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Case No. 2317-VCL

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

BEVERLY PFEFFER, individually and on behalf of all others similarly situated, Plaintiff, v. SUMNER M. REDSTONE, GEORGE S. AMBRAMS, DAVID R. ANDELMAN, JOSEPH A. CALIFANO, JR., WILLIAM S. COHEN, PHILIPPE P. DAUMAN, ALAN C. GREENBERG, JAN LESCHLY, SHARI REDSTONE, FREDERIC V. SALERNO, WILLIAM SCHWARTZ, PATTY STONESIFER, ROBERT D. WALTER, NATIONAL AMUSEMENT, INC., JOHN F. ANTIOCO, RICHARD J. BRESSLER, JACKIE M. CLEGG, MICHAEL D. FRICKLAS, LINDA GRIEGO, JOHN L. MUETHING, and CBS CORP. (f.k.a. VIACOM, INC.), Defendants.	)	C.A. No. 2317-VCL

THE BLOCKBUSTER DEFENDANTS' OPENING BRIEF IN SUPPORT OF THEIR MOTION TO DISMISS OR STAY

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Dated: April 27, 2007

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NATURE AND STAGE OF PROCEEDINGS

In 2004, Viacom Inc. ("Viacom") launched an exchange offer (the "Exchange Offer") whereby it intended to divest its approximately 81.5% interest in Blockbuster Inc. ("Blockbuster"). Beginning shortly after the announcement of the final terms of the Exchange Offer, multiple lawsuits were filed. Eventually, the substantial majority of the litigation was centralized in the United States District Court for the Northern District of Texas.

Almost two years after the announcement of the final terms of the Exchange Offer, plaintiff Beverly Pfeffer initiated this action, primarily challenging the disclosures made in connection with the Exchange Offer. Defendants moved to dismiss this action for failure to state a claim. Defendants also moved to stay this action in favor of the litigation pending in federal court in Texas.

Instead of responding to defendants' motion to dismiss, plaintiff filed an amended complaint earlier this year. For the first time, plaintiff named as defendants certain members of the Blockbuster board of directors at the time of the announcement of the Exchange Offer, including John F. Antioco, Jackie M. Clegg, Linda Griego and John L. Muething (collectively, the "Blockbuster Defendants"). Also for the first time, plaintiff challenged a special dividend which was declared and paid by Blockbuster prior to the commencement of the Exchange Offer (the "Special Dividend").

The claim challenging the Special Dividend can and should be dismissed for two independent reasons. First, the claim is derivative, and plaintiff has made no attempt either to (i) demand that the current Blockbuster board of directors take the action that

she seeks or (ii) show that the current Blockbuster board of directors is incapable of considering such a demand. Second, the decision to pay the Special Dividend pro rata to all Blockbuster stockholders is subject to the presumptions of the business judgment rule. Because plaintiff has failed to rebut those presumptions, she has failed to state a claim.

Alternatively, this action should be stayed in favor of the broad litigation pending in federal court in Texas. The Blockbuster Defendants are all defendants in that litigation, and the declaration of the Special Dividend is at issue in that litigation. Comity and the efficient administration of justice dictate that the broader federal litigation should proceed uninterrupted by the narrower litigation here.

STATEMENT OF FACTS[1]

A. The Parties.

Plaintiff Beverly Pfeffer alleges that she tendered Viacom stock in the Exchange Offer in October 2004, and, in exchange, received Blockbuster shares. (Am. Cmplt. ¶ 7).[2] She also alleges to have owned Blockbuster Class A and B shares at the time of the declaration of the Special Dividend. (*Id.*). Plaintiff purports to represent a class of all former Viacom stockholders who tendered their Viacom stock in the Exchange Offer. (*Id.* ¶ 1). Plaintiff also purports to represent a class of all Blockbuster stockholders who held their shares at the time the Special Dividend was declared by the Blockbuster board of directors. (*Id.*).

Defendants Sumner Redstone, George S. Abrams, David R. Andelman, Joseph A. Califano, Jr., William S. Cohen, Philippe P. Dauman, Alan C. Greenberg, Jan Leschly, Shari Redstone, Frederic V. Salerno, William Schwartz, Patty Stonesifer and Robert D. Walter were members of Viacom's board of directors at the time of the Exchange Offer. (*Id.* ¶¶ 8-20). Also during this time, Mr. Redstone was chairman and chief executive officer of Viacom, as well as chairman of defendant National Amusements, Inc. ("NAI"), Viacom's controlling stockholder. (*Id.* ¶ 8). Mr. Redstone was also a director of Blockbuster from May 1999 until October 16, 2004, along with Mr. Dauman who was a director of Blockbuster from January 1995 until October 16, 2004. (*Id.* ¶¶ 8, 13).

