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IN THE

Supreme Court of the State of Delaware

Nos. 427 and 428, 1993 (Consolidated)

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 Below-Appellants,

COURT BELOW:
COURT OF CHANCERY OF THE STATE OF DELAWARE IN AND FOR NEW CASTLE COUNTY

—v.—

QVC NETWORK, INC.,

Plaintiff Below-Appellee.

CIVIL ACTION NO. 13208

IN RE PARAMOUNT COMMUNICATIONS INC. SHAREHOLDERS' LITIGATION

CIVIL ACTION NO. 13117 (CONSOLIDATED)

OPENING BRIEF OF THE PARAMOUNT DEFENDANTS–APPELLANTS

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Dated: November 30, 1993

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NATURE OF PROCEEDINGS AND THE ORDER SOUGHT TO BE REVIEWED

This is an appeal of an Opinion and Order of the Chancery Court (Jacobs, V.C.) dated November 24, 1993. The Chancery Court's Order preliminarily enjoined Paramount Communications Inc. ("Paramount") and the individual defendants from amending or redeeming Paramount's shareholder rights plan (the "Rights Plan") to facilitate the consummation of the pending tender offer by Viacom Inc. ("Viacom") until further order of the Chancery Court. The Order also preliminarily enjoined the exercise of a stock option granted to Viacom on September 12, 1993 in consideration of Viacom entering into the original merger agreement with Paramount (the "Merger Agreement").

The Chancery Court's Opinion and Order determine motions for preliminary injunctions that were filed on October 28, 1993 and November 12, 1993.[1] The Opinion and Order were premised upon an expedited discovery record that closed on November 21, 1993, and concerned events up to and including November 15, 1993. Argument was held on November 16. On November 12, 15, 16, 19, 20 and 22, plaintiff QVC Network, Inc. ("QVC") issued announcements concerning material changes to its tender offer for Paramount, including price, financing, an antitrust consent decree, a substitution of co-offerors, and waiver or modification of certain conditions. On November 22, 1993, QVC amended its Schedule 14D-1 to reflect material amendments to its offer and, as required by law, to extend it to November 29.

This is the Paramount defendants-appellants' opening brief in support of their appeal from the November 24 Opinion and Order.

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1. Citations to "Op. __" refer to the Chancery Court's November 24, 1993 Opinion, as corrected on November 29, which appears at JA 7187-7248. Citations herein to "JA __" refer to the parties' Joint Appendix on this appeal. Cites to "PAB __" refer to Paramount's answering brief below, filed on November 14; and cites to "PSB __" refer to Paramount's supplemental letter brief below, filed on November 21.

SUMMARY OF ARGUMENT

1. The court below acted contrary to existing law and created what amounts to a *per se* rule that a merger resulting in a change of voting control automatically triggers "*Revlon* duties," thus obligating a board of directors to abandon its long-term strategy and maximize immediate stockholder value. *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, Del. Supr., 506 A.2d 173 (1985). The court erred in holding that Paramount's entering into the Merger Agreement on September 12 triggered duties to obtain the "highest available premium-conferring transaction." *Revlon* is triggered by transactions that make a liquidation of stockholders' interests "inevitable" and not by a change of voting control alone. An indisputably strategic merger, in which Paramount shares were to be exchanged (at a significant premium) largely for stock in an ongoing enterprise, should not trigger any duty to sell Paramount to a later unsolicited bidder purporting to offer "higher" short-term consideration. The Chancery Court's opinion:

- violates the well-settled precept that an unsolicited offeror may not forcibly put its target up "for sale" within the meaning of *Revlon.*

- holds—contrary to *Revlon*; *Paramount Communications, Inc. v. Time, Inc.*, Del. Supr., 571 A.2d 1140 (1989) ("*Time-Warner*"); *Mills Acq. Co. v. Macmillan, Inc.*, Del. Supr., 559 A.2d 1261 (1989) ("*Macmillan*"); and *Barkan v. Amsted Indus., Inc.*, Del. Supr., 567 A.2d 1279 (1989) ("*Barkan*")—that a merger in which half of the consideration received consists of stock of the surviving corporation is equivalent to a "break-up" of the company or the "abandonment" (as opposed to the fulfillment) of "corporate policy."

- is predicated, fundamentally, on the erroneous assumption that minority stockholders are not adequately protected by Delaware statutory and case law which are designed specifically to assure "entire fairness," and thereby protect long-term values, in the context of a hypothetical squeeze-out merger. *See* Point I.

2. In reviewing the November 15 meeting of the Paramount Board of Directors, the court below ignored this Court's admonition in *Time-Warner* that a court should not engage "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. The opinion below:

• holds that a distinguished (Op. 3), unquestionably loyal (Op. 36 n.34, 52), informed (Op. 7, 52-53), well-motivated (Op. 36 n.34, 52), disinterested (Op. 36 n.34, 52), almost entirely independent Board (Op. 3) with a valid long term business plan (Op. 6-7, 54) that it "sincerely" believes is in the best interests of the stockholders (Op. 54), for laudable reasons (Op. 52), is nevertheless not entitled to the benefits of the business judgment rule for actions taken with respect to a strategic merger entered into *before* any alternative bidder surfaces.

• ignores the teachings of *Time-Warner* that a selected strategic merger partner may be reasonably favored and that enslaving a board to quantitative prophecies of "value" is a "distortion" of the process required under *Unocal Corp. v. Mesa Petroleum Co.*, Del. Supr., 493 A.2d 946 (1985) ("*Unocal*").

• ignores the plainly-stated holding of this Court that mathematical quantification of a long term strategy is not required (*Time-Warner*), and declares that henceforth such quantification is absolutely required.

• means that a corporation having a controlling stockholder can never engage in a strategic merger without thrusting its Delaware merger partner into an auction mode.

• finds breaches of fiduciary duty in decisions (*i.e.*, amending the Rights Plan for Viacom alone) that the Board never made.

• second-guesses a decision that the Board did make (*i.e.*, to recommend against a conditional, unfinanced non-strategic QVC offer), based on events that occurred *after* that decision was made.

• punishes Paramount's compliance with the perfectly valid "no-shop" provisions contained in the Merger Agreement, denigrating that compliance as "more pretext than a problem," even though the "no-shop" clause was not invalidated by the Chancery Court.

• disregards the fact that QVC's November 12 offer, unlike its earlier merger proposal, was legally incapable of acceptance because it was conditioned on the invalidation of the stock option and termination fee—both of which were pre-existing contractual obligations of Paramount agreed to, according to the Chancery Court's own findings, by a well-informed Board. Op. 52. *See* Point II.

3. The Chancery Court erred in holding that the stock option granted to Viacom in connection with the Merger Agreement before any QVC offer was made constituted a breach of fiduciary duty. Indeed, this conclusion is inconsistent with its own factual recitation, and with its express determination that there is "no basis to criticize the sufficiency of the board's information or processes up to November 12." Op. 52. *See* Point III.

STATEMENT OF FACTS

A. The Chancery Court Found That The Paramount Board Scrupulously Honored Its Duty Of Loyalty And Was Consistently Well-Informed As It Pursued A Strategic Merger

Fully 50 pages of the Chancery Court's 61-page opinion find no fault with the Paramount Board and the Board's exercise of its fiduciary responsibilities:

"Paramount's eleven 'outside' directors"—out of a total of 15 directors—"are persons of distinction experienced in the world of business and finance, and are present or former senior executives of public corporations or financial institutions." Op. 3.

