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Case Number 338,2020

IN THE SUPREME COURT OF THE STATE OF DELAWARE

OTTO CANDIES, LLC, et al.,	
	No. 338, 2020
Plaintiffs Below-Appellants,	
v.	CASES BELOW:
KPMG LLP,	COURT OF CHANCERY OF THE STATE OF DELAWARE
Defendant Below-Appellee.	C.A. No. 2018-0435-MTZ
	SUPERIOR COURT OF THE STATE OF DELAWARE
	C.A. No. N16C-02-260-PRW (CCLD)

APPELLANTS' REPLY BRIEF

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SUMMARY OF ARGUMENT

KPMG-US largely disregards or attempts to dispute the allegations of the Amended Complaint, and completely ignores the standard for stating a claim at the pleading stage. Instead, the answering brief ("Ans. Br.") repeatedly falls back on a policy-based plaint that KPMG-US could not possibly be vicariously liable in this case, because then it could be liable for the activities of other KPMG members in other cases. But this appeal will not determine liability; it will determine whether the Amended Complaint states a claim. And what matters at the pleading stage are Plaintiffs' specific allegations concerning KPMG-US's control over the audits at issue conducted by KPMGM, particularly given Defendants' relationship and the audits' substantial overlap with KPMG-US's own audits of Citigroup and the very transactions that harmed Plaintiffs. Accordingly, this case presents a fact pattern not present in the vast majority of cases.

In all events, accounting firms have no special exception to the usual rules for agency and vicarious liability. If KPMG-US controls other KPMG member firms (via KPMGI), then it *should* be held liable for their actions. There is no legal or practical reason why courts should simply assume, contrary to well-pled allegations, that KPMG-US does not control other KPMG firms. KPMG-US's effort to dispute the facts of those allegations—*e.g.*, whether KPMG-US's many high-level officers in KPMGI in fact control KPMGI, and whether KPMGI in fact controls the manner

and method by which KPMGM conducts its audits—is improper on a motion to dismiss. In short, this Court should reject KPMG-US's request for *de facto* immunity from any inquiry into whether it is vicariously liable for the wrongdoing of KPMGM.

In the absence of such an immunity, reversal is required under a straight-forward application of this Court's case law. KPMG-US identifies no precedent to refute this Court's repeated holdings that agency is established by a right to control. And KPMG-US makes virtually no attempt to argue that the right to control test is unsatisfied here, instead simply asserting that without explanation, while disregarding Plaintiffs' allegations to the contrary and the myriad cases accepting similar (or less specific) allegations. KPMG-US also posits waiver arguments that ignore the statements on point in Plaintiffs' briefing below and in the Court of Chancery's decision, either of which suffices to raise the issue in this Court. KPMG-US further relies on a theory that the allegations of control are not sufficiently connected to the wrongdoing, ignoring the simple logic that if KPMG-US controls KPMGM's auditing (via KPMGI) generally, then it necessarily controls KPMGM's auditing of OSA. KPMG-US's insistence that this Court should assume the contrary defies both the pleading standard, whereby reasonable inferences are made in Plaintiffs' favor, and the allegations showing why such an inference is reasonable here.

KPMG-US likewise errs in its arguments against joint venture liability, again disregarding and improperly disputing the factual allegations. The only elements of a joint venture under Delaware law that KPMG-US contests are joint control (or right to control) and sharing of profits and losses. As to joint control, KPMG-US's argument rests on its *ipse dixit* that there was no coordination between KPMG-US and KPMGM, ignoring the key allegation that "KPMG Mexico closely coordinates with KPMG US in connection with its … audits of U.S. companies and their subsidiaries, including Citigroup and Banamex." A411. Similarly, KPMG-US asserts that the allegations of profit- and loss-sharing are conclusory while ignoring detailed allegations that Defendants shared profits based on allocation percentages and were required to share the risks of loss. A412-14. The idea that Plaintiffs must identify precisely how profits and losses were allocated would impose a standard even beyond pleading with particularity (let alone the reasonably conceivable standard at issue here) and make pleading a joint venture in any case all but impossible.

