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**UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF TEXAS
Dallas Division**

IN RE:)
) **Bankruptcy Case**
VARTEC TELECOM, INC., et al.,) **No. 04-81694-SAF-11**
) **Jointly Administered**
Debtors.)

**OBJECTION OF TDS TELECOMMUNICATIONS CORPORATION TO DEBTORS’
MOTION FOR AUTHORITY TO SELL ASSETS FREE AND CLEAR OF ALL LIENS,
CLAIMS, RIGHTS, INTERESTS, AND ENCUMBRANCES AND FOR RELATED
RELIEF (SUBSTANTIALLY ALL OF THE DEBTORS’ REMAINING ASSETS); AND
MOTION TO COMPEL ASSUMPTION OF EXECUTORY CONTRACTS**

TDS TELECOMMUNICATIONS CORPORATION, on behalf of itself and its affiliated entities identified on Exhibit “A” hereto (collectively, “TDS”), by counsel, WILEY REIN & FIELDING LLP, hereby files this Objection to the Debtors’ Motion for Authority to Sell Assets Free and Clear of All Liens, Claims, Rights, Interests, and Encumbrances and for Related Relief (Substantially All of the Debtors’ Remaining Assets) (“Sale Motion”), and moves this Court to compel the Debtor to assume or reject its executory contracts with TDS in accordance with Section 365 of the Bankruptcy Code, stating as follows:

I. Preliminary Statement.

Approval of the proposed sale would violate Section 365 of the Bankruptcy Code by, *inter alia*, allowing Leucadia to receive the benefits of the Debtors’ contracts with TDS without cure, formal assumption and assignment. Consummation of the proposed sale without resolution of TDS’ arguments herein may as a practical matter extinguish TDS’ setoff rights related to the

unassumed contracts without providing due process of law. The proposed sale likewise violates TDS' tariffs and applicable regulations by not requiring assumption of underlying indebtedness owed to TDS prior to transfer of Vartec's customer accounts to or for the benefit of Leucadia. Further, the Court must resolve substantive issues pertaining to the assumption, rejection and proposed performance by Leucadia of TDS' contracts prior to or in conjunction with its consideration of the proposed sale, or any objection of TDS to same will be rendered moot upon consummation of the sale. The Debtors have already had ample time to review their contracts, and the services rendered by TDS are essential to the business Leucadia is purchasing. Therefore, the Court should set a short deadline – no later than the date any sale is approved – for the Debtors to assume and assign, or reject the TDS Contracts (hereafter defined) that is sufficiently in advance of any action on the proposed sale to permit TDS to respond to any such proposal on an informed basis.

II. Background.

1. TDS is an independent local exchange carrier (“ILEC”) that provides telecommunications services to the Debtors, including switched access, special access, and Customer Account Record Exchange (CARE), as well as billing and collection services.

2. Specifically, TDS and the Debtors are parties to an Agreement for Billing and Collection Services, dated February 1998 (“B & C Contract”) whereby TDS purchases accounts receivable from the Debtors, and invoices the Debtors' end users for payment of the Debtors' services. True-up adjustments are conducted based upon, *inter alia*, TDS' reimbursement rights that are applicable in the event collections are less than the amounts paid by TDS for the accounts receivable. The B & C contract allows end users of the Debtors' services to receive one bill for both local and long distance telecommunications services.

3. In addition to the B & C Contract, TDS provides services to the Debtors pursuant to federal and state tariffs (collectively, with the B & C Contracts, the “TDS Contracts”), including without limitation, switched access and special access services.

4. On November 1, 2004, (“Petition Date”) the Debtors each filed a voluntary petition for relief under Chapter 11 of the United States Bankruptcy Code.

5. On June 17, 2005, the Debtors filed the Sale Motion. Through the Sale Motion, the Debtors seek authorization to sell substantially all of their remaining assets and business operations to Leucadia National Corporation (“Leucadia”) or “another successful bidder” (“Leucadia Sale”).

