IN THE COURT OF COMMON PLEAS OF PHILADELPHIA COUNTY
FIRST JUDICIAL DISTRICT OF PENNSYLVANIA
TRIAL DIVISION- CIVIL

ISLAND PARTNERS, et al.,	:	MARCH TERM, 2004
Plaintiffs,	:	NO. 06280
v.	:	COMMERCE PROGRAM
DELOITTE & TOUCHE, LLP,	:	Control No. 18033530
Defendant.	:	

ORDER

AND NOW, this 6th day of September, 2018, upon consideration of defendant's Motion for Summary Judgment, the responses thereto, and all other matters of record, and in accord with the Opinion issued simultaneously, it is **ORDERED** that said Motion is **GRANTED** and **JUDGMENT** is **ENTERED** against the sole remaining plaintiff, Zito Media, L.P., and in favor of defendant on all of plaintiff's claims.

BY THE COURT

GLAZER, J.

Island Partners Inc Eta-ORDOP

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DELOITTE & TOUCHE, LLP,	:	Control No. 18033530
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OPINION

In this action, plaintiff Zito Media, L.P. ("Zito") asserts claims against defendant Deloitte & Touche LLP ("Deloitte") for breach of contract, professional negligence, and negligent misrepresentation in connection with certain audit services that Deloitte provided to Zito's predecessor-in-interest, Coudersport Television Cable Company Inc. ("Coudersport") as part of Deloitte's provision of services to many entities affiliated with Adelphia Communications Corporation ("Adelphia").[1]

Deloitte has moved for Summary Judgment on all of Zito's claims. Upon careful consideration of the facts admitted, and the expert opinions asserted, by Zito, as well as the relevant decisions and findings of the federal courts in this and related actions, this court finds that Zito is barred from further prosecuting its malpractice claims against Deloitte because Zito f/k/a Coudersport was *in pari delicto* with Deloitte, or, more accurately, Zito bears greater fault than Deloitte for the improper activities that gave rise to this action.[2]

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[1] This case was commenced in March, 2004, by numerous plaintiffs, including many entities affiliated with Adelphia and several members of the Rigas family, who controlled Adelphia, Coudersport, and the other companies. This case was removed to federal court in 2006, and was not remanded until 2015. While it was in federal court, it shed all but the remaining plaintiff, Zito Media, L.P.

[2] "[N]o court will lend its aid to an action grounded upon immoral or illegal conduct [because] the law will not suffer itself to be prostituted." Feld & Sons, Inc. v. Pechner, Dorfman, Wolfee, Rounick, & Cabot, 312 Pa.

Deloitte began providing services to Adelphia and its affiliates in the 1980s, but the audit services that form the basis for this lawsuit were provided between 1996 and 2002. In 1996, as part of its growth plan as a cable TV operator, Adelphia and several related entities, including Coudersport,[3] entered into the first of several Co-Borrowing debt agreements, which are described by one of Zito's expert witnesses, Mr. Brulenski, as follows:

> An element of Adelphia's approach to continually source financing involved the use of Co-Borrowing debt agreements with various bank syndicates whereby certain Adelphia subsidiaries and RFE's[4] would be grouped as the borrowers. The first Co-Borrowing group credit facility was established February 28, 1996, as amended March 29, 1996, for the amount of $200,000,000. Thereafter three different additional Co-Borrowing groups were set and related Co-Borrowing agreements established May 6, 1999, April 14, 2000, and September 28, 2001 for the respective amounts of $850,000,000; $2,250,000,000; and $2,030,000,000. The banks' Co-Borrowing agreements required the submission of audited combined financial statements for each of the respective Co-Borrowing groups. As a result, Deloitte's scope of audit services expanded as the firm was engaged to perform audits of each of the separate Co-Borrowing groups' combined[5] financial statements.[6]

Super. 125, 138, 458 A.2d 545, 552 (1983) ("Were we to aid appellants—confessed perjurers—in their attempt to recover compensatory and punitive damages in excess of $250,000 [from their attorneys], we should indeed 'suffer the law to be prostituted.' For we should reward appellants, with a great deal of money, for their criminal conduct; we should soften the blow of the fines and sentences imposed upon them; and we should encourage others to believe that if they committed crimes on their lawyers' advice, and were caught, they too might sue their lawyers and be similarly rewarded.")

