IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re KaloBios Pharmaceuticals, Inc., Debtor.[1]	Chapter 11 Case No. 15-12628 (LSS) **Re: D.I. 238 & 273**

DECLARATION OF ALEXANDRE ZYNGIER IN SUPPORT OF DEBTOR'S MOTION FOR AN ORDER: (I) APPROVING LETTER OF INTENT AND TERM SHEET WITH CHEVAL HOLDINGS, LTD., BLACK HORSE CAPITAL LP AND BLACK HORSE CAPITAL MASTER FUND LTD.; (II) APPROVING BIDDING PROCEDURES GOVERNING SUBMISSION AND CONSIDERATION OF COMPETING AND SUPPLEMENTAL PLAN SPONSORSHIP PROPOSALS; (III) APPROVING BREAKUP FEE; (IV) SCHEDULING AND AUTHORIZING THE DEBTOR TO CONDUCT AN AUCTION PURSUANT TO SUCH PROCEDURES; AND (V) GRANTING RELATED RELIEF, AS AMENDED

I, Alexandre Zyngier, pursuant to section 1746 of title 28 of the United States Code, hereby declare under penalty of perjury as follows:

Introduction

1. I submit this declaration (the "Declaration") in support of the *Debtor's Motion For An Order: (I) Approving Letter Of Intent And Term Sheet With Cheval Holdings, Ltd., Black Horse Capital LP And Black Horse Capital Master Fund Ltd.; (II) Approving Bidding Procedures Governing Submission And Consideration Of Competing And Supplemental Plan Sponsorship Proposals; (III) Approving Breakup Fee; (IV) Scheduling And Authorizing The Debtor To Conduct An Auction Pursuant To Such Procedures; And (V) Granting Related Relief*, dated March 16, 2016 (D.I. 238) (the "Original Motion"), as amended by the *Notice Of Amendment To Debtor's Motion For An Order: (I) Approving Letter Of Intent And Term Sheet With Cheval Holdings, Ltd., Black Horse Capital LP And Black Horse Capital Master Fund*

[1] The last four digits of the Debtor's federal tax identification number are 7236. The Debtor's address is 442 Littlefield Ave., San Francisco, CA 94080.

Ltd.; (II) Approving Bidding Procedures Governing Submission And Consideration Of Competing And Supplemental Plan Sponsorship Proposals; (III) Approving Breakup Fee; (IV) Scheduling And Authorizing The Debtor To Conduct An Auction Pursuant To Such Procedures; And (V) Granting Related Relief, dated March 18, 2016 (D.I. 273) (the "Amendment Notice," and together with the Original Motion, the "Amended Motion").

2. The statements in this Declaration are, except where specifically noted, based on either my personal knowledge or opinion, on information that I have received from the employees or advisors for KaloBios Pharmaceuticals, Inc. (the "Debtor" or the "Company"), or employees of Batuta Capital Advisors LLC ("Batuta") working directly with me or under my supervision, direction, or control, or from the Debtor's records maintained in the ordinary course of their business. I am not being specifically compensated for this testimony other than through payments received by Batuta as a professional retained by the Debtor. If I were called upon to testify, I could and would competently testify to the facts set forth herein on that basis. I am authorized to submit this Declaration on behalf of the Debtor.

Professional Background and Qualifications

3. I hold a Master's in Business Administration in Finance and Accounting from the University of Chicago and a Bachelor of Science in Chemical Engineering from UNICAMP in Brazil.

4. I am the founding partner and managing director of Batuta, 475 Park Avenue South, Floor 12, New York, New York 10016. Batuta has been engaged by Court order as the Debtor's financial advisor in this chapter 11 case.

5. I have extensive knowledge of and experience advising in regard to financial issues in bankruptcy cases. I have over 20 years of investment strategy and operating

experience. Prior to founding Batuta in 2013 to pursue investment and advisory opportunities in the distressed and turnaround sectors, I was a Portfolio Manager at Alden Global Capital, Goldman Sachs & Co., and Deutsche Bank Co. and a strategy consultant at McKinsey & Company.

6. I am currently a director of Atari SA and AudioEye, Inc. and formerly was Chairman of the Board of Vertis, Inc., a director of Island One LLC, and Executive Chairman of DTV American Corporation.

