JAMES T. McKINSTRY
MAX S. BELL, JR.
RICHARD J. ABRAMS
CHARLES F. RICHARDS, JR.
THOMAS P. SWEENEY
PIERRE S. DuPONT IV
ROBERT H. RICHARDS, III
R. FRANKLIN BALOTTI
MARTIN I. LUBAROFF
RICHARD G. ELLIOTT, JR.
WENDELL FENTON
ALLEN M. TERRELL, JR.
GLENN C. KENTON
RICHARD G. BACON
STEPHEN E. HERRMANN
JULIAN H. BAUMANN, JR.
DANIEL L. KLEIN
DONALD A. BUSSARD
WILLIAM J. WADE
THOMAS L. AMBRO
JESSE A. FINKELSTEIN
SAMUEL A. NOLEN
THOMAS A. BECK
GREGORY P. WILLIAMS
JOHN A. PARKINS, JR.
PAUL M. ALTMAN
GREGORY V. VARALLO
MARK J. GENTILE
ROBERT J. KRAPF
KEVIN G. ABRAMS
ERIC A. MAZIE
ROBERT W. WHETZEL
W. DONALD SPARKS, II
C. STEPHEN BIGLER
C. MALCOLM COCHRAN, IV
ANNE C. FOSTER
CYNTHIA D. KAISER

RICHARDS, LAYTON & FINGER
ONE RODNEY SQUARE
P.O. BOX 551
WILMINGTON, DELAWARE 19899
TELEPHONE (302) 658-6541
TELECOPIER (302) 658-6548
WRITER'S DIRECT DIAL NUMBER

ALLISON L. AMORISON
DAVID J. ANDERSON
SYBIL M. L. BURGE
MARK D. COLLINS
FREDERICK L. COTTRELL, III
DONEENE K. DAMON
DANIEL J. DeFRANCESCHI
CLAUDIA A. DELGROSS
JOHN T. DORSEY
DANIEL A. DREISBACH
DARLENE M. FASIC
MATTHEW J. FERRETTI
MATTHEW E. FISCHER
CRAIG D. GREAR
SCOTT R. HAIBER
WILLIAM J. HAUBERT
TODD V. JONES
BERNARD J. KELLEY
JAMES G. LEYDEN, JR.
JACQUELINE A. LOUGHMAN
SEAN P. McDEVITT
MARK A. MORTON
LISA A. PAOLINI
HOWARD J. POLLACK
DAVID L. RENAULD
HELEN M. RICHARDS
ROBERT J. STEARN, JR.
HELEN L. WINSLOW
WILLIAM A. YEMC

CONFIDENTIAL
RESTRICTED – FILED UNDER SEAL

(302) 651-7738

November 21, 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., Del Ch., C.A. No. 13208; In re Paramount Communications Inc. Shareholders Litig., Del. Ch., C.A. No. 13117**

Dear Vice Chancellor Jacobs:

We submit this letter on behalf of Paramount Communications Inc. ("Paramount") to address the Court's inquiry concerning the actions taken by the Paramount Board at the Special Meeting of the Board on November 15, 1993. This

letter reflects the discovery conducted by the parties on November 19 and 20 pursuant to the direction of the Court.[1/]

Paramount welcomes the opportunity to supplement the record before the Court. In this connection, the Court will recall that QVC Network, Inc. ("QVC") amended its tender offer at 5:29 p.m. on Friday, November 12. The Paramount Board considered QVC's amended offer on Monday, November 15. This Court heard argument on the motion of QVC and the plaintiff stockholders for a preliminary injunction at 10:00 a.m. on Tuesday, November 16. Consequently, the Court did not have the benefit of a full evidentiary record concerning either the materials that were before the Board on November 15 or the actions taken by the Board at its meeting.

Nonetheless, nothing that happened on November 12 or November 15 altered

---

1/ See November 18, 1993 Transcript of Telephone Conference Hearing before the Court at 4. On November 18, Paramount produced all documents considered by Paramount's Directors in advance of and at the November 15 Board meeting, as well as the minutes of the November 15 meeting. Copies of these documents were submitted to the Court the following day. On November 19 and 20, Paramount produced for depositions three independent directors, James A. Pattison, Irwin Schloss, and Irving R. Fischer. Steven Rattner of Lazard Freres & Co. ("Lazard"), Paramount's financial advisor, was also deposed by plaintiffs' counsel on November 19. In addition, Lazard produced documents relating to its presentation to the Board on November 15.

In order to minimize the volume of paper submitted to the Court, Paramount will not resubmit copies of the deposition transcripts of Messrs. Pattison, Schloss, Fischer, and Rattner and the exhibits thereto, delivered to the Court by the Young, Conaway firm. Paramount has submitted herewith a Second Affidavit of Anne C. Foster dated November 21, 1993, references to which are noted as "PSEx. __". As in the Brief of the Paramount Defendants in Opposition to the Motion of the Plaintiffs for a Preliminary Injunction dated November 14, 1993 ("Paramount Brief"), citations herein to "PEx. __" refer to the exhibits submitted with the previously submitted Affidavit of Anne C. Foster. Citations to "QEx. __" refer to the exhibits submitted with the affidavits of David C. McBride, counsel for plaintiff QVC.

the bedrock facts and law governing this case: (1) under Delaware law, directors manage corporations, not bidders or arbitrageurs; (2) the Paramount Directors never intended, by their thoughts, words or actions, to sell the Company; (3) not even QVC tries to challenge the determination that a merger with Viacom is an excellent strategic fit for Paramount; and (4) accordingly, Paramount's directors have no obligation to check the daily stock prices and "sell" the company to the so-called "bidder" with a higher offer at a given moment.

(1) Plaintiffs' Motion for Injunctive Relief

Since September -- and certainly in the last ten days -- QVC's "offer" for Paramount has been a continuously changing set of terms, conditions, co-bidders, and "prices" that has substantially complicated the Board's job and this litigation. The relevance of these changing circumstances to the motion before the Court thus needs to be clarified.

First, Paramount believes that QVC's changing offers have little or nothing to do with QVC's request that the termination fee and option granted to Viacom be retroactively eliminated. Those provisions were valid when agreed upon, and they are valid now; later events simply do not reflect back upon the business judgment of the Paramount Board in September.[2/] Indeed, in one sense, QVC's everchanging tender

---

2/ It is hornbook law that a board's judgment must be viewed on the basis of the information available to it when the judgment is exercised. Smith v. Van Gorkom, (continued...)

offer has been constant: it is conditioned upon elimination of those valid terms and thus is, as it has always been, not capable of acceptance.

Second, QVC's changing offers and its shifting array of backers and "Co-bidders" has had the effect of unnecessarily complicating this motion, even though the motion is not about offers or revisions made after the motion was filed. Paramount submits that the Court should resist granting relief on grounds that are anticipatory or prospective in nature. The Paramount Board has evaluated QVC's offers as they have been made. An advisory opinion concerning a possible future unconditional QVC offer, or a "higher" QVC offer, is both unnecessary and, we believe, improper. Further, at a certain point, QVC's refusal or inability to make an offer actually capable of acceptance is a factor that affects both a Board's evaluation of the facts before it, and a court's evaluation of the Board's business judgment. It is a well established principle of Delaware law that Paramount need not freeze its business plans to allow QVC to make additional indefinite "offers" in the hope of generating further litigation.[3] In

---

[2](...continued)
Del. Supr., 488 A.2d 858, 874 (1985); Moran v. Household Intern., Inc., Del. Ch., 490 A.2d 1059, 1075, aff'd, Del. Supr., 500 A.2d 1346 (1985); Aronson v. Lewis, Del. Supr., 473 A.2d 805, 812 (1984).

