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.	)	

ANSWERING BRIEF OF JOS. A. BANK CLOTHIERS, INC. IN OPPOSITION TO PLAINTIFF'S MOTION FOR SUMMARY JUDGMENT

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PRELIMINARY STATEMENT

Plaintiff Norfolk County Retirement System ("Norfolk") moves for summary judgment to obtain every single document demanded in its initial demand letter without acknowledging its "burden of proving that each category of books and records is essential to the accomplishment of the stockholder's articulated purpose for the inspection." *Security First Corp. v. U.S. Die Casting and Dev. Co.*, 687 A.2d 563, 569 (Del. 1997). Nor does Norfolk acknowledge that it has already received the report of the special litigation committee of Jos. A Bank Clothiers, Inc. (the "SLC" of the "Company"), the exhibits to that report and the related Board and SLC minutes -- the "basic documents [that] 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 v. DSC Commc'ns Corp.*, 724 A.2d 561, 567 (Del. Ch. 1998), *quoted in Kaufman v. C.A., Inc.*, 905 A.2d 749 (Del. Ch. 2006) ("*Kaufman II*"). Since Norfolk has not articulated any facts sufficient to establish that any other documents are essential to Norfolk's purposes, Norfolk cannot establish that it is entitled to summary judgment as a matter of law.

Further, Norfolk has not identified undisputed facts sufficient to establish a "credible basis" from which the Court can infer mismanagement, waste or wrongdoing. The allegations of the federal securities complaint on which Norfolk relies, far from being undisputed, have been comprehensively refuted by the findings of the SLC. In the absence of any undisputed facts forming a credible basis of inferable wrongdoing, Norfolk is not entitled to summary judgment.

STATEMENT OF FACTS

Through this 220 action, Norfolk seeks documents that would enable it to file a derivative action concerning what it allegedly suspects was wrongdoing by Company management surrounding the drop in the Company's stock price in June of 2006. (*See* 220 Complaint ¶¶ 7A, B & C.) The only identified basis for Norfolk's inspection demand is the set of unproven allegations in a single federal securities class action complaint. (*See* 220 Complaint ¶¶ 14-25; Norfolk Mot. ¶ 10.) That federal complaint asserts that the drop in stock price was caused by senior management's attempt to conceal excessive inventory by conducting liquidation sales, and that in connection with that concealment the Company issued allegedly false and misleading statements concerning its financial condition. (*See* SLC Report at 2 & Ex. 2 at 1-4; 220 Complaint at pp.6-7.)[1] The allegations of the federal securities complaint are nothing more than that – allegations.

After an investigation into the claims of wrongdoing concerning the drop in the Company's stock price in 2006 – the same subject matter that Norfolk seeks to investigate – an SLC formed by the Company's Board at the behest of a Company stockholder concluded that the allegations set forth in the federal securities complaint are simply untrue. The SLC found, among other things, that the Company's Fall/Winter 2005 inventory was not excessive (SLC Report at 26-31); there was no unprecedented effort to slash prices at the Company in the first quarter of 2006 because there was no need to do so (SLC Report at 31-36); the Company's inventory was never impaired and

[1] The SLC Report and the exhibits thereto are attached as Exhibit A to the Transmittal Affidavit of Sean Brennecke, dated September 10, 2008 ("Brennecke Aff."), and are referenced hereafter as "SLC Report at __".

its financial statements comported with GAAP (SLC Report at 36-40); and statements by senior management at the Company relating to the Company's financial condition were accurate, not false and misleading as alleged (SLC Report at 40-43).

Despite having received the SLC Report, the exhibits thereto and the related Board and SLC minutes, Norfolk is seeking to inspect not only numerous documents that essentially would allow it to try to replicate the SLC'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. For example, Norfolk seeks inspection of documents concerning the Company's financial data reporting procedures and controls, inventory management procedures and controls, and pricing strategies for the period June 1, 2005 through June 15, 2006, as well as documents relating to the Company's audit procedures and controls. (*See* 220 Complaint ¶ 6.)