7. Since being engaged on January 19, 2016, I have become familiar with the Debtor's business and its present circumstances. In particular, I have focused on the following activities: (a) supporting the Debtor's efforts to negotiate a consensual resolution of the Adversary Proceeding commenced by the PIPE Plaintiffs (as defined herein); (b) supporting the Debtor's efforts to finalize negotiations with Savant on the letter of intent approved by this Court on February 29, 2016; (c) supporting the Debtor's efforts to develop a business plan and a plan of reorganization built around the Savant transactions and the continued development of the Debtor's pre-existing drug programs; and (d) identifying sources of financing to allow the Debtor to execute its business plan and exit chapter 11.

The Debtor's Prepetition Efforts To Obtain Financing

8. Like many other development stage biotech ventures, the Company historically has financed its operations primarily through offerings of its equity securities in private placement and public offering transactions. Indeed, it appears to me that it was the Company's perceived inability to raise additional capital or consummate another strategic alternative within the time period allowed by its then limited cash resources that led the Company to announce on November 13, 2015 its intention to discontinue operations.

9. However, that wind-down of the business was never fully implemented. As the Company announced on November 19, 2015, the Company came to believe that it has received a commitment from Martin Shkreli and other investors for an equity investment of at least $3.0 million and for a $10 million equity financing facility, subject to applicable shareholder approval. Less than two weeks later, the Company would announce that it had signed an agreement (the "Savant Prepetition LOI") to acquire a benznidazole program for the treatment of Chagas Disease from Savant Neglected Diseases, LLC ("Savant"). It is my understanding that it was the expectation of the Company that most of this financing would be devoted to funding the transactions contemplated by the Savant Prepetition LOI.

10. Unfortunately, the proceeds actually realized through the announced financing transactions fell far short of the Company's expectations. Whereas the Company had expected to realize at least $13 million from the announced financings, it only received approximately $8.2 million from the private placement sale of its equity securities (such transaction, the "PIPE Transaction"). This left the Company significantly short of the funding level it needed to consummate the transactions contemplated by the Savant Prepetition LOI, continue its other drug development programs and otherwise operate its business.

11. Thereafter, the Company was rocked by Mr. Shkreli's indictment on securities fraud and other charges related to his activities at his former hedge fund and in connection with Retrophin, Inc. Within days, most of the Company's officers and directors had resigned and it was confronted with demands from certain participants in the PIPE Transaction (the "PIPE Plaintiffs") for the return of funds that they had transferred to the Company. The Company's commencement of this chapter 11 case on December 29, 2015 soon followed.

The Debtor's Capital Requirements to Successfully Reorganize

12. Securing sufficient financing to implement its business plan continues to be critical to the Company's ability to reorganize and emerge from bankruptcy.

13. A central feature of the Debtor's business plan remains the contemplated transaction with Savant to acquire the worldwide rights to its benznidazole program for the treatment of Chagas disease. The Court previously approved a Binding Letter of Intent between the Debtor and Savant (the "Savant LOI") on February 29, 2016.

14. The Debtor needs to be adequately capitalized to consummate the Savant transaction. To carry out the Savant LOI, the Debtor will need to expend approximately $1 million between February 29 and June 30, 2016 (of which the Debtor had already expended approximately $587,500 as of March 18, 2016). The Savant LOI also requires the Debtor to pay to Savant the balance of the $3 million initial payment as consideration for the regulatory and other assets under the Savant LOI (less any portion previously paid to Savant). In addition, the Savant LOI requires the Debtor to have at least $10 million of unencumbered cash when it exits bankruptcy, an event that the Savant LOI requires to occur by June 30, 2016.

15. Furthermore, the Debtor's business plan includes continued development of its existing KB003 (lenzilumab) and KB004 drug programs, with a particular emphasis on KB003. I understand that the KB003 program is ready to commence clinical testing. But to do so, the Company must possess adequate liquidity to manufacture the necessary medication, among other costs that will be incurred. To move forward, the Company must improve its near-term liquidity.

16. Moreover, I and the Debtor's management and other professional advisors are mindful of the bankruptcy-related costs being incurred and that will have to be funded for the

Debtor to confirm a plan of reorganization and emerge from chapter 11. The professional fees incurred in this chapter 11 case have been higher than originally anticipated, largely due to ongoing litigation with the PIPE Plaintiffs. Moreover, some uncertainty still exists about the size the claims pool that will have to be satisfied under such a plan. The Debtor's Schedules of Assets and Liabilities reflect claims totaling approximately $2.8 million. The bar date for most creditors to file proofs of claims will not pass until April 1, 2016, so the size of that claim pool could ultimately increase.

