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SUPERIOR COURT OF NEW JERSEY
APPELLATE DIVISION
DOCKET NO. A-4140-08T2

RICHARD COLLINS, SAM GARLOCK, IVAN BELAN, LARRY GOLDBERG, GLEN SCHOEN, and HOSSEIN AFSHARI, On Behalf of Themselves and All Others Similarly Situated,

Plaintiffs-Appellants,

vs.

RAYMOND P. WARRELL, JR., LORETTA M. ITRI, GARY SIEGEL, MARTIN J. DRISCOLL, CHRISTOPHER P. PARIOS, DANIEL D. VON HOFF, DOUGLAS G. WATSON, and GENTA INCORPORATED,

Defendants-Respondents.

Submitted: September 22, 2010 - Decided: August 3, 2011

Before Judges Cuff and Fisher.

On appeal from Superior Court of New Jersey, Law Division, Union County, Docket No. L-3046-08.

The Rosen Law Firm, P.A., attorneys for appellants (Laurence M. Rosen, on the briefs).

Morgan, Lewis & Bockius, LLP, attorneys for respondents (Marc J. Sonnenfeld, of counsel; Robert A. White, on the brief).

PER CURIAM

Plaintiffs, a group of individual shareholders of Genta Incorporated (Genta), a Delaware corporation, filed a class action complaint on behalf of holders of common stock after defendants, seven individually-named officers and directors of Genta and the corporation itself, sold twenty million dollars of promissory notes convertible into two billion shares of common stock at one penny per share. Plaintiffs appeal two orders, one dismissing their complaint with prejudice, and the other denying plaintiffs' subsequent motion for relief from final judgment and to file an amended complaint. Defendants argue the motion judge properly dismissed the complaint because plaintiffs only asserted derivative claims. Further, defendants argue plaintiffs did not set forth newly discovered evidence warranting relief or justifying the filing of an amended complaint.

We hold that the judge properly dismissed the complaint but should have permitted plaintiffs to file their amended complaint. We, therefore, affirm in part and reverse in part and remand for further proceedings.

Given the procedural posture of the case, the facts are derived from the complaint and the documents referred to in the complaint. Plaintiffs Richard Collins, Sam Garlock, Ivan Belan, Larry Goldberg, Glen Schoen, and Hossein Afshari are shareholders of Genta, a publicly traded biopharmaceutical company in the business of developing anti-cancer treatments. Defendants are Genta and Raymond P. Warrell, Jr., Loretta M. Itri, Gary Siegel, Martin J. Driscoll, Christopher P. Parios, Daniel D. Von Hoff, and Douglas G. Watson, all of whom are the officers and directors of Genta. Defendant Raymond P. Warrell, Jr., is the Chief Executive Officer (CEO) of Genta, as well as the Chairman of the Board of Directors (the Board). Defendant Loretta M. Itri, who is married to Warrell, serves as President of Pharmaceutical Development and Chief Medical Officer. Defendant Gary Siegel is Genta's Vice President of Finance. The remaining defendants are members of Genta's Board: Martin J. Driscoll, Christopher P. Parios, Daniel D. Von Hoff, and Douglas G. Watson.

By the end of the first quarter of 2008, Genta "had a very high level of uncertainty inherent in [the] business and in [its] liquidity position." The Board warned investors through its March 2008 Form 10-K and a corresponding media press release that Genta faced the possibility of bankruptcy if it were unable to secure additional funds. Thereafter, Genta reduced its workforce in both April and May 2008, and undertook several additional steps to conserve cash. Genta explored various options to avoid bankruptcy, including the possibility of an acquisition or merger, an attempt to license company products, and efforts to seek investors in financial transactions favorable to the corporation. However, by mid-2008, Genta announced the only viable alternative to bankruptcy was the transaction that precipitated plaintiffs' complaint.

