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Case Number 322,2024

IN THE SUPREME COURT OF THE STATE OF DELAWARE

BENJAMIN WARNER,

Plaintiff-Below/Appellant,

v.

TIMOTHY C. TYSON, RICHARD CUNNINGHAM, CLIVE KABATZNIK, VINCENT PALMIERI, EDWARD ROFFMAN, and MICHAEL TAGLICH,

Individual Defendants-Below/Appellees,

-and-

ICAGEN, INC. nka IXC DISCOVERY, INC.,

Nominal Defendant-Below/Appellee.

No. 322, 2024

On appeal from the Court of Chancery, C.A. 2023-0159-PAF

PUBLIC VERSION
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APPELLANT'S OPENING BRIEF

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

NATURE OF THE PROCEEDINGS

This appeal presents the apparently novel question of whether a stockholder states a cognizable claim when alleging that directors approving a transaction face a disabling conflict of interest when the transaction, as presented, inured to their personal benefit to the tune of more than $19 million dollars even if the totality of that benefit is ultimately not realized. Here, the Chancery Court committed reversible error in refusing to consider the apparent conflicts the directors faced at the time of approving the transaction or alternatively, at the time the complaint was filed.

Plaintiff Benjamin Warner ("Plaintiff") brought this class action/derivative action challenging Icagen, Inc.'s ("Icagen") unfair asset sale of its core assets located in North Carolina to Ligand Pharmaceuticals, Inc. ("Ligand"). Plaintiff alleged that the sale was consummated both at an unfair price - $15 million – and utilizing a process that was unfair to the minority unaffiliated stockholders, such as Plaintiff. (the "Transaction").

As to price, although somewhat in financial distress at the time of the Transaction, Icagen's future business prospects at that time were promising. Later events, as demonstrated in the Complaint, confirm Icagen's financial success. As to process, the majority of directors both approving the Transaction and serving at the time the Complaint was filed engaged in self-dealing, in that approval of the Transaction personally assured them of a financial package consisting of, in whole or in part, the awarding of significant warrants and options, the repayment of loans at sizable interest rates, and, the likelihood of a preference payment totaling approximately $19 million. Moreover, the Transaction was consummated without Icagen's utilization of a special committee of independent and disinterested directors, without Icagen's obtaining or even seeking a fairness opinion from independent financial advisors stating that the terms of the transaction are fair from a financial point of view, and, without Icagen obtaining the consent of any unaffiliated stockholders. In short, Defendants took no steps to adequately safeguard the interests of all stockholders in connection with defendants' self-dealing transaction.

In response to Plaintiff's Verified Class Action Complaint (the "Complaint"), Defendants moved to dismiss. The defendants in this action are Icagen (now known as IXC Discovery, Inc.), Timothy Tyson, Richard Cunningham, Clive Kabatznik, Vincent Palmieri, Edward Roffman, and Michael Taglich.

Following oral argument, the Chancery Court granted the motion to dismiss in an Order dated July 12, 2024. Vice Chancellor Fioravanti declined to apply entire fairness, finding that Plaintiff did not state a non-exculpated claim of breach of fiduciary duty against three of the five individual director defendants who had approved the Transaction - namely Timothy Tyson, Clive Kabatznik or Michael Taglich. The Vice Chancellor declined to find that Plaintiff had adequately pled that these directors approving the Transaction were "interested" in the Transaction in that Plaintiff had supposedly failed to allege that any interest that inured to the benefit of the defendant was material as to that director. Mere ownership by a director defendant of the weaponized Series C Preferred Stock at the time of the Transaction, which, by its terms created, among other things, the potential for an enormous personal return for the director trough a Cash Liquidity Event or the repayment of personal loans was insufficient on its face, according to the Vice Chancellor, to demonstrate interestedness.

As argued herein, the Chancery Court's ruling overlooks various facts alleged by Plaintiff supporting the allegations that the directors who both approved the Transaction, and, served as directors at the time the Complaint was filed, in whole or in part, as specified below: 1) received payment on their outstanding loans with substantial interest (from the approved Transaction); 2) received substantial and valuable warrants and options as part of the Transaction; and, 3) stood in line to profit handsomely from what seemed at the time to be a forthcoming profitable Cash Liquidity Event. These defendants had a disabling interest in the Transaction.

Plaintiff timely appealed.

SUMMARY OF THE ARGUMENT

1. Because a majority of the directors at the time of the challenged Transaction and/or a majority of the directors at the time of the filing of the Complaint did or stood to personally profit substantially from the Transaction in ways that were not available to the unaffiliated common stockholders, those individual defendants were disablingly interested in the transaction. Each of the individual defendants Tyson, Taglich and Kabatznik profited handsomely from the Transaction and also stood to personally profit from the anticipated $19 million liquidation preference that was to be triggered as set forth in the relevant disclosure documents.

2. The Individual Defendants pushed through the Transaction, selling off "the crown jewels" of the Company for their own financial advantage for an inadequate price and utilizing a process that did not provide for procedural safeguards for unaffiliated investors.

3. Entire fairness applies whenever a majority of the corporation's directors approving a transaction engages in a conflicted transaction.

STATEMENT OF FACTS

I. Icagen's Business

Icagen is a drug discovery company that described its business model in 2020 as "focus[ed] on research collaborations with large pharmaceutical and biotechnology companies and foundations to support the discovery and development of innovative pharmaceuticals." (A015 ¶ 2; A021 ¶ 28). In May 2018 the Company announced its first collaboration with the Cystic Fibrosis Foundation to discover therapies to treat cystic fibrosis, and, in December 2018, it announced its second collaboration with F. Hoffmann-La Roche Ltd. and Hoffmann-La Roche Inc. (collectively, "Roche") to discover therapies for certain neurological diseases. *Id.*

The Company operated out of two locations – Durham, North Carolina and Tucson, Arizona. *Id.*

II. The Defendants

The defendants in this action are Icagen (now known as IXC Discovery, Inc.); Timothy Tyson ("Tyson") (director and non executive chairman of the board); Richard Cunningham ("Cunningham"), former President, CEO of the Company and Director (starting in April 2020), former directors Clive Kabatznik ("Kabatznik"), Vincent Palmieri ("Palmieri"), Edward Roffman ("Roffman") and Director Michael Taglich ("Taglich"). (A019-A021¶¶ 15, 17, 19, 22, 24-26).

