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IN THE SUPREME COURT OF THE STATE OF DELAWARE

JASON TERRELL, Plaintiff Below, Appellant, v. KIROMIC BIOPHARMA, INC., Defendant Below, Appellee.	)	No. 299,2022 On Appeal from the Court of Chancery of the State of Delaware C.A. No. 2021-0248-MTZ

APPELLEE'S ANSWERING BRIEF

November 7, 2022

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NATURE OF PROCEEDINGS

Plaintiff Dr. Jason Terrell ("Terrell") commenced the underlying action on March 22, 2021, by filing a verified complaint in Chancery Court against defendant Kiromic Biopharma, Inc. ("Kiromic"), seeking: (i) a declaratory judgment that he is entitled to exercise certain options allegedly granted to him under a December 2014 consulting agreement and January 2017 non-employee director agreement, and specific performance for Kiromic to reserve shares corresponding to those options; and (ii) a declaratory judgment that he was entitled to indemnification from Kiromic in connection with fees and costs incurred in this action. A010-A021.

On May 20, 2021, Kiromic moved to dismiss the verified complaint under Court of Chancery Rule 12(b)(6) for failure to state a claim. A093-A124. As to the claim for declaratory judgment in connection with alleged options, Kiromic argued, *inter alia*, that any such prior options were superseded by a release in a later options agreement that Terrell entered into with Kiromic in November 2017 (months after Terrell had joined Kiromic's board) as part of the board's effort to create a standardized equity incentive plan. As to the indemnification claim, Kiromic asserted that it failed as a matter of law because Terrell's suit was brought in his personal capacity.

On June 21, 2021, Terrell filed his opposition to the motion to dismiss. A125-A142. In that opposition, however, he voluntarily dismissed his indemnification

claim, leaving only the options-related declaratory judgment claim. Kiromic filed its reply brief on July 7, 2021. A143-A158.

Oral argument on the motion to dismiss was held before the Court of Chancery on October 20, 2021. A171-A202. During that argument, the Court invited the parties to submit further briefing on the issue of whether Section 15.1 of the November 2017 Stock Option Agreement between the parties—which invested the "Committee" (defined as a committee, composed of at least one director, tasked with administering Kiromic's equity incentive plan) with exclusive jurisdiction to resolve disputes regarding the interpretation of the agreement itself—impacted the Chancery Court's jurisdiction to resolve the parties' contract dispute. The parties simultaneously submitted letter briefs on the issue on November 15, 2021. A159-A170.

On January 20, 2022, the Court issued a letter decision on the motion to dismiss (attached as Exhibit A to Terrell's opening appellate brief (Trans. ID 68222479))[1] that instructed the parties to submit two questions Committee: (i) whether the Committee's exclusive jurisdiction to interpret the November 2017 Stock Options Agreement also extended to the release in the accompanying grant notice that was incorporated by reference into the Stock Options Agreement; and

[1] The Chancery Court's January 20, 2022 decision is cited herein as "Ex. A." Terrell's opening appellate brief is cited herein as "Br."

(ii) if so, whether the release in the grant notice superseded and extinguished any options granted to Terrell under prior agreements.

Thereafter, the parties agreed on special procedures to present the dispute to the Committee (which is Kiromic's compensation committee, composed of three independent directors) via letter briefs and exhibits. On July 21, 2022, following the parties' submissions of their respective letter briefs and exhibits, the Committee informed the parties via e-mail that it answered both questions in the affirmative.

On July 26, 2022, Kiromic's counsel submitted a joint letter to the Chancery Court on behalf of both parties informing the Chancery Court of the process the parties followed to submit the contract interpretation dispute to the Committee and the Committee's determinations. A203-A207. In response, the Chancery Court issued an order on August 2, 2022 (attached as Exhibit B to Terrell's opening appellate brief (Trans. ID 68222479)),[2] granting Kiromic's motion to dismiss.

Terrell filed his Notice of Appeal on August 23, 2022 (A208-A209), and filed his opening appellate brief with this Court on October 7, 2022.

This is Kiromic's answering brief.

[2] The Chancery Court's August 2, 2022 order is cited herein as "Ex. B."

SUMMARY OF ARGUMENT

1. Denied. Chancery Court correctly determined that the provision in question was not an arbitration provision, and therefore not subject to the heightened judicial scrutiny applied by this Court in *Worldwide Ins. Grp. v. Klopp*, 603 A.2d 788 (Del. 1992) (Terrell's lead case) and similar cases, which involved arbitration provisions. Rather, Chancery Court correctly determined that the provision of the stock options agreement that allowed Kiromic's compensation committee (composed of independent directors) was a non-arbitration alternative dispute resolution ("ADR") provision, and the scope of the provision determined the committee's authority, which the Chancery Court could not disturb as a matter of freedom of contract. *See, e.g.*, *Penton Business Media Holdings, LLC v. Informa PLC*, 252 A.3d 445 (Del. Ch. 2018). *See infra* Point I.C.1.

2. Denied. This Court's and the Chancery Court's jurisprudence hold squarely that parties may agree by contract to delegate exclusive authority to a non-arbitrator to interpret the underlying contract itself. *See, e.g.*, *Kuhn Construction, Inc. v. Diamond State Port Corp.*, 990 A.2d 393, 394–95 (Del. 2010); *Penton*, 252 A.3d at 448. Terrell was on the board when it approved the equity incentive plan (of which Terrell's November 2017 stock options agreement was a part) and the parties agreed that, with respect to the question of interpretation of the stock options agreement only, the Committee has exclusive jurisdiction, with all other legal and

factual questions to be decided by the courts. Chancery Court correctly determined that the parties vested the Committee with such exclusive interpretive jurisdiction. *See infra* Point I.C.1.

3. Denied. Chancery Court correctly determined that, per Section 15.1 of the Stock Options Agreement, the Committee held exclusive jurisdiction to interpret the release in Terrell's November 2017 grant notice and stock options agreement, and that Chancery Court was therefore without jurisdiction to consider those contract interpretation issues. *See infra* Point I.C.2. To the extent that this Court determines to review the underlying contract interpretation issues pursuant to its *de novo* review, Kiromic's position that the release in the grant notice superseded and extinguished all prior options agreements is correct as a matter of contract interpretation, and there was adequate consideration to support such release. *See infra* Point II.

