SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: **HON. JOEL M. COHEN** **PART** IAS MOTION 3EFM

Justice

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EMPERY ASSET MASTER, LTD, EMPERY TAX EFFICIENT, LP, EMPERY TAX EFFICIENT II, LP,

Plaintiffs,

- v -

AIT THERAPEUTICS, INC.,

Defendant.

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INDEX NO. 651306/2018

DECISION AFTER NON-JURY TRIAL

This is a breach of contract case. It concerns two "anti-dilution" provisions contained in a 2016 Warrant Agreement between Defendant AIT Therapeutics, Inc. ("AIT"), a developer of pharmaceutical products, and a group of its early outside investors, including Plaintiffs (collectively, "Empery" or Empery Funds"). The first provision gave Empery and other warrant holders the benefit of a lower Warrant Exercise Price if AIT sold or issued common stock to subsequent investors for a price lower than the original Exercise Price ("Price Adjustment"). The second provision required that for "each such adjustment" in "the immediately preceding sentence" of the agreement, AIT must issue additional warrant shares to account for the fact that subsequent shareholders received more shares per dollar of investment ("Share Adjustment").

The dispute centers on a 2018 transaction in which AIT issued additional warrants and common stock to second-round investors for a share price lower than the 2016 Warrant Exercise Price. Empery contends that when it exercised its warrants in March 2020, it was entitled to a Price Adjustment *and* a Share Adjustment to bring them to parity with the second-round investors. AIT agrees that the Price Adjustment was triggered (though it differs as to the amount of the adjustment) but disagrees that Empery is entitled to a Share Adjustment.

AIT contends that a sentence inserted between the Price Adjustment and Share Adjustment sentences by AIT's counsel late in the negotiations – which thus became the "immediately preceding sentence" to the latter – effectively limited Share Adjustment to the exceedingly unlikely situation in which AIT issued more than a specified percentage of its shares for zero consideration (*e.g.*, as employee compensation), which it did not do. Empery contends that the new sentence was explicitly designed to address a narrow logistical problem in *applying* the Share Adjustment, and was never intended to substantively limit (indeed, effectively eliminate) that protection. It claims that AIT's reading of the Share Adjustment protection reflects a drafting error that can and should be remedied simply by reforming the phrase "immediately preceding sentence" to "immediately preceding *sentences*," to reflect the intent of the parties.

The Appellate Division has twice held that Empery's allegations, if proven, would give rise to viable claims for reformation and breach of contract (*Empery Asset Master, Ltd v AIT Therapeutics, Inc.*, 179 AD3d 443, 444 [1st Dept 2020] ("*Empery I*") [affirming denial of AIT's motion to dismiss]; (*Empery Asset Master, Ltd. v AIT Therapeutics, Inc.*, 2021 NY Slip Op 05163 [1st Dept Sept. 30, 2021] ("*Empery II*") [affirming denial of AIT's motion for summary judgment]).

After a three-day non-jury trial, the Court finds that Empery has proven its claims. The contemporaneous documentary evidence and credible witness testimony clearly and convincingly prove that the Warrant Agreement contained a drafting error that inadvertently gutted the Share Adjustment provision to which the parties agreed. Although Empery was not involved in the correspondence that led to the drafting error in the first place, its subsequent correspondence with AIT's placement agent repeated and reinforced the error. In sum, the

evidence showed that Empery *and* AIT shared the same understanding and intention that the Share Adjustment provision applied in tandem with Price Adjustment whenever AIT sold or issued shares at lower than the Warrant Exercise Price. The evidence offered by AIT to the contrary was unpersuasive. Although AIT certainly did not *want* to grant Share Adjustment protection, it nevertheless agreed to do so. Finally, Empery's calculation of the Price Adjustment and Share Adjustment it should have received in connection with its March 2020 exercise of its Warrants, and its resulting damages arising from AIT's breach of contract, are supported by the preponderance of the evidence.

Accordingly, for the reasons described in greater detail below, the Court finds that: (i) the Warrant Agreement must be reformed to reflect the intent and agreement of the parties; (ii) AIT breached the Agreement by failing to properly calculate the Price Adjustment and Share Adjustment when Empery exercised its Warrants in March 2020; and (iii) the three Empery funds collectively are entitled to damages collectively in the amount of $5,814,176.64 plus prejudgment interest running from March 4, 2020.

PROCEDURAL HISTORY

Plaintiffs filed their Summons and Complaint (NYSCEF 1) on March 16, 2018. It asserted claims for Breach of Contract (First Claim for Relief) for failing to provide a Certificate of Adjustment that is correct as to exercise price and share amount; Declaratory Judgment (Second Claim for Relief) seeking a determination as to the proper exercise price and share amount; and Reformation/Mutual Mistake (Third Claim for Relief) seeking to change the phrase "immediately preceding sentence" in Section 3(b) of the Warrant Agreement to read "immediately preceding sentences," to reflect the intent of the parties.

On October 12, 2018, the Court (Bransten, J) denied Defendant's motion to dismiss the Complaint (*see* NYSCEF 20). The First Department affirmed that decision in *Empery I*, finding that: (i) "[t]he complaint states a cause of action for breach of section 3 (d) of the warrants by alleging that defendant's issuance of Tranche A and Tranche B warrants [in the 2018 Capital Raise] in accordance with the [Warrant Agreement] triggered defendant's obligation to provide plaintiffs with an adjustment to the exercise price;" and (ii) "[t]he complaint also states a cause of action for reformation of section 3 (b) of the warrants. The complaint alleges that the relevant clause, which provides for the increase of the number of shares subject to plaintiffs' option after a dilutive transaction, misstates the parties' agreement by limiting the increase of the number of shares to an issuance of stock described in the 'immediately preceding sentence'—which deals with the issuance of stock for no consideration—rather than the 'immediately preceding sentences,' which would include the issuance of stock for a price lower than the exercise price. In this regard, plaintiffs' complaint sufficiently alleges that the parties intended for the warrants to permit the increase of plaintiffs' shares under both circumstances. Accordingly, the cause of action for reformation was properly sustained" (179 AD3d at 443-44).

On August 20, 2020, the Court denied Defendant's motion for summary judgment, other than with respect to the Second Claim for Relief (Declaratory Judgment), which was dismissed as moot (NYSCEF 245). The First Department affirmed that decision in *Empery II*. The court rejected AIT's argument that Section 3(b) of the Warrant Agreement "is unambiguous and must be applied as written," noting that "the immediately preceding sentence (the second sentence) says nothing about adjusting the Exercise Price; instead, it is the first sentence of section 3(b) that addresses adjusting the Exercise Price." The Court further rejected AIT's contention that Empery's "reformation claim should be dismissed because there is no evidence that [AIT] – as

opposed to nonparty Deerfield Special Situations Fund, LP, the lead investor for the relevant capital raise by [AIT] – reach an agreement with [AIT] that was not reflected in the warrant and because [Empery was] negligent." The Court found that there were issues of fact as to whether there was mutual mistake and/or scrivener's error: "We cannot conclude, as a matter of law, that a reasonable person reviewing a 20-page warrant and a 42-plus-page Securities Purchase and Registration Rights Agreement would have realized that the work 'sentence'(in 'immediately preceding sentence') should have been 'sentences'" (2021 NY Slip Op 05163, *1). Finally, the Court rejected AIT's contention that "its 2018 capital raise did not trigger section 3(d) of plaintiffs' warrants because it did not issue options in connection with the issuance or sale of other securities but merely issued warrants," noting that AIT's testimony on that front was disputed not only by Empery witnesses but also by witnesses from "Deerfield, which has no stake in the dispute between [Empery] and AIT" (*id*.).

The case came before the Court for a three-day bench trial via Microsoft Teams on April 19-21, 2021. Direct testimony was presently principally by affidavit, followed by cross-examination and re-direct.

FINDINGS OF FACT

The Court makes the following findings of fact based on its review of the evidence admitted at trial, including its evaluation of the credibility of the witnesses who testified during the proceedings:

The Parties

1. Plaintiffs Empery Asset Master, Ltd, Empery Tax Efficient, LP, and Empery Tax Efficient II, LP (collectively, "Empery") are investment funds based in New York managed by Ryan Lane ("Lane") and Martin Hoe through Empery Asset Management, L.P (Statement of

Joint Stipulated Facts and Procedural History ("Stip. Facts"), NYSCEF 324, ¶ 1). The Empery Funds routinely invest in emergent companies, largely in the med tech and biotech sector (Transcript of trial proceedings (NYSCEF Doc. Nos. 341-44) ("Tr.") at 13:13-15).

