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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

	X	
In re	:	Chapter 11 Case No.
	:	03-___________ ( )
Allegiance Telecom, Inc., et al.,	:	
	:	Jointly Administered
Debtors.	:	
	X	

MOTION OF DEBTORS PURSUANT TO SECTIONS 105(a) AND 363(b) OF THE BANKRUPTCY CODE FOR AUTHORIZATION TO CONTINUE THE DEBTORS' WORKERS' COMPENSATION PROGRAMS, INSURANCE POLICIES, AND AGREEMENTS RELATING THERETO AND PAY CERTAIN PREPETITION OBLIGATIONS IN RESPECT THEREOF

TO THE HONORABLE UNITED STATES BANKRUPTCY JUDGE:

Allegiance Telecom, Inc. and its direct and indirect subsidiaries, as debtors and debtors in possession (collectively, "Allegiance" or the "Debtors"), respectfully represent:

Introduction

1. On the date hereof (the "Commencement Date"), the Debtors each commenced with this Court a voluntary case under chapter 11 of title 11, United States Code (the "Bankruptcy Code"). The Debtors continue to be authorized to operate their business and manage their properties as debtors in possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code. Simultaneously with the filing of their petitions and this Motion, the Debtors

have requested an order directing the joint administration of their chapter 11 cases pursuant to rule 1015(b) of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules").

Jurisdiction

2. This Court has subject matter jurisdiction to consider and determine this motion pursuant to 28 U.S.C. § 1334. This is a core proceeding pursuant to 28 U.S.C. § 157(b). Venue is proper before this Court pursuant to 28 U.S.C. §§ 1408 and 1409.

An Overview of Allegiance's Business

3. Allegiance is a facilities-based national local exchange carrier that provides integrated telecommunications products and services to small and medium-sized business customers, large businesses (i.e., national customers with multiple locations), governmental entities, wholesale customers and other institutional users. Allegiance offers its customers a variety of services, including:

- local and long distance voice services, including basic telephone services and advanced calling features;
- broadband and other Internet and data services, including high-speed Internet access, wide area network interconnection, domain name registration, web hosting, email and colocation services;
- integrated local long distance/Internet access offerings, which provide customers with integrated voice and Internet access over a single broadband line;
- wholesale services to other regional and national service providers, including equipment colocation, managed modem ports and Internet protocol traffic aggregation; and
- customer premise equipment sales and maintenance services.

4. Allegiance serves more than 100,000 business customers in 36 markets. Allegiance employs approximately 3,560 people, of which approximately 97 employees are covered by collective bargaining agreements.

5. As of the Commencement Date, the Debtors have approximately $245 million of cash. As of December 31, 2002, the Debtors' consolidated books and records reflected assets totaling approximately $1.441 billion and liabilities totaling approximately $1.397 billion. For the three months ending December 31, 2002, the Debtors, on a consolidated basis, reported revenues of approximately $204.91 million, EBITDA (i.e., earnings before interest, taxes, depreciation, amortization, non-cash deferred compensation expense and non-cash goodwill impairment charges) of approximately negative $34 million and net losses of approximately $120 million.

Allegiance is Critical to Promoting Sustainable
Competition in the Local Telecommunication Marketplace

The Telecommunications Act of 1996

6. In February of 1996, Congress enacted the Telecommunications Act of 1996 (the "Telecom Act"), with the stated purpose of:

> promot[ing] competition and reduc[ing] regulation in order to secure lower prices and higher quality services for American telecommunications consumers and encourage the rapid deployment of new telecommunications technologies.

H.R. REP No. 104-204(I), 104th Cong. 1st Sess. 1995 (July 24, 1995), reprinted in 1996 U.S.C.C.A.N. 10, **10. In that regard, the Telecom Act required Incumbent Local Exchange Carriers, including the Regional Bell Operating Companies ("ILECs") – i.e., existing telecommunications monopolies – to allow newly created Competitive Local Exchange Carriers ("CLECs") to (a) interconnect with the ILECs, (b) access portions of the ILEC network and (c) collocate their equipment in ILEC facilities all at forward-looking cost based rates. In addition, CLECs were permitted to purchase ILEC services at wholesale prices and resell them to customers at retail prices.

