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UNITED STATES BANKRUPTCY COURT
 SOUTHERN DISTRICT OF NEW YORK

—	X	
In re	:	
	:	Chapter 11 Case No.
Allegiance Telecom, Inc., <u>et al.</u> ,	:	03-13057 (RDD)
	:	
Debtors.	:	Jointly Administered
—	X	

**FIRST SUPPLEMENTAL AFFIDAVIT OF MATTHEW A. CANTOR
 IN SUPPORT OF APPLICATION SEEKING ENTRY OF AN
 ORDER AUTHORIZING THE EMPLOYMENT AND RETENTION
 OF KIRKLAND & ELLIS AS ATTORNEYS FOR THE DEBTORS**

Matthew A. Cantor, being duly sworn, hereby deposes and says:

1. I am a partner of Kirkland & Ellis (K&E), Citigroup Center, 153 East 53rd Street, New York, New York 10022-4611. I am admitted to practice in the Southern District of New York and the Eastern District of New York.

2. On May 14, 2003, the Debtors¹ filed with this Court the application (the “Application”) of Allegiance Telecom, Inc. and its direct and indirect subsidiaries, as debtors and debtors in possession (collectively, the “Debtors”), for approval of the Debtors’ retention of K&E,

¹ Unless otherwise defined herein, capitalized terms shall have the meanings ascribed to them in the Original Affidavit.

as their attorneys in these chapter 11 cases, at their normal hourly rates in effect from time to time and in accordance with their normal reimbursement policies, in compliance with sections 328(a), 329 and 504 of title 11 of the United States Code (the“Bankruptcy Code”).

3. On May 14, 2003, K&E filed with this Court the Affidavit of Matthew A. Cantor in support of Application Seeking Entry of an Order Authorizing the Employment and Retention of Kirkland & Ellis As Attorneys for the Debtors (the“Original Affidavit”).

4. On June 11, 2003, Akin Gump Strauss Hauer & Feld LLP, on behalf of the statutory committee of unsecured creditors appointed in these chapter 11 cases, filed an objection to the Application asserting that K&E is not disinterested as required under the Bankruptcy Code (the“Committee Objection”). The Committee Objection alleged that K&E failed to disclose certain significant past and present connections to major parties interested in the chapter 11 cases.

5. I, along with all of the attorneys at K&E, take the disclosure rules set forth in rule 2014(a) of the Bankruptcy Rules very seriously and the inadvertent failure to disclose any connections in the Original Affidavit is of great concern to me and my colleagues. In that regard, after receiving the Committee Objection, I reviewed it with extreme care and immediately commenced the process of investigating the allegations asserted therein to determine whether additional disclosures needed to be made. In accordance with such investigation, I became aware that certain connections and information inadvertently was not disclosed. To remedy this, and with deep respect for this Court and the disclosure rules governing the retention of professionals in chapter 11 cases, I have prepared this Supplemental Affidavit.

6. Specifically, I submit this Supplemental Affidavit in connection with the Application to provide additional disclosure required under rules 2014(a) and 2016(b) of the Federal Rules of Bankruptcy Procedure (the“Bankruptcy Rules”). Unless otherwise stated in this Affidavit, I have personal knowledge of the facts set forth herein. To the extent any information disclosed herein requires amendment or modification upon K&E’s completion of further review or as additional party-in-interest information becomes available to it, a supplemental affidavit will be submitted to the Court reflecting such amended or modified information.

7. None of the additional representations described herein are materially adverse to the interests of the Debtors’ estates or any class of creditors or equity security holders thereof. Moreover, pursuant to section 327(c) of the Bankruptcy Code, K&E is not disqualified from acting as the Debtors’ counsel merely because it represents creditors, equity security holders, and/or other parties in interest in matters unrelated to these chapter 11 cases.

8. K&E will periodically review its files during the pendency of these chapter 11 cases to ensure that no conflicts or other disqualifying circumstances exist or arise. If any new relevant facts or relationships are discovered or arise, K&E will use its reasonable efforts to identify any such further developments and will promptly file a supplemental affidavit as required by Bankruptcy Rule 2014(a).

9. In connection with the preparation of the Original Affidavit, K&E conducted an extensive conflicts search for all known or potential conflicts. Notwithstanding this extensive search, certain potential conflicts were not identified or were inadvertently omitted from the Original Affidavit. This Affidavit supplements the Original Affidavit to include additional disclosures.