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[1] Solely for the purposes of this motion, all well-pleaded allegations of the amended complaint are accepted as true. *Grobow v. Perot*, 539 A.2d 180, 187 n.6 (Del. 1988).

[2] A copy of the amended complaint is attached as Exhibit A to the Affidavit of Jon E. Abramczyk dated April 27, 2007 ("App.").

Defendant Richard J. Bressler was a director of Blockbuster from May 2001 until October 16, 2004. During that time, he was also senior executive vice president and chief financial officer of Viacom. (*Id.* ¶ 24).

Defendant Michael D. Fricklas was a director of Blockbuster from June 2, 2004 until October 16, 2004. During that time, he was also executive vice president, general counsel and secretary of Viacom. (*Id.* ¶ 26).

The Blockbuster Defendants -- John F. Antioco, Jackie M. Clegg, Linda Griego and John L. Muething -- were members of the Blockbuster board of directors when the Special Dividend was declared. (*Id*. ¶¶ 23-28). At that time, Mr. Antioco was chairman and chief executive officer of Blockbuster. (*Id.* ¶ 23).[3]

B. The Viacom/Blockbuster Split-Off Transaction.

On February 10, 2004, Viacom announced that it would pursue the divestiture of its approximately 81.5% interest in Blockbuster, most likely through a split-off transaction. (*Id.* ¶ 37). On June 18, 2004, Viacom and Blockbuster jointly announced that Blockbuster anticipated declaring a special dividend of $5 per share prior to the split-off. (*Id.* ¶ 38; Veet Aff. Ex. A).[4]

On August 20, 2004, Blockbuster declared a special dividend of $5 per share payable on September 3, 2004 to all Blockbuster stockholders of record as of August 27, 2004. (Am. Cmplt. ¶ 39). The Special Dividend was recommended to Blockbuster's

[3] All defendants other than the Blockbuster Defendants are collectively referred to herein as the "Viacom Defendants."

[4] Citations to "Veet Aff." refer to the Affidavit of Jennifer J. Veet filed contemporaneously herewith.

board of directors by a special committee comprised of three independent and disinterested board members -- Ms. Clegg, Ms. Griego and Mr. Muething -- following receipt by the special committee of (i) a report by its financial advisor regarding the Special Dividend and its potential impact on Blockbuster's financial condition and (ii) an opinion by a separate financial advisor to the special committee and the board of directors regarding the financial condition of Blockbuster after giving effect to the Special Dividend. (App. Ex. B at 52-66).

At the time of the declaration of the Special Dividend, the Blockbuster board of directors consisted of the following eight individuals: Mr. Antioco, Ms. Clegg, Mr. Muething, Ms. Griego, Mr. Fricklas, Mr. Redstone, Mr. Bressler and Mr. Dauman. (Am. Cmplt. ¶¶ 8, 13, 23-28).

On September 8, 2004, Viacom issued a press release announcing the terms of the Exchange Offer. (*Id.* ¶ 43). Under the terms of the Exchange Offer, each holder of Viacom Class A Common Stock and Viacom Class B Common Stock would receive 5.15 shares of Blockbuster stock, consisting of 2.575 shares of Blockbuster Class A Common Stock and 2.575 shares of Blockbuster Class B Common Stock in exchange for each Viacom share tendered. (*Id.* ¶ 44).

The Prospectus issued in connection with the Exchange Offer (the "Prospectus") disclosed that Viacom would not be required to complete the Exchange Offer unless approximately 1% of the outstanding shares of Viacom Class A and Class B stock were validly tendered. (*See* App. Ex. B at 79). The Prospectus also disclosed that Viacom

would not be required to accept shares for exchange and could extend, terminate or amend the Exchange Offer if, among other things:

- any event occurred which Viacom believed would be likely to cause the Exchange Offer to be taxable to Viacom or its stockholders;
- Viacom notified Blockbuster that it was pursuing a transaction involving Blockbuster which was more favorable to Blockbuster's stockholders than the Exchange Offer;
- a material adverse change in the business, conditions, results of operations or stock price of Blockbuster occurred;
- a material adverse change in the business, prospects, conditions or results of operations of Viacom occurred;
- Blockbuster breached certain covenants or agreements with Viacom;
- litigation was instituted that was "reasonably likely to enjoin, prohibit, restrain, make illegal, make materially more costly or materially delay completion of" the Exchange Offer;
- any order was issued which was "reasonably … likely to restrain, prohibit or delay completion of this exchange offer or materially impair the contemplated benefits of this exchange offer to Viacom or Blockbuster"; and
- the shares of Blockbuster Class B common stock issuable in the Exchange Offer were not approved for listing on the New York Stock Exchange.

