Hearing Date and Time: November 16, 2004 at 10:00 a.m.

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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re:	:	Chapter 11
RCN CORPORATION, et al.,	:	Case No. 04-13638 (RDD)
Debtors.	:	Jointly Administered

OBJECTION OF THE NOTEHOLDER INVESTORS TO DEBTORS' MOTION FOR ORDER UNDER 11 U.S.C. §§ 105(A), 363(B), 503(B) AND 507 AUTHORIZING, APPROVING AND RATIFYING (I) COMMITMENTS FOR CONVERTIBLE SECOND-LIEN NOTES, (II) PLACEMENT AGENT AGREEMENT, AND (III) PAYMENT OF RELATED FEES AND EXPENSES

TO THE HONORABLE ROBERT D. DRAIN,
UNITED STATES BANKRUPTCY JUDGE:

Tejas Securities Group, Inc. ("Tejas") and the holders of approximately $170 million in aggregate face amount of RCN Corporation Senior Notes, who together have submitted a competing commitment for the purchase of convertible second-lien notes (collectively, the "Noteholder Investors"),[1] by and through their undersigned counsel, hereby object to the Motion (the "Motion") of RCN Corporation ("RCN") for an Order Under 11 U.S.C. §§ 105(a), 363(b),

[1] The Noteholder Investors consist of the following entities and/or certain of their affiliates: (i) Tejas; (ii) Lampe Conway Master Fund; (iii) Greywolf Capital Partners II LP; (iv) JANA Master Fund; and (v) Phoenix Partners.

503(b) and 507 Authorizing, Approving and Ratifying (I) Commitments For Convertible Second-Lien Notes, (II) Placement Agent Agreement, and (III) Payment of Related Fees and Expenses, and in support thereof respectfully represent as follows:

<u>PRELIMINARY STATEMENT</u>

1. Through the Motion, the Debtors seek authorization, approval and ratification of a series of related transactions proposed to the Debtors by D.E. Shaw Laminar Lending 2, Inc. ("Laminar") pursuant to which the reorganized RCN will issue up to $150 million in Convertible Second-Lien Notes bearing interest at 7.5% per year to: (a) Laminar, who has committed to purchase not less than 51% of the principal amount of notes offered, (b) general unsecured creditors who qualify as accredited investors or qualified institutional buyers, in an amount not to exceed 49% of the notes offered; and (c) certain members of the Creditors' Committee (collectively, the "Committee Purchasers"), who have committed to purchase all of the remaining notes that are offered to and not purchased by the Debtors' general unsecured creditors. The Debtors' plan of distribution for the Convertible Second-Lien Notes calls for Deutsche Bank Securities, Inc. and Deutsche Bank AG Cayman Islands Branch (together, "Deutsche Bank") to offer the Convertible Second-Lien Notes in exchange for a placement fee of 1.5% of the aggregate amount of notes sold.

2. The Noteholder Investors have submitted to the Debtors a commitment letter for the purchase of convertible second-lien notes on terms more favorable than those proposed by Laminar (collectively, the "Noteholder Investor Proposal"). Specifically, and as set forth in more detail on <u>Exhibit A</u> hereto, the Noteholder Investors are prepared to accept a .25% reduction in the interest rate on the Convertible Second-Lien Notes, and will commit to purchase up to an aggregate amount of $150,000,000 of 7.25% convertible second-lien notes

(the “Investor Notes”) from reorganized RCN.[2] In addition, Tejas will act as placement agent for the Investor Notes for a fee of 1.0% of the aggregate amount of Investor Notes sold, which is .5% less than the placement fee proposed by Deutsche Bank.

3. The Debtors, as fiduciaries for the creditors of these estates, in the face of competing alternative exit financing proposals, must accept the proposal that maximizes the benefits for all creditors. The Noteholder Investor Proposal is clearly superior because of its reduced interest rate and lower proposed transactions costs. Because the Noteholder Investors are offering the Debtors exit financing which is virtually identical to the financing proposed by Laminar, but which contains certain terms which are obviously better for these estates, this Court should deny the Motion and authorize the Debtors to consummate the alternative exit financing contemplated by the Noteholder Investor Proposal.

