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9 Attorneys for Defendant and Counterclaimant,
 Blockbuster Inc.

11 UNITED STATES DISTRICT COURT
 12 NORTHERN DISTRICT OF CALIFORNIA

13 NETFLIX, INC., a Delaware corporation,

14 Plaintiff,

15 vs.

16 BLOCKBUSTER INC., a Delaware
 corporation, DOES 1-50,

17 Defendants.

19 BLOCKBUSTER INC., a Delaware
 corporation,

21 Counterclaimant,

22 vs.

23 NETFLIX, INC., a Delaware corporation,

24 Counterclaim Defendant.

CASE NO. C 06 2361 WHA

**ANSWER TO FIRST
 AMENDED COMPLAINT;
 COUNTERCLAIMS**

DEMAND FOR JURY TRIAL

Complaint Filed: April 4, 2006

25 **ANSWER**

26 Blockbuster Inc. ("Blockbuster") responds as follows to the First
 27 Amended Complaint for Patent Infringement ("Complaint") filed against it by
 28 Netflix, Inc. ("Netflix").

1 1. Answering paragraph 1, Blockbuster admits the allegations about
2 Netflix's corporate status and principal place of business, as well as Netflix's
3 website address and that it has for some time been renting DVDs on a subscription
4 basis. Except as expressly admitted, Blockbuster lacks knowledge or information
5 sufficient to form a belief as to the truth of the allegations of paragraph 1 and
6 thereon generally and specifically denies the allegations thereof.

7 2. Answering paragraph 2, Blockbuster admits that it is a Delaware
8 corporation; that its principal place of business is in Dallas, Texas; that it has a
9 registered agent for service as stated in paragraph 2; that Blockbuster launched
10 Blockbuster Online in 2004; that it has described Blockbuster Online in words
11 similar to those in paragraph 2; that it is registered to do business in the State of
12 California; and that it has conducted business in California and in this District.
13 Except as expressly admitted, Blockbuster lacks knowledge or information
14 sufficient to form a belief as to the truth of the allegations of paragraph 2 and
15 thereon generally and specifically denies the allegations thereof.

16 3. Answering paragraph 3, Blockbuster admits that this action
17 arises under 35 U.S.C. § 101 *et seq.* and that this Court has subject-matter
18 jurisdiction under 28 U.S.C. §§ 1331 and 1338(a). Blockbuster denies that Netflix
19 has any meritorious claims against Blockbuster. Except as expressly admitted and
20 denied, Blockbuster generally and specifically denies the allegations of
21 paragraph 3.

22 4. Answering paragraph 4, Blockbuster admits that this Court has
23 personal jurisdiction over Blockbuster and that Blockbuster regularly conducts
24 business in this District. Blockbuster denies that it has committed any act of patent
25 infringement. Except as expressly admitted and denied, Blockbuster generally and
26 specifically denies the allegations of paragraph 4.

27 5. Answering paragraph 5, Blockbuster does not contest venue in
28 this case and admits that it regularly conducts business in this District. Blockbuster

1 denies that it has committed any act of patent infringement. Except as expressly
2 admitted and denied, Blockbuster generally and specifically denies the allegations
3 of paragraph 5.

4 6. Answering paragraph 6, Blockbuster admits the allegations
5 thereof.

6 **ANSWER TO FIRST CAUSE OF ACTION**

7 **(Alleging Infringement of U.S. Patent No. 7,024,381)**

8 7. Answering paragraph 7, Blockbuster admits that Netflix is listed
9 on the '381 patent as its assignee; that the number, title, and issuance date of the
10 patent are as stated in paragraph 7; and that a copy of the '381 patent was attached
11 as Exhibit A to the copy of the Complaint served on Blockbuster. Blockbuster
12 lacks knowledge or information sufficient to form a belief as to the truth of the
13 allegation that Netflix is the "sole and exclusive owner" of the '381 patent, and
14 Blockbuster thereon denies that allegation. Blockbuster admits and alleges that the
15 scope of each of the numbered claims of the '381 patent is as stated in those
16 respective claims, and Blockbuster denies that paragraph 7 accurately sets forth the
17 scope of the patent. Except as expressly admitted and denied, Blockbuster
18 generally and specifically denies the allegations of paragraph 7.

19 8. Answering paragraph 8, Blockbuster generally and specifically
20 denies the allegations thereof. Without limiting the generality of the foregoing
21 denial, Blockbuster denies that it has violated 35 U.S.C. § 271(a) and denies that it
22 has infringed any rights of Netflix under the '381 patent, whether under § 271(a) or
23 any other provision of the patent laws.

24 9. Answering paragraph 9, Blockbuster denies generally and
25 specifically the allegations thereof. Without limiting the generality of the foregoing
26 denial, Blockbuster denies that it has violated 35 U.S.C. § 271(b) or (c) and denies
27 that it has infringed any rights of Netflix under the '381 patent, whether under
28 § 271(b), § 271(c), or any other provision of the patent laws.

1 10. Answering paragraph 10, Blockbuster admits that it has known
2 of the '381 patent since Blockbuster received Netflix's original complaint in this
3 case. Except as expressly admitted and denied, Blockbuster generally and
4 specifically denies the allegations of paragraph 10. Without limiting the generality
5 of the foregoing denial, Blockbuster further denies that it has infringed or is
6 infringing the '381 patent, whether willfully, deliberately, or in any manner
7 whatsoever; denies that Netflix has suffered or will suffer any injury whatsoever –
8 whether irreparable or otherwise – due to any infringement by Blockbuster; and
9 denies that Netflix is entitled to an injunction or to any other relief, order, or
10 judgment against Blockbuster whatsoever.

11 **ANSWER TO SECOND CAUSE OF ACTION**

12 **(Alleging Infringement of U.S. Patent No. 6,584,450)**

13 11. Answering paragraph 11 of the Complaint, Blockbuster repeats
14 its foregoing responses to paragraphs 1 through 10.

15 12. Answering paragraph 12 of the Complaint, Blockbuster admits
16 that Netflix is listed on the '450 patent as its assignee; that the number, title, and
17 issuance date of the patent are as stated in paragraph 12; and that a copy of the '450
18 patent was attached as Exhibit B to the copy of the Complaint served on
19 Blockbuster. Blockbuster lacks knowledge or information sufficient to form a
20 belief as to the truth of the allegation that Netflix is the "sole and exclusive owner"
21 of the '450 patent and, on that basis, Blockbuster denies that allegation. Answering
22 the remainder of paragraph 12, Blockbuster admits and alleges that the scope of
23 each of the numbered claims of the '450 patent is as stated in those respective
24 claims, and Blockbuster denies that paragraph 12 accurately sets forth the scope of
25 the patent. Except as expressly admitted and denied, Blockbuster generally and
26 specifically denies the allegations thereof.

27 13. Answering paragraph 13, Blockbuster denies generally and
28 specifically the allegations thereof. Without limiting the generality of the foregoing

1 denial, Blockbuster denies that it has violated 35 U.S.C. § 271(a) and denies that it
2 has infringed any rights of Netflix under the '450 patent, whether under § 271(a) or
3 any other provision of the patent laws.

4 14. Answering paragraph 14, Blockbuster denies generally and
5 specifically the allegations thereof. Without limiting the generality of the foregoing
6 denial, Blockbuster denies that it has violated 35 U.S.C. § 271(b) or (c) and denies
7 that it has infringed any rights of Netflix under the '450 patent, whether under
8 § 271(b), § 271(c), or any other provision of the patent laws.

9 15. Answering paragraph 15, Blockbuster admits that it knew of the
10 '450 patent before Netflix commenced this case. Except as expressly admitted and
11 denied, Blockbuster generally and specifically denies the allegations of
12 paragraph 15. Without limiting the generality of the foregoing denial, Blockbuster
13 further denies that it has infringed or is infringing the '450 patent, whether
14 willfully, deliberately, or in any manner whatsoever; denies that Netflix has
15 suffered or will suffer any injury whatsoever – whether irreparable or otherwise –
16 due to any infringement by Blockbuster; and denies that Netflix is entitled to an
17 injunction or to any other relief, order, or judgment against Blockbuster
18 whatsoever.

19 **ALLEGATIONS COMMON TO BLOCKBUSTER'S AFFIRMATIVE**
20 **DEFENSES AND COUNTERCLAIMS**

21 **BACKGROUND**

22 16. In its Complaint, Netflix alleges that Blockbuster's online DVD
23 rental service infringes two U.S. patents, Nos. 6,584,450 (the '450 patent)
24 and 7,024,381 (the '381 patent). Blockbuster denies Netflix's allegations of
25 infringement, as set forth herein. In addition, Blockbuster sets forth affirmative
26 defenses that both the '450 patent and the '381 patent are invalid and unenforceable
27 and that Netflix's Complaint is barred by patent misuse, laches, and estoppel.
28 Blockbuster also counterclaims against Netflix, under federal antitrust laws, for

1 monopolizing and attempting to monopolize the DVD rental market through
2 fraudulent patenting and sham litigation. Additionally, Blockbuster counterclaims
3 for a Court judgment declaring that Blockbuster has not violated any patent rights
4 of Netflix.