[3] *See* Zito's Opposition to Deloitte's Motion in Limine to Exclude the Testimony of Jeffrey Brandon, ¶ 60 ("Coudersport was involved in the 1996 co-borrowing agreement as a subsidiary of Highland Video Associates, L.P., another Rigas family privately-owned cable company.")

[4] "RFE" stands for "Rigas Family Entities," *i.e.*, companies owned by members of the Rigas family.

[5] According to the expert's footnote: "The term 'combined' refers to the fact that for special reporting purposes the individual financial statements of the entities in a particular Co-Borrowing group had to have their individual entity financial statements combined or aggregated into one single Co-Borrowing group financial statement for bank reporting purposes." Expert Report of Francis C. Brulenski, CPA, dated May 27, 2014 ("Brulenski Report"), p. 4, ftnt. 13.

[6] *Id.*, p. 4 (footnotes citing the record omitted).

According to Zito's liability expert, Mr. Brulenski, the significant Co-Borrowing debt incurred by Adelphia-related entities should have been treated differently than was done in the audits Deloitte performed for the Adelphia entities for fiscal years 1996-2001:

> In order to finance business activity, a basic concept is that of a single company borrowing funds via a term loan or a line of credit facility with a single bank. In a direct and straightforward process, the single company records receipt of the borrowed funds and thereafter makes payments on the outstanding balance pursuant to terms of the loan agreement. The balance of the bank debt outstanding is then reported as a financial statement element in the company's balance sheet at any point in time for a specific report date (i.e. –December 31st) with typical reference such as note payable or long-term debt.
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> The Co-Borrowing bank debt reported as an element of the Adelphia and Co-Borrowing group financial statements was not of a nature having the direct one-to-one single company to single bank relationship. In each instance, it involved several Adelphia subsidiaries and RFE's put together as a Co-Borrowing group and several banks put together as a syndicate to provide the loan or credit facility. The arrangement was different and more complex than the basic one-to-one scenario. Deloitte audit engagement staff however, viewed the Co-Borrowed debt no differently than other bank debt of Adelphia and the Co-Borrower groups. Deloitte failed to consider or chose to ignore that the Co-Borrowing debt was different in substance that [sic] the other bank debt.[7]
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> Based upon [the expert's] review of Deloitte work paper documents available in this matter, it is evident that the framework for the Adelphia audit work remained generally consistent over seven financial statement audit reporting dates from 1996 through 2001 particularly with respect to Co- Borrowing bank debt.[8]
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> * * *
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> Despite the new . . . Co-Borrowing agreement entered into March 29, 1996, there is no mention of its occurrence in the [Audit Planning Memo] or the [Audit Summary Memorandum]. There is also no mention of any risk regarding off balance sheet debt. The initial 1996 audit is what served as the basis for Deloitte's performance on each subsequent audit up to March 27, 2002. . . . Deloitte's Co-Borrowed debt accounting determination was that the joint and several liability provision was a contingent liability akin to a guarantee of the indebtedness of other Co-Borrowers. Therefore the contingency was not to be recorded on Adelphia's books, but only disclosed in the financial statements.[9]

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[7] Brulenski Report, pp. 8-9.

[8] *Id.*, p. 10.

[9] *Id.*, p. 11.

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> Deloitte's understanding included a view that the Co-Borrowing arrangements allowed "the Co-Borrowers to determine" who was the particular borrower with respect to the allocation of debt reflected on the respective Co-Borrower's financial statements. This view is striking considering the nature of the Co-Borrowing debt structure and related accounting process maintained and/or controlled by Adelphia. For example, Deloitte admits knowledge no later than 2000 that "co-borrowed debt originally recorded on one co-borrower's books was moved – or 'reclassified' – to another co-borrower's books." Deloitte also admits knowledge no later than 2000 that Co-Borrowed funds were used to acquire Adelphia stock. . . . [S]uch factors should have been red-flags to the Deloitte engagement team.[10]