Three of the five directors approving the Transaction (Tyson, Taglich, and Kabatznik) were alleged to be interested in the Transaction. (A040-045 ¶¶ 60-64).

The Company's directors at the time of the filing of the Complaint were Tyson, Cunningham and Taglich. (A060 ¶ 94). All three of them were alleged to be interested in the Transaction.

III. The Preferred C Shares

The Company's earlier issuance in 2018 of Series C Preferred Stock helped pave the way for the Board's entering into the unfair Transaction without notice to or consent from the unaffiliated shareholders. (A503).

As Plaintiff alleged, the "Company had earlier provided supervoting stock in the hands of its management and directors and improperly diluted the holdings of the common stockholders" by the issuance of the Preferred C shares. (A029 ¶ 41).

The Company (or more precisely its then Board) diluted the holdings of the common stockholders and served to weaponize the Preferred Shares at the time of the Transaction by providing that each holder of Series C Preferred Stock (which had been reserved for Board members and those chosen by the Board including the brother of a Board member) had the right to cast the number of votes equal to three times the number of shares into which the Series C Preferred Stock is convertible into and had the right to elect one director on the Corporation's Board of Directors. The holders of the Series C shares were also a necessary party to approving "any sale, lease, transfer, exclusive license or other disposition, in a single transaction or series of related transactions of all or substantially all the assets of the Corporation" in that at least 75% of the Series C Preferred Stock must approve the Transaction. Then, for good measure, the Board provided for handsome special renumeration for the Series C Preferred Stock holders in that "[i]n the event of the Corporation's liquidation, dissolution or winding-up" the holders of the Series C Preferred Stock "are entitled to a preference on liquidation equal to $5.25 per share of Series C Preferred Stock plus all accrued and unpaid dividends [with a dividend rate of 12% per annum]." "In addition, the Corporation has the right to redeem the shares of Series C Preferred at any time for a price per share equal to $5.25 subject to adjustments." (A029-034 ¶¶ 41-42; A504).[1]

As the Complaint alleged:

> In changing the capital structure and issuing the class of Preferred C shares, with super voting powers, the Board and management: 1) gave themselves enhanced voting rights (3x) that allowed insiders to take voting control (51%) of entire company; 2) gave themselves a $5.25 liquidation preference meaning that these insiders will receive 1.5

[1] Ironically, in issuing the Preferred C shares, the Board purposefully limited its ability and the Company's ability to raise financing (A040 ¶ 59).

> times their investment before any other shareholders received anything; 3) gave themselves 1x warrant coverage which effectively doubles their portion of the company in case of a situation like the Transaction (asset sale); 4) gave themselves 12% cumulative interest on the shares, and; 5) gave themselves the ability for each Series C holder to appoint a director. (A039-040 ¶ 58).

Importantly, the transaction also resulted in a Series C liquidation preference estimated to be $19.4 million. (A039-040 ¶¶ 56- 58).

The Series C Preferred Stock was not made available to Icagen stockholders but was instead owned by the majority of the Directors approving the Transaction. Namely, Defendants Tyson, Kabatznik, and Taglich and by the majority of the Director Defendants that comprised the Board at the time the Complaint was filed. (A040-045 ¶¶ 61-64; A060 ¶94).

IV. The Transaction

Faced with significant debt, Icagen, on April 2, 2020, completed the sale of its core assets of its North Carolina operations to Ligand for $15 million in cash pursuant to an asset purchase agreement. Ostensibly, Icagen was entitled to additional payments of up to $25 million dependent on the achievement of certain revenue achievements. (A015 ¶1; A017 ¶ 7).

At the time of approval of the Transaction, Icagen was party to a forbearance agreement (the "Second Forbearance Agreement") with its senior secured creditors (the "Creditors"). The Second Forbearance Agreement required, among other obligations, that Icagen either sell its North Carolina operations on terms acceptable to the Creditors by February 15, 2020, and use a portion of the proceeds to pay a portion of its obligations to the Creditors or issue the Creditors 600,000 shares of Series C Preferred to avoid re-entering default with respect to the company's senior secured debt and looming foreclosure on substantially all of the Company's assets. The Creditors already held at least 1,900,000 shares of Series C Preferred." (Court Opinion at 3-4, internal footnotes omitted, attached as Exhibit A, "Opinion").

Icagen's Definitive Information Statement filed with the SEC (on Schedule 14C) discussing the asset sale was filed on March 2, 2020 ("14C")." (A 015-16 ¶ 2). A Preliminary Information Statement had been filed on February 19, 2020. *Id.*

The Company went dark after Icagen's filing with the SEC on April 22, 2020 (A 019 ¶16).

Details of the Transaction are described in the Complaint as follows:

> Icagen and its wholly-owned subsidiaries Icagen Corp., XRPro Sciences, Inc. and Caldera Discovery, Inc. entered into an Asset Purchase Agreement dated as of February 11, 2020 (the "APA") with Adjacent Acquisition Co., LLC ("Buyer"), a subsidiary of Ligand Pharmaceuticals, Incorporated, a Delaware corporation ("Ligand"), for the sale to Buyer of all of the Corporation's assets that are located in its Durham, North Carolina facility for a price of $15 million. Those assets included, but were not limited to, the Corporation's research and development operations focused on ion channels and transporters, High Throughput Screening and lead optimization technology, assay development and x-ray fluorescence-based assays (the "Asset Sale").

These assets represented a significant portion of the assets of the Company. (A016 ¶ 3).

While the proceeds of the asset sale were to be primarily used to pay the Company's loans owed to its main creditor, Perceptive Credit Holdings II, LP ("Perceptive")[2], importantly, the Individual Defendants were to be personally repaid loans they had made to Icagen on terms that were very favorable to these Defendants. The remaining capital raised from the sale was to be used for other purposes including working capital. (A025-26 ¶ 37).

