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California Appellate Court Rejects Consumers' Sports Channel Bundling Lawsuit

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A California intermediate appellate court on Monday affirmed the dismissal of an unfair competition lawsuit brought by four subscribers to Time Warner Cable Inc. ("TWC") who were dissatisfied by having to pay rate increases associated with TWC's addition of three sports channels – owned by TWC and featuring Los Angeles Lakers and Dodgers games – to a general programming package. As detailed below, the Court found Plaintiffs' action to be expressly preempted by FCC regulations implementing federal communications statutes.[1]

While we have previously covered various challenges to the television industry's channel bundling ecosystem through the prism of federal antitrust "tying" law – including the Ninth Circuit's decision in the consumer class action case *Brantley v. NBC Universal, Inc.*, 675 F.3d 1192 (9th Cir. 2012), and Cablevision's ongoing litigation against Viacom in the Southern District of New York – the *Fischer* suit did not seek to upend the underlying "network of contracts between programmers and distributors" on antitrust grounds.[2] Rather, the suit solely involved a state-law unfair competition claim brought by consumers who did not want to pay $9 per month in additional subscriber fees for sports channels that they claimed not to want or watch.

Background and Lower Court Dismissal

In 2013, Plaintiffs brought a class-action lawsuit against TWC, the Los Angeles Lakers and the Los Angeles Dodgers, alleging that TWC violated California's Unfair Competition Law ("UCL") when it added three sports channels to its enhanced basic cable programming tier. A long-time cable distributor, TWC entered into separate, multibillion deals with the Lakers and Dodgers in 2011 and 2013, respectively, in which it was granted long-term licensing rights to televise those teams' games on sports channels to be run by TWC as a programmer: TWC SportsNet, TWC Deportes, and SportsNet LA.

By bundling those channels on its enhanced basic cable tier – rather than offering them on a stand-alone basis ("a la carte"), or on a specialized sports tier – TWC raised its expanded basic subscription rates by $9 per month

[1] *Fischer v. Time Warner Cable Inc. et al.* (Cal. App. Dist. 2, Feb. 23, 2015).

[2] *See* Class Action Complaint for Restitution and Injunctive Relief for Violations of Section 17200 *Et Seq.* of Cal. Bus. & Prof. Code, at ¶ 2 (filed June 18, 2013) (hereinafter, "Fischer Complaint"). Notably, *Fischer* was brought by the same counsel that had previously represented the *Brantley* plaintiffs, in which a different set of consumer plaintiffs argued that bundling of channels amounted to an illegal "tying" arrangement under the Sherman Act. Having failed to prevail on that issue before the Ninth Circuit, the *Fischer* complaint did not assert a federal or state antitrust claim, and instead merely noted in the introductory section of the Complaint that it was raising allegations within an industry purportedly already "impaired by artificial contract restrictions." *Id.* at ¶¶ 2-3.

for millions of its subscribers in Southern California and certain other Western markets. Plaintiffs' suit alleged that TWC was improperly forcing its subscribers to pay these additional monthly subscriber fees to offset its own programming costs – without giving them the chance to opt-out – even though the majority of its subscribers allegedly do not follow sports and purportedly had no interest in the three sports channels.[3] Plaintiffs further alleged that the Lakers and the Dodgers were also complicit in this arrangement, as they allegedly knew that TWC's would "pass on" these increased costs to its "unwilling" customers.[4]

The Defendants separately demurred to the complaint (the California equivalent of a motion to dismiss) on various grounds, and Los Angeles Superior Court Judge Amy Hogue sustained the demurrers and dismissed the suit without leave to amend in January, 2014. Specifically, Judge Hogue found that federal law permits the practice of "adding a new cable channel to an existing tier of service (rather than offering it as a separate channel)," while acknowledging that "any number of consumers" may find that practice "somehow 'unfair.'"[5] Judge Hogue also held, raising an issue that had not been briefed to her, that a federal regulation of the FCC implementing the federal statutes governing the cable television industry expressly preempted state unfair competition laws such as the UCL.

The Appellate Court's Analysis and Holding

In affirming Judge Hogue's ruling, California's Second District Court of Appeal agreed that the regulatory and statutory scheme governing the cable industry "necessarily" preempted Plaintiffs' state law UCL claim. The FCC regulates the industry pursuant to the Cable Television Consumer Protection and Competition Act of 1992 (the "Cable Act").[6] Of relevance here, Section 543 of the Cable Act prohibits the practice of "negative option billing"—*i.e.*, charging a subscriber "for any service or equipment" that was not "affirmatively requested by name."[7] As the Court explained, Section 543 "prohibits cable companies from providing a service the customer has not expressly requested and then charging for the service if the customer fails to exercise the negative option of cancelling the subscription or opting out of the service."[8]

In implementing this statutory prohibition on negative option billing, however, the FCC promulgated a regulation that carved out important exceptions to it. According to the FCC's regulation (47 C.F.R. § 76.981), negative option billing does *not* include, *inter alia*, "the addition or deletion of specific channels from an existing tier or service," so long as "such changes do not constitute a fundamental change in the nature of an existing service or

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[3] *Id.* at ¶ 35.