2. Defendant AIT Therapeutics, Inc. ("AIT" or "Defendant") is a public company that for the past several years has been developing equipment that seeks to use inhaled nitric oxide to treat respiratory infections and gaseous nitric oxide to treat solid tumors. It is now known as Beyond Air Inc. and trades under the symbol "XAIR." Amir Avniel served as CEO of AIT Ltd., an Israeli company that merged into Plaintiff in January 2017. He served as CEO of AIT until June 2017 when he was succeeded by Steven Lisi. Mr. Lisi served as a director and outside consultant to AIT Ltd. starting in June 2016 (DX-71, ¶¶ 1, 5, 7; DX-72, ¶¶ 4, 6; Tr. at 457:19-458:18).

3. On December 29, 2016, the Empery Funds, along with other investors, entered into a Securities Purchase Agreement ("SPA") with AIT and received warrants (the "Warrants") and shares of AIT.

Negotiation of the Anti-Dilution Provisions in the Warrants

4. In or about October 2016, AIT retained Ladenburg Thalman & Co. ("Ladenburg") to serve as its placement agent to raise capital and become a public company traded on the U.S. markets. AIT had identified Deerfield Special Situations Fund, L.P. ("Deerfield") as the lead investor in the capital raise. Deerfield and AIT negotiated the terms of an SPA and Warrant Agreement through an exchange of drafts in October and early November 2016. After AIT and Deerfield reached agreement on terms, the documents were then marketed to other potential investors, including Empery.

5. Negotiation concerning the documentation for the investment began October 11, 2016, when Amy Cooper, a Senior Vice President of Ladenburg, provided Deerfield with a

timeline for a closing on the placement of securities and for AIT's reverse merger with a public company in the United States. Her email transmitted a proposed SPA and form of Warrant (PX-6; Dkt No. 324, ¶ 11). Ms. Cooper thereafter acted as AIT's principal intermediary in negotiating with Deerfield over the draft documents (Tr. at 313:3-16).

6. On October 19, 2021, a senior executive at Deerfield offered to provide a draft warrant using Deerfield's preferred form (PX-7). Ms. Cooper responded with a form of warrant prepared by AIT's counsel, Greenberg Traurig LLP (*id*.; NYSCEF 324, ¶ 7). The form of warrant provided for adjustments to the exercise price in the event of changes to AIT's capitalization, such as stock splits and stock dividends (*id*. at §3(a)). It did not provide for adjustment to the exercise price or number of warrant shares in the event AIT were to issue shares for a price below the exercise price of the warrant.

7. The following day, Deerfield provided comments to Ladenburg on the form of warrant, which Ms. Cooper shared with AIT and its counsel (PX-8). The first comment was to "add full ratchet anti-dilution until two data readouts (the current bronchiolitis and NTM trial)" (PX-8 at 2852). Ms. Cooper understood that "full ratchet anti-dilution" referred to adjustments both in exercise price and the number of warrant shares. She testified that the term has "pretty consistently been used in one way . . . a full ratchet means price and share adjustment" (Tr. at 243:2-23, 290:23-291:7).

8. Although other witnesses at trial testified that there is no universally recognized definition of "full ratchet anti-dilution," the Court finds (as noted below) that its meaning was clear in the context of this particular transaction because the term was associated with specific terms upon which Deerfield insisted.

9. In particular, Deerfield's comment requesting "full ratchet anti-dilution" referred to adjustments to the exercise price of the warrant in the event AIT issued securities for a price below the existing exercise price, with a corresponding adjustment to the number of shares covered by the warrant. The adjusted number of warrant shares is determined by dividing the product of the original exercise price and original number of warrant shares by the new exercise price. Adjustments to price and the number of warrant shares are often sought by early-stage investors to provide protection from economic dilution to the value of their warrants in the event of a later "down round," a term referring to a placement below the exercise price in the warrants (Tr. at 242:23-243:23, 290:23-291:7, 317:3-318:22). For obvious reasons, issuers generally are resistant to such clauses which may complicate later financings (*see* Tr. at 571:14-572:12).

10. On October 21, 2016, Ms. Cooper, on behalf of AIT, transmitted a revised warrant to Deerfield and its attorneys that added a new Section 3(b), titled "Adjustment of Exercise Price upon Issuance of Ordinary Shares." The first sentence of the new Section 3(b) provided for adjustment to the exercise price as follows:

> Adjustment of Exercise Price Upon Issuance of Additional Ordinary Shares. Subject to the last sentence of this Section 3(b), if, following the Effective Date, the Company issues (or is deemed to have issued) Additional Ordinary Shares without consideration or for a consideration per share less than the Exercise Price in effect immediately prior to such issuance, then the Exercise Price shall be reduced, concurrently with such issuance, to a price (but not below the par value per Ordinary Share) equal to the per share price at which such Additional Ordinary Shares were issued (or deemed to have been issued).

(PX-9 at 222).

11. The first sentence of Section 3(b) recited above remained in the Warrant in substantially the same form through the closing (*see id.*; PX-1-3). It provided for adjustments to

the exercise price on any later issuance of securities below the existing exercise price, with exclusions for specified exempt offerings.

12. Counsel for Deerfield responded with a new draft on October 25, 2016, with the following language in Section 3(b):

> Adjustment of Exercise Price **and Number of Shares** upon Issuance of Ordinary Shares. If and whenever on or after the Effective Date, the Company issues or sells, or is deemed to have issued or sold, any Ordinary Shares (including the issuance or sale of Ordinary Shares owned or held by or for the account of the Company, but excluding Exempted Issuances (as defined below)), for a consideration per share (the "New Issuance Price") less than a price equal to the Exercise Price in effect immediately prior to such issuance or sale (the "Applicable Price"), then immediately after such issuance or sale the Exercise Price then in effect shall be reduced to the New Issuance Price. **Upon each such adjustment of the Exercise Price pursuant to the immediately preceding sentence, the number of Warrant Shares issuable upon exercise of this Warrant shall be increased to the number of shares determined by multiplying the Exercise Price in effect immediately prior to such adjustment by the number of Warrant Shares issuable upon exercise of this Warrant immediately prior to such adjustment and dividing the product thereof by the Exercise Price resulting from such adjustment.**

(PX-11-12 [emphasis added]). The first sentence tracked AIT's earlier draft in substance regarding price adjustment. Deerfield added the second sentence to require adjustments to the number of warrant shares in the Warrant. These two sentences together comprise "full ratchet anti-dilution," as Deerfield (and later AIT) used that term. Moreover, the triggers for the two protections were expressly linked, with the Share Adjustment occurring "[u]pon each such adjustment of the Exercise Price pursuant to the immediately preceding sentence."

13. On October 29, 2016, AIT (via Ms. Cooper) responded with a draft that struck Deerfield's proposed second sentence in Section 3(b), thereby eliminating any adjustment to the number of warrant shares upon a change in the exercise price (PX-13 at 531).

14. Elliot Press, a Deerfield partner and in-house counsel working on the AIT transaction testified that when AIT continued to push back on this issue, Deerfield asked its outside counsel to make clear to AIT that Deerfield felt strongly that Share Adjustment protection be included in the warrants (*id.* at 325). He also confirmed that when using the term "full ratchet anti-dilution" in the context of the AIT transaction, Deerfield meant the combination of a Price Adjustment and a Share Adjustment, and that Deerfield's pursuit of that dual protection was "material" (Tr. at 317-18).

15. On October 30, Mark Wood, Deerfield's counsel, called Amy Cooper to advise that Deerfield wanted (as Ms. Cooper summarized) "the full ratchet around anti-dilution clause *put back into the warrant*," and that Deerfield felt "very strongly on this point, that this was the expectation" (PX-14; Tr. at 325:5-20 [emphasis added]).[1] Ms. Cooper reported on Mr. Wood's call by email to Mr. Avniel and AIT's counsel that evening (PX-14). She noted that the language in Section 3(b) was one of the "two open issues," that "beyond these two items we are mostly there," and that "I believe we are ok on the full ratchet" (PX-15 at 3875).

16. On October 31, 2018, in response to Ms. Cooper's email, and after various other comments had been made by Mr. Lisi and others about different issues raised by Deerfield, Mr. Avniel gave the following direction to AIT's counsel: "Can u pls incorporate [Mr. Lisi's] comments into the documents and ***leave the full ratchet***, we need to send it to deerfield" (PX-15 at 3874 [emphasis added]).

17. That same day, Deerfield's counsel sent a revised Warrant, using the same "full ratchet" language as in his October 25 draft, namely, restoring the second sentence in Section

[1] The Court does not rely on this email for the truth of the matter asserted by Mr. Wood (which in any event was confirmed by Mr. Press's testimony at trial), only for the fact that this position was conveyed to AIT.

3(b), so that the Warrant provided for adjustments to exercise price *and* the number of warrant shares, with the same language linking the triggering events for the two protections (*e.g.*, "immediately preceding sentence") (PX-17).

