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Case Number 152,2022

IN THE SUPREME COURT OF THE STATE OF DELAWARE

LONG DENG AND MARK FANG,	)	
	)	
	)	
Defendants/Counterclaim and Third Party Claim Plaintiffs Below, Appellants,	)	Case No. 152, 2022
	)	
	)	On Appeal From the Court of
v.	)	Chancery:
	)	
DENGRONG ZHOU,	)	C.A. No. 2021-0026-JRS
	)	
	)	
Plaintiff/Counterclaim Defendant below, Appellee.	)	

APPELLANTS' [CORRECTED] OPENING BRIEF

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NATURE AND STAGE OF PROCEEDINGS

In December 2019, when iFresh was trading below $1/share and facing delisting from the Nasdaq, Dengrong Zhou ("Appellee" or "Zhou") presented himself to iFresh CEO and founder Long Deng ("Deng"). Appearing to be a connected, wealthy businessman, Zhou claimed he would bring in multi-million-dollar investments if iFresh followed his business advice and acquired supposedly highly synergistic companies Zhou would introduce.

Deng's research revealed an online article about a pyramid scheme in China called "Xiangtian" that seemed to be potentially associated with Zhou. But Zhou reassured Deng by vehemently denying having the "slightest connection" to Xiangtian. Deng proceeded with Zhou's investment, which he made with a "co-investor"; appointed an experienced CPA who Zhou recommended as iFresh's CEO; and finally undertook two additional all-stock M&A transactions Zhou brokered. iFresh also obtained a contractual warranty that Zhou's purported "co-investor" was not Zhou's "nominee or agent" and was investing for his "own account."

One week after the last Zhou-brokered transaction closed, Zhou and his supposed "co-investor," buying for his "own account," filed a Form 13D disclosing the two were in fact operating as a "group." Within a month, Zhou informed Deng that iFresh's new "shareholders in China" had decided Deng should step down and Zhou should take over. Deng and his fellow board member, Mark Fang ("Fang"),

made clear that they would resist, so Zhou and his co-shareholders delivered a written consent to remove Deng and Fang, simultaneously filing suit seeking a declaration of the consent's validity under Section 225 of the DGCL. Deng and Fang counterclaimed, alleging that Zhou and his co-voters obtained the shares they voted through deception.

It was not until discovery that Deng and Fang learned that iFresh had fallen prey to Zhou, who intended to use iFresh in a criminal pyramid scheme he was operating in China, and to do so through Trojan horse shareholders who obtained iFresh shares at his behest. As for the CFO that Zhou had recommended, she turned out to have been working behind the scenes for Zhou the whole time.

At trial, Deng and Fang presented unrebutted evidence that iFresh's CFO was Zhou's puppet and that Zhou told restless investors in his scheme that iFresh would soon be absorbed. Zhou even admitted that he operated the scheme and that he was to "get" all the iFresh shares issued to the supposed "co-investor" contractually warranted not to be his "nominee or agent."

Following a two-day bench trial in January 2022, the Court of Chancery issued a Memorandum Opinion dated April 6, 2022 (hereinafter "Opinion" or "Op."), declaring that the written consent validly removed Deng and Fang from iFresh's board and replaced them with Zhou's board candidates. Ex. A, hereto. Deng and Fang timely appealed.

SUMMARY OF THE ARGUMENT

1. The "peculiar knowledge" rule: even though "Zhou was indisputably investigated, detained and sentenced for criminal activity in China in connection with Xiangtian and a multi-level 'pyramid' scheme," Op. at 28, the trial court concluded the defendants could not have justifiably relied on Zhou's extra-contractual misrepresentations and omissions regarding the Xiangtian pyramid scheme because his criminal history was in the public record. *Id.* at 30. This erred in three respects.

a. *First*, New York law allows sophisticated parties to prove justifiable reliance if the true facts are within the "peculiar knowledge" of the misrepresenting person, even where some related information is public. The trial court erred in ruling that the peculiar knowledge rule did not apply because of the defendants' sophistication. Op. n. 122.

b. *Second*, in considering only the public nature of Zhou's past criminal conviction to assess reliance, the trial court ignored the facts adduced at trial that were in Zhou's *peculiar* knowledge, including that Zhou was continuing to operate the Xiangtian pyramid scheme and that his very purpose in transacting with iFresh was to absorb it into that scheme. Op. at 30.

c. *Third*, the trial court erroneously found that Zhou's denials regarding Xiangtian were not reliable because of "a rather broad integration clause," and furthermore, "were not the subject of any specific representations in the [] Purchase Agreement[]" through which Zhou obtained his shares. *Id.* at 29. But under the peculiar knowledge rule, frauds are not insulated by even specific contractual disclaimers, and the party defrauded by omission of information that is another's peculiar knowledge is discharged from any duty to discover or contractually guard against such fraudulent omission.

2. Breach of contractual warranty: where a buyer has protected himself with a contractual warranty against a foreseeable concern, New York law makes those warranties "absolutely" enforceable. Here, Zhou warranted that his co-investor was not his nominee or agent, which warranty the evidence revealed to be false. The trial court, however, erroneously required "fraud reliance" upon this express contractual warranty and applied a clear and convincing standard to the evidence.

a. Building upon this error of law, the trial court ignored a slew of evidence to erroneously conclude, despite a direct admission at trial by Appellee that he would "get" all the shares issued to his "co-investor," that the co-investor was not Appellee's agent or nominee.

3. Waiver: the trial court erred by holding that the defendants had waived their claim that Zhou aided and abetted iFresh CFO Amy Xue's breach of fiduciary duty. Overwhelming evidence revealed in discovery and presented at trial established fiduciary misconduct, and Xue's and Zhou's fiduciary misconduct was raised hundreds of times in discovery, pretrial, at depositions, at trial, and post-trial. Equally erroneously, having found waiver of the theory, the trial court declined to evaluate the evidence underlying such fiduciary misconduct when considering defendants' consistently argued fraud theory for invalidating the written consent.

STATEMENT OF FACTS

I. In Late 2019, iFresh Seeks To Maintain Its Nasdaq Listing And Is Introduced To Zhou.

iFresh, Inc. is an east-coast grocery chain founded by Long Deng and incorporated in Delaware. A1546. In July 2019, Nasdaq notified iFresh, then a publicly-listed company, that its listing was at risk. A0119-0123. At the time, iFresh was in the midst of a proposed merger with a company called Xiaotai, which would have enabled it to regain listing compliance. *Id.* But when iFresh learned that Xiaotai was under investigation by Chinese authorities for illegal fundraising, it immediately cancelled the merger, even though this deprived it of much needed capital needed to regain listing compliance, again jeopardizing iFresh's Nasdaq listing. A0115-0118; A0119-0123.

Deng explored options for returning to compliance, including that iFresh acquire a Florida-based fruit company he owned, and obtained a compliance extension from Nasdaq to make that acquisition. A0202. This is when Dengrong Zhou was introduced to Deng. A1245-1246; A0164. After the two met, Zhou immediately suggested that iFresh should instead acquire a synergistic company based in China called Jiuxiang Lantian ("Jiuxiang"), and that Zhou would broker the deal. A0166.

