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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.	No. 279, 1989
IN RE: TIME INCORPORTED SHAREHOLDER LITIGATION	Interlocutory Appeal From The Court Of Chancery Of The State Of Delaware In And For New Castle County C.A. No. 10866, Consolidated C.A. No. 10670 and C.A. No. 19835
LITERARY PARTNERS, L.P., et al. Plaintiffs Below-Appellants, v. TIME INCORPORATED, et al. Defendants Below-Appellees.	

ANSWERING BRIEF OF TIME APPELLEES

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NATURE OF THE PROCEEDINGS AND THE ORDER TO BE REVIEWED

These are appeals from an order of the Court of Chancery denying motions by three groups of plaintiffs -- (i) Paramount Communications, Inc. and KDS Acquisition Corp. (collectively "Paramount"), (ii) Literary Partners, L.P., Cablevision Media Partners, L.P. and A. Jerrold Perenchio (collectively "Literary Partners"), and (iii) certain other shareholder plaintiffs -- for a preliminary injunction against consummation by Time Incorporated ("Time") of its tender offer for 100,000,000 shares of common stock of Warner Communications, Inc. ("Warner").

After development of an extensive record through discovery and affidavits, and after briefing and argument, the court below denied plaintiffs' motions in a 79-page Opinion and Order entered July 14, 1989 (the "Opinion"), holding that plaintiffs were unlikely to prevail on the merits. This Court accepted plaintiffs' interlocutory appeals on an expedited basis on that same day. Paramount and the other two groups of plaintiffs each filed opening briefs (the "Paramount Brief" and the "Joint Brief," respectively) on July 17, 1989. This is the answering brief of Time and its directors.

SUMMARY OF ARGUMENT

1. The court below properly held that the Time Board could seek to maximize long-term value even at the cost of immediate value maximization. Neither Delaware law nor sound public policy requires that directors abandon long-term strategies in favor of unsolicited tender offers that may provide a higher short-term share price.

2. The Time Board's decision on March 3 to combine with Warner was "chiefly motivated by strategic business concerns," Opinion (B71), and the decision on June 16 to proceed with that combination by means of the tender offer for Warner is presumptively valid under the business judgment rule.

a. The Board, in good faith and based upon reasonable investigation, reasonably perceived the Paramount tender offer as a threat to Time corporate policy and effectiveness. Apart from the inadequacy of the offer price -- conceded by, among other things, the $219 to $248 per share valuation by Paramount's own investment banker -- the Paramount offer threatened to delay or even scuttle altogether the Time Board's long-standing plan to expand its national and international presence in a wide cross-section of media businesses through an acquisition of Warner. Paragraphs 1 and 2 of Paramount's summary of argument and Part I of the summary of argument in the Joint Brief are therefore denied.

b. The tender offer for Warner is entirely reasonable in relation to the threat posed by the Paramount offer. Effectuation of the Board's pre-existing long-term strategy by that means not only protected that corporate policy, but did so in a manner that by all accounts enhanced the value of the company, did not preclude a takeover, did not confer a controlling or even substantial equity stake on management, and did not discriminate against any particular stockholder or group of stockholders. Paragraph 3 of Paramount's summary of argument and Part II of the summary of argument in the Joint Brief are therefore denied.

3. The Time Board's March 3 decision to acquire Warner did not compel the Board to forego long-term value maximizing strategies in favor of short-term value enhancement, as would be the case had the Board determined to sell the company.

4. Plaintiffs have failed to establish a threat of irreparable harm, and the balance of hardships weighs against granting a preliminary injunction.

STATEMENT OF FACTS

A. Time's Independent Board.

Eight of the twelve members of Time's Board are "outside" directors. (Of those eight, Paramount chose to depose only four.) When the Board approved the merger agreement with Warner on March 3, the Board consisted of sixteen directors, twelve of whom were "outside" directors. In approving the transaction in March, the Board knew that four directors would step down. Three of the four directors who stepped down were solidly in favor of the deal, while the other director voted in favor of the deal because it would be profitable, but resigned because of a personal distaste for the entertainment business.[1]

The Board has acted independently throughout. Although the Board set up a special committee on March 3, consisting of Mr. Finkelstein, Mr. Kearns and Mr. Opel, to deal with issues relating to the merger as they might arise between Board meetings, the members of that committee concluded, once the Paramount offer was made, that there was no reason for it to meet because the entire Board would consider the Paramount offer. Moreover, on a number of occasions, the

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1 Opinion (B9-10 n.2); Bere (A1597, A1605); Dingman (B136-37, B142-43); Finkelstein (B183-88, B201-03); Goodrich (B942-43, B947, B951-53); Grum (B966-67, B970-72); Horner (A1582-83); Kearns (A1614-15); Luce (B376); Opel (B574-77, B580); Perkins (A1555-56); Temple (A1441, B681-82, B690-91, B694-95); Wharton (B773-75, B780-81); Levin (B293-94, B358-59, B374); McManus (B956); Munro (B417-19, B448).

outside directors met to consider the Paramount offer without any management directors present. The outside directors also considered whether they should retain separate counsel and investment bankers and decided not to. This decision was based on their conclusions that further counsel would be redundant in view of the completeness of the advice being rendered and that the Board was receiving "adequate and objective counsel."[2] Thus, the court below concluded:

> After consideration, the outside directors concluded they had no need for investment banking advice or legal counsel in addition to, or independently of, the advice that they had been receiving from those advisors who had been retained by management for the company. Given the origin and nature of the transaction, I am inclined to agree that there was no special need for an additional source of advice. I also take this occasion to note that after Paramount emerged, the investment bankers' retention agreements were amended to remove contingencies to their compensation -- giving them a flat fee not contingent upon 'who buys who.' Opinion (B32-33).[3]

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2 Finkelstein (B219-22; B242a-44); Dingman (B159-65); Luce (A1077, B388); Munro (B437-38); Opel (B578-79).

3 The shareholder plaintiffs are incorrect in arguing that there was an "obvious conflict" in the initial fee arrangement (Joint Brief at 22-23), which was negotiated when no other transaction was contemplated. Moreover, when Paramount made its offer, the fee arrangement was changed to give the financial advisors a flat fee which would be paid whether there was a transaction with Warner or Paramount or no transaction at all, an arrangement that was operative before the Board ratified it on June 16. A1868-70.

B. Time's Strategic Development.

Time has for several years evaluated its original core publishing business to determine the best long-term strategy for Time. The key conclusion of this evaluation was that Time should be a vertically integrated media and entertainment company that is able to compete in the international arena. Time's independent Board fully supported and, indeed, urged this strategy.[4]

This conclusion was based in part on "a comprehensive long-term planning document prepared by senior division level managers". Opinion (B15). Time and Warner had held discussions on "the mutual advantages of a joint venture involving at least each company's cable television franchises and perhaps HBO and Warner Brothers Studios" (Opinion (B15)), but after Time concluded that such a venture was impractical for tax and other reasons, Time began to consider an acquisition of Warner. In June and July, 1988, Mr. Munro and Mr. Nicholas sent to each member of the Time Board both the comprehensive long-term planning document and a description of Warner as a potential acquisition candidate. Mr. Munro and Mr. Nicholas

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4 See, e.g., Bere (A1598-1600); Horner (A1584-86); Luce (B380-81); Finkelstein (B197, B231); Perkins (A1557-58); Opel (B586-87); see also Opinion (B11-12); Levin (B295-96, B354-56); Munro (B452); Nicholas (B543-44); Rossoff (A1515).

thereupon met with each of the directors to discuss both the strategic vision in general and Warner in particular.[5]

At a Board meeting on July 21, 1988, the Board, which had previously received a thorough presentation on future strategy and whether Time should expand into the entertainment business on a world-wide basis, reviewed a presentation on a number of entertainment companies -- including Columbia, Disney, MCA-Universal, Paramount (then Gulf + Western), Twentieth Century Fox and Warner -- as potential vehicles to implement such a strategy. The Board endorsed that strategy and its implementation through the acquisition of Warner rather than any of the other studios. The outside directors used phrases such as "a very imaginative and fine business deal", "an extraordinary company heading into the future". One decisive factor in reaching this decision was Warner's international distribution capability. Other factors were the success of Warner's movie studio, the fact that its cable operations would meld easily with Time's, and the success of Warner's music business.[6]

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5 See, e.g., Bere (A1600-02); Wharton (B776-77); Kearns (A1615); Perkins (A1558-60); Dingman (B141, B162); Temple (B688-92); Opel (B584-85, B590-91); see also Grum (B967-68); Levin (B297-302, B322-26); Nicholas (B455-61); Aboodi (B124-25); Ross (B655-59). The memorandum to directors is B546-70.