5 17. The patents asserted by Netflix fail to describe any technology
6 that was not already widely known and in general use well before any purported
7 inventions of Netflix. Instead, the patents merely describe use of existing
8 technology to practice business methods for renting movies and other items to
9 customers. The business of renting movies, as well as renting other items, was
10 widely known long before any purported invention by Netflix. So was renting on a
11 subscription basis. From at least the mid-1990s, it was obvious to adapt “brick-
12 and-mortar” businesses to the Internet – as Netflix did with Blockbuster’s highly
13 popular movie rental business. The advent of the DVD format in the late 1990s
14 provided the opportunity to send and receive video disks by mail at a far lower cost
15 than VHS videotapes, which increased the economic feasibility of renting movies
16 over the Internet. Netflix merely exploited an obvious market opportunity created
17 by developments in Internet and DVD technology, which had been entirely the
18 work of others. Netflix is not entitled to monopolize the resulting opportunities to
19 rent DVDs over the Internet.

20 18. The ’450 patent asserted by Netflix is particularly broad and is
21 not even limited to DVD or movie rental. It purports to cover stated methods for
22 renting any and all “items” whatsoever. Nor are the ’450 patent claims limited to
23 online rentals. They could cover in-store rentals having nothing to do with the
24 Internet.

25 19. While the claims of the later ’381 patent require rental of
26 “movies” and use of the Internet, along with other limitations, they too are directed
27 to rental business methods and, like the claims of the ’450 patent, are overbroad and
28 invalid, as set forth below.

1 20. Various claims of the '450 and '381 patents recite additional
2 features related to subscription rental and to implementing online subscription –
3 such as a “queue” of desired items. However, none of the claims is properly
4 patentable in view of the business methods that others had already used before
5 Netflix and the teachings of publications, products, and patents that predated
6 Netflix’s purported inventions (all as defined in 35 U.S.C. § 102 and collectively
7 referred to as “prior art”). Blockbuster is informed and believes and thereon alleges
8 that the '450 and '381 patents mostly or entirely claim subject matter that was
9 already known and used by others before Netflix. Such “anticipation” by prior art
10 renders some or all of Netflix’s patent claims invalid because they lack the novelty
11 required by 35 U.S.C. § 102. Blockbuster is informed and believes and thereon
12 alleges that the patent claims are also invalid because the matter claimed was
13 obvious under 35 U.S.C. § 103, as well as for other reasons alleged below.

14 21. Blockbuster is in the process of identifying and locating prior art
15 that illustrates and contributes to the invalidity of the patents asserted by Netflix.
16 Examples include:

17 a. Prior art subscription methods, systems, and publications,
18 ranging from libraries for the blind and other subscription libraries to cable
19 and satellite television services and pay television services such as HBO and
20 Showtime, as well as TiVo and other video and film subscription services;

21 b. Prior art video rental stores and related methods, systems,
22 and publications, including long-standing and widely-known practices in the
23 video rental industry, such as the use of waiting or reservation lists for out-of-
24 stock videos;

25 c. Prior art video rental on a subscription basis with no due
26 dates and no late fees, as well as related methods, systems, and publications;

27 d. Prior art audio rental stores and services and related
28 methods, systems, and publications, including audio rental on a subscription

1 basis and the use of an ordered list – in other words, a “queue” – of items
2 desired for subscription rental;

3 e. Prior art e-commerce businesses and related methods,
4 systems, and publications, including prior art related to the digital display,
5 selection, and ordering of items over the Internet;

6 f. Prior art patents on the foregoing and on other material
7 subjects, including, for example, U.S. Patent No. 5,699,526 (the '526 patent),
8 assigned to NCR Corporation, entitled “Ordering and Downloading
9 Resources from Computerized Repositories,” and issued on December 16,
10 1997, which disclosed, among other things, online search and retrieval based
11 on item attributes in digital form and permitting a customer to establish an
12 “interest list” of desired items; and

13 g. Blockbuster’s own prior art U.S. Patent No. 5,459,306,
14 entitled “Method and System for Delivering On Demand, Individually
15 Targeted Promotions,” and issued on October 17, 1995. This prior art patent
16 disclosed, among other things, computer-implemented automatic selection of
17 movies for potential rental to individual customers.

18 22. As is detailed below, Netflix obtained the '450 and '381 patents
19 without disclosing to the Patent Office prior art that Netflix knew about and that
20 was material to Netflix’s patent applications. Blockbuster is informed and believes
21 and thereon alleges that, by failing to disclose such prior art, Netflix violated its
22 duty of “candor and good faith” to the Patent Office (as explained further below)
23 and that, as a result, the '450 and '381 patents are not only invalid but also
24 unenforceable based on inequitable conduct.

25 **HISTORY OF NETFLIX’S PATENTS**

26 23. Netflix applied for the '450 patent on April 28, 2000. The
27 application for the '450 patent was designated by Serial No. 09/561,041 and was
28 filed in the names of W. Reed Hastings, Marc B. Randolph, and Neil Duncan Hunt

1 (collectively, the “Named Inventors”).

2 24. One of the Named Inventors, Reed Hastings, is the Chief
3 Executive Officer and President of Netflix, another, Marc Randolph, is former CEO
4 and President of Netflix or its predecessor entity, and the third, Neil Duncan Hunt,
5 is Netflix’s Chief Product Officer.

6 25. The ’450 patent was issued on June 24, 2003. The patent
7 purports to broadly cover stated methods for rental of any “items” as alleged above.
8 Blockbuster is informed and believes and thereon alleges that the ’450 patent is
9 blatantly over-broad, anticipated, obvious, and otherwise invalid, as well as
10 unenforceable, as is described in detail below.

11 26. Blockbuster began publicly operating its online video rental
12 service (“Blockbuster Online”) in August 2004. Although Netflix was well aware
13 of Blockbuster Online from that time forward, and was aware that Blockbuster was
14 investing millions of dollars developing and promoting Blockbuster Online, Netflix
15 did not assert the ’450 patent against Blockbuster at that time or for the next
16 eighteen months. Throughout that time and up through the date on which it filed
17 this lawsuit, Netflix provided no notice or warning to Blockbuster that Netflix
18 believed Blockbuster was infringing the ’450 patent. Blockbuster is informed and
19 believes and thereon alleges that Netflix also failed to assert any infringement
20 claims during this time against any other companies then operating online DVD
21 rental business, such as Wal-Mart.

22 27. Unbeknownst to Blockbuster and to the public at large, Netflix
23 had applied for the ’381 patent on May 14, 2003, some five weeks before the ’450
24 patent was issued. Netflix filed the application for the ’381 patent, Serial
25 No. 10/438,727, in the names of the Named Inventors, as a purported and sham
26 “continuation” of the application for the ’450 patent.

