



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. )

**PLAINTIFF'S REPLY BRIEF IN FURTHER  
SUPPORT OF ITS MOTION FOR SUMMARY JUDGMENT**

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Plaintiff Norfolk County Retirement System (“Norfolk”) respectfully submits this Reply Memorandum of Law in Further Support of Its Motion for Summary Judgment.

### **INTRODUCTION**

Summary judgment should be entered on behalf of Norfolk, as no genuine issues of material fact exist and it is entitled to judgment as a matter of law. In opposing plaintiff’s summary judgment motion, defendant primarily makes three arguments, each of which is unavailing. First, defendant argues that plaintiff does not have a “proper purpose” in asserting this *Section 220*<sup>1</sup> action because, supposedly, the report of its Special Litigation Committee (the “SLC Report”) rebuts the two decisions of the federal court in *Lefkoe v. Jos. A. Bank Clothiers*, Civ. No. WMN-06-1892 (D. Md.) (the “*Lefkoe* Action”). By those decisions, the court in that federal securities fraud class action twice sustained the complaint against defendant Jos. A. Bank Clothiers, Inc. (“Jos. A. Bank” or the “Company”) and certain of its officers and directors.<sup>2</sup> Contrary to defendant’s argument, reliance upon the federal court’s findings – including that of a “strong inference of scienter” – allows plaintiff to easily meet the applicable “credible basis” standard, which is the *lowest* possible burden of proof. As the Delaware Supreme Court has held, to show a proper purpose under *Section 220*, a plaintiff does not need to show

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<sup>1</sup> References to “*Section 220*” are to 8 *Del. C.* § 220.

<sup>2</sup> The two Memorandum Opinions from the *Lefkoe* Action referenced herein each have been provided to the Court in connection with previous submissions by plaintiff. The *Lefkoe* Court’s May 1, 2008 Memorandum (the “May 1 Mem.”) was attached as Exhibit 2 to the Transmittal Affidavit of Brian D. Long, Esquire, in Support of Plaintiff’s Motion for Summary Judgment. The *Lefkoe* Court’s September 10, 2007 Memorandum (the “Sept. 10 Mem.”) was attached as Exhibit C to Plaintiff’s Opposition to Defendant’s Motion for Summary Judgment.

that mismanagement is actually occurring, it need only show that “there is possible mismanagement that would warrant further investigation – a showing that may ultimately fall well short of demonstrating that anything wrong occurred.” *Seinfeld v. Verizon Commc’ns, Inc.*, 909 A.2d 117, 123 (Del. 2006) (quotations omitted). Here, plaintiff has more than done so.

Defendant next argues that the dismissal of an earlier, unrelated derivative suit (*In re Jos. A. Bank Clothiers, Inc. Deriv. Litig.*, Civ. No. L-06-2095, slip op. (D. Md. Sept. 13, 2007)) collaterally estops plaintiff from asserting this *Section 220* action. However, as this Court has held, when a subsequent plaintiff “makes substantially different allegations of demand futility based on additional information, issue preclusion, from both a logic and fairness standpoint, would not apply.” *West Coast Mgmt. & Capital, LLC v. Carrier Access Corp.*, 914 A.2d 636, 643 n.22 (Del. Ch. 2006). Issue preclusion plainly does not apply to this *Section 220* action. To the extent defendant is seeking to apply that doctrine to an as-yet unfiled derivative action, it has jumped the gun. Obviously, the Court will not know if Norfolk can make substantially different demand futility allegations based on additional information gathered here until Norfolk has actually asserted those allegations in a derivative complaint.

Third, defendant argues that *Grimes v. DSC Commc’ns Corp.*, 724 A.2d 561 (Del. Ch. 1998), and *Kaufman v. CA, Inc.*, 905 A.2d 749 (Del. Ch. 2006), limit the scope of documents obtainable in this action to the documents it already has provided. *Grimes* and *Kaufman*, however, stand for the unexceptional and settled proposition that a court must tailor the scope of production to the plaintiff’s *stated* purpose. Here, plaintiff’s

stated purpose is *not* the same as the stated purpose was in either *Grimes* or *Kaufman*. The result, therefore, should not be the same. Contrary to defendant’s argument and consistent with these cases and *Section 220*, Norfolk seeks documents that are tailored to its stated purpose here, not the stated purpose in either *Grimes* or *Kaufman*.<sup>3</sup>

## **ARGUMENT**

### **I. NORFOLK ASSERTS A PROPER PURPOSE**

The principles underlying the propriety of Norfolk’s purpose, as well as its entitlement to inspect Company books and records, are well-developed and well articulated. Namely, “[i]t is well established that a stockholder’s desire to investigate wrongdoing or mismanagement is a ‘proper purpose.’” *Seinfeld*, 909 A.2d at 121 (footnotes omitted).

