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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

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In re: : Chapter 11
: :
ALLEGIANCE TELECOM, INC., *et al.*, : Case No. 03-13057 (RDD)
: :
Debtors. :
(Jointly Administered) :
: :
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**OBJECTION OF WORLDCOM, INC. AND CERTAIN OF
ITS AFFILIATES TO DEBTORS'
DISCLOSURE STATEMENT**

WorldCom, Inc. and certain of its direct and indirect subsidiaries (collectively, "WorldCom") hereby object to court approval of the Disclosure Statement Pursuant to Section 1125 of the Bankruptcy Code (the "Disclosure Statement") pertaining to the Joint Plan of Reorganization Pursuant to Chapter 11 of the Bankruptcy Code (the "Plan") filed by Allegiance Telecom, Inc. ("ATI"), Allegiance Telecom Company Worldwide ("ATCW"), and ATCW's direct and indirect subsidiaries (collectively, "Allegiance"), and represent as follows:

SUMMARY OF WORLDCOM'S OBJECTION

1. The Disclosure Statement does not provide adequate information, pursuant to section 1125(a) of the Bankruptcy Code, sufficient to enable a hypothetical

reasonable investor typical of holders of claims against or interests in Allegiance to make an informed judgment about the Plan. As more specifically described below, the Disclosure Statement lacks facts that are critical to WorldCom's evaluation of the Plan in general, and its expected recovery under the Plan. Allegiance has failed to provide, *inter alia*, sufficient factual detail about (1) the proposed compromises and settlements with respect to Senior Lenders¹ and ATI Note Trustees, (2) the value of the ATLT assets, (3) the liquidation value for each debtor in these chapter 11 cases, (4) the necessity of "deemed consolidation" of the ATCW Debtors, and (5) the treatment of executory contracts related to Utility Services.

INADEQUACY OF DISCLOSURE

2. Section 1125 of the Bankruptcy Code requires that a holder of a claim or interest must be given adequate information before acceptance or rejection of a plan may be solicited. That is, information must be sufficient to enable a hypothetical reasonable investor typical of holders of claims against or interest in the debtor's estate to make an informed judgment about the plan.

3. A number of courts have enumerated the types of information which should be provided in a disclosure statement.² Such information includes, *inter alia*: (1) a complete description of the available assets and their value; (2) the source of the information provided in the disclosure statement; (3) information regarding claims

¹ Unless otherwise defined herein, all capitalized terms contained herein have the meaning ascribed to them in the Plan.

² See *In re Scioto Valley Mortg. Co.*, 88 B.R. 168, 170 (Bankr. S.D. Ohio 1988)(citing *In re Inforex, Inc.*, 2 C.B.C.2d 612 (Bankr. D. Mass. 1980); *In re William F. Gable Co.* 10 B.R. 248, 249 (Bankr. N.D.W. Va. 1981); *In re A.C. Williams Co.*, 25 B.R. 173, 176 (Bankr.N.D. Ohio 1982); *In re Malek*, 35 B.R. 443, 444 (Bankr. E.D. Mich. 1983); *In re Metrocraft Publishing Services, Inc.*, 39 B.R. 567, 568 (Bankr. N.D. Ga. 1984); *In re Jeppson*, 66 B.R. 269, 292 (Bankr. D. Utah 1986).

against the estate; (4) a liquidation analysis setting forth the estimated return that creditors would receive under chapter 7; (5) any financial information, valuations or pro forma projections that would be relevant to creditors' determinations of whether to accept or reject the plan; (6) the actual or projected value that can be obtained from avoidable transfers; (7) the existence, likelihood and possible success of non-bankruptcy litigation; (8) the relationship of the debtor with affiliates; and (9) an estimate of all administrative expenses, including attorneys' fees and accountants' fees. Allegiance's Disclosure Statement either omits this information entirely or gives only a cursory explanation.

4. There are four cornerstones of the Plan: (a) the asset sale to XO Communications, Inc. ("XO"); (b) the creation of ATLT; (c) the compromises and settlements involving the Senior Lenders and ATI Note Trustees; and (d) the "deemed consolidation" of the ATCW Debtors. Although a hypothetical reasonable investor would require disclosure of all material facts related to these components in order to make an informed decision regarding the Plan, Allegiance has left creditors with nothing more than guesswork on the following issues, among others.

