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**I. INTRODUCTION**

The Rigases committed a massive fraud. No one denies that. It is the primary reason why, nearly four years into this bankruptcy case, creditor constituencies remain at war with each other over how to distribute too few assets on account of too many liabilities.

Indeed, much of the remaining controversy in this case involves, in one way or another, whether the burden of the Rigas fraud should be borne equitably by all or by a disfavored few. The Hearing 3 briefs of Huff and the Arahova Committee starkly illustrate this dynamic. Both devote the majority of their briefs to knocking down a straw man by trying to “prove” that the Rigases engaged in criminal and fraudulent conduct. They did. We agree. We further agree that the fraud included the Rigases’ failure to disclose the full extent of Adelpia’s liability under the Olympus Facility, which was made possible by the September ’01 Transaction that Huff and the Arahova Committee now seek to dissect, pick apart, and avoid, but only as to Step 7 of the integrated ten-step transaction. (As we describe below, it goes too far to say, as does the Arahova Committee, that the “*procurement*” of the Olympus Facility itself, as opposed to the non-disclosure of Adelpia’s joint and several liability for the Rigases’ borrowings under the facility, was itself a fraudulent act.)<sup>1</sup>

Where we diverge is with respect to the consequences of these agreed facts. Reminiscent of the positions taken at Hearings 1 and 2 – where they argued that the Rigas fraud should be borne solely by creditors of ACC on the (false) ground that ACC somehow was more complicit in the fraud than any other Adelpia entity<sup>2</sup> – Huff and the Arahova Committee now assert that, due to the fraud, Step 7 (and *only* Step 7) of the September ’01 Transaction should be avoided so that (not coincidentally) Arahova’s creditors reap all the benefit and the creditors of ACC and Olympus incur all the pain. This makes no sense for several fundamental reasons.

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<sup>1</sup> Ara. H3 Br. ¶ 1 (“The September 28 Dividend was part and parcel of the Rigases’ fraudulent procurement of the . . . Olympus Co-Borrowing Facility . . .”). In this Brief, “ACC H3 Br.,” “Ara. H3 Br.,” and “Huff H3 Br.” refer to the Opening Briefs for Hearing 3 filed by the ACC Committee, the Arahova Committee, and Huff, respectively, and “H3 Supp. Ex.” refers to exhibits to the accompanying Supplemental Appendix. Capitalized terms not defined in this Brief have the meanings given to them in our prior Briefs submitted pursuant to the MIA Order.

<sup>2</sup> See, e.g., ACC H2 Rpy. at 3-4 and 14-17.

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*First*, if the mere act of obtaining the Olympus Facility (as opposed to the failure to disclose Adelpia's liability for the Rigases' use of loan proceeds to line their own pockets) was a fraudulent act, then the Rigases' prior act of obtaining the Century Facility through the April '00 Transaction also was a fraudulent act. **Both** the Century Facility and the Olympus Facility were co-borrowing facilities to which the Rigases had access; **both** were made possible by the movement of legal entities and cable systems around the Adelpia enterprise; and **both** ultimately resulted in the Adelpia entities becoming liable for massive amounts of borrowings made by the Rigases. Yet, Huff and the Arahova Committee are curiously silent when it comes to the April '00 Transaction and the Century Facility, and they certainly do not suggest that Arahova and its subsidiaries should return to ACC Ops the entities and cable systems, servicing 800,000+ subscribers, that moved *into* the "Arahova family" (to use the Arahova Committee's term) in order to facilitate the Century Facility and the Arahova Bridge Facility.

*Second*, even if the "fraud" is viewed to be the procurement of the Olympus Facility, that conduct hurt the creditors of ACC and Olympus far more than it hurt the creditors of any of the Arahova entities. To recap, the September '01 Transaction resulted in Olympus paying off the \$680 million Arahova Bridge Facility (a liability that originated in the "Arahova family") and then incurring unpaid liabilities for more than \$1 billion of Rigas borrowings, which debt will have to be repaid before any unsecured creditor of Olympus (much less ACC) will see a nickel (absent success in the pending bank litigation).

*Third*, even if there were grounds for avoidance, the remedy would run in favor of CCHC, the entity that owned the assets ultimately transferred to Olympus as part of the September '01 Transaction. While conceding that Step 7 merely "was one step in th[e] overarching plan by the Rigases to strip value from the Debtors,"<sup>3</sup> Huff and the Arahova Committee seek to "atomize" the transaction and obtain a recovery *solely* on behalf of Arahova, the conduit through which the assets metaphysically and instantaneously passed on their way

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<sup>3</sup> Huff H3 Br. at ¶ 13.

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from CCHC to Olympus, rather than on behalf of CCHC (which itself is insolvent and unable to satisfy all of its own liabilities).

Thus, under the theory advanced by Huff and the Arahova Committee –

- Olympus would have to give to Arahova the legal entities and cable systems servicing 460,000 subscribers that were transferred to Olympus (*by CCHC, not Arahova*) as part of the September '01 Transaction;
- Arahova would be able to keep those assets (or their value) for itself, and would not be obligated to deliver them to CCHC, the owner of the assets at the time of the September'01 Transaction;
- the \$1 billion+ in outstanding Rigas debt run up under the Olympus Facility (which is secured by the very same assets that Huff and the Arahova Committee now claim solely for Arahova) would remain an obligation of Olympus (and, hence, a burden on Olympus' creditors and equity owners);
- Olympus would receive no compensation for paying off the \$680 million Arahova Bridge Facility (which was a liability in the "Arahova Family" before the September '01 Transaction); and
- Arahova's subsidiaries would get to keep the additional legal entities and cable systems servicing 350,000 subscribers that were transferred *to* them in the April '00 Transaction that facilitated the Century Facility (a borrowing as equally "fraudulent," to use the term loosely, as the Olympus Facility).

