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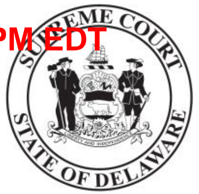


**IN THE SUPREME COURT OF THE STATE OF DELAWARE**

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|---|---|
| LABORERS' DISTRICT COUNCIL CONSTRUCTION INDUSTRY PENSION FUND and HALLANDALE BEACH POLICE OFFICERS AND FIREFIGHTERS' PERSONNEL RETIREMENT FUND, derivatively on behalf of LULULEMON ATHLETICA INC.,<br><br>Plaintiffs Below,<br>Appellants<br><br>v.<br><br>ROBERT BENSOUSSAN, MICHAEL CASEY, ROANN COSTIN, CHRISTINE M. DAY, WILLIAM H. GLENN, MARTHA A.M. MORFITT, RHODA M. PITCHER, THOMAS G. STEMBERG, JERRY STRITZKE, EMILY WHITE and DENNIS J. WILSON,<br><br>Defendants Below,<br>Appellees<br><br>– and –<br><br>LULULEMON ATHLETICA INC., a Delaware Corporation,<br><br>Nominal Defendant Below,<br>Nominal Appellee. | No. 358, 2016<br><br>COURT BELOW:<br><br>COURT OF CHANCERY OF THE STATE OF DELAWARE,<br>C.A. No. 11293-CB |

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## NATURE OF PROCEEDINGS

This stockholder derivative action on behalf of lululemon athletica inc. ("lululemon") challenges stock sales in June 2013 by Dennis J. Wilson, lululemon's founder and at the time the chairman of lululemon's board of directors. Plaintiffs allege an insider trading claim against Mr. Wilson under *Brophy v. Cities Servs. Co.*[1] and a claim that lululemon's other directors breached their fiduciary duties by not investigating and pursuing the *Brophy* claim. It is undisputed that a Rule 10b5-1 trading plan was in place pursuant to which Mr. Wilson's broker at Merrill Lynch had sole discretion to sell stock in amounts and at prices set by the plan, and that the timing, amounts and prices of Merrill Lynch's sales coincided with the plan. Lululemon's directors are not alleged to have profited from Mr. Wilson's stock sales or to have been controlled by Mr. Wilson, and they are protected by lululemon's charter from liability for duty of care violations. Mr. Wilson left lululemon's board five months before this action was commenced.

Chancellor Bouchard dismissed the case because plaintiffs' claim that demand is excused is precluded by federal court decisions in New York requiring a demand.[2] Here, moreover, and unlike most decisions finding preclusion in demand futility cases, plaintiffs were heard in New York, spurned an offer to re-argue demand futility in New York in a manner that would have avoided multi-forum litigation, and consented on the record to the relief granted in New York.

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[1] 70 A.2d 5 (Del. Ch. 1949).

[2] *Canty v. Day*, 13 F. Supp. 3d 333 (S.D.N.Y. 2014), *aff'd*, 599 F. App'x 20 (2d Cir. 2015).

## **SUMMARY OF ARGUMENT**

1. Denied. Plaintiffs' claim that demand is excused is precluded under New York law by res judicata (or claim preclusion), as in *City of Providence v. Dimon*, a decision affirmed by this Court earlier this year.[3] Unlike the Arkansas law governing the *Wal-Mart* action also now before this Court,[4] "it is well-established under New York law, and conceded by plaintiffs, that privity exists in derivative actions between different stockholders."[5] Res judicata applies to claims actually litigated and claims that could have been litigated in a first action, and a dismissal for failure to make a demand is res judicata if the dismissal is with prejudice with respect to the need for demand. The New York action was dismissed "without prejudice, *in the event plaintiffs seek to pursue these claims after making a demand on the Board*."[6] Thus, the claim that demand is excused was dismissed with prejudice, and claims *other* than the claim that demand is excused were dismissed without prejudice. Plaintiffs were not, as they claim, "rebuffed" in their attempt to participate in the New York action: defendants *invited* plaintiffs' intervention and offered to allow plaintiffs to argue demand futility in the New York action after plaintiffs' Section 220 action was concluded

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[3] 2015 WL 4594150 (Del. Ch. July 29, 2015), *aff'd*, 134 A.3d 758 (Del. 2016).

[4] *In re Wal-Mart Stores, Inc., Del. Deriv. Litig.*, 2016 WL 2908344 (Del. Ch. May 13, 2016), *appeal pending*, No. 295, 2016.

[5] Opinion ("Op.") at 35 n.77; *see also id*. at 18 ("[p]laintiffs do not dispute that privity exists here"); *id*. at 33 ("[p]rivity is not contested"); Mar. 15, 2016 Transcript at 67 ("we do not contest that") (A599).

[6] *Canty*, 13 F. Supp. 3d at 350 (emphasis added).

in order to avoid multi-forum litigation, the court heard plaintiffs, and *plaintiffs consented on the record to the relief granted in New York.*

2. Denied. The issue whether demand is excused is also precluded by collateral estoppel (or issue preclusion), as in *Asbestos Workers Local 42 Pension Fund v. Bammann*,[7] another decision affirmed by this Court this year. The question whether demand is excused is identical in both cases. Plaintiffs conceded in their motion to intervene in New York that the New York plaintiffs asserted *Brophy* and "failing to investigate" claims "virtually identical" to the plaintiffs' claims here. Plaintiffs contend that the demand issue differs because the New York court applied the *Rales v. Blasband*[8] test for demand futility when *Aronson v. Lewis*[9] in fact governs. *Rales* and *Aronson* are essentially the same, and "minor variations in the application of what is in essence the same legal standard do not defeat preclusion."[10] The New York plaintiffs – with whom plaintiffs are in privity – had a full and fair opportunity to litigate the demand issue. Plaintiffs themselves had their own full and fair opportunity to litigate in New York.

3. Denied. Inadequate representation requires "grossly deficient" representation. This Court in *Pyott v. La. Mun. Police Emps.' Ret. Sys.* rejected a "'fast-filer' irrebuttable presumption of inadequacy" for "derivative plaintiffs who

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[7] 2015 WL 2455469 (Del. Ch. May 21, 2015), *aff'd*, 132 A.3d 749 (Del. 2016).

[8] 634 A.2d 927 (Del. 1993).

[9] 473 A.2d 805 (Del. 1984).

[10] *B&B Hardware, Inc. v. Hargis Indus., Inc.*, 135 S. Ct. 1293, 1307 (2015).

file their complaints without seeking books and records" in the absence of "record support for the . . . premise."[11] There is no record support here. Plaintiffs all but admitted in New York that they could not show grossly deficient representation. The New York plaintiffs' and Delaware plaintiffs' fight to control multi-forum derivative litigation on behalf of lululemon did not render the New York plaintiffs inadequate representatives of lululemon. Plaintiffs cannot collaterally attack a federal court action under the guise of grossly deficient representation when they were heard in the very action they claim was grossly deficient, spurned an offer that would have been allowed argument of demand futility in that action using the fruits of their 220 demand in order to avoid the costs and burdens of multi-forum litigation, and consented on the record to the relief awarded in that action.

4. Demand is not excused by plaintiffs' allegation that disinterested and independent directors did not investigate stock sales made pursuant to a Rule 10b5-1 trading plan after management – of which Mr. Wilson was not a member – concluded that the sales complied with SEC guidelines. Plaintiffs' claim that lululemon's outside directors breached their fiduciary duties by relying on management's conclusion – without verifying that conclusion in a manner resulting in a writing that could be produced in response to a Section 220 demand – is not an inference that logically flows from particularized facts that would excuse demand. *At worst*, plaintiffs allege a breach of the duty of care by directors protected by a charter provision exculpating them from breaches of the duty of care.

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[11] 74 A.3d 612, 618 (Del. 2013).

