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IN THE SUPREME COURT OF THE STATE OF DELAWARE

JEFF HIMAWAN, JOSH TARGOFF and STEPHEN TULLMAN, as the duly-appointed Representatives of the former stockholders of CEPTION THERAPEUTICS, INC., Plaintiffs-Below, Appellants, v. CEPHALON, INC. and TEVA PHARMACEUTICALS USA, INC., Defendants-Below, Appellees.	No. 226, 2024 Case Below: Court of Chancery of the State of Delaware, C.A. No. 2018-0075

APPELLANTS' REPLY BRIEF

Dated: September 9, 2024.

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TABLE OF CONTENTS

Page

TABLE OF CITATIONS

Cases

INTRODUCTION

Plaintiffs do not ask this Court to accept, as Defendants claim, any "fanciful retelling of the facts." (AB 3.) To the contrary, the trial court's factual findings, even when applied as found, lead to the inescapable conclusion that the court erred as a matter of law when it misinterpreted the CRE Clause[1] and applied to the facts of this case a lower standard than the CRE Clause demanded.

Specifically, the trial court found, and Plaintiffs do not dispute, that (i) on April 5, 2010, Cephalon acquired Ception and agreed to the CRE Clause to develop RSZ for EoE, with full knowledge of the results of the "failed" EoE study (Op. 8, 10; *see also* OB 8-9, 12; AB 9-10); (ii) Cephalon terminated the development of RSZ for EoE in ***September 2011*** before Teva acquired Cephalon, and a mere eighteen months after it first acquired RSZ for EoE (Op. 14-15, 38 & n.183; *see also* OB 15; AB 14-15); and (iii) "Teva did not restart the program" after the October 2011 acquisition of Cephalon. (Op. 38; *see also* OB 16-17; AB 16-17.)

Thus, the only question on this appeal is whether Defendants' actions from April 5, 2010, through October 2011 (when Defendants terminated development efforts, such as they had been, for RSZ for EoE) fulfilled their continuing obligation under the CRE Clause. The facts, as found post-trial, show that Cephalon's ***only***

[1] Unless otherwise stated, capitalized terms used herein shall mean as defined in the Opening Brief.

actions in that time period were (i) creating proposals with input from two former Ception employees to attempt to achieve FDA approval for RSZ for EoE using the existing study data and converting an ongoing study; and (ii) attending two FDA meetings where it submitted those proposals for RSZ for EoE. (Op. 10-14). Under a proper interpretation of the CRE Clause, which required Defendants to use "such efforts and [commit] such resources by a company with substantially the same resources and expertise as [Defendants]" and to take all reasonable steps to develop RSZ for EoE "so as to achieve the Developmental Milestones," those perfunctory actions failed to meet Defendants' contractual obligation set forth in the CRE Clause.

The only way those steps could have satisfied Defendants' obligations under the CRE Clause is if the trial court misinterpreted the CRE Clause. The trial court did exactly that. It reduced the CRE Clause, which contractually required Defendants to ***use efforts*** and to ***commit resources***, to a mere good faith decision, permitting Defendants to terminate development simply because it was not in their "self-interest" to continue development a mere eighteen months after they acquired Ception (including its asset, RSZ). To reach that conclusion, the trial court (i) ignored the contractual language, which required Defendants to act in Plaintiffs' interest "so as to achieve the Developmental Milestones," and (ii) rejected this Court's precedent, which requires a party contractually bound by a CRE clause to

take "all reasonable actions" to achieve the contractual objective (here, the Developmental Milestones). Defendants did not come close to meeting that standard.

