IN THE SUPREME COURT OF THE STATE OF DELAWARE

PARAMOUNT COMMUNICATIONS, INC.,
and KDS ACQUISITION CORP.,

Plaintiffs Below-
Appellants,

v.

TIME INCORPORATED, et al.,

Defendants Below-
Appellees.

IN RE: TIME INCORPORATED
SHAREHOLDER LITIGATION

LITERARY PARTNERS, L.P., et al.,

Plaintiffs Below-
Appellants,

v.

TIME INCORPORATED, et al.,

Defendants Below-
Appellees.

No. 279, 1989

Interlocutory Appeal
from the Court of
Chancery of the State of
Delaware in and for
New Castle County,
C.A. Nos. 10670, 10866
and 10935

ANSWERING BRIEF OF DEFENDANT-APPELLEE WARNER COMMUNICATIONS INC.

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STATEMENT OF NATURE OF PROCEEDINGS AND ORDER APPEALED FROM

This is an appeal from the Court of Chancery's denial on July 14, 1989 of plaintiffs' preliminary injunction motions. An interlocutory appeal was certified on July 14 and, by order of July 17, an injunction pending appeal was granted until 5:00 p.m. on July 24. This is the answering brief of defendant Warner.

SUMMARY OF ARGUMENT*

1. Denied. The court below properly applied the Unocal standard based upon its findings of fact after a thorough review of the extensive record.

2. Denied. The court below correctly held that the Time board could respond, after reasonable investigation, to a threat to the long-term business strategy of Time.

3. Denied. The court below correctly found that the response of Time's board to Paramount's offer was reasonable and does not preclude Time shareholders from obtaining a control premium for their shares.

4. Denied. Unocal does not introduce new procedural requirements into our law. Here, the outsider-dominated Time board, acting on advice of the professional advisors to the board, reasonably determined that the Paramount offer constituted a threat to the long-term strategy of Time. Thus, there were no "procedural lapses" in the process employed by the board.

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* Points 1-3 in this Summary of Argument respond to the Summary of Argument in the Paramount brief. Points 4-5 respond to the stockholder plaintiffs.

5. Denied. Time's takeover defenses were of no use to it in responding to the threat posed by Paramount, a threat to the long-term strategy of Time. The response to that threat was proportional and did not create a "functional alternative" to the Paramount offer.

STATEMENT OF FACTS

The pertinent facts are summarized below. For a fuller recitation of the facts, Warner respectfully refers the Court to Warner's brief in the Court of Chancery.

A. Time and Warner explore a business combination

The Time/Warner transaction had its inception in 1987 when Warner's chief executive officer, Steve Ross, approached Time with the idea that Time and Warner form a joint venture subsidiary in which each parent would own a 50% interest: Time would contribute its cable systems and HBO and Warner would contribute its cable systems and film studio; the parties would also contribute stock so that each company would have an equity interest in the other's overall businesses and to provide an additional equity base in the subsidiary that would facilitate future borrowing (Op. 12; A1873-74; BB167, 614-16, 644-51, 691-95, 821-22).* The stock would be non-voting (BB167). Discussions of the proposed joint venture continued throughout 1987 and into the spring of 1988 (BB166-68, 614-16, 694-96). As the discussions

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* Citations to Warner's Appendix are to "BB ___". Citations to Plaintiffs' Joint Appendix are to "A ___". Citations to the Chancellor's Opinion are to "Op. ___."

progressed, the parties looked forward to the possibility that the joint venture might ultimately lead to a full merger between Time and Warner (BB646).

By late May or early June 1988, Time and Warner had concluded that the joint venture concept presented a host of tax, legal and pragmatic problems (BB262, 617-18, 646, 648-51). By this time, the parties had been negotiating with one another for over a year: they had exhaustively explored each other's businesses and business philosophy; they had come to appreciate just how advantageous a combination of the two companies would be (BB168-70, 263, 615-18, 769-70, 776-85, 824-27, 874-75).

The uncontradicted evidence demonstrated that there are compelling business reasons why a combination of the businesses of the two companies would be highly desirable. A merger of Time and Warner would create a unique communications company with the resources to compete on a worldwide basis (BB653, 686-89, 849-52, 880-81). In the opinion of Time, Warner and others (including Paramount itself, see BB318, 336, 338-39, 760-62), the communications, media and entertainment businesses will in the future be dominated by companies of significant size having a major presence in many aspects of those businesses -- journalism and publishing, motion pictures and television production and distribution, cable, videocassettes, records, and related operations (A1874, 1876-81, 1887-88, 1896-91; BB612, 756-58, 779-81).

Time worried that "very large, vertically integrated media and entertainment companies" would dominate in the 1990s and that companies like Time could either choose to "build value by succeeding globally" or become an "also ran" and ultimately "lose steam and probably eventually . . . lose valued employees" (BB756; see also BB611-12). Time decided that it was critical to its future business success to own directly the "software" that would be distributed by its cable and direct-mail operations; and that it was essential to expand its international presence (BB265-66, 613, 756, 926). Time looked to the possibility of acquiring a film studio: Disney, Columbia, Paramount or Warner (BB448-50, 453-54, 642, 677, 682, 729-30, 757-58).

Warner stood out as uniquely satisfying Time's needs. Warner owned a major film studio and had just entered into a merger agreement to acquire Lorimar, a major producer of television programming (BB145, 267, 684-85). Alone among film companies, Warner owned an international film distribution operation (BB267, 729, 779-80, 782). Warner was the second largest record company in the world and was, subsequent to Sony's acquisition of CBS Records, the sole remaining significant domestically-owned record company -- again with an extensive international distribution network (A1897-98, BB145, 268-69). Time's direct mail order operations could be used to market Warner's video cassettes and records, and Time's hard cover book publishing business would be complemented by Warner's soft cover book publishing (A1897-98; BB683-84, 779). Warner, through its acquisition of Chappell, was the world's leading publisher of music -- again an area of interest and fit to Time (A1897-98, 1933-34; BB145, 269).

Warner, like Time, was a substantial owner of cable systems: Time had long been desirous of expanding the size of its cable business (BB684, 688, 782, 850-51). A combination of the cable systems in the New York City market was particularly advantageous: Time operated systems in Manhattan; Warner in Brooklyn and Queens; the combined systems would create a sufficiently large customer base to enable Time/Warner to develop and provide programming to subscribers on a profitable basis (A1880, 1897; BB777-78). Time and Warner also each already held significant ownership positions in Turner Broadcasting with its invaluable CNN programming for cable systems: together, they would control approximately 17% of Turner (BB269).

From Warner's vantage point, the advantages were reciprocal. In particular, the combination with Time's cable operations and major direct mail sales operation would provide Warner with an outlet for its television and motion picture programming, videocassettes and recorded music (A1896-97; BB782).

B. Time and Warner negotiate a merger

From the outset of the discussions of a possible Time/Warner merger, Time insisted that the transaction be structured as an acquisition of Warner by Time. Warner recognized the legitimacy of Time's position: as Ross testified, it would hurt Time's magazines enormously if Time were to be acquired by an "entertainment company" (BB853; see also BB179).

The evidence is also uncontradicted that Time, from the outset of the negotiations, sought to have the merger structured as an acquisition of Warner for <u>cash</u> (A1937-38; BB470, 629-30, 697-98, 754-55, 826, 914-15). At all times prior to June 15, 1989, Steve Ross categorically refused: he wanted the Warner shareholders to maintain their equity interest in the combined company. A stock-for-stock transaction was his "first, second and third choice" (BB883-84; Op. 18, BB474, 835).

Intensive discussions revolved around the subject of corporate governance. Both Time and Warner are engaged in lines of business that are primarily dependent upon people and hence it was critical that any merger transaction be so structured that the proposed combined enterprise would retain the loyalty, enthusiasm and continued performance of the journalistic and creative people upon whom the success of the combined enterprise would stand or fall (BB624-26, 783-84, 823, 873-877, 908-09).

