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Case No. 3443-VCP

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

NORFOLK COUNTY RETIREMENT SYSTEM,	)	
	)	
Plaintiff,	)	
	)	
v.	)	C.A. No. 3443-VCP
	)	
JOS. A. BANK CLOTHIERS, INC.,	)	
	)	
Defendant.	)	

COMBINED REPLY OF JOS. A. BANK CLOTHIERS, INC. IN SUPPORT OF ITS MOTION FOR PROTECTIVE ORDER AND REPLY OF NON-PARTIES WILLIAM E. HERRON, SIDNEY H. RITMAN AND ANDREW A. GIORDANO IN SUPPORT OF THEIR MOTION TO QUASH SUBPOENAS

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PRELIMINARY STATEMENT

Plaintiff's Opposition fails to address the governing law that requires the Court to grant the discovery motions filed by the Defendant and three of its directors. The Opposition also violates this Court's ruling that the parties would not be permitted to file summary judgment motions. Because there is no basis in Delaware law for the discovery Plaintiff seeks, those discovery motions should be granted.

During the June 11, 2008 telephone conference with counsel, this Court denied both parties' requests for leave to file summary judgment motions. (June 11, 2008 Tr. at 15) (Exhibit A). Pursuant to the Third Stipulated Amended Scheduling Order, June 27, 2008 was the date for plaintiff Norfolk County Retirement System ("Plaintiff") to file its opposition to the motion for protective order filed by defendant Jos. A. Bank, Clothiers, Inc. ("Jos. A. Bank" or the "Company") and to the motion to quash subpoenas filed by non-parties William E. Herron, Sidney H. Ritman and Andrew A. Giordano (the "Non-Party Directors") (collectively, the "Discovery Motions"). June 27, 2008 was also the Court-Ordered date for Plaintiff to file a reply in support of its five motions for commissions directed to each of the Non-Party Directors, as well as the two lawyers retained by the Company's Special Litigation Committee (the "SLC").

Despite this posture, and in violation of the Court's decision not to permit summary judgment motions, Plaintiff elected to devote the bulk of its opposition to the Discovery Motions (the "Opposition") to arguing the merits of the summary judgment motion the Court prohibited it from filing. The Opposition seeks three summary judgment rulings -- (1) that Plaintiff has established a proper purpose for inspection of the Company's books and records (Opposition at 9-10), (2) that the SLC's investigation and Plaintiff's receipt of the SLC Report are "legally irrelevant" to Plaintiff's Section 220

demand (*id.* at 10), and (3) that the future "demand-excused" derivative action Plaintiff wishes to file is not barred by a ruling of the United States District Court for the District of Maryland dismissing just such a claim (*id.* at 5 n.4). None of these issues are properly before the Court, and the Court should not address them. If the Court does elect to address them, they should be denied for the reasons stated in Section III of this Reply.

In addition to its poorly disguised summary judgment arguments, Plaintiff devotes two pages to the only issue before the Court, which is whether Plaintiff is entitled to massive document discovery regarding the work of the SLC, plus a Rule 30(b)(6) deposition of the Company and depositions of each of the three non-party directors. In those two pages, Plaintiff ignores the case law establishing that discovery in a books and records action may not be used by a plaintiff to gain access to books and records ultimately at issue, much less testimony that is unavailable even as part of any post-trial final order. Plaintiff also fails to address the statutory barrier to serving subpoenas on the non-party directors at the registered agent of the Company. Accordingly, the Discovery Motions should be granted.

ARGUMENT

I. PLAINTIFFS MAY NOT USE DISCOVERY IN A SECTION 220 ACTION TO OBTAIN EITHER THE DOCUMENTS THAT ARE ULTIMATELY AT ISSUE OR DEPOSITIONS THAT ARE STATUTORILY UNAVAILABLE

Jos. A. Bank voluntarily provided Plaintiff with a copy of the SLC Report, which fell within the scope of Plaintiff's original Section 220 demand. The ultimate issue to be determined after trial in this Section 220 action is whether Plaintiff is entitled to any additional documents.