[3] QVC's appetite for additional, time-consuming discovery was well illustrated by counsel's request, made during the November 18 conference call with the Court, that the closing of Viacom's tender offer be stayed for a week while QVC conducted six or seven depositions concerning the fully-documented events at the November 15 meeting. See November 18, 1993 Transcript of Telephone Conference Hearing before the Court at 3-8.

determining that QVC's November 12 offer did not constitute a better alternative to Paramount's existing merger plans with Viacom, the Board relied, in part, on the financing, regulatory and other conditions embodied in that offer which, at a minimum, threatened delays in the closing of the QVC offer and, quite possibly, could lead to the proposed merger never being consummated.[4/] Unquestionably, the Board was entitled to take these conditions into consideration in making its decision.

Third, QVC's motion was brought prior to the latest set of changes to QVC's offer. It remains true that QVC's unilateral actions do not thrust Paramount into "Revlon-Land", and do not cut off the Paramount Board's time horizon, which encompasses both the short-term (vis-a-vis the "front end" tender offers) and the long-term (the 49% "back end" equity stakes). Thus, the events of last week are simply not relevant to determination of QVC's contention that Revlon applies to this case.

4/ See Gilbert v. El Paso Co., Del. Supr., 575 A.2d 1131, 1135, 1145-56, 1148 (1990) (upholding board action against a highly-conditional Burlington offer which could be terminated "upon the occurrence of any one of a number of specified events"); Edelman v. Phillips Petroleum Co., Del. Ch., C.A. No. 7899, slip op. at 11-12, Walsh, V.C. (Feb. 12, 1985) ("Mesa's refusal to commit itself to the terms of the second-step clearly justified the belief by Phillips management and directors that Mesa . . . did not have the best interest of Phillips and all its shareholders in mind"); Unocal Corp. v. Mesa Petroleum Co., Del. Supr., 493 A.2d 946, 955-56 (1985) (directors entitled to consider "the risk of nonconsummation, and the quality of securities being offered in respect of Mesa's second-step proposal); Citron v. Fairchild Camera & Instrument Corp., Del. Supr., 569 A.2d 53, 63, 66 (1989) (upholding board's acceptance of lower Schlumberger offer and noting with approval the "overriding, and eminently reasonable, concern of the directors" regarding the "indefinite nature" of Gould's higher competing proposal).

Fourth, Paramount submits that it is simply misleading for QVC to tout its November 12 offer as a "$90 offer" or to quantify -- based upon hour-to-hour stock market prices -- an alleged billion dollar difference between offers. QVC's offer must be evaluated in detail apart from such short-sighted and fundamentally inaccurate advertisements, as the Paramount Board has done. Even though QVC has repeatedly attempted to oversimplify the economics of its "$90 offer," QVC understands full well the critical importance of considering the back end apart from speculation-driven stock market prices. Indeed, QVC's counsel stated during last Tuesday's oral argument that, in assessing the non-cash portion of Viacom's and QVC's proposals, the "momentary market value" of each company's stock is not "conclusive." 11/16/93 Hearing Tr. at 56.[5/] Does the Board have an obligation to appraise the non-cash consideration being offered? "Of course it does," according to QVC's counsel, Id. at 216. Indeed, QVC's counsel has correctly recognized the need for the Board to do exactly what it did on November 15:

> "I agree with Mr. Baskin. I don't think you can look at the stock market quotes . . . . I said it was a factor. It is indicative. I would not remotely say that the fact our offer is $1,150,000,000 more as of the close yesterday -- it will probably be different today -- is conclusive. I think it is relevant.

Id. at 218.

Moreover, even if $90 were a real and fair quantification of the QVC "offer"

5/ See also Senior Tr. at 51-52 (detailed analysis required).

-- which it is indisputably not -- "this Court has long recognized that the highest bid is not necessarily the best bid." Caruana v. Saligman, Del. Ch., C.A. No. 11135, slip op. at 10, Chandler, V.C. (Dec. 21, 1990). As Chancellor Allen wrote in In re J.P Stevens & Co. Shareholders Litig., Del. Ch., 542 A.2d 770 (1988), even in the context of a Revlon-type auction, achieving the best possible transaction for shareholders:

> does not mean that material factors other than "price" ought not to be considered and, where appropriate, acted upon by the board. Such consideration might include form of consideration, timing of the transaction or risk of non-consummation.

Id. at 781. See also Simkins Indus. Inc. v. Fibreboard Corp., Del. Ch., C.A. No. 5369, Marvel, C. (July 28, 1977) (finding it proper for board to accept lower bid that was more certain as to its terms); Smith v. Good Music Station Inc., Del. Ch., 129 A.2d 242 (1957) (upholding decision to accept a lower, but unconditional bid).

Fifth, QVC -- unlike Viacom -- still has not waived the financing condition to its offer and QVC's financing commitments are subject to, among other conditions, invalidation of the Viacom stock option and termination fee and it still does not have the money to pay for an offer that does not contain such conditions. Delaware courts repeatedly have disparaged such highly-conditional or ephemeral offers.

(2) The Action Taken at the November 15 Special Meeting

Discovery has now confirmed that the Paramount Board analyzed and considered QVC's amended tender offer before deciding, in the exercise of its business

judgment, that the Viacom offer was the best alternative available for the Paramount stockholders. The Directors therefore chose to recommend against tendering into the QVC offer. The record demonstrates that the Directors based their decision on the factors identified in the Schedule 14D-9 filed with the Securities and Exchange Commission the day after the Board meeting.[6/] Specifically, the Paramount Board concluded that the QVC offer was not real and that its long-term value was not superior to that available pursuant to the Viacom Merger Agreement.

QVC's offer was conditioned upon, inter alia, (i) the invalidation of the stock option and termination fee Paramount had contractually granted to Viacom; (ii) QVC obtaining approximately $5.5 billion in debt and equity financing to purchase the minimum number of shares pursuant to the QVC offer (excluding fees and expenses), none of which was in place on November 12 or November 15; and (iii) the unilateral determination of QVC that the back end merger could be satisfactorily completed, on terms and conditions that remain indefinite. Further, the Board determined that, even if all of the conditions of the QVC offer were satisfied, and the merger equity exchange made definite, the consideration to be received by the Paramount stockholders in the Viacom second-step merger would "have long-term values superior to the consideration"

6/ Rattner 11/19/93 Ex. 3; see Pattison 11/20/93 Tr. at 124. Mr. Pattison, Chairman and Chief Executive Officer of the Jim Pattison group, is one of the foremost industrialists in Canada. In addition to the Paramount Board, he sits on the board of the Toronto-Dominion Bank, Canadian Pacific Ltd., and Toyota's Canadian subsidiary.

offered in the QVC second-step merger.