By the terms of the APA, Icagen was to continue its operations at its only other facility, in Tucson. However, Icagen had agreed to promptly retain a commercial real estate broker for the sale of the Tucson Facility by July 16, 2020, which it was required to sell by August 15, 2020 in accordance with the terms of the Icagen-T Credit Agreement. It was anticipated that proceeds from the sale of the Tucson Facility, in conjunction with the proceeds raised in the Transaction would fully pay off all of the Company's debts including the loans provided by the individual defendants. (A018 ¶ 8; A026 – A028 ¶¶38-40; A 121; A498).

[2] Which loans were then in default but subject to forbearance until March 15, 2020, provided that no new default occurred before such date. (A016 ¶ 4; A026-27 ¶ 38).

Because the sale of the Tucson facility was both required and anticipated at the time of the approval of the Transaction, *Id.*, it was reasonably anticipated that Icagen would undergo a Cash Liquidity Event, triggering Icagen's obligation to pay the preference totaling approximately $19.4 million inuring to the benefit of the holders of the Series C Preferred stock, including individual defendants Tyson, Kabatznik, Taglich and Cunningham. To wit, Plaintiff's Complaint alleged in relevant part:

> In the event of the Corporation's liquidation, dissolution or winding-up, holders of the Series C Preferred Stock are entitled to a preference on liquidation equal to $5.25 per share of Series C Preferred Stock plus all accrued and unpaid dividends. Upon the occurrence of a Cash Liquidity Event (as defined below), the holders of the Series C Preferred Stock can require the Corporation to redeem their shares of Series C Preferred Stock for a price per share equal to $5.25, subject to adjustments. In addition, the Corporation has the right to redeem the shares of Series C Preferred at any time for a price per share equal to $5.25 subject to adjustments. A "Cash Liquidity Event" is defined as the closing of any sale, lease or licensing transaction relating to a single asset or multiple assets other than in the Corporation's ordinary course of business, including, but not limited to a sale of a building, sale of biological assets or other upfront payments, resulting in aggregate gross proceeds received by the Corporation at closing or closings in a transaction or transactions during any twelve (12) month period in excess of $40 million. **Thus, the Asset Sale together with the sale of the Tucson Facility may be considered to be a Cash Liquidity Event.** (emphasis added).

(A029-030 ¶41).

At the time the Complaint was filed, the Tucson facility had yet to be sold. (Opinion at 11 n. 28). The Company went dark after Icagen's filing with the SEC on April 22, 2020. (A019 ¶16).

V. The Majority of Individual Directors Were Conflicted As They Were Interested in The Transaction

Icagen itself warned in its 14C that its directors could be conflicted in voting on the Transaction inasmuch as they were financially interested in the Transaction. Icagen warned that it's "Board and management acknowledged" "that the Series C holders could have diverging interests that would prevent them from acting as fiduciaries for the common shares…." More specifically, Icagen disclosed that in connection with the Preferred Series C stock, "[t]hese preferential rights could also result in divergent interests between the holders of shares of the Series C Preferred Stock and holders of our common stock." (A040 ¶ 59).

As Plaintiff alleged, the majority of Icagen directors, individual defendants herein, who had voted to approve the Transaction suffered from disabling conflicts of interest that should have counseled them to abstain from voting to approve the Transaction that materially inured to their personal benefit. More specifically, each of the relevant individual directors voted for the Transaction at a time when they believed they were to receive, among other things, through their holdings of the then weaponized Series C preferred stock, a portion of the $19.4 million preference not available to the common stockholders.

To wit, the Transaction weaponized the Series C preferred for the benefit of the Individual Defendants. As Plaintiff alleged:

> In changing the capital structure and issuing the class of Preferred C shares, with super voting powers, the Board and management: 1) gave themselves enhanced voting rights (3x) that allowed insiders to take voting control (51%) of entire company; 2) gave themselves a $5.25 liquidation preference meaning that these insiders will receive 1.5 times their investment before any other shareholders received anything; 3) gave themselves 1x warrant coverage which effectively doubles their portion of the company in case of a situation like the Transaction (asset sale); 4) gave themselves 12% cumulative interest on the shares, and; 5) gave themselves the ability for each Series C holder to appoint a director.

(A039-040 ¶ 58).

In describing the weaponization of the Series C Preferred Stock, the Chancery Court noted:

> Each share of Series C Preferred held a liquidation preference that, upon election, required the Company to redeem their shares for $5.25 per share upon the sale of assets resulting in gross proceeds over $40 million (a "Cash Liquidity Event"). The Series C Preferred was also entitled to a 12% cumulative dividend and could be converted, at the option of the holder, to a number of shares of common stock equal to $3.50 and the value of accumulated dividends. The Series C Preferred also had the "right to cast the number of votes equal to three times the number of shares into which the Series C Preferred Stock is convertible and has the right to elect one director." The vote of a majority of the Series C Preferred was required for certain actions, including amending the certificate or bylaws, liquidating, redeeming

> any of the Company's stock, or increasing the size of the Board. The warrants, which had an exercise price of $3.50 per share, included protections for holders of the warrants against dilution and in the event of any "Fundamental Transaction." The Company did not make the Series C Preferred available to the entire stockholder base.

(Opinion at 2-3, internal footnotes omitted).

Because, as disclosed in the 14C, "[t]he asset sale, together with the sale of the Tucson Facility may be considered a Cash Liquidity Event." And, because at the time the vote on the transaction, the Company was required to sell the Tucson facility, a "cash liquidity event" would be triggered. Again, as the 14C disclosed, "[u]pon the occurrence of a Cash Liquidity event, the holders of the Series C Preferred Stock can require the Corp. to redeem their shares of Series C Preferred Stock for a price equal to $5.25, subject to adjustments." (A029-030 ¶41).

Critically, at the time of the approval of the Transaction, the sale of the Tucson Facility was mandated as part of the Transaction, thus it was reasonable for the voting directors to believe that the Transaction was tantamount to a "Cash Liquidity Event." Such Cash Liquidity Event triggered outsized financial benefits for the voting Directors and not for the unaffiliated stockholders. Such outsized benefits consisted of a preference on liquidation of up to $5.25 per share representing a return of 1.5 times (plus all accrued and unpaid dividends – with a dividend rate of 12% per annum). In addition, the Individual Defendants gave themselves 1x warrant coverage which effectively doubles their portion of the company in case of a situation like the Transaction. The financial benefit the interested directors provided for themselves amounted to approximately $19mm.