STATEMENT OF FACTS

A. Terrell and Kiromic Enter into the Prior Agreements

On December 10, 2014, Terrell and Kiromic entered into a consulting agreement (the "Consulting Agreement"), under which Kiromic granted Terrell the option to purchase 500,000 shares of its common stock at a strike price of $0.50 per share in exchange for Terrell's consulting services. *See* A023-27.[3] The exercise term for the options under the Consulting Agreement was to expire December 10, 2024. *See* A027.

On January 23, 2017, Terrell and Kiromic entered into a "Non-Employee Director Agreement" (the "Jan. 2017 Agreement," and together with the Consulting Agreement, the "Prior Agreements"), under which Kiromic granted Terrell the option to purchase 500,004 shares of its common stock at a strike price of $0.17 per share in exchange for Terrell's services as a non-employee member of Kiromic's board. *See* A031-32. The exercise term under the Jan. 2017 Agreement was scheduled to expire on January 23, 2027. *Id.*

As Terrell acknowledges in his Complaint, he "served on Kiromic's board of directors from January 2017 to September 2019." A013 (Compl. ¶ 16). As described in the next section, this included the period in which Kiromic's board approved a new equity incentive plan, which included a new options grant to Terrell.

[3] All Appendix citations herein are to Terrell's opening brief appendix.

B. Terrell Enters into the November 2017 Agreement, Which Extinguishes His Prior Option Rights Under the Prior Agreements

In a "Notice of Stock Option Grant / 2017 Equity Incentive Plan," dated as of November 10, 2017 (defined above as the "Grant Notice"), and accompanying Stock Option Agreement (defined above as the "SOA") and equity incentive plan (the "Plan"), signed by Kiromic and Terrell, Kiromic granted Terrell the option to purchase 500,004 shares of Kiromic's common stock at a fixed price of $0.19 per share. *See* A034-35 (Grant Notice); A036-50 (SOA); A051-67 (Plan). The exercise term for these options is due to expire on November 9, 2027 (ten years from the grant date of November 10, 2017). *See* A034 (Grant Notice, at 1).

The Grant Notice contains a robust merger clause (set forth in a larger font size) providing that the Grant Notice supersedes all prior commitments or communications regarding options (the "Release"):

> By signing this Grant Notice, you acknowledge and agree that other than the Shares, ***you have no other rights to any other options, equity awards or other securities of the Company (except securities of the Company, if any, issued to you on or prior to the date hereof, if any), notwithstanding any commitment or communication regarding options, equity awards or other securities of the Company made prior to the date hereof***, whether written or oral, including any reference to the contrary that may be set forth in ***your offer letter, consultant agreement or other documentation with the Company*** or any of its predecessors.

A035 (Grant Notice, at 2) (emphasis added).

The SOA provides that it "shall be governed by and construed in accordance with the internal laws of the State of Delaware as such laws are applied to agreements between Delaware residents entered into and to be performed entirely within Delaware." A046 (SOA § 18).

The SOA, in turn, provides that disputes between Kiromic and Terrell regarding the interpretation of the Grant Notice, the SOA, or the Plan shall be resolved exclusively by a special committee (or the Board). Specifically, Section 15.1 of the SOA requires that "[a]ny dispute regarding the interpretation of this Agreement shall be submitted by Optionee or the Company to the Committee for review." A045 (SOA § 15.1). Section 15.1 further provides that "[t]he resolution of such a dispute by the Committee shall be final and binding on the Company and Optionee." (*Id.*).

The phrase "this Agreement" in Section 15.1 refers not only to the SOA itself, but also to Terrell's Grant Notice, the Plan, and any exercise agreement. Section 15.2, entitled "Entire Agreement," provides explicitly that "[t]he Plan, the Grant Notice and the Exercise Agreement are each incorporated herein [that is, into the SOA] by reference. . . ." A045 (SOA § 15.2). As further confirmation that the Grant Notice and Plan are part and parcel of the SOA, the SOA's recitals provide that "[c]apitalized terms not defined in this Agreement shall have the meaning ascribed

to them in the Company's 2017 Equity Incentive Plan, as amended from time to time . . . , or in the Grant Notice, as applicable." A037 (SOA, at page 1).

The term "Committee" in Section 15.1 is not defined in the SOA itself, but is defined in the Plan as "the committee created and appointed by the Board to administer this Plan, or if no committee is created and appointed, the Board." *See* A064 (Plan § 14). To the extent that the Board creates such a committee, it must include "at least one member of the Board." A062 (Plan § 12.2).

Kiromic's Compensation Committee, as presently constituted, satisfies the Plan's definition of "Committee" because it is comprised of three independent directors appointed by the Board to administer the Company's incentive compensation and equity-based plans. *See* A167 (11/15/22 Kiromic supplemental letter brief) ("[S]uch a committee—the compensation committee, which is composed of three independent directors, and administers the Plan—has existed since 2020.") (citing Kiromic Compensation Committee Charter at 1, 4, *available at* https://ir.kiromic.com/static-files/9c1a79cb-7ed8-41a6-b755-174908035a77).

C. The Present Dispute

In September 2019, Terrell resigned from Kiromic's board. A014 (Compl. ¶ 26). On March 22, 2021, Terrell commenced the underlying action against Kiromic with the filing of a verified complaint, seeking, among other things, a declaration that he is entitled to exercise options under the Prior Agreements, as well

as under the November 2017 Agreement. *See* A010-21 (Terrell complaint). Kiromic then filed a Motion to Dismiss, which was briefed in the normal course. *See* A093-124 (Kiromic motion and opening brief); A125-142 (Terrell answering brief); A143-158 (Kiromic reply).

Oral argument on the motion was held before the Chancery Court on October 20, 2021. *See* A171-A202 (transcript). During argument, the Chancery Court invited the parties to submit supplemental briefing on the question of whether Section 15.1's delegation of exclusive interpretive authority to the Committee deprived the Chancery Court of jurisdiction over that question. *See* A201. The parties submitted simultaneous letter briefs on the issue to the Chancery Court on November 15, 2021. *See* A159-164 (Terrell letter brief); A165-170 (Kiromic letter brief).