This is the ultimate "win-win-win-win-win" for Arahova, Huff, and the Arahova Committee. Unfortunately for them, nothing in the law, the facts, or equity even remotely compels such an unfair result. We explain further below.<sup>4</sup>

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<sup>4</sup> We respond to Huff on these points notwithstanding the fact that Huff never filed a final issue statement as required by the MIA Order and that Huff's preliminary issue statement made no reference whatsoever to Step 7, the September '01 Transaction, or any allegedly avoidable fraudulent transfer.

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**II. THE EXISTENCE OF THE RIGAS FRAUD DOES NOT JUSTIFY THE RELIEF SOUGHT BY HUFF AND THE ARAHOVA COMMITTEE**

Huff and the Arahova Committee spill pages of ink “proving” an undisputed fact – that the Rigases committed “one of the most extensive cases of corporate fraud at a public company in U.S. corporate history.”<sup>5</sup> This unquestionably is true. In the context of the present controversy regarding Step 7 and the September ’01 Transaction as a whole, however, it is important to “step back” and consider exactly what it was that the Rigases actually did. *See In re Chase & Sanborn Corp.*, 848 F.2d 1196, 1199 (11th Cir. 1988) (in fraudulent transfer cases, courts must “step back and evaluate a transaction in its entirety to make sure that their conclusions are logical and equitable”).

The best place to start is with the grand jury’s indictment, which summarizes the allegations against the Rigases as follows:

From in or about 1999 through in or about May 2002, JOHN J. RIGAS, TIMOTHY J. RIGAS, MICHAEL J. RIGAS, JAMES R. BROWN and MICHAEL C. MULCAHEY, the defendants, and their co-conspirators, participated in a scheme to defraud Adelphia’s creditors and investors, by, among other things, making false and misleading statements, including misrepresentations and omissions concerning the following material facts:

- a. Adelphia’s “off-balance-sheet” debt, in particular, Adelphia’s joint and several liabilities under the Co-Borrowing Agreements . . . . ;
- b. Adelphia’s operating performance, including, among other things, its earnings and other financial results [and] the number and growth of its “basic cable subscribers” . . . ; [and]
- c. Adelphia’s compliance with certain debt covenants under the Co-Borrowing Agreements and Adelphia’s bond indentures . . . .<sup>6</sup>

The SEC’s complaint mirrors the allegations in the criminal indictment and further explains:

Between at least 1998 and May 2002, Adelphia, at the direction of J. Rigas, T. Rigas, J.P. Rigas and Brown – and with the assistance of Mulcahey – employed a variety of fraudulent practices, including misrepresentations and omissions of material fact and improper journal

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<sup>5</sup> Ara. H3 Br. ¶ 26.

<sup>6</sup> Indictment, Case No. 02CRIM1236 (“Indictment”) [Ara. H3 Br., Ex. 18], at ¶ 63.

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entries, to portray favorably Adelphia’s financial condition and performance: (a) First, Adelphia understated its liabilities by excluding from its balance sheet portions of its outstanding debt under certain of its Credit Facilities while misrepresenting that those portions had been included. . . . [and] (b) Second, Adelphia misstated certain of its reported results – its number of basic cable subscribers, its percentage of cable plant that had been upgraded or “rebuilt,” and its quarterly earnings, including net income and EBITDA – to convey the false impression that Adelphia was expanding its customer base, modernizing its network, and increasing its profitability. . . .<sup>7</sup>

Thus, with respect to the Co-Borrowing Facilities like the Olympus Facility *and* the Century Facility, the illegal conduct was not the Rigases’ direction that Adelphia enter into the financing agreements (which, after all, theoretically provided the Adelphia enterprise with access to billions of dollars of loan proceeds), but instead was their failure to disclose the nature and extent of Adelphia’s actual liabilities under those agreements and the fact that the Rigases themselves had “borrowed” billions of dollars that Adelphia ultimately would be liable to repay. (We discuss below the other aspect of the fraud, which related to the Rigases’ publication of inflated EBITDA figures, subscriber counts, and other measures of Adelphia’s financial performance.)

Viewed in this light, there is nothing about the fact that the September ’01 Transaction was intended to facilitate the Olympus Facility that makes the September Transaction, or Step 7 in particular, a *per se* fraudulent transfer as Huff and the Arahova Committee suggest. That the Olympus Facility, like the Century Facility before it, became an instrument of the Rigas fraud simply does not tend to establish that transfers made to facilitate otherwise legitimate structural changes put in place as a condition of the extension of credit by lenders under the Co-Borrowing Facilities were actually intended to hinder, delay, and defraud creditors. Put another way, had the Rigases not had unfettered access to proceeds of the Olympus Facility, no one could suggest that the entry into the Olympus Facility (or, necessarily, the transfers that enabled the facility to be put in place) were intentionally fraudulent.

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<sup>7</sup> *Securities and Exchange Commission for Adelphia Communications Corp., et al.*, Case No. 02 CV 5776 (“SEC Complaint”) [Ara. H3 Br., Ex. 13], ¶ 23.

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While there is no authority that confronts a fraud of the mammoth proportions of the Rigas fraud, the *Summit Place* case cited in our Opening Brief is relatively analogous. There, a debtor in the throes of financial distress (Summit Place) entered into an outrageously disadvantageous short term loan agreement, in which it agreed to an 18% rate of interest, a 50% default rate, and a loan fee of \$100,000 in exchange for a 90-day loan that netted the debtor only \$110,000 in proceeds. *In re Summit Place, LLC*, 298 B.R. 62, 67 (Bankr. W.D.N.C. 2002). Summit Place's sole shareholder (Crowell) promptly converted the entire amount of loan proceeds and deposited them into his personal account. *Id.* at 67-68 ("Crowell listed the conversion of the Summit Place disbursement to himself as a 'loan' and used it pay debts on his heavy equipment and to pay himself for 'draws.'"). Summit Place thereafter filed for bankruptcy and Crowell absconded to New Mexico. *Id.* at 68.