7. The enactment of the Telecom Act spurred entrepreneurs to start hundreds of new businesses to compete in the local telecommunications marketplace. During the late 1990s, investors recognized the growth opportunity inherent in the opening of a competitive local telecommunications marketplace and invested billions of dollars in equity and debt capital into a multitude of telecommunications companies primed to provide competing services to American consumers.

8. Funded with significant amounts of investment capital, two types of CLECs emerged. The first type of CLECs were "resellers". Specifically, "reseller" CLECs purchased telecommunications services from ILECs at a discount and resold the services to customers at a higher price. Thus, these CLECs simply offered consumers the same services supplied by ILECs - generally at lower prices. To be successful with this low margin business model, "reseller" CLECs invested their capital in sales and marketing efforts designed to acquire a substantial customer-base and attendant market-share in a relatively short period of time and ahead of their many competitors. However, because resellers were providing the identical services as the ILECs (with no differentiation) and were attempting to build a large market share in a highly competitive market, this business model was flawed and many in the telecommunications industry believe that the "resale" business will fail.

9. The second type of CLECs were "facilities-based" CLECs. These CLECs invested significant sums of money to build their own proprietary infrastructure and network in order to effectively compete with the ILECs. Specifically, facilities-based CLECs combined elements of an ILEC's network with their own to provide consumers with true differentiated services. As Michael Powell stated in his partial dissent to the FCC's 2003 Triennial Review:

> Facilities -based competition means a competitor can offer real differentiated service to consumers . . . . Facilities-based competitors own

> more of their own network and control more of their costs, thereby offering consumers real potential for lower prices. Facilities-based competitors offer greater rewards for the economy – buying more equipment from other suppliers . . . and creating more jobs. . . . . And, facilities providers create vital redundant networks that can serve own nation if other facilities are damaged by those hostile to our way of life.

F.C.C., 2003 Triennial Review - Open Meeting, Separate Statement of Chairman Michael R. Powell, dissenting in part (February 20, 2003) (transcript available at www.fcc.gov/wcb/cpd/triennial_review/). Allegiance is such a facilities-based CLEC with a nationwide network and a facility-based business strategy.

The Allegiance Nationwide Network – Servicing 36 Metropolitan Areas

10. In 1997, a management team of industry veterans launched Allegiance and focused on building a reliable nationwide network based on proven technologies, a nationwide direct sales force primarily focused on the small to medium sized business enterprise and information processing systems to support its operations. Allegiance was one of the first major local exchange carriers to open markets utilizing the "smart build" strategy. This strategy allowed a more rapid ramp-up in operations than the traditional competitive local exchange model in which extensive networks were built, including fiber networks, prior to the generation of significant revenues. In contrast, Allegiance's initial network build-out simply required (a) deploying digital switching platforms with local and long distance capability and (b) leasing transport facilities from the incumbent local exchange carriers and other competitive local exchange carriers to connect its switches with its transmission equipment colocated in the incumbent local exchange carrier's central offices. Once traffic volume justified further "success-based" investment, Allegiance leased dark fiber or built specific network segments. This strategy offered two major economic benefits. First, it enabled Allegiance to enter new markets with alacrity and reduce up-front capital requirements for entering individual markets

prior to revenue generation. Second, in contrast to the traditional competitive local exchange carriers that generally built their networks in highly concentrated downtown areas due to the high cost of constructing fiber networks, Allegiance's business model enabled it to provide services to customers in downtown areas as well as the more geographically dispersed, less competitive areas of its targeted markets.

11. Allegiance's initial business plan proposed entering into 24 of the largest metropolitan areas in the United States. Subsequently, management expanded its business plan to (a) increase the total number of target markets to 36, (b) increase its service area, i.e., its colocation "footprint" in its original 24 markets, and (c) acquire long-term rights to use dark fiber rings to replace network elements leased by the Debtors from the incumbent local exchange carriers.

12. In addition to internal growth, Allegiance's business plan included growth through strategic acquisitions. For example, in December 2001, Allegiance acquired certain assets of Intermedia Business Internet (the "Intermedia Acquisition"). The Intermedia Acquisition enabled Allegiance to (a) become a Tier 1 Internet access provider, (b) provide large quantities of data transmitted at high-speeds over the Internet to and from a customer's premises, (c) efficiently exchange traffic with other Internet backbone providers giving Allegiance greater control over its Internet access, and (d) leverage its local service presence to provide additional services to its target market. In June 2003, Allegiance acquired certain assets of Shared Technologies (the "Shared Technologies Acquisition"). The Shared Technologies Acquisition (a) added customer premises equipment sales, installation and maintenance to Allegiance's portfolio of integrated products and services, (b) strategically enhanced Allegiance's target market of small to medium size business enterprises, and (c) allowed Allegiance to provide a complete communications solution to business customers.