As Paramount director James Pattison testified yesterday:

> The issue in my mind is where are we going to go for the long term with the company, what was the best strategic fit with our assets, with another party, in this case Viacom and that the price of the stock on any given day has so many variables in it and so much volatility and is so fluid that it really didn't interest me, frankly, what the price of the stock was at 3 o'clock.
>
> I was more interested in where the price of the stock is going to be a year from now, two years from now, three years from now, four years from now, five years from now, that is my interest.
>
> You must understand that I am coming at it from not a stock market perspective but the idea of building a company.
>
> I am an operator, I have spent my whole life building a business and you don't build a business where everything you do is best for today. You have to build it over a period of weeks, months and years.
>
> I have had the benefit of being an advisor to the Toyota family and the company in Japan for their strategic plans in North America and for many years and one of the great success stories of the Japanese industry is the fact that <u>they don't look at things in such a short period of time and I think this is a very, very important point</u>.
>
> Therefore, if you are building long term values, the issue is where are we going to be down the pike three years, five years or whatever it is.
>
> <u>It is not based on today</u>. There are so many factors that include today that it did not have an impact on me what it [the stock price] was at 3 o'clock, up $9 or down $9. The issue is where are we going to go with the company.[7/]

Thus, the Board resolved to recommend that the stockholders not accept the

---

7/ Pattison 11/20/93 Tr. at 32-34.

QVC November 12 offer. Further, as at previous meetings, the Board did not close the door to consideration of bona fide alternatives, whether proposed by QVC or by any other third party. Indeed, the merger agreement with Viacom explicitly provides that Paramount will redeem its Rights Plan for the Viacom offer when the conditions for that offer have been satisfied unless the Board determines, on the advice of independent legal counsel, that "so amending the Rights Agreement would be inconsistent with the Board's satisfaction of its fiduciary duties to the stockholders under applicable law. . . ."[8/] As Mr. Pattison testified, the Board would have to take further action before redeeming its Rights Plan for anyone.[9/]

(3) The Basis for the Board's Actions

The record now compiled in accordance with the Court's request shows that on November 15 the Board had ample evidence before it to make a determination that the QVC "offer" was not in the best interests of Paramount or its stockholders, particularly because of the long-term strategic fit and benefits offered by a merger between Paramount and Viacom. Any effort by plaintiffs to dispute the Board's decision, or to nitpick the directors' judgment on November 15 by quibbling with the manner in which the deliberative process took place, represents a "fundamental misconception" of the

---

8/ PEx. 31 (§3.13).

9/ Pattison 11/20/93 Tr. at 90. Mr. Pattison also testified that the Board might have to meet again "if further developments came along." Id. at 90-91.

standard of review that applies to the Board's actions. See, e.g., Paramount Communications, Inc. v. Time, Inc., Del. Supr., 571 A.2d 1140, 1153 (1989) ("Paramount I"); see also Aronson v. Lewis, Del. Supr., 473 A.2d 805, 812 (1984). Accordingly, the Court's inquiry here is limited to whether the Board's decision on November 15 -- a determination to stick with its carefully-selected merger partner in the face of an illusory and highly conditional offer from a shopping network that offers little strategic benefit -- can be attributed to "any rational business purpose." See Cede & Co. v. Technicolor, Inc., Del. Supr., C.A. Nos. 336, 1991 & 337, 1991, slip op. at 38, Horsey, J. (Oct. 22, 1993, revised Nov. 1, 1993) (the business judgment rule protects a decision made by a loyal and informed board unless the decision "cannot be attributed to a rational business purpose.").[10/] As the Supreme Court explained in Paramount I, when a board is choosing between competing offers, the court should not become involved "in substituting its judgment as to what is a `better' deal for that of a corporation's board of directors." 571 A.2d. at 1153.

Indeed, even if we were to assume that the enhanced scrutiny of Unocal were applicable here, the Board's determination would still be entitled to substantial deference, and is hardly subject to dispute by an unsolicited offeror making a highly

---

10/ QVC and its advisors have never attempted to argue that the proposed Paramount/Viacom merger is anything other than a sound long-term business strategy. See Senior Tr. at 22-23; Allen Tr. at 92-93; see also Paramount Brief at 22-23.

conditional offer with a 49% equity back end. Unocal fully embraces reasonable responses to a threat to corporate strategy; here, the Board's careful examination of QVC's offer, its conditionality, and its long-term values, were not "defensive" at all. The Board examined the relative merits of the Viacom merger and the QVC offer and simply came to a reasoned conclusion that the QVC offer was not better. It then so recommended to the stockholders.

Likewise, the Board's actions were correct even in Revlon Land. QVC has admitted that Revlon does not require an auction, and that Revlon does require an examination of the prospective value of the back end equity securities.[11/] That is just what the Board did.

(4) Irrelevant Subsequent Developments

And, once again, the Board's judgment cannot be retroactively second-guessed by reliance upon later developments. This kind of disordered thinking -- in which the validity of today's decisions depends on events that occur tomorrow -- has been a hallmark of QVC's approach to this case. In the latest example, yesterday, QVC's counsel rushed to the Court and to counsel copies of bank commitment letters and an agreement with BellSouth that provide conditional financing for QVC's tender offer. In the letter accompanying these documents, QVC's counsel ignored the conditions and

---

11/ PEx 11/16/93 Hearing Transcript at 218.

emphasized: "QVC's offer is now fully financed"[12]. This assertion -- which is debatable -- supports one of the conclusions reached by the Paramount Board on November 15: Clearly, QVC did not have sufficient financing in place to consummate its offer as of the time it was announced and then considered by the Paramount Board on November 15.[13] Even today, QVC's tender offer remains subject to a number of material conditions -- including a financing condition -- and the financing itself remains contingent upon the invalidation of the Viacom stock option and termination fee.[14] And absolutely nothing has changed regarding the long-term prospects inherent in the 49% equity back end, and regarding QVC's reservation of the right to change the terms of the merger at will. There is thus nothing in the record with which to criticize the Board's evaluation on November 15.

(5) The Board's Deliberative Process

Undoubtedly, in its letter today, QVC will criticize the Paramount Board for its negative reaction to the "offer" that QVC put forward on November 12. Although we cannot predict the specifics of that criticism, a fair review of the QVC offer and the

---

12/ Letter dated November 20, 1993 from Josy W. Ingersoll, Esq. to the Honorable Jack B. Jacobs (emphasis in original).

13/ Those financing contingencies prevented the Board from discussing the offer with QVC under the "no shop" provisions of the merger agreement between Paramount and Viacom. See PEx. 31 (§6.02). See also Paramount Brief at 34, 56-60.

14/ The commitments appear to be sufficient to fund QVC's tender offer only in the event Viacom does not acquire Paramount stock pursuant to the Viacom tender offer. See Annex 1 to Chemical Bank commitment letter at 6, ¶ 3; 7, ¶ 7).

Board's examination of it should dispel concern about whether the Board is acting in the best interests of the stockholders.

(a) QVC's November 12 "Offer"

QVC's amended tender offer on November 12 was comprised of $90 in cash for up to 51% of Paramount's shares, and equity securities for 49% of the shares in a back-end merger.[15/] QVC's offer was, however, subject to numerous conditions, including the following:

- QVC "being satisfied in its sole discretion," that the Viacom stock option and termination fee granted to Viacom had been enjoined or QVC "otherwise being satisfied as to the invalidity of the Viacom Lockups";

- QVC "being satisfied in its sole discretion" that it had obtained sufficient financing to consummate the offer, including up to $3 billion in bank financing and $1.5 billion in equity financing from a potential new investor, BellSouth;[16/] and

---

15/ PEx. 54 at 1-2.

16/ Further by QVC's own admission, as of November 12 (and November 15, when the Paramount Board met), QVC did not have any bank financing commitments in place. When it announced its amended "offer" on November 12, and when the Paramount Board met on November 15, QVC had still not obtained the "necessary modifications" to these commitment letters to use the bank funds for the offer. See QVC's amended offer (PEx. 54 at 11) (stating that QVC intended to use up to $3 billion in bank financing "as described in the Offer to Purchase in the event that the commitments therefore are modified to permit the use of such funds in the Offer") (emphasis added). On Monday afternoon, November 14, QVC submitted to this Court the affidavit of Mr. Costello, QVC's Chief Financial Officer, who confirmed that he was still negotiating with banks for commitments. In addition, as of November 12, BellSouth's potential equity investment of $1.5 billion in QVC was, according to QVC, evidenced only by a "nonbinding statement of intention"

(continued...)

