

SHAREHOLDER CAPITAL LLC
Miami, Florida

April 25, 2024

BY ELECTRONIC MAIL

Independent Members of Vanda Pharmaceuticals Inc.’s Board of Directors:

Shareholder Capital LLC (together with its members and affiliates) is a significant shareholder of Vanda Pharmaceuticals Inc. (the “Company” or “Vanda”), collectively holding more than 200,000 shares of Vanda’s common stock. We are openly writing to you, the independent members of Vanda’s Board of Directors (the “Board”), to remind you that **your fiduciary duty is to Vanda’s shareholders, NOT Vanda’s Chairman & CEO, Dr. Mihael H. Polymeropoulos, other members of the Board or management team, nor any other insiders and their pecuniary interests.** We are compelled to remind you of this because of:

- 1) Vanda’s extraordinary underperformance and undervaluation;
- 2) the Board’s complete disregard of a [credible, fully-financed offer](#) by Future Pak, LLC (“Future Pak”) to acquire Vanda at a 79.0-91.4% premium to its closing price on 4/16/24; and
- 3) Vanda’s track record of ignoring shareholders’ interests — we are now the third voice to speak publicly on Vanda and its Board’s and management’s entrenchment in the past week, and Vanda’s only response has been to [reject Future Pak’s offer with an inadequate, <250-word press release](#) and to [adopt a poison pill](#).

[Butler Hall Capital’s public letter](#) highlighted several issues vis-à-vis the Future Pak offer, and we add to that with our own observations/experiences and recommendations below in the hopes that independent members of the Board, and shareholders alike, are aware of:

- 1) Vanda’s **poor oversight and execution of its unknown and value-destructive strategy;**
- 2) the underlying reasons: **entrenchment, misaligned incentives, and cronyism;** and
- 3) the best path forward for the Board.

First and foremost, please understand that **Vanda’s failure to represent the interests of shareholders is all too evident in Vanda’s striking underperformance:**

TSR and Vanda TSR vs. Peers & Indices (1)									
	TSR				Vanda TSR vs. Peers & Indices				
	1-Year	3-Year	5-Year	10-Year	1-Year	3-Year	5-Year	10-Year	
Vanda	(37%)	(76%)	(77%)	(70%)					
vs. Proxy Peers (2)	(27%)	(42%)	(20%)	75%	(10%)	(34%)	(57%)	(145%)	
vs. ISS Peers (3)	2%	(22%)	(23%)	117%	(39%)	(54%)	(54%)	(187%)	
vs. iShares Biotechnology Index (IBB)	(4%)	(16%)	16%	79%	(33%)	(59%)	(93%)	(149%)	
vs. S&P 600	10%	(2%)	40%	124%	(47%)	(74%)	(117%)	(194%)	

(1) Sources: FactSet as of 4/16/24. Total Shareholder Return (“TSR”) reinvests dividends as of the ex-dividend date.
(2) Source: Vanda’s Definitive Proxy Statement on Schedule 14A (“DEF14A”) filed on 4/24/23 with the U.S. Securities and Exchange Commission (“SEC”). Reflects an equal-weighted composite of peers listed by Vanda. Excludes peers that no longer trade publicly.
(3) Source: ISS’s Proxy Analysis & Benchmark Policy Voting Recommendations on Vanda published 5/18/23. Reflects an equal-weighted composite of peers listed by ISS. Excludes peers that no longer trade publicly.

This underperformance leaves Vanda's equity valued at a paltry 62% of its 12/31/23 net cash balance, or **nearly \$150M in negative enterprise value ("EV").**⁽⁴⁾ This is not a recent phenomenon as shares have been impaired for several years, and Vanda's negative EV has persisted for the last ~18 months.

We believe Vanda's press release rejecting Future Pak's offer reveals the governance failures alluded to above. In it, the Board asserted that Future Pak's offers are "... opportunistic attempts to purchase the Company's shares at a discount to Vanda's intrinsic value and would transfer significant value to Future Pak at the expense of Vanda shareholders" and they ascribe "very little value to the Company's significant revenue stream and pipeline."⁽⁵⁾

To this, and given to Vanda's lack of financial guidance and meaningful engagement with shareholders, we ask the Board:

- 1) Against what future revenue projections, pipeline value, and overall financial plan was Future Pak's offer measured?
- 2) What assessment of intrinsic value has the Board conducted? Absent a formal strategic alternatives process, and given Vanda's remarkable underperformance, on what basis did the Board reject Future Pak's offer, which values Vanda shares at nearly 2x their unaffected price?

How did we get here? Poor oversight and execution of an unknown and value-destructive strategy.