13. As of the date hereof, Allegiance provides its telecommunications services in major metropolitan areas across the United States, including the following 36 markets: Atlanta, Austin, Baltimore, Boston, Chicago, Cleveland, Dallas, Denver, Detroit, Fort Lauderdale, Fort Worth, Houston, Long Island, Los Angeles, Miami, Minneapolis/St. Paul, New York City, Northern New Jersey, Oakland, Ontario/Riverside, CA, Orange County, Philadelphia, Phoenix, Pittsburgh, Portland, Sacramento, St. Louis, San Antonio, San Diego, San Francisco, San Jose, Seattle, Tampa, Washington, D.C., West Palm Beach/Boca Raton and White Plains. Allegiance is colocated in 849 central offices and has a Tier 1 Internet backbone.

The FCC Recognizes the Importance of Allegiance

14. Federal policy recognizes the importance of facilities-based CLECs and Allegiance is the model. In that regard, the Federal Communications Commission (the "FCC") recently published its latest rules for local competition in the *FCC Triennial Review*. In reviewing these rules, a Kaufman Bros. Equity Research Report, dated March 4, 2003, stated that "*Allegiance is the blueprint for local competition proposed by the FCC*." In addition, Kevin J. Martin, Commissioner of the FCC has noted:

> Allegiance has focused on building a business that adheres to the letter of the Telecom Act while leveraging the entrepreneurial spirit of the law, as well. Today, Allegiance stands as a model of what Congress intended in 1996, and what we hope to achieve in the years ahead – new entrants that have the opportunity to continue to invest in infrastructure, bring innovation and offer new service offerings to consumers in local markets that are open to fair and robust competition.

Kevin J. Martin, Commissioner, F.C.C., Address to the Telecommunications Law Conference and the Texas Chapter of the Federal Communications Bar Association (March 7, 2002) (transcript available at www.fcc.gov/Speeches/Martin/2002/spkjm203.html).

15. Thus, it is clear that Allegiance, by focusing on an intelligent – well thought out business model – building its own network and offering its consumers innovative

services, is an integral player in the telecommunications marketplace and a model for the nation's policy of promoting sustainable facilities-based competition in the local telecommunications arena. With an appropriate capital structure and a reduction in unnecessary costs, Allegiance believes it will be one of the most successful telecommunications companies in the United States.

Capital Structure of the Debtors

Capital Stock

16. Allegiance Telecom, Inc. has two classes of authorized stock: (a) 750,000,000 shares of common stock, with par value of $0.01 per share and (b) 1,000,000 shares of preferred stock, with par value of $0.01 per share. As of December 31, 2002, Allegiance Telecom, Inc. had (i) 124,830,110 shares of common stock issued and outstanding, with 295 registered holders and at least 20,000 beneficial owners, and (ii) no shares of preferred stock outstanding. Allegiance Telecom, Inc.'s common stock is publicly traded on the Nasdaq National Market under the symbol "ALGX."

17. Allegiance Telecom, Inc. owns 100% of the capital stock of Allegiance Telecom Company Worldwide ("ATCW"), and ATCW directly or indirectly owns 100% of the capital stock of each of the other Debtors.

Prepetition Notes

18. In 1998, Allegiance Telecom, Inc. issued two series of notes: (i) 11 3/4% Senior Discount Notes with a face value of $445 million, due on February 15, 2008 (the "Senior Discount Notes") and (ii) 12 7/8% Senior Notes with a face value of $205 million, due on May 15, 2008 (the "Senior Notes"). The Senior Discount Notes were issued under that certain Indenture, dated as of February 3, 1998, between Allegiance Telecom, Inc. and The Bank of New York, as Indenture Trustee. The Senior Notes were issued under that certain Indenture,

dated as of July 7, 1998, between Allegiance Telecom, Inc. and The Bank of New York, as Indenture Trustee. Neither the Senior Discount Notes nor the Senior Notes are secured by any assets of the Debtors or guaranteed by any of the Debtors.