Defendants attempt to distract this Court with a lengthy and irrelevant discussion of facts that occurred after 2011. Defendants consistently point to findings that they "prioritize[d]" RSZ for "EA over EoE" to justify their lack of efforts relating to RSZ for EoE (AB 17; Op. 38) and retained RxC, a third-party biopharma strategy consulting firm, to conduct an "opportunity assessment" of RSZ for EoE ***in 2017*** (AB 20; Op. 19). But those facts are merely ***rationalizations*** for Defendants' ***inaction*** subsequent to their decision to terminate development of RSZ for EoE, which, per the trial court's decision, occurred in 2011. Defendants do not get the benefit of hindsight to support their decision in 2011 to stop any development of RSZ for EoE. To the extent the trial court considered these facts, it only did so because it misinterpreted the CRE Clause to allow such *post hoc* rationalizations.

This Court should reverse and remand for further proceedings so that the trial court can consider the evidence under the correct interpretation of the CRE Clause.

ARGUMENT

I. DEFENDANTS' SELECTIVE READING OF THE OPINION IGNORES THE REALITY OF THE TRIAL COURT'S MISINTERPRETATION OF THE CRE CLAUSE.

Defendants point to each instance in which the trial court used the words "objective" or "commercially reasonable" as evidence that the court correctly interpreted and applied the CRE Clause. (*See* AB 29-30.) But Defendants ignore four substantive errors that prove the trial court did ***not*** in fact apply a seller-friendly, "objective" or "commercially reasonable" standard, notwithstanding the trial court's incantation of those magic words.

First, the trial court interpreted the CRE Clause to permit Defendants to terminate development if it were no longer in their perceived "self-interest" to commercialize and develop RSZ for EoE. But that is not the standard for, or required deference under, the CRE Clause, as this Court's precedent interpreting CRE clauses establishes.

Second, the trial court did not consider evidence of the efforts exercised and resources spent by comparable companies that chose to commercialize and develop biologics comparable to RSZ for the treatment of EoE. That was contrary to the plain language of the Agreement, which required the trial court to analyze other companies with substantially similar resources and expertise as a "benchmark" for Defendants' conduct. This Court should reverse and remand so that the trial court

can fully consider the evidence of comparable companies that exercised efforts and committed resources to the development of biologics like RSZ for EoE.

Third, the trial court misunderstood the relationship between the general discretion clause and the CRE Clause. Defendants were contractually committed to undertake efforts to commercialize and develop RSZ for EoE—and to do so for the express purpose of achieving the milestones payments due to Plaintiffs. Thus the only question was the ***amount*** of resources Defendants were required to commit and the ***extent*** of efforts Defendants were required to exercise. Instead, the trial court applied the general discretion clause to let Defendants off the hook by suggesting that in all events they had the discretion to terminate development, so long as it was, perhaps in hindsight even, a commercially reasonable decision to do so. That read the relationship between the clauses completely backwards.

Fourth, the trial court erred when it permitted Defendants to terminate development of RSZ for EoE in 2011, despite the continuing obligation to use CRE that remains unrestricted by any outside date. All of these are independent reasons to reverse and remand, so that the trial court can apply the correct standard to the factual evidence.

A. Whether Development and RSZ for EoE Was in Defendants' "Self-Interest" Is Not the Standard under the CRE Clause.

Under the CRE Clause, Defendants could not terminate development simply because it was not in their perceived "self-interest" to develop RSZ for EoE. Defendants argue that a party should not be required to pursue development if it would be against their self-interest to do so. (AB 32.) But that misses the entire point of the CRE Clause. Defendants ***already decided*** that it would be in their self-interest to pursue commercialization and development of RSZ for EoE when they entered into the Agreement. Once that decision was made, Defendants were further contractually obligated to act in Plaintiffs' interest by using "commercially reasonable efforts to develop and commercialize" RSZ for EoE "***so as to achieve the Developmental Milestones***." (A00262 § 3.4(a)(iii) (emphasis added).)

This Court's interpretation of other CRE clauses is highly instructive. In *Williams Companies, Inc. v. Energy Transfer Equity, L.P.*, 159 A.3d 264 (Del. 2017), a downturn in the energy market caused "a significant loss in the value of assets of the type held by Williams and ETE. This caused the transaction to become financially undesirable to ETE." *Id.* at 267. In fact, it would have been in ETE's self-interest to ***not consummate the transaction***. *See id.* Nonetheless, the Court reasoned that the CRE clause in *Williams* "not only prohibited the parties from preventing the merger, but obligated the parties to take all reasonable actions to complete the merger." *Id.* at 273.

