commerce.

21. During the time period covered by this Complaint, Defendants sold, distributed and/or rented Warner's new-release Video titles throughout the United States.

22. Defendants have sold, shipped, and rented substantial quantities of Warner's new-release Video titles in a continuous and uninterrupted flow of interstate commerce to customers located throughout the U.S.

V. FACTS

23. Movie rental companies have operated successfully in the U.S. for decades. The movie rental market has also been enjoyed by consumers, allowing them to watch movies in the comfort and convenience of their own home at affordable prices.

24. Since the introduction of Videos into the marketplace, Videos have become the dominant medium for the distribution of movies for home viewing. Video rental companies are able to purchase titles and rent them to customers without permission from copyright owners as a result of the First Sale Doctrine. This First Sale Doctrine is a limitation on copyright that was first recognized by the U.S. Supreme Court and subsequently codified in the Copyright Act of 1976, 17 U.S.C. § 109. The doctrine allows a purchaser to transfer (*i.e.*, sell, give away, or rent) a lawfully made copy of a copyrighted work (*i.e.*, a Video) without permission of the copyright holder once it has been obtained. As a result, Video rental companies can purchase copies of Video titles and rent them out to customers without having to share any revenue with the copyright owners of the movies.

25. At first, "brick & mortar" stores were the dominant distribution method for movie rentals. These are physical stores, such as Blockbuster and Hollywood Video, located throughout the U.S. that typically charge customers a set fee to rent a new-release Video title.

26. Other methods of distribution for movie titles have recently emerged. Video on Demand ("VOD"), which is offered by cable and telecommunications companies throughout the world, provides customers with direct access to new-release movies for rent or purchase through their cable box. Because VOD does not involve a physical Video, the First Sale Doctrine does not apply. Studios or copyright owners, therefore, have control over the distribution of movie titles through the Video medium and can determine the amount of fees that must be paid to the

studio or copyright owner for each rental.

27. The internet has also spawned numerous distribution channels for the sale and rental of new-release movies. Apple, Amazon.com, and Blockbuster are just a few of a growing number of internet retailers that rent or sell movies directly to customers through the internet. Customers use computers or set-top devices, such as TIVO, Roku, and/or video game consoles, to view the movies purchased or rented from these internet retailers. Because these internet distribution channels do not involve a physical Video, the First Sale Doctrine does not apply with respect to rentals through the internet, and the studios or copyright owners control pricing and revenue sharing for the rentals. Although VOD and internet rentals are very convenient, the costs of a rental are, on average, much higher than the cost of renting a movie on a physical Video due to the copyright holders or studios' ability to command a share of the revenue from each rental. Because Warner receives a greater portion of revenue from each rental through the internet or VOD than it does from Netflix Video rentals, Warner has not limited access to new-release movies distributed to consumers through the internet or VOD.

28. Netflix has developed a Video-by-mail rental distribution model which provides Netflix subscribers with convenient, low cost access to Video titles. Netflix uses an internet-based rental system in which customers pay a monthly subscription fee and choose from a list of Video titles on Netflix's website. The Videos are delivered to customers through the U.S. Postal Service, which also enables Netflix to reach every potential Video rental consumer in the United States. Customers create a list, or "queue," of Video titles that they want delivered. Once a customer creates a queue, Netflix immediately delivers the first movie in the customer's queue to the customer. After the customer is finished viewing a Video title, they place the Video in a pre-paid postage stamped envelope provided by Netflix and drop it into a mailbox. Netflix does not

charge late fees. Customers can hold on to a Video as long as they like, but they will not receive the next Video title in their queue until they return the Video to Netflix. Once Netflix receives the movie, it automatically sends out the next Video title in the customer's queue.

29. Netflix's pricing model is subscription based. One of Netflix's most popular plans costs \$16.99 per month, allowing a subscriber to rent up to three DVDs at a time, with unlimited exchanges. Netflix also has a plan for \$13.99 per month for up to two DVDs at a time, with unlimited exchanges, a plan for \$8.99 per month for one DVD at a time, and a plan that costs \$4.99 per month for one DVD at a time and a limit of two rentals per month. Since November 21, 2008, Netflix has offered its subscribers access to Blu-ray discs for an additional fee, depending on the subscription package.

30. Netflix also offers internet video streaming ("Watch Instantly") to its subscribers, enabling the viewing of films directly on a PC or TV at home. The "Watch Instantly" service offers 12,000 choices of mostly older movies and TV shows; by contrast, the Video-by-mail service offers over 100,000 new-release and older titles.