Prepetition Credit Agreement

19. Prior to the Commencement Date, ATCW entered into that certain Credit and Guaranty Agreement, dated as of February 15, 2000, as amended as of November 27, 2002 (the "Prepetition Credit Agreement"), among ATCW, as borrower; all of the other Debtors, as guarantors; Goldman Sachs Credit Partners L.P. ("Goldman Sachs"), as syndication agent and sole lead arranger; General Electric Capital Corporation ("GECC") (as successor to Toronto Dominion (Texas), Inc.), as administrative agent, BankBoston, N.A. ("BankBoston") and Morgan Stanley Senior Funding, Inc. ("Morgan Stanley"), as co-documentation agents; Goldman Sachs, GECC, BankBoston, Morgan Stanley, certain managing agents, and lenders party thereto from time to time (collectively, the "Prepetition Lenders"). As of the Commencement Date, the amount outstanding under the Prepetition Credit Agreement was approximately $465.3 million. The Debtors have pledged substantially all of their assets as collateral under the Prepetition Credit Agreement, including (a) the capital stock of ATCW and (b) substantially all of the assets of ATCW and its direct and indirect subsidiaries, including the capital stock owned by ATCW in each of its Debtor subsidiaries. As of the Commencement Date, there were 27 Prepetition Lenders under the Prepetition Credit Agreement.

Events Leading to Chapter 11 Filing

20. The distressed economic environment in the United States that followed the economic boom of the late 1990s has had a global and adverse impact on the telecommunications industry. In the late 1990s, in an effort to finance operations and build their networks, telecommunications companies borrowed significant amounts of money from lenders

and the public through the issuance of debt. The resulting significant indebtedness incurred by telecommunications companies, combined with poor economic conditions required many companies, including the Debtors, to focus on reducing their debt either through out of court restructurings or the chapter 11 process.

21. Many of Debtors' existing and potential customers have experienced their own financial difficulties, thereby decreasing customer demand for existing and new services. The financial difficulties of the Debtors' customers has led to non-payment, partial payment, or slow payment of bills for services provided by the Debtors. The financial instability of other companies in the telecommunications industry has adversely affected the willingness of potential customers to move their telecommunications services to the Debtors. In addition, certain of the Debtors' suppliers have requested deposits, letters of credit, or other types of security. Moreover, telecommunications carriers that owe reciprocal and/or intercarrier compensation to the Debtors have either refused to pay or failed to pay in a timely manner for the services provided by the Debtors.

22. As a consequence of the foregoing, the Debtors' business operations were adversely impacted and, due to revenue trends and continuing negative EBITDA, the Debtors determined that their current level of indebtedness needed to be significantly reduced. Thus, in order to maximize the long-term wealth generating capacity of their business operations, the Debtors, among other things, (a) established a special restructuring committee of the Board of Directors of Allegiance Telecom, Inc., (b) retained restructuring advisors, and (c) commenced extensive negotiations with their senior lenders and bondholders, as detailed below.

Negotiations with the Prepetition Lenders and the Ad Hoc Committee of Bondholders

23. The Debtors, in the exercise of their sound business judgment - and in recognition of the distressed economic environment and the need for the Debtors' businesses to

focus on profitability instead of high revenue growth - determined that a meaningful de-leveraging of their capital structure was crucial for the preservation and maximization of the value of their businesses. In that regard, the Debtors, in conjunction with their financial advisors and the Board of Directors of Allegiance Telecom, Inc., commenced the process of determining the appropriate capital structure for their business operations. After determining the appropriate capital structure, the Debtors commenced negotiations with the Prepetition Lenders and the Ad Hoc Committee (as defined below) to effectuate a restructuring transaction.

24. In October of 2002, Allegiance began negotiations with its Prepetition Lenders regarding a potential restructuring of its long-term debt. On November 27, 2003, Allegiance and its Prepetition Lenders entered into that certain First Amendment to the Prepetition Credit Agreement (the "Amendment"). Pursuant to the Amendment, the Debtors obtained a moratorium on their financial covenants through April 30, 2003. In exchange for the Amendment, Allegiance agreed, among other things, (a) that an event of default would occur on April 30, 2003 unless it reduced its long term debt to a level not to exceed $645 million, and (b) to repay $15 million to the Prepetition Lenders on account of debt owed under the Prepetition Credit Agreement. During the latter part of 2002 and to meet covenants under the Amendment, the Debtors significantly lowered their capital expenditures, reduced headcount, substantially decreased growth, eliminated less profitable products and services, and continued to optimize their existing network assets.