Norfolk has failed entirely to adduce facts to challenge the independence or good faith of the SLC or the reasonableness of its investigation. Indeed, Norfolk's own witness acknowledged that he has no basis to suspect wrongdoing on the part of the SLC. (*See* Brennecke Aff. Ex. E at 30-36.)

Instead, Norfolk asserts that the securities class action complaint "pleads specific and compelling facts leading to a strong inference that the [Company's senior corporate officers] made … multiple, material misstatements [concerning the Company's inventory during the class period] with the intent to defraud." (Norfolk Mot. ¶ 10.) Norfolk fails to acknowledge that those bare allegations have been affirmatively refuted by the SLC. Thus, the "undisputed facts" on which Norfolk relies are not facts at all for summary

judgment purposes; they are simply allegations that have already been refuted in a comprehensive SLC investigation that is entitled to deference under Delaware law.

ARGUMENT

Summary judgment is awarded only "when there are no material issues of fact in dispute and the moving party is entitled to judgment as a matter of law. In evaluating the record, the court will view the facts in a light most favorable to the nonmoving party, accepting as true unconverted facts from the record. . . . [T]he moving party bears the burden of proof in showing that there are no questions of material fact[.]" *Freund v. Lucent Tech., Inc.*, 2003 Del. Ch. LEXIS 3, *6 (Jan. 9, 2003) (footnotes omitted) (Ex. A).

I. NORFOLK HAS FAILED TO DEMONSTRATE THAT IT IS ENTITLED TO JUDGMENT AS A MATTER OF LAW

A. *Grimes* and *Kaufman II* Confirm that Norfolk Already Possesses Those Documents Necessary and Essential to Its Stated Purpose

This case is governed by *Grimes* and *Kaufman II*, and these cases demonstrate that Norfolk is not entitled to judgment as a matter of law. *Kaufman II* makes clear that "relief under Section 220 is limited only to the inspection of books and records that are necessary and essential to the satisfaction of the stated purpose." 905 A.2d at 753. 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." *Id.*

This case, like *Grimes*, necessarily implicates the determinations of an SLC. The SLC determined that the claims it investigated are meritless and that pursuit of them is not in the best interests of the Company. (SLC Report at 54-56) Those determinations stand as a bar to Norfolk's ultimate goal of pursuing a derivative action, unless Norfolk can establish a reason why the SLC's determinations are not owed deference.

Kaufman II quotes *Grimes* for the proposition that certain categories of "basic documents should suffice for the purposes of establishing or raising reasonable grounds for suspicions about a special committee's independence, good faith, and due care." *Id.* at 754 (quoting *Grimes*, 724 A.2d at 567). Those documents are "the committee's '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.'" *Id.* (quoting *Grimes* 724 A.2d at 567). A "further showing of need" is required for the production of any additional documents. *Id.*

Norfolk has not articulated such a need. Norfolk has come forward with no evidence to raise even the slightest grounds for suspicions about the SLC's independence, good faith, and due care. Rather, representatives of Norfolk and it investment advisors have affirmatively testified that they are not aware of any facts that would cast doubt on the independence, good faith, and due care of the SLC, or the thoroughness and objectiveness of its investigation and Report. (Company's Op. Br. at 9-10.) Norfolk has also failed to show why the documents it has already received do not suffice for its articulated purpose, and failed to articulate a reasonable need to inspect any additional records. As a result, it is not entitled to summary judgment.

Norfolk attempts unsuccessfully to distinguish *Grimes* and *Kaufman II*, and maintains that they do not limit the scope of documents Plaintiff can inspect in this action. (Norfolk Mot. at 9-12.) Both cases, however, directly address the issue before this Court, which is whether Norfolk is entitled to inspect additional documents beyond those it has already received.