- QVC "being satisfied, in its sole discretion, that, following consummation of the offer, QVC will have the ability to effectuate a second-step merger" upon terms and conditions not yet decided by QVC.[17]

Announcing this offer in the press and in Court as a "$90" offer, QVC simply presumed that the 49% equity stock would be worth $90 per share because QVC stock was trading at or around that level on Monday. QVC has since admitted that such a calculation is not "remotely" appropriate.[18]

(b) Materials Presented to the Paramount Board

During the weekend before the Board meeting, Paramount's management advised the directors that there would be a meeting on Monday, November 15.[19] On Monday morning, Paramount's General Counsel distributed to the directors a copy of QVC's press release about its latest "offer" and a three page memorandum outlining the conditions and uncertainties associated with QVC's November 12 offer, including the

---

16/ (...continued)
that did not create any "legal obligations. . . ." Pex. 54 at 12. Further, if BellSouth determined that its investment would violate the telephone company consent decree (or Modification of Final Judgment), or if the waiting period under the Hart-Scott-Rodino Act had not expired, the QVC offer was dependent on QVC obtaining a "bank bridge loan" for as much of BellSouth's $1.5 billion investment as possible. Id. No such bridge financing had been lined up on November 12 or 15.

17/ See PEx. 54 at 2: "QVC has not made a final decision with respect to the actual form, timing or terms of the Revised QVC Second Step Merger. . . ."

18/ 11/16/93 Hearing Transcript at 218.

19/ See, e.g., Fischer Tr. at 7-10.

financing issues described above.[20]

At the meeting, the Paramount directors were given the following additional materials: (1) an agenda for the meeting; (2) two charts concerning the conditions, financing and terms of the QVC offer; (3) a Lazard presentation book; (4) a revised Lazard fairness opinion regarding the Viacom offer; and (5) a "price update" sheet indicating differences in market value between the common stock portions of the Viacom offer and the QVC offer based on market prices one hour before the Board meeting.[21]

(c) Presentations to the Paramount Board

The meeting was called to order at 4:00 p.m. and lasted approximately an hour and a half.[22] Martin Davis, Chairman and Chief Executive Officer of Paramount, opened the meeting by making an oral presentation to the Board. Mr. Davis noted that the directors had already received a memorandum describing conditions and uncertainties associated with QVC's new offer, and he directed the Board's attention to the detailed charts that compared the terms of the QVC and Viacom offers and the

---

20/ Fischer Ex. 6; Schloss Ex. 1. See also Schloss Tr. at 7-8; Fischer Tr. at 8-9; Pattison Tr. at 4-8.

21/ Fischer Exs. 2-4; Schloss Ex. 3.

22/ Schloss Ex. 4; PSEx. A (Outline; Board minutes); Schloss Tr. at 5 (an hour and a half); Fischer Tr. at 6 (about two hours); Pattison Tr. at 10 (an hour and 45 minutes to two hours, "in that range").

financing sources and conditions of each.[23] He then led a discussion of the Board about the conditions and uncertainties of the QVC offer, including QVC's requirement that the Viacom stock option and termination fee be enjoined by this Court, the lack of any bank financing commitments, and the non-binding nature of the BellSouth investment commitment.[24]

During the meeting, Paramount's financial advisors, Messrs. Rohatyn, Rattner, and Ezersky of Lazard, made a detailed presentation. The Lazard representatives submitted to the Board a written presentation on their research and analysis (the "Lazard Book").[25] The Lazard Book included a stock price performance chart with key dates, a comparison of the offers based on the November 12 closing prices for the common stock portion of the offers (as well as a separate sheet updating those market prices as of an hour before the meeting), financial statistics relating to the current Viacom offer and the current QVC offer, issues relating to the evaluation of common stock on a current market basis, a weighted average multiple analysis, including observations and limitations, a discussion of the potential synergies arising from a Paramount/Viacom and a Paramount/QVC combination, a discussion of

---

23/ PSEx. A; Fischer Ex. 3; Pattison Ex. 6 (Board minutes; Outline; two charts).

24/ Pattison Ex. 6 at 2 (Outline).

25/ Schloss Ex. 3.

the Liberty "put" option[26] and a comparison of the QVC and Viacom preferred stock. Lazard also focused on the inherently speculative nature of stock market prices day to day in the midst of this lawsuit. Lazard specifically noted the volatility of the market prices of both QVC and Viacom, which "has been exacerbated by the market's perception at different times as to which party is likely to succeed." Schloss Ex. 3. The Lazard representatives reviewed these materials in great detail, explaining their analyses page by page.[27]

In discussing the weighted average multiple analysis, Mr. Rattner explained that it was a theoretical tool used to eliminate the effects of merger speculation from the market price of a stock. He cautioned the Board that the weighted average multiple analysis is not a "predictive" tool in the sense of ascertaining future stock trading prices, but that it was a financial tool that would be useful in a comparison of the QVC and

---

26/ During the Lazard presentation, Mr. Ezersky explained that, in connection with QVC's settlement with the FTC, QVC had in effect granted Liberty a "put" option by agreeing to either purchase more than two-thirds of Liberty's equity interest in QVC if Liberty is unable to otherwise divest or to make up any shortfall if Liberty's shares are sold for less than $60. See Schloss Ex. 3 at 14 (November 15 Lazard Presentation at 14). Mr. Ezersky further explained that using a standard financial model for evaluating options, this "put" option was equivalent to a $100 million contingent liability of QVC, and that if the QVC stock price dropped more than the amount assumed by the model, the "put" option would result in a greater cost to QVC.

27/ Rattner 11/19/93 Tr. at 13-14; Pattison 11/20/93 Tr. at 66.

Viacom back end securities on a non-speculative basis.[28] A weighted average multiple analysis does not consider strategic fit, synergies, potential cost savings and other operating changes that might ensue after a merger.

The Lazard presentation also summarized data that had been presented to the Board by Booz Allen & Hamilton at the October 24 Board meeting.[29] (Booz Allen had estimated the incremental earnings potential of a Paramount/Viacom combination compared to that of a Paramount/QVC combination.[30]) These factors were examined separately from the purely financial analyses conducted by Lazard itself.

At the conclusion of their presentation, the Lazard representatives distributed Lazard's written opinion reconfirming Lazard's previous opinion that the Viacom offer and consideration was "fair to the Stockholders from a financial point of view."[31]

28/ See Schloss Ex. 3 at 8-9 (11/15/93 Lazard Presentation at 8-9); Rattner 11/19/93 Tr. at 81-82. Following the Board meeting, Lazard discovered that the weighted average multiple analysis contained a computational error that had the effect of overvaluing QVC's November 12 offer quite substantially. In Lazard's presentation to the Board, the weighted average multiple value of QVC's offer was $3.69 higher than Viacom's proposal when the termination fee and stock option were included and $5.72 higher when the termination fee and stock option were not included. Lazard's corrected weighted average multiple analysis showed that the November 12 offer was only $1.47 higher than Viacom's offer when the termination fee and stock option were not included and was $.56 lower than Viacom's offer when the termination fee and stock option were included. Rattner 11/19/93 Tr. at 30.

