

**ONTARIO  
SUPERIOR COURT OF JUSTICE  
COMMERCIAL LIST**

**IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*,  
R.S.C. 1985, c. C-36, AS AMENDED**

**AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT  
OF ARALEZ PHARMACEUTICALS INC. AND  
ARALEZ PHARMACEUTICALS CANADA INC.**

**Applicants**

**MOTION RECORD OF THE APPLICANTS  
(Returnable November 16, 2018)  
(Re: KERP and KEIP Approval)**

November 8, 2018

**STIKEMAN ELLIOTT LLP**  
Barristers & Solicitors  
5300 Commerce Court West  
199 Bay Street  
Toronto ON M5L 1B9

**Ashley Taylor** LSO#: 39932E  
Tel: (416) 869-5236  
E-mail: ataylor@stikeman.com

**Maria Konyukhova** LSO#: 52880V  
Tel: (416) 869-5230  
E-mail: mkonyukhova@stikeman.com

**Kathryn Esaw** LSO# 58264F  
Tel: 416-869-6820  
E-mail: kesaw@stikeman.com

Lawyers for the Applicants

TO: The Service List

**ONTARIO  
SUPERIOR COURT OF JUSTICE  
COMMERCIAL LIST**

**IN THE MATTER OF THE COMPANIES' CREDITORS ARRANGEMENT ACT,  
R.S.C. 1985, c. C-36, AS AMENDED**

**AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT  
OF ARALEZ PHARMACEUTICALS INC. AND  
ARALEZ PHARMACEUTICALS CANADA INC.**

**I N D E X**

<b>TAB</b>	<b>DOCUMENT</b>
<b>1.</b>	Notice of Motion, returnable November 16, 2018
<b>2.</b>	Affidavit of Adrian Adams, to be sworn
<i>A</i>	Exhibit "A" - Filed Objection of the Unsecured Creditors Committee to the Proposed KEIP in the Chapter 11 Proceedings
<i>B</i>	Exhibit "B" - Consolidated DIP Budget from August 10, 2018 through December 7, 2018
<b>3.</b>	Draft KERP and KEIP Order

**TAB 1**

**ONTARIO  
SUPERIOR COURT OF JUSTICE  
COMMERCIAL LIST**

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*,  
R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT  
OF ARALEZ PHARMACEUTICALS INC. AND ARALEZ PHARMACEUTICALS CANADA  
INC.

**Applicants**

**NOTICE OF MOTION  
(Returnable November 16, 2018)  
(Re KERP and KEIP Approval)**

Aralez Pharmaceuticals Inc. ("**API**") and Aralez Pharmaceuticals Canada Inc. ("**Aralez Canada**", and with API the "**Applicants**"), will make a motion to the Justice presiding over the Commercial List on November 16, 2018 at 8:30 AM at 361 University Avenue, Toronto, Ontario.

**PROPOSED METHOD OF HEARING:**

The motion is to be heard orally.

**THE MOTION IS FOR:**

1. An Order, substantially in the form of the draft order located at Tab 3 of the Motion Record, providing for, *inter alia*:

- (a) The approval of a Key Employee Retention Plan (the "**KERP**") and Key Employee Incentive Plan (the "**KEIP**"), offered by the Applicants to certain employees deemed critical to a successful restructuring and a charge on the current and future assets, undertakings and properties of the Applicants to secure the Applicants' obligations under the KERP and KEIP (the "**Key Employee Charge**");

- (b) The sealing of the Confidential Supplement (the “**Confidential Supplement**”) to the Report of the monitor to be filed in respect of this motion (the “**Monitor's Report**”); and
2. Such further and other relief as counsel may request and this Court may permit.

**THE GROUNDS FOR THE MOTION ARE:**

3. The Applicants, together with Aralez Pharmaceuticals Management Inc., Aralez Pharmaceuticals R&D Inc., Aralez Pharmaceuticals U.S. Inc., POZEN Inc., Halton Laboratories LLC, Aralez Pharmaceuticals Holdings Limited, and Aralez Pharmaceuticals Trading DAC (collectively, the “**Chapter 11 Entities**” and with the Applicants, the “**Aralez Entities**”) are in the business of acquiring, developing, marketing and selling specialty pharmaceutical products, with a focus on cardiovascular health and pain management, in Canada, the U.S. and Ireland;
4. The Aralez Entities experienced financial difficulties, resulting in the Applicants seeking protection from their creditors;
5. On August 10, 2018, the Applicants sought and were granted creditor protection and related relief under the CCAA (the “**CCAA Proceedings**”) pursuant to the Initial Order of the Honourable Mr. Sean Dunphy (the “**Initial Order**”). The Initial Order appointed Richter Advisory Group Inc. as monitor of the Applicants;
6. Also on August 10, 2018, the Chapter 11 Entities filed voluntary petitions under Chapter 11 of Title 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the Southern District of New York;
7. The Aralez Entities (including the Applicants) are working diligently with their advisors and stakeholders to complete a sales process of substantially all of the assets of the Aralez Entities;
8. On October 10, 2018, the Canadian Court granted an order (the “**Process Order**”) approving the proposed sales process;

9. The Applicants are seeking to approve a KERP and KEIP providing for, respectively, the payment of retention bonuses or incentive bonuses to certain highly skilled and experienced employees of the Aralez Entities (the “**KERP Participants**” and “**KEIP Participants**”, respectively, and collectively the “**Key Employees**”).

10. With respect to the KERP, this means Key Employees—those who are deemed to be critical to the Aralez Entities’ ongoing operations and who present retention risk and would be difficult to replace—will receive payments after the completion of the sales process;

11. With respect to the KEIP, this means Key Employees—those who are in senior management positions—are rewarded with tiered incentive payments based on both the outcome of the sales process and on certain operating metrics during the pendency of the proceedings. The tiered incentive payments are designed to align senior management with the success of the sales process and properly incent individuals who have control and oversight of the sales process. By incenting the performance of senior management, the sales process is expected to be carried out in a more efficient and diligent value-maximizing manner;

12. The restructuring of the Aralez Entities depends on the KERP Participants and KEIP Participants as these groups of individuals are comprised of skilled and experienced employees who perform roles critical to advancing the Aralez Entities’ restructuring goals. The KERP Participants and KEIP Participants perform important management or business function roles and the knowledge and skills possessed by them is invaluable, making their continued employment vital to providing stability to the Aralez Entities’ strategic direction and/or day-to-day operations;

13. Without the KERP and KEIP, there is a significant risk that the KERP Participants and/or KEIP Participants will terminate their employment with the Aralez Entities;

14. In order to secure payment of the amounts payable under the KERP and KEIP, the Applicants are seeking the Key Employee Charge on the Applicants’ current and future assets, undertakings and properties of every nature and kind whatsoever, and wherever situated, including all proceeds thereof;

15. The Key Employee Charge will rank subordinate to the Administration Charge, the DIP Lender's Charge (as defined in the Initial Order) and the Bid Protections Charge (as defined in the Process Order) but in priority to the D&O Charge and the Transactional Charge (as defined in the Initial Order) and to all other security interests, trusts, liens, charges and encumbrances, claims of secured creditors, statutory or otherwise in favour of any individual, firm, corporation, governmental body or agency, or any other entities;

16. The Confidential Supplement contains individually identifiable personal and financial information of the KERP Participants and KEIP Participants and should be sealed;

### **GENERAL**

17. The provisions of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, C-36 and the inherent and equitable jurisdiction of this Court;

18. Section 137 of the *Courts of Justice Act*, R.S.O. 1990, c. C-43 and rules 1.04, 1.05, 2.03, and 37 of the *Rules of Civil Procedure*, R.R.O. 1990, Reg. 194, as amended; and

19. Such further grounds as counsel may advise and this Court may see fit.

**THE FOLLOWING DOCUMENTARY EVIDENCE** will be used at the hearing of the motion:

20. The Affidavit of Adrian Adams, to be sworn, and the exhibits attached thereto;

21. The Monitor's Report to be filed; and

22. Such further and other materials as counsel may advise and this Court may permit.

November 8, 2018

**STIKEMAN ELLIOTT LLP**  
Barristers & Solicitors  
5300 Commerce Court West  
199 Bay Street  
Toronto, Canada M5L 1B9

**Ashley Taylor LSO#: 39932E**  
Tel: (416) 869-5236

E-mail: ataylor@stikeman.com

**Maria Konyukhova LSO#: 52880V**

Tel: (416) 869-5230

E-mail: mkonyukhova@stikeman.com

**Kathryn Esaw LSO#: 58264F**

Tel: (416) 869-5230

Email: kesaw@stikeman.com

Fax: (416) 947-0866

**Lawyers for the Applicants**

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

Court File No. CV-18-603054-00CL

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT  
OF ARALEZ PHARMACEUTICALS INC. ET AL.

**ONTARIO  
SUPERIOR COURT OF JUSTICE  
(COMMERCIAL LIST)**

Proceeding commenced at Toronto

**NOTICE OF MOTION  
(RETURNABLE NOVEMBER ●, 2018)**

**STIKEMAN ELLIOTT LLP**  
Barristers & Solicitors  
5300 Commerce Court West  
199 Bay Street  
Toronto, Canada M5L 1B9

**Ashley Taylor LSO#: 39932E**  
Tel: (416) 869-5236  
E-mail: ataylor@stikeman.com

**Maria Konyukhova LSO#: 52880V**  
Tel: (416) 869-5230  
E-mail: mkonyukhova@stikeman.com

**Kathryn Esaw LSO#: 58264F**  
Tel: (416) 869-5230  
Email: kesaw@stikeman.com  
Fax: (416) 947-0866

**TAB 2**

**ONTARIO  
SUPERIOR COURT OF JUSTICE  
COMMERCIAL LIST**

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*,  
R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT  
OF ARALEZ PHARMACEUTICALS INC. AND ARALEZ PHARMACEUTICALS CANADA  
INC.

**Applicants**

**AFFIDAVIT OF ADRIAN ADAMS**

I, Adrian Adams, of the Town of Devon, in the State of Pennsylvania, MAKE OATH  
AND SAY:

1. I am the Chief Executive Officer of the Applicant, Aralez Pharmaceuticals Inc. ("**API**") which is the parent company of Aralez Pharmaceuticals Canada Inc. ("**Aralez Canada**" and, together with API, the "**Applicants**" or the "**CCAA Entities**"). As a result of my role with API, I have certain knowledge of the matters to which I hereinafter depose. I have also reviewed certain books and records of the Applicants and have spoken with and relied upon certain of the directors, officers, employees and/or advisors of the Applicants, as necessary and applicable. Where I have relied upon such information, I believe such information to be true.
2. All references to currency in this affidavit are references to United States dollars, unless otherwise indicated.
3. This motion is brought by the Applicants seeking:
  - (a) An order, substantially in the form of the draft order attached at Tab "3" of the Motion Record:
    - (i) approving the Key Employee Retention Plan (the "**KERP**") and Key Employee Incentive Plan (the "**KEIP**"), which provide for retention or incentive bonuses, respectively, to certain employees (the recipients under the KERP being the "**KERP Participants**", the recipients under

the KEIP being the “**KEIP Participants**”, and together, the “**Key Employees**”);

- (ii) approving a charge in respect of the KERP and KEIP (the “**Key Employee Charge**”) on the Applicants’ current and future assets, undertakings and properties of every nature and kind whatsoever, and wherever situated, including all proceeds thereof; and
- (iii) Sealing the confidential supplement (the “**Confidential Supplement**”) to the report (the “**Monitor’s Report**”) of Richter Advisory Group Inc. in its capacity as court-appointed monitor of the Applicants (the “**Monitor**”) containing financial information about the Key Employees, to be filed; and

(b) Such further and other relief as the Court deems just.

## I. BACKGROUND OF THE APPLICANTS

4. The Applicants are two entities within a larger corporate structure that includes Aralez Pharmaceuticals Management Inc., Aralez Pharmaceuticals R&D Inc., Aralez Pharmaceuticals U.S. Inc., POZEN Inc. (“**Pozen**”), Halton Laboratories LLC, Aralez Pharmaceuticals Holdings Limited, and Aralez Pharmaceuticals Trading DAC (“**Aralez DAC**” and collectively, the “**Chapter 11 Entities**” and, with the Applicants, the “**Aralez Entities**”). The current corporate structure of the Aralez Entities is the result of a business combination between Pozen and Aralez Canada<sup>1</sup> that was completed in early 2016.