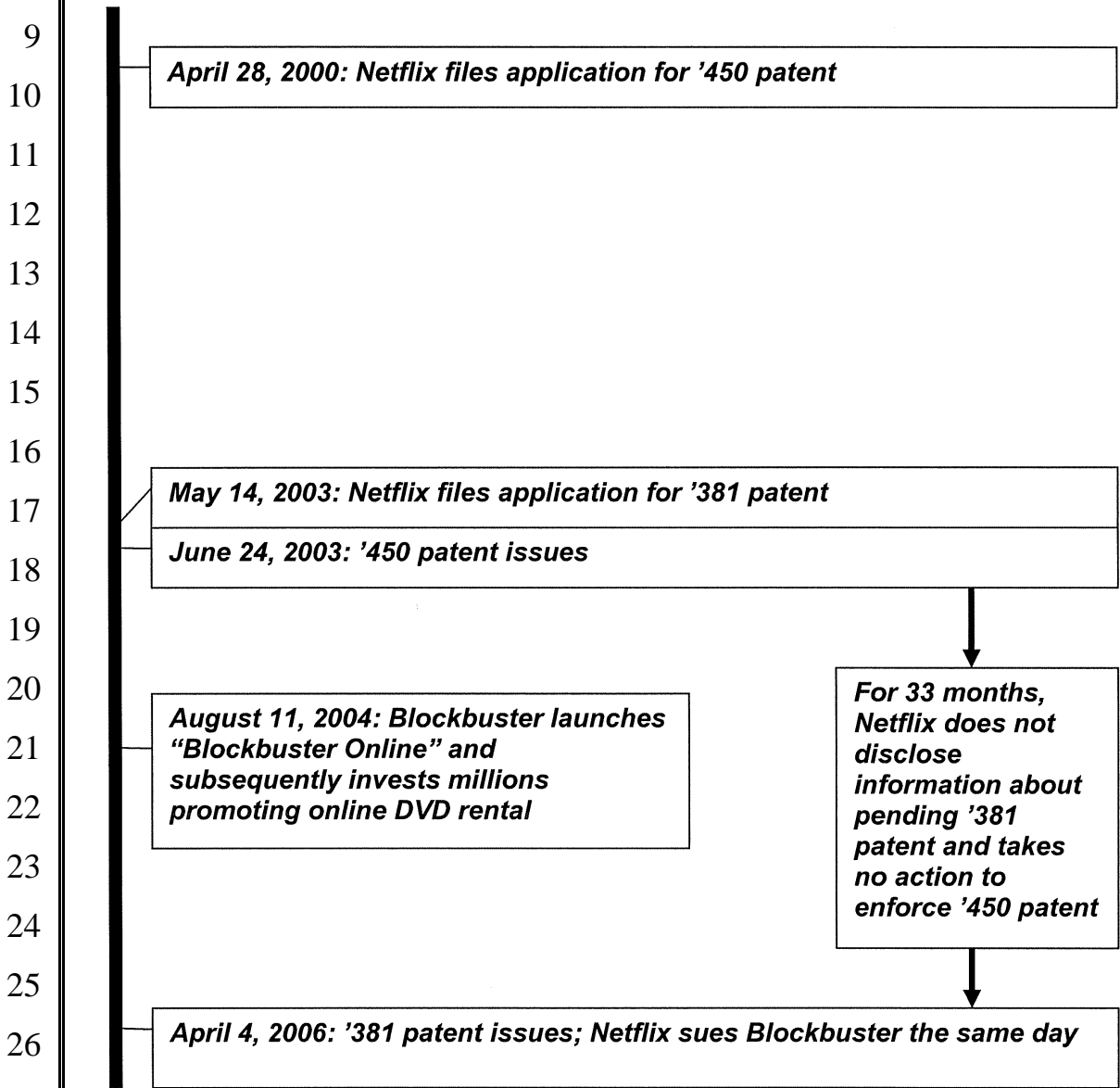
27 28. Information about the second application was not available to
28 Blockbuster or the public at large until April 4, 2006. It was on that date that the

1 '381 patent was issued and this very lawsuit was filed.

2 29. Blockbuster is informed and believes and thereon alleges that
3 the '381 patent, like the '450 patent, is invalid and unenforceable for the reasons
4 alleged below.

5 30. The following timeline illustrates key events described above:

6
7 **Time Line: Applications for and Issuance of**
8 **the '450 and '381 Patents**



#

NETFLIX’S DUTY OF CANDOR TO THE PATENT OFFICE

1
2
3 31. Netflix’s officers, employees, attorneys, assignors, and agents
4 involved for applying for and obtaining the ’450 and ’381 patents (collectively,
5 “Netflix’s Applicants and Representatives”) owed a legal and ethical “duty of
6 candor and good faith” to the Patent Office under the decisional law of the United
7 States and the regulations and procedures of the Patent Office, including 37 C.F.R.
8 § 1.56(a).

9 32. This “duty of candor and good faith” extended to all
10 “[i]ndividuals associated with the filing and prosecution of” the patent applications
11 that resulted in the ’450 and 381 patents,” 37 C.F.R. § 1.56(a), including, as to each
12 application:

- 13 “(1) Each inventor named in the application;
14 (2) Each attorney or agent who prepare[d] or
15 prosecute[d] the application; [and]
16 (3) Every other person who [was] substantively involved
17 in the preparation or prosecution of the application and
18 who [was] associated with the inventor, with the
19 assignee or with anyone to whom there [was] an
20 obligation to assign the application.”

21 37 C.F.R. § 1.56(c).

22 33. Netflix’s Applicants and Representatives who were under a duty
23 of candor and good faith to the Patent Office in applying for and obtaining the ’450
24 and 381 patents included the Named Inventors, the patent attorneys acting on behalf
25 of the Named Inventors and Netflix in applying for and prosecuting the applications
26 (the “Patent Attorneys”).

27 34. The duty of candor and good faith owed by Netflix’s Applicants
28 and Representatives’ included a continuing obligation, at all times during the

1 pendency of either of the applications for the '450 and '381 patents, to disclose to
2 the Patent Office all prior art known to be material to a pending application.

3 35. Netflix's Applicants and Representatives submitted a
4 declaration and power of attorney (the "Declaration") to the Patent Office in
5 support of both the application for the '450 patent and the application for the '381
6 patent. The Declaration states that it was signed by Named Inventor W. Reed
7 Hastings on September 28, 2000, by Neil Duncan Hunt on September 29, 2000, and
8 by Marc B. Randolph on October 3, 2000.

9 36. In the Declaration, each of the Named Inventors expressly
10 "acknowledge[d] the duty to disclose information which is known to me to be
11 material to patentability in accordance with Title 37, Code of Federal Regulations,
12 Section 1.56."

13 37. Each Named Inventor also stated in the Declaration:

14 "I hereby declare that all statements made herein of my
15 own knowledge are true and that all statements made on
16 information and belief are believed to be true; and
17 further that these statements were made with the
18 knowledge that willful false statements and the like so
19 made are punishable by fine or imprisonment, or both,
20 under Section 1001 of Title 18 of the United States Code
21 and that such willful false statements may jeopardize the
22 validity of the application or any patent issued thereon."

23 **NETFLIX'S VIOLATIONS OF THE DUTY OF CANDOR**

24 38. Blockbuster is informed and believes and thereon alleges that
25 Netflix's Applicants and Representatives violated their legal and ethical duties of
26 candor and good faith in applying for, prosecuting applications for, and obtaining
27 the '450 and '381 patents, by engaging in inequitable and deceptive conduct as
28 alleged below.

1 39. Blockbuster is informed and believes and thereon alleges that
2 Netflix obtained the '450 and '381 patents by means of a scheme in which some or
3 all of Netflix's Applicants and Representatives manipulated and distorted the patent
4 process by inequitable conduct including:

5 a. Obtaining an absurdly broad and invalid patent (the '450
6 patent) without proper and meaningful examination by concealing and failing
7 to disclose any prior art before the '450 patent was issued, in violation of the
8 duty of candor that was owed by Netflix's Applicants and Representatives
9 and that the Named Inventors had acknowledged under penalty of perjury;

10 b. Failing to disclose any prior art in applying for and
11 obtaining the '450 patent, despite being aware of multiple items of prior art,
12 as alleged below, and despite their acknowledged and well-established duty
13 to disclose all known material prior art to the Patent Office;

14 c. Prior to the issuance of the '450 patent, filing a
15 "continuation" patent application to pursue claims narrower than – and
16 therefore possibly more defensible in litigation than – the blatantly over-
17 broad claims of the '450 patent, although still broader than permitted under
18 the patent laws;

19 d. During the pendency of the continuation application
20 (which resulted in the '381 patent), flooding the Patent Office with such a
21 large volume of prior art or possible prior art (more than 100 references) that
22 the examiners would be overwhelmed and overtaxed in their attempt to
23 examine the application;

24 e. Under cover of its belatedly large submissions, still
25 withholding certain known and material prior art throughout the pendency of
26 the application for the '381 patent, as alleged below;

27 f. Withholding information about the continuation
28 application from the public and from competitors until issuance of the '381

1 patent;

2 g. Foregoing assertion or enforcement of the '450 patent
3 pending issuance of the '381 patent despite actual knowledge of competitive
4 online DVD rental businesses, including Blockbuster Online;

5 h. Deceptively lulling and enticing competitors, including
6 Blockbuster, into entering into and remaining in the online DVD rental
7 market after they reviewed the '450 patent and reasonably concluded that
8 Netflix lacked any valid and enforceable patent rights that would prevent
9 their entry into the market;

10 i. Benefiting from the promotion of the online DVD rental
11 market by Blockbuster and other competitors and their creation of an
12 expanded group of customers interested in or accustomed to renting DVDs
13 online; and

14 j. On the very day that the '381 patent was issued, suing
15 Blockbuster, without warning, for alleged infringement of both the '381 and
16 '450 patents.

17 40. In January 2005, Netflix CEO and Named Inventor Reed
18 Hastings met with Blockbuster's then-Executive Vice President and General
19 Counsel, Edward Stead. Hastings praised Blockbuster's competitive position in the
20 online rental business and asked Stead when he had figured out that Netflix's '450
21 patent was a "joke."

