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November 12, 1993

By Hand

The Honorable Jack B. Jacobs
Vice Chancellor
Court of Chancery
Public Building
Wilmington, Delaware 19801

Re: QVC Network, Inc. v. Paramount Communications Inc., et al., C.A. No. 13208

Dear Vice Chancellor Jacobs:

Enclosed are four copies of the Plaintiff's opening brief in support of its motion for a preliminary injunction. The brief is being filed with the Register in Chancery this morning, and the enclosed copies contain a completed table of authorities.

Respectfully yours,

James P. Hughes, Jr.

James P. Hughes, Jr.

JPH:vp
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cc: Register in Chancery
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bcc: Theodore N. Mirvis, Esquire (by fax)
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November 11, 1993

By Hand

The Honorable Jack B. Jacobs
Vice Chancellor
Court of Chancery
Public Building
Wilmington, Delaware 19801

Re: QVC Network, Inc. v. Paramount Communications Inc., et al., C.A. No. 13208

Dear Vice Chancellor Jacobs:

Enclosed are four copies of the Plaintiff's opening brief in support of its motion for a preliminary injunction, two copies of my affidavit and three volumes of referenced exhibits, two copies of a compendium of unreported opinions and two notebooks containing minuscript versions of all the deposition transcripts taken through the end of yesterday (which are being provided for the Court's convenience). Tomorrow we will file under seal the brief, the affidavit and exhibits and all deposition transcripts and exhibits, as well as the compendium not under seal.

Due to logistical problems transporting the brief to Wilmington, the enclosed copies of the brief do not contain a completed table of authorities. However, the brief to be filed with the Register tomorrow will contain a

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RESTRICTED" MATERIAL

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

QVC NETWORK, INC., Plaintiff, v. PARAMOUNT COMMUNICATIONS INC., VIACOM INC., MARTIN S. DAVIS, GRACE J. FIPPINGER, IRVING R. FISCHER, BENJAMIN L. HOOKS, FRANZ J. LUTOLF, JAMES A. PATTISON, IRWIN SCHLOSS, SAMUEL J. SILBERMAN, LAWRENCE M. SMALL, and GEORGE WEISSMAN, Defendants.	)	C.A. No. 13208

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OPENING BRIEF OF PLAINTIFF QVC NETWORK, INC. IN SUPPORT OF ITS MOTION FOR A PRELIMINARY INJUNCTION

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NATURE AND STAGE OF PROCEEDINGS

On September 12, 1993, defendants Paramount Communications Inc. and Viacom Inc. announced their entry into a merger agreement providing for the Paramount stockholders to receive principally non-voting Viacom shares and $9.10 per share in cash in exchange for their Paramount equity. The agreed terms were then valued at $69.14 per Paramount share. Under the transaction, Sumner Redstone, the chairman and 85% controlling stockholder of Viacom, would obtain 70% voting control of the merged Paramount. In connection with the merger agreement, Paramount agreed to a $100 million break-up fee as well as a lockup stock option on 20% of its stock in favor of Viacom, priced at the $69.14 level of the Viacom proposal.

On September 20, 1993, plaintiff QVC Network, Inc. made a written proposal to negotiate a merger with Viacom at a value of $80 per share, approximately $2 billion higher than the Viacom proposal. The QVC bid offered $30 per share in cash and the remainder in (voting) QVC common stock.

On October 21, 1993, after Paramount had refused to negotiate with QVC over the several weeks following QVC's merger proposal, QVC announced a tender offer for 51% of the Paramount shares at $80 cash per share to be followed by an equal value second-step common stock merger. The new QVC bid increased the cash consideration by $10 per share (or approximately $1.2 billion more in cash than its September 20 offer). QVC continued to offer to negotiate a merger on the same increased terms. On the same day, QVC commenced the present action, seeking relief against the lockups in the Paramount-Viacom agreements and to require the Paramount directors to abide by their fiduciary duties under Delaware law.

On October 24, 1993, in response to QVC's offer but without any contact with QVC, Paramount entered into an amended merger agreement with Viacom, providing for a Viacom tender offer at $80 cash per share for 51% of the shares, to be followed by a second-step merger of largely non-voting Viacom Common stock and preferred stock exchangeable at Viacom's option into debt. The lockups were renewed. The Viacom $80 tender offer was commenced on October 25, and is scheduled to close on November 22. QVC's tender offer commenced on October 27, and is scheduled to close on November 24. On November 6, Viacom increased its tender offer to $85 per share for 51% of the stock, with a second step of equal indicated value on Viacom stock.

The relief sought by QVC is a preliminary injunction enjoining the Paramount board from taking any further steps to facilitate the closing of the Viacom tender offer (pending further order of the Court). If the current Viacom tender offer closes at midnight on November 22, the Paramount stockholders will have been forever deprived of the right to receive the best bid available. The injunction sought will permit Paramount's board to comply with its fiduciary duties to fully consider both the QVC and Viacom proposals on their merits.

This is plaintiff QVC's opening brief in support of its motion for a preliminary injunction.

PRELIMINARY STATEMENT

The present motion brings before this Court a change of control transaction in which the directors of a Delaware corporation have agreed to the elimination of their stockholders' voting control, and the vesting of that voting control in a single individual, without even the shadow of compliance with the fiduciary duty requirements of Revlon and Barkan. The Paramount directors have consented to a 51% cash tender offer by defendant Viacom -- whose chairman, Sumner Redstone, will absolutely control the voting power of the combined Paramount-Viacom entity -- as the last stage in an acquisition process in which Paramount has systematically refused to negotiate with another ready, willing and able bidder, whose proposed transaction would leave control of Paramount in the hands of its public shareholders. The Paramount directors have acquiesced in and rubber-stamped a one-sided process controlled by Paramount senior management whose positions the 70-year old Mr. Redstone has agreed to maintain if the Viacom transaction succeeds. The Paramount directors have utterly failed to play the active, engaged role required under the recent Technicolor decision of the Supreme Court and have failed to conduct an even-handed, nondiscriminatory change of control process. The Viacom transaction cannot stand under the applicable precedents.

To judge by their deposition testimony, the Paramount directors have apparently been led to believe that, if they use the terms "long-term strategy" and "strategic fit" to describe the Viacom transaction they are excused from their fiduciary duties under Delaware law. Stated another way, the directors appear to believe that by using language from the Supreme Court's decision in Paramount Communications Inc. v. Time Inc. to describe the Viacom transaction, they need not take any further steps to satisfy themselves that the transaction is the best available financial alternative for the Paramount public stockholders. We will show below that that position both misreads the Paramount decision and essentially eviscerates settled Delaware jurisprudence on the enhanced responsibilities and obligations of directors in the change of corporate control context.

Moreover, the record shows that the Paramount directors acted so hastily, and were so ill-informed, that for this independent reason the Viacom transaction cannot stand. While repeating the mantra of "fit" and "continuing equity interest," the directors did not obtain and did not even seek any guarantee that Redstone will in fact continue the Paramount stockholders' equity interest. Paramount meanwhile refused to have any discussions with QVC whose transaction assures that the public stockholders will remain in control of their company. The Paramount directors accepted a price of $69 from Viacom, and gave unprecedented "lock-up" stock options and break-up fees worth almost $500 million at current bidding levels (more than $4 per Paramount share), although other bidders and Viacom itself were prepared to offer billions of dollars more. The Paramount directors did not know of or understand the crucial "lock-up" features in the Viacom transaction, did not know that Redstone had engaged in heavy trading in Viacom securities in the weeks leading up to the final negotiation of the Viacom transaction -- trading that may have temporarily inflated the price of the Viacom stock (largely nonvoting) that the stockholders would receive from Viacom -- and did not inform themselves in anything like the thorough manner required by their offices in this context. Paramount's actions have been unreasonable in their defensive aspects, and have discriminated against a bona fide competing offer without any justification. The Viacom transaction is the result of a process that makes a mockery of Delaware principles of corporate governance.

STATEMENT OF FACTS*

A. The Parties

1. **QVC**. QVC Network Inc. ("QVC") is a Delaware corporation headquartered in West Chester, Pennsylvania. QVC is a nationwide general merchandise retailer, and is the leading televised shopping retailer in the United States. Ex. 5 at 20.

QVC's Chairman and Chief Executive Officer is Barry Diller, who joined the company in January 1993. From 1984 to 1992, Mr. Diller served as Chairman and Chief Executive Officer of Fox, Inc. Before that, he had served for ten years as Chief Executive Officer of Paramount Pictures Corporation, a motion picture studio that was a subsidiary of Gulf+Western Inc. Mr. Diller left Paramount Pictures in 1984, the year after defendant Martin S. Davis became Chairman and Chief Executive Officer of Gulf+Western (which in 1989 was renamed Paramount Communications Inc.). Ex. 5 at 52; Davis Dep. 4.

2. **Paramount**. Paramount Communications Inc. ("Paramount"), is a Delaware corporation headquartered in New York City. The businesses of Paramount are entertainment and publishing. Paramount's Chairman and CEO is Martin S. Davis, who

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* This Statement of Facts is based upon the record available from expedited discovery proceedings in this case, which are still proceeding. Deposition testimony is cited as "[Witness name] Dep. __" and deposition transcripts have been lodged with the Court. Deposition exhibits, along with certain other documents produced in discovery and certain public filings and other public information, are attached as exhibits to the Affidavit of David C. McBride being submitted herewith. Exhibits to the McBride Affidavit are cited herein as "Ex. _" and the McBride Affidavit contains a descriptive listing of such exhibits, including their deposition exhibit identification information (if any).

has held those positions since 1983. Ex. 9 at V3383. Paramount's board is comprised of four inside directors (Messrs. Davis, Donald Oresman, Stanley Jaffe and Ronald Nelson) and eleven nonemployee directors. Paramount's financial advisor is Lazard Freres & Co. ("Lazard"). Ex. 9 at V3383-84. Paramount has approximately 118 million shares outstanding.

3. **Viacom**. Defendant Viacom Inc. ("Viacom"), a Delaware corporation headquartered in Massachusetts, is a diversified entertainment and communications company. Silberman Ex. 2 at 4.

Viacom is controlled by Sumner M. Redstone, its Chairman and CEO and controlling stockholder. Redstone, who is 70 years old, owns approximately 85.2% of Viacom's Class A stock -- the only voting class of Viacom stock -- through National Amusements, Inc. ("NAI"), a corporation of which he owns 91.7%. NAI also owns 69.2% of Viacom's Class B stock, its non-voting stock. Ex. 6 at 14; Ex. 9 at 3; Ex. 21 at 5. Viacom's investment banker is Smith Barney.*

Redstone and Davis have long been close personal friends. In Davis's words:

> we go back -- actually it's about 40 years -- when we were both kids in the entertainment industry . . . . We have been professional colleagues and personal friends ever since.

Ex. 22 at 10; see also id. at 10 (Redstone, describing Davis as "my long-time friend"). In a September 17, 1993 letter to Paramount shareholders, Davis similarly describes Redstone as "a good friend for more than 40 years." Ex. 24.

B. Events Leading to the Original Viacom Merger Agreement

1. **Paramount Is An Extremely Attractive Acquisition Candidate.**

There is no dispute that Paramount, in the words of its investment banker, "is an extremely

* Under his current estate planning arrangements, Redstone's controlling interest in Viacom (and thus in the merged Paramount/Viacom entity) will be placed upon his death in a trust. Dauman Dep. 111-16.

attractive company, with a collection of unique assets that includes the last 'independent' major studio as well as one of the world's largest publishing companies." (Ex. 54 at 21) On September 12, the day the Paramount board approved the original merger agreement with Viacom, Lazard advised the directors that there were ten companies Lazard had identified as "potential acquirors of [Paramount]," although Lazard had talked to none of them. (Ex. 54 at 22; Rattner Dep. 52-53). As one outside director testified, "there were a lot of people interested in Paramount, and had been for some time." Pattison Dep. 25; see also Pattison Dep. 22-23; Greenhill Dep. 78 ("There had always been speculation about a takeover of Paramount").

Paramount's CEO, Martin S. Davis, had for a number of years publicly maintained that Paramount was seeking a major acquisition -- in fact, in 1989, he launched an unsuccessful unsolicited tender offer for Time Inc. See Paramount Communications Inc. v. Time Inc., Del. Supr., 571 A.2d 1140 (1989). According to Davis, "[m]ost" of the transactions considered "would have [involved] us, Paramount, as the acquirer." Ex. 35 at 20. Indeed, except for the pending Viacom transaction, Lazard could not recall any transaction involving a change in control of Paramount that ever had been brought to the Paramount board for action. Rattner Dep. 6-7. Further, Lazard could only recall two negotiations or discussions with third parties that related to a possible, "partial" change of control of Paramount and one of those discussions involved Viacom. Rattner Dep. 6-14.

Paramount's determination to be the "acquiror", and not the "acquired", was attributable, at least in part, to Davis' determination to remain CEO after any transaction. According to one investment banker who was involved in Paramount's earlier search for acquisition candidates:

> Davis had always taken the position that he would not look at any bid in which he did not end up being CEO.

Senior Dep. 65; see also id. at 66, 67, 131-32, 173. Davis's insistence on retaining control was the real "problem" preventing a Paramount transaction; getting a premium for stockholders was not. Senior Dep. 67 ("A premium was always discussed, [but] that was not the real problem. The problem was Mr. Davis wanted to be CEO.").

2. **Viacom, the Persistent Suitor**. Redstone has long been interested in acquiring Paramount for Viacom. Redstone first mentioned to his friend Davis the subject of a possible Paramount/Viacom combination in 1989. Davis Dep. 17-18; Redstone Dep. 23. Viacom was the pursuer -- indeed, Redstone's own correspondence to his investment banker makes clear that Redstone's "aspirations" involved the acquisition of Paramount. Ex. 63. And so what followed, in Redstone's words, was a "three and a half year romance," during which Redstone persistently tried to persuade Davis to sell Paramount. Ex. 22 at 8; accord Ex. 67 at 6-7. But Davis, who insisted on control of any merged company, was "tough" to catch. As Redstone noted in a recent press conference, it took "four years to get him [Davis] to the altar." Ex. 22 at 7. Redstone was unwilling to consider any transaction that would not result in his absolute, majority control of the merged company. Rattner Dep. 7, 55; Dauman Dep. 30-36; Greenhill Dep. 29-30 ("Sumner was always going to maintain the voting standing that he had in Viacom. He was not going to change that in any transaction.")

3. **Takeover Speculation Intensifies**. Takeover speculation about Paramount intensified in early 1993. Paramount's earnings plummeted 95% for its first fiscal quarter of 1993. Yet its stock price had begun to rise. The Wall Street Journal reported, for example, that this rise in stock price was in part

> fueled by speculations that Paramount is discussing a merger or an acquisition of another entertainment company. Among companies Paramount is said to have talked to are Viacom, Inc., Turner Broadcasting System, Inc., and Capital Cities/ABC, Inc.

Ex. 69. <u>See</u> also Pattison Dep. 24 ("common knowledge" that Turner and Tele-Communications Inc. ("TCI"), a major cable television company, were interested in acquiring Paramount). Reuters likewise reported that Paramount stock had been repeatedly the subject of takeover rumors. Ex. 70.

The takeover speculation about Paramount did not escape Davis' attention. Prior to the board approval of the Viacom merger, both Davis and Lazard were aware of the press reports, including press reports that QVC and TCI might have an interest in acquiring Paramount. Rattner Dep. 14, 18 and 22; Davis Dep. 6 (knew of press reports "specifically on QVC"); Malone Dep. 73. Indeed, Davis had discussed the possibility of a QVC bid with Lazard on more than one occasion during 1993. Rattner Dep. 22-24. Yet Davis never asked Lazard to investigate whether QVC or TCI had any interest in Paramount or to obtain any information on QVC's reported interest. Rattner Dep. 23, 28. Rather, as discussed below, Davis talked privately with Barry Diller of QVC and John C. Malone of TCI. Rattner Dep. 28-29, 32-36.

4. <u>The Private Negotiations of Martin Davis and Sumner Redstone: April 20, 1993 to July 1, 1993</u>. The takeover speculation about Paramount also provoked interest on the Viacom side. On April 14, 1993, Robert Greenhill, Viacom's investment banker, faxed to Redstone a press report of the takeover speculation concerning Paramount, with a note that "he [Davis] is feeling the pressure." Ex. 64. See Dauman Dep. 64.

On April 20, 1993, Davis, Redstone and Greenhill met in the first of a series of private meetings. Other such meetings occurred on June 10, June 23, June 28 and June 30. Ex. 38 at P30907. Neither Paramount's directors nor its investment banker were ever present; Greenhill, later formally retained by Redstone to represent <u>Viacom</u>, acted for <u>both</u> parties throughout this period. Greenhill Dep. 63. Indeed, Lazard did not even learn of the possibility of a Viacom transaction until late June. Rattner Dep. 37; Rohatyn Dep. 8. By that time, Davis and Redstone had essentially agreed on the key elements of the deal eventually signed in September -- that Redstone would have control of the merged entity

(Rattner Dep. 45-46, 49); that Davis would be CEO (Dauman Dep. 38); that the exchange ratio would be 1/10th of an A Viacom share and 9/10th of a (non-voting) B Viacom share (Rattner Dep. 61); and that the total price -- stock plus cash -- would be in the 60's. Rattner Dep. 56; Dauman Dep. 30-36.

In a memorandum he later wrote to his financial advisor, Redstone described his one-on-one negotiations with Davis as follows: "[W]hen I suggested that price was a critical issue, what I heard was that that was <u>not</u> the most important issue, that that could be easily resolved, but that management was the issue." Ex. 85 at V008943 (emphasis supplied). See also Greenhill Dep. 46-47 ("definitely" were "issues of ego" involved in the Davis/Redstone negotiations). Redstone described the discussions: "And so we discussed management, directly and indirectly, including a series of personal meetings, reaching all kinds of solutions at various times" to the management issue. Ex. 85 at V8943. Viacom viewed the management issue as "difficult". Dauman Dep. 39. And it was difficult because, while Davis had been promised the <u>title</u> of CEO in the combined company, he nevertheless had substantial concerns over the scope of what his "<u>authority</u>" would be in an entity under Redstone's control. Greenhill Dep. 35-36.

Meanwhile, rumors about Paramount continued to swirl. On June 26, 1993, the <u>Los Angeles Times</u> reported speculation Paramount would be acquired, but noted that "[o]ne big question mark, however, is what would happen to Paramount chief Davis." Ex. 71. The <u>Wall Street Journal</u> ran a similar story on June 28. Ex. 72. Negotiations between Redstone and Davis accelerated within a matter of days of these reports. Davis and Redstone met alone on June 23, June 28 and June 30. The only other person involved in those discussions was Stanley Jaffe, Paramount's President, and he attended only one of the meetings. Ex. 38.

5. **<u>The Negotiations Intensify and Collapse: July 1-7, 1993 - Paramount Rejects 1/10th of an A Share, 9/10ths of a B Share and $13.50 in Cash As Inadequate</u>.** On July 1, members of Paramount's senior management (led by Davis) and Lazard

personnel met with Greenhill and Phillippe Dauman, Viacom's General Counsel. Ex. 38 at P30907. That same day, the parties executed and exchanged confidentiality agreements (but no information) to facilitate due diligence. Ex. 6 at 18.

On July 6, representatives of Paramount -- including Donald Oresman, Paramount's General Counsel, and Felix Rohatyn of Lazard -- met with Greenhill and Dauman to talk about the terms of a possible deal. Ex. 38 at P30908; see also Ex. 6 at 18. Viacom reiterated Redstone's prior proposal that Paramount stockholders receive 0.9 shares of Viacom of nonvoting Class B stock, 0.1 shares of Viacom voting Class A stock, (this time with $13.50 in cash) for each Paramount share, with a "cap" of $65 per share. Dauman Dep. 74-75; Oresman Dep. 30-31. The market value of the proposal at the time was $60.86 including the $13.50 in cash. Ex. 6 at 18; Ex. 51 at L004930. Neither a chronology of the negotiations given to the Paramount board on September 9 nor an internal chronology prepared by Lazard mention any condition to this proposal. Ex. 53 at P30072; Ex. 51 at L4930. Specifically, there is no mention of Viacom demanding a 20% stock option or any other type of lock up. No outside director participated in any of these discussions. Ex. 6 at 18; Ex. 38 at P30907-08.

Discussions broke down on July 7, 1993. Both Davis and Redstone realized that a transaction involving a change of control of Paramount required a premium for the Paramount shareholders. Davis Dep. 20-21; Rattner Dep. 57-58. As Lazard explained, "there is an economic value to that control for which [the stockholders] should be compensated." Id. at 58. In early July, Paramount management advised Lazard that "a price less than $70 would not be attractive." Rattner Dep. 63-65. Consequently, on July 7, Paramount rejected Viacom's proposal as "inadequate". Rattner Dep. 67; Ex. 11; Silberman Dep. 19-22. Viacom was told that Paramount could not accept a price below $70 -- which was also the "highest price" Paramount ever sought from Viacom. Dauman Dep. 85-91. Lazard testified that the July 6 proposal "was substantially below any estimate of value for

Paramount with which we were familiar." Rattner Dep. 70. Indeed, Lazard and Paramount considered the proposal so inadequate that Paramount did not even make a counter-proposal. Rattner Dep. 70-71. After Paramount rejected Viacom's proposal, negotiations with Viacom "terminated until such time as someone had a good idea as to how to bridge this large gap." Rattner Dep. 75.

6. Davis's Increasing Concern About QVC and Diller. Meanwhile, Davis had become greatly fearful of a possible hostile bid from Paramount Pictures' former CEO and QVC's current chairman, Barry Diller. Davis testified that John C. Malone (the CEO of TCI and a QVC director) had alerted him to a potential hostile bid by QVC. Davis Dep. 60, 66. Davis therefore invited Diller to a lunch meeting at Paramount's headquarters on July 21, 1993. During this lunch meeting, Davis said that he was disturbed by rumors and other reports that Diller was readying an unsolicited attempt to acquire Paramount. Davis also said that he believed Diller was interested in acquiring Paramount; that he believed Diller was the source of various reports and rumors that QVC would try to acquire Paramount; and that he knew of meetings held by QVC in preparation for a takeover bid for Paramount. Ex. 5 at 24; Diller Dep. 33, 181; Davis Dep. 55-56; see also Senior Dep. 14; Small Ex. 1 at 24. Davis also flatly told Diller that Paramount was not for sale (Davis Dep. 57, 59; Diller Dep. 180; Senior Dep. 14), and "that he had a whole series of defenses that people both understood and didn't understand to prevent a sale". Diller Dep. 180. Throughout the lunch, Davis "consistently" told Diller, "I know you are after my company." Diller Dep. 181. Paramount's outside directors were never told about this meeting, let alone what Davis said -- on behalf of Paramount -- at this meeting. Silberman Dep. 33-34; Pattison Dep. 19, 26-28; Small Dep. 48-50.*

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* Davis testified that his "recollection" now is that Diller told Davis that "he did not have an interest at that time." Davis Dep. 58. Davis also recalls that he (Davis) responded to this by asking how that could be in light of all the reports, including from close Diller associates, of QVC's interest in Paramount. Id. Davis also claims that he took Malone's report to him to be a fabrication on Malone's part, meant to "drive us into his arms." Id. at 66-67.

Davis expressed his concerns about Diller to others as well. Several times in June and the early summer of 1993, Davis told Malone "that he [Davis] would be very upset if Mr. Diller made a hostile proposal to Paramount, and that he was looking at [Malone] to prevent such an event from taking place." Malone Dep. 59, 73. Davis was "very upset" about rumors he had heard about QVC. Malone Dep. 73. According to Malone,

> Davis indicated to me that he was not an enthusiast of Mr. Diller's. . . . of course, Mr. Diller had been an employee of Paramount at one time, and Mr. Davis felt that it would be very unfortunate if Mr. Diller ended up in some way making a proposal for Paramount, and also asserted that he had many defenses against such a move. . . .
>
> [Davis] alluded to a very strong and supporting group of shareholders, many of them European. He alluded to, of course, his antitakeover defenses, and he alluded to other interested parties who would presumably come to his rescue should a hostile move be made on the company.

Malone Dep. 60.

7. **July 6-August 20: "Bridging the Large Gap" with a Runup in Viacom B Stock**. When negotiations terminated on July 6, the Viacom B stock, which was by far the largest component of the Viacom offer, was trading at $46.875. Ex. 53 at 1. Even with the $13.50 in cash and 1/10 share of Viacom A, the value of the Viacom offer was substantially below Paramount's asking price of $70 per share. However, six weeks later, when negotiations resumed, this critical component to the Viacom offer was trading at $57.25. Ex. 53 at 1.

The sharp increase in the price of the Viacom B stock concerned Lazard and Paramount's management. Rattner Dep. 88-91. Lazard learned that Redstone had been a heavy purchaser of Viacom B Shares through July and August. On August 10, 1993, Lazard sent Davis and four other top executives at Paramount an analysis of Redstone's purchases. The analysis showed that Redstone had acquired 6.4% of the Viacom A shares traded in June and 4.6% of the Viacom B Shares traded that month. Ex. 58 at P190332. Lazard was concerned that Redstone's purchases "could possibly cause the value of the shares of the [Viacom]. . .to be higher than they might otherwise be in the absence of such purchases." Rattner Dep. 78.* Paramount's concern that Redstone's purchases had significantly increased the Viacom stock price was made known to Viacom. Dauman Dep. 116-17; Rattner Dep. 89-90.