On June 5, 2008, Genta entered into a "binding securities purchase agreement" with institutional and accredited investors. Under this agreement, Genta agreed to sell the investors forty million dollars worth of convertible promissory notes (the Notes). The Notes were convertible into Genta common stock at a price of one penny per share. On June 9, 2008, the investors purchased twenty million dollars worth of the Notes, with the option to purchase the remaining twenty million dollars worth at a later date and under the same terms (the Notes Transaction). The group of investors who purchased the Notes included defendants Warrell and Itri, who purchased $1,950,000 and $300,000 respectively of the Notes.

In the Board's proposal for Genta stockholders to amend Genta's Certificate of Incorporation to authorize an increase in the number of shares of capital stock (the Proxy), the Board noted that its remaining members had independently discussed Warrell's and Itri's participation in the Notes Transaction, and concluded such participation would not interfere with their "exercise of independent judgment in carrying out their responsibilities in their respective positions." Furthermore, "[b]ased upon their internal discussions regarding strategic alternatives and advice from their financial advisor," the Board found the Notes Transaction "was fair and in the best interests of the non-affiliated stockholders . . . ." The Board warned the stockholders that "[f]ailure to approve this proposal will likely lead to a default under the financing agreements and may lead to bankruptcy of the Company."

At the time of the Notes Transaction, Genta's common stock traded in the range of $0.20 to $0.40 per share. The Proxy informed Genta stockholders that approval of the proposed amendment and subsequent issuance of common stock "will increase the outstanding number of shares of [c]ommon [s]tock, thereby causing dilution in earnings per share and voting interests of the outstanding [c]ommon [s]tock." Further, in the event all of the Notes are converted to common stock, there would be a large increase in the number of shares of common stock, "thereby causing significant dilution in earnings per share . . . ." At the time the Proxy was issued, there were 36,760,558 shares of outstanding Genta common stock.

On October 6, 2008, Genta conducted its Annual Meeting of Stockholders, at which time the stockholders were asked to vote on the proposal to amend Genta's Certificate of Incorporation to increase the total number of authorized shares of capital stock available for issuance. By a majority vote, the stockholders approved the amendment.

Plaintiffs filed their complaint on September 8, 2008. They alleged that prior to the Notes Transaction and corresponding amendment to Genta's Certificate of Incorporation, Genta's public stockholders owned approximately ninety-five percent of the corporation, whereas afterwards, the public stockholders owned just 1.8 percent of the corporation and the investors who purchased the Notes owned ninety-eight percent of the corporation. Plaintiffs further asserted they were never offered the opportunity to participate in the Notes Transaction, the value of their economic interests "was expropriated entirely by the sale of the Notes," and Genta and the Board did not take any steps to protect their interests during the negotiations preceding the Notes Transaction. Moreover, plaintiffs claimed the individually-named defendants "essentially put a gun to the heads of shareholders" in requesting their approval of the proposed amendment to the Certificate of Incorporation.

In their motion to dismiss, defendants argued the decision to enter the Notes Transaction, given the dire financial circumstances of Genta preceding the Transaction, was reasonable. Further, defendants contended they "acted aggressively and diligently to safeguard the interests of shareholders." Defendants also emphasized the detailed Proxy made available to shareholders prior to the vote on the amendment, which outlined the reasons for entering the Notes Transactions and truthfully alerted shareholders of the consequences of an amendment approval.

In response to plaintiffs' legal claims that the individually-named defendants had breached their fiduciary duty, and that Genta had aided and abetted these defendants in doing so, defendants responded the claims were "both fatally flawed as a matter of law." Among other things, defendants argued that plaintiffs were essentially asserting an "equity dilution claim," which save for a few exceptions, can only be brought as a derivative, not direct, claim. Because plaintiffs did not satisfy either exception, including the exception that involves conduct by a controlling shareholder, defendants contended they lacked standing to bring a direct claim.

Plaintiffs countered that defendant Warrell operated as Genta's controlling shareholder, and as such, they could bring an equity dilution claim as a direct suit. They asserted, "[d]efendant Warrell, as the CEO and Chairman controlled everything from when to hold board meetings, who to hire and fire, who to manage, etc." Plaintiffs also argued the Notes Transaction implicated defendants' "Revlon[1] duties" to seek out alternative competing transactions and obtain the best possible price for the public shareholders. In a reply memorandum, defendants insisted that plaintiffs could not establish either an equity dilution claim or a Revlon claim, because both claims require the presence of a controlling shareholder.

