

Delaware Court of Chancery Dismisses Complaint Challenging Amendment to Conform Indenture to Offering Memorandum

On May 24, 2019, in *AG Oncon, LLC et al. v. Ligand Pharmaceuticals Inc.*,¹ the Delaware Court of Chancery dismissed a complaint by investor-plaintiffs alleging that an amendment conforming an indenture to the related offering memorandum was invalid. The Court held that the corporate issuer-defendant had properly exercised its right to conform the terms of the indenture to the description of notes in the offering memorandum without noteholder consent primarily because the indenture contained a provision expressly allowing the indenture to be so conformed without any such consent. The Court also held that doing so did not violate the Trust Indenture Act of 1939 (the “Trust Indenture Act”).

I. Background

In August of 2014, Ligand Pharmaceuticals Incorporated (“Ligand”) marketed and sold \$245 million aggregate principal amount of convertible notes (the “Notes”) in an offering pursuant to Rule 144A under the Securities Act of 1933 (the “Securities Act”), and at the closing of the offering, Ligand entered into an indenture governing the Notes (the “Indenture”).² After an inadvertent error was discovered in the conversion provisions of Indenture that was inconsistent with the same term as described in the offering memorandum used in connection with the original offering and sale of the Notes (the “Offering Memorandum”), in February of 2018, Ligand entered into a supplemental indenture in order to correct the error by conforming the denominator of the conversion formula in the Indenture to the conversion formula set forth in the Offering Memorandum.³ In so amending the Indenture, Ligand relied on Section 9.01(b) thereof, which permits amendments to the Indenture or the Notes in order to conform their terms to the “Description of Notes” section of the Offering Memorandum, without requiring the noteholders’ consent (the “Conforming Amendment Provision”).⁴

The plaintiffs acquired their Notes in the secondary market and held an aggregate principal amount of approximately \$212 million, or 95% of the outstanding Notes.⁵ The plaintiffs stated that they acquired the Notes “because of the conversion formula in the Indenture” (pre-conforming amendment) and that based on that conversion formula, the conversion value of their notes was approximately \$3.8 billion.⁶

On July 27, 2018, the plaintiffs filed a complaint in the Court of Chancery of the State of Delaware seeking a declaratory judgment and damages, asserting that the supplemental indenture was invalid because it (1)

¹ [*AG Oncon, LLC v. Ligand Pharmaceuticals Inc.*, C.A. No. 2018-0556-JTL \(Del. Ch. May 24, 2019\).](#)

² *Id.* at 2-3, 6.

³ *Id.* at 9. The error involved misuse of a defined term in the conversion formula. The Court noted that the use of that term “made no sense in light of what the formula attempted to calculate.” *Id.* at 1.

⁴ *Id.* at 9-10. Section 9.01(b) of the Indenture provides that Ligand “may amend or supplement this indenture or the Notes without the consent of any Holder to: . . . conform the terms of this Indenture or the Notes to the ‘Description of the Notes’ section of the Offering Memorandum.” [*Ligand Pharmaceuticals Incorporated 0.75% Convertible Senior Notes Due 2019 Indenture Dated as of August 18, 2014.*](#)

⁵ *Ligand* at 1-2, 9. The Court noted that, post-offering, Ligand’s public filings described the conversion formula “in a manner consistent with the Offering Memorandum.” *Id.* at 9.

⁶ *Id.*

“improperly elevated the Offering Memorandum over the Indenture as the controlling document, (2) breached the terms of the Indenture, and (3) violated Section 316(b) of the Trust Indenture Act.”⁷

In granting defendant’s motion to dismiss, the Court disagreed with each of the plaintiffs’ claims, holding that (1) the Offering Memorandum was not improperly elevated above Indenture because, in adopting the amendment, Ligand had relied solely on the Conforming Amendment Provision of the Indenture and not the Offering Memorandum, (2) the amendment did not contravene restrictions in the Indenture that required noteholders’ consent when a material and adverse amendment is made because the amendment fell within the Conforming Amendment Provision, and (3) Section 316(b) of the Trust Indenture Act does not apply to the Notes, which were not registered under the Securities Act, because the Indenture was not an “indenture security” for purposes of the Trust Indenture Act, but even if Trust Indenture Act did apply, it had not been violated because the conversion provisions at issue were not payment terms protected by Section 316(b).⁸