On August 20, 1993, Lazard sent Davis and four other top Paramount executives at Paramount a further analysis of Redstone's trading in Viacom stock in July. Silberman Ex. 6 That analysis showed that Redstone's trading as a percentage of the market had increased from 4.6% of the B shares traded in June to 13.91% of the B shares traded in July. Moreover, on the days when Redstone traded, his purchases in July constituted 18.79% of the B Shares traded. Ex. 57 at P190336. During the period after July 6, 1993, when the negotiations terminated, and August 20, when they resumed, the Viacom B shares appreciated 22.1% and Redstone accounted for 15.5% of the purchases.**

On August 20, the day negotiations resumed between Viacom and Paramount, Redstone stopped trading in Viacom stock. At that time, the B shares were trading at $57.25. By September 8, the day before the Viacom proposal was first submitted to the Paramount board, and without any trading in the interim by Redstone, the run up in the B shares had reversed itself, with the price declining to $57.75. Ex. 53 at 1-2.***

8. <u>August 20-September 7: Negotiations Resume</u>. Negotiations between Viacom and Paramount resumed on August 20. Ex. 51; Ex. 53. By this time, the price of Viacom Class B stock had shot up from $46 per share on July 7 to $57.25, and the price of Viacom Class A stock had risen from $51.13 to $62.75. Ex. 66 at SB3293. Lazard could not recall what had occurred since July 7 and August 20 to cause the

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* In discovery, Lazard explained that Viacom's stock was "very thinly traded" and very volatile, thereby increasing the effect of Mr. Redstone's purchases on the market price. Rattner Dep. 101.

** This information was contained in an analysis of Redstone's trading by Smith Barney. Ex. 66 at SB3387.

*** In addition, Malone of TCI testified that he had heard indications that Redstone "had engaged in a process of calling and tipping people that a very favorable transaction to Viacom was in the works, and encouraging them to purchase Viacom stock in the open market." Malone Dep. 89.

resumption of negotiations (Rattner Dep. 82-83), and no Paramount witness has testified as to why they were resumed. Redstone's August 16 memo states that the purpose of the resumption of talks was to "discuss management" issues. Ex. 85 at V008943.

Negotiations resumed with a meeting between only Redstone and Davis. Ex. 38 at P30908. At that meeting, price was not discussed, but "structural issues" were discussed. Ex. 53 at 1. Greenhill, Viacom's banker, had suggested to Redstone that "management" should be the "lead-in topic" for Viacom to use to resume discussions. Dauman Dep. 154.* After that private meeting, Davis and Redstone agreed to have their senior managers and advisors start talks anew. Ex. 6 at 18; Ex. 38 at 30908. Ex. 51 at L4930. The basis for renewal of discussions included the parties' understanding of a $65 bid/$70 asked range. Ex. 51 at L4930; Ex. 53 at 1. No Paramount outside director, however, had ever authorized limiting Paramount's "asking" price to $70. Small Dep. 41-44. The outside directors took no part in the new round of negotiations; they were not even briefed about the terms being discussed in the negotiations until the board meeting of September 9, by which time the terms of the transaction had already been set by management. Ex. 38 at P30910. Small Dep. 40-43.**

Between the resumption of the negotiations on August 20 and the presentation of the transaction to the Paramount directors on September 9, very little changed to the advantage of the Paramount shareholders. According to a detailed chronology produced by Lazard, on August 24, Viacom offered "$60 in stock and $9 in cash." Ex. 51 at 2. The

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* The nonmanagement members of the Paramount board's Executive Committee were never told that management issues stood as an obstacle to a transaction. Silberman Dep. 25 ("Q: Was the committee told that any issues concerning management of a merged company stood as an obstacle to such a transaction? A: No."). They were never told that Paramount negotiator Davis did not consider price, as opposed to management, to be the most important issue. Silberman Dep. 25, 30-32. Davis told them precisely the contrary: that "the discussions were broken off because of price." Silberman Dep. 19; see also id. at 20.

** On the subject of director involvement in negotiations for the sale of the company, one director expressed his views this way: "I mean, an outside director, my golly, they don't do that." Liedtke Dep. 45. The director did not even know who on the Paramount board had been involved in the negotiations. Id. at 46.

deal submitted to the directors on September 12 was $60.04 in stock and $9.10 in cash. Ex. 54. As Davis had told Redstone, price was not to be a problem; it would be easy. Ex. 85.

During the negotiations in this period, Paramount attempted to obtain two principal concessions from Viacom, but received neither of them. First, due to the sharp increase in Viacom's stock, Paramount expressed an "interest" in obtaining price protection, a "stock collar", that would guarantee a certain minimum price for the Paramount shareholders if the Viacom stock fell in value before the merger could be consummated. Ex. 53 at 1. Viacom refused. Rattner Dep. 101-03.

Without the "collar", Paramount sought either the right to terminate the merger agreement if the price of the Viacom stock fell below a certain "floor". Rohatyn Dep. 17-18; Ex. 51 at 1. Viacom rejected this proposal. Rohatyn Dep. 18. Finally, Paramount sought a right to terminate the merger if Lazard could not update its "fairness" opinion at the time of the stockholders meeting. Rohatyn Dep. 18. Viacom rejected this proposal. Rohatyn Dep. 18. In fact, the original merger agreement, as interpreted by Paramount, would only allow Paramount to begin discussions with a third party if that third party had evidence of a fully financed offer, regardless of any decline in the value of the Viacom stock, and obligated the Paramount directors to submit Viacom's proposal to the Paramount stockholders even when the directors were precluded by their fiduciary duties from recommending the offer. Rohatyn Dep. 21, 25-27.

From the Viacom side, the negotiations between August 20 and September 9 were markedly more successful. In addition to avoiding the price protections sought by Paramount, Viacom obtained the lockup stock option which entitled Viacom to a virtual bonanza if, as Paramount feared, the Viacom stock dropped in value, the Paramount shareholders rejected the Viacom deal and a third party acquired Paramount at a higher price.

Another extraordinary aspect of the negotiations between August 20 and September 9 is the apparent fact that Viacom, or its investment banker, withdrew its request for a "lockup stock option". In a chronology of the negotiation produced by Lazard, there is an entry on August 25 that Viacom "[w]ithdrew request for lock-up, [but] repeated $150 break-up fee and expense reimbursement with a cap." Ex. 51 at 3. While both Lazard witnesses testified that Viacom did not withdraw its request for the stock option (Rohatyn Dep. 32), Mr. Rohatyn testified that the author of the chronology, Peter Ezersky, who was present at the meetings described, was unlikely to "have made a mistake with so material a fact." Rohatyn Dep. 39.

On Tuesday, September 7, the day after Labor Day, the negotiations culminated in a meeting between the investment bankers in which Viacom again offered 9/10th of a share of Viacom nonvoting Class B stock, 1/10th of a share of voting Class A stock, and $8.80 cash, with no price protection, a $100 million break-up fee and a lockup option on 20% of Paramount's outstanding shares, exercisable at the transaction price. Ex. 51 at L4928. This formula offered the same amount of stock -- but $4.70 per share less in cash -- than the formula rejected as inadequate by Paramount in July. See Davis Dep. 101-02. Due solely to the run-up in Viacom stock during the summer, however, the new proposal had an indicated value of $68.74 per share. Paramount responded by saying that it would agree to the lockups if the cash portion were increased to $10 per share -- resulting in total consideration of $69.94, an additional $1.20 per share. Redstone and Viacom responded by offering to make the cash portion $9.10 per share (for a total of $69.04, a 30¢ increase over its first bid that day). Ex. 53 at 3; Dauman Dep. 192. On this basis, Davis and his management team were satisfied, and the parties turned to due diligence and the drafting of documentation. Ex. 53 at 3.

Thus, on September 7, Paramount's management and advisors agreed to the massive lockup option (on top of a $100 million break-up fee) for a deal at roughly $69 per share, with absolutely no price protection -- even though two months earlier virtually the same formula had been rejected by both management and Lazard as inadequate, and no studies of Paramount's value had been performed in the intervening period.

Even apart from the plain effect of the lockups, which will be discussed below, there is evidence that shows why Paramount's management was so willing to accept the lockups. A handwritten note from Lazard's files taken during the negotiating session at Smith Barney on September 7 explains the rationale:

> Lock-up -- Want deal to look strong --
> Option on 20% of stock at deal price.

Ex. 61 at L6625 (emphasis added). Lazard's Rattner testified that Viacom requested the option, not to induce a bid, but to deter other bidders. Rattner Dep. 134-35 (Viacom's only reason for the lockup was to "reduce the possibility of third parties coming in.") In other words, the lockup was sought in order to deter another bid -- not to obtain one. Indeed, a director of Paramount has testified that this was exactly why Paramount agreed to the lockup option:

> Q: Did you understand at the September 12th meeting that the effect of the break-up fee and the stock option was to make it more difficult for a competing transaction to emerge than would otherwise be the case?
>
> A: 1, it would be more difficult. 2, this was obviously a protection to Mr. Redstone that we couldn't go out capriciously. His deal was the first deal that we wanted to make and did make.
>
> And this was a question of protecting the deal as it was constituted, because we felt this was favorable to Paramount as well as to Viacom.

Silberman Dep. 108 (emphasis added). Similarly, another outside director of Paramount testified that the lockup option was "deemed necessary . . . [b]y both parties" since "Paramount had no -- had absolutely no intention of . . . having an auction [or] doing anything that would stimulate other bidders to come out of the woodwork . . . ." Small Dep. 51, 63-64, 198-99 (emphasis added).

10. <u>**September 8-12, 1993: Due Diligence and Presentation to the Paramount Board**</u>. In four days, September 8 through 11, Viacom and Paramount "exchanged financial and legal due diligence materials, conducted due diligence, and negotiated [a] Merger Agreement, the [lockup] Stock Option Agreement, and [a related] Voting Agreement." Ex. 6 at 18-19. Again, negotiations on the Paramount side were conducted by Davis, Lazard, and by Davis's management team, with no involvement by the outside directors. Ex. 38 at P30909-10; Small Dep. 55.

During the week before September 9, Davis telephoned members of the Paramount board in anticipation of the regularly-scheduled board meeting on September 9; he perfunctorily told those directors "that there would be discussions of [a] merger" with Viacom at the board meeting, and "that there would probably be a proposal to be considered." Silberman Dep. 34, 35. Davis did not give the directors any details or terms -- not even the price -- of what the proposal would be. Silberman Dep. 36; Small Dep. 41-42, 45. Before September 9, the outside directors were never told about any terms Paramount was seeking from Viacom; were never told about any terms Viacom was seeking from Paramount; were never told the "bid" and "ask" prices in the negotiations; and were never asked for their views as directors on any issue in the negotiations. Small Dep. 41-42; <u>see also</u> Liedtke Dep. 48. And the board was given <u>no</u> written materials in anticipation of the board meeting. Small Dep. 32-33.

At the meeting on September 9, the discussion of the merger -- the terms of which had already been set by management -- lasted forty-five minutes. Silberman Dep. 37. According to the minutes of the meeting, the Paramount board was advised that control of Paramount was going to be sold to Redstone, and that the stockholders would be receiving a "premium because of the sale of control":

> Mr. Davis pointed out that whether the Corporation merged into Viacom or Viacom merged into the Corporation, Mr. Sumner Redstone, the principal shareholder of Viacom, would emerge as the controlling shareholder of the combined company.

> The Lazard Freres group . . . said they believed that the market would respond positively if the transaction was done at a premium <u>because of the sale of control</u> and was done largely for stock so that shareholders would have a significant continuing interest in a combined company with strong potential.

Ex. 12 at P20097 (emphasis added). The board fully understood that control of Paramount would pass from the public to Redstone. As one outside director aptly put it, after the proposed Paramount/Viacom combination is effected, "I believe there will be a new entity created that will have a dominant shareholder." Small Dep. 13 (emphasis added). As Mr. Davis testified:

> A. Because there was a controlling shareholder we felt very strongly we were entitled to a premium and that's what we negotiated about and that's what we discussed clearly at the board meeting. So the premium clearly represents that control value.
>
> Q: That you were giving up control to Mr. Redstone?
>
> A: That he was paying a premium for it.
>
> Q: And was it discussed that once you did the transaction there would no longer be a potentiality for a control premium?
>
> A: I don't believe that was discussed.

Davis Dep. 108; see also Pattison Dep. 119-20, 123.

At the September 9 meeting, the directors were given a small Lazard book that contained a brief (and incomplete) chronology of events, along with general information about Viacom and Paramount, their stock trading histories, and brief analyses of premiums paid and price multiples in other transactions. Ex. 53.* A substantial portion of the forty-five minute presentation was devoted to the Lazard book. Silberman Dep. 62. No other written document was presented to the directors at the meeting -- no draft of the proposed merger or lockup stock option agreements, no written summary of the proposed merger or lockup stock option terms, no analysis of comparable stock option agreements, and no analysis of alternative merger or acquisition candidates. Silberman Dep. 60-61.

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* Although the detailed Lazard chronology of the negotiations (Ex. 2) was prepared in a format for inclusion in the board book, it was <u>not</u> included.

And despite the fact that the Lazard book contained a price history for Viacom stock, it contained no information -- not a footnote, not even a word -- about Sumner Redstone's open market purchases of Viacom stock and their impact on the stated price of the deal they were being asked to approve. See Ex. 53 at P30102-05.

C. The September 12 Paramount/Viacom Merger Agreement and its Aftermath

1. **The September 12, 1993 Paramount Board Meeting**. The Paramount board held a special meeting on Sunday, September 12 to approve a merger agreement with Viacom. The terms were those offered by Viacom on September 7. See Ex. 13 at P20101; Ex. 54 at P30136. The meeting began at noon, and lasted two and a half to three hours. Davis Dep. 128-29. At this meeting, the Paramount board gave its approval to the original merger agreement and the lockup Stock Option Agreement.

The only document placed before the Paramount board on September 12 was a short book prepared by Lazard. Ex. 54; Silberman Dep. 70-71. According to one director, the directors at the September 12 meeting "hadn't had time to look at" the written material before listening to an oral report that was "not nearly as detailed." Liedtke Dep. 8, 9. See also id. at 11 (outside director received the written material the day after the meeting). The directors were not provided with copies of the merger agreement or the stock option agreement. Silberman Dep. 71-72; Small Dep. 34-35. Nor were they given written summaries of those agreements. Silberman Dep. 71. Indeed, negotiations were continuing through the night of the 11th and until the meeting on the 12th. Oresman Dep. 24. The Lazard book did not contain any information about the agreements; it contained exactly one line about the terms of the transaction: ".9 B shares, .1 A shares & $9.10 cash." Ex. 54 at P30136. There was nothing in writing about the lockup option, its potential value, its deterrent effect on other potential bids; and nothing about its size relative to those in other transactions (even though Lazard had such information in its files). Indeed, the Lazard book did not disclose the amount ($100 million) of the break-up fee. While Lazard's book contained a page listing approximately ten potential bidders for Paramount, including QVC, Lazard had not contacted any of the companies because it had "no authorization to do so." Rohatyn Dep. 46.

The minutes do not indicate any discussion of the merger agreement's termination provisions, the break-up fee, or the lockup option. If there was any such discussion, it clearly did not inform -- in fact, it misinformed -- the Paramount board. Two outside directors incorrectly testified that Paramount had a right to terminate the Original Merger Agreement:

> Q: My question was, did you have the right to terminate the Viacom merger?
>
> A: We did, I believe we had that right with the -- but if we did, then there were certain of the, as you pointed out before, there is [$100 million] for expenses and an option at the price we had agreed to merge to Viacom.
>
> Q: But your understanding is, you did have a right to terminate the merger agreement?
>
> A: Yes.

Silberman Dep. 73 (emphasis added).

> Q: If after consideration [Paramount] determined the other offer was better than Viacom['s] is it your understanding that Paramount could enter into the other proposal?
>
> A: Yes, it was.
>
> Q: Was it your understanding that Paramount could do so without breaching the contract with Viacom?
>
> A: Yes.

Small Dep. 72. In fact, there was no such right to terminate. Ex. 1, Section 8. And CEO Davis likewise was mistaken. See Davis Dep. 130-33 (also testifying that board's "fiduciary responsibility" required board have right to "leave the transaction").

Moreover, the Paramount board was given no information that could have allowed it to judge whether the $100 million break-up fee was reasonable. As one director testified:

> Q: Okay. Did you have any understanding of whether this $100 million break-up fee was reasonable compared to other transactions?

> A: I have no -- I would have no way of knowing what was reasonable or not reasonable.

Silberman Dep. 91-92. Likewise, one critical provision of the lockup stock option -- the provision allowing Viacom to pay most of the purchase price for the lockup stock option not with cash, but with a subordinated note -- was apparently not explained to the Paramount board. Silberman Dep. 92-93. Nor was the board told that this provision was highly unusual. Silberman Dep. 93; Small Dep. 193. Yet as Mr. Greenhill testified, in his 31 years' experience as an investment banker, he could not recall any transaction that had such a provision. Greenhill Dep. 4, 172.

Beyond this, no one at the September 9 or September 12 board meetings told the outside directors about, or discussed with them, many subjects that were vitally material to the transaction the directors were soon to approve:

-- No one told the board why a transaction with the same exchange ratio that had been rejected as "inadequate" in July was now being recommended. Davis Dep. 139.

-- No one told the directors what price numbers had been negotiated back and forth during the summer. Small Dep. 58.

-- No one told the directors whether it was Paramount or Viacom that had proposed the inclusion of the lockup stock option in the Paramount/Viacom transaction. Small Dep. 52.

-- No one told the directors whether Viacom would be willing to enter into a transaction without the lockups. Small Dep. 53-54.*

-- No one discussed with the Paramount board the desirability of obtaining a price collar for the Viacom stock in the proposed transaction. Small Dep. 95-96.

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* Understandably, the Viacom side felt a "market check" was not "relevant." Greenhill Dep. 78-79. They also deemed QVC's competing bids not "relevant" (id. at 185).

-- There was no discussion, despite the emphasis on Paramount shareholders retaining equity in the merged company, of the fact that Redstone had never been requested to bind himself not to cash-out that equity in a future merger (which, as a 70% stockholder, he could accomplish). Davis Dep. 112-13; Oresman Dep. 44-46.* At least one director viewed protecting the public stockholders from the future controlling stockholder as "I don't think a board should be expected to do that." Liedtke Dep. 118.

-- No one told the directors about Davis's meeting with Diller, or what was said at that meeting, or about Davis's belief that QVC had been readying a hostile takeover bid for Paramount. Silberman Dep. 54; Small Dep. 49-50, 240; Pattison Dep. 26-27. Davis testified that he did not even refer to QVC or Diller at either the September 9 or 12 board meetings, Davis Dep. 95-97, and could recall no discussion with the board of other potential acquirors.

-- No one told the board about Sumner Redstone's extensive open-market purchases of Viacom stock -- even though the stock's dramatic rise was the only reason why the new Viacom proposal was not worth less than the one rejected in July -- and even though the author of two reports on Redstone's purchases, as well as six recipients of those reports (none of them outside directors) were all present in the boardroom. Silberman Dep. 57; Small Dep. 100, 102; Pattison Dep. 65, 77. This was so despite Oresman's candid admission that Redstone's purchases "might" have had an impact on

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* Oresman's testimony is illuminating: he acknowledges that management was aware enough of the issue to have raised it in conversations with Redstone, but admits that Paramount <u>never</u> sought (let alone obtained) a binding commitment from Redstone to protect Paramount stockholders. Oresman Dep. 44-46.

Viacom's stock price, Oresman Dep. 81, and Lazard's earlier concerns to the same effect. Rattner Dep. 78.*

-- No one told the directors that Viacom had been willing in August to give up the lockup stock option in a transaction involving consideration of $69 per share -- virtually the same consideration on the table in September -- although persons present at that negotiating session were present in the boardroom. Silberman Dep. 54 ("It was only reported that each of these items [including the break-up fee] had been negotiated"); Small Dep. 192; Pattison Dep. 81.

-- There was no discussion about the preclusive effect of the lockups, Pattison Dep. 85-86; Small Dep. 229-30.

Whatever they did during the September 9 and September 12 board meetings, the directors did not ask any of the questions that mattered:

-- No director asked Davis or Lazard whether there was anyone else interested in acquiring Paramount. Silberman Dep. 50.

-- No director can recall if anyone asked whether Paramount stockholders would be receiving the best price available for their shares. Silberman Dep. 53; Small Dep. 122.**

-- No director asked whether Viacom was going to be paying the best price that could be obtained for the sale of voting control of the company. Silberman Dep. 79; Small Dep. 122.

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* Oresman's testimony (Oresman Dep. 75-76) that <u>he</u> raised the issue with the board is simply not credible in light of the other witnesses' testimony; the complete absence of contemporaneous documentation supporting his assertions; and management's decision not to show existing Lazard documents to the board.

** Davis, the Paramount CEO and chief negotiator, testified that he thought the September 12 Viacom offer (with an indicated value then of $69.14) was "the best possible deal from Mr. Redstone." Davis Dep. 120. This complacency, of course, proved misplaced -- Redstone would soon prove willing to offer over $2 billion more than the "best possible deal" Davis could obtain.

-- No director asked for any written description of the terms of the proposed merger agreement. Silberman Dep. 61.

-- No director asked for a written summary of the proposed stock option agreement. Silberman Dep. 61.

-- No director asked for any written presentation about stock options and break-up fees in other transactions. Silberman Dep. 61.

2. **Description of the September 12 Agreements**. Under the September 12 Paramount-Viacom merger agreement, Paramount was to be merged into Viacom in a single step, with Viacom to be renamed "Paramount Viacom International Inc."* Under the original merger agreement, each share of Paramount common stock was to be converted into the right to receive (a) one-tenth of a share of Viacom Class A Common Stock, (b) nine-tenths of a share of nonvoting Viacom Class B Common Stock, and (c) $9.10 in cash. The aggregate value of the deal at that point was $69.14 per share. Ex. 1 at P72579-80. The effect of the transaction was to transfer absolute voting control -- 70% -- over Paramount from the public stockholders to Redstone, since his private company would own 70% of the voting power of Paramount/Viacom. Davis Dep. 106-08; Oresman Dep. 38, 44; Rattner Dep. 57-58, 167; Dauman Dep. 102; Ex. 21 at P30828.

The merger agreement (Ex. 1) contained no price "collar" provision or other device that would protect Paramount stockholders from a decline in the value of Viacom stock prior to the closing of the proposed second-step merger. This omission was highly significant: in agreeing to forego a price collar in the original merger agreement, which contemplated a one-step merger, the Paramount board claims that it took comfort in the fact that its stockholders could -- and would -- turn the deal down if the "price of Viacom crater[ed]." Pattison Dep. 110-11.

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* Because the price of Viacom's Class A and Class B stock later dropped, the Viacom merger proposal was worth only $65.45 on October 24, 1993, three days after QVC announced its $80 tender offer for Paramount. Ex. 55 at P190223; see also Rattner Dep. 128 (during week of September 12, value of Viacom merger consideration dropped to $62).

The original merger agreement obligated Paramount to amend its "poison pill" to allow the merger to be consummated, and required Paramount to use its best efforts to secure stockholder approval of the merger. Paramount also agreed to withdraw its other structural defenses, agreeing to exempt the transaction from the provisions of 8 Del. C. § 203 and Article XI of Paramount's certificate of incorporation, which contains requirements for 80% supermajority voting approval of certain transactions. As detailed below, the original merger agreement contained no "fiduciary out" entitling Paramount to terminate the Agreement, even if Paramount were to be presented with a superior offer.

The original merger agreement, and the "Stock Option Agreement" executed with it (Ex. 2), contain provisions (the "Lockup Agreements" or "Lockups") that were plainly designed to "lock up" the transaction for Viacom. (The critical provisions of these Lockups are also incorporated in the new Lockups Paramount granted in the second Viacom merger agreed to on October 24.) They provide that, if Paramount is acquired by a company other than Viacom, (a) Paramount would pay Viacom $100 million in cash; and (b) Viacom would have the right, at Viacom's election, either to purchase 19.9 percent of Paramount's outstanding stock (23,699,000 shares) at $69.14 per share, or to receive from Paramount in cash a sum equal to (i) the amount by which the successful acquiror's price exceeds $69.14 per share, multiplied by (ii) the number of shares given to Viacom under the Stock Option Agreement, a total that would equal 16.7 percent of the amount by which the higher bid exceeds $69.14 per share.

The Lockup stock option provides that Viacom can choose to exercise the stock option by paying in cash only the par value of the stock -- a mere $1.00 per share, compared to the exercise price of $69.14 in order to exercise the option. As for the bulk of the option price, the remaining $68.14 per share, the Lockups allow Viacom to pay with a senior subordinated note of a Viacom subsidiary, Viacom International, Inc.* Thus, the

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* As Mr. Greenhill testified, this provision represented a "compromise" between Paramount's alleged desire for cash and Viacom's desire not to pay it. Greenhill Dep. 171.

buyer of Paramount gets diluted by 20% and finds only a note in Paramount's treasury. The result, at the present price of QVC's offer, is that the lockups are worth approximately $500 million to Viacom.

Section 8.05 of the Original Merger Agreement provided for the $100 million break-up "fee". This fee provision was retained in the October 24 amended merger agreement and remains in effect to this day. As a general matter, the fee is to be paid if the merger agreement is terminated either because of a competing bid or transaction, or because of a failure to obtain from Paramount stockholders the necessary approval of the merger agreement as a result of a competing bid. Ex. 1 at P72624-25.