The Court highlighted evidence "recognized by the trial court, from which it could have concluded that ETE did breach its covenants, including evidence that ETE 'did not direct Latham to engage earlier or more fully with Williams' counsel, failed itself to negotiate the issue directly with Williams, failed to coordinate a response among the various players, went public with the information that Latham had declined to issue the 721 Opinion, and generally did not act like an enthusiastic partner in pursuit of consummation of the [merger agreement].'" *Id.* at 273. In other words, under this Court's jurisprudence, a party contractually bound by a CRE clause cannot "throw up its hands" or "drag its feet" when the agreement no longer becomes in its self-interest to pursue.

Defendants build a strawman when they argue that "a provision requiring *commercially reasonable* efforts could not require a firm to act against its own economic self-interests." (Op. 32.) That is a gross misreading of Plaintiffs' argument. Of course, a Defendant is not required to risk insolvency or even throw "good money after bad" when they are bound by a CRE clause. (AB 2.) That is obvious from the very use of the words "commercially reasonable," and Plaintiffs never argued otherwise. But Defendants were contractually obligated to take "***all reasonable actions***," *Williams*, 159 A.3d at 273 (emphasis added), "***so as to achieve the Developmental Milestones***," (A00262 § 3.4(a)(iii) (emphasis added)). Terminating development of RSZ for EoE a mere eighteen months after acquiring

RSZ is not fulfilling Defendants' commitment to take "all reasonable actions" "to develop and commercialize" RSZ for EoE so as to achieve the milestones.

Defendants argue that they did, in fact, take steps to develop and commercialize RSZ for EoE. What were those steps? The evidence recognized by the trial court shows that, at most, Defendants:

- spoke with Dr. Henkel to discuss potential remedies for the "failed" EoE Study (Op. 10);
- drafted proposals for FDA approval based on the participant data already obtained from the prior studies and to convert an ongoing study (with neither study, the EoE Study nor the Open-Label Extension Study, being designed, initiated, or primarily funded by Defendants but instead by Ception) (Op. 6, 11);
- held a meeting with the FDA to discuss those proposals (Op. 11-12);
- prepared an alternative proposal after the FDA rejected their initial proposals (Op. 13); and
- met with the FDA a second time telephonically (*Id.*).

Thus, a mere eighteen months after Cephalon acquired RSZ, it terminated development of RSZ for EoE altogether simply because the FDA rejected three proposed plans that were based on already-obtained data and a preexisting patient population. (Op. 12-14 ("Ultimately, on November 8, 2011, Cephalon notified the FDA that it was discontinuing developing RSZ for EoE since it was not feasible to study the existing patient population to support regulatory approval."), 35.) This was despite the fact that "the FDA was encouraging, and stated it 'remain[ed] eager to work with [Cephalon] on further development of' RSZ for EoE." (Op. 13.) Under

any reasonable interpretation of the CRE Clause, such perfunctory efforts would not constitute "all reasonable actions." Such evidence was only sufficient under the trial court's misinterpretation of the CRE Clause, which permitted Defendants to eschew development as soon as development of RSZ for EoE was not "in its own self-interest." (Op. 30-31.)

Defendants also rely heavily on the "due regard" provision, which requires Defendants to use "such efforts and [commit] such resources by a company with substantially the same resources and expertise as [Defendants], with due regard to the nature of efforts and cost required for the undertaking at stake." (A00262 § 3.4(a)(iii).) Defendants argue that "[h]ad the parties intended to obligate Defendants to pursue RSZ even against their own economic self-interests, the CRE provision would have required development *without regard* to costs." (AB 32.) But, again, Defendants assume that they could eschew development of RSZ for EoE. The decision to pursue development was already made when the Agreement was signed. The CRE Clause contractually obligated them to ***use efforts*** and to ***expend costs***. The "due regard" provision only permitted them to ***limit*** those efforts and costs to that of a company with substantially the same resources and expertise.