On January 20, 2022, the Chancery Court issued a letter decision to the parties on the motion to dismiss (the "Decision"). *See* Ex. A. The Chancery Court determined in the Decision that it is for the Committee to decide whether (i) Section 15.1 of the SOA gives the Committee the authority to interpret the Grant Notice, and (ii) if so, whether the Release in the Grant Notice superseded and nullified Terrell's options under the Prior Agreements. *See* Ex. A, at 17. The Chancery Court directed the parties to submit these issues to the Committee and "inform the Court of the

Committee's decision(s)." *Id.* Pending receipt of the Committee's decision(s), the Chancery Court stayed the action. *See id.*

Thereafter, as counsel subsequently informed the Chancery Court, the parties agreed on *ad hoc* procedures for submitting the contract interpretation issues to the Committee via letter briefs and exhibits, given that the SOA did not contain procedures for submission of disputes to the Committee. *See* A203-A204 (7/26/22 joint letter from Kiromic's counsel to Chancery Court). The parties' respective counsel submitted their letter briefs to the Committee on March 31, 2022. *Id.* at A204. On July 21, 2022, the Committee (through its separate counsel) issued determinations on the contract interpretation questions posed via e-mail:

> i. the Committee has the exclusive authority, pursuant to Section 15.1 of Dr. Jason Terrell's Stock Option Agreement with Kiromic BioPharma, Inc., to interpret Dr. Terrell's November 2017 "Notice of Stock Option Grant"; and
>
> ii. the merger clause in Dr. Terrell's grant notice supersedes and nullifies any option rights Dr. Terrell may have had under Dr. Terrell's prior agreements with Kiromic.

A206.

The parties, through Kiromic's counsel, thereafter notified the Chancery Court of the Committee's determinations via letter dated July 26, 2022. *See* A203-207. On August 2, 2022, the Chancery Court issued an order granting Kiromic's

motion to dismiss based on the reasoning in its prior Decision and the Committee's determinations. *See* Ex. B. Terrell thereafter mounted this appeal. A208-A209.

ARGUMENT

The Chancery Court properly framed the inquiry regarding its jurisdiction as dependent on whether Section 15.1 of the SOA is an arbitration or non-arbitration ADR provision. To the extent that Section 15.1 is a non-arbitration provision, the heightened judicial review applicable to arbitration provisions does not apply, and the Chancery Court was required, as a matter of the parties' contractual intent, to defer to the Committee as to the meaning of the SOA—specifically, whether the Grant Notice was part of the SOA, and if so, whether the Grant Notice extinguished and superseded all of Terrell's prior alleged options agreements. Terrell's arguments that, as a matter of law, non-arbitral private parties such as the Committee may not resolve contract interpretation issues is meritless under this Court's and the Chancery Court's prior jurisprudence, under which parties may contract to allow such a private party to interpret the underlying contract. *See infra* Point I.

Terrell nonetheless attempts, in reliance on this Court's *de novo* review, to sidestep the Chancery Court's determinations and have this Court decide the underlying contract interpretation issues that the Chancery Court properly determined were for the Committee to decide—and that the Committee appropriately decided against Terrell. Such review by this Court is not warranted: Terrell approved the equity incentive plan (of which the Grant Notice and SOA were a part) when he was on the Kiromic board, and should be held to the bargain.

Nonetheless, to the extent that this Court determines to review the underlying contract interpretation issues, Kiromic's position that the Release superseded the Prior Agreements (and was entered into for good consideration) should be vindicated as a matter of law. *See infra* Point II.

I. THE COURT OF CHANCERY CORRECTLY DETERMINED THAT SECTION 15.1 OF THE SOA WAS AN ENFORCEABLE NON-ARBITRAL DISPUTE RESOLUTION PROVISION THAT DELEGATED EXCLUSIVE CONTRACT INTERPRETATION AUTHORITY TO THE COMMITTEE

A. Questions Presented

The Court of Chancery determined that, per Section 15.1 of the SOA, it was without jurisdiction to review the contract interpretation question of whether (i) the Grant Notice was part of the SOA, and if so, (ii) whether the Release in the Grant Notice superseded and extinguished options grants under the Prior Agreements and—upon the Committee answering both of these questions in the affirmative—granted Kiromic's motion to dismiss Terrell's complaint for failure to state a claim. Did Chancery Court correctly defer to the Committee's determinations on these contract interpretation issues?

The parties briefed the applicability of Section 15.1 of the SOA to the Chancery Court's jurisdiction via letter briefs. *See* A159-170.

B. Scope of Review

A Vice Chancellor's decision to grant a motion to dismiss is reviewed *de novo*. *See, e.g.*, *Norton v. K-Sea Transportation Partners L.P.*, 67 A.3d 354, 359–60 (Del. 2013) ("We review the Vice Chancellor's decision to grant a motion to dismiss under Court of Chancery Rule 12(b)(6), *de novo*.") (citation omitted).

C. Merits of the argument

Terrell concedes that the reviewability of the Committee's determination

hinges on whether Section 15.1 is an arbitration or a non-arbitration dispute resolution provision. *See* Br. 20 (arguing that "the grant of power to the Committee to unilateral[l]y resolve all questions of law arising under the interpretation of the SOA was a creature of an arbitration clause—not an expert designation—and its substantive scope was thus subject to judicial review"). This settles the question of whether Section 15.1 is an unconscionable provision as well, as Terrell's lead case in support of unconscionability—*Worldwide Ins. Grp. v. Klopp*, 603 A.2d 788, 791 (Del. 1992) (*see* Br. 3, 15)—did not involve an expert determination clause, but rather an "arbitration provision"—and the question there was whether the provision, "which permits either party to demand trial *de novo* from the uninsured/underinsured arbitrators' decision only if the arbitrators' award exceeds the financial responsibility limits of the State of Delaware, [was] contrary to public policy." *Worldwide*, 603 A.2d at 789. As the Chancery Court found here, and as set forth below, Section 15.1 is not an arbitration clause, and it was proper for the Chancery Court to defer to the Committee's determinations as to the meaning of the scope of both Section 15.1 itself as well as whether the Release in the Grant Notice extinguished Terrell's prior options.