[4] *Id.* at ¶¶ 8-9.

[5] *See* Eriq Gardner, *Judge Blocks Class Action Lawsuit Over Lakers and Dodgers Channels*, THE HOLLYWOOD REPORTER (Jan. 29, 2014), *available at* http://www.hollywoodreporter.com/thr-esq/judge-blocks-class-action-lawsuit-675254.

[6] *See* 47 U.S.C. § 521 *et seq.*

[7] *Id.* at § 543(8)(f).

[8] Slip Op. at 7.

tier of service and are otherwise consistent with applicable [FCC] regulations."[9] The FCC's regulation also states that "state and local governments may not enforce state and consumer protection laws that conflict with or undermine" the FCC's determination that a cable operator may make non-fundamental changes to a service tier without a subscriber's advance agreement.

Against this regulatory backdrop, the Court considered whether TWC adopted a "fundamental change" to its expanded basic tier by unilaterally adding three sports channels and adjusting its subscribers' rates upwards as a result. If the change was "fundamental" in nature, as the Appellants submitted, it would likely be a "negative option billing practice" under the Cable Act, and the FCC's implementing regulation would not apply to preempt the Complaint. If, however, the change was not "fundamental," as TWC and the other Respondents argued, the FCC regulation expressly allows the practice and also preempts the lawsuit.

On this dispositive issue, the Court sided with Respondents, and held that "state consumer protection laws are preempted in regard to negative option billing practices that result in rate hikes due to the addition of a small number of channels because those rate hikes do not represent a 'fundamental change' in service."[10] The Court offered several reasons for this holding.

First, the Court noted that its decision was in line with the only other Court to have considered § 76.981's preemptive effect, *TWC v. Doyle*, 66 F.3d 867 (7th Cir. 1995). In *Doyle*, the Seventh Circuit reversed a grant of summary judgment to the State of Wisconsin, which had sued TWC for unfair trade practices after TWC (i) deleted certain channels from its basic tier; (ii) began to offer the channels on an a la carte basis, and (iii) charged its existing customers for those channels without first notifying them. The Seventh Circuit found the State's claim preempted under § 76.981, relying in part on FCC reports that reflected the FCC's awareness that "§ 76.981 was always intended to have preemptive effect where state consumer protection laws impinged on rate regulations" (as a non-fundamental service change).[11] Similarly, the *Fischer* Court found that Plaintiffs' claims implicated rate regulations, because Plaintiffs sought restitution of TWC's raised rates, "thereby retroactively affecting rates [TWC] has already charged its customers."[12]

Second, the Court found that a literal application of the Cable Act's proscription on negative option billing to "every minor change" to the make-up of a programming tier would be "seriously burdensome to cable operators."[13] For example, the Court noted that if negative option billing were prohibited in all events, cable operators could not delete *any* channels, no matter how insignificant, without first obtaining affirmative customer consent.[14]

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[9] *Id.* at 8 (citing 47 C.F.R. § 76.981(b)).

[10] *Id.* at 15.

[11] *Id.* at 12 (citing *Doyle*, 66 F.3d at 878-881).

[12] *Id.* at 13.

[13] *Id.* at 14.

[14] *Id.* at 11 n. 15.

Third, the Court determined that because only three of nearly 100 channels in TWC's expanded basic tier were affected by TWC's actions, such a change was "minor, [and] not fundamental," and therefore subject to preemption under § 76.981.[15] The Court acknowledged that "[b]y contrast, deleting all existing channels from a particular tier and replacing them with an entirely new set of channels would constitute a fundamental change to a tier of channels. In that hypothetical setting, negative option billing would be implicated and state laws that addressed such changes would not be preempted."[16]

Accordingly, while the Court empathized with the purported "lament of cable television subscribers" that despite expanding television line-ups and higher associated monthly fees, "mostly nothing's on that they wish to view," the court circumscribed the options available to such consumers under state consumer protection laws, at least in California: they "must present such complaints to Congress or the FCC."[17]

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[15] *Id.* at 14.

[16] *Id.* at 13.

[17] *Id.* at 15 n. 18.