UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

DODOCASE VR, INC., et al.,

Plaintiffs,

v.

MERCHSOURCE, LLC, et al.,

Defendants.

Case No. 17-cv-07088-JCS

ORDER GRANTING IN PART AND DENYING IN PART PLAINTIFFS' MOTION TO STRIKE AND DENYING PLAINTIFFS' MOTION FOR SANCTIONS

Re: Dkt. Nos. 129, 140

Plaintiffs Dodocase VR, Inc ("Dodocase") and DDC Technology, LLC ("DDC") (together, "Plaintiffs") filed a motion to strike Defendants MerchSource LLC ("MerchSource") and Threesixty Brands Group LLC's ("Threesixty") (together, "Defendants") amended answer to the second amended complaint ("SAC").[1] Plaintiffs also filed a motion for sanctions against Defendants. Having reviewed the parties' submissions, the Court concludes that these matters are suitable for decision without a hearing. The Court GRANTS IN PART AND DENIES IN PART Plaintiffs' motion to strike. The Court further DENIES Plaintiffs' motion for sanctions.

I. BACKGROUND

On December 13, 2017, Plaintiff Dodocase filed its original complaint seeking declaratory judgment and injunctive relief. Dkt. No. 1. Plaintiffs filed a second amended complaint on January 07, 2019. Dkt. No. 98, SAC. Plaintiff Dodocase manufactured accessories for mobile devices, including virtual reality accessories for smartphones. Id., ¶¶ 10, 11. Plaintiff Dodocase

[1] As an initial matter, the briefs for both motions often refer to activities by "Defendants," but Defendant ThreeSixty was not a party to the MLA or otherwise involved in the activities or alleged activities on which plaintiffs' claims are based. Likewise, Plaintiff DDC was not a party to the MLA when it was executed. This Order often refers to "Defendants" or "Plaintiffs" for convenience but recognizes the limited roles of Defendant ThreeSixty and Plaintiff DDC in the

has been awarded multiple patents for its virtual reality accessories, including three patents that are at issue in this case. Id., ¶ 13. Those three patents are United States Patent No. 9,420,075, entitled "Virtual Reality Viewer and Input Mechanism," issued August 16, 2016 (the "'075 Patent"); United States Patent No. 9,723,117, entitled "Virtual Reality Viewer and Input Mechanism," issued on August 1, 2017 (the "'117 Patent"); and United States Patent No. 9,811,184, entitled "Virtual Reality Viewer and Input Mechanism," issued on November 7, 2017 (the "'184 Patent"). Id. The complaint refers to these three patents collectively as the "Dodocase Patents." Id.

MerchSource designs, sources, and distributes a wide-range of consumer goods, including toys, electronics, and home decor, to large retailers. Id., ¶ 17. MerchSource is wholly owned by ThreeSixty. Id., ¶ 19. Plaintiff Dodocase alleges that MerchSource sells, manufactures, designs, and/or imports certain products under the brand name "Sharper Image" that threaten to infringe the Dodocase Patents. Id., ¶ 20.

On or about June 16, 2016, MerchSource contacted Plaintiff Dodocase about obtaining a license to the '075 Patent. Id., ¶ 26. Subsequently, on or about October 3, 2016, MerchSource and Plaintiff Dodocase entered into a Master License Agreement regarding the Dodocase Patents ("MLA"). Id., ¶ 27. The MLA states that "MerchSource desires to manufacture and sell virtual reality viewer products having a capacitive touch input mechanism containing the Licensed IP." Id., ¶ 23. The MLA also provides that "MerchSource shall not (a) attempt to challenge the validity or enforceability of the Licensed IP; or (b) directly or indirectly, knowingly assist any Third Party in an attempt to challenge the validity or enforceability of the Licensed IP except to comply with any court order or subpoena." Id., ¶ 79.

Starting on or about June 9, 2017, MerchSource began contacting Plaintiff Dodocase to express dissatisfaction with the MLA. Id., ¶ 29. On or about July 10, 2017, MerchSource told Plaintiff Dodocase that in light of its perception that Plaintiff Dodocase was not enforcing its intellectual property sufficiently, MerchSource would "have no choice but to impute a zero percent royalty rate under the [MLA] in order to be similarly advantaged." Id., ¶ 30. On October 5, 2017, MerchSource sent Plaintiff Dodocase a letter which stated, "We have reviewed the

Licensed Patents, including the allowed claims of U.S. Patent Application Serial No. 15/448,785 [the application for the later-issued '184 Patent], and have concluded that all relevant claims are invalid under 35 U.S.C. § 102 and/or § 103. Accordingly, MerchSource will not be paying royalties on any products sold hereafter." Id., ¶ 32. Plaintiffs allege that MerchSource did not identify any prior art for Plaintiff Dodocase to consider. Id. Plaintiff Dodocase responded that refusal to pay royalties despite its continued manufacture, use, sale, and/or offer for sale of products using the Dodocase Patents constituted a breach of the MLA. Id., ¶ 33. One day after the deadline to cure the breach, on November 17, 2017, MerchSource provided a royalty check and royalty report. Id., ¶ 36. The royalty report included a statement that "MerchSource considers the dispute over royalty rate and owed royalties under the Agreement outstanding and not yet resolved." Id. Plaintiffs allege that MerchSource made no further suggestion of patent invalidity. Id. MerchSource has not paid royalties on products sold after October 5, 2017. Id., ¶¶ 52, 66, 92-94.