The Debtor's Postpetition Efforts to Raise Capital

17. Upon being engaged by the Debtor on January 19, 2016, I and others at Batuta began assisting the Debtor to assemble an investor presentation to educate potential investors about the KaloBios investment opportunity.

18. I and others at Batuta also immediately began leveraging our extensive roster of contacts for potential financial and strategy investors. By the end of February 2016, we had contacted approximately 190 parties to solicit their interest in pursuing a transaction with the Debtor. Our efforts focused primarily on trying to locate exit financing for the Debtor, but we did not foreclose exploring other strategic alternatives with potential transaction parties. Of the approximately 190 parties contacted, approximately 100 expressed in interest in further investigating a potential transaction with the Debtor and 27 such parties actually executed non-disclosure agreements and were provided with access to confidential information about the Debtor and its drug development programs.

19. The Debtor's efforts to raise capital during the early part of this period also included reaching out to the PIPE Plaintiffs to explore their interest in pursuing a potential transaction. In my view, the PIPE Plaintiffs were a natural first choice to approach about

providing additional financing. The PIPE Plaintiffs presumably already have some familiarity with the Debtor and its drug development programs (including the acquisition of Savant's benznidazole program, which was announced in early December 2015, at approximately the same time as their original stock purchase commitments were disclosed). Unfortunately, those discussions did not progress. Indeed, to my knowledge, since the commencement of this chapter 11 case, none of the PIPE Plaintiffs has ever proposed to provide the Debtor with additional financing.

20. Meanwhile, serious discussions about potential transactions eventually ensued with several of parties with which Batuta had been in contact. Several funds managed by Black Horse Capital LP, Black Horse Capital Master Fund Ltd. and Cheval Holdings, Ltd. (collectively, "Black Horse") were among those parties that made meaningful expressions of interest and who engaged in active discussions concerning a potential investment in the Debtor at the level then believed to be necessary to allow the Debtor to successfully reorganize. Other serious candidates for a potential transaction included an investment fund associated with a major financial institution. This other investment fund, because of its connection with a major financial institution, was unable to secure the internal approvals required to move forward with the transactions in the timeframe the Debtor required to serve as the stalking horse plan sponsor. Based on my communications with representatives of this other fund, it is my belief that Mr. Shkreli's brief but disastrous association with the Debtor and the ongoing negative press coverage surrounding Mr. Shkreli and his legal troubles were the main reasons for the slowness of its internal investment approval schedule.

21. I have had somewhat similar experiences with other potential investors. Indeed, in several instances, potential investors made clear to me that the "Shkreli factor" was a

significant deterrent to their willingness to further pursue a potential transaction with the Debtor, even though they were interested in the Debtor's pipeline of pharmaceutical projects.

22. Since late January 2016 when we first became aware of Black Horse's interest in pursuing a financing transaction with the Debtor, I, the Debtor's legal counsel Hogan Lovells US LLP and Morris, Nichols, Arsht & Tunnell LLP, and the Debtor's Board of Directors have worked closely together to negotiate the most favorable DIP and exit financing terms available to the Debtor under the circumstances. Despite our best efforts, Black Horse initially was only willing to commit to $10 million of DIP an exit financing, as reflected in the Letter of Intent and Term Sheet, each dated March 9, 2016, attached as Exhibit B to the Original Motion (the "Original Stalking Horse LOI").

23. As I discuss above, however, as this proceeding has progressed, the anticipated funding requirements have grown for the Debtor to confirm a plan of reorganization with sufficient remaining liquidity for the Savant transaction and its other drug development programs. The Amended Letter of Intent and Amended Term Sheet, each dated March 18, 2016, attached as Exhibit A to the Amendment Notice (together, the "Amended Stalking Horse LOI"), among other things, increase the size of the exit financing facility from $7 million to $11 million for an aggregate financing commitment of $14 million in order to address the Debtor's liquidity concerns.[2] In this, Black Horse was instrumental in bringing Nomis Bay LTD (collectively with Black Horse, the "Stalking Horse") to the table as an additional investor so that the Debtor can obtain the level of DIP and exit financing that it believes it needs to successfully reorganize.