Since 1983, Paramount's management team has been "devoted to transforming [Paramount] into a major entertainment and publishing Company." Op. 6. "The record establishes that Paramount's board was well informed of Paramount's strategic goals and of the steps taken by management to achieve those objectives." Op. 7. These steps included exploring—over the course of several years—business combinations with a number of diversified media and entertainment companies, among them Viacom. *Id.* Thus, "the reasons for [the Board's] partiality [to a Viacom transaction on November 15] are not venal but *laudatory*." Op. 52 (emphasis added).

"The independent directors have no demonstrated self-interest in the Viacom transaction, or in perpetuating Mr. Davis or themselves in office." Op. 52. Plaintiffs' duty of loyalty allegation is wholly "without merit." Op. 36, n.34.

Throughout *six* meetings—September 9, 12 and 27, October 11 and 24, and November 6—at which the Board considered the Viacom transaction, and later QVC's unsolicited offers, the Board's deliberations were sound and informed: "I find no basis to criticize the sufficiency of the board's information or processes up to November 12." Op. 52. Any "arguable defects" in the Board's information-gathering process were "immaterial." Op. 52-53.

Even on November 15—the *only* meeting criticized—the Board reached an "honestly-held" and "sincere" judgment that the Viacom transaction remained the best alternative for Paramount's stockholders, a judgment the court does *not* find to be incorrect. Op. 52 and 54.

Prior to November 15, the Board had already properly determined that: (1) Viacom was an ideal strategic merger partner (PAB 34-46); (2) the Merger Agreement was in the stockholders' best interests (*id.*); (3) the stock option and the termination fee were required to induce Viacom to enter into a transaction that, at the time, afforded Paramount's stockholders a premium of approximately 30% over Paramount's pre-merger trading range (*id.* 31-23, 41); (4) QVC, as a small, single-channel television retailer largely dependent upon one individual, could not replicate the strategic advantages of a merger with Viacom, which was based on concrete plans for combining a wide array of valuable programming, distribution and entertainment assets (*id.* 69-70, 85, 136-37); and (5) under the provisions of the "no-shop" clause of the Merger Agreement, Paramount was contractually prohibited from entering into discussions with QVC if QVC's offer was "subject to any material contingencies relating to financing." *Id.* 55-61.

When the Chancery Court turned to consider the November 15th Board meeting, however, its opinion of the Board and its deliberations abruptly soured. Thus, as the court below viewed it, the same directors who for the preceding nine weeks (indeed, for several years) had consistently kept themselves well informed were now—suddenly—uninformed, in effect writing on a blank slate, with only "business instinct and experience" (Op. 55) to guide them in reacting to QVC's latest bid.

Why this sudden reversal? The Chancery Court gives only two reasons:

First, the court apparently concluded that the Board should have talked with QVC before concluding that QVC's November 12 offer was conditional and unfinanced. Op. 53-54. However, the court simply disregarded the express contractual "no-shop" restriction, which the court neither criticized nor invalidated, that *prohibited* such talks concerning conditional and unfinanced proposals. The "no-shop" provision undeniably applied to the November 12 QVC offer because it was explicitly conditioned on financing that was not in place. More importantly, the Chancery Court attached no significance to the fact that Paramount did *not* amend its Rights Plan for Viacom on November 15.

Second, the court below found that the Board was required to obtain a "quantification" of long-term values. The court exercised *its own* business judgment to conclude that QVC's offer, based on that day's market trading levels (influenced by speculation and by this lawsuit itself), might offer higher "short-term" value (Op. 54-55), despite *this Court's* express warning in *Time-Warner* against such a "mathematical exercise." The lower court then found the directors' decision on November 15 poorly-informed, despite the Vice Chancellor's contrary findings that voluminous information on Viacom and QVC had been previously provided to the Board. Op. 54-55.

B. The Court Erroneously Assumed that the Paramount Board Decided on November 15 to Amend the Rights Plan for Viacom

The Chancery Court's opinion is also predicated on the assumption that the Board made a *final* decision on November 15 to reject QVC and to amend the Rights Plan to permit Viacom to consummate its tender offer. In fact, on November 15 the Board decided only to recommend against the QVC offer because it was highly conditional and because the Viacom transaction remained the best available alternative under all the then-existing circumstances. JA 6668-69. The Chancery Court itself recognized that the Board specifically retained the power to lift the Rights Plan for the best available alternative. Op. 20, 32. The Board anticipated a subsequent meeting to consider such action, which would be based on the status of the QVC offer at the time of such a determination, JA 6234, and the lower court was so informed by letter dated November 21, 1993. JA 6874.

C. The Court's Finding Of "Pretext" Disregarded Valid Contractual Obligations To Viacom And Was Erroneously Based On Events After November 15

(1) QVC's Changing Offer

QVC waited until Friday, November 12 at 5:29 p.m. to issue a new highly conditional, supposedly $90, offer. During the next ten days, even *after* oral argument on QVC's pending motion and, more important, *after the November 15 Board meeting*, QVC announced repeated changes to that "offer," eliminating conditions that the Board had found objectionable on November 15, obtaining conditional financing and, finally, on November 20, announcing that although the offer was fully financed, it was still conditioned on invalidation of the stock option and termination fee granted to Viacom.

Rather than excoriating QVC's last-minute antics, or recognizing that it had no record of events after November 15 on which to evaluate the evolving QVC offer, the Chancery Court was decisively influenced by these post-November 15 changes. It erroneously concluded that QVC's mad scramble for *bona fides after* November 15 and its own unprecedented decision invalidating the stock option should have been foreseen by the Paramount directors when they recommended against the highly conditional and unfinanced QVC offer that the Board had before it on November 15. The result is an opinion that imposes unprecedented *Revlon* duties on an admittedly strategic merger and that criticizes loyal and diligent directors based on events that happened *after* the Board met, for actions the Board *never* took.

(2) The No-Shop Provision

The Chancery Court failed to recognize that pursuit of QVC's November 12 "offer" was, on November 15, *flatly prohibited* by a valid "no-shop" provision in the Merger Agreement. The "no-shop" provision in the Merger Agreement--the validity of which the court did not question--had been a product of compromise: Paramount rejected a proposal that would have completely barred it from exploring any other combination. PAB 34. By its express terms, the "no-shop" clause permitted Paramount to enter into discussions with any third party who made an "unsolicited written, *bona fide* proposal, which is not subject to any material contingencies relating to financing," if the Board, upon the advice of counsel, determined in good faith that its fiduciary obligations so required. JA 1562. Discussions with any third party making a conditional, unfinanced proposal could have given rise to termination of the Merger Agreement and breach of contract claims by Viacom.

QVC knew that to satisfy the "no-shop" clause it should not condition an offer on financing and it should provide more than bare assertions of financing commitments. Op. 52; PAB 56-59. Nonetheless, QVC *expressly* conditioned its November 12 tender offer on financing, and, by its own admission, on November 15 QVC did not have its equity or bank financing commitments in place for that offer.[2] Indeed, QVC concedes that its November 12 offer was not financed until November 20, five days after the Board meeting and four days after oral argument on QVC's supposedly ripe motion. In addition, as of November 15, QVC reserved the complete right to change the terms of the back-end merger, JA 2122, and still conditioned its bid on the invalidation of

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2. QVC's BellSouth equity commitment was "nonbinding." JA 2148. The only bank commitments QVC had obtained before November 12 were the commitments to finance QVC's prior *merger proposal*, and, as QVC disclosed on October 27, those commitments could not be used to purchase shares in the QVC tender offer. JA 2654.