The motion judge agreed with defendants and granted the motion to dismiss on the basis plaintiffs lacked standing to bring a direct claim. In his March 20, 2009 written opinion, the judge found plaintiffs had failed to establish a controlling shareholder either before or after the Notes Transaction.

After filing a notice of appeal, plaintiffs moved for relief from judgment pursuant to Rule 4:50-1 and to file an amended complaint pursuant to Rule 4:9-1. Plaintiffs averred they had "discovered additional evidence which would probably alter the judgment and which they could not have discovered prior to the filing of the initial complaint." Plaintiffs purported this new evidence demonstrated defendants had misrepresented and falsified documents concerning the Notes Transaction.

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[1] Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173 (Del. 1986).

Defendants argued plaintiffs' "new evidence" merely consisted of two documents, neither of which related to the underlying issue of whether a controlling shareholder existed before and after the Notes Transaction. Further, defendants alleged plaintiffs did not establish an exceptional circumstance envisioned by Rule 4:50-1 to justify their relief from the March 20 decision, especially since plaintiffs had these documents in their possession prior to that decision.

Plaintiffs' motion was initially denied for lack of jurisdiction because plaintiffs had filed a notice of appeal. Following our order remanding this matter to address plaintiffs' motion, the motion judge denied plaintiffs' motion. In doing so, the judge again characterized the crucial issue as being whether plaintiffs' claims qualified as direct claims. The judge reviewed the asserted new evidence, three separate emails, and concluded the evidence still did not establish defendant Warrell acted as a controlling shareholder of Genta either before or after the Notes Transaction. In addition, because plaintiffs had failed to demonstrate actions by a controlling shareholder, the motion judge concluded plaintiffs could not support a direct Revlon claim to permit filing of the amended complaint.

On appeal, plaintiffs contend the motion judge erred in dismissing their complaint with prejudice because the decision "failed to afford plaintiffs the opportunity to pursue and defend its well-founded claims." Defendants, by contrast, assert plaintiffs have not demonstrated how the motion judge erred in rendering this decision.

Rule 4:6-2(e) permits a defendant to move for dismissal of a complaint for "failure to state a claim upon which relief can be granted." "'[T]he plaintiff is entitled to a liberal interpretation of [the complaint's] contents and to the benefits of all its allegations and the most favorable inferences which may be reasonably drawn from them.'" Burg v. State, 147 N.J. Super. 316, 319-20 (App. Div.) (quoting Rappaport v. Nichols, 31 N.J. 188, 193 (1959)), certif. denied, 75 N.J. 11 (1977). Further, "all facts alleged in the complaint and the legitimate inferences drawn therefrom are deemed admitted." Smith v. City of Newark, 136 N.J. Super. 107, 112 (App. Div. 1975). Ordinarily, if the trial court grants the motion to dismiss, it is done so without prejudice, and the court has the discretion to permit the plaintiff to amend the complaint and allege additional facts that could support a cause of action. Hoffman v. Hampshire Labs, Inc., 405 N.J. Super. 105, 116 (App. Div. 2009).

In reviewing the trial court's disposition of a motion made pursuant to Rule 4:6-2(e), this court is bound by the same standard that governed the trial court. Seidenberg v. Summit Bank, 348 N.J. Super. 243, 250 (App. Div. 2002). The inquiry is "'confined to a consideration of the legal sufficiency of the alleged facts apparent on the face of the challenged claim.'" Rieder v. N.J. Dep't of Transp., 221 N.J. Super. 547, 552 (App. Div. 1987) (quoting P. & J. Auto Body v. Miller, 72 N.J. Super. 207, 211 (App. Div. 1962)). The reviewing court "'searches the complaint in depth and with liberality to ascertain whether the fundament of a cause of action may be gleaned even from an obscure statement of claim, opportunity being given to amend if necessary.'" Printing Mart-Morristown v. Sharp Elecs. Corp., 116 N.J. 739, 746 (1989) (quoting Di Cristofaro v. Laurel Grove Mem'l Park, 43 N.J. Super. 244, 252 (App. Div. 1957)). Although the review is "one that is at once painstaking and undertaken with a generous and hospitable approach," ibid., dismissal is nonetheless required "where the factual allegations are palpably insufficient to support a claim upon which relief can be granted," Rieder, supra, 221 N.J. Super. at 552.