The fact that the Tucson Facility was not sold as anticipated at the time the Transaction was approved does not minimize the conflict presented to the directors who approved a Transaction they were interested in at the time of approving the Transaction.

Moreover, and as further stated below with specificity, the majority of the directors approving of the Transaction and/or serving as directors at the time the complaint was filed assured themselves of additional warrants and enhanced the likelihood that they would personally be paid for their loans at high interest rates.

More specifically, Individual Defendant Tyson was financially interested in the Transaction he voted to approve in that he personally controlled 19.9% of the Series C Preferred Stock and stood to gain financially from the $19.4 preference. He also stood to gain financially by receiving attendant warrants. In addition, he personally profited in the Transaction from the repayment of a bridge note (along with the attendant warrants) in the principal amount of $300,000 (raised to $344,000) with an interest rate of 15% (having been raised from 10%). (A040-42 ¶¶ 60, 61; A052-53 ¶73).

Individual Defendant Taglich was financially interested in the Transaction he voted to approve in that he personally controlled 3.3% of the Series C Preferred Stock and stood to gain financially from the $19.4 million preference. He also stood to gain financially by receiving attendant warrants. In addition, he personally profited in the Transaction from the repayment of a 15% subordinated promissory note in the aggregate amount of $250,000 (along with the attendant warrants). In addition, Taglich's brother, Robert Taglich, also controlled 3.3% of the Series C Preferred Stock (along with attendant warrants) and also held a 15% subordinated promissory note in the aggregate amount of $250,000 (along with attendant warrants). (A 040, 042-44 ¶¶ 60,62-63).

Individual Defendant Kabatznik was financially interested in the Transaction he voted to approve in that he personally controlled 0.8.% of the Series C Preferred Stock (or 28,571 shares) and stood to gain financially from the $19.4 million preference. He also stood to gain financially by receiving attendant warrants. (A040, A044-45, ¶ ¶ 60,64).

Individual Defendant Cunningham, Icagen's President and CEO and a director at the time the Complaint was filed, personally received compensation after Icagen was no longer a reporting company, which amounted to a bribe in that documents produced by Icagen show that [redacted]

[redacted] (A045 ¶65; A055-56 ¶77; A056-57¶79; A057 ¶ 82).

VI. The Transaction Was Materially Flawed As To Price

Although the Defendants disclosed in 2019 that Icagen's working capital was "insufficient to meet its short-term cash requirements and fund any future operating losses" raising doubt as to whether the Company could continue as a "going concern" for the following year (A035-36 ¶47), Defendants did not accurately portray the financially bright future that lay ahead. Ironically, it was Ligand, in justifying the Transaction, that set forth the more accurate portrayal. Ligand, in an investor presentation dated February 11, 2020, portrayed Icagen as a "profitable, cash flow positive company; expected to be immediately accretive" quantifying the projected revenue to be $7 million in 2020 and $12 million in 2021. (A036¶ 48). Ligand was expecting to make back more than the $15 million it was spending right from the very start. (A500-01).

Later, just months after the Transaction closed, Ligand announced in a press release that Ligand and GSK had entered into a Global Collaboration and License Agreement that leveraged Icagen's Technology and that based on this agreement, "Ligand Group is eligible to receive an upfront payment of $7 million and potential milestone payments and fees of up to $154.5 million and tiered royalties." (A036-37 ¶ 51).

Then, to show the continued good fortunes of the Icagen partnership, Ligand disclosed in 2022 that "Ligand expanded an existing collaboration and license agreement with GlaxoSmithKline (GSK) to leverage Ligand's Icagen Ion Channel Technology to target neurological diseases. Ligand received an upfront payment of $10 million and is eligible for milestones of up to $247.5 million, and tiered royalties on net sales of any drug from the collaboration commercialized by GSK." (A038 ¶ 53).

VII. The Transaction Was Materially Flawed As To Process Beyond the Interestedness of a Majority of the Directors

The Transaction was materially flawed as to process even aside from the financial interestedness of a majority of the directors approving the Transaction.

The Defendants ran roughshod over Plaintiff and the other unaffiliated shareholders in that the Defendants failed to obtain an independent fairness opinion. The defendants failed to share with the unaffiliated stockholders any valuation materials addressed to the fairness or reasonableness of the Transaction.[3]

In fact, approval of the Transaction was a foregone conclusion as early as the filing of the Preliminary Information Statement with the SEC on February 19, 2020. The Board of Directors had approved the Transaction on February 10, 2020. A majority of the voting power of the outstanding shares and 100% of the holders of the Company's Series C Convertible Redeemable Preferred Stock, $0.001

[3] Instead, the 14C noted in passing the conclusory statement that the "[T]ransaction is in the best interests of the Corporation's shareholders because it believes that the purchase price represents a fair valuation of the Assets and that the Corporation will have a better chance of increasing shareholder value by selling the Assets in this transaction than it would if the Creditor were to foreclose on all of the Corporation's assets including the assets of Icagen-T." (A027-028¶ 39). *See also* (A028¶ 40). ("The Board has carefully considered the Asset Sale and the price for the assets to be sold. The Board believes that it has found the best reasonably available price. After considering the past performance of the assets and lack of interest from other suitors in a sale or financing, the Board concluded that the price we will receive for the Asset Sale is fair to us and to our stockholders…"). *Id*.

par value per share ("Series C Preferred Stock" or "Series C") voted in favor of the Transaction by written consent on February 19, 2020.

This majority of the voting power was vested in the individual defendants only because the interested directors voted for the Transaction using the 3x enhanced voting rights of the Series C. Without this enhanced voting power, the Transaction could not have been approved by the insiders (individual defendants). Consequently, there was no general stockholder vote on the Transaction.

Notice to the shareholders only followed thereafter as no general shareholder vote was solicited or required. As the 14C made clear, "[b]ecause the written consent of the holders of a majority of our voting power satisfies all applicable stockholder voting requirements, we are not asking for a proxy: please do not send us one." (A 016-17 ¶¶ 5-6; A018 ¶ 9; A025 ¶ 35).