4. To the extent that this Court finds that the Noteholder Investor Proposal does not offer the Debtors exit financing on terms more favorable than those described in the Motion, or to the extent that Laminar is able to provide the Debtors with even more attractive exit financing terms, the Noteholder Investors object to the Motion on the limited grounds that there is no legitimate basis to provide Deutsche Bank with a windfall of up to $2.25 million for acting as placement agent when it appears they will have no substantive roll in the placement of the notes. The Debtors should be able to place the Convertible Second-Lien Notes themselves or,

[2] The Noteholder Investors will reduce their total commitment to purchase Investor Notes by up to $50 million upon their receipt of executed commitment letters from the Committee Purchasers to purchase Investor Notes in the individual aggregate face amounts set forth for each Committee Purchaser in the Motion. Such commitment letters shall be in form and substance acceptable to the Noteholder Investors.

alternatively, the Debtors can engage Tejas to serve as placement agent for a fee of 1.0%, a savings of up to $750,000 for the creditors of these estates.[3]

BACKGROUND

A. The Chapter 11 Cases

5. On May 27, 2004 (the "Petition Date"), RCN and certain other Debtors filed voluntary petitions under chapter 11 of title 11 of the United States Code (the "Bankruptcy Code").[4] RCN Cable TV of Chicago, Inc., an affiliate of RCN, commenced its chapter 11 case on August 5, 2004. Certain additional Debtors commenced their chapter 11 cases on August 20, 2004.[5]

6. The Debtors continue to manage and operate their business as debtors-in-possession pursuant to sections 1107 and 1108 of the Bankruptcy Code.

7. On June 14, 2004, the United States Trustee appointed the Official Committee of Unsecured Creditors of RCN Corporation, et al. (the "Creditors' Committee").

B. The Deutsche Bank Exit Facility

8. On May 24, 2004 Deutsche Bank executed a commitment letter and related documents (collectively, the "Deutsche Bank Commitment Letter") that set forth Deutsche Bank's commitment to provide a new senior exit financing facility to the Debtors. Pursuant to the Deutsche Bank Commitment Letter, Deutsche Bank would provide an exit facility (the "Exit

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[3] The Noteholder Investors were advised by the Debtors counsel at approximately 6:30 p.m. on November 15, 2004, that Deutsche Bank has agreed not to seek a placement fee if they do no substantive work in connection with the placement of the Convertible Second-Lien Notes. Unless and until the Debtors can assure the Court that no placement fee will be paid to Deutsche Bank, the Noteholder Investors stand by their objection.

[4] In addition to RCN, TEC Air, Inc., RLH Property Corporation, RCN Finance, LLC and Hot Spots Productions, Inc., all affiliates of RCN, commenced their chapter 11 cases on May 27, 2004.

[5] RCN Telecom Services of Virginia, Inc., RCN Entertainment, Inc., 21st Century Telecom Services, Inc. and ON TV, Inc., all affiliates of RCN, commenced their chapter 11 cases on August 20, 2004.

Facility") comprised of two components: (i) a senior first-lien secured credit facility in the principal amount of $285 million plus a $25 million letter of credit facility (the "Senior First-Lien Financing") and (ii) second-lien floating rate notes in the principal amount of $150 million (the "Second-Lien Notes").

9. On June 22, 2004, this Court entered an order authorizing, approving, and ratifying the Deutsche Bank Commitment Letter and the Debtors' payment of certain fees and expenses related thereto.

C. The Convertible Second-Lien Notes

10. In August of 2004, Laminar began discussions with the Debtors concerning an alternate exit financing scenario involving the issuance of second-lien notes that would be convertible into the common stock of reorganized RCN in lieu of the Second-Lien Notes contemplated by the Exit Facility (the "Convertible Second-Lien Notes").

11. On October 13, 2004, this Court entered an order approving the Debtors' disclosure statement with respect to their proposed joint plan of reorganization (the "Disclosure Statement"). In the Disclosure Statement, the Debtors stated that they were considering alternative exit financing structures, including convertible second-lien notes, which, if implemented, would alter certain terms of the Exit Facility.