31. Netflix currently has approximately 100 shipping points throughout the U.S., which enables Netflix to provide almost all of its subscribers with delivery of their Video titles in one business day. Netflix's business model has become so successful that it has grown into the largest subscription Video-by-mail rental business in the world with over 12 million customers. Netflix's subscription model gives customers access to over 100,000 DVD titles. As a result of Netflix's success, traditional brick and mortar stores have become unprofitable, and thousands of such stores have closed throughout the U.S. Indeed, in February 2010, Movie Gallery Inc., the owner of Hollywood Video, filed for bankruptcy for the second time in three years. Blockbuster has also been closing down stores at a rapid pace.

32. In an effort to increase its Video, VOD and internet sales and rentals, and circumvent the First Sale Doctrine, Warner threatened to cut off sales to Video rental companies such as Netflix if they did not agree to implement a 28-day period before renting newly released Warner Videos beginning on the date that the Warner Video titles were first made available for sale to the public.

33. For example, on October 26, 2009, Netflix filed a Form 10-Q with the SEC in which it stated:

Some studios have expressed a desire to delay the availability of new releases DVDs [sic] for rental for a brief period of time following the DVDs' release to the retail market and, in connection therewith, would prohibit certain of their wholesalers from selling to various rental outlets, such as Netflix and Redbox. In fact, Universal Studios, Twentieth Century Fox and Warner Bros are engaged in litigation brought by Redbox over this practice. This practice could impact our ability to receive content in an efficient manner and in sufficient quantity to satisfy demand in which case our business could be adversely affected.

<http://www.sec.gov/Archives/edgar/data/1065280/000119312509213071/d10q.htm>.

34. On January 6, 2010, Warner and Netflix announced that they reached a new distribution deal. Warner and Netflix issued a press release announcing the deal that stated, among other things, that "[n]ew release titles on DVD and Blu-ray will be made available to Netflix members after a 28-day window, giving Warner Bros. the opportunity to maximize the sales potential of those titles and Netflix the benefits of reduced product costs and significantly more units and better in-stock levels four weeks after street date." The press release further stated:

The agreement covering DVD and Blu-ray provides a means for Warner Bros. to continue to directly supply Netflix with new titles while establishing a schedule that allows Warner Bros. to get the most from the sales potential of those titles (75 percent of sell-through occurs in the first four weeks) and maximize VOD usage.

<http://www.timewarner.com/corp/newsroom/pr/0,20812,1952041,00.html>.

35. Netflix subscribers were shocked by the news. As explained in media reports, the increased availability of Videos at the end of the 28-day window will mean little to Netflix customers because their demand for the Videos will have diminished by that time. Meanwhile, Warner reaps a share of each of the new-release VOD rentals made by cable companies in the absence of immediate Netflix availability. Rick Aristotle Munarriz, *Netflix Sells Out Its Subscribers*, The Motley Fool, January 7, 2010.

36. Warner's agreement with Netflix is currently being adhered to by both parties, and Netflix customers no longer have access to Warner Video titles through their Netflix subscription service until 28 days after they are released for sale to the public. For example, two new releases, *The Informant!* and *The Box*, both released on Video by Warner on February 23, 2010 for sale to the public, are listed on Netflix's website as not being available for rental by its subscribers until March 23, 2010.

37. Netflix dominates the Video-by-mail business, and its customers are dependent upon it for fast delivery of low priced and convenient Video rentals. As such, most of its customers will continue to use Netflix's services, but many will turn to higher priced rentals for Warner's new-release Video titles. Warner benefits from the Netflix customers that turn to higher-priced VOD or other retailers to rent or purchase Warner movies (where Warner gets a higher percentage of revenue), and Netflix benefits by acquiring Warner Video titles at lower costs for rental to its customers after the 28-day window expires..

38. Netflix apparently has no intention of passing any cost savings along to its customers. Netflix customers are still paying the same monthly subscription fees that they paid prior to enactment of the 28-day window, even though the value of their subscription service has decreased. See MG Siegler, *Netflix Stabs Us In The Heart So Hollywood Can Drink Our Blood*,

TechCrunch.com, January 7, 2010, <http://techcrunch.com/2010/01/07/netflix-hollywood-deal>.

VII. MARKET EFFECTS OF DEFENDANTS' CONDUCT

39. Prior to the Agreement, Plaintiff and the Class received a fixed array of benefits for the subscription fees they paid to Netflix. As a result of the Agreement, Plaintiff and the Class have still been required to pay the same fees, but the value of the benefits received has been substantially reduced.

VIII. CLASS ACTION ALLEGATIONS

40. Plaintiff brings this action individually and on behalf of a Class defined as follows:

All persons who have been subscribers of Netflix at any time since January 6, 2010.