Time has a long history as a journalism company and a strong tradition of journalistic independence (B624-25, 731-32). Time had adopted a unique corporate structure designed to protect that journalistic independence. Under this structure, the editors-in-chief of the Time magazines report directly to the Time board of directors rather than to management (Op. 15; A1560-62; BB625-26, 676). It was essential to Time to reassure the people on whom its success depends that Time's long-standing tradition of journalistic independence would not be compromised in any way by a business combination with an entertainment company (BB823; <u>see also</u> BB452).

Warner, for its part, had similar concerns. Its motion picture and record businesses are critically dependent upon relationships with key people: in the case of its motion picture business, upon relationships with the key personnel at the film studio and particular stars and directors; in the case of its record business, upon the key personnel at the record company and particular recording artists (BB22, 75, 266-67, 783-84). The evidence demonstrates, moreover, that a large number of the relationships upon which Warner is dependent for continued success in its businesses run directly to the company's chief executive, Steve Ross (BB472-73, 643).

Accordingly, Time and Warner carefully focused on devising structures that would serve to reassure their constituencies. This effort resulted in the formulation of a comprehensive set of governance procedures that were designed to mesh the two companies from the board of directors level all the way down to the subordinate executive level: certain businesses such as the cable businesses of Time and Warner would actually be combined; for others, careful lines of authority were devised to ensure that there would be full cooperation among the various core groups and at the same time deeply rooted traditions of autonomy would be preserved (A1875; BB237, 280-84, 912-21).

At the board level, the parties sought to provide reassurance to the Warner constituencies by expanding the Time board to 24 directors -- 12 previous Time directors and 12 previous Warner directors (Op. 19; A1874). Time's policy of having editors-in-chief report directly to the board would be preserved: an editorial committee of the board consisting of a majority of former Time directors would be formed (A1874-75; BB234, 282, 700, 917). Reciprocally, an entertainment committee, consisting of a majority of former Warner directors, would be formed to ensure the continuity of Warner's relationships with key core group managers and creative artists (Op. 19; BB234, 282, 700, 844-45, 917-18).

At the chief executive level, Time's plan for executive succession had long been set: Munro would retire as CEO in 1990 and would be succeeded by Nicholas. Nonetheless, recognizing the special relationship of Ross with the Warner constituencies, Munro and Nicholas proposed a <u>sharing</u> of the CEO position: there would be co-CEOs: first Munro-Ross, then Nicholas-Ross (BB238, 283-85, 831-32).

Warner also proposed that preexisting plans for executive compensation of senior Time executives be revised to reflect the approach which Warner used in compensating its executives: a bonus system tied to enhancement of stock values. Warner, an entertainment company, had significantly higher executive compensation than did Time and believed it desirable that the disparity be reduced. Munro, Nicholas and Levin refused the Warner proposal (BB205-07, 833-34).

By early August 1988, however, the negotiations ran into difficulty. Time's outside directors were not comfortable with the concept of perpetual co-CEOs: they wanted Ross' role as co-

CEO to be merely for a "transitional" period (BB178, 829-30). Ross formed the impression that this indicated a lack of personal confidence in him; that he would be undermined in his relations with the board; and that if he was perceived from the outset as a "lame duck" incumbent, the Warner constituencies would never get on board with the new company and the business combination would not work (BB177-78, 829-30). On August 11, 1988, Ross advised Time that Warner was terminating discussions (Op. 19-20; A1063, 1255; BB828, 838).

C. Final negotiations and agreement on a plan of merger

In early 1989, negotiations resumed after Ross had met with an outside Time director, Michael Dingman, and then with Munro (Op. 20; BB839-43). The air was cleared: the concern of the Time outside directors had been structural, not personal; they thought that an indefinite co-chief executive arrangement was not desirable (BB839-43). Upon reflection, Ross came to the conclusion that the Time outside directors were correct in this view (BB839-43; see also BB622-23, 708-710, 771-73). The parties agreed that Ross would remain co-CEO for a 5-year period at which point he would become chairman and Nicholas would become the sole CEO of the combined company (Op. 20; BB832). Ross was fully in accord with the prospect of Nicholas' ultimate position as sole-CEO: he had an extremely high opinion of Nicholas' abilities (BB832).

Representatives of Time and Warner then entered into a detailed and complex arm's-length negotiation concerning the terms and conditions of a stock-for-stock merger transaction that would be structured as an acquisition of Warner by Time. Intensive negotiations were had with respect to the exchange ratio. Myriad factors were discussed, including income, historic growth, anticipated future growth, cash flow, nature of businesses, asset values, market values, tax bases and the like (BB171-73, 619-21; see also BB701-05).

Ultimate agreement upon the exchange ratio -- .465 shares of Time common stock for each share of Warner stock -- was not reached until the morning of March 3, even as the boards of the two companies were meeting to consider the proposed transaction (A1896; BB180-81). At this ratio and at then-current market prices, Time as the acquiring company would have been paying a modest 12% premium over market for Warner shares (Op. 21; A1327). However, the price of Time stock had been buoyed by an extensive stock repurchase program (BB174-75, 929-30); Warner's growth projections were far greater than Time's -- as Paramount's own counsel put it on oral argument below, "Warner is the one that is going through the roof" (BB162) -- and, on a number of critical factors (including dilution with respect to the key factor of earnings per share) the exchange ratio operated negatively to Warner shareholders (BB794, 877-78).

At the agreed-upon exchange ratio the former Warner shareholders would have received 62% of the common stock of the proposed combined company (Op. 21). Warner, with its acquisition of Lorimar, was a larger company than Time; Warner's market capitalization was larger than Time's; Warner's net income in 1988 was significantly higher than Time's (A1925; BB722, 724-26, 846, 877-79). Warner's common stock is held by approximately 80,000 shareholders throughout the country (BB847). The Time common stock that would have been issued in connection with the proposed merger would therefore have been widely dispersed (Op. 59).

D. The March 3 merger agreement

On March 3, 1989, Time and Warner entered into a merger agreement providing for a stock-for-stock merger transaction at the .465 ratio. The transaction was approved after two lengthy meetings of the Warner and Time boards. Highly-qualified outside directors constitute a majority of the board of each company (Op. 21; A208-11, 230-32). Both Time and Warner received full presentations from their advisors, all of whom recommended the transaction unequivocally (see A1716-65, 1871-1915). The respective investment bankers for Warner (Lazard Freres & Co.) and for Time (Wasserstein Perella & Co., Inc. and Shearson Lehman Hutton Inc.) delivered fairness opinions. The transaction was unanimously approved by the Warner directors (excluding Chris-Craft's Herbert Siegel, who abstained*) and was unanimously approved by the directors present at the Time board meeting (see A1716-65, A1871-1915). Felix Rohatyn, a senior partner of Lazard Freres,

* There is a long history of divisiveness between Siegel on the one hand and the rest of the Warner board on the other (see, e.g., BB854). In May, Siegel resigned from the Warner board pursuant to the terms of a Stipulation and Judgment entered in Warner Communications Inc. v. Chris-Craft Industries, Inc., Del. Ch., C.A. No. 10817.

told the Warner board that, in his view, the merger would be the "seminal transaction" in the communications and media industries; that, if internal friction was kept to a minimum and executive succession was smooth, the transaction would be a "blockbuster" and "the best deal I've seen in thirty years" for all concerned. (A1876, 1896; see also A1877-78).

The press release issued by the parties to announce the merger expressly set forth that Time was acquiring Warner (BB927-28). While Warner understood this to be the fact, Warner felt the transaction was a hybrid: its shareholders were retaining their interest in the combined company; it was essentially a merger of equals (Op. 59-60; BB870-71). But as Steve Ross testified, the one thing that was clear was that the transaction "was definitely not an acquisition of Time by Warner" (BB871).

The agreement contemplated a stockholders vote of both Warner and Time: Warner because it was being merged into a subsidiary of Time; Time to satisfy an NYSE listing rule because it would be issuing common stock to the Warner stockholders (Op. 22; A1938; BB188).

