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MGA Ruling Guides On Time Limits For Trade Secret Claims

By **Stephen Moses** (November 18, 2019, 4:37 PM EST)

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On Oct. 29, the California Court of Appeal's Second Appellate District, Division Eight, issued an opinion in MGA Entertainment Inc. v. Mattel Inc., upholding the trial court's dismissal of MGA's trade secret misappropriation claims against Mattel over the irreverent Bratz dolls made by MGA.[1] MGA appealed the judgment of Superior Court Judge Carolyn B. Kuhl, who granted Mattel's motion for summary judgment on the grounds that MGA filed its state court lawsuit for trade secret misappropriation under the California Uniform Trade Secrets Act[2] after the three-year statute of limitations had expired.

This latest ruling in a case that has been litigated over the course of the last 15 years, resulting in no fewer than three published appellate opinions, addresses what constitutes notice of a trade secret claim sufficient to trigger the statute of limitations. MGA must have thought victory was assured when it filed its trade secret misappropriation case in superior court, having successfully tried the case once before in the U.S. District Court for the Central District of California.

But, in affirming the trial court's decision, the court of appeal determined that once MGA had a reason to suspect an injury and some wrongful cause, the statute of limitations began to run. "[The] same suspicions that allowed MGA to request discovery and plead the unclean hands defense in federal court in 2007 were sufficient to trigger the statute of limitations."[3]

The main lesson of the most recent state court of appeal decision is that claims uncovered in the course of discovery trigger the statute of limitations for the new claims. The fact that the parties are engaged in litigation does not toll the statutory period or result in new claims relating back to the date the complaint was filed.

Even a party hiding the ball or dragging its feet in discovery is not sufficient to toll the statute on newly suspected claim, if a party is on notice of such claim. In order to address such issues, practitioners should be prepared to move to compel discovery or to extend the date or scope of discovery, and move to amend the pleadings.

It is important to note that the trade secret misappropriation claims brought by both MGA and Mattel were based on the California UTSA, not the federal Defend Trade Secrets Act[4], which was not yet law. The DTSA borrows the statute of limitations from state law, so the result would not have been any

different under the DTSA. Any contribution DTSA might make to uniformity to federal and state trade secret litigation remains to be seen as that law is still in its infancy.

Barbie Vs. Bratz

The fight between Mattel and MGA began when one of Mattel's Barbie doll fashion designers, Carter Bryant, pitched his idea for Bratz dolls to MGA. MGA accepted Bryant's pitch, and he left Mattel. Bratz dolls were an overnight success, threatening Barbie's reign.

Mattel sued, arguing that Bryant's initial work on the Bratz dolls idea was owned by Mattel based on his employment agreement. Mattel won a jury verdict in its favor for copyright infringement and the trial court awarded $10 million in damages and issued a constructive trust over all of MGA's Bratz trademark portfolio worth over $1 billion.

That is, until Judge Alex Kozinski of the U.S. Court of Appeals for the Ninth Circuit vacated the verdict and the constructive trust issued by the district court.[5] As Judge Kozinski noted in his opinion, "Barbie captured Bratz."[6]

Bratz Fights Back

MGA and Bratz fought back. And, for a time, they appeared to have Barbie on the ropes. In 2004, MGA sued Mattel for copyright infringement in the Central District of California.

It was in the course of discovery that MGA uncovered Mattel's efforts to obtain MGA's trade secret information. Such as, for example, Mattel employees masquerading as retailers in order to gain access to MGA's showrooms and toy fair displays under false pretenses. In 2007, MGA asserted an equitable defense of unclean hands in response to a counterclaim by Mattel, relying on the same evidence of trade secret misappropriation it uncovered in discovery.

MGA asserted a counterclaim in reply for trade secret misappropriation three years and three days after it responded to Mattel's counterclaim asserting the affirmative defense of unclean hands. In the federal litigation, Mattel had filed a motion to amend seeking to add a new cause of action for trade secret misappropriation.

The district court denied its motion, but allowed Mattel to bring its misappropriation claims in a counterclaim. MGA responded with a counterclaim in reply asserting its own misappropriation claim. Mattel moved to dismiss it, but the district court determined it was related to Mattel's counterclaim and allowed it.