Moreover, Defendants were contractually required to use CRE to develop RSZ for EoE "***so as to achieve the Developmental Milestones***." (A00262 § 3.4(a)(iii) (emphasis added); Op. 10.) Again, this was meant for Plaintiffs' benefit.

Thus, any "due regard" for the costs of the undertaking could not include the ***costs of the milestones***, which they were contractually required to pursue and the cost of which were known as of the date of execution of the Agreement. Of course, payment of a milestone obligation would not be in Defendants' "self-interest," yet the trial court erroneously held Defendants were permitted to consider the milestones as a reason not to proceed with development.

B. The Trial Court Rejected Objective Evidence of Comparable Companies and Held Defendants to a Subjective Standard.

To determine whether Defendants used commercially reasonable efforts, the trial court must analyze whether Defendants "exercise[d] . . . such efforts and commit[ted] . . . such resources [of] a company with substantially the same resources and expertise as" Defendants. (A00262 § 3.4(a)(iii).) Therefore, the Agreement demanded that the trial court look at comparable companies to set the benchmark to determine what resources they committed and what efforts they exercised to develop and commercialize RSZ for EoE.

At trial, Plaintiffs presented ample evidence regarding the conduct of Defendants' competitors "with substantially the same resources and expertise," which devoted resources to the development of EoE treatments and progression of their clinical programs. (Op. 25-26.) The trial court chose to ignore that evidence because it found "unworkable" "compar[ing] the efforts of similarly-situated pharmaceutical companies and their actions in the real world . . . no exemplar

companies operate under the actual conditions of Defendants, who, I note, are also different from one another as to their circumstances." (Op. 29). That was reversible error. The trial court was required to use the evidence of comparable companies to set a benchmark to determine what resources and efforts Defendants were contractually obligated to commit to the development of RSZ for EoE. The contract did not require the Court to compare Defendants' efforts to a company that operated under Defendants' ***exact*** conditions. It only required the trial court to assess ***substantially similar*** companies, i.e., companies with similar resources and expertise, to determine whether Defendants exerted similar efforts and applied similar resources during the eighteen months at issue to satisfy their CRE obligation. The Court should remand to require the trial court to assess the evidence of comparable companies to construct a benchmark by which to measure Defendants' conduct, and evaluate whether Defendants met that contractual benchmark.

Notwithstanding the obvious import of the trial court's statement, Defendants argue that "the Vice Chancellor *did measure* the efforts of Cephalon and Teva against an external benchmark, informed by the conduct of other companies." (AB 36 (emphasis added).) This argument strains credulity, since the trial court expressly stated that it found any comparison unworkable.

Instead, the trial court purported to construct a "similarly-situated hypothetical company." (Op. 32.) But nowhere does the trial court explain *how* it

created that hypothetical company, or what evidence it relied upon to create the hypothetical company that it then measured Defendants' actions against. As Defendants point out, the trial court highlighted only two companies, Oxygen and Allakos, but the trial court "cite[d] these examples only to bolster [its] finding of commercial reasonableness, not as determinative of themselves." (Op. 36, n.175.) The trial court (and Defendants) cannot have it both ways: rejecting comparisons of comparable companies as unworkable with the one hand, while cherry-picking the companies that "bolster" its conclusion with the other, without ever explaining *how* it reached its purported hypothetical company-based conclusion.[2] A fair reading of the trial court's Opinion shows that it rejected evidence of comparable companies, in contravention of the plain terms of the Agreement. That was reversible error.