## STATEMENT OF FACTS

### A. The Parties

Plaintiffs Laborers' District Counsel Construction Industry Pension Fund ("LDC") and Hallandale Beach Police Officers and Firefighters' Personnel Retirement Fund ("Hallandale") allege that they own lululemon common stock.[12]

Nominal Defendant lululemon is a Delaware corporation based in Vancouver, Canada that produces yoga-inspired athletic wear.[13]

Defendant Dennis J. Wilson, lululemon's founder, was the chairman of lululemon's board until May 2014 and a board member until February 2015.[14] In December 2012, Mr. Wilson owned approximately 42.6 million shares, or approximately 29.7%, of lululemon's stock.[15] On January 10-14, May 10-21 and June 4-7, 2013, Mr. Wilson sold 2,392,455 shares, or approximately 5.6% of these shares.[16] This appeal involves only the June 2013 sales, representing less than 1.5% of Mr. Wilson's holdings at the time.[17] In September 2014, subsequent to the conduct challenged in this lawsuit, Mr. Wilson sold 50% of his remaining 40.2 million shares, reducing his ownership to 13.85% of lululemon's shares.[18]

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[12] Complaint ("Compl.") ¶ 10 (A101).

[13] *Id.* ¶ 11 (A101-102).

[14] *Id.* ¶ 22 (A103-104).

[15] *Id.* ¶¶ 30-31 (A107-108); Apr. 25, 2012 Lululemon Form 14A at 41 (B103).

[16] *See* footnotes 26-31 and accompanying text below.

[17] Opening Brief ("Op. Br.") at 5-6.

[18] Aug. 7, 2014 Lululemon Form 8-K Ex. 99.2 (B112).

Defendants Robert Bensoussan, Michael Casey, RoAnn Costin, William H. Glenn, Martha A.M. Morfitt, Rhoda M. Pitcher, Thomas G. Stemberg and Emily White were members of lululemon's board at the time of Mr. Wilson's June 2013 stock sales and eight of the eleven members of lululemon's board on July 15, 2015, the date this action was filed.[19] Plaintiffs do not allege that any of these directors ever served as officers or employees of lululemon.

Defendants Christine M. Day and Jerry Stritzke were members of lululemon's board in June 2013 but not in July 2015.[20] Ms. Day served as lululemon's chief executive officer from June 2008 to December 2013.[21]

### B. <u>Mr. Wilson's 10b5-1 Trading Plan</u>

In December 2012, Mr. Wilson entered into a trading plan under Rule 10b5-1, which "permits insiders to implement written, pre-arranged stock trading plans" that "establish predetermined trading parameters that do not permit the person adopting the plan to exercise any subsequent influence over how, when, or whether to effect trades."[22] The plan provided for the sale of up to 5.7 million of Mr. Wilson's 42.6 million shares: (1) up to 300,000 shares at market prices and (2) up to 5.4 million shares (but no more than one million shares in any month) at prices no less than $81.25 per share.[23] The plan conferred sole discretion to "a

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[19] Compl. ¶¶ 13-20 (A102-103).

[20] *Id.* ¶¶ 23-24 (A104).

[21] *Id.* ¶ 23 (A104).

[22] *Id.* ¶¶ 30-31 (A107-108).

[23] *Id.* ¶¶ 32-33 (A109).

Merrill Lynch trader to use reasonable brokerage judgment, exercising price and time discretion, as to when to execute" sales within the plan's parameters.[24]

Mr. Wilson "ma[d]e the following representations, warranties and covenants": (1) "I will not disclose to any employee of Merrill Lynch . . . any material nonpublic information" and (2) "I will not attempt to exercise any influence over how, when or whether to effect sales of Shares."[25]

### C. Merrill Lynch's Stock Sales Under The Plan

From January 10 to 14, 2013, Merrill Lynch sold the 300,000 shares permitted to be sold at market prices below $81.25 per share.[26]

On May 10, 2013, lululemon's stock price reached the $81.25 trigger price for the first time, and from May 10 to 21 Merrill Lynch sold one million shares, the maximum number of shares permitted to be sold in one month.[27]

On June 4, 2013, lululemon's stock price reached $81.25 for the first time in June, and Merrill Lynch sold 392,455 shares.[28] On June 5 and 6, the stock traded below $81.25 and there were no sales.[29]

On June 5, 2013, Ms. Day informed Mr. Wilson that she intended to

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[24] Rule 10b5-1 Trading Plan §§ 1.1, 2.1 (B072).

[25] *Id.* §§ 6, 6.6, 6.7 (B074-075).

[26] Compl. ¶ 35 (A110).

[27] *Id.* ¶¶ 39, 43 (A111, 113).

[28] *Id.* ¶ 46 (A115); Lululemon Stock Price Chart (B095).

[29] Lululemon Stock Price Chart (B095).

resign as chief executive officer.[30]

On Friday June 7, 2013, lululemon's stock price reached $81.25 and Merrill Lynch sold 607,545 shares, the remaining portion of the monthly one million shares permitted to be sold under the plan during June.[31]

On Monday June 10, 2013, lululemon announced Ms. Day's resignation and lululemon's stock price dropped, closing on June 11 at $67.85.[32] The market value of the 607,545 shares Merrill Lynch sold on June 7 for approximately $49.5 million dropped to approximately $41.2 million, an alleged $8 million insider trading benefit for Mr. Wilson, who then owned approximately 40.9 million shares of stock worth more than $2.7 billion.[33] Following media reports concerning the sales, lululemon management – of which plaintiffs do not allege Mr. Wilson was a member – concluded that Mr. Wilson's "stock sales under his 10b5-1 plan are in alignment with SEC guidelines for these types of sales."[34]

Plaintiffs allege that Mr. Wilson "*potentially* engaged in insider trading" because his June 7, 2013 sales were "sufficiently suspicious such that Wilson's personal stockbroker was, in all likelihood, made aware by Wilson,

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[30] Compl. ¶¶ 47-51 (A115-117).

[31] *Id.* ¶ 52 (A117).

[32] *Id.* ¶ 53 (A117-118).

[33] 42,600,000 shares owned in Dec. 2012 (Apr. 25, 2012 Lululemon Form 14A at 41 (B103)) less 1,692,455 shares sold from Jan. 10, 2013 to June 4, 2013 (Compl. ¶¶ 35, 43, 46 (A110, 113, 115)) equals 40,907,545 shares. 40,907,545 shares at $67.85 per share equals $2,775,576,928.

[34] Compl. ¶¶ 22, 61 (A103-104, 124) (emphasis omitted).

directly or indirectly, of certain material, non-public, and market-moving events."[35] Plaintiffs also allege that "notwithstanding the suspicious nature" of these sales and "prominent media attention to those trades, the Board failed to investigate."[36]

### D. Prior Litigation

Beginning in July 2013, securities and derivative actions were filed in federal court in New York arising out of a March 2013 announcement by lululemon concerning black luon yoga pants that became unacceptably sheer when stretched during exercise, Ms. Day's June 2013 resignation, stock sales by Ms. Day, and Mr. Wilson's stock sales.[37]

#### 1. The Federal Securities Class Action

The district court dismissed the securities action on multiple grounds, including the court's conclusion that the "suspicious timing and amounts" of Mr. Wilson's stock sales did not "give rise to a strong inference of scienter."[38] Judge Katherine B. Forrest stated that "[t]rades made pursuant to a Rule 10b5-1 trading plan do not give rise to a strong inference of scienter" and that "Merrill Lynch could only have sold shares on the days on which it did so – days on which the stock price hit $81.25."[39] The court also pointed to the fact that Mr. Wilson

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[35] *Id.* ¶¶ 1, 84 (A096-097, 133-134).

[36] Op. Br. at 7.