Fiscal Year 2001 was the second time that Zito's predecessor, Coudersport, was a Co-Borrower,[11] and the amount of the 2001 Co-Borrowing credit facility was over $2 billion.[12] When Deloitte undertook the FY2001 audit in early 2002, it apparently proceeded in the same manner as it had in prior years[13] until late March, 2002, when the SEC began to ask questions about Deloitte's "audit performance regarding Co-Borrowing debt."[14]

> Adelphia issued an earnings press release on March 27, 2002 reporting its "Full Year 2001 Results," which was reviewed by Deloitte beforehand. Adelphia was left with the understanding that the audit was substantially complete but for some miscellaneous closing items. Adelphia also held a conference call with investors

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[10] Brulenski Report, p. 12.

[11] "Coudersport was [also] involved in the 1996 co-borrowing agreement as a subsidiary of Highland Video Associates, L.P., another Rigas family privately-owned cable company." Zito's Answer to Deloitte's Motion in Limine to Exclude the Testimony of Jeffrey Brandon, ¶ 60.

[12] *See* Brulenski Report, p. 9; Deloitte's Motion for Summary Judgment filed March 26, 2018, ¶¶ 23-24, admitted in Zito's Answer to Motion for Summary Judgment filed June 7, 2018, ¶¶ 23-24.

[13] *See* Brulenski Report, p. 13. ("In the subsequent 2001 period, the fourth OCH Facility agreement was executed for an additional $2,030,000,000 Co-Borrowing credit facility. A 2001 Deloitte audit planning 'Year End Audit Procedures' memo states 'Same procedures as last year will be performed' regarding debt. The work papers are consistent with this statement as they indicate use of the same old approach implemented in the prior periods.")

[14] Brulenski Rebuttal Report dated August 11, 2014 ("Brulenski Rebuttal"), p. 9. *See also* Island Partners v. Deloitte and Touche, LLP, 2017 WL 4862765, at * 3 (Pa. Super. Oct. 27, 2017) ("In early 2002, following the Enron debacle, the SEC announced new guidance regarding disclosures of off-balance sheet debt. . . . Within days [after Adelphia issued its earnings report] the SEC began investigating Adelphia's accounting treatment and disclosure of the co-borrowing agreements.")

> and analysts the same day. We understand the press release included for the first time an explicit disclosure of the amount of Co-Borrowing debt outstanding not recorded on Adelphia's balance sheet. There appears to be no dispute in this matter that after the press release, the stock market reacted negatively to the Co-Borrowing debt information and Adelphia's stock value dropped.[15]

At that point, Deloitte apparently refused to issue an audit similar to the ones it had issued in past years, so "Adelphia and the Co-Borrowing groups were left unable to file their financial reports by the respective April 1, 2002, and April 30, 2002 deadlines."[16] Adelphia and its affiliates sought bankruptcy protection and several members of the Rigas family were convicted of fraud in connection with their management of Adelphia and related companies, including the incurrence and treatment of the Co-Borrowing debt.[17]

According to Zito's liability expert, "Deloitte had failed in its auditing of Co-Borrowing debt up to the March 27, 2002 Earnings Release with respect to its 2001 and prior fiscal year audits" of the Adelphia entities.[18] In the Spring of 2002, Deloitte apparently realized its mistake and refused to sign off on a 2001 audit that contained the same mistakes in it.

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[15] Brulenski Report, p. 15. *See* United States v. Rigas, 490 F.3d 208, 212 (2d Cir. 2007) (Adelphia "announced its 2001 Fourth Quarter and Full–Year results in a March 27, 2002 press release. In a footnote on the final page of that press release, Adelphia, at the recommendation of its accounting firm, Deloitte & Touche, first disclosed publicly that it had approximately $2.2 billion in liabilities not previously reported on its balance sheet. On the day of disclosure, Adelphia's stock price plummeted by about twenty-five percent to $20.39; by the time the stock was delisted in May 2002, the price per share was $1.16. The company filed for bankruptcy in June 2002, wiping out all shareholder value. A month later, John Rigas, his sons Michael and Timothy, and two other Adelphia employees were arrested and charged with looting the company.")

[16] Brulenski Report, p. 16.