5. As described in greater detail in the affidavit sworn by Andrew I. Koven on August 9, 2018 in support of the Applicants’ application for protection under the CCAA (the “**Initial Affidavit**”), the Aralez Entities are in the business of acquiring, developing, marketing and selling speciality pharmaceutical products. API is the public holding company that is the ultimate parent of the other Aralez Entities. Canadian operations are largely conducted through Aralez Canada, with supply chain management and quality assurance conducted by Aralez DAC.

---

<sup>1</sup> Originally, Tribute Pharmaceutical Canada Inc. but pursuant to an internal reorganization, Aralez Canada.

6. As a result of events detailed in the Initial Affidavit, on August 10, 2018, the Applicants sought and were granted creditor protection and related relief under the CCAA (the “**CCAA Proceedings**”) pursuant to an order (as subsequently amended and restated, the “**Initial Order**”) of this Court (the “**Canadian Court**”). Richter Advisory Group Inc. was appointed as Monitor of the CCAA Entities.

7. Also on August 10, 2018, the Chapter 11 Entities filed voluntary petitions under chapter 11 of title 11 of the United States Code (the “**Chapter 11 Proceedings**” and together with the CCAA Proceedings, the “**Restructuring Proceedings**”) in the United States Bankruptcy Court for the Southern District of New York (the “**U.S. Court**”).

8. The Aralez Entities retained Alvarez & Marsal Healthcare Industry Group, LLC and Alvarez & Marsal Canada Inc. (together, “**A&M**”), to assist the Aralez Entities in their restructuring efforts, including assistance in cash management and implementing a restructuring plan. The Aralez Entities also engaged the services of Moelis & Company LLC (“**Moelis**”) to act as the investment banker to the Aralez Entities during these Restructuring Proceedings.

9. A copy of each of the Initial Affidavit and the Initial Order is available, together with all other filings in the CCAA Proceedings, on the Monitor’s website for these proceedings at: <<http://insolvency.richter.ca/A/Aralez-Pharmaceuticals>>.

10. Additional details regarding the background to these CCAA Proceedings are set out in the Initial Affidavit and, unless relevant to the present motion, are not repeated herein.

#### **A. Sales Process and Claims Process**

11. On September 18, 2018, certain of the Aralez Entities entered into three stalking horse agreements (the “**Canadian Stalking Horse Agreement**”, the “**Vimovo Stalking Horse Agreement**” and the “**Toprol Stalking Horse Agreement**”, together the “**Stalking Horse Agreements**”):

- (a) The Canadian Stalking Horse Agreement is an agreement between API, Aralez Canada and Nuvo Pharmaceuticals Inc. (the “**Canadian Purchaser**”), pursuant to which the Canadian Purchaser will purchase all of the shares of Aralez Canada (the “**Canadian Assets**”), which are held by API, for the purchase price of

\$62,500,000, subject to higher or otherwise better offers and the approval of the Canadian Court (the “**Canadian Stalking Horse Bid**”). The Canadian Stalking Horse Agreement is the only Stalking Horse Agreement to which the CCAA Entities are parties.

- (b) The Vimovo Stalking Horse Agreement is an agreement between Pozen, Aralez DAC and Nuvo Pharmaceuticals (Ireland) Limited (the “**Vimovo Purchaser**”), an affiliate of the Canadian Purchaser for the purchase of, among other things, royalties collected for the pain-management drug product Vimovo (the “**Vimovo Assets**”), for the purchase price of \$47,500,000, subject to higher or otherwise better offers and the approval of the U.S. Court (the “**Vimovo Stalking Horse Bid**”). The Vimovo Assets are assets of the Chapter 11 Entities.
- (c) The Toprol Stalking Horse Agreement is an agreement between Aralez DAC and Toprol Acquisition LLC (the “**Toprol Purchaser**” and, together with the Canadian Purchaser and the Vimovo Purchaser, the “**Stalking Horse Purchasers**”), which contemplates a credit bid of \$130,000,000 for the drug Toprol-XL® (“**Toprol-XL**”) and its authorized generic (together with Toprol-XL, the “**Toprol Assets**”), subject to higher or otherwise better offers and the approval of the U.S. Court (the “**Toprol Stalking Horse Bid**”, together with the Canadian Stalking Horse Bid and the Vimovo Stalking Horse Bid, the “**Stalking Horse Bids**”). The Toprol Purchaser is an affiliate of Deerfield Management Company, L.P., as administrative agent. The Toprol Assets are assets of the Chapter 11 Entities.

Pursuant to the Stalking Horse Agreements, the majority of the Aralez Entities’ assets are proposed to be sold to the Stalking Horse Purchasers or such other bidder(s) who offer the highest or otherwise best bid(s) for these assets (the “**Sales**”) subject to the terms of those agreements.

12. On October 10, 2018, the Canadian Court granted an order (the “**Process Order**”) approving the proposed sales process (the “**Sales Process**”) and authorizing the CCAA Entities to enter into the Canadian Stalking Horse Agreement for the purpose of the Canadian

Purchaser acting as the stalking horse bidder within the Sales Process. The Canadian Court further approved a claims process (the “**Claims Process**”) pursuant to which the CCAA Entities would call for claims against the CCAA Entities and their directors and officers. The Applicants anticipate returning to Court to seek an order for the adjudication and resolution of any filed claims.

13. The U.S. Court approved the bidding and sale procedures in respect of the Chapter 11 Entities’ proposed sales process on October 10, 2018.

14. The key dates under the Sales Process are as follows:

<b>Proposed Sale Timeline</b>	
Bid Deadline	November 26, 2018 at 5:00 p.m. ET
Deadline to Notify Qualified Bidders	November 28, 2018 at 5:00 p.m. ET
Auction (if required)	November 29, 2018 at 11:00 a.m. ET
Notice of Successful Bidders	December 3, 2018 at 5:00 p.m. ET
Sale Hearing	December 4, 2018 at 11:00 a.m. ET in the U.S. Court  The earliest date available after December 4, 2018 in the Canadian Court

## **II. KEY EMPLOYEE RETENTION AND INCENTIVE PLANS**

### **A. Overview**

15. The Aralez Entities’ restructuring depends upon the Key Employees, a group of skilled and experienced employees who perform roles critical to advancing the Aralez Entities’ restructuring goals. These Key Employees perform important management or business functions and the knowledge and skills possessed by them is invaluable, making their continued employment vital to providing stability to the Aralez Entities’ daily operations and Sales Process.

16. As of the date of this affidavit, the CCAA Entities have approximately 41 employees and the Chapter 11 Entities have approximately 23 employees.

17. As noted above, the CCAA Entities are in the midst of a Sales Process which would see the Canadian operating business preserved through a share deal. The CCAA Proceedings have, to date, been intensive, and interest from prospective bidders in the court-approved Sales

Process has been robust. The dedicated assistance of the Key Employees during the Sale Process is a critical component to the ultimate objective of maximizing the value received for the Applicants' business and assets upon conclusion of the Sales Process.

18. To ensure that employees who are critical to value preservation maintain their employment with the Aralez Entities during the pendency of the CCAA Proceedings, the Aralez Entities, with the assistance of their advisors, developed the KERP to ensure retention of three KERP Participants. The maximum aggregate amount which may become payable under the KERP is \$256,710.

19. The Aralez Entities, with the assistance of their advisors, also developed the KEIP for nine KEIP Participants to incentivize these Key Employees to maximize proceeds from a sale transaction while maintaining operational efficiencies. The amounts payable to the KEIP Participants are dependent upon the Aralez Entities (a) closing one or more sale transactions with a total consideration of at least \$230 million (the "**Asset Sale Target**") and/or (b) achieving or outperforming the net operating cash flow projected in the consolidated debtor in possession rolling 13-week budget (the "**Consolidated DIP Budget**"), which consolidates the rolling 13-week budget required under the CCAA Entities' and Chapter 11 Entities' respective DIP financing facilities from the filing date through to the date of approval of one or more asset sales (the "**Cash Flow Target**" and together with the Asset Sale Target, the "**Performance Targets**"). The Performance Targets are coordinated among the CCAA Entities and Chapter 11 Entities as described in greater detail below.

20. A KERP and KEIP are also contemplated in the Chapter 11 Proceedings. The participants in the Chapter 11 Proceedings KEIP are the same participants in the CCAA KEIP. There is no overlap between KEIP Participants and KERP Participants, and none of the KERP Participants in the CCAA Proceedings are proposed to be the subject of a KERP in the Chapter 11 Proceedings.

#### **B. Development of and Need for the KERP and KEIP**

21. In light of the Aralez Entities' insolvency proceedings and the need to complete a successful sale and wind down process free of operational disruptions, the CCAA Entities determined that it was necessary to develop an incentive plan and a CCAA retention plan to retain and incentivize the Key Employees.

22. Development of the KERP and KEIP began before the commencement of the Restructuring Proceedings. The Aralez Entities requested that A&M formulate key employee retention and incentive programs. To that end, A&M formulated (a) a KEIP that focused on the sales of the Aralez Entities' assets and/or business and the Aralez Entities' operational success prior to approval by this Court and the U.S. Court of the sales, and (b) a KERP that focused on retaining non-insiders to ensure a continuous and smooth operation of the business and to accomplish the sales and associated tasks. The Aralez Entities, in consultation with A&M, also took into consideration the Aralez Entities' existing compensation packages, including historical bonuses and severance policies offered to all employees, and the circumstances of these proceedings.

23. In determining who the Key Employees would be, the Aralez Entities undertook a rigorous selection process, considering among other things:

- (a) Whether the employee could be replaced if they resigned from the Aralez Entities;
- (b) Whether the employee was critical to:
  - (i) the daily operations and management of the Aralez Entities; and/or
  - (ii) the completion of the Sales Process; and
- (c) With respect to the KERP Participants, whether an employee had a high level of retention risk.

24. The compensation committee (the "**Compensation Committee**") of API's board of directors (the "**Board**") and certain senior management, in consultation with A&M and the Aralez Entities' legal counsel, reviewed, commented on and modified the terms of the KEIP in order to ensure that those employees subject to the KEIP were properly incentivized to maximize the Aralez Entities' operational success prior to any sale as well as to maximize the value of the Aralez Entities' assets. The Board and certain senior management, in consultation with A&M, also determined that implementing the KERP was necessary for the success of the CCAA Proceedings in ensuring operational success and maximizing the value of the Aralez Entities' assets. The results of these efforts are memorialized in the KEIP and KERP, which have

been approved by the Board as well as the boards of directors of each of the Aralez Entities that employ the participants in the KEIP and KERP.<sup>2</sup>

25. The CCAA Entities worked with the Monitor throughout the KERP/KEIP process, sharing drafts and adapting the programs to reflect comments from the Monitor and its counsel. I understand the Monitor will be submitting a report on the reasonableness and necessity of the KERP and KEIP in advance of this motion.

26. The Aralez Entities shared the KEIP and KERP with Deerfield Private Design Fund III, L.P. and Deerfield Partners, L.P. (collectively, including related affiliates, "**Deerfield**"), the Aralez Entities pre-filing secured lender and their DIP lender, and Deerfield does not object to the KEIP and KERP.

27. I understand from U.S. counsel to the Applicants (also U.S. counsel to the Chapter 11 Entities) that in connection with resolving concerns raised by the United States Trustee for Region 2 (the "**UST**"), the KEIP, which is structured to be identical to the KEIP in the CCAA Proceedings, was revised. Such revisions have had the effect of raising the threshold levels required to receive a payout under the KEIP. I also understand from U.S. counsel that the official committee of unsecured creditors has raised objections to the KEIP in the Chapter 11 Proceedings. A copy of the objection is attached hereto as **Exhibit "A"**. In the event that further changes to the KEIP are resolved consensually, the CCAA Entities will update this court accordingly.

28. Each of the Key Employees has been with the Aralez Entities since at least 2016, the year the current structure of the Aralez Entities was formed.