Finally, KPMG-US identifies almost nothing to support the Court of Chancery's holding that Mexican law requires a written agreement to form an agency relationship or a joint venture. KPMG-US does not cite a single Mexican case to support this position, instead relying solely on one sentence in one U.S. law review article. In contrast, Mexican courts have held expressly that a written

agreement is not required. There is accordingly no legal basis to hold that Mexican law categorically precludes the existence of an agency or joint venture here.

ARGUMENT

In a telling omission, KPMG-US fails to mention the legal standard at issue even once in its brief: whether the Amended Complaint "states a cognizable claim under any 'reasonably conceivable' set of circumstances inferable from the alleged facts." *Winshall v. Viacom Int'l, Inc.*, 76 A.3d 808, 813 n.12 (Del. 2013). The facts alleged here make it far more than just reasonably conceivable that KPMG-US is vicariously liable based on agency and joint venture under Delaware, New York, or Mexican law.

While KPMG-US argues (Ans. Br. 11) that choice of law can be resolved at this time, it presents no argument for doing so, nor does it identify *which* law should apply under the "most significant relationship" test. Instead, KPMG-US rests on the assertion (Ans. Br. 11-12) that Plaintiffs did not raise the issue below. This is simply false: Plaintiffs argued that Delaware law should apply, but "[a]t a minimum, the application of foreign law should not be decided on a motion to dismiss with its limited factual record." A3130. The Court of Chancery also did not resolve the issue, applying Delaware law only because it found no actual conflict of law. Op. 10. Thus, because there is no plausible means of determining which jurisdiction has the most significant relationship to the claims at this stage, the Court of Chancery's

decision should be reversed if Plaintiffs state a claim under Delaware, New York,[1] or Mexican law. Regardless, as discussed below, Plaintiffs state a claim under all three.

[1] Both sides agree there is no material difference between Delaware and New York law on the agency issues in this appeal. Opening Br. 14; Ans. Br. 12, 15-16, 21, 27-28.

I. The Court Of Chancery Erred In Holding That The Amended Complaint Did Not Sufficiently Allege KPMGM Was A Sub-Agent Of KPMG-US

KPMG-US fails to confront the Court of Chancery's errors in its legal test for agency and refusal to credit the factual allegations of the Amended Complaint. Instead, KPMG-US spends roughly 20% of its Argument section (Ans. Br. 12-19) attacking a straw man by arguing that agency requires a connection between control and the wrongdoing. But as KPMG-US itself recognizes (Ans. Br. 18) after its exegesis, Plaintiffs do not dispute this point. *See* Opening Br. 24.

What Plaintiffs dispute is KPMG-US's giant leap (Ans. Br. 16-17) from the need for a connection between control and the wrongdoing to the notion that allegations that control extended *beyond* the wrongdoing somehow do not suffice to allege agency. KPMG-US cites nothing for this remarkable proposition, which is nonsensical: Where the agency relationship applies to numerous transactions, there is no legal basis to disregard allegations establishing a *broader* agency relationship that *includes* the transaction at issue. *See, e.g.*, *Billops v. Magness Constr. Co.*, 391 A.2d 196, 197-98 (Del. 1978) (finding disputed issue of fact on agency based on general right to control agent). Simply put, it is more than reasonably conceivable that if KPMG-US has a right to control (via KPMGI) *all* of KPMGM's auditing practices, then it has a right to control KPMGM's audits of OSA conducted pursuant to those practices. Regardless, as discussed below, there are detailed allegations here explaining precisely why there was control *both* over KPMGM's audits

generally *and* the OSA audits in particular, which far exceed any pleading-stage requirement.

A. The Court Of Chancery Erred As A Matter Of Law In Holding That Agency Requires Exercise Of Control Over, Rather Than A Right To Control, The Agent

KPMG-US's argument that a right to control does not suffice for agency, and that exercise of control is required, conflicts with well-established law. This Court has held repeatedly that the proper test is right to control, not exercise of control. *See* Opening Br. 16-17 (citing *Billops*, 391 A.2d at 197-98; *Lester C. Newton Trucking Co. v. Neal*, 204 A.2d 393, 395 (Del. 1964); *Melson v. Allman*, 244 A.2d 85, 87-88 (Del. 1968)). KPMG-US attempts to distinguish *Billops* as concerning a franchisor and franchisee, but *Billops* held the vicarious liability of a franchisor "flows from an actual agency relationship," not some special rule for franchisors. 391 A.2d at 197; *see id.* at 198 (if there is "the right to exercise control," then "an agency relationship exists").[2] Similarly, KPMG-US's attempt to distinguish *Newton Trucking* and *Melson* as employer-employee cases fails to explain why that factual difference matters here (nor does it, as the employer-employee relationship

