#188

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

PARAMOUNT COMMUNICATIONS INC. AND KDS ACQUISITION CORP., Plaintiffs, v. TIME INCORPORATED, et al., Defendants.	C.A. No. 10866
LITERARY PARTNERS, L.P., et al., Plaintiffs, v. TIME INCORPORATED, et al., Defendants.	C.A. No. 10935
IN RE TIME INCORPORATED SHAREHOLDER LITIGATION	CONSOLIDATED C.A. No. 10670

AFFIDAVIT OF JONATHAN O'HERRON

STATE OF NEW YORK)
: ss.:
COUNTY OF NEW YORK)

JONATHAN O'HERRON, being duly sworn, deposes and says:

1. I am a general partner of Lazard, Freres & Co., financial advisors to Warner Communications Inc. ("Warner") in connection with the proposed merger transac-

tion between Warner and Time Incorporated ("Time"). I understand that this transaction may be the subject of an application by Paramount Communications Inc. ("Paramount") for an injunction pending appeal that would prevent consummation of Time's first step tender offer for Warner shares when that offer expires at midnight, July 17, 1989.

2. I have reviewed the affidavit of Stephen M. Waters of Morgan Stanley & Co. Incorporated, financial advisors to Paramount, previously submitted in support of Paramount's motion for a preliminary injunction. In my view, the Waters affidavit is fundamentally flawed in the respects set forth below and hence the affidavit does not support Mr. Waters' conclusion (at ¶ 10) that the acquisition of Warner by Time will foreclose the possibility of an acquisition of the combined Time-Warner enterprise by a third-party at anything close to $200 per share and may foreclose it altogether.

3. First, Mr. Waters assumes, contrary to fact, that the merged Time-Warner "will be 'tapped out' in terms of debt capacity" (Waters Aff. ¶ 5) by the borrowings Time contemplates making in connection with the acquisition of Warner. Based upon my knowledge of Time's banking arrangements and of the businesses of the two companies, I believe that the merged Time-Warner could support additional debt if

required.* In this connection, I respectfully refer the Court to the affidavit of Kevin D. Senie, Vice President and Treasurer of Time, which discloses that Time received commitments from 40 banks for a total of $27.525 billion during a relatively short period (or more than three times as much financing as Time had sought) and that none of Time's lenders has ever suggested that the proposed Time-Warner combination will not support additional debt. I agree with Mr. Senie's presentation of the facts and circumtances as well as with his conclusions.

4. Second, Mr. Waters' analysis is premised on the unwarranted assumption that a putative acquiror of the combined Time-Warner enterprise would not bring any equity to the transaction itself but, rather, "would necessarily be forced to rely on its own borrowing capacity to finance any bid for Time-Warner" (Waters Aff. ¶ 6). In fact, however, a bootstrap takeover is not the only acquisition technique known to the investment community. Mr. Waters has ignored the possibility that a bidder could issue debt or equity securities either for cash with which to make the acquisition or alternatively as part of the acquisition consideration. Mr. Waters has also ignored the possibility that a

* It should be noted that Time's banking arrangements do not contemplate any asset sales which indicates that Time has by no means reached the limit of its borrowing capacity.

bidder with excess cash on hand might choose to utilize its own resources to provide some or all of the financing required for an acquisition of the combined Time-Warner enterprise. And Mr. Waters has ignored the possibility of a joint bid by two or more parties interested in ultimately acquiring various portions of the combined Time-Warner enterprise.

5. Third, Mr. Waters has overlooked the fact that if the Time-Warner transaction is consummated, the parent Company, which will have been renamed Time-Warner, will hold 100% of the stock of a subsidiary that will consist of the present Warner. Paramount or any other would-be acquiror of the combined enterprise could purchase Time-Warner, then sell the entire Warner subsidiary and use the proceeds to pay down the acquisition debt.*

6. Fourth, Mr. Waters appears to ignore the possibility that a putative acquiror could reduce the cost of an acquisition of the combined Time-Warner enterprise by selling assets of Time-Warner or alternatively of the acquiror. Thus, for example, if Paramount were to make a bid for Time-Warner -- a possibility I am advised Paramount's chief executive officer, Mr. Davis, has left open -- Para-

* Paramount would not incur any tax upon the sale of the Warner subsidiary unless it received more than the $70 per share that Time had paid.

mount might contemplate selling Warner's film studio (or alternatively selling Paramount's own film studio) in order to pay down the acquisition debt.* Other putative acquirors might contemplate a more sweeping program of post-acquisition divestitures. It is pertinent to note in this connection that earlier this week Sir James Goldmith and others announced a $21.2 billion bid for B.A.T. Industries, Inc. and expressed the intent to sell off Farmers Group Inc (a California insurer that B.A.T. had acquired for $5.2 billion only last year) as well as everything else B.A.T. owns except for its core tobacco holdings (see Exhibit A hereto).

7. For the foregoing reasons, I disagree with Mr. Waters' contention that a putative acquiror of Time-Warner would necessarily require $27 billion in debt financing in order to make a bid for the combined enterprise. And in any event, even assuming, arguendo, that a putative acquiror would need $27 billion in debt financing, I agree with the

* As noted above, a disposition of all of Warner would be tax free unless the acquiror received more than $70 per share. Other asset sales might or might not be tax free, depending upon the particular circumstances, but even if taxes were payable, the asset sales might well be desirable from the point of view of a would-be acquiror of Time-Warner. I note in this connection that KKR undertook the obligation to make asset sales aggregating about $5 billion in connection with the acquisition of RJR, even though the divestitures would give rise to tax obligations. And in any event Warner has tax attributes that might be used to reduce the tax on potential asset sales to acceptable levels.

conclusion reached by Time's investment bankers that there is no reason to believe that the capital markets could not handle such a transaction (see affidavit of Frederic M. Seegal of Shearson Lehman Hutton Inc. (at ¶ 4)).

8. Finally, in my view, there is no basis for Mr. Waters' conclusion that a hypothetical acquiror of the combined Time-Warner enterprise would be unwilling to pay anything close to $200 per share. Thus, if Time in its present form is worth at least $200 per share (which Paramount itself evidently believes to be the case) and if Warner in its present form is worth the $14 billion in cash and securities that Time has agreed to pay the Warner shareholders (which I believe and which I am told even Paramount's investment bankers believe to be the case) then there is no reason to conclude that a would-be acquiror of the combined enterprise would be unwilling to pay $200 per share to buy out the present Time shareholders who would then be shareholders of Time Warner. A fortiori, there is no reason to suppose that a would-be acquiror would be unwilling to pay at least $200 per share if the present Time is worth more than $200 per share (as Time's investment bankers and I

believe to be the case) and if the combined Time-Warner is an even more valuable enterprise.

Jonathan O'Herron

Sworn to before me this
14th day of July, 1989.

Notary Public

WILLIAM C. STERLING, INC.
Notary Public, State of New York
No. 30-9181236
Qualified in Nassau County
Certificate Filed in New York County
Commission Expires January 31, 1991