12. As described in the Motion, the Debtors contemplate issuing up to $150 million principal amount of the Convertible Second-Lien Notes bearing interest at a rate of 7.5% per year using Deutsche Bank as the Debtors' placement agent in connection with the offer and sale of the Convertible Second-Lien Notes. As compensation for Deutsche Bank's services, and subject to certain adjustments, the Debtors are asking the Court to authorize payment to Deutsche Bank of a placement fee in an amount up to 1.5% of the aggregate amount of

Convertible Second-Lien Notes sold by Deutsche Bank, plus reasonable out-of-pocket costs and expenses (including the costs of counsel) (collectively, the "Deutsche Bank Placement Fee").

13. The Debtors, through Deutsche Bank, will offer up to 49% of the Convertible Second-Lien Notes to the Debtors' general unsecured creditors that are "accredited investors" or "qualified institutional buyers" as those terms are defined pursuant to the Securities Act of 1933, as amended (the "Securities Act") in a transaction intended to be exempt from registration under the Securities Act. The Debtors have agreed to facilitate the offering of the Convertible Second-Lien Notes by furnishing Deutsche Bank with a list of holders of general unsecured claims that the Debtors believe qualify as accredited investors.

14. Laminar has agreed to purchase up to $100 million principal amount of the Convertible Second-Lien Notes pursuant to a commitment letter, dated November 3, 2004 (the "Laminar Commitment Letter"). Pursuant to the terms of the Laminar Commitment Letter, Laminar's commitment to purchase the Convertible Second-Lien Notes may be reduced to the extent that the Debtors' general unsecured creditors purchase Convertible Second-Lien Notes.

15. Pursuant to the executed commitment letters attached to the Motion, the Committee Purchasers have committed to purchase those Second Lien Notes not purchased by the Debtors' unsecured creditors or Laminar in the following aggregate principal amounts: (a) Romulus Holdings, Inc. - up to $10 million; (b) Tudor Investments Corporation - up to $29 million; and (c) York Capital Management - up to $11 million. In the aggregate, Laminar and the members of the Creditors' Committee have committed to purchase the entire amount, or $150,000,000, of the Convertible Second-Lien Notes to be issued by the reorganized RCN.

D. Noteholder Proposals

16. The Noteholder Investors originally became interested in providing an alternative to the Convertible Second-Lien Notes described in the Debtors' Disclosure

Statement to ensure that the recoveries on their Senior Note claims would not be materially harmed by the Debtors' exit financing. Specifically, the terms of the Convertible Second-Lien Notes described in the Disclosure Statement included a reset of the conversion price on the 12 month anniversary of the Effective Date that had the potential to dilute materially the equity to be received by the holders of Senior Notes.

17. Accordingly, on October 25, 2004, the Noteholder Investors submitted a term sheet for the Convertible Second-Lien Notes on terms similar to those outlined in the Disclosure Statement, but without the conversion price reset provisions.

18. Although there were subsequent discussions and negotiations between the Noteholder Investors and the Debtors, ultimately Laminar revised its commitment to match the original proposal made by the Noteholder Investors. The Motion seeks approval of the Laminar Commitment Letter.

19. The Noteholder Investor Proposal provides the Debtors with alternative exit financing on virtually identical terms to those described in the Laminar Commitment Letter, but with two significant improvements: (i) the Investor Notes will be issued at an interest rate of 7.25%, a reduction of .25% from the interest charged on the Convertible Second-Lien Notes contemplated in the Laminar Commitment Letter; and (ii) the placement agent's fee has been reduced from 1.5% to 1.0%. The Noteholder Investors have executed a commitment letter, attached hereto as Exhibit A (the "Noteholder Investor Commitment Letter"), to purchase up to $150,000,000 of the Investor Notes.[6]

[6] The Noteholder Investors will reduce their total commitment to purchase Investor Notes by up to $50 million upon their receipt of executed commitment letters from the Committee Purchasers to purchase Investor Notes in the individual aggregate face amounts set forth for each Committee Purchaser in the Motion. Such commitment letters shall be in form and substance acceptable to the Noteholder Investors.