41. Numerosity: Joinder of all Class members is impracticable. While the size of the Class is not yet known with certainty, based on the nature of the trade and commerce involved, Plaintiff reasonably believes that the Class numbers potentially in the tens of millions. Class members are geographically dispersed throughout the United States. The Class members are identifiable from information and records in Defendants' possession, as well as warranty and other records.

42. Commonality: Questions of law and fact are common to the Class, including, but not limited to:

- a. whether Defendants engaged in agreements, contracts, combinations, or conspiracies, which had the purpose and/or effect of unreasonably restraining competition and limiting consumer access to competing and lower-priced rentals of new-release Warner Video titles;
- b. whether Defendants' unreasonably anti-competitive contracts, combinations, and

conspiracies have caused Plaintiff and the members of the Class to suffer antitrust injury in the nature of overcharges;

- c. whether Defendants' unlawful conduct caused Plaintiff and the Class members to pay more for the rental of Warner's new-release Video titles than they otherwise would have paid;
- d. the appropriate Class-wide measure of damages; and
- e. whether Defendants' anti-competitive conduct is continuing, thus entitling the Class to injunctive relief to promote unrestrained trade and free and fair competition.

43. **Typicality:** Plaintiff's claims are typical of the claims of the members of the Class. Plaintiff and the Class members are subscribers of Netflix and were overcharged and thus injured by the same wrongful conduct of Defendants. Defendants' violation of the antitrust laws, the effects of such violations, and the relief sought are all issues or questions that are common to Plaintiff and the Class members.

44. **Adequacy:** As representatives of the Class, Plaintiff will fairly and adequately protect the interests of all Class members. Plaintiff has retained competent counsel experienced in litigation of this nature.

45. **Predominance:** The questions of law and fact that are common to the members of the Class predominate over any questions affecting only individual Class members. Whatever possible difficulties may exist in the management of the class action are greatly outweighed by the advantages of the class action procedure. Those advantages include, but are not limited to, providing Class members with a method for redress of claims that might otherwise not warrant individual litigation.

46. Superiority: Class action treatment is a superior method for the fair and efficient adjudication of the controversy, in that, among other things, such treatment will permit a large number of similarly situated persons to prosecute his or her common claims in a single forum simultaneously, efficiently, and without the unnecessary duplication of evidence, effort, and expense that numerous individual actions would engender. A class action enables injured persons or entities to obtain redress on claims that might not be practicable to pursue individually. Class treatment also eliminates the potential for inconsistent adjudications.

COUNT I

VIOLATION OF 15 U.S.C. § 1 (AGREEMENTS RESTRAINING TRADE)

47. Plaintiff hereby incorporates each preceding and succeeding paragraph as though fully set forth herein.

48. This claim is pled as to Warner and Netflix.

49. The Agreement, and its enforcement, constitute contracts, combinations and conspiracies that substantially, unreasonably, and unduly restrain trade in the relevant market, and harmed Plaintiff and the Class thereby.

50. The Agreement covers a sufficiently substantial percentage of the relevant market to harm competition.

51. There is no legitimate, pro-competitive business justification for the Agreement that outweighs its harmful effect. Even if there were some conceivable justification, the Agreement is broader than necessary to achieve such a purpose.

52. Plaintiff and members of the Class were injured by the collusion and conspiracy alleged above which facilitated, enabled, assisted or furthered Defendants' substantial foreclosure and exclusion of competition in the relevant markets. Without limiting the generality

of the foregoing, Plaintiff and the members of the Class have been forced to pay artificially inflated subscription fees.

REQUEST FOR RELIEF

WHEREFORE, Plaintiff on behalf of herself and the Class, respectfully request that:

- A. The Court determine that this action may be maintained as a class action pursuant to Rule 23 of the Federal Rules of Civil Procedure and direct that reasonable notice of this action, as provided by Rule 23, be given to the Class;
- B. The acts alleged herein be adjudged and decreed to be unlawful acts in violation of Section 1 of the Sherman Act and that Defendants be enjoined from further violative conduct;
- C. Each member of the Class recovers threefold the damages determined to have been sustained by each of them, and that judgment be entered against Defendants in favor of the Class;
- D. The Class recover its costs of suit, including reasonable attorneys' fees and costs as provided by law; and
- E. The Class be granted such other appropriate relief as may be determined to be just, equitable, and proper by this Court.

JURY DEMAND

Plaintiff hereby demands a trial by jury on all issues so triable.

Dated: March 4, 2010

WEINSTEIN KITCHENOFF & ASHER LLC

By: 

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