The original merger agreement had no customary "fiduciary out" -- no provision allowing the Paramount board, in the exercise of its fiduciary duties, to terminate the agreement to accept a higher and better offer, or for that matter, to terminate under any circumstance at all prior to the Paramount stockholders' meeting. Rohatyn Dep. 26-27, 116 ("very onerous"). See Ex. 1 at P72622-23. The Paramount board bound itself to present the merger agreement to its stockholders -- regardless of whether a higher and better bid was made. Dauman Dep. 206. For Paramount's board, the only way out of the agreement short of a shareholders' meeting was to breach it. And that would trigger not only exercise of the Lockups, but possibly damages as well: The agreement expressly provided that "nothing herein" -- not even the exercise of the Lockups -- "shall relieve any party from liability for the willful breach of any of its representations, warranties, covenants or agreements set forth in this [Merger] Agreement." Ex. 1 at P72624.

As for the Lockup agreements, it becomes exercisable when the conditions for payment of the $100 million "fee" are met (e.g., if Paramount's board recommends a better offer), and may be exercised, at Viacom's discretion, "in whole or in part, at any time or from time to time" thereafter. Ex. 2 at P20073. Under the Stock Option Agreement, Viacom may also choose -- within 30 days of the consummation of, or the execution of an agreement for, a competing transaction (called a "Put Event") -- to receive a cash payment in lieu of exercising the option. Ex. 2 at P20080-81. The value of the option is calculated by multiplying the number of shares subject to the option by the difference between (a) the average closing price of Paramount stock during the five days preceding the Put Event, and (b) the option price, $69.14. Ex. 2 at P20081. (As will be described below, this provision was later amended to make it even more beneficial to Viacom.) The operation of this provision would allow Viacom to collect in cash -- on approximately 16.7 percent of Paramount's then outstanding shares -- any premium resulting from a higher takeover bid.

The purpose and effect of the Lockup Agreements are plain: they were intentionally crafted to block bids other than Viacom's from succeeding. The Lockups are designed to block competing bids by dramatically tilting the playing field in Viacom's favor: First, regardless of how they are exercised, the Lockups would impose a massive economic burden upon any competing offer,* by having Paramount give away $100 million plus 16.7 percent of the aggregate increase in price of offers that compete with Viacom's initial offer. If the Lockups are exercised, this value would forever be lost to anyone other than Viacom.

Second, by allowing Viacom to exercise its massive stock option by paying only a minimal amount of cash, the Lockups by their very existence threaten the value of any partial tender offer or stock-for-stock merger proposal that would compete with any proposal from Viacom. Viacom is entitled under the Lockups to receive 23,699,000 shares of Paramount -- which (as of the market close on November 10, 1993) are now trading at roughly $80.50 per share -- without infusing any more than $1 per share of cash into Paramount to pay for it. This right allows Viacom to threaten, for example, to exercise the option for 23,699,000 Paramount shares by paying less than $24 million in cash, and thus receive Paramount stock that would be worth $1.9 billion (assuming a price of $80.50 per

* Even Viacom's investment banker conceded that, in an endgame bidding situation when "the last dollar" is at stake, the stock option would make a difference. Greenhill Dep. 174.

share). And Viacom can then tender the shares into a partial tender offer and receive the tender offer consideration (here $80 in cash per share) for a prorated portion of those shares. That would substantially reduce the aggregate amount of cash available to be paid to the public, non-Viacom stockholders of Paramount.*

Importantly, the lockup not only punishes higher competing bids, but actually rewards Viacom for having made a lowball bid. Because the lockup rewards Viacom with a percentage of any value obtained above the announced value of its initial offer, it initially encouraged Viacom to offer as low a price as possible in order to increase the size of the spread between its bid and the topping bid that would determine its payoff.

3. **Paramount and Viacom Acknowledged That the Transaction Was a Sale of Paramount**. Paramount's minutes and the contemporaneous statements of Davis, Redstone, and others make abundantly clear that Paramount, Viacom, and their directors, officers and advisors, all understood that Paramount was being sold -- whatever their rhetoric about "strategic" merger and "fit." The minutes of the September 9 board meeting acknowledge that Lazard told the board that the transaction would be "done at a premium because of the sale of control." Ex. 12 at 4 (emphasis added). At a press conference on September 13, Davis, referring to Paramount, said that "we're being acquired" by Viacom. Ex. 22 at 21 (emphasis added). And on September 17, Davis signed a letter sent to stockholders stating that "Viacom will acquire Paramount" under the Original Merger Agreement. Ex. 24.

Moreover, the signing of the original merger agreement on Sunday, September 12, was accompanied by a joint Paramount/Viacom press release stating that

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* Alternatively, where a competing proposal involves a stock-for-stock exchange (such as is the case with QVC's proposed second-step merger), Viacom may exchange the 23,699,000 Paramount shares for the stock of the competing bidder (such as QVC), and then dump the competing bidder's stock into the open market -- thereby depressing the price of the competing bidder's stock. The mere threat that Viacom may do this would itself depress the value of the competing bidder's stock -- and would reduce the value of any stock-for-stock merger proposal that a competing bidder might offer.

> Viacom will acquire Paramount by exchanging each outstanding share of Paramount stock for 0.1 of a share of Class A Viacom common stock, 0.9 of a share of Class B Viacom common stock, and $9.10 in cash.

Ex. 21 at P30824 (emphasis added). The release further acknowledged that control of Paramount was being turned over to one man, Summer M. Redstone:

> Viacom has 53.4 million Class A voting common shares outstanding and 67.3 million Class B non-voting shares outstanding.
>
> Mr. Redstone's privately-owned company, National Amusements, Inc., currently owns approximately 76 percent of Viacom's common stock, on a combined basis. After the merger of Viacom and Paramount, Mr. Redstone, through National Amusements, will be the combined company's controlling shareholder, with a stake of approximately 69.8 percent of the combined company's Class A voting stock and approximately 38.5 percent of the combined company's common stock on a combined basis.

Ex. 21 at P30828 (emphasis added).

A joint preliminary Paramount/Viacom proxy statement filed on September 30 by Paramount and Viacom with the SEC, likewise echoed the fact that there was to be a sale of control of Paramount. It disclosed that the "premium" to be paid to Paramount stockholders was appropriate to reflect the fact that the proposed transaction involved a change in control of Paramount." Ex. 9 at V3354 (emphasis added).

In addition, Paramount and Lazard signed an engagement letter dated September 12 setting Lazard's fees. Ex. 52 at P30362. That letter makes clear that both Paramount and Lazard understood that the transaction contemplated in the Original Merger Agreement was a "sale" of Paramount. The engagement letter provided that Lazard would be entitled to a $3 million fee upon the execution of a definitive agreement for a "Sale." Ex. 52 at P30363. "Sale" was defined to mean

> a possible sale, in one or a series of transactions, of all or a substantial portion of the Company's stock or assets to Viacom Inc. ("Viacom"), or any substantially similar transaction or arrangement with Viacom, . . . or any other such sale, transaction or arrangement proposed by a party other than Viacom (a "Competing Transaction") prior to termination of any definitive merger agreement between the Company and Viacom . . . .

Ex. 52 at P30362. This fee has been paid. Ex. 7 at 15.

Redstone, too, understood that he was buying Paramount -- and proudly said so. On September 13, 1993, he sent a memorandum to all Viacom employees announcing just that. The first sentence of his memo stated that "I am thrilled to share with you the announcement that Viacom Inc. has agreed to acquire Paramount Communications Inc." Ex. 68 at V6893 (emphasis added). Two weeks later, he sent out another memorandum to his employees that led off with the statement: "since we were first able to share with you the exciting news that Viacom Inc. has agreed to acquire Paramount Communications Inc., massive media attention has been devoted to this historic merger." Ex. 68 at V6898 (emphasis added). And Smith Barney's fairness opinion to the Viacom board refers to the transaction as an "acquisition" of Paramount. Ex. 91 at SB3379.

4. Paramount Management Warns Off Potential Interlopers. On September 13, 1993, Viacom and Paramount held a joint press conference at which Redstone, Davis, and other members of their management teams appeared. Davis's and Redstone's comments at the press conference evinced an unrelenting effort and intent to deter and to defeat any potential third-party bids for Paramount, also reflected in many later statements. Redstone announced flatly that he and Davis would "guarantee" the Paramount/Viacom transaction would not be broken up. He described the proposed transaction as

> a marriage made in heaven. . . . But, as I noted this morning, unlike other marriages, which are subject to no-fault divorce laws, this marriage will never be torn asunder. Martin and I guarantee that.

Ex. 22 at 5; Ex. 67 at 4. In a separate interview, Redstone told a reporter that only a "nuclear attack" could break up the deal. Redstone Ex. 4.

On the day after the announcement of the Original Merger Agreement, Redstone called Malone of TCI to discourage Malone from making a bid for Paramount, and suggesting that Malone would be rewarded with other business opportunities if he refrained from such a bid. Malone Dep. 87-88.

Davis disingenuously downplayed to the press the possibility of another bid. In response to a reporter's question, Davis announced flatly that "I don't expect to receive any offers from either Mr. Malone or Mr. Diller, and have not." Ex. 22 at 13. But Davis knew better. And his financial advisors knew better, and have admitted as much:

> [p]rivately, both Redstone's and Davis's investment bankers saw the possibility of at least one bid. "We recognize that we're opening the door to other bidders. No question," Steven Rattner, a partner at Lazard Freres, told me. The biggest threat, he predicted, was likely to come from Diller and his allies. "They want a studio in order to claim its library and its capacity to produce product," Rattner said. "They know this is the last studio play -- until the Japanese get rid of their toys."

Ex. 81 (emphasis added).

Not surprisingly, the week after the announcement of the original merger agreement with Viacom at $69.14 was rife with speculation of an unsolicited bid from QVC or some other third party. E.g., Ex. 55 at P190169; Ex. 75. Determined to deter or to defeat such a bid before it could even be made, Davis and Redstone on September 16, 1993 issued a "Joint Statement" saying that

> Paramount and Viacom are absolutely firm in their belief that this combination will deliver the greatest benefits to stockholders and audiences around the world. No one else can give Paramount what Viacom has to offer. No one else can give Viacom what Paramount has to offer.

Ex. 83 (emphasis added). This statement was not reviewed or authorized by any of Paramount's outside directors before its release. Small Dep. 213-14.

On the morning of September 20, 1993, the Wall Street Journal reported that a bid from QVC was imminent. Ex. 76. Even before that bid was made, Davis and Redstone fired off a joint release that reads in part:

> No hostile takeover bid will be allowed to obstruct the well-considered and well-studied judgement of the Boards of Directors of Paramount and Viacom that the merger of the two companies will create for their shareholders a global media entity unparalleled in the entertainment world. Both companies are unequivocally committed to the consummation of this transaction.

Ex. 25 at P71836 (emphasis added). This statement also was never reviewed or authorized by Paramount's board or by the Executive Committee of Paramount's board before its release. Silberman Dep. 114; Small Dep. 213-14.

D. The September 20, 1993 QVC Proposal and Paramount's Response.

1. The September 20 QVC Proposal. On September 20, 1993, only eight days after the signing of the original merger agreement, QVC delivered a letter to Davis proposing to negotiate an acquisition of Paramount valued at approximately $80 per share, or $9.5 billion -- $2 billion more than the eight-day-old Viacom deal. QVC stated that:

> The QVC Board of Directors has authorized a combination of our two companies in a merger in which each of Paramount's outstanding common shares would be converted into .893 shares of QVC common stock and $30 in cash (which, based on the September 20, 1993 QVC closing market price, would have a value of $80 per Paramount share). Our proposal represents a premium of approximately 14.9% over the $69.625 closing market price of Paramount common stock today, and 26.6% over the $63.175 value of the Viacom transaction today.

Ex. 39 at V1297. The letter added that QVC's financial advisors had assured QVC that "all of the financing for our proposal is readily available," and concluded by stating that "[w]e and our advisors are available to meet with you and your Board and advisors at any time to discuss our proposal and to answer any questions you may have." QVC stated it was ready and willing to negotiate a customary merger agreement at a price $2 billion higher. Ex. 39 at V001297-1300.

Paramount responded to QVC's letter by promptly issuing a press release that yet again evinced hostility toward any and all competing bids. The release stated:

> Our agreement to merge our company with Viacom represents our Board's considered judgement that the combination would fulfill our long-term strategic plan for maximizing shareholder values. We believe that a Viacom merger provides the best fit for the growth of our businesses. However, the Board of the company will, in fulfillment of its responsibilities, evaluate the QVC proposal.

Ex. 26 (emphasis added).*

Paramount also responded to the QVC offer by scheduling a board meeting for September 27, 1993. Before that board meeting, QVC delivered a letter to Davis and

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* Viacom's reaction to the QVC offer was initially "to scoff at it." Dauman Dep. 70. As noted below, however, Viacom eventually raised its bid by approximately $2.5 billion to compete with QVC.

the directors of Paramount informing them unequivocally of the availability of financing for QVC's tender offer. The letter stated:

> The QVC offer is not subject to any condition with respect to financing. QVC will enter into a merger agreement that does not contain any condition with respect to financing. There is no question as to the financing of the QVC offer. We have commitments for $1 billion in new equity. We have the assurance of Allen & Company that the financing for our offer is available. Indeed the financial markets show that there are no doubts about our offer -- QVC shares have risen from $56.00 when we made our offer to $60.75 on Friday [September 23]. At Friday's price, our offer is worth $84.25 for each Paramount share.

Ex. 40. The QVC September 26 letter concluded as follows:

> We are prepared to meet with you, your board and your advisors to answer any questions you may have. We are prepared to enter into a customary merger agreement without any contingencies that would make the terms of our offer less favorable to Paramount than the agreement you entered into with Viacom.

Ex. 40. Meanwhile, on September 21, 1993, Viacom and Paramount filed Premerger Notification and Report Forms with federal regulators, pursuant to the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (the "H-S-R Act"). This set in motion a thirty-day waiting period, after which -- barring any further informational requests by regulators -- the Paramount/Viacom merger could be allowed to proceed under the federal law. Ex. 6 at 37.* The H-S-R Act waiting period can begin to run <u>only</u> if there exists a signed merger agreement or a pending tender offer: otherwise, the government will not accept a filing for review. The Paramount side well understood the timing advantage they had given Viacom. Rohatyn Dep. 92-93.

2. **<u>Paramount's September 27, 1993 board meeting</u>**. Paramount's board discussed the QVC offer at a special board meeting on September 27. Ex. 14. Davis presided. Davis began the meeting by reading from a prepared script. Silberman Ex. 12;

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* In addition, on September 23, Viacom filed an action in the United States District Court for the Southern District of New York against TCI, QVC, and others, alleging, among other things, that an acquisition of QVC would violate federal antitrust law. Ex. 6 at 40-41. At a Paramount board meeting, even Davis later expressed justifiable skepticism about the merit of the suit, noting that "[t]here is general agreement that the suit will not derail the QVC offer." Ex. 15 at P31487.

Silberman Dep. 123. He briefly described the QVC offer, noting that the QVC proposal had a market value of $83.80 on Friday, September 24; the Viacom offer, he added, had a market value of $65.45 as of that day. Ex. 15 at P31487.

Given that the original merger agreement allowed Paramount to talk to competing bidders who did not have material financing contingencies, and given that QVC's offer was not subject to such a contingency, the fact that QVC's bid was superior by $17.35 per share should have been enough to allow Paramount to talk to QVC even under the restrictive no-shop clause of the Original Merger Agreement. Various press reports, indeed, quote Paramount representatives as stating that Paramount had no doubt QVC could and would obtain the necessary financing. Reuters quoted Davis as saying, "I would expect that QVC would obtain financing. They are professional people." Ex. 80 (emphasis added). The Wall Street Journal quoted a Paramount advisor as saying that "we fully expect that within a few days QVC will manage to satisfy us in the financing issue and we will be in auction mode." Ex. 79 (emphasis added); see also Ex. 78 (according to "executive close to Paramount," "`[t]here is no doubt in my mind that the [QVC] bid is eminently financeable'").

What Davis told the press was one thing; what he told his board, quite another. The merger agreement had said nothing about requiring bidders to provide "evidence of financing", but Davis told his board that the agreement required QVC to provide just that. Reading from his prepared script, Davis said:

> 11. Under the terms of our merger agreement with Viacom, we are prohibited from having discussions with QVC or any other party unless they satisfy certain conditions, the principal one of which is evidencing [sic] that its proposal is not subject to financing.
>
> 12. Although not contained in its original letter Sunday afternoon, we were advised by a new letter that QVC's proposal is not subject to financing.
>
> 13. The letter contains mere assertions, not evidence that QVC has financing lined up.

14. We plan to tell QVC just that.

Ex. 15 at P31487-88.

Davis noted that Redstone had not said whether he would "raise his bid," but said that nonetheless "[w]e expect him to come back with a higher bid." In addition, Davis noted that Paramount had been contacted by another potential bidder, BellSouth, which had informed Paramount and Viacom that it was interested in acquiring Paramount, part of Paramount, or part of a combined Paramount/Viacom entity. Davis said that NYNEX had also expressed an interest in acquiring Paramount, and that "[t]here is always a possibility that others may appear." Still, Davis told Paramount's Board of Directors that "[w]e are continuing to proceed with the Viacom merger." Ex. 15 at P31488-89.

The directors were given a Lazard book that contained information about QVC, its stock, and its proposal to acquire Paramount. Ex. 55; Silberman Dep. 124. This book confirmed the superiority of the QVC proposal, which Lazard valued at $83.80 per Paramount share -- some $18.35 more than the $65.45 per Paramount share offered by Viacom. Ex. 55 at P190223. QVC's proposal, Lazard noted, offered a 10.8% premium to the market price on September 24, while Viacom's bid represented a 13.5% <u>discount</u>. Ex. 55 at P190223. One director admits that, at this point, he fully recognized that Paramount stockholders would reject the proposed merger with Viacom. Silberman Dep. 132.

Despite this obvious fact, none of the directors bothered to question Davis's proposed course of action -- or the decisions that had locked the Paramount board into an inferior transaction its stockholders would never approve:

-- No director raised the issue of whether Paramount should proceed to have discussions with QVC. Silberman Dep. 142-44.

-- No director expressed any criticism of Davis for having locked Paramount into the inferior Viacom deal. Silberman Dep. 128.

-- No director discussed the effect of the lockups on a competing bid such as QVC's. Silberman Dep. 136-37.

-- No director discussed the effect of the charter's supermajority voting provision on a competing bid such as QVC's. Silberman Dep. 137.

In short, the Paramount directors once again did not dare to question Davis; once again, they did just as they were told. As Davis was later to note, Paramount's board was "functioning in <u>lockstep</u>." Ex. 35 at 21.

After the meeting, Paramount announced that it would refuse to consider the merits of the QVC offer, to enter into negotiations about it, or even to discuss it with QVC -- for the supposed reason that "satisfactory evidence of financing" for the QVC offer had not been presented, a prerequisite that was <u>not</u> called for even by the terms of the tight "no shop" in the merger agreement. Davis issued the following statement to the press in his own name:

> 1. We have a signed merger agreement with Viacom.
>
> 2. It is the best strategic fit for Paramount.
> It provides the greatest L/T growth potential for our shareholders
>
> and
>
> We are proceeding with the Viacom transaction.
>
> <u>We believe in it</u>.
>
> <u>We are committed to it</u>.
>
> Consistent with our legal obligations - we will consider the QVC offer if and when we have satisfactory evidence of financing.
>
> If we ever get into discussions with QVC, we will have other business concerns that go beyond the threshold issue of financing.
>
> In any case we will conduct ourselves in a thoughtful, responsible, deliberate way.

Ex. 28 (emphasis in original). But Davis well knew QVC could obtain financing -- as noted above, he had publicly said so. Davis Dep. 235-36. Thus, from the standpoint of the interest of Paramount's stockholders, there was nothing to be lost by holding discussions with QVC even in the absence of written evidence of financing. The only purpose served by Davis's statement was to create delay and to require QVC to incur substantial costs in commitment fees to its banks.

3. **<u>Paramount's October 11, 1993 Board Meeting</u>**: After Paramount refused to open discussions with QVC, QVC proceeded to obtain bank financing commitments, for which it paid substantial amounts. On October 5, 1993, QVC delivered to Paramount proof of its financing: $1 billion in preferred stock, and $3 billion in bank financing. Ex. 17 at P31499. QVC once again asked that merger negotiations begin. Ex. 5.*

But Paramount, at Davis's behest, continued to stall. It held another special board meeting on October 11. Again, Davis used a script -- one that was produced in discovery only after being heavily redacted. Davis announced that Paramount's management had engaged the consulting firm of Booz, Allen & Hamilton to assess the "incremental earnings potential" from mergers with Viacom and with QVC. Ex. 17 at P31495-97. Davis next recounted some recent developments. Then, according to Davis's script, Davis turned "to the reason for today's meeting -- consideration of the adequacy of the evidence of the QVC financing." Ex. 17 at P31498.

The script reveals that Davis described the package of financing materials. Ex. 17 at P31499. The next two and one-half pages of the script were redacted by Paramount's lawyers. Ex. 17 at P31499-501. The next two paragraphs, after the redactions, read:

> 24. Therefore, under the terms of the Merger Agreement, we are free to open discussions with QVC.
>
> 25. The Merger Agreement does not require us to further explore the QVC proposal.

Ex. 17 at P31501 (emphasis added).

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* Paramount later gave QVC's financing documents to Viacom, so that Viacom could try to find holes in them. Dauman Dep. 251-52.

Then, after a few more paragraphs, and a few more redactions, the script reveals that discussion, Davis stated -- without asking for discussion -- that "we are proceeding with our merger with Viacom under the terms of the Merger Agreement." Ex. 17 at P31503. And then, according to the minutes, the following resolution was adopted:

> Resolved, that, in accordance with Section 6.02 of the Merger Agreement between the Corporation and Viacom, <u>the Board of Directors has determined that it is necessary to authorize management to enter into discussions with QVC Network, Inc. with respect to its proposal</u>.

Ex. 7 at P31506 (emphasis added).

Thus, the Paramount board finally recognized on October 11 that its fiduciary obligations under Delaware law <u>required</u> it enter into discussions with QVC. That is confirmed in the SEC Schedule 14D-9 later filed in response to Viacom's subsequent tender offer. That Schedule 14D-9 expressly admits that, by October 13, Paramount's board had made findings that

> (i) the QVC Proposal was not subject to any material financing contingency and (ii) that such discussions [with QVC regarding the QVC Proposal] <u>were necessary for the Board to comply with its fiduciary duties to the Paramount stockholders</u>.

Ex. 7 at 14 (emphasis added).

However, the October 11 board resolution for negotiations was never implemented. Management invented and imposed a brand new condition for merger talks to begin. On October 13, Paramount demanded that QVC supply documents and respond to a lengthy series of questions concerning QVC's business, finances, sources of funds, and other items. Ex. 7 at 14; Ex. 41. On its face, this strategy was an effort by Davis and his management team to play for time -- to delay any serious consideration of QVC's offer in the hope that the investment community would view QVC's offer as doomed by Paramount's intransigence, and in the hope that QVC would give up.

On October 13, when it made its request for information from QVC, Paramount delivered to QVC a form of confidentiality agreement that would protect Paramount's confidential information from disclosure. Ex. 95. QVC promptly executed and returned the confidentiality agreement, and sent Paramount a reciprocal and virtually identical form agreement for QVC's benefit, an agreement that would enable QVC to provide confidential information to Paramount. Ex. 94. Paramount -- the same company that had investigated, negotiated and executed the merger agreement in five days -- took seven days (until October 20) to return the simple form confidentiality agreement. Ex. 5 at 18. Meanwhile, the H-S-R Act waiting period was running for Viacom, but could not even start for QVC.

On Wednesday, October 20 -- the same day Paramount returned the signed confidentiality agreement -- QVC provided the requested documents and answered the questions propounded by Paramount. Ex. 5 at 26. Also that day, QVC delivered to Paramount a letter informing Paramount that representatives of QVC were available for negotiations at any time on Wednesday, Thursday, and Friday, October 20 through 22, and asking Paramount to confirm that Paramount was prepared to enter into good-faith negotiations and to arrange a meeting as soon as possible. All Paramount would say in response was that it would "be in touch." Ex. 43; Ex. 45.

E. The QVC Tender Offer

In light of Paramount's unwillingness to open serious negotiations with QVC despite QVC's stated desire and ability to pay approximately $2 billion more in value than Viacom, QVC on Thursday, October 21, 1993 announced a tender offer for Paramount shares and filed this action. QVC announced that it would offer $80 in cash for 51% of the Paramount shares outstanding, to be followed by the acquisition of the remaining Paramount shares in an equal-value second-step merger. Ex. 5 at 1-2. The QVC tender offer was even more attractive than QVC's September 20 proposal -- the cash portion of the consideration was increased by approximately $1.2 billion. At stock market closing prices on October 20, 1993, the value of the proposed second-step stock-for-stock merger was $80.71 per Paramount share, and the aggregate value of the QVC tender offer and merger proposal was approximately $9.5 billion -- approximately $2 billion in excess of the initial Viacom deal.

F. Paramount's October 24, 1993 <u>Board Meeting</u>

What Paramount's board did next was absolutely extraordinary -- extraordinary in light of its conclusion that its fiduciary duties required it to negotiate with QVC; and extraordinary in light of the directorial duty of care that is a first principle of our corporate law.

1. <u>The Saturday Negotiations</u>. Even though QVC had stated that it was willing at any time to discuss its proposal with Paramount, Paramount made <u>no</u> effort to contact QVC. Instead, it responded to QVC's $2 billion-higher offer by furiously negotiating with Viacom on the morning of Saturday, October 23. Ex. 6 at 19. Viacom proposed to Paramount that the original merger agreement be amended to provide for a two-step transaction in which the first step would be a tender offer by Viacom for <u>43.75%</u> of Paramount's outstanding shares at $80 per share in cash. Ex. 6 at 19. Viacom also proposed that Paramount amend its poison pill to permit the consummation of Viacom's proposed tender offer, but not to amend the pill to permit consummation of an offer by any other bidder. Viacom's revised proposal retained most of the other provisions of the original merger agreement -- including the Lockup break-up fee and stock option. Ex. 18 at P31511. Paramount gave no consideration to using this opportunity to re-negotiate the unfavorable terms of the September 12 agreement. Mr. Davis testified that "I didn't even think of" rejecting Viacom's request for a revision of the merger agreement on October 23, and could not recall any consideration given to insisting that Viacom modify any provisions of the September 12 merger agreement. Davis Dep. 176-77.

