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Case Number 152,2022

IN THE SUPREME COURT OF THE STATE OF DELAWARE

LONG DENG AND MARK FANG,	)	
	)	
	)	
Defendants/Counterclaim Plaintiffs below, Defendants,	)	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.	)	

DEFENDANTS' REPLY BRIEF

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I. THE TRIAL COURT ERRED IN NOT APPLYING NEW YORK'S "PECULIAR KNOWLEDGE" RULE.

A. The Peculiar Knowledge At Issue Relates to Zhou's Undisclosed "Xiangtian Supermarket" Scheme, Not Solely To His Prior Criminal Convictions.

Zhou does not deny that in New York, represented sophisticated parties can invoke the "peculiar knowledge" rule to establish justifiable reliance, as established in the Opening Brief. *See* OB, 24-27. Instead of confronting Defendants' argument head-on, Zhou sets up straw men founded on the false premise that the "peculiar knowledge" at issue was limited to Zhou's criminal convictions, which was publicly available. AB, at 8, 13, 15, 25, 28.

But the Opening Brief made plain that "Zhou's conviction was *not* the focus of Defendants' peculiar-knowledge argument[.]" OB, 32 (emphasis original). Rather, "it was Zhou's *ongoing* operation of that same criminal pyramid scheme—and plan to make iFresh a part of it[.]" OB, 31. (emphasis original).

Deng and Fang learned of these facts via discovery into Zhou's private WeChat conversations. Zhou does not dispute that that plan was within Zhou's peculiar knowledge. OB, 14-20. Instead, Zhou touts the trial court's holding that the public nature of his prior criminal convictions precludes justifiable reliance. This misses the point. The trial court's singular focus on publicly-available

information—while ignoring Zhou's peculiar knowledge as to his plans—was precisely where the trial court erred. OB, at 28, 31-33.

B. Zhou's False Denial Triggered A Duty To Disclose His "Xiangtian Supermarket" Plans And Fears Of Being "Finished Completely" Should That Plan Fail.

Zhou's only attempt to substantively grapple with the actual peculiar knowledge at issue—his active plans to make iFresh the "Xiangtian Supermarket" and fears of being "finished completely" by "class action" litigation in China if it did not work out—is to recite the trial court's holding that Zhou did not have a freestanding duty to disclose intent to control. Op. 22; *cf.* AB, 13-14; OB, 16-17.

Deng and Fang never claimed the existence of a freestanding duty to disclose an intent to control. Nor could they. It was evident to all parties that the transactions at issue would necessarily result in Deng giving up his majority stake in iFresh. Despite relinquishing controlling shares, Deng remained the second largest shareholder with over 20.6% of the Company's shares. A1033 (PTO ¶¶ 19, 28). And as the shareholder-CEO of the company he founded, Deng wanted to know if Zhou had been involved with Xiangtian, and if so, whether Zhou's proposed investment in iFresh tied in with such involvement. Zhou suggests this Court should ignore the resulting duty to disclose the whole truth, and divert the issue toward the undisputedly irrelevant "intent to control." This is a red herring, however, given Zhou's false to Deng's direct inquiry.

The real nub, as Defendants have emphasized, was that Zhou's choice to mollify Deng's concerns about Xiangtian "triggered a duty to speak fully and truthfully on the topic." A1567 (citing *Prairie Capital III, Ltd. P'ship v. Double E Holding Corp.*, 132 A.3d 35, 52 (Del. Ch. 2015) ("[O]nce [a] party speaks, it . . . cannot do so partially or obliquely such that what the party conveys becomes misleading.")); *see also Scharf v. Tiegerman*, 166 A.D.2d 697, 698 (N.Y. App. Div. 1990) ("By making such a representation, the sellers had an affirmative duty to disclose any material facts relating to the substance of the representation which might affect the recipient's conduct in the transaction in hand[.]") (internal quotations omitted). Zhou's false assertion that Xiangtian was a "made up rumor" that did not have the "slightest connection" to the transactions he was brokering triggered at least: (1) a duty to disclose his *active* management of Xiangtian; and (2) a duty to disclose his plan to absorb iFresh into it. OB, 7-8.

