

<b>Empery Asset Master Ltd. v GT Biopharma, Inc.</b>
2020 NY Slip Op 31562(U)
April 26, 2020
Supreme Court, New York County
Docket Number: 656408/2018
Judge: Andrew Borrok
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SUPREME COURT OF THE STATE OF NEW YORK  
COUNTY OF NEW YORK: COMMERCIAL DIVISION PART IAS MOTION 53EFM

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EMPERY ASSET MASTER LTD., EMPERY TAX  
EFFICIENT, L.P., EMPERY TAX EFFICIENT II, L.P.

Plaintiff,

- v -

GT BIOPHARMA, INC., PAUL KESSLER,

Defendant.

INDEX NO.	656408/2018
MOTION DATE	04/24/2020
MOTION SEQ. NO.	001
<b>DECISION + ORDER ON MOTION</b>	

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HON. ANDREW BORROK:

The following e-filed documents, listed by NYSCEF document number (Motion 001) 35, 36, 37, 38, 39, 40, 41, 42, 43, 44, 45, 46, 47, 48, 49, 50

were read on this motion to/for DISMISS.

Upon the foregoing documents, and for the reasons set forth below, Paul Kessler’s motion pursuant to CPLR § 3211 (a) (7) to dismiss the sixth (tortious interference with contract), seventh (defamation), and eighth (civil conspiracy) causes of action in Biopharma III (hereinafter defined) as set forth in the First Amended Complaint (**FAC**) is granted in part as set forth below.

**I. The Relevant Facts and Circumstances**

GT Biopharma, Inc. (**GT Biopharma**) is a publicly-traded biopharmaceutical company based in California. In 2017, GT Biopharma retained an investment banker to help it secure financing to fund its operations. The investment banker connected GT Biopharma with Empery Asset Master Ltd. (**Empery Asset**), Empery Tax Efficient, L.P. (**Empery Tax I**), and Empery Tax Efficient II, L.P.’s (**Empery Tax II**; Empery Asset, Empery Tax I, and together with Empery Tax II, collectively, the **Empery Funds**).

On January 23 2018, GT Biopharma issued certain convertible notes (the **Notes**) and warrants (the **Warrants**) to the Empery Funds (FAC., ¶ 2; NYSCEF Doc No. 2-4). The terms of the Notes and Warrants are governed by a certain Securities Purchase Agreement (the **SPA**), dated as of January 22, 2018, by and among GT Biopharma and the Empery Funds (NYSCEF Doc. No. 19).

Pursuant to the SPA, GT Biopharma issued (i) Notes in the aggregate principal amount of \$963,000.96 to Empery Asset for the purchase price of \$876,000.00 and Warrants representing the right of Emery Asset to acquire 210,394 shares of GT Biopharma common stock (the **Common Stock**), (ii) Notes in the aggregate principal amount of \$333,000.00 to Empery Tax I for the purchase price of \$366,300.37 and Warrants representing Empery Tax I's right to acquire 79,979 shares of Common Stock, and (ii) Notes in the aggregate principal amount of \$870,100.87 to Empery Tax II for the purchase price of \$791,000.00 and Warrants representing Empery Tax II's right to acquire 189,979 shares of Common Stock (NYSCEF Doc No. 2-4).

Pursuant to Section 4 of each Note, the failure to pay the holder any principal, interest, late charges or other amounts when due either under the Note or "the Other Notes" constitutes an Event of Default. And, upon the occurrence of an Event of Default, the Notes provide for an adjustment to the conversion price (NYSCEF Doc No. 2-4, § 11).