1. Section 15.1 is a Non-Arbitral ADR Provision

Both parties, as well as the Chancery Court, agree that the Vice Chancellor Laster's scholarly opinion in *Penton Business Media Holdings, LLC v. Informa PLC*,

252 A.3d 445 (Del. Ch. 2018), supplies the framework for distinguishing between an arbitration and non-arbitration contractual provision, and reflects this Court's and other Delaware courts' prior jurisprudence on the issue. "Under Delaware law, '[w]hen interpreting a contract, the role of a court is to effectuate the parties' intent.'" *Id.* at 461 (quoting *Lorillard Tobacco Co. v. Am. Legacy Found.*, 903 A.2d 728, 739 (Del. 2006)). With respect to contractual dispute resolution mechanisms, "Delaware decisions have maintained the distinction between an arbitration and an expert determination" (*id.* at 456), and have, accordingly, not "applied arbitral principles to all contractual dispute resolution mechanisms. This outcome comports with Delaware's position as 'a freedom of contract state, with a policy of enforcing the voluntary agreements of sophisticated parties in commerce.'" *Id.* at 458 (quoting *Personnel Decisions, Inc. v. Bus. Planning Sys.*, 2008 WL 1932404, at *6 (Del. Ch. May 5, 2008)). As Vice Chancellor Laster explained in *Penton*:

> An expert determination—whether by an appraiser, an auditor, or a different type of expert—is not an arbitration unless the parties specifically "designate that expert as an arbitrator for that purpose," thereby invoking the body of law governing arbitrators. The court interprets and enforces the contract provisions governing the expert determination; the court does not apply arbitral principles.

Id. at 458-459 (citation omitted). Indeed, Vice Chancellor Laster in *Penton* explicitly rejected the notion that "arbitral principles, including the doctrines of

substantive and procedural arbitrability, always apply whenever parties have selected a private third-party to decide a dispute." *Id.* at 454.

Whether a dispute resolution mechanism in a contract is or is not an arbitration provision "presents a question of contract interpretation." *Id.* at 461. "Arbitration provisions typically broadly encompass the entire legal and factual dispute between the parties." *Ray Beyond Corp. v. Trimaran Fund Mgmt., L.L.C.*, 2019 WL 366614, at *8 (Del. Ch. Jan. 29, 2019) (citation omitted); *accord Penton*, 252 A.3d at 463-64. Moreover, "[a]rbitration provisions typically include procedural rules affording each party the opportunity to present its case; indeed, this is viewed as a defining characteristic of arbitration provisions." *Ray Beyond*, 2019 WL 366614, at *7 (citation omitted); *see also Penton*, 252 A.3d at 463 ("[a]ppraisal proceedings are . . . attended by a larger measure of informality and appraisers are not bound to the strict judicial investigation of an arbitration") (citation and internal quotation marks omitted).

As noted, Section 15.1 provides simply that the Committee has the exclusive role to interpret "this Agreement," a defined term that—per Section 15.2—includes the Grant Notice. (A045.) Neither the SOA nor any of the documents incorporated by reference therein (including the EIP or the Grant Notice) specify procedural rules for the conduct of the Committee's interpretation. To the contrary, Kiromic's counsel's letter to the Chancery Court apprising it of the Committee's determination

explained that the parties agreed to *specialized, ad hoc* rules for submitting their dispute to the Committee—a recognition that the SOA itself did not contain such rules:

> Following issuance of the Decision, the parties agreed that they would each (through their respective counsel) submit letter briefs (not to exceed 20 pages, with no limitation on exhibits) to the Committee, addressing both the threshold issue as to the scope of Section 15.1 and the question of whether the Release superseded Dr. Terrell's prior options agreements. The parties submitted their respective letter briefs and exhibits, via counsel, to the Committee on March 31, 2022.

A204. Accordingly, Section 15.1, by its terms, is not an arbitration provision.

Despite this, Terrell makes two main arguments in support of the notion that Section 15.1 is an arbitration provision. First, Terrell argues that Section 15.1 cannot be a non-arbitration provision because, according to Terrell, non-arbitrators cannot decide legal issues such as contract interpretation. *See* Br. 20-22. Second, Terrell maintains that Section 15.1 is not a non-arbitration provision because it purportedly gives the Committee the authority to resolve "the entire controversy between the parties." *Id.* at 23. Neither contention is correct.

a. Parties Can Contract to Assign a Non-Arbitrator Exclusive Jurisdiction to Interpret the Underlying Contract

Penton and this Court's own precedent make clear that a non-arbitrator private party may, per contract, resolve legal questions such as the interpretation of the

contract itself. "Parties *could* give an expert the authority to interpret a contract." *Penton*, 252 A.3d at 448 (emphasis added). Indeed, "[t]here is no general principle either that the expert *always* has exclusive jurisdiction to decide the meaning of the terms of the contract, or that the expert *never* has exclusive jurisdiction to do so. Rather, [i]n each case it is necessary to examine the contract itself in order to decide what the parties intended should be a matter for the exclusive jurisdiction of the expert." *Id.* at 465 (footnotes and internal quotation marks omitted).

This Court has previously held that a dispute resolution provision that gave a referee interpretive authority over underlying contract documents was not an arbitration provision. Specifically, in *Kuhn Construction, Inc. v. Diamond State Port Corp.*, the parties agreed to the following referee clause:

> The Director, or his designee, shall act as referee in all questions arising under the terms of the Contract between the parties hereto, and the Decision of the Director shall be final and binding. On all questions concerning the interpretation of Plans and Specifications, the acceptability, quality and quantity of materials or machinery furnished and work performed, the classification of material, the execution of the work and the determination of payment due or to become due, the decision of the Director, or his designee, shall be final and binding.