In considering this offer, Deng investigated. He found an article about a pyramid scheme in China called Xiangtian, which he thought might have been

related to Jiuxiang, and asked Zhou about it. A0165. Zhou denied any connection: "the company that is prepared to work with you is called Beijing Jiuxiang Lantian Company! This company is engaging in e-commerce supermarket! Not Xiangtian company! You don't mix it up! The due diligence work of the U.S. auditor Friedman was completed yesterday! Sales performance is spectacular!" A0166.

Deng forwarded Zhou the article he found, which discussed a "'Xiangtian' original share scam that went on [for] 8 years." A0167. In response, Zhou reiterated that "Jiuxiang … [h]as not the slightest connection with Xiangtian! Jiuxiang [] is an e-commerce supermarket! It's an independent legal person! The Friedman U.S. that went to perform due diligence, they are not idiots! Legal due diligence is not child's play! Rest assured!" A0167-0168. Zhou described the article as consisting of "[i]ntentionally made up rumors" and an effort at "[b]lackmail and extortion[.]" *Id.*

Having thus mollified Deng, Zhou continued to ingratiate himself to iFresh's founder, including by helping Deng raise humanitarian aid for the emerging covid outbreak. A1487. Believing Zhou to be a decent person, and with others having vouched for him, Deng decided to hold off on acquiring the Florida fruit company and to instead explore the Jiuxiang acquisition. A1514.

II. Zhou Influences iFresh To Acquire Various Entities And Appoint His Recommended CFO.

Soon, Zhou offered to broker an additional acquisition of an herbal wine company called Rongentang ("RET Wine"). A0219. By March 2, 2020, discussions had advanced sufficiently that Zhou introduced Deng to his business associate David Cheng ("Cheng"), who launched a group chat announcing a "Game Plan" for "IFMK" *i.e.*, iFresh's Nasdaq ticker, to acquire RET Wine and Jiuxiang; increase the number of board seats; and hire a new CFO that Zhou recommended, Amy Xue, to replace the CFO it just lost. *Id.* Xue, a CPA, became iFresh's CFO on March 10, 2020. A0225.

Xue immediately became responsible for conducting diligence into RET Wine and for negotiating a proposed $2.5 million private investment into iFresh by Zhou and a co-investor named Qiang Ou. A1173; A1185-1186 (Deng testimony that she was responsible for diligence); A1416 (Zhou testimony that she negotiated for iFresh).

Based on her fluency in both English and Chinese, Deng also asked Xue to "explain [both transactions] to the board." A1527. In that capacity, Xue assured an iFresh board member that RET Wine's financials were reliable because it was "audited by Friedman LLP [when the RET Wine entities] were subsidiaries of XT Energy … a OTCQB Company." A0236.

On March 20, 2020, Xue presented the "deal structure of [the proposed] private placement of $2.5m[illion] and acquisition of [RET Wine]" to the iFresh board for approval. A0239. Between then and when the deal was signed, she also sent the board diligence and valuation information for RET Wine, "spoke" with board members about it, and provided "information of [the] investors" who would be doing the private placement. *Id.* (showing that information conveyed to the board about RET Wine and the "two investors," Zhou and Ou, came from conversations "with Amy[,]" documents sent "[o]n behalf of Amy[,]" and "call[s] with Mr. Deng *and Amy*"). A0238-A0239.

On March 22, 2020, Deng and Zhou discussed terms that Zhou had asked Amy to transmit, and Deng himself "talked to Amy to see what approach can be used to convince the independent … directors." A0178-0180.

On March 25, 2020, Zhou entered into a Share Purchase Agreement ("SPA") to purchase iFresh shares along with Ou as his purported "co-investor." A0321. To ensure that Ou was not a straw buyer, iFresh negotiated a contractual warranty that both investors were "purchasing the Shares for [their] own account" and "not as a nominee or agent." A0317 (§ 3(c)).

Zhou conditioned $1 million out of the $2.5 million he and Ou would invest on the RET Wine acquisition. A0323. So, on March 26, 2020, the day after signing

the SPA, iFresh also entered into an agreement to buy RET Wine for 3,852,372 iFresh shares. A0328. The Zhou-Ou private placement closed on April 6, 2020.[1]

Zhou was adamant that the Jiuxiang transaction go through. Over the next several months, he badgered Deng about Jiuxiang, touting its sales, membership, and growth figures, A0184-0185; promising that completing the deal would attract $5-10 million in *additional* investment, *id.* at A0189; and warning that failure to timely complete the deal would result in the purchase price increasing. *Id.* at A0190. The Jiuxiang transaction closed on August 24, 2020, with iFresh issuing 5,036,298 shares in consideration for the acquisition. A0486-0515.[2]

[1] Ex. D, April 6, 2020 iFresh Form 8-K: iFresh SEC filing (sec.gov)
[2] Ex. E, August 24, 2020 iFresh Form 8-K: iFresh SEC filing (sec.gov)

III. Zhou And His Allies Deliver A Written Consent Purporting To Remove iFresh CEO Deng And Board Member Fang And File A Section 225 Action.

On September 4, 2020, one week after the Jiuxiang transaction closed, Zhou and Ou jointly filed a Form 13D pursuant to 17 C.F.R. §240.13d-1(a), disclosing for the first time that they were holding iFresh shares as a "group." A0519-0521. The filing also disclosed for the first time that Zhou and Ou had borrowed the $1.5 and $1 million they respectively used to purchase iFresh shares, both from Zhou's nephew through "oral" agreements. *Id.*

On October 7, 2020, Zhou told Deng that iFresh's "shareholders in China" (*i.e.*, the sellers of RET Wine and Jiuxiang who'd only recently received their iFresh shares) had determined that Deng should relinquish control of iFresh, and threatened to instigate a criminal investigation in China if Deng did not comply. A0196-0197.

Now suspecting that the RET Wine and Jiuxiang acquisitions probably had been Trojan horses, Deng attempted to rescind them. On November 17, 2020, a month after Zhou's threats, Deng told one of Jiuxiang's sellers that iFresh intended to cancel shares issued as part of the RET Wine and Jiuxiang transactions and unwind the mergers, and that iFresh's attorneys were drafting the paperwork. A0640.

On January 12, 2021, in response to Deng's move to unwind the transactions and before Deng could convene a board meeting to do so, Zhou delivered a Written

Consent signed by himself, Ou, as well as the sellers of RET Wine and Jiuxiang, purporting to resolve to remove Deng and Fang from the board. A0539-0551. He simultaneously filed the Section 225 action against Deng and Fang in the Court of Chancery, seeking a declaration that the consent was valid. A0553. Deng and Fang counterclaimed, seeking to invalidate the consent. A0562.

IV. Discovery Reveals That Zhou Founded The Xiangtian Pyramid Scheme And Sought To Take Over iFresh, A Nasdaq-Listed Company, To Further His Scheme.

Discovery was stymied by Zhou, and some of his highly relevant messages on WeChat, the most popular messaging application in China, were not produced until weeks before trial and only then after defendants had pressed for this information for months and engaged in motions practice. A0889-890; A0898-0899; A0912-0914. These messages, other discovery, and evidence at trial told a starkly different story from the information the defendants had at the time iFresh entered into transactions with Zhou and the entities promoted by him.