II. The “Complete and Final” Agreement

The plaintiffs’ first claim was that the amendment was invalid because the Indenture was the complete and final agreement governing the Notes, and Ligand could not rely on the Offering Memorandum in amending the terms of the Indenture.⁹ The Court held that Ligand was not improperly relying on the Offering Memorandum, or “elevating” the Offering Memorandum above the Indenture, because the Indenture itself contained the Conforming Amendment Provision and, thus, Ligand was relying on the Indenture in entering into the amendment.¹⁰

In support of its claim, plaintiffs cited language from the Offering Memorandum providing that the Offering Memorandum is subject to all provisions of the Notes and the Indenture.¹¹ The plaintiffs further claimed that, under common law, when an indenture and the related offering document conflict, “the indenture controls.”¹² The plaintiffs argued that because the Indenture was the controlling document, it superseded the Offering Memorandum, and therefore Ligand could not subsequently rely on the Offering Memorandum conversion formula.¹³ The Court reasoned that neither of these arguments were persuasive because Ligand was relying on the Conforming Amendment Provision, which was included within the Indenture and expressly stated that the terms of the Indenture could be conformed to the terms of the Offering Memorandum, concluding that “[a]t all times and for all purposes, Ligand has relied on the terms of the Indenture, not the Offering Memorandum.”¹⁴

Plaintiffs also argued that, because the global certificates representing the Notes referenced only the Indenture and not the Offering Memorandum, Section 8-202(a) of the New York Uniform Commercial Code limited the terms of the Notes to the terms set forth in the referenced Indenture.¹⁵ However, the Court reasoned that because

⁷ *Id.* at 9-10.

⁸ *Id.* at 11-13, 16-18, 21, 25-27.

⁹ *Id.* at 11.

¹⁰ *Id.* at 11-13.

¹¹ *Id.* at 11-12. The offering memorandum provides that “We will issue the notes under an indenture This summary is subject to, and is qualified by reference to, all of the provisions of the notes and the indenture, including the definitions of certain terms used in the notes and the indenture. We urge you to read these documents because they, and not this description, define your rights as a holder of the notes.” *Id.* (citation omitted).

¹² *Id.* at 12 (quoting *In re W.T. Grant Co.*, 4 B.R. 53, 73) (Bankr. S.D.N.Y. 1980) (additional citations omitted).

¹³ *Ligand* at 12.

¹⁴ *Id.* at 12-13.

¹⁵ *Id.* at 13. The New York Uniform Commercial Code provides that the terms of the certificated security are limited to the

the global certificate refers to the Indenture and in effectuating the amendment, Ligand relied on the Conforming Amendment Provision within the Indenture, Ligand's reliance on the Conforming Amendment Provision was "consistent with the terms stated on the certificate."¹⁶

III. Material and Adverse Amendment Requiring Noteholders' Consent

The plaintiffs' second claim was that the amendment materially and adversely affected their rights without their consent, in contravention of consents required by Sections 6.07 and 9.02 of the Indenture.¹⁷ The Court agreed with Ligand's position "that the Conforming Amendment Provision . . . permits any amendment necessary to conform the Indenture to the Offering Memorandum."¹⁸ The Court reasoned that Section 9.02(d), which requires noteholders' consent when the conversion rights in the Notes are adversely affected, did not supersede the Conforming Amendment Provision, and that the Conforming Amendment Provision was likewise not subject to Section 9.02(d).¹⁹ The Court noted that the purpose of Section 9.02(d) is to "prohibit[] departures from the original deal" without noteholders' consent, whereas "invoking the Conforming Amendment Provision does not amend the deal at all. It maintains the original deal by conforming the terms of the Indenture to the original deal."²⁰ Similarly, the Court reasoned that, while Section 6.07 does use the qualifying term "notwithstanding," it "does not apply to a change in the conversion formula; it protects the right to bring suit."²¹ The Court held that because the plaintiffs' right to sue was not affected, Section 6.07 was inapplicable.²² Thus, because the amendment was effectuated through the Conforming Amendment Provision, it was not in contravention of Section 6.07 or Section 9.02.