Here, plaintiffs' original complaint asserted two counts. First, plaintiffs alleged the individually-named defendants breached their fiduciary duty owed to the common stockholders of

Genta. Among the several allegations, plaintiffs assert that defendants sold the convertible Notes at a price far below the true fair-market value of the common shares into which such Notes are immediately convertible. Plaintiffs also contend defendants failed to take steps to maximize the value of Genta to its public shareholders and defendants failed to solicit better competing financing options for Genta. In addition, plaintiffs allege defendants failed to invite or permit existing Genta shareholders to participate equally in the Notes Transaction, failed to value Genta properly, and failed to disclose explicitly to shareholders in the Proxy or elsewhere the unfairly low price at which Note holders may convert the Notes into shares of Genta common stock. Plaintiffs also contend defendants unfairly expropriated the economic value and voting interest of existing common stockholders' interest in the company, and failed to put in place an independent committee of the Board of Directors to negotiate and evaluate the Notes Transaction in a manner that would protect the interests of common stockholders. Plaintiffs also averred Genta aided and abetted the individually-named defendants in breaching their fiduciary duty.

"A claim for wrongful equity dilution is premised on the theory that the corporation, by issuing additional stock for inadequate consideration, made the complaining stockholder's investment less valuable." Feldman v. Cutaia, 951 A.2d 727, 732 (Del. 2008). Ordinarily, such claims are regarded as derivative claims and not direct claims.[2] Gentile v. Rossette, 906 A.2d 91, 99 (Del. 2006). This is so "because any dilution in the value of the corporation's stock is merely the unavoidable result (from an accounting standpoint) of the reduction in the value of the entire corporate entity, of which each share of equity represents an equal fraction." Ibid.

An equity dilution claim is viewed as a direct suit where "(1) a stockholder having majority or effective control causes the corporation to issue 'excessive' shares of its stock in exchange for assets of the controlling stockholder that have a lesser value;" and "(2) the exchange causes an increase in the percentage of the outstanding shares owned by the controlling stockholder, and a corresponding decrease in the share percentage owned by the public (minority) shareholders." Id. at

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[2] A derivative claim is one that is brought on behalf of the corporation for harm done to the corporation, and any recovery must go to the corporation. Tooley v. Donaldson, Lufkin & Jenrette, Inc., 845 A.2d 1031, 1036 (Del. 2004). By contrast, a direct claim involves allegations that an individual stockholder suffered an injury affecting his or her legal rights, and any recovery flows directly to the individual stockholder and not the corporation. Ibid.; see also Feldman, supra, 951 A.2d at 732 (summarizing the analytical framework for distinguishing between direct and derivative suits).

100. In such cases, the public (minority) stockholders have a separate direct claim as a result of "an improper transfer--or expropriation--of economic value and voting power from the public shareholders to the majority or controlling stockholder." Ibid. In other words, "the public shareholders are harmed, uniquely and individually, to the same extent that the controlling shareholder is (correspondingly) benefited." Ibid.

Only a controlling shareholder owes fiduciary duties to other shareholders. In re Primedia, Inc. Derivative Litig., 910 A.2d 248, 257 (Del. Ch. 2007) (citing Kahn v. Lynch Commc'n Sys., Inc., 638 A.2d 1110, 1113-14 (Del. 1994)). A controlling shareholder exists when the shareholder: "(1) owns more than 50% of the voting power of a corporation; or (2) exercises control over the business and affairs of the corporation." Feldman v. Cutaia, 956 A.2d 644, 657 (Del. Ch. 2007) (internal quotation omitted), aff'd, 951 A.2d 727 (Del. 2008). Bare allegations that the subject shareholder possesses the "potential ability to exercise control" are insufficient. Primedia, supra, 910 A.2d at 257. And, although a plaintiff need not demonstrate that the subject shareholder "oversaw the day-to-day operations" of the corporation, "[a]llegations of control over the particular transaction at issue are enough." Ibid.