Under Delaware law, “[a] stockholder is not required to prove by a preponderance of the evidence that waste and [mis]management are actually occurring. Stockholders need only show, by a preponderance of the evidence, a credible basis from which the Court of Chancery can infer there is possible mismanagement that would warrant further investigation – a showing that may ultimately fall well short of demonstrating that anything wrong occurred. That threshold may be satisfied by a credible showing, through documents, logic, testimony or otherwise, that there are legitimate issues of wrongdoing.” *Id.* at 123 (footnotes and quotations omitted). “[T]he ‘credible basis’ standard sets the lowest possible burden of proof,” *id.*, but, at the same time,

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<sup>3</sup> Defendant does not argue that Norfolk has not complied with the technical requirements set out in *Section 220*. And, in fact, the complaint in this action and the exhibits thereto demonstrate that plaintiff has met such requirements.

“safeguard[s] the right of the corporation to deny requests for inspection that are based only upon suspicion or curiosity.” *Id.* at 118 (footnote omitted).

Public policy also supports plaintiff’s inspection demand. Indeed, “the Delaware Supreme Court has made it clear that the public policy of this State is to encourage stockholders to utilize *Section 220* before filing a derivative action.” *Freund v. Lucent Tech.*, 2003 Del. Ch. LEXIS 3, at \*13 (Del. Ch. Jan. 9, 2003). This should be done “in order to meet the heightened pleading requirements of Court of Chancery Rule 23.1 that are applicable to such actions.” *Id.*

Here, plaintiff’s *Section 220* demand – and this action – clearly are based on more than mere “suspicion or curiosity.” Likewise, Norfolk’s desire to inspect Company books and records is based on more than just the *complaint* in the *Lefkoe* Action. *See, e.g.*, Answering Brief of Jos. A. Bank Clothiers, Inc. in Opposition to Plaintiff’s Motion for Summary Judgment (cited as “Def. Opp. Br.”) at 1, 3, 11, 12. Rather, plaintiff has based its inspection demand on two *decisions* in the *Lefkoe* Action in which a United States District Judge held that the *Lefkoe* complaint stated a claim and was not subject to dismissal. In these decisions, the federal court held, among other things, that:

- The plaintiffs had adequately alleged that “on approximately 12 separate occasions, defendants affirmatively misrepresented inventory issues and omitted from public statements their knowledge of the Company’s excessive levels of inventory over the class period, its need to steeply discount inventory, and the resulting harm to sales of core merchandise and the Spring 2006 line.” Sep. 10 Mem. at 11-12.
- The plaintiffs had adequately alleged that defendants’ “statements and omissions were fraudulent or misleading because they concealed the fact that the Company’s inventories of Fall/Winter 2005 merchandise had swelled to unprecedented levels, forcing the Company to take drastic action to liquidate the merchandise.” *Id.* at 12.

- The plaintiffs had adequately alleged that “Defendant Ullman knew ‘that gross profit margins were dramatically decreasing due to the steep price discounts, virtually continuous sales, and other aggressive pricing strategies undertaken by the Company to alleviate the excessive Fall/Winter 2005 inventories.’” *Id.* at 12-13.
- The plaintiffs had adequately alleged that defendants’ statements and omissions “concealed the fact that the Company’s inventories of Fall/Winter 2005 merchandise had swelled to unprecedented levels, forcing the Company to take drastic action to liquidate the merchandise.” *Id.* at 12.
- The plaintiffs had adequately alleged “specific statements concerning forecasts of growth in earnings and sales, and confidence in inventory . . . . The plaintiffs have also alleged specific failures to disclose the excessive inventory build-up and the resultant need to engage in steep discounting.” *Id.* at 14.
- The plaintiffs had adequately alleged “facts sufficient to support an inference of scienter at least as compelling as any opposing inference,” *id.* at 17, including “Defendant Wildrick’s sale of 74% of his common stock in the Company during the class period, for an alleged profit of \$36 million.” *Id.* at 16.
- The plaintiffs had adequately alleged “facts sufficient to support an inference of scienter at least as compelling as these opposing inferences. Individual Defendants’ knowledge of the alleged inventory surplus and unusual promotional activity creates a strong inference of recklessness given the public statements found to be false and/or misleading during the Class Period.” May 1 Mem. at 20.