6. Also on June 17, 2005, the Debtors filed their Motion for Order (A) Approving Sale Procedures and Bid Protections in Connection with Sale of Certain Acquired Assets; (B) Scheduling an Auction and Hearing to Consider Approval of the Sale; (C) Approving Notice Relating to Sale; and (D) Granting related Relief (Sale of Substantially All of the Debtors’ Remaining Assets) (“Sales Procedures Motion”).

7. Several parties objected to the Sales Procedures Motion (“Sale Procedures Objections”), including Southwestern Bell Telephone, L.P. and its affiliates (“SBC”); BellSouth Telecommunications, Inc. (“BellSouth”); Qwest Corporation and Qwest Communications Corporation (“Qwest”); and the operating subsidiaries of Verizon Communications, Inc. (“Verizon” and collectively, with SBC, BellSouth and Qwest, the “RBOCs”).

8. By order entered on June 30, 2005 (“Procedures Order”), the Court approved the Sales Procedures Motion with certain modifications. The Procedures Order provides that issues raised in the Sale Procedures Objections as to, *inter alia*, “assumption, assignment, and rejection of executory contracts and unexpired leases” and “substantive issues as to any asset purchase agreement” are reserved for the Sale Hearing. Procedures Order at 3.

9. Subsequently, each of the RBOCs filed motions seeking to compel assumption of their executory contracts (“Assumption Motions”).

III. Argument.

A. The Sale Motion Should Be Denied.

If approved, the Leucadia Sale will be implemented over the course of up to one year and in several separate steps. As proposed, upon entry of an order approving the Leucadia Sale, Leucadia will have the right to demand substantial modifications to the Debtors’ business network. *See* Asset Purchase Agreement, dated June 17, 2005 (“Asset Purchase Agreement”) at Section 5.1(b)(iv). Thereafter, on the “Early Funding Date,”¹ Leucadia will deposit \$54 million² into escrow, and risk of loss will be transferred to Leucadia. *See* Asset Purchase Agreement at Section 2.15. Leucadia and the Debtors also intend to enter into a Management Services Agreement whereby, effective as of the Early Funding Date, Leucadia will be granted complete authority to operate the Debtors’ business.³ *See* Asset Purchase Agreement at Section 5.1(b)(v). The Management Services Agreement will as a practical matter confer upon Leucadia many if not all of the benefits under the Debtors’ executory contracts.

Subsequent to execution of the Management Services Agreement, an initial “Closing” will occur upon the expiration of the waiting period prescribed by the Hart-Scott-Rodino Antitrust Improvements Act of 1976, at which time all of the subject assets will be transferred to Leucadia, except for transfers requiring the approval of state or federal regulatory agencies and the transfer of executory contracts. The so-called “Final Closing” and the formal transfer of

¹ The Debtors do not state when the Early Funding Date will occur, but have represented that it may occur as soon as two days following approval of the Sale Motion. *See* Omnibus Response to Objections to Sale Motion at 5.

² The total purchase price is \$61.5 million. Leucadia has already posted a deposit of \$7.5 million.

³ While not addressed in the Asset Purchase Agreement or Sale Motion, it appears that Leucadia may actually operate the Debtors’ business prior to the entry into the Management Services Agreement due to among other things the fact that Leucadia will have the right to demand changes to the Debtors’ network.

executory contracts may not take place until up to one year after the approval of the Sale Motion. See Asset Purchase Agreement at Sections 2.14(b), 6.6(a).

As described, the Leucadia Sale is inconsistent with both the Bankruptcy Code and applicable regulatory requirements and, therefore, should not be approved.

1. The Proposed Sale Does Not Provide for the Assumption of Executory Contracts Consistent with the Requirements of Section 365.

Neither the Sale Motion nor the attached Asset Purchase Agreement includes a list of all executory contracts to be assumed or rejected, nor do they provide cure amounts for the cure of any defaults under the assumed contracts. Yet, under the terms of the proposed sale, Leucadia will as a practical matter begin to receive the benefits of the Debtors' contracts, including the TDS Contracts, after sale approval and prior to "Final Closing," which could take up to one year. Specifically, after entry of the Sale Order, Leucadia will enjoy the following rights and obligations with respect to those contracts:

- Upon entry of an Order approving the Sale Motion, to demand modifications to the Debtors' network.
- At the "Early Funding Date," to suffer the risk of loss.
- To operate the Debtors' business after entering into a Management Services Agreement.