Below are what we believe to be key strategic concerns impairing Vanda shares:

- 1) \$502M in R&D + \$1.14B in SG&A in the 10 years since first commercializing products in 2014, a massive investment yielding a mere \$145M in free cash flow (i.e., OCF – CapEx) in that time;⁽⁶⁾
- 2) Lack of communication regarding capital allocation/needs, including cancellation of guidance;
- 3) The risk of potential value-/metric-dilutive acquisitions, which was realized with Vanda's \$100M PONVORY® acquisition in Dec-23 that immediately exacerbated shares' underperformance;⁽⁷⁾
- 4) Vanda's three ill-fitting commercial businesses that operate in highly competitive markets, require substantial, discrete operating expense, and provide little operating leverage:
 - a) HETLIOZ®, marketed mostly to sleep medicine specialists — less so now given its mismanagement into years-early generic competition in 2023 that has already diminished run-rate revenue by ~50%;⁽⁸⁾
 - b) Fanapt®, marketed mostly to psychiatrists; and
 - c) PONVORY®, marketed mostly to neurologists — acquired at 3.3x LTM revenue while Vanda traded at a significantly negative valuation; requires substantial investment (including a sizeable portion of the upwards of 190 Vanda job specs posted on LinkedIn in recent months, mostly for a "neuroscience" salesforce);⁽⁹⁾ and
- 5) A hodgepodge of pipeline assets, several of which do not leverage the three businesses mentioned above and appear to be projects that satisfy Dr. Polymeropoulos's genetics background more than they provide a return to shareholders.

More importantly, how could this happen? Entrenchment, misaligned incentives, and cronyism.

The Future Pak debacle is the latest in a string of concerning, anti-shareholder, and entrenched behavior. We have experienced this ourselves, with (a) the Board's and management's unwillingness to engage

⁽⁴⁾ Calculated as fully-diluted equity value, minus cash and equivalents as of 4/16/24, the day preceding Future Pak's offer disclosure.

⁽⁵⁾ Source: [Vanda Pharmaceuticals Confirms Rejection of Unsolicited Takeover Proposals from Future Pak](#).

⁽⁶⁾ Sources: Vanda's Annual Reports on Form 10-K ("10-Ks") filed with the SEC.

⁽⁷⁾ Source: FactSet. Vanda's excess TSR vs. Proxy Peers, ISS Peers, iShares Biotechnology Index (IBB), and the S&P 600 was (7%), (8%), (8%), and (10%), respectively, in the t+5 days post-announcement and (13%), (10%), (2%), and (5%), respectively, in the t+132 days from announcement to the unaffected date of 4/16/24.

⁽⁸⁾ Sources: Vanda's Interim Reports on Form 10-Q filed with the SEC. HETLIOZ® net product sales were \$21M in 4Q23 and \$40M in each of 4Q22 and 1Q23, the quarters preceding Teva's launch of generic tasimelteon.

⁽⁹⁾ Source: [Vanda's LinkedIn Jobs page](#). 131 job specs are listed as of 4/23/24 but were as high as 190 post-PONVORY® acquisition (in early March 2024).

with us in recent months on paths to create value and (b) the Board rejecting highly-qualified Board candidates that Mr. Cole personally put forth for shareholders' consideration at the upcoming 2024 Annual Meeting of Shareholders (who themselves own 105,000 shares of the Company's common stock), denying shareholders the ability to vote on them.

Misaligned incentives

Despite the value destruction detailed above, Dr. Polymeropoulos has been awarded increasingly large compensation packages over the years: nearly \$5M/year beginning in 2016, or almost 2x the \$2.5M+/year in the years preceding 2016.⁽¹⁰⁾ In fact, in the past ten reported years (2013-2022), **Dr. Polymeropoulos has been awarded \$40M+**, nearly \$10.5M of which came in the past two years as Vanda shares deteriorated.⁽¹¹⁾ Dr. Polymeropoulos was relatively insulated from the pain shareholders have felt as his compensation is significantly more cash-weighted compared to peer CEOs: 35% cash and 65% equity in 2022, for example, compared to the peer CEOs at ~16-18% cash and ~82-84% equity.⁽¹²⁾ With that, it is unsurprising that Dr. Polymeropoulos has not bought a single share of Vanda on the open market since February 2012; in fact, since then, Dr. Polymeropoulos has sold 833K shares at an average price of \$14.13, 3.5x Vanda's unaffected share price, for nearly \$12M.⁽¹³⁾

What's more, three of Dr. Polymeropoulos's children work at Vanda, and they were awarded compensation packages valued at nearly \$4.5M over the past four years (once fully-disclosed).⁽¹⁴⁾

In short, money talks: the Polymeropoulos family has been awarded by Vanda \$46M+ in disclosed compensation over the past ten years,⁽¹⁵⁾ nearly 20% of Vanda's vastly diminished equity value.⁽¹⁶⁾

Cronyism

We believe the Polymeropoulos family has evaded accountability for their actions, and incentives have remained misaligned because several independent members of the Board have ties to Dr. Polymeropoulos. Certain fact patterns suggest as much:

- 1) Director Chrousos, a long-time family friend of Dr. Polymeropoulos, had zero public company board and biotech experience before her appointment to the Board.
- 2) Director Mitchell had zero public company board experience before his appointment to the Board and is a dean at the medical school (a) that two of the three Polymeropoulos children attended and (b) of the university where Dr. Polymeropoulos donates to the "Parents Council, Lombardi Cancer Center, Partners in Research and men's basketball."⁽¹⁷⁾
- 3) Lead Independent Director Dugan, who we approached to grant us access to independent members of the Board so we could discuss Vanda's situation and potential new Board candidates, rejected our request and told us that such access could only be granted by the very individual we sought to replace with Mr. Cole's Board candidates, Dr. Polymeropoulos. Neither followed up.

Given these facts, it seems clear to us why these 'independent' directors are not fulfilling their fiduciary duties and are unwilling to put their nearly \$300K/year directorships at risk to do so.

⁽¹⁰⁾ Sources: Vanda's DEF14As filed with the SEC. Reflects averages of the periods identified.

⁽¹¹⁾ Sources: Vanda's DEF14As filed with the SEC. Reflects the sum of the periods identified.

⁽¹²⁾ Sources: Vanda's, Proxy Peers', and ISS Peers' DEF14As filed with the SEC. "Peer CEOs" compensation mix ranges provided reflect median CEO compensation among Proxy Peers' and ISS Peers' constituents for the calendar year ended December 31, 2022. Compensation mix percentages exclude often-immaterial perquisites.

⁽¹³⁾ Source: Vanda's Statements of Changes in Beneficial Ownership of Securities on Form 4 and 4/A filed with the SEC.

⁽¹⁴⁾ Sources: Vanda's DEF14As filed with the SEC. Reflects the sum of the periods identified.

⁽¹⁵⁾ Sources: Vanda's DEF14As filed with the SEC. The \$46M figure reflects the sum of disclosed compensation over the periods identified, which, for the Polymeropoulos children prior to 2019, only included base salaries; for conservatism, we did not presume the level of achievement of disclosed target bonuses nor the grant date fair value of disclosed RSU counts.

⁽¹⁶⁾ Calculated as fully-diluted equity value, minus cash and equivalents as of 4/16/24, the day preceding Future Pak's offer disclosure.

⁽¹⁷⁾ Source: ["Donors Get Firsthand Look at How Funds for New Medical Research Are Used"](#).

Most importantly, how can the Board fix this? Exert independence and face the market.

We believe the Board should take the following steps:

- 1) Select/retain an independent, nationally-recognized investment bank to run a strategic alternatives process that widely markets all or parts of Vanda and measures the best offer(s) against:
 - a) Future Pak's final offer;
 - b) Vanda's unknown (internal, if it exists) standalone strategic and financial plan; and
 - c) A Vanda plan that includes returning to shareholders a substantial portion of excess cash on Vanda's overcapitalized balance sheet to reestablish valuation versus holding it at a discount or spending it on yet-identified, risky acquisitions.
- 2) [To accomplish #1 above:] Form a Special Committee of the Board to ensure shareholders are best-served given credibility concerns, including that of the independence of this Board; this Special Committee should:
 - a) be led by Director Ward and Director Honoré;
 - b) be the individuals who select the investment bank and serve as their primary contact; and
 - c) provide oversight of the process such that Dr. Polymeropoulos and other management / Vanda personnel engage earnestly or be sidelined;
- 3) Simultaneous to the investment bank's work, engage with shareholders on the aforementioned strategy, including providing detailed financial guidance for the first time in over one year.
- 4) Provide shareholders with a clearly-defined timeline for the steps above, progress updates in the interim, and an expedient resolution.

If Vanda does not take the steps above, shareholders cannot be expected to underwrite this entrenched Board's and management team's unknown strategy, leaving Future Pak's offer the best option to recoup some of the **equity and enterprise value destroyed by Vanda: ~\$1B each since mid-2021 and \$1.2+ and nearly \$1.4B, respectively, since late-2018.** ⁽¹⁸⁾

We again remind the Board of **your fiduciary obligation to Vanda's shareholders** and strongly encourage you to take advantage of this opportunity, in the manner laid out above, to establish your independence, rebuild the credibility of the Board, and create shareholder value.

As we have offered repeatedly before, we are available to constructively discuss the path forward for Vanda at your convenience.

Sincerely,

/s/ Michael P. Cole

Michael P. Cole
Managing Member
Shareholder Capital LLC

/s/ Jeremy R. Lichtman

Jeremy R. Lichtman
Member
Shareholder Capital LLC

⁽¹⁸⁾ Source: FactSet as of 4/16/24. "Equity value" reflects fully-diluted equity value, and "enterprise value" reflects fully-diluted equity value, minus cash and equivalents.