On December 13, 2017, Plaintiff Dodocase filed its original complaint seeking declaratory judgment and injunctive relief. Id., ¶ 38. On December 22, 2017, Defendants MerchSource LLC and Threesixty Brands Group LLC (together, "Defendants") filed a motion for an extension of time to answer or otherwise respond to the complaint. Id., ¶ 40. In their motion, Defendants stated that they required more time to investigate the complaint's allegations, in part due to the fact that the twenty-one day answer period under Rule 12 included the year-end holidays and relevant MerchSource personnel and its attorneys had previously scheduled travel, holiday, and vacation plans during that time. Id. The Court granted Defendants' request for a twenty-nine day extension over the objection of Plaintiff. Dkt. Nos. 15 & 18.

On January 12, 2018, counsel for Plaintiff Dodocase and Defendants held a telephone conference to discuss potential resolution of this case, including renegotiation of the MLA's royalty option. Dkt. 98, ¶ 41-45. In anticipation of that meeting, Defendants' counsel requested that Plaintiff Dodocase sign a non-disclosure agreement to allow "MerchSource to provide certain information and documents to DODOcase that are confidential and/or protected by privilege or attorney work product." Id., ¶ 43. Plaintiffs allege that it became clear that the "work product"

was alleged prior art. Id. Thus, Plaintiffs allege that Defendants' sought to "(a) use alleged prior art to extort a favorable settlement of this action and a running-royalty license to the DODOCASE Patents while simultaneously (b) shielding said alleged prior art from the public (including their competitors)" and Plaintiff Dodocase refused to execute the nondisclosure agreement because it believed that such an agreement would be unethical in light of Plaintiff's obligations of disclosure to the Patent Office for continuing applications and in future licensing discussions or litigation with third parties. Id., ¶ 43.

Although Plaintiff Dodocase did not sign the non-disclosure agreement, the parties still held the scheduled meeting but could not, however, reach agreement on resolution. Id., ¶ 45-46. Defendants stated that they were prepared to file challenges to the Dodocase Patents with the PTAB. Id., ¶ 46. On January 15, 2018, Defendants identified the three alleged prior art references for Plaintiff for the first time. Id., ¶ 47. Plaintiff Dodocase reviewed the information and told Defendants that it did not think the alleged prior art supported their claim of invalidity. Id., ¶ 48.

Defendants then filed three separate PTAB Petitions, challenging each of the three Dodocase Patents, on January 15, 2018. Id., ¶ 54. The PTAB Petitions rely on the same three "primary references": (1) U.S. Patent Publication No. 2013/0141360, which issued as U.S. Patent 9,423,827 ("Compton"); (2) a comment posted on a blog entitled, "Why Google Cardboard is Actually a Huge Boost for Virtual Reality" ("Gigaom"); and (3) a YouTube video entitled, "Use Google Cardboard without Magentometer (Enabling Magnetic Ring Support to Every Device)" ("Tech#"). Id., ¶ 55.

On February 2, 2018, Defendants answered the complaint and filed a counterclaim against Plaintiff Dodocase. Dkt. No. 22, Counterclaim. The counterclaim sought declaratory judgment that each of the three Dodocase Patents is invalid for at least the reasons set forth in the PTAB Petitions. Id., Counterclaim, ¶¶ 6-26.

As a result of the failed negotiations, the PTAB Petitions, and Defendant MerchSource's failure to make their royalty payment for the fourth quarter of 2017, Plaintiff terminated the MLA on February 14, 2018. Dkt. No. 98, SAC, ¶¶ 52-53. Section 3.6 of the MLA further provides:

"Upon termination of this Agreement, MerchSource shall have no further obligation to pay any

fees to Licensor under this Article 3, except for royalties owed under this Section 3 and for the sale of Licensed Products during the Sell-Off Period, as applicable." Id., ¶ 78. Section 8.1.6 of the MLA provides: "Upon termination of any Term Sheet or this Agreement for any reason, MerchSource shall be entitled, for eighteen (18) months (the "Sell-Off Period") after termination, to continue to sell any Licensed Product, that is the subject of a purchase order, is in transit to a customer or MerchSource, or is in inventory with MerchSource at the time of termination. Such sales shall be made subject to all the provisions of the Agreement and any respective Term Sheet, including the payment of royalties which shall be due quarterly until the close of the Sell-Off Period." Id., ¶ 83.

On March 23, 2018, the Court granted Plaintiff Dodocase's motion for preliminary injunction and ordered Defendants to request a withdrawal of the PTAB Petitions. Dkt. No. 47. Defendants appealed the Court's order. On July 12, 2018, the Court ordered a stay in this case until the PTAB proceedings ended.

On October 16, 2018, DODOCASE transferred to DDC all right, title and interest in and to the DODOCASE Patents, including all causes of action and enforcement rights for past, current and future infringement of the DODOCASE Patents. Dkt. No. 98, SAC, ¶ 6. On January 7, 2019, Plaintiffs filed their second amended complaint.

On April 22, 2019, the Court of Appeal affirmed this Court's order granting Plaintiff Dodocase's motion for preliminary injunction. Dkt. No. 103, 104. The petition for panel rehearing was denied on July 10, 2019. Dkt. No. 113. On July 17, 2019, the Court ordered Defendants to withdraw their PTAB Petitions. Dkt. No. 115. The PTAB terminated the proceedings on August 16, 2019. Dkt. No. 119.

On September 25, 2019, at the request of the parties, the Court ordered the parties to file motions regarding: (1) When MerchSource provided sufficient Lear notice; and (2) Whether a sufficient Lear notice applies during the Sell-Off period under the MLA. The Court also lifted the stay.

On October 29, 2019, Defendants filed their amended answer to Plaintiffs' second amended complaint. On November 12, 2019, Plaintiffs filed a motion to strike Defendants'

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