18. The following morning, AIT's counsel sent an internal email to Mr. Avniel, Ms. Cooper and others with comments on the latest Deerfield draft, stating, "Regarding Deerfield comments, I understand from Amir [Avniel] that **we should accept them all…unless there is something egregious**" (PX-19 [emphasis added]).

19. In his email, AIT's counsel flagged a logistical issue with respect to the Share Adjustment provision if AIT decided to issue a substantial number of shares to employees for zero consideration: "For the full ratchet – note that your incentive compensation pool will be limited to 5% of the outstanding each year, otherwise it will trigger the ratchet (at zero price – so, basically $0.01). Note that this would result in the warrant being exercisable for an extraordinary number of shares. We need to include in the warrant a provision that in no event will the consideration received for a share be deemed to be less than $0.01 per share (otherwise, if the company accidentally went over the option pool allotment, it would result in an infinite number of shares being issuable under the warrants – or perhaps an 'irrational' number – it would be a real number divided by zero)."

20. Again, counsel's use of "full ratchet" makes clear that AIT understood that phrase to mean an adjustment to the exercise price *and* the number of warrant shares.

21. On November 2, AIT's counsel circulated internally to Mr. Avniel, Ms. Cooper and others a draft that "basically accepted all changes [from Deerfield]" (PX-22). The "*only things*" changed in the draft, counsel noted, were five specific points, with item 2 being: *"Clarifying* that if shares are issued for no consideration, then deemed to be issued at $0.01/share

(avoids irrational number issue)" (PX-22 [emphasis added]). No mention is made of any intention to reject Deerfield's substantive revision to add "full ratchet" price and share protection, which is consistent with Mr. Avniel's earlier direction. The email concluded by saying that "[Deerfield's counsel] has either agreed or otherwise shouldn't have issues with the above."

22. To implement counsel's change, the draft added a new sentence in Section 3(b): "If any sale or issuance, or deemed issuance, is for no consideration, then the New Issuance Price shall be deemed to be $0.01 per Ordinary Share" (PX-22 at AIT-0004043). Fatefully, however, the new sentence was placed *between* the first and second sentences in Section 3(b), rather than as a proviso to the first sentence or somewhere else in the paragraph, and without changing the reference to "immediately preceding *sentence*" to "immediately preceding *sentences*."

23. On November 4, 2016, Amy Cooper sent the revised Warrant Agreement to Deerfield, accepting Deerfield's revisions and advising that "the changes that appear are limited to the following, which I believe have all been discussed" (PX-23). Her list included the same item 2 from AIT's counsel's November 2 internal email: "Clarifying that if shares are issued for no consideration, then deemed to be issued at $0.01/share (avoids irrational number issue)." She concluded with: "Please let us know if you are signed off on these as acceptable, and if so we will prepare execution copies."

24. Ms. Cooper's email included a redline which showed the insertion of the new sentence in Section 3(b) addressing the "zero consideration" scenario as follows:

> "(b) Adjustment of Exercise Price Upon Certain Issuances of Ordinary Shares. If and whenever after the Effective Date, the Company issues or sells, or is deemed to have issued or sold, any Ordinary Shares (excluding Exempted Issuances (as defined below)), for a consideration per share (the "New Issuance Price") less than a price equal to the Exercise Price in effect immediately

> prior to such issuance or sale (the "Applicable Price"), then immediately after such issuance or sale the Exercise Price then in effect shall be reduced to the New Issuance Price. **If any sale or issuance, or deemed issuance, is for no consideration, then the New Issuance Price shall be deemed to be $0.01 per Ordinary Share**. Upon each such adjustment of the Exercise Price pursuant to the immediately preceding sentence, the number of Warrant Shares issuable upon exercise of this Warrant shall be increased to the number of Ordinary Shares determined by multiplying the Exercise Price in effect immediately prior to such adjustment by the number of Warrant Shares issuable upon exercise of this Warrant immediately prior to such adjustment and dividing the product thereof by the Exercise Price resulting from such adjustment."

(PX-23 at 979-980.).

25. Through outside counsel, Deerfield responded, "we are good to go on the docs" (PX-24). The first three sentences of Section 3(b) would remain substantively unchanged through the closing.

26. In retrospect, the internal inconsistency created by inserting the "clarifying" zero-consideration sentence between what had been the contiguous Price Adjustment and Share Adjustment sentences, without changing "immediately preceding *sentence*" to "immediately preceding *sentences*," is clear. The Share Adjustment sentence refers to "each such adjustment," which indicates that multiple adjustments might occur to the Exercise Price and the share number. That was certainly true when the "immediately preceding sentence" was the basic Price Adjustment sentence, which envisions an adjustment each time AIT offered shares at a price lower than the Exercise Price. But it makes no sense if limited to the zero-consideration sentence. An "adjustment" pursuant to that sentence would be to the lowest possible number ($0.01), and thus could only happen once. Moreover, all sides agree that AIT could never, as a practical matter, trigger such an adjustment. An adjustment of the Exercise Price to $0.01 not only would permit warrant holders to acquire AIT shares immediately for almost nothing, it

would also require AIT to issue *billions* of shares to the warrant holders (the $0.01 being the denominator to calculate the Share Adjustment), which would be catastrophic to AIT (Tr. at 527:17-528:17; *see also id.* at 471:23-472:21). Accordingly, if the Share Adjustment provision were truly intended to be limited to a zero-consideration issuance, it would be a dead letter.

27. The drafting history described above demonstrates that was not the intention of the parties. That is confirmed by the testimony. Mr. Press (Deerfield) testified credibly at trial that he did not view AIT's insertion of the "zero consideration" sentence as limiting the scope of the Share Adjustment protection for which Deerfield successfully negotiated (Tr. at 327-28, 339).[2] He understood the reason for the addition of that sentence – to avoid a requirement to issue an infinite amount of shares – but it did not believe the sentence limited the scope of the Share Adjustment protection for which Deerfield fought so vigorously (*id.* at 331, 337-38, 389). In the end, he simply did not catch the drafting error at the time. The first time he heard AIT take the position that the Share Adjustment protection was, in effect, a dead letter was in the context of the 2018 Capital Raise, discussed below.

28. Based on the documentary evidence described above, as well as the testimony presented at trial, the Court finds that AIT accepted – albeit reluctantly – Deerfield's demand for the "full ratchet" protection comprised of Price Adjustment *and* Share Adjustment triggered by sale of AIT common stock at *any* price below the Exercise Price. The record shows that the

[2] Unlike AIT and Empery, Deerfield has no dog in this fight. After AIT and Deerfield agreed on the SPA and Warrant, they continued to refine the business terms of the offerings. Later in November, Deerfield and AIT agreed that the pre-investment value of the business would be set at $30 million; that the warrants would be exercisable at a 15% premium to the common stock price of $6.00 per share; and that the closing would require a minimum of $10 million, with AIT to raise an additional $5 million from retail investors. (DX-17 at 2463.) They further agreed that if AIT did not raise the additional $5 million within 60 days, the number of warrant shares would double. This last concept was memorialized in a new Section 3(h) in the Warrant.

zero-consideration sentence in Section 3(b) was added solely as a "clarification" to address the "infinity problem," namely how a share adjustment would work if the exercise price did not adjust to a finite number. Neither party intended that the second sentence would limit the share adjustment language solely to an issuance for no consideration

29. Moreover, given that the same form of Warrant Agreement would be used with all warrant holders, the Court finds that AIT (led by Mr. Avniel) understood that the Share Adjustment protection negotiated by Deerfield would apply to all warrant holders, including Empery. Subsequent communications with Empery confirm that fact.[3]

AIT's Evidence with Respect to Intent of the Parties

30. The evidence offered by AIT to the contrary was not persuasive.

31. In response to the substantial contemporaneous documentary evidence that AIT acceded to Deerfield's demand for "full ratchet" price *and share* protection, AIT relies principally on the testimony of Mr. Avniel, Mr. Lisi, and John Shroer (an executive with Allianz, a warrant holder in the 2016 transaction and lead investor in the 2018 transaction).

32. The thrust of Mr. Avniel's testimony was that his principal role was to "answer science-related questions" (NYSCEF 329 ¶8); that he was not familiar with the details of the warrant arrangement (in particular, the Share Adjustment provision); and that he deferred to Mr. Lisi who advised him that AIT was only providing "price" protection to warrant holders and that the focus was on limitations of issuance of stock to employees (*e.g.*, Tr. at 467-71).