22 41. It was only after having wrongfully obtained issuance of the
23 '450 patent that Netflix's Applicants and Representatives began submitting prior art
24 to the Patent Office in connection with the application for the '381 patent.
25 Ultimately, Netflix's Applicants and Representatives submitted more than 100
26 references to prior art or possible prior art in connection with the '381 patent
27 application. Netflix's Applicants and Representatives disclosed none of these
28 references in obtaining the '450 patent, even though at least 100 of them predated

1 that patent and therefore could have been submitted in connection with it.

2 42. Even after having submitted more than 100 prior art references
3 to the Patent Office, Netflix's Applicants and Representatives withheld and failed
4 to disclose other material prior art that they knew about, as alleged below.

5 43. Blockbuster is informed and believes and thereon alleges that, in
6 engaging in all their conduct alleged herein, the Applicants and Representatives
7 were acting on behalf of Netflix and that Netflix directed, controlled, and ratified
8 their conduct.

9 **PRIOR ART CONCEALED BY NETFLIX**

10 44. In addition to failing to disclose any of more than 100 prior art
11 references described above during the pendency of the '450 patent application,
12 Netflix's Applicants and Representatives knew about other prior art but failed to
13 disclose it to the Patent Office in connection with either of the two patent
14 applications. Such prior art included some or all of the following:

15 a. Certain prior art United States patents purportedly owned
16 by NCR Corporation (the "NCR Patents"), which Netflix knew about while
17 both the application for the '450 patent and the application for the '381 patent
18 were pending, but which Netflix never submitted to the Patent Office;

19 b. Certain prior art video rental stores and related methods,
20 systems, and publications, including long-standing and widely-known
21 practices in the video rental industry, such as the use of waiting or reservation
22 lists for out-of-stock videos;

23 c. Certain prior art subscription methods, systems, and
24 publications, including cable and satellite television services and pay
25 television services such as HBO and Showtime, as well as TiVo and other
26 video and film subscription services; and

27 d. Certain prior art e-commerce businesses and related
28 methods, systems, and publications, including prior art related to the digital

1 display, selection, and ordering of items over Internet.

2 45. The NCR Patents include, without limitation:

3 a. The '526 patent, entitled "Ordering and Downloading
4 Resources from Computerized Repositories," which names as inventor David
5 M. Siefert, issued December 16, 1997, on an application filed August 21,
6 1996;

7 b. U.S. Patent No. 5,951,643 (the '643 patent), entitled
8 "Mechanism for Dependably Organizing and Managing Information for Web
9 Synchronization and Tracking Among Multiple Browsers," which names as
10 inventors James A. Shelton, Michael I. Ingrassia, Jr., and Thomas M. Roland,
11 issued September 14, 1999, on an application filed October 6, 1997;

12 c. U.S. Patent No. 5,991,791 (the '791 patent), entitled
13 "Security Aspects of Computer Resource Repositories," which names as
14 inventor David M. Siefert, issued November 23, 1999, on an application filed
15 January 10, 1997;

16 d. U.S. Patent No. 6,026,403 (the '403 patent), entitled
17 "Computer System for Management of Resources," which names as inventor
18 David M. Siefert, issued February 15, 2000, on an application filed
19 March 24, 1994;

20 e. U.S. Patent No. 6,169,997 (the '997 patent), entitled
21 "Method and Apparatus for Forming Subject (Context) Map and Presenting
22 Internet Data According to the Subject Map," which names as inventors
23 Karen A. Papierniak, James E. Thaisz, Luo-Jen Chiang, and Paresh B. Shah,
24 issued January 2, 2001, on an application filed April 29, 1998;

25 f. U.S. Patent No. 6,253,203 (the '203 patent), entitled
26 "Privacy-Enhanced Database," which names as inventors Kenneth W.
27 O'Flaherty, Richard G. Stellwagen, Jr., Todd A. Walter, Reid M. Watts,
28 David A Ramsey, Adriaan W. Veldhuisen and Renda K. Ozden, issued

1 June 26, 2001, on an application filed October 2, 1998;

2 g. U.S. Patent No. 6,480,855 (the '855 patent), entitled
3 "Managing a Resource on a Network Where Each Resource Has an
4 Associated Profile with an Image," which names as inventor David M.
5 Siefert, issued November 12, 2002, on an application filed August 22, 2000;

6 h. U.S. Patent No. 6,502,096 (the '096 patent), entitled
7 "Computerized Asset Management System," which names as inventor David
8 M. Siefert, issued December 31, 2002, on an application filed August 22,
9 2000; and

10 i. U.S. Patent No. 6,714,931 (the '931 patent), entitled
11 "Method and Apparatus for Forming User Sessions and Presenting Internet
12 Data According to the User Sessions," which names as inventors Karen A.
13 Papierniak, James E. Thaisz, Luo-Jen Chiang, Anjali M. Diwekar, issued
14 March 30, 2004, on an application filed April 29, 1998.

15 46. The '526 patent is prior art to both the '450 and '381 patents
16 under 35 U.S.C. § 102(b). Blockbuster is informed and believes and thereon
17 alleges that the subject matter disclosed in each of the NCR Patents is prior art to
18 both the '450 and '381 patents under, without limitation, 35 U.S.C. § 102(a) and
19 (e).

20 47. Netflix's own admissions in a case pending in this Court,
21 *Netflix, Inc. v. NCR Corporation*, Case No. C 06 1892 ("*Netflix v. NCR*") show that
22 Netflix was well aware of the NCR Patents during the pendency and prosecution of
23 the applications for both the '450 and '381 patents. Netflix filed *Netflix v. NCR*, on
24 March 10, 2006, seeking a declaratory judgment with respect to the same NCR
25 Patents listed above. That complaint shows that, since on or about January 17,
26 2003, Named Inventor Reed Hastings, who is also the Chief Executive Officer and
27 President of Netflix, has been aware, not only that the prior art NCR Patents exist,
28 but also that NCR claims that they cover the very same online rental service

1 claimed in Netflix's patents.

2 48. Netflix's allegations in *Netflix v. NCR* include each of the
3 following admissions showing its knowledge of the NCR Patents:

4 a. "On January 7, 2003, Bruce A. Langos, Vice President of
5 Business Operations and Intellectual Property Management at NCR, wrote to
6 Reed Hastings, the Chief Executive Officer of Netflix claiming notice [sic]
7 'that various Netflix.com offerings infringe at least the following patents
8 owned by NCR Corporation.'" (*Netflix v. NCR Compl.*, ¶ 22.)

9 b. Mr. Langos's letter "identified ten separate patents that
10 NCR claimed were infringed, and enclosed several exemplary claim charts,
11 each of which accused Netflix of infringing the claims described therein."
12 (*Id.*) These ten patents evidently included the nine NCR Patents listed above,
13 which are identified in the paragraphs immediately preceding the above-
14 quoted paragraph of Netflix's complaint in *Netflix v. NCR*. (*Id.* ¶ 22; *see id.*
15 ¶¶ 12-21.)

16 c. NCR "even threatened to sue for an injunction should
17 Netflix not license NCR's technology" (*Id.* ¶ 22.)

18 d. "On August 1, 2005, Mr. Langos once again wrote to
19 Mr. Hastings of Netflix concerning '[Netflix's] infringements of NCR
20 patents . . .'" and, on this occasion, Mr. Langos "enclosed updated claim
21 charts that again accused Netflix of infringing the claims described therein,
22 and threatened that should Netflix refuse to license the technology NCR was
23 'prepared to pursue other options.'" (*Id.* ¶ 23.)

24 e. "NCR continued to press its allegations of infringement"
25 thereafter. (*Id.* ¶ 24.) NCR's counsel met with Netflix's counsel on
26 November 28, 2005, "during which meeting NCR's counsel once again
27 asserted that Netflix infringed the NCR patents, and that NCR was prepared
28 to file suit against Netflix to enforce its patents." (*Id.*)

1 f. “[O]n January 11, 2006, counsel for NCR sent via email
2 to San Francisco revised charts purporting to show that Netflix was currently
3 infringing the claims described therein.” (*Id.*)

4 49. Netflix’s own complaint in *Netflix v. NCR* shows that the letter
5 bringing the prior art NCR Patents to Netflix’s attention was addressed to Netflix
6 CEO and Named Inventor Reed Hastings more than six months before the ’450
7 patent issued. Although NCR expressly described its prior art patents as
8 encompassing the same online video rental service that Netflix was attempting to
9 patent, Netflix’s Applicants and Representatives failed to disclose any of the NCR
10 Patents to the Patent Office.

11 50. On March 10, 2006, prior to the issuance of the ’381 patent,
12 Netflix had even filed suit against NCR over the NCR Patents, alleging that, “[b]y
13 virtue of NCR’s actions, Netflix has a reasonable apprehension that NCR intends to
14 sue it for infringing the NCR patents” (*id.* ¶ 25) and that “[a]n actual and judicable
15 controversy exists between Netflix and NCR concerning whether Netflix infringes
16 any valid claim of the NCR patents.” (*Id.* ¶ 27.)

