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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 THE DEBTORS PURSUANT TO SECTION 105(a) OF THE BANKRUPTCY CODE FOR AUTHORIZATION TO PAY PREPETITION CLAIMS OF CRITICAL VENDORS

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 $16 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 strong 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 strong nationwide direct sales force primarily focused on the small to medium sized business enterprise and efficient 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.

<u>Events Leading to Chapter 11 Filing</u>

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 EBIDTA, 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.

Critical Vendor Claims

28. As described in detail below, the Debtors purchase products and services from approximately 39 vendors that are essential and critical for the operation of their businesses (the "Critical Vendors"). The Debtors estimate that, as of the Commencement Date, the aggregate amount of unpaid prepetition claims of the Critical Vendors does not exceed $4,000,000 (the "Critical Vendor Claims").

29. The Debtors' ability to continue its operations, serve its customers, and preserve the Debtor's estates will largely depend upon the continued provision of products and services by the Critical Vendors. Ongoing maintenance and provision of such products and services by certain Critical Vendors is essential to maintaining the value of the Debtors' assets

and preserving their value as a going concern. At this precarious stage in these chapter 11 cases, an interruption in the supply of products and services by the Critical Vendors would have a severely pernicious effect on the Debtors' efforts to rehabilitate and reorganize. The provision of products and services by the Critical Vendors must continue unabated during the pendency of the Debtors' chapter 11 cases if substantial harm and loss of enterprise value is to be avoided. Consequently, the Debtors have performed an in-depth and extensive review of its vendors to determine those that are critical and necessary to avoid potentially significant disruptions to the Debtors' business operations.

30. The criteria used to determine which vendors would be deemed critical and be paid on account of prepetition amounts to avoid business interruption were as follows:

a. Unique vendors that supply specific services and/or equipment critical to the Debtors' business operations;

b. Other known suppliers, if available, that may provide similar goods and services, but historically were more expensive; and

c. The start-up and delay in time necessary for training replacement vendors was considered to determine the extent of service interruption that would occur.

31. The Debtors use the specialized products and services of Critical Vendors daily in connection with (a) the Debtors' enterprise system software (e.g., software that is crucial for functions such as billing, security, usage collection, trouble ticketing, and customer order entry), (b) the Debtors' exclusive telecommunications network, (c) the Debtors' equipment, and (d) certain other products and used or sold by the Debtors to their customers. In several instances, such Critical Vendors are the designer and/or manufacturer of the software and/or equipment at issue, and thus, are uniquely qualified and skilled to modify, install, or maintain the software, equipment, or network component at issue. In other instances, the Critical Vendor is

highly skilled and experienced in dealing with the particular software, equipment, or network component, and cannot be practicably replaced.

32. Many of the Critical Vendors are used by the Debtors to support the Debtors' billing and collection efforts. The cessation of the services provided by such Critical Vendors would have an immediate negative impact on the Debtors' estates by affecting the Debtors' ability to generate revenue. In addition, as telecommunication services providers, any disruption in the Debtors' billing software capability directly impacts on the Debtors' ability to market and maintain services to their customers.

33. The Debtors also use Critical Vendors to provide maintenance and installation services for its products and services when the Debtors are unable themselves to provide such services to their customers. For example, as part of its customer premises business, the Debtors use Critical Vendors to install and maintain customer premises equipment for customers located in areas where Debtors do not have employees. In addition, the Debtors may use Critical Vendors when the Debtors need some form of specialized work performed as part of an installation or maintenance of customer premises equipment – such as electrical contractor work. Finally, the Debtors use such Critical Vendors to perform certain kinds of installation work that the Debtors typically do not perform for customers, such as the installation of inside wire. An inability to promptly obtain such services would delay or perhaps even cancel the installation of customized networks for the Debtors' customers, resulting in a loss of business, reputation, and goodwill. Moreover, such an outcome would endanger some of the Debtors' most valuable customer relationships.

34. For those Critical Vendors that supply equipment and services resold by the Debtors to their customers, an inability to obtain such equipment and services could result in

the Debtor being in breach of their agreements with their customers and directly result in a reduction of revenue. In addition, the Debtors will be unable to respond to competitive market offers by other carriers, and as a result, the Debtors will have a higher customer churn and lower growth rate.

Relief Requested

35. By this Motion, subject to the provisions set forth herein, the Debtors request permission to pay, in the ordinary course, and in their sole discretion and business judgment, the prepetition fixed, liquidated, and undisputed Critical Vendor Claims, as more particularly described and on the terms set forth below.

36. The Debtors also request that all banks and financial institutions be authorized and directed to receive, process, honor, and pay any and all prepetition and postpetition checks drawn on the Debtors' accounts in respect of payments of Critical Vendor Claims, whether such checks were presented prior to or after the Commencement Date, except to the extent that the Debtors and the applicable financial institution agreed prior to the Commencement Date that an account on which the Debtors draw such checks could be closed.

Grounds For Relief

37. Section 105(a) of the Bankruptcy Code empowers the Court to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title." 11 U.S.C. § 105(a). A bankruptcy court's use of its equitable powers to "authorize the payment of prepetition debt when such payment is needed to facilitate the rehabilitation of the debtor is not a novel concept." In re Ionosphere Clubs, Inc., 98 B.R. 174, 175 (Bankr. S.D.N.Y. 1989). "Under Section 105, a court can permit pre-plan payment of pre-petition obligations when essential to the continued operation of the debtor." In re NVR L.P., 147 B.R. 126, 127 (Bankr. E.D. Va. 1992) (citing Ionosphere Clubs, 98 B.R. at 177).