Defendants attempt to defend as reasonable the trial court's interpretation of the CRE Clause by pointing to the repeated references to a "reasonable actor" and an "objective" standard. But the trial court never explained how it determined what

[2] Indeed, Plaintiffs presented evidence that Oxygen and Allakos could not have been considered in a benchmark analysis given that they are not substantially similar companies, i.e., they do not have substantially the same resources or expertise as Defendants. (*See* A03940-44 (opining, as an expert, on similar companies and explicitly *not* including Allakos or Oxygen in that list). *See also* A04755/575:13-15 (MacFarlane) ("I did not consider Allakos a substantially similar company because they're actually a much smaller company."); A04757/581:14-16 (MacFarlane) ("Allakos has far less resources. And again, I did not include them in the similarly situated companies list[.]").)

a "reasonable actor" looked like, and what "objective" standards it applied. (Op. 30-32.) The Agreement clearly required the trial court to determine commercial reasonableness ***by reference to other similar companies***. But the trial court did not do that. Instead, the trial court relied upon this Court's decision in *ev3, Inc. v. Lesh,* 114 A.3d 527 (Del. 2014). But *ev3* involved a ***subjective, good faith*** standard. Defendants argue that there was nothing improper with the trial court's reliance on *ev3*, because "the Vice Chancellor explained that modifying *ev3* to fit an objective standard meant Defendants could 'refuse . . . to proceed' with RSZ development efforts if those efforts were 'not expected to yield . . . a commercially reasonable profit,' considered objectively …." (AB 29). But that is like saying you modified a circle to be a square.

In any event, the trial court's reliance on *ev3*, modified by an "objective" standard would (at most) create an ***objective, good faith*** standard. But that is not what Plaintiffs bargained for when they negotiated the CRE Clause. In *ev3*, "funding to pursue achievement of any of the [m]ilestones" was "at [ev3's] sole discretion, to be exercised in good faith." *Ev3*, 114 A.3d at 533. By contrast, Defendants agreed to the CRE Clause, which contractually committed them to use commercially reasonable efforts to develop and commercialize RSZ for EoE.

Thus, unlike in *ev3*, Defendants here ***could not simply refuse to proceed***. Instead, they were contractually obligated to commit such resources and exercise

such efforts as a company ***committed*** to the development and commercialization of RSZ for the treatment of EoE. *See Williams*, 159 A.3d at 273 (recognizing that ETE breaching its covenant to use commercially reasonable efforts when it failed to take "***all*** reasonable actions" and refused to "act like an enthusiastic partner ***in pursuit of consummation of the*** [merger agreement]" (emphasis added)).

C. The General Discretion Clause Is Irrelevant to the Commercialization and Development of RSZ for EoE.

The trial court repeatedly misstated the relationship between the general discretion clause, which gave Defendants "discretion with respect to all decisions related to the business of the Surviving Corporation[,]" and the CRE Clause, which eliminated that discretion with respect to the development of RSZ for EoE. Instead, Defendants were contractually committed to using CRE to develop and commercialize RSZ for EoE.

The trial court's error is best understood in its efforts to distinguish *Williams*. In a footnote, the trial court contends that, unlike *Williams*, which involved a CRE clause that "placed an affirmative obligation on the acquiring company to take all reasonable steps to complete the milestone and complete the merger, "[h]ere, the provisions are reversed; the buyer has complete discretion over development, cabined only by CRE." (Op. 30, n. 166.) But it is not clear from where the trial court is getting that "reversal" of provisions. In fact, the general discretion clause, Section 3.4(c), is clearly subject to the CRE Clause, and thus the CRE Clause

"trumps" any general discretion Defendants may have had when it comes to development of RSZ for EoE. *See Penn Mut. Life Ins. Co. v. Oglesby,* 695 A.2d 1146, 1150 (Del. 1997) ("But this general coverage provision is expressly made 'subject to all provisions of this policy.' Therefore, any other provision of the policy that may be inconsistent with this 'first manifest' provision can sublimate-or 'trump'-the first manifest provision.").