17 51. Despite all of these alleged communications and notices from
18 NCR about the NCR Patents, the ongoing controversy alleged by Netflix over the
19 NCR Patents, and Netflix’s expressed apprehension that it would be sued for
20 infringement of those patents, Netflix and its Applicants and Representatives failed
21 to disclose any of the NCR Patents to the Patent Office at any time up through and
22 including the date of issuance of the ’381 patent on April 4, 2006.

23 52. Regardless of whether the claims of the NCR Patents do in fact
24 cover online DVD rental services like those operated by Netflix and Blockbuster,
25 and regardless of whether those claims are legally valid, NCR’s assertion of its
26 patents against Netflix’s online rental service provided Netflix with ample notice
27 that the patents were material prior art and should be disclosed to the Patent Office
28 for its consideration in deciding whether Netflix’s then-pending applications for

1 patents on that service met the statutory requirements of novelty and
2 nonobviousness. Instead, even after Netflix had sued NCR over the issue of
3 whether the NCR Patents cover the same rental service Netflix was engaged in
4 patenting, Netflix and its Applicants and Representatives failed to submit the NCR
5 Patents to the Patent Office.

6 53. The NCR patents are replete with disclosures of features that are
7 the same as or similar to features Netflix has claimed in the '450 and '381 patents.
8 To provide only a few examples:

9 a. The '450 and '381 patents are directed to a computer-
10 implemented method and system for renting items – or sometimes, more
11 specifically, movies – to customers. Similarly, NCR's '526, '403, '791, '855,
12 and '096 patents disclose a computer-implemented method for distributing
13 items including movies and video tapes to customers. (*E.g.*, '526 patent, col.
14 2:55-57, 5:10-15 & Fig. 1B.) All nine NCR Patents disclose computer-
15 implemented methods and systems for online management and provision of
16 resources.

17 b. Ninety-five claims of the '450 patent include “receiving
18 one or more item selection criteria that indicates one or more items that a
19 customer desires to rent” ('450 patent, Claims 1-95.) NCR's '526,
20 '403, '791, '855, and '096 patents disclose use of item selection criteria – for
21 example, a “display [that] prompts the user to request a search based on three
22 criteria (or less).” (*E.g.*, '526 patent, col. 10:57-58 & Figs. 9-11.)

23 c. All fifty-one claims of the '381 patent include “providing
24 electronic digital information that causes one or more attributes of movies to
25 be displayed” The NCR patents disclose just such a process. Electronic
26 digital information is provided that allows resources (including movies) to be
27 selected. This causes display of “an associated PROFILE, which contains
28 descriptive information about the RESOURCE.” (*E.g.*, '526 patent,

1 col. 4:42-43.)

2 d. All claims of the '381 patent, and several claims of the
3 '450 patent, include an "item rental queue" or "movie rental queue"
4 containing items desired by a customer. ('381 patent, Claims 1-51; '450
5 patent, Claims 7, 22, 42, 57, 72, 87.) In the claims of the '381 patent, the
6 queue is "establish[ed] in electronic digital form, from electronic digital
7 information received over the Internet" ('381 patent, Claims 1, 14, 24,
8 34, 44.) NCR's '526, '791, '403, '855, and '096 patents all disclose a
9 process of establishing in electronic digital form, from electronic digital
10 information received over a computer network, a list associated with a
11 customer that indicates his or her interests in searching for resources. (*E.g.*,
12 '526 patent, col. 18:48-49.)

13 e. All independent claims of the '381 patent provide for
14 electronically updating a movie rental queue in response to electronic digital
15 information received from a customer over the Internet. ('381 patent,
16 Claims 1, 14, 24, 34, 44.) This ability to update the list is what apparently
17 makes it a so-called "dynamic queue" as touted by Netflix. (First Am.
18 Compl. ¶ 7.) Numerous claims of the '381 patent specifically recite updating
19 the queue by adding or deleting items. ('381 patent, Claims 3, 4, 16, 17, 26,
20 27, 36, 37, 46, 47.) Similarly, NCR's '526, '799, '403, '855, and '096
21 patents all disclose updating a customer's interest list via a computer
22 network, including the ability to "add or delete interests in your current
23 listing." (*E.g.*, '526 patent, col. 18:49-51.)

24 f. Claims of both the '450 and '381 patents include the step
25 of delivering items to a customer by mail or via a "delivery agent." ('450
26 patent, Claims 12, 13, 27, 28, 34, 35, 62, 64, 77, 78; '381 patent, Claims 7,
27 20, 30, 40, 48.) NCR's '526, '791, '403, '855, and '096 patents disclose
28 delivery of items electronically selected by a customer via an organization's

1 “internal mail service,” or a “public, common carrier” (*E.g.*, ’526
2 patent, col. 15:23-27.)

3 54. Blockbuster is informed and believes and thereon alleges that
4 the NCR Patents and all of the other prior art that Netflix’s Applicants and
5 Representatives knew about and failed to disclose to the Patent Office, as described
6 above, was material to both the ’450 and ’381 patents.

7 55. Blockbuster is informed and believes and thereon alleges that
8 the deceptive and inequitable conduct of Netflix and its Applicants and
9 Representatives as alleged herein occurred at locations including, without
10 limitation, Netflix’s principal place of business in Los Gatos, California, and the
11 offices of Netflix’s patent attorneys in San Jose, California, as well as being
12 reflected in, and implemented through, documents transmitted to the Patent Office
13 in Alexandria, Virginia.

14 56. Blockbuster is informed and believes and thereon alleges that
15 the deceptive and inequitable conduct of Netflix and its Applicants and
16 Representatives as alleged herein occurred at times including the entire period from
17 April 28, 2000 through June 24, 2003, during which the application for the ’450
18 patent was pending, and the entire period from May 14, 2003 through April 4,
19 2006, during which the application for the ’381 patent was pending.

20 **NETFLIX’S DECEPTIVE INTENT**

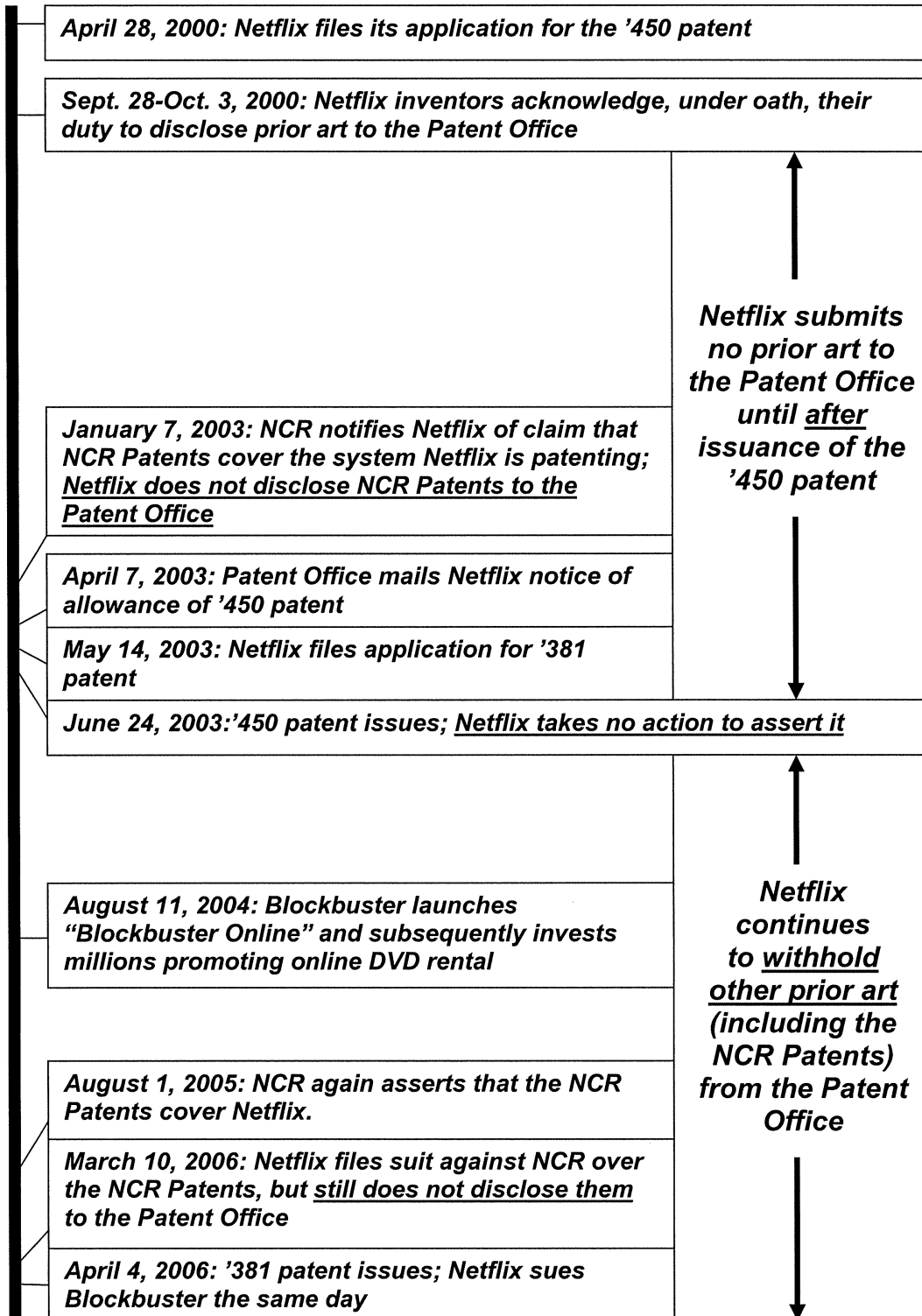
21 57. Blockbuster is informed and believes and thereon alleges that
22 Netflix’s Applicants and Representatives knew of the materiality of the prior art
23 that they failed to disclose to the Patent Office as alleges above.