Viacom's option and the termination fee, which were existing and valid contractual obligations of Paramount. JA 2137, 6890-6892; PAB 77-78.

(3) The Lower Court's Ex Post Facto Review

Besides ignoring the significance of the "no-shop" restriction as of November 15, the Chancery Court also concluded that the conditionality of QVC's offer was "more a pretext than a problem." Op. 54. In doing so, the Chancery Court disregarded the testimony of Paramount's independent directors (PSB 26-27) *and* improperly chose to rely upon events that took place *after* the Board met on November 15. Thus, the Chancery Court focused on QVC's announcements of additional financing commitments on November 20—*five days after the Board meeting*—and concluded that discussions with QVC "*would have* revealed" that QVC's "financing commitments *would soon* be in hand," Op. 54 (emphasis added). In a similar vein, the Chancery Court determined with the benefit of hindsight that, because financing commitments were ultimately obtained, "as of the November 15th Paramount board meeting, QVC was, in fact, *very close* to eliminating some of the conditions and uncertainties that motivated the board's decision not to even consider the QVC proposal." Op. 30 (emphasis added). There is nothing in the record to support this finding. In reality, the announcements by QVC on November 20 were nothing more than admissions by QVC that financing was *not* in place on November 15 and that the Board's earlier reaction to the November 12 "offer" was in fact correct under the "no-shop" provision and otherwise. Moreover, the court's after-the-fact analysis was itself less than complete and did not consider, for example, that QVC's new financing commitments *remained* contingent upon the invalidation of the Viacom stock option and termination fee—valid contractual obligations that the Board could not have abrogated either on November 15 or even five days later. JA 2122.

D. The Court's Own Findings Of Fact Demonstrate That The Board Was Not Uninformed On November 15

On November 15, the Board had ample information on which to base its recommendation, including the highly conditional nature of the QVC offer, a range of financial information, a management study by Booz Allen and a fairness opinion from Lazard, see Point II.B.4 *infra*. The detailed publicly-available information on QVC presented to the Board, by itself, made plain that QVC was a less attractive merger partner than Viacom. Op. 17, n.16. In the six meetings before November 15, the Board received substantial information on Viacom and QVC. Op. 11, 13-14, 17, n.16, 21-22; JA 166-944, 950-952, 964-1360, 1419-1492. Although the Board remained able and willing to consider all *bona fide* alternatives, the information available to the Board through November 15 established that the Viacom transaction remained a very attractive strategy.

A fraction of the size of Viacom (or Paramount), QVC has assets of roughly $750 *million* (as opposed to Viacom's $4.5 *billion* and Paramount's $7.2 *billion*). Op. 4-5; PAB 72-74. In contrast to the many companies that the Board had studied as potential merger or acquisition candidates, *see, e.g.*, JA 178-81, QVC is *not* a diversified media and entertainment company with a broad array of programming assets and valuable entertainment franchises. PAB 74-77. Rather, it is an "800" number "electronic retailer" that depends, in the view of several independent directors, too much on Mr. Diller's talents—"a heartbeat deal" (JA 6031-6032)—and that has a very volatile stock price (affecting the reliability of any "short-term" calculation of the back-end merger consideration). PAB 80-81; JA 5929. And, unlike Viacom, QVC offered no synergies and had no concrete plans for a combination with Paramount except to conduct a "further review" (JA 3834; PAB 70-77, 83, 85, 136-37) and, suddenly on November 12, a single plan to develop an "interactive" programming service at some point in the future. JA 2146.

Since Paramount would contribute approximately 90% of the hard assets of a combined Paramount-QVC entity, Paramount's directors were in a position to assess the prospects of a Paramount-QVC combination. The Board had long ago reached the conclusion that the "status quo" or "going it alone" was an unattractive alternative. PAB 17-21. A combination with QVC, however, would represent only a modest change from that status quo because QVC is a relatively small one-product company in a non-complementary line of business. JA 5120, 5354-55; PAB 74-76. Thus, a strategic assessment of a QVC merger was not a complex exercise compared to what might be entailed in a merger with a diversified entertainment company such as Disney or Time-Warner or Viacom. A QVC merger is, inherently, a short-term financial play in which the "back end" equity interest consists substantially of Paramount *itself* under new management.

Because the QVC November 12 offer was both highly contingent and non-strategic, the Paramount Board unanimously rejected it. In doing so, the Board remained free to consider a *bona fide* QVC offer, if and when one was made (Op. 20, 32), and indeed expected to meet again prior to pulling the Rights Plan for Viacom, or for anyone else. JA 6234.

ARGUMENT

I.

THE CHANCERY COURT ERRED IN HOLDING THAT *REVLON* DUTIES APPLY TO A STRATEGIC MERGER IN WHICH A SUBSTANTIAL PORTION OF STOCKHOLDER EQUITY WILL CONTINUE IN THE NEW AND STRENGTHENED COMPANY

A. Standard and Scope of Review

The question whether the Board breached its fiduciary duties presents issues of both fact and law. As to the question of law presented, the standard of review is for error of law and this Court may review issues *de novo*. *Cede & Co. v. Technicolor, Inc.*, Del. Supr., Nos. 336,1991 and 337,1991, slip op. at 35, Horsey, J. (Oct. 22, 1993, revised Nov. 1, 1993); *Rohner v. Niemann*, Del. Supr., 380 A.2d 549, 552 (1977). This Court may reject the Chancery Court's factual findings if they are not the product of a logical and deductive reasoning process. *Macmillan*, 559 A.2d at 1278; *Ivanhoe Partners v. Newmont Mining Corp.*, Del. Supr., 535 A.2d 1334, 1340-41 (1987); *Smith v. Van Gorkom*, Del. Supr., 488 A.2d 858, 871 (1985); *Levitt v. Bouvier*, Del. Supr., 287 A.2d 671, 673 (1972).

B. Agreeing To A Merger With Viacom Did Not Trigger *Revlon*

On September 12, Paramount and Viacom executed a Merger Agreement in which 85% of the consideration for Paramount stockholders was a common equity stake in Paramount Viacom International. That transaction included a premium of approximately 30% over pre-agreement market values, or 70% over one year-ago unaffected trading levels. PAB 2, 40-41. Indisputably—and as recited *passim* by the Chancery Court—this merger was the culmination of strategic analyses and discussions by Paramount and its directors for many years and with many companies. *See* Op. 6-7; PAB 16-21. Paramount's decision to execute the Merger Agreement with Viacom—a decision which was made before any other bidder emerged—is protected by the business judgment rule. The Chancery Court improperly applied *Revlon* to actions taken in pursuit of this admittedly strategic merger.

1. Revlon Duties Are Not Implicated When the Board Seeks To Protect Stockholder Interests in an Ongoing Enterprise

The circumstances under which this Court has held *Revlon* duties are triggered are well-defined. *Revlon* and *Time-Warner* set forth the analysis fully applicable here, and are perfectly consonant with each other. Those decisions establish that *Revlon* duties do not arise unless the board abandons the ongoing corporate enterprise to pursue either a liquidation of the stockholders' interests or a break-up of the company. *Time-Warner*, 571 A.2d at 1150-54; *Revlon*, 506 A.2d at 182-83. In those circumstances, the board has deliberately discontinued managing the company for the benefit of the ongoing interests of its stockholders and other corporate constituencies, and it is perfectly appropriate to telescope the board's duties to achieve the maximum, immediate and realizable sale price because there remains no long-term to consider.

A review of *Revlon* itself shows that *Revlon* duties do not apply here:

- "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 . . . ."