[2] Capitalized terms not otherwise defined herein have the meanings ascribed to such terms in the Amended Stalking Horse LOI or, if not defined therein, the Original Motion.

The Breakup Fee and Related Bid Protections

24. In my view, based on my active participation in negotiations on behalf of the Debtor, the Debtor and Black Horse, with respect to the Original Stalking Horse LOI, and the Debtor, Black Horse and Nomis Bay, with respect to the Amended Stalking Horse LOI, the parties negotiated the terms of these agreements in good faith and at arms'-length.

25. It is my further understanding based on my involvement in the foregoing negotiations with the Stalking Horse that the Stalking Horse views all of the terms of the Amended Stalking Horse LOI, including the Breakup Fee (as defined therein) and the other bidder protections it contains (collectively, the "Bid Protections"), as material to its bargain with the Debtor and that the Stalking Horse would not be willing to proceed with the Amended Stalking Horse LOI without those Bid Protections in place and approved by this Court.

26. Certain features of the Bid Protections, I expect, may be viewed as unusual by the Court based on its experience in other, more traditional chapter 11 cases. In particular, the Breakup Fee provisions of the Amended Stalking Horse LOI give the Stalking Horse the discretion to select either the "Cash Option Breakup Fee" or the "Stock Option Breakup Fee" if a Triggering Event (as defined therein) occurs. The Stock Option Breakup Fee, if selected by the Stalking Horse, would allow it (x) if the DIP Financing has not been funded, the option to purchase $2.8 million of stock in the reorganized Debtor at a price of $1.75 per share, or (y) if the DIP Financing has been funded, the option to purchase $2 million of stock in the reorganized Debtor at a price of $1.75 per share. Further, in the event that the DIP Financing has been funded, the Stalking Horse has the right to require repayment of the DIP Financing obligations through the issuance to it of common of the reorganized Debtor at a rate of $1.75 per share.

27. In my opinion, these Bid Protections, though unusual, are appropriate to the unique circumstances of this case and this Debtor for several reasons. First, as I discuss above, the "Shkreli factor" has proven to date to be a significant deterrent to potential investors, especially at this relatively early stage of the case when the ultimate dispositions of Mr. Shkreli's ownership interest in the Company and his claims, if any, are not yet known. Thus far, only the Stalking Horse has been willing to commit to provide the Debtor with DIP and exit financing at the level it requires to successfully reorganize and implement its business plan. The Stalking Horse's willingness to commit to these financings provides real and substantial benefits to the Debtor's estate by providing other potential bidders with an objective basis against which to value the Company and thereby setting a floor for future bidding.

28. Second, pursuant to the Amended Stalking Horse LOI, the Stalking Horse and the Debtor have committed to a set of Milestones that will require the Stalking Horse to act quickly to commit resources to and document the DIP and exit financing transactions before, for reasons almost entirely outside of its control, it will have certainty about whether those transactions will go forward. Specifically, the Debtor's reorganization prospects are dependent upon on the Debtor's ability to consummate the Savant transactions contemplated by the Savant LOI. The Savant LOI, in turn, requires, among other things, that the Debtor emerge from bankruptcy with $10 million of unencumbered cash on its balance sheet by no later than June 30, 2016. Thus, in my view, the Milestones contained in the Amended Stalking Horse LOI, are not the result of demands of the Stalking Horse, but are driven by the external conditions imposed by the requirements of the Savant LOI and the Debtor's other business needs.

29. Third, it needs to be emphasized that the Stock Option Breakup Fee is just that – an option to purchase common stock in the Debtor as it may be reorganized under an as

yet to be filed and confirmed chapter 11 plan. To exercise the Stock Option Breakup Fee, the Stalking Horse would have purchase such shares and would thereby be committing to infuse capital in the Debtor under circumstances in which it likely would be only a minority shareholder of the reorganized Debtor. The Stalking Horse in that situation would not have the benefit of the anti-dilution provisions that otherwise apply to shares to be issued to it under the Amended Stalking Horse LOI. Nor would the Stalking Horse have any assurances that such shares would be freely transferrable. To me, the very fact that the Stalking Horse has negotiated for the Stock Option Breakup Fee under these circumstances should do exactly what a break-up fee is supposed to do - signal potential bidders that a sophisticated investor has done its diligence about this Company and concluded that this is an investment worth pursuing, even if it will not hold a control block of the Company's common stock after it emerges from bankruptcy.