29/ Schloss Ex. 3 at 11-13.

30/ See PEx. 25. See also Paramount Brief at 69-70.

31/ Fischer Ex. 4.

(d) The Board's Deliberations

The testimony of Paramount's directors and their financial advisor, Mr. Rattner of Lazard, establishes that the directors utilized the information provided to them to engage in "lengthy discussions involving many questions and many comments" regarding the QVC offer and the strategic benefits of both proposals.[32]

The Board's deliberations included consideration of several factors:

(i) Viacom Is a Better Strategic Fit

Of continuing and paramount importance to the directors was their judgment, based on all of the information previously submitted to them, that a merger with Viacom held out the prospect of greater long-term strategic benefits and values for Paramount and its stockholders than did a combination between QVC and Paramount. "You can't run a business and build a business with the idea of what the price of the stock is everyday. . . ."[33]

As reflected in the Paramount Schedule 14D-9 filed with the S.E.C. the next day, the Paramount Board's judgment that a merger with Viacom offered Paramount stockholders greater long-term values was based on the following factors:

"(1) The business operations of Viacom are larger and more

32/ Rattner 11/19/93 Tr. at 14, 75-76; SPEx. A at 2 (Board minutes at 2); see also Pattison 11/20/93 Tr. at 123-24 ("one of the liveliest board meetings that I have attended in the years that I have been a director").

33/ Pattison 11/20/93 Tr. at 33-34.

diversified than QVC.

"(2) The greater potential for creating new and enhanced business opportunities by putting together the complementary programming and distribution strengths of Paramount and Viacom as opposed to the more limited opportunities for growth arising from a combination of Paramount and the home shopping television network operations which is the principal line of business operations of QVC.

"(3) The long-term strategic objectives and corporate policies of Paramount."[34/]

The directors who were deposed testified in detail about these long-term considerations:

- Mr. Schloss and Mr. Fischer both relied on the financial work of Lazard and the strategic fit analysis by Booz Allen. Schloss testified that even without conditions, the QVC offer was not "so great for long term, for the Paramount shareholders."[35/] He recalled: "I felt that the synergy of a Paramount and a Home Shopping Network were not as great as someone who used product like an MTV to sell software and the cable networks that Viacom has."[36/] He testified: "I felt strongly that the product that Viacom had was a good match with Paramount."[37/]

- "Mr. Liedtke made a very strong statement and comments on his concern for the very puffy, if you like, price of QVC stock . . . . In addition, Mr. Liedtke as a result of talking about his concerns about the stock, got to the long term merger and putting together of the two companies, the long term strategic plan in that he was very concerned about

---

34/ Rattner Ex. 3 at 4 (Schedule 14D-9 at 4).

35/ Schloss Tr. at 156.

36/ Schloss Tr. at 159.

37/ Id. at 162; see also id. at 24 (the "long-term values and synergies were greater with Viacom than they would have been with QVC") and at 151 ("I do feel that the synergies and the abilities of them [Paramount and Viacom management] to work together and the avenues that they have are greater with Viacom than with QVC.").

the risk to the share holders with the stock of QVC being probably significantly overvalued."[38]

- In addition to discussing certain regulatory concerns, Ms. Fippinger also spoke about "the long term objectives of the company."[39]

- Mr. Hooks "brought up the discussion of the strategic long term plan and had quite a few comments to make in that regard."[40]

- Mr. Pattison testified that he "raised the issue of the importance on the game plan of the company, that we had been on the track for a number of years and that the strategic long term plan of the company was our main focus and we should not be deterred from this alternative that has come along that wasn't financed and had holes in it. . . ."[41]

- Mr. Pattison also recalled that his "whole focus on November 15 was to go to build the company on the plan that I have been involved with for five years and that the current snapshot of that day or the Friday at 4 o'clock or the coming Thursday, was a non-issue with me . . . ."[42]

- Similarly, he testified: "The issue in my mind is where are we going to go for the long term with the company, what was the best strategic fit with our assets, with another party, in this case Viacom and that the price of the stock on any given day has so many variables in it and so much volatility and is so fluid that it really didn't interest me, frankly, what the price of the stock was at 3 o'clock."[43]

- Mr. Pattison's judgment was "based on everything that I read to

---

38/ Pattison 11/20/93 Tr. at 118-119.

39/ Id. at 120.

40/ Id. at 121.

41/ Id. at 122.

42/ Id. at 105 (emphasis added).

43/ Id. at 32-33 (emphasis added).

> do with Viacom and QVC of my own independent assessment, plus the fact that we had some input in a presentation from Booz Allen, plus the fact I have been around this company for five years where we have talked to many other entities about trying to do something to build a long term strategic value; that it was my best judgment as a director of the company representing the owners of which I was one with 80,000 shares, was interested in where this company was going to go."[44/]

Undoubtedly, QVC and the shareholder plaintiffs will point to the fact that the "exact" long-term values of a Paramount/Viacom combination versus a Paramount/QVC combination were not "calculated" or "quantified" for the Paramount Board. It is incorrect to claim that the Board has received no quantitative data (it was given, among other things, a weighted average multiple analysis and the Booz Allen & Hamilton presentation concerning long-range prospects.[45/] Fundamentally, however, any insistence by plaintiffs on a "mathematical exercise" is directly contrary to the teachings of the Delaware Supreme Court in Unocal and in Paramount I, as would a "court's engaging in the process of attempting to appraise and evaluate the relative merits of a long-term versus a short-term investment goal for shareholders." 571 A.2d at 1153; see also Unocal, 493 A.2d at 955. Indeed, the calculations that QVC has sponsored -- most recently in yesterday's letter to the Court -- are the very same comparisons of "the discounted value[s] of [the] expected trading price[s]" that were rejected by the Supreme Court as a "distortion of the Unocal process." Paramount I, 571 A.2d at 1153. Further,

---

[44/] Id. at 34; see also id. at 37-38.

[45/] See PEx. 25; Paramount Brief at 69-70.

the exercise that QVC is sponsoring is not even based on "expected" trading prices; it is based on momentary market prices that are driven by market speculation about, inter alia, QVC's prospects in this lawsuit.

The long-term values inherent in the 49% back end mergers cannot be quantified with certainty; that is indeed why judgment must be exercised. QVC knows this as well as Paramount does; QVC's own financial advisor has testified that the relative values of post-merger stock in a Paramount-Viacom entity and a QVC-Paramount entity is a complicated matter of judgment, which requires, among other things, an evaluation of strategic "fit" and the amount of time it will take for each proposed transaction to close.[46/] QVC's counsel recognized the same fundamental concept during oral argument, even in so constricted an environment as Revlon-land. Full and fair appraisal of the values inherent on a back-end merger requires qualitative evaluation and experienced judgment. That kind of non-quantitative business judgment is precisely what Delaware law insists upon, and it is what the Board exercised here.

46/ Senior Tr. at 51-52, 59, 85-87. As Mr. Schloss testified when asked about precise calculations of long-term values: "I think you're dealing in a highly specialized area where not many have traveled before. * * * And looking at this on a combined basis, it was not hard, at least for me, to come the conclusion as to where the benefits were versus Viacom, versus a QVC." Schloss Tr. at 161.