The bankruptcy trustee sought to avoid the mortgage on Summit Place's property resulting from the short-term loan transaction as an actual fraudulent transfer, alleging that Crowell's misuse and conversion of the loan proceeds demonstrated that the entry into the loan transaction itself was fraudulent. The Court disagreed and held that the focus of the avoidance inquiry must be on the loan transaction and not on the subsequent misuse of the loan proceeds (emphasis provided by the Court):

The Trustee's claim suffers from a fundamental flaw since it largely focuses on Crowell's *conversion* of the proceeds of the transfer rather than the *transfer* itself. Section 548 allows a Trustee to seek to avoid a debtor's transfer when "*such transfer*" was made with actual intent to defraud. 11 U.S.C.A. § 548(a)(1)(A) (2001) (emphasis added). The Trustee demonstrated (at least for the purposes here) that Crowell converted approximately \$110,000 of the proceeds of the Mortgage Miracles loan to pay personal obligations on some of his heavy equipment and "draws" for himself. The Trustee also showed that Crowell later moved to New Mexico and eventually went into hiding. But, that evidence relates to Crowell's conversion of the proceeds of the transfer and not to the transfer itself.

*Id.* at 71. Similarly, here Huff and the Arahova Committee improperly want to conflate the fraudulent nondisclosure of Adelphia's true liabilities under the Olympus Facility (and the Century Facility) with the transfers leading to the actual procurement of the facility itself.

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Further, it proves nothing to state, as does the Arahova Committee, that the Rigases would have been unable to obtain the Olympus Facility had the proper disclosures been made.<sup>8</sup> There is no question that the Olympus Facility, like the Century Facility before it, was a bad deal for the Adelphia enterprise and for the creditors of the enterprise, and had creditors or their representatives been apprised of the true state of affairs, they immediately would have put an end to the Rigases' fraudulent scheme by blocking execution of the Co-Borrowing Facilities in the first place. Simply put, everyone (other than the Rigases and the banks) would have been better off had those Co-Borrowing Facilities never been executed. If given the choice, the creditors of Olympus and its equity owners surely would leap at the chance to go back in time to the *status quo ante*, thereby negating the Olympus Facility and unwinding the September '01 Transaction.

Unfortunately, that is impossible – absent success in the pending bank litigation (a success that will inure to the benefit of all creditors), the unpaid secured debts under the Olympus Facility will not simply go away. Yet, Huff and the Arahova Committee want the Court to *partially* unravel the transaction by ordering a return of the collateral for the Olympus

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<sup>8</sup> This is primarily couched in the guise of an argument that, “[a]bsent such concealment, the Arahova indenture trustee could have exercised its contractual rights (including acceleration) in the face of a prohibited transfer.” Ara. H3 Br. ¶ 49; *see id.* ¶ 9. However, as Huff concedes (at least when it suits its own purposes), it was not just the Arahova indenture trustee who was deceived. Specifically, in Huff's personal complaint against Deloitte and various bank and underwriter defendants, Huff alleges that Adelphia was in violation of covenants under *all* of the indentures for the *ACC Senior Notes* then outstanding (among other debt instruments):

Adelphia also repeatedly violated the ‘Limitation on Transactions with Affiliates’ covenant. The Rigases (who, as noted above, are Adelphia affiliates for purposes of the covenant) engaged in self-dealing of unprecedented breadth. The most obvious example of improper affiliate transactions were, of course, the co-borrowing arrangements, under which non-Adelphia entities controlled by the Rigases obtained access to Adelphia's credit for their own private purposes, while leaving Adelphia on the hook to repay the loans. These transactions conferred no benefit on Adelphia whatsoever, and no rational Board member would ever have considered entering into such an arrangement with a non-affiliate on such terms.

W.R. Huff Asset Management Co., et al., Second Amended Complaint, *In re Adelphia Communications Corp. Securities & Derivative Litigation*, Case No. 03 MD 1529 (LMM) [docket 26] (“Huff Complaint”) [*H3 Supp. Ex. A*], ¶ 265. The fact is that many, many transactions occurred in violation of the various covenants in Adelphia's numerous debt instruments. Indeed, the concealment of those covenant violations was one of the primary bases of the criminal case against the Rigases. *E.g.*, Indictment ¶ 165-166 (“From at least in or about 2001 through in or about May 2002, TIMOTHY J. RIGAS, JAMES R. BROWN and MICHAEL C. MULCAHEY . . . caused Adelphia to issue certifications of compliance with the indentures when, in numerous cases, Adelphia had not even undertaken the financial calculations necessary for determining whether Adelphia was actually in compliance. . . . In fact, in every quarter of 2001, Adelphia failed to comply with certain material financial covenants of its public indentures, including conditions relating to the maximum leverage Adelphia was permitted.”). ***Neither Huff nor the Arahova Committee even attempts to explain why the remedy for such flagrant, widespread and continuous misconduct by the Rigases should be something that benefits Arahova's creditors to the sole and exclusive detriment of creditors of the other Adelphia entities.***

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Facility to Arahova (which did not even own the collateral in the first place), while leaving the \$1 billion+ in outstanding liabilities under the Olympus Facility in place as obligations of Olympus and without restoring any of the liability associated with the Arahova Bridge Facility (which was paid off with proceeds from the Olympus Facility). That would be staggeringly unfair.<sup>9</sup>

Similarly, if Huff and the Arahova Committee are correct that the structural changes leading up the Olympus Facility are reflective of actual fraudulent intent and thus avoidable, then so too must the structural changes leading up to the Century Facility be reflective of actual fraudulent intent and thus avoidable. In a more candid moment, Huff essentially agrees:

***The larger plan or scheme here is the fraud conducted by the Rigases on an enterprise level over a sustained period of time. It is not simply just one or a series of transactions. In that regard, the Subscriber Transfer [i.e., Step 7 and the September '01 Transaction] was one step in this overarching plan by the Rigases to strip value from the Debtors and their creditors in order to spend hundreds of millions of dollars for their own personal pleasures. By defrauding creditors at one Debtor subsidiary, the Rigases were able to carry on a fraud of creditors at another Debtor subsidiary while at all times disguising their siphoning of estate assets. In effect, through devices such as the Subscriber Transfer, the Rigases manipulated the various Debtor subsidiaries like pieces on a chessboard with the sole goal of evading detection by creditors and preventing such parties from protecting their interests.***<sup>10</sup>