990 A.2d at 394–95. Notwithstanding that the agreement gave the referee exclusive authority "in all questions arising under the terms of the Contract" as well as over "all questions concerning the interpretation of Plans and Specifications," this Court

held that the dispute resolution provision was not an arbitration clause because "the terms in the referee clause did not clearly and unambiguously indicate the intention to arbitrate." *Id.* at 394-395, 397. Notably, Chancery Court discussed *Kuhn* in its decision as authority supporting its determination that Section 15.1 is not an arbitration provision (Ex. A at 12 n.35), but Terrell does not discuss it at all in his Opening Brief.

Here, as described *infra* Point I.C.2, Section 15.1 squarely assigned to the Committee exclusive authority to interpret the SOA, including the Grant Notice. The parties thus clearly evinced their intent to have the Committee decide legal questions of contract interpretation, on the one hand, but that the Committee's deliberative process should not be an arbitration.

b. The Committee Was Not Given Authority to Decide the "Entire Controversy" Between the Parties

Terrell's contention that Section 15.1 is an arbitration provision on the grounds that it allows the Committee to decide the "entire controversy" between the parties does not pass muster. As noted, the test for assessing whether a dispute resolution provision resolves the "entire controversy" depends not only on whether it necessarily resolves contract interpretation issues, but also on whether it resolves "the entire legal and *factual* dispute between the parties." *Ray Beyond*, 2019 WL 366614, at *8.

Terrell omits, however, that besides the meaning of Section 15.1 and the Grant Notice (both of which are admittedly contract issues that furnished grounds for the Chancery Court to dismiss the Complaint), there were other factual disputes between the parties that the Committee did not reach and that, if this dispute were to be litigated beyond the pleadings stage, would be in issue.

For example, the parties dispute whether, if the options under the Prior Agreements were not extinguished, whether those options are subject to reduction based on reverse stock splits subsequently undertaken by Kiromic: Terrell's position is that only the options granted under the Grant Notice and SOA were subject to adjustment based on the reverse stock splits, but not the options granted under the Prior Agreements. Kiromic, however, maintains that all options granted are subject to reverse stock splits, as it was always the intent of the parties that Terrell would have the option to own a specific percentage of company stock, not an absolute number of shares. *See* A015 (Compl. ¶¶ 29-30.)

Likewise, there is a further factual and legal dispute between the parties as to whether, even if the Grant Notice did not categorically extinguish all prior options, whether the January 2017 and November 2017 agreements were intended to be separate options agreements. Though Terrell disagrees, it is Kiromic's position that these two agreements pertained to the same options, as they both granted options for

the same amount of shares—500,004. *See* A198-99. This issue, however, does not depend on the meaning of the Grant Notice and SOA.

Accordingly, Section 15.1 does not *per se* vest the Committee with exclusive jurisdiction to resolve *all* legal and factual questions that may arise between the parties: it gives the Committee only jurisdiction to address the narrow question of contract interpretation. While that question may, in some cases (such as this one), be dispositive, it does not mean that Section 15.1 rises to the level of an arbitration provision.

2. The Parties Agreed in the SOA that the Committee Would Have Exclusive Authority to Interpret the SOA Itself, Including the Grant Notice

As noted, whether a dispute resolution provision allows the non-arbitrator to construe the scope of the contract and the dispute resolution provision itself "presents a question of contract interpretation." *Penton*, 252 A.3d at 465. The Chancery Court correctly determined that, per the plain language of the SOA, the Committee's exclusive authority under Section 15.1 of the SOA to review and resolve disputes "regarding the interpretation of this Agreement" extends to disputes regarding the interpretation of the Grant Notice. This is so for two reasons.

First, Section 15.2, which immediately follows Section 15.1 (and is part of the same article of the SOA), provides explicitly that "[t]he Plan, the Grant Notice and the Exercise Agreement are each incorporated herein [that is, into the SOA] by

reference. . . ." A045 (SOA § 15.2.) Put another way, Section 15.2 (which itself is entitled "Entire Agreement") was inserted into the SOA to address the very question of whether the Grant Notice and Plan are part of "this Agreement." Section 15.2 unambiguously teaches that they are.

Second, as a practical matter, the SOA, Grant Notice, and Plan form a unified, integrated agreement. It is literally impossible to interpret the SOA *without* considering the Grant Notice and the Plan: indeed, the SOA's recitals provide that "[c]apitalized terms not defined in this Agreement shall have the meaning ascribed to them in the Company's 2017 Equity Incentive Plan, as amended from time to time . . . , or in the Grant Notice, as applicable." A037 (SOA, at p.1). For example, the capitalized term "Committee," which appears in Section 15.1, is not defined in the SOA itself, but rather only the Plan. The structure of the SOA thus confirms, as Section 15.2 says outright, that the Grant Notice and Plan are part and parcel of "this Agreement."

Terrell cannot evade the agreement he made with Kiromic regarding who would decide the meaning of the Grant Notice. Terrell's own Complaint confirms that he was already on the board when the SOA and Grant Notice were signed, and was therefore part of the company's leadership that endorsed the EIP. *See* A013 (Compl. ¶ 16) ("Dr. Terrell served on Kiromic's board of directors from January 2017 to September 2019 . . . ."). Moreover, far from consisting of Kiromic insiders,

the members of Kiromic's compensation committee are independent directors. *See* A167 (Kiromic's supplemental brief, noting that the "Committee" exists and is "the compensation committee, which is composed of three independent directors").

Accordingly, it was proper for the Committee to resolve the two contract interpretation matters at issue and for the Chancery Court to dismiss the action upon receipt of the Committee's determinations.

II. IN THE ALTERNATIVE, CHANCERY COURT'S DISMISSAL OF THE COMPLAINT SHOULD BE AFFIRMED BECAUSE THE GRANT NOTICE UNAMBIGUOUSLY EXTINGUISHED ANY OPTIONS UNDER ANY PRIOR AGREEMENTS BETWEEN TERRELL AND KIROMIC

A. Questions Presented

To the extent that it was error for the Chancery Court not to have reviewed the Committee's contract interpretation determinations, notwithstanding Section 15.1 of the SOA, did (i) the Release in the Grant Notice unambiguously supersede and extinguish any options Terrell may have been granted under the Prior Agreements and, if so, (ii) was there adequate consideration for such Release, justifying Chancery Court's grant of Kiromic's motion to dismiss on these grounds?