[17] *See* United States v. Rigas, 490 F.3d 208 (2d Cir. 2007).

[18] Brulenski Rebuttal, p. 9.

Without another incorrect audit, Adelphia's "business model [that] focused on growth which was capital intensive and required continued sourcing and use of financing,"[19] *i.e.*, the Co-Borrowing agreements, fell apart. In other words, Zito claims that the problems encountered by Coudersport and the other Adelphia entities in the Spring of 2002 were not so much caused by Deloitte's alleged malpractice in 1996-2001, but were instead caused by Deloitte's refusal to keep committing that same malpractice by issuing yet another improper audit in 2002.

Specifically, Zito's damages expert, Mr. Brandon opines:

> That Deloitte's conduct in failing to provide timely audited financial statements for Adelphia and the Managed Entities [including Coudersport in April, 2002,] was a significant factor in destroying the value of Adelphia and the Managed Entities [including Coudersport] based upon their inability to finance their operations due to a lack of ability to borrow [in 2002.] The primary source of liquidity for both Adelphia and the Managed Entities during the March through June, 2002 time period was the Co-Borrowing agreements. Because of Deloitte's conduct, as of May 1, 2002, Adelphia and the Managed Entities were unable to provide the co-borrowing lenders with timely audited financial statements, which was a condition precedent to any further borrowings.[20]

To a significant extent, Zito's experts talk past each, *i.e.*, their opinions are inconsistent with one another. The liability expert, Mr. Brulenski, says that Deloitte's wrongdoing was in treating the Co-Borrowing debt too favorably in the FY 1996-2000 audits, but the damages expert, Mr. Brandon, spends significant time in his reports analyzing the decline in equity value of the Adelphia related entities beginning in 2001 (the "2001 Damages").[21] In other words, the two experts together claim that, by failing to

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[19] Brulenski Rebuttal, p. 4.

[20] Brandon Rebuttal Report dated August 11, 2014 ("Brandon Rebuttal"), pp. 3-4.

[21] "Scenario 2: Had Deloitte not refused to issue the audit opinion letters for the 2001 financials of Adelphia and the co-borrowing facilities, the assets owned by the Rigases and Adelphia as of 12/31/2001 are modeled through 2023." Brandon Expert Report dated May 27, 2014 ("Brandon Report"), p. 15.

add another faulty audit card to the financial house of cards that was Adelphia, Deloitte caused the entire house to fall down. Neither gravity nor the law of causation of damages works in that manner.

In order for Zito to prevail on any of its claims against Deloitte, Zito must prove that Deloitte's alleged breach of duty caused Coudersport's alleged damages.[22] In recognition that the 2001 Damages may not be the proper measure of damages, Zito's damages expert also calculates

> Scenario 1: Had the Rigas Family not received negligent advice from Deloitte relating to the accounting for and disclosure of co-borrowed debt, the Rigas Family would not have entered into the 1999, 2000 and 2001 co-borrowing agreements. Under this scenario, the assets held at the end of 1998, consisting of the Rigas assets (which were referred to as ME for Managed Entities) and the Adelphia owned assets both effectively as of 12/31/1998, were modeled through 2023.[23] (the "1999 Damages")

The damages expert then finds that Zito/Coudersport's loss of equity value was between $49 and 54 million.[24] In light of Zito's liability evidence, these 1999 Damages are the only damages that

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[22] *See, e.g.*, Hart v. Arnold, 884 A.2d 316, 332 (Pa. Super. 2005) ("To successfully maintain a cause of action for breach of contract the plaintiff must establish: (1) the existence of a contract, including its essential terms, (2) a breach of a duty imposed by the contract, and (3) resultant damages."); Nelson v. Heslin, 806 A.2d 873, 876 (Pa. Super. 2002) ("the elements a plaintiff must demonstrate in order to establish a claim of [professional] malpractice: 1) employment of the [professional] or other basis for a duty; 2) the failure of the [professional] to exercise ordinary skill and knowledge; and 3) that such negligence was the proximate cause of damage to the plaintiff."); Kramer v. Dunn, 749 A.2d 984, 991 (Pa. Super. 2000) ("Negligent misrepresentation requires proof of: (1) a misrepresentation of a material fact; (2) made under circumstances in which the misrepresenter ought to have known its falsity; (3) with an intent to induce another to act on it; and; (4) which results in injury to a party acting in justifiable reliance on the misrepresentation.")