[2] KPMG-US also errs in asserting (Ans. Br. 23) that the relevant language in *Billops* is *dictum*. It is the statement of the legal test, *see Billops*, 391 A.2d at 197, which is plainly part of the holding, and indeed, the Court found a disputed issue of fact on agency based not on the exercise of control, but on the "right" to terminate the franchisee for violation of the agreement or operating manual, *id.* at 198, which is similarly alleged here, A386, 392-94.

"springs" from the right to control, *Newton Trucking*, 204 A.2d at 395, not vice versa). Moreover, KPMG-US ignores that the Restatement (which this Court has consistently followed) adopts a "right to control" test, *see* Restatement (Third) of Agency § 1.01 cmt.f(1), and that agency necessarily involves the principal authorizing the agent to make decisions without the principal itself controlling each individual decision. *See* Opening Br. 17-18. The lone case KPMG-US cites (Ans. Br. 23) in fact refutes its argument. *See Patel v. Sunvest Realty Corp.*, 2018 WL 4961392, *5 (Del. Super. Ct. Oct. 15, 2018) ("[T]o establish actual agency … , a plaintiff must show the franchisor has the right to control the franchisee's business.").

KPMG-US errs in suggesting (Ans. Br. 21) that the Court of Chancery's fleeting reference to "right to control," Op. 24-25, fixes the problem. Rather, it only highlights the error. While *recognizing* the correct test of right to control, the Court of Chancery then proceeded to *apply* the wrong test of exercise of control. KPMG-US ignores the numerous places Plaintiffs cited in the opinion where the Court of Chancery applied the erroneous exercise of control test. Opening Br. 17 (*e.g.*, "KPMG[I] may have the right to control KPMG[M], but [Plaintiffs] do not allege that KPMG[I] has yet to do so in any sense," Op. 33).

KPMG-US's argument (Ans. Br. 20-21) that Plaintiffs waived this issue below is baseless. As noted above, the Court of Chancery *expressly* considered the

issue in its opinion, holding both that right of control sufficed (when stating the test) and that exercise of control was required (when applying the test). There is no plausible basis to preclude Plaintiffs from arguing against this inconsistency on the face of the opinion. *See Mumitt v. State*, 981 A.2d 1173, 2009 WL 3191709, *2 (Del. Oct. 6, 2009) (Table) ("issue is not waived for purposes of appeal" where "the trial judge addressed it *sua sponte*"). Regardless, Plaintiffs argued below that "an agency relationship exists where the principal *can control* the agent." A3116 (emphasis added); *see also* B947 (Plaintiffs' counsel at motion-to-dismiss hearing: "[T]he allegations are as to control, the same exact kind of *rights* that KPMG[I] had with respect to its member firms that were present in *Parmalat*.") (emphasis added).[3] And contrary to KPMG-US's suggestion (Ans. Br. 21), there is no requirement for Plaintiffs to have used the same exact words or cited the same precedent below.[4] In short, there is no doubt that Plaintiffs argued below that their allegations sufficed for control because they showed the ability and authority to control the conduct at

[3] There was no need to state explicitly that exercise of control was not required because KPMG-US first argued for exercise of control in its reply brief, B841, without ever mentioning this as the supposed test in its opening brief, B82-87.

[4] *See Robino-Bay Court Plaza, LLC v. West Willow-Bay Court LLC*, 985 A.2d 391, 2009 Del. LEXIS 655, *5 (Del. Nov. 30, 2009) (Table) ("argument [was] merely an additional reason in support of a proposition that was urged below"); *Wit Capital Grp., Inc. v. Benning*, 897 A.2d 172, 184 n.48 (Del. 2006) ("new" theory and arguments were "sufficiently related" to those raised below); *Watkins v. Beatrice Cos.*, 560 A.2d 1016, 1020 (Del. 1989) ("[T]he mere raising of the issue is sufficient to preserve it for appeal.").

issue—which is why the Court of Chancery decided it in its opinion, and why it is now squarely before this Court.