The parties briefed these issues in their original briefing on the motion to dismiss. *See* A099-158.

B. Scope of Review

A Vice Chancellor's decision to grant a motion to dismiss is reviewed *de novo*. *See, e.g.*, *Norton*, 67 A.3d at 359–60 ("We review the Vice Chancellor's decision to grant a motion to dismiss under Court of Chancery Rule 12(b)(6), *de novo*.") (citation omitted).

C. Merits of the argument

Had Terrell wanted Chancery Court to reconsider its position regarding the scope and impact of Section 15.1 of the SOA, and opine on the ultimate contract interpretation issues (which the Committee has already passed on), he could have

sought reargument in the Chancery Court. *Cf.* Ct. Ch. R. 59(f) ("A motion for reargument setting forth briefly and distinctly the grounds therefor may be served and filed within 5 days after the filing of the Court's opinion or the receipt of the Court's decision."). Terrell, however, declined to do so, and is pressing for this Court to provide the first judicial pronouncements on these fundamental contract interpretation issues on appeal.

Kiromic respectfully submits that no Delaware court need ever reach these issues, given Section 15.1 of the SOA and the Committee's prior determinations, and further submits that, to the extent this Court disagrees, the better option is remand to the Chancery Court to consider and rule on those issues. Nonetheless, in recognition of this Court's *de novo* scope of review on this appeal, Kiromic herein explains why, as a matter of contract interpretation under Delaware law, the Committee's decisions were correct and the Chancery Court's grant of the motion to dismiss should be affirmed on that basis.

1. The Grant Notice, By Its Terms, Superseded the Prior Agreements

Under Delaware law, an individual's rights with respect to stock options are determined solely by reference to the terms of the underlying stock option agreements. *See Reis v. Hazelett Strip-Casting Corp.*, 28 A.3d 442, 478 (Del. Ch. 2011) ("Until the warrant or option is exercised, the underlying shares are not issued, and *the warrant or option holder's rights are entirely contractual*.") (citation

omitted; emphasis added). Accordingly, stock options are governed by the general rules of contract interpretation under Delaware law. *See, e.g.*, *US HF Cellular Commc'ns, LLC v. Stiegler*, 2017 WL 4548461, at *7 (Del. Ch. Oct. 12, 2017) (finding that "the clear and unambiguous language of these agreements reveal[ed]" the terms of the stock options at issue); *Draini v. Naseeb Networks, Inc.*, 2017 WL 2544887, at *4 (Del. Ch. June 13, 2017) (applying Delaware canons of contract construction to employment contract and related stock option agreement).

Delaware courts "first and foremost" will look to the four corners of a stock option agreement to determine "'whether the intent of the parties can be [established] from its express language.'" *US HF Cellular*, 2017 WL 4548461, at *5 (citation omitted); *see also In re Viking Pump, Inc.*, 148 A.3d 633, 648 (Del. 2016) ("Under Delaware law, which governs the [ ] Stock Agreement, courts interpreting a contract will give priority to the parties' intentions as reflected in the four corners of the agreement, construing the agreement as a whole and giving effect to all its provisions.") (citation and internal quotation marks omitted). To do so, they will "apply the objective theory of contracts, giving 'words their plain meaning unless it appears that the parties intended a special meaning.'" *HUMC Holdco, LLC v. MPT of Hoboken TRS, LLC*, 2020 WL 3620220, at *6 (Del. Ch. July 2, 2020) (citation omitted); *see also US HF Cellular*, 2017 WL 4548461, at *5 (noting that "Delaware is more contractarian than other states") (citation omitted). "'The presumption that

the parties are bound by the language of the agreement they negotiated applies with even greater force *when the parties are sophisticated entities that have engaged in arms-length negotiations*.'" *Id.* (emphasis added) (citation omitted).

As especially relevant to this case, when a stock option agreement provides that it supersedes prior written or oral contracts regarding options, it effectively terminates all previous contractual commitments. *See Draini*, 2017 WL 2544887, at *4 (finding that exit agreement that addressed stock options that were the subject of a prior stock agreement "explicitly 'supersedes and terminates any and all previous agreements'" among the parties, including the prior stock agreement) (citation omitted); *see also Napolitano v. Town Sports Int'l Holdings Inc.*, 2007 WL 1521217, at *4 (E.D. Pa. May 23, 2007) (holding that when "the format, construction and general terms of the contract indicate that the prior duties on [the corporation] to issue options [were] entirely replaced by the newly created duties," the prior duties are extinguished).

Here, the Grant Notice contains a clear and unambiguous merger clause—*i.e.*, the Release—that provides explicitly that it supersedes and extinguishes the Prior Agreements:

> By signing this Grant Notice, you acknowledge and agree that other than the Shares, ***you have no other rights to any other options, equity awards or other securities of the Company (except securities of the Company, if any, issued to you on or prior to the date***

> ***hereof, if any)***, ***notwithstanding any commitment or communication regarding options, equity awards or other securities of the Company made prior to the date hereof***, whether written or oral, including any reference to the contrary that may be set forth in your offer letter, consultant agreement or other documentation with the Company or any of its predecessors.

A035 (emphasis added).

The Prior Agreements qualify as a "commitment or communication regarding options . . . of the Company made prior to the date hereof, whether written or oral." *Id.* If that were not enough, the Consultant Agreement (the first of the Prior Agreements) was a "consultant agreement . . . with the Company or any of its predecessors," which is squarely superseded. *See id.*

Accordingly, the Grant Notice, by its terms, extinguishes and supersedes "any options" set forth in the Prior Agreements, and the only options Terrell may exercise are those set forth in the Grant Notice.

2. <u>The Options Under the Prior Agreements Are Not "Securities of the Company . . . Issued to" Terrell Prior to the Grant Notice</u>

On appeal, as he did before Chancery Court, Terrell maintains that the Prior Agreements were not affected by the Grant Notice because the Release contains a parenthetical exception for "securities of the Company, if any, issued to you on or prior to the date hereof." *See* Br. 35. This interpretation, however, is contrary to the plain wording of the Release.