30. Fourth, the intrinsic value of the Stock Option Breakup Fee, in my view, is not readily measurable against the current trading price of the Debtor's shares, which, having been delisted in January 2016, now only trade over-the-counter. I am aware of the contention made by the PIPE Plaintiffs in their objection (D.I. 272, ¶ 6) to the Original Motion that the $1.75 per share strike price for the Stock Option Breakup Fee must be valued as a 50 cent per share discount relative to the trading price of the Debtor's common stock on March 18, 2016.

31. I disagree with this strained proposition. The Debtor's common stock has been and remains thinly traded in over-the-counter transactions since trading resumed after the Company was delisted from NASDAQ on January 13, 2016. Indeed, as set forth on **Exhibit A** hereto (http://finance.yahoo.com/q/hp?s=KBIOQ&a=10&b=6&c=2015&d=02&e=18&f=2016&g=d (last accessed March 20, 2016)), at no time during the period from January 25, 2016 through March 18, 2016 have more than 42,000 shares of the Company's common stock traded on any given day.

Moreover, on all but five days during this period, the trading volume was 15,000 shares per day or less. By comparison, the trading volume on NASDAQ for the Company's shares during the period from November 6, 2015 through December 16, 2015 (the day before Mr. Shkreli was indicted and trading was frozen) exceeded 200,000 shares per day on all but five days.

32. Moreover, selecting the closing price of the Debtor's stock on one day – March 18, 2016 – is not, in my view, a sound way draw conclusions about the value of such shares over time. I note that during the period from January 13, 2016 through March 18, 2016, the closing price for the Debtor's stock has ranged as high as $4.39 per share and as low as a $1.50 per share.

33. In summary, based on the extensive marketing process that has been conducted thus far, I have determined that the Bid Protections were a material inducement for, and a condition of the Stalking Horse's execution of the Amended Stalking Horse LOI. Further, I have concluded that the Breakup Fee and other Bid Protections are not only commensurate to the real and substantial benefits being conferred on the Debtor's estate by the Stalking Horse, but also fair, reasonable and appropriate in light of the size and nature of the proposed transactions and the efforts that have been and will be expended by the Stalking Horse.

The Bidding Procedures

34. In connection with the Original Stalking Horse LOI and the Amended Stalking Horse LOI, the Debtor has bargained for the opportunity to subject the Stalking Horse's proposed transactions to higher and better offers in accordance with the terms of the Bidding Procedures annexed to the Original Motion. Additionally, the Bidding Procedures not only permit the Debtor to solicit competing "Primary Plan Transaction" bids on terms superior to those being provided by the Stalking Horse, but also allow the Debtor to pursue "Secondary Plan

Transaction" bids. In substance, a Secondary Plan Transaction is one pursuant to which a Qualified Bidder would acquire equity in the reorganized Debtor along-side the Stalking Horse or another Primary Plan Sponsor. Hence, in my view, the ability to consider Secondary Plan Transaction bids gives the Debtor the option to raise additional capital without putting the Stalking Horse transaction at risk.

35. I believe that the Bidding Procedures will allow the Debtor to continue the marketing process that was commenced immediately after Batuta's engagement began. I believe that those additional parties most likely to have an interest in a financing transaction have been contacted and have already been provided an opportunity to access due diligence information. Nonetheless, I believe the process outlined in the Bidding Procedures is designed to attract additional third-party interest, if any exists, and to maximize returns to the Debtor's stakeholders. I also believe that the currently proposed process will reassure the Debtor's employees, vendors and other stakeholders that the chapter 11 case will proceed form this point forward swiftly and without major disruptions to the Debtor's business operations.

Conclusion

36. In conclusion, I believe that the Debtor and its advisors, including Batuta, have proposed and conducted a thorough marketing and sale process providing the best possible chance of preserving and maximizing the value of this estate. Approval of the Bidding Procedures and Bid Protections are appropriate and necessary steps in the Debtor's efforts to maximize the value of its estate for the benefit of all stakeholders.

Dated: March 21, 2016

Alexandre Zyngier
Managing Director
Batuta Capital Advisors LLC