Under New York law, that duty to disclose can exist "even when [the misrepresentations] relate to matters of public record." OB, 25 (quoting *LBBW Luxemburg S.A. v. Wells Fargo Securities LLC*, 10 F. Supp. 3d 504, 517 (S.D.N.Y. 2014); *see also Ruckstuhl v. Healy*, 222 App. Div. 152, 155 (N.Y. App. Div. 1927) ("Nor does the fact that the third mortgage was of record alter the situation. Having undertaken to speak concerning its nature, the defendant was obligated to speak truthfully, if not fully."). And Zhou's duty to make full and truthful disclosures

would exist even if his denials about Xiangtian were literally true, which they were not. *Von Au v. Magenheimer*, 126 App. Div. 257, 261 (N.Y. App. Div. 1908) ("The defendants at least owed the plaintiff the duty to speak the whole truth, if they spoke at all, not literally in words, but truthfully in substance.").

Zhou's failure to grapple with Defendants' argument and cited authorities is just as telling. As the WeChat evidence that Zhou intended to continue operating the Xiantian scheme and absorb iFresh into is damning. The trial court's failure to consider Defendants' peculiar-knowledge argument warrants reversal.

C. The Trial Court's Opinion Reveals It Did Not Consider The Facts Within Zhou's Peculiar Knowledge.

Zhou baldly asserts that the trial court did consider Zhou's "continuing pyramid scheme involving iFresh." AB, 15-16. But the subsequent arguments simply recite the trial court's examination of evidence relating to Zhou's *prior* criminal convictions and Defendants' failure to discover these pre-closing. *Id.* As the trial court found, Deng and Fang "likely would have accepted Zhou's investment *regardless of his criminal convictions* in China." *Id.* at 16 (emphasis added). By its own terms, the trial court's reasoning began and ended with the public convictions—reflecting prior deeds—and did not reach Zhou's "continuing pyramid scheme involving iFresh." AB, 15.

Zhou next seizes upon footnote 109 of the trial court's opinion, insisting it shows that the trial court did consider Zhou's peculiar knowledge regarding his

"intent to incorporate iFresh into" Xiangtian, and simply made adverse "factual determinations [that are] not a basis for reversal." AB, 16-17. Zhou's argument misses the mark in two ways.

First, footnote 109 dismissed Deng and Fang's arguments about Zhou's conversations with investors in the Xiangtian scheme as communications "discovered after" the iFresh transactions at issue, through discovery. Op. at 29 n.109. As such, the trial court concluded that "Defendants could not have relied on statements they did not know about." *Id.* Yet, the trial court did not consider the facts reflected in the statements, only the timing of their revelation to Defendants.

More importantly, the fact that Deng and Fang "did not know about" Zhou's private conversations with Xiangtian investors (none of which the trial court cited) is exactly what makes such conversations Zhou's peculiar-knowledge. OB, 14-17. Of course Deng and Fang did not know about them. Nor did they ever argue reliance on Zhou's statements to other parties, which would have been impossible. They relied instead on Zhou's failure to discharge his duty to disclose the facts reflected in these private conversations. The trial court's finding that Defendants could not have relied on statements they did not know about—instead of considering whether they were facts only known to Zhou and which he had a duty to disclose—neatly illustrates its error.

Second, in footnote 109 the trial court also rejected Deng and Fang's arguments about these private conversations on the ground that "Zhou's statements to unrelated parties [do not] have anything to do with his or his supposed allies' acquisition of iFresh shares." Op. at 28 n.109 (bracketed text added). But Zhou's entire conversation with one Xiangtian investor, "Eiffel Tower," revolved around iFresh's 8-K announcing the RET Wine transaction, as well as his and Ou Qiang's investment into iFresh. A0353-0358; A0322-0323. In that conversation, Zhou stated that iFresh's "stock issuance[s] [to] *me and Qiang Ou*," was, in addition to the RET Wine transaction, the reason that "[t]he number one major shareholder [of iFresh] is us"—meaning Xiangtian. *Id.*[1] Thus, contrary to the trial court's findings in footnote 109, the Eiffel Tower chat had *everything* to do with Zhou's acquisition of iFresh shares. This factual error strongly indicates that the trial court's decision to ignore Zhou's peculiar-knowledge meant that it did not examine the actual substance of Zhou's private WeChat conversations.