First, the plain reference of "securities of the Company . . . issued to you" is to shares of Kiromic *stock* that were already issued—including previously exercised options. This is confirmed by the fact that the term "issued" is *never* used in the SOA (of which the Grant Notice is a part) with respect to options, but only with respect to actual shares of stock. *See, e.g.*, A039 (SOA § 4.5) ("the Company shall *issue the Shares* issuable upon a valid exercise of this Option") (emphasis added); *id.* § 5 (referencing "[t]he exercise of this Option and the *issuance* and transfer of Shares") (emphasis added).[4] Conversely, the Grant Notice and SOA use the term "grant" exclusively to refer to the initial conferral of the option right—and do so no less than 110 times. *See, e.g.*, A034 (Grant Notice, at 1) ("By their signatures below, Optionee and the Company agree that this Option is *granted* . . . ."); A037 (SOA § 1) ("The Company hereby *grants* to Optionee an option . . . ."). The carve-out in the Grant Notice's Release for "securities of the Company, if any, issued" thus refers only to shares of stock that had been issued to the optionee prior to the option grant; those actually issued shares are (quite sensibly) not affected by the Grant Notice.

[4] This is consistent with Delaware case law, which provides that, "[u]ntil the warrant or option is exercised, the underlying *shares* are not *issued*." *See Reis*, 28 A.3d at 478 (emphasis added) (citing *Corp. Prop. Assocs. 14, Inc. v. CHR Hldg. Corp.*, 2008 WL 963048, at *4 & nn.27-33 (Del. Ch. Apr. 10, 2008); *Feldman v. Cutaia*, 2006 WL 920420, at *6 n.37 (Del. Ch. Apr. 5, 2006)).

Second, Terrell's interpretation that "securities of the Company . . . issued to you" encompasses prior (unexercised) options would completely negate and render meaningless the balance of the Release. To determine the parties' contractual intent under Delaware law, "'courts must read the specific provisions of the contract in light of the entire contract.'" *HUMC Holdco*, 2020 WL 3620220, at *6 (citation omitted). This whole-text canon of contract interpretation "'stems from the theory that context is the primary determinant of meaning.'" *Id.* (citation omitted).

Here, the Release provides that Terrell has no "other rights to any other options . . . notwithstanding any *commitment* or communication . . . whether written or oral, *including any reference to the contrary* that may be set forth in *your* offer letter, *consultant agreement or other documentation* with [Kiromic]." A035 (Grant Notice, at 2) (emphasis added). Plainly, this language encompasses prior "commitment[s]" to issue "options" pursuant to agreements—just like the Prior Agreements. If "securities of the Company . . . issued to you" is limited to shares of stock actually issued to Terrell, then it is consistent with the balance of the Release: If Terrell had exercised his options and received stock certificates, then the Release would have had no effect on those shares of stock, but otherwise supersedes and extinguishes any unexercised options.

Under Terrell's reading of the parenthetical carve-out for "securities of the Company . . . issued to you," however, there is no sort of option "commitment,"

whether exercised or unexercised, that is superseded by the Grant Notice. Terrell's interpretation would invalidate and render superfluous the balance of the Release, and should therefore be rejected.

Terrell's argument that the carve-out in the Release for "securities of the Company, if any, issued to you on or prior to the date hereof, if any" captures prior option grants because the federal Securities Exchange Act of 1934 defines "security" to include "option[s]" (*see* Br. 30 (citing 15 U.S.C. § 78c(a)(10)) is a red herring. The issue is not how the single word "security" is defined in federal securities statutes, but rather what the contractual meaning of the *complete* phrase "securities of the Company, if any, issued to you on or prior to the date hereof, if any" in the Release is. This requires the Court in the first instance to look to the plain meaning of the contract language and its context within the "four corners of the agreement, construing the agreement as a whole and giving effect to all its provisions." *In re Viking Pump, Inc.*, 148 A.3d at 648 (citation omitted)..

Accordingly, as a matter of plain language interpretation, Terrell's contract construction fails.

3. The Release of the Prior Agreements Was Commercially Reasonable and Made for Adequate Consideration

Terrell argues that the Release, if given Kiromic's interpretation, would fail for lack of consideration and commercial unreasonableness. *See* Br. 32-35. The basic premise of this argument is that no reasonable optionee would agree to

renounce options to purchase 1 million shares (under the Prior Agreements) in exchange for options to purchase a mere 500,000 shares (under the Grant Notice).

The argument, however, is predicated on a misunderstanding of what consideration is deemed sufficient under Delaware law, as well as incorrect factual assumptions (even taking the allegations in the Complaint and documents incorporated by reference as true). Specifically, Terrell ignores the benefit he gained through the Grant Notice in the form of (i) a lower exercise price per share, and (ii) a longer exercise period. This was a rational deal on Terrell's part, given that he was a member of the board at the time and had an interest not only in personal gain but also in the well-being of the company through the 2017 equity incentive plan that he and his fellow directors approved at the time.

a. Delaware Law Principles of Consideration and Contract Modification

"'Even if the consideration exchanged is grossly unequal or of dubious value, the parties to a contract are free to make their bargain.'" *Moscowitz v. Theory Ent. LLC*, 2020 WL 6304899, at *16 (Del. Ch. Oct. 28, 2020) (quoting *Acker v. Transurgical, Inc.*, 2004 WL 1230945, at *4 (Del. Ch. Apr. 22, 2004)); *id.* at *2 ("Delaware law presumes the plaintiff is bound by the language of the agreements he signed, no matter how draconian. It affords no occasion to weigh the sufficiency of the consideration the plaintiff received (0.1% equity) against the company's rights to repurchase all of his equity . . . The agreements unambiguously grant the company

the right to repurchase plaintiff's equity and extinguish his status as a member"). "Absent fraud or unconscionability, the adequacy of consideration is not a proper subject for judicial scrutiny." *Id.* at *16; *see also id.* at **13-15 (rejecting plaintiff's assertion that "the Incentive-1 Units were not consideration for the Award Agreement because he already owned those Units when he executed the Award Agreement" because the "clear and unambiguous" contract terms "d[id] not reflect . . . [plaintiff's] concern that the 0.1% stake was inadequate consideration for the significant enumerated consequences").