6 Dingman (B138-40, B151a); Finkelstein (B189-93, B200, B203a); Luce (B378-79); Wharton (B777-78); Bere (A1602); Goodrich (B945); Grum (B968); Horner (A1582); Kearns (A1615-16); Perkins (A1562-63); Rossoff (A1515-17); see also Opinion (B16-17); Levin (B302-03); Munro (B442, B449-52); Nicholas (B519-20); Wasserstein (B698-99).

In giving such approval, the Board made it clear that "'corporate governance' issues must be resolved in a way that assured that Time's senior management would ultimately come to control the combined entity." Opinion (B17). The Time Board was especially concerned that any Time-Warner merger be achieved in such a way that the journalistic independence of Time be preserved. The concern was to ensure that the projected long-term benefits of an acquisition would not erode the tradition of editorial integrity from which much of Time's success flows. Opinion (B12-13).[7]

To protect its editorial integrity, Time has developed a unique structure in which the editor-in-chief of Time reports directly to the Board and not to the CEO. Time believes that there is a direct relationship between editorial independence and value for shareholders. In Mr. Munro's words, the separation is "not simply culture for culture's sake" -- Time's magazines earn more than a third of the profits earned by all U.S. magazines, and have 22% of the revenues (as opposed to 8% for the number two company). "Publishing continues to be vitally important to [Time]". Opinion (B11). Although "Time's magazine business contributes about 40% to its gross income and will contribute about 20-25% of the revenue of a merged Time-Warner", the court below con-

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7 McManus (B958-63); Bere (A1602); Finkelstein (B208-09, B235); Grum (B968-69); Goodrich (B950); Perkins (A1559-62); Luce (B377); Opel (B592-94, B597-98); Kearns (A1616); Wharton (B791-93); see also Levin (B317-20, B327); Munro (B421-23); Hill (B248-49); Horner (A1586-87).

cluded that "maintaining a Time culture -- all the outside directors except Temple agree -- was the first and central requirement." Opinion (B19). Thus, the fact that the "'Time Culture' importantly includes directors' concerns for the larger role of the enterprise in society" does not mean that the directors have "sacrifice[d] or ignore[d] their duty to seek to maximize in the long run financial returns to the corporation and its stockholders". Opinion (B20-21).[8]

The Board was also concerned that "governance provisions" be worked out in advance to ensure that the combined entity would function effectively. In particular, the Board was concerned that the period of having co-CEOs have "a finite dimension to it." Opel (B581).[9]

The Board therefore was not prepared to go ahead with a transaction until the "governance issues" were resolved. Warner's failure to agree on these issues caused the negotiations to break down in August 1988. With the assistance of Mr. Dingman, one of Time's outside directors, who met directly with Mr. Ross of Warner, talks with Warner resumed in January

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8 Munro (B422-23, B446); Nicholas (B521-22); see also Opinion (B18-19); Bere (A1601-02); Grum (B968-69); Horner (A1587); Kearns (A1616-17); Perkins (A1560-62); Opel (B592-93, B599); McManus (B962, B965); Munro (A1082-83, A1094-97, B420); Dingman (B140-41); Finkelstein (B234-35); Wharton (B779); Levin (B318-19).

9 See also Finkelstein (B193-95, B203-07); Bere (A1601-02); Goodrich (B946); Grum (B968-69); Horner (A1586-87); Kearns (A1616); McManus (B962-63); Perkins (A1559-60, A1563-64); Opel (B581); Rossoff (A1518).

1989 and Warner agreed to the terms required by the Time Board.[10]

C. The Board's Approval Of The Merger Proposal.

On March 3, 1989, Time's management and its financial advisors made extensive presentations to the Time Board regarding all aspects of the proposed acquisition. Documents relating to the merger had been distributed to the Board two days prior to the meeting and copies of the principal documents were available to the Board at the meeting. Each outside director expressed support for the transaction, even though every Board member was aware that four of the directors would not serve on the Time Warner Board.[11]

Although several members of the Time Board would have preferred in March 1989 (and in July 1988) to acquire Warner for cash, Warner would not at that time agree to such an acquisition. Instead, Warner insisted on a stock-for-stock merger.[12]

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10 Finkelstein (A785, A788, B210-12, B246); Opel (B601-04); Goodrich (B946); Grum (B968-69); Horner (A1588); McManus (B962-63); Perkins (A1563-64); Dingman (A1132-40, B152-57); see also Nicholas (B469-70, B476-79, B482-84, B513-14); Munro (B421-22, B424-25); Hill (B250); Wasserstein (A1453, B700-01); Levin (A1037, B310-18, B352-53); Ross (B660).

11 A1717-25; Finkelstein (B219, B222); Temple (B682-83); Goodrich (B945-47); Grum (B968); Wharton (B782, B784); Opel (B596-98); Perkins (A1565); Horner (A1588, A1590-91); Bere (A1599-1603); Kearns (A1615-16); Dingman (A772-73, B151-51a).

12 Opel (B614-15); Nicholas (B461-62, B536); Ross (B667-68); Levin (B365-66); Wasserstein (B713); Horner (A1590);
(Continued)

One reason that Warner wanted to do a stock-for-stock merger was to achieve pooling of interests accounting. The Time Board was advised of the benefits of pooling of interests accounting -- namely that Time's earnings would not be reduced to reflect amortization of goodwill -- and its disadvantages -- namely rules that would reduce Time's flexibility to enter into a restructuring or to repurchase shares. The Board was advised further that pooling had no effect on Time's cash flow or the market value of its assets. Although pooling was particularly important to Warner in March 1989, Time persuaded Warner that pooling would not be a condition of the transaction. The Board decided that Time would proceed with the merger even if pooling of interest accounting became unavailable.[13]

The exchange ratio for the merger was negotiated at arms'-length. Although some Time directors had initially been opposed to a premium, the Board, after receiving advice from its financial advisors, concluded that a modest premium was appropriate in light of Warner's predicted faster growth in earnings and the fact that Time would be the surviving company.[14]

Kearns (A1617-18); Goodrich (B948-49); see also Opinion (B21).

13 Finkelstein (B196, B213); Opel (B600); Dingman (B178-79); Temple (A1719, A1722, B685-86); see also Levin (B336-37); Nicholas (B467-68, B515, B536-37); Wasserstein (B705).

14 Dingman (A772-73, B144-51); Temple (B693); Opel (B605-06); see also Nicholas (B480-81, B485-99); Levin (B304-08,
(Continued)

In approving this exchange ratio, the Time Board was aware that, after the merger, former holders of Warner shares would hold about 60% of Time Warner shares. This was the result of the fact that Warner (following its recent acquisition of Lorimar) had a larger market capitalization than Time, and Time was paying a modest premium to acquire Warner. The Board did not believe that this would result in a change of control of Time.[15]

The Board was also aware that the announcement of the merger proposal would raise the possibility that someone would seek to disrupt the transaction. The Board therefore approved the Share Exchange Agreement as a mild deterrent against someone's trying to disrupt the merger agreement.[16]

B341-42); Munro (B426-28); Wasserstein (B702, B706-08); _see also_ Aboodi (B126-32).