[23] Brandon Report, p. 15. The Superior Court previously held in this matter that Brandon's "methodology was reasonable, and that Zito Media should have the opportunity to present his valuation to the jury." Island Partners v. Deloitte and Touche, LLP, 2017 WL 4862765, at * 9 (Pa. Super. Oct. 27, 2017).

[24] Brandon Report, pp. 30, 42. Interestingly, Zito's alleged 2001 Damages are less, ranging from $37 to $41 million loss of equity value, but the losses for the other former plaintiffs are significantly greater in 2001 than in 1999. *See id*, p. 42. Coudersport apparently still held some value in 2005, when Zito acquired it, but how much, and how much more it could have been but for Deloitte's alleged malpractice, are questions of fact for the jury.

are arguably recoverable for Deloitte's alleged wrongdoing in connection with the 1996-2001 audits.[25]

Following Deloitte's refusal to sign another set of incorrect audit opinion letters, the Adelphia entities, including Coudersport, filed for bankruptcy in 2002. Subsequently, the principals of the Adelphia entities, including Coudersport, were charged with, and convicted of, numerous frauds in connection with their financial management of the Adelphia entities, including Coudersport.

Specifically, John Rigas, who founded Adelphia and who was the sole-owner of Coudersport in the late 1990s and early 2000s,[26] was convicted of securities and bank fraud in May 2005.[27] After John Rigas' conviction and in connection with the forfeiture of most of the other Adelphia entities and their assets, "control and ownership of Coudersport was transferred to Zito Media, an entity controlled by Michael Rigas and James Rigas,"[28] who are John Rigas' sons.[29]

The ownership interest in Coudersport that was transferred to Zito was the same interest that had been held by John Rigas. In other words, Zito took over from John Rigas, stepped into Coudersport's shoes, and thereby acquired the rights and liabilities of Coudersport, including its

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[25] In response to Deloitte's Motions in Limine, Zito concedes that the 1999 Damages are the only potentially viable measure of damages proffered by Brandon. *See* Zito's Memorandum of Law in Opposition to Deloitte's Motion in Limine to Exclude the Testimony of Jeffrey Brandon, pp. 8-10.

[26] Deloitte's Motion for Summary Judgment filed March 26, 2018, ¶ 3, admitted in Zito's Answer to Motion for Summary Judgment filed June 7, 2018, ¶ 3.

[27] *See* US v. Rigas, 490 F.3d 208 (2d Cir. 2007).

[28] Deloitte's Motion for Summary Judgment filed March 26, 2018, ¶ 4, admitted in Zito's Answer to Motion for Summary Judgment filed June 7, 2018, ¶ 4.

[29] *See* US v. Rigas, 490 F.3d at 212 (John's sons, Timothy, Michael, and James, as well as his son-in-law, Peter Venetis, were all officers and/or directors of Adelphia and related entities.)

claims for malpractice against Deloitte and all defenses thereto.[30] One of Deloitte's defenses is that Coudersport is *in pari delicto* with Deloitte because, at the time of Deloitte's alleged wrongdoing, Coudersport, acting by and through John Rigas, was a criminally active participant in such wrongdoing, and, therefore, Coudersport's successor, Zito, cannot recover damages from Deloitte for that wrongdoing.

Pennsylvania recognizes the defense of "*in pari delicto potior est conditio defendentis* (meaning in a case of equal or mutual fault the position of the defending party is the stronger one)."[31] In doing so,

> Pennsylvania requires the plaintiff be an active, voluntary participant in the wrongful conduct or transaction(s) for which it seeks redress, and bear substantially equal or greater responsibility for the underlying illegality as compared to the defendant. In this Commonwealth, as elsewhere, *in pari delicto* serves the public interest by relieving courts from lending their offices to mediating disputes among wrongdoers, as well as by deterring illegal conduct.[32]