(*See* App. Ex. B at 79-80). The Prospectus further disclosed that Blockbuster incurred additional debt of $950 million under a new credit agreement and through the issuance of senior subordinated notes in order to pay the Special Dividend and to finance the transaction costs in connection with the split-off. (*Id.* at 42; Am. Cmplt. ¶ 40).

C. The Litigation.

1. The Other Litigation.

The opening brief of the Viacom Defendants describes in detail the other litigation which has been filed challenging the Exchange Offer. The Blockbuster Defendants hereby incorporate by reference Section C of the Statement of Facts set forth in the Viacom Defendants' brief.

All of the Blockbuster Defendants are defendants in the consolidated securities action which is currently pending in the United States District Court for the Northern District of Texas. In addition, the second consolidated amended complaint in the consolidated securities action repeatedly references the declaration of the Special Dividend by the Blockbuster board of directors. (*See* App. Ex. J ¶¶ 37, 41, 45, 53, 55, 56, 63, 69, 94). These references include allegations that Viacom benefited from the Special Dividend at the expense of Blockbuster and the Viacom stockholders participating in the Exchange Offer. (*Id.* ¶ 45). They also include discussion of the debt incurred by Blockbuster to fund the Special Dividend. (*Id*. ¶¶ 53, 55, 56, 63, 69, 94).

2. Pfeffer's Original Complaint.

On August 3, 2006, plaintiff Beverly Pfeffer filed her original complaint in this Court. (Filing ID # 11974503). The original complaint primarily challenged the disclosures in the Prospectus. (*See* Cmplt. ¶ 2). Ms. Pfeffer purported to represent a class of Viacom stockholders who tendered their Viacom shares for Blockbuster shares in the Exchange Offer. (Cmplt. ¶ 1). None of the Blockbuster Defendants were named as defendants in the original complaint. (*See* App. Ex. T at 1).

The defendants in the original action filed a motion to dismiss or stay on October 27, 2006 and an opening brief in support of their motion on November 28, 2006. (*See* Filing ID # 12751065 & 13028959).

3. Pfeffer's Amended Complaint.

Instead of filing an answering brief in opposition to the defendants' motion, plaintiff filed an amended complaint on January 12, 2007. For the first time in this action, the Blockbuster Defendants were named as defendants. (Am. Cmplt. ¶¶ 23, 25, 27, 28). Ms. Pfeffer now not only purports to represent a class of Viacom stockholders who tendered their shares in the Exchange Offer, but she also purports to represent a class of Blockbuster stockholders who held their shares at the time the Special Dividend was declared. (*Id.* ¶ 1).

Count V of the amended complaint is the only claim made against the Blockbuster Defendants. (*Id.* ¶¶ 114-18). The allegations of Count V focus exclusively on alleged breaches of the fiduciary duties of loyalty and good faith in connection with the declaration of the Special Dividend. (*Id.*). In its entirety, Count V states as follows:

> 114. Plaintiff hereby realleges and incorporates the allegations of the preceding paragraphs as if fully set forth herein.
>
> 115. The entire fairness standard of review applies to this claim because Blockbuster's majority shareholder, Viacom, was financially interested in the transaction. They received, through their substantial Blockbuster holdings, the overwhelming majority of the $5 per share Special Dividend at a time when it was a known fact that Viacom was divesting itself of its Blockbuster holdings.
>
> 116. Corporate officers, directors and majority shareholders owe minority shareholders fiduciary obligations of honesty, loyalty, good faith and fairness. The Blockbuster Director Defendants breached those duties by causing Blockbuster to take on crippling debt in order to declare the

> Special Dividend. Under these circumstances, the Special Dividend unfairly benefited Viacom because it was known at the time of the declaration that Viacom was not going to remain a Blockbuster shareholder. Thus, while the Special Dividend was technically pro rata to all of Blockbuster's shareholders, Viacom's interests were not aligned with those of the Blockbuster minority because Viacom would divest itself of its Blockbuster shares within months and would not be present to share the fate of the Blockbuster minority.
>
> 117. The Blockbuster Director Defendants elevated the interests of Blockbuster's majority stockholder – Viacom – over the interests of Blockbuster's minority shareholders. By doing so, the Blockbuster Director Defendants breached their fiduciary duty of loyalty to the Blockbuster Class.
>
> 118. As a result of the Blockbuster Director Defendants' breaches of fiduciary duty, the Blockbuster Class was harmed.

(*Id.* ¶¶ 114-18).