Stated differently, the Board, in connection with the Transaction, never sought nor needed the approval of the unaffiliated stockholders because of the control they obtained by issuing themselves the Series C and because of the Series C enhanced voting rights that they exercised. (A506).

ARGUMENT

I. THE COURT OF CHANCERY ERRED IN DECLINING TO FIND THAT A MAJORITY OF THE DIRECTORS WERE INTERESTED IN THE TRANSACTION

A. Question Presented

Did the Court of Chancery err in finding that the Complaint did not adequately plead that a majority of the directors were interested in the transaction? (Opinion at 11, A510-528).

B. Scope of Review

The Court of Chancery's ruling on a motion to dismiss is subject to *de novo* review. *See Cent. Mortg. Co. v. Morgan Stanley Mortg. Capital Holdings, LLC*, 27 A.3d 531, 535 (Del. 2011). When considering a motion to dismiss for failure to state a claim under Court of Chancery Rule 12(b)(6), the Court is required to "(1) accept all well pleaded factual allegations as true, (2) accept even vague allegations as 'well pleaded' if they give the opposing party notice of the claim, (3) draw all reasonable inferences in favor of the non-moving party, and (4) do not affirm a dismissal unless the plaintiff would not be entitled to recover under any reasonably conceivable set of circumstances." *Id*. at 535.

C. Merits of Argument

Plaintiff alleged that a majority of the directors voting to approve the transaction were financially interested in the Transaction in that they would have reasonably anticipated at the time of the vote that the Transaction, in conjunction with the required sale of the Tucson Facility, would trigger a Cash Liquidity Event thereby creating a $19.4 million preference for them to share in. Even were there no Cash Liquidity Event, the majority of directors received outsized financial benefits as a result of their holding of the Series C preferred stock, then weaponized by entering into the Transaction, through, among other things the awarding of sizeable warrants inuring to their personal benefit. Lastly, the directors also personally benefitted financially from the Transaction by providing the Company with the liquidity that facilitated the payment to those individuals of personal loans payable at outsized interest. (A019-021 ¶¶ 17-23; A021 ¶¶ 26-27; A029-030 ¶ 41; A038-045 ¶¶ 55-65).

Plaintiff further argued that, in connection with his derivative allegations, the majority of directors serving at the time the complaint was filed were also conflicted in that they each had financially benefitted disproportionately and could still benefit even more were the Tucson facility to be sold at a certain price. (A60-61 ¶ 96). Given the conflicts facing the Individual Defendants, entire fairness applies.

In the Court's ruling, the Vice Chancellor declined to find that any disabling financial conflict had been alleged finding that Plaintiff had not sufficiently pled that the financial benefits conferred to the individual defendants were material as to them.

In the first instance, the Chancery Court limited its interestedness analysis to merely the allegations that the interested director simply held the Series C Preferred Stock. (Opinion at 9-10). Then, the Chancery Court noted: "[e]ven assuming that a director's ownership of Series C Preferred could give rise to a disabling interest in connection with the approval of the Ligand Transaction, the Complaint does not contain well-pleaded facts to create a reasonable inference that Kabatznik's ownership of Series C Preferred was material to him." (Opinion at 11).

Curiously, the Chancery Court found that Plaintiff failed to state a claim against Tyson and Taglich, two of the directors approving the Transaction, but provided no explanation supporting such claim. (Opinion at 9, 16). In limiting the finding as to materiality to Kabatznik, the Chancery Court committed reversible error in that materiality as to Kabatznik (as well as Tyson and Taglich) was sufficiently pled.

The Complaint asserted both direct and derivative claims. The Court dismissed finding that Plaintiff had failed to adequately allege breach of fiduciary claims and never determined which legal theory applied. (Opinion at 9). As argued herein, the Court of Chancery erred in dismissing the allegation of breach of fiduciary duty.

I. Plaintiff Adequately Demonstrated That A Majority of The Directors Were Interested In The Transaction

It is black letter law that the directors and officers owe fiduciary duties of care and loyalty to stockholders. "[T]he duty of loyalty mandates that the best interest of the corporation and its shareholders takes precedence over any interest possessed by a director, officer or controlling shareholder and not shared by the stockholders generally." *In re MultiPlan Corp. S'holders Litig.*, 268 A.3d 784, 799-800 (Del. Ch. 2022).[4]

As the *MultiPlan* Court set forth, a director or officer "competes with common stockholders when [he or she] (1) "receives greater monetary consideration for its shares than the minority stockholders"; (2) "takes a different form of consideration than the minority stockholders"; or (3) receives "a 'unique benefit' by extracting 'something uniquely valuable to the [director or officer], even if the [director or officer] nominally receives the same consideration as all other stockholders'" to the detriment of the minority." *In re MultiPlan Corp. S'holders Litig.*, 268 A.3d at 810 (internal citation omitted).

Plaintiff alleged that three of the five directors approving the Transaction, Tyson, Taglich and Kabatznik, engaged in self-dealing by having an actionable and disqualifying financial interest in the Transaction. In *DiRienzo v. Lichtenstein*, 2013 WL 5503034, at *12 (Del. Ch. Sept. 30, 2013) (Del. Ch. Sept. 30, 2013), the

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[4] *Citing* to *Cede & Co. v. Technicolor, Inc.*, 634 A. 2d 345, 361 (Del. 1993).