Norfolk's argument that *Grimes* does not apply in this case because the plaintiff in *Grimes* was in a "unique and different position" than Norfolk, and because its stated purpose for seeking documents was "markedly different," is simply contrary to fact. Norfolk's stated purpose for inspection of the Company's books and records might be articulated differently than the purpose stated in *Grimes*, but in practice it is the same. Norfolk's stated purposes for inspection are to investigate whether the wrongdoing alleged in the securities action occurred, to assess the ability of the Company's Board to impartially consider a demand for action related to that wrongdoing, and to take action in the event the Board did not properly discharge its fiduciary duties. (220 Complaint ¶ 7A-C.) In other words, Norfolk wants to inspect the Company's records for the purpose of evaluating and bringing a derivative action on the wrongdoing suspected. (Company Op. Br. at 14-15.) In order to do so Norfolk must challenge the business judgment of the SLC, just as the plaintiff in *Grimes* was required to do, and, as a result, Norfolk is "not entitled to receive or examine copies of other documents not directly relating to the Special Committee's conclusions and recommendations unless it can articulate a reasonable need to inquire further after review of those basic documents." *Grimes*, 724 A.2d at 567.

Put differently, Norfolk stands in virtually the same shoes as the potential derivative plaintiff who made a Rule 23.1 demand on the Board of the Company respecting the same potential claims and learned that the SLC had determined that it was not in the best interests of the Company to pursue claims the SLC found to be meritless. (Brennecke Aff. Ex. C.) Just as that derivative plaintiff would need to overcome the decision of the SLC to refuse the demand if he decided to pursue a derivative action,

Norfolk must overcome the business judgment of the SLC if Norfolk decides to pursue a derivative action, since Norfolk would face a future motion by the SLC to terminate any such litigation. This case is therefore controlled by *Grimes* and the documents it is allowed to inspect are limited to those it already has.

Kaufmann II is likewise applicable. The substantive issue before the Court in *Kaufman II* was the same as the issue before this Court -- whether the defendant should be compelled to produce documents "well outside the traditional reach of Section 220 as articulated in *Grimes*." 905 A.2d at 754. Here, as in *Kaufman II*, "[i]n compliance with *Grimes*, . . . the plaintiff has been given a wide range of basic documents that should provide [Norfolk] with a substantial basis to investigate potential misconduct . . . ." *Id.* And as in *Kaufman II*, Norfolk is not entitled to inspect additional documents, because "[i]n the face of that presumption [about the sufficiency of the basic documents described in *Grimes*], plaintiff has not explained, either in her papers or at oral argument, why the remaining documents are either necessary or essential to her proper investigative purpose under Section 220." *Id*. at 754-755.

In short, just as *Grimes* and *Kaufman* define the scope of any inspection for purposes of the Company's motion for summary judgment (*see* Company's Op. Br. at 12-17), those same cases are a bar to Norfolk's motion for summary judgment.

B. *Kaufman I* Is Irrelevant

Norfolk asserts that it "follows *a fortiori* from the holding in [*Kaufman v. Computer Assocs. Int'l Inc.*, 2005 Del. Ch. LEXIS 192 (Dec. 21, 2005) ("*Kaufman I*"),]" that the determination of the SLC has no bearing on its inspection demand. (Norfolk Mot. ¶ 19.) *Kaufman I* does not support Norfolk's motion for summary judgment. In

Kaufman I, the defendant sought a stay of the 220 action pending the outcome of a SLC investigation on the ground that the inspection would interfere with the Company's right to control litigation underlying the 220 demand. The Court in *Kaufman I* denied the request for a stay, reasoning that the burden on the Company to produce the discrete set of documents sought would be light and would not unreasonably distract the SLC from its primary task of investigating the claims made by the derivative plaintiff. *See Kaufman I*, 2005 Del. Ch. LEXIS 192, at *4.

The denial of a stay in *Kaufman I* pending the outcome of a SLC investigation says nothing about the situation in which the SLC has completed its investigation, determined there was no wrongdoing as alleged by Norfolk, provided Norfolk with the SLC Report and related basic documents, and where Norfolk can adduce no facts to challenge the independence and thoroughness of the SLC, its investigation or its Report. The fact that the Court in *Kaufman II* rendered its decision based on "the same principles" as *Grimes*, 905 A.2d at 754, despite the prior denial of a stay in *Kaufman I*, makes clear that the operative question now is whether Norfolk is entitled to anything more than the "basic documents" described in *Grimes*, without regard for whether a stay would have been appropriate at an earlier date.