At the time of the filing of the amended complaint, the Blockbuster board of directors consisted of the following eight individuals: Mr. Antioco, Ms. Clegg, Carl C. Icahn, Edward Bleier, Strauss Zelnick, Gary J. Fernandes, Robert A. Bowman and Jules Haimovitz. (Veet Aff. Ex. B at 47-49). In February 2007, James W. Crystal was appointed as a ninth director. (*Id.* at 48).

ARGUMENT

I. PLAINTIFF HAS FAILED TO SATISFY THE REQUIREMENTS OF COURT OF CHANCERY RULE 23.1.

Although the amended complaint was filed as a putative class action brought on behalf of the Blockbuster stockholders, Count V of the amended complaint (the only claim brought against the Blockbuster Defendants) is actually a derivative claim. However, plaintiff has neither made a demand that the Blockbuster board of directors pursue claims relating to the actions challenged in the amended complaint nor alleged that such demand would be futile and, therefore, should be excused. In addition, the allegations in the amended complaint do not raise any doubt concerning the disinterest, independence or business judgment of the members of the Blockbuster board of directors at the time the amended complaint was filed. Accordingly, the amended complaint fails to comply with the requirements of Court of Chancery Rule 23.1 ("Rule 23.1") and, therefore, should be dismissed.

A. The Claim Against the Blockbuster Defendants is Derivative.

A claim is not "direct" solely because it is pleaded as a direct claim. *Albert v. Alex. Brown Mgmt. Serv., Inc.*, 2005 WL 2130607, at *12 (Del. Ch. Aug. 26, 2005); *Dieterich v. Harrer*, 857 A.2d 1017, 1027 (Del. Ch. 2004); *Moran v. Household Int'l, Inc.*, 490 A.2d 1059, 1069 (Del. Ch. 1985), *aff'd*, 500 A.2d 1346 (Del. 1985). "Instead, the court must look to all the facts of the complaint and determine for itself whether a direct claim exists." *Dieterich*, 857 A.2d at 1027.

The analysis to determine whether a claim is direct or derivative is based on two questions: (1) who suffered the alleged harm and (2) who would receive the benefit of the

recovery. *Tooley v. Donaldson, Lufkin, & Jenrette, Inc*., 845 A.2d 1031, 1036 (Del. 2004). The first prong of the *Tooley* test asks this Court to look at the body of the complaint and, considering the nature of the wrong alleged and the relief requested, ask whether "the plaintiff demonstrated that he or she can prevail without showing an injury to the corporation?" *Id*. at 1036. The second prong asks whether recovery would properly belong to the corporation, rather than to the stockholders personally. *See id*. at 1039; *see also Dieterich*, 857 A.2d at 1026.

The amended complaint does not allege any direct harm to the individual stockholders. Rather, the essence of the harm alleged in the amended complaint is that "[t]he Blockbuster Director Defendants breached [their fiduciary] duties by causing Blockbuster to take on crippling debt in order to declare the Special Dividend." (Am. Cmplt. ¶ 116). If any harm was actually suffered due to the debt incurred by Blockbuster, the harm was suffered directly by Blockbuster, not by its stockholders. *See, e.g., Kramer v. W. Pac. Indus., Inc.*, 546 A.2d 348, 351 (Del. 1998) (claim alleging corporate mismanagement and a resulting drop in value of the company's stock is a classic derivative claim); *Golaine v. Edwards*, 1999 WL 1271882, at *9 (Del. Ch. Dec. 21, 1999) (claim alleging that the company became less valuable due to a $20 million payment as part of the merger agreement is derivative). Consequently, any claim related to the alleged harm would have to be brought on behalf of the corporation. *In re Syncor Int'l Corp. S'holders Litig.*, 857 A.2d 994, 997 (Del. Ch. 2004).

Therefore, plaintiff is unable to prevail without showing injury to Blockbuster. Further, any recovery for this alleged harm would be received by Blockbuster and not the

individual stockholders. Thus, under both prongs of the *Tooley* analysis, Count V of the amended complaint is derivative.

B. Rule 23.1.

Because Count V is actually a derivative claim brought on behalf of Blockbuster, plaintiff must satisfy the requirements of Rule 23.1. Rule 23.1 requires that in a derivative action brought by stockholders on behalf of the corporation, "[t]he complaint shall … allege with particularity the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires from the directors or comparable authority and the reasons for the plaintiff's failure to obtain the action or for not making the effort." Ct. Ch. R. 23.1.

The Delaware Supreme Court has repeatedly reaffirmed the rigorous pleading requirements of Rule 23.1 applicable to stockholder derivative complaints. The Supreme Court has noted that pleadings in derivative suits "must comply with stringent requirements of factual particularity that differ substantially from the permissive notice pleadings governed solely by Chancery Rule 8(a)." *Brehm v. Eisner*, 746 A.2d 244, 254 (Del. 2000). The pleadings "must set forth … particularized factual statements that are essential to the claim." *Id*.