"The value of an option has two components: (i) intrinsic value, which is the market value of the option at any specific moment in time; and, (ii) time value, which is the value attributable to the option's potential to appreciate in the future." *AT&T Corp. v. Lillis*, 953 A.2d 241, 244 n.2 (Del. 2008). When "old options [are] replaced with new options because the old (underlying) stock is being replaced with new (underlying) stock . . . by its very nature, the 'economic position' of the options will invariably incorporate the expected time value of the new options." *Id.* at 254-55; *see also In re Activision Blizzard, Inc. S'holder Litig.*, 124 A.3d 1025, 1067 (Del. Ch. 2015) (because of "the time -value of money, stockholders would not be

indifferent between $40 million in cash paid to them in 2014 and $63.5 million paid to Activision in 2015", and this benefit would be considered adequate).[5]

With respect to waiver or modification of a prior contract right, "the Delaware Supreme Court [has] ruled that all rights or privileges to which a person is legally entitled under a contract which are intended for his sole benefit, may be waived whether those rights are secured by contract or conferred by statute." *Components, Inc. v. Western Elec. Co.*, 267 A.2d 579, 582 (Del. 1970) (citing *Hirzel v. Silker*, 156 A. 360, 362 (Del. 1930)). Thus, in *Components*, the Delaware Supreme Court held that a licensor's "written and signed" agreement by letter to "two reductions in royalty [payments] . . . were therefore binding upon it," even though the letter was not counter-signed by the licensee, and therefore "constitute[d] amendments of the original [license] agreement." *Id.* at 581.[6]

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[5] *Accord Farina Focaccia & Cucina Italiana, LLC v. 700 Valencia St. LLC*, 2016 WL 5672961, at *11 (N.D. Cal. Oct. 2, 2016) ("'the time within which an option must be exercised . . . cannot be extended beyond that provided in the contract because to hold otherwise would give the optionee, not the option he bargained for, but *a longer and therefore more extensive option*'") (citation omitted; emphasis added); *Institutional Mgmt., Inc. v. Peck*, 2002 WL 31875548, at *4 (N.D. Ill. Dec. 24, 2002) (finding that the "clear and unambiguous language of [the writing] plainly indicate[d] that the terms of the agreement had been renegotiated for new consideration: Peck now had more time to secure the money needed to redeem the stock from PMG and Peck agreed to pay an additional premium to PMG should he chose to exercise the option").

[6] The court noted that Delaware law on this issue was the same as New York law (which governed the license agreement). *See Components*, 267 A.2d at 582 ("apart from the New York statute, the law is to the same effect generally and, particularly,

b. The Release in the Grant Notice of the Prior Agreements Was Supported by Adequate Consideration and Was Commercially Reasonable

As set forth above, Terrell unambiguously waived any prior option rights set forth in the Prior Agreements by signing the Grant Notice. In addition, to the extent that new consideration was required, the Grant Notice was indeed supported by sufficient consideration because it improved the terms of Terrell's option rights over and above those set forth in the Prior Agreements. Moreover, Terrell approved his own agreement as part of the overall equity incentive plan voted on by the board in 2017.

First, according to the Complaint, the Consulting Agreement granted Terrell options to purchase 500,000 shares of Kiromic common stock at a price of $0.50 per share. A012 (Compl. ¶ 11.) That was a relatively high exercise price. Indeed, after factoring in the reverse stock splits that have taken place since 2014, that $0.50/share exercise price would correspond to $17.50/share today. The Grant Notice, in

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in Delaware"). Under the New York statute applicable to the parties' contract in *Components* (Section 5-1103 of the General Obligations Law), "An agreement, promise or undertaking to change or modify, or to discharge in whole or in part, any contract . . . shall not be invalid because of the absence of consideration, provided that the agreement, promise or undertaking changing, modifying, or discharging such contract . . . shall be in writing and signed by the party against whom it is sought to enforce the change, modification or discharge, or by his agent." *Id.* at 581 (internal quotation marks omitted). As noted, this Court in *Components* deemed this New York statutory provision to be consistent with Delaware contract law.

contrast, furnished Terrell with options to purchase 500,004 shares at an exercise price of $0.19/share (adjusted to reflect further reverse stock splits)[7]—*i.e.*, less than *half* of the stated exercise price under the Consulting Agreement. *See* A014 (Compl. ¶ 22).

Second, the Grant Notice contains a longer exercise period than under either of the Prior Agreements. As described *supra*, the exercise term for the Consulting Agreement was scheduled to expire in December 2024 and the one for the Jan. 2017 Agreement in January 2027. The exercise term for the options in the Grant Notice extends beyond both of those expiration dates to November 2027, giving Terrell additional time and opportunity to unlock greater value from his options.[8]

Agreement 3 thus conferred on Terrell new and sufficient consideration, which improved on (and therefore supported replacing) Agreements 1 and 2. Given that Agreement 3 is clear on its face and its consideration is adequate, Kiromic

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[7] It is undisputed that the options granted to Terrell under the Grant Notice were adjusted by the reverse stock splits, such that Terrell now has the option under the Grant Notice to purchase only approximately 14,285 shares at an exercise price of approximately $6.65 per share. A015 (Compl. ¶ 33). To the extent this Court remands, Kiromic intends to show through discovery that the parties' intent under the Prior Agreements was that those options would be subject to reverse stock splits as well, as it was always the intent to confer a percentage of stock, rather than an absolute number of shares, on Terrell.

[8] As noted, to the extent this Court remands for discovery and further proceedings, Kiromic will demonstrate that the Jan. 2017 Agreement and the Grant Notice were always understood by the parties as pertaining to the same options. Indeed, they both purported to grant options to purchase 500,004 shares. *See* A198-199.

respectfully requests that the Court hold Terrell to his bargain and dismiss his claims under Agreements 1 and 2.

CONCLUSION

For the foregoing reasons, Kiromic respectfully requests that this Court affirm the judgment of the Court of Chancery in full.

November 7, 2022

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