- "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."

- "[C]oncern for non-stockholder interests is inappropriate when an auction among active bidders is in progress, and *the object no longer is to protect or maintain the corporate enterprise* but to sell it to the highest bidder."

- "*[N]othing remained for Revlon to legitimately protect*, and no rationally related benefit thereby accrued to the stockholders."

Revlon, 506 A.2d at 182-83 (emphasis added).

Likewise, *Time-Warner* reinforces these clear pronouncements. Consistent with *Revlon*, this Court recognized the need to protect strategic mergers that enhance the strength of business organizations. In *Time-Warner*, this Court concluded that unlike liquidations and bust-ups, a strategic merger will not trigger *Revlon* duties:

- Two primary circumstances—neither of which is present here—may implicate *Revlon* duties:

> "The *first*, and 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* . . . . [The second situation is] where, in response to a bidder's offer, a target abandons its long-term strategy and seeks an alternative transaction *involving the breakup of the company* . . . . *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.*"

- "Directors are *not obliged to abandon a deliberately conceived corporate plan* for a short-term shareholder profit unless there is clearly *no basis* to sustain the *corporate strategy*."

- "[W]e premise our rejection of plaintiffs' *Revlon* claim on different grounds [than the fact that the merger did not constitute change of control], namely, the absence of any substantial evidence to conclude that Time's board, in negotiating with Warner, *made the dissolution or break-up of the corporate entity inevitable, as was the case in Revlon.*

Time-Warner, 571 A.2d at 1150-54 (emphasis added) (footnote and citations omitted).

Here, the Board has not initiated an active bidding process seeking to sell itself or to effect a reorganization involving a clear break-up of the company. To the contrary, the Paramount directors all testified that Paramount has never been for sale and that they have not initiated a bidding process. See PAB 87-88. Nor has Paramount, in response to a bidder's offer, abandoned its long-term strategy and sought an alternative transaction involving the breakup of the company. *Id.* The Viacom merger *implements* Paramount's long-term strategy (*see, e.g.*, JA 5182, 5208, 5650, 6224-25) and it *predated* any offer by QVC.

The Board also has not "abandoned" the economic time horizon that, as a matter of law, has always been the Board's to establish. *Time-Warner*, 571 A.2d at 1150 (a board's "broad mandate" to manage the business and affairs of the corporation includes authority "to set a corporate course of action, including time frame, designed to enhance corporate profitability"). Far from breaking up Paramount, the Paramount-Viacom merger contemplates retaining *every* asset and *every* business of Paramount—indeed, "to maintain and expand the existing businesses of the Company and to promptly pursue new business opportunities made available as a result of the Merger." JA 2710. In a transaction involving a 49% equity exchange worth approximately $5 billion, it cannot be credibly claimed that the Board has abandoned its long-term time horizon.

Felix Rohatyn of Lazard Freres, Paramount's financial advisor, explained at his deposition why the Paramount-Viacom merger did not give rise to a sale of Paramount:

> [W]e really didn't view this as a sale of the company. We viewed this as a merger in which control of the company was transferred because of the ownership of Mr. Redstone; but that the continuing equity interest of our shareholders was so great that it was essentially, it was a hybrid transaction. It was not a sale.

JA 5828. Mr. Rohatyn identified several factors to be considered in determining whether a corporate enterprise continues to exist such that a Board can act free from constraints of *Revlon* duties. One factor is the "continuing interest[s] of [the] shareholders." *Id.* at 5828. In addition:

> I distinguish between a merger and a sale with respect to, as I said compositions/continuity of boards, of directorships, continuity of management, and the continuity of the businesses.

Id. at 5829.

When a board is not in a *Revlon* mode, it has the absolute right to enter into and protect strategic mergers. *Time-Warner*, 571 A.2d at 1151-55. The execution of a strategic merger agreement does not throw a company "into play" under *Revlon* and, paradoxically, compel exclusive focus on short-term quantifiable market "values." *See Time-Warner*, 571 A.2d at 1151; *Pogostin v. Rice*, Del. Supr., 480 A.2d 619, 627 (1984) (directors are empowered in the exercise of their business judgment to reject a takeover offer without negotiating). As this Court has recognized, a company is "under no duty to abrogate its well-established business plans to accommodate the demands of a tender offeror." *Gilbert v. El Paso Co.*, Del. Supr., 575 A.2d 1131, 1143 (1990) (discussing Chancery Court opinion in *Time-Warner*).

Thus, the Paramount Board retains the authority, indeed the obligation, to exercise its business judgment with a long-term perspective for the benefit of its stockholders. In short, unlike the facts of *Revlon*, the Paramount-Viacom merger does not present a scenario where the link between Paramount's present stockholders and the corporation as an entity will be severed, such that "no rationally related benefit" can be said to accrue to Paramount's stockholders from action taken by the Board to pursue its strategic plans. *Revlon*, 506 A.2d at 182-83.

The foregoing legal and strategic considerations have guided Paramount and its directors in making and implementing over the course of several years the long-range strategic plan that the Chancery Court has described in its opinion. Op. 6-7, 13; JA 4702-03, 4714, 4734-36, 4740, 5147-49, 5207, 5214-15, 5950. In particular, as the Court found, the merger with Viacom arose directly from this strategy.

The "breach of fiduciary duty" found by the lower court reduces to a criticism that the Paramount directors should have known in September that Paramount's strategic merger would paradoxically trigger a *Revlon* duty to abandon strategy. Yet the Chancery Court does not set forth a principle of law that can guide conduct of Paramount's directors or other directors of Delaware corporations; the Court was quite specific in *not* declaring "doctrine," *i.e.*, not examining its new "change of control" trigger in light of established law. The Chancery Court purported to limit its adoption of the "change of control" trigger for *Revlon* to the "peculiar circumstances" of this case. Op. 44. The Chancery Court then recited, as the "critical" peculiar circumstance, nothing more than the fact that the Viacom merger "will shift majority voting control from Paramount's public shareholders to Mr. Redstone." *Id.* That was, of course, the "doctrinal issue" in the first place, and this Court decided it years ago in *Time-Warner*.

Thus, by misapplying *Revlon*, the Chancery Court has criticized the Board mainly because it is ***still insisting*** on the importance of the strategic values embraced in *Time-Warner*. What the Chancery Court has done is to superimpose a *Revlon* short-term framework on a Board that knows it has a $5 billion long-term equity stake in a corporate bastion to protect. As this Court recognized in *Revlon* itself and in *Time-Warner*, the Board's task simply cannot be rationally carried out under a quantifiable short-term *Revlon* financial analysis.

2. The Chancery Court's Rule Would Significantly and Adversely Affect Strategic Mergers Involving Corporations With a Controlling Stockholder

The unavoidable conclusion of the Chancery Court's "change of control" ruling is that a company with a controlling stockholder can never enter into a strategic merger with a publicly-controlled company except via a *Revlon* auction based on short-term values. By virtue of Mr. Redstone's 85% control of the voting stock of Viacom, a merger with Viacom would nearly always involve a transfer of voting control to Mr. Redstone. If that change in control, by itself, forces the publicly-controlled company to seek only maximum short-term value, then a strategic merger (and the full benefit of Delaware law) is foreclosed to any company seeking to merge with a corporation having a controlling individual, family or corporate owner (such as The Washington Post, Dow Jones & Co., Independent News, Microsoft, Wal-Mart Stores, Harcourt General, McCaw Cellular Communications, The New York Times, or Berkshire Hathaway, just to name a few). *See also* JA 4664.