Finally, Zhou does not dispute the substantive fact that he was actively involved in the Xiangtian scheme and did intend to make iFresh a part of it. OB, 14-

[1] Zhou posits that this is a "strained translation" of the conversation. But he offered no alternative translation in the proceedings below, and does not do so here. Moreover, at trial, Zhou admitted that the substance of this conversation was that he was telling Eiffel Tower that Xiangtian would control iFresh through the challenged transactions, but claimed that he was merely blowing "hot air." A1430.

17. Rather, Zhou claims only that he had no duty to disclose these things. AB, 17. As set forth above, Zhou's false statements of January 16, 2020 in response to Deng's direct inquiry about Xiangtian triggered his duty of full and truthful disclosure.

D. Controlling New York Law Allows Sophisticated Parties Represented By Counsel To Rely On The Peculiar-Knowledge Rule.

In their Opening Brief, Defendants argue that the trial court erred as a matter of law in holding that the peculiar knowledge rule cannot be invoked by sophisticated, represented parties. Zhou, in turn, relies heavily on two cases: *HSH Nordbank AG v. UBS AG*, 941 N.Y.S.2d 59 (N.Y. App. Div. 2012) and *Centro Empresarial Cempresa S.A. v Am. Móvil, S.A.B. de C.V.*, 17 N.Y.3d 269 (N.Y. 2011), which *HSH* relied on. AB, 18, 20, 21. Zhou's reliance on these decisions is misplaced, however, because neither one deals with the subject of peculiar-knowledge.

HSH expressly "reiterate[d] [that] the facts allegedly misrepresented were *not* peculiarly within UBS's knowledge[.]" *HSH* at 70 (emphasis added). *Centro*, too, merely set forth the principle that "if the facts represented are *not* matters peculiarly within the party's knowledge," the other party will be required to conduct a certain amount of diligence. *Centro* at 278 (emphasis added); *cf.* AB, 19. The converse, of course, is that there is no obligation to discover peculiar, withheld knowledge through due diligence. By contrast, the cases on which Defendants rely hold that,

where facts misrepresented were the peculiar knowledge of the speaker, sophistication and representation are irrelevant, and diligence is obviated given that the underlying facts are, by nature, undiscoverable. OB, 24-27. Skirting the overwhelming weight of authority, Zhou argues that the trial court's decision not to apply the rule, as set forth in footnote 122 of the Opinion, was multilayered and based on the "factual circumstances here." AB, 19.

According to Zhou, these "factual circumstances" were that Deng and Fang were "sophisticated parties who were represented by counsel [who] could have negotiated contractual protections for themselves," and who failed to "conduct adequate due diligence." Op. fn. 122; *cf.* AB, 19. Zhou supports this argument by reference to the trial court's subsequent opinion denying a stay, which stated that its peculiar-knowledge decision was premised not only on sophistication, but also on "factual findings regarding the accessibility of information," "lack of any meaningful diligence," as well as "other[]" unidentified factors." AB, 19; *cf.* B429.

But neither the stay denial order, nor the Opinion on appeal, contain any factual finding about the "accessibility of" Zhou's private WeChats reflecting his plans to absorb iFresh into Xiangtian. The trial court's sole finding as to "accessibility" related to the publicly available fact of Zhou's prior convictions.

And Zhou's argument that a lack of due diligence weighs against application of the peculiar-knowledge rule flips the law on its head. As numerous New York

cases make clear, the withholding of peculiar knowledge negates any affirmative duty to conduct due diligence. OB, 25-27 (citing cases holding, for example, that the peculiar knowledge rule applies where "a sophisticated investor armed with a bevy of accountants … and lawyers could not have known" the undisclosed information). That makes sense, as truly private information—like Zhou's personal WeChats—are unlikely to be revealed by due diligence.