When an individual commits criminal fraud and uses a corporate entity of which he is the sole owner to perpetrate that fraud, then that corporation cannot sue another person or entity for negligently participating in that fraud.[33] Nor can the criminal owner insulate the corporation

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[30] *See* O'Melveny & Myers v. F.D.I.C., 512 U.S. 79, 86, 114 S. Ct. 2048, 2054 (1994) ("[T]he FDIC as receiver 'steps into the shoes' of the failed S & L, obtaining the rights 'of the insured depository institution' that existed prior to receivership. Thereafter, in litigation by the FDIC asserting the claims of the S & L - in this case California tort claims potentially defeasible by a showing that the S & L's officers had knowledge - any defense good against the original party is good against the receiver" including *in pari delicto*.) (internal citations and ellipses omitted); Official Comm. of Unsecured Creditors of Allegheny Health Educ. & Research Found. v. PriceWaterhouseCoopers, LLP ("AHERF v. PwC"), 605 Pa. 269, 989 A.2d 313 (2010) (court allowed accounting firm to assert *in pari delicto* defense against committee of unsecured creditors standing in shoes of debtor in liquidation.)

[31] AHERF v. PwC, 605 Pa. at 274, 989 A.2d at 316.

[32] *Id.*, 605 Pa. at 295–96, 989 A.2d at 329.

[33] *See id.*, 605 Pa. at 298–99, 989 A.2d at 331 ("Were the action between a corporation controlled by a single individual and a sole-proprietor auditor, there would be a good case to be made that *in pari delicto* should apply to negate all causes of action arising out of intentional auditor misrepresentations made at the behest of the owner, and thus, with full corporate complicity. At the very least, in the absence of some countervailing social policy at stake, the business can be deemed to have exposed itself to a just, judicial determination whether or not to simply leave the equally culpable parties in the condition in which they are found.") In the present case, Zito does

from application of *in pari delicto* by simply transferring his interests to another entity owned by his children.[34]

In this case, John Rigas was convicted of committing multiple frauds with and through the Adelphia entities, including Coudersport of which he was the sole owner. As explained by the Second Circuit Court of Appeals, which heard the appeal from his conviction, the (mis)treatment of the Co-Borrowing debts in the Adelphia financial statements was an important element of the securities fraud of which John Rigas was convicted:

> In 1986, John Rigas took Adelphia public. Adelphia issued two classes of common stock: Class A, with one vote per share, and Class B, with 10 votes per share. The Rigas family owned almost all of the Class B shares, and, as a result, was able to maintain control of the company and the Board of Directors. Indeed, Rigas family members filled many of the top positions in Adelphia.[35]
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> Not all of the companies controlled by the Rigas family went public when Adelphia did. Rather, Adelphia managed some of the cable companies - the Rigas Managed Entities ("RMEs") - that the family continued to own privately. Adelphia's management of the RMEs was disclosed in public filings; however, Adelphia did not disclose the amount of the fees charged to, or paid by, the RMEs, or that cash generated from the RMEs was commingled with that generated by Adelphia. Certain transactions between Adelphia and the RMEs were at issue during the trial; the government argued that Defendants utilized the Adelphia - RMEs business arrangement to effect and conceal aspects of their frauds.
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> Adelphia's disclosed bank borrowings were $5.4 billion in September 2001, more than a six-fold increase from March 1998. Generally, each separate bank loan was entered into by a group of Adelphia subsidiaries that pledged their assets as collateral; the group was referred to as a "borrowing group." Certain bank loans

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not allege intentional malfeasance against Deloitte, thereby admitting that Deloitte is less culpable than Coudersport, whose principal was found guilty of criminal conduct.

[34] There is no claim here that Zito, nor its owners James and Michael Rigas, acquired Coudersport as innocent purchasers for value, *i.e.*, without knowledge of Coudersport's and their father's fraudulent past, nor is it claimed that they were third party creditors of Coudersport who gave something of value to Coudersport prior to, or during, the course of the fraudulent scheme without knowledge of the fraud. *Cf.* AHERF v. PwC, 605 Pa. 269, 989 A.2d 313 (plaintiffs were creditors of non-profit entity whose officers allegedly conspired with the defendant accounting firm to commit fraud of which the independent board of trustees was unaware.)