We could not have put it better ourselves. Indeed, we explained at length in our Opening Brief why the April '00 Transaction, the January '01 Transaction, and the September '01 Transaction

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<sup>9</sup> The fact that the Rigases defrauded innocent creditors not just of Arahova but also of many other Adelphia entities is a critical dynamic that Huff and the Arahova Committee gloss over. Because the actions of the Rigases hurt creditors at every level, this case is not analogous to *RTC Mortgage, Canon*, and the other “intentional fraud” cases cited by Huff. Far from involving situations (like this one) in which innocent defrauded creditors would be hurt by avoidance of the alleged fraudulent transfers at issue, those cases involved parties who were complicit with the debtor and knowingly participated in schemes to hinder, delay, and defraud creditors. See *RTC Mortgage Trust 1995-S/N1 v. Sopher*, 171 F. Supp. 2d 192, 200-01 (S.D.N.Y. 2001) (transferee was a shell corporation, with no creditors, owned by principal of transferor); *In re Canon*, 230 B.R. 546, 593-94 (Bankr. W.D. Tenn. 1999) (transferee knew that transferor was stealing escrowed funds), *rev'd* 2000 WL 34400479 (W.D. Tenn.), *aff'd* 277 F.3d 838 (6th Cir. 2002).

<sup>10</sup> Huff H3 Br. ¶ 13 (emphasis added). The Arahova Committee agrees that the alleged harm accruing from the September '01 Transaction and entry into the Olympus Facility was not specific to creditors of Arahova. Instead, the Arahova Committee concedes that the Olympus Facility “only added to *Adelphia's* already overleveraged financial condition and further reduced the ability of the *enterprise* to satisfy its existing public and private debt.” Ara. H3 Br. ¶ 54 (emphasis added).

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giving rise to the Century Facility, the Arahova Bridge Facility, and the Olympus Facility are all properly considered together as part of the same overarching plan by the Rigases.<sup>11</sup>

What Huff and the Arahova Committee do not address, and apparently want to forget, is the fact that the Century Facility itself was a cornerstone of the “overarching plan by the Rigases to strip value from the Debtors and their creditors.” Indeed, as we explained in our Opening Brief, the Rigases caused ACC Ops to transfer *to* the “Arahova family” entities and cable systems serving over 800,000 subscribers in order to facilitate the Century Facility and the subsequent Arahova Bridge Facility.<sup>12</sup> Under the logic and reasoning of Huff and the Arahova Committee, those transfers were no less fraudulent than the transfers from CCHC (through Arahova) to ACC Ops and then Olympus, yet Huff and the Arahova Committee obviously do not want to return any one of the assets that ACC Ops gave to the Arahova entities.

In fact, relatively speaking, the “Arahova family” came out far ahead as a consequence of the Rigases maneuvers. Considered together, the April ’01 Transaction, the January ’01 Transaction, and the September ’01 Transaction resulted in CCHC (the Arahova subsidiary) receiving entities and cable systems servicing a net total of approximately 340,000 *more* subscribers than CCHC was servicing prior to the April ’01 Transaction was implemented. (This gives the lie to the Arahova Committee’s oft-repeated complaint that the September ’01 Transaction resulted in a decrease of seventeen percent of “Arahova’s consolidated subscriber base.”<sup>13</sup> That portion of the “subscriber base,” and much more, only existed in the first place as a result of contributions by ACC Ops to the “Arahova family.”)

Huff and the Arahova Committee cannot have it both ways. If the transfers leading up to the Olympus Facility were fraudulent, then so too were the transfers leading up to the Century Facility. Arahova’s creditors cannot rightly insist on a remedy for the former without paying the price for the latter.

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<sup>11</sup> ACC H3 Br. at 10-16.

<sup>12</sup> *Id.* at 5-7.

<sup>13</sup> See Ara. H3 Br. ¶¶ 2, 7, 11, 52, 56.

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**III. IF THE SEPTEMBER '01 TRANSACTION IS AVOIDABLE, THE REMEDY IS AN UNSECURED CLAIM IN FAVOR OF CCHC AGAINST OLYMPUS**

Our Opening Brief demonstrated that the September '01 Transaction was a unified, integrated transaction that originated with CCHC, not Arahova.<sup>14</sup> Neither Huff nor the Arahova Committee seriously dispute this. In fact, they rely on some of the same authority that we cited for the proposition that multi-step transactions like the September '01 Transaction must be considered together and cannot be “atomized” for purposes of a fraudulent conveyance analysis.<sup>15</sup> Yet, both Huff and the Arahova Committee seek to do just that – they want the Court to avoid Step 7, and only Step 7, such that any remedy for the alleged fraudulent transfer would reside with Arahova and not with CCHC.<sup>16</sup> Huff goes so far as to say that the value of the assets that originated with CCHC should be returned “to the rightful parties – the [Arahova] creditors.”<sup>17</sup>

This is frankly preposterous. There is not a shred of authority for the proposition that an integrated transaction like this one can be unwound halfway, thereby enabling an intermediate conduit like Arahova to reap the benefits of avoidance without itself turning over whatever is received to the initial transferor. In fact, all of the authority is to the contrary. *See, e.g., In re Chase & Sanborn Corp.*, 813 F.2d 1177, 1180, 1182 (11th Cir. 1987) (for avoidance action to proceed, the debtor must have had “sufficient control over the funds to warrant a finding that the funds were the debtor corporation’s property”; “a two-day layover in a special account then only recently opened and soon thereafter closed” is not sufficient to meet that standard); *In re Pharmed, Inc. Securities Litigation*, 185 B.R. 497, 502 (W.D. Pa. 1995) (“By its terms, section 548 does not apply to transfers of property in which the debtor has no interest. This is consistent with the purpose of the statute, which is to prevent a debtor from diminishing, to the detriment of

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<sup>14</sup> ACC H3 Br. at 10-16.