B. Applying The Correct Test For Agency, The Allegations More Than Suffice To Render It Reasonably Conceivable That KPMGM Is A Sub-Agent Of KPMG-US

KPMG-US fails to refute that the Amended Complaint's allegations make it reasonably conceivable that KPMGM is an agent of KPMGI and that KPMGI is an agent of KPMG-US. As Plaintiffs noted (Opening Br. 19-20), agency is a factual issue very rarely decided on the pleadings. KPMG-US ignores this Court's statement making precisely this point. *See Fisher v. Townsends, Inc.*, 695 A.2d 53, 59, 61 (Del. 1997). KPMG-US also ignores the Third Circuit's explanation for the importance of this principle, given that the facts relevant to agency are almost always within the defendant's exclusive control. *See Jurimex Kommerz Transit G.M.B.H. v. Case Corp.*, 65 F. App'x 803, 808 (3d Cir. 2003). Instead, KPMG-US string cites cases (Ans. Br. 28-29) while ignoring Plaintiffs' explanation (Opening Br. 20 n.4) as to why those cases are irrelevant here. Indeed, KPMG-US fails to cite a single case dismissing agency allegations even remotely as specific as those present here.

1. The Amended Complaint Alleges That KPMGI Is An Agent of KPMG-US

KPMG-US fails to address many of the allegations establishing its right to control KPMGI.

First, KPMG-US mischaracterizes and ignores (Ans. Br. 30) the allegations regarding the positions of KPMG-US's high-level personnel within KPMGI. For instance, KPMG-US treats as irrelevant that its "personnel make up 40% of KPMG[I]'s Global Management Team," A404, simply because this is a minority (Ans. Br. 30), notwithstanding that it is greater than any other KPMG member. KPMG-US also ignores that its Chairman and CEO was KPMGI's Global Chairman, that the last two Global Heads of Audit came from KPMG-US, and that its personnel were also KPMGI's Global Head of Advisory, Global Chief Operating Officer, and Global Head of Quality, Risk and Regulatory. A404-05. Instead, it understates the allegations as a "few shared personnel." Ans. Br. 30. But this is not a random group of employees; it is a cadre of senior KPMG-US officials acting at the highest levels of KPMGI.

Second, KPMG-US does not and cannot dispute its size and importance within KPMGI's global organization, or that it has control over the rights to the KPMG name. Opening Br. 21-22. Instead, KPMG-US notes (Ans. Br. 30) only that KPMG-US's income is less than half of the network's total. However, this fact does not rebut the strong (and certainly reasonable) inference that KPMG-US's importance to KPMGI (along with the roles of its employees within KPMGI) provides it with control over KPMGI.

Third, KPMG-US largely ignores the allegations of its particularly strong position to control KPMGI's audit practices—which are the core business of the global KPMG enterprise. Instead, KPMG-US attempts to understate the allegations as a "group of KPMG-US employees (from the Department of Professional Practice) liais[ing] with KPMG[I]." Ans. Br. 30. But the Amended Complaint alleges that—in addition to liaising with KPMGI—KPMG-US conducts both inspections of KPMG auditors and remedial responses, which entail control rights on their face. Opening Br. 22; A405-06.

In addition to sidestepping these allegations, KPMG-US fails to refute the numerous cases holding that far less detailed allegations suffice for agency (even under the more stringent federal pleading standard). *See* Opening Br. 22-23. KPMG-US's only response (Ans. Br. 13, 18-19) is that in these cases, the agency relationship was related to the claims at issue, but the allegations here are just as specific in linking agency to the claim as they were there. *See, e.g.*, *Jurimex*, 65 F. App'x at 808 (reversing dismissal based on allegations of "the necessary occurrences and reasons that [the principal] controlled its subsidiaries' actions").