(ii) QVC's "Lock Up" Condition

One of the Board's considerations on November 15 was that QVC continued to condition their offer upon the invalidation of the Viacom stock option and termination fee granted to Viacom in the Paramount/Viacom merger agreement.[47/] In so doing, QVC again ignored that the stock option and break up fee were and are existing and valid contractual obligations of Paramount, which induced Viacom to enter into a strategic merger to provide a premium to Paramount's stockholders, and to compensate Viacom for foregoing other potential opportunities.[48/] Because the QVC offer is conditioned on non-enforcement of Paramount's contract, Paramount is legally incapable of accepting the offer. Indeed, Delaware courts have recognized that corporate directors are not free to renege on valid and enforceable contractual obligations even if a more favorable alternative for shareholders presents itself. See, e.g., Corwin v. DeTrey, Del. Ch., C.A. No. 6808, Berger, V.C. (Dec. 1, 1989); Jewel Cos. v. Pay Less Drug Stores Northwest, Inc., 741 F.2d 1555, 1563-64 (9th Cir. 1984) (noting that "unanticipated business opportunities and exigencies of the market place" ensuing after a board of directors has concluded a merger agreement are insufficient to relieve the corporation of its contractual obligations under the agreement.)

47/ Schloss Tr. at 67; Pattison Exs. 1 and 6 (Conditions Memorandum and Outline).

48/ Paramount Brief at 31-32, 109-16.

(iii) QVC's Lack of Financing Commitments

At the Board meeting of November 12, several Paramount directors expressed concern about QVC's financing condition and lack of financing commitments for the purchase of shares pursuant to the QVC offer that, according to QVC's own estimates, could not be consummated without commitments of approximately $5.5 billion (excluding fees and expenses).[49/] The memorandum and charts provided to the Board described, among other conditions and uncertainties, the absence of any bank financing commitments for the offer and the non-binding nature of the potential BellSouth equity investment.[50/] The Board discussed QVC's conditions at length and concluded, as it had in similar circumstances on September 27, that Paramount could not hold discussions with QVC with respect to its new offer unless that offer was both a better alternative and

---

49/ PEx. 54 at 11.

50/ Pattison Ex. 1; Fischer Ex. 3. The memorandum distributed to directors before the meeting showed that there were other uncertainties, including the possibility that QVC would need to obtain a "bank bridge loan" in lieu of BellSouth's $1.5 billion investment and the fact that QVC did not have any bridge financing in place. Pattison Ex. 1 at 2. The memorandum also described that QVC's other equity financing of $1.5 billion by Advance Publications, Inc., Comcast Corporation, and Cox Enterprises, Inc. was still subject to negotiation of definitive agreements, receipt of necessary regulatory approvals and consummation of the Paramount acquisition. Moreover, any of these commitments could be withdrawn in the event QVC recruits additional or different equity investors for a Paramount acquisition. Id. at 1.

not conditional on obtaining financing:[51]:

- Mr. Silberman "brought up the subject and discussion that did the board have the right to really talk about this [proposition] because in fact it wasn't fully financed, it wasn't financed and our merger agreement with Viacom precluded us looking at this thing . . . ."[52]

- Mr. Pattison testified regarding his concerns: "[W]e had a deal with Viacom that prohibited us to get an unsolicited offer that wasn't fully -- that basically had -- that wasn't financed. Based on the information that I had in front of me, this was a non-offer, because it had a lot of holes in it as I testified and secondly, we had a deal with Viacom we wouldn't go out and solicit anything . . . ."[53]

- Similarly, Mr. Fischer testified "that the Board discussed the absence of bank financing commitments and the "iffiness of the BellSouth part of it."[54]

(iv) The Uncertain Value of QVC's Non-Cash Merger Consideration

The Paramount Board did not confine its deliberations to QVC's financing

---

51/ Rattner 11/19/93 Tr. at 71 ("The words that were used to describe the QVC offer were that it was subject to a great number of conditions, and thereby did not meet the task of the merger agreement that an offer not be subject to any material conditions."); see also id. at 70-71, 75-76.

52/ Pattison 11/20/93 Tr. at 119.

53/ Pattison 11/20/93 Tr. at 23; see also id. at 24-26: "There was a great deal of discussion about the fact that this was not a financed proposition in front of us from QVC; that in fact did the board have even the right to consider it because of our arrangement with Viacom and this was discussed at great length." Mr. Pattison also testified about the non-binding nature of the BellSouth commitment: "All I knew is, it said it had a non-binding memorandum of understanding which does not legally commit and I know what those are worth having gone through a few of them in my time." Id. at 60.

54/ Id. at 20-21. The uncertain status of BellSouth as a potential new investor in QVC was also a major concern of Mr. Schloss. Schloss Tr. at 88.

conditions and the lack of QVC financing commitments. The directors also discussed at some length the difficulties and uncertainties associated with valuing QVC's back-end merger consideration under the present terms of the QVC "offer."

One concern expressed by several Paramount directors was that QVC had reserved the right to change the terms of the back-end consideration:

- Mr. Fischer: "[I]t was a difficult piece to evaluate because, as I recall the conversation, QVC the way the proposal was put, would have had great latitude on the backend and Paramount stockholders could have come up short having already tendered their stock."[55/] Mr. Fischer was troubled that QVC "could do whatever they wanted" with the backend.[56/] He also testified that "[t]he backend of the QVC offering my opinion was very iffy and soft. I can't put a price tag on it."[57/]

- Mr. Schloss testified similarly: "And there were still some verbiage in the offering that could change the back end. * * * And any time, as far as I was concerned, you could change the terms of the back end, it did not constitute a legitimate bid."[58/]

Even without QVC's reservation of the right to change the terms of the non-cash merger consideration, the Paramount directors did not believe it was appropriate to compare the non-cash merger consideration offered by QVC with that offered by Viacom by simply performing a mechanical, arithmetic calculation based on the latest market prices for each stock. The directors were concerned about any such comparison because,

---

55/ Fischer Tr. at 23.

56/ Id. at 24.

57/ Id. at 76.

58/ Schloss Tr. at 23.

among other things, of the potential for delays due to the conditions and other uncertainties associated with the QVC offer. Mr. Schloss testified that reliance on the latest QVC stock market price was inappropriate, particularly because QVC could not guarantee that the same price would prevail upon consummation of a QVC second-step merger:

> There was an existing spread between the two [offers] at the time. . .
>
> And some of the comments were, and it was my own feeling, that that only represented the price at the time and did not impress me, because it did not talk about what that back end of the paper would be worth on consummation of the merger.[59/]

Although guarantees could not be given with respect to the value of the Viacom stock, the Board discussed the fact that "Viacom had satisfied all or virtually all of its conditions and would be in a position to complete its tender offer or would be expected to be in a position to complete its tender offer as scheduled on November 22nd."[60/] On the other hand, as Mr. Rattner of Lazard recalled, "[t]here was a discussion of the fact that QVC had a long list of conditions that needed to be satisfied and that there could be no assurance as to how long it would take QVC to satisfy those conditions."[61/]

Delaware courts have repeatedly held that a board of directors may favor one

---

59/ Schloss Tr. at 19-20; see also id. at 22 (testifying that he was aware of latest stock market spread and that "I also was aware that that is only a price at the time of the quote; that in no way did it reflect where it would be selling at a later date").

60/ Rattner 11/19/93 Tr. at 75-76.