33. The Court does not doubt that Mr. Lisi had more commercial and financial experience than Mr. Avniel, but Mr. Avniel's clear direction to his team to "leave the full

[3] The findings herein apply only to the Empery Funds as warrant holders. As discussed *infra* at ¶ 39, at least one other AIT warrant holder apparently believed that the Share Protection provision *was* limited to the narrow circumstances of a zero-consideration issuance of shares.

ratchet" is not a buck that can be so easily passed. Although AIT seeks to make much of the fact that English is not Mr. Avniel's first language, the Court found him to be a sharp and savvy person who had no difficulty understanding the issues or proceedings in this case. The record shows that he was substantively involved in the relevant correspondence, and that counsel and Ms. Cooper directed their substantive correspondence to him, at times to the exclusion of Mr. Lisi who was a "consultant" during the relevant period. Moreover, there is no evidence that anyone involved in the email chain approving the "full ratchet" (PX-15), including Mr. Lisi, objected to the direction given by Mr. Avniel. Indeed, AIT's counsel made clear that in sending the revised draft to Deerfield he understood his instructions *from Mr. Avniel* were to accept all of Deerfield's changes unless they were "egregious." In sum, AIT's attempt to minimize Mr. Avniel's role (or business acumen) is unavailing.

34. AIT relies principally on the testimony of Mr. Lisi. The thrust of his testimony was that it would be reckless and nonsensical for AIT to accept the "share explosion" provision Deerfield (his former employer) was seeking, and AIT (under his guidance) would never have agreed to such a thing, and that the contract – including the shifting reference to the "immediately preceding sentence" – meant exactly what it said. The problem with his testimony is that the contemporaneous evidence discussed above makes clear that AIT *did* agree to the Share Adjustment, with or without his assent.

35. The Court asked Mr. Lisi to explain how his version of events – that Share Adjustment was intentionally limited to the highly unlikely issuance of a substantial number of shares for zero consideration – squared with the documentary record. The response was not persuasive and cannot be squared with his prior testimony that he had no conversations with Deerfield (or Empery) about the anti-dilution provisions.

36. Mr. Lisi suggested that he had a conversation with Jeffrey Kaplan (Deerfield) *before* the exchange of draft agreements "to come to terms verbally," and that "Warrant explosion … wasn't part of the original negotiation that we had verbally" (Tr. at 565). Even assuming that is true, it does not address what happened once drafts were being exchanged and the parties' focused their attention specifically on the anti-dilution provisions.

37. Mr. Lisi attempted to explain away the absence of a documentary record supporting his testimony with general references to purportedly "ongoing" discussions with Deerfield *about which he had never before testified during the long course of this litigation*. Given that he was AIT's main witness on this critical point, it is worth setting forth his exchange with the Court in some detail:

> THE COURT: [T]he thing that's hard about this is there is a lot of internal back and forth between AIT people, between the AIT people and the lawyers and Ladenburg, and this idea that [you've] been talking about which is we're rejecting the share increase except in this one narrow circumstance. You don't see that expressed anywhere except[,] from my perspective[,] today. You don't see it in -- you know, there's a lot of back and forth about this paragraph, and not one of the back and forth that I've seen seems consistent with your recollection of it, and I'm just trying to understand why there was so much communication about this one paragraph.
>
> And again, you know, physically all that happened was another sentence got dropped in. The two sentences stay exactly the same before it and after it and just this one sentence is dropped in. And as you read it, and I understand why. You say that it -- it [effected] an enormously significant change. Obviously, that's why we're all here. It's puzzling that there is no record of it as to why it was done. The only record I've seen is it was done to deal with the infinity problem.
>
> THE WITNESS: Judge, I mean, in reading this, it clearly relates [to] the incentive compensation pool with what they're terming "full ratchet."
>
> * * *

THE COURT: I understand what you're saying, and as you said before, it's a negotiation and issuers never want to have a share adjustment and some option holders want it, and it's just question of what you all agreed to.

And it's just curious that every other change to that paragraph, you see a paper trail as to why it happened except that one.

THE WITNESS: Well, like I said, there is a lot of changes to the documents over time and not every change has a big paper trail on it. A lot of things are discussed. Some things are easier discussed verbally, then put down in writing. Sometimes the conversation has to be had, you know, face to face. And back then we could face to face. So I think it has to be face to face, some of these conversations.

THE COURT: But didn't we just agree that you didn't have a face to face or any kind of conversation about this last change?

The last change -- the only thing that happens --again, this is an unusual situation because you don't usually see drafting history this clear.

But so you have sentence one and two. Two says "immediately preceding sentence" which is the first one. And the last thing that happens is an explanatory sentence is dropped in between the two.

THE WITNESS: Yes.

THE COURT: It changes everything.

THE WITNESS: That's right.

THE COURT: It's never described as changing everything. There's no real description of what it's for.

So are you saying that there was a contemporaneous conversation to Deerfield saying, Hey, look, we put this in here and here's why. Or is it your view that it was just so clear, we didn't have to do that?

THE WITNESS: No. No. No. They knew exactly what we were doing, and I can tell you, Judge, with all due respect, the Black-Scholes calculation that's in this document is horrific for the company. It's horrible.

There's no e-mail chain about why the Black-Scholes was put in there and why we accepted it. There's nothing in there about that. That is a horrible -- it's the worst possible Black-Scholes calculation you could ever come up with. Okay. It's the worst.

If you say what's the worst for the company and the best for an investor, that Black-Scholes calculation is the best you'd possibly ever get for the investor. . . . I accepted that because I knew the Black-Scholes calculation would only be used in a very narrow situation. That's it. I accepted it. I accepted it. It's all part of the negotiation. They knew exactly what they were doing. I worked at Deerfield for five years. They are extremely smart guys. They do dozens of deals every year, if not hundreds now they have such a big team. They knew exactly what they're doing. They knew it. They knew exactly what I did, knew exactly what we did as a team. They knew what we were intending. They got the chance to read it, and they agreed. And then they came back and asked for more Warrant coverage because they knew that that's how the contract read in the first place. That's why they came back and asked for more.

THE COURT: Just so I'm clear, and I'll let you get back to it. There was no specific conversation you had with -- you personally or anyone, you know, had with Deerfield about this new sentence.

Your point is it was obvious, we didn't have to discuss it. That's -- there was -- there is nothing I'm missing. There is no e-mail. There is no conversation that explained why this third sentence was put in. Your point is that, well, we didn't have to explain it because it just says it on its face.

Is that basically right?

THE WITNESS: Almost. We did have conversations that they weren't getting the explosions that they were asking for. Those explosions would be tied to the employee stock option grants. . . . You know Katten and Mark Wood at Katten read it and accepted it, and I assume people at Deerfield did the same thing. They knew exactly what we were doing, why we were doing it. We sent them a red line. They accepted it. We were done.

* * *

THE COURT: Right. So chronologically, when did you have this discussion with Mr. Kaplan [Deerfield]? Was it before

> the first draft, between the first and the second or was it much later?
>
> THE WITNESS: It was ongoing because originally, we were trying to get this to be limited to when we completed our two studies. Any kind of explosion would be limited to the timing of when the two studies were completed. That was the original -- how it was originally written and that got changed…

(Tr. at 571:2-576:5 [emphasis added]). There is, however, no evidence of any such "ongoing" conversation – there is no mention of it in Mr. Lisi's direct testimony affidavit (which presumably he reviewed with care) or in his deposition testimony or in his communications surrounding the 2018 Capital Raise when the Share Adjustment protection became a point of dispute.

38. The Court does not doubt that Mr. Lisi views the Share Adjustment as not being in the best interests of AIT. And perhaps if it had been a subject of Mr. Lisi's focus during the negotiations, he might have pushed back and urged Mr. Avniel not to concede it. But AIT's intent is not limited to what Mr. Lisi may or may not have thought about the issue if it had been squarely presented to him. As described above, the documentary record makes clear that AIT (Mr. Avniel, acting through AIT's counsel and placement agent) did accede to Deerfield's clear and consistent demands for Share Adjustment protection, and the drafting history makes clear that the late insertion of a "zero consideration" proviso was not intended to have a substantive impact on the Share Adjustment provision for which Deerfield (a key investor with substantial leverage) successfully bargained.

39. Finally, AIT relies on the testimony of John Shroer, an executive with Allianz, which was an investor in the 2016 Capital Raise and became a "substantial" AIT shareholder in the 2018 Capital Raise. Although he stated in his direct testimony affidavit that he "engaged in negotiations on behalf of Allianz with AIT" (DX-73, ¶ 2), Mr. Schroer testified on cross

examination that he did not recall participating in any negotiations concerning the terms of the Warrants; nor did he recall receiving any drafts (Tr. at 633:8-19). His testimony, essentially, is that he believed Section 3(b) meant what it said (that is, no Share Adjustment unless shares were issued for zero consideration), and that it would be contrary to normal practice for a fledgling pharmaceutical company (or well-intentioned first round investors) to shackle itself to a broad Share Adjustment obligation that would complicate further fund-raising. While the Court found Mr. Shroer to be knowledgeable and credible, the question is not what a company in AIT's position might normally want, nor what reasonable investors normally might be willing to accept, but instead what AIT actually agreed to and what Empery actually understood it was receiving. As to those issues, Mr. Shroer's testimony sheds no light.