E. The Share Exchange Agreement

In agreeing to enter into the merger transaction, stock for stock, the parties recognized that the very announcement of the transaction would serve to put a "spotlight" on the two companies which carried with it the risk that they might end up being put "in play". Consideration had been given to actions that might be taken to minimize that potentiality and protect the transaction during the months that would pass before the merger could be consummated. One course that had been considered was to exchange blocks of common stock of "18.5% to 25%" (A1054). At its meeting held back on July 21, 1988, the Time Board had been told that this was a "structural safety measure" (id.). Ultimately, however, this was not done: the parties instead, simultaneously with the March 3 merger agreement, entered into a Share Exchange Agreement which provided for the exchange of far smaller blocks of stock: Warner would acquire 7,080,016 shares (11.1%) of Time and Time would acquire 17,292,747 shares (9.4%) of Warner (the exchange ratio being fixed based upon the average closing prices of Time and Warner common stock for the five days prior to the merger announcement) (BB62, 197-98, 858). And, with narrow exceptions, the voting of the exchange stock was effectively sterilized: there was "pass through" voting in the same proportion as the vote of the public shareholders (A350). The share exchange was not a "lock up" or a "blocking position." Indeed, Mr. Davis of Paramount has now conceded that the share exchange did not operate to preclude Paramount from having "a fair chance of acquiring [Time]" (BB462).*

* The evidence reflects that the parties' reasons for entering into the Share Exchange Agreement were: (a) if the merger was not consummated, each party wanted the benefit of an equity investment in the other; (b) Time and Warner wanted to send an immediate message down through the ranks and to the marketplace that each had a present economic interest in the other and of their strong commitment to the consummation of the proposed merger; and (c) if the merger was not successful, the disappointed party -- and particularly Warner, which anticipated that it would likely be giving up significant benefits under its shareholders' agreement with Chris-Craft and BHC -- desired to have a

(footnote continued)

F. The Paramount $175 offer

Immediately following the announcement of the merger, Paramount decided to explore a hostile offer for Time (Op. 25; BB477-82, 489-595). Nevertheless, it was not until June 7, 1989 -- just 16 days before the June 23 scheduled shareholder votes -- that Paramount launched its $175 offer for Time (BB596). And Paramount then chose to condition its offer on, among other things: (a) financing; (b) termination of the Time/Warner merger; (c) termination of the Share Exchange Agreement "without liability" to Time; (d) Paramount being satisfied "in its sole discretion" that it had received all necessary approvals for the transfer of Time's cable businesses on terms "satisfactory to [Paramount]"; (e) redemption of the Time Rights; and (f) determination that § 203 of the General Corporation Law is inapplicable to a Time/Paramount merger (BB596-609).

Paramount knew that its offer could not possibly be consummated for many months (BB485-86, 763-67). Indeed, Citibank, Paramount's commercial banker -- after consultation with Paramount's Chief Financial Officer (BB301-02) -- concluded in its

(footnote continued)

stock interest that would permit it to share to some extent in any premium offer for the other party. (BB30, 48, 65, 627-28, 727-28, 855-59).

The validity of the share exchange was not at issue upon the motion below. The Chancellor stated that "[f]or present purposes, I assume [the] principal purpose [of the share exchange] was to discourage any effort to upset the transaction" (Op. 23). This is one of a number of disputed facts that the Chancellor assumed (but did not decide) in favor of plaintiffs (Op. 5, 23).

Credit Initiation Memorandum that the first-step tender offer would not close until March or April 1990 (BB359, 362). Paramount nevertheless sought to foster a public misimpression that its offer could close promptly: Paramount, for example, widely publicized its creation of an FCC "voting trust" (BB922-23), while obscuring from the public -- as well as the FCC itself -- the fact that such voting trust would not permit it to circumvent the time-consuming process of obtaining local regulatory approvals for the transfer of Time's cable franchises (see BB467-68). Paramount knew, however, that its offer would have one immediate consequence: it would interfere with Time's ability to secure a favorable vote of its shareholders on the merger on June 23 (BB483-84, 487-88, 944-45).

G. Time and Warner seek to proceed with the merger

As noted, by June 7 Warner and Time were on the eve of consummating their merger: regulatory approvals were falling in place (BB683, 749). Time and Warner remained convinced that continued pursuit of their long-planned business combination remained in the best interests of their shareholders (A1595; BB184-86, 883-84). However, the commencement of Paramount's highly conditional offer and the illusion Paramount sought to foster of a potential for a prompt closing caused Time and Warner to conclude that it would not be feasible to obtain Time stockholder approval of the merger within the time frame anticipated under the original merger agreement (BB183-84, 189-90, 196, 199-201, 633-34, 733-36, 741-43, 860-61, 931-41).* And Warner was not prepared to sit in limbo for months (BB743, 745, 899-900).

Discussions then ensued concerning how the merger transaction could be accomplished without undue delay. Warner, which had a strong preference to stay with the original stock-for-stock transaction, suggested seeking an NYSE ruling that the transaction did not fall within its voting rule (BB884-86). Time was reluctant: Time preferred to go to a cash-for-stock deal -- the form of transaction that Time had desired from the outset (BB187, 193-95, 863, 883-890; see also A1938, 1954-55). Nevertheless, at Warner's strong insistence, Time agreed to present the issue to the NYSE; the NYSE disagreed with Warner's interpretation of the rule (A1284, 1938; BB631-32, 634-35, 863-64, 884-87).

Meanwhile, arduous arms' length negotiations of Time's proposed cash acquisition alternative had gone forward (Op. 38). There were extensive price negotiations with the parties ultimately agreeing to a $70 price (A1955; BB191) -- subject to the proviso insisted upon by Warner that there be the potential for Warner shareholders to receive some equity in the combined company on the back-end (A1918; BB192-94, 894-904).

A critical subject of negotiation involved Time's desire for "outs" to its obligation to consummate the tender offer (BB192-94, 204). Warner was totally unwilling to accede since

* The Court of Chancery assumed, for purposes of its decision, that Time, in revising its agreement with Warner, "sought to avoid the risk that the merger would not get an affirmative vote even if there were no confusion" (Op. 37).

Warner, by agreeing to a cash acquisition, was putting itself up for sale and was concerned about being left in the lurch by Time (BB204, 745, 866-67, 899). Warner therefore insisted upon a "hell or high water" deal that would not give Time the option of abandoning the transaction if Time later should decide that that course suited its own purposes (Op. 41; A1919, 1926, 1941, 1943; BB21-22, 192-93, 202-04, 866-67; see also A1286-87, 1289-90). Time ultimately agreed (BB639-41, 748-49; see also A1918-21). Late in the night of June 15, agreement was reached upon the remaining open issues (BB910-11).*

H. The revised merger agreement

The revised agreement provided that Time and Warner would proceed with a two-step merger transaction (A1918): a cash tender offer by Time at $70 per share for 100 million shares (just over 50%) of Warner stock to be followed by a second-step merger in which Warner stockholders would receive cash or equity securities valued at $70 per share, the specific package to be

* Mid-afternoon of June 15 -- at a point when the parties had yet to reach agreement on a revised transaction -- Warner determined to exercise its rights under the Share Exchange Agreement and asked Time to waive the 5 days' notice provision of that Agreement to allow an immediate closing (BB909-10; see A1918, 1929-30). Time refused: Time was upset that Warner was exercising its rights at a point when no agreement had been reached on a revised merger (BB862-64, 891-92, 913). Warner nonetheless proceeded unilaterally to give the 5 days' notice (A1929-30; BB862-64, 891-92, 909-11, 913). By the next morning, understanding had been reached on the revised merger; for technical SEC reasons, the share exchange would be precluded once the tender offer was announced; Warner's board was therefore not willing to proceed unless the share exchange had first been consummated. Time thereupon acquiesced in accelerating the closing of the share exchange (BB662, 737-38, 892, 910-14).

agreed upon in light of future circumstances. A "fail-safe" clause provided that, in the event that the parties could not agree upon the proportions of cash and stock to be issued on the back-end, the ratio would be fixed, at Time's election, either at 60% cash and 40% equity or at 40% cash and 60% equity (A1932, 1939). (Subsequently, it has been agreed that the back end would not consist of more than 50% cash.) The governance provisions would now be implemented upon the closing of the first-step tender offer: until the second-step merger occurred, the boards of both Time and Warner would consist of 12 "Time" directors and 12 "Warner" directors (A1941-42; BB744).

