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

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PARAMOUNT COMMUNICATIONS INC. :
and KDS ACQUISITION CORP., :
 :
Plaintiffs, : AFFIDAVIT
 :
v. : C.A. No. 10866
 :
TIME INCORPORATED, T.W. SUB INC., :
JAMES F. BERE, HENRY C. GOODRICH, :
CLIFFORD J. GRUM, MATINA S. HORNER, :
DAVID T. KEARNS, GERALD M. LEVIN, :
J. RICHARD MUNRO, N.J. NICHOLAS, JR., :
DONALD S. PERKINS, CLIFTON R. WHARTON, :
MICHAEL D. DINGMAN, EDWARD S. :
FINKELSTEIN, HENRY LUCE III, :
JASON D. McMANUS, JOHN R. OPEL, and :
WARNER COMMUNICATIONS INC., :
Defendants. :
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STATE OF NEW YORK)
 : ss.:
COUNTY OF NEW YORK)

STEPHEN M. WATERS, being duly sworn, deposes and says:

1. I am a Managing Director of Morgan Stanley & Co. Incorporated ("Morgan Stanley"), financial advisors to Paramount Communications Inc. ("Paramount") in connection with its tender offer for the stock of Time Incorporated ("Time"). I am familiar with the publicly disclosed information regarding Time's tender offer to purchase 100,000,000 shares of Warner

Communications Inc. ("Warner") for \$70 cash (the "front-end offer") and its plans subsequently to acquire the remaining outstanding Warner shares through merger (the "back-end merger"). I have read the Schedule 14D-1 filed by Time with the Securities and Exchange Commission in connection with its offer for Warner shares, and each of the Amendments to Schedule 14D-1 filed by Time to date, including Amendment No. 1 filed on June 19, 1989, which contained Time's Offer to Purchase, and Amendment No. 5 filed on June 28, 1989 ("Amendment 5").

2. Time originally announced that it was seeking a \$14 billion line of credit from a syndicate of commercial banks to finance the front-end offer and the cash portion of the back-end merger. (Offer to Purchase, Paramount Appendix, Ex. O)

3. In Amendment 5, Time updates its disclosure with respect to the bank financing and describes certain terms and conditions of its financing for the acquisition of Warner. The disclosure in Amendment 5 clearly indicates that Time was not able to secure a \$14 billion senior bank facility. Attached at Exhibit (b)(3) to Amendment 5 is a term sheet delivered to Time on June 27, 1989 (the "Term Sheet") by Bankers Trust Company and Manufacturers Hanover Trust Company, co-agents on a senior debt facility that will provide to Time \$8.35 billion consisting of \$5 billion to be used (along with \$2 billion raised by the sale of subordinated debt) to purchase Warner shares pursuant to the front-end offer, and \$3.35 billion to be used by Time, Warner and Time's American Television and Communications Corporation

subsidiary for certain refinancings, commercial paper programs and working capital.^{1/} The Term Sheet explicitly dictates that equity securities of Time must equal at least 25% of the total consideration paid for both the front-end offer and back-end merger.^{2/} Thus, the lending commercial bank syndicate has

^{1/} The initial funding of the senior bank debt is conditioned upon, among other things, at least \$2 billion of cash proceeds being received by Time from the issuance of subordinated debt which shall provide, among other things, that all interest for the first three years cannot be paid in cash but instead shall be payable in kind or accrue but not be payable until final maturity. Term Sheet at 14 (Exhibit (b)(3) to Paramount Reply Appendix, Ex. A).

^{2/} The Term Sheet provides in relevant part:

"Time and Warner will each agree that neither Time nor Warner, as the case may be, will propose or agree, or permit any investment banking firm retained by them for purposes of determining the Merger Consideration to propose or agree, that the Merger Consideration consist of cash or debt or equity securities of Time unless all of the following criteria are met:

(1) Equity securities of Time shall equal, as nearly as practicable, that percentage of the aggregate Merger Consideration such that at least 25% of the sum of (x) the aggregate consideration paid for the WCI [Warner] Stock pursuant to the Offer to Purchase (including, without limitation, any additional consideration equal to interest on the amount otherwise required to be paid) and (y) the aggregate Merger Consideration Amount, shall constitute equity securities. Such equity securities shall not be convertible into or exchangeable for any debt security at the option of the holder, and no debt security which is convertible into or exchangeable for an equity security shall, for such purpose, constitute an equity security. If the Merger Consideration should consist of pay-in-kind securities or convertible or exchangeable securities, the Credit Agreement should contain restrictions on Time's ability to make payment on such securities in consideration other than such securities or to convert or exchange such securities."

(continued...)

insisted that Time may not finance more than 75% of its total acquisition price for Warner with debt.^{3/}

4. The Term Sheet also contains significant restrictions on cash payments with respect to any debt or equity securities constituting the consideration paid in connection with the back-end merger.^{4/}

^{2/}(...continued)

Term Sheet at 4 (Exhibit (b)(3) Paramount Reply Appendix, EX. A).

^{3/} On Friday, July 7, Time announced that its \$8.35 billion senior bank facility had been greatly oversubscribed. This does not suggest the availability to Time of \$14 billion in bank credit, but merely a widespread willingness to participate in a credit of \$8.35 billion.

^{4/} The Term Sheet provides in relevant part:

"(2) No Restricted Junior Payment (as hereinafter defined) shall be made or be payable in respect of any debt or equity securities (other than ordinary dividend payments on the common stock of Time and the Time Series BB Preferred Stock to the extent otherwise permitted by the definitive credit agreement (the 'Credit Agreement')) constituting part of the Merger Consideration Amount before the occurrence of the eighth anniversary of the date of the Merger or as otherwise may be permitted by the Credit Agreement.