<sup>15</sup> *See* Ara. H3 Br. ¶ 33 (quoting *Checkmate Stereo* for the proposition that, “where a transfer is only a step in a general plan, the plan must be viewed as a whole with all its composite implications.”); Huff H3 Br. ¶ 12 (same).

<sup>16</sup> *See* Ara. H3 Br. ¶ 2 (seeking the return to Arahova “of the divided subsidiaries or the fair market value thereof”); Huff H3 Br. ¶ 2 (seeking to avoid Arahova’s dividend to ACC Ops).

<sup>17</sup> Huff H3 Br. ¶ 22.

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some or all creditors, funds that are generally available for distribution to creditors.”) (quotation omitted); *In re Flooring America, Inc.*, 302 B.R. 394, 399 (Bankr. N.D. Ga. 2003) (“the debtor must actually have the ability to use the funds as it sees fit”); *see also Securities Investor Protection Corp. v. Stratton Oakmont, Inc.*, 234 B.R. 293, 313 (Bankr. S.D.N.Y. 1999) (“the person whose hands touch the money or property simply to forward it to the initial transferee is but a mere conduit or intermediary”).

Simply put, any claim for avoidance of the September ’01 Transaction, and any accompanying remedy, resides solely and exclusively with CCHC. Because CCHC itself was insolvent, Arahova and its creditors had no interest whatsoever in the assets transferred by CCHC to Olympus in the September ’01 Transaction. If an avoidable transfer occurred, the “rightful parties” entitled to a remedy are the creditors of CCHC. (We note in this regard that the Arahova Committee makes many loose references to the “Arahova family” and to “Arahova’s consolidated subscriber base,”<sup>18</sup> undoubtedly to cover up the fact that Arahova itself is a holding company with none of its own “subscribers” and no hard assets whatsoever. Such imprecise language is ironic coming from litigants who recently accused Adelpia’s management and counsel of breaching their fiduciary duties by acting in the best interests of the enterprise rather than in the interests of each distinct legal entity.)

Moreover, even if a fraudulent transfer is proven, neither Arahova nor CCHC has any right to a “return of the divided subsidiaries” as alleged by the Arahova Committee.<sup>19</sup> Rather, because Olympus and every other Adelpia entity involved in the September ’01 Transaction is now a debtor in bankruptcy, the only remedy available is the allowance of a general unsecured claim in the amount of fair value of the assets transferred by CCHC (which, as described below, is negligible at best). *See, e.g., In re PRS Insurance Group, Inc.*, 331 B.R. 580,

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<sup>18</sup> *See, e.g., Ara. H3 Br.* ¶ 1 (assets “transferred from the Arahova corporate family”); ¶ 3 (“Arahova’s consolidated subscriber base”); ¶ 7 (“reduced the subscriber base of the Arahova corporate family”); ¶ 11 (Arahova’s “cash-flow generating subscriber base”); ¶ 52 (“Arahova’s subscriber base”); ¶ 53 (“[a]dding such additional debt to the Arahova corporate family” and “stripping of subscribers from Arahova”); ¶ 56 (“Arahova’s revenue-generating subscriber base” and “a large transfer of assets from the Arahova corporate family”).

<sup>19</sup> *Id.* ¶ 2.

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588 (Bankr. D. Del. 2005) (“the amount of ‘liability’ that the insolvent preference defendant must pay under section 502(d) is not the face amount of the judgment – but only the percentage payout that its other creditors will receive in the case”); *In re Shared Technologies Cellular, Inc.*, 293 B.R. 89, 97-98 (D. Conn. 2003) (concluding that a debtor who asserts an avoidance claim against an entity that itself is a debtor in another bankruptcy proceeding holds only an unsecured claim entitled to a ratable distribution with other unsecured claims; as a consequence, the debtor asserting the avoidance claim only has the right to demand payment of that ratable amount), *aff’g* 281 B.R. 804, 808 (Bankr. D. Conn. 2002) (“At this time in the administration of the [defendant/debtor’s] estate, it is unknown what funds may be available for distribution to unsecured creditors, and, thus, what percentage of the preference judgment may be satisfied. It would be this amount, not the amount of the preference judgment, that [the defendant/debtor] would be ‘liable’ to pay to the [plaintiff/debtor’s] Estate . . .”).

**IV. ARAHOVA HOLDINGS HAD A NEGLIGIBLE, IF NOT NEGATIVE, EQUITY VALUE AT THE TIME OF THE SEPTEMBER ’01 TRANSACTION**

In our Opening Brief, we established that CCHC received substantial value in connection with the September ’01 Transaction, most prominently the satisfaction of the \$680 million then coming due under the maturing Arahova Bridge Facility.<sup>20</sup>

We also showed that, using the conservative methodologies employed by our expert, Professor Cornell, the assets transferred by CCHC – *i.e.*, its equity interest in Arahova Holdings – had a negative or negligible value, and we explained that the Arahova Committee’s expert, Mr.

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<sup>20</sup> ACC H3 Br. at 17-22. The Arahova Committee ignores this value altogether, *see* Ara. H3 Br. ¶ 16 (stating that the transfer was for “no consideration”), while Huff asserts that the payoff of the Arahova Bridge Facility was simply a coincidence that had nothing to do with the September ’01 Transaction, *see* Huff. H3 Br. ¶ 20. This just denies reality. The Arahova Bridge Facility was immediately paid off with the initial draw on the Olympus Facility on the day that the facility was consummated. *See ACC H3 Exs. C and D*. Moreover, CCHC did not have sufficient cash to repay the bridge facility. There is no reasonable conclusion to be drawn other than that one of the primary purposes of the September ’01 Transaction was to enable repayment of the maturing bridge facility. Mr. Aronson’s testimony cited by Huff in footnote 9 of its brief is not to the contrary. Mr. Aronson merely refused to speculate, given the commingling of all funds within Adelphia’s cash management system, as to whether the specific dollars of proceeds from the Olympus Facility were used to satisfy the Arahova Bridge Facility, or whether other commingled cash within the cash management system was used instead. Huff H3 Br. ¶ 20 n.9 (“because cash is fungible in one specific account I don’t think you can necessarily track it that way, but I hear your point”).