25. After entering into the Amendment, the Debtors commenced negotiations with the Prepetition Lenders to consummate a permanent restructuring. In connection with the negotiations regarding the permanent restructuring, the Debtors commenced negotiations with an

ad hoc committee of noteholders, which is comprised of certain holders of the Senior Notes and the Senior Discount Notes (the "Ad Hoc Committee").

26. The Debtors, the Prepetition Lenders and the Ad Hoc Committee were not able to reach an agreement concerning the permanent restructuring prior to the April 30 deadline. On April 29, 2003, in order to avoid the occurrence of certain events of default under the Prepetition Credit Agreement, the Debtors and the Prepetition Lenders entered into a forbearance agreement (the "Forbearance Agreement"), which expires on May 15, 2003. The Forbearance Agreement provided for, among other things, a pay down of $5 million of principal owed under the Prepetition Credit Agreement.

27. After entering into the Forbearance Agreement, the Debtors continued their negotiations with the Prepetition Lenders and the Ad Hoc Committee. However, the parties were unable to reach an agreement prior to the expiration of the term of the Forbearance Agreement. Consequently, the Debtors, in the exercise of their prudent business judgment, determined that it was in the best interests of all of their stakeholders and for the maximization of the value of their businesses to commence these chapter 11 cases and consummate a restructuring of their indebtedness under the auspices of this Court.

The Debtors' Insurance Programs

28. In connection with the operation of their business, the Debtors maintain various workers' compensation programs, insurance policies, and related programs (the "Insurance Programs and Policies") through several insurance carriers (the "Insurance Carriers"). Annexed hereto as Exhibit "A" is a list of the Insurance Programs and Policies and the respective Insurance Carriers. As set forth below, the Insurance Programs and Policies include coverage for

current or future claims involving workers' compensation, property, general liability, automobile, excess liability, directors' and officers' liability, and other miscellaneous liabilities.[1]

Brokers

29. Prior to the Commencement Date, the Debtors entered into certain insurance brokerage agreements with Marsh USA, Inc. and Unimark Insurance Agency, Inc., respectively (together, the "Brokers"), for the administration of the majority of the Debtors' Insurance Programs and Policies. With respect to certain of these policies, the Insurance Carriers generally charge the Brokers directly for all premiums and other amounts due under such policies. Periodically, the Brokers send the Debtors a consolidated statement for payment and, once paid by the Debtors, the Brokers submit the payments to the Insurance Carriers. For all other Insurance Programs and Policies, the premiums are paid directly by the Debtors to the Insurance Carriers. The Brokers are paid a fee for servicing substantially all the Debtors' Insurance Programs and Policies and assisting in claims management with respect thereto.

Workers' Compensation Programs

30. Under the laws of the various states in which they operate, the Debtors are required to maintain workers' compensation policies and programs to provide their employees with workers' compensation coverage for claims arising from or related to their employment with the Debtors (the "Workers' Compensation Programs"). The Debtors maintain workers' compensation insurance that covers their statutory obligations in each of the states in which they operate, with the exception of Ohio, which requires individualized coverage. The Debtors

[1] In addition to the Insurance Policies listed on Exhibit "A," the Debtors maintain numerous insurance policies with respect to employee health, disability, and life insurance benefits. These policies are addressed in a separate motion filed contemporaneously herewith pertaining to the Debtors' employee benefits programs.

maintain a separate policy for Ohio that addresses the peculiar requirements of such state's workers' compensation laws.

31. The Workers' Compensation Programs consist of both funded and self-funded components and are administered by The Hartford Companies ("Hartford"). The Workers' Compensation Programs carry a $500,000 deductible per occurrence, which is self-funded by the Debtors. Any claim amounts above the deductible limits are fully funded by Hartford.

32. Premiums for the Workers' Compensation Programs are based on a fixed rate of estimated annual payroll. Following an annual audit of the Debtors' payroll, the Debtors either pay a retrospective premium owed or receive back overpayments that were made. On certain of the Workers' Compensation Programs, there are annual retrospective audits and annual "true-ups" of the premiums owed which are paid directly to the Insurance Carriers.