At trial, the jury found that Mattel misappropriated 26 (out of an alleged 114) categories of MGA's trade secret information and that the misappropriation was willful and malicious.[7] MGA won an award of $85 million in compensatory damages, $85 million in punitive damages and $2.172 million in attorney fees.[8]

The Ninth Circuit vacated the verdict in favor of MGA and directed the district court to dismiss MGA's misappropriation claim without prejudice.[9] In his second appellate decision in the case, Judge Kozinski overturned the jury verdict for MGA of $85 million, holding that MGA's misappropriation claims were not properly made in the counterclaim in reply, because they were not compulsory to the initial claims. Judge Kozinski suggested that MGA bring its misappropriation claims in state court before admonishing

Barbie and Bratz to "play nice."[10]

Bratz Brings Misappropriation Claim in California Superior Court

MGA took Judge Kozinski's advice and filed an action for trade secret misappropriation under the California UTSA in Los Angeles County Superior Court. However, in February 2018, MGA's claims were dismissed on summary judgment on statute of limitations grounds.

Mattel predicated its motion for summary judgment on the grounds that MGA was on notice of the misappropriation claim as far back as 2003, and that the 2007 discovery responses were sufficient to start the clock for the statute of limitations. MGA, on the other hand, argued that Mattel concealed evidence of bad conduct, and that a dismissal on statute of limitations grounds would only reward the bad behavior. Judge Kuhl sided with Mattel.

MGA's Theory of Distinct Injuries

MGA took two approaches in its appeal. The state court of appeal first addressed MGA's contention that it did not discover Mattel's misappropriations until 2010.[11] MGA contended that although it had discovered some misappropriation it had not discovered all of the misappropriation on which its claims are based.

In other words, MGA argued that there were 114 distinct misappropriations, so that the discovery of one misappropriation did not put it on notice of other misappropriations. Therefore, MGA argued, the statute of limitations "runs separately from the discovery of each distinct injury." The court of appeal rejected this argument.

Civil Code Section 3426.6 requires that a claim for trade secret misappropriation be brought within three years after the misappropriation is discovered or should have been discovered.[12] The court of appeal instructed that, in California, the statute of limitations begins to run "when the plaintiff has reason to suspect an injury and some wrongful cause."[13]

Once a plaintiff's suspicion arises, she cannot wait for the facts to find her, but must go and find them.[14] Although a defendant's fraud in concealing a cause of action tolls the statute of limitations, it does so only until the plaintiff is on notice of a potential claim.[15]

The court of appeal asked when did MGA have a reason to suspect that Mattel was using false pretenses to gain access to MGA's showrooms? The court of appeal determined that when MGA responded with an affirmative defense of unclean hands "on that very basis" in August 2017, MGA had reason to suspect the claim.[16]

Second, MGA argued that it did not discover the 114 misappropriations until 2010, when Mattel turned over its toy fair reports from 2000 to 2004, which MGA considered confidential, competitive information. The court of appeal determined that MGA's second argument also ignores the standard for accrual of the statute of limitations.

The question, the court of appeal stated, is when was MGA on notice of a potential claim?[17] The plaintiff need not be aware of the specific facts necessary to establish the claim, because that's what discovery is for.[18]

Fraudulent Concealment

The state court of appeal quickly dismissed MGA's fraudulent concealment argument, explaining that fraudulent concealment tolls the statute of limitations only "until the plaintiff discovers or should have discovered the claim."[19] The court of appeal explained that Bernson v. Browning-Ferris Industries instructs that the fraudulent concealment rule is a "close cousin of the discovery rule," and "its rationale is the culpable defendant should be estopped from profiting by his own wrong to the extent that it hindered an 'otherwise diligent' plaintiff in discovery his cause of action."[20]

As applied to MGA, it had already discovered its cause of action no later than 2007. The court of appeal reiterated that "if a plaintiff is on notice of a potential claim, the doctrine of fraudulent concealment does not come into play."[21]

Lastly, the court of appeal distinguished MGA's case from a line of cases addressing whether fraudulent concealment exists when there is a "legitimate hindrance to litigation," such as concealing relevant documents in the course of discovery. Again, the court of appeal concluded, "MGA clearly articulated the nature of the injury and its wrongful cause in its unclean hands defense."[22]

While Bratz and MGA might have lost the trade secret battle, it won the war. Barbie and Mattel have to share the aisle with Bratz.