Therefore, plaintiffs could withstand the motion to dismiss only if they demonstrated a direct claim under the theory a controlling shareholder existed both before and after the Notes Transaction. In their brief opposing the motion to dismiss, plaintiffs argued defendant Warrell was Genta's controlling shareholder for the following reasons: (1) he and his wife, defendant Itri, owned five percent of Genta's equity and were the most highly compensated employees prior to the Notes Transaction; (2) defendant Warrell was the only person who served as both an officer and director, thus he "controlled everything from when to hold board meetings, who to hire and fire, who to manage, etc.;" (3) the outside director defendants allowed defendant Warrell "all power to manage Genta and to find, evaluate, and negotiate all financing offers that culminated in the [Notes] Transaction;" (4) defendant Von Hoff "was beholden to [d]efendant Warrell because he held top positions at a company that generated hundreds of thousands of dollars per year in fees for services it provided to Genta, which would only continue if it pleased [d]efendant Warrell;" (5) the outside director defendants "cleared the way for [d]efendant Warrell to exercise control of Genta [because] they did not form an independent committee of disinterested directors to identify, evaluate, and negotiate financing options for

Genta;" (6) defendant Siegel's position as chief financial officer "naturally lent itself to his active participation in executing the Transaction," and defendant Siegel "was beholden to [d]efendant Warrell;" and (7) defendant Itri also benefited from the Notes Transaction and thus supported defendant Warrell's exercise of control over Genta.

The motion judge concluded plaintiffs' evidence did not demonstrate defendant Warrell actually exercised control over Genta. Rather, the judge summarized the evidence as only showing defendant Warrell had the potential to exert influence. Further, the judge distinguished plaintiffs' complaint from the complaint in Williamson v. Cox Communications, Inc., No. 1663-N (Del. Ch. June 5, 2006) (slip op. at 10-11), in which the Delaware Chancery Court denied a motion to dismiss because "the complaint contain[ed] facts that d[id] support, at a minimum, the inference that [the defendants] were controlling shareholders." There, the plaintiff public shareholders alleged the defendants - two cable companies that sold their joint control of an internet service provider (ISP) to a third cable company through a transaction that was alleged to be unfair to the ISP - had: (1) designated representatives to serve on the board of directors; (2) entered into a transaction with the corporation to their benefit; and (3) retained veto power over the board's decisions. Id. at 11-25. The Williamson judge noted that these allegations alone did not support an inference that the defendants were controlling shareholders, but taken together gave rise to the inference that the subject transaction was really the culmination of a process whereby the defendants "agreed to carve-up the assets" of the ISP for themselves, with no regard for the other shareholders' interests. Id. at 15-16.

Here, defendants entered the Notes Transaction in an effort to improve the precarious financial situation faced by Genta. Although defendant Warrell's position as CEO and Chairman of the Board provided a potential opportunity to exert control, see Primedia, supra, 910 A.2d at 257, there was insufficient evidence to even support an inference defendant Warrell operated as a controlling shareholder, see Feldman, supra, 956 A.2d at 657. At the time the judge granted defendants' motion to dismiss, plaintiffs had not alleged defendant Warrell owned more than fifty percent of the voting power either before or after the Notes Transaction. Further, plaintiffs did not provide facts sufficient to give rise to the inference defendant Warrell "exercise[d] control over the business and affairs" of Genta, including control over the Notes Transaction itself. Therefore, the judge properly dismissed plaintiffs' complaint on the grounds plaintiffs could not sustain a direct equity dilution claim. We also conclude plaintiffs' Revlon claim was unsustainable on the allegations of the initial complaint.