Where, as here, demand has not been made, the plaintiff bears the burden of alleging with particularity why demand should be excused as futile. *See, e.g., Aronson v. Lewis*, 473 A.2d 805, 815 (Del. 1984); *Zupnick v. Goizueta*, 698 A.2d 384, 386 (Del. Ch. 1997); *Haber v. Bell*, 465 A.2d 353, 357 (Del. Ch. 1983). If a derivative plaintiff fails to carry its burden of demonstrating that demand should be excused, the complaint must be

dismissed, even if the claim is otherwise meritorious. *See, e.g., Kaufman v. Belmont*, 479 A.2d 282, 286 (Del. Ch. 1984); *Haber*, 465 A.2d at 357.

Rule 23.1 is not merely a technical requirement of pleading, but rather a rule of substantive law. *See, e.g., Grimes v. Donald*, 673 A.2d 1207, 1216 (Del. 1996); *Levine*, 591 A.2d at 207; *Haber*, 465 A.2d at 357. Demand under Rule 23.1 "is an objective burden which must be met in order for the shareholder to have capacity to sue on behalf of the corporation. The right to bring a derivative action does not come into existence until the plaintiff shareholder has made a demand on the corporation to institute such an action or until the shareholder has demonstrated that demand would be futile." *Kaplan v. Peat, Marwick, Mitchell & Co.*, 540 A.2d 726, 730 (Del. 1988); *accord Levine*, 591 A.2d at 200; *Greenwald v. Batterson*, 1999 WL 596276, at *4 (Del. Ch. July 26, 1999). As the Supreme Court stated in *Grimes*,

> [t]he demand requirement serves a salutary purpose. First, by requiring exhaustion of intracorporate remedies, the demand requirement invokes a species of alternative dispute resolution procedure which might avoid litigation altogether. Second, if litigation is beneficial, the corporation can control the proceedings. Third, if demand is excused or wrongfully refused, the stockholder will normally control the proceedings.
>
> The jurisprudence of *Aronson* and its progeny is designed to create a balanced environment which will: (1) on the one hand, deter costly, baseless suits by creating a screening mechanism to eliminate claims … (2) on the other hand, permit suit by a stockholder who is able to articulate particularized facts showing that there is a reasonable doubt either that (a) a majority of the board is independent for purposes of responding to the demand, or (b) the underlying transaction is protected by the business judgment rule.

Grimes, 673 A.2d at 1216-17 (footnotes omitted).

C. Plaintiff Made No Demand on the Blockbuster Board of Directors and Demand Would Not be Futile.

Where, as here, a derivative plaintiff does not challenge a particular action undertaken by the current board of directors as a whole, the standard established in *Rales v. Blasband* governs the determination of demand futility. Under the *Rales* test:

> [A] court must determine whether or not the particularized factual allegations of a derivative stockholder complaint create a reasonable doubt that, as of the time the complaint was filed, the board of directors could have properly exercised its independent and disinterested business judgment in responding to a demand. If the derivative plaintiff satisfies this burden, then demand will be excused as futile.

Rales v. Blasband, 634 A.2d 927, 934 (Del. 1993). As set forth below, plaintiff has not come close to satisfying her burden.[5]

The composition of a majority of the Blockbuster board of directors changed between the time of the declaration of the Special Dividend and the time the amended complaint was filed.[6] Under such circumstances, the Court's inquiry should focus on the disinterestedness and independence of the board of directors in existence at the time the amended complaint was filed. *Rales*, 634 A.2d at 934; *In re Fuqua Indus., Inc. S'holder Litig.*, 1997 WL 257460, at *13 (Del. Ch. May 13, 1997). Therefore, for demand to be excused as futile, plaintiff must plead particularized facts creating a reasonable doubt that the Blockbuster board of directors in place at the time the amended complaint was filed

[5] Even assuming that the two-pronged test of *Aronson* rather than the one-pronged test of *Rales* applies to this case, for the reasons set forth in Section II below, plaintiff has not pled "particularized facts sufficient to create a reasonable doubt that the challenged transaction was the product of a valid exercise of business judgment." *Levine v. Smith*, 591 A.2d 194, 205 (Del. 1991).

[6] As noted above, the original complaint did not include the Blockbuster Defendants.

could have properly exercised its independent and disinterested business judgment in evaluating the demand. *Rales*, 634 A.2d at 934. Plaintiff has not -- because she cannot -- pled such facts.