29. The early departure of any of the KERP Participants would cause the CCAA Entities to rely on their professionals more, none of whom have the deep history, experience or understanding of the Aralez Business that the KERP Participants have. Relying on these professionals instead of the KERP Participants would undoubtedly be more expensive and would diminish the value of the CCAA Entities' business.

---

<sup>2</sup> After the commencement of the CCAA Proceedings, the number of members on the Board was reduced and there is no longer a compensation committee. The remaining members of the Board (excluding any KEIP Participants) approved the final terms of the KEIP and the KERP.

30. If such resignations occurred, finding and training qualified replacement employees with similar knowledge and skill sets to departing employees would be disruptive, time consuming and potentially impossible given the unattractive nature (from an employee's perspective) of working for a company undergoing a court protected restructuring, which concern is further exacerbated by the condensed timelines contemplated by the Sales Process.

31. I believe and have been advised by other members of the Aralez Entities' management team that the Key Employees are likely to consider other employment options if the KERP is not approved.

32. Implementing the KEIP, which is contingent upon certain financial performance targets and sale-based incentives, will encourage and incentivize the Aralez Entities' senior management team to remain focused and dedicated to successfully operating their business and maximizing their value during the court of the Restructuring Proceedings.

*Efforts of the Key Employees During the CCAA Proceedings*

33. Leading up to the commencement of the Sales Process, the Key Employees were fully engaged in a combination of operational efforts and sale-related efforts, including:

- (a) Leading/assisting with diligence related to the Stalking Horse Agreements. Letters of intent were entered into effective August 9, 2018, and definitive documents were not signed until September 18, 2018, meaning over five intensive weeks of negotiations occurred;
- (b) Preparing and populating data rooms for potential bidders;
- (c) Identifying potential bidders, in conjunction with Moelis;
- (d) Responding to potential bidders who have sought further information on the Canadian business;
- (e) Working with the Chapter 11 Entities to advance the Restructuring Proceedings and to achieve a coordinated approach to various matters of common interest;

- (f) Communicating with key suppliers to advise of the Restructuring Proceedings, confirming post-filing supply arrangements, and ensuring continued availability of drug and other products;
- (g) Communicating with employees to ensure business operations continued without interruption; and
- (h) Preparing updated financial budgets, with the assistance of A&M, as required under the debtor-in-possession financing agreement approved by the Canadian Court in the Initial Order.

34. Since the commencement of the Restructuring Proceedings, the need for the KERP and KEIP has become even more apparent. The Key Employees have had to assume considerable additional responsibilities in connection with the Restructuring Proceedings and the Sales Process, such as ensuring the Applicants' operations comply with the Canadian Stalking Horse Agreement, facilitating meetings with potential purchasers and preserving supplier and customer relationships. When the Key Employees commenced their employment with the Aralez Entities, the job functions they were hired to fulfill—and the compensation they agreed to receive—did not contemplate the demands, stress and job uncertainty associated with this increase in responsibility.

35. On a going forward basis, incentivizing the Key Employees during the Sales Process is essential to the Applicants' ability to maintain normal operations and preserve the value of their business, which is a critical component to the ultimate sale of the Canadian business. It is expected that Key Employees will, among other things, provide proper messaging to stakeholders; manage the CCAA Entities' relationships and contracts with wholesalers, distributors, vendors, suppliers and customers; continue to facilitate the Sales and all other sales, work with qualified bidders in any auction process, and spend significant time and effort with potential purchasers in providing diligence, answering questions and having management meetings, which will be critical to any potential purchaser of the CCAA Entities' assets; and confront and address any and all legal, operational and compliance issues that are likely to continue to arise as a result of the CCAA Proceedings. Without the continued commitment of

the Key Employees, the Applicants' ability to achieve a successful result in these proceedings would be severely compromised.

### **C. The KERP**

36. The objective of the KERP is to retain employees who are critical to value preservation during the pendency of the CCAA Proceedings.

37. The KERP covers three employees, all of whom are employees of Aralez Canada. The Aralez Entities' senior management team has evaluated the CCAA Entities' staffing needs and determined that these three employees are absolutely necessary to retain to ensure a successful sale process, including successful operations leading up to the consummation of the sales. Each KERP Participant has a specific qualification, skill and expertise and is indispensable to the core business functions of the CCAA Entities.

38. Without approval of the KERP, KERP Participants may resign to seek alternative employment with a workload and compensation structure similar to the one they enjoyed pre-filing. Significant work is still needed from the KERP Participants to ensure that the Canadian sale closes on the current terms and value in the CCAA proceedings is maximized. Further, the Canadian Stalking Horse Agreement contemplates that, if the Applicants seek a key employee plan, certain employees must be included in that plan (and those employees are accordingly included in the KERP). Accordingly, I believe that the KERP is a fair and just solution for the retention of Key Employees of the Applicants.

39. Under the proposed KERP, the proposed aggregate bonus pool is \$256,710, which represents less than 0.4% of the value of the \$62.5 million bid for the Canadian Assets. Per person, the KERP would pay on average \$85,570 per employee.

40. The KERP Participants' eligibility for, and proposed compensation under, the KERP is based on each respective KERP Participant's position, responsibilities, compensation package, and other factors. The KERP Participants will receive payment upon the earlier of (a) termination without cause by Aralez Canada or upon death or permanent disability; and (b) the closing of a sale transaction for the Canadian Assets. Any forfeited allocation will not be made available to the remaining KERP Participants.

41. To ensure the reasonableness of the KERP, the CCAA Entities' advisors reviewed recent CCAA proceedings and determined that the KERP is reasonable. In particular, A&M reviewed the terms of the KERP and believes that it is within the range of KERPs granted in comparable CCAA proceedings. The CCAA Entities also discussed the KERP with the Monitor and obtained its favourable feedback prior to finalizing the program.

42. The KERP Participants have been working hard since prior to the CCAA Proceedings to find a going concern solution for the Canadian business, and have been working even harder during the proceedings. Significant work remains to be done to conclude the Sales Process. The KERP Participants were advised early within the CCAA Proceedings that the CCAA Entities are seeking the KERP in order to incentivize them to remain with the Applicants through to the conclusion of these proceedings.

#### **D. The KEIP**

43. The objective of the KEIP is to:

- (a) Promote the achievement of financial performance objectives;
- (b) Ensure that key executives' interests are aligned with maximizing stakeholder value; and
- (c) Provide compensation packages that will motivate key executives during the proceedings and Sales Process.

44. The Aralez Entities have limited participation in the KEIP to nine individuals: (a) the Chief Executive Officer; (b) the President and Chief Business Officer; (c) the Chief Financial Officer; (d) the Executive Vice President, Human Resources; (e) the General Counsel and Chief Compliance Officer; (f) the Vice President, Business Development; (g) the Treasurer; and (h) two other individuals. One individual was added to the KEIP after discussions with the UST. This individual provides services for the primary benefit of the Chapter 11 Entities; as such, any KEIP payments owing to this individual will be entirely paid by the Chapter 11 Entities. Due to the corporate structure of the Aralez Entities, the other eight individuals provide value to both the Canadian and U.S. businesses. Other than the one individual described above, the KEIP was structured so that targets were identical across the CCAA Proceedings and the Chapter 11 Proceedings, to ensure that the applicable KEIP Participants were motivated to maximize operating and sale value in both jurisdictions.

45. The Chapter 11 Entities began winding up commercial operations starting in May 2018, and the KEIP Participants are not expected to transition to a purchaser in a sale transaction other than one individual as detailed in the Confidential Supplement.

46. The proposed KEIP contemplates a two-pronged incentive payment. The first prong is operating-based and focuses on the KEIP Participants' ability to achieve the Cash Flow Target, while the second prong is sales-based and focuses on the KEIP Participants' ability to achieve the Asset Sale Target. The total payout for each KEIP Participant is based on the level of achievement of the Cash Flow Target or the Asset Sale Target, as applicable, for the applicable performance period, with amounts allocated between the CCAA Entities and the Chapter 11 Entities as detailed below.

47. The Cash Flow Target measures the ability of the Aralez Entities to meet or exceed the cash flows contained in the Consolidated DIP Budget (the "**Cash Flow Target Variance**"). While the Cash Flow Target will be measured as of the approval date of a Sale, it is not payable until the first such Sale is consummated. The final determination of incremental positive cash flow will be adjusted to take into account any non-payment of any pre-filing or post-filing liabilities that were not paid from a timing perspective outside of the ordinary course of business. A copy of the Consolidated DIP Budget from August 10, 2018 through December 7, 2018 is attached hereto as **Exhibit "B"**.

48. The Asset Sale Target measures the Aralez Entities' ability to maximize the value of their assets by: (a) consummating one or more Sales; (b) generating incremental value above the purchase price consideration set forth in the bids made by the three Stalking Horse Purchasers; and/or (c) selling the Chapter 11 Entities' assets not included as part of the Stalking Horse Bids in a timely fashion. The Asset Sale Target is measured from the period commencing on August 10, 2018 and ending as of the consummation date of the Sales, provided that if the Sales or other sales of assets occur pursuant to multiple transactions, the date shall be the consummation of one or more sales that results in sale consideration of at least \$230 million in aggregate value.

49. The Performance Targets generally were chosen to ensure that the Aralez Entities maximize value for their stakeholders through, among other things: (a) minimizing the disruption to the Aralez Entities' business caused by the commencement of these cases; (b)

maximizing cost efficiencies; and (c) facilitating the successful sales of the Aralez Entities' assets at the highest or otherwise best offer(s) available.

50. The KEIP Participants' payout target level consists of, and is equally weighted between, the Cash Flow Target and the Asset Sale Target. The sum of both of these at the "target" payout level equals 50% of the base salary of all participants. If the "target" performance level is achieved for the Cash Flow Target and the "threshold" performance level is achieved for the Asset Sale Target, participants will receive a payment equal to 37.5% of each KEIP Participant's salary. This amount can be earned if the Aralez Entities (a) meet 100% of the Cash Flow Target and (b) consummate sales of assets prior to termination of employment (without cause or due to death or permanent disability) in an amount no less than \$230 million in the aggregate. Any additional KEIP payments are entirely dependent on the Aralez Entities exceeding the Cash Flow Target and/or obtaining combined sale consideration for the sales of their U.S. and/or Canadian assets equal to or greater than \$250 million, which is \$10 million more than that value of the sales under the Stalking Horse Agreements.

51. The Cash Flow Target and associated payouts are as follows:

Level	Payout as a Percentage of Salary	Payout as a Percentage of Target (as a percentage of weighted Target)	Cash Flow ("CF") Target Variance	Total Payouts
Below Target	0%	0%	Below Consolidated DIP Budget CF	\$0
Target	25%	100%	Consolidated DIP Budget CF	\$811,672
Stretch	37.5%	150%	Consolidated DIP Budget CF + \$2.4MM - \$4.1 million (incremental positive cash flow)	\$1,217,508
Super-Stretch	62.5%	250%	Consolidated DIP Budget CF + \$4.1 million or greater (incremental positive cash flow)	\$2,029,180

52. Payouts for the “target” performance level will be paid according to the chart above. However, payment above the “target” level for the “stretch” and “super-stretch” levels will be paid according to the actual performance achieved. For example, if actual performance exceeds the “target” level and is between the “stretch” and the “super stretch” levels, the payment will be one dollar of KEIP bonus paid for every two dollars of Cash Flow Target Variance achieved. The KEIP is self-funding in this regard due to the improved liquidity and cash position of the Aralez Entities.

53. Because the KEIP Participants generally provide services that benefit both the CCAA Entities and the Chapter 11 Entities, the Aralez Entities wanted to incentivize the KEIP Participants to maximize operational success for the entirety of the business. Therefore, the Cash Flow Target is based on the Consolidated DIP Budget for the CCAA Entities and the Chapter 11 Entities. Amounts to be awarded to the KEIP Participants for the “target” performance level will be split 50/50 between the CCAA Entities and the Chapter 11 Entities. Any incremental achievement above the “target” performance level (i.e., exceeding the Consolidated DIP Budget) will be paid proportionally between the CCAA Entities and the Chapter 11 Entities.