A. Zhou Was The Founder Of The Xiangtian Pyramid Scheme.

After this action was filed, the defendants uncovered a Chinese 2017 criminal verdict convicting Zhou's co-conspirator in a pyramid scheme, which discussed Zhou's own criminal record. A0084. The verdict revealed that Zhou founded a pyramid scheme selling shares of "Xiangtian Holdings (Group) Co., Ltd.," "under the pretext that [it] would soon be listed on the main board of NASDAQ in the United States," upon which the scheme would "distribute original [publicly listed] shares to the investors[.]" A0085-0086. The scheme "used [a] … system of remuneration to … recruit[] people" into a pyramidal structure. *Id.*[3]

[3] As Zhou would admit at trial, he is the founder of Xiangtian Holdings Group Co., Ltd., the entity referred to in the verdict. A1282-1284. And, as the verdict makes clear, that is the entity through which the Xiangtian pyramid scheme is carried out.

B. Zhou Sought To Incorporate iFresh Into His Criminal Scheme.

Discovery in the Section 225 action—especially discovery into Zhou's private WeChat conversations—revealed that Zhou sought to incorporate iFresh *into* his Xiangtian pyramid scheme, principally because iFresh was a Nasdaq-listed company—a fact that Zhou used to impress investors in the pyramid scheme. Zhou's private WeChats revealed a 2018 contract showing that David Cheng—whom Zhou later introduced to iFresh to facilitate the RET Wine transaction—had been retained to get Xiangtian's "company" up-listed to the Nasdaq. *See* A0095; A1296.

By late 2019, however, those efforts had failed. A1328-1330; A1336-1337. Zhou was panicked, telling Cheng in private WeChats that it was a "[c]ritical time!"; that they "[c]annot retreat!" from their Nasdaq run; and that it would be "[t]otal failure [if they] retreat[ed]!" A0104; *see also* A1337 ("Q. And the reason why this is a critical time was because XT Energy's NASDAQ uplisting attempt had failed. Right? A. Correct.").

On February 14, 2020—less than a month after Zhou had told Deng not to worry about Xiangtian—Zhou and Cheng discussed their plan to "re-b[r]and' [iFresh] as 'Xiangtian supermarket.'" A0114; *see also* A0217 (PowerPoint circulated between Zhou and Cheng, uncovered in discovery, in which iFresh is rebranded "Xiangtian Supermarket Group.").

Similarly, on March 27, 2020—the day iFresh agreed to acquire RET Wine in exchange for iFresh stock—Zhou forwarded the Form 8-K announcing the acquisition to a WeChat user with the username "Eiffel Tower," A0353, who was married to a Xiangtian pyramid scheme investor. A1430. Zhou confided to Eiffel Tower that iFresh's acquisition of RET Wine was part of a plan for *Xiangtian* to acquire *iFresh*, telling her that the shares issued to acquire RET Wine, added to the shares issued to Zhou himself and his "co-investor" Ou, made "us," *i.e.*, Xiangtian, iFresh's largest shareholder. A0353. Zhou also referenced iFresh's forthcoming acquisition of Jiuxiang, which would also involve an issuance of iFresh stock. *Id.* ("There is one more piece that will be listed soon afterwards! … By then Xiangtian will leap into the air and fly!"). *Id.* at A0355. He exhorted Eiffel Tower to secrecy. *Id.* ("Pay attention to confidentiality!").

A few days later, Zhou asked David Cheng to head off potential "class action" litigation in China, expressing concerns that otherwise the two of them would "be finished completely!" and "[i]ncluded in the [Interpol] red warrant!" A0214; A1431 (Q. "And you're telling Cheng to tell [a Xiangtian investor] to stop causing trouble. … A. "Correct."). As before, Zhou told Cheng to "be more low key!" A0214.

Zhou's concerns had a basis: by July 2020, a number of Xiangtian investors had formed a "shareholder rights" group to accuse him of fraud; Zhou responded by

threatening to revoke their share allocations and cajoling them with promises of a return soon. A0454; A0461.

At trial, Zhou admitted that Xiangtian is a pyramid scheme, but argued that the victims should blame those immediately above them in the pyramid for any losses, not him. A1439 ("Q. So the people below you took his money in the pyramid scheme, correct, not you? A. Correct. Well, I didn't take the money. They have a team leader. Their team leader took the money.").

C. Zhou Planned To Use iFresh To Sell A Xiangtian Cryptocurrency.

Zhou also marketed a Xiangtian cryptocurrency, XTT, to participants in the Xiangtian pyramid scheme. His private WeChats contained multiple versions of an XTT "whitepaper" touting the it as backed by "two high-quality stocks" that were "put on [N]asdaq with stock code of iFMK and XTEG"—that is, iFresh and XT Energy, another Xiangtian-affiliated company. A0444 (whitepaper); *cf.* A0371 (Zhou sending the whitepaper to his "co-investor" Ou). Zhou sent WeChats promoting XTT to investors in the Xiangtian pyramid scheme, proclaiming that Xiangtian would soon control iFresh and emphasizing that iFresh was a Nasdaq-listed stock. *See generally* A0526.

D. The iFresh Shares Issued To Zhou's "Co-Investor" Qiang Ou Were Really Controlled By Zhou, In Breach Of A Contractual Warranty That Ou Was Not Zhou's Agent.

Ou testified at his deposition that even before his purported co-investment in iFresh closed on April 4, 2020, he "report[ed] to Mr. Zhou," and "did … what [Zhou] asked [him] to do." A0744. Xue and Zhou's private WeChats confirmed that, when advising Zhou on how to obtain more iFresh shares, Xue always treated the entire $2.5 million investment as Zhou's. A0131-0133. Zhou and Xue's contemporaneous WeChat also showed that on April 1-2, 2020, Zhou personally arranged for the fund transfers underlying he and Ou's "co-investment." A0148-0153. Zhou also told Eiffel Tower that the iFresh shares issued to "me and Qiang Ou" and RET Wine's sellers meant "[t]he number one major shareholder *is us*." A353-0354 (emphasis added).

Zhou testified that the first proposed price for his and Ou's purported co-investment was "68 cents per share[,]" and that "[u]sing 68 cents [per share] as the price, *I would have gotten* 3,670,000 shares." A1265 (emphasis added). 3,670,000 times 68 cents is exactly $2.5 million. Put differently, Zhou expected to personally get all the shares issued pursuant to the $2.5 million "co-investment." This was contrary to both his and Ou's warranty that they were "purchasing the Shares for [their] own account … , not as a nominee or agent." A0317.

E. Zhou's Recommended CFO For iFresh, Amy Xue, Assisted Zhou In His Takeover.

It also turned out that Xue, who became iFresh's CFO in March 2020 at Zhou's recommendation, was working for Zhou all along, and had been part of his plan since long before her appointment. The week before Xue was appointed as iFresh's CFO, Zhou forwarded information about RET Wine to Xue and asked her to use it to "get [a] higher []valuation [of RET Wine], get more shares [of iFresh]!" A0124; A1351-1352; A0100 (showing Amy X[ue] present in a RET Wine "valuation working group" along with Zhou long before it was marketed to iFresh for acquisition).

Five days after being appointed CFO, Xue met with iFresh's board to discuss the RET Wine acquisition, telling Zhou beforehand she would "report" back to him. A0130. Several days later, Xue paid for and transmitted RET Wine's valuation to the board. A0134 (Xue obtaining RET Wine valuation); A0239 (Xue March 20, 2020 e-mail to board attaching valuation); A0248 (valuation). Over the same span of time, Xue and Zhou discussed how to maximize the number of iFresh shares Zhou would end up owning so he can take control of iFresh cheaply and efficiently. A0130-0133.

