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Dear Maverick: The Hard Deck Is June 4, 2027, Time for David Ellison to Do the Unthinkable

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While Paramount has repeatedly claimed that the State AGs and the WGA have ignored reality to invent an antitrust case to block the merger of Paramount Skydance and Warner Bros. Discovery, we believe it no longer matters. Nor does David Ellison's view that the State AGs' case is politically motivated and tied to CNN. Nor does Chief Legal Officer Makan Delrahim's view that the complaint is a "weaponization of antitrust law" designed to shield Netflix from real competition. All that matters now is June 4, 2027, the date the merger agreement expires and Paramount is required to pay WBD a $7 billion break fee. We believe Paramount must settle with the State AGs and the WGA or risk losing Warner Bros. Discovery entirely, even if it is ultimately right on the law. Paramount's problem is twofold: (1) the State AGs and the WGA do not appear interested in settling, and (2) there is no structural remedy that satisfies the State AGs and the WGA without hollowing out the deal's strategic and financial rationale.

Earlier this week, District Court Judge Araceli Martinez-Olguin scheduled the trial for March 2-19, 2027, with post-trial briefs due by April 5, 2027.

The District Court trial timetable implies three things:

1) Martinez-Olguin is not a fan of the team at Paramount, which proposed a November trial date. Combined with her comments when granting the temporary restraining order last month, it appears she is already favorably predisposed to the State AGs/WGA case.

2) There is no set timeframe for a judge to render an opinion after court hearings conclude, with historical timeframes ranging from weeks to months. Given the complexity of this case and Martinez-Olguin's lack of antitrust experience, there is no basis to assume she will render a decision quickly after the April 5th post-trial brief deadline.

3) If Martinez-Olguin finds in favor of the State AGs/WGA prior to June 4th, there will not be enough time for an appeal before the June 4th merger drop-dead date.

Given these three factors, Paramount must find a way to settle before the trial begins in March 2027.

What Happens on June 4th

If the legal process drags on until June 4th, the PSKY/WBD merger agreement terminates, and we see no reason why WBD would give Paramount additional time to solve its legal issues. Warner Bros. Discovery will almost certainly allow the merger agreement to terminate and collect $7 billion from Paramount. The payment would be funded directly by the Ellison family, which would contribute $7 billion in cash to Paramount in return for equity at $16/share (*even though PSKY is trading at half that level today*).

With $7 billion in cash, WBD would be in a much stronger financial position and would likely move quickly to split up the company into Warner Bros. studio/HBO and Discovery Global Networks, as it intended prior to the Paramount acquisition agreement. We have to believe there would be lots of buyers for Warner Bros. studio/HBO in late 2027. Would Netflix come back? Would a post-split NBC Universal have interest? Or would Warner Bros. simply operate as a standalone company with far less leverage than it was expected to have under the prior split? Who knows, but the optionality and lots of cash payment from Paramount would put

WBD in a much stronger financial position. Important to note that if Paramount cannot combine with Warner Bros. Discovery, it is unclear what M&A could get through, even if we are only talking about a portion of WBD.

We simply do not see any world in which Warner Bros. Discovery allows the merger to continue while Paramount appeals to the Ninth Circuit Court of Appeals or the Supreme Court, as Jeffrey Kessler, Paramount's former lead trial counsel (Beth Wilkinson is now lead counsel), discussed last month on CNBC (**link**).

Would State AGs Settle?

We highly doubt the State AGs or the WGA will settle for behavioral remedies (such as an Editorial Oversight Board at CNN, as proposed on CNBC by TKO Executive Chair and CEO Ari Emanuel), given that all signs point to a judge who is favorably disposed to their case, the broad-based dislike for the merger throughout the Hollywood community (*beyond certain movie theater owners who are just happy their businesses survived the COVID-19 pandemic*), and the time pressure Paramount is under to close before June 4th. Then add in how politicized the merger has become, regardless of whether the changes Paramount has made ultimately prove effective (*did Paramount really need to shake up 60 Minutes before the WBD merger closed?*).

Then add in that California Attorney General Rob Bonta has signaled he is not interested in any form of settlement (behavioral or structural). He simply wants the merger blocked. While some believe Bonta will soften his posture after November's midterms, once the political heat of an election year has passed, we disagree. Bonta will be a hero in Hollywood if this merger is blocked, and time pressure works against Paramount, not Bonta and the State AGs/WGA.

Despite Bonta's lack of interest in settling, we have to believe there are substantial structural remedies that Paramount could propose to bring the market share concentrations of the combined PSKY/WBD below the levels viewed as problematic in the State AGs/WGA lawsuits. And we are not talking about simply selling CNN. Paramount would need to buy Warner Bros. and then sell a substantial part of the combined asset base to a third party.

Studio Remedies: While Paramount has said it plans to retain both studio lots, it could offer to sell one of the two lots (either Paramount or Warner Bros.), the theatrical distribution infrastructure tied to that studio (duplicative to Paramount anyway) and several major franchise IP/content assets. Could Paramount offer to sell Harry Potter, all of DC Comics and Dune, among others? These IP franchises would have incredible value to a wide variety of industry players and, when combined with the sale of a certain percentage of library titles, the lot and distribution infrastructure could enable the creation of a new major Hollywood studio. Obviously, this would be painful for Paramount, as it would lose a significant portion of the transaction synergies, but it would still significantly bolster its existing library, retain HBO and be able to combine it with Paramount+ and Pluto to focus on winning in streaming.

Linear Networks Remedies: Rather than retain all 50 cable networks, Paramount could look to shed the Turner Networks, including TBS, TNT and CNN. Not only would this remove fears of transforming CNN editorially, but it would also reduce the sports and news distribution leverage Paramount would gain from the WBD acquisition. Paramount would effectively be acquiring only the Discovery Global Networks. Paramount would lose substantial distribution leverage with fewer total networks, in addition to TNT and TBS both having sports rights that add to Paramount's aggregate negotiating leverage with MVPDs/vMVPDs. Not being able to combine CBS News and CNN would also eat into the hoped-for merger synergies. But the worst part of shedding cable networks is that Paramount would likely be selling the networks at a fraction of the price it is paying WBD for the assets (*Disney just sold its 50% share of A&E Networks to Hearst for under 3.5x EV/EBITDA, albeit those networks had no sports or news*).

Bottom Line

We know David Ellison and his team at Paramount do not want to offer any structural remedies, as they are confident they can ultimately beat the State AGs/WGA in court. However, time is not on their side, and going to trial is simply too risky. We believe the odds of the Paramount-Warner Bros. Discovery merger closing fell rapidly once a trial date was set for March 2027. It is time for Ellison and his team to make the hard decision, do the unthinkable and offer substantial structural remedies that will weaken the combined company's strategic and financial positioning. Unfortunately, the alternative of owing $7 billion to WBD and walking away with nothing is the worst outcome of all.

The question becomes whether David Ellison realizes the transaction he hoped to close is now impossible and can accept a far less compelling combination, no matter how painful, before slamming into the hard deck on June 4th.

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