61/ Id.

merger proposal over another where the favored proposal is "more likely to close and sooner." J.P. Stevens, 542 A.2d at 785. See also Freedman v. Restaurant Assocs. Indus. Inc., Del. Ch., C.A. No. 9212, Allen, C. (Oct. 16, 1987) ("the likelihood that one [alternative proposal] may be less likely to close supplies a rational basis for preferring another proposal, even though it may be at a lower price"); Citron v. Fairchild Camera and Instrument Corp., Del. Ch., C.A. No. 6085, Allen, C. (May 19, 1988), aff'd, Del. Supr., 569 A.2d 53 (1989) (board entitled to accept unconditional "cash on the barrelhead" offer over uncertain conditional offer"); In re Fort Howard Corp. Shareholders Litig., Del. Ch., C.A. No. 9991, slip op. at 35, Allen, C. (Aug. 8, 1988) (disinterested board might legitimately prefer a deal at a lower price to one that is not all cash and not capable of closing as quickly).

At its November 15 meeting, the Board clearly was concerned that any delay by QVC in consummating its offer also exposes Paramount's stockholders to the risk of adverse changes in the securities or financial markets, as well as other adverse changes in the banking, regulatory or economic environment, which could force Paramount to enter into a less attractive transaction or no transaction at all. Indeed, Mr. Senior testified that such timing concerns are "always a factor" in evaluating competing offers.[62/] Obviously, these market risks were a significant reason for the Paramount Board's rejection of QVC tender offer. The Board concluded that such risks were particularly

---

62/ Senior Tr. at 87.

unacceptable in light of the availability of the unconditional Viacom offer that can close on November 22.63/

* * *

The foregoing discussion show that the Board's actions on November 15 were entirely proper, well-reasoned, and based upon the material facts. Those actions, which boil down to a recommendation that the stockholders not tender to QVC, should not even be particularly controversial in light of the conditionality of QVC's last-minute offer. Moreover, the Board remains free to consider alternatives to the Viacom merger. As has been the case since September, the Paramount Board continues to manage a very fluid and dynamic situation with the best interests of the stockholders in mind. There is no basis on the present record for the injunctive relief requested by QVC.

Respectfully,

Charles F. Richards, Jr.

CFR,jr/reb

63/ Mr. Schloss, as a sophisticated "Wall Street expert" (Pattison Tr. 11/20/93 at 120-21) was very concerned about market risk and the possibility that any delay exposed Paramount and its stockholders to the risk, especially if the securities and financial markets fell, that Paramount would be forced to enter into a less attractive deal or no transaction at all. Schloss Tr. at 170-71. Mr. Schloss specifically recalled the example of the proposed buy-out of United Airlines that had collapsed at the "11th hour and 59th minute." Id. at 171.

cc: David C. McBride, Esquire (by hand)
A. Gilchrist Sparks, III, Esquire (by hand)
Karen L. Morris, Esquire (by hand)
Stuart J. Baskin, Esquire (by facsimile)
Herbert Wachtell, Esquire (by facsimile)
Arthur Abbey, Esquire (by facsimile)
Register in Chancery

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

ORIGINAL

ROBERT CORWIN and PHYLLIS CORWIN, EVELYN SUMERS and GINSBURG ENTERPRISES,	)	
Plaintiffs,	)	
v.	)	Civil Action No. 6808
ROBERT J. deTREY, ROBERT K. PFISTER, FREDERICK O. SCHWEIZER, HENRY M. THORNTON, BERNARD J. BEAZLEY, BURTON C. BORGELT, PATRICK L. BURGIN, FRANK T. HAMILTON, MAYNARD K. HINE, EDWARD J. LIPAWSKY, JOHN G. POOLE, NANCY J. REYNOLDS-GOOREY, DAVID D. WAKEFIELD and DENTSPLY INTERNATIONAL, INC.	)	
Defendants.	)	

MEMORANDUM OPINION

Date Submitted: November 29, 1988
Date Decided: December 1, 1989

Joseph A. Rosenthal, Esquire of MORRIS, ROSENTHAL, MONHAIT & GROSS, P.A., Wilmington, Delaware; Of Counsel: MORDECAI ROSENFELD, P.C., New York, New York; A. ARNOLD GRESHON, P.C., New York, New York and MILBERG WEISS BERSHAD SPECTHRIE & LERACH, New York, New York, Attorneys for Plaintiffs

Edward B. Maxwell, 2nd, Esquire, William D. Johnston, Esquire and Bruce L. Silverstein, Esquire of YOUNG, CONAWAY, STARGATT & TAYLOR, Wilmington, Delaware; Of Counsel: J. Patrick Clark, Esquire of DENTSPLY INTERNATIONAL, INC., York, Pennsylvania, Attorneys for Defendants

BERGER, Vice Chancellor

This action arises from the December 23, 1982 merger between Dentsply International Inc. ("Dentsply") and a wholly-owned subsidiary of Dentsply Holdings, Inc. (both the subsidiary and parent will be referred to as "Holding Company") pursuant to which the public stockholders of Dentsply received $25.50 cash per share. Plaintiffs, stockholders of Dentsply, began filing their complaints against Dentsply and its thirteen directors in May, 1982, shortly after the merger plans were announced. The three separate lawsuits were consolidated in the summer of 1982 and, plaintiffs, after making several intermediate amendments, filed a Consolidated Amended and Supplemental Complaint (the "complaint"), in March, 1987. This is the decision on defendants' motion to dismiss the complaint.

Plaintiffs' legal theories, as indicated by their complaints, have shifted over time. For example, the original complaint in Civil Action No. 6808 attacked the Dentsply merger as being an entrenchment device, part of a "scorched earth" policy Dentsply's directors had adopted. The first Consolidated Amended and Supplemental Complaint also charges that the directors failed to shop Dentsply and that the proxy statement they issued in connection with the merger is materially false and misleading. The most recent version of the complaint, the one that is the subject of defendants' pending

motions, adds purported claims based upon changed circumstances between July 16, 1982 (the date on which Dentsply's stockholders voted to approve the merger) and December 23, 1982 (the date on which the merger was consummated). Plaintiffs allege that during that period the defendant directors could have terminated the merger agreement at any time at their discretion. According to plaintiffs, the stock market went up and interest rates went down between July and December, 1982. As a result, by the time the merger was effectuated, the $25.50 merger price had become inadequate and unfair. In their brief, plaintiffs resisted dismissal solely on the basis of their "post-approval" claim — that the Dentsply directors could have and should have terminated the merger because the merger price had become unfair by December, 1982. At oral argument, plaintiffs acknowledged that they were abandoning any "pre-approval" and disclosure claims. Accordingly, I will discuss and consider only those allegations and facts relevant to the "post-approval" claim.

At all relevant times, Dentsply was in the business of providing professional products for health care, primarily through the production and distribution of dental supplies and equipment. The company had approximately 4 million shares of common stock outstanding, which shares were traded on the New York Stock Exchange. Thirteen directors sat on the Dentsply

board, eight of whom were totally disinterested — they were neither present nor prospective employees of Dentsply and they had no financial interest in the Holding Company or in any of its affiliates.

The merger developed in response to a potential threat from Cooper Laboratories, Inc. ("Cooper"). In late 1980, Cooper, a Dentsply competitor, began acquiring Dentsply stock. In October, 1981, Cooper indicated in a Schedule 13D that it had no present intention of acquiring more than 25% of Dentsply. However, Dentsply's management was concerned that Cooper might ultimately attempt to gain control of Dentsply and that such a takeover would harm the company. Dentsply's management believed that Cooper would sell its block of Dentsply stock if it were paid a substantial premium. The Dentsply directors, however, were willing to consider such a buy-back only if all of the company's stockholders were offered the same premium.