[37] *Canty*, 13 F. Supp. 3d at 340; *In re Lululemon Sec. Litig.*, 14 F. Supp. 3d 553, 566-70 (S.D.N.Y. 2014), *aff'd*, 604 F. App'x 62 (2d Cir. 2015); *Canty* Compl. ¶¶ 193-98 (A283-285).

[38] *Lululemon Sec. Litig*, 14 F. Supp. 3d at 584.

[39] *Id.* at 585.

"retained over 94% of his . . . holdings" in 2013.[40] The Second Circuit affirmed "[f]or substantially the reasons provided by the District Court."[41]

### 2. **The Federal Derivative Action**

The district court dismissed the derivative action due to plaintiffs' failure to make a demand. Judge Forrest rejected plaintiffs' claim that the court should "infer that the Director Defendants were under such domination and control by Wilson that they deliberately exposed themselves to the risk of individual liability related to Wilson's June 2013 trading" because "no particularized allegations in the Amended Complaint . . . credibly suggest such a conclusion."[42] Judge Forrest held, for the same reason, that plaintiffs failed "to plead particularized allegations giving rise to a substantial likelihood of liability as to any of the Director Defendants arising out of Wilson's June 2013 trading."[43]

The Second Circuit affirmed, stating that plaintiff's "allegations of demand futility fall short of Delaware's stringent requirements."[44] The Second Circuit rejected the contentions that lululemon's board was "beholden to Wilson and thus cannot act independently" and that the litigation "expose[d]" directors "to personal liability because they intentionally facilitated Wilson's alleged insider

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[40] *Id*. at 586 n.23.

[41] *In re Lululemon Sec. Litig.*, 604 F. App'x 62, 63 (2d Cir. 2015).

[42] *Canty*, 13 F. Supp. 3d at 347.

[43] *Id*. at 349 n.12.

[44] *Canty v. Day*, 599 F. App'x 20, 22 (2d Cir. 2015).

trading."[45] The Second Circuit stated that plaintiffs alleged no "specific allegations that demonstrate a substantial likelihood of personal liability."[46]

**3. <u>The Section 220 Proceeding</u>**

While the New York action was proceeding, the plaintiffs here sought books and records under 8 *Del. C.* § 220. The broad scope of the requests necessitated a Section 220 action[47] in which the Court of Chancery found that plaintiffs stated a proper purpose with respect to only one of the numerous categories of documents plaintiffs sought: Mr. Wilson's June 7, 2013 trades.[48]

The Court pointed to Section 220's "very plaintiff-friendly" test requiring only "a credible basis for an inference" and stated that "[t]he fact that Plaintiffs may be entitled to review . . . books and records of the Company" "says nothing" about whether they could "survive a motion to dismiss if they choose to bring claims based on the information they review."[49] As noted in the Court's decision dismissing this action, the information plaintiffs obtained "tends to excul-

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[45] *Id.*

[46] *Id.*

[47] *See* Compl. Ex. A, Requests 1-3 (Mr. Wilson's trading plan), 4-5 (Mr. Wilson's Jan., May and June 4 and 7 stock sales), 6 (Ms. Day's departure), 7 (sheerness defects in yoga pants) (A144-145); Compl Ex. B Requests 1, 2(b)-(d), (f) (executive bonus plan), 2(a) (analyses of stock), 2(e) (financial projections) (A155-156).

[48] *Hallandale Beach Police Officers & Firefighters' Pers. Ret. Fund v. Lululemon Athletica Inc.*, Nos. 8522-VCP, 9039-VCP, Transcript at 25-32 (Del. Ch. Apr. 2, 2014) (June 7, 2013 sales) (B141-148); *see also id.* at 17-23 (no proper purpose with respect to Jan. 2013 sales) (B133-139); *id.* at 23-24 (no proper purpose with respect to May 2013 sales) (B139-140); *id.* at 24-25 (no proper purpose with respect to June 4, 2013 sales) (B140-141); *id.* at 32-37 (no proper purpose with respect to all other categories) (B148-153).

[49] *Id.* at 28, 15 (B144, 131).

pate Wilson and the board, rather than to bolster plaintiffs' theories of liability."[50]

#### 4. <u>Plaintiffs' Intervention In The Federal Action</u>

On March 25 and 27, 2014, shortly before a scheduled April 4, 2014 argument on motions to dismiss the New York action, plaintiffs moved to intervene in New York on the ground that their Section 220 action was proceeding and that if the New York action was "dismissed with prejudice, any subsequent action . . . may be forever barred by *res judicata* or other claim or issue preclusion principles."[51]

On March 28, 2014, the court informed the parties that on April 4 at 8 AM it would "issue a tentative [draft] ruling" and at 3 PM "listen to any argument the parties would like to make" and "*hear from the proposed intervenors*."[52]

On April 1, 2014, cognizant of Delaware's policy favoring Section 220 demands and seeking to mitigate the burden of multi-forum litigation, defendants proposed the following: (1) if Judge Forrest granted the motion to dismiss, the "claims premised on Mr. Wilson's stock sales should be dismissed '*without prejudice*'" and "the motions to intervene *should be granted* to allow LDC and/or Hallandale to file a single intervenor complaint . . . after the . . . production of . . . books and records," and (2) if Judge Forrest denied the motion to dismiss, "the motions to intervene *should be granted* and plaintiffs and intervenors should be

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[50] Op. at 32 n.70.

[51] Mar. 25, 2014 Mem. at 2 (A050); *see also* Mar. 27, 2014 Mem. at 3 (B215) (same).

[52] Mar. 28, 2014 Order (B223) (emphasis added).

required to litigate this action in a unified manner."[53] *Plaintiffs did not respond to this proposal*[54] and tell this Court that the proposal was "burdensome."[55] They do not say why – much less why the multi-forum litigation that proceeded instead was less burdensome on lululemon, the entity on whose behalf plaintiffs allege they are acting, or the four courts that have now heard motions and appeals in this matter.

At 8 AM on April 4, 2014, Judge Forrest issued a draft decision proposing dismissal "*without prejudice, in the event plaintiffs seek to pursue these claims after making a demand on the Board*" and denial of the motion to intervene "as moot."[56] During the 3 PM hearing, Judge Forrest invited the proposed intervenors' counsel to comment on the draft decision. He replied: "We're happy to sit back."[57] A few minutes later, *Judge Forrest asked counsel to confirm that the draft decision "corresponds . . . with what you are suggesting." He replied "Yes."*[58]

On April 9, 2014, the court issued its final decision, using the same words plaintiffs had consented to, "*without prejudice*, *in the event plaintiffs seek to pursue these claims after making a demand on the Board.*"[59]

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[53] Apr. 1, 2014 Letter to Court at 3-4 (B228-229) (emphasis added).

[54] Apr. 3, 2014 Letter to Court (B231-232).

[55] Op. Br. at 16 n.58.

[56] Apr. 4, 2014 Draft Opinion at 23-24 (A092-093) (emphasis added).

[57] Apr. 4, 2014 Transcript at 67 (A513).

[58] *Id*. at 74 (A520).

[59] *Canty*, 13 F. Supp. 3d at 350 (emphasis added).

# ARGUMENT

## I. Plaintiffs' Claim That Demand Is Excused Is Precluded

### A. Question Presented

Did the Court of Chancery correctly hold that plaintiffs are precluded from litigating the question whether demand is excused?

### B. Scope Of Review

"The Court of Chancery's legal conclusions are reviewed *de novo*."[60]

### C. Merits Of The Argument

"[T]he United States Supreme Court has held that a state court is required to give a federal judgment the same force and effect as it would be given under the preclusion rules of the state in which the federal court is sitting" – here, New York.[61] "Delaware law, likewise, requires our courts to afford the same respect to federal court judgments."[62] The obligation to apply the law of the forum in which a judgment is granted in assessing the preclusive effect of the judgment "is 'exacting'" and there is "no roving 'public policy exception.'"[63] "[T]he undisputed interest that Delaware has in governing the internal affairs of its corporations must yield to the stronger national interests that all state and federal courts have in respecting each other's judgments."[64]

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[60] *RBC Capital Mkts., LLC v. Jervis*, 129 A.3d 816, 849 (Del. 2015) (citation omitted).