Indeed, encompassing situations in which it would be merely difficult, as opposed to impossible, for diligence to discover peculiar knowledge, the rule applies even where "the truth theoretically might have been discovered," and where such information was "not exclusively" within a defendant's knowledge. *Id.* (citing *Basis Yield Alpha Fund Master v. Stanley*, 136 A.D.3d 136, 145 n.7 (N.Y. App. Div. 2015)). Zhou's effort to render due diligence a factor in whether the rule applies therefore places the cart before the horse.

Finally, the trial court's holding that Defendants "could have negotiated contractual protections for themselves," Op. 31 n. 122, again runs contrary to well-settled New York law, which "does not impose a duty on plaintiffs to insist on a 'prophylactic provision' in agreements" to protect against omissions of peculiar knowledge. OB, 29 (citing *ACA Fin. Guar. Corp. v. Goldman, Sachs & Co.*, 25 N.Y.3d 1043, 1045 (2015)). Just as one is not required to discover peculiar knowledge through diligence, one cannot demand contractual protections for

unknown—and often unknowable—facts. *Id.* (citing *ACA* and *Solutia Inc. v. FMC Corp.*, 385 F. Supp. 2d 324, 340 (S.D.N.Y. 2005)).

The key word is therefore "could have." Reflecting this predicate, the cases Zhou cites involved situations where the underlying risk was already known. *See* AB, 21 (citing *O.F.I. Imps. Inc. v. GE Capital Corp*., 2016 WL 5376208, at *6 (S.D.N.Y. Sep. 26, 2016) (peculiar knowledge inapplicable where plaintiff alleged it "*was aware* of the risk that the detail reports and accounts receivable records received from [defendant] were inaccurate."); *Silver Point Capital Fund, L.P. v. Riviera Res., Inc*., 198 A.D.3d 432, 433 (N.Y. App. Div. 2021) ("plaintiffs are sophisticated parties that *were aware* that they were not provided with full information" (emphases added)).

E. None Of The So-Called "Deeper Flaws" Go Any Deeper Than The Court's Erroneous Decision To Ignore Peculiar Knowledge.

The trial court's failure to apply the peculiar-knowledge rule vitiates each of the "several levels" of "deeper flaws" that Zhou contends existed in the fraud claims regardless of the peculiar-knowledge rule, which the trial court described as: (1) the lack of "a material misstatement in the purchase agreement"; (2) the SPA's integration clause; and (3) that "the transaction would [still] have been consummated had the fraud been detected pre-closing," *i.e.*, materiality. B429-30; AB, 7, 19-20.

The argument that there is no misstatement in the purchase agreement fails for the same reason as the argument that Defendants "could have" negotiated

contractual prophylaxis. As for materiality, the trial court never considered whether Defendants would have consummated the transaction even if they had been privy to Zhou's private WeChat conversations, which show that Zhou feared being "finished completely" by "class action litigation" and an Interpol arrest warrant should he fail to turn iFresh into the "Xiangtian Supermarket." OB, 15-16, 32. And the objective evidence—including iFresh's recent cancellation of a deal with another Chinese company over its violation of Chinese law, as well as Zhou's own efforts to prevent discovery in the face of Deng's affirmative inquiry—simply does not support a finding that the transaction would still have been consummated had these peculiarly known facts been disclosed. OB, 7, 31.

Concerning integration, each of the cases Zhou cites to support the *general* integration clause makes clear that in New York, only "specific recitals" concerning the "very matter as to which [the party] now claims it was defrauded" can bar fraud. AB, 26. New York law is equally clear that even where a contract *specifically* disclaims reliance on alleged statements and omissions, justifiable reliance can still exist where these statements and omissions concealed facts within the fraudster's peculiar knowledge. OB, 25, 29-30.

Moreover, Zhou argues that "[n]one of the cases on which Defendants rely support [the] broad proposition" that "the peculiar knowledge exception applies regardless of the level of sophistication of the parties" because those cases were

decided at "the pleading stage[.]" AB, 21. But, setting aside the fact that Zhou supplies no case where the "level" of sophistication mattered to the peculiar-knowledge analysis, the pleading stage is precisely when purely legal propositions are most scrutinized.