15 Dingman (B166-67, B176); Luce (B382, B390-91); Nicholas (B500-07); Ross (B661-63); Levin (B306-09); Opel (B607-08); Wasserstein (B703-04, B709-10); Wharton (B784-85).

16 Wharton (B783, B786); Opel (B609-13); Finkelstein (A798-99, B198-99, B214-15, B239-40); Temple (A1439-40); _see also_ Nicholas (B471-73, B507, B509-10); Wasserstein (B711-14); Munro (B440-41); Hill (B252).

The Share Exchange Agreement was also intended to be an investment and a symbol that the companies had taken the first step towards completing the merger. Levin (B338-39); Nicholas (B510-11); Ross (B664-66); Bere (A1608); Goodrich (B946); Perkins (A1571).

Time also obtained, as a standby, a $5 billion credit facility to create financial flexibility to protect the Time-Warner transaction from possible disruption. The credit facility could have been used for any number of possible transactions, including the purchase of Warner shares for cash or the purchase of Time shares for cash. Hill (B251); Nicholas (B474-75, B512). Several -- but not
(Continued)

The Board also reviewed with great care the employment contracts approved on March 3. The Board reviewed the contracts of Mr. Munro and Mr. Nicholas. Mr. Munro and Mr. Nicholas made it clear that they did not expect their compensation to be increased dramatically as a result of the level of Mr. Ross' compensation and, indeed, rejected a suggestion by Warner that their compensation be increased. Their compensation was comparable to their current agreements, which were extended to track the governance provisions. The Board had a full discussion and unanimously approved the contracts as reasonable. In Mr. Dingman's words, they were "fair and reasonable", "responsible" agreements.[17]

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all -- of the banks agreed as part of that financing that they would not finance any activity against Time, which was ancillary to arranging the line of credit, but also made it easier for the banks not to be in a conflict situation. Levin (B372-73); see also Perkins (A1570). There are no such provisions in the current financing to Time. Plaintiffs do not contend that Time has "dried up" the money in the world-wide banking system or indeed that the arrangements had any effect on Paramount. See also Opinion (B27).

Plaintiffs also refer rhetorically to a "black-out provision." Such a provision is "a logical tactic to take if you want the deal to go forward." Finkelstein (B217-18); see also Goodrich (B950); Perkins (A1570-71).

17 Dingman (B158-59, B168-69, B179); Temple (B146-48); Bere (A1604-05); Horner (A1592-93); Kearns (A1618); Opel (B595-96); see also Perkins (A1568).

> To summarize:
>
> On March 3, 1989, the boards of both companies authorized entering into the merger agreement . . . . Both corporations have a majority of outside directors. Both approved the transaction after receiving investment banking and legal advice. There were no dissenting votes. There is nothing in the large record . . . that would support a charge that the March 3 agreement was other than an arms'-length negotiated agreement between the parties seeking individual advantage through mutual action.

Opinion (B24).

D. <u>Public Reaction To The Merger Proposal.</u>

On March 9, 1989, Mr. Richard E. Snyder, Chairman and Chief Executive Officer of Simon & Schuster, a principal Paramount subsidiary, wrote to Mr. Nicholas:

> My congratulations, coupled with my jealousy, for making the greatest deal ever imaginable! Fear and trembling strikes when we view your colossus but I think we will muddle our way through. It's a great concept, a perfect company and my congratulations to all your colleagues as well.

Mr. Snyder was not alone. Market analysts and professional investors alike recognized the tremendous benefits of the acquisition of Warner and that the ability of a combined Time-Warner to compete globally in the entertainment/media business would lead to long-term value for shareholders. For example, Morgan Stanley told the Paramount Board: "Commercial logic of [the Time-Warner] merger . . . generally garnered favorable market-place support." Similarly, analysts with Drexel Burnham Lambert, Inc., and Wertheim Schroder & Co. wrote favorable reports. Even more important is the reaction of Gordon Crawford, a director of the Capital Group Inc., which manages accounts owning 7% of the common shares of Time, 7% of the common shares of Warner, and 5% of the common shares of Paramount. In his view, Time-Warner "will be the greatest media and entertainment company in the world."[18]

E. Paramount's Offer.

On June 7, 1989, Paramount announced a tender offer for Time at $175 per share. Paramount understood that the offer had to be made in time to disrupt the shareholder vote scheduled for June 23. Paramount had been advised that June 23 was a "critical day" and that the Time shareholders would approve the transaction on that day. Paramount expected that the consequence of announcing a tender offer for Time would be either that the vote would be "adjourned, postponed or canceled" or that the shareholders would vote against the transaction. "While the step had been under consideration from mid-March, the announcement was timed to await the distribution of proxy materials for the June 23 meeting so that Time would be publicly committed to a shareholder vote on the merger agreement."[19]

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18 B771; B876-903; Waters (B745, B751-52); Crawford (B112-13, B118, B122); Opinion (B39 n.9); see also Davis (B795); Waters (B744).

19 Hope (B147-48); Pattison (B646); Waters (B751-52); Opinion (B28); Hope (B282a); Pattison (B646a).

Paramount's offer was subject to numerous conditions. These included a condition that Paramount be satisfied in its sole discretion that all material approvals, consents and franchise transfers relating to Time's programming and cable television business had been obtained in terms satisfactory to Paramount. The Paramount Board was advised that it would take at least several months for Paramount to satisfy this condition.[20]

F. The Independent Board's Rejection Of Paramount's Offer And Reaffirmance Of The Strategy To Acquire Warner.

The Time Board met on June 8, June 11, June 15 and June 16 to discuss Paramount's $175 offer. The meetings were intensive -- the minutes consist of over 100 pages. The Board considered at these meetings whether it was appropriate to sell Time and concluded that it was not. The Board also considered, among other things, the acquisition of part of or all the business of Paramount, the acquisition of part of or all the business of certain other companies, a financial restructuring or recapitalization, and a material change in the present capitalization or dividend policy.[21] The Board concluded that a Warner transaction was more favorable than a Paramount

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20 Opinion (B28-29); Pattison (B643-45); Oresman (B623); Davis (B796-98, B799-805, B809); B288; B134; Waters (B747-49, B750).

21 A489-90; A1772; A1778; A1781; A1812-13; A1820; A1861; A1864.

transaction.[22] And the Board concluded that Paramount's offer was "grossly inadequate", and that until such time as the Board decided to sell the Company, there was no need to speak to Paramount, a "low-ball" bidder.[23]

1. The Inadequacy Of The $175 Offer.

Time's financial advisors advised the Board that, if the Board wanted to sell Time, the advisors could run an auction that would achieve a materially higher price than Paramount was offering. They advised the Board that on a pre-tax segment analysis, which in their view is the most relevant valuation technique for a sale of the company, Time's value is between $233 and $274 per share, and that the actual price achieved would likely be in the middle to the upper part of that range, i.e., that the price would likely be greater than $250 per share.[24]

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22 Bere (A1609-10); Horner (A1594-96); Kearns (A1620-21); A1766-86; A1787-1846; see also Finkelstein (B225-26); Levin (A1042-43, B360, B363, B371a-b); Munro (B443, B449-52); Nicholas (B519-22, B534-35, B540-42); Opel (A1306); Wasserstein (B715-18, B735-37).