[61] *Pyott*, 74 A.3d at 615-16 (citing *Semtek Int'l Inc. v. Lockheed Martin Corp.*, 531 U.S. 497, 507-08 (2001)).

[62] *Id*. at 616.

[63] *Baker v. Gen. Motors Corp.*, 522 U.S. 222, 232-33 (1998), *quoted in Pyott*, 74 A.3d at 616.

[64] *Pyott*, 74 A.3d at 616.

State and federal preclusion law is the same in New York.[65] Courts applying New York law – including the Court of Chancery's decisions affirmed by this court in *Asbestos Workers* and *Providence* – have held that the dismissal of a derivative action due to plaintiff's failure to make a demand precludes further litigation of the demand issue.[66] Here, moreover, plaintiffs appeared, were heard, rejected defendants' offer to allow them to litigate demand futility in New York in order to avoid multi-forum litigation, and consented to the relief granted in New York. They have no basis now to collaterally attack what they agreed to.

**1. Res Judicata Precludes Re-Litigation**

"Under the doctrine of res judicata, a party may not litigate a claim where a judgment on the merits exists from a prior action between the same parties involving the same subject matter."[67] The rule "applies not only to claims actually litigated but also to claims that could have been raised in the prior litigation."[68] "'[A] party must show that (1) the previous action involved an adjudication on the merits; (2) the previous action involved the parties or those in privity with them; [and] (3) the claims in subsequent actions were, or could have been raised in the

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[65] Op. at 17 (citing cases).

[66] *See Henik v. LaBranche*, 433 F. Supp. 2d 372, 377-78 (S.D.N.Y. 2006) (collateral estoppel and res judicata); *Wietschner v. Dimon*, 2015 WL 4915597, at *4-7 (N.Y. Sup. Ct. N.Y. Cnty. Aug. 14, 2015) (collateral estoppel and res judicata), *aff'd*, 32 N.Y.S.3d 77, 79 (N.Y. App. Div. 1st Dep't 2016) (res judicata); *Levin v. Kozlowski*, 2006 WL 3317048, at *7-14 (N.Y. Sup. Ct. N.Y. Cnty. Nov. 14, 2006), *aff'd*, 846 N.Y.S.2d 37 (N.Y. App. Div. 1st Dep't 2007) (collateral estoppel); *Providence*, 2015 WL 4594150, at *6-10 (res judicata); *Asbestos Workers*, 2015 WL 2455469, at *14-20 (collateral estoppel).

[67] *In re Estate of Hunter*, 827 N.E.2d 269, 274 (N.Y. 2005).

[68] *Id.*, *quoted in Wietschner*, 2015 WL 4915597, at *6 *and Providence*, 2015 WL 4594150, at *6.

prior action.'"[69] Privity is conceded.[70]

Plaintiffs contend that "demand futility is not a 'claim'" and can "only properly be discussed in the context of issue preclusion."[71] But federal and state courts in New York – and the Court of Chancery's decision in *Providence* affirmed by this Court – hold that res judicata precludes re-litigation of demand futility claims under New York law.[72]

#### a. The Federal Action Was An Adjudication On The Merits

"[D]ismissals for failure to adequately allege demand futility" are "on the merits and entitled to res judicata effect."[73] New York law also provides, however, "that 'a dismissal 'without prejudice,' lacks a necessary element of *res judicata* – by its terms such a judgment is not a final determination on the merits.'"[74]

Here, the New York court's dismissal was "without prejudice, *in the event plaintiffs seek to pursue these claims after making a demand on the Board*."[75]

Plaintiffs' contention that the New York court dismissed the action

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[69] *Henik*, 433 F. Supp. 2d at 378 (citations omitted).

[70] *See* footnote 5 and accompanying text above.

[71] Op. Br. at 17-18.

[72] *See Henik*, 433 F. Supp. 2d at 377-78; *Wietschner*, 2015 WL 4915597, at *4-7 and 32 N.Y.S.3d at 79; *Providence*, 2015 WL 4594150, at *6-10.

[73] *Wietschner*, 32 N.Y.S.3d at 79; *see also Providence*, 2015 WL 4594150, at *6 ("[u]nder New York law, the dismissal of a derivative action for failure to plead demand futility is a final judgment on the merits for purposes of res judicata'") (citing *Henik*, 433 F. Supp. 2d at 379).

[74] Op. at 34 (quoting *Landau, P.C. v. LaRossa, Mitchell & Ross*, 11 N.Y.3d 8, 13 (2008)).

[75] *Canty*, 13 F. Supp. 3d at 350 (emphasis added).

"without prejudice"[76] ignores the words after "without prejudice": "*in the event plaintiffs seek to pursue these claims after making a demand on the Board*."[77] The Court of Chancery described this sentence's "plain meaning" as follows:

> [T]he obvious intent . . . was to leave open the possibility that the plaintiffs could still make a demand on the board to pursue the derivative claims and, if the board refused to do so (either affirmatively or by inaction), the plaintiffs could then seek to initiate litigation if they believed such refusal was wrongful. But *what the district court did not leave open was the opportunity for plaintiffs to attempt to re-plead demand futility. Had that been the district court's intention, it simply would have made the dismissal "without prejudice" full stop, without any of the elaboration*.[78]

The Court of Chancery correctly followed the similar constructions of virtually identical dismissals by courts applying New York law in *Henik v. LaBranche* and *Asbestos Workers* – a decision affirmed by this Court.[79] Plaintiffs' counsel conceded in the Court of Chancery that the dismissal here "is essentially . . . identical" to the dismissal in *Henik*.[80] The Court of Chancery also correctly rejected plaintiffs' "extrinsic evidence" with respect to what plaintiffs think Judge Forrest

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[76] Op. Br. at 2, 11-12, 14-16, 22 n.81.

[77] *Canty*, 13 F. Supp. 3d at 350 (emphasis added).

[78] Op. at 35 (emphasis added).

[79] *Henik*, 433 F. Supp. 2d at 379 (dismissal "without prejudice to the bringing of a new action, if a pre-suit demand is either rejected or not considered within a reasonable amount of time" is "[b]y implication" a dismissal "with prejudice to the bringing of a new action, absent showing that a pre-suit demand was rejected or not considered"); *Asbestos Workers*, 2015 WL 2455469, at *18 n.149 (where action had been dismissed "'without prejudice for the Plaintiff to replead, if they are so advised, with respect to making a demand subsequent to this day,'" "[o]f course, though the dismissal was without prejudice to replead upon making demand, the Plaintiff, either here or in that case, would not be able to replead the *demand futility* issue").

[80] Mar. 15, 2016 Transcript at 76 (A608).

"understood" and why plaintiffs "presume[ ]" she ruled as she did, because her Opinion was unambiguous and thus, the Court of Chancery stated, "I do not consider extrinsic evidence to construe its meaning."[81] Plaintiffs' counsel conceded in the Court of Chancery that "I agree" the court "shouldn't be looking at anything other than the opinion itself."[82]

Plaintiffs insist that "[i]t simply cannot be" that the New York court's ruling "was intended to preclude the litigation of any *claims*" because that "would preclude subsequent claims not only by stockholders, but also by the corporation itself."[83] Plaintiffs are wrong. The claims that are precluded are the claims that a stockholder suing derivatively could assert without making a demand – not claims a stockholder who makes a demand or the corporation could assert.