Pursuant to Section 1 (b) of the Warrants, the Empery Funds had the right to purchase the number of shares of Common Stock set forth in each Warrant at the exercise price then in effect, which was initially set at \$4.58. And, significantly, the Warrants were subject to “anti-dilution” protection – *i.e.*, if GT Biopharma issued securities with a per-share purchase price lower than the exercise price of the Warrants, GT Biopharma was required to adjust the exercise price of the Warrants to the lowest per-share purchase price, conversion price or exercise price (FAC, ¶ 2). If GT Biopharma failed to deliver the common shares on the share delivery date, the Notes provide that GT Biopharma is liable for damages (NYSCEF Doc. No. 2-4, § 3 [c] [ii]). The parties expressly agreed that New York law would govern any dispute arising out of the SPA or the underlying Notes or Warrants and consented to personal jurisdiction in this court (NYSCEF Doc. No. 19, § 9 [a]). And, the maturity date of the Notes was July 23, 2018.

Finally, pursuant to Section 9 [k] of the SPA, each party agreed to indemnify and hold harmless the Empery Funds, including for reasonable attorneys’ fees and disbursements as a result of, or arising out of, or relating to any case of action made against the Empery Funds arising out of or resulting from the status of the Empery Funds as an investor in GT Biopharma pursuant to the transactions contemplated by the transaction documents.

GT Biopharma defaulted on the Notes by failing to pay the principal due on the Notes on or before the maturity date. Pursuant to the terms of the Notes, the Empery Funds served partial void redemption notices (the **Conversion Notices**) formally requesting to convert a portion of the outstanding Notes at the variable rate of \$1.22 (NYSCEF Doc. No. 9). Subsequently, GT

Biopharma repaid the portion of the outstanding principal that the Empery Funds chose not to convert but did not honor the Conversion Notices.

GT Biopharma filed a lawsuit (**Biopharma I**) against the Empery Funds in the United States District Court for the Southern District of New York on August 1, 2018 captioned *GT Biopharma, Inc. v Empery Asset Master Ltd. et al.*, Case No. 1:18-cv-06910-GDB (US Dist Ct, SD NY) alleging that the Empery Funds engaged in a “bad faith scheme” to “manipulate” GT Biopharma’s share price by short selling its stock. And, by letter, dated August 3, 2018, from GT Biopharma to the Empery Funds (the **August 3 Letter**), GT Biopharma indicated that it would not honor the conversion price applicable to the Notes because it believed that the conversion price had been artificially depressed based on the Empery Funds’ misconduct as alleged in the complaint in *Biopharma I* (NYSCEF Doc. No. 11).

GT Biopharma entered into a separate financing agreement with other investors on August 2, 2018, pursuant to which it issued convertible notes with a conversion price of \$2.00. Pursuant to the anti-dilution provisions described above, the FAC alleges that this triggered the Warrants’ price adjustment provisions requiring GT Biopharma to adjust the exercise price of the Warrants to from \$4.58 to \$2.00. GT Biopharma, however, refused to honor the price adjustment with respect to the Warrants.

On August 27, 2018, Anthony J. Cataldo, GT Biopharma’s founder and former Executive Chairman, filed another lawsuit against the Empery Funds, this time in the Superior Court of the State of California, Los Angeles County (**Biopharma II**) on August 27, 2018 captioned *Anthony*

*J. Cataldo v Empery Asset Master Ltd. et al.*, Case No. SC129731 (Cal Super Ct, L.A. County).

In Biopharma II, Mr. Cataldo alleged that he had been wrongfully forced to resign as Executive Chairman as a result of the Empery Funds' short selling and also due to negative feedback regarding GT Biopharma's management that the Empery Funds allegedly provided to GT Biopharma's investment banker. Biopharma I was voluntarily dismissed. Biopharma II is still pending.