The thinking of Paramount negotiators during the October 23 negotiations is reflected in a set of typewritten notes made on Oresman's typewriter. Ex. 92 at L007428-30; Oresman Dep. 128-29. These notes were produced in discovery by Lazard -- but Paramount's copies were apparently destroyed, and never produced. Oresman Dep. 129-30.

Oresman testified that the notes reflected the thinking of Paramount's management and the Lazard negotiators. Id. at 128-29, 134. The notes make clear that Paramount understood that Viacom's proposed 43% tender was potentially highly detrimental to stockholders. The notes read in part as follows:

> 2. . . . [T]here are onerous conditions that eliminate the assurance that the [Viacom] $80 package will stay in place as well as preclude a higher bid by QVC:
>
> > 1) We have to agree under the merger agreement to a coercive tender offer at the 43% level. Even worse than 51% tender, this stampedes stockholders to take front end. Back end may be worth a lot less.
> >
> > 2) Our pill was designed to protect against coercive two tier tender offers.
> >
> > 3) So is fair price amendment.
> >
> > 4) Viacom is asking us to pull the pill for it but for no one else.
> >
> > 5) The result is that if a higher offer were made by QVC, we would be precluded from giving our shareholders the benefit of it by our agreement not to pull the pill.
> >
> > 6) While QVC is blocked by us, Viacom can take whatever shares that come in -- and they'll come in because the QVC offer can't be consummated.
> >
> > 7) It is entirely possible that Viacom can get enough shares so that QVC can never prevail, no matter what its bid.
> >
> > 8) Under Viacom's new proposal, if Viacom doesn't get 43%, it can exercise its breakup fee and option by terminating the agreement.
> >
> > 9) Viacom also has the right not to complete the merger agreement if the tender offer fails.
>
> 3. The most prudent position is to keep the poison pill in place for everyone.

Ex. 92. (emphasis added). (This document was not given to the Paramount board. Davis Dep. 171-73.)

Despite these concerns, no one at Paramount expressed any opposition to Viacom's 43% proposal. Davis Dep. 168-69 ("quite sure of that."). In fact, Paramount agreed to 43% and the next day Lazard opined on 43%. Rohatyn Dep. 119. Paramount's negotiators certainly did not take the opportunity offered by Viacom's desire to proceed with a much-altered deal by seeking substantive improvement in the transaction. According to Redstone, Viacom had "acceded to just about everything that Paramount asked for" in the mini-negotiations of October 23-24 (Redstone Dep. 223); Davis simply never asked for the things that would benefit the stockholders.

2. **Paramount's October 24 board meeting**. In the late afternoon of Friday, October 22, board members were alerted that their presence was required at a special board meeting called for 9:00 a.m. Sunday, October 24. Only the briefest description of the subject of the meeting was provided to directors. Small Dep. 210 (Davis "did not give me the specific facts.")

The board assembled Sunday morning at the offices of Simpson Thacher. At that time Viacom's new proposal was still in flux -- the board was initially presented with a proposal for a Viacom tender offer for 43.75% of the shares of Paramount.* Davis presented Viacom's new proposal. He portrayed it as having two substantially attractive structural provisions that were not present in the September 12 agreement, and relied heavily on these two new provisions to urge approval by the independent directors. A substantial portion of the minutes of the October 24 meeting is devoted to a description of these two items. Ex. 18. However, the Paramount insiders misled the independent directors as to the significance of these provisions and the outside directors had, in any event, too sketchy an understanding of the deal structure to comprehend them.

The first item Davis said was changed in the structural provisions of the agreement was Viacom's agreement that Paramount "would permit the consummation of the Viacom offer only if, at the time that Viacom was prepared to accept shares for payment, it was consistent with the Board's fiduciary duties." Ex. 18. As Davis concluded, "[t]hat would allow the Board to accept a better offer." Id.

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* So hurried was the drafting of the Amended Merger Agreement that, in defining the term "Merger" in the agreement, Viacom and Paramount "agree[d] to promptly amend this Agreement subsequent to the execution and delivery thereof to provide for more precise defined terms and usage thereof." Ex. 3 at V1222.

But Davis did not tell the board the whole story about the new pill amendment provision. The October 24 amendment exacted a significant concession from Paramount that purports to come into effect if that "out" is exercised. Newly-added § 3.13(c) of the merger agreement provides that if the agreement is terminated by Paramount in the exercise of its "fiduciary out" (i.e., under § 8.01(i)), then -- notwithstanding that termination -- Paramount remains obliged to redeem its Rights Plan in favor of Viacom's tender offer, and to continue to approve that tender offer under 8 Del. C. § 203 and the supermajority provision of the Paramount charter.* In short, Paramount agreed in advance -- and regardless of what other offers are outstanding -- to pull its pill for Viacom from the moment it exercises its "out" and from then on, i.e., to stand defenseless as to Viacom regardless of whether that posture is, or is not, in the stockholders' best interests.** Needless to say, there is no mention of this unique provision in the board minutes, and none of the Paramount directors were advised of it when they voted to approve the amended merger agreement. Ex. 18; Oresman Dep. 156-58; Pattison Dep. 204-05.

Following his misleading reference to the pill amendment provision, Davis "pointed out that Viacom agreed to permit the Company to terminate the Merger Agreement whenever it decided to withdraw or modify its recommendation of the Viacom proposal in the exercise of its fiduciary duties. Previously the Company had no ability to terminate until after the stockholders' meeting was held." Ex. 18 at 2. Here Mr. Davis was correct. But what was being described to the board as one of two major improvements Viacom had consented to was in fact nothing of the kind -- Paramount's previous agreement to submit even a proposal its board could not recommend to Paramount's shareholders was a nullity (see Smith v. Van Gorkom, Del. Supr., 488 A.2d 858, 888 (1985)), and Viacom hardly

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* The same obligation applies if Viacom terminates the merger agreement because the Paramount board has changed its recommendation of the Viacom acquisition or recommended a "Competing Transaction" or other tender offer (or because anyone acquires more than 15% of Paramount stock). See Ex. 3 at V01216-17.

** Viacom thus has greater rights as against Paramount's pill if the merger agreement is terminated than if it is not.

made a real concession when it gave it up. On this basis -- a pill amendment provision that was in some ways worse than the original and a change in the fiduciary out that gave away nothing the law did not already prohibit -- Davis asked the Paramount board to approve a tender offer for 43.75% of Paramount's shares followed by a second-step merger.

Lazard then made a presentation concerning the "fairness" of the Viacom offer. While there is no written Lazard opinion for the October 24 Viacom proposal, it is clear from the minutes that Lazard's opinion was limited to the fairness of Viacom's offer and does not address the comparative merits of the QVC offer, i.e., Lazard did not opine that the Viacom offer was "fair" in view of the competing $80 per share offer from QVC.* Oresman Dep. 137.

Lazard's presentation did not take the form of a traditional financial advisor's "board book," apparently because Paramount did not think a written Lazard presentation was "important" for this board meeting. Oresman Dep. 111. Instead, the directors had (a) a one-page summary of the revised proposal; (b) 10 pages of material prepared by Smith Barney (Viacom's banker) describing Viacom's offer; and (c) 7 pages of Lazard material describing the QVC proposal and setting forth "hypothetical incremental value" analyses for both Viacom and QVC. Ex. 90 at P190248-51. These analyses show that Lazard believed that both Viacom and QVC could increase their offers significantly above $80.00 within the limits of their existing bank financing. Id. at P190248, 251.**

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* The fact that Paramount's negotiations had viewed the 43% Viacom tender as "even worse" than the QVC tender offer (Ex. 92) on October 23 demonstrates the limited nature of what Lazard was opining to on October 24. Defendants' counsel blocked testimony from Mr. Rohatyn of Lazard on the subject of whether Lazard has been asked to perform a comparative analysis of the QVC and Viacom bids since October 24, opinion, claiming a "strategy privilege" with respect to such testimony. Rohatyn Dep. 87-88.

** According to the Lazard document prepared for the October 24 meeting, the QVC proposal was then worth $79.11 per Paramount share and the revised Viacom proposal was worth $75.00 per share plus a $5.00 face value preferred stock which was not valued for trading purposes. Ex. 90. Lazard was able to achieve this calculation by (a) ignoring the likelihood (as actually occurred) that Viacom's stock price would drop after announcement of the higher offer; and (b) assuming that the Viacom convertible preferred to be issued in the second step would trade at face value. Ex. 90; Rohatyn Dep. 75.

Following the Lazard opinion, a note was brought in indicating that Viacom was prepared to buy 51% of Paramount in its tender offer. Ex. 18 at 3. No explanation was given as to why Viacom had agreed.

Next, management invited Michael Wolf of Booz-Allen & Hamilton to present a document entitled "Shareholder Value Creation Through Merger", that purported to quantify the cost savings and potential additional business revenues available from a Viacom merger as compared to those available in a QVC merger. Ex. 86. This report did not purport to compare the value to stockholders of the Viacom offer as compared with the QVC offer. In all events, the report is entitled to little, if any, weight: Under "Methodology", Booz-Allen describes this report as a "first cut." Ex. 86 at P190266. Mr. Wolf is not trained as a financial expert (Wolf Dep. 27-29); Booz-Allen is not a financial advisory firm; and it does not give opinions as to fairness or financial value. Wolf Dep. 16-19. Paramount has nowhere mentioned Booz-Allen in its public filings concerning either tender offer, as would be required by federal law if the board were relying on Booz-Allen's advice. Ex. 7 at 14-16.* Financial advisor Lazard was never asked to provide, nor did it provide, any opinion as to the relative values to stockholders of the respective Viacom and QVC offers that were on the table. Rohatyn Dep. 87-88.

The Paramount board then, after unspecified discussion, approved the new merger proposal. Paramount treated the October 24 proposal as if it were a minor modification of the existing transaction. Oresman Dep. 107-08. But in fact the change was enormous -- under the October 24 proposal, more than 51% of Paramount's equity would be cashed out, and a "free" shareholder vote would be replaced by a coercive two-tier tender offer. However, the discussion on October 24 did not include any consideration of

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* The board, moreover, was not told that Booz-Allen was currently performing other work for Paramount (for which it had been paid approximately $750,000) (Wolf Dep. 36); nor had the board approved the retention of Booz-Allen for the purpose of rendering advice on the Viacom/QVC alternatives. Small Dep. 97. Finally, although Booz-Allen did rely on non-public Viacom information made available to it by Paramount management (Wolf Dep. 56-57), Booz-Allen did not look at the non-public QVC information that Paramount had received from QVC on October 20. Wolf Dep. 47-48.

how Viacom's switch from a merger to a tender offer proposal affected the key presuppositions on which the board acted on September 12. First, the board on September 12 was willing to agree to a deal without a "collar" on Viacom's stock price because -- if Viacom stock fell too far in the interim between announcement of the deal and the shareholder vote -- the shareholders could reject the merger. The tender offer undercut this reasoning, since 51% of the Paramount equity could be purchased after 20 business days while the remainder would eventually be exchanged for Viacom shares whose market value might by the time of the second-step merger have dropped precipitously. The board did not discuss this issue with its advisors on October 24, nor did management or the advisors seek to obtain any price protection for the second-step.

Second, the concerns the board should have had on September 12 about Viacom's stock price should have been heightened in view of the October 24 proposal. The September 12 proposal, as a stock-for-stock merger, did not require Viacom to incur huge debt or leverage its assets. The October 24 Viacom proposal, with a 51% cash first step, required Viacom to borrow more than $3 billion and sell $1.8 billion in preferred stock. Ex. 6. These moves put enormous pressure on Viacom's balance sheet, thus increasing the likelihood that Viacom stock would fall in price from the heights it had reached in August. This point was not made in the discussion at the board meeting on October 24. It is not hard to find the reason why the Paramount directors had so little information on which to act. Paramount management simply does not believe that the board needs to be informed. As Davis testified in a moment of candor:

> Q: And now [on October 24] you had a bid from QVC, is that correct?
> A: QVC made a hostile bid.
> Q: And you now had Viacom coming forward and saying that they wanted to revise the deal and they wanted to do a front-end cash tender offer, et cetera; is that correct?
> A: That's correct.
> Q: And assuming that there was no Lazard book available for the board at that meeting, do you have any explanation to offer for that?
> A: No, I don't have any explanation, nor do I understand why they would even need one.

Davis Dep. 167 (emphasis added).

3. **The Amended Merger Agreement**. The amended merger agreement between Paramount and Viacom was signed on October 24, 1993, after the board meeting that day. Under that agreement, Viacom agreed to make a tender offer for 60,437,023 shares (approximately 51 percent of the outstanding shares) of Paramount at $80 per share -- the same price QVC had announced it would offer. Ex. 3 at V1156. Consummation of Viacom's tender offer is to be followed by a second-step merger of Paramount into Viacom, with Viacom being the surviving entity. In the second-step merger, Paramount's common stock is to be converted into the right to receive (a) 1.08317 shares of nonvoting Viacom Class B common stock, (b) 0.20408 shares of Viacom Class A common stock, and (c) 0.20408 shares of a new series of Viacom convertible exchangeable preferred stock -- exchangeable at Viacom's option into debt. Ex. 3 at V1160. (If Viacom's tender offer is not consummated before the merger is closed, Paramount stockholders are to be allowed to elect, subject to proration, whether they wish to receive cash or the package of stock.) As noted above, Paramount and Viacom asserted that the per share value of this package of stock was $80 as of the close of the stock market on Friday, October 22, 1993 (although, again, this assumed that the new preferred stock would trade at the face value). Like the original merger agreement, the amended merger agreement bound Paramount to use its best efforts to secure stockholder approval for the amended merger agreement, and required Paramount to amend its "poison pill" and to remove other structural defenses so that the Viacom tender offer and merger could proceed. Ex. 3.

In addition, as noted, Paramount once again granted Viacom lucrative lock-ups that would impede competing bids. Thus, the new Viacom merger agreement still contained the $100 million break-up fee -- payable upon termination under the same circumstances under which the break-up fee had been payable under the Original Merger Agreement, and under certain additional circumstances.

Likewise, Paramount once again granted Viacom a massive lockup stock option -- indeed, the option was actually enhanced from Viacom's standpoint: The topping bid price that would determine Viacom's payoff if it were to opt to receive cash instead of the option stock was changed to the greater of either (a) a five-day average price of Paramount stock or (b) the offer price in any competing tender offer (such as QVC's) for Paramount stock. This amendment guaranteed to Viacom that, if it did not become entitled to exercise its lockup stock option before the consummation of a competing tender or exchange offer, it could still reap the benefit of that offer.

Finally, even though it had refused to talk with QVC without evidence of financing, the Paramount board entered into the amended merger agreement and regranted the lockups even though Viacom did not have financing commitments for its tender offer, and that offer was made subject to obtaining the required financing. Dauman Dep. 231-32.

In short, for a transaction that (at best) was the equivalent of QVC's, the Paramount board once again granted lockups worth at least $350 million to Viacom -- while not even bothering to find out whether QVC might once again make a higher and better bid. Indeed, at this point, by consistently stonewalling QVC's overtures while hurriedly negotiating with Viacom, Paramount greatly enhanced Viacom's regulatory and timing advantage. In the words of one arbitrageur quoted in the New York Times, "Time is on Viacom's side. If the offers are roughly the same, I would tender to Viacom." Ex. 82.

On Monday, October 25, the day after the signing of the Amended Merger Agreement, Viacom filed an SEC Schedule 14D-1 launching its tender offer, and Paramount filed a Schedule 14D-9 recommending that its stockholders tender into the Viacom Offer. The directors were not shown the Schedule 14D-9 before it was filed and sent to stockholders. Small Dep. 170. The Schedule 14D-9 stated that the Amended Merger Agreement reflected "the best available alternative for Paramount, its stockholders and its constituencies." Ex. 7 at 15. This statement impliedly represented that the Paramount board had an informed basis upon which to reach this conclusion. The Paramount board plainly did not have such an informed basis, having never engaged in discussions with QVC, and having never made any investigation as to whether QVC could or would in fact offer a better alternative to that of Viacom's new bid.

The Paramount Schedule 14D-9 was misleading in another way as well. In asserting that Viacom's bid was the best available alternative, Paramount stated in its Schedule 14D-9 that its "Board [had] reviewed and considered, to the extent of available information, the QVC Proposal and the QVC Offer." Ex. 7 at 15. This statement, too, was misleading, since more information about QVC's bid clearly was "available" -- it was Paramount's for the asking if Paramount negotiated in good faith. Ex. 7 at 15.

G. The Aftermath of the October 24 Paramount/Viacom Agreement

Davis and Redstone appeared at a celebratory press conference on October 25 to announce the amended merger agreement. Together they looked and sounded triumphant; the New York Times the next day carried a picture of Davis and Redstone, their hands clasped and raised in a sign of victory. Ex. 83. They clearly believed that they had won.

Once again, Redstone described the Paramount/Viacom merger as "a marriage made in heaven, and take my word for it, it won't be torn asunder." Ex. 35 at 2. He described the amended merger agreement as "a step that demonstrates our unwavering commitment and determination and perseverance." Ex. 35 at 2. For his part, Davis described a transaction between Paramount and any other company as "unthinkable." Ex. 35 at 9 (emphasis added). And he emphasized to the press that "we [Paramount] have a board that is functioning in lockstep." Ex. 35 at 21 (emphasis added).

In announcing the new transaction on October 24, Paramount and Viacom made clear that they understood themselves to be in a bidding contest. They said in a joint press release that their amended merger agreement was executed "[i]n response to a tender offer announced by QVC Network, Inc." Ex. 32. Still, consistent with Davis' intransigent public statements, Paramount and its board continued to refuse to negotiate with QVC or to conduct a fair sale process for the company that the Paramount board had twice agreed to sell.

Viacom's tender offer commenced on Monday, October 25; the documents for that offer were prepared in such a hurry that Paramount's Schedule 14D-9 had to be restated and reissued in its entirety to correct material mistakes. Compare Ex. 7 with Ex. 88. QVC commenced its tender offer on October 27.

On October 28, 1993, QVC sent a letter to the Board of Directors of Paramount, requesting once again that negotiations begin. The letter emphasized that QVC's "goal is, and has always been, to negotiate with the Paramount Board of Directors on a level playing field in order to ascertain whether we could achieve a transaction that is the best available for the Paramount stockholders." Ex. 46. The letter was addressed to the Paramount Board of Directors, and was sent to Paramount's corporate headquarters, but Paramount's directors (at least its outside ones) never saw it; the letter was intercepted by management and not given to members of the board. Small Dep. 137-38; Pattison Dep. 227. According to one director, QVC's requests on October 28 to begin negotiations "kind of amused the entire board" who "kind of laughed about it," choosing to deem it a "tactic" to justify a tender offer. Liedtke Dep. 92.

Representatives of Paramount responded by agreeing -- finally -- to meet face-to-face with representatives of QVC. Ex. 47. The meeting took place at Paramount's headquarters on the morning of November 1. It lasted seven and one-half minutes. At the meeting QVC presented Paramount's representatives with a list of proposed guidelines for a fair bidding process. Those guidelines read as follows:

> 1. Paramount will provide the same information about its business and operations to QVC as it has previously provided to Viacom.
>
> 2. Paramount will provide the same access and the same financial information about Paramount to bank financing sources of QVC and Viacom.
>
> 3. No new agreements or amendments with Viacom during the bidding process.

4. The Paramount Rights Plan, supermajority charter provision (Article XI), and § 203 of the Delaware General Corporation Law will be used non-discriminatorily with respect to QVC and Viacom.

5. If the Paramount Board is going to consider antitrust or other regulatory issues in relation to Viacom or QVC offers, outside regulatory counsel for QVC and Viacom will be provided a reasonable opportunity to address any concerns with the Paramount directors.

6. Same merger agreement for both QVC and Viacom.

7. Best bids to be received on November __, 1993, or on __ days' advance notice.

8. If Viacom Lock-up Option and Bust-up Fee are invalidated, Viacom will not be accorded any further arrangements of that nature.

Ex. 48. Paramount made no response.

Later that day, Paramount management rejected these procedures out of hand. Wrote Oresman: "We believe your proposed auction procedures are inappropriate and, in addition, are inconsistent with contractual obligations which we plan to meet." Ex. 49 at 1. The Paramount directors had no part in this flat rebuff.* Oresman Dep. 161-62.

On the following day, a representative of QVC wrote a letter to Oresman that noted that Oresman's letter of November 1 did not indicate whether the decision to reject QVC's proposed fair bidding procedures was that of Paramount's board or of management alone. Ex. 49 at 3. Paramount did not respond. Days later, discovery made clear that the directors had never seen either QVC's proposed bidding procedures or management's letter rejecting them. Oresman Dep. 161-62.

To this day, even though Viacom has twice raised its bid in response to or in anticipation of higher bids from QVC, Paramount and its directors have disclaimed any

* One director, who never saw the QVC procedures proposal, dismissed it all as "this damned stuff you've handed me [at the deposition] from the lawyers . . . . I have no idea what it's all about and it's not my business to." Liedtke Dep. 101.

attempt to conduct a fair bidding process or to obtain the highest possible bid for its stockholders.* Paramount's position was officially confirmed when, on November 8, it filed its Schedule 14D-9 in response to the QVC offer, stating that Paramount would "not place itself up for sale." Ex. 8 at 12.

H. Viacom's Raise to $85 Per Share on November 6

On November 6, Viacom unilaterally raised its tender offer to $85 cash for 51% of the shares, and a back-end of Viacom stock that Viacom asserts is also worth $85. This raise was apparently provoked by press reports that BellSouth was about to join QVC's bid and provide additional financing. Ex. 83. Paramount's board met briefly by telephone the morning of November 6 to accept the increased Viacom bid. Small Dep. 108. Apparently QVC was not mentioned. Small Dep. 111. Paramount has produced no notes, minutes or agendas concerning this meeting.

The November 6 meeting was called for a time less than 24 hours after Viacom proposed to amend its bid for the second time. Davis Dep. 248. No documents

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* See, e.g., Silberman Dep. 49 (this was "not a bidding situation"), 52 ("This is not a bidding contest with prices"), 191 ("I do not see this as a bidding contest"); 192 ("I would not be in favor of an auction"); Liedtke Dep. 88 ("I'm trying to repeatedly indicate to you that the company is not up for sale, has never been up for sale, is not up for bid, is not up for auction, is not interested in that. The fact that QVC has seen fit to try to interfere with it, I've already testified to"); 89 ("But we're not going to entertain bids. . . . To the extent that under the law we have to look at it, we'll look at it. . . . It's not something we want to do."); Pattison Dep. 236 (board "very much opposed to the auction process," never considered the company was for sale, never considered an auction process that I'm aware of"), 237 (can't recall any "discussion of having an auction for the company" at board meetings), 243 ("board did not, in my recollection, ever consider the auction process," and "never considered the company was for sale"); Small Dep. 10-11 (there is no "bidding contest" for Paramount; "[a]bsolutely not" the board's objective to conduct an auction), 11 ("it hasn't been a sale process"), 19-20 (not the board's objective to get highest price; rather, "objective of the Paramount board is to carry out the transaction that it agreed to"), 25 ("wouldn't make much sense" to find out if other firms were interested in buying Paramount), 27 (board has no desire to elicit additional potential transactions), 111 (board is not "trying to enter into a bidding contest or a sale to the highest bidder"), 114 (Paramount did not contact BellSouth because "we weren't trying to put the company up for sale, we weren't trying to put the company up for auction"), 161-62 (Paramount is "not trying to seek out alternative partners"), 198 ("[t]he word that would be farthest away from the thinking of Paramount would be auction . . . ."), 198-99 (Paramount has no intention of "doing anything that would stimulate other bidders to come out of the woodwork"), 200 ("I have never thought about the issue of Paramount having a sale or an auction of itself or soliciting buyers for it").

were distributed in advance of the November 6 meeting. Liedtke Dep. 105 (also commenting as to who made the presentation: "I don't recall who the messenger was that day."). The meeting lasted about 30 minutes. Id.; Small Dep. 108. There was no discussion of the now greatly-enhanced impact of the Lockup on QVC. Davis Dep. 252. Davis characterized Viacom's November 6 proposal as an attempt at a "preemptive bid." Davis Dep. 255. Davis' prejudice against QVC, of course, remained constant: "May I remind you that we're not having a bidding contest or an auction, so I am looking upon the QVC documents one way, or whatever they discussed, and I'm looking at the Viacom situation far differently." Davis Dep. 253.

Actions, of course, speak louder than words. If there is no bidding contest, who was Viacom bidding against on November 6?

I. Paramount's Refusal to Maintain Normal Corporate Documentation.

The record presented to the Court on this motion is highly unusual. According to the sworn testimony of Donald Oresman, Paramount's Senior Vice-President for Administration, Corporate Secretary, General Counsel and a director (and a former partner of Simpson, Thacher & Bartlett, Paramount's counsel):

-- There exist no contemporaneous documents known to Paramount that reflect what transpired at the six relevant board meetings, other than the (unusually cursory) minutes. Oresman Dep. 10-11, 14.