Thus, in a private WeChat group involving both Zhou and Cheng, Xue stated their goal plainly: "*Our purpose* is very clear: use the simplest and [most] convenient method … to acquire [iFresh] and control the risk of the other party [] mess[ing]

around." A0228; A1415 (Zhou acknowledging that Xue was referring to iFresh). As she explained: "[t]he higher [iFresh's] stock price, *our* cost of acquisition will be higher. … Right now, the key is *how to negotiate with Long Deng*." A0228-0229 (emphases added).

F. Zhou's Representations That Jiuxiang Had No Relationship To Xiangtian Were False.

Discovery revealed deep, undisclosed ties between Jiuxiang and Xiangtian. In April 2019, Zhou messaged a WeChat group, announcing the launch of Jiuxiang's e-commerce platform, Jiayoubei. A0101. A large proportion of Jiuxiang's sales during its pre-acquisition audit were driven by "Xiangtian group cash order sales." A0221. Zhou also thanked "Xiangtian's business colleagues … shareholders and … staff" for "continu[ing] to work hard to complete the marketing and sales work of Jiayoubei marketplace!" A0365.

V. The Case Proceeds To Trial; The Trial Court Rules In Zhou's Favor.

A. Zhou Knew Of Defendants' Focus On Xue's Fiduciary Misconduct In This Litigation.

As discovery progressed, Zhou had been on notice for many months that the defendants were focused on Xue's fiduciary misconduct at Zhou's direction. The defendants' original counterclaims pled "on information and belief" that "Zhou's sole purpose in appointing Amy Xu[e] [as iFresh's CFO] was to ensure that the RET Wine and Jiuxiang acquisitions proceeded." A0584 (Counterclaims ¶47). Since inception, defendants also alleged a "conspiracy" that "fraudulently induced iFresh to sell [its] stock" to Zhou and his collaborators. A0585-0586; A0592; A0595; A0598; A0600-0601.

In discovery, defendants subpoenaed Xue and Zhou's counsel represented her, ultimately producing nothing because she had already deleted her WeChat with Zhou. *See* A0912; A1139-1140[4] Zhou was then extensively deposed about her using existing discovery, with her name coming up 47 times during his deposition. A0787.

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[4] *Every single party* to these transactions who communicated with Zhou either deleted, or "lost" phones containing, those communications. In addition to Xue, who was outside of the trial court's subpoena power and did not testify at trial, both of the third-party defendant sellers of Jiuxiang and RET wine who were deposed claimed to have lost their phones. A0622 (Meng Liu); A0685 (Kairui Tong). Ou, Zhou's "co-investor," "erased" all of the relevant chats he had with Zhou. A0905. For his part, Zhou "dropped the phone [he used to chat with Cheng] in water." A1332-1333.

On the eve of trial, Zhou moved in limine seeking to exclude evidence regarding, *inter alia*, Zhou's behind-the-scenes dealings with Amy Xue, which defendants opposed by pointing to the "our purpose chat" and arguing that Xue was "Zhou's co-conspirator." A1071. Defendants also sought adverse inferences given Zhou and Xue's mutual deletion of voice messages between them, again pointing to the same chats. A1077-1080.

Xue's name was mentioned 57 times in Appellants' pre-trial brief, in which they argued that her and Zhou's conduct constituted "fraud and fiduciary misconduct" that warranted invalidating Zhou's votes. A1020. Xue's name came up 54 times in two days of trial, with all three witnesses testifying extensively about her activities, and Zhou's generated over 10 transcribed pages of testimony regarding his WeChat messages with Xue, essentially claiming that their WeChat conversations reflected Xue's negotiations on behalf of iFresh. A1410-1419.

B. The Trial Court Ruled That The Consent Was Valid, Finding The Defendants' Counterclaims Waived.

The trial court issued an opinion declaring the consent to be valid and rejecting the defendants' counterclaims. Ex. A. First, the trial court rejected the defendants' argument that Zhou's denials of being involved in the Xiangtian pyramid scheme constituted fraud, concluding that Zhou's misrepresentations and omissions could not form a basis for fraud where the SPA contained a broad integration clause, that the defendants did not prove by clear and convincing evidence that the transaction

would not have been consummated had the misrepresentation been detected before closing, mainly because Zhou's conviction was a matter of public record. *Id.* at 22-31. The trial court did not consider evidence showing Zhou's peculiar knowledge of his continuing operation of the Xiangtian pyramid scheme and his plan to incorporate iFresh into the scheme. *Id.*

Next, the trial court concluded that Zhou did not induce iFresh to enter into the SPA with Zhou and Ou by falsely warranting that Ou was acting on his own account when in fact he was a straw buyer acting at Zhou's behest. *Id.* at 23-25, 31-32. The trial court explicitly applied fraud elements and evidentiary standards to this express contractual warranty, and failed to consider the defendants' breach of warranty theory.

Finally, the trial court rejected the defendants' contention that Zhou aided and abetted Xue's breach of her fiduciary duties to iFresh as its CFO, finding that the argument was waived. *Id.* at 15-16. Having found the fiduciary duty theory waived, the trial court did not consider the evidence supporting such a breach of duty for any purpose, such as fraud.

Deng and Fang timely appealed.

ARGUMENT

I. THE TRIAL COURT MISAPPLIED NEW YORK LAW TO ZHOU'S MISSTATEMENTS AND OMISSIONS.

A. Question Presented.

Did the trial court reversibly err in holding that New York's peculiar-knowledge rule cannot be invoked by sophisticated parties?

Preserved at A1636-1644; A1752-55.

B. Standard and Scope of Review.

"This Court has previously held that determinations of foreign law 'are treated as rulings on a question of law and are subject to *de novo* review.'" *N. River Ins. Co. v. Mine Safety Appliances Co.*, 105 A.3d 369, 381 (Del. 2014).

C. Merits of the Argument.

i. The trial court erred in holding that the peculiar knowledge rule cannot apply to sophisticated parties.

The trial court held that "New York's 'peculiar knowledge' carve out to fraudulent misrepresentation is inapplicable" where "Defendants and iFresh are sophisticated parties who were represented by counsel when entering into each of the purchase agreements at issue." Op. at 31 n.122. For this proposition, the trial court cited to *Psenicska v. Twentieth Century Fox Film Corp.*, 409 F. App'x 368, 371 (2d Cir. 2009), and *RAA Mgmt., LLC v. Savage Sports Hldgs., Inc.*, 45 A.3d 107, 115 (Del. 2021). But as an unpublished *federal* case that predates governing New York state cases arriving at opposite results, *Psenicska* is not binding authority. *See*

Berkshire Bank v. Pioneer Bank, 2021 NY Slip Op 50619(U), ¶ 12 (Sup. Ct. 2021) ("this Court is obliged to follow the precedent of the New York State Court of Appeals and the Appellate Divisions, not the lower federal courts."). Further, while the trial court cited *RAA* as a recent *2021* decision (Op. n. 122), it is in fact a *2012* decision that relied exclusively on *Psenicska* and its equally outdated precursor from 1998—*Warner Theatre Assocs. Ltd. P'ship v. Metro. Life Ins. Co.*, 149 F.3d 134, 136 (2d Cir. 1998).