The Empery Funds commenced this lawsuit (**Biopharma III**) against GT Biopharma for breach of contract, liquidated damages, and attorneys' fees and costs pursuant to the SPA, as well as the underlying Notes and Warrants. Subsequently, the Empery Funds filed the FAC adding Mr. Kessler as an additional defendant. Mr. Kessler is an investor in GT Biopharma. The Empery Funds allege in the FAC that Mr. Kessler caused GT Biopharma to breach the SPA and the Notes and Warrants issued thereunder, including by instructing GT Biopharma to file Biopharma I and Biopharma II (FAC, ¶ 106). The Empery Funds also allege that the allegations of insider trading with respect to the short-selling scheme set forth in Biopharma I and Biopharma II were based on statements made by Mr. Kessler to GT Biopharma that the Empery Funds had sold short GT Biopharma securities and that he knew the specific investment banks through which such trading occurred (*id.*, ¶ 113). And, significantly, the Empery Funds allege that GT Biopharma's then CEO, Ray Urbanski, acknowledged to a representative of the Empery Funds that the lawsuits filed by GT Biopharma were "not only baseless, but concocted by Paul Kessler" (*id.*, ¶ 61).

## II. Discussion

A party may move for judgment dismissing one or more causes of action on the ground that the pleadings fail to state a cause of action for which relief may be granted (CPLR § 3211 [a] [7]). On a motion to dismiss pursuant to CPLR § 3211 (a) (7), the court must afford the pleadings a liberal construction and accept the facts alleged in the complaint as true, according the plaintiff the benefit of every favorable inference (*Morone v Morone*, 50 NY2d 481, 484 [1980]). The court's inquiry on a motion to dismiss is whether the facts alleged fit within any cognizable legal theory (*id.*). Bare legal conclusions are not accorded favorable inferences, however, and need not be accepted as true (*Biondi v Beekman Hill House Apt. Corp.*, 257 AD2d 76, 81 [1st Dept 1999]).

**A. Dismissal of the Tortious Interference (Sixth) Cause of Action is granted solely with respect to the failure to repay the Notes as of the Maturity Date**

To state a cause of action for tortious interference with contract, a plaintiff must allege “the existence of a valid contract between the plaintiff and a third party, defendant’s knowledge of that contract, defendant’s intentional procurement of the third-party’s breach of the contract without justification, actual breach of the contract, and damages resulting therefrom” (*Lama Holding Co. v Smith Barney Inc.*, 88 NY2d 413, 424 [1996], citing *Israel v Wood Dolson Co.*, 1 NY2d 116, 120 [1956]). A plaintiff must specifically allege that the defendant’s conduct was the proximate cause of the third-party’s breach of the contract, *i.e.*, that the breach would not have occurred “but for” the conduct of the defendant (*Burrowes v Combs*, 25 AD3d 370, 373 [1st Dept 2006]). As the First Department has observed, “[a]though on a motion to dismiss the allegations in a complaint should be construed liberally, to avoid dismissal of a tortious interference with contract claim a plaintiff must support his claim with more than mere speculation” (*id.*, citing *Williams & Co. v Collins, Tuttle & Co.*, 6 AD2d 302 [1958]).

The Empery Funds allege that as an investor in GT Biopharma who was active in its management, and due to his close relationship with Mr. Cataldo, Mr. Kessler had knowledge of the SPA and caused GT Biopharma to breach the SPA and the Notes and Warrants issued thereunder by instructing its management to file the allegedly frivolous Biopharma I and Biopharma II (FAC, ¶¶ 105-106). Mr. Kessler argues that the claim for tortious interference must be dismissed because (i) the Empery Funds fail to allege a causal connection between Mr. Kessler's alleged conduct and GT Biopharma's breach of the SPA and underlying Notes and Warrants or the allegedly frivolous complaints filed in Biopharma I and Biopharma II, and (ii) Mr. Kessler's alleged statements are protected under the economic interest privilege.