-- No one took notes to prepare the minutes: the minutes were prepared by Oresman based not on notes taken by him or anyone else at the meeting but from the agendas (although agendas have been produced for only two of the six relevant board meetings). Oresman Dep. 11-12.

-- Although draft versions of Oresman's minutes were commented upon by Simpson Thacher, no drafts were kept. Oresman Dep. 12-13.

-- Paramount retained no written notes or other documents reflecting the terms proposed or negotiating positions of either Paramount or Viacom during the course of the negotiations in July, August, September or October of 1993. Oresman Dep. 18-20. Paramount retained no such documents received from anyone else, including Viacom, Lazard or Smith Barney. Id.

-- No draft merger agreements, stock option agreements, term sheets, or correspondence exchanged between Paramount and Viacom have been retained by Paramount or Viacom. Oresman Dep. 18-20.

-- The record reflects that Paramount's directors were given so-called "legal" advice about whether to take notes at board meetings and what to do with them if they did, although Paramount has blocked testimony about the content of this advice. Small Dep. 83-85; Pattison Dep. 54-56; Oresman Dep. 15-16.

-- Mr. Davis testified that he takes notes, but "[a]s soon as the meetings are over, I throw them away." Davis Dep. 90.

This record is an extraordinary one for a large corporation about to engage in a $10 billion transaction that will put an end to its independent existence.* By this time in corporate history, the counsel, secretaries and directors of Delaware corporations are surely on notice that a transaction of this importance to shareholders is not one that should be undertaken casually. Moreover, after September 13, Paramount was on notice that it was a defendant in litigation challenging the due care and good faith with which the transaction was arranged.

Under these circumstances, Paramount should be estopped from arguing that events that directors and other participants could not recall in fact occurred. By depriving this Court and Paramount stockholders of a normal record of corporate decision-making,

* Only two "board packages" can be found among Paramount's production -- for the September 9 and September 27 board meetings. On September 9, the board was given: (a) draft minutes for June 7-8; (b) a 1994 First Quarter Review; and (c) a draft press release for Paramount's regular quarterly dividend. For September 27, the board received: (a) a copy of a week-old joint Paramount/Viacom press release; (b) a copy of the merger agreement approved September 12; (c) the QVC September 20 proposal letter and Paramount statement in response; (d) SEC filings by QVC.

Paramount is responsible for any negative inferences that the Court believes are reasonable under the circumstances. See Smith v. Van Gorkom, Del. Supr., 488 A.2d 588, 877 (1985); Wilmington Trust Co. v. General Motors Corp., Del. Supr., 51 A.2d 584, 593 (1947).

ARGUMENT

I. STANDARDS FOR ISSUANCE OF PRELIMINARY INJUNCTIVE RELIEF

The factors that this Court must consider in determining whether to grant a preliminary injunction are familiar: likelihood of success on the merits, irreparable injury, and balance of the hardships. Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., Del. Supr., 506 A.2d 173, 179 (1986); Ivanhoe Partners v. Newmont Mining Corp., Del. Supr., 535 A.2d 1334, 1341 (1987); Robert M. Bass Group, Inc. v. Evans, Del. Ch., 552 A.2d 1227, 1238 (1988).

II. THE ENHANCED DUTIES AND JUDICIAL REVIEW TO WHICH THE PARAMOUNT BOARD IS SUBJECT UNDER DELAWARE LAW

The directors' duties of care and loyalty are the bedrock measures of director responsibility. Delaware law has long recognized that these duties are greatly enhanced in the context of merger, sale and change of control transactions. The various strands of these duties, set out below, unite to form the proposition that in the present circumstances, the Paramount directors were under the strictest obligation to act solely to achieve the highest price for the stockholders, to abjure discrimination against competing bidders not reasonably designed to achieve the greatest stockholder value, to be directly and actively involved in the process, and to act only after thorough investigation and consideration of all available information.

A. Revlon: the directors' duty to act as "auctioneers charged with getting the best price for the stockholders at a sale of the company"

1. The Revlon duty.

In Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., Del. Supr., 506 A.2d 173 (1986), the Delaware Supreme Court set out, with unmistakable clarity, the duty of directors of a Delaware corporation in the context of a sale of the company -- emphasizing their unyielding obligation to act only to achieve the highest price, and forbidding discrimination against the unsolicited bidder:

> The Revlon board's authorization permitting management to negotiate a merger or buyout with a third party was a recognition that the company was for sale. The duty of the board had thus changed from the preservation of Revlon as a corporate entity to the maximization of the company's value at a sale for the stockholders' benefit. This significantly altered the board's responsibilities under the Unocal standards. It no longer faced threats to corporate policy and effectiveness, or to the stockholders' interests, from a grossly inadequate bid. The whole question of defensive measures became moot. The 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.
>
> . . . Selective dealing to fend off a hostile but determined bidder was no longer a proper objective. Instead, obtaining the highest price for the benefit of the stockholders should have been the central theme guiding director action.
>
> . . . [W]hen bidders make relatively similar offers, . . . the directors cannot fulfill their enhanced Unocal duties by playing favorites with the contending factions. Market forces must be allowed to operate freely to bring the target's shareholders the best price available for their equity.

Id. at 182, 184. The Supreme Court there affirmed this Court's injunction against a board's agreements to a lock-up option, a no-shop provision and a breakup fee. See MacAndrews & Forbes Holdings, Inc. v. Revlon, Inc., Del. Ch., 501 A.2d 1239 (1985).

Our courts have never wavered from enforcing these "Revlon duties." In Mills Acquisition Co. v. Macmillan Inc., Del. Supr., 559 A.2d 1261 (1989), the Supreme Court pointedly noted that Revlon "requires the most scrupulous adherence to ordinary standards of fairness in the interest of promoting the highest values reasonably attainable for the stockholders' benefit," and further focused specifically on the special responsibilities of the outside directors to provide "serious oversight." Id. at 1264-65. And the Macmillan court reiterated that in a sale process, "[t]he proper objective of Macmillan's fiduciaries was to obtain the highest price reasonably available for the company. . . ." Id. at 1282.

To like effect, the Supreme Court stated in Barkan v. Amsted Industries, Inc., Del. Supr., 567 A.2d 1279, 1286 (1989):

> Notably, in Revlon we held that when several suitors are actively bidding for control of a corporation, the directors may not use defensive tactics that destroy the auction process. Revlon, 506 A.2d at 182-85. When it becomes clear that the auction will result in a change of corporate control, the board must act in a neutral manner to encourage the highest possible price for shareholders. Id.

Most recently, in Cede & Co. v. Technicolor, Inc., Del. Supr., No. 336, 1991, Horsey, J. (Oct. 22, 1993), the Supreme Court expressly reaffirmed that, under Revlon, in a transaction involving a "sale of control", the directors have a duty to obtain "the highest value reasonably available under the circumstances," Technicolor, slip op. at 39.*

It is important to recall that the fundamental duty articulated in Revlon was not new. Prior to Revlon, the law had been well settled in Delaware that directors have a fiduciary duty to pursue the best price available in disposing of the corporation's assets. Pennsylvania Co. v. Wilmington Trust Co., Del. Ch., 186 A.2d 751 (1962), aff'd sub nom. Wilmington Trust Co. v. Coulter, Del. Supr., 200 A.2d 441 (1964); Lockwood v. OFB Corp., Del. Ch., 305 A.2d 636 (1973); Robinson v. Pittsburgh Oil Refining Corp., Del. Ch., 126 A. 46 (1924); Thompson v. Enstar Corp., Del. Ch., 509 A.2d 578 (1984); Thomas v. Kempner, Del. Ch., C.A. No. 4138, Marvel, C. (March 22, 1973).

This duty to sell corporate assets for the best price possible pre-dated Revlon, and it exists absent any special "trigger." Thus, in Thomas v. Kempner, supra, the Court of Chancery held that the directors had made a fundamental error of business judgment by continuing to deal solely with one buyer "after it was readily apparent that at least one other group was not only interested in acquiring the [property] in issue but was willing to top [the initial potential buyer's] offer as to cash." See also Robinson v. Pittsburgh Oil Refining Corp., Del. Ch., 126 A. 46, 49 (1924) ("Where the standard of comparison is the absolute one of dollars in hand for the same identical thing, a discretion which would choose the smaller amount would be so manifestly absurd as to convict itself of fraud."); cf. Gimbel v.

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* Technicolor also makes clear that it is not an element of the plaintiff's case on a Revlon claim to establish harm or loss. Technicolor, slip op. at 56, 63-64.

Signal Cos., Inc., Del. Ch., 316 A.2d 599 (1974) (enjoining sale of assets for inadequate consideration), aff'd, Del. Supr., 316 A.2d 619 (1974). These are duties that exist whether or not Revlon has been triggered, and the nature of these duties inform the question of when Revlon is triggered.*

When Revlon is triggered, the various factors the board may consider in responding to competing bids and the measure of value the board may apply in assessing the "best" bid are narrowed. When Revlon is triggered, the directors are obligated to evaluate competing bids solely on the basis of which bid provides the most immediate value to the stockholders. The impact of the bid on the corporate enterprise or other constituencies, the long term or intrinsic value of the corporation, or corporate "policies" or "plans" are no longer at issue. See Revlon, 506 A.2d at 182; Paramount Communications Inc. v. Time Inc., Del. Supr., 571 A.2d 1140, 1150 (1990) (Revlon duty is "to maximize immediate shareholder value"); TW Services, Inc. v. SWT Acquisition Corp., Del. Ch., C.A. Nos. 10427, 10298, Allen, C. (Mar. 2, 1989), slip op. at 21 (Revlon duty is "the duty to exercise judgment (in good faith and prudently) in an effort to maximize immediate share value"). See also id. at 25 ("current share value maximizing mode"); cf. this Court's decision in Paramount, Del. Ch., C.A. Nos. 10866, 10670 and 10935, Allen, C. (July 14, 1989), slip op. at 50 (when Revlon is triggered, the directors are under the "obligation to act so as to maximize the immediate value of the corporation or its shares").

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* See also the Chancellor's comment in Paramount:

> I have earlier expressed the view that Revlon was not a radical departure from existing Delaware, or other, law (i.e., it has "always" been the case that when a trustee or other fiduciary sells an asset for cash, his duty is to seek the single goal of getting the best available price), as well as the view that to be in a Revlon mode is for a director to be in a radically altered state.

Paramount Communications Inc. v. Time Inc., Del. Ch., C.A. Nos. 10866, 10670 and 10935, Allen, C. (July 14, 1989), slip op. at 63, aff'd, Del. Supr., 571 A.2d 1140 (1990).

2. **The applicability of Revlon.**

In the present case, there can be no question that the Paramount board's responsibilities under Revlon have been triggered -- i.e., that, in Revlon's terms, the board's agreement to "a merger or buyout with a third party was a recognition that the company was for sale." Revlon, 506 A.2d at 182. Whether measured against language from prior decisions describing the Revlon trigger or measured against the types of transactions that have been held to trigger Revlon, the board's decision to exclusively support the Viacom transaction cannot be sustained unless it represents the best present value to the stockholders of Paramount.

By virtue of the Viacom transaction, the Paramount directors have approved and recommended the transfer of outright control of the corporation from its public stockholders to Sumner Redstone. Under the Viacom deal, Redstone will receive 70% of the voting power of Viacom/Paramount. In addition, the majority (51%) of the Paramount stockholder equity will be cashed out, and the remaining equity will be converted predominantly into non-voting common stock, plus some amount of preferred stock exchangeable at Viacom's option for debt. Following the transaction, Redstone will have absolute control over what is now Paramount, and will have the voting power, by himself, to cash out or otherwise extinguish that equity via a merger under 8 Del. C. § 251.* In addition, under Delaware law, Redstone could sell his control of the merged Paramount and retain the entire control premium for himself, leaving the public again to the mercies of another controlling shareholder.

If these facts do not "trigger" a Revlon duty to obtain the best price available, both Revlon and the pre-existing, bedrock fiduciary duties upon which it rests will be a

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* By the same token, Redstone will have the voting power necessary to dissolve the merged company or approve the sale of all or substantially all of its assets. See 8 Del. C. §§ 271, 275.

hollow mockery. The Revlon decision will have become a convoluted and empty intellectual exercise to allow directors to do that which they should never be permitted to do -- to sell the assets of the corporation for less than the best price available.

In Barkan, the Delaware Supreme Court stated that "the general principles announced in Revlon [and in other cited decisions] govern this case and every case in which a fundamental change of corporate control occurs or is contemplated." Barkan, 567 A.2d at 1286 (emphasis added). Under that formulation, it is clear that the Paramount directors were subject to Revlon as of both September 12 and October 24. On both occasions, the Paramount directors agreed to merger agreements with Viacom under which control of Paramount would shift into the hands of one man, Mr. Redstone.

The Barkan "change of corporate control" formulation of the Revlon trigger finds direct support in both Revlon itself and the Supreme Court's later decision in Macmillan. In Revlon, the Supreme Court referred to the triggering event as Revlon's board having taken action which recognized "that the company was for sale." Revlon, 506 A.2d at 182. It is inherent in the concept of a "sale" of a corporation that control over its assets is changing hands; "sale" and "change of corporate control" are one and the same thing. In Macmillan, the Supreme Court made this equivalence explicit -- that "sale" equals "change of corporate control" -- in the very context of elaborating upon the Revlon trigger:

> At a minimum, Revlon requires that there be the most scrupulous adherence to ordinary principles of fairness in the sense that stockholder interests are enhanced, rather than diminished, in the conduct of an auction for the sale of corporate control. This is so whether the "sale" takes the form of an active auction, a management buyout, or a "restructuring" such as that which the Court of Chancery enjoined in Macmillan I. Revlon, 506 A.2d at 181-82.
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> . . .

> As we held in Revlon, when management of a target company determines that the company is for sale, the board's responsibilities under the enhanced Unocal standards are significantly altered. Revlon, 506 A.2d at 182. Although the board's responsibilities under Unocal are far different, the enhanced duties of the directors in responding to a potential shift in control, recognized in Unocal, remain unchanged. This principle pervades Revlon . . . .

Macmillan, 559 A.2d at 1285, 1287 (emphasis added).

That change of control is the appropriate test of what transactions trigger Revlon can also be derived from review of those transactions that have been held to do so. In Revlon and its progeny, the transactions held to have triggered Revlon duties have some or all of the following characteristics: (i) a third party would obtain actual control of the corporate entity from the public stockholders, (ii) the termination of a substantial part of the shareholders' equity by conversion into cash or debt, and (iii) a substantial alteration in the structure or businesses of the corporate entity. In Revlon, each of these factors were present (506 A.2d at 178, 182), as they will always be when the transaction involves a sale of all of the stockholders' equity for cash. No case has ever held that Revlon is not triggered where control of the corporation is changing hands.

Other transactions have been held to trigger Revlon duties without all three of these elements present, and the focus has been upon the change in control of the corporation. In Robert M. Bass Group, Inc. v. Evans, Del. Ch., 552 A.2d 1227, 1236-37 (1988), a restructuring was held to trigger Revlon duties notwithstanding that the stockholders would continue to own the majority of the equity of the restructured corporation. The restructuring would have given "effective control" of the corporation to the management group (see 552 A.2d at 1243), albeit it would not result in the transfer of a majority of the equity to the management group. The restructuring was held to have triggered Revlon duties by the Supreme Court. Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d at 1285 ("This case does not require a judicial determination of when Macmillan was 'for sale.' By any standards this company was for sale both in Macmillan I and II.") (emphasis in original).

Conversely, in the two decisions rejecting the applicability of Revlon, there was neither a change in corporate control nor were any of the other factors present. In Ivanhoe Partners v. Newmont Mining Corp., Del. Supr., 535 A.2d 1334, 1344-45 (1987), the Supreme Court concluded that Revlon was not triggered by a board's decision to pay a special dividend which financed a third-party stockholder's acquisition of 49.9% of the stock. The Court concluded that the dividend and share acquisition was not designed to and did not result in the third party obtaining control over the corporate entity because of special provisions in a standstill agreement that assured continued public stockholder control of the company and its board.*

Likewise, in Paramount Communications Inc. v. Time Inc., supra, the Supreme Court held that Revlon duties were not triggered where none of these factors were present. In that case, under the originally proposed Time/Warner stock-for-stock merger, control of the merged corporation would have remained in the hands of the public stockholders; the shareholders of Time Inc. would not have had any portion of their equity cashed out, otherwise terminated, or converted into non-voting stock. See also Paramount

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* The Delaware Supreme Court's reasoning in Newmont directly supports holding Revlon applicable here:

> Revlon applies here only if it was apparent that the sale of Newmont was "inevitable". The record, however, does not support such a finding for two reasons.
>
> First, Newmont was never for sale. During the short period in which these events occurred, the Newmont board held fast to its decision to keep the company independent. Ultimately, this goal was achieved by the standstill agreement and related defensive measures.
>
> Second, there was neither a bidding contest, nor a sale. The only bidder for Newmont was Ivanhoe. Gold Fields was not a bidder, but wished only to protect its already substantial interest in the company. . . .

Here, the Paramount board is not seeking "to keep the company independent," and here there is a "bidding contest." To like effect, see this Court's opinion in Ivanhoe Partners v. Newmont Mining Corp., Del. Ch., 533 A.2d 585, 603 (1987) (Revlon not triggered because "Gold Fields was not a bidder competing with Ivanhoe to acquire (and thereafter to control) Newmont. . . . Thus Gold Fields' willingness to enter into a standstill agreement which limited its ability to seize control of the company.").

Communications Inc. v. Time Inc., Del. Ch., C.A. Nos. 10666, 10670 and 10935, Allen, C. (July 14, 1989), slip op. at 59-60.*

The two most recent decisions by the Delaware Supreme Court treating this issue are Paramount and Barkan. In Barkan, as previously noted, the Supreme Court stated that Revlon governs in "every case in which a fundamental change of corporate control occurs or is contemplated." 567 A.2d at 1286. In Paramount, the Supreme Court appeared to broaden the test; the Supreme Court certainly did not suggest that change of control was not by itself sufficient to trigger Revlon. The Supreme Court in Paramount noted the Chancellor's conclusion that Revlon had not been triggered by the original Time/Warner merger agreement because control of the corporation remained "in the market" -- a conclusion the Court held to be factually supported and "correct as a matter of law." 571 A.2d at 1150. The Court further stated:

> Under Delaware law there are, generally speaking and without excluding other possibilities, two circumstances which may implicate Revlon

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* The Chancellor there read the Supreme Court's decision in Macmillan, and in particular the Supreme Court's citation to this Court's earlier Macmillan I decision, as defining the Revlon trigger as a "change in corporate control":

> Elsewhere in Macmillan our Supreme Court did indicate that a board may find itself in a Revlon mode without reaching an express resolve to "sell" the company [quoting Macmillan, 559 A.2d at 1285].
>
> . . . Thus, I do not find it dispositive of anything that the Time board did not expressly resolve to sell the company. I take from Macmillan, however, and its citation of the earlier Macmillan I opinion in this court, that a corporate transaction that does represent a change in corporate control does place the board in a situation in which it is charged with the single duty to maximize current share value. . . .
>
> 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. . . . [N]either corporation could be said to be acquiring the other. Control of both remained in a large, fluid, changeable and changing market.

Paramount, slip op. at 58-60 (emphasis added).

> duties. The first, and the clearer one, is when a corporation initiates an active bidding process seeking to sell itself or to effect a business reorganization involving a clear break-up of the company. . . . However, Revlon duties may also be triggered where, in response to a bidder's offer, a target abandons its long-term strategy and seeks an alternative transaction involving the break-up of the company.

Id. (emphasis added).

By broadening the Revlon test from sole reliance on change of control, the Supreme Court recognized that the change of control standard potentially was under-inclusive. Thus, there are transactions that should trigger Revlon duties without necessarily involving an outright change of control. For example, the management restructuring undertaken in Macmillan I certainly should trigger Revlon duties regardless of whether management obtained actual or practical control as a result of it. See Macmillan, 559 A.2d at 1285.

Moreover, it certainly cannot be supposed that the Supreme Court in Paramount intended to exclude from Revlon the case of a consensual sale of a company for cash that is not preceded by active bidding. Surely Revlon must apply -- for the very reason that such a transaction represents the stockholders' one chance to receive a control premium. Paramount certainly cannot mean that Revlon is not triggered unless the target board itself approves an auction/bidding process or agrees to break up the company. In Technicolor, this Court held -- well after Paramount -- that Revlon applied to a consensual cash merger even though there was no auction and no suggestion of an intended break-up or dissolution; this Court indeed stated that there was a "material possibility" that the merger would have been preliminarily enjoined under Revlon precisely because there had been no auction or meaningful pre- or post-agreement market check. Cinerama, Inc. v. Technicolor, Inc., Del. Ch., C.A. No. 8358, Allen, C. (June 21, 1991), slip op. at 40. The Chancellor's opinion explicitly tied the applicability of Revlon to "the sale of corporate control." Id. at 2. And the Supreme Court's Technicolor opinion approved the Chancellor's holding on Revlon's applicability. See Technicolor, Del. Supr., slip op. at 65. Here, the majority of the Paramount stockholders' equity is being sold to Viacom for cash, and the remaining shares are to be exchanged primarily for non-voting shares, and Paramount's separate continued corporate existence will come to an end.*

In all events, unless Paramount was intended to overrule Barkan and other decisions, sub silentio, there can be no dispute that change of control is the single most important factor in determining that a transaction triggers Revlon duties. And, as this Court has already observed, there is no adequate basis to conclude that Barkan has been overruled by Paramount. In re Wheelabrator Technologies Inc. Shareholder Litigation, Del. Ch., C.A. No. 11495, Jacobs, V.C. (Sept. 1, 1992), slip op. at 13-15.** This Court's reasoning in Wheelabrator is now even further supported by the Supreme Court's Revlon holding in Technicolor just referred to.

To hold that Revlon was triggered here would not suggest any new doctrinal development. Under the change of control test, the typical stock-for-stock merger agreement would not trigger Revlon. In such mergers -- as with the originally-proposed Time/

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* The Supreme Court's decision in Paramount, immediately following the "two circumstances" quoted above, reflects just how absurd it would be to hold Revlon inapplicable here:

> Thus, in Revlon, when the board responded to Pantry Pride's offer by contemplating a "bust-up" sale of assets in a leveraged acquisition, we imposed upon the board a duty to maximize immediate shareholder value and an obligation to auction the company fairly. If, however, the board's reaction to a hostile tender offer is found to constitute only a defensive response and not an abandonment of the corporation's continued existence, Revlon duties are not triggered, though Unocal duties attach.

Paramount, 571 A.2d at 1150-51. Here, the Paramount board's reaction to QVC has not been "only a defensive response." Rather, it has been to lockup a control-changing deal with Viacom, then to accept bid after bid from Viacom through weeks of exclusionary dealing with Viacom, all with the end result of "an abandonment of the corporation's continued existence."

** As there stated:

> It is, of course, possible that Paramount rejects the more generic Barkan formulation of when Revlon duties arise, and, thus, overrules Barkan sub silentio on that point. Absent a clear indication to that effect by our Supreme Court, however, I am not prepared to so conclude. Paramount gives no such clear indication; indeed, it does not even cite Barkan, a case the Supreme Court decided only three months earlier.

Warner merger -- control of the corporation would always remain with the public stockholders, "in the market."* It is only the unique circumstances of this case that causes the Viacom/Paramount transaction to trigger Revlon -- to wit, the fact that Sumner Redstone has total control over Viacom and proposes to use cash and non-voting Viacom stock as the basic acquisition consideration, thereby giving him absolute, total control over the combined entity, transferring control over Paramount's assets from the public stockholders to him.** Any chance of a future sale of corporate control at a premium for the public stockholders will not exist here. And Redstone's absolute control over Paramount/ Viacom and its assets will include the ability to squeeze out the remaining equity at a time and in a manner of his choosing (or to sell his control position to a third party who could then likewise squeeze out the remaining equity at its sole option).***

Moreover, the factual record here establishes the common understanding of all key participants on the Paramount-Viacom side that their transaction is not a "merger of equals" but rather is in fact a sale of Paramount to Viacom. Thus: (1) the minutes of Paramount's September 9 board meeting reflect Lazard's advice that the Viacom transaction was "at a premium because of the sale of control" (Ex. 12 at P20097); (2) the Paramount-Lazard engagement letter defined the Paramount/Viacom transaction as a "Sale" -- and expressly contemplated a "Competing Transaction" which it included in the definition of "Sale" (Ex. 52 at P30362); (3) the September 12 joint Paramount/Viacom press release announced that "Viacom will acquire Paramount" and indeed emphasized that Redstone

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* Paramount, 571 A.2d at 1150.

** Even the Paramount directors, who professed that "price" was not something they concerned themselves with as regards Viacom (see Silberman Dep. 64-68), acknowledged that unlike a "straight merger of stock for stock" Viacom was paying a "premium" as part of the "price" for "control" (which had been presented as a "nonnegotiable item" on Redstone's part). Id. at 76-77.

