



**IMPALA
PARTNERS, LLC**

Impala Partners, LLC
18 Marshall Street
Suite 112
Norwalk, Connecticut 06854

July 11, 2003

Dan Yost
President and COO
Allegiance Telecom, Inc.
9201 N. Central Expressway
Dallas, Texas 75231

Dear Dan:

This letter agreement (this "Agreement") confirms the engagement of Impala Partners, LLC ("Impala") to serve as the chief restructuring officer of Allegiance Telecom, Inc., a Delaware corporation and its subsidiaries and affiliates (collectively, the "Company"), in connection with the financial restructuring of the Company (the "Restructuring").

The Company is presently operating as debtor in possession in a case pending under Chapter 11 of Title 11 of the United States Code, 11 U.S.C. § 101, et seq. (the "Bankruptcy Code") before the United States Bankruptcy Court for the Southern District of New York (the "Bankruptcy Court") under Case No. 03-13057 (RDD). It is understood and agreed by Impala and the Company that the obligations of each party hereto is subject to the approval of the Bankruptcy Court. Within ten (10) business days after the execution and delivery of this Agreement, the Company shall file with the Bankruptcy Court motion papers requesting an order authorizing and approving this Agreement and its terms and conditions. The order authorizing this Agreement must be acceptable to Impala in its sole discretion and shall approve the terms of this Agreement, including, without limitation, that: (i) Impala shall not be required to maintain time records or file fee applications with the Bankruptcy Court for payment, (ii) Impala shall be paid in accordance with the terms of this Agreement without further application to the Bankruptcy Court, and (iii) all obligations of the Company hereunder to Impala (including any indemnification obligations of the Company contained in Section 14 hereof) shall be afforded administrative expense priority status.

Services. Impala shall serve as the Company's chief restructuring officer and provide advice and information to the Company in connection with the Restructuring. Impala's specific responsibilities are set forth below in paragraph 5. Impala shall report to the Company's special restructuring committee of independent directors of the board

of directors (the "Special Committee") and shall include in such reporting those members of management as directed by the Special Committee.

1. Term. The term of this Agreement shall commence on the date of approval of this Agreement by the Bankruptcy Court (the "Effective Date") and shall continue in full force and effect until the date that is one (1) year thereafter, subject to earlier termination pursuant to Sections 2 or 9 hereof or extension of such period by written agreement executed by Impala and the Company (the "Term").

2. Compensation for Services.

(a) As compensation for Impala's services under this Agreement, the Company shall pay to Impala a fee of \$ 250,000 for each 30 days work (a "monthly fee payment"), payable in advance. The first payment shall be due by the Company and payable to Impala on the Effective Date and each monthly fee payment shall be due and payable 30 days thereafter.

(b) As additional compensation for Impala's services under this Agreement the Company agrees to pay, subject to Bankruptcy Court approval, to Impala a mutually acceptable success fee (the "Success Fee"). The terms of the Success Fee shall be negotiated and agreed between the Company and Impala during the first forty-five days following the Effective Date. If the parties are unable to agree upon such Success Fee within forty-five days of the Effective Date, either party shall have the right to terminate this agreement, in which case the Company shall have no obligation with regard to the Success Fee. After the Company and Impala agree on the Success Fee, but prior to filing an application with the Bankruptcy Court to approve the Success Fee, the Company and Impala shall consult with the Company's lenders, the creditors committee and the United States Trustee for the Southern District of New York (the "U.S. Trustee") regarding the Success Fee and the justification for the Success Fee. To the extent the Company's lenders, the creditors committee and/or the U.S. Trustee have any issues or concerns with respect to the Success Fee, the Company and Impala shall, for a period of ten days, attempt to resolve with the Company's lenders, the creditors committee and/or the U.S. Trustee, in good faith, such issues and/or concerns. If the Company and Impala are not able to resolve such issues and/or concerns with the Company's lenders, creditors committee and/or the U.S. Trustee within such ten day period, Impala may file an application with the Bankruptcy Court to approve the Success Fee on no less than twenty days notice. Notwithstanding the foregoing, the Success Fee shall be payable in accordance with the requirements of section 330 of the Bankruptcy Code.

3. Expense Reimbursement. In addition to the monthly fee payments and Success Fee, the Company agrees to reimburse Impala for all reasonable out-of-pocket expenses incurred by Impala in carrying out the terms of this Agreement, including communication charges, travel expenses, copying expenses, delivery and distribution charges, and reasonable fees and expenses of legal counsel that Impala determines is required to advise Impala in connection with carrying out its duties under this

Agreement; provided, however, that a request for any such fees and expenses must be filed in the Company's chapter 11 cases pending in the United States Bankruptcy Court for the Southern District of New York in accordance with the "order establishing procedures for the compensation of professionals" entered therein. All reimbursements shall be made promptly after such payments accrue and are submitted to the Company with appropriate documentation for payment hereunder.