These determinations, especially the federal court’s finding of a “strong inference of recklessness,” demonstrate that Norfolk has shown a “credible basis” in this action, thereby easily satisfying this “lowest possible burden of proof.”<sup>4</sup>

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<sup>4</sup> Given plaintiff’s minimal evidentiary burden, the limited issues before the Court, and the strength of plaintiff’s evidence, this action is ripe for summary adjudication. *See Compaq Computer Corp. v. Horton*, 631 A.2d 1 (Del. 1993) (affirming grant of summary judgment in *Section 220* action, finding plaintiff asserted a proper purpose); *Freund*,

The SLC Report does not – and indeed cannot – rebut the showing that plaintiff has made. Defendant’s arguments in that regard, therefore, are unpersuasive. As the Delaware Supreme Court has indicated, plaintiff does not need to show that mismanagement is actually occurring, it need only show that “there is possible mismanagement that would warrant further investigation – a showing that may ultimately fall well short of demonstrating that anything wrong occurred.” *Seinfeld*, 909 A.2d at 123 (footnotes and quotations omitted). Here, regardless of the SLC Report’s contents, the federal court’s findings in its two decisions upholding the federal class action complaint easily meet the “credible basis” standard, which can be satisfied “through documents, logic, testimony or otherwise.” *Id.*<sup>5</sup>

Finally, contrary to defendant’s argument, plaintiff *does not* “stand[] in virtually the same shoes as the potential derivative plaintiff who made a Rule 23.1 demand.” *See* Def. Opp. Br. at 6. Simply because Norfolk *may* commence a derivative action *if* it obtains documents that lead it to conclude that a derivative action *is* warranted, does not

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2003 Del. Ch. LEXIS 3 (granting summary judgment to plaintiff, finding proper purpose asserted).

<sup>5</sup> Plaintiff bases its action on the *Lefkoe* court’s *two* decision upholding the federal plaintiffs’ complaint, as well as the findings of that court. No testimony is necessary to establish the reliability of these two opinions. They are what they appear to be, and defendants cannot dispute their reliability. On the other hand, the existence and hearsay conclusions of the SLC Report, in and of themselves do nothing to counteract the “credible basis” that is established by the federal court’s decisions (irrespective of the reliability of the SLC Report). Despite these facts, defendants have stated in open court that are going to rely exclusively on the hearsay SLC Report. *See* July 18, 2008 Transcript at 10 (“We can have a very short trial. We can tender the SLC Report. But that is all we are going to do, is authenticate it as a trial exhibit . . . . I don’t think the record would be any different than it is as we are standing here today.”) attached as Exhibit A to the Opening Brief of Defendant Jos. A. Bank Clothiers, Inc. in Support of its Motion for Summary Judgment.

mean that it currently has decided to or will do so. As such, plaintiff cannot, and should not, be held to the standards of a plaintiff in a hypothetical derivative action that plaintiff has not even decided to commence.

## **II. COLLATERAL ESTOPPEL DOES NOT BAR THIS SECTION 220 ACTION**

Unless and until plaintiff obtains additional information and commences a derivative action on the basis of that information, there is no way to consider whether an earlier-filed, unrelated derivative action precludes plaintiff's hypothetical derivative claims. Defendant, in its opening brief in support of its motion for summary judgment (Point II) and briefly in its opposition to plaintiff's motion (Point IC), argues that the dismissal of an earlier, unrelated derivative suit collaterally estops plaintiff from prosecuting this *Section 220* action. However, as explained more fully in plaintiff's brief in opposition to defendant's motion (Point II), the imagined merits of a hypothetical future derivative action do not determine whether plaintiff is entitled to inspect documents pursuant to *Section 220*. As this Court has stated: "While a prior suit by another plaintiff with similar allegations of demand futility may bar a second plaintiff from filing the same suit, if the second plaintiff makes substantially different allegations of demand futility based on additional information, issue preclusion, from both a logic and fairness standpoint, would not apply." *West Coast Mgmt.*, 914 A.2d at 643 n.22.