C. Norfolk Has Articulated No Basis to Allege Demand Futility

Norfolk also argues that its inspection is not barred by issue preclusion. (Norfolk Mot. ¶ 25.) But as discussed in the Company's opening brief in support of summary judgment, Norfolk has never articulated a factual or legal basis to overcome the prior adjudication that a majority of the Company's Board is independent. (*See* Company's Op. Br. at 17-18.) Norfolk makes no such effort in its motion for summary judgment. It

simply makes no sense to allow Norfolk to impose the burden and expense of a massive books and record inspection into the events of 2005 and 2006 when Norfolk has no credible basis to overcome Judge Legg's prior decision that the Company's Board, including the members of the SLC, are independent and capable of analyzing a pre-suit demand.

II. NORFOLK HAS NOT IDENTIFIED ANY EVIDENCE CONSTITUTING A CREDIBLE BASIS FROM WHICH WRONGDOING CAN BE INFERRED, MUCH LESS THE ABSENCE OF ANY GENUINE ISSUE OF FACT

Norfolk erroneously argues that "there are no disputed issues of fact respecting the proper purpose of [its] Complaint." (Norfolk Mot. ¶ 5.) To the contrary, Norfolk cannot obtain judgment in this case because it has not presented any evidence, much less the lack of any genuine dispute of fact respecting such evidence, that would suggest "a credible basis from which the court can infer that mismanagement, waste or wrongdoing may have occurred." *Seinfeld v. Verizon Commc'ns, Inc.*, 909 A.2d 117, 118 (Del. 2006) (internal quotations omitted). Indeed, the SLC Report refutes the untested allegations on which Norfolk exclusively relies.

Typically, the necessary "credible showing, through documents, logic, testimony or otherwise," is an issue decided after trial, based on a preponderance of the evidence. *Security First Corp.*, 687 A.2d at 568 (affirming finding of credible basis, which was based on "credibility assessments of live witnesses"); *Polygon Global Opportunities Master Fund v. West Corp.*, 2006 Del. Ch. LEXIS 179, at *20 (Oct. 12, 2006) ("at trial Polygon did not carry its burden of showing a credible basis from the court could infer fiduciary misconduct warranting further investigation") (Ex. B); *Mattes v. Checkers Drive-in Rest., Inc.*, 2001 Del. Ch. LEXIS 47, at *13 (Mar. 28, 2001) ("The evidence at

trial did not show a credible basis to find probable wrongdoing on the part of corporate management.") (internal quotation omitted) (Ex. C).

For example, in *Carapico v. Philadelphia Stock Exch., Inc.*, 791 A.2d 787 (Del. Ch. 2000), this Court found after trial that the plaintiff had demonstrated a credible basis to infer wrongdoing where the plaintiff's stated purpose was to investigate "the misconduct identified in the SEC Order and the payment of severance benefits to officers or employees implicated in the SEC inquiry," the "SEC Orders contain detailed information reflecting possible corporate mismanagement," and "trial testimony showed a credible basis to suspect mismanagement sufficient to justify some investigation." *Id.* at 792.

Here, of course, there is no allegation or evidence of any SEC investigation into misconduct by the Company, and no potential trial witness for plaintiff. Moreover, the Company tenders the SLC Report, which refutes any allegations of excess inventory, liquidation sales, impaired inventory, depressed earnings, and false statements. (SLC Report at 3-5, 54)

We are aware of only one case in which a credible basis of inferable wrongdoing was established in the context of a motion for summary judgment, and the facts of that case bear no resemblance to those here. In *Freund v. Lucent Tech., Inc.*, 2003 Del. Ch. LEXIS 3, the plaintiff created a record that included "the SEC's formal investigation into Lucent's accounting practices," "Lucent's revisions of its financial statements for fiscal year 2000," and "commencement of litigation by other shareholders of Lucent following the precipitous decline in the value of Lucent's stock." *Id.* at *9-10. Lucent's

restatement of revenues and profits "resulted from the reversal of sales that, apparently, were improperly recognized." *Id.* at *2-3.