40. In the end, the Court finds that AIT acceded to Deerfield's demands as lead investor, and therefore *agreed* (albeit reluctantly) that Share Adjustment would be triggered by "each such" Price Adjustment described in the "immediately preceding sentences" of Section 3(b).

Empery's Investment in AIT

41. After AIT and Deerfield reached an understanding on the transaction documents, including the anti-dilution provisions, Ladenberg prepared a Term Sheet to market the investment to other potential investors. The draft Term Sheet went through a series of iterations in November 2016 (DX-14-16). On November 28, 2016, Ms. Cooper and Edwin Gordon of Ladenburg, each provided a revised Term Sheet to Steven Lisi, Amir Avniel, and AIT's counsel, Adam Newman (PX-26-27). The attached document was two pages and included the following language under the heading "Anti-Dilution Protection":

> The Warrants will contain a provision such that if the Company issues or sells Ordinary Shares for a consideration (the "New Issuance Price") less than the Exercise Price, then the Exercise

> Price shall adjust to the New Issuance Price. **In addition, the number of Warrant Shares issuable upon exercise of the Warrants shall be increased to the number of Ordinary Shares determined by multiplying the Exercise Price in effect immediately prior to such adjustment by the number of Warrants Shares issuable upon exercise of the Warrants immediately prior to such adjustment and dividing the product thereof by the New Issuance Price**

(*id*. [emphasis added]).

42. Although AIT's witnesses have disclaimed the above description during this litigation, the Court finds that it accurately summarizes the understanding of both AIT and Deerfield as to "Anti-Dilution Protection" provided in the Warrant Agreement document described above, thus further confirming that there was a scrivener's error and that the accurate intention of the parties was being communicated to additional entities to whom investments were being solicited, including Empery (PX-29, PX-31).

43. On December 16, 2016, Amy Cooper at Ladenburg sent the Empery Funds proposed transaction documents and the Term Sheet that summarized the key terms of the documents (PX-29). The transaction documents included a form of Warrant with Section 3(b) containing the same language as when AIT and Deerfield completed the drafting in early November 2016.

44. The Term Sheet was dated November 28, 2016 and was the same as that approved by AIT earlier. As noted above, the Term Sheet confirmed that the Warrants in the offering would have anti-dilution protections involving adjustments to share price *and* the number of warrant shares (PX-29 at 083).

45. Later in December 2016, Brett Director, general counsel of the Empery Funds, reviewed the transaction documents and offered comments on certain provisions (PX-30; PX-32; PX-34-37). Ryan Lane and Brett Director both understood that the Empery Funds were

receiving anti-dilution protection in the Warrants consistent with the Term Sheet. Neither noticed that the cross-reference to the "immediately preceding sentence" in Section 3(b)'s third sentence to include only the "zero consideration" sentence conflicted with their understanding of the intended scope of Share Adjustment protection described in the Term Sheet (PX-69, ¶¶ 10, 12; PX-70, ¶¶ 4-10).

46. On or about December 29, 2016, Empery, Deerfield and the other investors in the deal executed the SPA and subscribed for shares and warrants (PX-5 at 4 and Ex. 10.2; PX-69, ¶ 4; Tr. at 11:9-20). Like Deerfield and (the Court finds) AIT, Empery understood that Section 3(b) of the Warrant provided for an adjustment in the number of warrant shares on any change in exercise price.

47. The transaction closed on January 13, 2017 (PX-5). The Empery Funds invested $500,004 receiving 83,334 shares of AIT common stock and warrants to purchase 83,334 shares at $6.90 per share, subject to adjustment. Deerfield invested approximately $2.5 million receiving common stock and a warrant to purchase 416,667 shares that was identical in form to the ones issued to the Empery Funds (PX-1-4; Tr. at 59:1-3).

48. Under Section 3(h), the number of warrant shares in the Warrants doubled sixty days later when AIT failed to raise an additional $5 million. The Empery Funds then held the following warrants: Empery Asset Master, Warrants exercisable for 72,804 warrant shares; Empery Tax Efficient, Warrants exercisable for 36,372 warrant shares; and Empery Tax Efficient II, Warrants exercisable for 57,492 warrant shares (NYSCEF 324, ¶ 22; PX-1-4; PX-69, ¶ 13).

The 2018 Capital Raise

49. In December 2017, AIT retained Maxim Group LLC ("Maxim") to act as its placement agent for the 2018 Capital Raise (DX-38). Brad Hoffman of Maxim served as the lead banker for Maxim.

50. In December 2017 and January 2018, Maxim contacted potential investors, including Empery, to gauge their interest. Empery went "OTW" or "over the wall," in December 2017 (DX-39; DX-41). "OTW" is a term of art meaning the investor has agreed to receive confidential, non-public information. The Empery Funds thereafter received periodic updates from Maxim.

51. By January 24, 2018, the deal terms had evolved so that AIT was offering common stock for $4.25 per share, with a warrant exercisable at $4.25 per share for no additional consideration (PX-47; DX-45; Tr. at 397:1-401:6).

52. On January 25, 2018, Maxim advised Empery that the offering was expected to be announced the following day at $4.25 per unit, with a unit comprised of one share of common stock and a warrant exercisable at $4.25 per share (DX-49).

53. On January 25, 2018, an interesting exchange took place between Maxim's counsel (Loeb & Loeb) and AIT's counsel (Latham & Watkins) concerning the impact that the new capital raise would have on the existing Warrants by virtue of the adjustment language in Section 3(b) (PX-48). Maxim's counsel forwarded a copy of the Warrant Agreement to AIT's counsel, who responded, in part: "We agree that this transaction invokes this provision and that, therefore, the price of the existing warrants would ratchet down to match the price of the warrants being issued in this transaction, and the number of shares into which the existing warrants are exercisable would be increased pursuant to the formula in this provision."

54. Forty-five minutes later, however, AIT's counsel took a different view: "On a re-read of the provision, I'd actually revise what I said below…. The language is actually pretty clear that the increase in the number of shares only applies in cases where the New Issuance Price is deemed to be $0.01 per Ordinary Share (i.e., the 'immediately preceding sentence')." The Court does not read anything sinister into counsel's change of position, which reflects a reasonable reading of the text, but it does demonstrate that the wording of Section 3(b) of the Warrant Agreement was confusing even to sophisticated readers.

55. Maxim's counsel asked whether there is "someone from the Company or the counsel who represented the Company in that transaction who can confirm this interpretation?" Perceptively previewing the central issue raised in this litigation, she continued:

> While I agree that the language does refer to the "immediately preceding sentence" rather than "immediately preceding sentences", the language also refers to "dividing the product by the Exercise Price resulting from such adjustment" rather than "dividing the product be $.01". It also refers to "each such adjustment of the Exercise Price" which is vague at best because in the case where the Company did multiple issuances for no consideration the Exercise Price would never go below $0.01 so there wouldn't any adjustments after the first one. I want to make sure that we get this right so that investors in this deal understand fully what will happen to these warrants once this deal is done. I also want to make sure that there is no problem with the warrant holders in the prior deal. My question is whether the Company is comfortable that the reference to "sentence" was not meant to be "sentences"

(*id.*).

56. The following day, Maxim's counsel circulated a revised SPA which included a representation by AIT that the new offering "will not result in any increase in the number of Common Stock or other securities issuable upon the exercise of any currently outstanding warrants" (PX-50 at 1567).

57. AIT deleted this language in the next draft. On Saturday, January 27, Maxim's counsel responded, "Your deletion of the specific representation regarding the warrants is not

acceptable to investors so we will not be making that change" (PX-50). Mr. Lisi voiced his disagreement to the senior managers at Maxim (PX-50).

58. On Monday, January 29, 2018 at 8 am, AIT's counsel, Adam Newman, sent "final versions of the SPA (with schedules)" to Maxim. The proposed SPA provided for the sale of a share of common stock at $4.25, with investors receiving a warrant exercisable at $4.25 for no additional consideration (PX-51 at 2207-2209). The proposed SPA deleted the representation sought by Maxim and added a provision that the investors would "acknowledge that an exercise price adjustment with respect to the Existing Warrants…should be the sole adjustment required thereunder as a result of the transactions contemplated by the Transaction Documents" (PX-51 at 2309). Mr. Lisi demanded that Maxim provide an "answer" to the draft SPA by 11:00 a.m. that morning (PX-52).

59. Maxim and AIT spoke several times on January 29, 2018, but could not resolve their differing views on the treatment of the existing warrants in the SPA (PX-52-54). Later on January 29, Maxim advised AIT, "Maxim will not be able to participate in the transaction absent including the warrant issue as a risk factor" (PX-54). The "warrant issue" referred to the impact of the proposed offering on Section 3(b) of the existing Warrants. Maxim resigned from the engagement (Tr. at 420:4-16).