Defendants try to defend the trial court's obvious misunderstanding of the two provisions when they argue that "The Vice Chancellor never held that Defendants could choose *not* to exercise commercially reasonable efforts; rather, he held (correctly) that *if* further development was not commercially reasonable, *then* Defendants could choose not to engage in further development—but if further development *were* commercially reasonable, Defendants would be 'contractually obligated to' pursue it." (AB 34.) But this cannot be, as this interpretation affords Defendants more discretion than the Agreement provided them. By agreeing to the CRE Clause, Defendants already committed to act in Plaintiffs' interest to develop and commercialize RSZ for EoE "so as to achieve" said milestones. They could not "choose . . . [whether] to engage in further development." (AB 34.) To hold otherwise would gut the CRE Clause, and other CRE clauses, of their value. Unlike a good faith clause, or a clause that affords a party discretion whether to act, a CRE clause is a contractual commitment ***to take an action***. The breach of the CRE Clause

is even more stark here, where Defendants terminated development in 2011, a ***mere eighteen months*** after acquiring RSZ and agreeing to develop RSZ for EoE.

D. The Trial Court Absolved Defendants' of Their Continuing Obligation to Pursue Development of RSZ for EoE.

By its terms, the Agreement did not permit Defendants to cease developing RSZ for EoE upon the occurrence of a defined event or date certain. Thus, under Delaware law, the Agreement required Defendants to put forth "persistent efforts for the entire . . . contractual period." *S'holder Representative Servs., LLC v. Alexion Pharm., Inc.*, 2021 WL 3925937, at *6 (Del. Ch. Sep. 1, 2021). Defendants did not. Indeed, as Vice Chancellor Glascock found, "Cephalon had ended the EoE program" eighteen months after it acquired Ception and the RSZ asset. (Op. 15.)

Defendants try to avoid their breach of the Agreement a mere eighteen months after signing it by suggesting that "if and when the facts establish that additional efforts would be contrary to Defendants' objective interests, Defendants need not undertake them." (AB 35.) But that is a different agreement than the one Defendants actually signed. Here, Defendants were contractually obligated to "use . . . commercially reasonable efforts to develop and commercialize (or cause the development and commercialization of) [RSZ] so as to achieve the Developmental Milestones." (A00262 § 3.4(a)(iii); Op. 10.) Thus, absent such conduct being demonstrably similar to that of a similarly situated company with like resources and expertise, there was no "off-ramp" in which it could decide to stop using those

commercially reasonable efforts simply because it was no longer in their "interest" to do so. Instead, they were required to continue to use those efforts for the entire contractual term "so as to achieve the Developmental Milestones." (*Id.*) Defendants failed to do that, and the trial court let them off the hook by suggesting they were allowed to make the decision to terminate development completely in 2011, simply because it was, in the trial court's view, a "reasonable" decision.

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II. THE TRIAL COURT ERRED BY HOLDING DEFENDANTS TO A LOWER STANDARD THAN REQUIRED BY THE CONTRACT, WHICH INCORPORATED DELAWARE JURISPRUDENCE INTERPERATING THE MEANING OF CRE.

The contract at issue here was "governed by and [to be] construed in accordance with" Delaware law. (A00322 § 14.10.) As discussed in Plaintiffs' Opening Brief, Delaware cases such as *Williams* and its progeny *Menn*,[3] *Channel MedSystems*,[4] and *Chordia*,[5] interpret efforts clauses utilized in contracts governed by Delaware law as imposing "an affirmative obligation" to take all reasonable steps to achieve a contractual promise. (OB 42-44; A00322 § 14.10.) The trial court erred by ignoring such jurisprudence and rendering it not "particularly helpful" simply because this case involves an earn-out context. (Op. 29.) Plaintiffs' Opening Brief pointed to eight cases (some merger consummation cases, some earn-out cases) where Delaware courts applied this affirmative obligations standard to contracts containing different variations of efforts provisions at different stages of the business context. (OB 43-44.) Defendants do not disagree (nor can they) that such jurisprudence imposes an affirmative obligation standard to contractually negotiated CRE clauses regardless of whether the context is pre-merger or post-merger.