Accordingly, one would suspect that if party sophistication were a bar to the peculiar-knowledge rule as a matter of law—or, indeed, if party sophistication were even relevant—New York pleading-stage cases would routinely reject sophisticated parties' attempts to rely on peculiar-knowledge. But Defendants' litany of cases—where the world's most sophisticated parties represented by the highest-powered counsel available successfully invoke the peculiar-knowledge rule—demonstrate that the opposite is true: sophistication and representation by counsel is *irrelevant* to the peculiar-knowledge analysis.

Thus, while Zhou quotes *Rekor*'s holding that sophistication "is relevant to the issue of reasonable reliance," he omits the next phrase: "but it is not dispositive of it." AB, 23; *cf. Rekor Sys., Inc. v. Loughlin*, 2022 WL 789157, at *7 (S.D.N.Y. Mar. 14, 2022) finding sophistication is irrelevant where peculiar knowledge is involved, as "even if [a party] were sophisticated, that would not give Defendants license to tell him one thing and then conceal from him facts peculiarly in Defendants' possession that would demonstrate something to the contrary."

In sum, all that matters is the extent to which knowledge of the withheld information is "peculiar" to the defendant, *i.e.*, the degree of discoverability—and even Zhou does not contend his private WeChats were discoverable pre-closing.

F. Zhou Admitted To His Xiangtian Involvement At Trial, And Still Does Not Dispute The Plan To Absorb iFresh Into It—Condoning This Deception Takes Caveat Emptor Too Far.

As the foregoing demonstrates, it is undisputed that at the very beginning of their relationship, Deng raised concerns about Xiangtian; that Zhou issued the false denial that Xiangtian had "not the slightest connection" with the transactions at issue; and that the truth—which was only revealed in private WeChat conversations pried from Zhou in discovery—was that Zhou planned to absorb iFresh into Xiangtian. Despite this undisputed narrative, the trial court concluded, in essence, that this all was just too bad. Zhou's prior convictions were public, and even after Zhou's false assurances of January 16, 2020, Deng should have known better.

But that is not the law. Indeed, in arguing for affirmance, Zhou relies heavily on *HSH Nordbank AG*, 941 N.Y.S.2d, at 68. But even *HSH* recognized that a misleading answer to an affirmative inquiry changes the reliance analysis. There, the court dismissed a fraud claim for lack of justifiable reliance. In so doing, it pointed out that the plaintiff "[n]ever asked UBS . . . to produce any alternative analysis" of the challenged transaction. *Id.* Had the plaintiff asked, and had UBS "falsely den[ied]" the existence of such an analysis, that "arguably would have been

fraudulent[.]" *Id.* "But no false denial is alleged; HSH simply assumes that, in the absence of a request, UBS was obligated to disclose its internal analyses of the deal." *Id.*

Here, the facts line up with *HSH*'s counterfactual. Zhou's false denial is not even contested. To say that this did not trigger a duty to disclose, but rather that Deng had an affirmative obligation to doubt Zhou, conduct additional diligence, and obtain contractual prophylaxis, would take caveat emptor far beyond what is reasonable, and it is not the law. *See, e.g.*, *Nacco Industries v. Applica Inc.*, 997 A.2d 1, 32 (Del. Ch. 2009) (resisting "the idea of insulating wrong-doers and penalizing victims because a fraud arguably became sufficiently apparent that the victim should have known better"). The trial court's erroneous contrary conclusion warrants reversal.

II. THE TRIAL COURT CLEARLY ERRED BY IGNORING ZHOU'S UNAMBIGUOUS ADMISSION THAT HE CONTROLLED OU'S SHARES—A FACT THE ANSWERING BRIEF DID NOT ADDRESS.

Zhou does not dispute that the trial court's analysis of the relationship between him and Ou was both internally inconsistent and riddled with factual errors. Given the law that factual findings must be "supported by the record" and be "the product of an orderly and logical deductive process," the trial court's muddled findings warrant reversal. *See Wilcox v. LaClaire*, 263 A.3d 1014, 1021 (Del. 2021).