60. On January 30, 2018, Maxim reported to Empery's Ryan Lane that the placement was off (PX-55). Mr. Lane reached out to Mr. Lisi to get more information and to express an interest in participating on the terms proposed by Maxim. The conversation was brief. Mr. Lane asked Mr. Lisi to confirm how the existing Warrants would be treated in light of the new placement. Mr. Lisi answered that the transaction would have no effect on the existing Warrants (Tr. at 68:18-69:21).

61. On or about January 29, 2018, AIT retained a new placement agent, Laidlaw & Company (UK) Ltd. ("Laidlaw"). On January 30, 2018, AIT's counsel provided Laidlaw with a draft SPA providing for the issuance of common stock at $4.25 per share, with a warrant exercisable at the same price for no additional consideration (PX-56; Tr. at 505:18-20).

Deerfield's Involvement in the 2018 Capital Raise

62. In February 2018, AIT asked Deerfield to participate in the new capital raise transaction. The draft Securities Purchase Agreement sent to Deerfield provided that an "exercise price adjustment . . . shall be the sole adjustment required" under the Warrants issued in 2017 (PX-39 at 0004163). Deerfield responded:

> Section 4.12 of the SPA needs to be revised to delete the last three lines (from "and further acknowledge" through the end of the sentence). We cannot acknowledge that a price reduction is the only anti-dilution trigger. ***We believe there is also an adjustment to the number of warrant shares***.

(PX-40 [emphasis added]).

63. Deerfield withdrew its investment commitment but offered "to enter into a waiver of any claim Deerfield may have to an adjustment of the number of Warrant Shares by virtue of the offering" (DX-56). After some negotiations with AIT, Deerfield agreed to invest $100,000 with a similar waiver (DX-57-58). AIT also agreed to modify Section 4.12 and to enter into a side letter that provided Deerfield's acknowledgements were limited to its own warrants (PX-41-43). Deerfield's waiver was based on a business judgment to support AIT and its existing investment (Tr. at 345:15-346:17), and did not reflect agreement with AIT's reading of Section 3(b) of the Warrant Agreement.

The Revised 2018 Capital Raise Structure

64. Around the same time, and in light of the questions raised concerning the impact of the Warrant Agreement's anti-dilution provisions, AIT modified the structure of the proposed

transaction. Taking into account the evidence presented, and the surrounding circumstances, the Court finds that the purpose of the modifications (discussed below) was to make it *seem* like the Revised 2018 Capital Raise no longer involved the issuance of "shares of Common Stock" for $4.25 plus an option to acquire shares for the same price with no additional consideration. In substance, however, it was the same deal as in the prior iterations of the transaction, with a change in form designed at least in part to minimize any Price and Share Adjustments under the Warrant Agreement.

65. Under the revised structure, the Securities Purchase Agreement (the "2018 SPA") offered investors a Common Stock Purchase Warrant for $0.01 with a Tranche A and Tranche B warrant, each exercisable at $4.25 per share (DX-59 at 3/149, 121/149). The offering closed on February 16, 2018, the same day that the parties signed the 2018 SPA (PX-45). It was announced by filing a Form 8-K with the SEC on February 22, 2018 (PX-45).

66. The purported "Common Stock Purchase Warrant" was not, in the common meaning of the word, a "warrant." It did not contain an exercise price or a term within which it must be exercised. Instead, the instrument simply provided that the holder may exercise two *other* warrants, Tranche A and B, each with its own exercise price, term, and other provisions (PX-46; PX-69, ¶¶ 20-21; PX-70, ¶¶ 11-18).

67. While the Tranche A Warrant states that its term for exercise is three "business days," (PX-46 at p. 83/99), the 2018 SPA effectively eliminated the three-day option, providing that:

> **On or prior to the Closing Date**, each Purchaser shall deliver or cause to be delivered to the Company or the Escrow Agent, as applicable, the following:
>
> (i) to the Company, this Agreement duly executed by such Purchaser;

> (ii) to the Escrow Agent, via wire transfer of immediately available funds to the account specified in the Escrow Agreement and set forth on Exhibit F hereto, such Purchaser's (1) Purchase Price [$0.01 per warrant share] and (2) Tranche A Exercise Amount [$4.25 per warrant share], each as set forth across from such Purchaser's name on Schedule 1 attached hereto;
>
> (iii) to the Company, a duly executed Notice of Exercise with respect to the total amount of such Purchaser's Tranche A Warrant Shares.

(*id*. § 2.2 [emphasis added]).

68. In other words, investors in the offering were required to commit *on signing* the 2018 SPA to exercise its Tranche A Warrant and pay $4.25 per share as of the closing date of the transaction. The 2018 SPA required that the "Closing" occur "substantially concurrent with the execution and delivery of this Agreement by the parties hereto" (*id*. § 2.1). AIT's Form 8-K confirms that "Immediately following the Closing, each Purchaser exercised the full amount of their Tranche A Warrants," and received a share of common stock (PX-45).

69. The Court finds that the Tranche A "Warrant" is, in substance, the sale of AIT Common Stock. Both Ryan Lane of the Empery Funds and Elliot Press of Deerfield testified that they could not recall ever seeing a similar structure despite their decades of industry experience (Tr. at 347:21-348:9; PX-69, ¶ 21). The Tranche A Warrant is simply the sale of Common Stock. In other words, the substance of the transaction did not change from that offered by Maxim and documented in the "final SPA" that AIT provided to Maxim on January 29, 2018.

70. Section 3(e) of the Warrants provides, "If any event occurs of the type contemplated by the provisions of this Section 3 but not expressly provided for by such provisions (including the granting of stock appreciation rights, phantom stock rights or other rights with equity features), then the Company Board will make an appropriate adjustment to the

Exercise Price and the number of Common Stock acquirable upon exercise of this Warrant so as to protect the rights of the Holders of the Warrants…." (PX-1 § 3(e).)

71. Looking through form to substance, as Section 3(e) requires, the Court finds that the structure of the Revised 2018 Capital Raise is one "contemplated by the provisions of this Section 3." The issuance was the sale of Common Stock with a warrant in a single transaction for a combined total of $4.26 per unit. The AIT Board was therefore required under the Warrant Agreement to make an adjustment consistent with the other provisions in Section 3, including the anti-dilution provisions of Section 3(b).

72. Even if that were not the case, the issuance of the Common Stock Purchase Warrant, Tranche A warrant and Tranche B warrant constitutes the issuance of "Options…issued in connection with the issuance or sale of other securities of the Company, together comprising one integrated transaction or series of related transactions," under Section 3(d) of the Warrants. (PX-1-3). Section 3(d) requires that the aggregate consideration received in the placement be allocated between the "options" and the "other securities."

The Adjustments Required By the 2018 Capital Raise

73. Applying Section 3(e) and looking to the substance of the transaction, the 2018 capital raise involved the sale of common stock for $4.26 per share, with a warrant exercisable at $4.25 per share for no additional consideration. Section 3(d) of the Warrants required AIT to value the warrants issued in the 2018 capital raise using the Black-Scholes formula set forth in Section 3(d)(A)(II), and then to subtract that figure from the total consideration, $4.26 per share, to value the common stock. The formula in Section 3(d), discussed below, results in a value of $2.68 for the Tranche B Warrant (and $0.01 for the common stock purchase warrant), leaving a balance of $1.57 for the common stock issued in the 2018 capital raise.

74. Under Section 3(d), the "options," are to be valued first with that value deducted from the "aggregate consideration," and the balance treated as the value for the "other securities" (PX-1-3).

75. The Tranche B Warrant is an "Option." Under Section 3(d)(A), the "Options will be deemed to have been issued for a consideration equal to the greater of…" three alternatives. Here, the greatest alternative is the Black Scholes value, for which specific pricing criteria are set (PX-1 § 3(d)(A)(III) & Schedule I). The application of that formula results in a price per warrant of $2.68 (PX-69 at ¶¶ 19-27). Section 3(d) further provides that the "other securities" are deemed to have been issued based on the "aggregate consideration received by [AIT]…less the Option Consideration" (PX-1). Here, the aggregate consideration is $4.26, leaving a value of $1.57 for the common stock issued pursuant to the Tranche A Warrants (PX-69 at ¶¶ 19-27).

76. Under Section 3(b) of the Warrants, the exercise price should have adjusted to $1.57 per share, an adjustment that AIT was obligated to report to warrant holders "promptly" (PX-1 § 3(f)). AIT, however, notified the Empery Funds and other warrant holders that the exercise price had adjusted only to $4.25 per share. AIT also failed to notify the Empery Funds that there was a corresponding increase in the number of warrant shares pursuant to the third sentence in Section 3(b) (PX-61).