Plaintiffs' Opposition claims entitlement before trial to documents and other discovery responsive to its newly "narrowed" discovery requests, including:

- "all Documents concerning the SLC Report, including but not limited to the minutes of any meeting of the SLC or the Company's Board of Directors at which the SLC Report was considered or discussed";
- "all Documents reviewed or considered in connection with the SLC Report";
- "all Documents concerning any interviews taken in connection with the SLC Report";
- a deposition of a Company representative on undisclosed topics (the original Notice of Deposition, dated March 20, 2008, sought to examine the person or persons most knowledgeable about the subject matter of the Plaintiff's interrogatories and document requests); and
- depositions of each of the three members of the SLC.

(Opposition at 13-14).

This self-described "narrow" discovery actually resembles the discovery a plaintiff might seek in a shareholder derivative action, if it has survived a motion to dismiss pursuant to Court of Chancery Rule 23.1, or perhaps when a plaintiff is confronted by a *Zapata* committee's motion to terminate the derivative action. Plaintiff's "narrow" discovery request is far broader than what Plaintiff might obtain as part of any final order in this Section 220 action.

As an initial matter, Section 220 does not authorize any Court-ordered depositions of a defendant's directors or officers. *See* 8 *Del. C.* § 220(c).

Moreover, as established in the Discovery Motions, a plaintiff in a Section 220 action cannot obtain in discovery documents that are ultimately at issue in trial. The Discovery Motions quoted a treatise and a Court of Chancery case making that exact point. *See* Donald J. Wolfe, Jr. & Michael A. Pittenger, Corporate & Commercial Practice in the Delaware Court of Chancery § 8-6[h], at 8-126.22 n.422 (2007) ("Too expansive a scope of discovery in a books-and-records case would result in a plaintiff's securing the ultimate relief sought in the action, or its practical equivalent, without judicial resolution of the substantive, underlying right to such inspection. This is clearly to be avoided."); *U.S. Die Casting and Development Co. v. Security First Corp.*, 1995 Del. Ch. LEXIS 49, at *7-8 (Apr. 28, 1995) ("To grant U.S. Die its complete requested discovery would obviate the need for the § 220 action because U.S. Die would obtain through discovery all of the documents requested before a determination of the scope of its rights under § 220.").

Plaintiff's Opposition simply ignores the Company's core argument and the above-cited authorities. Plaintiff's Opposition also ignores a recent opinion by the Chancellor, *Maitland v. Int'l Registries, LLC*, C.A. No. 3669-CC (Del. Ch. June 6, 2008) (Exhibit B), which relies on *U.S. Die Casting* to reach the exact same result.

Maitland bears an uncanny resemblance to this case. Maitland filed an action for books and records of two limited liability companies pursuant to 6 *Del. C.* § 18-305, the statutory analog to Section 220. Maitland then moved for a commission to obtain documents and deposition testimony from the outside auditor of one of the defendants, purportedly to show that the documents turned over by the defendants were not sufficient

to moot his claim. The Chancellor denied the motion for commission, articulating two rationales. Both rationales apply to the facts of this case.

First, the Chancellor observed that "[t]o grant the motion for commission would be effectively to grant Maitland final relief in this proceeding." *Maitland*, let op. at 4. The documents sought in the motion for commission overlapped with those initially demanded, and, "[as] the Court held in *Security First*, Maitland cannot use the discovery process in a books and records case to gain access to the books and records ultimately at issue." *Id.*

The same rationale applies here. Plaintiff's demand letter seeks eleven categories of documents in connection with a disclosure in the Company's Form 10-Q for the first fiscal quarter of 2006 that profits had declined relative to the first quarter of the prior year. (*See* Motion for Protective Order Ex. H). To afford Plaintiff access in discovery to all or any documents related to the SLC Report would be the equivalent of a grant of final relief on Plaintiff's demand for various documents bearing on the drop in that quarter's profits.