5. The Value of XO Stock – By Allegiance's own admission, "the value of XO Common Stock has fluctuated materially over time, reaching a value as low as \$3.00 per share and as high as \$8.36 per share." Allegiance also discloses that an entity owned and controlled by Mr. Carl Icahn is the majority shareholder of XO; these shares either do not trade or have historically traded in only very small amounts in the public market. Allegiance has not disclosed how many shares of XO stock are currently traded by the public, the source of the shares offered in exchange for

Allegiance assets, and whether the current value of XO stock will be significantly diluted by such shares. In light of the fact that XO's market capitalization has decreased by approximately \$100 million in the weeks following this Court's approval of the Sale Transaction, the market appears to expect a substantial dilution of XO's stock value.

6. The Liquidating Trust – The ATLT will consist of the XO Common Stock, the New STFI Common Stock, the Available Cash, and Allegiance's causes of action. It will also own assets excluded from the XO Asset Purchase Agreement. Neither the Plan nor the Disclosure Statement provides a valuation of these assets. The value of the ATLT Certificates that are likely to be distributed to holders of Class 4 and Class 5 Unsecured Claims is inextricably tied to the value of the ATLT assets. Without any estimate of the ATLT assets, unsecured creditors are at a loss when trying to evaluate their expected distribution under the Plan.

7. The Compromises and Settlements –According to the Disclosure Statement, the ATI Notes are obligations solely of ATI and are not guaranteed by any of the ATCW Debtors. Further, ATI appears to have no assets with which to satisfy claims other than the stock of ATCW. Nevertheless, the Plan creates a classification scheme based on the incorporation of certain compromises and settlements with the ATI Note Trustees and the Senior Lenders. Allegiance posits, without further explanation, that the “terms of the Plan represent a fair and equitable compromise and settlement” with respect to the issues and disputes among Allegiance, the Senior Lenders and the ATI Note Trustees. Creditors, however, are forced to accept this proposition on blind faith given that Allegiance fails to disclose how these

compromises and settlements are incorporated into the Plan and how they impact the ultimate recovery of the remaining creditors. Nothing in the Plan or Disclosure Statement indicates how these compromises are actually “fair” or “equitable.” Based on the limited information available, it appears that the compromise contemplated in the Plan provides ATI Note Claims with approximately \$26 million in value from the Senior Lenders while the remaining creditors will contribute one-half of their expected distributions to structurally subordinate ATI noteholders. Plainly, additional disclosure is needed as to just how this compromise is fair and equitable to creditors other than the Senior Lenders and ATI noteholders.

8. Intercompany Claims and “Deemed Consolidation” – Allegiance provides no justification for its “deemed consolidation” of the ATCW Debtors for distribution purposes. Rather, Allegiance states only that the “books and records of the Debtors reflect a large amount of Intercompany Claims,” a fact to which Allegiance devotes a single sentence. Because the Disclosure Statement lacks details about the Intercompany Claims, how values are assigned among the debtor entities, how Intercompany Claims are settled, and why deemed consolidation is necessary or justified, the Disclosure Statement cannot be approved.³

9. Executory Contracts – With respect to executory contracts, the Disclosure Statement fails to identify those to be assumed and rejected. Rather,

³ *Eastgroup Properties v. Southern Motel Ass’n*, 935 F.2d 245, 248 (11th Cir. 1991); *In re Augie/Restivo Baking Co.*, 860 F.2d 515, 518 (2d Cir. 1988) (recognizing that substantive consolidation “must be used sparingly”); *In re Flora Mir Candy Corp.*, 432 F.2d 1060, 1062 (2d Cir. 1970) (holding that substantive consolidation “is no mere instrument of procedural convenience . . . but a measure vitally affecting substantive rights”); *In re United Stairs Corp.*, 176 B.R. 359, 368-69 (D.N.J. 1995) (stating that substantive consolidation “should be considered with extreme caution and granted only in extraordinary situations”).

Allegiance simply refers to Schedules 1 through 5 which are “to come.” In Section 6.2 of the Plan, however, Utilities are obligated to continue to provide services to Allegiance, the Reorganized Debtors, or XO without interruption. The Disclosure Statement lacks any explanation of the relationship between the provisions governing contract rejection and those governing Utilities.

10. Valuations and Distributions – In addition to the points raised above, Allegiance has also failed to estimate the amount of ATCW Unsecured Claims, the percentage recovery of allowed ATCW or ATI Unsecured Claims, and the administrative priority claims it expects to incur. Allegiance also fails to provide a complete liquidation analysis.

CONCLUSION

For the foregoing reasons, WorldCom respectfully requests that this Court deny approval of the Disclosure Statement.

Dated: April 13, 2004
Houston, Texas

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