Moreover, as Plaintiffs explained (Opening Br. 24) and KPMG-US ignores, the relationship between the control and the wrongdoing need only be a relationship between the *right* to control (not the *exercise* of control) and the wrongdoing. Here, it is far more than reasonably conceivable that KPMG-US's right to control

KPMGI—especially with respect to audits—extends to the right to control the audits at issue. Indeed, KPMG-US makes no argument as to why this Court should conclude, on the pleadings, that the extensive right to control auditing alleged for KPMG-US should be assumed not to cover KPMGM's OSA audits.[5]

In any event, the Amended Complaint *does* provide specific allegations of control for the OSA audits based on the overlap between KPMGM's OSA, Banamex, and Pemex audits and KPMG-US's Citigroup audits. *See* Opening Br. 25. KPMG-US does not dispute the overlap, whereby KPMG-US and KPMGM annually audited all sides of the same credit-facility advances from Citigroup to OSA based on fraudulent Pemex invoices—totaling $750 million and comprising 97% of OSA's revenue—that were the basis of Plaintiffs' harm. A285-88, 301-03, 311-39. Instead, KPMG-US argues that this does not establish control because KPMGM "was the sole auditor for both OSA and Banamex." Ans. Br. 31-32. But this factual argument evades the critical point: the question is not which entity signed the OSA and Banamex audit opinions, but which entity had a right to *control* those audits. And it is more than reasonable to infer that KPMG-US had such control given its power within KPMGI (especially over auditing practices) and the need to align the

[5] Contrary to KPMG-US's suggestion (Ans. Br. 18), Plaintiffs argued below that their allegations of control over auditing generally were sufficient. A3118, 3123. Regardless, the Court of Chancery addressed the issue, Op. 22, 33, and thus there is no basis to preclude Plaintiffs from raising it here, *supra* at 9-10.

OSA and Banamex component audits with KPMG-US's own Citigroup audits. Moreover, while KPMG-US suggests (Ans. Br. 31) that the overlapping audits go only to direct agency (rather than a sub-agency relationship), the Amended Complaint alleges control given the overlapping audits specifically based on KPMG-US's control over KPMGI, A410, which makes sense because (as alleged) KPMG-US exercised control over auditing practices of KPMG entities through KPMGI, A403-07.

2. The Amended Complaint Alleges That KPMGM Is An Agent of KPMGI

KPMG-US likewise fails to refute the extensive allegations of KPMGI's control over KPMGM. KPMG-US ignores the Court of Chancery's own conclusion that "Plaintiffs allege that KPMG[I] may have the right to control KPMG[M]," Op. 33, which suffices for agency (*supra* at 8-9) and should be the end of the inquiry at the pleading stage. KPMG-US states in a footnote (Ans. Br. 25 n.21) that there was no right to control, but without any explanation to support this assertion.

KPMG-US also ignores the factual allegations that KPMGI, at KPMG-US's behest, controls the manner and method by which KPMGM conducts its audits, and that KPMGI enforces compliance with its audit policies and procedures. Opening Br. 26; A385-88, 393-94, 399-400. Rather than address these allegations, KPMG-US characterizes them as "generalized allegations concerning the relationship between" KPMGI and KPMGM. Ans. Br. 25. But there is nothing "generalized"

about the fact that KPMGI determines, at KPMG-US's behest, precisely how KPMGM conducts its audits—including everything from audit methodology to what software it uses—and can punish or expel KPMGM if it deviates from those requirements. A387-94. Indeed, KPMG-US's position seems to be that there can be no agency (and thus no liability) unless KPMGI actually "performed [the] audit work," Ans. Br. 26, which is legally baseless, *supra* at 14. KPMG-US's suggestion (Ans. Br. 27) that the allegations of control over all audits should be read not to include control over the specific OSA audits is nonsensical, as discussed *supra* at 7, and at best raises a factual dispute that cannot be resolved on the pleadings.

KPMG-US further errs in disregarding the import of KPMGI's uncontested control over KPMG South Africa ("KPMG-SA"). Opening Br. 27-28; A389-92. According to KPMG-US (Ans. Br. 27), this does not concern the relationship between KPMGI and KPMGM. But KPMG-US provides no explanation for why KPMGM would be exempt from the same control that KPMGI exercises over other member firms—as evidenced by its control over KPMG-SA—let alone why an inference of control is unreasonable at the pleading stage given the context provided by the KPMG-SA episode.