The merger agreement also prohibited Time from redeeming its Rights in the period prior to the consummation of the merger (A568). (Warner was unwilling to find itself relying upon some stranger for fulfillment of Time's contractual commitment to effectuate the merger, including negotiation of the open terms of the back end.) The merger agreement, however, placed no restriction on the Time Warner board's redemption of the Rights once the merger was consummated; moreover, even prior to that time, there is no restriction on the Time board's _agreeing_ with an offeror that it will redeem the Rights in favor of the offer as soon as the merger is consummated (_id_.).

The boards of Time and Warner met separately on June 15 and 16 to consider the terms of the revised merger transaction (_see_ A1809-70, 1916-56; BB654-74). Warner's board was fully briefed by its advisors; received a fairness opinion from Lazard on the $70 purchase price; and intensively debated whether or not to proceed with the sale of the company to Time (see generally A1916-56; BB654-74). The ultimate vote in favor was unanimous (BB661).

Pursuant to the revised merger agreement, Time's Offer for Warner at $70 per share was commenced on June 16, 1989. The offer is now scheduled to be consummated at 5 p.m. on July 24, 1989.

I. Paramount's reaction

On June 23, 1989, Paramount increased the price of its offer to $200 per share; all the conditions to Paramount's offer remained (see A686). Thus, Paramount's offer continues to be conditioned upon abandonment of the Time-Warner combination even though Davis in his testimony conceded:

-- that in his opinion, after merging with Warner, Time could be more vulnerable to a takeover (BB455-60);

-- that Paramount's decision that it wished to acquire only Time -- and not Warner as well as Time -- was a "business decision" (BB461, 465);

-- that he knows of nothing, other than "Paramount's choice", that prevents Paramount from going ahead with its offer for Time even if the revised Time-Warner merger agreement stays in place (BB464, 466); and

-- that in the event the Delaware court does not enjoin the revised Time-Warner merger agreement, Paramount will then "evaluate" the situation and decide whether or not to proceed anyway; as Davis put it, "from a business judgment standpoint, we'll get to that point when we get there" (BB463, 465-66).

And Paramount did not even attempt to claim that the revised merger structure made it more difficult for it to acquire the combined company than the original merger structure.*

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* In its original motion papers below, Paramount did not attempt to make an evidentiary showing to support a claim that Time's acquisition of Warner would preclude (or even inhibit) a Paramount acquisition of the combined entity. Then, for the first time, in reply, Paramount proffered an affidavit of its investment banker, Waters, which sets forth his opinion that _if_ one assumed certain premises, then "the possibility of an acquisition of Time-Warner at anything close to $200 per share" would be foreclosed and that the possibility of an acquisition of Time Warner "may" altogether be foreclosed (A1511).

The Waters affidavit and the underlying premises for Waters' opinion were thoroughly refuted by affidavits of Frederick Seegal of Shearson Lehman Hutton Inc. (BB119-34) and of Kevin D. Senie, Vice President of Time (BB135-41). (_See also_ affidavit of Jonathan O'Herron of Lazard Freres, sworn to on July 14, 1989, submitted in opposition to motion for injunction pending appeal (BB51-59)). And Paramount's own counsel thereafter conceded of record that "[o]n Tuesday [at oral argument of the preliminary injunction motion] there was no representation that we had absolutely ruled out bidding at a lower price for the combined companies" (BB164).

ARGUMENT

I. THE CHANCELLOR CORRECTLY CONCLUDED THAT PLAINTIFFS FAILED TO SHOW A REASONABLE PROBABILITY OF SUCCESS ON THE MERITS OF THEIR CLAIMS AGAINST THE TIME DEFENDANTS

A. Standard and scope of review

As an exercise of its discretionary powers, the Court of Chancery's denial of plaintiffs' motions for a preliminary injunction may only be reversed for abuse of discretion, *see, e.g.*, *Gimbel* v. *Signal Cos.*, Del. Supr., 316 A.2d 619, 620 (1974) (*per curiam*) -- that is, if "the action taken below was arbitrary or capricious." *Daniel D. Rappa, Inc.* v. *Hanson*, Del. Supr., 209 A.2d 163, 166 (1965). This Court's scope of review is even more limited here, for the Chancellor's exercise of discretion was based largely upon his considered rejection of plaintiffs' disputed interpretation of the factual record. This Court may reach its own conclusions only "if the findings of the trial court are clearly in error and justice so requires," and must accept those of the Chancellor "if they are supported by the record, and otherwise are the product of an orderly and logical deductive reasoning process." *Mills Acquisition Co.* v. *Macmillan, Inc.*, Del. Supr., Nos. 415, 416, slip op. at 39, Moore, J. (May 3, 1989); *Levitt* v. *Bouvier*, Del. Supr., 287 A.2d 671, 673 (1972).

B. The Chancellor did not abuse his discretion

The Chancellor held that plaintiffs failed to show a reasonable probability of success on the merits of their claims against the Time defendants. The Chancellor therefore did not reach the questions whether plaintiffs had established their "aiding and abetting" claims against Warner or whether plaintiffs had shown irreparable injury and that the balance of equities tipped in their favor (<u>see</u> Points II and III, <u>infra</u>).

In reaching the conclusion that plaintiffs had failed to prove their case as against the Time defendants, the court reviewed thousands of pages of testimony and documentary exhibits and reasoned to several critical findings of fact. The most important of the Chancellor's findings of fact compel the affirmance of the decision below which involved issues that are preeminently fact intensive. These findings are:

-- In pursuit of its long-term strategy of developing film production capacity to feed its HBO division and expanding its international markets (Op. 8-9, 11), Time reviewed various "'studios' -- including Disney, Paramount . . . MCA-Universal, Columbia and Twentieth Century Fox" (Op. 13).

-- Of these companies, Warner was considered "the most desirable . . . for several reasons, including the success of its movie studio . . . ; the fact that its existing cable operations would meld easily with Time's; its important presence in the music business where Time had no presence; and because of its international distribution assets and capability" (Op. 13).

-- As to the "thoughtfully planned consolidation" (Op. 2) of Time and Warner announced on March 3, the Chancellor found:

    -- that it was "chiefly motivated by strategic business concerns" (Op. 68);

    -- that plaintiffs failed to provide <u>any</u> record evidence that the deal "was other than an arm's-length negotiated agreement between two parties seeking individual advantage through mutual action" (Op. 21); and

-- that the deal "did not legally preclude or impede a later sale or change in control transaction" (Op. 61).

-- As to the June revision to the Time-Warner plan of consolidation, the Chancellor found:

-- that the "record contains no evidence to support a supposition" that the decision to revise the deal was not taken in good faith (Op. 46);

-- "there is no persuasive evidence that the board of Time has a corrupt or venal motivation in electing to continue with its long-term plan" (Op. 76-77);

-- the revised deal "has its origin and central purpose in _bona fide_ strategic business planning, and not in questions of corporate control" (Op. 73);

-- "[t]he revamped transaction was negotiated at arm's-length" (Op. 38); and

-- the revised deal "does not legally" (Op. 76) or "practical[ly]" (_id._) foreclose a hostile offer for the combined company.

These findings are fully "supported by the record" and there is no indication that they are not "the product of an orderly and logical deductive reasoning process". _Macmillan_, slip op. at 39.

On the basis of these findings, the court properly rejected each of plaintiffs' claims of breach of fiduciary duty as against the Time defendants.

1. _The Time defendants did not violate Unocal; their actions were reasonable in relation to the threat posed_

The Chancellor applied this Court's decision in _Unocal v. Mesa Petroleum Co._, Del. Supr., 493 A.2d 946 (1985), in determining the legality of the Time board's actions. Assuming, _arguendo_, that _Unocal_ is applicable here, the Time defendants clearly did not violate their enhanced _Unocal_ duties. To the contrary, as the Chancellor concluded (Op. 68-76), and as the evidence established, "the revised merger agreement and the Warner tender offer _do_ represent actions that are reasonable in relation to the specific threat posed to the Warner merger by the Paramount offer" (Op. 76) (emphasis added).