* * *

'Restricted Junior Payment' means (i) any dividend or other distribution, direct or indirect, on account of any shares of any class of stock of Time, except a dividend payable solely in shares of that class of stock to the holders of that class, (ii) any redemption, retirement, sinking fund or similar payment, purchase or other acquisition for value, direct or indirect, of any shares of any class of stock of Time or (iii) any payment or prepayment of principal of, premium, if any, or interest on, redemption, purchase, retirement, defeasance, sinking fund or similar payment with respect to, any Indebtedness, in each case, constituting Merger
(continued...)

5. Taken together, I believe these bank-dictated financing restraints demonstrate that Time's own bankers -- who have complete access to information about Time's financial position -- have made the determination that a combined Time-Warner entity will not support additional debt.^{5/} The only inference I can draw from this financing scheme is that the merged Time-Warner will be "tapped out" in terms of debt capacity. If Time is permitted to proceed with its current tender offer for Warner shares and proposed merger, therefore, Time will have effectively exhausted the borrowing capacity of the combined Time-Warner entity in order to pay an acquisition premium to Warner's shareholders.

6. If, post merger, Time-Warner has no remaining debt capacity, any third party acquiror would necessarily be forced to rely solely on its own borrowing capacity to finance any bid for Time-Warner. In our experience, an acquisition based on the acquiror's borrowing capacity alone is a rare event

4/(...continued)

Consideration; provided, however, that regularly scheduled semi-annual cash interest payments may be made on pay-in-kind or zero coupon debentures issued as part of the Merger Consideration after the time interest on such debentures may only be paid in cash according to their original terms or as otherwise may be permitted by the Credit Agreement."

Term Sheet at 5, 7 (Exhibit (b)(3) to Paramount Reply Appendix Ex A).

5/ Time is permitted to continue paying the regular dividend on the Time common stock. Presumably, if Time were to cut its dividend it could modestly increase borrowing capacity.

for large cash acquisitions, including those by strategic corporate buyers and leveraged buy-outs.

7. This debt capacity exhaustion renders an acquisition of Time-Warner by a financial or leveraged buy-out buyer virtually impossible; such a buyer would necessarily rely on the borrowing capacity of Time-Warner to finance the purchase price.

8. At the same time, I believe that the number of strategic or corporate buyers large enough to finance an acquisition of a Time-Warner entity, without relying on the borrowing capacity of such entity, is extremely limited. In fact, most of the handful of corporate buyers who theoretically could afford such an acquisition have shown no interest in the media industry generally and no specific interest in Time and Warner's lines of business. Clearly, it is extremely unlikely that a large corporate buyer which does not have a strategic interest in the Time-Warner businesses would proceed if it was required to finance an acquisition solely on the basis of its own assets or cash flow. Indeed, it is extremely unlikely in my judgment that even a large corporate buyer which does have a strategic interest in such businesses would proceed on this basis.

9. As a result, consummation of the Time-Warner transaction will have -- and seems designed to have -- the effect of precluding any subsequent acquisition of the combined entity. Simply put, there may be no buyers willing to pursue

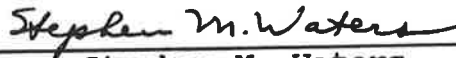
Time-Warner, stripped of its capacity to service debt. Even if such an acquisition were attempted, I believe that it certainly could not be at a price equal to or near the price that could be obtained for the sale of Time alone. To replicate the current bid at \$200 per share for the combined entity, the payments for the stock of Time-Warner plus the associated refinancing costs and expenses would require the unprecedented and staggering sum of \$30 billion.^{6/} It would rank by a wide margin as the largest acquisition ever attempted. I believe such a bid could require as much as \$27 billion of total debt (assuming an equity contribution of approximately 10%). I sincerely doubt that the combined worldwide capacity of the senior and subordinated debt markets could even fund so large a single credit, particularly given Time's attempt -- and successes -- at "drying up" financing capacity for an unwanted offer for Time through the payment of "bankmail fees". Though theoretically possible, no deal with a combined Time-Warner entity which is economically equivalent to the Paramount bid of \$200 per share of Time could, as a practical matter, be consummated. Indeed, merely the fees and expenses of completing the proposed Time-Warner transaction (which we estimate at over \$500 million) plus the taxes required

^{6/} The \$30 billion estimate roughly consists of the following components:

- (a) \$12 billion to purchase shares,
- (b) \$16 billion of refinancing, and
- (c) \$2 billion both to purchase cable minority and to cover fees and expenses.

to be paid upon the asset sales which would be required of the buyer of the combined Time-Warner entity would likely amount to billions of dollars -- a cost which would ultimately have to be borne by Time's current shareholders in the form of a substantially lower purchase price.

10. Thus, in my opinion, the amount of funds required to acquire a combined Time-Warner entity, together with Time's decision to exhaust the borrowing capacity of a combined Time-Warner entity if the acquisition is not enjoined, will foreclose the possibility of an acquisition of Time-Warner at anything close to \$200 per share and may foreclose it altogether. As a result, if Time's acquisition of Warner is consummated, Time's shareholders will have lost the opportunity to sell control of their company for anywhere near the premium being offered by Paramount.



Stephen M. Waters

Subscribed to and sworn to
before me this 10th day of
July, 1989.



Notary Public

MICHAEL RANDOLPH AMBRECHT
Notary Public, State of New York
No. 01AM4931440
Qualified in Nassau County
Certificate Filed in New York County
Commission Expires May 31, 1990