Additional Disclosures

10. Over the last several years, certain partners of K&E have organized investment entities to passively invest in a diversified group of high-quality, professionally-managed venture capital, LBO and private equity funds (PEFs) formed by some of K&E's venture capital and private equity clients. One of the PEFs, *i.e.*, K&E Partners/Venture 21, which is an Illinois general partnership formed in 1995 and comprised of certain K&E partners (the '95 PEF),² owns a limited partnership interest in Madison Dearborn Capital Partners II, L.P. (the 'MDCP II Fund'), a private equity fund - and equity holder of the Debtors (as described in paragraph 13 of the Original Affidavit)- that makes investments in a variety of companies. The 95 PEF committed to invest \$2 million in the MDCP II Fund, which had a total commitment of \$925.2 million. In that regard, the \$2 million commitment of the 95 PEF represents 0.216169% of the total commitments made to the MDCP II Fund. Importantly, the 95 PEF does not—and, therefore, K&E partners do not—have any management or control rights over the investment decisions made by the MDCP II Fund. In 1997, the MDCP II Fund invested \$18,174,579 in Allegiance Telecom, Inc.³ As of March 31, 2003, the current market value of the MDCP Fund's investment in the Allegiance Telecom, Inc. was approximately \$1,801,000.⁴ Accordingly, the

² Neither Jonathan S. Henes nor I, the two partners primarily responsible for the representation of the Debtors in these chapter 11 cases, invested in the 95 PEF.

³ See paragraph 11 below for the disclosure that K&E represented Madison Dearborn in this investment.

⁴ Despite the current market value, the Debtors are hopelessly insolvent. In that regard, the Debtors have distributed to their senior secured lenders and the Committee a proposal, on a confidential basis, that provides for the cancellation of all equity interests. In addition, on June 17, 2003, Jonathan S. Henes, a partner of K&E, sent a letter to Pamela Lustrin, of the United States Trustee's office for the Southern District of New York, responding to a request by certain shareholders for the appointment of an equity committee in these chapter 11 cases, provided that the Debtors are hopelessly insolvent.

market value of the 95 PEF's investment in the MDPC II Fund as it relates to Allegiance Telecom, Inc. was approximately \$3,900 as of March 31, 2003.⁵

11. In the Original Affidavit, I disclosed that K&E represented (a) Madison Dearborn in connection with corporate and litigation matters unrelated to the Debtors; (b) Morgan Stanley in connection with corporate, intellectual property and litigation matters unrelated to the Debtors and (c) Frontenac Company and its affiliates ('Frontenac') in connection with corporate matters unrelated to the Debtors. In addition to the foregoing types of representation, K&E may have periodically represented or may periodically represent the aforementioned entities in connection with bankruptcy, tax, real estate and other matters unrelated to the Debtors. In addition, although currently not representing the foregoing entities in any matters related to the Debtors, in 1997, K&E, including Mark Tresnowski, the current Executive Vice President and General Counsel of the Debtors, who, at the time, was a partner of K&E, represented a group of investors, including Madison Dearborn, Morgan Stanley and Frontenac, in the consummation of their private equity investment in Allegiance, which closed on August 13, 1997.

12. None of the K&E attorneys primarily responsible for representing the Debtors in these chapter 11 cases, i.e., Jonathan S. Henes, Samuel Kohn, Ludmila Chuplygina, Michael Frishberg or I, were involved in the representation of the group of investors described in paragraph 11 herein. All partners and associates of K&E that were involved in such representation will be screened from K&E's representation of the Debtors. To the best of my

⁵ Eighty K&E partners invested in the 95 PEF. As a result, if K&E partners who invested in the 95 PEF were the owners of the Debtors' securities, which they are not, the average current value of the securities owned by each partner would be approximately \$48.75.

knowledge, there are no actions by Madison Dearborn, Morgan Stanley or Frontenac pending against the Debtors relating to the foregoing investment or any other matter.

13. Paul J. Finnegan, one of the members of the Debtors' board of directors, is a managing director of Madison Dearborn. James E. Crawford, who I disclosed in the Original Affidavit is a board member and a client of K&E in matters unrelated to the Debtors, is a managing director of Frontenac. In its capacity as attorneys for the Debtors, K&E has been providing and will continue to provide legal advice to members of the Debtors' board of directors in connection with these chapter 11 cases.