24 58. Blockbuster is informed and believes and thereon alleges that, in
25 engaging in the deceptive and inequitable conduct alleged above, including their
26 failures to disclose material prior art, Netflix’s Applicants and Representatives
27 intended to deceive the Patent Office.

28 59. The conduct demonstrating such deceptive intent has included,

1 without limitation, the acts and omissions by Netflix’s Applicants and
 2 Representatives as alleged above and as illustrated by the following time line:

3 **Time Line: Illustrative Circumstances**
 4 **of Netflix’s Deceptive Intent**



**BLOCKBUSTER’S AFFIRMATIVE DEFENSES TO NETFLIX’S
COMPLAINT**

FIRST AFFIRMATIVE DEFENSE

(Invalidity)

60. Blockbuster repeats all allegations of paragraphs 16 through 59 above.

61. Either or both of the '450 and '381 patents are invalid for failure to satisfy one or more of the conditions of Title 35 of the United States Code, including, without limitation, Sections 101, 102, 103, and 112 thereof.

62. The reasons for the invalidity of the patents include that they claim subject matter that was and is unpatentable because it had already been conceived of by others, was already publicly known, and was otherwise within one or more of the categories of prior art established by 35 U.S.C. § 102.

63. The reasons for the invalidity of the patents also include that they claim subject matter that was and is unpatentable because it was obvious under 35 U.S.C. § 103.

64. Blockbuster is informed and believes and thereon alleges that either or both of the '450 and '381 patents fail to set forth what the inventors regarded as the best mode for practicing the claimed inventions, in violation of 35 U.S.C. § 112, and fail to fulfill the written description requirement of §112.

65. Blockbuster is informed and believes and thereon alleges that, depending on the constructions of the claims of the '450 and '381 patents as ultimately determined in this litigation, some or all of those claims may also fail to fulfill the definiteness requirement of 35 U.S.C. § 112.

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SECOND AFFIRMATIVE DEFENSE

(Unenforceability)

66. Blockbuster repeats all allegations of paragraphs 16 through 59 above and of Blockbuster’s First and Second Counterclaims below.

67. Blockbuster is informed and believes and thereon alleges that the ’450 and ’381 patents are unenforceable because of inequitable conduct in obtaining the patents. Blockbuster’s grounds for this defense include, without limitation, the failure of Netflix’s Applicants and Representatives to disclose material prior art as alleged above.

68. A reasonable examiner would have been substantially likely to consider the prior art that Netflix knew about but failed to disclose important in deciding whether to allow the applications for the ’450 and ’381 patents (including amendments to those applications) to issue as patents.

69. Blockbuster is informed and believes and thereon alleges that, in failing to disclose material prior art, Netflix’s Applicants and Representatives knew of the prior art and knew of its materiality to either or both of the applications for the ’450 patent and the ’381 patent.

70. Blockbuster is informed and believes and thereon alleges that, in failing to disclose material prior art, Netflix’s Applicants and Representatives intended to deceive the Patent Office.

THIRD AFFIRMATIVE DEFENSE

(Patent Misuse)

71. Blockbuster repeats all allegations of paragraphs 16 through 59 above and of Blockbuster’s First and Second Counterclaims below.

72. Blockbuster is informed and believes and thereon alleges that Netflix has misused each of the ’450 and ’381 patents and, as a result, is barred from asserting either of them against Blockbuster.

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FOURTH AFFIRMATIVE DEFENSE

(Laches)

73. Blockbuster repeats all allegations of paragraphs 16 through 59 above and of Blockbuster’s First and Second Counterclaims below.

74. Netflix has unreasonably and inexcusably delayed its assertion of the ’450 patent against Blockbuster, causing material prejudice to Blockbuster. Such prejudice has included Blockbuster’s expenditure of millions of dollars on its Blockbuster Online system.

75. As a result of its delay in asserting the ’450 patent, Netflix is barred from asserting some or all of its claims against Blockbuster and from obtaining any of the relief that it has requested.

76. Blockbuster is informed and believes and thereon alleges that Netflix unreasonably and inexcusably delayed its filing and prosecution of a patent application for the subject matter claimed in the ’381 patent, as part of the deceptive and manipulative scheme alleged above and that Netflix’s unreasonable and unexplained delay constituted an egregious misuse of the patent system.

77. Netflix’s delay in filing and prosecuting a patent application for the subject matter claimed in the ’381 patent has caused material prejudice to Blockbuster including Blockbuster’s expenditure of millions of dollars on its Blockbuster Online system without notice of Netflix’s claims to such subject matter or an opportunity to contest such claims. As a result of this delay, Netflix is barred from asserting some or all of its claims against Blockbuster and from obtaining any of the relief that it has requested.

FIFTH AFFIRMATIVE DEFENSE

(Estoppel)

78. Blockbuster repeats all allegations of paragraphs 16 through 59 and 74 through 77 above and of Blockbuster’s First and Second Counterclaims below.

1 79. Blockbuster is informed and believes and thereon alleges that
2 Netflix is estopped by its conduct alleged herein from asserting some or all of its
3 claims against Blockbuster and from obtaining any of the relief that it has
4 requested. Such conduct includes Netflix's deceptive and manipulative scheme
5 alleged above and the statement by Netflix's CEO to Blockbuster's Executive Vice
6 President as alleged above.

7 80. By its conduct alleged herein, Netflix led Blockbuster to
8 reasonably infer that Netflix did not intend to enforce the '450 patent or any related
9 patent against Blockbuster. Blockbuster reasonably relied on Netflix's conduct in,
10 without limitation, expending millions of dollars on its Blockbuster Online system
11 without notice of Netflix's claims to such subject matter or an opportunity to
12 contest such claims. As a result, Blockbuster would be materially prejudiced by
13 enforcement of Netflix's patents against it.

14 **COUNTERCLAIMS**

15 Blockbuster, for its counterclaims against Netflix, alleges and avers as
16 follows:

17 **JURISDICTION**

18 81. Blockbuster's First and Second Counterclaims assert
19 monopolization and attempted monopolization by Netflix in violation of federal
20 antitrust laws, including Section 2 of the Sherman Antitrust Act, 15 U.S.C. § 2.
21 Blockbuster seeks injunctive, monetary, and equitable relief under Sections 15 and
22 16 of the Clayton Act, 15 U.S.C. §§ 25-26.

23 82. Blockbuster brings its Third and Fourth Counterclaims under the
24 Federal Declaratory Judgment Act, 28 U.S.C. §§ 2201-02, seeking declaratory
25 judgments under the patent laws of the United States, United States Code Title 35,
26 that Blockbuster has not violated and is not violating patent rights of Netflix and
27 that the '450 and '381 patents asserted by Netflix are invalid and unenforceable.

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83. This Court has jurisdiction over the Counterclaims under 28 U.S.C. §§ 1331 and 1337(a) and 15 U.S.C. § 26.

VENUE

84. This Judicial District is a proper venue for adjudication of the counterclaims under 15 U.S.C. § 22 and 28 U.S.C. § 1391(b) because Netflix transacts business, is found, and has agents in this District and because a substantial portion of the affected trade and commerce described below has been carried out in this District.

INTRADISTRICT ASSIGNMENT

85. This is an Intellectual Property Action subject to district-wide assignment under Civil Local Rule 3-2(c).

THE PARTIES

86. Blockbuster is a Delaware corporation with its principal place of business in Dallas, Texas. Blockbuster is duly registered and authorized to conduct business in the State of California. Blockbuster owns and operates an online DVD rental service known as “Blockbuster Online,” which is accessible from Blockbuster’s website, www.blockbuster.com. Blockbuster Online rents DVDs on a subscription basis to customers throughout the United States.