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Henkin, used admittedly erroneous, pre-restatement financial data to derive his inflated estimate of the Arahova Holdings' equity.<sup>21</sup> Our analysis demonstrated that the September '01 Transaction was not avoidable as a constructively fraudulent transfer.

In its Opening Brief, the Arahova Committee clings to Mr. Henkin's use of the pre-restatement data, while (amazingly and ironically) criticizing Professor Cornell for using the corrected, restated data. In this regard, the Arahova Committee is still fighting the battle it lost at Hearing 1, trying to denigrate the restated data as information "that management will only vouch for in terms of mathematical accuracy"<sup>22</sup> notwithstanding this Court's clear pronouncement that "both databases [the prepetition Millennium and the restatement database] must be used in order to arrive at reasonable answers about balances and accounts."<sup>23</sup>

This is brash, to say the least. We can return again the criminal indictment and SEC actions against the Rigases to show why. *A cornerstone of both the criminal and civil cases was conduct by the Rigases to inflate the very EBITDA data, subscriber counts, and other measures of financial performance now relied upon by Mr. Henkin.* For example, the Indictment alleges that:

From in or about 1999 through in or about May 2002, JOHN J. RIGAS, TIMOTHY J. RIGAS, MICHAEL J. RIGAS, JAMES R. BROWN and MICHAEL C. MULCAHEY, the defendants, along with other Adelphia employees, *engaged in a pattern and practice of misrepresenting Adelphia's performance by artificially inflating the EBITDA disclosed by Adelphia* in its Forms 10-K, Forms 10-Q, quarterly press releases, and quarterly results conference calls. The defendants and other Adelphia employees artificially inflated Adelphia's publicly-disclosed EBITDA by, among other means (1) engaging in sham transactions with affiliates to create the false appearance of revenue to Adelphia; and (2) engaging in sham transactions with other corporations to give the false appearance of revenue to Adelphia. Through these and other methods, the defendants and other Adelphia employees *artificially inflated Adelphia's publicly disclosed EBITDA by approximately \$160 million in 2000, and approximately \$210 million in 2001. . . .*

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<sup>21</sup> ACC H3 Br. at 22-24.

<sup>22</sup> Ara. H3 Br. ¶ 24.

<sup>23</sup> H1 Tr., Vol. 7, at 22; *see id.* at 15 ("We are now talking about financials that have been corrected to the best of the knowledge of an individual who has very extensive knowledge gained after extensive effort, to say the least.").

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From in or about August 15, 2000 through on or about March 23, 2002, at the direction of TIMOTHY J. RIGAS and JAMES R. BROWN, the defendants, and with the knowledge and approval of JOHN J. RIGAS and MICHAEL J. RIGAS, the defendants, Adelphia employees ***fraudulently and misleadingly inflated the number of Adelphia’s “basic cable subscribers”*** by (1) misleadingly including in its publicly reported number of “basic cable subscribers,” categories of subscribers that were no “basic cable subscribers” as publicly reported by Adelphia; and (2) by failing to disclose that when new categories of subscribers were added to the number of “basic cable subscribers” for a given quarter, the numbers for the preceding twelve months were not adjusted to include those additional categories of subscribers. As a result, Adelphia’s subscriber growth rate, which already had been fraudulently inflated, was inflated even further.<sup>24</sup>

The SEC made similar allegations:

T. Rigas and Brown directly and knowingly ***caused Adelphia to inflate fraudulently its reported earnings, including its net income and EBITDA. . . .***

T. Rigas and Brown directly and knowingly ***caused Adelphia to inflate fraudulently its reported results in connection with the numbers of its basic cable subscribers. . . .***<sup>25</sup>

Indeed, Appaloosa Investment, L.P. – the most prominent member of the Arahova Committee – has commenced its own personal lawsuit against Adelphia’s banks, underwriters, and auditors, specifically on the ground that “the data reported in Adelphia’s pre-2002 SEC filings [*i.e.*, the data relied upon by Mr. Henkin] turned out to be materially false and incomplete.”<sup>26</sup> Appaloosa alleged that, in those pre-restatement financial statements, “Adelphia misled the public about the economic fundamentals of its business. The Company overstated its earnings by hundreds of millions of dollars, created fictitious subscribers to its various services, deflated its operating expenses and misrepresented how much of its cable network had been upgraded to broadband capabilities.”<sup>27</sup> Yet, as a member of the Arahova Committee, Appaloosa

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<sup>24</sup> Indictment ¶¶ 96, 132 (emphasis added). For a complete description of this aspect of the Rigas Fraud, *see* Indictment ¶¶ 92-158.

<sup>25</sup> SEC Complaint ¶¶ 112, 93 (emphasis added). For a complete recitation of the allegations in this regard, *see* SEC Complaint ¶¶ 82-113.

<sup>26</sup> Appaloosa Investment Limited Partnership I, et al., First Amended Complaint, *In re Adelphia Communications Corp. Securities & Derivative Litigation*, Case No. 03 MD 1529 (LMM) [docket 25] (“Appaloosa Complaint”) [*H3 Supp. Ex. B*], ¶ 43.

<sup>27</sup> *Id.* ¶ 108.

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now offers an expert who relies upon the very same misleading and false data about the “economic fundamentals” as evidence of the alleged value of Arahova’s subsidiaries!

Similarly, in its own personal lawsuit against those banks, underwriters, and auditors, Huff has alleged that the pre-restatement financial information resulted in “the deceptive overstatement of Adelphia’s revenues, gross margins, and Earnings Before Interest, Taxes, Depreciation and Amortization (‘EBITDA’).”<sup>28</sup> Among other things, Huff alleged that “Adelphia’s previously-reported EBITDA was inflated by at least . . . six fraudulent accounting practices.”<sup>29</sup> Yet it too curiously now stands behind Mr. Henkin’s use of pre-restatement EBITDA figures as a benchmark for determining the value of the Arahova Holdings equity.