23 Finkelstein (A795-97); Opel (A1306); Munro (B436); Dingman (A775, B177).

24 A1816-18; Wasserstein (B729-31, B736, B738-42); Rossoff (A1529-30). Plaintiffs argued below that this advice "is quite inconsistent with the advice that the exchange ratio (.465) in the merger transaction was fair and that the $70 per share offer to Warner was fair, which together imply about $150 per share value for Time." Opinion (B33 n.7). They repeat that argument here. See Joint Brief at 9, 10, 13. They are wrong for the reason given by the court below in rejecting their argument:

> This argument . . . rests upon the assumption that the ratio between the value of Time in a control (takeover) market and the

(Continued)

Plaintiffs argue that the March analysis and the June valuations are inconsistent. Paramount Brief at 4; Joint Brief at 9 n.6, 10 n.7, 13. Plaintiffs are incorrect. The June analysis considered a change in control market, while the earlier analysis was for a different purpose and, in addition, more recent projections and changes in the market for entertainment companies justify the difference. The purpose of the March analysis was not to establish the value at which Time could be sold, but to establish a consistent relationship between the asset values of the two companies for purposes of opining on the fairness of the exchange ratio. In contrast, the June analysis was specifically intended to identify values on a detailed basis to estimate what someone would be prepared to pay for each of Time's assets if those assets were sold. In performing the June analysis, the financial advisors, including a team of specialists, reviewed Time's major businesses, asset by asset, to determine what each asset is worth in the market. The financial advisors estimated values based on multiples of expected 1989 financial measures. The financial advisors used updated multiples to reflect entertainment and cable company transactions that had been announced since

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> value of Time shares in a normal trading market . . . would be the same as the ratio between Warner's control market value ($70) and the trading value of Warner shares prior to the original merger agreement. There is no reason why this need be the case.

Opinion (B33-34 n.7).

March, including, for example, the sale of the National Enquirer, the News Corp. Travel Magazines and Centel Cable Corp. And the June valuations took into account more recent projections prepared by Time.[25]

In preparing the June figures, the financial advisors were trying to be conservative, and some of the directors questioned whether the figures were too conservative.[26] The financial advisors stated that additional factors -- such as "ego value", the unique nature of Time's properties; synergy/cost savings of a combination; the rapidly expanding markets in which Time operates; and the potential for inter-

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25 Levin (B344-45); Hill (B253-66, B271); Rossoff (A1523-24); A1773-75; A1796.

Plaintiffs' analysis of the relative difference between the March and June analyses of Time and Warner (Joint Brief at 13) is incorrect. Time's advisors estimated Warner's reference valuation range as $11.8 billion to $13.4 billion in March and its pre-tax segment valuation range as $13.6 billion to $15.3 billion in June. Thus, the difference between these ranges is 14-15%. Plaintiffs' statement that the <u>per share</u> value of Warner "increased only 5.8%-6.2%" (Joint Brief at 13) is misleading because it is based on their incorrect use of different numbers of shares in their calculations. <u>See</u> B268; B275; B277; Rinaldini (B649-51).

26 The conservative nature of the valuations used by Time's financial advisors is illustrated by the fact that in many instances Paramount's advisors used <u>higher</u> assumptions. For example, Time's financial advisors estimated the value of Time's cable operations using a per subscriber value of $2,200 to $2,500. B276a. Morgan Stanley performed a valuation of the same cable operations using higher per subscriber values of $2,300 to $2,600. B768.

national expansion -- could contribute to the realization of higher values.[27]

The Board also took into account the delay that will result from the conditions in Paramount's offer. Because obtaining transfer approval from local franchising authorities can be very time-consuming -- and may take between six months and a year -- the Board was advised that it was appropriate to discount the face amount of the price offered.[28]

The Board's conclusion was, in Mr. Finkelstein's words, that "the Paramount offer was just wildly insufficient" -- it was "widely, widely, widely short of . . . the value to be in [the] shareholder interest".[29]

2. The Superiority Of The Acquisition Of Warner.

At the June 8 meeting, the Board was advised that Time now had an opportunity to acquire Warner for cash, an opportunity that it had never had before. After receiving detailed presentations at several meetings, the Board con-

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27 Wasserstein (B729-31, B739-41); Finkelstein (B223, B245); Opel (B616); see also Bere (A1609, A1612); Horner (A1593-94); A1027; A1798-1800; A1816-18.

28 A1791-92; Munro (B445). Paramount has claimed that Time's concern over the delay due to the regulatory process is self-created. Not so. Time's 82% owned cable subsidiary ATC has actively petitioned local authorities, but only with respect to the right of those authorities to insist on exercising their power and duty to scrutinize in advance a proposed change of control of a franchise. Time has never urged any authority to delay considering whether to approve such a change. B941j-m.

29 Finkelstein (B223, B245).

cluded, in Mr. Finkelstein's words, that if a revised deal could be negotiated with Warner, that would lead "to a much higher shareholder value." The Board concluded, after reviewing a possible acquisition of Paramount, that the Time-Warner "fit" of businesses was in the best interest of Time and the Paramount offer did not alter that conclusion. The key elements were the strength of Warner's international distribution capability, as well as Warner's music business. By comparison, the fit with Paramount was inferior -- Paramount lacked an international distribution capability and has no music business.[30]

Time and Warner negotiated a price of $70 per share. Time's financial advisors opined that such a price is fair. Morgan Stanley, Paramount's advisor, agrees with that opinion. The Board concluded that such a purchase for cash was at least as favorable to Time shareholders as the initial deal. Paramount and Morgan Stanley agree.[31]

Warner insisted on a firm commitment. The Warner Board would not agree to give Time, in effect, an option to buy Warner. The Time Board considered whether Warner's insis-

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30 Bere (A1616, A1780-81); Finkelstein (A795-96, B225-26, B229); Wasserstein (B717-18, B736-37); Nicholas (B516-22, B530-33); Levin (B356-57, B371a-c); Munro (B435, B444, B447, B449-52); Kearns (A1620-21); Horner (A1594-95); Perkins (A1572-74, A1580).

31 Rossoff (A1524-25); Nicholas (B525-26, B534-37); Munro (B429-32); Levin (B342-43, B364-65); Finkelstein (B230, B232-33); Wasserstein (B723-24, B732-33); Bere (A1611); Kearns (A1620-21); Goodrich (B948-49); Perkins (A1574-77); Hope (B280a-b); Waters (B746, B761).

tence was reasonable from Time's point of view and concluded that it was. Although there is no financing contingency, the Board considered the risks of not including such a contingency and concluded that they were minimal. The Board was correct. The financing was quickly put in place. And there is no contingency with respect to regulatory approval because the Board was confident that the approvals -- which relate only to Warner's franchises and were largely already secured -- would be in place by the time of the closing or be immaterial.[32]

The Board considered whether the acquisition for cash would have an adverse effect on Time. The Board concluded that the debt service is manageable. The Board also considered the effect that the goodwill amortization will have on reported earnings. The Board understood further that, as a result of interest charges and goodwill amortization, Time would record a loss in reported earnings for two years, but that there will always be substantial positive cash flow and that this cash flow increases at a substantial rate.[33]

Time's investment bankers advised the Board that the financial community should value Time based on a multiple of cash flow rather than a multiple of earnings. Paramount agrees. Indeed, Morgan Stanley advised the Paramount Board

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32 Britt (B955); Levin (B370-71); Finkelstein (B236-38); Perkins (A1575); Nicholas (B527-28); Bere (A1611); Perkins (A1575-76).

33 Luce (B386, B389); Dingman (B170-71); Munro (B433-34, B439); Finkelstein (B242); Bere (A1610-11); Kearns (A1621); Perkins (A1574-76); A1833.

that the market will value media companies at a multiple of cash flow.[34] The financial advisors predicted, under one scenario, a trading value range of $288-402 for 1993.[35]

The Board therefore concluded that the "Time-Warner transaction is clearly a superior transaction", "quite superior" to a Time-Paramount transaction, "the best way that Time could go to increase its shareholder value" -- "the best acquisition we could make would be Warner. By quite a wide margin . . . . [E]ssentially -- it's a very unique company."[36]

3. The Inadequacy Of The $200 Offer.

Time's financial advisors informed the Board that Paramount might raise its offer from $175 because that price was very low. Indeed, at the June 16 meeting, the Board was

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34 Bere (A1606-07); B932; Finkelstein (B227-28); Dingman (B172-74); B287; Waters (B759-60).