## **III. THE SCOPE OF DOCUMENTS NORFOLK SEEKS IS APPROPRIATE**

### **A. *Grimes* and *Kaufman* Do Not Limit the Scope of Production**

As demonstrated in Plaintiff's Opposition to Defendant's Motion for Summary Judgment at 4-6, neither *Grimes* nor *Kaufman* limit the scope of production here to the

SLC Report and the few other documents that defendant has produced. In *Grimes* the Court tailored the scope of production to those documents that are “essential to achieving [plaintiff’s] stated purpose as required by Section 220.” *Grimes*, 724 A.2d at 567. (Emphasis added). Given the specific, stated purpose in that particular case, which related solely to the Special Litigation Committee, the Court held that plaintiff was entitled to that committee’s report and minutes related to the committee.<sup>6</sup> *Id.*

In *Kaufman*, the stated purpose was different than in *Grimes*, and, unsurprisingly, so was the result. Thus, in *Kaufman*, the stated purpose was to investigate specific misconduct related to the company’s giving releases to certain individuals related to a settlement of an ERISA class action. *See Kaufman*, 905 A.2d at 751. In response to the plaintiff’s Section 220 action, the defendant in *Kaufman* voluntarily agreed to produce the requested documents, *id.*, which included the following “wide range of documents”:

- (1) lightly redacted copies of minutes of meetings of CA’s board of directors and Audit Committee from April 1, 1998 through April 30, 2004;
- (2) correspondence between CA’s former counsel, Wachtell, Lipton, Rosen & Katz (“WLRK”), and the government concerning the government investigation of CA’s past accounting practices;
- (3) chronologies of 42 CA license agreements CA entered into during CA’s fiscal year 2000 for which CA prematurely recognized the associated revenue
- (4) summaries of the five Audit Committee interviews of Kumar and Richards; and
- (5) talking points prepared by WLRK in connection

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<sup>6</sup>The stated purpose in *Grimes* was to investigate “the formation, investigation and report of the Special Committee . . . [and] the DSC board’s decision to accept the Special Committee’s recommendation.” *Grimes*, 724 A.2d at 563. Defendant misses the point when it attempts to limit the scope of production here by stating, “This case, like *Grimes*, necessarily implicates the determinations of an SLC.” Def. Opp. Br. at 4. What defendant fails to acknowledge is that plaintiff’s stated purpose here is different than in *Grimes*, and, therefore, the inspection here should be “tailored” to that different stated purpose. Significantly, in *Grimes*, the plaintiff was not seeking documents in his Section 220 action concerning his underlying claim that the CEO’s compensation package should be rescinded. *See Grimes*, 724 A.2d at 564-65.

with oral briefings to the government and to CA's board of directors concerning the government investigation.

*Id.* at 751-52. The Court found these documents to be sufficient to allow the plaintiff to investigate the potential misconduct related to the releases. *See id.* at 754. After providing these documents to the plaintiff, the defendant offered to produce "voluminous quantities of other documents." *Id.* at 754. However, the Court found that "many of these [other] documents *are not responsive to the demand*, as they provide information more relevant to the subject of the settled 2003 suits than to the new questions raised by the releases." *Id.* (emphasis added). Thus, the Court in *Kaufman* did nothing more than what the Court did in *Grimes*, which was to tailor the scope of production to the plaintiff's *stated* purpose. Here, plaintiff's stated purpose is *not* the same as the stated purpose was in either *Grimes* or *Kaufman*. Therefore, the result should not be the same. As demonstrated below (and in plaintiff's opening papers and in opposition to defendant's motion), Norfolk seeks documents that are tailored to *its* stated purpose, as required by *Section 220* and the cases interpreting that statute, including both *Grimes* and *Kaufman*.

**B. Norfolk Seeks Documents that Are "Necessary and Essential" to its Stated Purpose**

As with Defendant's Summary Judgment Motion, Defendant's Opposition to Plaintiff's Summary Judgment Motion seeks to mischaracterize plaintiff's demand as overly burdensome. Thus, in a flourish of hyperbole, defendant incorrectly states that "Norfolk is seeking to inspect not only numerous documents that essentially would allow it to try to replicate the Special Litigation Committee's investigation, but also documents

that have nothing to do with that investigation but instead seem to be an attempt to second-guess the Company's entire business model and internal control structure." Def. Opp. Br. at 3. On the contrary, and as explained in Plaintiff's Opposition to Defendant's Summary Judgment Motion, plaintiff seeks only "Board Materials" related to the allegations in the federal class action that the federal court sustained. The Company's corporate secretary should easily be able to gather these documents. Aside from not being burdensome, the categories of documents that plaintiff seeks are, as required, tailored to plaintiff's stated purpose. Thus, plaintiff seeks Board Materials concerning the Company's inventory levels, pricing strategies, accounting, and auditing, and any investigation concerning these issues. These are the issues that surrounded the allegations that the federal court found compelling when it twice upheld the complaint in the federal class action.

### **CONCLUSION**

For the foregoing reasons and those set forth in its previous submissions, plaintiff respectfully requests that the Court grant its motion for summary judgment.

Dated: October 17, 2008

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