Substantial policy considerations militate against adopting the Chancery Court's new rule. It effectively eviscerates the business judgment of directors. It discourages boards from developing strategic plans, because once a plan is announced, a third party bidder can force the board to abandon its strategy and simply sell the company to the highest bidder. Moreover, it would prevent some of our most dynamic, entrepreneur-founded-and-controlled corporations from growing through strategic mergers.

Such a rule would have bizarre economic consequences generally because it would establish two sets of merger rules: one for mergers involving companies with no controlling interests and one for mergers involving companies with controlling stockholders. Those two sets of rules would not govern *those* companies, but would define the fiduciary duties *of their merger partners*, thrusting *them* into *Revlon* if they contemplate a merger. This Court has never countenanced such a binary view of the law of Delaware.

3. Change of Control Does Not Make the Dissolution or Break-up of Paramount "Inevitable"; A Theoretical "Cash-Out" Merger Does Not Change That Fact

The "change of control" trigger for *Revlon* announced by the lower court cannot survive a reading of the relevant cases. *Revlon* itself had nothing to say about "voting control." As authority for its *per se* "change of control" *Revlon* trigger, the Chancery Court briefly discussed two auction cases, *Macmillan* and *Barkan*, and centered its discussion of those pre-*Time-Warner* authorities on ambiguous language referring to "change" or "shift" in control in the context of a declared "auction." Op. 42-44. Neither of those two cases, however, is inconsistent with the long line of Delaware authorities that make clear that change of control is *not* the dispositive issue; rather, as *Revlon* itself holds, the issue is whether there is a significant continuation of stockholder equity participation in an ongoing enterprise that is the critical factor. 506 A.2d at 182-83. *Time-Warner* should have and *did* put this issue to rest. There, this Court expressly premised its decision on grounds other than the "change of control" approach taken by the Chancery Court, instead requiring that the transaction lead to the "inevitable" liquidation or break-up of the company. 571 A.2d at 1150.

The Chancery Court premises its application of *Revlon* in large part on QVC's alleged concern that the controlling stockholder of Paramount-Viacom International will "have the power to use his control at any time to eliminate the shareholders' interest by a 'cash out' merger." Op. 48. This is, of course, inherent in *any* change of control transaction, and it does not warrant the application of *Revlon*.

First, it is plainly wrong to suggest that a change of control merger inevitably means "dissolution" under the standard set forth in *Time-Warner* simply because a squeeze-out is theoretically possible. The record in this case contains *no* evidence that a "squeeze out" is likely, reasonably realistic or even possible in anything other than a hypothetical sense. The only evidence in the record is that Mr. Redstone has no intention to cash-out the minority stockholders of Paramount Viacom International. *See* JA 2710-2711, 5275-5276. In addition, there is no evidence that a cash-out transaction of the minority stockholders, which would require in excess of an additional $5 billion, is even economically feasible. Under these circumstances, liquidation of the stockholders' interests is far from "inevitable"; it is, at most, a theoretical possibility simply because Delaware law permits it. Thus, the Chancery Court's imposition of Revlon duties takes off from a completely speculative base that is contrary to the factual record before the Court.

Second, no court has ever determined that the theoretical possibility of a cash-out merger at some future time triggers the application of *Revlon*.

Third, and equally important, the notion that the minority stockholders of Paramount Viacom International can, through a "squeeze out," be deprived of the undisputed long-term benefits and synergies of the merger is wrong as a matter of law. Minority stockholders of Paramount Viacom International will be protected against any "cash out" of long-term benefits and synergies, because the issue of "fair price," whether in an appraisal action or an action for breach of fiduciary duty seeking rescissory damages, always entails consideration of the *future prospects* of the merged corporation. *See, e.g., In re Shell Oil Co.*, Del. Supr., 607 A.2d 1213, 1218 (1992) (in the appraisal process, "the corporation must be viewed as an on-going enterprise, occupying a particular market position in the light of future prospects"); *Rosenblatt v. Getty Oil Co.*, Del. Supr., 493 A.2d 929, 937, 940 (1985) (future prospects is an element of fair price); *Weinberger v. UOP, Inc.*, Del. Supr., 457 A.2d 701, 713 (1983) ("*future prospects* of the merged corporation . . . *must be considered*") (quoting *Tri-Continental Corp. v. Battye*, Del. Supr., 74 A.2d 71, 72 (1950)). Indeed, even "synergies" must be evaluated. *See TV58 Limited Partnership v. Weigel Broadcasting Co.*, Del. Ch., C.A. No. 10798, slip op. at 6, Chandler, V.C. (July 22, 1993) (noting appropriateness of discounted cash flow technique as most accurately valuing goodwill and synergy).

Thus, the minority stockholders of Paramount Viacom International will have a substantial long-term equity interest in the combined entity and the value of such long-term interest will be protected under Delaware law even if a cash-out transaction were eventually to occur. The Vice Chancellor's implicit holding that the statutory appraisal remedy and the rigorous entire fairness doctrine are poor substitutes for "structural protections" (Op. 48) is therefore unfounded and does not support his application of *Revlon* to this case.

II.

THE BOARD DID NOT BREACH ITS FIDUCIARY DUTIES ON NOVEMBER 15

A. Standard and Scope of Review

See I.A. *supra.*

B. The Board's Recommendation Concerning QVC's November 12 Proposal Was Made In Good Faith And Based On Careful Investigation Of The Facts As They Then Existed

Since September, the Paramount Board "had as its goal the carrying forward of a pre-existing transaction in an altered form." *Time-Warner*, 571 A.2d at 1155. At each step, they have carefully evaluated the alternatives *then* available. Only by superimposing *Revlon* time frames, by overlooking the information received by the Board, by ignoring the no-shop restrictions, and by assessing the Board's conduct *ex post facto*, was the court below able to find a breach of fiduciary duty.

1. Under *Unocal* and *Time-Warner*, the Board's Responses to QVC Have Been Reasonable at all Times

The Paramount-Viacom merger started out in September as a predominantly stock-for-stock exchange on a premium basis. There was no competing proposal.

On October 21, however, QVC announced an unsolicited two-tier tender offer. At that point, the Board recognized that the QVC offer was a threat to the Viacom merger. In response, Paramount permitted Viacom to (a) commence a similarly structured tender offer with (b) a substantial *increase* in consideration. Under *Unocal* and *Time-Warner*, and under even the Chancery Court's opinion, Op. 52-53, this was a reasonable response. The Board did not interpose defenses, did not foreclose any better alternative, and obtained the right to amend the Rights Plan at its discretion for the best alternative. Indeed, in response to the QVC offer and as part of the restructuring of the Viacom merger, the Board insisted that the agreement be amended so that Paramount could terminate the Merger Agreement in order to accept a better alternative without further obligation to amend the Rights Plan for the Viacom Offer.

Under *Unocal*, once the Board can establish that it had reasonable grounds for believing that a threat to corporate policy and effectiveness exists, the Board is entitled to the protection of the business judgment rule so long as the responsive measure taken by it is reasonable in relation to the threat posed. *Unocal*, 493 A.2d at 955.

A board can satisfy this burden "by showing good faith and reasonable investigation." *Id. See also Revlon*, 506 A.2d at 181. Further, the directors' ability to make this showing is "materially enhanced" where, as in this case, the board is comprised of a majority of outside, independent directors. *Unocal*, 493 A.2d at 955.