Finally, KPMG-US has no response to this Court's precedent establishing that allegations that the principal set the policies and procedures for the alleged agent suffice for control. *See* Opening Br. 26-27 (citing, *inter alia*, *Billops*, 391 A.2d at

198). Instead, KPMG-US cites (Ans. Br. 26 n.23) only cases from outside Delaware, all of which are readily distinguishable.[6]

3. Other Cases Examining Agency Relationships Among Audit Firms Confirm The Sufficiency Of The Allegations Here

KPMG-US fails to refute the cases particular to the audit context that have accepted similar allegations as sufficient to allege agency, including *Cromer Fin. Ltd. v. Berger*, 245 F. Supp. 2d 552, 560-61 (S.D.N.Y. 2003), which denied summary judgment on a claim that Deloitte-International was vicariously liable for Deloitte-Bermuda conduct.

Moreover, as Plaintiffs explained (Opening Br. 29-30), the allegations here are virtually identical to those in *In re Parmalat Sec. Litig.*, 598 F. Supp. 2d 569, 573-80 (S.D.N.Y. 2009), for agency of Grant Thornton LLP ("GT-US") over Grant Thornton S.p.A. ("GT-Italy"), via Grant Thornton International ("GTI"). Plaintiffs noted (Opening Br. 30-31) the Court of Chancery's error in relying on a different

[6] One focused on apparent authority rather than the implied actual authority alleged here. *See McBride v. KPMG Int'l*, 2014 WL 3707977, *9 (N.Y. Sup. Ct. July 25, 2014). Another involved plaintiffs that conceded the international organization did not control member firms. *See Howard v. KPMG*, 977 F. Supp. 654, 662 (S.D.N.Y. 1997). And the rest involved plaintiffs that relied solely on allegations that member firms were a "unitary" or "combined" organization without any of the detailed allegations of control or overlapping audits present here. *See Star Energy Corp. v. RSM Top-Audit*, 2008 WL 5110919, *3 (S.D.N.Y. Nov. 26, 2008); *In re Royal Dutch/Shell Transp. Sec. Litig.*, 380 F. Supp. 2d 509, 571-72 (D.N.J. 2005); *In re Lernout & Hauspie Sec. Litig.*, 230 F. Supp. 2d 152, 171-72 (D. Mass. 2002).

Parmalat case, concerning federal securities claims, but KPMG-US still relies thereon (Ans. Br. 27-28). As to the *Parmalat* case on point, KPMG-US rests on the idea that "the vicariously liable entities *exercised* control over the audits at issue by taking steps such as removing audit personnel who raised questions about the specific audit work at issue[.]" Ans. Br. 24. But the personnel allegation KPMG-US refers to comes from the inapposite *Parmalat* opinion and concerned Deloitte, not GTI, *see In re Parmalat Sec. Litig.*, 375 F. Supp. 2d 278, 293-94 (S.D.N.Y. 2005), which was subject to agency liability based on facts materially identical to those here.

II. The Court Of Chancery Erred By Holding That The Amended Complaint Did Not Sufficiently Allege That Defendants Were In A Joint Venture

A. The Court Of Chancery Erred In Holding That The Existence Of A Joint Venture Is An Issue Of Law, Rather Than An Issue Of Fact

KPMG-US does not attempt to defend the Court of Chancery's statement that the existence of a joint venture is not a question of fact. Op. 52. As Plaintiffs explained (Opening Br. 34-35), this is a factual issue where the facts are almost always within the defendants' control, which is why it generally should not be decided on the pleadings. KPMG-US once again falls back on a waiver argument (Ans. Br. 34), but the Court of Chancery expressly decided the issue, Op. 52, which suffices for this Court's review, *supra* at 9-10. Regardless, a prior ruling in this case held that joint venture is a factual issue that could not be resolved at that time. Opening Br. Ex. C at 13-14. KPMG-US never challenged this ruling or suggested in its briefing that joint venture should be treated as a non-factual issue. Plaintiffs then treated joint venture as a factual issue in their briefing, A3126-29, and at oral argument, B944.