14. In the Original Affidavit, I disclosed the percentage of K&E's gross revenues relating to parties in interest in these chapter 11 cases that accounted for more than .99% of K&E's gross revenues. In addition to such disclosure, the percentage at K&E's gross revenue for the fiscal year ending March 31, 2003 relating to the representation of Frontenac was approximately 0.29%.⁶

15. As I disclosed in the Original Affidavit, K&E will not represent the Conflict Parties, which include Madison Dearborn and Morgan Stanley, in any matters relating to the Debtors and K&E will not represent the Debtors in any matters related to the Conflicts Parties. In addition, K&E will not represent Frontenac in any matters related to the Debtors and K&E will not represent the Debtors in any matters related to Frontenac.

16. In the chapter 11 cases of Focal Communications Corporation and its subsidiaries (In re Focal Communications Corporation, et al., Case No. 02-13709(KJC)), K&E disclosed, out of an abundance of caution, that it represented James N. Perry, Jr. in certain

⁶ In paragraph 12 of the Original Affidavit, I disclosed K&E's representation of Frontenac. However, because Frontenac does not represent more than 1% of K&E's annual gross revenues, I did not disclose Frontenac's percentage of K&E's annual gross revenues in the Original Affidavit.

corporate and transactional matters. Mr. Perry is a current member of the Debtors' Board of Directors and a principal of Madison Dearborn. Prior to the commencement of these chapter 11 cases, K&E conducted a thorough and extensive conflicts search and determined that there were no open client matters for Mr. Perry. Subsequent to this conflicts search, K&E conducted an additional search for any open client matters for Mr. Perry and I sent an email to all attorneys of K&E to determine if any attorney was representing Mr. Perry in an individual capacity. This additional search determined, once again, that there are no open client matters for Mr. Perry. Accordingly, K&E has determined that no disclosure regarding Mr. Perry's representation is necessary. In an abundance of caution, it is important to note that certain K&E attorneys may have provided legal advice to Mr. Perry, on an ad hoc basis and without opening a formal client matter, (a) individually on personal matters, (b) in his capacity as a principal of Madison Dearborn in connection with the Debtors and other matters, and (c) in his capacity as a member of the board of directors of the Debtors.

17. In February 1999, the Debtors employed Mark B. Tresnowski as Executive Vice President and General Counsel. Prior to such employment, Mr. Tresnowski was a partner of K&E. Mr. Tresnowski has received all capital he contributed to K&E. In that regard, Mr. Tresnowski does not have an economic interest in K&E, other than a continued right to payments arising pursuant to a special contingency fee arrangement. This continued right to payments is an interest in revenue that was earned by K&E during Mr. Tresnowski's tenure at K&E and prior to his departure in 1999. Moreover, during Mr. Tresnowski's tenure at K&E, Mr. Tresnowski made certain contributions to a Defined Contribution Retirement Plan sponsored by K&E (the "DC Plan"). Mr. Tresnowski's contributions to the DC Plan have fully vested and K&E's financial performance does not have any impact thereon. Mr. Tresnowski also made

contributions to a 401(k) Plan sponsored by K&E. These contributions have been ‘rolled over’ into an Individual Retirement Account, which is in no way connected to K&E. In addition to the foregoing, Mr. Tresnowski invested in a PEF formed by certain K&E partners in 1997. Mr. Tresnowski’s interest in the PEF is in no way affected by K&E’s financial performance.

18. In the Original Affidavit, I disclosed that William S. Kirsch, a partner at K&E, is the outside general counsel of Madison Dearborn and, as a result, will not work on any matters for the Debtors during the pendency of these chapter 11 cases. In addition, and as a clarification, Mr. Kirsch will not represent Madison Dearborn in any matters related to the Debtors or these chapter 11 cases.⁷

⁷ In paragraph 15 of the Original Affidavit, I disclosed that K&E would not represent, among others, Madison Dearborn in any matters relating to the Debtors and K&E would not represent the Debtors in any matters related to, among others, Madison Dearborn.

Pursuant to 28 U.S.C. § 1746, I declare under penalty of perjury that the foregoing
is true and correct.

/s/ Matthew A. Cantor
Matthew A. Cantor
Kirkland & Ellis
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(212) 446-4800
(212) 446-4900 (fax)

Subscribed and sworn to before me on
this 20th day of June, 2003.

/s/ Nathanael F. Meyers
Notary Public
State of New York
No. 01ME5057476
My Commission Expires: March 25, 2004