New York law is clear that failure to discover matters within the "peculiar knowledge" of the party accused of fraud does not preclude justifiable reliance. *Tahini Invs., Ltd. v. Bobrowsky*, 99 A.D.2d 489, 490 (N.Y. App. Div. 1984) ("[E]ven where the parties have executed a specific disclaimer of reliance on a seller's representations, a purchaser may not be precluded from claiming reliance on any oral misrepresentations if the facts allegedly misrepresented are peculiarly within the seller's knowledge."); *see also Basis Yield Alpha Fund v. Goldman Sachs Grp., Inc.*, 980 N.Y.S.2d 21, 30 (N.Y. App. Div. 2014) (same) ("*Basis Yield I*").

The rule also applies where "the truth theoretically might have been discovered," *Basis Yield Alpha Fund Master v. Stanley*, 136 A.D.3d 136, 145 n.7 (N.Y. App. Div. 2015) ("*Basis Yield II*"), and "even when [the misrepresentations] relate to matters of public record." *LBBW Luxemburg S.A. v. Wells Fargo Securities LLC*, 10 F. Supp. 3d 504, 517 (S.D.N.Y. 2014).

And, contrary to the trial court's decision, the peculiar knowledge rule "applies regardless of the level of sophistication of the parties." *TIAA Glob. Invs., LLC v. One Astoria Square LLC*, 2015 NY Slip Op. 01768, ¶ 7 (App. Div. 1st Dept.). Thus, in *Loreley Fin. (Jersey) No. 3 Ltd. v. Citigroup Global Markets Inc.*, the court allowed "sophisticated commercial parties" to pursue a fraud claim against Citigroup based on "Citigroup's peculiar knowledge" about "a scheme that no investor, sophisticated or not, could have discovered." 987 N.Y.S.2d 299, 307 (N.Y. App. Div. 2014). And in *Basis Yield II*, the court found that a mutual fund—which the court expressly identified as "a sophisticated investor"—"justifiably relied" on facts that "were peculiarly, even if not exclusively, within Morgan Stanley's knowledge." 136 A.D.3d 136 (N.Y. App. Div. 2015).

In recent years, the peculiar knowledge rule has been successfully used to establish reliance by major international banks, global insurance companies, and famously aggressive hedge funds. *See China Dev. Indus. Bank v. Morgan Stanley & Co. Inc.*, 927 N.Y.S.2d 52, 53 (App. Div. 1st Dept.); *Allstate Ins. Co. v. Ace Sec. Corp.*, 2013 NY Slip Op 31844(U), ¶ 28 (Sup. Ct.); *Metro. Life Ins. Co. v. Stanley*, 2013 NY Slip Op 31544(U), ¶ 26 (Sup. Ct.); *Harbinger Capital Partners Master Fund I, Ltd. v. Wachovia Capital Mkts., LLC*, 2010 NY Slip Op. 51046(U), ¶ 7 (Sup. Ct.).

The peculiar knowledge rule has also been applied to a wide variety of factual settings. *See, e.g.*, *KS Trade LLC v. Int'l Gemological Inst.*, 141 N.Y.S.3d 452, 456 (N.Y. App. Div. 2021) (gems trade); *Koch v. Greenberg*, 626 F. App'x 335, 338 (2d Cir. 2015) (wine trade); *Dandong v. Pinnacle Performance Ltd.*, 2011 WL 5170293, at *14 (S.D.N.Y. Oct. 31, 2011) (in "credit-linked notes" transaction, where "even a sophisticated investor armed with a bevy of accountants, financial advisors, and lawyers could not have known that [a party] would select inherently risky underlying assets and short them").

The Southern District of New York recently rejected the argument that a party "led by sophisticated businesspeople and represented by sophisticated legal counsel," and who "failed to conduct minimal due diligence," could not show reasonable reliance as a matter of law." *Rekor Sys., Inc., v. Loughlin*, 2022 WL 789157, at *1, *7 (S.D.N.Y. Mar. 14, 2022). The court reasoned that one party's sophistication does not give another party "license to tell him one thing and then conceal from him facts peculiarly in [the counterparty's] possession that would demonstrate something to the contrary." *Id.*

These authorities establish that New York does not regard a party's sophistication as a bar to application of the peculiar knowledge rule, as the trial court here held. The trial court's application of New York law was erroneous and this Court should reverse.

ii. The trial court erred in concluding that there could be no reasonable reliance on a misrepresentation where the true facts were a matter of public record.

The trial court erred in concluding that "Defendants could not have reasonably relied on Zhou's [January 16] messages to Deng because Zhou's conviction was a matter of public record." Op. at 29-30. Under New York law, "where … the facts were peculiarly within the knowledge of the defendants and were willfully misrepresented, the failure of the plaintiffs to ascertain the truth by inspecting the public records is not fatal to their action." *Todd v. Pearl Woods, Inc.*, 20 A.D.2d 911 (N.Y. App. Div. 1964); *see also LBBW*, at 517-519 (same); *Basis Yield II* at 144-45, n.7 (plaintiff can "justifiably rely" on facts that "were peculiarly, *even if not exclusively*, within Morgan Stanley's knowledge.") (emphasis added).

iii. The trial court erred by applying a general integration clause to bar reliance on peculiar knowledge, and by obligating defendants to self-protect against the same.

Compounding its error, the trial court applied a "rather broad" disclaimer of "prior agreements, … understandings [or] communications," *i.e.* a classic, boilerplate integration clause, to insulate "Zhou's omissions or misleading statements, which it held were "not the subject of any specific representations." Op. at 29. This holding is doubly wrong. Normally, "general disclaimers are insufficient to defeat reasonable reliance on material misrepresentations as a matter of law, even by a sophisticated party." *FIH, LLC v. Found. Cap. Partners LLC*, 920 F.3d 134, 140–41 (2d Cir. 2019); *see also Mikada Grp., LLC v. T.G. Nickel & Assocs., LLC*, 2014 WL 7323420, at *10 (S.D.N.Y. Dec. 19, 2014) ("Notwithstanding any general merger clause, an 'omnibus statement' disclaiming reliance on any oral representation does not preclude a claim for fraud in the inducement in New York"). But New York law goes even further and annuls even *specific* disclaimers of reliance, much less boilerplate integration clauses, in cases of peculiar knowledge. *Supra*, at 22 (citing *Tahini Invs., Ltd*. and *Basis Yield I*).

Moreover, New York law "does not impose a duty on plaintiffs to insist on a 'prophylactic provision' in agreements" against omissions of peculiar knowledge. *ACA Fin. Guar. Corp. v. Goldman, Sachs & Co.*, 25 N.Y.3d 1043, 1045 (2015); *Solutia Inc. v. FMC Corp*., 385 F. Supp. 2d 324, 340 (S.D.N.Y. 2005) ("Although

sophisticated parties can normally … bargain for specific contractual warranties, the peculiar knowledge exception applies if a party would face high costs in determining the truth or falsity of representations."); *see also HealthNow New York, Inc. v. APS Healthcare Bethesda, Inc.*, 2006 WL 659518, at *5 (N.D.N.Y. Mar. 10, 2006) (information relied upon being "proprietary" meant that a "sophisticated" counterparty was not obligated to "bargain for specific contractual warranties").

iv. The trial court's error requires reversal.