54. Meeting or exceeding the Cash Flow Target will require diligent efforts on the part of the KEIP Participants. The Aralez Entities have a limited number of parties with whom they directly conduct business. To meet the “target” performance level of the Cash Flow Target, the KEIP Participants must manage relationships with their wholesalers, customers, vendors and government entities on a day-to-day basis as these parties are the primary purchasers of the Applicants’ pharmaceutical products (and, in turn, their main sources of revenue). Further, earlier this year, the United States Food and Drug Administration approved several new generics for Toprol-XL, the Chapter 11 Entities’ main revenue generating product. The new generic competition may result in price erosion on this product and could lead to loss of material contracts and revenue. During the course of these proceedings, the KEIP Participants have been working hard to maintain these relationships as a result of the new general competition to ensure asset sales are maximized. The loss of any contract could materially impact the Aralez Entities’ revenues and, in turn, the ability to maximize the proceeds of Toprol Assets. These factors create risk in the Aralez Entities’ cash flows and any payout under the Cash Flow Target.

55. The Asset Sale Target (as a percentage of the weighted target) and associated payouts are as follows:

<b>Level</b>	<b>Payout as a Percentage of Salary</b>	<b>Payout as a Percentage of Target</b>	<b>Asset Sales Consideration</b>	<b>Total Payouts</b>
Below Threshold	NA	0%	\$0 - \$229.99 million	\$0
Threshold	18.75%	75%	\$230 - \$249.99 million	\$608,754
Target	25%	100%	\$250 - \$259.99 million	\$811,672
Stretch	37.5%	150%	\$260 million	\$1,217,508
Super-Stretch	62.5%	250%	\$280 million	\$2,029,180

56. No incremental amounts are paid for achievement of asset sales consideration between performance levels.<sup>3</sup>

57. If the minimum “threshold” performance level is met, then each KEIP Participant will be entitled to 18.75% of his or her salary. Because the KEIP Participants generally provide services that benefit the CCAA Entities and the Chapter 11 Entities, the Asset Sale Target is based on the aggregate consideration for the sale of all of the Aralez Entities’ assets and operations in the U.S. and in Canada and will be allocated on a pro rata percentage depending upon the ultimate purchase price, which is then further adjusted to allocate KEIP payments to the Chapter 11 Entities for the one participant whose services do not benefit the CCAA Entities. For example, based solely on the Stalking Horse Bids, it is anticipated that, at the “threshold” performance level, 76% of the total payments (i.e., \$426,641) would be paid by the Chapter 11 Entities and 24% of the total payments (i.e., \$146,113) would be paid by the CCAA Entities.

58. Meeting the Asset Sale Target is incentivizing for the KEIP Participants. In order to achieve the “threshold” performance level, the KEIP Participants must secure asset sales valued from \$230 million to \$249.99 million. The current asset value under the Stalking Horse Agreements is \$240 million, which includes a \$130 million credit bid. The “target” performance

---

<sup>3</sup> Any additional assumed liabilities by any purchaser in excess of those currently provided for in the Stalking Horse Bids and any proceeds from asset sales of the Aralez Entities’ assets in addition to the assets included in the Sales, in each case, will count toward the sale consideration listed in the column “Asset Sales Consideration” for purposes of calculating the KEIP payment in respect of the Asset Sales Target.

level for the aggregate purchase consideration for the Sales is between \$250 - \$259.99 million. This represents an increase of \$10 million to \$20 million over the Stalking Horse Bids.

59. For illustrative purposes, the payout structure (from both the Chapter 11 Entities and the CCAA Entities) on an aggregate basis if both Performance Targets are met at corresponding levels is set forth below:

<b>Level</b>	<b>Payout as a Percentage of Salary</b>	<b>Payout as a Percentage of Target</b>	<b>Net Operating Cash Flow Variance</b>	<b>Total Payouts</b>
Below Threshold for both Targets	NA	0%	\$<230 million + <100% of Consolidated DIP Budget CF	\$0
Threshold for Asset Sale Target and Target for Cash Flow Target	18.75%	75%	\$230 million - \$249.99 million	\$608,754
Target for both Targets	50%	100%	\$250 million - \$259.99 million + 100% Consolidated DIP Budget CF	\$1,623,344
Stretch for both Targets	75%	150%	\$260 million - \$279.99 million; + Consolidated DIP Budget CF + \$2.4 million - \$4.1 million (incremental positive cash flow)	\$2,435,016
Super-Stretch for both Targets	125%	250%	\$280 million or greater Consolidated DIP Budget CF; + \$4.1 million or greater (incremental positive cash flow)	\$4,058,360

60. Assuming the Aralez Entities meet the Cash Flow Target and close the sales currently contemplated under the Stalking Horse Agreements, the CCAA Entities would pay a total of \$520,161 in respect of the KEIP, representing \$374,049 on the Cash Flow Target component and \$146,113 on the Asset Sale Target component.

61. To ensure the reasonableness of the KEIP, the Aralez Entities sought assistance from A&M, who reviewed the KEIP in comparison to key executive incentive plans implemented in

similar cases to determine whether the KEIP payments are within the range of market practice as compared to incentive programs for similarly situated companies.

62. A&M first looked to the historical compensation of the KEIP Participants and the Aralez Entities' overall compensation plans. The senior executives had performance goals based on net revenues, adjusted EBITDA and adjusted net income as well as individual goals. Each performance goal was assigned a threshold, target, stretch and super-stretch level. The payout as a percentage of target for each level of achievement was the same as proposed here (i.e., below threshold (where applicable) 0%; threshold (where applicable) 75%; target 100%; stretch 150%; and super-stretch 250%). Another key element of the Aralez Entities' prepetition executive compensation program was the long-term equity-based incentive compensation. As a consequence of the Restructuring Proceedings, the previously granted equity incentive awards have no or little value and additional equity incentive awards during these proceedings will not occur.

63. A&M also compared the KEIP to other asset-sale and financial metric-based incentive plans implemented by companies that filed for chapter 11 protection. The comparison group involved companies: (a) that implemented incentive plans for which the payout was dependent in part on the sale of the company or significant assets thereof; (b) with prepetition assets between \$100 million and \$965 million; and (c) that implemented incentive plans for 15 or fewer employees (together, the "**KEIP Bankruptcy Peer Group**").

64. In comparison to the KEIP Bankruptcy Peer Group, A&M determined that the payments contemplated under the proposed KEIP are: (a) similar to other plans where there is no minimum payout; (b) near the average in terms of total cost with respect to the target payment; (c) below the average on a per person basis with the target plan; and (d) below the maximum potential payout when compared to the Performance Targets' super-stretch performance level.

65. The CCAA Entities also discussed the KEIP with the Monitor and obtained its feedback prior to finalizing the program.

66. The termination provisions in the KEIP are identical to the termination provisions in the KERP.

### **E. The Key Employee Charge**

67. The CCAA Entities contemplate that amounts owing under the KERP and the KEIP would be secured by the Key Employee Charge, up to the maximum amount of \$2.8 million, which consists of \$256,710 for the aggregate bonus pool for the Canadian KERP Participants and approximately \$2.5 million of the aggregate bonus pool for KEIP Participants in Canada. In order for the CCAA Entities to be allocated a payout of this magnitude, the CCAA Entities' cash flow would have a favourable variance of at least \$4.1 million, with the Chapter 11 Entities failing to realize a cash flow variance of 100% of target, and the sale of the CCAA Entities assets would exceed \$102 million, with the Chapter 11 Entities' assets not exceeding the value of the Vimovo Stalking Horse Agreement and Toprol Stalking Horse Agreement.

68. Each Key Employee will only obtain the benefit of the Key Employee Charge up to their respective individual entitlements under the KERP or the KEIP.

69. The Key Employee Charge will rank subordinate to the Administration Charge, the DIP Lender's Charge (as defined in the Initial Order) and the Bid Protections Charge (as defined in the Process Order) but in priority to the D&O Charge and the Transactional Charge (as defined in the Initial Order).

70. Deerfield does not object to the granting of the Key Employee Charge.

71. The Key Employee Charge does not include a charge for the individual who does not provide services to the CCAA Entities, whose KEIP payments (if any) are 100% attributable to the Chapter 11 Entities.

### **F. Sealing the Confidential Supplement**

72. The Confidential Supplement includes a detailed listing of the KERP and KEIP Participants along with their current positions, salaries and proposed payments under the KERP and KEIP. Salary information is highly personal to the Key Employees and is not generally made public by the Aralez Entities. Further, most of the CCAA Entities' employees are not proposed to receive payments under the KERP or the KEIP. Identifying who is part of these programs and what amounts they will be paid on the closing of the transaction (if any, in the case of the KEIP) may create tension at a time when these key employees particularly need to coordinate with the other employees to close a transaction and maintain operational efficiency. In order to protect the KERP Participants and to minimize disruption during the

CCAA proceedings, the Applicants are seeking an order sealing the Confidential Supplement subject to a further court order.

**III. CONCLUSION**

73. I am of the view that the terms of the proposed KERP and KEIP are fair and reasonable in the circumstances, will provide an incentive for the Key Employees to continue to perform their critical roles throughout the Applicants' restructuring, and are, therefore, in the best interests of the Applicants and their stakeholders. Further, the KERP and KEIP are supported by a number of key stakeholders in the Restructuring Proceedings (including the Monitor and Deerfield).

74. The Confidential Supplement contains individually identifiable personal and financial information of the Key Employees. In order to protect the Key Employees and to minimize disruption during the CCAA Proceedings, the Applicants seek an order sealing the Confidential Supplement pending further order of this Court.

SWORN BEFORE ME at the Town of  
Devon, State of Pennsylvania, on  
November \_\_\_\_, 2018.

\_\_\_\_\_  
Commissioner for Taking Affidavits

\_\_\_\_\_  
**ADRIAN ADAMS**

IN THE MATTER OF THE COMPANIES' CREDITORS ARRANGEMENT ACT, R.S.C. 1985, c. C-36, AS AMENDED

Court File No. CV-18-603054-00CL

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT  
OF ARALEZ PHARMACEUTICALS INC. AND ARALEZ PHARMACEUTICALS CANADA  
INC.

**ONTARIO  
SUPERIOR COURT OF JUSTICE  
(COMMERCIAL LIST)**

Proceeding commenced at Toronto

**AFFIDAVIT OF ADRIAN ADAMS SWORN ON  
NOVEMBER , 2018**

**STIKEMAN ELLIOTT LLP**  
Barristers & Solicitors  
5300 Commerce Court West  
199 Bay Street  
Toronto, Canada M5L 1B9

**Ashley Taylor** LSO#: 39932E  
Tel: (416) 869-5236  
E-mail: [ataylor@stikeman.com](mailto:ataylor@stikeman.com)

**Maria Konyukhova** LSO#: 52880V  
Tel: (416) 869-5230  
E-mail: [mkonyukhova@stikeman.com](mailto:mkonyukhova@stikeman.com)

**Kathryn Esaw** LSO#: 58264F  
Tel: (416) 869-6820  
E-mail: [kesaw@stikeman.com](mailto:kesaw@stikeman.com)  
Fax: (416) 947-0866

Lawyers for the Applicants

TAB A

**EXHIBIT "A"**

referred to in the Affidavit of

**ADRIAN ADAMS**

Sworn November , 2018

---

Commissioner for Taking Affidavits

**BROWN RUDNICK LLP**

Robert J. Stark  
Howard S. Steel  
Uchechi Egeonuigwe  
Seven Times Square  
New York, NY 10036  
Telephone: (212) 209-4800  
Facsimile: (212) 209-4801

-and-

Steven B. Levine  
One Financial Center  
Boston, MA 02111  
Telephone: (617) 856-8200  
Facsimile: (617) 856-8201

*Counsel to the Official Committee of Unsecured Creditors*

**UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF NEW YORK**

---

In re:	:	Chapter 11
	:	
Aralez Pharmaceuticals US Inc., <i>et al.</i> , <sup>1</sup>	:	Case No. 18-12425-mg
	:	
Debtors.	:	(Jointly Administered)
	:	

---

**OBJECTION OF THE OFFICIAL COMMITTEE OF  
UNSECURED CREDITORS TO THE DEBTORS' MOTION  
FOR ORDER AUTHORIZING IMPLEMENTATION OF (A) KEY  
EXECUTIVE INCENTIVE PLAN AND (B) KEY EMPLOYEE RETENTION PLAN**

<sup>1</sup> The Debtors in these Chapter 11 cases and the last four digits of each Debtor's federal taxpayer identification number and/or its equivalent are as follows: Aralez Pharmaceuticals Holdings Limited (5824); Aralez Pharmaceuticals Management Inc. (7166); POZEN Inc. (7552); Aralez Pharmaceuticals Trading DAC (1627); Aralez Pharmaceuticals US Inc. (6948); Aralez Pharmaceuticals R&D Inc. (9731); Halton Laboratories LLC (9342). For purposes of these chapter 11 cases, the Debtors' mailing address is Aralez Pharmaceuticals, c/o Prime Clerk LLC, P.O. Box 329003, Brooklyn, NY 11232.