Allowing Leucadia to operate the Debtors' business and, thereby, receive the benefits of the Debtors' executory contracts without incurring the concomitant obligation to cure defaults and provide adequate assurance of performance of those contracts is impermissible under the Bankruptcy Code. TDS should not be forced to perform for the benefit of a non-party to its contracts while being exposed to risk and uncertainty with respect to its future dealings with Leucadia. During the one-year period prior to assumption, Leucadia may seek alternative providers of services and/or demand concessions from contract parties prior to assumption and assignment. If Leucadia wishes to receive the benefits of the TDS Contracts and can establish

that it is qualified to perform them, those contracts should be assumed and assigned. Leucadia is not entitled to operate with the contracts for a period of time to “test the waters.” Indeed, the proposed sale is nothing less than a *de facto* temporary assignment, for the period prior to Final Closing. Contrary to the Debtors’ claims, there is no authority to support such an “end run” around the requirements of Section 365.

In their response to certain of the Sales Procedures Objections addressing this issue, the Debtors rely upon *In re Ames Department Stores, Inc.*, 287 B.R. 112, 115 (Bankr. S.D.N.Y. 2002). However, *Ames* is factually distinguishable from this case. There, the acquiring entity - Stop and Shop - did not operate the debtors’ business. It only purchased certain designation rights with respect to leases that remained after much of the estate had been liquidated. Indeed, the debtors had previously announced that they were liquidating and had conducted “going out of business” sales at their retail locations.

The Leucadia Sale involves much more than the transfer of “designation rights” as Leucadia is committing to purchase substantially all of the Debtors’ remaining assets and will be operating the Debtors’ business prior to closing. Thus, this Court should follow *In re Omniplex Communications Group, LLC*, Case No. 01-42079-399 (Bankr. E.D. Mo. 2001), cited by Verizon in its Sale Procedures Objection. In that case, the bankruptcy court refused to approve a similarly structured sale that would result in the *de facto* assignment of contracts without providing the protections of Section 365.

Moreover, the proposed sale is a *sub rosa* plan of reorganization. The sale will have the effect of establishing the essential terms of a plan while short circuiting many of the procedural requirements thereof. Once the sale is consummated, the case will effectively be over. Pursuant to Section 365(d)(2), debtors are afforded until confirmation of a plan to assume or reject contracts. Notwithstanding this requirement, the Debtors do not intend to assume or reject contracts for up to a year after the sale is approved. The Court should not permit the Debtors to

eschew the requirement of assumption or rejection simply by altering the preferred statutory vehicle for a sale of this kind from 11 U.S.C. §1129 to 11 U.S.C. § 363. *See, e.g., In re Continental Air Lines, Inc.*, 780 F.2d 1223, 1226 (5th Cir. 1986).

2. Approval of the Proposed Sale Could Impair TDS' Setoff Rights.

Under the proposed sale, Leucadia will obtain “all billed and unbilled accounts receivable, notes receivable and other rights to payment ..., including Acquired PARs[.]” Asset Purchase Agreement at Section 2.1(b).⁴ All assets are to be transferred “free and clear of all Liens, Excluded Liabilities and other interests, except Permitted Liens and Assumed Liabilities, in accordance with Sections 363 and 365 of the Bankruptcy Code[.]” *Id.* at Section 2.1. TDS holds setoff rights against any amounts owed to the Debtors. The right of TDS to withhold payment and preserve its setoff claims should not be separated from the TDS Contracts and related receivables to be acquired by Leucadia. Otherwise, TDS' setoff rights may be lost.