Second, the Chancellor in *Maitland* rejected the argument that the plaintiff was entitled to documents in order to rebut an affirmative defense of mootness. The Chancellor reasoned that the requested documents were not necessary to rebut the defense: "Maitland must already have a reason to believe that the initial production was insufficient, and he is, therefore, already equipped to present this reason in response to defendants' argument his claim is moot. It would create a perverse precedent to allow Maitland to use the discovery process as an end-run around the LLC Agreement and the

statute simply because [the defendants] attempted to comply with Maitland's demand and produce the requested materials." *Maitland,* let op. at 4.

Again, the same logic applies here. Jos. A. Bank provided the SLC Report to Plaintiff and offered to provide Plaintiff with the exhibits to the SLC Report. Jos. A. Bank is defending this action, in part, based on the defense that the Company already has discharged any obligation it may have under Section 220. Plaintiff cannot justify a discovery request for all documents relating to the SLC Report with the assertion that those documents are needed to test the sufficiency of the SLC Report. That maneuver is simply an attempted end-run around Plaintiff's burden at trial to prove why additional documents are "necessary and essential" to satisfy a proper purpose. *Kaufman v. CA, Inc.*, 905 A.2d 749, 753 (Del. Ch. 2006).

Following *Maitland,* Plaintiff must rely on information already in its possession to articulate why it believes that the SLC Report is insufficient to defeat Plaintiffs' claim. It is noteworthy that the Opposition contains no such argument. It is also telling that the corporate designee of the Plaintiff testified that *he had no basis to question the independence and good faith of the SLC members in preparing the SLC Report.* (*See* Connelly Deposition at 33-34) (Exhibit C).

There simply is no legal authority supporting Plaintiff's attempt to short-circuit its burden to establish the merits of its Section 220 claim. Plaintiff's two-page argument about why it is supposedly entitled to discovery regarding the SLC rests on the following proposition: "plaintiff is entitled to discovery to explore the *bona fides* of the SLC at least as expansive as the discovery allowed in *Grimes* [*v. DSC Commc'ns Corp*., 724 A.2d 561

(Del. Ch. 1998)] and *Kaufman*." (Opposition at 13). Plaintiff apparently does not realize that neither *Grimes* nor *Kaufman* mentions, much less authorizes, any pre-trial discovery.

Grimes and *Kaufman* are both Section 220 decisions on the merits. Both cases deal with the question whether the plaintiff demonstrated a statutory entitlement to documents in addition to those voluntarily provided by the corporate defendant. They do not support a grant of document discovery (or depositions) to a Section 220 plaintiff in order to test the adequacy of documents voluntarily turned over the by the corporate defendant. The two decisions therefore support Jos. A. Bank's position, not Plaintiff's.

In *Grimes*, the corporate defendant voluntarily produced approximately 2,800 pages of documents in response to a Section 220 demand, but refused to produce a special committee report or the documents accompanying it. 724 A.2d at 565, 567. *Following a trial*, this Court granted the plaintiff Section 220 relief as to specified "basic documents" concerning the special committee. *Id.* at 567. *Grimes* makes no mention of any production of demanded documents in pre-trial discovery. The post-trial analyses of the plaintiff's actual purpose and privilege issues is wholly inconsistent with any suggestion that future plaintiffs need only serve discovery requests to get the same documents.

Kaufman arose "in the somewhat unique procedural posture of a motion, styled as one to compel, in a Section 220 case in which the defendant has conceded the propriety of the plaintiff's demand and has already furnished substantial documentation to the plaintiff." 905 A.2d at 753. Because the defendant conceded the propriety of the plaintiff's purpose (an unsurprising concession given that the Section 220 arose out of "a series of financial accounting scandals that have wracked [defendant]" and which had led to criminal indictments and guilty pleas, *id.* at 750, 751), the critical question was whether

the plaintiff had established why the documents sought were "either necessary or essential to her proper investigative purpose under Section 220." *Id.* at 754-55. This Court ruled that the plaintiff failed to satisfy the statutory standard, as the documents fell "well outside the traditional reach of Section 220 as articulated in *Grimes*." *Id.* at 754. The Court did not apply a Chancery Court Rule 26 discovery standard to the plaintiff's motion.