This Court has repeatedly emphasized, under both *Unocal* and even *Revlon*, the significance of an offer's conditionality, nature, timing, certainty, feasibility, legality and back-end value to a board's evaluation. *See, e.g., Time-Warner*, 571 A.2d at 1153; *Citron v. Fairchild Camera and Instrument Corp.*, Del. Supr., 569 A.2d 53, 68 (1989); *Macmillan*, 559 A.2d at 1282 n.29, 1285 n.35; *Unocal*, 493 A.2d at 955-56. Likewise, the Board's strategic judgment, its pre-existing plans, its choice of time-frame or value-enhancement, and its method of assessing value are all entitled to deference. *Time-Warner*, 571 A.2d at 1151-54.

2. The Lower Court's Opinion Reflects Significant Confusion Resulting From QVC's Last-Minute Announcements

The confusing inconsistencies and anomalies in the Chancery Court's opinion may have been caused by the tremendous transactional flux orchestrated by QVC while its motion was being briefed and argued and afterwards. The Chancery Court's opinion fully vindicated the Paramount Board's "information and processes" up to November 12. Op. 52. At 5:29 P.M., November 12, a Friday—the day after QVC filed its opening brief below and two weeks after it filed its motion—QVC announced a new "offer," which was touted as a "$90 offer," comprised of $45 per share for 51% of the shares, and equity in an amount that (based upon the November 12 price of QVC stock) was tallied at $45 as well. The November 12 offer included BellSouth as a potential co-offeror, which would replace Liberty Media as QVC's largest stockholder. JA 2122-42.

a. The Board Acted Reasonably In Recommending Against the November 12 Offer

On November 15, the Board did no more than respond to the QVC offer (as federal law required it to do within five business days) by stating its position at that point in time with respect to the offer then before it. The Board determined that the conditional, unfinanced, non-strategic QVC proposal was inferior for Paramount's stockholders to the Viacom transaction, and was legally incapable of acceptance because it was conditioned on (among other things) invalidation of the stock option and termination fee granted to Viacom. When considering that offer, the Board was entitled—indeed required by federal law—to evaluate the offer on its stated terms. 17 C.F.R. § 240.14e-2(a); *see also Fairchild Camera*, 569 A.2d at 68-69 ("We will not hold a target board of predominantly disinterested directors liable for allegedly failing to exhibit due care when the bidder does not provide the target with a definitive bid."); *In re RJR Shareholders Litig.*, Del. Ch., C.A. No. 10389, slip op. at 51-52, Allen, C. (Jan. 31, 1989), *appeal refused*, 556 A.2d 1070 (1989).

The Board's recommendation was sound: as a matter of *fact*, (i) the QVC offer *was* contingent upon invalidation of Paramount's contractual obligations to Viacom (*i.e.*, the stock option and termination fee), JA 2122; (ii) there *was* a material financing contingency; (iii) there *was no* legally valid commitment from BellSouth, QVC's co-bidder and newest (and largest) equity investor; (iv) there *was no* actual tender offer financing in place; and (v) the offer still contained a second step merger for 49% of the Paramount stock, the terms, conditions and very existence of which would later be determined by QVC "in its sole discretion." Delaware courts have repeatedly recognized a board's authority to reject conditional offers. PSB 6-7, 29-30. Significantly, although the QVC offer was not financed on November 12, the Paramount Board did *not* decide to amend the Rights Plan for the Viacom offer. JA 6234, 6874.

b. The Chancery Court Incorrectly Reviewed The Board's November 15 Recommendation On an Ex Post Facto Basis

The Board was required by federal law to evaluate the November 12 offer as it then existed and not something else. And its pre-existing contract with Viacom—a binding commitment—could not be breached on the basis of a highly contingent offer with no financing, or on the basis of speculation about what might happen next. Business judgment must be assessed as of the time it is exercised. *See Van Gorkom*, 488 A.2d at 874; *Moran v. Household Int'l*, 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).

The QVC-orchestrated flux, however, reached its crescendo *after* the Paramount Board met on November 15, and *after* November 16, when oral argument on QVC's supposedly ripe motion was held. On the morning of November 16 (less than one hour before oral argument on the preliminary injunction motion), QVC announced that on November 15 the FTC had accepted for public comment the proposed divestiture by Liberty and that QVC had reached agreement with BellSouth for an equity infusion. On Saturday, November 20—two days before the scheduled decision in this case—QVC wrote to the Chancery Court to say that its offer was, finally, "fully financed." JA 6670. The offer, nevertheless, remained conditioned on invalidation of the contractual stock option and termination fee.

When the Chancery Court rendered its decision, it had before it a formal record only through the events of November 15 (supplemented, however, with various QVC letters about financing developments thereafter). Rather than determine the merits on the record facts as they existed on November 15—*i.e.* the facts extant when the Board met—the Chancery Court erroneously criticized the directors for not anticipating *future* events.

3. The Court Erred in Ignoring The "No-Shop" Provision

"No-shop" provisions are widely used in the context of corporate combinations and have repeatedly been held to be valid and enforceable. *See, e.g., Time-Warner,* 571 A.2d at 1151 n. 15 (upholding "no-shop" clause where "Time had adopted 'no-shop' clause at Warner's insistence and for Warner's protection"); *In re Vitalink Communications Corp. Shareholders Litig.,* Del. Ch., C.A. No. 12085, slip op. at 13-14, Chandler, V.C. (Nov. 8, 1991) (upholding "no-shop" clause with "fiduciary out" provision), ***aff'd sub nom., Grimes v. John P. McCarthy Profit Sharing Plan,*** **Del. Supr., 610 A.2d 725,** ***cert. denied,*** **113 S. Ct. 179 (1992). The Chancery Court did not question the "no-shop" provision; it simply ignored it.**

Since September, QVC was familiar with the Merger Agreement and fully understood the "no-shop" restrictions. QVC knew that Paramount was contractually bound not to discuss any offer with "material contingencies relating to financing."

Nevertheless, on November 12, QVC proffered a completely conditional and unfinanced offer. Paramount was precluded from discussing such an offer with QVC. *See supra*, Facts at C-2. The

Chancery Court's finding that "discussions would have revealed . . . that QVC's financing commitments would soon be in hand," Op. at 54, obviously puts the proverbial cart before the horse. Paramount was *unable* to "talk" to QVC *until* QVC eliminated the condition and produced satisfactory evidence of financing. To do so, as QVC well knew, would have exposed Paramount to damages for breach of contract, or to the risk that Viacom would terminate the Merger Agreement.

Indeed, QVC's unfinanced November 12 offer was classic tactical litigation maneuvering. Coupled with the piecemeal announcements during the following ten days, QVC clearly intended to muddle the record, and succeeded. Although the "no-shop" restriction was recognized by the Chancery Court in other contexts (Op. 12, 16-17), the court held that a board subject to a valid "no-shop" restriction in a valid contract breached its fiduciary duty by complying with its contract.

4. The Lower Court Erred in Presuming that the Directors Would Not Fairly Consider a *Bona Fide* QVC Offer

In assessing the directors' judgment in light of later events, the Chancery Court enjoined the Paramount Board for decisions it never made. On November 15, the Board did not close the door to consideration of *bona fide* alternatives including a non-conditional, financed QVC offer. And, as the undisputed record made clear, the Paramount Board would have had to take further action in order to amend its Rights Plan for Viacom. PSB at 10; JA 6234. In presuming that the directors would—in the future—breach their fiduciary duties, the court simply usurped their prerogatives by prematurely enjoining them from acting at all.