**TABLE OF CONTENTS**

	<u>Page</u>
PRELIMINARY STATEMENT .....	1
BACKGROUND .....	4
I.    General Case Background.....	4
II.   The Proposed KEIP.....	5
ARGUMENT .....	9
I.    Applicable Legal Standard Governing Consideration Of The KEIP.....	9
II.   The KEIP Is A Disguised Insider Retention Plan That Fails To Satisfy Bankruptcy Code Section 503(c)(1). .....	12
A.  Asset Sale Target. ....	12
B.  Net Operating Cash Flow Target. ....	13
III.  The KEIP Does Not Satisfy Bankruptcy Code Sections 363(b)(1) and 503(c)(3).....	15
A.  The KEIP Is Not Justified By The Facts and Circumstances Of The Chapter 11 Cases.....	15
B.  The KEIP Is Not A Sound Exercise Of The Debtors’ Business Judgment. ....	16
RESERVATION OF RIGHTS .....	18
CONCLUSION.....	19

**TABLE OF AUTHORITIES**

	<b>Page(s)</b>
<b>Cases</b>	
<i>In re Borders Group Inc.</i> , 453 B.R. 459 (Bankr. S.D.N.Y. 2011) .....	4, 10, 11, 12
<i>In re Ciber, Inc.</i> , Case No. 17-10772 (BLS) (Bankr. D. Del. May 11, 2017) .....	17
<i>In re Dana Corp.</i> , 358 B.R. 567 (Bankr. S.D.N.Y. 2006) .....	11, 12, 15
<i>In re Dana Corp.</i> , 351 B.R. 96 (Bankr. S.D.N.Y. 2006) .....	10
<i>In re Global Home Prods., LLC</i> , 369 B.R. 778 (Bankr. D. Del. 2007) .....	10, 11, 12
<i>In re Hawker Beechcraft, Inc.</i> , 479 B.R. 308 (Bankr. S.D.N.Y. 2012) .....	10, 11, 14, 16
<i>In re Mesa Air Group, Inc.</i> , Case No. 10-10018 (MG), 2010 WL 3810899 (Bankr. S.D.N.Y. Sept. 24, 2010) .....	4, 10, 11
<i>In re Residential Capital, LLC</i> , 491 B.R. 73 (Bankr. S.D.N.Y. 2013) .....	9, 10, 12, 16
<i>In re Residential Capital, LLC</i> , 478 B.R. 154 (Bankr. S.D.N.Y. 2013) .....	<i>passim</i>
<i>In re Velo Holdings, Inc.</i> , 472 B.R. 201 (Bankr. S.D.N.Y. 2012) .....	4, 9, 10, 11
<i>In re Visteon Corp., et al</i> , No. 09-11786 (Bankr. D. Del. 2009) .....	11
<b>Statutes</b>	
11 U.S.C. 503(c)(1) .....	9
11 U.S.C. § 1108 .....	4
Bankruptcy Code Sections 363 and 503(c)(3) .....	9

Bankruptcy Code Section 363(b).....11  
Bankruptcy Code Section 363(b)(1) .....15, 16  
Bankruptcy Code Section 503(c) ..... *passim*  
Bankruptcy Code Section 503(c)(1) ..... *passim*  
Bankruptcy Code Section 503(c)(3) .....10, 11, 15, 16  
Bankruptcy Code Sections 1107 .....4

The Official Committee of Unsecured Creditors (the “Committee”), appointed in the Chapter 11 cases of Aralez Pharmaceuticals US Inc. and its affiliated debtors and debtors in possession (collectively, the “Debtors”), by its undersigned counsel, hereby submits its Objection to the *Motion For Order Authorizing Implementation Of (A) Key Executive Incentive Plan And (B) Key Employee Retention Plan* (the “Motion”) [Docket No. 152].<sup>1</sup> In support of this Objection, the Committee respectfully states as follows:

**PRELIMINARY STATEMENT**

1. By the Motion, the Debtors seek approval of: (i) a key executive incentive plan (the “KEIP”) for eight C-Suite executives (the “Executives”), with aggregate awards between \$1.1 million and \$3.7 million; and (ii) a key employee retention plan (the “KERP”) for fourteen non-management employees sharing a bonus pool of \$826,250.

2. The Committee recognizes that, as a general matter, incentive and retention plans that meet applicable statutory requirements and are well-designed to achieve value-accretive objectives are appropriate. With that framework in mind, and after conducting appropriate diligence, the Committee has determined that the KERP should be approved.

3. The Committee does not, however, reach the same conclusion respecting the KEIP. As discussed herein, the KEIP does not comport with Section 503(c) and is not designed to achieve value-accretive objectives. Rather, it bears the hallmarks of a disguised retention plan, with targets that are quintessential “lay-ups” and that reward the Executives for simply showing up for work (for which they otherwise draw salary) until estate assets are sold over the next few weeks.

---

<sup>1</sup> Capitalized terms not otherwise defined in this Objection shall have the meanings set forth in the Motion.

4. KEIP payments are triggered by two types of performance targets. *First*, the “Asset Sale Target” is based on proceeds received from the sales of the U.S. and Canadian assets. While asset sale targets are not an uncommon feature of incentive plans, the targets are typically set at aspirational (i.e., *incentive*) levels. Not so here.

5. To begin, the Executives will be paid bonuses (over and above salary) exceeding \$560,000 if estate assets are sold for \$175 million. For all intents and purposes, the Executives have already “banked” these bonuses—without having to do anything other than showing up for work—because the Debtors today hold in hand “Stalking Horse Bids” of \$240 million. This situation does not rationalize better at elevated levels, and value is not generated for any creditors other than Deerfield until the “Super Stretch Target” is met. If the Asset Sales yield only \$10 million more than the Stalking Horse Bids (i.e., only 4.2% improvement to the bids in hand), Executives’ bonuses grow to about \$750,000. Add only another \$10 million in sales proceeds (i.e., the so-called “Stretch Target” of \$260 million, or 8.33% improvement to the Stalking Horse Bids) and the Executives are paid \$1.12 million. The “Super-Stretch Target,” set at \$280 million, yields \$1.87 million. High bonuses might make sense, perhaps even at such modest increments above the Stalking Horse Bids, if the Motion (or the Committee's own diligence) revealed any basis to conclude that the Executives—as opposed to the business assets themselves and/or the Debtors' financial advisors and investment bankers—are the ones driving the auction results. We have no such evidence.

6. *Second*, KEIP bonuses are earned based on “Net Operating Cash Flow Targets,” or levels of business earnings. This also is a common feature of incentive plans, but only where the targets are (i) forward-looking for some appreciable period of time, and (ii) again, set at aspirational levels. Here too, the KEIP fails to serve its purpose.

7. The cash flow giving rise to targeted bonuses is measured only during the 18-week period contained in the Debtors' DIP budget (for \$5 million of DIP financing), and cuts off when the Sale Order is entered. Almost axiomatic, a cash flow target covering such a remarkably short period of time and relatively modest DIP financing, and determined *after* (perhaps weeks after) the Sale Order has been entered, has absolutely nothing to do with enhancing estate value. Presumptively, an 18-week measuring period is a woefully insufficient time for the Executives to do anything meaningful to impact cash flow, other than simply showing up for work and following their pre-sale business plan. Moreover, the level of effort that goes into managing a budget under a \$5 million DIP financing is whole lot less exacting than if the DIP financing was \$100 million. And, regardless, an incentive scheme that produces data available only *after* the auction has concluded is a scheme untethered to any appreciable value-enhancing strategy (i.e., there is no "audience" for improved performance data, other than the already-approved purchaser).

8. Furthermore, the "Net Operating Cash Flow Targets" are far from aspirational. The "Threshold" performance target level is actually *under*-performance: If the business generates only 95% of DIP budget forecasts, the Executives are paid \$560,000. If the business simply meets DIP budget forecasts, Executives' bonuses grow to \$750,000. If cash flow jumps only by \$2.3 million, the bonuses grow to \$1.12 million. And, at a mere \$3.7 million over DIP budget forecasts, the Executives are paid \$1.87 million in bonuses. And, this is before any assessment is made as to whether the Debtors' DIP budget incorporates any opportunistic "massaging" by management.

9. *Finally*, special observation should be made of the fact that Executives earn both "Asset Sale Target" and "Net Operating Cash Flow Target" bonuses: no crediting, no off-sets.

Special observation also should be made of the fact that, today, the Executives run what is essentially a “virtual” business, selling products developed by others, manufactured by others, and transported by others into pre-established channels and networks. These eight individuals need only come to the office each day, conduct business as usual and otherwise help the Debtors’ professionals run the sales process (for which they are paid healthy salaries) and, with a little luck, collect an incremental \$3.74 million over salary. It is retentive in nature and functionality.

10. The KEIP is not consistent with Section 503(c). It is not in keeping with surrounding jurisprudence, including this Court’s decisions in *Rescap*, *Borders*, *Velo* and *Mesa Air*. It should be denied.

## **BACKGROUND**

### **I. General Case Background.**

11. On August 10, 2018 (the “Petition Date”), each of the Debtors filed with this Court a voluntary petition for Chapter 11 relief. On that same date, the Debtors’ parent-company (Aralez Pharmaceuticals Inc.) as well as a Canadian affiliate (Aralez Pharmaceuticals Canada Inc.) filed for CCAA relief with the Ontario Superior Court of Justice. Respecting the United States proceedings, the Debtors remain in the possession of their assets pursuant to Bankruptcy Code Sections 1107 and 1108.

12. On August 27, 2018, the United States Trustee for Region 2 appointed the Committee.<sup>2</sup> As of the date hereof, no trustee or examiner has been appointed in any of the Debtors’ cases.

13. Prior to the Petition Date, the Debtors engaged Moelis & Company LLC

---

<sup>2</sup> See *Notice of Appointment of Official Committee of Unsecured Creditors* [Docket No. 53].

(“Moelis”) to assist in marketing the Debtors’ assets.<sup>3</sup> The prepetition marketing process managed by Moelis resulted in the execution of letters of intent with Deerfield,<sup>4</sup> and submission of Stalking Horse Agreements shortly thereafter. The aggregate value of the Stalking Horse Bids is \$240 million or \$65 million more than the “Threshold” Asset Sale Target necessary for the Executives to start receiving lucrative bonuses under the KEIP. It is also approximately \$38.6 million short of the purported secured debt hurdle for value to flow to unsecured creditors.

14. Under the Bid Procedures Order, the Auction and Sale Hearing are scheduled to occur November 29, 2018 and December 4, 2018, respectively. Thus, within the two weeks between the hearing on the Motion and the Auction, the Executives have extremely limited time and capability to positively impact the value proposition of this case. The Debtors have few remaining employees and are essentially running a “virtual” pharmaceutical business. The Debtors point to no specialized expertise or extra efforts by the Executives warranting the bonuses under the KEIP, and the Committee is otherwise aware of none.

## **II. The Proposed KEIP.**

15. The payments under the KEIP are premised upon the Debtors achieving certain specified performance targets, which include: (i) financial performance targets for the Debtors and Canadian Debtors (the “Net Operating Cash Flow Target”); and (ii) aggregate proceeds from the asset and/or stock sales in U.S. and Canada (the “Asset Sale Target,” and together with Net Operating Cash Flow Target, the “Performance Target”).