33. Employees who are injured while working for the Debtors submit their claims (the "Workers' Compensation Claims") directly to Hartford. Thereafter, Hartford pays the injured employees. Subsequently, Hartford bills the Debtors for the amount of Workers' Compensation Claims paid by Hartford up to the deductible limits. In connection with the payment of Workers' Compensation Claims, the Debtors have obtained, and there is currently outstanding, a letter of credit for the benefit of Hartford in the amount of $3,000,000.

34. The aggregate annual premiums with respect to the Workers' Compensation Programs, including letter of credit fees, total approximately $600,000. The Debtors estimate the amount outstanding, as of the Commencement Date, in respect of premiums and costs associated with the Workers' Compensation Programs is approximately $245,000.

35. As of the Commencement Date, there were approximately 42 Workers' Compensation Claims pending against the Debtors. Because payment of the prepetition Workers' Compensation Claims is essential to the continued operation of the Debtors' business, the Debtors request authority to pay any and all amounts due and owing with respect to any Workers' Compensation Program. In addition, the Debtors request authority to maintain and continue prepetition practices with respect to the Workers' Compensation Programs, including, among other things, allowing workers' compensation claimants, to the extent they hold valid Workers' Compensation Claims, to proceed with their claims under the applicable insurance policy or program. The Debtors estimate that, as of the Commencement Date, the aggregate amount that may be payable with respect to Workers' Compensation Claims is approximately $2,200,000, although such obligations would likely be paid over an extended period of time.

General Liability and Property Insurance

36. The Debtors also maintain many general liability and property insurance policies, which provide the Debtors with insurance coverage for claims relating to, among other things, general liability, automobile liability, umbrella liability, errors and omissions-technology liability, directors' and officers' liability, fiduciary liability, commercial crime, kidnap and ransom, boiler and machinery, and blanket real and personal property (the "Liability Insurance Policies"). These policies are essential to the ongoing operation of the Debtors' business.

37. The Debtors are required to pay premiums based upon a fixed rate established and billed by each Insurance Carrier. The premiums for most of the Liability Insurance Policies are determined annually and are paid at policy inception directly to the Insurance Carrier or to the Brokers[2] (who pay the Insurance Carrier). The Debtors' general

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[2] The Broker for the blanket real and personal property policy is Unimark Insurance Agency, Inc.

liability and auto policies are both fully and self-insured programs administered by Hartford, which mirrors the system described above with respect to the Workers' Compensation Programs. The aggregate annual premiums for all the Liability Insurance Policies is approximately $4,300,000.

38. The Debtors estimate that, as of the Commencement Date, approximately $500,000 is owed in respect of the Liability Insurance Programs, whether paid directly to the Broker or the Insurance Carriers.

Relief Requested

39. Pursuant to sections 105(a) and 363(b) of the Bankruptcy Code, the Debtors seek authorization to continue the Insurance Programs and Policies on an uninterrupted basis, consistent with their prepetition practices, and pay, when due in the ordinary course of business, all prepetition premiums, administrative fees, and other prepetition obligations to the Insurance Carriers and/or the Brokers to the extent due and payable postpetition. To the extent premium payments or other costs of the Insurance Programs and Policies relating to a period prior to the Commencement Date are outstanding, the Debtors seek authority to make such payments.

40. Section 363(b)(1) of the Bankruptcy Code provides "[t]he trustee, after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate." 11 U.S.C. § 363(b)(1). Section 105(a) of the Bankruptcy Code provides, in relevant part, that "[t]he court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title." Id. § 105(a).

41. In a long line of well-established cases, federal courts have consistently permitted postpetition payment of prepetition obligations where necessary to preserve or enhance the value of a debtor's estate for the benefit of all creditors. See, e.g., Miltenberger v.

Logansport Ry., 106 U.S. 286 (1882) (payment of pre-receivership claim prior to reorganization permitted to prevent "stoppage of [crucial] business relations"); Mich. Bureau of Workers' Disability Compensation v. Chateaugay Corp. (In re Chateaugay Corp), 80 B.R. 279 (S.D.N.Y. 1987), appeal dismissed. 838 F.2d 59 (2d Cir. 1988) (approving lower court order authorizing payment of prepetition, wages, salaries, expenses and benefits).

42. This doctrine of "necessity" functions in a chapter 11 reorganization as a mechanism by which the bankruptcy court can exercise its equitable power to allow payment of critical prepetition claims not explicitly authorized by the Bankruptcy Code. See In re Boston & Me. Corp., 634 F.2d 1359, 1382 (1st Cir. 1980) (recognizing the existence of a judicial power to authorize trustees to pay claims for goods and services that are indispensably necessary to the debtors' continued operation).