[35] US v. Rigas, 490 F.3d at 212.

were set up through a "co-borrowing" arrangement (the "Co–Borrowing Arrangement") between the RMEs and Adelphia subsidiaries. . . . Under this Co–Borrowing Arrangement and at the Rigases' direction, Adelphia entered into three separate "Co–Borrowing Agreements" - loans for which the RMEs and Adelphia subsidiaries were jointly and severally liable. These Co–Borrowing Agreements totaled about $5.5 billion. Adelphia's accounting firm, Deloitte & Touche, reviewed and approved the manner in which Adelphia disclosed and accounted for the co-borrowed debt on its public financial statements.

The Rigas family wished not only to expand Adelphia, but also to maintain control over the company, in part because Adelphia's loan agreements provided that the Rigases' loss of voting control would constitute default. To maintain family control, every sale of stock to the public required a concurrent sale of stock to the Rigases. . . . During the relevant time, family members purchased $1.6 billion in new shares.[36]

The Rigases did not have enough cash to provide the promised "fresh money" for the shares they purchased to maintain control over Adelphia. The steps they took to purchase these shares constitute several of the charged frauds. The purchase agreements for the stocks required that at the closing date, the Rigases "shall deliver to the Company the purchase price for the Shares in immediately available funds"; Adelphia's public filings and press releases suggested to investors and analysts that the Rigases had paid cash for the stocks. However, this was not the case. Instead, for the earlier purchases, Defendants borrowed funds to pay Adelphia, but then caused Adelphia to use that cash to pay off other family debts. For the later purchases, Defendants caused Adelphia to "move" debt it owed under the Co–Borrowing Agreements from its books to the books of one of the RMEs. The process of moving debt from Adelphia's financial statement to one of the RMEs' financial statements was called "reclassification," and the debt, itself, was referred to as having been "reclassified."[37]

* * *

After the first reclassification of over $200 million, additional debt was reclassified on a quarterly basis. In total, the Rigases reclassified over $2.8 billion dollars' worth of debt, including the stock purchase reclassifications, from the first quarter of 2000 until the end of the conspiracy.

These reclassifications were memorialized only in general ledger journal entries; neither Adelphia nor the RMEs executed formal assumption agreements. As the reclassified funds had been borrowed under the Co–Borrowing Agreements, Adelphia would still be liable for the full amount due if the RMEs were unable to pay the debt. The government argued, and the jury apparently agreed, that these

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[36] US v. Rigas, 490 F.3d at 212–14.

[37] *Id.* at 214.

> ledger entries were fraudulent and intended to mislead stockholders and analysts about the debt the Rigas family and the RFEs[38] owed to Adelphia.[39]

The fraudulent activities for which John Rigas and his son Timothy were found guilty are the same events that form the basis for Zito's allegations of negligence against Deloitte in this action. In fact, John Rigas' own, malpractice claims against Deloitte were barred by the District Court under the doctrine of *in pari delicto* because of his convictions:

> John Rigas has already been held criminally responsible for each of these alleged misdeeds. For example, the Second Circuit specifically discussed the improper documentation of related party transactions when outlining the conduct of which John Rigas was convicted. . . . As in Feld, were this Court to permit John Rigas to recover against Deloitte, the Court would "reward [him] with a great deal of money, for [his] criminal conduct; [would] soften the blow of the fines and sentences imposed upon [him]; and [would] encourage others to believe that if they committed crimes on their [accountants'] advice, and were caught, they too might sue their [accountants] and be similarly rewarded."[40]

John Rigas was convicted of fraud involving the improper "reclassification" of the Co-Borrowing debt. Zito claims that Deloitte was negligent in failing to flag these improper "reclassifications":

> Deloitte admits knowledge no later than 2000 that "co-borrowed debt originally recorded on one co-borrower's books was moved – or 'reclassified' – to another co-borrower's books." Deloitte also admits knowledge no later than 2000 that Co-Borrowed funds were used to acquire Adelphia stock. . . . [S]uch factors should have been red-flags to the Deloitte engagement team.[41]

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[38] "RFE" means "Rigas Family Enterprises," which includes the RMEs, as well as the Rigas-owned Non-Cable Entities ("RNCEs"). US v. Rigas, 490 F.3d at ftnt. 3.