At the time of the declaration of the Special Dividend, the Blockbuster board of directors consisted of Mr. Antioco, Ms. Clegg, Mr. Muething, Ms. Griego, Mr. Fricklas, Mr. Redstone, Mr. Bressler and Mr. Dauman. (Am. Cmplt. ¶¶ 8, 13, 23-28). At the time of the filing of the amended complaint, however, the only individuals that remained as directors were Mr. Antioco and Ms. Clegg. The other six directors were Messrs. Icahn, Bleir, Zelnick, Fernandes, Bowman and Haimovitz. (Veet Aff. Ex. B at 47-49). Therefore, even assuming that Mr. Antioco and Ms. Clegg were interested in the Special Dividend or lacked independence from Viacom -- which they were not and did not -- plaintiff has not even attempted to allege that the six new directors are interested or that they lacked independence. Accordingly, plaintiff has not adequately pled demand futility, and the amended complaint must be dismissed.

II. PLAINTIFF HAS FAILED TO STATE A CLAIM UPON WHICH RELIEF CAN BE GRANTED BASED ON RULE 12(b)(6).

A. The Applicable Standard.

Even assuming plaintiff's Count V were a direct (as opposed to derivative) claim -- which it is not -- the amended complaint also fails to state a claim upon which relief can be granted. The standards that apply to a motion to dismiss are well settled. Court of Chancery Rule 12(b)(6) requires dismissal where, as here, it appears to "a reasonable certainty that a plaintiff would not be entitled to the relief sought under any set of facts which could be proven to support the action." *Rabkin v. Philip A. Hunt Chem. Corp.*, 498

A.2d 1099, 1104 (Del. 1985). A complaint must allege facts which, if taken as true, would establish each element of a claim upon which relief can be granted. *Lewis v. Honeywell, Inc.*, 1987 WL 14747, at *4 (Del. Ch. July 28, 1987). Furthermore, in applying this standard, unsupported factual inferences and conclusions of law will not be accepted as true. *Grobow*, 539 A.2d at 187.

A "motion to dismiss concedes only well pleaded allegations of fact. It does not concede conclusory allegations of law or fact where there are no allegations of specific fact that would support such conclusions." *Lewis*, 1987 WL 14747, at *4 (emphasis omitted). Moreover, as the Delaware Supreme Court has stated, on a motion to dismiss under Rule 12(b)(6), "all facts of the pleadings and reasonable inferences to be drawn therefrom are accepted as true, but neither inferences nor conclusions of fact unsupported by allegations of specific facts upon which the inferences or conclusions rest are accepted as true." *Grobow*, 539 A.2d at 187 n.6.

B. Plaintiff's Amended Complaint Fails to State a Claim that the Blockbuster Defendants Breached their Fiduciary Duties.

The business judgment rule is "a presumption that directors making a business decision, not involving self-interest, act on an informed basis, in good faith and in the honest belief that their actions are in the corporation's best interest." *Grobow*, 539 A.2d at 187. Because of this presumption, a court may not "assume that the transaction was a wrong to the corporation requiring corrective measures by the board." *Pogostin v. Rice*, 480 A.2d 619, 624 (Del. 1984). Instead, plaintiffs must "plead particularized facts creating a reasonable doubt as to the 'soundness' of the challenged transaction sufficient

to rebut the presumption that the business judgment rule attaches to the transaction." *Levine*, 591 A.2d at 206.

The declaration and payment of dividends is one of the paradigmatic managerial decisions within the discretion of directors and protected by the business judgment rule. Under Section 170 of the Delaware General Corporation Law, directors of Delaware corporations are specifically authorized, subject to any restrictions in the certificate of incorporation, to declare and pay dividends either out of the corporation's surplus or out of the corporation's net profits. 8 *Del. C.* § 170(a).

Delaware law plainly leaves the questions of whether, and when, dividends should be paid to the discretion of directors:

> It is settled law in this State that the declaration and payment of a dividend rests in the discretion of the corporation's board of directors in the exercise of its business judgment; that, before the courts will interfere with the judgment of the board of directors in such matter, fraud or gross abuse of discretion must be shown.

Gabelli & Co. v. Liggett Group Inc., 479 A.2d 276, 280 (Del. 1984) (citation omitted); *see also Horbal v. Three Rivers Holding, Inc.*, 2006 WL 668542, at *3 (Del. Ch. Mar. 10, 2006); *Garza v. TV Answer, Inc.*, 1993 WL 77186 (Del. Ch. Mar. 15, 1993). Moreover, "[i]n today's financial world, dividends and self-tender offers are viewed as conventional methods of delivering to shareholders a return on their investment." *Weiss v. Samsonite Corp.*, 741 A.2d 366, 371 (Del. Ch. 1999), *aff'd*, 746 A.2d 277 (Del. 1999) (TABLE). Such "transactional choices" -- whether to "enhance shareholder value" through methods such as "paying an extraordinary dividend" or "conducting a partial self-tender at a substantial above-market premium" -- are "classic business judgment decisions of the

kind that are normally protected by the business judgment rule." *Id.* at 371-72; *see also Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 721 (Del. 1971) (court will interfere with board's payment of dividend only if "a plaintiff can meet his burden of proving that a dividend cannot be grounded on any reasonable business objective"); *Moskowitz v. Bantrell*, 190 A.2d 749, 750 (Del. 1963) (court will interfere with board's judgment to issue a dividend only on showing of fraud or gross abuse of discretion). Plaintiff has made no allegation sufficient to rebut the presumptions of the business judgment rule.[7]