The shareholder plaintiffs seek to rely on the testimony of Paramount's litigation expert to show that "Time-Warner will trade in a range of between $90 and $140 per share". Joint Brief at 17. That reliance is misplaced. In the first place, Mr. Phillips' methodology is incorrect due to his use of "comparable" companies having considerably higher leverage than Time Warner. Rossoff (A1525-29). In the second place, Mr. Phillips should have used the same assumptions that Morgan Stanley used for the Paramount Board. Those assumptions -- including a multiple of between 11 and 12 -- are largely the same as those used by Time's advisors. B290-91; B625; B770a; B273-76; contrast Phillips (A377-83).

35 A1477. Because of the poor legibility of the copy of the analysis attached to the Nagy reply affidavit, the opinion below recites this range as $208-402. Opinion (B36).

36 Finkelstein (B231-33, B241); Opel (B582-83).

advised that Paramount might raise its offer to $200. After Paramount did so, the Board was advised, based on the prior analysis, that the offer was inadequate.[37]

Paramount's own investment bankers consider Time to be worth substantially more than $200 per share. Thus, Morgan Stanley, based on its knowledge of transactions in the marketplace, concluded that Time was worth between $218.83 and $248.36 per share. Moreover, Morgan Stanley calculated a 1989 "value per share" for Time of $216.91, which increases to $250 per share if a higher assumption for cable franchise values is used. Indeed, Morgan Stanley advised the Paramount Board that, even at an acquisition price for Time of $200 per share, the trading price of Paramount's shares will increase much more rapidly if Paramount acquires Time than if Paramount makes no acquisition. In fact, the projections show an increase -- in the acquisition case -- of about 30% per year, so that Morgan Stanley predicts that Paramount's share price five years from now will be, with an acquisition of Time, twice the level it would be without an acquisition. In addition, Morgan Stanley presented to the Paramount Board estimates of Time's value by ten analysts. Of these, seven were above $200 per share.[38] For example, Morgan Stanley noted

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37 A1842-43; A1859; Wasserstein (B725-28, B738-42).

38 B285; A1030; B625; B625a; B764a; B765; B767; Waters (B753-55, B757-58, B762-63). The shareholder plaintiffs argue that the $200 price is "well with the ranges of fairness reflected in a substantial array of investment banking opinions". Joint Brief at 2; see also id. at 16. Understandably, Paramount does not make this argument. The (Continued)

that Paul Kagan Associates concluded that $240 per share was the break-up value for Time; that Merrill Lynch had concluded that $231 per share was the appropriate price; and that First Boston reported a value of at least $230 per share.

4. Stockholder Vote.

The merger proposal was subject to approval by Time's shareholders because of New York Stock Exchange regulations relating to the issuance of common shares in the transaction as structured in accordance with Warner's demands. Although Delaware law required approval by Warner shareholders because "its stock [would have been] converted into something else in the merger", Delaware law "does not require a vote of the shareholders of Time (since its stock will remain unaffected by the merger and the issuance of additional shares did not require amendment of Time's certificate of incorporation)." Opinion (B25); see also 8 Del. C. § 251. The tender offer is not subject to shareholder approval. The advantage of the tender offer is the speed with which the transaction can be consummated. By way of contrast, it would have been difficult after June 7 to seek approval for the original proposal. And

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shareholder plaintiffs, however, have not accurately described this "array". Their error with respect to Time's financial advisors is discussed above (pp. 17-19); they have cited the decided minority of analysts' views collected by Morgan Stanley (see B289a; B625a); and the March Salomon Brothers report they cite shows valuations of Time much higher than $180 per share, and in any event that report uses valuation multiples below those used by Morgan Stanley. See A297-99; B767. We note further that the shareholder plaintiffs suggest that Warner could economically acquire Time at over $228 per share. Joint Brief at 35-36.

the rapid and continuing turnover of Time Stock caused by the Paramount offer made it difficult to obtain the required majority of affirmative votes.[39]

5. Public Reaction To The Tender Offer.

Analysts and investors have once more recognized the benefits of the Time acquisition of Warner. Gordon Crawford, the investment manager for one of the largest investors in Time, Warner and Paramount stated:

> We're long-term investors, . . . Time-Warner as it was originally proposed was going to be an incredible company with a great long-term outlook, and I'd just as soon continue to be invested in both companies. . . . [Many in the investment community] want to see instant gratification in every stock, and that's not always in the best long-term interests of all the shareholders, or of the economy.

Similarly, among others, analysts at Smith Barney and Wertheim Schroder have expressed approval for the Time tender offer.[40]

6. The Viability Of A Takeover Of Time Warner.

Time's acquisition of Warner does not prevent anyone from making a bid for both companies. That is the testimony

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39 Opinion (B25); Luce (B384); Levin (A1041, B362, B366-69); Nicholas (B514, B538-39, B541-42); Dingman (B175, B180-81); Wasserstein (B719-23); Opel (B617-19). The court below did not reach the issue of "confusion." Opinion (B40).

40 B121; Opinion (B39 n.9, 52-53); B904-37.

of Time's directors and Time's advisors.[41]

That is also the conclusion of Paramount's executives. Thus, Paramount's chairman testified that Paramount has as yet made "no determination" as to whether Paramount will make an offer for Time Warner -- he will decide "from a business judgment standpoint" when they "get to that point," "we will evaluate -- should that happen, I'm sure we will evaluate it . . . . There's been no determination." Paramount believes that size provides little protection against a takeover and that the leverage of the target is not a significant deterrent, so that it believes that Time Warner may be more vulnerable to a takeover than Time is alone.[42]

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41 Levin (A1040); Nicholas (B528); Seegal (B940-41); Bere (A1612); Goodrich (B951); Perkins (A1574).

42 Davis (B808, B811-14); Hope (B281-82). Paramount has attempted to adduce proof (and to impeach its own CEO) that the Time offer would effectively preclude a takeover of Time. Paramount Brief at 47. From a term sheet relating to the financing of the Time offer, which contemplates that 25% of the total acquisition price of Warner will be in equity, Paramount's investment banker inferred that the continuing enterprise "will be 'tapped out' in terms of debt capacity." Waters (A1508). That inference is simply speculation, and it is erroneous as well. Time's principal lenders were highly confident that $14 billion could be raised, enough to fund the cash purchase of all of Warner's shares at $70 per share. Senie (B828, B830-41). The 25% equity term on which Mr. Waters relied simply enabled lenders to review and approve the tender offer financing more promptly. Senie (B830). In no way did the lenders assert that they would never agree to lend more money; to the contrary, the fact that the tender offer financing was oversubscribed by a factor of three strongly suggests otherwise. Senie (B830-31). In fact, according to Shearson, one of Time's financial advisors, "there are a significant number of parties that would be able to finance an acquisition of the combined Time-Warner." Seegal (B940).

Thus, the court below concluded that the offer for Warner:

> . . . does not legally preclude the successful prosecution of a hostile tender offer. And while effectuation of the Warner merger may practically impact the likelihood of a successful takeover of the merged company, it is not established in this record that that is foreclosed as a practical matter. Recent experience suggests it may be otherwise. Opinion (B79).

ARGUMENT

I. THE COURT BELOW PROPERLY ARTICULATED THE FIDUCIARY DUTIES AND AUTHORITY OF THE BOARD OF DIRECTORS.

A. Standard And Scope Of Review.

As stated in the Opinion, "Delaware law does recognize that directors, when acting deliberately, in an informed way, and in good faith pursuit of corporate interests, may follow a course designed to achieve long-term value even at the cost of immediate value maximization." Opinion (B53-54). This articulation of the fiduciary duties of directors of a Delaware corporation will be set aside only if it is erroneous as a matter of law. Rohner v. Niemann, Del. Supr., 380 A.2d 549, 552 (1977).

B. Merits.

It is the essence of plaintiffs' claim that in electing on June 16 to proceed with the Warner acquisition and not pursue Paramount's offer, the Time Board chose the alternative of inferior value because Time shares might trade below $175 in the near future. (Paramount Brief at 28, 33, 37-38, 41, 44; Joint Brief at 2, 17, 19, 37, 46).