4. Access to Information. Subject to paragraph 8 herein, the Company agrees to furnish, or cause to be furnished, to Impala such current, historical and projected financial information and other information regarding the business of the Company as Impala may request from time to time. The Company agrees to make available to Impala such representatives of the Company, including, among others, directors, officers, employees, outside counsel and independent certified accountants, as Impala may request from time to time. The Company represents and warrants to Impala that all such information provided to Impala will be as complete and correct as possible under the circumstances and will not contain any known untrue statements of material fact or omit to state a known material fact necessary in order to make the statements therein not misleading in light of the circumstances under which the statements are made. The Company agrees to keep Impala advised of all developments materially affecting the Company or its financial or legal position. The Company represents and warrants to Impala that any projections or other information provided to Impala will have been prepared in good faith and will be based upon assumptions which, in light of the circumstances under which they are made, are reasonable. The Company acknowledges and agrees that, in rendering its services hereunder, Impala will be using and relying on the information provided to it by the Company and its representatives without independent verification by Impala. Impala does not assume responsibility for the accuracy or completeness of any of such information.

5. Role as Advisor. It is hereby agreed by the Company and Impala, that in performing its services under this Agreement, Impala is not assuming any responsibility for the Company's decision to pursue (or not to pursue) any business strategy or to effect (or not to effect) any Transaction. It is further agreed that neither Impala nor any other Indemnified Party (as hereinafter defined) shall be liable to the Company or any affiliate of the Company in connection with any matter arising out of or relating to the engagement of Impala under this Agreement, or any actions taken or omitted to be taken, services performed or matters contemplated by or in connection with this Agreement, except to the extent that such liability is finally judicially determined to have resulted primarily from the willful misconduct or gross negligence of such Indemnified Party. Impala's primary responsibility is to advise on the operational restructuring of the Company, including but not limited to (a) the reduction of costs and increase in efficiencies; (b) the improvement in sales productivity and profitability; (c) management of the "operational bankruptcy task forces" established within the Company; and (iv) developing the Company's long-term business strategy.

6. Advice. Any opinions or advice (whether written or oral) rendered by Impala pursuant to this Agreement are intended solely for the benefit and use of the Company, and, except as may be required by law or court order and after prior notice thereof to Impala, may not be publicly disclosed in any manner or made available to third parties (other than the Company's management, directors, accountants and attorneys) without the prior written consent of Impala (which consent shall not be unreasonably withheld).

7. Communications with Creditors. Impala agrees that the work product it produces shall be shared with the Company's lenders, the creditors committee and their respective counsel and advisors (collectively, the "Interested Parties"), subject to appropriate confidentiality measures as it relates to members of the creditors committee that are competitors of the Company. In addition, as an officer of the Company, serving at the pleasure of the Special Committee, Impala shall communicate with the Interested Parties. Impala agrees to (a) maintain a log of all communications, both verbal and written, with the Interested Parties, (b) respond promptly to inquiries made by the Interested Parties and (c) promptly report to the Special Committee regarding all communications with the Interested Parties.

8. Confidentiality. All information provided by the Company to Impala will be considered as confidential information and shall be maintained as such by Impala, except to the extent that Impala shall be required to disclose such information pursuant to the laws, rules or regulations of any governmental authority, by compulsion of civil or criminal process or by any court of competent jurisdiction acting pursuant to its powers. It is understood and agreed that confidential information shall not include any information provided by the Company to Impala that: (a) is known to Impala prior to disclosure thereof by the Company, (b) hereafter becomes, other than through no fault of Impala, generally available to the public, (c) is disclosed to Impala by a third party other than in breach of an obligation of confidentiality owed by such third party to the Company, or (d) is independently developed by Impala.

9. Termination. The Company or Impala may, at any time, terminate the Term and this Agreement, without liability or continuing obligation, by providing thirty (30) days prior written notice thereof to the other party; provided, however, that except as otherwise provided in Section 2 as to the Success Fee, no termination of the Term and this Agreement pursuant to this Section 9 or expiration of the Term pursuant to Section 2 shall affect Impala's right to receive, and the Company's obligation to provide: (a) indemnification pursuant to Section 13 of this Agreement; or (b) the payments required by Sections 2(b) and 3 of this Agreement. To the extent the Agreement is terminated, Impala shall reimburse the Company for any payments received that are not yet earned.

10. Governing Law; Jurisdiction. THIS AGREEMENT SHALL BE GOVERNED BY THE LAWS OF THE STATE OF NEW YORK, WITHOUT REGARD TO SUCH STATE'S RULES CONCERNING CONFLICTS OF LAWS. EACH OF THE COMPANY

AND IMPALA WAIVES ANY RIGHT TO TRIAL BY JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM (WHETHER BASED UPON CONTRACT, TORT OR OTHERWISE) RELATED TO OR ARISING OUT OF THE ENGAGEMENT OF IMPALA PURSUANT TO, OR THE PERFORMANCE BY IMPALA OF THE SERVICES CONTEMPLATED BY, THIS AGREEMENT. THE BANKRUPTCY COURT SHALL HAVE EXCLUSIVE JURISDICTION TO ADJUDICATE ALL MATTERS PERTAINING TO THIS AGREEMENT.