Delaware courts repeatedly have rejected claims of self-dealing in cases involving the payment of a pro rata dividend. For example, in *Sinclair Oil Corp. v. Levien*, 280 A.2d 717 (Del. 1971), this Court found there was no possibility of self-dealing where a company (Sinven) allegedly paid out excessive dividends to benefit its 97% stockholder (Sinclair). The dividends that were paid over a six-year period exceeded Sinven's earnings over that period, and the Chancellor found that Sinclair caused the dividends to be paid during a time when it had a special need (unshared by other stockholders) for large amounts of cash. Nevertheless, the Delaware Supreme Court concluded that, even though "[t]he dividends resulted in great sums of money being transferred from Sinven to Sinclair," the dividends were not self-dealing as a matter of law because "a proportionate share of this money was received by the minority shareholders of Sinven." *Id.* at 721-22. The Supreme Court stressed that "Sinclair received nothing from Sinven to the exclusion

[7] The amended complaint does not even mention the fact that the Special Dividend was recommended to the Blockbuster board of directors by a special committee of independent directors.

of its minority stockholders." *Id.* The Supreme Court applied the business judgment standard to the transaction, and found that the dividend payments complied with that standard because they did not amount to "waste," "fraud," or "gross overreaching." *Id.* at 722.

This Court has reaffirmed the holding of *Sinclair* that a pro rata dividend cannot, as a matter of law, be self-dealing. In *Ivanhoe Partners v. Newmont Mining Corp.*, 533 A.2d 585 (Del. Ch. 1987), *aff'd*, 535 A.2d 1334 (Del. 1987), a company paid a $33 dividend to all stockholders, which enabled its largest stockholder to engage in a "street sweep" of the company's stock. The Court applied the business judgment rule to the transaction because "no self-dealing is shown…. [T]he dividend is to be paid to all Newmont shareholders in proportion to their stock interest, and the defendants will receive no greater proportionate share than would the minority stockholders." *Id.* at 602.

The Court reached the same conclusion most recently in *Teachers' Retirement System of Louisiana v. Anschutz*, C.A. No. 444-N (Del. Ch. June 1, 2004) (TRANSCRIPT). In *Teachers'*, Chancellor Chandler stated:

> Regarding Count I, the duty of loyalty claim, I conclude that the plaintiff has not demonstrated a reasonable likelihood of success because there is absolutely no evidence, not a shred of evidence, that Mr. Anschutz or his affiliates have received anything from Regal to the exclusion of or detriment to the minority stockholders.
>
> The Supreme Court in *Sinclair Oil*, and this Court in *Ivanhoe Partners*, found that a pro rata dividend is not self-dealing. The pro rata dividend here is also not self-dealing. The idea for the dividend did not even originate with Anschutz. I also believe, in the circumstances of this case, that simply because Anschutz and others are large shareholders in Regal or that they purchased [at] a price different than the public did in an IPO does not somehow magically transform the pro rata dividend into a form of self-dealing. Based on the evidence in the record, abbreviated as it

> is on a motion of this kind, it appears that Anschutz's large holdings only serve to align his interest with that of plaintiff and other minority shareholders.

Id. at 4-5 (Veet Aff. Ex. C).

Here, plaintiff concedes that "the Special Dividend was technically pro rata to all of Blockbuster's shareholders." (Am. Cmplt. ¶ 116). She goes on to allege, however, that "Viacom's interests were not aligned with those of the Blockbuster minority because Viacom would divest itself of its Blockbuster shares within months and would not be present to share the fate of the Blockbuster minority." (*Id.* ¶ 116). This allegation cannot save the amended complaint for at least two reasons.

First, it is contrary to the undisputed facts. At the time of the declaration of the Special Dividend, there was no guarantee that the Exchange Offer would be completed, since it was subject to a number of conditions. In fact, the Special Dividend was declared on August 20, 2004 -- almost three weeks before Viacom issued its press release announcing the terms of the Exchange Offer on September 8, 2004. In addition, Viacom would only cease to be a Blockbuster stockholder if the Exchange Offer were fully subscribed -- certainly not a foregone conclusion. Therefore, when the Special Dividend was declared, it was not definitively known that Viacom was not going to remain a Blockbuster stockholder.