[3] *Menn v. ConMed Corp.*, 2022 WL 2387802, at *34 (Del. Ch. June 30, 2022).

[4] *Channel MedSystems, Inc. v. Bos. Sci. Corp.*, 2019 WL 6896462 (Del. Ch. Dec. 18, 2019).

[5] *Chordia v. Lee*, 2024 WL 49850, at *24 (Del. Ch. Jan. 4, 2024).

Instead, Defendants argue (i) the trial court was permitted to disregard Delaware jurisprudence because the Agreement language takes "privilege" over standards articulated in decisional law (AB 41-42); and (ii) the trial court's decision essentially applied the affirmative obligations standard, which Defendants claim was satisfied here. (AB 42-44.) Neither argument absolves the trial court of its reversible error.

A. The Agreement's Language Bolsters CRE Standards Under Delaware Jurisprudence.

In arguing that the contractual language instructs the trial court's analysis above all else, Defendants implicitly agree with Plaintiffs' argument that the trial court should have applied the contract as written. Instead, the trial court *sua sponte* rejected the contractually called-for comparable company analysis as "unworkable" in its post-trial decision and erroneously prevented Plaintiffs from enjoying the benefit of their contractual bargain, which was a measure of CRE that demanded real efforts, per Delaware law, comparable to those of a similarly situated company engaged in pharmaceutical development and commercialization.

The trial court also did not hold Defendants to this bargained-for CRE standard when it refused to follow Delaware law holding Defendants accountable for affirmative obligations because this case, unlike certain of the "affirmative obligations" cases, occurred in the post-merger context. In the world of the trial court's post-trial decision, no affirmative efforts obligations exist in the post-merger context under Delaware law. Such an outcome is indisputably inconsistent with

Delaware law and amounts to reversible error.

Defendants cite *Menn*, *Neurvana*,[6] and *Chordia* as permitting the trial court to read out the "affirmative obligations" standard from CRE clauses containing subjective measures. (AB 41-42.) But that argument falls flat. The inclusion of a comparable company benchmark in the Agreement's CRE Clause does not supplant the "affirmative obligations" standard in Delaware but bolsters that standard to afford more protections to the seller.[7] Defendants entered into an agreement containing a seller-friendly CRE provision that was to be construed in "accordance with" Delaware law, and the trial court erred by absolving Defendants of the legal obligation under Delaware law to undertake affirmative action.

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[6] *Neurvana Med., LLC v. Balt USA, LLC*, 2020 WL 949917, at *16 (Del. Ch. Feb. 27, 2020).

[7] Two decisions in this past week by the Court of Chancery have interpreted similar CRE clauses in the earn-out context, have reached different results, *and* have articulated the standard to be applied differently—neither of which is consistent with what the trial court did in this case. *See generally Fortis Advisors LLC v. Johnson & Johnson*, 2024 WL 4048060, at *24-34 Del. Ch. Sept. 4, 2024) (Will, V.C.); *S'holder Representative Servs., LLC v. Alexion Pharm.*, 2024 WL 4052343, at *36-46 (Del. Ch. Sept. 5, 2024) (Zurn, V.C.). *Fortis* and *Alexion* both underscore the need for this Court to provide clarity on interpretation of CRE clauses as there is obvious conflict at the trial court level. Given where these opinions were issued within the briefing schedule for this matter, Appellant would respectfully ask the Court to order supplemental briefing to provide both Appellants and Appellees an opportunity to fully and fairly address these lengthy opinions for the Court.

B. The Trial Court Erred By Failing to Apply the "Affirmative Obligations" Standard, and Defendants Have Not Otherwise Satisfied This Applicable Standard.