Instead, Zhou rests entirely on yet more specious arguments, specifically: (i) that Ou does not hold enough shares to change the outcome of the vote; (ii) that Deng and Fang waived the breach of warranty argument; and (iii) the trial court's determination that Ou's *deposition* testimony was "credible," while dismissing the analytical errors identified by Defendants as "simply a collateral attack" on that credibility determination. None of these arguments have merit.

A. Defendants Have Consistently Argued That *Both* Zhou And Ou's Votes Should Be Invalidated Based On Zhou's Admitted Control Of Ou's Shares—There Has Been No Waiver.

Zhou argues that Defendants waived their argument that his vote should be invalidated because Ou was his agent, claiming it "is an entirely new argument, presented for the first time on appeal." AB, 31. But from their very first complaint through post-trial briefing, Defendants have expressly and consistently requested judgment against *Zhou* on the basis that *Zhou* engaged in wrongdoing by causing Ou

to hold himself out as independent when he was in fact investing on Zhou's behalf. For example, Defendants' very first counterclaim requested declaratory relief on the basis that *Zhou* "fraudulently induced iFresh to sell stock to Qiang Ou" and wrongfully "position[ed] Qiang Ou as an ostensibly independent and unrelated party, when Qiang Ou was not an independent or unrelated party." A0586.

Further, Defendants' opening post-trial brief argued that "Ou's false statements, made as Zhou's agent, mean that his *and Zhou's* votes should be invalidated." A1583 (emphasis added). Finally, at post-trial argument, Defendants made clear that "Ou and Zhou's *joint* misrepresentation about Ou's 'nominee or agent' status" meant that Ou acting as Zhou's agent "infect[] Zhou as well[.]" A1689, 1720. Indeed, Zhou and Ou *both* signed the contract containing the false representation as one another's "co-investor." A0321. The argument was not waived, and given the Zhou group's thin 2.29% majority, Zhou's 2.844% shareholding, combined with Ou's 2.072%, *is* outcome determinative. A1033-34 (PTO ¶¶ 18, 23). On these facts, this Court should hold the argument was preserved.

B. The Court Did Not Consider Ou And Zhou's Breach Of Their Joint Contractual Warranty That Zhou Was Independent.

Zhou makes the bold assertion that Defendants "conceded at post-trial oral argument that [fraud] was the only way … to invalidate Ou's vote[,]" and "affirmatively conceded that 'clear and convincing' is the appropriate standard[.]" AB, at 33. But Zhou cited only the fraud-centered snippet of a long colloquy with

the trial court about the different standards governing breach of warranty and fraud, which began with Defendants making clear that "[c]ontractual breach of warranty claim are subject to a preponderance of the evidence standard in New York. … [And] there wouldn't be such a thing as fraud claims based on representations in the contract unless Your Honor rejects our breach of warranty claim." A1718-19.

The trial court directly engaged with this argument, asking whether indemnification provisions existed that limited the available remedies for breach of a warranty to legal (money damages) as opposed to equitable (rescissionary) remedies. A1720. Counsel responded that there were none in the Zhou/Ou SPA—meaning rescission was a remedy available to the court—whereupon the trial court acknowledged that a contractual warranty could "induce the contract such that a breach would give rise to rescission … as an available remedy in order … to strip someone of their voting rights of shares [obtained] in alleged breach of contract." A1721-22. Counsel then reiterated that this was precisely Defendants' argument, and that "if we're in the universe of these [contractual warranties and] representations [being] breached and this breach is sufficient to rescind this contract, then we're in the preponderance of the evidence." A1724. Yet the trial court's resulting opinion did not address breach of warranty at all. Far from revealing any affirmative concessions, the exchange only reinforces Defendants' argument that the

trial court was presented with, and simply disregarded, breach of warranty as a basis for invalidation. OB, 35-37.