The results and analyses in *Kaufman* and *Grimes* are absolutely inconsistent with any suggestion that a Section 220 plaintiff can obtain additional document discovery to test the sufficiency of whatever documents were voluntarily provided by the corporate defendant in response to the Section 220 demand. *Kaufman* and *Grimes* are thus perfectly consistent with *U.S. Die* and *Maitland*. The law is uniform that a Section 220 plaintiff must first demonstrate that it satisfies the statutory standard to obtain any additional documents. As stated in *Maitland*, it would be a "perverse precedent" to allow the use of the discovery process to end-run the inspection statute. *Maitland*, let op. at 4.

Plaintiff gains nothing by the empty assertion that this Court "grants discovery of affirmative defenses." (Opposition at 13). The Company's Fifth Affirmative Defense is functionally no different than the defense in *Maitland* that the inspection demand is moot by virtue of the documents already turned over in response to the inspection demand. Here, as in *Maitland*, Plaintiff is seeking an end-run around the inspection statute and "has failed to show why the proposed commission seeks materials relevant or would lead to the discovery of materials relevant to the narrow issues in this case[.]" *Maitland*, let op. at 4.

Finally, as Vice Chancellor Lamb made clear in *Grimes*, because there has already been a SLC investigation into the Defendant's alleged wrongdoing, even a successful Section 220 plaintiff, who, unlike the Plaintiff in this case, has established a proper purpose for inspection after a trial, is "not entitled to receive or examine copies of other documents not directly related to the Special Committee's conclusions or recommendations unless he can articulate a reasonable need to inquire a further after review of those basic documents [*i.e.*, the Special Committee's report and certain Committee and Board minutes]." *Id.* at 567. Interview summaries, in particular, will only be made part of a Section 220 final order upon "a further showing of need." *Id.*

II. THE SUBPOENAS ARE INEFFECTIVE

The Non-Party Directors' motion to quash explained how 10 *Del. C.* § 3114 only operates as consent to service of process in a breach of fiduciary cases, not for service of subpoenas in a statutory action. (*See* Motion to Quash ¶ 34). Plaintiff ignores the language of the statute, and cites no statute or case decision authorizing the subpoenas. The subpoenas are plainly ineffective.

III. PLAINTIFF'S ARGUMENTS ON THE MERITS ARE DISPUTED AND IRRELEVANT TO THE PENDING DISCOVERY MOTIONS

As noted above, Plaintiff asserts arguments regarding the merits of the summary judgment motion that it was denied permission to file. The summary judgment issues are not properly before the Court. While the Company has no interest in arguing the merits of issues raised improperly, the Company feels obliged to respond, as it is hardly inconsequential that Plaintiff is pressing a Section 220 claim with the express purpose of filing a derivative action without regard for the facts that (i) another shareholder lost on demand futility when challenging the same underlying conduct, (ii) that shareholder

subsequently made a demand, (iii) the Company formed an SLC that investigated the demand and found it meritless, (iv) the SLC Report was provided to Plaintiff, and (v) the Plaintiff's corporate representative testified that he has no basis to challenge the good faith or thoroughness of the SLC's investigation.

If the Court elects to address the substantive arguments improperly made by Plaintiff in its Opposition, those arguments are without merit and must be rejected for the reasons stated below.

A. Plaintiff Has Not Established a Proper Purpose for Inspection of the Company's Books and Records

The fact of the SLC investigation, and the absence of any articulated basis to challenge the good faith or thoroughness of that investigation, despite the provision of the SLC Report to Plaintiff, raises serious questions whether Plaintiff is seeking books and records of the Company for a proper purpose that is supported by some evidence to suggest a credible basis that any wrongdoing may have occurred. *See Seinfeld v. Verizon Commc'ns*, 909 A.2d 117, 118 (Del. 2006). Additionally, the fact that Plaintiff is in possession of the SLC Report, and yet has no articulated basis for challenging the conclusions of the report, calls into serious question whether any additional documents "are necessary and essential to the satisfaction of the stated purpose." *Kaufman*, 905 A.2d at 753; *see Grimes*, 724 A.2d at 567.