That seems fitting. This beauty contest is better left to consumers, not juries.

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[1] MGA Entertainment, Inc. v. Mattel, Inc., Case No. B289709, ___ Cal.Rptr.3d ____, 2019 WL 5558188 (October 29, 2019) ("MGA 2019").

[2] Ca. Civ. C., sec. 3426 et seq.

[3] MGA 2019, supra. Note 1.

[4] 18 U.S.C. 1832 et seq.

[5] Mattel, Inc. v. MGA Entertainment, Inc. (9th Cir. 2010) 616 F. 3d 904, 908. Judge Kozinski vacated the verdict and the constructive trust on the grounds that Bryant's employment agreement did not transfer copyright over the "idea" of Bratz to Mattel while he worked there, and the issuance of a constructive trust was an abuse of discretion. Judge Kozinski noted that the Bratz idea had much less value at the time it was created than after their development and marketing into a billion-dollar brand. He also determined that the copyright over such dolls was "thin," meaning that the dolls mostly constituted features that were generic and, therefore, not subject to copyright protection. It was here that Judge Kozinski planted the idea that the intellectual property in the dolls was based in trade secret law, not copyright law.

[6] Id.

[7] See Mattel, Inc. v. MGA Entertainment, Inc. (C.D. Cal. 2011) 801 F. Supp. 2d 950.

[8] Id. The District Court observed that jury found Mattel's conduct reprehensible, including encouraging employees to use false pretenses to obtain information about MGA's plans, using MGA's trade secret information to preempt product releases, and causing tens of millions of dollars of harm. In declining to award punitive damages of twice the amount of compensatory damages, the District Court called the Mattel's conduct "silly, not evil," and noted that Mattel ceased such conduct in 2005. "Faced with competition and innovation that it didn't relish, Mattel resorted to nefarious tactics in an attempt to cling to its market position." Id. at 955-6.

[9] See Mattel, Inc. v MGA Entertainment, Inc. (9th Cir. 2013) 705 F.3d 1108, 1110-11. In his second opinion between Bratz and Barbie, Judge Kozinski determined that MGA's misappropriation claim was not compulsory and, therefore, was not properly made by a counterclaim in reply. On that basis, he overturned the jury verdict in favor of MGA. Mattel had already asserted a statute of limitations defense to MGA's misappropriation claim, but that issue was not addressed by the Court of Appeal. On remand, the District Court was instructed to dismiss MGA's misappropriation claim without prejudice. Judge Kozinski ordered the dismissal "without prejudice" so as not to interfere with MGA bringing its misappropriation claim in state court, as he suggested that MGA do.

[10] Id. 1111.

[11] MGA 2019, supra. Note 1.

[12] Id., recognizing Intermedics, Inc. v. Ventritex, Inc. (N.D.Cal. 1992) 804 F.Supp.35, 44.

[13] Id., citing Fox v. Ethicon Endo-Surgery, Inc. (2005) 35 Cal.4th 797, 803.

[14] Id., citing Jolly v. Eli Lilly & Co. (1988) 44 Cal.3d 1103, 111.

[15] Id., citing Bernson v. Browning-Ferris Industries (1994) 7 Cal.4th 925, 931.

[16] Id. (italics in original). The Court of Appeal also rejected MGA's argument that did not have a reason to suspect that Mattel would attempt to get into other toy fairs only by discovering that its employees had infiltrated one.

[17] Id., citing Rita M. v. Roman Catholic Archbishop (1986) 187 Cal. App. 3d 1453, 1460.

[18] Id., citing Jolly, supra., 44 Cal. 3d at 1111.

[19] Id., citing Bernson, supra., 7 Cal.4th at 931.

[20] Id.

[21] Id., citing Rita M., supra., 187 Cal. App. 3d at 1460.

[22] Id.