This was error *per se*. Under similar circumstances, Delaware courts have declined to dictate to directors the outcome of future decisions concerning the deployment of rights plans. *See, e.g., MAI Basic Four, Inc. v. Prime Computer, Inc.*, Del. Ch., C.A. No. 10428, slip op. at 5, Hartnett, V.C. (Dec. 20, 1988) (refusing to direct board to redeem rights where, although board deemed current hostile offer inadequate, the board stated it was "willing to consider any further or improved offers"); *BNS, Inc. v. Koppers Co.*, 683 F. Supp. 458, 474-76 (D. Del. 1988) (refusing to invalidate rights plan where the board acted in good faith: "the directors had not taken any irrevocable steps to defeat" a hostile offer and "the board left open the possibility that it would later redeem the rights"). The court's injunction also violated the fundamental jurisdictional mandate of courts everywhere:

> A court cannot render hypothetical opinions dependent on supposition and 'whenever a court examines a matter where facts are not fully developed it runs the risk of not only granting an incorrect judgment, but also of taking an inappropriate or premature step in the development of the law.'

In Re Holly Farms Shareholders Litig., Del. Ch., C.A. No. 10350, slip op. at 9, Hartnett, V.C. (May 18, 1989, revised May 19, 1989), (*quoting Stroud v. Milliken Enters.*, Del. Supr., 552 A.2d 476, 480 (1989)).

Instead of showing any degree of deference to an admittedly loyal and highly qualified Board operating under "real world" time constraints in a highly complex and dynamic situation,[3] and instead of reviewing the Board's November 15 action based upon the facts extant when that action was taken, the Chancery Court issued an advisory injunction predicated upon an anticipatory or assumed breach of fiduciary duty.

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3. *Cf.* Bayless Manning, *The Business Judgment Rule and the Director's Duty of Attention: Time for Reality*, 39 Bus. Law. 1477, 1492-98 (1984).

5. The Court Erred In Evaluating QVC's "Offer" Based Upon Speculative Market Trading Values

Numbed by continuous assertions that the QVC November 12 offer was worth $90 per share—or "$1.3 billion more than the Viacom merger" (Op. 24-25)—the Chancery Court criticized the Board and substituted its own economic judgment, its own time frame, and its own preferred form of information.

Momentary speculation-driven market values in the midst of a contest for corporate control are misleading measures of "value." It is, indeed, to the directors' *credit* that they have not permitted arbitrage volatility to color their strategic judgment. It would be bad law, pure and simple, for this Court to compel directors to halt their strategic plans because of the momentary trading values of two 49%, multi-billion-dollar, long-term back-end equity exchanges.

In the seminal decision of *Smith v. Van Gorkom*, this Court stated unequivocally that to evaluate the adequacy of an offer to purchase shares based on short-term market values is to proceed "from a clearly faulty, indeed fallacious premise. . . ." 488 A.2d at 875-76. This principle was echoed in *Time-Warner*:

> Thus, we endorse the Chancellor's conclusion that it is not a breach of faith for directors to determine that the present stock market price of shares is not representative of true value or that there may indeed be several market values for any corporation's stock.

571 A.2d at 1150 n.12. Thus, in assessing QVC's then-current offer on November 15, Paramount's directors correctly declined to base their

business judgment on current market prices, which they understood to be unreliable.[4]

Nonetheless, reliance on the market price of QVC securities on November 12 and 15 permeates every aspect of the Chancery Court's decision.[5] Indeed, this kind of "valuation" is the turning point of the court's analysis whereby Paramount's independent directors are transformed from well-informed, well-intentioned "persons of distinction" into poorly-informed wrongdoers.

6. The Board Was Adequately Informed

From the foregoing faulty premise about the significance of affected market values, the Chancery Court found that Paramount's directors failed to come forward with any "quantitative valuation data" to support their judgment that "the *future* incremental value of the Viacom combination will exceed that $1.3 billion." Op. 54. This appears to be the heart of the court's finding of a breach of fiduciary duty.

At the outset, this holding presumes that long-range values and "business fit" are susceptible to tallying up on a credible and "final" basis as if they were short-term prices. Thus, while the court credits—and applauds—the Board's strategic vision until mid-November, and the informational base it was premised on, as soon as QVC's conditional offer surpassed the Viacom merger in terms of trading prices, the Chancery Court demands numbers. The court's revised opinion appears to emphasize this sudden switch. Op. 53. Moreover, the Chancery Court demands numbers that are "final"; it completely dismisses a "first cut"

4. *See, e.g.*, JA 6224-25 ("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."); JA 6181-82; PSB 9, 28-29.

5. *See, e.g.*, Op. 24, 25, 53, 54.

Booz Allen report, Op. 55 n.45, and disregards an enormous range of other quantitative data, as well as a fairness opinion. While referring to the validity of long-range benefits, the Chancery Court paradoxically requires such benefits to be immediately and totally quantifiable. This is wrong as a matter of fact and of law.

As a matter of law, the amount of information that a Board determines it is "prudent to have before a decision is made is *itself* a business judgment of the very type that courts are institutionally poorly equipped to make." *In re RJR Shareholders Litig.*, slip op. at 51 (emphasis added). Indeed, the decision whether to obtain a "fairness" opinion is, itself, a question of business judgment. *Citron v. Steego Corp.*, Del. Ch., C.A. No. 10171, slip. op. at 22, Allen, C. (Sept. 9, 1988). *See also Oberly v. Kirby*, Del. Supr., 592 A.2d 445, 472 (1991)("Although Delaware law requires that corporate directors evaluate the propriety of a given transaction on the basis of a full complement of information, it does not require that they seek a formal fairness opinion.").

Furthermore, the Chancery Court's conclusion that the directors should have, or could have, obtained a specific quantification of the long-term values of their strategic plan misconstrues this Court's teaching about the meaning of "enhanced scrutiny" in, among other cases, *Time-Warner*. There, this Court explained that the *Unocal* standard is not intended to serve as "a structured and mechanistic procedure of appraisal" or to lead to "a simple mathematical exercise" requiring a comparison of the discounted value of a target company's expected trading price "at some future date" with the current value of a tender offer "and determining which is the higher." 571 A.2d at 1153. On the contrary, the

> precepts underlying the business judgment rule militate against 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. *To engage in such an exercise is a distortion of the Unocal process . . . .*

Id. (emphasis added). Yet this is *exactly* what the Chancery Court has done, right down to a citation to the "mathematical exercise" that Time undertook. Op. 54-55.

Furthermore, informational needs depend in part on the nature of the "alternative" being considered. Put another way, what would be needed to compare a *diversified* media and entertainment company such as, for example, Time Warner, to Viacom, is, by order of magnitude, different from that needed to compare to Viacom a small single channel electronic retailer that does not have any comparable array of entertainment assets. Thus, the lower court's insistence on quantification, and its bootstrap conclusion that "talking" with QVC was indispensable to a proper analysis, completely ignore the Board's ability to analyze the 80% to 90% of a combined QVC-Paramount that would consist of Paramount's own businesses.