43. Notably, numerous courts in other large chapter 11 cases have granted the relief requested herein. See, e.g., In re WorldCom, Inc., Ch. 11 Case No. 02-13533 (AJG) (Bankr. S.D.N.Y. July 21, 2002); In re Global Crossing Ltd., Ch. 11 Case No. 02-40187 (REG) (Bankr. S.D.N.Y. January 28, 2002); In re Ames Dep't Stores, Inc., Ch. 11 Case No. 01-42217 (REG) (Bankr. S.D.N.Y. August 20, 2001); In re Casual Male Corp., Ch. 11 Case No. 01-41404 (REG) (Bankr. S.D.N.Y. May 18, 2001); In re Nextwave Personal Communications, Inc., Ch. 11 Case No. 98-21529 (ASH) (Bankr. S.D.N.Y. June 8, 1998); In re Maidenform Worldwide, Inc., Ch. 11 Case No. 97-44869 (CB) (Bankr. S.D.N.Y. July 22, 1997).

44. It is essential to the continued operation of the Debtors' business and their efforts to reorganize that the Insurance Programs and Policies be maintained on an ongoing and uninterrupted basis. The failure to pay premiums when due may affect the Debtors' ability to renew certain of the Insurance Programs and Policies, some of which are set to expire as soon as

July 1, 2003. If any of the Insurance Programs and Policies is allowed to lapse, the Debtors could be exposed to substantial liability for damages resulting to persons and property of the Debtors and others. Continued effectiveness of the directors' and officers' liability policies is necessary to maintain the retention of a qualified and dedicated senior management team. Furthermore, pursuant to the terms of many of their leases and contracts, as well as the guidelines established by the Office of the United States Trustee for the Southern District of New York, the Debtors are obligated to remain current with respect to certain of their primary insurance policies.

45. The maintenance of the Workers' Compensation Programs is indisputably justified, as applicable state law mandates this coverage. Moreover, with respect to the Workers' Compensation Claims, the risk that eligible claimants will not receive timely payments with respect to employment-related injuries could have a devastating effect on the financial well-being and morale of their employees, and their willingness to remain in the Debtors' employ. Departures by employees at this critical time may result in a severe disruption of the Debtors' business to the detriment of all parties in interest. A significant deterioration in employee morale undoubtedly will have a substantially adverse impact on the Debtors, the value of their assets and businesses, and their ability to reorganize.

46. In addition, certain Insurance Carriers are in possession of approximately $3,000,000 of irrevocable letters of credit securing certain obligations under the Insurance Programs and Policies. Accordingly, failure by the Debtors to honor their obligations under the Insurance Programs and Policies would likely result in the drawing down of these letters of credit in amounts far in excess of the currently outstanding obligations, and (in the case of the irrevocable letters of credit) would unnecessarily deplete the assets of the estate.

47. Certain of the Insurance Programs and Policies contain deductible amounts for each claim that is submitted or for the policy as a whole. To the extent a deductible payment or reimbursement relating to a period prior to the Commencement Date is outstanding with respect to any Insurance Program and Policy, the Debtors seek authority, in their sole discretion, to make such payments in the same manner that such payments were made prior to the Commencement Date.

48. In sum, the amounts the Debtors propose to pay in respect of the Insurance Programs and Policies are minimal in light of the size of the Debtors' estates and the potential exposure of the Debtors absent insurance coverage.

49. To the extent any of the Insurance Programs and Policies, or related agreements are deemed executory contracts within the meaning of section 365 of the Bankruptcy Code, the Debtors do not at this time seek to assume such contracts. Accordingly, the Debtors request if the Court authorizes the payments described above, such payment should not be deemed to constitute postpetition assumption or adoption of said programs, policies, or agreements as executory contracts pursuant to section 365 of the Bankruptcy Code.

50. Based on the foregoing, the Debtors submit the relief requested herein is necessary and appropriate, is in the best interests of their estates and creditors, and should be granted.

Waiver of Memorandum of Law

51. This Motion includes citations to the applicable authorities and does not raise any novel issues of law. Accordingly, the Debtors respectfully request that the Court waive the requirement contained in rule 9013-1(b) of the Local Bankruptcy Rules for the Southern District of New York that a separate memorandum of law be submitted.