87. Netflix is a Delaware corporation with its principal place of business in Los Gatos, California. Netflix owns and operates a DVD rental business through its website, www.netflix.com, renting DVDs on a subscription basis to customers throughout the United States.

INTERSTATE COMMERCE

88. Netflix has substantially affected interstate commerce by illegally monopolizing, and attempting to monopolize, the relevant market, as alleged below.

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1 89. Throughout the period from at least April 28, 2000, through the
2 present (the “relevant time period”):

3 a. Netflix rented and distributed substantial numbers of
4 DVDs in a continuous and uninterrupted flow of commerce across state lines
5 and throughout the United States;

6 b. Netflix distributed rental DVDs and received returns of
7 rental DVDs across state lines and through the United States mails;

8 c. Netflix solicited and entered into DVD rental contracts,
9 obtained DVD rental orders, received payments for DVD rentals, and
10 promoted its online DVD rental service over the Internet, across state lines,
11 and using interstate telephone lines; and

12 d. Netflix employed the Internet, interstate telephone lines,
13 and the United States mails in furtherance of its monopolization and attempt
14 to monopolize the relevant market, as alleged below.

15 **RELEVANT MARKET**

16 90. The relevant product market with respect to Blockbuster’s First
17 and Second Counterclaims is the market for online DVD rentals and related
18 subscription services. The relevant geographical market is the United States and its
19 territories as a whole.

20 91. Blockbuster is informed and believes and thereon alleges that,
21 throughout the relevant time period up to and including the present, Netflix has had
22 market power in the relevant product and geographical markets.

23 92. Blockbuster is informed and believes and thereon alleges that
24 Netflix’s share of the relevant product and geographical markets exceeds 65%.

25 93. Following Blockbuster Online’s entry into the relevant product
26 and geographical markets, Netflix lowered its online DVD rental prices.

27 Blockbuster is informed and believes and thereon alleges that Netflix’s price
28 reduction was in response to Blockbuster Online’s own prices, which were lower

1 than Netflix's prices. Blockbuster is informed and believes and thereon alleges
2 that, should Netflix succeed in inducing Blockbuster Online to exit the relevant
3 market, Netflix would again be without significant competition in that market.

4 **FIRST COUNTERCLAIM**

5 **(Monopolization in Violation of Section 2 of the Sherman Antitrust Act)**

6 94. Blockbuster repeats all allegations of paragraphs 16 through 93
7 above.

8 95. Blockbuster is informed and believes and thereon alleges that
9 Netflix has engaged in monopolization in the relevant market during the relevant
10 time period, in violation of Section 2 of the Sherman Antitrust Act. Blockbuster is
11 informed and believes and thereon alleges that Netflix's acts of unlawful
12 monopolization have included procuring either or both of the '450 and '381 patents
13 by knowing and willful fraud and baselessly asserting them in bad faith in sham
14 litigation against Blockbuster.

15 96. Blockbuster is informed and believes and thereon alleges that
16 the knowing and willful fraud by Netflix and its Applicants and Representatives in
17 procuring the '450 and '381 patents has included all of their deceitful conduct
18 alleged above, including:

19 a. The Named Inventors' representations to the Patent
20 Office in applying for the '450 and '381 patents that the Named Inventors
21 were aware of their duty to disclose known material prior art, implicitly also
22 representing that they had complied with or would comply with this duty;

23 b. The intentional and fraudulent concealment from the
24 Patent Office by Netflix's Applicants and Representatives that, despite their
25 well-established and acknowledged duty of candor and good faith, they had
26 no intention of disclosing, and had not disclosed, all known material prior art;

27 c. The intentional and fraudulent concealment from the
28 Patent Office by Netflix's Applicants and Representatives of known, material

1 prior art, as alleged above; and

2 d. Their intentional and fraudulent concealment from the
3 Patent Office of the deceptive scheme in which they were engaged in
4 applying for and obtaining the '450 and '381 patents, as alleged above.

5 97. Blockbuster is informed and believes and thereon alleges that
6 Netflix and its Applicants and Representatives, in applying for the '450 patent and
7 at all times thereafter through the issuance of the '381 patent, intentionally,
8 fraudulently and materially deceived the Patent Office in knowing violation of their
9 legal and ethical duties of candor and good faith to the Patent Office as alleged
10 above.

11 98. For example, despite the Named Inventors' express
12 acknowledgment of their obligation to disclose material prior art, they disclosed no
13 prior art whatsoever to the Patent Office during the pendency of the application for
14 the '450 patent.

15 99. Having obtained issuance of the '450 patent, Netflix's
16 Applicants and Representatives thereafter began submitting prior art to the Patent
17 Office in connection with the application for the '381 patent and ultimately
18 submitted a total of more than 100 references. Blockbuster is informed and
19 believes and thereon alleges that Netflix's Applicants and Representatives
20 submitted this plethora of prior art or purported prior art for the purpose and with
21 the intention of confusing, distracting, misleading, and overtaxing the Patent Office
22 personnel charged with examining the application for the '381 patent.

23 100. Throughout the pendency of the application for the '381 patent,
24 even after having submitted more than 100 prior art references to the Patent Office,
25 Netflix's Applicants and Representatives from the Office withheld other material
26 prior art that they knew about, as alleged above.

27 101. Blockbuster is informed and believes and thereon alleges that, in
28 making and submitting the declarations and representations referred to above, and

1 in concealing and failing to disclose the material prior art and other material facts
2 referred to above, Netflix's Applicants and Representatives intended to deceive the
3 Patent Office and intended, by such fraud and deception, to obtain a patent to which
4 they were not otherwise entitled. In the alternative, Blockbuster is informed and
5 believes and thereon alleges that Netflix's Applicants and Representatives
6 intentionally disregarded their obligations to the Patent Office with a state of mind
7 so reckless with respect to the consequences of their conduct that it was the legal
8 equivalent of expressly fraudulent intent.

9 102. Blockbuster is informed and believes and thereon alleges that, in
10 issuing the '450 and '381 patents, the Patent Office justifiably relied on the
11 foregoing misrepresentations, concealment, and omissions of material prior art and
12 other material facts by Netflix's Applicants and Representatives and that the Office
13 would not otherwise have issued those patents.

14 103. Blockbuster is informed and believes and thereon alleges that
15 Netflix knows of the fraudulent origin, invalidity, and unenforceability of the '450
16 and '381 patents and that, in asserting the patents against Blockbuster – as well as
17 in any other past, present or future attempts to enforce the patents – Netflix has
18 been, is, and will be acting with full knowledge of the patents' fraudulent origin,
19 invalidity, and unenforceability.

20 104. Blockbuster is informed and believes and thereon alleges that
21 Netflix's infringement lawsuit against Blockbuster is a sham and is both objectively
22 and subjectively baseless for reasons including the suit's lack of any reasonable
23 merit, and Netflix's lack of any probable cause for bringing it, in view of, without
24 limitation, the clear invalidity and unenforceability of the patents as alleged above,
25 all of which is known to Netflix.

26 105. Blockbuster is informed and believes and thereon alleges that
27 Netflix, in filing this lawsuit, in prosecuting this lawsuit up to the present date, and
28 in any and all prosecution of this lawsuit hereafter, has acted, is acting, and will be

1 acting in bad faith, as a mere sham, and without belief in the merits of its claims.
2 Blockbuster is informed and believes and thereon alleges that Netflix, has been, is,
3 and, in any and all prosecution of this lawsuit hereafter, will be using this lawsuit to
4 conceal an attempt to directly interfere with Blockbuster's business relationships
5 and business, to monopolize the relevant market, and to conceal by deceit Netflix's
6 maintenance of that monopoly.

7 106. As examples of Netflix's bad faith, Blockbuster is informed and
8 believes and thereon alleges that, at the time of filing this lawsuit, Netflix knew,
9 and now knows:

10 a. That the blatantly over-broad '450 patent was and is
11 invalid because its claims were anticipated by – and obvious in view of –
12 prior art that Netflix had failed to disclose to the Patent Office during the
13 pendency of the application for the '450 patent;

14 b. The '450 patent was and is unenforceable because
15 Netflix's Applicants and Representatives had withheld known, material prior
16 art from the Patent Office in prosecuting the application that resulted in the
17 '450 patent; and

18 c. As alleged above, even Netflix's own CEO, Reed
19 Hastings, who is also a Named Inventor on the patent, described the '450
20 patent as a "joke."

21 107. Netflix has market power in the relevant market as alleged
22 above.