Second, even if it were known that Viacom was not going to remain a Blockbuster stockholder when the Special Dividend was declared, plaintiff still has not stated a claim. As set forth above, the fact that a large stockholder may have interests that are arguably different than the interests of other stockholders has repeatedly been rejected by

Delaware courts as a basis to challenge a pro rata dividend. *See Sinclair Oil Corp.*, 280 A.2d at 722; *Teachers'*, tr. at 4-5; *Ivanhoe Partners*, 533 A.2d at 602. Moreover, nothing prevented the other stockholders from the taking the dividend and then selling their shares of Blockbuster stock just as Viacom did.

In summary, the amended complaint concedes that the Special Dividend was pro rata to all Blockbuster stockholders. A pro rata dividend is not self-dealing, and, therefore, the business judgment rule applies. Accordingly, plaintiff has failed to satisfy the requirements of Rule 12(b)(6), and her complaint against the Blockbuster Defendants should be dismissed.

III. THE CASE SHOULD BE STAYED IN FAVOR OF THE FIRST-FILED CONSOLIDATED SECURITIES CLASS ACTION.

This Court should exercise its discretion to stay this action in favor of the consolidated securities action that is pending in federal court in Texas. "When similar actions between the same parties involving the same issues are filed in separate jurisdictions the court in which either of said actions is filed may in the exercise of its discretion hold that action in abeyance to abide the outcome of the action pending in the other court." *Gen. Foods Corp. v. Cryo-Maid, Inc.*, 198 A.2d 681, 683 (Del. 1964).

It is well-settled under Delaware law that the Court should exercise its discretion freely in favor of a stay "when there is a prior action pending elsewhere, in a court capable of doing prompt and complete justice, involving the same parties and the same issues." *McWane Cast Iron Pipe Corp. v. McDowell-Wellman Eng'g Co.*, 263 A.2d 281, 283 (Del. 1970). "[A]s a general rule, litigation should be confined to the forum in which it is first commenced…." *Id.*; *see also Gen. Video Corp. v. Kertesz*, 2006 WL 2051023,

at *3 (Del. Ch. July 19, 2006) ("[i]t is well established that a Delaware court typically will defer to a first-filed action in another forum and stay Delaware litigation pending adjudication of the same or similar issues in the competing forum.").

Further, "in class action suits there is less reason for reluctance in granting a stay, since the purpose of a class action is to adjudicate the claims of many persons in a single proceeding." *Stepak v. Columbia Pictures Entm't, Inc.*, 1988 WL 55307, at *1 (Del. Ch. May 27, 1988); *see also Joseph v. Shell Oil Co.*, 498 A.2d 1117, 1123 (Del. Ch. 1985) ("[t]he very nature of a class action precludes each claimant from maintaining a separate suit"). "There is no need for two identical class actions brought on behalf of the same class to proceed simultaneously." *Stepak*, 1988 WL 55307, at *2.

The free exercise of granting such a stay is "impelled by considerations of comity and the necessities of an orderly and efficient administration of justice." *McWane*, 263 A.2d at 283. Thus, Delaware courts grant stays in order to avoid wasteful, duplicative, litigation and the risk of inconsistent judgments. *Id.*

In the interest of brevity, the Blockbuster Defendants join in the arguments set forth in the Viacom Defendants' opening brief in support of a stay. The Blockbuster Defendants add two additional points.

First, all of the Blockbuster Defendants are also defendants in the consolidated securities action. Thus, the "identity of parties" requirement is satisfied with respect to the Blockbuster Defendants.

Second, the second amended complaint in the consolidated securities action includes numerous allegations regarding the declaration of the Special Dividend -- the

only subject matter of the claim against the Blockbuster Defendants in this action. (*See* App. Ex. J ¶¶ 37, 41, 45, 53, 55, 56, 63, 69, 94). The consolidated securities action is a broader action which includes substantially the same issues as this action. Accordingly, this action should be stayed in favor of the first-filed and broader consolidated securities action. *See, e.g., Schnell v. Porta Sys. Corp.*, 1994 WL 148276, at *4 (Del. Ch. Apr. 12, 1994) (staying a second-filed Delaware action alleging breach of fiduciary duty, fraudulent misrepresentation, concealment and nondisclosure in favor of a federal court action alleging violations of Section 10(b) and Section 20 of the Securities and Exchange Act of 1934).

CONCLUSION

For the foregoing reasons, the Blockbuster Defendants' motion to dismiss, or, in the alternative, to stay, should be granted.

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