Plaintiff can point to nothing more substantial in this case than a federal securities class action complaint that survived a motion for judgment on the pleadings to establish a "credible basis" of wrongdoing – but the existence and result of the SLC investigation

substantially outweighs any inference of wrongdoing arising from the unsupported allegations of the securities class action.[1]

Further, as addressed in more detail below, the prior dismissal of a "demand-excused" derivative lawsuit challenging the exact same conduct negates the propriety of Plaintiff's purpose to obtain documents to pursue an identical lawsuit. *See West Coast Mgmt. & Capital, LLC v. Carrier Access Corp.*, 914 A.2d 636, 645-46 (Del. Ch. 2006) (no "proper purpose" for Section 220 inspection existed where federal district court's dismissal of shareholder's first derivative suit due to failure to adequately plead demand futility precluded shareholder from pursuing a second derivative suit under the doctrine of issue preclusion).

B. The SLC Report Is Relevant to the Books and Records the Plaintiff Would Be Entitled to Inspect after Establishing a Proper Purpose for Inspection at Trial

Grimes and *Kaufman* undeniably establish that the existence of such a special litigation committee report affects the scope of books and records a Section 220 plaintiff can inspect. When a books and records action is brought with the goal of evaluating a possible derivative suit, as here, "the books and records that satisfy the action are those that are required to prepare a well-pleaded complaint." *Kaufman*, 905 A.2d at 753. More

[1] Plaintiff repeatedly quotes a sentence from the District Court's decision that was subsequently withdrawn by the District Court, by Order dated May 13, 2008. (Opposition at 3, 9-10). The modified Order makes it clear that there have been no findings as to the existence of misleading statements. The modified Order reads in pertinent part as follows:

> Plaintiff's allegations that the Individual Defendants had knowledge of the alleged inventory surplus and unusual promotional activity create a strong inference of recklessness given the alleged false and/or misleading public statements that this Court has already determined were plead with sufficient particularity to survive a motion to dismiss.

See May 13, 2008 Letter Order withdrawing previously issued Memorandum Opinion (Exhibit D).

to the point, in Section 220 cases involving investigations by independent committees, the committees "report, minutes of the meetings of the Special Committee, and minutes of any meeting of the board relating to the creation or functioning of the Special committee, including any meeting of the board of directors … should suffice for the purposes of establishing or raising reasonable grounds for suspicions about a special committee's independence, good faith, and due care." *Grimes* 724 A.2d at 567. Plaintiff's argument that the Company's SLC Report is not legally relevant is contrary to law.

C. The Hypothetical Future "Demand-Excused" Derivative Action Plaintiff Wishes to File Is Barred by the Ruling of the United States District Court for the District of Maryland in a Prior Shareholder Derivative Action Addressing the Same Underlying Conduct

This Court has recognized that the failure of a prior plaintiff to pursue a Section 220 demand will not prevent application of issue preclusion principles to allegations of demand futility by a second derivative plaintiff. *In re Career Education Corp. Deriv. Litig.*, 2007 Del. Ch. LEXIS 184, *34 & n.58 (Sept. 28, 2007) (Exhibit E). As observed in *West Coast Management & Capital, LLC v. Carrier Access Corporation*, "recent federal case law . . . holds that collateral estoppel bars all subsequent plaintiffs from relitigating demand futility." 914 A.2d at 643 (citing *Leboyer v. Greenspan*, 2006 WL 2987705, at *1 (C.D. Cal. Oct. 16, 2006), *Henik ex rel. LaBranche & Co. Inc. v. LaBranche*, 433 F.Supp.2d 372, 381 (S.D.N.Y. 2006), and *In re Sonus Networks, Inc. S'holder Deriv. Litig.*, 422 F.Supp.2d 281, 294 (D. Mass. 2006)) (internal citations omitted). Thus, Plaintiff is estopped from relitigating demand futility under the doctrine of issue preclusion.

CONCLUSION

For all the foregoing reasons, Defendant Jos. A. Bank, Clothiers, Inc. and non-party directors William E. Herron, Sidney H. Ritman and Andrew A. Giordano respectfully request that the Court enter an order prohibiting Plaintiff from taking any of the discovery it requests.

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