*** The Paramount directors did not even attempt to bargain for protection of the public stockholders following the acquisition by Viacom, even though they were aware that Redstone would be able to sell out his control position at a premium and leave the public stockholders behind. See Pattison Dep. 122-23.

would be "the combined company's controlling shareholder with approximately 69.8%" of the voting power (Ex. 21); (4) on September 13, Paramount's Davis himself noted that "we're being acquired" by Viacom (Ex. 68); (5) likewise on September 13 Viacom's Redstone announced that "Viacom Inc. has agreed to acquire Paramount Communications Inc." (Ex. 68); (6) Davis' September 17 letter to the Paramount stockholders describes the transaction as "Viacom will acquire Paramount" (Ex. 24); (7) the joint Paramount/Viacom preliminary proxy statement stated that the deal was at a premium because it "involved a change in control of Paramount" (Ex. 9 at P72090); (8) Lazard recognized that by agreeing to being acquired by Viacom, Paramount was "opening the door to bidders. No question" -- with the expected "biggest threat" being Barry Diller (Ex. 81); (9) on September 27, a Paramount advisor acknowledged that "[w]e fully expect that within a few days QVC will manage to satisfy us on the financing issue and we will be in an auction mode" (Ex. 79); (10) Smith Barney's fairness opinion to the Viacom board described the deal as "the proposed acquisition ("the Acquisition") by Viacom of Paramount" (Ex. 91).*

Furthermore, it is certainly clear that Revlon was triggered by the Paramount board's actions by October 24. The Paramount board was persuaded of the merits of the October 24 $80 merger/tender offer/lock-up agreement with Viacom -- in the face of QVC's $80 offer without lock-ups -- on the ground that it permitted a virtual auction to

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* Even Davis was forced to tell his board on September 27 that Paramount was nearing an auction mode:

> 27. Let me give you some sense of what I think will happen next.
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> 28. Under the terms of the merger agreement with Viacom, we expect to be in a position to discuss the Diller proposal with Diller. And ultimately, if we thought it in the best interests of the stockholders, recommend the Diller proposal to our shareholders.
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> 29. Of course, before that happens, Sumner could raise his bid, or other bidders could appear, so we can't predict the future.

Ex. 15 at P31489. For all the rhetoric about "strategic" mergers, even the carefully-scripted Davis -- perhaps to hold his board in line -- had to appear ready to recommend "the Diller proposal" if his friend "Sumner" did not "raise his bid."

unfold. The board was told by Davis that Paramount had secured Viacom's agreement that Paramount could use its Rights Plan to block Viacom's tender offer if the directors' fiduciary duties so required -- a right that, Davis explained, "would allow the Board to accept a better offer." Ex. 18 at P31511. The Paramount directors themselves had previously determined (on October 11) that discussions with QVC "were necessary for the Board to comply with its fiduciary duties to the Paramount stockholders" (Ex. 7 at 14; see Ex. 16, at P0031506) -- a determination that the directors understood to call for "negotiations" with QVC. See Pattison Dep. 157. Paramount's Schedule 14D-9 of October 25 trumpeted its newly-obtained "fiduciary out" and its newly-obtained right to keep its pill in place if a "better alternative" to the Viacom offer were to be proposed. Ex. 7 at 15. The October 24 joint Paramount/Viacom press release quotes Davis as claiming that the board's acceptance of the increased Viacom $80 bid was "consistent with its [the board's] commitment to deliver value to our stockholders," and admits that the increased Viacom offer was "[i]n response to" QVC's tender offer." Ex. 32.

Thus, even if initiation of an "active bidding process"* is thought to be a prerequisite to application of Revlon, the Paramount board on October 24 did precisely that. And, if anything more were needed, there quickly followed Viacom's newly-increased $85 bid of November 7. There is an "active bidding process" here. The Paramount board cannot blind itself to the reality of its own making.**

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* Paramount, 571 A.2d at 1150.

** Under the circumstances of this case, the sale of control of Paramount to Redstone also may be viewed as leading to "a business combination involving a clear break-up of the company." Paramount, 571 A.2d at 1150. Through the exercise of his majority voting control over the Paramount/Viacom entity, Redstone (or his heirs) will be perfectly free to dissolve, liquidate, or break-up the company. Alternatively, Redstone will be free to sell his majority voting control (at a premium) to a third party that would be free to dissolve, liquidate or break-up the company. The Paramount board did not obtain (or even seek) any constraints upon Redstone's ability to single-handedly determine the future of Paramount (and its stockholders). Pattison Dep. 121-23; Small Dep. 14-19. In the absence of any protection against Redstone's dismantling Paramount, the sale of control to Redstone triggers the "break-up" example referred to by the Supreme Court in Paramount.

In the final analysis, a determination of what transactions "trigger" the Revlon duty must return to the fiduciary bedrock that underpins that duty -- directors may not sell an asset, any asset, for less than the best available price. In this case, the Paramount directors admittedly are selling control of Paramount, or, more specifically, attempting to compel the stockholders to sell control to Sumner Redstone and to preclude the alternative QVC bid. In addition, the Paramount directors are attempting to compel the stockholders to surrender most of their equity in the corporation for cash retaining only largely non-voting stock (and non-voting preferred stock which Viacom may convert to debt). In these circumstances, there is no real "long term" value for the stockholders to enjoy with respect to most of their equity -- and what there is could be extinguished by Redstone unilaterally whenever he so chooses. Most of their equity and all of their control is being sold now, and it is not being retained for the long-term. The chance of a future takeover premium for the stockholders is not being preserved. The directors ought not be allowed to compel the stockholders to surrender that equity now for a price that is less than the best price now available. Revlon and the principles which underlie it are meaningless if they have no application to this case.

B. Technicolor: the directors' duty "to take an active and direct role in the context of a sale of a company from beginning to end"

The Supreme Court's recent decision in Cede & Co. v. Technicolor, Inc., supra, focused with particularity on the directors' personal and direct responsibilities in the corporate sale process, declaring:

> [W]e have stated that a director's duty of care requires a director to take an active and direct role in the context of a sale of a company from beginning to end. Citron, 569 A.2d at 66; Unocal, 493 A.2d at 954 (directors cannot be passive instrumentalities during merger proceedings).

Technicolor, slip op. at 59 (emphasis added).

The Supreme Court there cited its discussion in Citron v. Fairchild Camera & Instrument Corp., Del. Supr., 569 A.2d 53 (1989), which warned against the directors' sole reliance on "hired experts and management":

> We look for evidence as to whether a board has acted in a deliberate and knowledgeable way in identifying and exploring alternatives. Within the context of this analysis, we are, of course, ever mindful of the realities of corporate directorship. We recognize that management is often the catalyst in the decision-making process. We further recognize that a board will receive substantial information from third-party sources. As we have noted on various occasions, however, in change of control situations, sole reliance on hired experts and management can "taint[] the design and execution of the transaction." Mills Acquisition Co. v. Macmillan, Inc., Del. Supr., 559 A.2d 1261, 1281 (1988). Thus, we look particularly for evidence of a board's active and direct role in the sale process.

Citron, 569 A.2d at 66 (emphasis added).

The focus on outside director involvement highlighted in Technicolor was foretold by earlier decisions of the Supreme Court. In Macmillan the Court warned:

> Without board planning and oversight to insulate the self-interested management from improper access to the bidding process, and to ensure the proper conduct of the auction by truly independent advisors selected by, and answerable only to, the independent directors, the legal complications which a challenged transaction faces under Revlon are unnecessarily intensified.

559 A.2d at 1282. See also id. at 1281 (board "may not avoid its active and direct duty of oversight in a matter as significant as the sale of corporate control"); id. at 1285 (board's duties require the "intense scrutiny and participation of the independent directors, whose conduct comports with the standards of independence enunciated by us in Aronson v. Lewis, 473 A.2d at 816.").

C. Unocal/Macmillan: the duty to act reasonably in relation to the stockholder advantage to be achieved in order to obtain the best available alternative

Even if Revlon is not triggered, directors considering a transaction that involves a change of control of a corporation are under enhanced duties and must satisfy an enhanced level of scrutiny. In Yanow v. Scientific Leasing Inc., Del. Ch., C.A. No. 9536, Jacobs, V.C. (July 31, 1991), this Court noted that these enhanced duties derived from

Macmillan and Unocal,* apply whenever "issues of corporate control are at stake," and require that the directors act reasonably in relation to the stockholder advantage to be achieved, with the goal of obtaining the best available alternative:

> Where, as here, issues of corporate control are at stake, the actions of even a disinterested board must satisfy an enhanced level of scrutiny before they will qualify for the deference that courts ordinarily accord to good-faith business judgments. Roberts v. General Instrument Corp., Del. Ch., C.A. No. 11639, Allen, C. (August 13, 1990), Mem. Op. at 17-18.
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> . . .
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> In applying the Unocal/Macmillan standard to the facts at bar, this court must determine whether there was disparate treatment of bidders; if so, whether the board properly perceived that shareholder interests were enhanced by such treatment; and if so, whether the board's action was reasonable in relation to the advantage it sought to achieve. Macmillan, 559 A.2d at 1288. This court recently described that standard as involving inquiry into:
>
>> whether the circumstances afford a disinterested and well motivated director a basis reasonably to conclude that if the transaction contemplated by the merger agreement close, they will represent the best available alternative for the corporation and its shareholders.
>
> Roberts, Mem. Op. at 18.

Yanow, slip op. at 17-18.

As was further explained in Roberts, this enhanced level of scrutiny is required whenever a merger agreement is signed, even one with a fiduciary out (see slip op. at 18), and "requires a judicial judgment of reasonableness in the circumstances" (id., emphasis added).

D. Van Gorkom: the directors' duty to inform themselves of all available material information

In Smith v. Van Gorkom, Del. Supr., 488 A.2d 858 (1985), the Delaware Supreme Court held that, in deciding whether to vote for a proposed merger transaction, the duty of care requires the directors to have informed themselves "'of all material information reasonably available to them,'" id., at 872, quoting Aronson v. Lewis, Del. Supr., 473

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* Unocal Corp. v. Mesa Petroleum Co., Del. Supr., 493 A.2d 946 (1985).

A.2d 805, 812 (1984), and that the directors "may not abdicate that duty by leaving to the shareholders alone the decision to approve or disapprove the agreement." Van Gorkom, 488 A.2d at 873. Accord Technicolor, slip op. at 59.

Directors who bury their heads in the sand cannot satisfy this duty. In the corporate control context, the duty to inform oneself normally "demands a canvas of the market to determine if higher bids may be elicited." Barkan v. Amsted Industries, Inc., Del. Supr., 567 A.2d 1279, 1287 (1989). As the Supreme Court in Barkan further explained:

> "A decent respect for reality forces one to admit that . . . advice [of an investment banker] is frequently a pale substitute for the dependable information that a canvass of the relevant market can provide." In re Amsted Indus. Litig., letter op. at 19-20. The need for adequate information is central to the enlightened evaluation of a transaction that a board must make. . . .

Id. While a failure to canvass the market may be ameliorated in certain circumstances by a post-merger agreement "market check," that course obviously is ineffective where, as here, the agreement has not only a very tight "no shop" but hundreds of millions of dollars of impediments in break-up and stock option costs.* See Barkan, 567 A.2d at 1288 (emphasis added):

> The evidence that will support a finding of good faith in the absence of some sort of market test is by nature circumstantial; therefore, its evaluation by a court must be open-textured. However, the crucial element supporting a finding a good faith is knowledge. It must be clear that the board had sufficient knowledge of relevant markets to form the basis for its belief that it acted in the best interests of the shareholders. The situations in which a completely passive approach to acquiring such knowledge is appropriate are limited.

Moreover, as Van Gorkom itself makes clear, directors are certainly required to be fully familiar with the transaction they are approving -- and to take the time and expend the effort necessary. Directors may not act hastily or permit themselves to be rushed into acting at management's instance. See Citron, 569 A.2d at 67:

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* See In re Fort Howard Corp. Shareholders Lit., Del. Ch., C.A. No. 9991, Allen, C. (Aug. 8, 1988), slip op. at 31-32.

The imposition of artificial time limits on the decision-making process of a board of directors may compromise the integrity of that deliberative process. See Van Gorkom. However, whether the constraints are self-imposed or attributable to bargaining tactics of an adversary seeking a final resolution to a belabored process must be considered. Boards that have failed to exercise due care are frequently boards that have been rushed.

III. THE PARAMOUNT BOARD BREACHED ITS DUTIES

A. Revlon

If the Paramount board was subject to Revlon duties on either September 12 or October 24, or thereafter, there can be no dispute but that it breached such duties. Nothing that the board has done can be claimed to have been reasonably related to obtaining the highest current price for the Paramount stockholders. Everything has been to the direct opposite -- signing up massive lock-ups with Viacom; permitting management to stonewall QVC's requests to negotiate; weeks of exclusive dealing with Viacom; in short, a continued professed belief that Paramount has no interest in anything and anybody other than Viacom.

Discovery has revealed that the Paramount directors appear to have been led to believe that because they deem a merger with Viacom to be "strategic," they need not concern themselves with whether the Paramount stockholders are obtaining the best available price for their stock or with whether someone other than Viacom was proposing a better alternative from the stockholders' viewpoint.* Although the Paramount board minutes and related documents (such as Davis' scripts) have been heavily redacted, this position is explicitly adopted in the directors' deposition testimony -- as their only justification for having failed to concern themselves with QVC or other alternatives or even whether Viacom was paying the highest price for Paramount that could be negotiated with Viacom. See Silberman Dep. 52, 65; Small Dep. 19-20, 111, 114, 161-62, 200 ("never thought about the issue of Paramount having a sale or an auction or soliciting other buyers for it"); Pattison Dep. 82 ("we weren't trying to sell the company. . . . We were trying to go

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* Paramount has blocked all discovery into such advice by claiming an "attorney client" privilege for all legal advice to the board. See, e.g., Silberman Dep. 90; Pattison Dep. 54-56; Small Dep. 73.

forward and merge the Company to have a global giant"); Liedtke Dep. 56-57, 88, 89 ("we're not going to entertain bids . . . it's not something we're interested in. It's not something we want to do").*

The Delaware Supreme Court's opinion in Paramount v. Time is no license for the Paramount board to ignore its fiduciary duties to the stockholders. It has already been shown that the Paramount board's Revlon duties were triggered, and that Paramount does not support the contrary argument. But, beyond that, Paramount cannot be invoked in support of any contention that a board's belief in a "strategic" merger creates some immunity from all other fiduciary duties in the circumstances here.

In Paramount, the Time board had determined to agree to a stock-for-stock merger with Warner at no premium to the Time stockholders -- a true "merger of equals." The merger would have preserved 100% of the Time stockholders' equity in the combined company; there would be no change of corporate control. Paramount then appeared with a hostile tender offer for Time, whereupon Time changed the form of its combination with Warner from a stock merger into a cash tender offer by Time for Warner which did not require a vote of the Time stockholders.

The Supreme Court in Paramount thus did not have occasion to address itself to the duties of a board of directors that has entered into a sale of corporate control transaction. Time's directors at no point had approved a transaction in which Time would be acquired, in which there would be a change of control of Time, or in which the Time

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* The directors' testimony makes clear beyond argument that the Paramount board knowingly determined not to seek to elicit higher bids or to take any steps to seek the highest price (or the best alternative) for Paramount and its stockholders:

> The word that would be farthest away from the thinking of Paramount that I can think of would be auction or sale or up for grabs or anything of that nature. Paramount had no -- had absolutely no intention at any time of putting itself in play, in having an auction, having a sale, doing anything that would stimulate other bidders to come out of the woodwork. . . .

Small Dep. 198. A board acting on those premises clearly cannot be acting in compliance with Revlon duties.

stockholders' equity would be converted into cash or (non-voting) stock of another corporation. Accordingly, the Supreme Court did not address the fiduciary duties of a board of directors -- like Paramount's here -- which has agreed (three times) to a transaction in which (a) control of the corporation would shift from the public stockholders to a single person, (b) where an absolute majority of the stockholders' equity would be cashed out, and the remainder exchanged largely for non-voting stock, and (c) the stockholders' continuing equity, such as it is, would be in shares of another company subject to the absolute control of one person (with no structural restraint whatsoever on his freedom to squeeze out even that remaining equity at any time of his choosing). The Paramount decision may have significance if there were to be a tender offer for Viacom; it has no significance here, where there is a tender offer for Paramount.

Relatedly, the Paramount directors' testimony seems to reflect the peculiar view that, having entered into the September 12 merger agreement, their hands were tied vis-a-vis QVC. E.g., Silberman Dep. 142-43. Any attempt to excuse their failure to act on this basis would be misguided. In Macmillan II, this Court recognized that a board cannot, by agreeing to one bidder's pre-conditions to its bid, thereby seek to evade its legal duties to the stockholders:

> . . . Macmillan's representatives should not have bound themselves to conduct the auction by KKR's one sided rules. . . . The no-shop condition thus came perilously close to tying Macmillan's advisors' hands so tightly that they could not function effectively as auctioneers. To be sure, the Macmillan Board (or, as here, its representatives) had discretion to exercise, in good faith, their independent, informed business judgment to fashion appropriate auction procedures. But that discretion was necessarily constrained by the directors' duties under Revlon. In that case, the Delaware Supreme Court recognized that, "the shareholders' interests necessitated that the board remain free to negotiate" in order to fulfill its duty to achieve the best available price. 506 A.2d at 184.

Macmillan II, slip op. at 43-45 (emphasis added), rev'd on other grounds, Del. Supr., 559 A.2d 1261 (1988). Just as the board in Revlon was not heard to argue that its obligations to the noteholders prevented it from acting in the interests of the stockholders, see 506 A.2d at

184, so too here, the Paramount directors cannot be heard to argue that their contractual obligations to Viacom under the original, or amended, merger agreements excuse their failure to act in the best interests of the stockholders.

Thus, the Paramount board cannot be heard to argue that its hands were tied by the "one sided rules" it agreed to at Viacom's request on September 12 or October 24 -- even if those agreements were not otherwise the product of misinformation and a lack of due care. Rather, "the shareholders' interests necessitated that the board remain free to negotiate." Revlon, 506 A.2d at 184.

B. The Paramount board breached its duties by selling control of Paramount without a "market check" of any type

Since the Revlon case in 1986, no decision of the Delaware courts has approved the conduct of a board that approved the sale or merger of a corporation without some form of "market check." Put another way, a board that determines to sell control without determining whether there is a reasonable basis to believe another bidder would be willing to pay a higher price has breached its duties. See, e.g., Cede & Co. v. Technicolor, Inc., Del. Ch., C.A. No. 8358, Allen, C. (June 21, 1992), slip op. at 40, aff'd in part and rev'd in part on other grounds, Del. Supr., No. 336, 1991 (Oct. 22, 1993); Barkan v. Amsted Industries, Inc., Del. Supr., 567 A.2d 1279, 1287 (1989); Roberts v. General Instrument Corp., Del. Ch., C.A. No. 11639, Allen, C. (Aug. 13, 1990), slip op. at 20-21; In re Formica Corp. Shareholders Lit., Del. Ch., C.A. No. 10598, Jacobs, v.c. (March 22, 1989), slip op. at 34-35. In re Fort Howard Corp. Shareholders Lit., Del. Ch., C.A. No. 9991, Allen, C. (Aug. 8, 1988), slip op. at 31-32; Yanow v. Scientific Leasing, Inc., Del. Ch., C.A. No. 9536, Jacobs, V.C. (Feb. 5, 1988), slip op. at 11-12 & n.6.

None of these cases require a "single methodology or blueprint." Yanow, slip op. at 11. By the same token, each of these cases recognizes that a board must do something reasonably to assure itself that there is not a better transaction available prior to the close of the contemplated sale or merger. The techniques that have, in various combinations, been approved by the courts include: (a) redemption of a rights plan to expose a company to unsolicited offers (Barkan); (b) 30-day post-agreement market check provided by a fiduciary out that is not "hobbled by lock-ups, termination fees or topping fees" (Fort Howard); (c) 30 day post-agreement market check during which the corporation obligated itself to actively seek higher bids (Formica); (d) a "window shop" and "fiduciary out" that permitted a bidder to trigger the board's ability to supply information if anyone made a bona fide higher bid (Yanow); and (e) 30-day market check and announcement of terms under which better offers may be accepted (General Instrument).

But no case approves what Paramount has done here. No case permits a board to agree to a merger and sell control without any market check, without any obligation to seek out higher bids post-agreement, or without any "window shop" period in which potential bidders know they can obtain information. Equally important, no case permits a board to sell without such protections but with impediments such as stock option lock-ups, bust-up fees and a public relations campaign proclaiming that even "nuclear attack" will not derail the deal.*

Indeed, the September 12 Paramount/Viacom merger agreement appears to be unique among those merger agreements that have come before this Court in having no fiduciary out. Under the September 12 agreement, Paramount was obligated to submit the merger proposal to its shareholders even if it withdrew its recommendation, in what appears to be a per se violation of 8 Del. C. § 251. See Van Gorkom, 488 A.2d at 888. The current agreement is only slightly less egregious -- it allows Paramount's board to withdraw its recommendation and terminate the agreement, but only after subjecting Paramount to a half a billion dollar liability for optioned stock and a bust-up fee.

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* Here, Paramount's refusal to even talk to QVC led it to recite, in its Schedule 14D-9, that it had "reviewed and considered" the QVC bid "to the extent of available information" (Ex. 8 at 14) -- i.e., Paramount blinded itself and then complained it could not see.

By refusing to include the kind of "market check" or market check proxies that have become customary in merger agreements since Revlon, the Paramount directors have breached their duty to approve the merger or sale of the company only upon a reasonable basis to believe that either there is no better transaction available or that any such transaction can surface and be consummated if it indeed exists. See Yanow, slip op. at 11-12. Indeed, here the Paramount board has candidly admitted that it sought no information about other potential bids and has no interest or intention of eliciting other bids. If the teaching of Technicolor, Barkan, Roberts, Fort Howard, Formica, and Yanow is that a board must do something to allow other bidders to come forward and be able to consummate a better transaction, then the Paramount board has clearly breached its duties here.

C. Paramount's consistently unfair and discriminatory treatment of QVC

From the moment QVC announced its $80 per share merger proposal on September 20, Paramount has adopted a consistent strategy -- giving favored treatment at every point to Viacom, while stonewalling QVC.

A comparison of Paramount's disparate treatment of QVC and Viacom demonstrates this point. By way of example:

-- While Paramount took a full five days to execute and return a simple form confidentiality agreement to protect the privacy of QVC internal business information Paramount had asked to see, Paramount managed to conduct the due diligence for a multi-billion-dollar merger with Viacom and complete all the related legal documentation in the space of four days (September 8 through 11). Similarly, Paramount negotiated the terms and documents for a multi-billion-dollar Viacom tender offer in less than 24 hours -- from the morning of October 23 until 9:00 a.m. on October 24. For weeks -- and continuing through today -- Paramount has refused to sit down and negotiate with QVC.

-- While Paramount insisted that it would not even talk to QVC unless QVC made a bid that included evidence of an absence of financing contingencies, it agreed to a tender offer by Viacom that was entirely subject to financing. Paramount, moreover, did this despite the fact that the no-shop in its September 12 contract with Viacom nowhere required "evidence" of financing, only that the third party bid have no financing contingency.

-- While Paramount has insisted on conducting informational due diligence on QVC prior to holding any substantive merger discussions, Paramount negotiated all the material structural terms of a merger with Viacom prior to commencing due diligence on September 8.

In light of this record, it is no surprise that discovery has shown that Paramount's public posture -- that it will give due consideration to QVC's offer -- is simply a charade. The Paramount management and director witnesses testified that there is nothing for them to talk to QVC about, since they believe there is no "strategic fit" between the two companies. Despite the fact that the directors have been told on several occasions that Paramount could talk to QVC, and indeed the board has formally resolved that such discussions were "necessary," Paramount's management clearly never intended to have meaningful discussions:

> Q: Was there an interest in Paramount in pursuing a business combination with QVC?
>
> A: No. We are not putting the company up for sale to QVC.
>
> Q: What did you understand the Paramount board was doing on October 11th when it authorized discussions with QVC?
>
> A: Just that: Authorizing discussions. Probably to seek more information, find out what QVC had on its mind. Not being mind readers, we did not perceive to know that, nor presume to know it.
>
> Q: And that's all?
>
> A: Pardon?
>
> Q: And that's all?

A: What else could there be?

Davis Dep. 200-01. As noted, Paramount gave only the most cursory consideration to QVC's repeated efforts to set up a meeting and no consideration to QVC's suggested "Fair Bidding Procedures" (Ex. 48).* When Paramount finally allowed a meeting on November 1, it lasted for under ten minutes and Paramount expressed no views. This is not the conduct of a board that has any intention of fulfilling its fiduciary responsibilities, or even of living up to its self-proclaimed willingness to consider the QVC offer on its merits.

D. Duty of Care

As noted above, the Paramount directors are required to act only upon full information when approving a merger or sale of the company, and to involve themselves actively and to supervise Paramount's management and advisors in negotiating a merger or sale. Technicolor, slip op. at 58-65. In addition, the management directors are required to be candid with the board and not to obstruct the directors from obtaining adequate information. Technicolor, slip op. at 59, 64-66.

Even on a record developed in only seven days of expedited discovery, a pattern of conduct is clear from the undisputed facts. The breaches of the duty of care -- nearly too numerous to list in detail -- fall into three main categories. First, the board failed to involve itself in setting the ground rules of the negotiation on critical issues such as what price would be asked for the sale of control; who would represent Paramount; structural issues (such as the stock option, the exchange ratio and the acceptance of Viacom's

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* One Paramount director explained what course would be the way to obtain the best price -- the exact opposite, in his view, of what Paramount was doing:

> . . . if Paramount had wanted to sell out, the very last thing they ought to do is what they did. If you want to sell something, why, you go at it in an entirely different way. . . . You go around and talk to a whole bunch of people and get them all charged up and bidding against each other and that type of thing, a whole lot of thing. That was never ever the desire of Paramount.

Liedtke Dep. 133-34 (emphasis added).

non-voting stock as the key "currency" for the transaction); and future management (including Davis' desire to be CEO of any merged company). Second, the board failed to deliberate in a careful, informed manner on issue after issue. Instead, it allowed management to require attendance at hastily called meetings without any opportunity to study written material in advance and, typically, without significant written materials being distributed at the meetings themselves. The directors then failed to engage in active deliberation or questioning once the meetings began. The inside directors (and advisors) failed to tell the independent directors of critical facts known only to them. Third, the board failed to exercise any supervision over management as Messrs. Davis and Oresman arrogated to themselves the power to tell QVC whether Paramount would meet with QVC and on what conditions.