11. Attorneys' Fees and Court Costs. If the Company brings an action directly or indirectly against Impala based on this Agreement or the matters contemplated hereby, and Impala prevails in such action, Impala shall be entitled to recover, in addition to any other appropriate amounts, its reasonable costs and expenses in connection with such action, including but not limited to, reasonable attorneys' fees and court costs.

12. Successors. The provisions hereof shall inure to the benefit of and be binding upon the successors and permitted assigns of the Company and Impala. Neither party hereto may assign or otherwise transfer any of its rights or obligations under this Agreement with the prior written consent of the other party hereto.

13. Indemnification. The Company agrees to indemnify and hold harmless Impala and each of its members, managers, officers, agents, employees and controlling persons (within the meaning of the Securities Act of 1933, as amended) (each, an "Indemnified Person") in accordance with the indemnification provisions attached hereto as Exhibit A.

14. Survival. The provisions of Sections 2(b), 3, 5, 6, 7, 8, 10, 11, 12 and 13 and this Section 14 shall survive the termination and expiration of the Term and this Agreement.

If the foregoing correctly sets forth the understanding between us, please so indicate on the enclosed signed copy of this Agreement in the space provided therefor and return it to us, whereupon this Agreement shall constitute a binding agreement between us. For the convenience of the parties, any number of counterparts of this Agreement may be executed by the parties hereto. Each such counterpart shall be, and shall be deemed to be, an original instrument, but all such counterparts taken together shall constitute one and the same Agreement.

Very truly yours,

IMPALA PARTNERS, LLC

By: Paul Street
Title: Member

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AGREED TO AND ACCEPTED
as of the date first above written:

Allegiance Telecom, Inc.

By: Mark Tresnowski

Title: Executive Vice President and General Counsel

Exhibit A

1. To the extent consistent with the Company's obligations to indemnify its officers and directors, the Company agrees to indemnify and hold harmless Impala and each of its members, managers, officers, agents, employees and controlling persons (within the meaning of the Securities Act of 1933, as amended) (each, an "Indemnified Person") against any losses, claims, damages or liabilities (or actions or proceedings in respect thereof) brought by any third party (i.e., a person not a party to this Agreement or an Indemnified Party hereunder) arising out of or related to this Agreement, any actions taken or omitted to be taken by an Indemnified Party (including acts or omissions constituting ordinary negligence) in connection with this Agreement and will reimburse each Indemnified Person for all reasonable legal and other expenses as incurred in connection with investigating or defending any such loss, claim, damage, liability, action or proceeding; provided, however, that the Company will not be liable in any such case for losses, claims, damages, liabilities or expenses which are finally judicially determined to have resulted primarily from the gross negligence or willful misconduct of any Indemnified Party. In case any proceeding shall be instituted involving any Indemnified Party, such person shall promptly notify the Company, and the Company, upon the request of the Indemnified Party, shall retain counsel reasonably satisfactory to the Indemnified Party to represent the Indemnified Party and any others the Company may designate in such proceeding and shall pay all reasonable fees and expenses of such counsel related to such proceeding. In any such proceeding, any Indemnified Party shall have the right to retain its own counsel at its own expense, except that the Company shall pay as incurred the fees and expenses of counsel retained by the Indemnified Party only in the event that (i) the Company and the Indemnified Party shall have mutually agreed to the retention of such counsel, or (ii) the named parties to any such proceeding (including any impleaded parties) include both the Company and the Indemnified Party and representation of both parties by the same counsel would be inappropriate, in the reasonable opinion of the Company, due to actual or potential differing interests between them.

2. The Company will not, without the prior written consent of Impala, settle or compromise or consent to the entry of any judgment in any pending or threatened claim, action, suit or proceeding in respect of which indemnification may be sought hereunder unless such settlement, compromise or consent includes an unconditional release of each party for which indemnification is sought hereunder from all liability arising out of such claim, action, suit or proceeding.

3. In the event that the indemnity provided for in paragraph 1 hereof is unavailable or insufficient to hold any Indemnified Party harmless, then the Company shall contribute to amounts paid or payable by an Indemnified Party in respect of such Indemnified Party's losses, claims, damages and liabilities as to which the indemnity provided for in paragraph 1 hereof is unavailable or insufficient, except for acts of gross negligence or willful misconduct, (i) in such proportion as appropriately reflects the relative benefits received by the Company, on the one hand, and Impala, on the other hand, in connection with the matters as to which such losses, claims, damages or

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liabilities relate, or (ii) if the allocation provided by clause (i) above is not permitted by applicable law, in such proportion as appropriately reflects not only the relative benefits referred to in clause (i) but also the relative fault of the Company, on the one hand, and Impala, on the other hand, as well as any other equitable considerations. The amounts paid or payable by a party in respect of losses, claims, damages and liabilities referred to above shall be deemed to include any reasonable legal or other fees and expenses incurred in defending any litigation, proceeding or other action or claim.