First, with respect to GT Biopharma's alleged failure to repay the Notes on or before the maturity date, the FAC fails to allege that Mr. Kessler's actions were the proximate cause of this alleged breach – *i.e.*, a pleading deficiency that is fatal to this portion of the tortious interference claim. Specifically, the Empery Funds allege in the FAC that, as of July 2018, “GT Biopharma had failed to secure, and had no realistic plan to secure, additional financing,” and that “[w]ithout additional financing, GT Biopharma would be unable to satisfy its obligations to the Empery Funds by repaying the Notes” (FAC, ¶¶ 34-39). The Empery Funds further allege that, “[o]n July 23, 2018, counsel for GT Biopharma informed the Empery Funds that GT Biopharma would be unable to repay the Notes on or before the maturity date,” and that “GT Biopharma's failure to repay the Notes was a breach of Section 3 of the Notes and constituted an event of default under the terms of the Notes” (*id.*). In other words, taking these allegations as true, GT Biopharma's breach of the SPA with respect to its failure to repay the Notes by the maturity date

was caused by its inability to secure additional financing, not by any statements allegedly made by Mr. Kessler or by the lawsuits allegedly filed at his behest. Put another way, the breach to repay on the maturity date would have occurred irrespective of Mr. Kessler's alleged conduct.

But, the Empery Funds sufficiently plead causation with respect to the other alleged acts forming the basis of their tortious interference claim, namely, GT Biopharma's refusal to honor the Empery Funds' conversion request and refusal to adjust the conversion price of the Notes or the exercise price of the Warrants. As alleged in the FAC, GT Biopharma's reason for taking these actions was that the Empery Funds had artificially depressed GT Biopharma's share price through its insider trading scheme (*id.*, ¶ 48). In the August 3 Letter, GT Biopharma explains that it would not honor the conversion price because "it is [GT Biopharma's] position that the conversion price applicable to the Notes has been artificially depressed as a result of [the Empery Funds'] . . . misconduct" (NYSCEF Doc. No. 48). The Empery Funds allege that the source of this information, *i.e.*, that the Empery Funds engaged in insider trading and sold short GT Biopharma stock to artificially depress the share price, was Mr. Kessler (*id.*, ¶¶ 63-64). And, with respect to the portion of the tortious interference claim based on the filing Biopharma I and Biopharma II, the Empery Funds allege that Mr. Kessler exerted his influence over GT Biopharma's management and instructed them to commence the lawsuits rather than honor GT Biopharma's contractual obligations (*id.*, ¶¶ 105-106) – *i.e.*, Mr. Kessler's statements and the exertion of his influence were proximate causes of GT Biopharma's breaches of the SPA and the Notes and Warrants and of the filing of these lawsuits and damages that resulted. Therefore, taking the allegations in the FAC as true and affording them every favorable inference, the Empery Funds state a cause of action for tortious interference with contract as it relates to (i) the

filing of Biopharma I and Biopharma II, (ii) the refusal to honor the conversion request, and (iii) the refusal to adjust the conversion price of the Notes or the exercise price of the Warrants.

To the extent that Mr. Kessler attempts to invoke the economic interest defense as an investor of GT Biopharma, the defense is inapplicable at this stage of the proceedings. The economic interest defense is applicable in cases where the defendant “acted to protect its own legal or financial stake in the breaching party’s business” (*White Plains Coat & Apron Co., Inc. v Cintas Corp.*, 8 NY3d 422, 426 [2007]). Overcoming a defense of economic interest requires a showing of malice, fraud, or illegality (*Foster v Churchill*, 87 NY2d 744, 750 [1996]). But, significantly, the First Department has held that the economic interest defense does not automatically apply to causes of action for tortious interference with an *existing contract* (*Havana Central NY2 LLC v Lunney’s Pub, Inc.*, 49 AD3d 70, 72-72 [1st Dept 2007]; *Kronish Lieb Weiner & Hellman LLP v Tahari, Ltd.*, 35 AD3d 317, 318-319 [1st Dept 2006]), and that in such cases, whether a defendant acted in his or her economic self interest “merely creates a factual issue for trial” (*Bank of N.Y. v Berisford Intl.*, 190 AD2d 622, 623 [1st Dept 1993]). Accordingly, because this is a cause of action for tortious interference with an existing contract, the economic interest defense is not available to Mr. Kessler on a pre-answer motion to dismiss. Therefore, the motion to dismiss is granted solely to the extent that the portion of the sixth cause of action that is based on GT Biopharma’s failure to repay the Notes on or before the maturity date is dismissed, but is otherwise denied.