C. The Trial Court's Unsupported Credibility Determination Does Not Shield Its Error-Laden Factual Analysis.

Without disputing any of the panoply of evidence and admissions showing Zhou completely controlled Ou and his shares (OB, 38-41), Zhou argues that Ou's *deposition* testimony that he was independent was found to be "credible." AB, 34 (citing Op. 24, which in turn at n. 97 cites to Ou's deposition testimony). As an initial matter, Ou did not "testif[y] under oath in court before the trial judge," *Greene v. Greene*, 105 A.3d 989 (Del. 2014), and the trial court's credibility determination is thus not based on actual observation of the witness—but a deposition transcript. *Cf., e.g., Lank v. Steiner, Del.*, 224 A.2d 242, 245 (Del. 1966) ("[T]he Chancellor who *heard and saw the witnesses* was in a much better position to judge the credibility of their testimony.") (emphasis added); *see also, e.g., Ware v. Howell*, 614 S.E.2d 464, 468 (W. Va. 2005) ("[W]hen evidence is presented by deposition, the reviewing court may draw its own conclusions about the credibility of the testimony since it is in the same position as the trial judge for evaluating such evidence." (internal quotation marks, ellipses, and citation omitted)).

Even if a transcript-derived credibility determination were entitled to deference, "[f]indings on credibility determinations[] are subject to the [same]

'clearly erroneous' standard" as other factual determinations. *See, e.g.*, *Diggs v. State*, 257 A.3d 993, 1005 (Del. 2021).

Here, Zhou does not claim that the trial court's credibility determination was *itself* "supported by the record" or was "the product of an orderly and logical deductive process." And a mountain of (unaddressed) facts contradicted Ou's deposition testimony, including Zhou's critical trial testimony that "*I* would have gotten [all of the shares]" issued pursuant to his and Ou's purported "co-investment." OB, 18, 38. Zhou's silence only underscores the clear error of the trial court's factual finding that Ou "credibly" testified he was independent.

III. THE TRIAL COURT ERRED BY HOLDING THAT DEFENDANTS WAIVED THE ARGUMENT THAT ZHOU DIRECTED XUE'S BREACHES OF FIDUCIARY DUTY.

Zhou does not deny that it would make no sense to require Section 225 litigants to plead precisely labeled legal theories, as opposed to facts, in support of the lone declaratory judgment cause of action typical of Section 225 cases. Nor does he dispute that Defendants pleaded the facts underlying their theory that Zhou directed Xue's breach of fiduciary duty; namely, that iFresh hired Xue as CFO at Zhou's recommendation, and that Xue and Zhou then colluded to increase the number of iFresh shares Zhou got at iFresh's expense.

The trial court's waiver analysis, and the answering brief, both heavily rely on a single sentence from *Bäcker*, which they say distinguishes it: "Palisades has *consistently argued* that Bäckers deceived their fellow directors by representing support for the board's original agenda while concealing a secret counter-agenda to seize control of the company." AB, 38 (emphasis added).

But as the facts of *Bäcker* make clear, that sentence was *not* about the assertedly waived theory. Specifically, this Court agreed that the assertedly waived theory had *not* been explicitly raised below, and that only a deception theory "focused on D'Addario's appointment" as a director had been. Nevertheless, this Court concluded that the defendants had notice of the new theory, which focused on

"Grauman's appointment" because the theory had been *implicitly* raised. *Bäcker v. Palisades Growth Capital II, L.P.*, 246 A.3d 81, 103 (Del. 2021).

In so holding, this Court pointed to discovery and pretrial briefing, noting that Grauman's "appointment was the subject of discovery requests and [a single passage of] deposition testimony," including document requests relating to his "performance as Chief Executive Officer" and the waiver opponents' "refusal to vote for" his appointment as director. *Id.* at 104 & nn. 176-177. It also pointed out that plaintiff Palisades had "noted in its pretrial brief" that the Bäckers "fire[d] Grauman as CEO" even though they did not question his performance. *Id.* at 104.

Similarly, here Deng and Fang explicitly accused Zhou of fraudulent wrongdoing relating specifically to Amy Xue from the outset, such that Zhou did not need to deduce her significance, as was required of the Bäckers. As the first complaint alleged, "Dengrong Zhou's sole purpose in appointing Amy Xu[e] was to ensure the RET Wine and Jiuxiang acquisitions proceeded." A0584; OB, 21. These allegations were far more on-point to the argued theory of liability than anything alleged in *Bäcker*.