Management satisfied the directors' condition by initiating a leveraged buy-out. The merger price — $25.50 per share — was the highest amount agreed to in arms-length negotiations between the company and several of its major stockholders (including Cooper), and Dentsply's investment banker opined that the price was fair from a financial point

of view. Under the terms of the merger agreement, approval was contingent on the affirmative vote of a majority of the publicly held stock (approximately 88% of the outstanding shares). The merger agreement provided for termination either by mutual consent of the parties or by either party on notice to the other, if the merger were not consummated before December 31, 1982 and if the party terminating the agreement had exercised best efforts to satisfy all conditions precedent. Merger Agreement, ¶13(b) and (c). The buyer obtained its financing on or about December 23, 1982 and the merger was consummated that day.

The legal premise of plaintiffs' claim is not readily apparent. Both the complaint and plaintiffs' brief refer to defendants' purported contractual right to terminate the merger agreement. Plaintiffs suggest that defendants acted wrongly by failing to to exercise that right after changed circumstances allegedly made the merger price unfavorable to Dentsply's stockholders. To the extent that plaintiffs are alleging such a contractual claim, I find it to be without merit. Paragraph 13(b) of the merger agreement provides for termination by mutual consent of the parties. As plaintiffs recognized at oral argument, the Dentsply directors could not have terminated the merger agreement unilaterally pursuant to paragraph 13(b). Plaintiffs' reliance on paragraph 13(c) of

the merger agreement is likewise misplaced. That paragraph provides for termination by either party if the merger were not consummated on or before December 31, 1982 and if the party terminating the agreement had exercised its best efforts to fulfill all applicable conditions precedent. Plaintiffs argue that, had market conditions gone against the Holding Company, it would have avoided the merger agreement simply by not obtaining the necessary financing and letting the contract lapse on December 31, 1982. Plaintiffs suggest that, since the Holding Company could have avoided its contractual obligations, Dentsply and its stockholders should not be bound by the merger agreement. This argument, which plaintiffs advanced without any supporting authority, is based on the faulty premise that the "best efforts" clause is unenforceable. In fact, such clauses are not illusory, as plaintiffs contend. They are fairly routine and the failure of a party to exercise best efforts can form the basis for liability in a breach of contract action. See Carteret Bancorp, Inc. v. The Home Group, Inc., Del. Ch., Civil Action Nos. 9380 and 9386, Allen C. (January 13, 1988) Mem. Op. at 19-22 (analyzing plaintiff's claim of breach of best efforts clause, but finding that plaintiff's allegations did not adequately allege such a claim); Eckmar Corp. v. Malchin, Del. Ch., 297 A.2d 446, 450 (1972) (noting that plaintiff was bound by best

efforts clause). Thus, paragraph 13(c) gave neither party the right to ignore its pre-closing obligations and simply let the contract lapse by the passage of time.

Plaintiffs' fiduciary duty claim fares no better. Although they bring these actions against the entire Dentsply board, it appears that plaintiffs are charging only the three Dentsply directors who are also directors of the Holding Company with breach of fiduciary duty. The claim seems to be that those three directors, as part of their continuing fiduciary duties, were obliged to give up their contractual rights under the merger agreement when circumstances changed so as to favor them at the Dentsply stockholders' expense. Plaintiffs rely upon several decisions involving stock options for the proposition that an executory contract between a fiduciary and cestui que trust, even if fair when made, may be avoided if it later becomes "inequitable to the minority stockholders." Kingston v. Home Life Ins. Co. of America, Del. Supr., 104 A. 25 (1918). See also Gamble v. Penn Valley Crude Oil Corp., Del. Ch., 104 A.2d 257, 261-62 (1954).

First, I note that the early Delaware decisions upon which plaintiffs rely are distinguishable. They both involved stock options of unlimited duration and it appears disinterested stockholders had given no approval of those options. Moreover, the premise that even a dramatic increase in the

value of stock options may render them unenforceable has been subject to serious question. In Forman v. Chesler, Del. Supr. 167 A.2d 442, 445 (1961), the Delaware Supreme Court, when considering warrants exercisable for five years, stated that 8 Del. C. §157 (the statute authorizing the issuance of stock options and warrants) "contemplates that the warrant holder or optionee may, at least under ordinary circumstances, lawfully expect to enjoy the advantages of any future increase in value of the shares, to the same extent as if he had invested in the stock itself." Thus, it is not clear that a stock option of limited duration could be avoided solely because of changed circumstances prior to its exercise.

Even if a self-dealing transaction between a fiduciary and a cestui must be entirely fair, not only when the agreement is reached but also when it is executed, this principle does not void, or make voidable, the transaction at issue. The five Dentsply directors who had an interest in the merger neither set the terms of the merger nor controlled the decision to approve it. As noted earlier, the price was set at the highest amount at which three substantial stockholders agreed to sell their shares after arms-length negotiations. A majority of the Dentsply directors, who approved the merger unanimously, were disinterested and, even though close to 90% of Dentsply's stockholders were disinterested, the merger

agreement required that a majority of the public shares be voted in favor of the transaction. The merger price was fair, at least at the time it was agreed to, and the transaction was approved by the stockholders after full disclosure. In short, the special scrutiny given to a self-dealing transaction is not appropriate here. The "entire atmosphere [has been] freshened" and plaintiffs must overcome the presumptive validity accorded to an action undertaken in the exercise of business judgment. See Marciano v. Nakash, Del. Supr., 535 A.2d 400 (1987); Sinclair Oil Corp. v. Levien, Del. Supr., 280 A.2d 717, 721-22 (1971); Gottlieb v. Heyden Chemical Corp., Del. Supr., 91 A.2d 57, 59 (1952); 8 Del. C. §144.

In finding that the business judgment rule applies, this court, in essence, is saying that it will evaluate this transaction not as one involving self-dealing but rather as if it were one between the corporation and an unrelated third party. In such a third-party transaction, the directors of the selling corporation are not free to terminate an otherwise binding merger agreement just because they are fiduciaries and circumstances have changed. Smith v. Van Gorkom, Del. Supr., 488 A.2d 858, 888 (1985). Cf. Wilmington Trust Co. v. Coulter, Del. Supr., 200 A.2d 441 (1964); Pennzoil Co. v. Getty Oil Co., Del. Ch., Civil Action No. 7425, Brown, C. (October 15, 1984) Mem. Op. at 23-26. The buyers, likewise,

are not required to give up their rights under a binding contract simply because they are fiduciaries and changed circumstances make their bargain more favorable. In Pogostin v. Rice, Del. Supr., 480 A.2d 619 (1984), for example, plaintiffs attacked an executive stock bonus plan on the ground that the amounts payable under the plan were artificially inflated by a premium tender offer made by a third party. The plan payments were tied to the market price of the company's stock and the market price rose sharply in response to the tender offer. Since the increase in market price was not related to the executives' efforts on behalf of the company, plaintiffs argued, the executives breached their fiduciary duty by accepting payments under the plan. Id. at 625. The Delaware Supreme Court rejected this claim as part of its analysis of the demand requirement of Chancery Court Rule 23.1. After noting that the bonus plan had been adopted by a majority of disinterested directors and ratified by the company's stockholders, the Court stated that plaintiffs would have to allege that the bonus plan was a waste of corporate assets. Id. at 626. In other words, the mere allegation that fiduciaries were benefitting from changed circumstances does not mandate a finding of self-dealing and, therefore, does not make the transaction void or voidable. See In re Thomas, Del. Supr., 311 A.2d 112, 115 (1973) (trustee benefitting from

"factors extrinsic to [his] duties as a trustee" in transaction with the trust is not self-dealing.)

Based upon the foregoing, I find that the complaint must be dismissed for failure to state a claim. **IT IS SO ORDERED.**