The trial court's error prejudiced the defendants and merits reversal. Its focus on the single fact that Zhou's Chinese criminal history was a public record failed to consider that it was Zhou's *ongoing* operation of that same criminal pyramid scheme—and plan to make iFresh a part of it—that is at the heart of the defendants' peculiar-knowledge argument. And the defendants could not have discovered Zhou's private conversations reflecting these facts pre-suit.

Put another way, in concluding that "iFresh needed investors and … likely would have accepted Zhou's investment *regardless of his criminal conviction in China*," Op. at 30-31, the trial court myopically focused solely on the public nature of Zhou's criminal *history*, while ignoring undisclosed *present* acts and intentions, (emphasis added). To illustrate, the finding ignored that iFresh had *just cancelled* a transaction over allegations of criminal conduct *notwithstanding* its need for financial support. A0116. It also ignored that iFresh had a ready alternative to Zhou, namely Deng's Florida fruit farm. A202; A1514.

By focusing exclusively on what was in the *public* record, the trial court also ignored substantial evidence of Zhou's peculiar-knowledge, in particular his numerous private WeChats expressing fears of "class action" litigation by Xiangtian's Chinese investors, of being put on an Interpol wanted list, of being

"finished completely" if that happened, and his attempts to placate or suppress the dissatisfied investors in his pyramid scheme to head off these existential concerns.

Without even a passing glance at these facts, the trial court concluded that the Zhou's investment was not "tainted by fraud to [such] a degree that it is reasonable to conclude the transaction would not have been consummated had the fraud been detected pre-closing." Op. at 30. While it is difficult to foresee any circumstance in which a company trying to retain its Nasdaq listing would want to end up being absorbed by a criminal pyramid scheme, the deeper problem is that the trial court failed to grapple with these facts at all. Instead, the trial court based its reasonable reliance holding solely on the fact that "Zhou's conviction was a matter of public record." *Id.* But Zhou's conviction was not the focus of Appellants' peculiar-knowledge argument, his plan to absorb iFresh into Xiangtian was. And as set forth above, New York law does not preclude a finding of reliance where a defendant's peculiar knowledge is at issue, even if related matters are public.

The trial court did not find that iFresh or the defendants would have accepted Zhou's investment, or would have proceeded with either the RET Wine or Jiuxiang transactions, had they been privy to Zhou's private WeChats and plans. Nor could it have reasonably done so on this record. After all, if iFresh and the defendants truly did not care about Xiangtian, Deng would not have bothered asking Zhou about it. And Zhou's vehement denials, as well as his repeated private exhortations to

maintain confidentiality about the scheme, show that Zhou knew that the truth would have jeopardized the transactions that led iFresh to issue the shares voted in this action. This Court should remand for further proceedings, so that Zhou's peculiar knowledge may be considered for justifiable reliance.

II. THE COURT ERRED LEGALLY BY FAILING TO CONSIDER ZHOU AND OU'S BREACH OF THEIR CONTRACTUAL WARRANTY, AND ERRED FACTUALLY BY IGNORING CRITICAL EVIDENCE AND MISINTERPRETING OTHER EVIDENCE.

A. Questions Presented.

Did the trial court err by failing to consider Zhou and Ou's false contractual warranty and representation as a breach of contract—leading to a misapplication of New York law as well as the wrong evidentiary standard?

Did the trial court err by ignoring key evidence, including trial admissions, showing that Ou was Zhou's agent in connection with his purchase of iFresh stock?

Preserved at A1581-83; A1628, 1631-33.

B. Standard and Scope of Review.

This Court reviews *de novo* interpretations of written agreements and law. *Gotham Partners, L.P. v. Hallwood Realty Partners, L.P.*, 817 A.2d 160, 170 (Del. 2002); *CompoSecure, L.L.C. v. CardUX, LLC*, 206 A.3d 807, 816 (Del. 2018) (questions of law and contractual interpretation are subject to *de novo* review).

This Court must "review the sufficiency of the evidence and to test the propriety of the findings," but "will not disturb the court's findings of fact unless they are clearly erroneous." *Wilcox v. LaClaire*, 263 A.3d 1014, 1021 (Del. 2021). The court only makes its on factual findings if the trial court's findings were "not supported by the record and are not the product of an orderly and logical deductive process … ." *Id.*

C. Merits of the Argument.

i. The trial court failed to apply New York law to consider Zhou and Ou's contractual misstatement as a breach of warranty.

As the defendants argued below, the evidence demonstrated a breach of the warranty that Ou was "purchasing the Shares for [his] own account [and] not as a nominee or agent." A0316-17 (§ 3(c)); A1581-82. Yet the trial court erroneously analyzed Zhou and Ou's non-nominee/agent warranty under the framework of "fraud," holding that the defendants had to prove the falsity of that warranty by "clear and convincing evidence." Op. at 22, 24.

The trial court further held that, under New York law, a plaintiff must "prove reasonable reliance upon an express contractual representation for the purposes of fraud," and to do so, "must prove that he 'believed [the representation] to be true.'" *Id.* at 33 n. 127 (citing to *CBS, Inc. v. Ziff-Davis Publishing Co.*, 75 N.Y.2d 496 (N.Y. 1990)). The trial court's ruling erred by imposing the wrong evidentiary standard (clear and convincing, as opposed to preponderance of the evidence), the incorrect framework (fraud, as opposed to breach of warranty), and an unnecessary element (reliance).

As New York's highest court made clear in *Ziff-Davis*, "reliance is established if, as here, the express warranties are bargained-for terms of the seller." *Ziff-Davis*, 75 N.Y.2d at 506 n.5. Accordingly, "[o]nce the express warranty is shown to have

been relied on as part of the contract, the right to [] damages for its breach *does not depend on proof that the buyer thereafter believed that the assurances of fact made in the warranty would be fulfilled*. [It] depends only on establishing that the warranty was breached." *Id.* (emphasis added).

Plus, as the defendants emphasized below, under New York's breach of warranty law, it is irrelevant "whether [iFresh]'s reliance on the representations and warranties that it bargained for was reasonable since, when one procures an express contractual warranty, one may absolutely rely on it," with the plaintiff's "knowledge, policies, understanding, due diligence, and retrospective review … all [being] irrelevant[.]" A1631-32 (quoting *Assured Guar. Mun. Corp. v. DLJ Mortg. Capital, Inc.*, 2014 NY Slip Op 51044(U), ¶ 4 (Sup. Ct. 2014)).

In New York, "the general rule is that a buyer may enforce an express warranty even if it had reason to know that the warranted facts were untrue." *Merrill Lynch & Co. v. Allegheny Energy, Inc.*, 500 F.3d 171, 186 (2d Cir. 2007). The only exception is where the warrantor affirmatively and "actively disclosed" the falsity of a warranty prior to closing. *Preferred Fragrance v. Buchanan Ingersoll & Rooney PC*, 2015 WL 6143612, at *4 (E.D.N.Y. Oct. 18, 2015)

In addition to making a contractual warranty "absolutely" reliable, New York law establishes a preponderance standard to prove a breach of contractual warranty—not the clear and convincing standard the trial court erroneously required.