**B. Dismissal of the Defamation (Seventh) Cause of Action is denied**

Defamation is defined as “the making of a false statement which tends to expose the plaintiff to public contempt, ridicule, aversion or disgrace, or induce an evil opinion of him in the minds of right-thinking persons, and to deprive him of their friendly intercourse in society” (*Foster v Churchill*, 87 NY2d 744, 751 [1996] [internal quotation marks omitted]). Defamation requires “(1) a false statement that is (2) published to a third party (3) without privilege or authorization, and that (4) causes harm, unless the statement is one of the types of publications actionable regardless of harm” (*Stepanov v Dow Jones & Co., Inc.*, 120 AD3d 28, 34 [1st Dept 2014]). Special damages are a necessary element of a defamation claim unless the alleged defamation falls within one of the categories of statements that constitute defamation *per se*: “(1) statements charging the plaintiff with a serious crime; (2) statements that tend to injure the plaintiff in her trade, business or profession; (3) statements that impute to the plaintiff a ‘loathsome disease’; and (4) statements that impute unchastity to a woman” (*Nolan v State*, 158 AD3d 186, 195 [1st Dept 2018]). As the Court of Appeals has explained, “[w]hether particular words are defamatory presents a legal question to be resolved by the court in the first instance” (*Aronson v Wiersma*, 65 NY2d 592, 593 [1985]).

Mr. Kessler argues that the cause of action for defamation must be dismissed because, among other reasons, as an investor of GT Biopharma, Mr. Kessler’s statements were made in regard to a matter of common interest between GT Biopharma and Mr. Kessler and are therefore protected by the “common interest” privilege. The argument fails.

In the seminal case of *Lieberman v Gelstein* (80 NY2d 429 [1992]), the Court of Appeals discussed the “common interest” privilege. *Lieberman* involved a defamation lawsuit brought by

the landlord against a tenant who was on the board of governors of the tenants' association (*id.* at 432). As relevant to the instant motion, the second cause of action was based on a conversation that the defendant allegedly had with another tenant who also served on the board. Allegedly, the defendant asked the other member of the board if he could check with his friend at the local police precinct which police officers the plaintiff was bribing to permit him to park in violation of the traffic laws with impunity (*id.* at 433). Following discovery, the defendant moved for summary judgment based on the "common interest" qualified privilege characterizing his conversation as an inquiry to uncover wrongdoing by the landlord affecting tenants (*id.*). And, at his deposition, the defendant testified that the source of his concern stemmed from two building employees (who he identified) but admitted did not know whether the allegations were true (*id.* at 433-434). This according to the defendant is precisely why he asked the other tenant, who was a friend of the captain of local precinct, to determine if the allegations were true (*id.* at 434). In his opposition papers, the plaintiff argued that there was an issue of fact as to malice because of long standing disputes between the parties (*id.*). The trial court dismissed the second cause of action, holding that the statements were subject to the qualified privilege and that the plaintiff did not meet its burden in raising a triable issue of fact (*id.*). The Appellate Division affirmed and leave was granted (*id.*). The Court of Appeals affirmed, holding that although a qualified privilege may be overcome if the plaintiff can demonstrate that the defendant spoke with "malice," the plaintiff failed to raise a triable issue of fact under either the common law definition of malice (*i.e.*, spite or ill will) or the definition announced in *New York Times Co. v Sullivan* (376 US 254 [1964]) (*i.e.*, a high degree of awareness of their probable falsity (*id.* at 437-439). Furthermore, the Court commented that,

[s]ignificantly, Gelstein did not make a public announcement of his suspicions – from which an inference could be drawn that his motive was to defame Liberman – but relayed them to a colleague who was in a position to investigate. (*id.* at 349).