In Revlon, the board of directors of the corporation adopted various defensive measures to thwart a takeover of the company. 506 A.2d at 176-79. The Supreme Court of Delaware held that defensive measures, such as lock-ups[3] and related agreements, are permitted under Delaware law when the adoption of the measures is not tainted by director self-interest or other breaches of fiduciary duty. Id. at 176. Moreover, the board of directors may consider "various corporate constituencies" when developing and adopting defensive measures, but there must be "some rationally related benefit" to shareholders. Ibid.

The court explained that the business judgment rule may insulate corporate directors from personal liability for business decisions and can apply when corporate directors fashion responses to a takeover threat. Id. at 180. Their decisions, however, must be grounded on the bedrock principles

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[3] A lock-up is "an arrangement or transaction by which the target corporation in a contested takeover gives one proposed acquirer a competitive advantage over other bidders or prospective bidders. Usually, a lock-up involves granting the favored suitor (the 'white knight') an option to buy shares or assets of the target." Note, Lock-Up Options: Toward A State Law Standard, 96 Harv. L. Rev. 1068, 1068 (1983) (footnotes omitted).

of "care, loyalty and independence" to the corporation and its shareholders. Ibid. Thus, when a board rejects a takeover bid as grossly inadequate and the directors make an informed decision in good faith to adopt a defensive measure reasonable in relation to the threat posed to the corporation, directors will be insulated from personal liability due to the business judgment rule and the action itself will be insulated from attack by the business judgment doctrine. Id. at 181. On the other hand, when directors change course from corporate preservation to a sale of the corporation or certain parts of it, the directors' duty changes, and measures adopted by the board must be infused with the goal maximizing the company's value in a sale for the benefit of stockholders. Id. at 182. If, as in Revlon, the board adopts measures calculated to insulate directors from liability or favor one corporate constituency at the expense of shareholders, the board will have breached its fundamental duty of loyalty, and its action is not entitled to the deference afforded to it by the business judgment rule. Id. at 184.

In their initial complaint, plaintiffs assert the Notes Transaction was, in substance, a sale of nearly the entire Company (98%-99%) to a close knit investor group. Prior to the Notes Transaction, public shareholders owned 95% of Genta's shares while afterwards, plaintiff public investors owned less than 2% of Genta's shares. Plaintiffs contend that the Notes Transaction constituted a "change in corporate control" subject to heightened judicial scrutiny.

It is well-settled that a change in corporate control transaction is subject to heightened judicial scrutiny as opposed to simply the business judgment rule. Paramount Commc'ns Inc. v. QVC Network Inc., 637 A.2d 34, 42 (Del. 1994). However, plaintiffs' initial complaint failed to overcome the initial hurdle that the Notes Transaction constituted a change in corporate control. In Paramount, a group of public stockholders who owned a majority of the corporation's voting stock challenged a transaction which would permit the defendant entity to purchase the controlling stock in the corporation, even though a more valuable sale option was available to the corporation. Id. at 36. Following the transaction, the defendant entity would become the controlling stockholder of the corporation, and would have the voting power to, among other things, elect directors, cause the corporation to break-up, merge the corporation with another company, cash-out the public stockholders, amend the certificate of incorporation, sell any and all of the corporate assets, or otherwise materially alter the nature of the corporation and the interests of the public stockholders. Id. at 43. As this was truly a "sale of control" of the corporation, the Paramount court found the transaction should be evaluated under a heightened standard and in accordance with the directors' duties as set forth in Revlon. Id. at 44. That is, "[i]n the sale of control context, the directors must focus on one primary objective--to secure the transaction offering the best value reasonably available for the stockholders--and they must exercise their fiduciary duties to further that end." Id. at 44 (citing Revlon, supra, 506 A.2d at 182).