**b. Plaintiffs' Claims Were Or Could Have Been Raised In The Federal Action**

Res judicata applies "not only to claims actually litigated but also to claims that could have been raised in the prior litigation."[84] "'[O]nce a claim is brought to a final conclusion, all other claims arising out of the same transaction or series of transactions are barred, even if based upon different theories or if seeking a different remedy.'"[85] "When alternative theories are available to recover what is

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[81] Op. at 34 n.75.

[82] Mar. 15, 2016 Tr. at 70-72 (A602-604).

[83] Op. Br. at 17.

[84] *Hunter*, 827 N.E.2d at 274, *quoted in Providence*, 2015 WL 4594150, at *6.

[85] *Hunter*, 827 N.E.2d at 274 (quoting *O'Brien v. Syracuse*, 429 N.E.2d 1158, 1159 (N.Y. 1981)), *quoted in Providence*, 2015 WL 4594150, at *7.

essentially the same relief for harm arising out of the same or related facts such as would constitute a single 'factual grouping,' the circumstance that the theories involve materially different elements of proof will not justify presenting the claim by two different actions."[86] "That the complaints set forth different theories of recovery and that the claims in the [second] action were not actually raised in the [first] actions present no impediments to application of the doctrine."[87]

The Court of Chancery correctly rejected plaintiffs' contention that plaintiffs' claims were not and could not have been raised in New York.[88] Plaintiffs' only response is a contention that "the claim against members of the Board for failing to investigate and take action against Wilson . . . was not raised in the New York Action."[89] But this claim *was* raised, as plaintiffs admitted when they intervened in the New York action. In their own words:

> LDC has a potential claim that is *virtually identical* to one of the numerous claims asserted in the Derivative Actions: namely, whether certain of Wilson's suspiciously timed stock sales were in fact executed pursuant to a Rule 10b5-1 trading plan, and whether members of the Board breached their fiduciary duties *by failing to investigate* the suspicious trades.[90]

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[86] *O'Brien*, 429 N.E.2d at 1160, *quoted in Providence*, 2015 WL 4594150, at *9.

[87] *Wietschner*, 32 N.Y.S.3d at 78.

[88] Op. at 37-40.

[89] Op. Br. at 18.

[90] Mar. 25, 2014 Mem. at 6 (A054) (emphasis added); *see also* Mar. 27, 2014 Mem. at 7-8 ("one of Hallandale Beach's key potential claims – whether certain of Wilson's suspiciously-timed stock sales were completed while using inside information and whether the Board breached its fiduciary duty *by failing to investigate* these suspicious trades – *is virtually identical* to one of the claims asserted in the Derivative Actions") (B219-220) (emphasis added).

And, of course, the fact that a claim was "not raised" does not mean that it "could not have been raised."[91]

### c. *Parkoff* Is Not To The Contrary

Plaintiffs also contend that there is no preclusion – res judicata or collateral estoppel – under *Parkoff v. Gen. Tel. & Elec. Corp*.[92] This claim fails on its merits and because plaintiffs did not make this argument in the Court below.[93]

*Parkoff* holds only that a judgment has no preclusive effect on stockholders who were "*frustrated in an attempt to join or to intervene* in the action that went to judgment" or "sought intervention and was *excluded from participation* in that action," and requires that the excluded stockholders' "*attempts to participate in the litigation have been rebuffed* and *no other appropriate provision for the*

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[91] *Hunter*, 827 N.E.2d at 275.

[92] 425 N.E.2d 820 (N.Y. 1981); Op. Br. at 2-3, 14, 18-22, 30.

[93] Plaintiffs concede they did not make this argument in the Court of Chancery. Op. Br. at 19 n.73. "Only questions fairly presented to the trial court may be presented for review." Supr. Ct. R. 8; *see also Scion Breckenridge Managing Member, LLC v. ASB Allegiance Real Estate Fund*, 68 A.3d 665, 678 (Del. 2013) ("[w]e 'adhere to the well settled rule which precludes a party from attacking a judgment on a theory he failed to advance before the trial judge'") (citation omitted). Plaintiffs' footnote "request that this Court consider and determine this issue" under Supr. Ct. R. 8's "interests of justice" exception (Op. Br. at 19 n.73) fails, procedurally and substantively. Procedurally, "[t]he merits of any argument that is not raised in the body of the opening brief shall be deemed waived and will not be considered by the Court on appeal" (Supr. Ct. R. 14(b)(vi)(A)(3)), and "'[a]rguments in footnotes do not constitute raising an issue in the 'body' of the opening brief.'" *Lum v. State*, 101 A.3d 970, 972 (Del. 2014) (citation omitted); *id.* at 972 n.8 (collecting additional authorities); *see also Seaport Vill., Ltd. v. Terramar Retail Ctrs. LLC*, 2016 WL 5373085, at *1 (Del. Sept. 26, 2016) (an "argument . . . not fairly presented to the Court of Chancery . . . is waived"). Substantively, Rule 8's "interests of justice" exception is applied only under circumstances where (i) "the issue is outcome-determinative and may have significant implications for future cases," *Sandt v. Del. Solid Waste Auth.*, 640 A.2d 1030, 1034 (Del. 1994), *quoted in Scion*, 68 A.3d at 679, (ii) consideration of the issue will promote judicial economy because it will avoid the necessity of" addressing the issue later in the litigation," *id.*, or (iii) the trial court *sua sponte* decides an unbriefed issue. *Reddy v. MBKS Co.*, 945 A.2d 1080, 1086 (Del. 2008). The New York law issue here falls into none of these categories.

*protection of their interests has been made*."[94] Plaintiffs cite (and we know of) no case denying preclusion on this ground in the 35 years since *Parkoff* was decided. Commentators have observed that "[i]t is not clear how far this approach may undo the res judicata effects of derivative actions."[95]

It certainly cannot undo preclusion here. Plaintiffs were not "frustrated in an attempt to join" and their "attempts to participate" in the New York action were not "rebuffed." They were not, as they claim, "thwarted."[96] Defendants were not, like the defendants in *Parkoff*, "agents of . . . exclusion" opposing intervention.[97]

To the contrary, defendants *invited* plaintiffs' participation in the case, affirmatively proposing a without prejudice dismissal on the demand issue in return for plaintiffs' agreement not to subject defendants to the burdens of multi-forum litigation – an offer to which plaintiffs chose not to respond.[98] They chose instead to "jockey for control of a case in an effort to secure a payday for themselves."[99] Judge Forrest also invited plaintiffs' participation, twice requesting their

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[94] 425 N.E.2d at 420-22 (emphasis added) (citation omitted).

[95] 18A Charles Alan Wright, Arthur R. Miller & Edward H. Cooper, *Federal Practice and Procedure* § 4460, at 643 n.43 (2d ed. 2002 & Supp. 2016).

[96] Op. Br. at 3, 14, 20.

[97] *See Parkoff*, 425 N.E.2d at 421 n.5 ("Had Defendants expected to impose *res judicata* consequences on Parkoff they should either have consented to, or at least refrained from opposing, his application for intervention. They cannot at once be the agents of his exclusion and yet lay claims to the same benefit as if he had been included.").

[98] *See* footnotes 53-54 and accompanying text above.

[99] Op. at 30.

views concerning her draft decision proposing a dismissal "without prejudice, *in the event plaintiffs seek to pursue these claims after making a demand on the Board*."[100] The first time, plaintiffs' counsel replied: "We're happy to sit back."[101] The second time, when Judge Forrest asked counsel to confirm that her draft decision "corresponds . . . with what you are suggesting," counsel replied "yes."[102] Litigants who consent to relief in one court cannot then claim that their participation in that action was "rebuffed," "frustrated," and "thwarted."