The Arahova Committee’s only justification for Mr. Henkin’s use of such tainted data is that, as part of the Restatement Process, Adelphia did not prepare audited, legal-entity level financial statements.<sup>30</sup> So what? The lack of audited, legal-entity financial statements does not mean that one should revert to the fraudulent pre-restatement information. As this Court has found, the restated information “must be used in order to arrive at reasonable answers about balances and accounts.”<sup>31</sup> Moreover, as our accounting expert, Mr. Mills, has demonstrated, it is entirely possible to derive a reasonable estimate of the relevant EBITDA information using the restated financial information and other data generated in the Restatement Process.<sup>32</sup> Indeed, as Mr. Mills explains, his determination (based on the restated financial information) that *the prepetition financial statements inflate EBITDA for the relevant Arahova entities by more than 100%* is in fact perfectly consistent with the fact, disputed by no one and conclusively established by the Restatement Process, that Adelphia’s prepetition consolidated reported EBITDA also was inflated by more than 100%.<sup>33</sup>

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<sup>28</sup> Huff Complaint ¶ 20.

<sup>29</sup> *Id.* ¶ 58.

<sup>30</sup> Ara. H3 Br. ¶¶ 24-25.

<sup>31</sup> H1 Tr., Vol. 7, at 22.

<sup>32</sup> Mills Rebuttal ¶¶ 63-66.

<sup>33</sup> *Id.* ¶ 65.

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In any event, Mr. Mills concludes that use of the restated information “is far more accurate than relying on an EBITDA based on financial statements filed by Adelphia prior to bankruptcy” as Mr. Henkin has done.<sup>34</sup> *Mr. Henkin in fact has now admitted that the data he relied upon “is pre-petition and therefore may be affected by Rigas fraud.”*<sup>35</sup> The Henkin opinion should be given no credence whatsoever.

Mr. Henkin’s report also is infected with other fatal errors. For example, Mr. Henkin relies on figures for intercompany liabilities that were derived in late 2003 and early 2004 *in the middle of the Restatement Process*. As Mr. Mills explains, after the data on which Mr. Henkin relies was compiled, Adelphia made nearly a half a million *additional* restatement entries in the intercompany restatement database. Mr. Mills used the entirety of the data produced in the Restatement Process; Mr. Henkin did not.<sup>36</sup>

Similarly, Mr. Henkin used a flawed comparable company/value-per-subscriber analysis based on values derived from well run cable companies, not values that actually existed for the mismanaged, fraudulent Adelphia enterprise. Other than Mr. Henkin, no one would seriously suggest that the value of a subscriber to Adelphia in September 2001 was anywhere near the value of a subscriber to, say, Charter, Comcast or Cox, but Mr. Henkin uses those companies as examples of what a subscriber “should have been worth” to Adelphia in 2001. This is unsupportable – underperforming companies like Adelphia deserve a lower valuation because they are underperforming. A valuation analysis, without adjustment, based on well run

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<sup>34</sup> Mills Rebuttal ¶ 64.

<sup>35</sup> Direct Testimony And Declaration Of Expert Witness Michael Henkin, 2/8/06, ¶ 23 (emphasis added). *We strongly object to and will be moving to strike this “Declaration.” Contrary to the Court’s clear and express ruling, the Declaration contains vast amounts of material and opinions that are not contained in Mr. Henkin’s original report. It is, in sum and substance, a thinly-veiled sur-rebuttal report. Since we have not had the opportunity to depose Mr. Henkin or arrange for other expert testimony with respect to any of Mr. Henkin’s new opinions, the allowance of such testimony will greatly prejudice the ACC Committee and should not be permitted. See, e.g., Lamarca v. U.S., 31 F. Supp. 2d 110, 122 (E.D.N.Y. 1998) (“duty to disclose information concerning expert testimony is intended to allow opposing parties to have a reasonable opportunity [to] prepare for effective cross examination and perhaps arrange for expert testimony from other witnesses”).*

<sup>36</sup> Mills Rebuttal ¶ 66.

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companies in the same industry does not provide a reasonable comparable comparison until the underperforming company is rehabilitated.

As a consequence of Mr. Henkin's errors, the Arahova Committee ultimately wants to forget the expert analysis and fall back on alleged "values placed on [the] assets by the Debtors and their advisors."<sup>37</sup> The materials cited by the Arahova Committee actually prove how it will grasp at any straw, no matter how flimsy. For example, the Arahova Committee cites to an internal Adelpia email from February 2005 that attached a chart showing the "Gross **Book Value**" for the assets at issue,<sup>38</sup> and again to an earlier internal Adelpia email from January 2005 purporting to show a "Net **Book Value**" figure.<sup>39</sup> How the Rigases booked the value of these assets is, of course, utterly irrelevant to what they actually were worth at the time of transfer in September 2001. *See, e.g., In re Roblin Industries, Inc.*, 78 F.3d 30, 36 (2d Cir. 1996) ("book values are not ordinarily an accurate reflection of the market value of an asset"); *Rubin v. Manufacturers Hanover Trust Co.*, 661 F.2d 979, 995 (2d Cir. 1981) ("The market value of particular property may of course differ substantially from its book value . . . ."); *In re Flutie New York Corp.*, 310 B.R. 31, 52 (Bankr. S.D.N.Y. 2004) ("an asset's book value may not generally be the appropriate measure of its fair value"); *In re Euro-Swiss International Corp.*, 33 B.R. 872, 885 (Bankr. S.D.N.Y. 1983) ("Assets are to be valued at market value, not book value."). Finally, the Arahova Committee also cites to an internal Adelpia email from 2003 that references the same incomplete, pre-restatement intercompany liability figures that Mr. Henkin later purports to adopt in his analysis.<sup>40</sup>

None of this is comparable to the rigorous analysis performed by Professor Cornell and by Mr. Mills, and it is not even remotely probative with respect to the value of the Arahova Holdings equity.

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<sup>37</sup> Ara. H3 ¶ 23.

<sup>38</sup> Ara. Ex. 5 (emphasis added).