The court below, however, chose not to measure the conduct of Time's Board by exclusive reference to the current or short-term market price of Time's shares: it "is far from irrational and certainly not suspect for directors to believe that a likely immediate market valuation of the Time-Warner merger will undervalue the stock." Opinion (B52).

As a matter of law, that conclusion is unassailable. Delaware law has long recognized that intrinsic share value is by no means inexorably equal to its value as reflected in market price. In 1934, the Court of Chancery wrote:

> When it is said that the appraisal which the market puts upon the value of the stock of an active corporation as evidenced by its daily quotations, is an accurate, fair reflection of its intrinsic value, no more than a moment's reflection is needed to refute it. There are too many accidental circumstances entering into the making of market prices to admit them as sure and exclusive reflectors of fair value. The experience of recent years is enough to convince the most casual observer that the market in its appraisal of values must have been woefully wrong in its estimates at one time or another within the interval of a space of time so brief that fundamental conditions could not possibly have become so altered as to affect true worth.

Chicago Corp. v. Munds, Del. Ch., 172 A. 452, 455 (1934). Fifty years later, this Court reaffirmed that view, finding even a premium to market an insufficient basis, standing alone, for director assessment of the fairness of a merger price. Smith v. Van Gorkom, Del. Supr., 488 A.2d 858, 875-76 (1985).

The appropriateness -- indeed, acute desirability -- of encouraging director attention to long-term value, and not requiring director conduct to be dictated by short term swings in market price, is also borne out in fact. As this Court has noted, there is substantial evidence that director resistance to hostile bids, even at a premium over market price, tends in the long run to enhance market prices. Unocal Corp. v. Mesa

<u>Petroleum Co.</u>, Del. Supr., 493 A.2d 946, 956 n.11 (1985). And with respect to the entertainment industry in particular, the court below noted recent instances in which even the market prices of shares reached heights dwarfing hostile bid prices within just five years of the bids. Opinion (B52-53) (citing Crawford (B113-14)). In 1984, the market price of Warner stock was $10-12 per share; Warner shareholders would not be in a position to receive $70 per share today if Steven Ross and his fellow directors had accepted a bid by Rupert Murdoch or simply shopped around to find the best marginally higher bid then available.

Perhaps anticipating such situations, this Court has recognized that "the ultimate loss would, of course, be on the shareholders" if directors were required to accept a hostile bid at a premium over the market price, or even to negotiate with the bidder. <u>Pogostin v. Rice</u>, Del. Supr., 480 A.2d 619, 627 (1984). This Court has further recognized, repeatedly, that "a board of directors is not a passive instrumentality," even in matters of fundamental corporate change, and that directors are empowered and indeed obligated to take affirmative corporate action to protect stockholder interests in the face of a tender offer even at a premium to market. <u>Unocal Corp. v. Mesa Petroleum Co.</u>, 493 A.2d at 954; <u>Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.</u>, Del. Supr., 506 A.2d 173, 179-81 (1986); <u>Ivanhoe Partners v. Newmont Mining Corp.</u>, Del. Supr., 535 A.2d 1334, 1341, 1345 (1987), all citing 8 <u>Del</u>. <u>C</u>. § 141(a). Entirely consistent with this principle was the conclusion of the court below that "directors, not shareholders, are charged with the duty to manage the firm," and that "the corporation law does not operate on the theory that directors, in exercising their powers to manage the firm, are obligated to follow the wishes of a majority of shares." Opinion (B80-81).

From that solid foundation, the opinion below appropriately rejected each of plaintiffs' various legal theories, as we show below.[43]

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43 Plaintiffs' manipulation/disenfranchisement theory, fully addressed by the court below (Opinion (B67-71)), appears on appeal only in vestigial form in a footnote in the Paramount Brief (at 40 n.17) and is therefore not separately addressed in this brief.

II. THE TIME BOARD REASONABLY PERCEIVED THE PARAMOUNT OFFER AS A THREAT TO CORPORATE POLICY AND EFFECTIVENESS, AND THE TENDER OFFER FOR WARNER IS REASONABLE IN RELATION TO THAT THREAT.

A. Standard and Scope of Review.

On an interlocutory appeal from the denial of a preliminary injunction, the Court may reverse factual findings of the Court below only if they are clearly wrong, and justice requires the Court to do so. If the findings of the Court below are sufficiently supported by the record and are the product of an orderly and logical deductive process, the Court will accept them even though independently the Court might have reached another conclusion. Mills Acquisition Co. v. Macmillan, Inc., Del. Supr., [Current] Fed. Sec. L. Rep. (CCH) ¶ 94,401, at 92,595 (May 8, 1989); Ivanhoe Partners v. Newmont Mining Corp., 535 A.2d at 1340-41.

B. Merits.

Although Paramount asserts that the "sole goal" of Time's outside directors "was to preserve management" (Paramount Brief at 29; see also Joint Brief at 7), the court below found otherwise:

- "[T]he original Time-Warner merger agreement was, or appears at this stage to have been, chiefly motivated by strategic business concerns." Opinion (B71).

- "While the record reflects the directors' concerns for the larger role of the enterprise in society, there is insufficient basis to suppose at this juncture that such concerns have caused the directors to sacrifice or ignore their duty to seek to maximize in the long run financial returns to the corporation and its stockholders." Opinion (B20).
- "[T]here is no persuasive evidence that the board of Time has a corrupt or venal motivation in electing to continue with its long-term plan . . . ." Opinion (B79-80).

Accordingly, the court below scrutinized the Board's actions on June 16 under the business judgment rule as expressed in Unocal, with the threshold requirements of proof that case articulates. 493 A.2d at 954. As shown below, the results of that scrutiny are fully supported in the record and unquestionably the product of an orderly and logical deductive process.

1. The Time Board Reasonably Perceived The Paramount Offer As A Threat To Time's Long-Term Corporate Policy and Effectiveness.

A board meets its burden under Unocal of showing "reasonable grounds" for believing that there existed a threat to corporate policy and effectiveness by demonstrating its "good faith and reasonable investigation." Unocal, 493 A.2d at 955. Proof of good faith and reasonable investigation is materially enhanced where a majority of the board comprises outside independent directors. Unocal, 493 A.2d at 955; Ivanhoe Partners, 535 A.2d at 1343; Grobow v. Perot, Del. Supr., 539 A.2d 180, 190 (1988); Moran v. Household International, Inc., Del. Supr., 500 A.2d 1346, 1356 (1985). That enhancement is particularly forceful here, where plaintiffs chose to depose only four of the eight outside directors. Moreover, evidence that such a board acted upon advice of investment bankers and legal counsel, as Time's Board did, "constitute[s] a prima facie showing of good faith and reasonable investigation." Polk v. Good, Del. Supr., 507 A.2d 531, 537 (1986).

Nor can there be any doubt that the Time Board was entitled to consider a threat to its "long-term strategic plans." Indeed, noting that "a refusal to entertain offers may comport with a valid exercise of business judgment," this Court in Mills identified a series of criteria by which the existence of a threat to corporate policy and effectiveness could be measured: "the nature and timing of the offer; its legality, feasibility and effect on the corporation and the stockholders; the company's long-term strategic plans; and any special factors bearing on stockholder and public interests." Fed. Sec. L. Rep. ¶ 94,401 at 92,599-92,600 n.35 (emphasis added). Nothing in Mills suggests that these criteria -- particularly "long-term strategic plans" -- become inoperative in the face of an all-cash, all-shares tender offer.

To be sure, directors may not blindly invoke long-term goals to justify their conduct; identifying a threat to such goals is unavailing if there is a showing that such goals are mere post hoc fabrications. See Crouse-Hinds Co. v. InterNorth, Inc., 634 F.2d 690, 701-03 (2d Cir. 1980). In this case, however, no such showing has been made. As the court below found, "the achievement of the long-term strategic plan of the Time-Warner consolidation is plainly a most important corporate policy; . . . [it] has, in a most concrete way, its origin in non-defensive, bona fide business considerations . . . . [T]he board . . . continues to manage the corporation for long-term profit pursuant to a pre-existing business plan that itself is not primarily a control device or scheme . . . ." Opinion (B77-78).