Here, at the time defendants moved to dismiss plaintiffs' initial complaint, plaintiffs only made the bare allegation that, after the Notes Transaction, "Genta is effectively . . . a close corporation 98% owned by a small group of closely-knit Note Holders." Plaintiffs did not demonstrate how the "not more than 21 unaffiliated purchasers of the notes" are even remotely similar to the single entity subject to the sale of the corporation in Paramount which gave rise to a Revlon claim. Id. at 36. Further, as noted previously, plaintiffs did not establish that the Notes Transaction constituted a sale of Genta or a change in corporate control on the basis defendant Warrell, as an individual, was a controlling shareholder.

In sum, the motion judge correctly dismissed plaintiffs' complaint pursuant to Rule 4:6-2(e). Even when viewed liberally, plaintiffs' complaint cannot be sustained as either an equity dilution or change in corporate control matter. Simply stated, "the factual allegations are palpably insufficient to support a claim upon which relief can be granted." Rieder, supra, 221 N.J. Super. at 552.

Plaintiffs also object to the March 20, 2009 order dismissing their complaint with prejudice. They argue that the nature of the litigation supports the notion they should be afforded the opportunity to amend the complaint at least once, and that they received important discovery documents late.

Although motions to dismiss should be granted rarely and "the dismissal should be without prejudice to a plaintiff's filing of an amended complaint," Printing Mart-Morristown, supra, 116 N.J. at 772, it remains within the motion judge's discretion to dismiss with prejudice if amendment of the complaint would be futile, see Johnson v. Glassman, 401 N.J. Super. 222, 246-47 (App. Div. 2008); see also J.D. v. Davy, 415 N.J. Super. 375, 397-98 (App. Div. 2010) (describing instances where the courts have not hesitated to dismiss a complaint with prejudice). However, where the court determines dismissal with prejudice is proper, it should explain its reasons for doing so.

Klajman v. Fair Lawn Estates, 292 N.J. Super. 54, 61 (App. Div.), certif. denied, 146 N.J. 569 (1996).

Here, dismissal without prejudice of the original complaint was entirely appropriate. Plaintiffs, however, should have had the opportunity to amend their complaint because there are circumstances, albeit limited, when the business judgment rule will not insulate directors' actions. This is particularly true in this case where plaintiffs sought to file an amended complaint.

In their May 13, 2009 motion, plaintiffs sought permission to file an amended complaint. Leave to amend a complaint should be freely granted. R. 4:9-1; Kernan v. One Washington Park Urban Renewal Assocs., 154 N.J. 437, 456-57 (1998). The decision rests in the motion judge's sound discretion and requires a two-step process: "whether the non-moving party will be prejudiced, and whether granting the amendment would nonetheless be futile." Notte v. Merchs. Mut. Ins. Co., 185 N.J. 490, 501 (2006). Thus, the motion judge is "'free to refuse leave to amend when the newly asserted claim is not sustainable as a matter of law. In other words, there is no point to permitting the filing of an amended pleading when a subsequent motion to dismiss must be granted.'" Id. at 501-02 (quoting Interchange State Bank v. Rinaldi, 303 N.J. Super. 239, 257 (App. Div. 1997)); see also Pressler & Verniero, Current N.J. Court Rules, comment 2.2.1 on R. 4:9-1 (2011).

Plaintiffs contend the new information advanced in their motion supports a Revlon claim because both prior to and at the time of the Notes Transaction, defendants were actively seeking to sell Genta or effect a change in control of the corporation, "[h]aving initiated a process aimed at selling control of Genta, the defendants' [sic] were obligated under Revlon to negotiate a transaction that would provide the greatest possible economic benefit to the public shareholders." Additionally, plaintiffs aver that the defect in the initial complaint of insufficiently presenting a direct claim was cured because the new evidence demonstrates defendant Warrell had de facto control over Genta at all relevant times. Lastly, plaintiffs assert the new evidence establishes a direct cause of action on the basis defendants falsified certain documents and failed to disclose material facts to the public shareholders in relation to the Notes Transaction.

In his August 28, 2009 decision, the motion judge correctly stated the viability of plaintiffs' proposed amended complaint turned on whether it asserted derivative or direct claims. The judge then summarized the law governing an equity dilution claim as well as a Revlon claim, reviewed the alleged newly discovered evidence, and determined the proposed amended complaint did not assert a direct claim.