1. Technicolor.

In Technicolor, our Supreme Court reiterated the due care standards applicable to directors of a corporation agreeing to a merger or sale. Technicolor holds that business judgment rule protection of any kind is available only to directors "who have both adequately informed themselves before voting on the business transaction at hand and acted with the requisite care." Slip op. at 58 (emphasis in original). Specifically, Technicolor states that "a director's duty of care requires a director to take an active and direct role in the context of a sale of a company from beginning to end"; directors "cannot be passive instrumentalities during merger proceedings." Id. at 59. Technicolor also makes clear that directors have a duty to insure that other directors know material facts: "In a merger or sale, we have stated that the director's duty of care requires a director, before voting on a proposed plan of merger or sale, to inform himself and his fellow directors of all material information that is reasonably available to them." Id. at 59 (emphasis added).

In Technicolor, the CEO negotiated a sale of the company without consulting the outside board members about the material elements of the transaction. Slip op. at 15, 18-25. Technicolor's CEO set the maximum asking price for the company without consulting the full board, id. at 16, and he negotiated stock options and management employment issues without prior board authorization. Id. at 16-17. The CEO retained an investment banker and law firm to work on the deal "without consulting" the directors. Id. at 19. Technicolor's board -- unlike Paramount's -- at least received an account of the to-and-fro of the price term negotiation. Id. at 25. The Court noted that "[t]here is some question whether the documents were in fact present and available for the directors to study" at the Technicolor board meeting. Id. at 27 n.19. Here it is clear that the basic deal documents -- the merger agreement and the stock lock-up -- were not before the Paramount board when it approved them on September 12. At least one Technicolor director suggested that the company solicit other offers -- something that not one Paramount director suggested. Id. at 27-28. Thus, the Technicolor record is in some respects more favorable than the record the Paramount directors have made for themselves. Nonetheless, our Supreme Court affirmed the Chancery Court's holding that the Technicolor directors were "grossly negligent." Id. at 55.

The Technicolor court affirmed five key findings of the Chancery Court that established the gross negligence of the Technicolor directors:

(1) that the [merger] agreement was not preceded by a "prudent search for alternatives;"

(2) that, given the circumstances, the directors had no reasonable basis to assume that a better offer from a third party could be expected to be made following the public announcement [of the proposed merger];

(3) that, although Kamerman had discussed Perelman's "approach" with several of the directors before the meeting, most of the directors had no knowledge of an impending sale of the company until they arrived at the meeting and only a few of them had any knowledge of the terms of the sale and of the required side agreements;

(4) that Perelman "did, probably, effectively lock-up the transaction on October 29 when he acquired rights to buy the Kamerman and Bjorkman shares (about eleven percent together) and acquired rights under the stock option agreement . . . to purchase stock that would equal 18% of the company's outstanding stock after exercise" given Technicolor's charter provision and Perelman's prior stock ownership of about five percent; and

(5) that the board did not "satisfy its obligations [under Revlon] to take reasonable steps in the sale of the enterprise to be adequately

informed before it authorized the execution of the merger agreement."

Id. at 64-65 (bracketed material included in original). Further, the Supreme Court approved the Chancery Court's application of Revlon to the Technicolor facts -- the Chancery Court had noted that the Technicolor merger probably would have been preliminarily enjoined had such relief been sought,* and the Supreme Court observed with approval that the Chancery Court had "noted the relevance of Revlon in 'illuminat[ing] the scope of [the] [B]oard's due care obligations . . .' and implied that the Technicolor board's failure to auction evidenced a breach of their duty of care." Technicolor, slip op. at 65.

Applying Technicolor to the case at bar, it is clear that Paramount's directors have breached their duty of due care. Like Technicolor's directors, they approved a merger agreement that was concededly not "preceded by a 'prudent search for alternatives'"; like Technicolor's directors, they had "no reasonable basis to assume that a better offer from a third party could be expected to be made" despite the contractual provisions of the merger agreement since the board had not fully informed itself about the effect of the agreements with Viacom upon the ability of others effectively to bid for Paramount; as in Technicolor, here at most only "a few of [the Paramount directors] had any knowledge of the terms of the sale and of the required side agreements" prior to arriving at two key board meetings; here Viacom "did, probably, effectively lock-up the transaction" on September 12 when it "acquired rights under the stock option agreement" given, among other things, Paramount's supermajority charter provision and the extreme impact of the option resulting from its low-ball price (a per share price Viacom itself has now outbid by $15 per share); and most clearly, the Paramount board "did not satisfy its obligations [under Revlon] to take reasonable steps in the sale of the enterprise to be adequately informed before it authorized the execution of the merger agreement." See Technicolor, slip op. at 64-65.

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* Cinerama, Inc. v. Technicolor, Inc., Del. Ch., C.A. No. 8358, Allen, C. (June 24, 1991), slip op. at 40.

Technicolor is the Supreme Court's latest holding applying due care standards to board conduct resulting in a merger agreement. But its principles are not new. The actions of the Paramount board would fail any version of the well-established principle that directors must act on the basis of "all material information reasonably available" when approving a merger or sale. See Aronson v. Lewis, Del. Supr., 473 A.2d 805, 812 (1984) (emphasis added).*

2. Breaches of care prior to the September 9 and September 12 board meetings.

Negotiations leading up to the Viacom agreement were conducted from April through August 1993 by Davis and Oresman, with Lazard (after June 28), acting for Paramount. Small Dep. 55. The board never authorized these negotiations to begin. Key terms were set even before the involvement of Lazard. Rattner Dep. 37; Dauman Dep. 30-36. The board was not given progress reports about the substance of the negotiations, although apparently individual board members were told in general terms that discussions were going on. Small Dep. 41-45, 226; Pattison Dep. 19, 48.

Paramount took several critical negotiating decisions in July and August that shaped the material elements of the deal. By August 20, 1993, for example, a "bid and asked" range of $65/$70 had been established. Ex. 51 at L4930. Yet the board was never asked to approve management's decision to ask a maximum of $70 per share for Paramount. Small Dep. 43. Nor was there any presentation to the board prior to September 9 that could have given the directors an informed basis for making a judgment that $70

* Paramount's board's conduct also has many parallels with the conduct of the Trans Union board in Van Gorkom. In Van Gorkom, as here, the CEO did not consult the board as to the price and stock option terms negotiated with an acquiror before presenting them to the board, 488 A.2d at 866, 874, 877 n. 19; the board's approval process was rushed, id. at 866; the board did not have before it critical legal documents, or summaries, relating to the merger proposal, id. at 867-69, 874; the CEO misinformed the board about certain matters, id. at 869; and the directors failed to exercise their judgment "with specificity on the transactions," id. at 872, failed to ask questions and generally failed to use a "critical eye." Id. at 872, 877.

was reasonable, even if Davis had asked them to do so. As events have shown, $70 was a grossly inadequate asking price.

Equally important, the board was never given the opportunity to approve a negotiating posture that included elevation of Davis to the new position of CEO of the merged company -- a posture that implied concessions to Viacom on other issues. Small Dep. 41-43. Nor was the board asked to authorize Paramount's decision to not seek additional voting (as opposed to non-voting) stock from Redstone -- the 9-to-1 non-voting to voting ratio remained unchanged all spring and summer, and unchallenged by Paramount's negotiators. Small Dep. 43. And the board was not asked to authorize Paramount's willingness to negotiate an enormous (19.9%) stock option and an equally enormous ($100 million) break-up fee. All these negotiating decisions were made by Davis (in some cases with Lazard). Small Dep. 43, 55. The board members heard about them for the first time when the deal terms were already set, at the September 9 meeting. Small Dep. 41-42.

Our Supreme Court has recently made clear that independent directors need to be "directly involved" in negotiations leading to a merger agreement. Technicolor, slip op. at 59. Here there was no direct involvement, and no supervision.

3. Breaches of due care in connection with the original September 12 merger agreement.

On September 12, Paramount's directors approved a sale of control to Redstone, a 19.9% stock option, and a $100 million break-up fee, all as part of a contract with no fiduciary out. They did this without informing themselves of facts that any director of a Delaware corporation would be expected to consider when confronting such a decision. Specifically, the board by September 12:

-- had not been given any detailed description of the negotiations leading up to the proposed agreement. Small Dep. 57-58.

-- had not considered the potential effect of the stock option and termination fee on the ability of potential bidders other than Viacom to make a competing offer. Small Dep. 51-52, 64, 229-30, 249; Silberman Dep. 91-92; Pattison Dep. 116, 119.

-- had not considered how the size and structural terms of the Lockups compared with stock options and break-up fees approved in prior transactions. Small Dep. 194; Pattison Dep. 92, 116, 119. The board was not given any analysis of the potential value of the option to Viacom. Small Dep. 61.

-- did not have any information from which it could conclude that Viacom (or other companies) could not have been induced to bid for Paramount by some device less onerous than the stock option and break-up fee. Small Dep. 51-52; CEO Davis certainly did not believe that granting lockups was the only way to induce bids. Davis Dep. 114, 300.

-- did not have any information from which it could conclude that bidders other than Viacom were unwilling or unable to offer more money and/or a better-structured deal to stockholders. See Pattison Dep. 35; Small Dep. 200-02, 227-29; Silberman Dep. 95-100.

-- did not discuss whether higher bids might be available. Small Dep. 122.

-- had not considered whether the absence of a fiduciary out tied Paramount's hands too tightly in the event a higher bid materialized, and had not compared the termination provisions of the Viacom merger agreement with comparable terms in previous transactions. Pattison Dep. 103 (concedes board "abdicated" its judgment on this issue); but see Silberman Dep. 72-73 (mistakenly thought board could terminate).

-- did not have sufficient information to conclude that the equity investment of Paramount's public shareholders could be safely committed to Mr. Redstone, since no effort had been made to seek to restrain Mr. Redstone's unfettered ability to consummate a cash-out merger after the creation of the "Paramount/Viacom" entity. Pattison Dep. 121-23; Small Dep. 14-19; Liedtke Dep. 118.*

One critical subject on which information was withheld from the board was Redstone's stock purchases of Viacom. Redstone's purchases in the summer of this year had been such a large percentage of the total trading volume that there was concern at Lazard that Viacom's public trading price was being temporarily inflated. Rattner

* The Paramount side never sought any protections from Redstone restraining his ability to squeeze out the public, either during his lifetime or via action of the trustees who will control Paramount/Viacom upon his death (under his current estate planning). See Dauman Dep. 105-06, 111-16.

Dep. 88-91. The stock purchase information was critical to the Paramount board's decision, since Viacom's stock was the "currency" Paramount stockholders were to receive.* Lazard vice-president Peter Ezersky had collated this information and distributed it in written form to various Paramount insiders and other members of the Lazard team in advance of the September 12 meeting. It could easily have been included in either Lazard's September 9 or September 12 board book. It was not. Ezersky himself and at least six of the recipients of Ezersky's analyses were at the board meetings. None thought to provide it to the directors. Davis Dep. 104-05.** The outside directors who were deposed did not recall being informed about Redstone's stock purchases. Small Dep. 100-02; Silberman Dep. 57; Pattison Dep. 68. There is not one word about it in the minutes. Ex. 18.

In addition to these substantive breaches, there were also serious breaches of due care "process" at the September 12 meeting. The board did not discuss retention of Lazard (although a resolution "ratifying" such retention was contained in the resolutions);*** the board did not have the opportunity to review the transaction documents (or even summaries of them) prior to the meeting;**** the draft agreements were not reviewed by the board members prior to the vote;† and neither the minutes nor the

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* Indeed, it was <u>only</u> the run up in Viacom stock over the summer that made the September Viacom deal look more attractive than the July 7 Viacom proposal (the same .1 A shares, .9 B shares and even more cash, $13.50 per share) that the Paramount negotiators had <u>rejected</u> and which Lazard had declared <u>inadequate</u>. Ex. 11 at 2; Davis Dep. 101-02.

** Davis himself received Ezersky's memoranda but does not recall discussing them with <u>anyone</u>. Davis Dep. 80. He claims not to recall if he deemed the information "significant" at that time -- even while he was negotiating a deal whose currency was the Viacom stock being inflated by Redstone's purchases. Davis Dep. 82-83.

*** Ex. 13; Small Dep. 221.

**** Silberman Dep. 72-73; Small Dep. 32-33.

† Silberman Dep. 71; Small Dep. 35-36.

discovery record contain evidence of active participation by any outside directors in discussion or questioning about the transaction.*

4. Breaches of care at the October 24 board meeting.

The board meeting of October 24 was the critical moment at which the Paramount board, in the face of the just-announced QVC $80 tender offer, decided to ignore that offer and to block QVC by agreeing to the new but equally locked-up Viacom $80 tender offer/second-step merger proposal -- a proposal which gave Paramount shareholders not one cent more than QVC was then offering; which would replace 51% of their equity with cash; which effectively deprived the stockholders of a vote on the Viacom transaction; and which nonetheless provided no "collar" protection against a drop in Viacom's stock. The circumstances of this meeting clearly merit detailed scrutiny.

No satisfactory explanation has been offered by any Paramount witness for the extraordinary haste in which directors were summoned and presented with Viacom's new offer. The only logical inference is that management and its advisors -- knowing well the tactical advantage that could accrue to Viacom if its tender offer could be scheduled to close a day or two earlier than QVC's -- were willing to curtail the consideration to be given to the new Viacom bid as compared with the QVC offer if that meant a tactical timing advantage could be obtained.

* Silberman Dep. 82-109; Small Dep. 154-55; Ex. 13. The board was also never told that a merger with Viacom would violate the USA Network joint venture agreement between a Paramount subsidiary and MCA. Under that agreement, each participant in the venture is prohibited from providing to cable television systems a national video basic cable entertainment network except through the venture. (For example, under the joint venture agreement, Viacom would be prohibited from running MTV or any other of its basic cable programming services.) Davis admitted that the prohibition extends to the parent company and, were Paramount and Viacom to be merged, it would "clearly" extend to Viacom. Davis admitted that the contractual bar had already been the subject of discussions with MCA, which discussions had "not concluded anything." See Davis Dep. 266-73. Rattner of Lazard testified that his understanding was that a "buy/sell" right under the agreement would be triggered by a change of control involving Paramount, and that the issue had been raised and not resolved. Rattner Dep. 138-42. See also id. at 138 (referring to a Lazard September note, Ex. 61, that MCA "going to be tough via USA").

When the board assembled on Sunday morning, it was hardly in a well-prepared position to take action that would impede QVC's offer or that would facilitate and lock-up Viacom's tender offer:

- As of 9:00 a.m. Sunday, Viacom's tender offer had not even taken final form. It was a proposal for Paramount to agree to a tender for 43.75% of Paramount's shares, and that was the proposal Lazard was prepared to opine on -- and the proposal Lazard actually opined on. It was only substantially <u>after</u> the board process had begun and Lazard's opinion rendered, that a note was passed in to the meeting changing Viacom's proposal to a 51% tender offer. Ex. 18; Small Dep. 206. The board never discussed why Viacom had suddenly changed its offer. Pattison Dep. 170. "It all happened very quickly." Small Dep. 209.

- There were no written drafts or summaries of the proposed restated merger agreement available at the meeting. Small Dep. 35-36.

- No financial advisor for Paramount offered an analysis of the comparative merits of the QVC and Viacom offers (or its new provisions) which (at least after Viacom modified its proposal from 43.75% to 51%) were roughly comparable economically on a market value basis. Rohatyn Dep. 87; Pattison Dep. 176; Small Dep. 156-57. According to the minutes, Lazard opined only with respect to the Viacom offer, which it deemed "fair" -- hardly enlightening to the board, since Lazard had previously opined that Viacom's $69.14 offer of September 12, some $2 billion <u>less</u>, was also "fair." See Ex. 18. Lazard's entire written presentation to the board on October 24 consisted of 7 short pages (Ex. 62). These materials reflected that QVC's proposal had a market value of $79.30 and Viacom's proposal had a market value of $75 per share plus a convertible preferred stock with a "face value" of $5 per share (but which had no trading value and which Lazard's written materials did not otherwise value). (Ex. 62) Lazard further presented materials indicating that both Viacom and QVC could <u>increase</u> their bids without negotiating new bank financing -- surely a fact which argued that no definitive action was required immediately. Ex. 62.

- The Booz-Allen presentation was misleading, since it was used to persuade the directors that the Viacom offer was economically superior, while in fact Booz-Allen is not financially expert enough to render such advice, and the Booz-Allen report was admittedly only a "first cut." Wolf Dep. 16-17; Ex. 86.

- <u>Because management had successfully avoided having any substantive discussions with QVC, the board on October 24 lacked any basis in knowledge for evaluating the competing bids</u>. As one director testified, the board has not had "an opportunity to do -- to listen to an in depth review of all the issues" concerning a QVC merger. Small Dep. 168. The board was <u>not</u> informed that QVC, prior to starting its tender offer, had offered a merger agreement without a lock-up, without a stock option, without a break-up fee and with a fiduciary out. Small Dep. 67-69; Pattison Dep. 227-28.

-- Whether because of haste or dereliction of duty, <u>the independent directors simply did not understand crucial features of the agreement put before them on October 24</u>. The board accepted Davis' bland and misleading assurance, as reported in the minutes, that the agreement "would allow the board to accept a better offer." Ex. 18. But the October 24 agreement continued to contain a burdensome stock option and break-up that added at least $3 a share to the cost of any bidder except Viacom. And the specific provision of the agreement Davis referred to -- the change in the Rights Plan amendment obligation -- did not do what Davis said it did, and was in any event not comprehended by the directors. <u>See</u> Small Dep. 184-85; Pattison Dep. 193-206.

-- No one at the October 24 board meeting considered that, given events since September 12, Paramount was now in a position where it could renegotiate the more onerous provisions of its agreement with Viacom, such as the no-shop and the stock option. Pattison Dep. 147. Instead, the board accepted that no further concessions from Viacom were available or, indeed, even desirable.* No one suggesting first talking to QVC. Davis Dep. 198.

5. **<u>Further breaches of due care</u>**.

From September 12 until the present, Paramount's management has engaged in a concerted campaign first to warn off interlopers from the Viacom deal, and second, to delay and frustrate QVC's efforts to negotiate after QVC made its September 20 offer. Discovery has shown that:

-- The outside directors were not consulted prior to issuance of press releases stating Paramount's unshakable commitment to Viacom and (after September 20) skepticism about QVC. Small Dep. 213; Pattison Dep. 213-14, 226, 230-31.

-- The outside directors were not consulted prior to Paramount's initial refusal to meet with QVC. Small Dep. 127, 130-31, 133.

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* Davis' attitude on what faced the Paramount board on October 24 is highly revealing:

> ... we were not, you know, in a bidding situation.
> We were not for sale. We were not running an auction.
> We were running a -- we were trying to engage in a merger.

Davis Dep. 185. Davis makes no pretense of even-handedness as between QVC and Viacom: "we were renegotiating the terms on a deal that we wanted to make, on a merger agreement that we wanted to succeed." <u>Id</u>. at 190.

-- The outside directors were not consulted about Paramount's decision to spend a week considering whether to sign a confidentiality agreement with QVC (in the same form Paramount had previously sent to QVC, and which QVC had returned in twenty-four hours). Small Dep. 127, 130-31, 133.

-- The outside directors were not consulted about Paramount's decision to refuse QVC's request, after QVC had supplied all the evidence of financing and internal business information Paramount had demanded, to schedule a meeting between QVC and Paramount. Small Dep. 130-31, 133.*

-- Paramount management refused to transmit to board members an October 28, 1993 letter (Ex. 46) from QVC chairman Barry Diller, addressed to the Paramount board at Paramount's corporate office (Small Dep. 137-38; Pattison Dep. 213-14; Liedtke Dep. 90-91). The letter affirmed QVC's desire to negotiate an agreed-upon transaction despite the commencement of the QVC tender offer. As a result, the outside directors appear unaware that QVC continues to seek such a negotiated transaction. Pattison Dep. 230; Small Dep. 135.

-- The outside directors were not consulted prior to Paramount's rejection of the "Fair Bidding Process" procedures proposed by QVC (Ex. 25) at the seven-minute meeting Paramount finally deigned to permit on November 1, and have not been informed of the nature of the procedures sought by QVC. Pattison Dep. 227-31; Small Dep. 138-40; Liedtke Dep. 101.

This list makes clear two things: first, Paramount management has usurped to itself the prerogatives which, when competing bids are made for a company and merger agreements are being signed on the average of once every two weeks, belong <u>only</u> to the board of directors; and second, that Paramount's outside directors are supine enough to have permitted this to occur and to continue for close to two months.

* * *

The conduct described above is, in its particulars and in the aggregate, at least as far below established standards of due care as the director conduct found to have

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* To the extent Paramount management belatedly informed the board of this conduct, management twisted the facts by reporting to the board that QVC had sought to schedule a meeting for the "next day" after delivery of the business materials. Ex. 20; Small Dep. 131-32. In fact, QVC's letter asks for a meeting on any of three days, October 20, 21 or 22 (Ex. 42) and Paramount management refused to agree to schedule any meeting at any time. <u>See</u> Exs. 43-45. Management purposefully made QVC sound unreasonable in order to mislead the board into believing management was acting responsibly.

breached the board's duties in Smith v. Van Gorkom, Macmillan II and Technicolor. Those cases -- and the many cases applying their principles -- compel the conclusion that Paramount's board has not fulfilled its duties of care.

E. The Lockups

The $100 million break-up fee and 20% stock option here are unprecedented in their size and preclusive effect. Together, they exact a toll of nearly $500 million on any competing bidder at the current level of Viacom's $85 bid. Moreover, perversely, the stock option operates to reward Viacom for having made a low initial bid, since its cost to a competing bidder remains tied to the $69.14 value of the original Viacom offer of September 12. These Lockups dwarf those that have been before the Delaware courts in the past.*

Under our law, the only circumstances under which Lockups may be justified are if they (a) "confer a substantial benefit upon the stockholders" as in the case of a lock-up that is "necessary to draw any of the bidders into the contest" and (b) are approved by a decision of directors that was fully informed. Macmillan, 559 A.2d at 1284, 1286. Macmillan makes clear that these analyses require a comparison of what the locked-up bidder receives in relation to its offer, and that "[t]he care and attention which independent directors bring to this decision are crucial to its success." Id. at 1286. Here, the break-up fee and the stock option fail on both grounds.

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* Cf., e.g., Lewis v. Leaseway Transp. Corp., Del. Ch., C.A. No. 8720, Chandler, V.C. (May 16, 1990) ($15 million break-up fee, lockup on 18% of stock at offer price); Roberts v. General Instrument Corp., Del. Ch., C.A. No. 11639, Allen, C., (Aug. 13, 1990) ($33 million break-up fee, no lockup); In re Formica Corp. Shareholders' Litigation, Del. Ch. C.A. No. 10598, Jacobs, V.C. (Mar. 22, 1989) ($5 million break-up fee, $5.5 million cap on expenses, no lockup); Braunschweiger v. American Home Shield Corp., (Oct. 26, 1989) ($2.5 million break-up fee, no lockup); Zirn v. VCI Corp., Del. Ch., C.A. No. 9488, Hartnett, V.C. (July 17, 1989) ($2.5 million break-up fee, no lockup); In re KDI Corp. Shareholders Litigation, Del. Ch., C.A. No. 10,278, Berger, V.C. (Nov. 1, 1988) ($7.5 million break-up fee, plus 20% of the difference between $19.00 ($1.00 above bid price) and amount of any higher bid accepted by company); In re Holly Farms Corp. Shareholders Litigation, Del. Ch., C.A. No. 10350, Hartnett, V.C. (Dec. 30, 1988) ($15 million break-up fee, lockup on various operations).

The record here demonstrates that the Lockups cannot be justified as having been necessary to induce Viacom to bid (even putting to one side the demonstrably low level of its original bid). Redstone has publicly stated that it was Viacom that had been trying for four years to induce Paramount into a deal -- in Redstone's words, it had taken him four years to get Davis "to the altar." Ex. 22 at 7. Moreover, Redstone has repeatedly, publicly claimed that from Viacom's perspective, a Paramount-Viacom combination is a "marriage made in heaven," a matter of "destiny," not a matter of economics or "dollars" (Ex. 22 at 2, 5) -- and thus can hardly claim with any credibility that he would have had no interest in Paramount but for the Lockups. And Davis himself admitted that he had "never heard" anyone say that the Lockups were the only way to induce anybody to bid for Paramount, or that it was even necessary to induce Viacom to bid -- a bid from QVC would have been forthcoming without any lockups. Davis Dep. 114, 300.*

The Lazard chronology prepared by Ezersky shows that the Lock-ups certainly did nothing to induce a better bid from Viacom. Ex. 51. That chronology establishes that: (1) on July 7 Paramount rejected the same exchange ratio it then agreed to on September 12, with the only change in value being the rise in Viacom stock price that accompanied Redstone's massive purchases -- a circumstance that obviously troubled even Lazard; (2) in late August, Viacom withdrew its request for a lock-up while offering a $69 transaction; (3) when Paramount's management agreed to the Lock-ups on September 7, it got in return a deal that was no more valuable than the deal without the lock-up that Viacom had offered only two weeks earlier. The note in Lazard's files offers the only rational

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* Davis Dep. 300 (emphasis added):

> Q: Now, did you believe, or do you believe that the Viacom bid was necessary to elicit a bid from QVC?
>
> A: I have no idea. I don't believe so and I can't think one had anything to do with the other.