Notice

52. Notice of this Motion has been provided to: (a) the Office of the United States Trustee for the Southern District of New York; (b) attorneys for the Prepetition Lenders; and (c) attorneys for the Ad Hoc Committee. In light of the nature of the relief requested herein, the Debtors submit that no other or further notice is required.

53. No previous request for the relief sought herein has been made by the Debtors to this or any other court.

WHEREFORE the Debtors respectfully request that the Court grant the Motion in all respects and grant the Debtors such other and further relief as it deems just and proper.

Dated: New York, New York
May 14, 2003

Respectfully submitted,

/s/ Matthew A. Cantor

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Exhibit A
Allegiance Telecom Insurance Policy Coverage

Type of Coverage	Insurance Broker Name	Insurance Broker Contact	Insurance Carrier	Policy Period Start	Policy Period Expiration	Premium Policy Period	Premium Annualized
Property - Blanket Real and Personal Property	Unimark Insurance Agency, Inc.	John Sutter 8950 N. Central Expressway Suite 302 Dallas, Texas 75231 ph: 214-891-9494 fax:214-891-9417	Liberty Mutual	Jan. 1, 2003	Sept. 30, 2003	$708,952	$945,269
General Liability	Marsh USA	Robert A. Kelly Vice President 500 West Monroe Street Chicago, IL 60661 ph:312-627-6240 fax:312-627-6257	The Hartford	Jan. 1, 2003	Aug. 31, 2003	$37,229	$55,899
Auto Liability	Marsh USA	Robert A. Kelly Vice President 500 West Monroe Street Chicago, IL 60661 ph:312-627-6240 fax:312-627-6257	The Hartford	Jan. 1, 2003	Aug. 31, 2003	$254,415	$382,005
Workers Compensation	Marsh USA	Robert A. Kelly Vice President 500 West Monroe Street Chicago, IL 60661 ph:312-627-6240 fax:312-627-6257	The Hartford	Jan. 1, 2003	Aug. 31, 2003	$390,201	$576,826
Umbrella	Marsh USA	Robert A. Kelly Vice President 500 West Monroe Street Chicago, IL 60661 ph:312-627-6240 fax:312-627-6257	St Paul (Primary), & Westchester (Excess)	Jan. 1, 2003	Aug. 31, 2003	$252,451	$378,677

Type of Coverage	Insurance Broker Name	Insurance Broker Contact	Insurance Carrier	Policy Period Start	Policy Period Expiration	Premium Policy Period	Premium Annualized
Directors & Officers	Marsh USA	Robert A. Kelly Vice President 500 West Monroe Street Chicago, IL 60661 ph:312-627-6240 fax:312-627-6257	National Union Fire Insurance Company (Primary), & Allied World Assurance Company (Excess)	July 1, 2002	July 1, 2003	$2,125,000	$2,125,000
E & O (Errors & Omissions - Technology)	Marsh USA	Robert A. Kelly Vice President 500 West Monroe Street Chicago, IL 60661 ph:312-627-6240 fax:312-627-6257	American Internationa l Specialty Lines Insurance Co (AIG)	Jan. 1, 2003	Jan. 1, 2004	$335,218	$335,218
Fiduciary Liability	Marsh USA	Robert A. Kelly Vice President 500 West Monroe Street Chicago, IL 60661 ph:312-627-6240 fax:312-627-6257	Federal insurance Company	Jan. 1, 2003	Jan. 1, 2004	$7,260	$7,260
Crime	Marsh USA	Robert A. Kelly Vice President 500 West Monroe Street Chicago, IL 60661 ph:312-627-6240 fax:312-627-6257	Continental Casualty Company	May 1, 2003	May 1, 2004	$30,000	$30,000
Kidnap & Ransom	Marsh USA	Robert A. Kelly Vice President 500 West Monroe Street Chicago, IL 60661 ph:312-627-6240 fax:312-627-6257	Liberty Insurance Underwriter s, Inc	Jan. 1, 2002	Jan. 1, 2005	pd in full	$4,000
Storage Tank (Florida Only)	Marsh USA	Robert A. Kelly Vice President 500 West Monroe Street Chicago, IL 60661 ph:312-627-6240 fax:312-627-6257	Commerce & Industry Insurance Industry	April 15, 2003	April 15, 2004	$1,000	$1,000