16. The Asset Sale Target is broken down into four levels which increase the KEIP payout as each level is surpassed. The “Threshold” is \$175–\$249.99 million in aggregate Asset

---

<sup>3</sup> See Declaration Of Michael Kaseta In Support Of Chapter 11 Petitions And First Day Pleadings at ¶ 35 [Docket No. 4].

<sup>4</sup> *Id.* at ¶ 36-37.

Sales. The “Target” level is \$250–\$259.99 million. The “Stretch” level is \$260–\$280 million. Lastly, the “Super-Stretch” level is anything over \$280 million in total asset sales.

17. Below is a chart summarizing the Asset Sale Target payout schedule:

<b>Asset Sales</b>				
<b>Level</b>	<b>Payout as a Percentage of Salary</b>	<b>Payout as a Percentage of Target</b>	<b>Asset Sales Consideration</b>	<b>Total Payouts</b>
Below Threshold	NA	0%	\$0 - \$175 million	\$0
Threshold	18.75%	75%	\$175 - \$249.99 million	\$561,073
Target	25%	100%	\$250 - \$259.99 million	\$748,097
Stretch	37.5%	150%	\$260 million	\$1,122,146
Super-Stretch	62.5%	250%	\$280 million	\$1,870,243

18. Thus, to achieve the “Threshold” Asset Sale Target and over half a million dollars of bonuses, the Debtors need only consummate the Stalking Horse Bids, which were negotiated pre-petition and have an aggregate purchase price of \$240 million. If the Executives meet the “Stretch” or the “Super-Stretch” Asset Sale Target, they would receive \$1.1 million and 1.8 million, respectively, in total payouts.

19. The Net Operating Cash Flow Target measures the ability of the Debtors and the Canadian Debtors to meet or exceed the net operating cash flow projected in the 18-week consolidated DIP budget for a \$5 million DIP financing, with a projected Total Net Operating Cash Flow of negative \$9.9 million over the 18 week period (on total sales of less than \$27 million).

20. This Net Operating Cash Flow Target is measured as of the entry of the Sale

Order. The Net Operating Cash Flow Target is also broken down into four levels which increase the KEIP payout as each level is surpassed. The “Threshold” level is met if the Debtors meet between 95% and 99.99% of the Consolidated DIP Budget Net Operating Cash Flow (the “NOCF”). The “Target” level is met if the Debtors meet the NOCF. The “Stretch” level is met if the Debtors meet the NOCF plus add \$2.3 million to \$3.699 million in incremental positive cash flow. Lastly, the “Super-Stretch” level is met if the Debtors meet the NOCF plus add \$3.7 million or greater in incremental positive cash flow.

21. Below is a chart summarizing the Net Operating Cash Flow Target payout schedule:

<b>Financial Performance: Net Operating Cash Flow Target</b>				
<b>Level</b>	<b>Payout as a Percentage of Salary</b>	<b>Payout as a Percentage of Target (as a percentage of weighted Target)</b>	<b>Net Operating Cash Flow Target Variance</b>	<b>Total Payouts</b>
Below Threshold	NA	0%	<95% of NOCF	\$0
Threshold	18.75%	75%	95% - 99.99% of NOCF	\$561,073
Target	25%	100%	NOCF	\$748,097
Stretch	37.5%	150%	NOCF + \$2.3 million - \$3.699 million (incremental positive cash flow)	\$1,122,146
Super-Stretch	62.5%	250%	NOCF + \$3.7 million or greater (incremental positive cash flow)	\$1,870,243

22. The Debtors state that, in order to achieve the “Threshold” NOCF target, the Executives under the KEIP must “manage relationships with their wholesalers, customers, vendors, and government entities.” See Motion ¶ 51. In other words, the KEIP “incentivizes” the Executives to perform their basic job responsibilities, in a way already mandated by their

fiduciary duties.

23. The overall Performance Target payout is equally weighted between Net Operating Cash Flow Target and Asset Sale Target.<sup>5</sup> The payout structure on an aggregate basis if both Performance Targets are met at corresponding levels is set forth below.<sup>6</sup> The Debtors, without any support, evidence or explanation, contend in conclusory fashion that “achieving even the threshold level of the Performance Targets is challenging.”<sup>7</sup> As set forth below, that is far from the case and an unsupported proposition.

<b>Aggregate KEIP Payout Structure</b>			
<b>Level</b>	<b>Payout as a Percentage of Salary</b>	<b>Performance Target</b>	<b>Total Payouts</b>
Below Threshold	NA	Asset Sales: \$<175 million Cash Flow: <95% of NOCF	
Threshold	37.5%	Asset Sales: \$175 – \$249.99 million Cash Flow: + 95% – 99.99% of NOCF	\$1,122,146
Target	50%	Asset Sales: \$250– \$259.99 million Cash Flow: NOCF	\$1,496,194
Stretch	75%	Asset Sales: \$260 – \$279.99 million Cash Flow: NOCF + \$2.3 million – \$3.799 million (incremental positive cash flow)	\$2,244,291
Super-Stretch	125%	Asset Sales: \$280 million or greater Cash Flow: NOCF + \$3.7 million or greater (incremental positive cash flow)	\$3,740,485

---

<sup>5</sup> *Id.*

<sup>6</sup> *Id.* at 37.

<sup>7</sup> Motion at ¶¶ 38, 51-52, and 56.

## ARGUMENT

### **I. Applicable Legal Standard Governing Consideration Of The KEIP.**

24. Key executive incentive plans are analyzed under Bankruptcy Code Section 503(c)(1) to determine if they are primarily incentivizing or retentive in nature. If the KEIP is primarily retentive and the payment is to an insider, it must satisfy the strict requirements of Bankruptcy Code Section 503(c)(1).<sup>8</sup> If the KEIP is primarily incentivizing, it will be permitted if it satisfies Bankruptcy Code Sections 363 and 503(c)(3). *See generally In re Residential Capital, LLC (“Rescap I”)*, 478 B.R. 154, 169-171 (Bankr. S.D.N.Y. 2013); *In re Residential Capital, LLC (“Rescap II”)*, 491 B.R. 73, 82-84 (Bankr. S.D.N.Y. 2013) (noting that when a KEIP is “designed to motivate employees to achieve specified performance goals, it is primarily incentivizing, and thus not subject to section 503(c)(1).”).

25. Bankruptcy Code Section 503(c)’s restriction on retention plans for insiders, added to the Bankruptcy Code in 2005, is intended to “limit the scope of ‘key employee retention plans’ and other programs providing incentives to management of the debtor as a means of inducing management to remain employed by the debtor.” *In re Velo Holdings, Inc.*, 472 B.R. 201, 209 (Bankr. S.D.N.Y. 2012) (citing 4 Collier on Bankruptcy ¶ 503.17 (15th rev. ed. 2007)). Its genesis was to “eradicate the notion that executives were entitled to bonuses simply for

---

<sup>8</sup> Specifically, Bankruptcy Code Section 503(c)(1) provides:  
there shall neither be allowed, nor paid . . . a transfer made to . . . an insider of the debtor for the purpose of inducing such person to remain with the debtor’s business . . . unless (A) the transfer . . . is essential to retention of the person because the individual currently has a bona fide job offer from another business at the same or a greater rate of compensation; (B) the services provided by the person are essential to the survival of the business; and (C) either — (i) the amount of the transfer to the insider is not greater than ten (10) times the amount of the mean transfer of a similar kind given to non-management employees for any purpose during the calendar year of the insider transfer, or (ii) if no such similar transfers were made to non-management employees during the calendar year, the amount of the insider transfer does not exceed twenty-five percent of any similar transfer made to the insider for any purpose during the prior calendar year.

See 11 U.S.C. 503(c)(1).

staying with the Company through the bankruptcy process.” *Rescap I*, 478 B.R. at 169 (quoting *In re Global Home Prods., LLC*, 369 B.R. 778, 784 (Bankr. D. Del. 2007)); accord *In re Hawker Beechcraft, Inc.*, 479 B.R. 308, 312-13 (Bankr. S.D.N.Y. 2012); *In re Velo Holdings, Inc.*, 472 B.R. at 209.

26. The proponent of the plan bears the burden of proving that the plan is truly incentivizing, and therefore governed by Section 503(c)(3), rather than a disguised retention plan prohibited by Section 503(c)(1). See *Rescap I*, 478 B.R. at 170; *In re Hawker Beechcraft*, 479 B.R. at 313; *In re Mesa Air Group, Inc.*, Case No. 10-10018 (MG), 2010 WL 3810899 at \*3 (Bankr. S.D.N.Y. Sept. 24, 2010). A debtor’s characterization of a plan as incentive-based is not determinative. *Rescap II*, 491 B.R. at 83.

27. Bankruptcy Courts have frequently uncovered retention plans masquerading as incentive plans, finding that “courts must be wary of attempts to characterize what is essentially an insider retention plan as an ‘incentive’ plan ‘to bypass the requirements of section 503(c)(1).’” *Hawker Beechcraft*, 479 B.R. at 313 (quoting *In re Velo Holdings, Inc.*, 472 at 209); see also *In re Borders Group Inc.*, 453 B.R. 459, 470 (Bankr. S.D.N.Y. 2011); *In re Dana Corp.* (“*Dana I*”), 351 B.R. 96, 102 n.3 (Bankr. S.D.N.Y. 2006) (“If it walks like a duck ([retention plan]) and quacks like a duck ([retention plan]), it’s a duck ([retention plan]).”). Courts look with disfavor upon such attempts. See *In re Velo Holdings*, 472 B.R. at 209; *Rescap II*, 491 B.R. at 83; *Borders Group*, 453 B.R. at 470-71.

28. For a plan to be incentivizing and thus fall under Bankruptcy Code Section 503(c)(1), it should be tied to significant goals that are difficult to achieve. *Rescap I*, 478 B.R. at 164 (when analyzing a KEIP, “the issue is whether each of these hurdles is sufficiently challenging and incentivizing”); see also *Hawker Beechcraft*, 479 B.R. at 313 (performance

targets must be “designed to motivate insiders to rise to a challenge”); *In re Velo Holdings*, 472 B.R. at 209 (section 503(c) requires “a set of challenging standards and high hurdles”) (internal quotations omitted); *Mesa Air Group*, 2010 WL 3810899 at \*4 (incentive plans must “motivate [] the employees to achieve certain goals”); *Global Home Prods.*, 369 B.R. at 784–85 (section 503(c) “impose[s] a set of challenging standards debtors must meet”); *See* Transcript of Hearing, October 7, 2009, *In re Visteon Corp., et al*, No. 09-11786 (Bankr. D. Del. 2009), [Docket. No. 1132] at 158:1 - 159:1 (“the Court has to be careful that what is said to be an Incentive Plan is actually an Incentive Plan and that the targets that have to be reached are not so easy that they in effect are softballs that can be easily met--or hit.”).

29. If a KEIP is found to be truly incentivizing, the Debtors then have the burden to prove that the development of the KEIP was: (1) a proper exercise of their business judgment, under Bankruptcy Code Section 363(b); and (2) that it is justified by the facts and circumstances of the case under Bankruptcy Code Section 503(c)(3). *See In re Dana Corp.* (“*Dana II*”), 358 B.R. 567, 584 (Bankr. S.D.N.Y. 2006). The “facts and circumstances of the case” test under Bankruptcy Code Section 503(c) is “no different than the business judgment standard under section 363(b).” *Borders*, 453 B.R. at 473; *see also In re Velo Holdings*, 472 B.R. at 212; *Mesa Air Group*, 2010 WL 3810899, at \*4. Accordingly, the Debtors must establish that any incentive payment is an actual, necessary cost or expense of preserving the estate. *See Dana II*, 358 B.R. at 575.

30. Factors that courts consider when determining whether a KEIP meets the business judgment test include:

- (i) whether there is a reasonable relationship between the plan proposed and the results to be obtained;
- (ii) whether the cost of the plan is reasonable in the context of the debtor’s assets, liabilities and earning potential;
- (iii) whether the scope of the plan is fair and reasonable, whether it applies to all employees, whether it

discriminates unfairly; (iv) whether the plan or proposal is consistent with industry standards; (v) the due diligence efforts of the debtor in investigating the need for a plan, analyzing which key employees need to be incentivized, and what is generally applicable in a particular industry; and (vi) whether the debtor received independent counsel in performing due diligence and in creating and authorizing the incentive compensation.