Thus, the Board's long-term plans are bona fide, and the threat posed by the Paramount offer to their fulfillment was reasonably viewed by the Board as a basis for defensive action. That view, moreover, was bolstered by the Board's perception of the inadequacy of the Paramount offer, a perception based upon what the court below found to be "competent advice." Opinion (B48); see also Opinion (B32-35). Plaintiffs failed to rebut the resulting prima facie showing of reasonable investigation, and they were scarcely in a position to do so: Paramount's own investment bankers had valued Time in the range of $219 to $248 per share. See B767.

In sum, the Time Board reasonably perceived that Paramount's offer price was substantially below Time's intrinsic value; that the original merger agreement was likely to enhance that value; that proceeding with the revised agreement would also enhance that value;[44] and, therefore, that the Board should effectuate the Warner acquisition. Thus, as the court below noted, the question becomes whether the Board's actions to accomplish the acquisition were reasonable in relation to the threat posed by the Paramount offer.

2. The Determination To Continue With The Acquisition Of Warner Is A Reasonable Limited Response To The Threat Posed By The Paramount Offer.

The court below found the revised merger agreement with Warner "reasonable in relation to the specific threat posed to the Warner merger by the Paramount offer." Opinion (B76). That finding is fully supported in the record and an entirely appropriate conclusion to draw. Paramount incorrectly argues that the court applied an erroneous "subjective" standard in this regard and failed to examine "the objective effect of the proposed merger" (Paramount Brief at 30-32); to the contrary, as discussed below, the court specifically considered -- and rejected -- Paramount's claims as to the effect of the Warner acquisition.

In evaluating the reasonableness of the Time Board's action under Unocal, this Court should examine the "measures employed and the results achieved" by such measures. Ivanhoe Partners, 535 A.2d at 1342-43. Here, just as in Ivanhoe Part-

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44 Paramount's investment banker so concedes. Waters (B761).

ners, the revised merger agreement approved on June 16 achieved "two essential objectives": it had the direct effect of "insuring the continued interest of the public shareholders in the independent control and prosperity of [Time]," and a possible incidental effect with respect to the inadequate Paramount offer. 535 A.2d at 1345. No one disputes that a combination of Time with a major entertainment company is a highly desirable long-term strategy; what the revised merger agreement achieves is to ensure that Time's stockholders, not Paramount's, will reap the benefits of that strategy. The Time Board was not free, let alone obligated, to permit Paramount and its stockholders to obtain the advantage which both companies saw in a combination of Time's business with a major movie studio, simply because Paramount made an above-market cash offer. Mills, ¶ 94,401 at 92,596, 92,599-92,600 n.35.

The revised merger agreement can in no way be considered a draconian "scorched earth" measure. No prize assets are to be sold or optioned at less than their intrinsic worth. Cf. Revlon; Mills. To the contrary, as noted above, it is undisputed that the Warner acquisition will enhance both the trading price and intrinsic value of Time stock; it does no "harm to the value structure of the corporation." Moran, 500 A.2d at 1354.[45]

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45 The shareholder plaintiffs complain that the Time tender offer for Warner contained no fiduciary out. Joint Brief at 15, 26, 36-37. The court below found that "the record is uncontradicted at this stage that Warner would not have
(Continued)

Nor can the revised form of acquisition be considered a "show-stopper." It is "not established that [a successful takeover of Time] is foreclosed as a practical matter." Opinion (B79). Certainly Paramount's Chairman Mr. Davis has not so concluded, and this case does not involve a transaction such as an issuance of a controlling block of stock to friendly hands that might preclude any future takeover. See Statement of Facts part F(6).

To be sure, the Warner acquisition would make Time a larger enterprise, requiring more financing for a takeover of Time. That fact alone, however, does not demonstrate that the action is unreasonable. See City Capital Associates v. Interco Inc., Del. Ch., 551 A.2d 787, 801 (1988) ("I do understand that [selling a key division] complicates [the bidder's] life and indeed might imperil [the] ability to complete its transaction. They, however, have no right to demand that their chosen target remain in status quo while their offer is formulated, gradually increased and, perhaps, accepted."); see also Danaher Corp. v. Chicago Pneumatic Tool Co., 633 F. Supp. 1066, 1073-74 (S.D.N.Y. 1986) (funding of ESOP which renders tender offer more expensive does not support claim of irreparable harm or tilt balance of hardships in plaintiffs' favor).

In fact, any substantial corporate investment -- building a factory, commencing research and development on a

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agreed to such a provision." Opinion (B44). If it were proper for the Board to pursue the acquisition of Warner in the face of the Paramount offer, a fortiori, it could not have been a breach of duty to fail to obtain some "out" to which Warner would not agree.

new product, or borrowing funds for corporate purposes -- might have the same effect of making an acquisition more costly, but the company potentially more profitable over the long term. Such a focus on long-term profitability is entirely consistent with Delaware law. TW Services, Inc. v. SWT Acquisition Corp., Del. Ch., [Current] Fed. Sec. L. Rep. ¶ 94,334 at 92,178 (March 2, 1988) ("directors, in managing the business and affairs of the corporation may find it prudent (and are authorized) to make decisions that are expected to promote corporate (and shareholder) long-run interests even if short run share value can be expected to be negatively affected . . .").

Ultimately, Time stockholders may collectively disagree with the Board's long-term vision of Time as one of the few global media giants, and may prefer a focus on realizing short-term value. "If the stockholders are displeased with the action of their elected representatives, [however,] the powers of corporate democracy are at their disposal to turn the board out." Unocal, 493 A.2d at 959. The revised merger agreement does nothing to alter or obstruct the electoral process by which such a change of management could be carried out.

The transaction selected by the Time Board treats all stockholders equally. All stockholders are entitled to share in the long-term benefits that will be created by the acquisition of Warner. The decision to proceed with that long-planned combination was fully reasonable in relation to the threat posed by the Paramount offer, and is presumptively valid under the business judgment rule.

III. THE TIME DIRECTORS WERE UNDER NO LEGAL OBLIGATION ON JUNE 16 TO SEEK TO MAXIMIZE ONLY CURRENT SHARE VALUE: THE SHAREHOLDER PLAINTIFFS' REVLON ARGUMENT.

A. Standard and Scope of Review.

See Argument II(A), supra.

B. Merits.

In its opening brief on appeal Paramount makes no separate Revlon argument. The shareholder plaintiffs still maintain that the Revlon duty to maximize immediate shareholder value was triggered by the Time Board's approval of original merger agreement because 62% of the Time equity would have been owned by former Warner shareholders after consummation of the original stock for stock merger. Joint Brief 43; but see Opinion (B57-59). The court below properly rejected the shareholder plaintiffs' mechanistic argument that a stock for stock merger necessarily reflects a sale of control of the surviving company if the former shareholders of the acquired company obtain the larger share of the equity in the continuing enterprise:

> If the appropriate inquiry is whether a change in control is contemplated, the answer must be sought in the specific circumstances surrounding the transaction. Surely under some circumstances a stock for stock merger could reflect a transfer of corporate control. That would, for example, plainly be the case here if Warner were a private company. But 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. This in my

> judgment was the situation with respect to the original merger agreement.

Opinion (B62).