See, e.g., LaSalle Bank Nat'l Ass'n v. Nomura Asset Capital Corp. & Asset Securitization Corp., 2006 NY Slip Op. 33876(U), ¶ 60, 2006 WL 2006 (Sup. Ct. Sept. 6. 2006), *aff'd*, 47 A.D.3d 103 (1st Dept. 2007) ("the court finds, by a preponderance of the evidence, that the defendants breached the Section 2 (b) … the origination representation and warranty"); *see also* A1724 ("if we're in the universe of these representations were breached … then we're in the preponderance of the evidence").

These errors prejudiced the defendants. Had the trial court applied the correct elements and evidentiary standard, it may well have found a breach of warranty invalidating the consent. Therefore, this Court should reverse and remand for application of the correct New York law governing breach of warranty.

ii. The trial court ignored dispositive evidence, including a trial admission, and misunderstood the main piece of evidence it did consider.

The record evidence indicates that, in buying iFresh shares, Ou was acting as Zhou's straw buyer. *First*, Ou testified that, at the time of his purchase of iFresh shares as Zhou's "co-investor," he already "reported to" Zhou and did "what [Zhou] asked him to do." A0744.

Second, Zhou and Xue treated shares issued to Ou as belonging to Zhou. A0131-33. Their WeChat record also showed Zhou personally arranged for the transfer of Ou's "co-investment" funds. A0148-0153.

Third, Zhou stated in writing to a Xiangtian investor's spouse that the iFresh shares issued to "me and Qiang Ou" meant "[t]he number one major shareholder *is us*." A0353-0354 (emphasis added).

Fourth, in September 2020, *after* all the transactions at issue, and shortly before Zhou made his takeover demand, Zhou and Ou jointly filed a Form 13D, disclosing that *both* Zhou and Ou had borrowed the $1.5 and $1 million they respectively used to purchase iFresh shares from Zhou's nephew. A0521.

Fifth, Zhou conclusively testified at trial that "*I would have gotten* [all of the] shares" issued pursuant to his and Ou's $2.5 million "co-investment." A1265 (emphasis added).

Applying the wrong evidentiary standard, legal framework, and elements, the trial court required defendants to prove subjective reliance by clear and convincing evidence. Op. at 33, fn. 127; *cf.* A1631-1633.

Even ignoring this threshold error, discussed above, the trial court's factual conclusion that there was no fraud was based solely on evidence regarding Ou's *source* of funds. Specifically, the trial court found no justifiable reliance because "no inquiry was made" into his source of funds at the time of the transaction, and iFresh "took no action to address th[is] supposed issue," when the source of funds (*i.e.,* Zhou's nephew) was later disclosed. Op. at 32. This conclusion misses the forest for the trees and is clearly wrong for several reasons.

First, the warranty at hand is not about Ou's *source* of funds per se, but about his *agency relationship with Zhou*. Ou's borrowing of his entire investment from Zhou's nephew is only relevant to this inquiry in that it is evidence that supports the existence of that relationship. Thus, given that iFresh already had the warranty about there being no agency relationship, there was no reason for iFresh to further inquire into Ou's source of funds. What is more, in focusing only on the *source* of Ou's funds, the trial court ignored material evidence, such as Zhou's admission at trial that he was going to get all the shares issued to Ou. A1265. The trial court's focus on the irrelevant, while failing to address a critical admission, was clearly erroneous.

The trial court also appears to have misapprehended the September 2020 Form 13D disclosure about Ou's source of funds as having come from *iFresh*. In particular, the trial court called the Form 13D "an iFresh 13D filed after the fact," which the trial court construed as "reveal[ing] that, contrary to Defendants' feigned ignorance, the company itself was well aware of the source of funds Ou used to acquire iFresh shares." Op. at 23 n. 91. The trial court then repeatedly cited to what it thought of as an "iFresh" filing as evidencing no justifiable reliance on Ou's source of funds. *See* Op. at 25, 32.

But Forms 13D are not filed by issuers like iFresh; rather, they are filed by investors, who are obligated by 17 C.F.R. §240.13d-1(a) to make the filing whenever they form a group holding more than 5% of a company's stock. Not being the filer, iFresh could not have "feigned ignorance" of a fact about which it had no knowledge. And since Zhou and Ou only filed the Form 13D several months *after* they acquired iFresh shares, the trial court's holding that the Form 13D undermined reliance *at the time* of those acquisitions does not follow.

The trial court's flawed analysis of the Zhou-Ou transaction extended to its finding that Ou "was brought in as an investor because Zhou did not have enough US dollars to meet iFresh's needs," resulting in him signing the SPA "as Zhou's co-investor." Op. at 24. But this holding is irreconcilable with the fact that, according to their Form 13D, both Zhou and Ou borrowed all of their investment funds from

Zhou's nephew. This raises the question that, if the total investment was $2.5 million U.S. dollars, and Zhou's nephew was willing to lend that amount in the aggregate, why would Zhou need to "bring in" Ou for a lack of U.S. dollars? The only conclusion that squares with Zhou's clear trial testimony that he considered the iFresh shares nominally issued to Ou to be *his* shares, is that Ou was brought in to mask and understate how much control Zhou would actually acquire of iFresh as a result of the transaction—making him a nominee and agent of Zhou.

Thus, the trial court's contrary findings were "not supported by the record and are not the product of an orderly and logical deductive process." *Wilcox v. LaClaire*, 263 A.3d 1014, 1021 (Del. 2021).

III. THE COURT ERRED IN FINDING THE BREACH OF FIDUCIARY DUTY THEORY WAIVED WHILE FAILING TO CONSIDER THE DECEPTIVE ACTS UNDERLYING IT FOR THE FRAUD THEORY.

A. Questions Presented.

Did the trial court err in finding the defendants' argument that the consent was invalid due to breach of fiduciary duty waived, even though Zhou was on notice of the issue throughout the case, and actively litigated the facts underlying this theory?

Did the trial court err in completely ignoring the underlying deceptive acts when considering Appellants' fraud theory?

Preserved at: A0584; A0943-45, 51, 54, 57-60; A1071.

B. Standard and Scope of Review.

The Supreme Court "reviews the interpretation and application of legal precepts, such as the statute of limitations and the doctrine of laches, de novo." *Levey v. Brownstone Asset Mgmt., LP*, 76 A.3d 764, 768 (Del. 2013).

C. Merits of the Argument.

The trial court rejected defendants' arguments that iFresh CFO Amy Xue breached her fiduciary duties, aided and abetted by Zhou, on the basis that this theory was "not introduced as grounds to invalidate the Consent until after trial," and that this was "too late to argue a new *claim*." Op. at 16 (quoting *CanCan Dev., LLC v. Manno*, 2015 WL 3400789, at *22 (Ch. May 27, 2015) ("*CanCan*") (emphasis added). This holding misapplied the law governing waiver.

As this Court recently held in a Section 225 setting, where a propounding party "has consistently argued that [a party] deceived their fellow directors, and where: (i) the parties had the opportunity to take discovery into an allegedly fraudulent act; (ii) defendants' pre-trial brief discussed the act; and (iii) the allegations sounded in fraud generally, there is no waiver of an argument raised post-trial that the act was deceptive. *Bäcker v. Palisades Growth Capital II, L.P.*, 246 A.3d 81, 104 (Del. 2021) ("*Bäcker*").