The case at bar is very different than *Liberman*. In this action, the FAC alleges:

**The True Motivation Behind the Lawsuits Filed Against Empery Funds is Revealed by GT Biopharma’s CEO**

61. The true motivation behind both of [Biopharma I] and [Biopharma II] was finally revealed by the former CEO of GT Biopharma himself. On January 22, 2019, then CEO Ray Urbanski explicitly admitted to a representative of the Empery Funds that the lawsuits filed by GT Biopharma and Mr. Cataldo ***were not only baseless, but concocted by Paul Kessler***, an individual who had no official role in the management of GT Biopharma and no position on its board.

62. Specifically, Mr. Urbanski explained that the claims in both actions were ***fabricated by Paul Kessler*** – an investor in GT Biopharma and a longtime friend and associate of Mr. Cataldo who wielded immense control over GT Biopharma management and Mr. Cataldo. According to Mr. Urbanski, ***Kessler “coordinated” the filing of each of the complaints***, including by having several meetings with GT Biopharma’s and Cataldo’s counsel without representatives of GT Biopharma or Mr. Cataldo being present.

63. Among other things, Kessler:

- Insisted to GT Biopharma management and its counsel that the Empery Funds had committed insider trading by selling short shares in GT Biopharma, ***even though he had no basis to make such an accusation***
- ***Falsely provided GT Biopharma management with the names of certain investment banks who Kessler claimed to have carried out the alleged short-selling, even though none of those banks had traded a single GT Biopharma security on behalf of the Empery Funds***
- ***Provided the false information outlined above to GT Biopharma’s New York counsel and coordinated the filing of [Biopharma I]***
- Convinced Mr. Cataldo to allow a frivolous lawsuit to be filed on his own behalf

64. Accordingly, ***Kessler acted with improper motives, and plainly misrepresented to GT Biopharma management***, including Mr. Urbanski, facts that were eventually used as

the basis for both . . . [Biopharma I] and [Biopharma II] (FAC, ¶¶ 61-64 [emphasis added]).

In other words, unlike in Liberman, here the allegations set forth in the FAC which must be taken as true at this stage of the proceedings, allege that Mr. Kessler’s statements were made with spite or ill will or with a high degree of awareness of their probable falsity which, if true, would be sufficient to overcome or dissolve the qualified common interest privilege (cf., *Ashby v ALM Media, LLC*, 110 AD3d 459, 459 [1st Dept 2013] [affirming the trial court’s dismissal based on the common interest privilege]). Accordingly, the branch of the motion seeking dismissal of the seventh cause of action is denied.

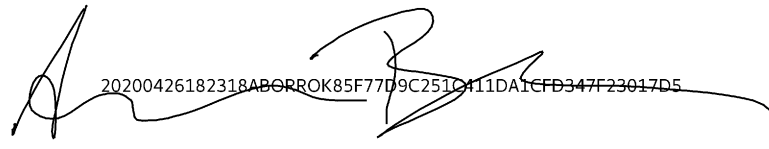
**C. Dismissal of the Civil Conspiracy (Eighth) Cause of Action is granted**

Inasmuch as the Empery Funds consent to the dismissal of the eighth cause of action (civil conspiracy), it is dismissed (see Pl. Mem. in Opp. at 17 n 4).

Accordingly, it is

ORDERED that the motion to dismiss is granted solely to the extent of dismissing that portion of the sixth cause of action that is based on GT Biopharma’s failure to repay the Notes on or before the maturity date, and the seventh and eighth causes of action are dismissed.

4/26/2020  
DATE



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ANDREW BORROK, J.S.C.

CHECK ONE:  CASE DISPOSED

NON-FINAL DISPOSITION

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APPLICATION:	<input type="checkbox"/>	SETTLE ORDER	<input type="checkbox"/>		<input type="checkbox"/>	SUBMIT ORDER	<input type="checkbox"/>	
CHECK IF APPROPRIATE:	<input type="checkbox"/>	INCLUDES TRANSFER/REASSIGN	<input type="checkbox"/>		<input type="checkbox"/>	FIDUCIARY APPOINTMENT	<input type="checkbox"/>	REFERENCE