Here, again by way of contrast, there is no such restatement of financials and no such SEC investigation. And unlike the "series of lawsuits [that] were filed against Lucent," which included allegations of the "retaliatory firing of an employee for 'whistle blowing,'" 2003 Del. Ch. LEXIS 3, at *3, here there is only a single federal securities case, and its allegations have been duly investigated and found to be meritless.

Sole reliance on refuted allegations in someone else's complaint does not compare favorably to *Louisiana Mun. Police Employees' Ret. Sys. v. Countrywide Fin. Corp.*, 2007 Del. Ch. LEXIS 138 (Oct. 2, 2007) (Ex. D), *clarified*, 2007 Del. Ch. LEXIS 175 (Dec. 6, 2007), in which the Court identified the "outer limits of the minimal quantum of evidence a shareholder must adduce in order to demonstrate a credible basis to suspect corporate wrongdoing…." *Id.* at *1. The Court ruled that a statistical analysis by a "well-credentialed expert in economics," supported by "his credible testimony at trial," constituted the necessary credible basis. *Id.* at *37. Here, there is no testimony by anyone, and no admissible evidence of any kind, to support the allegations in the federal securities complaint.

To the contrary, the SLC report refutes the allegations of the federal securities complaint. The SLC Report not only has legal standing in itself as the basis for a determination by independent directors that no derivative litigation should be pursued, it consistutes "affirmative rebuttal evidence" that attacks "the sufficiency of the evidence presented by the plaintiff to establish its credible basis to infer possible issues of wrongdoing." *Id.* at *44.

Norfolk presents far less than the "minimal quantum of evidence." To support its demand, Norfolk cannot point to an SEC investigation of the Company, a restatement of the Company's financials, a fact witness, an expert witness, any analysis of publicly available documents, or any analysis of the SLC Report and its exhibits. Rather, as Norfolk's representative admitted, the only event that precipitated the 220 demand was the temporary drop in the Company's stock price in June of 2006; and the only facts that Norfolk cites to support a "credible basis" of wrongdoing are the untested allegations of the securities class action complaint. (*See* the Company's Op.Br. at 9; Norfolk Mot. ¶10.) The untested allegations are not evidence worthy of credit,[2] and the stock price drop is legally insufficient. *Everett v. Hollywood Park, Inc.*, 1996 Del. Ch. LEXIS 2, *18 (Jan. 19, 1996) ("[d]eclines in financial performance, even if substantial, do not, in and of themselves, support and inference of mismanagement.") (Ex. F); *see also Thomas & Betts Corp. v. Leviton Mfg. Co., Inc.*, 681 A.2d 1026, 1031 (Del. 1996) (refusing inspection when presented evidence of "purportedly substandard financial performance, the company's failure to pay dividends, [the] poor cash flow and the company's higher

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[2] In light of the SLC investigation and its findings, the District Court's decisions on the Company's motions to dismiss and for judgment on the pleadings in the securities class action do not provide Norfolk with undisputed facts required to obtain summary judgment in this case. (Norfolk Mot. ¶¶ 1, 2, 13.) There have been no findings in that case as to the existence of misleading statements by Company management, only an assessment of the adequacy of unproven allegations. (*See* Order of May 13, 2008, and Mem. Op.) (Ex. E).

Further, the standard for dismissal on both of the Company's motions in the securities class action is entirely different than the standard Norfolk must meet on summary judgment. *See* Del. Ch. Ct. R. 56(c). While it is entirely appropriate for this Court to consider the facts established by the SLC's Report in this action, the District Court in the securities class action declined to do so on the Company's preliminary motions. (Ex. E at 12-13.) Because of the vastly different procedural postures in the two matters, the District Court's decision not to consider the SLC Report has no relevance to this Section 220 action.

than average expenses"). Given that Norfolk has not established the "minimum quantum of evidence," Norfolk can only be seen as asking this Court to allow inspection based on its suspicion and mere curiosity, which Delaware law forbids. *Seinfeld*, 909 A.2d at 118.

CONCLUSION

For all the foregoing reasons, Defendant Jos. A. Bank, Clothiers, Inc. respectfully requests that the Court deny Plaintiff's Motion for Summary Judgment.

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