IV. The Trust Indenture Act

The plaintiffs' final argument was that the amendment violated Section 316(b) of the Trust Indenture Act.²³ Section 316(b) provides in relevant part that "the right of any holder of any indenture security to receive payment of the principal of and interest on such indenture security . . . shall not be impaired or affected without the consent of such holder . . ."²⁴ An "indenture security" is defined as "any security issued or issuable under the indenture to be qualified."²⁵ An "indenture to be qualified" is defined as "(A) the indenture under which there has been or is to be issued a security in respect of which a particular registration statement has been filed or (B) the indenture in

terms stated "on the certificate and terms made part of the security by reference on the certificate to another instrument, indenture, or document . . . to the extent the terms referred to do not conflict with the terms stated on the certificate." N.Y. U.C.C. § 8-202(a).

¹⁶ *Ligand* at 13.

¹⁷ *Id.* Section 6.07 of the Indenture provides that "[n]otwithstanding any other provision of this Indenture, the right of any Holder to bring suit for the enforcement of payment of principal, accrued and unpaid interest . . . shall not be impaired or affected without the consent of such Holder . . ." *Indenture* at 43 (emphasis added).

¹⁸ *Ligand* at 14. Section 9.02(d) of the Indenture provides "that, without the consent of each affected Holder of an outstanding Note, no amendment or supplement to this Indenture or the Notes may: . . . make any change that impairs or adversely affects the conversion rights of any Notes . . ." *Indenture* at 52 (emphasis added).

¹⁹ *Ligand* at 15, 17.

²⁰ *Id.* at 18.

²¹ *Id.* at 19.

²² *Id.*

²³ *Id.* at 20.

²⁴ 15 U.S.C. § 77ppp(b).

²⁵ § 77ccc(11).

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respect to which a particular application has been filed.”²⁶ The Notes were offered under Rule 144A, and no registration statement was filed under the Securities Act, nor did Ligand apply for qualification.²⁷ Thus, the Court held that “Section 316(b) does not apply to the Indenture because the Indenture was not an ‘indenture security’ for purposes of the Trust Indenture Act”²⁸ and the plaintiffs did not have a right to consent thereunder.

The Court went on to hold that even if Section 316(b) did apply, the amendment to the conversion formula would not be prohibited.²⁹ Focusing on the “plain language” of Section 316(b) (“the right . . . to receive payment of principal and interest”), the Court noted that “the most expansive reading” of the terms protected by Section 316(b) “encompasses the timing of payments of principal and interest” and not the consideration to be received upon conversion,³⁰ and that “[n]o court has held that Section 316(b) protects” that consideration. As result, even if Section 316(b) did apply to the Indenture, it would not prohibit the amendment.

V. Conclusion

The Court granted defendant’s motion to dismiss primarily based on the language of Conforming Amendment Provision, which provided that the Indenture could be modified to conform to the Offering Memorandum without the noteholders’ consent. The Court held that Ligand’s reliance on the Conforming Amendment Provision was valid and did not elevate the Offering Memorandum over the Indenture and that Ligand did not amend the Indenture in contravention of its terms. The Court dismissed the argument that the amendment violated Section 316(b) of the Trust Indenture Act because the Notes were not sold pursuant to a registration statement and conversion rights were in any event not protected by that Section. The decision makes clear the importance of including in an indenture provisions that allow the issuer to amend or supplement the indenture or the related notes without the consent of the noteholders to, among other things, conform the terms thereof to the description of notes section of the related offering document.

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If you have any questions about the issues addressed in this memorandum, or if you would like a copy of any of the materials mentioned in it, please do not hesitate to call or email Helene Banks at 212.701.3439 or hbanks@cahill.com; Bradley J. Bondi at 202.862.8910 or bbondi@cahill.com; Charles A. Gilman at 212.701.3403 or cgilman@cahill.com; Elai Katz at 212.701.3039 or ekatz@cahill.com; Geoffrey E. Liebmann at 212.701.3313 or gliebmann@cahill.com; Ross Sturman at 212.701.3831 or rsturman@cahill.com; or Paul Rafla at 212.701.3388 or prafla@cahill.com.

²⁶ § 77ccc(9).

²⁷ *Ligand* at 21.

²⁸ *Id.* Section 316(b) protects “the right of any holder of any indenture security to receive the payment of the principal and interest” § 77ppp(b).

²⁹ *Ligand* at 25.

³⁰ *Id.* at 27-28.