Moreover, the court below simply disregarded the information that the Board *did* use. The Board drew on years of experience, synthesized in a two-day strategy session in May 1993 to discuss merger possibilities. JA 166-510. The Board had access, obviously, to a deep knowledge of Paramount's businesses and needs. Between September and November 15, in seven separate meetings, Lazard presented Paramount's Board with a massive amount of information regarding QVC and Viacom on both a stand-alone and a combined basis, which included asset values and descriptions, income and revenue figures, an assorted array of trading and other multiples and an analysis of the strategic advantages that could be expected from a Paramount-Viacom merger. *See, e.g.*, PAB 36-38; JA 166-510, 522-697, 717-944, 950-52, 1297-1350, 1419-92, 6626-52. *See also* Op. 11, 13-14, 17 n.16, 21-22. Those materials contain substantial information about QVC, numerical and otherwise. Lazard also presented a weighted average multiple analysis, which tended to eliminate speculative influences arising from this contest for control. JA 6668. Weighted average multiples are a tool which a board can use to evaluate the alternative offers. JA 6168. Lazard presented such analyses on various occasions, including November 15. *See, e.g.*, PSB 17; JA 1306, 6641-44.

In addition, Booz Allen & Hamilton provided the Board with an evaluation which, *inter alia*, concluded that a merger with Viacom could create over $3 billion more incremental stockholder value than a merger with QVC. JA 1419-1427. The Booz Allen reports are an extensive and detailed examination conducted by a management consulting firm to ascertain cost savings and revenue enhancements from the Viacom merger. *Id.* Although the Chancery Court completely dismisses the report as a "first cut" (Op. 53), neither QVC nor the court has disputed the merits of what that first cut found.

In addition, Lazard issued oral and written fairness opinions at several stages in the process. *See, e.g.*, JA 950-52; 6620-25. Although Lazard did not assess the fairness of the conditional and unfinanced QVC offer, on November 15, after noting the higher current "market value" of the QVC offer, Lazard reaffirmed its opinion that the Viacom transaction was fair to Paramount's stockholders from a financial point of view. JA 6620-6625.

The Board relied on all of this information, as well as their many years of experience with Paramount's business. *See, e.g.*, JA 6225. For these reasons, the court's summary trivializing of the information received by directors—premised on the Court's own views of what directors can use to inform their business judgment—is error. *See Ivanhoe Partners v. Newmont Min. Corp.*, Del. Ch., 533 A.2d 585, 608, *aff'd*, 535 A.2d 1334 (1987).

Finally, the court below occasionally and half-heartedly refers to a "market check" as a source of valuation information. The court ignored: (1) the long history of Paramount's exploration of strategic options, (2) the wealth of information shared at no fewer than *seven* Board meetings since September 9, as well as at a two-day strategic meeting in May, and (3) the obvious fact that the net result of the Board's actions has been an *extraordinary increase* in the value of Paramount's shares.

Regardless of whether such a market check was required, however, in fact both a pre-transaction market check and a post-transaction market check occurred. As Paramount's investment banker testified:

> [A]s a practical matter, there had been ample opportunity for anybody interested in Paramount to contact us during the two months that our discussions with Viacom had been a matter of public speculation in the press. And under normal circumstances, at least based on my experience in this business, with that kind of a situation and the rumors going on, anybody seriously interested in a discussion with Paramount would have contacted us. . . . we didn't feel it was necessary, because in effect we felt that ample publicity had been given to the discussions between Paramount and Viacom, and nobody so much as picked up the phone to call us and say 'Before you do anything here, be sure to talk to us because we have a serious interest.'

JA 5827. Significantly, QVC was the only party to come forward with an alternative proposal either before or after the Viacom merger was announced. Furthermore, it was the opinion of Paramount's investment banker that "shopping" Paramount would have been imprudent. *Id.*

Of course, a duty to perform a market check may arise *only* in the ***Revlon*** context. Even then, it is not required because as long as "the directors possess a body of reliable evidence with which to evaluate the fairness of a transaction, they may approve that transaction without conducting an active survey of the market." *Barkan*, 567 A.2d at 1287; *see also Time-Warner*, 571 A.2d at 1153 (rejecting claim that Time board was uninformed because "the Time board's lengthy pre-June investigation of potential merger candidates, including Paramount, mooted any obligation on Time's part to halt its merger process with Warner to reconsider Paramount.").

III.

THE CHANCERY COURT IMPROPERLY INVALIDATED THE STOCK OPTION

A. Standard and Scope of Review

See I.A. *supra.*

B. The Stock Option Is A Valid And Enforceable Contractual Obligation Entered Into In Good Faith And In The Exercise Of Sound Business Judgment

After incorrectly concluding that the September 12 merger triggered *Revlon ab initio*, the Chancery Court—after finding that everything the Board had done through November 12 was proper (Op. 52)—circled back to conclude that the Viacom stock option was invalid.

In keeping with this Court's admonition to avoid duplication, Paramount refers the Court to its prior submission concerning the negotiation and validity of the options. PAB 31-32, 109-19. Paramount offers the following additional arguments which make clear that in granting the option on September 12, the directors did not breach their fiduciary duties.

First, the court's suggestion that granting the stock option was ill-advised "in light of the fact that Viacom was committed to a merger with Paramount" uses 20-20 hindsight in the worst way. In the arm's-length negotiations leading to the September 12 merger agreement (which had broken down several times), there certainly was no basis to assume that "Viacom was committed to a merger with Paramount." Op. 60. Indeed, the granting of the stock option was the *sine qua non* of the transaction. PAB 31-32.

Second, the Chancery Court's two evidentiary citations to establish Paramount's "intent" to discourage other bidders are both misunderstood. Op. 58. The first reference, to a Lazard banker's due diligence notes (JA

3227) reflected *Viacom's* desire to make the "deal. . . look strong," which is hardly impermissible for Viacom to desire. Similarly, one director's deposition answer that the option "was a question of protecting the deal" simply reflects the reality that options are demanded for that reason, among others. JA 5042. *See also* JA 5213-5214; JA 5151-5152; *Time Warner*, 571 A.2d at 1151 n.15 (approving lower court's ruling that "various safety devices adopted to protect the original agreement," such as a share exchange agreement, "predated any takeover threat . . . and had been adopted for a rational business purpose: to deter Time and Warner from being 'put in play' by their March 4 Agreement"). Nor, given the events since September 12, can it be reasonably concluded that the stock option has had the "effect" of "locking up" Paramount.

Third, the Chancery Court's criticism of the original "price" of the option is inconsistent with the court's own recitation of the extensive arms-length bargaining over price and over the terms of the option. Op. 7-10; PAB 27-34. Paramount submits that it is an intrusion upon the Board's business judgment for the Chancery Court to criticize that process with unerring hindsight, and to purport to bootstrap that untenable criticism into something that "distinguishes" this case from others in which Delaware courts have approved similarly sized options, even under *Revlon*. Op. 60. When the option was granted, it was set at the deal price. The Court's criticism would be equally applicable to such standard arrangements which are part of countless similar transactions. In any event, the proportionality of the option as a percentage of the total deal price was in line with options approved in other transactions and was not, in fact, inhibiting.

CONCLUSION

By imposing *Revlon* time frames on the Paramount Board's implementation of a sound long-range merger strategy, the Chancery Court unreasonably restricted directors who have undoubtedly acted in a fair and well informed manner. The Paramount directors have not set policy with an unfettered devotion to immediacy, nor with faith in momentary market prices as true value. The Chancery Court, pressed by an unsolicited offeror who claimed, at the last minute, to have finally obtained financing, improperly usurped the directors' judgment about strategy, value and time frame. All of this was driven by an auction frame of mind; none of it is a proper judicial function under *Time-Warner*.

By this appeal, the Paramount Board seeks the opportunity to continue to act—as it has always acted—with the best interests of their stockholders in mind. That involves *making* judgments, *having* a strategy, and testing it against *bona fide* alternatives as they arise. By this appeal, the Paramount Board seeks authority to do what directors are required to do by law.

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