Thus, the Time defendants had "reasonable grounds for believing that a danger to corporate policy and effectiveness existed" (_Unocal_, at 955), in that the Paramount offer posed a threat to Time's long-planned acquisition of Warner. The Chancellor noted that the Paramount offer made it "problematic" whether shareholder approval could be obtained, at least in the near term, for a transaction that had been "widely supported as a fine transaction" (Op. 28-29, 36) and that the Warner acquisition had "its origin and central purpose in _bona fide_ strategic business planning" (Op. 73, 74). The Chancellor also concluded that realization of Time's strategic plan by completing the Warner acquisition was "reasonably seen as of unquestionably great importance" by the Time board (Op. 76).* And this Court has squarely held that a board may properly take such

* The lower court's findings belie plaintiffs' strained argument (Paramount Br. 32) that the Chancellor somehow "rejected" the _Unocal_ standard and adopted instead a "subjective bad faith" standard of review. In fact, the Chancellor _expressly_ applied the _Unocal_ standard, holding, as noted above, that the revised transaction was "reasonable in relation to the specific threat posed to the Warner merger" (Op. 76) and the decision below is replete with factual findings supporting this holding. Moreover, it is hardly surprising that the Chancellor also made findings as to the Time defendants' motives inasmuch as Paramount's attack upon those motives was the centerpiece of its case.

long-term strategic plans into account in determining how to respond to a tender offer. Macmillan, slip op. at 55 n.35.

The decision by the Time board to seek to accomplish the Warner acquisition by means different than originally contemplated was also "reasonable in relation to the threat posed." Unocal, 493 A.2d at 955. As the Chancellor put it, the board's action was not "overly broad" and Time "did only what was necessary to carry forward a preexisting transaction in an altered form" (Op. 76). It is difficult to imagine a more measured response than that adopted by Time which simply restructured a beneficial transaction so that it could be accomplished notwithstanding a threat reasonably perceived.

Furthermore, as the Chancellor found (Op. 76), the transaction as presently structured, like the original proposal, would not as a practical matter foreclose the possibility of a future takeover of the combined company (BB461, 462a-466). And while the acquisition of Warner by Time might complicate Paramount's plans, it is "well established that a tender offeror has no right to freeze the business he seeks to acquire while his offer goes forward". See UIS v. Walbro Corp., Del. Ch., C.A. No. 9323, slip op. at 8-9, Allen, C. (Oct. 6, 1987); GM Sub Corp., v. Liggett Group, Inc., Del. Ch., C.A. No. 6155, slip op. at 5, Brown, V.C. (Apr. 25, 1980). A fortiori that is the case here where the Time-Warner business combination antedated Paramount's appearance on the scene and Paramount, for its own business purposes, chose to condition its offer upon Time's abandonment of a pre-existing transaction.

Plaintiffs place principal reliance on a series of cases involving defensive restructurings by target corporations. Grand Metropolitan PLC v. The Pillsbury Co., Del. Ch., C.A. Nos. 10319, 10323, Duffy, J. (Dec. 16, 1988); City Capital Associates v. Interco, Inc., Del. Ch., 551 A.2d 787, appeal dismissed, Del. Supr., 556 A.2d 1070 (1988); Robert M. Bass Group, Inc. v. Evans, Del. Ch., 552 A.2d 1227, appeal dismissed, Del. Supr., 548 A.2d 498 (1988); AC Acquisition Corp. v. Anderson, Clayton & Co., Del. Ch., 519 A.2d 103 (1986). Regardless of the validity of the holdings of these cases, they are clearly not applicable here, as Chancellor Allen (who wrote two of those decisions) recognized. Each of those cases involved:

-- two alternative transactions -- one management, one non-management -- directed to the same shareholder body, the management transaction having been put forward as an alternative to the hostile offer;

-- the substantial cashing out of the target's shareholders in a transaction which was the "functional alternative" to a sale of the company (see TW Services, Inc. Shareholders Litigation, Del. Ch., C.A. Nos. 10427, 10298, slip op. at 25, Allen, C. (Mar. 2, 1989));

-- the management and non-management transactions being closely comparable in value with the superiority of the management transaction being questionable at best;

-- the hostile offer being ready to close or virtually ready to close; and

-- the target's board -- by use of a rights plan or other device -- acting to foreclose the non-management alternative so as to cram down the management alternative.

In _these_ circumstances, the Court of Chancery held that the failure to offer shareholders a "choice" between the transactions did not withstand scrutiny under _Unocal_.

These precedents are not remotely applicable here. As repeatedly conceded by Paramount (which has not ruled out a bid for the combined Time Warner), the Time tender offer for Warner and the Paramount offer for Time are not mutually exclusive. The two offers are not directed to the same shareholder body. The Time offer for Warner was not cooked up as a management-sponsored alternative to the Paramount offer for Time. The Time offer for Warner does not involve the break-up of Time or the cashing out of any equity of Time shareholders, and is thus not at all a "functional alternative" to the Paramount offer for Time. And critically, the motions below did not involve any issue of the Time board blocking the closing of the Paramount offer through the use of a rights plan or any other device. Rather, Paramount cannot close its offer anytime in the near future because it has barely begun the process of obtaining the necessary FCC and local cable authority approvals. Indeed, there is no assurance that Paramount will ever be in a position to close its offer -- or will desire to do so.* In

* The words "on terms satisfactory to [Paramount]" in Paramount's "regulatory approvals" condition were not idly chosen; rather they reflected Paramount's own recognition that local authorities, as the price of approval of transfer of cable franchises, might impose conditions upon Paramount (_e.g._, requirements for capital expenditures) that might lead Paramount to conclude that it preferred, for economic reasons, not to proceed with the acquisition.

these circumstances there was nothing "unreasonable" in the Time board's decision that it was not required to sacrifice the highly desirable Warner transaction -- at a concededly fair price -- while it waited for perhaps up to a year to see whether Paramount would ever be able and willing to close the Paramount offer.

Mills Acquisition Corp. v. Macmillan, Inc., Del. Supr., Nos. 415, 416, Moore, J. (May 2, 1989), heavily relied on by the shareholder plaintiffs principally for its approving summary of Bass Group, supra, (Sh. Br. 29-31), is inapposite here. In addition to the distinctions between Bass Group and this case noted above: (a) the Macmillan restructuring involved a year-long management scheme to gain control of key assets of a corporation as a takeover defense; in its final form it transferred to management 39% of the stock of a new corporation holding such assets (slip op. at 5, 19, 42); (b) in Macmillan, the directors were not fully informed about the hostile offer because management affirmatively misled it as to both the putative acquiror's character and the bona fides of "negotiations" conducted by management with it (slip op. at 9-10 & n.7, 16-17);* and (c) in Macmillan, although the huge

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* Plaintiffs do not make any serious case that the Time board did not adequately inform itself as to the Paramount offers. Their case amounts to the sole contention that Time's directors erred by not negotiating with Paramount to find out its highest price. Delaware law is clear that there is no duty to negotiate with a hostile bidder where a board believes in good faith that it is not in the best interests of stockholders to do so. See Pogostin v. Rice, Del. Supr., 480 A.2d 619, 627 (1984); MacAndrews & Forbes Holdings, Inc. v. Revlon, Inc., Del. Ch., 501 A.2d 1239, 1251, Walsh, C. (1985), aff'd, Del. Supr., 506 A.2d 173 (1986). Bass Group, where the board was affirmatively misled

(footnote continued)

equity interest that management was receiving in the restructuring plainly required the board to form a special committee with independent advisors, management hand-picked and secretly pre-conditioned those advisors, seriously impairing their independence (slip op. at 11-12, 15-16 & n.11). There is no counterpart in the present case to any of these factors in Macmillan. Finally, the supposed parallels between the ultimate Macmillan auction and this case are far-fetched. There has been no auction here; there is no "management bidding partner"; and there is not even any allegation of the gross misconduct that marred the Macmillan auction.