Further, not only was Amy Xue "the subject of discovery requests," she was the recipient of a subpoena in which she was represented by Zhou's own counsel. OB, 21-22. At his deposition, Zhou was shown his private WeChat conversations with Xue and directly and pointedly asked why she "reported" to him even after

becoming iFresh's CFO, to which he responded, "because I'm older." A0811-12 (Tr. at 97:12-98:5, 98:21-25). He was also asked about WeChats between them in which Xue—as iFresh's CFO—advised him on how he could get more iFresh shares. A0812-14. (Tr. at 99:8-106:14). And Zhou was also deposed about the critical chat in which Xue openly states that "our goal very clearly is to use the simplest, fastest method … the lowest cost to control and buy out iFresh and … control the risk of the other side being mischievous." A0816 (Tr. at 116:7-23).

Zhou's counsel also deposed both Deng and Fang, each twice, with Xue's wrongdoing coming up pointedly and repeatedly. As Fang testified: "You know, Amy Xue, these people are deceptive. She came into the company and then she is communicating with Zhou behind the scenes. . . . [T]hey have their own machinations behind the scenes … ." B312. Fang also testified that "it's not speculation that she was two-timing, Amy Xue. You look at this … this little comment at the end here, 'Nice to meet everyone via WeChat, looking forward to working with you,' but what we don't know is, you know, that now she is whispering in the ear of Zhou that we are going to take over iFresh." *Id.* Zhou's counsel then demonstrated a keen awareness of the theory that they now claim is waived by asking Fang directly: "[D]o you have any personal knowledge of the allegations that Amy Xue was trying to help plaintiff … ?" B380.

Similarly, at his second deposition, Deng clearly explained why he felt he'd been wronged by Zhou and Xue: "Later on, … we figured out it was part of the scheme, and during the whole negotiation of the transaction it was Amy Xue who reported to the board, and Amy Xue was his person." A1203 (Tr. 42:14-21).

In an amended complaint following discovery, Defendants repeatedly accused Zhou of colluding with Xue at iFresh's expense. For example, the complaint alleges that "[o]n March 3, 2020, Zhou asked Cheng and Xue to figure out how to increase RET Wine's valuation so they could get more shares of iFresh." A0932 (¶ 51).

It further alleges that "on March 19, 2020, in a group chat between Xue, Zhou, and Cheng, Xue stated that 'our goal very clearly is to use the simplest fastest method, using the lowest possible expense to control and buy out iFresh[.]' This communication was not disclosed to iFresh's board. Had it been disclosed, Deng and Fang would not have agreed to [the] sale of iFresh stock to Zhou, or to the RET Wine or Jiuxiang transactions." A0941 (¶¶ 97-98). And there is still more, in the form of pretrial briefing and page after page of trial transcripts in which Xue comes up repeatedly. *See e.g.* A1404, 1415-16, 1585, 1640, 1705.

As the foregoing illustrates, if the handful of discovery requests, snippets of deposition testimony, and comparatively vague allegation in the complaint touching on an alternative theory was enough to put the *Bäckers* on notice about the plaintiff's theory, it cannot possibly be that the targeted and explicit discovery requests,

deposition testimony, and detailed allegations about Zhou and Xue's collusion was not enough to put Zhou on notice here simply because the label "fiduciary duty" was not written into the single count declaratory judgment complaint.

Just as important, Zhou contends that the trial court did not, as Defendants argued, simply ignore all facts underlying Xue's breach of fiduciary duty for fraud. AB, 40-41. But the sole record evidence cited to support this assertion is the trial court's finding that an e-mail from her describing certain corporate actions related to one of the three transactions litigated below did not contain a false statement. But that isolated e-mail containing statements the trial court found to be literally true is neither here nor there. It does, however, illustrate the point, which is that in taking the literally true e-mail as a sign of non-fraud, while completely ignoring the extensive collusion between iFresh CFO and Zhou, the trial court erred by overlooking an entire body of critical evidence showing fraud. OB, 47-48.

CONCLUSION

For the foregoing reasons, Defendants respectfully request this Court reverse in the respects detailed above.

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CERTIFICATE OF SERVICE

I, John G. Harris, hereby certify that the foregoing DEFENDANTS' REPLY BRIEF was served upon the following in the manner and on the date indicated below:

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