KPMG-US's citation (Ans. Br. 34) of a few decisions where the existence of a joint venture was decided on the pleadings only highlights how rarely this occurs and how deficient the allegations must be to dismiss at this stage. In one, as Plaintiffs explained (Opening Br. 34-35) and KPMG-US ignores, an entity undisputedly had "exclusive authority to manage" the alleged joint venture. *Wenske v. Blue Bell*

Creameries, Inc., 2018 WL 5994971, *8 (Del. Ch. Nov. 13, 2018). In the others, there were no allegations of sharing of profits and losses.[7] Here, in contrast, the Amended Complaint expressly alleges all elements of a joint venture, including sharing of profits and losses. Indeed, KPMG-US does not even attempt to distinguish the cases Plaintiffs cited, which found much less detailed allegations sufficient to survive a motion to dismiss. *See* Opening Br. 35 (citing *In re Carlisle Etcetera LLC*, 114 A.3d 592, 606-07 (Del. Ch. 2015); *Providence Creek Acad. Charter Sch., Inc. v. St. Joseph's at Providence Creek*, 2005 WL 2266490, *1-2 (Del. Ch. Sept. 9, 2005)).

B. The Allegations More Than Suffice To Render It Reasonably Conceivable That Defendants Are Part Of A Joint Venture

Replicating the Court of Chancery's analysis, KPMG-US disregards the factual allegations establishing a joint venture. KPMG-US mentions the elements under Delaware law and asserts that New York law is "substantially the same," but then proceeds to analyze the joint-venture issue using only the elements of New York law. Ans. Br. 35-39. As Plaintiffs explained (Opening Br. 36 n.9), while some

[7] *See First State Orthopaedics, P.A. v. Gallagher Bassett Servs., Inc.*, 2018 WL 2733344, *6-7 (Del. Super. Ct. May 3, 2018) ("there is nothing to suggest that [the entities] split profits, or share losses with their customers") (quotation marks omitted); *N.S.N. Int'l Indus., N.V. v. E.I. DuPont De Nemours & Co.*, 1994 WL 148271, *8 (Del. Ch. Mar. 31, 1994) ("the parties did not agree to share losses"); *J. Royal Parker Assocs., Inc. v. Parco Brown & Root, Inc.*, 1984 WL 8255, *4 (Del. Ch. Nov. 30, 1984) ("no allegations that [defendant] contributed money, property or know-how … or that [it] was to share in the profits").

of the elements are overlapping, the element of intent to form the joint venture exists only under New York law, and regardless, the allegations show such intent. KPMG-US argues that the allegations do not suffice by conflating intent to form a joint venture with "inten[t] to audit OSA together." Ans. Br. 37-38. But there is no requirement that joint venture members must intend to perform each individual aspect of the venture together, rather than have joint control over it. In any event, as discussed below, the Amended Complaint alleges facts supporting all elements of a joint venture under Delaware law.

1. Defendants Share A Community Of Interest And A Proprietary Interest In The Enterprise

KPMG-US does not dispute that the Amended Complaint adequately alleges the first and third elements—community of interest and joint proprietary interest in the enterprise. *See* Opening Br. 37, 39.

2. Defendants Jointly Controlled The Activities Of The Venture

Plaintiffs have demonstrated right of control for the reasons stated *supra* at 11-17, but regardless, the second element is satisfied based on joint control. KPMG-US does not dispute Plaintiffs' point (Opening Br. 38) that Defendants' "polic[ing] one another's day-to-day conduct" (A414) is sufficient to show joint control. Instead, KPMG-US questions (Ans. Br. 38-39) as a factual matter whether there was such policing. However, there is no basis to resolve this dispute at the pleading stage, and it is more than reasonably conceivable that such policing occurred here.

A386-94. Similarly, KPMG-US errs in disputing (Ans. Br. 39) as a factual matter whether Defendants needed to align the OSA audits with the Citigroup/Banamex audits, given that they were auditing the very same transactions. While KPMG-US asserts that Plaintiffs "do[] not allege any overlap in personnel or coordination as between the OSA and Banamex audits (much less the Citigroup audits performed by KPMG-US)," Ans. Br. 39, that is simply incorrect. The Amended Complaint alleges that "KPMG Mexico closely coordinates with KPMG US in connection with its PCAOB registration and audits of U.S. companies and their subsidiaries, including Citigroup and Banamex." A411. This allegation must be accepted at the pleading stage.