Plaintiffs also argue that it was error for Chancellor Allen to find the Warner transaction reasonable because in plaintiffs' view if one discounts anticipated trading prices of the stock of the combined Time-Warner to present value, the result is supposedly less than $200 per share (Paramount Br. 4, 26, 28, 37-38, 41-42, 44; Sh. Br. 16-18). This attempt to transmute the reasonable judgment of the Time board into a numbers game is fallacious for numerous reasons, including:

- -- Plaintiffs' argument in essence assumes that the combined enterprise will cease to exist in 1993 and that there will be no growth thereafter.
- -- Plaintiffs mix "apples and oranges" when they compare the present value of anticipated future

(footnote continued)

as to negotiations and where there was a sale of control that triggered Revlon duties, see Macmillan, supra, slip op. at 16-17, 55-56, is not to the contrary.

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stock prices (which do not include a premium for control) with a "$200" Paramount offer which presumably does include a premium for control (A1529).

-- Plaintiffs purport to discount expected future trading prices to present value but fail to discount Paramount's "$200" per share offer to reflect delay and uncertainty of consummation.

And, significantly, as the Chancellor observed (Op. 36 n.9), the determination by the Time directors that the Warner transaction serves long-term shareholder interests is supported by the expert opinion of a senior official of Time's single largest (7%) shareholder: "the proposed Time-Warner combination is superior for Time shareholders . . . to the currently outstanding Paramount [$200 per share cash] offer" (see BB3-7).

2. Plaintiffs' "entrenchment" claims are frivolous

While plaintiffs' briefs attempt to create the misleading impression that Time's effort to acquire Warner stemmed from impermissible motives of management entrenchment, plaintiffs do not -- because they cannot -- seriously argue that the Time tender offer for Warner must be enjoined on that basis. The well-settled legal test applicable to such claims is whether the board's action is motivated "solely or primarily" for the purpose of retaining office for personal reasons and not for reasons relating to the corporation's welfare. See Unocal Corp. v. Mesa Petroleum Co., supra, 493 A.2d at 955; Cheff v. Mathes, Del. Supr., 199 A.2d 548, 556 (1964); Johnson v. Trueblood, 629 F.2d 287, 293 (3d Cir. 1980) (Seitz, C.J.), cert. denied, 450 U.S. 999 (1981).

Here, the evidence establishes, and the Chancellor found, that the original March 3 transaction "was, or appears at this stage to have been chiefly motivated by strategic business concerns" (Op. 68) and that the revised transaction "has its origin and central purpose in *bona fide* strategic business planning and not in questions of corporate control" (Op. 73). This is the short answer to plaintiffs' entrenchment claim.

Moreover, as the evidence established, the corporate governance arrangements the parties entered into were essential. They were not some code word for "entrenchment" but were rather designed to retain the continued performance of key management personnel, journalists and creative talent upon whom the businesses of the two corporations both plainly depend. Indeed, far from being an entrenchment device, Time management and directors had each agreed to *share* power with Warner personnel as the price of accomplishing an advantageous transaction. And, to the extent the Time board was motivated by a desire to maintain Time as an independent company (Op. 9-10), there is nothing improper about this. *See Ivanhoe Partners* v. *Newmont Mining Corp.*, Del. Supr., 535 A.2d 1334, 1344 (1987).

3. *Time was never in a "Revlon mode"; the Time directors had no fiduciary duty to maximize current share values*

Although Paramount relied extensively in the court below on this Court's decision in *Revlon, Inc.* v. *MacAndrews & Forbes Holdings, Inc.*, Del. Supr., 506 A.2d 173 (1986), Paramount has apparently abandoned its *Revlon* argument on appeal.

The shareholder plaintiffs argue that -- because the original merger plan would have resulted in over 60% of Time's stock being held by former Warner stockholders, Warner management and directors would continue at Time, and Warner would supposedly have a "blocking position" in Time -- adoption of the original Time/Warner stock merger placed Time in a Revlon mode, so that once Paramount appeared as an offeror, Time's directors had no alternative but either to sell Time or otherwise to maximize Time's short-term share value (Sh. Br. 43-46).

This argument is fallacious both in fact and in law. First, the original proposed stock merger of Time and Warner neither put Time up "for sale", see Macmillan, slip op. at 55 & n.35 ("clearly not every offer or transaction affecting the corporate structure involves the Revlon duties"), nor would have resulted in a change in control of Time. Time was to be the surviving entity; none of its stockholders' equity interests was to be terminated. Contrary to the shareholder plaintiffs' arguments (Sh. Br. 43-44), and as the Chancellor found (Op. 59-60), the fact that this would result in former Warner stockholders holding over 60% of Time's shares no more indicated occurrence of a change of control than would a commensurate public stock offering. As the Chancellor reasoned, "where, as here, the shares of both constituent corporations are widely held, corporate control can be expected to remain unaffected by a stock for stock merger . . . control of both [Time and Warner] remained in a large, fluid, changeable and changing market" (Op. 59-60).

Second, the fact that certain Warner directors and executives were being afforded a post-merger role at Time did not mean that the company was being sold. This argument is totally inconsistent with the Chancellor's finding that Time and its culture were surviving and predominating in the merger. Moreover, both before and after the proposed merger, Time's and Warner's board and management were and would have been controlled by public stockholders.

Third, as to the so-called "blocking position" received by Warner in the share exchange, the 11.1% of the stock issued to Warner pursuant to the share exchange (which has pass-through voting) does not remotely constitute a blocking position. Moreover, by definition, once the merger is accomplished, these shares would cease to exist and revert to treasury shares. There is no "blocking position."

In sum, the Time/Warner stock merger did not put Time into a Revlon mode. (A fortiori, the transaction now on the table does not put Time in a "Revlon mode". The Time shareholders are not being cashed out. Time is acquiring Warner, and plaintiffs do not argue otherwise.)

Furthermore, the facts of this case do not remotely resemble those of Revlon, where the directors agreed to a leveraged buyout. 506 A.2d at 178.* If any post-Revlon case

* The other cases cited by plaintiffs are likewise distinguishable. Thus, in Macmillan the board formally decided "that it would be in the best interests of the stockholders to sell the company" (slip op. at 55-56). Black & Decker Corp. v. American Standard, Inc., 682 F. Supp. 772 (D. Del. 1988), involved a re-

(footnote continued)

is applicable here, it is Newmont, supra -- in which, although the target of a hostile offer had reached an agreement allowing a third party to purchase up to 49.9% of the target's stock and to control 40% of the target's board, this Court concluded that the record did not support a finding that "the sale of Newmont was 'inevitable'," because "[f]irst, Newmont was never for sale," and, "[s]econd, there was neither a bidding contest nor a sale." Newmont, supra, 535 A.2d at 1345. Here, as in Newmont, Time was never for sale; the Time board "held fast to its decision to keep the company independent (id.)"; and there was neither a bidding contest nor a contemplated sale. Indeed, this case is a fortiori of Newmont: whereas in Newmont control of 49.9% of the outstanding stock, and 40% of the board seats, passed to a single entity, here there is no such entity or group.

In the absence of any factual similarity between this case and Revlon or its progeny, shareholder plaintiffs urge, as the Chancellor recognized (Op. 63), a radical extension of Revlon: that case would no longer be limited to cases in which a company's "sale" or "break-up" is inevitable; it would govern any transaction that might be considered "extraordinary" or as "preclud[ing] a future control premium or private market trans-

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(footnote continued)

structuring that would have given management control of approximately 55% of the company. And Freedman v. Restaurant Associates, Inc., Del. Ch., C.A. No. 9212, Allen, C. (Oct. 16, 1987), and Edelman v. Freuhauf Corp., 798 F.2d 882 (6th Cir. 1986), involved leveraged buyouts.

action" for the corporation (Op. 60, 63). Leaving aside the lower court's holding -- plainly supported by the record -- that neither the original nor the revised merger would preclude or impede a later sale or change in control of Time (Op. 76), plaintiffs' novel reading of Revlon would radically alter Delaware corporation law.