The record fully supports the finding below that no change of control of Time would have taken place as a result of the original stock for stock merger simply because the former Warner shareholders would have held more than 50% of the equity in Time-Warner, the survivor in the merger.[46] Ownership of both Time and Warner was widely dispersed among many shareholders and no entity or entities controlled either company and no single entity or entities would control Time after the merger. Luce (B391); Hill (B93-94). Moreover, publicly available information shows that enough of the outstanding Time stock was owned by persons who also owned a sufficient amount of Warner common stock so that they would have owned approximately 60% of Time-Warner's equity after the merger. Munro (B107-08). See also Dingman (B176); Levin (B307); Nicholas (B502, B505-06). Thus, even the identity of

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46 In their Joint Brief, the shareholder plaintiffs argue that there was to be a "change in control" in the original merger like the change in control in other decisions applying Revlon such as, Black & Decker Corp. v. American Standard, Inc., 682 F. Supp. 772 (D. Del. 1988), the discussion by this Court concerning the Macmillan restructuring in Mills Acquisition Co. v. Macmillan, Inc., ¶ 94,401 at 92,599-600, Freedman v. Restaurant Associates Industries, Inc., Del. Ch. [1987-88 Transfer Binder] Fed. Sec. L. Rep. ¶ 93,502 (October 18, 1987) and Edelman v. Fruehauf Corp., 798 F.2d 882, 884-86 (6th Cir. 1986). Each of these cases involved a shift in voting control and stock ownership from the public shareholders to management in a management-sponsored LBO or similar restructuring. No such change was to occur under the original merger. Voting control and ownership of a majority of the equity in Time was to remain in diverse public hands.

60% of Time's owners would not have changed. There could be no change of control.

In support of the argument that approval of the original merger agreement triggered the Revlon duty to maximize immediate shareholder value, Literary Partners below took a different tack from the other shareholder plaintiffs. Literary Partners' Revlon argument, as distilled by the court below, is founded on the assumption that even if the original merger did not represent a change in control of Time it would make Time "takeover-proof" by its "very size" and thus preclude the future payment of a control premium to the Time shareholders. Joint Brief at 44-46. As a consequence, Literary Partners claims that the Time directors had a present Revlon duty to permit the current Time shareholders to accept the control premium offered by Paramount for the termination of their equity interest in Time. Opinion (B63); Joint Brief at 45.

In rejecting Literary Partners' separate Revlon argument, the court below held that "it is plain that the original merger transaction did not legally preclude or impede a later sale or change in control transaction" (Opinion (B64)), and none of the shareholder plaintiffs takes issue with that holding. In addition, the court below rejected as a factual matter Literary Partners' claim that the original merger and the revised merger would make Time "takeover-proof" by virtue of its very size. It found that "while effectuation of the Warner merger may practically impact the likelihood of a successful takeover of the merged company, it is not established in this record that that is foreclosed as a practical matter." Opinion (B79), citing In re RJR Nabisco, Inc. Shareholders Litigation, Del. Ch., [1988-89 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 94,194 (January 31, 1989) (takeover valued at $25 billion); see also Opinion (B64).

The record evidence demonstrates that the court below was correct. Time will not be "takeover proof" after the acquisition of Warner; a takeover of the merged company by Paramount or by others remains a distinct possibility (see Davis (B806, B808, B810-14); Seegal (B939-41); Senie (B830-31); Levin (B361, A1040); Nicholas (B528-29)); and mere size alone no longer precludes a takeover. Davis (B807); Hope (B281-82); Pattison (B647); Oresman (B621-22); Seegal (B940-41). Literary Partners ignores this evidence of record.

Rather than argue from the record, Literary Partners urges this Court to find that the Chancellor misread their Revlon argument when he found that its adoption would extend the reach of the Revlon case beyond sales or other change in control transactions. Opinion (B66). Literary Partners argues that no extension of Revlon is required because (1) that case is not limited to a sale of control and (2) "Revlon does not mean that Time must conduct an auction." Joint Brief at 46. Both elements of that argument are inconsistent with the holding in Revlon that "when the duty of the board had thus changed from preservation of Revlon as a corporate entity to the maximization of the Company's value at a sale for the stockholders' benefit . . . [t]he directors' role changed from defenders of the corporate bastion to auctioneers charged with getting the best price for the stockholders at a sale of the company." Revlon, 506 A.2d at 182 (emphasis added); see also Mills, ¶ 94,401 at 92,599.

We respectfully submit that the court below was correct in its view that Literary Partners' Revlon argument requires an extension of the specific holding of this Court in Revlon in a way that would dramatically restrict the board in carrying out its duty to act in a takeover context. The court below was also correct in concluding that board-adopted changes in corporate structure which impact on hostile acquirors are better addressed under a Unocal analysis, as we did in Section II above. Opinion (B66).

IV. PLAINTIFFS WILL SUFFER NO IRREPARABLE INJURY IF TIME ACQUIRES WARNER, AND THE BALANCE OF HARDSHIPS WEIGHS AGAINST GRANTING AN INJUNCTION.

A. Standard and Scope of Review.

The absence of irreparable injury justifies affirmance even though the court below did not reach a conclusion on this issue. Smith v. Bank of Delaware, Del. Supr., 219 A.2d 576, 577 (1966). The factual findings of the court below pertaining to this issue, however, are entitled to deference as set forth in Argument II(A).

B. Merits.

To obtain a preliminary injunction, plaintiffs must demonstrate that "some irreparable harm will occur" absent such relief, and that "the harm they will suffer if the relief is denied outweighs the harm defendants will suffer if the relief is granted." Ivanhoe Partners, 535 A.2d at 1341. Plaintiffs here satisfy neither of these requirements.

Paramount's offer remains a highly conditional, speculative possibility, capable of consummation only at some indefinite time in the future, if ever. Likewise, the claim that Time's acquisition of Warner will deter or devalue future takeover bids for Time is also speculative.

The acquisition of Warner does not make Time less valuable. No one contends that Time is paying too much for Warner, and investment bankers on all sides place the $70 per share acquisition price within the range of fairness. B275; B653; Waters (B746).

Paramount's Chairman Mr. Davis does not claim that a takeover of Time is no longer viable. To the contrary, he conceded in sworn testimony that Paramount had simply made "no determination" whether it would proceed with its offer if Time completed its tender offer for Warner. Davis (B811-12). With respect to "strategic or corporate buyers large enough to finance an acquisition of a Time-Warner entity, without relying on the borrowing capacity of such entity," all that Paramount's investment banker would say is that their number is "extremely limited." Waters (A1509). And according to Shearson, one of Time's financial advisors, "there are a significant number of parties that would be able to finance an acquisition of the combined Time-Warner." Seegal (B940). Indeed, far from asserting that no takeover of Time following a Warner acquisition is possible, Paramount's litigation expert Dillon, Read twice explicitly qualified its trading range predictions by excluding the effect of a takeover control premium resulting from a bid for the combined entity. Phillips (A380, A384); Waters (A376, 384).

Plaintiffs' claim that a takeover of the combined entity will necessarily be at less than $200 per share is based on an erroneous comparison of that acquisition price with predicted trading ranges. As the court below recognized, however, a trading value is not the equivalent of an acquisition value because the trading value does not include a requisite premium for control. Opinion (B33-34 n.7). The trading value for Time will increase as a result of the Warner acquisition. Independent investment analysts have predicted that the stock of the combined entity will trade at the high end of the range predicted by Time's financial advisors. Opinion (B35-36 n.8); Rossoff (A1529). Nor will the acquisition of Warner eliminate the control premium for Time. An appropriate acquisition value for Time would be at a substantial premium over the trading value. Rossoff (A1529). Thus, plaintiffs' fears of irreparable loss of a control premium currently available are unsubstantiated.

On the other hand, Time is ready to proceed with its offer for Warner and to achieve the benefits of that long planned for transaction. An injunction delaying the acquisition of Warner denies Time and its stockholders the benefits of that expansion, continues the internal turmoil among Time's valued employees, to the resulting detriment of the corporation as a whole, and increases the risk that changing market conditions will erode the feasibility of accomplishing the Warner acquisition. It is Time, and in the long run its stockholders, that would be irreparably harmed if the acquisition of Warner were enjoined.

CONCLUSION

For the reasons set forth above, Time and its directors respectfully urge that the order appealed from should be affirmed.

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that two copies of the foregoing Answering Brief of the Time Appellees and its accompanying Appendix (Volumes I and II) were served by hand on July 19, 1989 upon the following:

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