**2. Collateral Estoppel Precludes Re-Litigation**

"[O]nly two requirements must be satisfied" to invoke collateral estoppel against "a party, or one in privity with a party":

> First, the party seeking the benefit of collateral estoppel must prove that the identical issue was necessarily decided in the prior action and is decisive in the present action. Second, the party to be precluded from relitigating an issue must have had a full and fair opportunity to contest the prior determination.[103]

**a. The Federal Action And This Action Involve The Same Issue**

Plaintiffs contend that "the New York Plaintiffs never raised the issue of the Board's failure to investigate . . . , asserting instead that the Board ''facilitated' Wilson's June 2013 stock sales'" and that "[t]he central issue raised by the Delaware Plaintiffs to support their demand futility argument – the Board's failure

[100] Apr. 4, 2014 Draft Opinion at 23 (A092) (emphasis added).

[101] Apr. 4, 2014 Transcript at 67 (A513).

[102] *Id*. at 74 (A520).

[103] *D'Arata v. N.Y. Cent. Mut. Fire Ins. Co.*, 564 N.E.2d 634, 636 (N.Y. 1990) (citation omitted).

to investigate – was never alleged in the New York Action."[104] As noted above, when plaintiffs intervened in the New York action, they said the opposite.[105]

Ignoring this concession, plaintiffs next argue that an alleged failure to investigate "squarely implicates a specific Board decision," that plaintiffs' "demand futility facts go to whether that decision is deserving of the protections of the business judgment rule," and that the need for demand thus is governed by the *Aronson* test for director action rather than the *Rales* test for director inaction.[106] Plaintiffs argue that "this issue" – whether demand is excused under *Aronson*, as opposed to *Rales* – "was not litigated or decided in New York."[107]

The New York court explicitly rejected plaintiffs' contention that demand was excused due to "the Director Defendants' 'conscious inaction in the face of Wilson's illicit trading.'"[108] For sure, the New York court applied *Rales* to evaluate plaintiffs' allegations that lululemon's directors "failed to take action as to Wilson's June 2013 stock sales,"[109] but, "'[a]s many members of [the Court of Chancery] have recognized, the *Rales* test functionally covers the same ground as the *Aronson* test in determining the impartiality of directors.'"[110] "[M]inor varia-

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[104] Op. Br. at 26; *see also id*. at 24 (quoting *Canty*, 13 F. Supp. 3d at 343 n.5).

[105] *See* text footnote 90 and accompanying text above.

[106] Op. Br. at 25.

[107] *Id*.

[108] *Canty*, 13 F. Supp. 3d at 345.

[109] *Id*. at 343 & n.5.

tions in the application of what is in essence the same legal standard do not defeat preclusion."[111]

The cases plaintiffs cite for the proposition that issues must be "identical in all respects" are easily distinguished.[112] "[T]he identity element does not require that the issues be exactly identical, and . . . two issues may be identical for estoppel purposes if they are substantially or essentially the same."[113] "[T]he underlying conduct is what is at issue, not whether the Complaint raises additional facts, or a more compelling characterization of those facts, regarding the same

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[110] *Sandys v. Pincus*, 2016 WL 769999, at *12-13 & n.59 (Del. Ch. Feb. 29, 2016) (collecting cases), *appeal pending*, No. 157, 2016; *In re China Agritech, Inc. S'holder Deriv. Litig.*, 2013 WL 2181514, at *16 (Del. Ch. May 21, 2013) ("*Aronson* and *Rales* have been described as complementary versions of the same inquiry"); *Guttman v. Huang*, 823 A.2d 492, 501 (Del. Ch. 2003) (although the "*Rales* test looks somewhat different from *Aronson*, in that [it] involves a singular inquiry[,] . . . that singular inquiry makes germane all of the concerns relevant to both the first and second prongs of *Aronson*"), *quoted in Sandys*, 2016 WL 769999, at *12 n.59.

[111] *B&B Hardware*, 135 S. Ct. at 1307.

[112] *See Bader v. Goldman Sachs Gp., Inc.*, 455 F. App'x 8, 9-10 (2d Cir. 2011) (Op. Br. at 27) (issues differed in cases challenging statements concerning stock options in different proxy statements, where the court in the first case "did not reach" a claim that three directors who received the options were interested because those allegations "only related to a minority of the directors" and the claim in the second case was that six of twelve directors "were interested by virtue of having received undervalued stock options" and therefore, unlike the first case, "the question of whether the receipt of undervalued options renders a director 'interested'" was "dispositive of the demand futility issue"); *Brautigam v. Blankfein*, 8 F. Supp. 3d 395, 402 (S.D.N.Y. 2014) (Op. Br. at 23-24, 26-28) (issues differed in cases challenging different collateralized debt obligations), *aff'd sub nom. Brautigam v. Dahlback*, 598 F. App'x 53 (2d Cir. 2015); *Bansbach v. Zinn*, 801 N.E.2d 395, 402 (N.Y. 2003) (Op. Br. at 27) (issues differed where the first case challenged the independence of directors in connection with a grant of stock options and warrants to directors and the second case challenged the independence of directors with respect to unlawful campaign contributions by corporation's founder, majority shareholder and chairman).

[113] *Kreinik v. Showbran Photo, Inc.*, 400 F. Supp. 2d 554, 562 (S.D.N.Y. 2005) (citation omitted) (collecting cases); *see also Levin*, 2006 WL 3317048, at *8 (claim that demand excused collaterally estopped where court in prior action rejected "substantially identical claims").

conduct previously at issue."[114] It is not enough to assert a fiduciary duty claim that "essentially repackages in the form of a claim the core of the NY plaintiffs' demand futility allegations – that the outside directors failed to do anything after supposedly knowing that Wilson had engaged in insider trading."[115] Otherwise, "issue preclusion would almost never apply – subsequent plaintiffs could simply add more allegations (or more specific allegations) of corporate malfeasance, and then claim there was no identity of the issues."[116] "The interests of efficiency and finality (and, with respect to litigation in different jurisdictions, comity) require a practical view of the issues presented, to preclude such gamesmanship."[117]

**b. Plaintiffs Had A Full And Fair Opportunity To Litigate In The Federal Action**

Plaintiffs do not contend that the New York plaintiffs did not have a full and fair opportunity to litigate. Plaintiffs contend only that *they* did not have a full and fair opportunity to litigate.[118] But plaintiffs concede privity.[119] That ends

[114] *Asbestos Workers*, 2015 WL 2455469, at *18, *quoted in* Op. at 35; *see also In re Duke Energy Corp. Deriv. Litig.*, 2016 WL 4543788, at *12 n.164 (Del. Ch. Aug. 31, 2016) ("to the extent this Complaint seeks to vindicate a similar claim, no matter how much better or persuasive the pleadings, the Plaintiffs are collaterally estopped") (North Carolina law).

[115] Op. at 31-32 (footnote omitted); *see also id.* at 40.

[116] *Id.* at 24 (quoting *Arduini v. Hart*, 774 F.3d 622, 630 (9th Cir. 2014)) (Nevada law); *see also Asbestos Workers*, 2015 WL 2455469, at *18 ("[i]t cannot be the case that the 'controlling facts' . . . are simply those facts presented in the *complaint*, because "[i]f that were the case, collateral estoppel would never apply and the plaintiff could litigate serially by endlessly alleging more factual support for the proposition he chooses to advance – this is clearly contrary to the efficiency and fairness principles underlying collateral estoppel").

[117] *Duke Energy*, 2016 WL 4543788, at *13; *id.* (urging that courts not "open the door to artful crafting by plaintiffs of new causes of action . . . in an attempt to avoid collateral estoppel").