38. The "necessity of payment" doctrine further supports the relief requested herein. This doctrine recognizes the existence of the judicial power to authorize a debtor in a reorganization case to pay prepetition claims where such payment is essential to the continued operation of the debtor. Ionosphere Clubs, 98 B.R. at 176; see also In re Chateaugay Corp., 80 B.R. 279 (S.D.N.Y. 1987). This doctrine is consistent with the paramount goal of chapter 11 - "facilitating the continued operation and rehabilitation of the debtor. . . ." Ionosphere Clubs, 98 B.R. at 176.

39. The Debtors believe that the relief requested is reasonable and necessary under the circumstances. Without a seamless continuation of the provision of products and services by the Critical Vendors after the Commencement Date, the Debtors would experience significant decreases in revenue and a notable degradation of service quality. The Payments of Critical Vendor Claims are necessary to ensure the continued support of the Critical Vendors whose assistance is vital to the Debtors' efforts to maximize the value of their estates.

40. The Debtors submit that authority to pay the Critical Vendor Claims will not create an imbalance of their cash flows because the majority of these obligations have customary payment terms and are either currently due, not significantly past due, or will not be payable immediately. Cash maintained by Debtors, together with cash generated in the ordinary course of Debtors' business, will provide more than sufficient liquidity for payment of the Critical Vendor Claims in the ordinary course of business. In addition, many of the Critical Vendors provide products and services that result in a positive cash flow for the Debtors, such as those products and services which are resold to the Debtors' customers.

41. The Debtors believe that some Critical Vendors may, among other things: (a) refuse to provide products and services; (b) refuse to provide products and services on

reasonable credit terms absent payment of prepetition claims; or (c) suffer significant financial hardship if their prepetition claims are not paid in whole or in part. In cases when a Critical Vendor either refuses to or cannot provide products and services unless payment is made, the Debtors should be able to exercise their discretion and business judgment to pay such Critical Vendor Claims.

42. The Debtors submit that the uninterrupted provision of products and services by the Critical Vendors, on customary terms, and the continuing support of their customers, are imperative to the ongoing operations and viability of the Debtors. The Debtors only seek to pay Critical Vendor Claims where nonpayment of such claims would lead to the interruption of the delivery of products and services or would seriously disrupt the Debtors' operations. Notably, the ratio of Critical Vendor Claims to the estimated total of general unsecured claims against the Debtors is approximately four tenths of one percent (4/10 of 1%). Thus, the Debtors submit that the relief requested is narrowly tailored to facilitate the Debtors' chapter 11 reorganization process.

43. Similar relief has been granted in other large chapter 11 cases in this District. 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 Nos. 02-40187 through 02-40241 (REG) (Bankr. S.D.N.Y. Jan. 28, 2002); In re Enron Corp., Ch. 11 Case No. 01-16034 (AJG) (Bankr. S.D.N.Y. Dec. 2, 2001); In re PSINet, Inc., Ch. 11 Case No. 01-13213 (REG) (Bankr. S.D.N.Y. May 31, 2001); In re AI Realty Mktg. of N.Y., Inc., Ch. 11 Case Nos. 01-40252 through 01-40290 (AJG) (Bankr. S.D.N.Y. Feb. 6, 2001); In re Indesco Int'l., Inc., Ch. 11 Case No. 00-15452 (REG) (Bankr. S.D.N.Y. Jan. 9, 2001).

44. In sum, the Debtors believe that the proposed payments of the Critical Vendor Claims are necessary for the continuing operation of the Debtors' businesses and the preservation of the Debtors' enterprise value for the benefit of their estates, creditors, and all parties in interest. The sums involved are insignificant in relation to the potential disruption that would occur if relationships with these suppliers were to be terminated. Under these circumstances, approval of payments of the Critical Vendor Claims is appropriate.

45. To implement the terms of the authority requested by the Motion, the Debtors propose that the Court enter an order (the "Order") providing authorization for the Debtors to do one or a combination of the following in order to satisfy the Critical Vendor Claims:

a. The Debtors are authorized, in their sole discretion and the exercise of their business judgment, to make payment to the Critical Vendors on the condition that (i) such a claim is paid in cash or via wire transfer, (ii) by accepting payment, the Critical Vendor agrees to maintain or reinstate customary trade terms during the pendency of these chapter 11 cases, (iii) the Critical Vendor releases, waives and otherwise relinquishes any prepetition claims such Critical Vendor might have related to the products and services for which it is receiving payment, and (iv) the Debtors mail a copy of the Order to each Critical Vendor to which any payment permitted hereunder is made;

b. A Critical Vendor's acceptance of payment is deemed to be acceptance of the terms of the Order and effects a release, waiver and relinquishment of all prepetition claims held by such Critical Vendor relating to the products and services for which it is receiving payment, and, if the Critical Vendor, thereafter, does not provide the Debtors with customary trade term during the pendency of these cases, then any payments of prepetition claims made after the Commencement Date may be deemed to be unauthorized postpetition transfers and therefore recoverable by the Debtors in these chapter 11 cases; and

c. The Debtors are authorized to obtain written verification of trade terms to be supplied by the Critical Vendors before issuing payment hereunder.

46. The Order shall not, however, be construed to limit, or in any way affect, the Debtors' ability to contest any invoice of a Critical Vendor on any grounds.

47. Nothing in this Motion should be construed as an assumption of any executory contract or unexpired lease between the Debtors and any of the Critical Vendors, nor should it be construed as a rejection of any executory contract or unexpired lease with any creditor. The Debtors are in the process of reviewing these matters and reserve all of their rights with respect to the assumption or rejection of any executory contracts or unexpired leases. Furthermore, the Debtors reserve the right to contest on nonbankruptcy grounds the amount claimed to be due by any of the Critical Vendors.

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

Memorandum of Law

49. 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

50. 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 Agent; 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.

51. No previous motion for the relief sought herein has been made 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,

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