Thus, plaintiffs' reading of Revlon is at odds with Revlon itself. In Revlon, this Court recognized that long-term strategic plans have no significance when a company is to be sold or broken up, and thus that the only appropriate goal for a board in a Revlon mode is maximization of short-term share value. See Revlon, supra, 506 A.2d at 182. To argue, as plaintiffs do, that a transaction such as the Time/Warner combination designed to effectuate long-term corporate policies and to achieve long-term gains for stockholders somehow triggers a Revlon duty to consider only short-term maximization of share value is absurd on its face.*

More fundamentally, plaintiffs' vision of Revlon would eviscerate the right and duty of boards to engage in long-term business and strategic planning, see TW Services, supra, slip op. at 18-19; Hahn v. Carter-Wallace, Inc., Del. Ch., C.A. No. 9097, slip op. at 5, Hartnett, V.C. (Oct. 9, 1987), and inject

* Before the Court of Chancery, Paramount argued that Revlon should be read to mean that a vote -- or some sort of "shareholder choice" -- was required before Time could commence its tender offer for Warner. Paramount has now apparently abandoned any Revlon argument and the shareholder plaintiffs do not argue that Revlon requires any sort of "shareholder choice" here.

undesirable uncertainty into Delaware corporate law. A corporation such as Time could decide to engage in fundamental corporate change in pursuit of a long-term business plan only at the risk that -- because of its decision -- it might find itself required by law to abandon its long-term goals and seek only to maximize short-term share values in the event of an intervening bid for its shares. Plainly this would discourage and hinder long-term business and strategic planning by Delaware corporations.

4. The Time defendants did not violate Schnell; no doctrine of Delaware law required a vote of the Time shareholders

Plaintiffs argued in their briefs below that, by restructuring the transaction so as to eliminate a Time shareholder vote, the Time defendants had manipulated the corporate machinery in violation of this Court's decision in Schnell v. Chris-Craft Industries, Inc., Del. Supr., 285 A.2d 437 (1971), and related cases. Plaintiffs upon appeal appear to have virtually abandoned this argument, which is relegated to a footnote in Paramount's Opening Brief (p. 40, n.17).

In any event, as the Chancellor correctly concluded, Time was not required to give its shareholders a vote, or any other "choice", in connection with its tender offer for Warner. The power of the Time board to commence a tender offer without a shareholder vote rests on firm statutory and case-law authority and is confirmed by the practice of hundreds of Delaware corporations that have commenced tender offers without a shareholder vote.

Thus, the original transaction contemplated a shareholder vote to satisfy a New York Stock Exchange listing rule because the transaction involved the issuance of Time stock. The revised transaction does not call for a shareholder vote because it does not involve the issuance (at this stage) of Time stock. And Delaware law contains no requirement for a Time shareholder vote with respect to either the original or the revised transaction.*

Moreover, as the Chancellor recognized (Op. 66), even if Delaware law had required a shareholder vote on the original transaction, the classic doctrine of independent legal significance would preclude any argument that once having embarked on a transaction in a form requiring a shareholder vote, the Time board had gone down the path of no return so that it could no longer change to a form that did not require such a vote. E.g., Orzeck v. Englehart, Del. Supr., 195 A.2d 375, 378 (1963). See also Lowenschuss v. Option Clearing Corp., Del. Ch., C.A. No. 7972, Brown, C. (Mar. 27, 1985) (transaction reformulated after shareholders had rejected the original proposal); American International Rent A Car, Inc. v. Cross, Del. Ch., C.A. No. 7583, Berger, V.C. (May 9, 1984) (withdrawing proposal from shareholders and submitting it to board when defeat at shareholder meeting seemed inevitable) (Op. 67).

* Delaware law did not require a shareholder vote on the original merger proposal -- a reverse triangular merger between Warner and a wholly-owned subsidiary of Time -- because Time was not a constituent corporation to the proposed merger (see 8 Del. C. § 251).

Furthermore, the Time board's authority to proceed without a shareholder vote is predicated upon 8 Del. C. § 141(a) which establishes the "bedrock" rule that the business and affairs of a corporation are to be managed under the direction of its board. See Pogostin v. Rice, Del. Supr., 480 A.2d 619, 624 (1984). The board's authority also derives from Section 123 of the General Corporation Law, which authorizes Delaware corporations to purchase shares of other corporations. Nothing in the statute, or case law, remotely suggests that exercise of the Section 123 power requires any form of shareholder vote or choice, and implication of such a requirement is disfavored under Delaware law. See Moran v. Household International, Inc., Del. Supr., 500 A.2d 1346, 1351 (1985); Unocal Corp. v. Mesa Petroleum Co., Del. Supr., 493 A.2d 946, 957 (1985).

Nor does this case implicate Schnell. The Schnell line of cases involve interference with voting rights in situations where shareholders are indisputably entitled to a vote. The issue in this litigation is not one of manipulation of corporate machinery in a case where shareholders are entitled to vote. The issue in this litigation is whether Delaware law imposes any requirement of a shareholder vote in the first place. As shown, the Time board was authorized by 8 Del. C. §§ 141(a) and 123 to proceed with the tender offer for Warner without a shareholder vote.

In sum, the laws of this state vest directors with the power to manage the business of a corporation, except where a statute otherwise provides. If shareholders object to the directors' actions, their remedy is to elect new directors who will follow a different course. This of course does not mean that directors can violate their fiduciary duties of loyalty and care but, as the Chancellor found, no such breach has been established here. To the contrary, the Time board properly exercised "perfectly conventional powers" (Op. 77) in authorizing a transaction believed to be highly beneficial to shareholders.

II. PLAINTIFFS FAILED TO SHOW A REASONABLE PROBABILITY OF SUCCESS ON THE MERITS OF THEIR "AIDING AND ABETTING" CLAIMS AGAINST WARNER

A. Standard and scope of review

In light of its holding that there was no breach of duty by the Time board, the Court of Chancery explicitly did not opine whether Warner was liable as an aider and abettor, Op. at 79, an issue raised by Warner in the court below. Nevertheless, the court made several findings of fact which preclude that legal finding. This Court's review of the factual findings is constrained by the clear error standard (see Argument I.A. above); however, the legal conclusions which flow from those facts may be reached here *de novo*. See *Weinberg v. Baltimore Brick Co.*, Del. Supr., 112 A.2d 517, 518 (1955).

B. The evidence refutes plaintiffs' claim that Warner aided and abetted the Time defendants' alleged breaches of fiduciary duty

Tacitly conceding the frivolous nature of their claims, plaintiffs devote not one word on appeal to support their claims that Warner is liable as an aider and abettor. Not only have plaintiffs failed to meet any of the well-established elements of an aiding and abetting claim, see Greenfield v. Tele-Communications, Inc., Del. Ch., C.A. No. 9814, Allen, C. (May 10, 1989); but the Chancellor's findings (a) that the Time board was not engaged in any breach of fiduciary duty; and (b) that both the March 3 and June 16 transactions were the product of arm's-length negotiations precludes the conclusion that Warner's contract rights may be abrogated here.

Specifically, the Court found that "[t]here is nothing in the large record that has been created . . . that would support a charge that the March 3 agreement was other than an arm's-length negotiated agreement between two parties seeking individual advantage through mutual action" (Op. at 21). Similarly, the Court below found that: "The revamped transaction was negotiated at arm's length" (Op. at 38).