[118] Op. Br. at 29.

the matter. Here, however, there is more. As the Court of Chancery correctly stated, "plaintiffs moved to intervene . . . and made arguments to the district court in an effort to prevent it from adjudicating a motion to dismiss in a manner that could impede their ability to pursue their claims in Delaware after obtaining books and records from the Company. Thus, plaintiffs had the opportunity to present their views to the district court."[120]

### 3. Plaintiffs Have Not Established Inadequate Representation In The New York Action

There is no preclusion "where the plaintiff shareholder in the first action is alleged to have inadequately represented the interests of all of the shareholders."[121] Plaintiffs concede that inadequate representation requires "grossly deficient" representation.[122] The record in the New York action shows hard-fought representation by law firms specializing in stockholder derivative litigation. Plaintiffs' argument is *not* that New York plaintiffs "didn't write good briefs or make good arguments to the Judge."[123] Instead, plaintiffs allege inadequate representa-

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[119] *See* footnote 5 and accompanying text above.

[120] Op. at 27.

[121] *Henik*, 433 F. Supp. 2d at 381; *see also Restatement (Second) of Judgments* § 42(1) (1982) ("[a] person is not bound by a judgment for or against a party who purports to represent him if . . . (e) [t]he representative failed to prosecute or defend the action with due diligence and reasonable prudence"), *quoted in Pyott*, 74 A.3d at 618 n.21; *see also* Op. at 28 (collecting cases showing that New York courts follow Section 42 of the *Restatement Second of Judgments*).

[122] Op. Br. at 32 (quoting *Restatement (Second) of Judgments* § 42(1)(e) cmt. f); Mar. 15, 2016 Tr. at 77-78 (A609-610).

[123] Mar. 15, 2016 Transcript at 79 (A611).

tion because the New York plaintiffs did not make a Section 220 demand.[124]

Preclusion "does not depend upon the approval by the plaintiff in a subsequent suit of the conduct of the litigation by counsel in the earlier action" or whether the plaintiff in the first action pursued "an unsuccessful legal theory or strategy" or "chose the wrong strategy."[125] "The mere fact that a representative fails to develop all possible proofs does not make his representation inadequate."[126] "[A] strategic calculation by one plaintiff's attorney that puts a different plaintiff's attorney at a disadvantage in a later lawsuit does not necessarily mean that the original plaintiff's calculation was harmful to the corporation or a mark of inadequate representation."[127] "The failure of a representative to invoke all possible legal theories or to develop all possible resources of proof does not make his representation legally ineffective, any more than such circumstances overcome the binding effect of a judgment on a party himself."[128]

This Court in *Pyott* thus rejected a "'fast-filer' irrebuttable presumption of inadequacy" for "derivative plaintiffs who file their complaints without seeking books and records" in the absence of "record support for the . . . pre-

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[124] Op. Br. at 3, 31-35.

[125] *Greco v. Local.com Corp.*, 806 F. Supp. 2d 653, 658, 659, 660 (S.D.N.Y. 2011) (citation omitted).

[126] *Univ. Club v. City of N.Y.*, 655 F. Supp. 1323, 1327 (S.D.N.Y. 1987), *aff'd*, 842 F.2d 37 (2d Cir. 1988).

[127] *Norfolk Cty. Ret. Sys. v. Jos. A. Bank Clothiers, Inc.*, 2009 WL 353746, at *8 n.68 (Del. Ch. Feb. 12, 2009), *aff'd*, 977 A.2d 899 (Del. 2009).

[128] *Restatement (Second) of Judgments* § 42(e) cmt. f.

mise."[129] Plaintiffs *acknowledged* that they had no such "record support" in their motion to intervene in New York, stating that "the failure by a derivative plaintiff to make a books and records demand . . . does not constitute inadequate representation *per se*" and that if "the present action is dismissed with prejudice on the basis of demand futility" they "*will have a difficult time rebutting the presumption that the Company was adequately represented in this matter*."[130]

Plaintiffs also allege a second ground for inadequate representation: the New York plaintiffs copied allegations from the securities action.[131] We do not condone this conduct, which, the Court of Chancery noted, "pervade[s] representative litigation."[132] But it does not amount to "grossly deficient" representation absent, as here, any explanation "as to how the copying of . . . allegations substantively impacted the[ ] litigation of the demand futility issues so as to call into question the legitimacy of the district court's determination of that issue."[133]

The New York plaintiffs' decision not to make a Section 220 demand and copying of allegations occurred long before plaintiffs represented to the New

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[129] 74 A.3d at 618; *see also Asbestos Workers*, 2015 WL 2455469, at *18 n.147 ("*Pyott* makes clear that a presumption of inadequacy does not arise upon a showing that the prior plaintiff failed to use a section 220 request to develop its case"); *Fuchs Family Tr. v. Parker Drilling Co.*, 2015 WL 1036106, at *6 (Del. Ch. Mar. 4, 2015) ("a prior plaintiff's decision against making a Section 220 demand before pleading demand futility does not prevent collateral estoppel") (Texas law).

[130] Mar. 25, 2014 Mem. at 13 (citing *Pyott*, 74 A.3d at 617) (A061) (emphasis added).

[131] Op. Br. at 3, 9-10, 33.

[132] Op. at 30.

[133] *Id.*

York court that they "will have a difficult time rebutting the presumption that the Company was adequately represented in this matter." If plaintiffs thought the federal court proceeding was inadequate, they had an obligation to tell that to the federal court when they appeared in the action. Plaintiffs cannot collaterally attack a federal court action under the guise of grossly deficient representation when plaintiffs were heard in the action they claim was grossly deficient, spurned an offer to allow re-argument of demand futility in that action using the fruits of their Section 220 demand in order to avoid the costs and burdens of multi-forum litigation, and consented on the record to the relief awarded in that action.

Plaintiffs' final ground for inadequate representation is the "'antagonism' between the New York and Delaware plaintiffs" evidenced by the New York plaintiffs' opposition to plaintiffs' motion to intervene.[134] The antagonism required to show inadequate representation of lululemon is antagonism with lululemon – not the "reality that counsel for any set of plaintiffs involved in multi-jurisdictional litigation would face."[135] The New York plaintiffs' opposition to the motion to intervene obviously had no impact on the proceeding in New York, where plaintiffs rejected defendants' offer to let them intervene and plaintiffs consented to the relief awarded.[136]

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[134] Op. Br. at 4, 11, 33-34.

[135] *Wal-Mart*, 2016 WL 2908344, at *19.

[136] *See* text footnotes 53-54, 57-58 and 100-102 and accompanying text above.

## II. Plaintiffs Do Not Allege Particularized Facts Excusing Demand

"This Court may affirm on the basis of a different rationale than that which was articulated by the trial court, if the issue was fairly presented to the trial court."[137] The demand issue was briefed and argued fully in the trial court.[138]

### A. Question Presented

Is demand excused by an allegation that disinterested and independent directors did not investigate stock sales made pursuant to a Rule 10b5-1 trading plan providing a Merrill Lynch broker sole discretion to sell stock in amounts and at prices set by the plan, where there is no claim that the stock sales were not made at times and in amounts permitted by the plan and where the corporation's management concluded that the sales complied with SEC guidelines?

### B. Scope Of Review

If this Court reaches this issue, this Court would decide the issue *de novo* because the Court of Chancery did not reach the issue.

### C. Merits Of The Argument

"The key principle upon which this area of our jurisprudence is based is that the directors are entitled to a *presumption* that they were faithful to their fiduciary duties."[139] Plaintiffs must "rebut the presumption at the pleading

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[137] *RBC*, 129 A.3d at 849.

[138] Motion to Dismiss Op. Br. at 36-53 (B048-065); Motion to Dismiss Ans. Br. at 46-57 (A354-565); Motion to Dismiss Rep. Br. at 25-34 (B195-204); Mar. 15, 2016 Transcript at 36-56, 95-102 (A568-588, 627-634).