The Empery Funds' Response Upon Learning of the 2018 Capital Raise

77. In February 2018, Ryan Lane learned from public filings that AIT had completed a financing which was in substance identical to the one that he had discussed with Maxim in late January (PX-45). In its public filings, AIT indicated that the exercise price in the Warrants would adjust to $4.25 and that there would be no adjustment to the number of warrant shares (PX-69, ¶ 18).

78. On February 26, 2018, Mr. Lane contacted AIT to demand an adjustment to the exercise price and the number of warrant shares in the Warrants consistent with the anti-dilution disclosure in the Term Sheet and AIT's deemed sale of common stock at $1.57 per share (PX-61). With a share adjustment under Section 3(b), the Empery Funds' Warrants should have adjusted to an aggregate of 732,490 warrant shares, allocated 319,967 warrant shares for Empery Asset Master; 159,851 warrant shares for Empery Tax Efficient; and 252,672 warrant shares for Empery Tax Efficient II. AIT rejected the demand (PX-69, ¶ 26). Empery did not seek to exercise any Warrants at that time.

79. As noted above, Empery brought this lawsuit on March 16, 2018.

The Empery Funds' Exercise of the Warrants

80. On March 2, 2020, the Empery Funds sought to exercise their Warrants. They delivered exercise notices that day using the exercise price that AIT had demanded ($4.25 per share), but reserved all of their rights in a footnote added to the notice of exercise form. (PX-63.) The form was otherwise identical to that annexed to the Warrants.

81. AIT rejected this notice the next morning. (PX-64.) AIT took the position that it would only honor an exercise notice without language that qualified or added to the form of notice annexed to the Warrants. AIT advised that the price of the warrant shares was adjusted to $3.66 per share (*id.*).

82. On March 3, 2020, the Empery Funds sent exercise notices that utilized an exercise price of $1.57 and the adjusted number of warrant shares that they contended were appropriate under Section 3(b) (PX-65). AIT rejected these notices (PX-69, ¶ 28). Later that day, the Empery Funds sent exercise notices that conformed to AIT's demands. In a cover email, the Empery Funds reserved all of their rights and claims (PX-66).

83. The Empery Funds exercised with a cash payment, delivering the full amount due under the Warrants based on AIT's calculations (PX-69, ¶ 28). Under the Warrants, shares were due within two trading days (PX-1 at § 1(a)(i)).

84. On March 4, 2020, AIT issued 166,668 shares to the Empery Funds, the number of Warrant shares without adjustment (Tr. at 91:13-14; PX-66). AIT failed to deliver 565,822 shares which were due as a result of the adjustment provisions in Section 3(b). These shares would have been allocated 43.7% to Empery Asset Master (247,163 shares), 21.8% to Empery Tax Efficient (123,479 shares), and 34.5% to Empery Tax Efficient II (195,180 shares). These Share Adjustments are based on an assumed exercise price of $1.57 per share (PX-69, ¶ 30).

85. From March 2 through March 5, 2020, AIT shares traded as follows:

	High	Low	Mid-point	Close
March 2	10.64	8.60	9.62	9.31
March 3	10.8799	9.00	9.94	10.93
March 4	12.50	9.96	11.23	10.39
March 5	12.00	7.26	9.63	9.38

(PX-67.)

86. Based on the mid-point between the high and low prices, the shares that were due on March 4, 2020, had an aggregate value of $6,354,181.06 ($11.23 x 565,822), allocated $2,775,640.49 for Empery Asset Master, $1,386,669.17 for Empery Tax Efficient, and $2,191,871.40 for Empery Tax Efficient II. In order to receive these shares, the Empery Funds would have had to pay an additional $540,004.42 on exercise, allocated as follows: $235,885.55 for Empery Asset Master, $117,844.55 for Empery Tax Efficient, and $186,274.32 for Empery Tax Efficient II.

CONCLUSIONS OF LAW

Reformation of the Warrants

"'The purpose of reformation is … to restate the intended terms of an agreement when the writing that memorializes that agreement is at variance with the intent of both parties.'" *Empery Asset Master, Ltd v. AIT Therapeutics, Inc.*, 179 A.D.3d 443, 444 (1st Dep't 2020) (quoting *Warberg Opportunistic Trading Fund, L.P. v. GeoResources, Inc.*, 112 A.D.3d 78, 86 (1st Dep't 2013)). "'A claim for reformation of a written agreement must be grounded upon either mutual mistake or fraudulently induced unilateral mistake'…" *Warberg Opportunistic Trading Fund, L.P., v. GeoResources, Inc.*, 151 A.D.3d 465, 470 (1st Dep't 2017).

Under New York law, "a scrivener's error, like a mutual mistake, occurs when the intention of the parties is identical at the time of the transaction but the written agreement does not express that intention because of that error; this permits a court acting in equity to reform an agreement.'" *Washington v. NYC Med. Prac., P.C.*, No. 18-CV-9052 (PAC), 2021 WL 918753, at *5 (S.D.N.Y. Mar. 10, 2021) (quoting *Wilton Reassurance Life Co. of New York v. Smith*, No. 12-CV-5131 SLT VMS, 2015 WL 631973, at *16 (E.D.N.Y. Feb. 13, 2015)).

The evidence shows that both AIT and the Empery Funds intended, at the time of the transaction, for the Warrants to provide for "full ratchet" anti-dilution protection—*i.e.*, an adjustment to both the share price and number of warrant shares upon any subsequent issuance of AIT securities at a lower price. The drafting history and other contemporaneous correspondence plainly shows that AIT inserted the second sentence of Section 3(b) not to remove "full ratchet" anti-dilution protection, but simply to ""[c]larify[ ] that if shares are issued for no consideration, then deemed to be issued at $0.01/share…." so that there would not be an infinite adjustment to the number of warrant shares (PX-22). That is consistent with Mr. Avniel's instruction to "leave the full ratchet" (PX-14).

And then there is the dog that didn't bark in the night.[4] In all the contemporaneous correspondence presented at trial, there is not a single reference to an intention to limit the protection to circumstances in which shares were issued for no consideration. To the contrary, as noted above, *all* of the relevant correspondence indicates an intention to provide "full ratchet" protection, including a reduction in strike price plus issuance of additional shares. Moreover, there was persuasive evidence that such a reading would make no sense in context. In those circumstances, the absence of any contemporaneous evidence supporting Defendant's position is telling.

AIT makes much of the fact that Empery was not directly involved in the negotiations between AIT and Deerfield that led to the initial drafting error in Section 3(b) of the Warrant Agreement. As the First Department recently held, however, that fact does not preclude a claim for reformation based on mutual mistake and scrivener's error (*Empery II*, 2021 NY Slip Op 05163, *1). It is sufficient that the evidence at trial clearly and convincingly demonstrated that both AIT and Empery understood and intended that the Share Adjustment provision in the Warrant Agreement applied to "each such adjustment" in the "immediately preceding *sentences*" of Section 3(b), such that the trigger for the Price Adjustment and Share Adjustment is the same.

Accordingly, the Empery Funds' Warrants must be reformed so that the third sentence of Section 3(b) is revised to substitute the word "sentences" for the word "sentence."[5] Therefore,

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[4] "The absence of particular evidence may sometimes provide clues as important as the presence of such evidence. In literature, a common way of expressing this truth, although not always accurately, is to refer to the dog that did not bark" (*Leopold v Cent. Intelligence Agency*, 987 F3d 163, 167 [DC Cir 2021] [citing Arthur Conan Doyle's Silver Blaze (1892), reprinted in II THE ANNOTATED SHERLOCK HOLMES 261 [1967, Wm. S. Baring-Gould ed.]).

[5] The same result would obtain, perhaps more naturally, by combining the "zero consideration" sentence with the preceding Price Adjustment sentence (with the revision in bold): "If and whenever after the Effective Date, the Company issues or sells, or is deemed to have issued or

the Share Adjustment provision would be triggered by *any* Price Adjustment referenced in the first two sentences of Section 3(b), not just for one based on the issuance of AIT shares for zero consideration.

The Price Adjustment Claim

Based on the evidence admitted at trial, the Court finds that AIT's 2018 SPA constitutes the sale of "Options…issued in connection with the issuance or sale of other securities of the Company, together comprising one integrated transaction or series of related transactions," under Section 3(d) of the Warrants. Section 3(d) requires that the aggregate consideration received in the placement be allocated between the "options" and the "other securities," with the Tranche B Warrants treated as "options" and the Tranche A Warrants as "other securities" (PX-1, PX-2, PX-3).