3. Defendants Have A Right To Share In The Profits And Losses

As to the fourth and fifth elements—right to share in profits and losses—KPMG-US argues (Ans. Br. 38) only that the allegations are conclusory, ignoring the key allegations at issue, including that "[u]nder KPMG[I]'s regular practices as well as KPMG[I]'s governing agreements, [Defendants] had a duty to share, and did share, in both profits and losses in their provision of services to clients worldwide." A412. As to profit-sharing, the Amended Complaint further details "profit transfers based on allocation percentages" and "payment of referral fees and service charges between and among [Defendants]." A412-13.

As to loss-sharing, the Amended Complaint alleges that Defendants "share the risk of losses flowing from their global engagements and fee commitments, including Citigroup, Banamex and Oceanografía," A413; that KPMGI requires participation in risk-sharing programs and joint management of risks, A388, 413-14; and that any problems with the OSA audits would necessarily affect the Citigroup/Banamex audits and create risk for all Defendants, A408. KPMG-US does not mention any of these allegations or the case law (Opening Br. 39-41) establishing that they suffice at the pleading stage.

III. The Court Of Chancery Erred By Holding That The Amended Complaint Did Not Sufficiently Allege A Claim Under Mexican Law

KPMG-US does not dispute it has the burden of establishing the substance of Mexican law. *See* Opening Br. 43. It failed to meet that burden here.

A. The Court Of Chancery Erred In Holding That Agency Requires A Written Agreement Under Mexican Law

KPMG-US errs in relying (Ans. Br. 41-42) on Article 2546 of the Mexican Federal Civil Code as supposedly requiring a written agreement for an agency relationship. As Plaintiffs explained (Opening Br. 44; A3198-99) and KPMG-US does not dispute, Article 2546 concerns only the relationship of a power of attorney. Instead, KPMG-US asserts (Ans. Br. 41-42) that power of attorney in Mexico covers agency relationships more generally. KPMG-US's lone citation (Ans. Br. 42) for this proposition is a one-sentence aside in a U.S. law review article, which in turn cites nothing except Article 2546 itself. *See* Humberto Gayou & Robert G. Gilbert, *Legal Building Blocks for Structuring Sales in the Mexican Market*, 25 St. Mary's L.J. 1115, 1136 & n.87 (1994).

In sharp contrast, Plaintiffs cited *Mexican case law* holding that there was an agency relationship absent a written agreement. *See* Opening Br. 44. KPMG-US argues (Ans. Br. 42-43) that the policy justifications for recognizing an agency relationship were stronger in those cases than they are here. But that misses the point: If, as Plaintiffs have established, policy rationales can justify an agency

relationship under Mexican law, then the Court of Chancery's interpretation of Article 2546 (which has no public-policy exception) necessarily is wrong. *See* Opening Br. 44-45. Absent that interpretation, neither the Court of Chancery nor KPMG-US provides any basis under Mexican law to deny the existence of an agency relationship here. And there is no basis to hold that a law on power of attorney and a single inapposite U.S. law review article satisfy KPMG-US's burden to prove that the substance of Mexican law precludes an agency relationship under any reasonably conceivable view of the alleged facts.

B. The Court Of Chancery Erred In Holding That A Joint Venture Requires A Written Agreement Under Mexican Law

KPMG-US likewise fails to justify the Court of Chancery's holding that there must be a written agreement for a joint venture. KPMG-US recognizes (Ans. Br. 44) that Article 1988 allows for joint liability based on a written agreement *or* by law. And as Plaintiffs explained (Opening Br. 45-46), a law—Article 1917—creates joint liability for "all parties that cause a common injury." A3194-95, 3413. KPMG-US asserts that Article 1917 is about joint liability, not joint ventures, but the same is true of Article 1988—and regardless, the issue here *is* liability (not some other legal implications of joint ventures). KPMG-US's only other argument (Ans. Br. 44) is that Plaintiffs supposedly did not allege causation. But the Amended Complaint alleges that KPMG-US, together with KPMGI and KPMGM, caused Plaintiffs' injuries. A256-57, 286, 335-36, 339. KPMG-US cites no Mexican law

or precedent for its unsupported suggestion that vicarious liability is incompatible with causation.

CONCLUSION

This Court should reverse the dismissal of the Amended Complaint and remand for further proceedings.

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CERTIFICATE OF SERVICE

I, David E. Ross, hereby certify that on February 8, 2021, I caused true and correct copies of the foregoing *Appellants' Reply Brief* to be served through File & ServeXpress on the following counsel of record:

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