In his testimony, Davis emphatically would not even say that Paramount had even objected to the Viacom demand for the stock option. Davis Dep. 86.

explanation: "Lock-up -- want deal to look strong." Ex. 6. Similarly, as one director conceded: "this was a question of protecting the deal." Silberman Dep. 108. In short, the Lock-up was not to induce Viacom to do anything; it was to "protect the deal" by impeding others -- a purpose and effect that is not permissible under Delaware law.*

Moreover, one key feature of the stock option -- Viacom's ability to purchase the optional shares with a note rather than cash -- is irreconcilable with any purpose other than to deter competing bids. This highly unusual feature requires a competing bidder to finance the entire cost of acquiring the optioned shares, unlike the typical option which at least requires the optionee to pay cash at the option price. The note feature thus exacts an enhanced financing cost on a competing bidder, with no possible justification in terms of "compensating" Viacom for anything.**

The record further demonstrates that the Lockups were certainly not the subject of the requisite careful consideration by the Paramount directors. As set out in the Statement of Facts supra, before they approved the Lockups, the directors received no copies or summaries of its provisions (or any writing on the subject whatever), no information about stock options and break-up fees in other transactions, no advice (even oral) as to the Lockups' effect on other possible bidders. Nor was there discussion about such matters at board meetings. No director asked for any analysis of the Lockups. The minutes of the September 9 and 12 board meetings contain not one word on the terms of the Lockups. The directors were never told that Viacom had, only two weeks before, offered

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* Events have more than established that the Lockups certainly did not induce Viacom to make its best bid on September 12. Moreover, discovery has shown that on the very next day after the initial Viacom deal was announced, Redstone was ready and willing to pay more for Paramount: on that day Redstone urged Malone to stay out of the bidding for Paramount because "all we would succeed in doing is increasing the price of the transaction to him." Malone Dep. 88. Redstone called Diller on the same day with the same message. Diller Dep. 183 ("He said all you will do is cost me money.").

** Even Greenhill of Smith Barney, with his long experience in the acquisition field, was not aware of any other stock option with such a note provision. Greenhill Dep. 172. This unusual feature of the option was not explained to the Paramount directors (at least not so that they understood it or remembered anything). See Silberman Dep. 92-93.

essentially the same deal without lockups. The directors, admittedly, made no determination of the Lockups' reasonableness nor did they have a basis to do so. Small Dep. 51-52, 61, 64, 194, 229-30, 249; Pattison Dep. 116, 119.

The directors' lack of care before agreeing to give Viacom an option on 20% of their company, plus a $100 million break-up fee, is simply astounding. The directors did not even know whether Paramount or Viacom had proposed the Lockups. Small Dep. 52. No one told the board that Viacom had insisted on the Lockups. Small Dep. 64. They apparently believed that the Lockups -- far from any notion of being a pre-condition on Viacom's part -- had been included because "<u>we</u> wanted it to happen." Small Dep. 51. There was no consideration given to whether the Lockups could deter other bidders. Small Dep. 229-30; Pattison Dep. 85, 115-17; Davis Dep. 125.* There was apparently no consideration of the fact that the higher the competing bid, the greater the deterrent effect of the option. Davis Dep. 116. There was no consideration to the interplay between the 20% stock option and the 80% supermajority vote requirement for business combinations in Paramount's charter. Pattison Dep. 90.

And when the board agreed to the amended merger agreement on October 24 -- including their agreement to allow Viacom to proceed by tender offer and remove the Right Plan in Viacom's favor, at a time that QVC was offering the same $80 without any lock-ups -- there was no consideration given to even asking that Viacom, in return, relinquish the Lockups or that their terms be at least renegotiated. Pattison Dep. 146-47. Importantly, the Paramount board at that point had all the leverage. Viacom was obviously desperate to launch a tender offer to gain a timing advantage on QVC, which had just announced its plan to commence a tender offer at $80. As Redstone testified, in the October 23-24 negotiations, Viacom "gave everything that [Paramount] demanded." Redstone Dep.

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* Typical of the directors' arrogance, director Pattison simply assumed that it was "highly unlikely that there would be a new entrant into the situation" and, on that (mistaken -- and known by Davis to be false) basis, he "was not concentrating on that point." Pattison Dep. 116, 118.

223. The Paramount directors surely must have realized how foolish they had been to have locked up the original Viacom deal at $69.14. But neither the Paramount directors, nor the Paramount management that was running the show, even asked to undo or diminish the Lockups. Instead Paramount renewed the Lockups, getting in return nothing but an $80 deal that QVC was offering without Lockups.

These Lockups cannot stand.

F. The Viacom tender offer and merger are coercive and preclusive defensive reactions violative of Unocal

Before the business judgment rule is applied to a board's adoption of defensive measures, the burden lies with the board of directors to prove (a) reasonable grounds for believing that a danger to corporate policy and effectiveness exists; and (b) that the defensive measure adopted is reasonable in relation to the threat posed. Paramount, 571 A.2d at 1152; Unocal Corporation v. Mesa Petroleum Co., Del. Supr., 493 A.2d 946, 954-55 (1985). At a minimum, each and every response to a hostile offer is tested under this Unocal standard, Gilbert v. El Paso Co., Del. Supr., 575 A.2d 1131, 1143 (1990), including the substitution of a new acquisition proposal for a pre-existing merger agreement. Paramount, 571 A.2d at 1152.

This enhanced standard is not only applicable to action taken in response to a pending bid; it extends to action taken in anticipation of such a bid. See Moran v. Household International, Inc., Del. Supr., 500 A.2d 1346, 1354 (1985); Paramount, Del. Ch., slip op. at 69 n.21 ("Unocal form of analysis will also be utilized when a preemptive defensive measure is deployed, where the principal purpose of the action (and not simply a collateral, practical effect) is defensive in a change of control sense.").

In the present case, the Unocal analysis applies, at a minimum, to each of the decisions made by the Paramount directors subsequent to QVC's first proposal: the refusals to negotiate, the approval of the new merger agreement with Viacom with the renewed and modified Lockups, the conditional agreement to lift the Rights Plan with respect to

Viacom's tender offer but leave the Rights Plan in place with respect to the QVC offer, and the approval of the Viacom merger and option agreements under 8 Del. C. § 203. These decisions cannot withstand scrutiny under the Unocal test.

The stock option and termination fee provisions of the original merger agreement also were defensive responses, viz, their principal purpose was to deter a potential, competing bidder. As noted, supra, even Paramount's directors have testified that Paramount agreed to these provisions in order to deter others from bidding for Paramount. And the record is replete with testimony that both Paramount and Viacom were anticipating such bids and acted to preclude or discourage them.

For example, in June of 1993, Davis called John Malone of TCI and told Malone that Malone "needed to keep Barry essentially on a leash and that [Davis] felt that I was probably the only guy who could prevent Barry Diller form doing something aggressive relative to Paramount." Malone Dep. 73-75. Davis testified that he had a "good number" of discussions with Malone "on the subject of Mr. Diller's intention to mount a bid for Paramount." Davis Dep. 64. Davis conceded that he was repeatedly told by Malone that Barry Diller was readying a bid for Paramount (Davis Dep. 60-66), and although at his deposition Davis professed that he disbelieved Mr. Malone (Davis Dep. 62,66), the evidence is to the contrary: in July Davis told Diller that he knew Diller was planning to make a bid for Paramount. Diller Dep. 181.

Shortly thereafter, on June 28, Paramount for the first time began "serious" negotiations with Viacom. PCI 14D-9. When these talks collapsed, on July 7, Davis tried a different tack, inviting Diller to a lunch at which he told Diller that he knew Diller was planning a hostile bid for Paramount. Diller Dep. 180-81.

Following Davis' lunch with Diller, Davis continued to pursue the concept of a transaction with Viacom, albeit the formal negotiations had been broken off. In Davis' words, he never considered the discussions "stopped" or "cancelled" -- during this period "they were always ongoing." Davis Dep. 69-70. Lazard continued communicating on the subject with Smith Barney, and Lazard monitored the rising price of Viacom stock and Redstone's continuing heavy purchases (and sent this information on to Davis and the other Paramount executives involved in the transaction). And Paramount sought to re-open discussions with Viacom by seeking an August meeting with a skeptical Redstone to resolve the "management issue." Ex. 85. Ultimately, these efforts were successful and led to the resumption of negotiations.

At the September board meetings, both Lazard and the directors recognized that QVC and other companies were potential bidders for Paramount. Ex. 54 at 21-22; Pattison Dep. 28, 30-31 (QVC or TCI were possible suitors "that had the keenest interest").

Finally, Redstone was well aware that his deal with Paramount needed to be "protected" from Diller and Malone. The day after the Viacom merger agreement was announced on September 12, Redstone called Malone:

> He basically wanted to say that it would most unfortunate if we found ourselves bidding against each other for Paramount, because all we would succeed in doing is increasing the price of the transaction to him.

Malone Dep. 87-88. Redstone made a similar call to Diller the same day. Diller Dep. 182-83. Given the above facts, it would deny reality to treat the Lockups as anything other than a "defensive reaction".

* * *

In its most recent application of the <u>Unocal</u> test, the Delaware Supreme Court described it as a flexible, not abstract standard which is not to be mechanically applied. <u>Paramount</u>, 571 A.2d at 1153. The flexibility of the standard is evidenced by both prongs of the test: threat and reasonable response. The threats to which a board may respond are broadly stated and fact specific to each case. <u>Id</u>. By the same token, the reasonableness of the response to any threat "requires an evaluation of the importance of the corporate objective threatened; alternative methods of protecting that objective; impacts of the 'defensive' action, and other relevant factors." <u>Id</u>. at 1154.

In Paramount, the Supreme Court reiterated the importance of the second prong, stating: "[i]t is not until both parts of the Unocal inquiry have been satisfied that the business judgment rule attaches to defensive actions of a board of directors," and the Supreme Court specifically rejected the view that the reasonableness test is satisfied merely by demonstrating objective, good faith deliberations by the board. Id. at 1154 n.18. In particular, the Supreme Court suggested that responses which coerce the shareholders to accept a board-sponsored alternative and which preclude alternative transactions are suspect. Id. at 1153.

In the present case, the tender offer being mounted by Viacom with the approval of Paramount is admittedly coercive and unquestionably will preclude the shareholders from choosing any alternative transaction. The Viacom tender offer is a classic product of discrimination by the Paramount board against one bidder and in favor of management's preferred bidder. As with the transactions enjoined in Revlon, Macmillan I and Macmillan II, this defensive tender offer should be enjoined.

The Threat: QVC's interest in acquiring Paramount and the original QVC merger proposal cannot be considered any material threat to Paramount or its shareholders. Indeed, the original QVC proposal provided $2 billion value in excess of Viacom's presumably non-threatening, "locked up" $69 merger. Felix Rohatyn, Paramount's investment banker, testified that he did not consider the QVC merger proposal to be a threat to Paramount or its shareholders. Rohatyn Dep. 80. However, Paramount responded to QVC's proposal with the stonewall of contractual prohibitions on discussions and then delay when these supposed contractual restrictions on discussions were overcome.

The QVC tender offer, announced on October 21, was QVC's only vehicle for commencing regulatory review of its acquisition. Otherwise, Paramount had placed QVC in the "catch-22" of refusing to negotiate because QVC lacked regulatory approvals which QVC could only obtain if it either (i) commenced a tender offer or (ii) executed a merger agreement with Paramount. Faced with this dilemma, well known to Paramount and its advisers, QVC was forced to announced a tender offer. Rohatyn Dep. 91-94; see Diller Dep. 163-66.

At the time the QVC tender offer was commenced, QVC told Paramount, both publicly and privately, that it desired negotiations with Paramount designed to obtain the best transaction for the Paramount shareholders. Rohatyn Dep. 95-96. While QVC's tender offer is a partial tender offer, QVC made clear -- on the very cover of its Offer to Purchase, and in its communications to the Paramount board -- its willingness to enter into a merger agreement which would provide for a shareholder vote, the same consideration for all shareholders, and would not contain any of the "lockups" which Viacom supposedly demanded. Id. Indeed, the proposed merger agreement did not have any financing contingency and already was fully financed. Again, Felix Rohatyn testified that he did not consider the QVC tender offer to be a threat to Paramount or its shareholders. Rohatyn Dep. 94-95.

The Response: Rather than negotiate under the ample protection of its Rights Plan, Paramount went to Viacom and refashioned their $69 merger agreement into a significantly different transaction that responded to QVC's "two-tiered" offer (which QVC was prepared to withdraw in favor of a merger agreement) with a tender offer and merger agreement more threatening to shareholders than QVC's while, at the same time, continuing a policy of completely refusing to deal with QVC.

In a document that Paramount's general counsel thought had been destroyed, Lazard's and Paramount's analysis about how Paramount should respond to the new Viacom offer is candidly set forth. The document is significant enough to be reviewed in its entirety because it reveals the assessment that Viacom's proposal was "onerous" and coercive." The document states that:

> We have to agree under the merger agreement to a coercive tender offer at 43% level. Even worse than 51% tender, this stampedes stockholders to take front end. Back end may be worth a lot less . . . The result is that if higher offer were made by QVC, we would be precluded from giving our shareholders the benefit of it by our agreement not to pull the pill . . . while QVC is blocked by

> us, Viacom can take whatever shares that come in -- and they'll come in because the QVC offer can't be consummated.

Ex. 92.

It was recommended that the most prudent position would be to "keep the pill in place for everyone." Id.; Rohatyn Dep. 110-11. But it was not to be. Rather, the next day Lazard orally would opine that the Viacom tender offer for 43% with a second step merger was "fair." The pill would be lifted for Viacom's offer, but not for QVC, and not utilized by the board to seek to obtain the best bid. Now, only this Court can preclude this "response" -- which threatens to leave the shareholders with less than the best available value.

IV. THE PARAMOUNT RIGHTS PLAN AND OTHER IMPEDIMENTS TO THE QVC OFFER CANNOT BE UTILIZED TO FAVOR THE VIACOM OFFER AND PRECLUDE THE QVC OFFER.

No one has ever thought that a Rights Plan could be utilized by a board of directors to make one tender offer beat a competing tender offer. That simple, and basic, principle requires that the Paramount board not use the Rights Plan to favor the Viacom tender offer over the QVC tender offer. Both the Viacom and VC tender offers have the same structure (cash for 51% of the shares, with an equal value stock second-step).

This principle is so clear that the Delaware Supreme Court remarked in Barkan:

> Because potential bidders know that a pill may not be used to entrench management or to unfairly favor one bidder over another, they have no reason to refrain from bidding if they believe that they can make a profitable offer for control of the corporation.

Barkan, 567 A.2d at 1287, citing Moran v. Household International, Inc., Del. Supr., 500 A.2d 1346, 1354-56 (1985). See also Mills Acquisition Co. v. Macmillan Inc., Del. Ch., C.A. No. 10168, Jacobs, V.C. (Oct. 18, 1988), slip op. at 50 (requiring Macmillan board to remove its Rights Plan as to Maxwell tender offer even though relief denied against management-sponsored KKR bid), rev'd on other grounds, Del. Supr., 559 A.2d 1261

(1989); MacAndrew & Forbes, Inc. v. Revlon, Inc., Del. Ch., 501 A.2d 1239, 1251 (1985) (the Rights Plan "cannot now stand in the way of the bidding process. . . . Pantry Pride is entitled to market its latest bid without the entanglements of the Rights Plan."); CRTF Corp. v. Federated Department Stores, Inc., 683 F. Supp. 422, 439 (S.D.N.Y. 1988) (a Rights Plan "provides the directors with a shield to fend off coercive offers, and with a gavel to run an auction"; it is "not a 'show stopper'").

Paramount's own documents reflect its recognition that its pill could not legitimately be used to make Viacom a winner over QVC. See the discussion in Ex. 92.

Any claim by the Paramount directors that they should be entitled to use their pill to favor Viacom over QVC would be grotesque. In Robert M. Bass Group, Inc. v. Evans, Del. Ch., 552 A.2d 1227 (1988), appeal dismissed as moot, Del. Supr., 548 A.2d 498 (1988), this Court categorically rejected the claim that directors could preclude the stockholders from choosing between their deal (a restructuring) and a third party tender offer -- even though the directors believed that their deal was preferable because it permitted the stockholders to retain their equity and the prospect of long term value:

> The defendants respond that the restructuring is reasonable because: (i) it allows shareholders to realize immediate value while retaining their equity interest, with the prospect of receiving long term value; (ii) it creates a structure designed to result in a higher market value for each separate component, and (iii) it "incentivizes" [sic] management to efficiently manage the companies by "tying up" a large portion of management's net worth in the equity of these companies, thereby inducing them to increase their stock value.
>
> But these rationales, even if accepted, do not justify forcing shareholders to accept an economically inferior transaction while, at the same time, precluding them from considering an economically superior one. The directors certainly were free to propose the restructuring to their shareholders. However, as fiduciaries they were not free to "cram down" that transaction in order to "protect" their shareholders from a noncoercive, economically superior one. (footnote omitted). Under Unocal the directors were obligated to give the shareholders a choice. The restructuring, because it deprives them of that choice, is manifestly unreasonable.

Id. at 1243-44.

In City Capital Associates v. Interco Inc., Del. Ch., 551 A.2d 787 (1988), this Court recognized the stockholders' right to control their own investment, and the impermissibility of using a Rights Plan to defeat the stockholders' choice of whether to sell their shares:

> Our corporation law exists, not as an isolated body of rules and principles, but rather in a historical setting and as part of a larger body of law premised upon shared values. To acknowledge that directors may employ the recent innovation of "poison pills" to deprive shareholders of the ability effectively to choose to accept a noncoercive offer, after the board has had a reasonable opportunity to explore or create alternatives, or attempt to negotiate on the shareholders' behalf, would, it seems to me, be so inconsistent with widely shared notions of appropriate corporate governance as to threaten to diminish the legitimacy and authority of our corporation law.

Id. at 799-800. Accord, Grand Metropolitan PLC v. Pillsbury Co., Del. Ch., 558 A.2d 1049, 1060 (1988).*

The Paramount Rights Plan cannot be used to favor Viacom and preclude QVC. By the same token, the Paramount board cannot legitimately use 8 Del. C. § 203 or the supermajority vote requirement of the Paramount charter (Article XI) in a discriminatory, and preclusive, manner to favor Viacom and defeat QVC.

V. IRREPARABLE HARM AND THE BALANCE OF HARDSHIPS

There can be no doubt that QVC, as well as Paramount's public stockholders, face imminent, irreparable harm if the Lock-Ups are not enjoined, and Paramount and

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* Interco and Pillsbury ordered pills removed even where (unlike here) the target's board had not agreed to remove the pill for a favored bidder. This case is thus a far easier one since it is inconceivable that a pill could be used to favor a management-supported bid while precluding a competitive bid.

Thus, whether or not the Supreme Court's Paramount opinion can be read as suggesting that, contrary to Interco and Pillsbury, a board of directors can use its pill to "Just Say No" to an unsolicited takeover bid, that issue has no pertinence here. The Paramount board has not "Just Said No." The Paramount board has "Said Yes, Yes, Yes" to Viacom and "Said Never, Never, Never" to QVC. (Moreover, both this Court's and the Supreme Court's opinions in Paramount distinguished between blocking a takeover bid via implementation of a well-planned corporate strategy, as contrasted with "a decision not to redeem a poison pill, which by definition is a control mechanism and not a device with independent business purposes." Paramount, Del. Ch., slip op. at 77 n.22; see Paramount, Del. Supr., 571 A.2d at 1155 n.19 (contrasting an ESOP defense as not "primarily a device to affect or secure corporate control").)

Viacom are permitted to coerce the stockholders into accepting the Viacom offer and ending this bidding contest on November 22. Nor can there be any doubt that the balance of hardship favors the entry of an injunction.

As Justice Walsh wrote for this Court in Revlon:

> From the standpoint of irreparable harm, unless Pantry Pride is permitted to market its bid free of the restrictions imposed by the lock-up option, with its triggering mechanism, its acquisition effort is at an end. In terms of relative hardship to the parties the need for both bidders to compete in the marketplace far outweighs the limiting of Forstmann Little's contractual rights.

Revlon, 501 A.2d at 1251.* See also In Re Holly Farms Corporation Shareholders Litigation, Del. Ch., C.A. No. 10350, Hartnett, V.C. (Dec. 30, 1988), slip op. at 17 (finding irreparable harm to bidder and public stockholders based on analysis identical to that of Justice Walsh in Revlon); accord, Yanow v. Scientific Leasing, Inc., Del. Ch., C.A. No. 9536, Jacobs, V.C. (Feb. 5, 1988, revised Feb. 8, 1988), slip op. at 15 (irreparable harm shown in a case where a "bidder or higher bidder has been shown to be waiting in the wings" or where "an injunction is needed to enable a higher bidder to materialize").

In Robert M. Bass Group, Inc. v. Evans, Del. Ch., C.A. No. 9953, Jacobs, V.C. (June 10, 1988) ("Macmillan I"), this Court reached a similar conclusion:

> This transaction, if found to constitute a breach of the defendants' fiduciary duty to the plaintiffs, unless restrained, will result in irreparable damage to Macmillan shareholders, including the Bass Group. The harm . . . would be irreparable, because the restructuring will irretrievably alter Macmillan's capital and corporate structure and would adversely affect the quality of the shareholders' investment and prevent or drastically reduce the shareholders' opportunity to realize a greater value for their shares than is being afforded by the restructuring, all without any opportunity for the shareholders to have any say.

Transcript at 9.

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* On appeal, the Supreme Court affirmed Justice Walsh's grant of a preliminary injunction, and expressly approved his irreparable harm analysis. See Revlon, 506 A.2d at 184-85.

In the later proceeding on the plaintiffs' motion for a preliminary injunction in Macmillan I, the Court reaffirmed its finding of irreparable harm, rejected the defendants' argument that the threat of jeopardizing the company-favored transaction outweighed any harm to the plaintiffs and decided against defendants on the balance of hardship point:

> Finally, the balance of equities favors the grant of a preliminary injunction. Macmillan's contrary argument appears to be that any injunction will sound the "death knell" of the restructuring, and that as a result, the Bass Group would be able to withdraw their offer but the shareholders would be left without any opportunity to realize value on their investment. However, the Bass Group has represented its willingness to make a tender offer (contingent on Board approval) if an injunction is granted. Moreover, defendants have not shown why if the restructuring is ultimately found to be valid, it could not be revived and allowed to go forward at the that time.

Robert M. Bass Group, Inc. v. Evans, Del. Ch., 552 A.2d 1227, 1247 (1988), appeal dismissed as moot, Del Supr., 548 A.2d 498 (1988) at 1247.

Here, as in each of these cases, the consummation of the Viacom/Paramount deal will "irretrievably alter" Paramount's capital and corporate structure. As the Court recognized in Gimbel v. Signal Cos., Inc., Del. Ch., 316 A.2d 599 (1974), aff'd, Del. Supr., 316 A.2d 619 (1974), once a transaction of the complexity and magnitude of the Viacom/Paramount transaction closes, it will be impossible to "unscramble the eggs" if it is later determined that the transaction was improper.

As in Macmillan I, the Paramount stockholders have no true say in the matter because they will, absent injunctive relief, be coerced into tendering into the Viacom partial tender offer.* See Ivanhoe, 533 A.2d at 605 (tender offer is coercive if it is "structured and timed so as to effectively deprive stockholders of the ability to choose a competing offer -- also at a fair price -- that the shareholders might have found preferable"); AC Acquisitions Corp. v. Anderson, Clayton & Co., Del. Ch., 519 A.2d 103, 116 (1986) (recognizing the coercion inherent in a tender offer containing no promise of equivalent cash in a follow-up merger, where the target company has cut off the stockholders' ability to consider competing offers).

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* See Rattner Dep. 200-01.

In previous cases, this Court has not hesitated to enjoin manipulative conduct that interferes with stockholder choice in the face of a company-sponsored transaction -- even granting mandatory injunctive relief to remedy fiduciary breaches of the type here shown. See Mills Acquisition Co. v. Macmillan, Inc., Del. Ch., C.A. No. 10168, Jacobs, V.C. (Oct. 17, 1988, revised Oct. 18, 1988) (ordering redemption of poison pill), rev'd on other grounds, Del. Supr., 559 A.2d 1261 (1988); Grand Metropolitan PLC v. Pillsbury Co., Del. Ch. 558 A.2d 1049 (1988) (same); City Capital Associates L.P. v. Interco Inc., Del. Ch., 551 A.2d 787, 800 (1988) (same). And, in still other cases, the Court has enjoined the company-sponsored transaction altogether -- compelling the company to go back to the bargaining table and deal fairly with the competing bidders. See Robert M. Bass Group, Inc. v. Evans, Del. Ch., 552 A.2d 1227 (1988) (enjoining reorganization of company that would preclude success of competing proposal), appeal dismissed as moot, Del. Supr., 548 A.2d 498 (1988); AC Acquisitions Corp. v. Anderson, Clayton & Co., Del. Ch., 519 A.2d 103 (1986) (enjoining self-tender that would preclude success of competing tender offer being blocked by company); accord Macmillan II, 559 A.2d at 1288 (enjoining various provisions of merger agreement with company-favored bidder, so that competing bids could be evaluated on a level playing field); In Re Holly Farms Corporation Shareholders Litigation, Del. Ch., C.A. No. 10350, Hartnett, V.C. (Dec. 30, 1988) (same).

CONCLUSION

Plaintiff QVC's motion for a preliminary injunction should be granted.

Dated: Wilmington, Delaware
November 11, 1993

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Josy W. Ingersoll, hereby state that I caused the foregoing document to be served on the persons listed below by causing true copies thereof to be delivered at the addresses shown on November 11, 1993:

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