Furthermore, the facts that were known to the Warner directors all indicated that the Time directors were fulfilling their fiduciary duties. Warner's directors believed -- and had every reason to believe -- that the Time directors, an overwhelmingly independent board, acted entirely properly and in an informed manner in approving the transaction (BB22-24). Paramount made no attempt below to argue that the $70 price offered by Time was improvident in any way and, indeed, Paramount's own investment banker testified that the $70 price falls within the range of fairness (see BB943). Paramount's banker also testified that, in his view, the revised transaction was preferable for Time shareholders to the original transaction (BB946-49). The Warner directors understood that Time's board had devoted substantial time back in March to consideration of the original merger transaction; that Time's board had met on both June 15 and 16 to consider in detail Paramount's offer and the revised merger proposal; and that Time's board was being advised by experienced and sophisticated law firms and investment bankers (who were rendering opinions on the fairness of the revised merger from Time's perspective and on the inadequacy of Paramount's offer) (BB22-24). The Warner directors knew that the revised merger transaction which resulted from these negotiations was highly desirable from Time's perspective (as well as Warner's); and that a cash acquisition of Warner had in fact been Time's first choice and was even more desirable from Time's perspective than the original transaction (A484-91, 1924-25, 1931, 1938-39; BB865, 882, 890, 905-06). There was absolutely no indication to Warner's directors that the Time directors were breaching their fiduciary duties by agreeing to proceed with the long-planned transaction (BB20-24).

III. PLAINTIFFS HAVE NOT ESTABLISHED ENTITLEMENT TO INJUNCTIVE RELIEF

A. Standard and scope of review

Although the Chancellor did not find it necessary to reach the issues of irreparable harm and balance of equities, certain findings made by the Chancellor with respect to the issue of probability of success on the merits are germane to irreparable injury and the balance of the equities. These findings are factual in nature and accordingly are governed by the clear error standard. *See* Argument I.A. above. However, the legal conclusions which flow from those facts may be reached here *de novo*. *See Weinberg* v. *Baltimore Brick Co.*, Del. Supr., 112 A.2d 517, 518 (1955).

B. Plaintiffs have not established imminent irreparable harm

Plaintiffs claim that irreparable injury will result if the lower court's opinion is upheld because Paramount will lose its preferred method of acquiring Time and Time shareholders will lose an opportunity to tender their shares at a premium. In the face of the factual record below, however, plaintiffs are reduced to *ipse dixit* to support their unsupportable claims of harm.

The record is devoid of any evidence that the completion of the Time tender offer for Warner would make it impossible for Paramount (or anyone else) to acquire Time. The Waters Affidavit (A1504-11) -- the only evidence submitted below by plaintiffs on this point and then only upon *reply* --

does not support plaintiffs' preclusion argument. Based upon unfounded assumptions, Waters reasons to incorrect conclusions. That Waters' assumptions (and his conclusions) are wrong is demonstrated beyond peradventure in the Seegal and Senie Affidavits. Moreover, the Waters Affidavit is totally undercut by the concession of Paramount's Chief Executive Officer Davis that consummation of the Time-Warner transaction would not necessarily preclude a Paramount bid for the combined company and by the admission to the same effect made by Paramount's counsel in open court (BB164, 464-66). In finding that the Time tender for Warner did not preclude an offer for the combined company (Op. 76), the Chancellor necessarily rejected the Waters Affidavit.* In light of the foregoing, Paramount's argument that: "There is not a shred of evidence that such an offer [all cash] would be possible for a merged Time-Warner" (Paramount Br. 48) is stunningly disingenuous and turns the ordinary allocation of burdens of proof on a motion such as this upside down.

Finally, Paramount commenced its tender offer with full knowledge of the merger agreement and thereby accepted the risk purportedly posed by the agreement's existence. <u>See</u>, <u>e.g.</u>, <u>Goodman</u> v. <u>Futrovsky</u>, Del. Supr., 213 A.2d 899, 902-03 (1965), <u>cert. denied</u>, 383 U.S. 946 (1966). Plaintiffs are not entitled to enjoin the Time tender offer to permit Paramount to

* It may be noted that footnote 11 on page 39 of the Opinion notes the opposing views of Waters and Seegal without expressly resolving the conflict.

"catch-up." This self-created harm cannot justify injunctive relief. See, e.g., FMC Corp. v. R.P. Scherer Corp., Del. Ch., C.A. No. 6889, slip op. at 11-12, Longobardi, V.C. (Aug. 6, 1982).

As to the claim that the shareholders of Time have lost the opportunity to sell their shares at a premium, the assertion is flawed in fact and law. As demonstrated above, Paramount has not ruled out a tender for the combined company, and nothing about the merger would "preclude" such an offer. (Op. at 76). And the concept that any bid for Time-Warner would have to be at a price lower than $200 per share does not withstand even superficial scrutiny. There is no claim here that Time's acquisition of Warner constitutes a waste or improvident expenditure of Time's assets. The transaction is expected to make Time more valuable, not less. The anticipation is that Time shares will trade even in the short term in the neighborhood of $150 (Op. 32) -- a price far higher than the $109-7/8 at which they traded prior to the initial announcement of Time's proposed business combination with Warner. And, in a somewhat longer range, Time Warner shares are projected to trade in a range with an upper end as high as $402 by 1993 (Op. 33). Thus, the concept that the Time Warner shareholders are doomed to be taken over at a price of under $200 is rather fanciful, to say the least (see also BB51).

The evidence shows that other entertainment companies -- including Warner itself -- that repelled hostile bids went on to achieve values for their shareholders far eclipsing the prices that would have been obtained from the takeover bid (see BB7-8 (quoted at Op. 49-50)). Moreover, the law is clear: shareholders have no legal right to receive takeover bids. Moran v. Household International, Inc., Del. Supr., 500 A.2d 1346, 1353-54 (1985).

C. Plaintiffs' claims of harm are highly speculative and not imminent

Even assuming that Paramount's offer is somehow impeded by the Time tender offer for Warner, the alleged "injury" to both Paramount and Time stockholders is highly speculative. Paramount's offer for Time is highly conditional; for example, there is no assurance that Paramount would ever obtain its financing or regulatory approvals for transfer of Time's cable systems on terms "satisfactory to it," and, as the court below found, could be viewed as a "'request' to terminate the Warner deal and to grant Paramount a free option on the company for some period . . . . " (Op. at 34). Loss of such a "request" for a "free option" is no harm cognizable on these motions. It is, therefore, entirely conjectural for anyone -- Paramount, the stockholder plaintiffs, or anyone else -- to say that there is an imminent, concrete threat of a "loss" of the Paramount offer.

D. The balance of hardships tips overwhelmingly in favor of defendants

Warner and its stockholders will be severely injured by grant of an injunction against the Time tender offer for

Warner. It is undeniable that Time is ready to close its offer at 5 p.m. on July 24 (see BB2; and see Op. at 1). Warner shareholders are to receive $7 billion upon that tender offer to be followed by another $7 billion in value upon the back end. There is no other offer currently available to Warner's shareholders nor is there any basis for concluding that another offer at the same or higher price is likely to emerge. This harm has often been the decisive factor in denying preliminary injunctive relief. See, e.g., Solash v. The Telex Corp., Del. Ch., C.A. No. 9518, Allen, C. (Jan. 19, 1988).

The grant of a preliminary injunction would also delay the integration of Time and Warner, thereby depriving both corporations of numerous benefits (BB72-74; see also BB868, 900). Further, injunctive relief at the behest of Paramount, a competitor of Warner, would disrupt Warner's business by adversely affecting the vital personal relationships between its management and its writers, artists and performers (BB75).

Preliminarily enjoining Time's offer for Warner would also result in a precipitous drop in the market price of Warner common stock, leaving it in an extremely precarious position (considering the "spotlight" on Warner) by making it vulnerable to offers below $70 per share by other interested acquirors (BB74). Reversal of the opinion of the Court of Chancery would not only nullify Warner's bargained-for contractual rights, but would leave Warner in precisely the uncertain posture its board was unwilling to assume.

Moreover, where, as here, plaintiffs failed to make _any_ showing of wrongdoing by Warner (_see_ Point II, _supra_), the consequences of an injunction interfering with Warner's rights tips the balance of hardships overwhelmingly in its favor.

*   *   *

In sum, the balance of equities weighs overwhelmingly against the grant of injunctive relief. Paramount's highly conditional offer may never be consummated; certainly it will not be consummated soon. Time and Warner, on the other hand, have agreed to an indisputably beneficial transaction at a fair price which is scheduled to go forward now.

CONCLUSION

For the foregoing reasons, the decision of the Court of Chancery should be affirmed.

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