[39] *Id.* at 215.

[40] Island Partners v. Deloitte & Touche LLP, 2013 WL 6838899, at *8 (S.D.N.Y. Dec. 27, 2013) citing Feld & Sons, Inc. v. Pechner, Dorfman, Wolfee, Rounick, & Cabot, 312 Pa. Super. 125, 138, 458 A.2d 545, 552 (1983).

[41] Brulenski Report, p. 12.

The "Co-Borrowing Agreements . . . formed the basis of [John Rigas'] securities fraud conviction,"[42] and Coudersport was one of the entities that he employed as a Co-Borrower with respect to those fraudulent transactions.[43] According to Zito's experts, the Co-Borrowing debt benefitted all the Adelphia entities, including Coudersport, in that it enabled them to grow and thrive, at least until the fraud was discovered and their value plummeted.[44]

Coudersport was solely owned by John Rigas, and Coudersport was one of the corporate entities utilized by John Rigas in his intentional, criminal, activity. John Rigas' wrongdoing is therefore imputed to Coudersport and to its successor-in-interest, Zito, under the doctrine of *in pari delicto*.[45] As a result, this court will not now "lend its offices to mediate" Zito's claim that Deloitte's alleged negligence makes Deloitte financially responsible for the damage to Coudersport caused by its owner's criminal conduct.

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[42] US v. Rigas, 490 F.3d at 219. *See also id.*at ftnt. 30 ("Defendants do not contest that the government proved a scheme to defraud the banks.")

[43] The federal court that denied Deloitte's prior Motion for Summary Judgement based on the *in pari delicto* defense did not take into consideration the fact that Coudersport participated as a Co-Borrower in the fraudulent borrowing scheme for which John Rigas, Coudersport's sole owner, was convicted. *See* Island Partners v. Deloitte & Touche LLP, 2014 WL 6982140, at *10 (SDNY 05-CV-2770). The federal court also necessarily did not consider this Commonwealth's "public interest in relieving [its] courts from lending their offices to mediating disputes among wrongdoers." AHERF v. PwC, 605 Pa. at 295–96, 989 A.2d at 329.

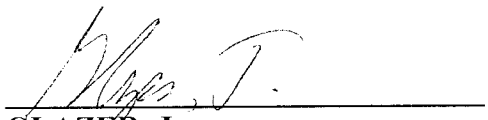
[44] *See* Brandon Rebuttal, pp. 3-4; Brulenski Rebuttal, p. 4.

[45] *See* AHERF v. PwC, 605 Pa. at 305-6, 989 A.2d at 335-6 ("On balance, we believe the best course is for Pennsylvania common law to continue to recognize the availability of the *in pari delicto* defense (upon appropriate and sufficient pleadings and proffers), via the necessary imputation, in the negligent-auditor context. . . . In terms of other important policy concerns, we do not believe it undermines the objectives of our tort and contract schemes to deny recovery to one whose agents have acted for the benefit of the corporation with culpability exceeding that of the defendant [auditor]. Similarly, we conclude that the traditional, liberal test for corporate benefit should apply in such scenarios.") *See also* Columbia Med. Grp., Inc. v. Herring & Roll, P.C., 829 A.2d 1184, 1193 (Pa. Super. 2003) ("[W]e conclude that the issues presented in the criminal and instant civil action are the same and that contributory negligence was a proper defense, which barred [the corporate and individual clients'] negligence claims. The jury in [the individual clients'] criminal trial established that [they] withheld/misrepresented information to [their accountant] and chose to disregard his advice. As such, we conclude that [both the corporate and individual clients] are estopped from adjudicating whether [their accountant] was negligent with regard to the preparation of the income tax returns/discussion with the IRS at issue, and, therefore, the first element of the collateral estoppel test has been met.")

CONCLUSION

For all the foregoing reasons, Deloitte's Motion for Summary Judgment is granted, and judgment is entered in favor of Deloitte and against Zito on all of Zito's claims.

Dated: September 6, 2018



GLAZER, J.