*See Rescap II*, 491 B.R. at 84-85 (citing *Dana II*, 358 B.R. at 584); *Borders*, 453 B.R. at 474-77 (same); *Global Home Prods.*, 369 B.R. at 786 (same).

**II. The KEIP Is A Disguised Insider Retention Plan That Fails To Satisfy Bankruptcy Code Section 503(c)(1).**

31. As presently proposed, the KEIP Payments are too easily “earned.” They are the quintessential “lay-ups.” Given the Executives’ limited means of influence over cash-flows and the quantum of the Stalking Horse Bids, the Performance Targets amount to nothing more than requiring the Executives to show up for work (for which they draw salary). The Debtors can present no evidence that the KEIP is “directly tied to *challenging* financial and operational goals for the businesses, tailored to the facts and circumstances of the case” which is required to satisfy Bankruptcy Code Section 503(c)(1). *In re Rescap I*, 478 B.R. at 173 (emphasis added). Thus, the KEIP should be denied.

**A. Asset Sale Target.**

32. The Asset Sale Target requires no effort by the Executives to meet the Threshold payout amount. The Stalking Horse Bids alone deliver \$561,073 to the executives. To obtain this award, the Executives are simply required to remain with the Debtors until the closing of the Sales that were substantially negotiated pre-petition. Levels above the Stalking Horse Bids are too low and, separately, too far out of the Executives' control to warrant different analysis under Section 503(c). This reflects a pure “pay to stay” plan. *See Rescap II*, 491 B.R. at 83.

33. The Debtors maintain that the Executives’ knowledge of the business and day-to-day operations makes them critically important “to maximize the value of the estates and ensure

a successful sale process.”<sup>9</sup> However, the day-to-day involvement and oversight by the Executives is nothing more than the discharge of their fiduciary duties and does not support the allowance and payment of a bonus award, especially given the limited time remaining until the conclusion of these cases. *See Rescap I*, 478 B.R. at 168 (“While it is no doubt true that the requirements of these chapter 11 cases and the proposed assets sales have altered or increased the work required of insiders, such would also be true in virtually all chapter 11 cases; section 503(c) requires more than increased responsibilities to justify increased pay for insiders[.]”).

34. Moreover, given the impending November 29, 2018 Auction and December 4, 2018 Sale Hearing, it is unclear what if any extra efforts the Executives bring to bear on maximizing the value the Sales process that is not otherwise covered by the Debtors’ case professionals. The Debtors present no factual support that the Asset Sale Target is sufficiently challenging or that the Executives will have to “do more” to realize substantial bonuses—while creditors face the prospects of limited or no recoveries. Accordingly, the Asset Sale Target is not sufficiently challenging and the KEIP must be denied.

**B. Net Operating Cash Flow Target.**

35. As indicated above, this aspect of the KEIP is utterly untethered to any value-maximizing agenda, and must be contextualized. The measuring period is far too short to facilitate operational changes, and the relevant performance data will not become available until after the winning bidder has been determined, and it is only a \$5 million DIP financing to manage. With only fourteen employees remaining, the Debtors are essentially running a “virtual” pharmaceutical business. The Debtors do not have any manufacturing capabilities and cannot change the price point of their products to alter cash flows. Thus, the Executives have

---

<sup>9</sup> Motion at ¶¶ 28, 63, 65.

limited ability to drive “improved” operating cash flow results, and the Net Operating Cash Flow Target seems an unlikely benchmark here to measure the Executives’ contributions to increasing estate value.

36. Moreover, simply meeting the Net Operating Cash Flow Target cannot be considered an aspirational business objective. Indeed, the Debtors *conceded* to this Court that the DIP budget simply reflects reasonable expectations. *See* DIP Financing Motion at ¶ 24 [Docket No. 12] (the “Budget . . . is based on assumptions believed by the Loan Parties to be reasonable”). Failing to comply with the DIP Budget constitutes a default under the DIP Credit Agreement. *See* DIP Credit Agreement 6.11; 8.1(b) [Docket No. 12]. If the Consolidated DIP Budget was characterized as a “high hurdle” to meet, as the Debtors now allege in connection with the Motion, it is unlikely the Debtors use of cash collateral would have been approved. Thus, the NOCF metric falls far short of the requirement that “the proposed targets . . . motivate insiders to rise to a challenge” and not “merely report to work.” *Hawker Beechcraft*, 479 B.R. at 313.

37. Where challenging performance metrics do not exist, a KEIP is primarily retentive and should not be approved absent the debtor satisfying the strict requirements of Bankruptcy Code Section 503(c)(1). The Debtors allege that Bankruptcy Code Section 503(c)(1) does not apply here. *See* Motion ¶ 47. They are wrong. The Debtors have failed to present sufficient evidence that the Performance Targets are tied to challenging and incentivizing goals as opposed to easily obtainable targets designed to provide retention bonuses to insiders. Because the KEIP does not contain adequately challenging performance targets, it is a disguised retention plan that must be analyzed under Bankruptcy Code Section 503(c)(1). The Debtors,

have failed to satisfy their burden of demonstrating the KEIP is a true incentive plan and therefore the KEIP should be denied.

**III. The KEIP Does Not Satisfy Bankruptcy Code Sections 363(b)(1) And 503(c)(3).**

**A. The KEIP Is Not Justified By The Facts and Circumstances Of The Chapter 11 Cases.**

38. Even if the Court were to find that the KEIP is incentivizing and thus subject to Bankruptcy Code Section 503(c)(3), the program still falls short of applicable statutory requirements. Bankruptcy Code Section 503(c)(3) prohibits transfers to insiders that are “not justified by the facts and circumstances of the case, including transfers made to, or obligations incurred for the benefit of, officers, managers, or consultants hired after the date of the filing of the petition.” 11 U.S.C. § 503(c)(3).<sup>10</sup>

39. The Debtors are in the process of completing a sale of substantially all of their assets in approximately four weeks and the Stalking Horse Bids were primarily negotiated prepetition. The Executives should not benefit from simply showing up for work over the next few weeks while Deerfield forecloses on its collateral and unsecured creditors are severely impaired. The KEIP is not tied to the consummation of a Chapter 11 plan, or the creation of distributable value for unsecured creditors. Further, the Motion fails to explain what tasks the Executives, during the short amount of time left in these cases, will perform above and beyond their typical job functions or those already being performed by the Debtors’ case professionals. In light of these facts and circumstances, the KEIP is not justified under Bankruptcy Code Section 503(c)(3).

---

<sup>10</sup> Courts determine whether section 503(c)(3) has been satisfied by examining whether the compensation plan meets the “sound business judgment” test. *See, e.g., Dana II*, 358 B.R. at 576-577 (collecting cases).

**B. The KEIP Is Not A Sound Exercise Of The Debtors' Business Judgment.**

40. The Debtors fail to demonstrate that the KEIP is a sound exercise of their business judgment under Bankruptcy Code Section 363(b)(1), and the factors set forth in *Rescap II*.<sup>11</sup> See *Rescap II*, 491 B.R. at 84-85 (citing *Borders*, 453 B.R. at 473). Under these factors, it is clear that the KEIP is inappropriate.

41. *First*, the KEIP is not constructed to catalyze improved asset sales or performance. The Executives meet the “Threshold” if the Debtors achieve \$175 million in Asset Sales and 95% of the NOCF. Therefore, the Executives achieve the Performance Target by achieving *worse* than the status quo. An incentive plan for executives should be tied to additional contributions and benefits to the estates and creditors, and should entail goals that are challenging to accomplish. The Performance Targets provide no incentive to the Executives to enhance the proceeds from the Debtors’ asset sales or improve cash flow. See, e.g., *In re Hawker Beechcraft, Inc.*, 479 at 313-314 (denying a motion to approve incentive plans where the targets “d[id] not seem to be *much of a challenge*” and bonuses were contingent upon events “*likely to occur*”) (emphasis added).

42. *Second*, the cost of the KEIP is not justified in a case where general unsecured creditor recoveries are in doubt. The Debtors provide no analysis of the cost of the KEIP compared to the Executives’ compensation expectations, including any historical bonus programs. Although the Debtors assert that there are historical compensation programs for the Executives, they fail to provide any details regarding such programs, including the potential

---

<sup>11</sup> Section 363(b)(1) provides that debtors “may use, sell, or lease, other than in the ordinary course of business, property of the estate.” 11 U.S.C. § 363(b)(1). In approving a transaction conducted pursuant to section 363(b)(1), courts consider whether the debtor exercised sound business judgment. *Rescap II*, 491 B.R. at 84 (citing *Borders*, 453 B.R. at 473).

bonus payments or the actual amounts earned. As a result, the Debtors have not provided sufficient evidence that the KEIP was reasonably designed to correspond to historical earnings expectations.

43. *Third*, the Debtors' reliance on the KEIP Bankruptcy Peer Group is misplaced. The Debtors fail to identify the particulars of the comparable cases cited and metrics used in those incentive plans, including whether they included other variables, such as confirmation of a Chapter 11 plan or distributions to unsecured creditors.

44. Moreover, the KEIP Bankruptcy Peer Group consists of cases that are not comparable to the Debtors' cases in size, scope or breadth of challenges. For instance, the length of the Debtors' cases (from the Petition Date to the Sale Order) is anticipated to be approximately four months, with only four weeks remaining from now until the Sale Hearing. In contrast many of the cases in the KEIP Bankruptcy Peer Group lasted much longer, requiring extra efforts from management. *See e.g., In re Borders Grp., Inc.*, Case No. 11-10614 (MG) (Bankr. S.D.N.Y. April 22, 2011) [Docket No. 697] (approving KEIP plan that provided payments to executives at nine months after the petition date). Furthermore, the KEIP Bankruptcy Peer Group includes cases where the proposed incentive plans were entirely self-funding, unlike these cases where the Executives may receive a bonus by simply closing the Stalking Horse Bids. *See e.g., In re Ciber, Inc.*, Case No. 17-10772 (BLS) (Bankr. D. Del. May 11, 2017) [Docket Nos. 119, 199] (providing KEIP payments when executives close stalking horse bids *and* generate at least \$2 million in additional incremental cash flow).

45. Based on the foregoing, the Debtors fail to make a sufficient showing that the KEIP is justified by the facts and circumstances of the chapter 11 cases or that it is an exercise of the Debtors' sound business judgment. The KEIP merely provides the Executives with an

opportunity to benefit from lucrative bonuses simply for showing up to work, all at the expense of the Debtors' estates and creditors. Accordingly, the KEIP must be denied

**RESERVATION OF RIGHTS**

46. The Committee reserves all of its rights, claims, defenses, and remedies, including, without limitation, the right to amend, modify, or supplement this Objection, to seek discovery, and to raise additional objections during the hearing on the Motion.

**CONCLUSION**

**WHEREFORE** the Committee respectfully requests that the Court: (i) deny the Motion as to the KEIP; and (ii) grant the Committee such further relief as the Court deems just and appropriate.