Citing *Bäcker*, the Court of Chancery recently held that, when considering waiver, "[t]he real question is whether the plaintiffs gave the defendant adequate notice that they were litigating a particular theory such that the defendant had 'a fair opportunity to respond.'" *In re Cellular Tel. P'ship Litig.*, 2021 WL 4438046, at *61 (Ch. Sept. 28, 2021). As Vice Chancellor Laster—who also decided *CanCan*—observed:

> Delaware has … rejected the antiquated doctrine of the "theory of the pleadings'"—*i.e.*, the requirement that a plaintiff must plead a particular legal theory. … and it is unnecessary to set out a legal theory for the plaintiff's claim for relief." [The rules provide that] "particular legal theories of counsel yield to the court's duty to grant the relief to which the prevailing party is entitled, whether demanded or not."

Id. at *172-3 (citing *Federal Practice and Procedure (Wright & Miller)* § 1219 (3d ed. 2004 & Supp. 2020)).

Whereas *Bäcker* was a Section 225 decision, the cases the trial court cited in support of its waiver ruling were exclusively plenary actions. For example, *CanCan*

was a plenary action where no amendments to the complaint were sought to add causes of action. *CanCan*, at *33. Thus, when one of the parties sought to introduce an entirely "new claim" in post-trial argument, the Court found that it was too late. *Id.* at *66.

Likewise, *ABC Woodlands, L.L.C. v. Schreppler* was a plenary land dispute in which one party attempted to introduce a previously un-mentioned "agreement" to support their claim to the land one day before trial, even though the case was four years old, and the parties had already stipulated pretrial that their claims rested on interpretation of a written deed. 2012 WL 3711085, at *3 (Del. Ch. Aug. 15, 2012).

Consider too, *Snow Phipps Grp., LLC v. KCAKE Acquisition, Inc.*, 2021 WL 1714202, at *43-44 (Ch. Apr. 30, 2021), which cites *ABC Woodlands*, and which was likewise a plenary action. There, a party consistently took one position throughout the litigation, but "pivoted" to an "inconsistent position" for the first time in its pre-trial brief, which position the court found waived. *Id.*

None of these cases support the trial court's waiver ruling, which would have litigants in a summary Section 225 case plead the precise legal labels for the wrongful conduct justifying the invalidation of a Section 225 plaintiff's vote. Rather, as the *Bäcker* and *In re Cellular Telephone Partnership* cases make clear, the inquiry is whether the defending party had "a fair opportunity to respond." *Supra*, at 38. This makes sense. As the trial court emphasized, Section 225 actions are very

different from plenary ones. Op. at 9. Unlike plenary actions, no "claims" are pled in Section 225 actions. Rather, complaints plead a single count under Section 225, requesting declaratory relief based on *facts* reflecting wrongful conduct. *See, e.g.*, Ex. B (Genelux Complaint); Ex. C (Backer Complaint).

Even where the facts alleged support separate a fiduciary duty claim, such a claim would not—and indeed *could not*—be part of the Section 225 summary proceeding. Op. at 9. Instead, such a claim *must* be brought as a separate cause of action in a plenary setting. *Id.*; *see also Kahn Bros. & Co. v. Fischbach Corp.*, 1988 WL 122517, at *1 (Ch. Nov. 15, 1988) (sustaining a Section 225 cause of action for declaratory relief, and noting that an ancillary claim for breach of fiduciary duty had been brought separately).

In light of *Bäcker*, and considering the non-plenary, declaratory, and summary nature of Section 225 proceedings, the trial court's waiver ruling erred in several respects.

First, the trial court's holding that defendants did not introduce a fiduciary argument "as grounds to invalidate the Consent until after trial" is factually incorrect, as Appellants' pretrial brief expressly argued "fiduciary misconduct" as a basis for invalidation. Op. at 16; *cf.* A1020.

Second, the trial court imposes erroneous pleading and waiver standards on Section 225 litigants and misapplied *Bäcker*'s holistic, notice test. The trial court's

waiver ruling was predicated on its finding that defendants argued "a new claim." Op. at 16. But the sole claim in this Section 225 action is for declaratory judgment. A0953-58. No fraud, breach of contract, breach of fiduciary duty, or other ancillary causes of action were asserted. From inception, only facts were pled, including an allegation that "Dengrong Zhou's sole purpose in appointing Amy Xu[e] [to be iFresh's CFO] was to ensure that the RET Wine and Jiuxiang acquisitions proceeded." A0584 (¶47).

Through comprehensive discovery, the defendants uncovered unambiguous evidence that while serving as iFresh's CFO, Xue deceived and was disloyal to iFresh and instead worked to benefit Zhou at iFresh's expense. *Supra*, at 17-18. Zhou and Xue's deceptive and disloyal acts were then spelled out in the defendants' amended pleadings. *See, e.g.*, A0931-33; 0940-41 (¶¶ 49-53; ¶¶ 94-98).

The defendants again recounted these same facts in their pre-trial brief, which specifically argued that "[f]raud or *fiduciary misconduct* bear upon the validity of shares voted in a Section 225 contest." A0994-0999, 1020 (emphasis added). At trial, Zhou testified about his conversations with Xue on direct examination in a prepared effort to head off arguments about his direction of her deception and disloyalty. A1266-70. On cross-examination, Zhou then offered explanations for his and Xue's private WeChats. *See, e.g.*, A1411.

And as the defendants made clear in post-trial briefing, the trial record left no doubt that these private WeChat conversations revealed obvious deception and disloyalty on Xue's part, constituting breaches of her fiduciary duty to iFresh. A1583-87. Zhou made a substantive, factual rebuttal, arguing under the heading that Appellants "Did Not Prove That Amy Xue Breached A Fiduciary Duty or that [Appellee] Aided And Abetted Such Breach." A1607-10. In all, Xue's deception and disloyalty were raised hundreds of times in depositions, multiple evidentiary and trial briefings, at trial, and post-trial. Because Zhou had every opportunity to dispute Xue's deceptiveness and disloyalty—and did, in fact, dispute it—the legal theory supported by those facts, breach of fiduciary duty, was not waived under *Bäcker*.

The trial court's erroneous waiver decision was prejudicial because it led to the trial court altogether ignoring the deceptive and disloyal acts underlying the fiduciary duty theory. The defendants have consistently argued a fraudulent conspiracy to induce iFresh into various transactions, which conspiracy included Xue's disloyal conduct. A0584. But, after finding waiver, the trial court did not discuss, cite, or tangentially reference even one of the numerous private WeChats between Zhou and Xue.

Given that this evidence of blatant deception was tested at trial and was a core part of the case, the trial court's decision to ignore this body of evidence was reversible error under *Bäcker*—which held that newly developed facts could support

a "consistently" argued theory of fraud—even if its waiver ruling was not. *Bäcker*, at 104. Accordingly, this Court should reverse because the defendant's fiduciary theory argument was not waived. At a minimum, based on substantial evidence that Xue was deceptive and disloyal to iFresh at Zhou's direction for Zhou's benefit, as was consistently argued, this Court should remand for further proceedings to consider the acts underlying Xue and Zhou's fiduciary misconduct for the purposes of fraud.

CONCLUSION

Wherefore, Appellants respectfully submit that the trial court's Opinion be reversed in the respects stated above.

Respectfully submitted,

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Dated: June 20, 2022

CERTIFICATE OF SERVICE

I, John G. Harris, hereby certify that the foregoing APPELLANTS' [CORRECTED] OPENING BRIEF was served upon the following in the manner and on the date indicated below:

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