In the proposed amended complaint, plaintiffs cited three emails. The first email dated June 4, 2008, from defendant Warrell's secretary to the Board, indicated the "'Pricing Committee' will consist of <u>Gary Siegel</u> and <u>Doug Watson</u>, as opposed to Raymond Warrell and Doug Watson." According to plaintiffs, defendant Warrell's participation in this pricing committee, which apparently oversaw the Notes Transaction, demonstrates defendant Warrell "spearheaded the financing efforts throughout the prior years and . . . continued to do so after the debt transaction giving rise to the claim."

A second email dated June 4, 2008, from defendant Siegel to the other Board members, discussed whether the Notes Transaction would trigger the "poison pill" provision of Genta shareholders' "Rights Plan." Defendant Siegel suggested that, rather than reconvening for a Board meeting, they could amend the minutes from a prior Board meeting to reflect that the triggering of the Rights Plan was actually discussed. Plaintiffs contend that defendants' willingness to falsify Board meeting minutes in conjunction with the Notes Transaction provides further evidence defendant Warrell had de facto control over Genta and its Board.

A third email dated January 20, 2008, from defendant Warrell to representatives of the investment bank that assisted Genta with securing a financial solution for the corporation in the months preceding the Notes Transaction. In this email, defendant Warrell considered various financial solutions and stated:

> Everything should be on the table. Control will not be an issue; board seats are available and we're recruiting in any event. If someone believes they can find superior executive leadership, please have at it.
>
> FYI: I have offered to personally pony up $1.5M to 3MM in case we find an investor who desires owner/manager-led deals . . . . (That would obviously not apply if there's a control issue.)

Plaintiffs allege that this email establishes the Board "was well aware of the conflicting position that [defendant] Warrell was in," and that despite this conflict, defendants repeatedly permitted defendant Warrell to sit on the pricing committee that led to the eventual approval of the Notes Transaction.

The motion judge stated he could not discern how the first email established control and was not prepared to make "the leap of faith" taken by plaintiffs. He concluded the second email did not reference any actions taken by defendant Warrell or why other board members were obligated to him. Finally, the judge interpreted the third email as simply a discussion of options.

Therefore, the motion judge concluded that the newly discovered evidence could not support plaintiffs' allegations that defendant Warrell acted as a controlling shareholder either before or after the Notes Transaction. Thus, plaintiffs' amended complaint could not support a direct equity dilution claim.

Next, the judge evaluated the proposed amended complaint to determine whether it could support a Revlon claim. Plaintiffs contend the newly discovered evidence shows that defendants actively sought to sell Genta prior to the Notes Transaction. Quoting from Lyondell Chemical Co. v. Ryan, 970 A.2d 235, 242 (Del. 2009), the motion judge held that "'Revlon duties do not arise because a company is "in play.["] The duty to seek the best available price applies only when a company embarks on a transaction . . . that will result in a change of control.'" Here, the judge reasoned, plaintiffs' amended complaint could not support a Revlon claim because no change in control resulted from the Notes Transaction.

Given the facts alleged in the proposed amended complaint as well as the governing law, we hold that the judge should have permitted plaintiffs to file the amended complaint and permitted discovery to ensue. We acknowledge that the Revlon exception is limited, and that we may be simply delaying entry of an inevitable summary judgment. Here, however, construing the facts alleged in the proposed amended complaint and viewing those fact indulgently, we are satisfied that plaintiffs marshaled sufficient, albeit debatable, evidence that would establish a direct claim. For example, the innocent or illicit motives behind an amendment to the minutes is not readily determinable. In addition, a change of control was a real possibility, perhaps even probability, given the corporation's dire need for funds. Under these circumstances, plaintiffs should have been permitted to file the amended complaint.

Affirmed in part; reversed in part; and remanded for further proceedings. We do not retain jurisdiction.

I hereby certify that the foregoing is a true copy of the original on file in my office.

CLERK OF THE APPELLATE DIVISION