Dated: November 6, 2018  
New York, New York

**BROWN RUDNICK LLP**

/s/ Robert J. Stark

Robert J. Stark  
Howard S. Steel  
Uchechi Egeonuigwe  
Seven Times Square  
New York, NY 10036  
Telephone: (212) 209-4800  
Facsimile: (212) 209-4801  
Email: rstark@brownrudnick.com  
Email: hsteel@brownrudnick.com  
Email: uegeonuigwe@brownrudnick.com

-and-

Steven B. Levine  
One Financial Center  
Boston, MA 02111  
Telephone: (617) 856-8200  
Facsimile: (617) 856-8201  
Email: slevine@brownrudnick.com

*Counsel to the Official  
Committee of Unsecured Creditors*

**TAB B**

**EXHIBIT "B"**

referred to in the Affidavit of

**ADRIAN ADAMS**

Sworn November , 2018

---

Commissioner for Taking Affidavits

DIP Cash Flow Forecast: US, Ireland, and Canada Consolidated Cash Flow

(\$ in Millions)	Forecast	Forecast	Forecast	Forecast	Forecast	Forecast	Forecast	Forecast	Forecast	Forecast	Forecast	Forecast	Forecast	Forecast	Forecast	Forecast	Forecast	Forecast	Forecast	18 Week
	Week 1	Week 2	Week 3	Week 4	Week 5	Week 6	Week 7	Week 8	Week 9	Week 10	Week 11	Week 12	Week 13	Week 14	Week 15	Week 16	Week 17	Week 18	Total	
	8/10/18	8/17/18	8/24/18	8/31/18	9/7/18	9/14/18	9/21/18	9/28/18	10/5/18	10/12/18	10/19/18	10/26/18	11/2/18	11/9/18	11/16/18	11/23/18	11/30/18	12/7/18		
<b>1 United States / Ireland<sup>1</sup></b>																				
2 Receipts	\$0.0	\$1.0	\$1.3	\$0.8	\$1.1	\$0.2	\$0.2	\$1.7	\$0.1	\$0.1	\$1.5	\$0.8	\$0.3	\$0.7	\$4.4	\$0.6	\$2.4	\$1.5		\$18.7
3 Disbursements	\$0.0	(\$1.1)	(\$0.3)	(\$2.5)	(\$0.1)	(\$2.1)	(\$1.0)	(\$2.8)	(\$1.1)	(\$0.1)	(\$0.4)	(\$3.4)	(\$0.5)	(\$0.1)	(\$0.4)	(\$0.2)	(\$3.9)	(\$0.1)		(\$20.1)
<b>4 Sub-Total Net Operating Cash Flow</b>	<b>\$0.0</b>	<b>(\$0.1)</b>	<b>\$1.0</b>	<b>(\$1.7)</b>	<b>\$1.0</b>	<b>(\$1.9)</b>	<b>(\$0.8)</b>	<b>(\$1.1)</b>	<b>(\$1.0)</b>	<b>(\$0.0)</b>	<b>\$1.2</b>	<b>(\$2.6)</b>	<b>(\$0.2)</b>	<b>\$0.6</b>	<b>\$4.0</b>	<b>\$0.4</b>	<b>(\$1.5)</b>	<b>\$1.4</b>		<b>(\$1.4)</b>
<b>5 Canada<sup>2</sup></b>																				
6 Receipts	\$0.0	\$0.5	\$0.3	\$0.7	\$0.4	\$0.5	\$0.5	\$0.5	\$0.5	\$0.3	\$0.4	\$0.4	\$0.4	\$0.4	\$0.4	\$0.4	\$0.4	\$0.5		\$7.7
7 Disbursements	\$0.0	(\$1.1)	(\$1.3)	(\$1.4)	(\$0.5)	(\$3.1)	(\$0.1)	(\$0.9)	(\$0.5)	(\$0.7)	(\$0.8)	(\$0.7)	(\$1.4)	(\$0.3)	(\$1.2)	(\$1.3)	(\$0.5)	(\$0.2)		(\$16.1)
<b>8 Sub-Total Net Operating Cash Flow</b>	<b>\$0.0</b>	<b>(\$0.5)</b>	<b>(\$1.0)</b>	<b>(\$0.8)</b>	<b>(\$0.0)</b>	<b>(\$2.6)</b>	<b>\$0.4</b>	<b>(\$0.4)</b>	<b>(\$0.1)</b>	<b>(\$0.4)</b>	<b>(\$0.4)</b>	<b>(\$0.3)</b>	<b>(\$1.0)</b>	<b>\$0.1</b>	<b>(\$0.8)</b>	<b>(\$0.8)</b>	<b>(\$0.1)</b>	<b>\$0.3</b>		<b>(\$8.5)</b>
<b>9 Total Net Operating Cash Flow</b>	<b>\$0.0</b>	<b>(\$0.7)</b>	<b>(\$0.0)</b>	<b>(\$2.5)</b>	<b>\$1.0</b>	<b>(\$4.6)</b>	<b>(\$0.4)</b>	<b>(\$1.4)</b>	<b>(\$1.1)</b>	<b>(\$0.4)</b>	<b>\$0.7</b>	<b>(\$2.9)</b>	<b>(\$1.2)</b>	<b>\$0.7</b>	<b>\$3.2</b>	<b>(\$0.5)</b>	<b>(\$1.5)</b>	<b>\$1.7</b>		<b>(\$9.9)</b>
<b>10 Cumulative Cash Flow</b>	<b>\$0.0</b>	<b>(\$0.7)</b>	<b>(\$0.7)</b>	<b>(\$3.2)</b>	<b>(\$2.2)</b>	<b>(\$6.7)</b>	<b>(\$7.1)</b>	<b>(\$8.6)</b>	<b>(\$9.6)</b>	<b>(\$10.0)</b>	<b>(\$9.3)</b>	<b>(\$12.2)</b>	<b>(\$13.4)</b>	<b>(\$12.7)</b>	<b>(\$9.5)</b>	<b>(\$10.0)</b>	<b>(\$11.5)</b>	<b>(\$9.9)</b>		

**Notes:**

1 - US and Ireland: Weeks 1 - 5 are Original DIP Budget from 8/10/18; Weeks 6 - 18 are Revised DIP Budget from 9/11/18

2 - Canada: Weeks 1 - 2 are Original DIP Budget from 8/10/18; Weeks 3 - 8 are Revised 8/24/18, Weeks 9 - 18 are Revised DIP Budget from 10/2/18

**TAB 3**



## DEFINITIONS

1. **THIS COURT ORDERS** that capitalized terms used in this Order and not otherwise defined shall have the meanings ascribed to them in the Adams Affidavit.

## KERP AND KEIP

2. **THIS COURT ORDERS** that the KERP described in the Adams Affidavit, the details of which are contained in the Confidential Supplement, is hereby approved and the Applicants are authorized and directed to make payments in accordance with the terms thereof.

3. **THIS COURT ORDERS** that the KEIP described in the Adams Affidavit, the details of which are contained in the Confidential Supplement, is hereby approved and the Applicants are authorized and directed to make payments in accordance with the terms thereof.

4. **THIS COURT ORDERS** that the KERP Participants and the KEIP Participants shall be entitled to the benefit of and are hereby granted a charge (the “**Key Employee Charge**”) on the Property (as that term is defined in the Initial Order dated August 10, 2018 (as amended and restated, the “**Initial Order**”), which charge shall not exceed an aggregate amount of US\$2.9 million, to secure the amounts payable to the participants in the KERP and KEIP pursuant to paragraphs 2 and 3 of this Order;

5. **THIS COURT ORDERS** that the Key Employee Charge shall have the benefit of paragraphs 50-55 of the Initial Order and shall rank in priority to all other Encumbrances and Charges (as those terms are defined in the Initial Order) other than the Administration Charge, the DIP Lenders’ Charge and the Bid Protections Charge such that the Charges shall rank as follows:

**First** – Administration Charge (to the maximum amount of \$1 million);

**Second** – DIP Lender’s Charge;

**Third** – Bid Protections Charge;

**Fourth** - Key Employee Charge (to the maximum amount of US \$2.9 million)

**Fifth** - D&O Charge (to the maximum amount of \$1 million); and

**Sixth** - Transactional Fee Charge (to the maximum amount of \$2.5 million);

6. **THIS COURT ORDERS** that the filing, registration or perfection of the Key Employee Charge shall not be required, and that the Key Employee Charge shall be valid and enforceable for all purposes, including as against any right, title or interest filed, registered, recorded or perfected subsequent to the Key Employee Charge coming into existence, notwithstanding any such failure to file, register, record or perfect.

7. **THIS COURT ORDERS** that except as otherwise expressly provided for herein or in the Initial Order or the Sales Process Order, or as may be approved by this Court, the Applicants shall not grant any Encumbrances over any Property that rank in priority to, or *pari passu* with, the Key Employee Charge unless the Applicants also obtain the prior written consent of the KERP Participants, KEIP Participants, or by further Order of this Court.

8. **THIS COURT ORDERS** that the Key Employee Charge shall not be rendered invalid or unenforceable and the rights and remedies of the KERP Participants and KEIP Participants entitled to the benefit of the Key Employee Charge thereunder shall not otherwise be limited or impaired in any way by: (a) the pendency of these proceedings and the declarations of insolvency made herein; (b) any application(s) for bankruptcy order(s) issued pursuant to the *Bankruptcy and Insolvency Act* (Canada) (the "**BIA**"), or any bankruptcy order made pursuant to such applications; (c) the filing of any assignments for the general benefit of creditors made pursuant to the BIA; (d) the provisions of any federal or provincial statutes; or (e) any negative covenants, prohibitions or other similar provisions with respect to borrowings, incurring debt or the creation of Encumbrances, contained in any existing loan documents, lease, sublease, offer to lease or other agreement (collectively, an "**Agreement**") which binds the Applicants, and notwithstanding any provision to the contrary in any Agreement:

- (x) the creation of the Key Employee Charge shall not create or be deemed to constitute a breach by the Applicants of any Agreement to which it is a party; and
- (y) none of the KERP Participants or KEIP Participants shall have any liability to any person whatsoever as a result of any breach of any Agreement caused by or resulting from the creation of the Key Employee Charge.

9. **THIS COURT ORDERS** that payments made by the Applicant pursuant to this Order do not and will not constitute preferences, fraudulent conveyances, transfers at undervalue, oppressive conduct, or other challengeable or voidable transactions under any applicable law.

#### **SEALING**

10. **THIS COURT ORDERS** that the Confidential Supplement is hereby sealed and shall not form part of the public record until further order of the Court.

#### **GENERAL**

11. **THIS COURT HEREBY REQUESTS** the aid and recognition of any court, tribunal, regulatory or administrative body having jurisdiction in Canada or in the United States, to give effect to this Order and to assist the Applicants, the Monitor and their respective agents in carrying out the terms of this Order. All courts, tribunals, regulatory and administrative bodies are hereby respectfully requested to make such orders and to provide such assistance to the Applicants and to the Monitor, as an officer of this Court, as may be necessary or desirable to give effect to this Order, or to assist the Applicants and the Monitor and their respective agents in carrying out the terms of this Order.

---

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*,  
R.S.C. 1985, c. C-36, AS AMENDED

Court File No: CV-18-603054-00CL

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT  
OF ARALEZ PHARMACEUTICALS INC. AND  
ARALEZ PHARMACEUTICALS CANADA INC.

---

**ONTARIO**  
**SUPERIOR COURT OF JUSTICE**  
Proceeding commenced at Toronto

---

**ORDER**  
**(RE: KERP AND KEIP APPROVAL)**

---

**STIKEMAN ELLIOTT LLP**  
Barristers & Solicitors  
5300 Commerce Court West  
199 Bay Street  
Toronto, Canada M5L 1B9

**Ashley Taylor** LSO#: 39932E  
Tel: (416) 869-5236  
E-mail: ataylor@stikeman.com

**Maria Konyukhova** LSO#: 52880V  
Tel: (416) 869-5230  
Email: mkonyukhova@stikeman.com

**Kathryn Esaw** LSO#: 58264F  
Tel: (416) 869-6820  
E-mail: kesaw@stikeman.com

Lawyers for the Applicants

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF ARALEZ PHARMACEUTICALS INC. AND ARALEZ PHARMACEUTICALS CANADA INC.

Court File No. CV-18-603054-00CL

---

**ONTARIO**  
**SUPERIOR COURT OF JUSTICE**  
**(COMMERCIAL LIST)**  
Proceeding Commenced at Toronto

---

**MOTION RECORD OF THE APPLICANTS**  
**(Returnable November 16, 2018)**  
**(Re: KERP and KEIP Approval)**

---

**STIKEMAN ELLIOTT LLP**  
Barristers & Solicitors  
5300 Commerce Court West  
199 Bay Street  
Toronto, Canada M5L 1B9

**Ashley Taylor** LSO#: 39932E  
Tel: (416) 869-5236  
E-mail: [ataylor@stikeman.com](mailto:ataylor@stikeman.com)

**Maria Konyukhova** LSO#: 52880V  
Tel: (416) 869-5230  
E-mail: [mkonyukhova@stikeman.com](mailto:mkonyukhova@stikeman.com)

**Kathryn Esaw** LSO#: 58264F  
Tel: (416) 869-5230  
E-mail: [kesaw@stikeman.com](mailto:kesaw@stikeman.com)

Lawyers for the Applicants