OBJECTION

I. The Debtors Have a Duty to Select the Exit Financing Alternative That Maximizes Creditor Recoveries

20. The Debtors have a fiduciary obligation to maximize the value of their estates for the benefit of creditors and, thus, carefully select each corporate opportunity. See, e.g., In re Hampton Hotel Investors, L.P., 270 B.R. 346, 362 (Bankr. S.D.N.Y. 2001) (a debtor in possession is bound by a duty of loyalty that includes an obligation to . . . maximize the value of the estate."); Morin v. Galan (In re Lantzatella), 254 B.R. 84, 88 (Bankr. W.D.N.Y. 2000) (trustee in bankruptcy "has a duty to maximize the return for unsecured creditors").

21. The Noteholder Investors are not just competing bidders motivated by potential profits associated with the placement of or investment in the Convertible Secured Second-Lien Notes transaction. They are also significant creditors of these estates whose interests are aligned with the Debtors' fiduciary duty to maximize creditor recoveries. The Noteholder Investors, who will hold substantial equity positions in the reorganized RCN by virtue of their significant holdings of Senior Notes, want these estates to take advantage of the best exit financing terms available. The reduced cost Investor Notes provide the best terms available.

22. The Noteholder Investor Proposal is clearly the best deal for all parties concerned because the Investor Notes provide alternative exit financing to the Debtors at less cost as a result of reductions in the interest rate on the Investor Notes and the placement fee proposed to be charged by Tejas. The benefits of the Investor Notes will include a reduced interest burden on the reorganized RCN and increased cash on the Effective Date. As fiduciaries, the Debtors must choose the exit financing alternative that is most likely to maximize the value of reorganized RCN and thus maximize creditor recoveries. Accordingly,

the Motion should be denied, and the Debtors should be authorized to consummate the alternative exit financing described in the attached term sheet.

II. The Deutsche Bank Placement Fee Is Unnecessary and Excessive

23. Even if this Court disagrees with the Noteholder Investors and does not deny the Motion on the grounds that as fiduciaries the Debtors are obligated to enter into a superior exit financing transaction, this Court should refuse to authorize and approve the Deutsche Bank Placement Fee because the Debtors have not established any reasonable basis for providing Deutsche Bank with such a sizeable fee for limited participation in the offering of the Convertible Secured Second-Lien Notes.

24. As a result of Laminar's purchase commitment and the backstop commitments of the Committee Purchasers, the Convertible Secured Second-Lien Notes issuance is fully subscribed and may be oversubscribed to the extent that any qualifying general unsecured creditors decide to purchase Convertible Secured Second-Lien Notes. There is little, if any, need for a placement agent in the Laminar deal, as it is fully subscribed and is, therefore, from Deutsche Bank's perspective, a risk free note issuance. This is even more the case here where the Debtors have agreed to identify the unsecured creditors that it believes are likely accredited investors. Plainly stated, absent this Court's intervention, Deutsche Bank stands to make substantial fees for doing nothing more than acting as a mailing agent for the Debtors. This is particularly troubling considering that Deutsche Bank will also be receiving a 1.5% break-up fee for not providing the financing being provided through the Convertible Second-Lien Notes.

25. If the Debtors insist that the retention of a placement agent is a necessary pre-requisite to a successful offering of the Convertible Secured Second-Lien Notes to pre-identified accredited investors and/or Laminar and the Committee Purchasers, the Debtors can retain Tejas at a 1% fee and save the estates up to $750,000.

WHEREFORE, the Noteholder Investors respectfully request that this Court deny the Motion in its entirety and approve the transactions contemplated by the Noteholder Investor Proposal, or in the alternative, refuse to ratify and approve the Debtors' selection of Deutsche Bank as placement agent at the Deutsche Bank Placement Fee, and grant the Noteholder Investors such other and further relief as this Court deems just, equitable and proper.

Dated: New York, New York
November 15, 2004

Respectfully submitted,

/s/ Michael S. Stamer__________________
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