The trial court then compounded its error by imposing *sua sponte* a limit on its reading of the Agreement's CRE Clause to require from Defendants only those efforts that aligned with Defendants' "self-interest"—a phrase and buyer-friendly benefit neither incorporated in nor relevant to the Agreement's CRE Clause. The trial court's baseless and improper application of a "self-interest" limitation undermines Defendants' second argument, which suggests that the affirmative obligation jurisprudence otherwise "readily maps onto the Vice Chancellor's decision here" because what was reasonable under that jurisprudence would be reasonable here. (AB 43.) However, Defendants do not identify what reasonable affirmative actions the trial court identified in its decision, or that Defendants otherwise demonstrated were taken at trial, that would satisfy the "affirmative obligations" jurisprudence. Instead, Defendants suggest that Plaintiffs themselves purportedly failed to "identif[y] any actions that would be required under *Williams*, but not under the decision below." (AB 43-44.) Plaintiffs refer to pages 19-21 of their Opening Brief, wherein Plaintiffs identify the types of efforts Plaintiffs and their testifying expert would have expected Defendants to undertake to develop and commercialize RSZ for EoE, and the trial court's recitation of such evidence at pages 39-40 of its Opinion, all of which were not considered as necessary action by the

trial court. (*See also* A03944 (discussing obstacles that are typically overcome in drug development by way of efforts; A05195 (discussing how Plaintiffs are not required to make such a showing).) These types of affirmative efforts beyond 2011 are the type of efforts that Delaware law would expect Defendants to undertake based on their agreement to perform CRE.

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III. THE TRIAL COURT ERRED BY DISMISSING PLAINTIFFS' CLAIM FOR BREACH OF THE IMPLIED COVENANT OF GOOD FAITH AND FAIR DEALING.

Defendants' argument that the trial court properly dismissed Plaintiffs' claim for breach of the implied covenant of good faith and fair dealing because "[t]here is no gap here" misses the mark. (AB 47.) Delaware "case law suggests there are two strains of the implied covenant: (i) gap-filling ***and*** (ii) protecting against arbitrary and bad faith exercise of discretion." *Osios LLC v. Tiptree, Inc.*, 2024 WL 2947854, at *5 (Del. Ch. June 12, 2024) (emphasis added). "Under the first strain, the implied covenant is implicated when an agreement is truly silent on a term and requires a party to identify a gap in the contract to state a claim." *Id.* "Under the second strain, the implied covenant is implicated when a party 'is given discretion to act as to a certain subject and it is argued that the discretion has been used in a way that is impliedly proscribed by the contract's express terms.'" *Id.* Defendants' brief ignores Plaintiffs' arguments as to the second strain (abuse of discretion) and instead focuses singularly on the first (gap filling). (AB 45-47.)

As explained in Plaintiffs' Opening Brief, Plaintiffs' Complaint identified a contractual grant of discretion, which Plaintiffs alleged Defendants exercised in an unreasonable, arbitrary way that was impliedly proscribed by the contract's express terms. (OB 50.) This was sufficient to state a claim under Delaware law, and the trial court erred by granting Defendants' motion to dismiss this claim. *See Osios*,

2024 WL 2947854, at *6 (dismissing claim because plaintiff alleged "Defendants acted unreasonably and arbitrarily, yet fail[ed] to identify any discretion granted to Defendants under Section 3.12 of the LLC Agreement"). Because this claim was improperly dismissed at the pleadings stage and never tried, Defendants' argument regarding the trial court's factual findings at trial is gratuitous and irrelevant. (AB 47.)

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CONCLUSION

For the reasons stated herein, and in the Opening Brief, Plaintiffs respectfully request the Court reverse the trial court's decision and enter judgment in favor of Plaintiffs or, in the alternative, remand with instructions to review the evidence presented pursuant to the seller-friendly, objective CRE Clause, which required Defendants to take "all reasonable steps necessary" to commercialize and develop RSZ, as compared to companies with substantially similar resources and expertise. In addition, Plaintiffs respectfully request a new trial as to their implied covenant of good faith and fair dealing claim.

Dated: September 9, 2024.

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