[139] *Beam v. Stewart*, 845 A.2d 1040, 1048 (Del. 2004).

stage."[140] Inferences are drawn in favor of plaintiffs only where they "logically flow from particularized facts."[141] This presumption is incorporated into the well-known *Aronson* and *Rales* tests – "complementary versions of the same inquiry," which together require that plaintiffs allege particularized facts showing a reason to doubt director disinterest or independence or a substantial likelihood of liability, such as for approving a transaction not protected by the business judgment rule.[142]

### 1. Plaintiffs Fail To Allege A Lack Of Disinterestedness Or Independence

"A director is considered interested where he or she will receive a personal financial benefit . . . that is not equally shared by the stockholders."[143] The complaint contains no such allegations with respect any member of lulu-lemon's board on the date this action was filed, July 15, 2015, after Mr. Wilson's departure from the board in February 2015.[144]

A director lacks independence where the director is dominated or otherwise controlled by or "beholden" to an individual having a financial interest.[145] The complaint alleges in conclusory fashion that *in 2013* Mr. Wilson was

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[140] *Id*. at 1049.

[141] *Wood v. Baum*, 953 A.2d 136, 140 (Del. 2008) (quoting *Beam*, 845 A.2d at 1048).

[142] *Id.*; *Rales*, 634 A.2d at 933-35; *Aronson*, 473 A.2d at 814; *Duke Energy*, 2016 WL 4543788, at *14-15; *Sandys*, 2016 WL 769999, at *11-13; *see also* footnote 110 and accompanying text above.

[143] *Rales*, 634 A.2d at 936; *Beam*, 845 A.2d at 1049 n.21 (quoting *Rales*).

[144] *See* footnote 19 and accompanying text above.

[145] *Beam*, 845 A.2d at 1050; *Rales*, 634 A.2d at 936; *Grobow v. Perot*, 539 A.2d 180, 189 (Del. 1988); *Aronson*, 473 A.2d at 815.

"influential," "powerful" and "wanted control over the strategic vision of Lululemon."[146] But plaintiffs do not allege that Mr. Wilson dominated or controlled lululemon's board *even in 2013*, when he served as chairman of the board and owned 29.7% of lululemon's stock – *before* his sale of 50% of his stock in September 2014 and *before* his departure from lululemon's board in February 2015.[147] To allege domination or control, a plaintiff must allege that "because of the nature of a relationship or additional circumstances other than the interested director's stock ownership or voting power, the non-interested director would be more willing to risk his or her reputation than risk the relationship with the interested director."[148] Nothing of the sort is alleged here with respect to any lululemon director on July 15, 2015.

### 2. Plaintiffs Fail To Allege A "Substantial Likelihood of Liability" On The Part Of – Or Even A Cause of Action Against – Lululemon's Disinterested And Independent Directors

Many cases hold that a board's failure to take action or file a lawsuit with respect to an issue the board is aware of does not excuse demand. "[B]oard approval of a challenged transaction" does not "automatically connote[ ] 'hostile interest' and 'guilty participation' by directors, or some other form of sterilizing

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[146] Compl. ¶¶ 3, 64, 50 (A097-098, 125-126, 116).

[147] *Aronson*, 473 A.2d at 815 ("[i]n the demand context even proof of majority ownership of a company does not strip the directors of the presumptions of independence"), *quoted in Beam*, 845 A.2d at 1054 n.37.

[148] *Beam*, 845 A.2d at 1052.

influence upon them."[149] "[W]ere that so, the demand requirements of our law would be meaningless, leaving the clear mandate of Chancery Rule 23.1 devoid of its purpose and substance."[150]

Accordingly, the Court of Chancery held in *Jacobs v. Yang* that demand was not excused by an allegation that "the current board had knowledge of" alleged wrongdoing and "failed to 'recover on behalf of Yahoo! for any wrong-doing'" and thus "'breached its fiduciary duty by acquiescing to the wrongful conduct.'"[151] This Court "affirmed on the basis of the Court of Chancery's well-reasoned opinion."[152] The Court of Chancery in *Hartsel v. Vanguard Gp., Inc.* likewise rejected an allegation that "the fact that the Trustee Defendants failed to take appropriate action after becoming aware of the other Defendants' wrong-doing" excuses demand, because "[m]ere inaction on the part of a board after a corporation's claim accrues does not relieve the plaintiffs of the requirement to make demand."[153] Again, this Court "affirmed on the basis of and for the reasons set forth in its well-reasoned decision."[154] This Court held in *Kaplan v. Peat, Marwick, Mitchell & Co.* that even the refusal of a demand by one stockholder does not

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[149] *Aronson*, 473 A.2d at 814.

[150] *Id.*

[151] 2004 WL 1728521, at *6 n.31 (Del. Ch. Aug. 2, 2004), *aff'd*, 867 A.2d 902 (Del. 2005).

[152] *Jacobs v. Yang*, 867 A.2d 902 (Del. 2005) (text available at 2005 WL 277920).

[153] 2011 WL 2421003, at *21, 27 (Del. Ch. June 15, 2011), *aff'd*, 38 A.3d 1254 (Del. 2012).

[154] *Hartsel v. Vanguard Gp., Inc.*, 38 A.3d 1254 (Del. 2012) (text available at 2012 WL 171881).

excuse demand by a second stockholder.[155]

The notion that outside directors risked their reputations by willingly participating in securities fraud to enrich Mr. Wilson but not themselves is not an inference that "logically flow[s] from particularized facts."[156] The notion that outside directors breached their fiduciary duties by not inferring that Mr. Wilson "in all likelihood" "directly or indirectly" made Merrill Lynch "aware" of inside information[157] is not an inference that "logically flow[s] from particularized facts."

Plaintiffs' claim that lululemon's outside directors breached their fiduciary duties by relying on – without verifying in a manner documented in a writing that could be produced in response to a Section 220 demand – the conclusion by lululemon's management (of which plaintiffs do not allege Mr. Wilson was a member) that Mr. Wilson's "stock sales under his 10b5-1 plan are in alignment with SEC guidelines for these types of stock sales"[158] is not an inference that "logically flow[s] from particularized facts." Plaintiffs, of course, "must rebut the presumption that the directors properly exercised their business judgment, including their good faith reliance" permitted by 8 *Del. C.* § 141(e).[159] Plaintiffs' claim that Mr. Stritzke – a single director who left lululemon's board before this action

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[155] 540 A.2d 726, 731 n.2 (Del. 1988).

[156] *Wood*, 953 A.2d at 140 (quoting *Beam*, 845 A.2d at 1048).

[157] Compl. ¶ 84 (A133-134).

[158] *Id*. ¶¶ 22, 61 (A103-104, 124) (emphasis omitted).

[159] *Brehm v. Eisner*, 746 A.2d 244, 261 (Del. 2000).

was filed – breached his fiduciary duties by relying on an email communicating the judgment of lululemon's Director of Legal with respect to whether it was necessary for "an attorney" to "look at the facts"[160] is also not an inference that "logically flows from particularized facts." That no other documents were produced in response to a Section 220 demand does not mean there were no oral communications. As the Court of Chancery noted in its Section 220 decision, "I would not be surprised that there are no documents in this category," "I wouldn't expect to be drawing any kind of adverse inferences from that fact," and "I'm not encouraging anybody to do anything like that."[161]

At most, plaintiffs allege a breach of the duty of care by directors protected by a Section 102(b)(7) charter provision exculpating them from breaches of the duty of care. As plaintiffs have not "plead[ed] a non-exculpated claim for breach of fiduciary duty," lululemon's directors are "entitled to be dismissed from the suit" even under Chancery Rule 12(b)(6).[162] They certainly do not face a substantial likelihood of liability under Court of Chancery Rule 23.1.

## CONCLUSION

For the reasons stated above, this Court should affirm the Court of Chancery's decision dismissing this action.

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[160] Compl. ¶¶ 24, 62, 74 (A103, 124-125, 130-131) (emphasis omitted).

[161] *Hallandale*, Nos. 8522-VCP, 9039-VCP at 42 (B158).

[162] *In re Cornerstone Therapeutics Inc., S'holder Litig.*, 115 A.3d 1173, 1179 (Del. 2015).

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