Chancery Court held that "[w]hen a fiduciary appears on both sides of a transaction or receives a personal benefit that is not shared by all stockholders, that fiduciary has an impermissible self-interest in the transaction that implicates the duty of loyalty.[5] Not all personal benefits, however, create a disqualifying self-interest for a fiduciary. Only benefits that are material to the fiduciary, as judged from the perspective of the fiduciary herself, raise issues under the duty of loyalty."[6]

The Delaware Supreme Court has set forth the materiality standard as one that is "reasonably likely to affect the decision-making process of a reasonable person[.]'" *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 363 (Del. 1993), *modified on reargument*, 636 A.2d 956 (Del. 1994)). The *DiRienzo* Court expanded on its view of materiality in noting that "[a] director's potentially conflicting financial interest need not be large, but there must be some basis to conclude it is material enough to that director that it could overcome their rational business judgment."[7]

In its Order deciding this matter, the Chancery Court appeared to perceive Plaintiff's allegations of interestedness to rest on the directors' mere possession of Preferred C shares. The Court noted, "Plaintiff argues that Tyson, Taglich, and

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[5] *Citing* to *Benihana of Tokyo, Inc. v. Benihana, Inc.*, 891 A.2d 150, 191 (Del. Ch. 2005).
[6] *Citing* to *In re Transkaryotic Therapies, Inc.*, 954 A. 2d 346, 364 (Del.Ch. 2008).
[7] *Citing* to *Gantler v. Stephens*, 965 A.2d 695, 708 (Del. 2009)

Kabatznik were interested in the Ligand Transaction because they held Series C Preferred." (Opinion 10-11).

But Plaintiff's allegations did not rest on the mere possession of the Series C Preferred shares, but on the triggering weaponization of such shares (which had been made available to the directors and certain officers, but not the common stockholders) ***triggered by the approval by the conflicted individual defendants of the Transaction itself***. The weaponization contained multiple prongs, alleged to have been super majority voting rights making it easy for the directors to approve the Transaction without a stockholder vote, warrants which effectively doubled their portion of the company as a result of the Transaction, a 12% cumulative interest on the shares and a $5.25 liquidation preference (meaning that the approving directors awarded themselves 1.5 times their investment before other shareholders received anything). (A039-040 ¶ 58; A514-16).

As the Court recognized at oral argument, an aspect of this interestedness analysis was the payment of the liquidation preference which could be triggered by a "Cash Liquidity Event." At oral argument, the Chancery Court asked counsel for the defendants "[d]id that transaction constitute a cash liquidity event?" (A555). Defendants' counsel responded "[n]o." (A556).

But as Plaintiff's counsel pointed out at oral argument, and as the pleadings showed, the cash liquidity event was expected, at the time of approval of the

Transaction, to be triggered by the combination of the asset sale and the required later sale of the Tucson facility. The liquidation preference was valued at $19.4 million. (A568-570).

Because Icagen went dark following the Transaction, there was no record evidence as to whether the Tucson facility had indeed eventually been sold. The Court noted in its Order that there was no evidence that it had been sold (Opinion at 11, n.28). However, as Plaintiff has argued, and the Court ignored, it does not matter whether or not the Tucson facility was sold, what matters is that <u>at the time of the vote</u>, the directors voted to approve a transaction that contemplated that the cash liquidity event would occur resulting in the payout of the $19 million plus the other benefits. To that end, Plaintiff's counsel stated at oral argument, "[s]o what you have, Your Honor, is that when a vote and a decision is presented to the directors of the company, they are voting for an asset sale that by its terms also contemplates the sale of the Tucson facility, contemplates the repayment of all of the debts, contemplates the payment of the preference." (A570-71).

Importantly, the Court ignored the argument and the evidence that at the time of the vote the directors were conflicted in that they expected the cash liquidity event to occur and the payment of the $19.4 million preference (in addition to all the other substantial benefits described).

Critically, in analyzing the alleged interestedness of the majority of the directors who approved the Transaction, the Court did not analyze the interestedness of two of the directors, Tyson and Taglich, focusing instead on Kabatznik.

The Court wrote:

> Plaintiff's theory appears to be that, even though the holders of the Series C Preferred or unsecured debt received none of the proceeds from the $15 million cash payment in the Ligand Transaction, there was an expectation that they could potentially receive payments if a contingent payment was made or other assets were later sold. Even assuming that a director's ownership of Series C Preferred could give rise to a disabling interest in connection with the approval of the Ligand Transaction, the Complaint does not contain well-pleaded facts to create a reasonable inference that Kabatznik's ownership of Series C Preferred was material to him.

(Opinion at 11, internal footnotes omitted).

While one is left guessing as to why the Court dismissed the breach of fiduciary allegations as against Defendants Tyson and Taglich, the Chancery Court erred in its materiality finding with regard to Defendant Kabatznik. To the extent that the Court had any misgivings as to the adequacy of Plaintiff's allegations as to materiality regarding Defendants Tyson and Taglich, those misgivings, as explained below, should also be put to rest.

In considering materiality, the Court, in its Order, undertook a discussion of the applicable legal standard. The Court wrote:

> This court has opined, even in the absence of director-specific allegations, that payments of a certain level may be presumptively

> material. *See In re MultiPlan Corp. S'holders Litig.*, 268 A.3d 784, 813 (Del. Ch. 2022) ("A greater than half-million-dollar payout is presumptively material at the motion to dismiss stage."); *Orman*, 794 A.2d at 31 ("I think it would be naïve to say, as a matter of law, that $3.3 million is immaterial."). There are no allegations that any Defendant received or expected to receive any payment from the proceeds of the Ligand Transaction, or that Kabatznik's interest in the Series C Preferred was material to him. *McMullin v. Beran*, 765 A.2d 910, 923 (Del. 2000) ("In assessing director independence, Delaware courts apply a subjective 'actual person' standard to determine whether a 'given' director was likely to be affected in the same or similar circumstances.") (citing *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1167 (Del. 1995)); *Orman*, 794 A.2d at 24 ("In determining the sufficiency of factual allegations made by a plaintiff as to either a director's interest or lack of independence, the Delaware Supreme Court has rejected an objective 'reasonable director' test and instead requires the application of a subjective 'actual person' standard to determine whether a *particular* director's interest is material and debilitating or that he lacks independence because he is controlled by another.").

(Opinion at 13-14, n. 31).

But again, curiously, the Court did not analyze the allegations of interestedness as against defendants Tyson and Taglich. Instead, the Court merely repeated Plaintiff's allegations of interestedness.

As to defendant Tyson, the Court noted:

> Tyson held 685,704 shares (19.9%) of the Series C Preferred, 164,284 shares of common stock, warrants to purchase 820,704 shares of common stock, and options to purchase 223,500 shares of common stock, of which options to purchase 223,292 shares were vested or would vest within 60 days, altogether representing beneficial ownership of 23.3% of the Company's common stock, and a $300,000 bridge note with, at the time, a 10% interest rate.