Even if that were not the case, Defendant's 2018 SPA is a transaction covered by 3(e) of the Warrants which provides, "[i]f any event occurs of the type contemplated by the provisions of this Section 3 but not expressly provided for by such provisions (including the granting of stock appreciation rights, phantom stock rights or other rights with equity features), then the Company Board will make an appropriate adjustment to the Exercise Price and the number of

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sold, any Ordinary Shares (excluding Exempted Issuances (as defined below)), for a consideration per share (the "New Issuance Price") less than a price equal to the Exercise Price in effect immediately prior to such issuance or sale (the "Applicable Price"), then immediately after such issuance or sale the Exercise Price then in effect shall be reduced to the New Issuance Price**; provided, however, that if** any sale or issuance, or deemed issuance, is for no consideration, then the New Issuance Price shall be deemed to be $0.01 per Ordinary Share. Upon each such adjustment of the Exercise Price pursuant to the immediately preceding sentence, the number of Warrant Shares issuable upon exercise of this Warrant shall be increased to the number of Ordinary Shares determined by multiplying the Exercise Price in effect immediately prior to such adjustment by the number of Warrant Shares issuable upon exercise of this Warrant immediately prior to such adjustment and dividing the product thereof by the Exercise Price resulting from such adjustment."

Common Stock acquirable upon exercise of this Warrant so as to protect the rights of the Holders of the Warrants…." (PX-1, PX-2, PX-3).

In accordance with the valuation required pursuant to Section 3(d) of the Warrants, the consideration received by AIT is $1.57 for each share of common stock. Thus, the sale of the Tranche A Warrants is deemed the sale of a share of common stock for $1.57 per share in accordance with the valuation required by Section 3(d) of the Warrants. Accordingly, under Section 3(b), the Exercise Price of the Warrants adjusted to $1.57 per share on February 16, 2018.

In addition, under the Share Adjustment provision in the Warrant Agreement as reformed, Empery was entitled to acquire an aggregate of 732,490 shares of Defendant's common stock at $1.57 per share, allocated 319,967 warrant shares for Empery Asset Master; 159,851 warrant shares for Empery Tax Efficient; and 252,672 warrant shares for Empery Tax Efficient.

Breach of Contract and Damages

"The elements of a breach of contract claim are (1) the existence of a contract, (2) the plaintiff's performance, (3) the defendant's breach, and (4) resulting damages." *Alloy Advisory, LLC, et al. v. 503 W. 33rd St. Assocs., Inc., et al.*, No. 14001, 2021 WL 2229654, at *1 (1st Dep't June 3, 2021). "Under New York law, damages for breach of contract should put the plaintiff in the same economic position he would have occupied had the breaching party performed the contract." *Oscar Gruss & Son, Inc. v. Hollander*, 337 F.3d 186, 196 (2d Cir. 2003).

"'[T]he proper valuation for the [W]arrants was the date of the breach—the date [defendant] failed to deliver the warrants.'" *Iroquois Master Fund, Ltd. v. Quantum Fuel Sys. Techs. Worldwide, Inc.*, 641 F. App'x 24 (2d Cir. 2016) (quoting *Oscar Gruss*, 337 F.3d at 197). "The proper measure of damages for a breach of an option contract is the difference between the

market value of the stock and the option price." *Id*. at 26 (citing *Hermanowski v. Acton Corp.*, 729 F.2d 921, 922 (2d Cir. 1984)). *See also Maxim Grp. LLC v. Life Partners Holdings, Inc.*, 690 F. Supp. 2d 293, 301 (S.D.N.Y. 2010); *Remsen Funding Corp. of New York v. Ocean W. Holding Corp.*, No. 06 CIV. 15265 (DLC), 2009 WL 874212, at *1 (S.D.N.Y. Mar. 31, 2009).

"For publicly-traded stock, the market price of the stock on the date of the breach is calculated as 'the mean between the highest and lowest quoted selling prices, as provided by the public exchange upon which the stock traded.'" *Iroquois Master Fund, Ltd. v. Quantum Fuel Sys. Techs. Worldwide, Inc.*, No. 13 CIV. 3860 CM SN, 2014 WL 2800752, at *1 (S.D.N.Y. June 17, 2014), *aff'd*, 641 F. App'x 24 (2d Cir. 2016) (citations and quotation marks omitted). The mid-point measure has been widely accepted. *See Maxim Grp. LLC v. Life Partners Holdings, Inc.*, 690 F. Supp. 2d at 301 ("to determine the stock's value on the date of breach, we use 'the mean between the highest and lowest quoted selling prices,' as provided by the public exchange upon which the stock traded'"); *Alpha Capital Anstalt v. Imaging3, Inc.*, No. 1:17-CV-6966-GHW, 2018 WL 3597520, at *6 (S.D.N.Y. July 26, 2018) ("'For publicly-traded stock, the market price of the stock on the date of the breach is calculated as the mean between the highest and lowest quoted selling prices, as provided by the public exchange upon which the stock traded'" (quotation marks omitted)); *see also Remsen Funding Corp. of New York v. Ocean W. Holding Corp.*, 2009 WL 874212, at *1.

The shares were due no later than the standard settlement date, commonly called "T+2." 17 CFR § 240.15c6-1 (effective May 2017). The Empery Funds' March 2 exercise was proper and shares were due no later than March 4, 2020, the second trading day after exercise. *Iroquois Master Fund, Ltd. v. Quantum Fuel Sys. Techs. Worldwide, Inc.*, 641 F. App'x at 26 (error in exercise notice immaterial where intent to exercise is clear). Defendant breached the Warrants

by failing to deliver 565,822 shares that were due on March 4, 2021, allocated 247,163 shares to Empery Asset Master Fund, 123,479 shares to Empery Tax Efficient I, and 195,180 shares to Empery Tax Efficient II.

The Empery funds are entitled to damages in the aggregate amount of $5,814,176.64, based on a value of $11.23 per AIT share, which represents the midpoint between the high and the low trading price for defendant's common stock on March 4, 2020. The total value of the undelivered shares on the date of the breach is $6,354,181.06, less $540,004.42, representing the additional exercise price that would have been paid based on the operation of a Warrants at $1.57 per share. The damages are allocated $2,539,754.94 to Empery Asset Master Fund, $1,268,824.62 to Empery Tax Efficient I, and $2,005,597.08 to Empery Tax Efficient II.

AIT's argument that damages must be measured as of March 1, 2018 is unavailing. The premise of AIT's argument is that its issuance of a Certificate of Adjustment on that date – with a Price Adjustment to $4.25 and no Share Adjustment – constituted an anticipatory repudiation of the Warrant Agreement that mandates measuring Empery's damages from that date. But that characterization is not supported by the facts. "A claim of anticipatory repudiation must be supported by evidence of an unqualified and clear refusal to perform with respect to the entire contract." *Joseph P. Carrara & Sons, Inc. v A.R. Mack Const. Co., Inc.*, 89 AD3d 1190, 1191 (3d Dept 2011). Moreover, "[t]he expression of intent not to perform by the repudiator must be 'positive and unequivocal.'" *Princes Point LLC v Muss Dev. L.L.C.*, 30 NY3d 127, 133 (2017).

AIT's Certificate did not constitute a positive and unequivocal repudiation of the Warrant Agreement. Indeed, it confirmed that AIT *would* continue its performance under the agreement (if and when Empery exercised) on the terms AIT contended should govern. Nor did Empery act in a manner that suggested it considered the contract to be repudiated. Although March 2020

turned out to be a high-water mark for AIT's stock price, Empery could not have known at the time that would be the case and it would have been held to that number even if AIT's stock price continued to rise. Based on the evidence presented at trial, the Court concludes that Empery's damages claim arose when it exercised its warrants in March 2020 and AIT failed make the required price and share adjustments at that time.

CONCLUSION

It is, therefore:

ORDERED and ADJUDGED that Plaintiffs have established their first claim for relief (reformation). The Empery Funds' Warrants are reformed so that the third sentence of Section 3(b) is revised to substitute the word "sentences" for "sentence;" and it is further

ORDERED and ADJUDGED that Plaintiffs' have established their third claim for relief for breach of contract. The Clerk is directed enter judgment in favor Plaintiff Empery Asset Master Fund in the amount of $2,539,754.94, Plaintiff Empery Tax Efficient I in the amount of $1,268,824.62, and Plaintiff Empery Tax Efficient II in the amount of $2,005,597.08, with each sum to bear prejudgment interest pursuant to CPLR 5001 from March 4, 2020 through the date of judgment.

This constitutes the decision and order of the Court. Plaintiff is directed to submit a proposed judgment for the Court's review and approval.

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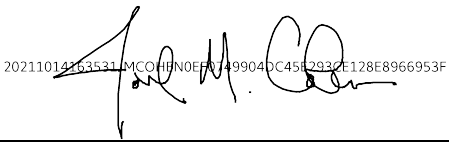

DATE: 10/14/2021 **JOEL M. COHEN, JSC**

Check One: [X] **Case Disposed** [ ] **Non-Final Disposition**

Check if Appropriate: [ ] **Other (Specify _____)**