23 108. Blockbuster is informed and believes and thereon alleges that
24 Netflix has used and is using its '450 and '381 patents and its sham infringement
25 litigation against Blockbuster to restrain competition by, without limitation,
26 attempting to induce Blockbuster to leave the relevant market, attempting to
27 damage Blockbuster's ability to compete in the relevant market, and attempting to
28 deter other potential competitors from entering the market.

1 109. Blockbuster is informed and believes and thereon alleges that
2 Netflix has succeeded in restraining competition in the relevant market during the
3 relevant time period by fraudulently obtaining and asserting the '450 and '381
4 patents and by filing and prosecuting its sham infringement litigation against
5 Blockbuster. Netflix's monopolistic conduct as alleged herein is already harming
6 competition by causing Blockbuster to devote substantial resources to the defense
7 of this patent infringement action. Blockbuster is informed and believes and
8 thereon alleges that Netflix's monopolistic conduct is further harming, or will
9 further harm, competition by deterring other potential competitors from entering the
10 relevant market.

11 110. As a direct and proximate result of Netflix's acts of
12 monopolization, Blockbuster has suffered damages including attorneys' fees and
13 litigation expenses required to defend against Netflix's infringement lawsuit.
14 Blockbuster is informed and believes and thereon alleges that other damages
15 directly and proximately resulting from Netflix's monopolistic conduct include lost
16 profits and lost goodwill sustained or to be sustained by Blockbuster as well as
17 harm to other competitors or would-be competitors in the relevant market and to
18 online DVD rental consumers. Blockbuster is informed and believes and thereon
19 alleges that it and others will suffer additional such damages in the future suffer if
20 Netflix continues its monopolistic conduct, including its assertion of fraudulently
21 obtained patents and its sham litigation.

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SECOND COUNTERCLAIM
**(Attempted Monopolization in Violation of Section 2
of the Sherman Antitrust Act)**

111. Blockbuster repeats all allegations of paragraphs 16 through 110 above.

112. Blockbuster is informed and believes and thereon alleges that Netflix has attempted to monopolize the relevant market during the relevant time period, in violation of Section 2 of the Sherman Antitrust Act. Blockbuster is informed and believes and thereon alleges that Netflix's acts of attempted monopolization have included procuring either or both of the '450 and '381 patents by knowing and willful fraud and baselessly asserting them in bad faith in sham litigation against Blockbuster.

113. Blockbuster is informed and believes and thereon alleges that, in fraudulently obtaining and asserting the '450 and '381 patents as alleged herein, Netflix has acted with the specific intent to monopolize the relevant market.

114. Blockbuster is informed and believes and thereon alleges that, in filing and prosecuting its sham infringement litigation against Blockbuster as alleged herein, Netflix has acted with the specific intent to monopolize the relevant market.

115. Blockbuster is informed and believes and thereon alleges that Netflix's attempts to monopolize the relevant market, as alleged herein, have had and now have a dangerous probability of success.

116. Blockbuster is informed and believes and thereon alleges that Netflix has had market power in the relevant product and geographical markets, throughout the relevant time period or, in the alternative, that Netflix has a dangerous probability of success of obtaining such market power.

117. Blockbuster is informed and believes and thereon alleges that, if successful, Netflix's monopolistic conduct as alleged herein would harm

1 competition in the relevant market by depriving consumers of the increased output,
2 broader choice, and lower prices that would result from competition on the merits.

3 118. Blockbuster is informed and believes and thereon alleges that, if
4 Netflix succeeded in its attempt to cause Blockbuster Online to exit from the
5 relevant market because of fraudulently-obtained patents and sham litigation,
6 Netflix would obtain a virtually complete monopoly in the relevant market.

7 119. As a direct and proximate result of Netflix's acts of attempted
8 monopolization, Blockbuster has suffered damages including, without limitation,
9 attorneys' fees and litigation expenses required to defend against Netflix's
10 infringement lawsuit. Blockbuster is informed and believes and thereon alleges that
11 other damages directly and proximately resulting from Netflix's acts of attempted
12 monopolization include lost profits and lost goodwill sustained or to be sustained
13 by Blockbuster as well as harm to other competitors or would-be competitors in the
14 relevant market and to online rental consumers. Blockbuster is informed and
15 believes and thereon alleges that it and others will suffer additional such damages in
16 the future suffer if Netflix continues its acts of attempted monopolization, including
17 its assertion of fraudulently obtained patents and its sham litigation.

18 **THIRD COUNTERCLAIM**

19 **(Declaratory Judgment as to the '450 Patent)**

20 120. Blockbuster repeats all allegations of paragraphs 16 through 119
21 above.

22 121. A case and actual controversy exists between Blockbuster and
23 Netflix with regard to infringement, validity, and enforceability of the '450 patent
24 as a result of Netflix's filing of this case against Blockbuster, contending that
25 Blockbuster's Blockbuster Online service infringes the '450 patent and seeking an
26 injunction and monetary award based on that contention.

27 122. Blockbuster contends that it and its Blockbuster Online service
28 do not infringe and have not infringed any valid claim of the '450 patent as properly

1 construed, whether directly or through inducement of infringement or contributory
2 infringement.

3 123. Blockbuster contends that the '450 patent is invalid for reasons
4 including, without limitation, each of the reasons alleged above.

5 124. Blockbuster contends that the '450 patent is unenforceable for
6 the each of the reasons alleged above and in view of the conduct of Netflix and its
7 Applicants and Representatives as alleged above including, without limitation, their
8 failures to disclose known, material prior art to the Patent Office.

9 125. Blockbuster has no adequate remedy at law.

10 **FOURTH COUNTERCLAIM**

11 **(Declaratory Judgment as to the '381 Patent)**

12 126. Blockbuster repeats all allegations of paragraphs 16 through 119
13 above.

14 127. A case and actual controversy exists between Blockbuster and
15 Netflix with regard to infringement, validity, and enforceability of the '381 patent
16 as a result of Netflix's filing of this case against Blockbuster, contending that
17 Blockbuster's Blockbuster Online service infringes the '381 patent and seeking an
18 injunction and monetary award based on that contention.

19 128. Blockbuster contends that it and its Blockbuster Online service
20 do not infringe and have not infringed any valid claim of the '381 patent as properly
21 construed, whether directly or through inducement of infringement or contributory
22 infringement.

23 129. Blockbuster contends that the '381 patent is invalid for reasons
24 including, without limitation, each of the reasons alleged above.

25 130. Blockbuster contends that the '381 patent is unenforceable for
26 the each of the reasons alleged above and in view of the deceptive conduct of
27 Netflix and its Applicants and Representatives as alleged above including, without
28 limitation, their failures to disclose known, material prior art to the Patent Office.

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131. Blockbuster has no adequate remedy at law.

PRAYER FOR RELIEF

Blockbuster respectfully requests judgment as follows:

- 1. That Netflix recover nothing by its Complaint;
- 2. For a declaratory judgment determining and declaring:
 - a. That Blockbuster has not violated, and is not violating, any rights of Netflix under the '450 patent or '381 patent;
 - b. That each claim of the '450 and '381 patents is invalid;
- and
- c. That the '450 and '381 patents are unenforceable;
- 3. For compensatory damages according to proof;
- 4. Determining that this is an "exceptional" case and awarding Blockbuster its attorneys' fees and expenses under 35 U.S.C. § 285 or on any other applicable ground;
- 5. For costs of suit;
- 6. For pre-and post-judgment damages on all amounts awarded to Blockbuster; and
- 7. For general relief.

DATED: Sept. 11, 2006 ALSCHULER GROSSMAN STEIN & KAHAN LLP

By _____ /S/
 William J. O'Brien
 Attorneys for Defendant and Counterclaimant,
 Blockbuster Inc.

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DEMAND FOR JURY TRIAL

Under Rule 38(b) of the Federal Rules of Civil Procedure and Civil Local Rule 3-6 of the United States District Court for the Northern District of California, Blockbuster hereby demands a trial by jury of all issues properly triable by jury.

DATED: Sept. 11, 2006 ALSCHULER GROSSMAN STEIN & KAHAN LLP

By _____ /S/ _____
William J.O'Brien
Attorneys for Defendant and Counterclaimant,
Blockbuster Inc.

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CERTIFICATION OF INTERESTED ENTITIES OR PERSONS

Pursuant to Civil L.R. 3-16, the undersigned certifies that the following listed persons, association of persons, firms, partnerships, corporations (including parent corporations) or other entities (i) have a financial interest in the subject matter in controversy or in a party to the proceeding, or (ii) have a non-financial interest in that subject matter or in a party that could be substantially affected by the outcome of this proceeding:

Blockbuster Inc.

Netflix, Inc.

DATED: Sept. 11, 2006 ALSCHULER GROSSMAN STEIN & KAHAN LLP

By _____ /S/ _____
William J. O'Brien
Attorneys for Defendant and Counterclaimant,
Blockbuster Inc.