(Opinion at 4-5).

At no time did the Court consider Plaintiff's allegations that Tyson voted for the preference payout to him of approximately $3,599,946 (685,704 shares x $5.25/share) plus interest, based upon the likelihood of the cash liquidity event at the time of the vote. Nor did the Court consider the sizeable warrants and options Tyson voted to award himself as part of the Transaction nor did the Court consider the personal loan that Tyson voted for the ability to repay at sizeable interest. Strikingly, the Chancery Court ignored Icagen's own representations, as alleged in the Complaint, that Tyson was conflicted when voting to approve the Transaction. Plaintiff alleged, as Icagen disclosed: "As such, Mr. Tyson has the ability to influence the manner and order in which the Corporation repays its debts and the payments under the Series C Preferred Stock and thus may be in a position to favor the repayment of his 10% Note and payments under the Series C Preferred Stock to the detriment of the holders of the Common Stock." (A041-42 ¶61). It was error for the Chancery Court to ignore this analysis.

As to defendant Taglich, the Court noted:

> Taglich held 114,285 shares (3.3%) of the Series C Preferred, 453,314 shares of common stock, warrants to purchase 340,461 shares of common stock, and options to purchase 57,500 shares of common stock, of which options to purchase 57,292 shares were vested or would vest within 60 days, altogether representing beneficial ownership of 14% of the Company's common stock, and a $250,000 promissory note with a 15% interest rate. Taglich's brother, Robert

> Taglich, a non- party, held 114,284 shares (3.3%) of the Series C Preferred and warrants to purchase 301,544 shares of common stock, together representing beneficial ownership of 10.7% of the Company's common stock, and a $250,000 promissory note with a 15% interest rate.

(Opinion at 5).

At no time did the Court consider Plaintiff's allegations that Taglich voted for the preference payout to him and his brother of approximately $1,199,987 (228,569 shares x $5.25/share) plus interest, based upon the likelihood of the cash liquidity event at the time of the vote. Nor did the Court consider the sizeable warrants and options Taglich voted to award himself and his brother as part of the Transaction nor did the Court consider the personal loans that Taglich voted for the ability to repay at sizeable interest. Strikingly, the Court ignored Icagen's own representations, as alleged in the Complaint, that Taglich was conflicted when voting to approve the Transaction. Plaintiff alleged, as Icagen disclosed: As such, Mr. Taglich has the ability to influence the manner and order in which the Corporation repays its debts and the payments under the Series C Preferred Stock and thus may be in a position to favor the repayment of his 15% note and payments under the Series C Preferred Stock to the detriment of the holders of the Common Stock." (A042-44 ¶¶62-63). It was error for the Chancery Court to ignore this analysis.

To the extent the materiality standard inquiry is properly framed as whether their interestedness could plausibly affect their ability to reasonably consider the merits of the transaction, both Tyson and Taglich satisfy the materiality standard.

The lone defendant the Court chose to conduct a materiality analysis was Kabatznik. In considering Kabatznik's holdings, the Court noted:

> Kabatznik held 28,571 shares (0.8%) of Series C Preferred, 25,000 shares of common stock, warrants to purchase 58,571 shares of common, and options to purchase 85,000 shares of common, of which options to purchase 84,792 shares were vested or would vest within 60 days, altogether representing beneficial ownership of 3% of the Company's common stock.

(Opinion at 5).

Then, in finding that voting to approve the Transaction was immaterial as to Kabatznik, the Court analyzed his holdings as follows:

> Kabatznik held 28,571 shares of Series C Preferred, which had a liquidation preference of $149,997.75 and represented only 0.8% of the outstanding Series C Preferred. He also owned 25,000 shares of common stock, options to purchase 85,000 shares of common stock, and warrants to purchase 58,571 shares of common stock. Plaintiff has not pleaded any facts regarding Kabatznik's financial circumstances. Plaintiff has, therefore, not alleged facts that provide a basis to conclude that Kabatznik's Series C Preferred interest "was of a sufficiently material importance, in the context of [his] economic circumstances, as to have made it improbable that [Kabatznik] could perform [his] fiduciary duties without being influenced by [his] overriding personal interest." *Gen. Motors (Hughes)*, 2005 WL 1089021, at *8 (internal quotation marks omitted). As a result, it is not reasonable to infer that Kabatznik was interested in the Ligand Transaction.

(Opinion at 13-14, internal citations omitted).

Importantly, in analyzing Kabatznik's holdings, the Chancery Court has inexplicably dropped from its analysis the material fact that Kabatznik, in voting to approve the Transaction, had created an opportunity for him to generate an added benefit to himself representing 1.5 times his investment (plus 12% interest), in addition to the opportunity to achieve a 3% beneficial ownership in the company through the generous grant of warrants. (Compare A039-40 ¶58 with Opinion at 5, 13-14).

Having determined, as the Court has, that "even in the absence of director-specific allegations, that payments of a certain level may be presumptively material. *See In re MultiPlan Corp. S'holders Litig.*, 268 A.3d at 813. And, given that the Court must draw all reasonable inferences in favor of Plaintiff, *Savor, Inc. v. FMR Corp.*, 812 A.2d 894, 896–97 (Del. 2002) (footnotes and internal quotation marks omitted), then it was error for the Chancery Court to determine as a matter of law that a director voting to award himself a $149,997.75 liquidation preference, plus sufficient warrants and options so that he may achieve a 3% beneficial ownership interest in the Company, and, through the liquidation preference earn 1.5 times his investment, is immaterial as a matter of law. This is particularly true, when, as here, as Plaintiff alleged and the Chancery Court ignored, Icagen itself warned that any director holding the Series C Preferred stock was susceptible to conflict.

Plaintiff alleged: "Our obligations to the holders of Series C Preferred Stock could limit our ability to obtain additional financing or increase our borrowing costs, which could have an adverse effect on our financial condition. These preferential rights could also result in divergent interests between the holders of shares of the Series C Preferred Stock and holders of our common stock." (A040 ¶ 59).