<sup>39</sup> Ara. Ex. 4 (emphasis added).

<sup>40</sup> Ara. Ex. 6.

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**V. ACC OPS IS NOT LIABLE FOR RECEIVING AN ALLEGEDLY ILLEGAL DIVIDEND FROM ARAHOVA**

Finally, Huff argues that, independent of any remedy for the alleged constructive fraudulent transfer, there is some sort of stand-alone independent cause of action available for the allegedly illegal dividend by Arahova as part of the September 01 Transaction.<sup>41</sup> In fact, however, the provisions of the Delaware General Corporation Law cited by Huff provide that the remedy for an illegal dividend is an action against the directors who declared the dividend, not against the shareholder who received the dividend. *E.g., PHP Liquidating, LLC v. Robbins*, 291 B.R. 592, 597 (D. Del. 2003) (“there is no statute imposing liability on stockholders who receive unlawful dividends”) (quoting 1 R. Franklin Balotti & Jesse A. Finkelstein, *The Delaware Law of Corporations and Business Organizations* § 5.32 (3d ed. 2002)), *aff’d* 128 Fed. Appx. 839 (3d Cir. 2005) [*PHP*]; *In re Color Tile, Inc.*, 2000 WL 152129, \*2-\*3 (D. Del. Feb. 9, 2000) (“The DFTA [Delaware’s fraudulent transfer act] thus focuses on ensuring that creditors recover fraudulent transfers to third parties. . . . [T]he DGCL [Delaware’s corporations law], on the other hand, imposes liability on corporate directors for approving unlawful dividend payments. Because *it makes directors (rather than recipients of the dividends) primarily liable*, [the corporations law] is designed to discourage directors from depleting a corporation’s ability to repay its debts. [The corporations law] thus focuses on deterrence rather than on returning fraudulent payments to creditors.”) (emphasis added) [*H3 Supp. Ex. C*].

Some courts have suggested (but never actually held) that, because the Delaware law provides a director found liable for declaring an illegal dividend with a right of subrogation against the shareholder who received the dividend, there is an implied right to recover an illegal dividend directly from the shareholder. At most, however, those courts have observed that such an implied right, if it exists at all, only arises when the shareholder acted in bad faith and knew that the dividend was illegal. *See PHP*, 128 Fed. Appx. at 846 (“*if* Section 174 creates or recognizes a right of debtors-in-possession to sue stockholders who receive payments for

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<sup>41</sup> Huff H3 Br. ¶¶ 5-6.

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unlawful stock redemptions, it does so only against those stockholders with knowledge of facts indicating that such redemption was unlawful”) (emphasis added). In this case, Huff has not made any such allegation independent from its claim (addressed above) that the September ’01 Transaction was an intentionally fraudulent conveyance.

Thus, with respect to the claim for an illegal dividend, if Huff wants to sue the Rigases (who were the only directors of Arahova at the time of the September ’01 Transaction) for violating the Delaware General Corporation Law, it should go ahead and do so. There is nothing in that Code, however, that gives Huff any right to extract a pound of flesh from other innocent creditors who were equally victimized by the Rigases.

**VI. CONCLUSION**

The Supreme Court long ago held that, when many creditors are victimized by the same fraudulent scheme, “equality is equity, and this is the spirit of the bankrupt law.” *Cunningham v. Brown*, 265 U.S. 1, 13 (1924) (holding creditors/investors in the original Ponzi scheme must be treated ratably); *see, e.g., In re M & L Business Machine Co.*, 164 B.R. 148, 151 (D. Colo. 1994) (“all of the victims of the fraudulent scheme should be treated equally [because] equality is equity and thus the spirit of the bankruptcy law”) (paraphrasing *Cunningham*); *In re Taubman*, 160 B.R. 964, 981 (Bankr. S.D. Ohio 1993) (same). Here, Huff and the Arahova Committee seek to turn that venerable principle on its head by using the fact of the Rigas fraud to wrest an unequal recovery for themselves. Neither facts, nor law, nor equity authorize such an unfair and unprincipled outcome.

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For all of the reasons set forth above and in our Opening Brief, Huff and the Arahova Committee have not satisfied and cannot satisfy their burden of proving that the September '01 Transaction, properly considered as an integrated transaction, is avoidable as an actual or constructive fraudulent conveyance. Accordingly, all of the relief requested by Huff and the Arahova Committee in connection with Hearing 3 should be denied.

DATED: New York, New York  
February 10, 2006

HENNIGAN, BENNETT & DORMAN LLP

By: /s/ Bruce Bennett  
Bruce Bennett

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**EXHIBITS**

**(attached to accompanying supplement appendix)**

*Documents*

<b><i>Tab</i></b>	<b><i>Description</i></b>
A	W.R. Huff Asset Management Co., et al., Second Amended Complaint, <i>In re Adelpia Communications Corp. Securities &amp; Derivative Litigation</i> , Case No. 03 MD 1529 (LMM) [docket 26]
B	Appaloosa Investment Limited Partnership I, et al., First Amended Complaint, <i>In re Adelpia Communications Corp. Securities &amp; Derivative Litigation</i> , Case No. 03 MD 1529 (LMM) [docket 25]
C	<i>In re Color Tile, Inc.</i> , 2000 WL 152129 (D. Del. Feb. 9, 2000)

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*Attorneys for Ad Hoc Committee of ACC Senior Noteholders*

**UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF NEW YORK**

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<i>In re</i>	:	Chapter 11
	:	
	:	Case No. 02-41729 (REG)
ADELPHIA COMMUNICATIONS CORPORATION, <i>et al.</i>	:	(Jointly Administered)
	:	
<i>Debtors.</i>	:	
	:	

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**SUPPLEMENTAL APPENDIX TO  
REPLY BRIEF OF THE AD HOC COMMITTEE  
OF ACC SENIOR NOTEHOLDERS FOR HEARING 3 CONDUCTED  
PURSUANT TO THE ORDER IN AID OF CONFIRMATION**

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*Documents*

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DATED: New York, New York  
February 10, 2006

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