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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

HEARING DATE: 2/19/04
AT: 10:00 A.M.

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In re: : Chapter 11
: Case No. 03-13057 (RDD)
: ALLEGIANCE TELECOM, INC., *et al.*, : (Jointly Administered)
: Debtors. :
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DEBTORS' RESPONSE TO OBJECTIONS FILED BY VERIZON COMMUNICATIONS, INC., AT&T, BELL SOUTH TELECOMMUNICATIONS, AND ABOVE NET, INC. TO THE DEBTORS' MOTION FOR AN ORDER (I) APPROVING THE SALE OF THE DEBTORS' ASSETS FREE AND CLEAR OF ALL LIENS, CLAIMS AND ENCUMBRANCES TO THE SUCCESSFUL BIDDER, (II) AUTHORIZING THE ASSUMPTION AND ASSIGNMENT OF CERTAIN EXECUTORY CONTRACTS AND UNEXPIRED LEASES, AND (III) GRANTING RELATED RELIEF

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

Allegiance Telecom, Inc. and its direct and indirect subsidiaries, as debtors and debtors-in-possession (collectively, the "Debtors"), by their co-bankruptcy counsel, Togut, Segal & Segal LLP, as and for their Response to the objections (the "Objections") filed by Verizon Communications, Inc. ("Verizon"), AT&T Communications, Inc. ("AT&T"), BellSouth Telecommunications, Inc. ("BellSouth"), and AboveNet, Inc. ("AboveNet," and together with Verizon, AT&T, and BellSouth

the “Objecting Utility Companies”), to the Debtors’ motion dated December 18, 2003 (the “Sale Motion”) for, among other things, an Order, pursuant to sections 105(a), 363, 365 and 1146(c) of the Bankruptcy Code, (i) approving the sale of the Debtors’ assets free and clear of all liens, claims, encumbrances and interests, and certain taxes; (ii) authorizing the assumption and assignment of certain executory contracts and unexpired leases; and (iii) granting certain related relief, respectfully state that:

PRELIMINARY STATEMENT¹

1. This Response incorporates by reference the discussion of factual background, auction procedures and results contained in the Debtors’ “Statement In Support of the Motion For Orders Pursuant to Sections 105(a), 363, 365 and 1146(c) of the Bankruptcy Code (A) Approving the Sale to the Successful Bidder Free and Clear of All Liens, Claims and Encumbrances, (B) Authorizing the Assumption and Assignment of Certain Executory Contracts and Unexpired Leases and (c) Granting Related Relief” previously filed with the Court by Kirkland & Ellis LLP.

THE OBJECTIONS

2. The Objecting Utility Companies object to the Sale Motion and certain provisions of the Sale Order that address the assumption and assignment procedures for executory contracts and tariffs of the Objecting Utility Companies. Verizon, and to the extent relied upon by AT&T and AboveNet, focus on seven paragraphs of the Sale Order that allegedly adversely affect their rights in connection with the assumption and assignment of their respective agreements and tariffs.

¹ Capitalized terms used herein and not otherwise defined herein shall have the meaning ascribed to such terms in the Sale Motion.

BellSouth argues that the Debtors must assume and cure any defaults under their respective tariffs prior to entry of the Sale Order.

RESPONSE

3. The Debtors are not attempting to abrogate rights of non-debtor contracts parties. The Sale Order does not contemplate the assumption and assignment of the Debtors' executory contracts, and issues regarding the assumption and/or assignment of executory contracts and the Objecting Utility Companies' tariffs (to the extent such agreements are executory contracts) are not appropriately the subject of the Sale Hearing and need not be addressed by the Court because the sale is currently structured as a stock sale. Pursuant to the XO Purchase Agreement, XO is committed to purchase the assets of Allegiance Telecom, Inc. ("ATI") and Allegiance Telecom Company Worldwide ("ATCW"), and to purchase the stock of the reorganized subsidiaries of ATCW, other than Shared Technologies, pursuant to a plan of reorganization. Accordingly, issues regarding the assumption of executory contracts and the Objecting Utility Companies' tariffs will be determined at plan confirmation, not at the Sale Hearing.

4. To the extent that the sale transaction were to proceed as an asset sale under section 363 of the Bankruptcy Code, the non-debtor contract parties would receive sufficient notice of the proposed assumption and assignment (in the event XO determines it seeks assignment of an executory contract) and the non-debtor contract party would have an opportunity to object to the proposed assumption and assignment at such time.

5. Notwithstanding the foregoing, the Debtors have agreed to revise the following provisions of the Sale Order to clarify certain provisions concerning

assumption and assignment of executory contracts that were specifically objected to by the Objecting Utility Companies:²

(a) **Paragraph 12 of the Sale Order.** The Objecting Utility Companies argue that they should have the right to contest whether their contracts may be assumed and assigned.

The Debtors have agreed to revise the Sale Order to clarify that assumption and assignment of executory contracts must be in accordance with the provisions of section 365 of the Bankruptcy Code.

(b) **Paragraph 13 of the Sale Order.** The Objecting Utility Companies argue that the assumption and assignment cannot be free and clear of “any interest of any kind or nature whatsoever”.

The Debtors have agreed to add a reference to section 363 of the Bankruptcy Code in paragraph 13 and the following clause: “provided, however, that the assignment shall not affect the rights of the non-debtor contract parties under the Assumed Contracts.”

(c) **Paragraph 14 of the Sale Order.** The Objecting Utility Companies object to the paraphrasing of 363(k) of the Bankruptcy Code and the limitation of the Debtors’ liability upon assignment.

The Debtors have agreed to add the following language to last sentence in paragraph 14: “except for any Cure Amounts that the Debtors are obligated to pay.”

(d) **Paragraph 16 of the Sale Order.** The Objecting Utility Companies object to the provision requiring the telecommunication service providers to provide services to the Buyer.

The Debtors have agreed to revise the Sale Order to provide for continuation of service to the Debtors.

(e) **Paragraph 19 of the Sale Order.** The Objecting Utility Companies object to the proposed setoff of amounts owing to the Debtors to satisfy cure amounts.

The Debtors have agreed to remove the last sentence of paragraph 19.

² These paragraphs of the Sale Order would not apply in the event it is determined that the tariffs or any other agreements of the Objecting Utility Companies are not “executory contracts”.

6. To the extent the Objecting Utility Companies' agreements with the Debtors are subject to these provisions of the Sale Order, the Debtors believe that the Objecting Utility Companies are adequately protected.

WHEREFORE, the Debtors respectfully request that the Court overrule the Objections, approve the Sale Order and grant such other and further relief as it deems just.

DATED: New York, New York
February 19, 2004

ALLEGIANCE TELECOM, INC., et al.,
Debtors and Debtors-in-Possession,
By their Co-Bankruptcy Attorneys,
TOGUT, SEGAL & SEGAL LLP,
By:

/s/ Albert Togut
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