As the *MultiPlan* court noted, taking into account a plaintiff-friendly pleading standard, while "[t]he defendants may 'ultimately be correct . . . that it was not material' to the directors but, at this point, the court can reasonably infer that a majority of the directors were self-interested.[8] *See In re MultiPlan Corp. S'holders Litig.*, 268 A.3d at 814. Here, as in *MultiPlan*, the interested director defendants facilitated, among other things, the awarding of shares, options and warrants to themselves through their approval of the Transaction representing significant value to them personally and not made available to the common stockholders. *Id.* at 810-811. Accordingly, the Vice Chancellor could have and should have inferred that the interest was of a sufficiently material importance, in the context of the

[8] *Citing Frank v. Elgamal*, 2012 WL 1096090, at *11 (Del. Ch. Mar. 30, 2012); Voigt, 2020 WL 614999, at *15 (noting that although "[s]pecific information about the wealth of particular individuals is generally available," "the magnitude" of the compensation the director received was "sufficiently large to support an inference of materiality at the pleading stage").

director's economic circumstances, as to have made it improbable that the director could perform his fiduciary duties without being influenced by her overriding personal interest." *In re Gen. Motors (Hughes) S'holder Litig.*, 2005 WL 1089021, at *8 (Del. Ch. May 4, 2005). For example, in *Orman v. Cullman,* 794 A.2d 5 (Del. Ch. Feb. 26, 2002)*,* the Court concluded that "[e]ven though there is no bright-line dollar amount at which consulting fees received by a director become material, at the motion to dismiss stage and on the facts before me, I think it is reasonable to infer that $75,000 would be material…" *Id.* at 45-46.

Here, the Chancery Court recognized that the liquidation preference to Katbatznik was approximately double the amount the *Orman* Court found to be material (compare $149,997.75, Opinion at 13-14), with $75,000). That alone should satisfy the materiality standard. Then, when the Chancery Court would have added, as it should have under the plaintiff-friendly review standard the Court was obligated to abide, the facts that the liquidation preference resulted in a 1.5 times return on Kabatznik's investment, interest was payable at 12% and that he had voted to approve the issuance of warrants that would allow him to achieve a 3% interest in the Company, the benefits voted for by Kabatznik satisfy the materiality standard. The allegations regarding Tyson and Taglich, as previously described, also satisfy the materiality standard.

In this regard, Plaintiff's reliance on *In re Trados Inc. S'holder Litig.*, 2009 WL 608552 (Del. Ch. 2009) is well placed. The Chancery Court noted that in *Trados*, "this court found it reasonable to infer that the interests of the preferred and common stockholders diverged with respect to a corporate decision and the directors improperly favored the interests of the preferred." (Opinion, at 14, n.32). The Chancery Court however distinguished *Trados* noting that "[b]ut there, the allegations in the complaint gave rise to a reasonable inference that a majority of the board was either interested in or lacked independence with respect to the challenged decision." *Id.* A key fact informing the *Trados* decision was that the challenged transaction there triggered a $57.9 million liquidation preference of the preferred stockholders. Here, as already demonstrated, although the $19.4 million liquidation preference was apparently not triggered, the fact that the directors voted to approve a transaction that they reasonably believed would trigger the liquidation preference inasmuch as the conditions necessary for the triggering were required as part of the transaction satisfies the materiality test. That materiality test is also independently satisfied, as argued previously, by the awarding of the warrants, options, outsized interest and payment on the personal loans.

Although the Court never reached the issue, Plaintiff's allegations regarding interestedness also apply to the three directors who comprised the Board at the time the Complaint was filed – Tyson, Taglich and Cunningham. (A060 ¶94).

With regard to the allegations against Cunningham, the Chancery Court noted:

> Defendant Richard Cunningham, the Company's CEO, owned 21,428 shares of common stock and options to purchase 959,616 shares of common stock. After the Ligand Transaction was approved, the board authorized renewal of Cunningham's employment agreement, which had expired in November 2019. Several weeks after the Ligand Transaction closed, the Company approved a $300,000 bonus for Cunningham, and the Creditors agreed to transfer 500,000 shares of Series C Preferred to Cunningham for his work on the Ligand Transaction.

(Opinion at 6, internal citations omitted).

The Chancery Court's description, however, omitted key allegations that Plaintiff had asserted. Those allegations, in summary, were:

> Although discovery is needed to ascertain when exactly Cunningham [redacted] (A 525).[9]

[9] Curiously, the Chancery Court found that Plaintiff had waived any argument regarding Cunningham by failing to brief any argument as to Cunningham's personal liability or respond at oral argument. (Opinion at 16). Plaintiff addressed Cunningham's personal liability both in its briefing (*See*, *e.g.*, A525) and at oral argument (*See*, *e.g.*, A573).

As alleged, each of Tyson, Taglich and Cunningham, or, in any event, certainly a majority of the three of them were conflicted from considering a demand at the time the Complaint was filed as a result of their personal pecuniary gains from the Transaction which either had been already realized – warrants, options, stock, repayment of loans at high interest rates, or, the possibility of achieving the liquidation preference.

i. The Chancery Court Erred In Not Applying The Entire Fairness Doctrine

"The standard of review can also change from business judgment to entire fairness when a complaint 'allege[s] facts supporting a reasonable inference that there were not enough sufficiently informed, disinterested individuals who acted in good faith when taking the challenged actions to comprise a board majority." *MultiPlan*, 268 A.3d at 812. As the MultiPlan Court further noted, "Directors are self-interested in a transaction when they 'expect to 'derive any [material] personal financial benefit from it in the sense of selfdealing.'" If the majority of the Board "labors under actual conflicts of interest," entire fairness applies." Id. at 813 (internal citations omitted).

Here, the Chancery Court held that "[t]he Complaint does not give rise to a reasonable inference that at least three members of the five-person board that approved the Ligand Transaction lacked independence or were interested in the transaction. Therefore, Plaintiff has not rebutted the presumption that the business judgment rule applies to the directors' approval of the Ligand Transaction." (Opinion at 14, internal citations omitted).

However, as demonstrated above, Plaintiff has sufficiently alleged that three members of the five-person board that approved the Ligand Transaction were interested in the Transaction, thus triggering the entire fairness standard.

CONCLUSION

The Court should reverse the Court of Chancery decision and sustain Plaintiff's Complaint.

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