3. Approving the Sale May Moot Disputes Related to the Assumption and Assignment of Executory Contracts.

In addition to the potential loss of setoff rights, the absence of formal assumption of contracts at the time the sale is approved may render moot disputes regarding the requirements for assumption and assignment. The doctrine of equitable mootness in bankruptcy cases is well established. *See, e.g., In re Rickel Home Centers, Inc.*, 209 F.3d 291 (3rd Cir. 2000) (appeal from order approving assignment of lease as part of a Section 363 sale held moot); *In re U.S. Brass Corp.*, 169 F.3d 957 (5th Cir. 1999) (appeal from order confirming plan held moot where plan was substantially consummated); *In re Gibraltar Resources, Inc.*, 211 B.R. 225, 226 (N.D. Tex. 1997) (appeal from consummated sale is moot); *Directional International, Ltd. v. Illinois Bell Telephone (In re Personal Computer Network)*, 85 B.R. 507 (Bankr. N.D. Ill. 1988). Parties to

⁴ Acquired PARs are “[a]ll PARs related to any ILEC with which [Leucadia] enters into a material commercial relationship (by assumption or otherwise) for the Business prior to Final Closing Date [sic] together with all PARs related to the billing and collection agreements that are Assumed Contracts as of the Final Closing Date [.] Asset Purchase Agreement at Section 5.16(a)

executory contracts such as TDS are entitled, *inter alia*, to the opportunity to contest the proposed amount and timing of any cure and to assess and challenge the ability of a proposed purchaser to provide adequate assurance of future performance. Indeed, if the sale is approved, TDS will be forced to do business with a party whom TDS has not approved and whose credentials have not been tested by any court.

To allow a sale to close without resolving these potentially disputed legal issues would render them moot without the opportunity for a hearing, and thus would violate TDS' due process rights. *See, e.g., Huddleston v. Nelson Bunker Hunt Trust Estate*, 109 B.R. 197 (N.D. Tex. 1989) (refusing to dismiss as moot appeal from confirmation order where due process rights violated). Therefore, the Sale Motion should be denied. However, in the event the Court approves the Sale Motion, the stay provided for in Federal Rule of Bankruptcy Procedure 6004 should remain so as to allow objecting parties to seek appellate review.

4. The Proposed Sale Violates TDS' Tariffs.

In addition to violating provisions of the Bankruptcy Code, allowing the interim assumption of contracts as contemplated by the proposed sale while not compelling formal assumption and assignment violates TDS' tariffs. Leucadia apparently seeks to transition customer accounts from the Debtors to Leucadia. This is impermissible under TDS' tariffs, absent the assumption of all outstanding indebtedness. Specifically, TDS' tariffs provide in relevant part:

The customer may assign or transfer the use of services provided under this tariff only where there is no interruption of use or relocation of the services. Such assignment or transfer may be made to:

- (1) Another customer, whether an individual, partnership, association or corporation, provided the assignee or transferee assumes all outstanding indebtedness for such services

*See, e.g., National Exchange Carrier Association, Inc., Tariff F.C.C. No. 5.*⁵ A tariff is similar to a contract in that it establishes certain salient terms of the parties' legal and commercial relationship and obligations, but a tariff also carries with it the force and effect of law. *See, e.g., Evanns v. AT&T Corp.*, 229 F.3d 837, 840 n. 9 (9th Cir. 2000) (collecting authority); *MCI Telecomm. Corp. v. Garden State Inv. Corp.*, 981 F.2d 385, 387 (8th Cir. 1992) (“[F]ederal tariffs are the law, not mere contracts.”); *Carter v. American Tel. & Tel. Co.*, 365 F.2d 486, 496 (5th Cir. 1966) (“[A] tariff, required by law to be filed, is not a mere contract. It is the law.”). Thus, in order for the Debtor to transition the provision of tariffed services to Leucadia so that it may continue to provide uninterrupted service to Vartec's customers, all outstanding indebtedness under those tariffs must be assumed. The Court should not approve a transition that permits Leucadia or any other purchaser to operate in a manner that violates those tariffs, and therefore, does not comply with applicable regulatory law.⁶ *E.g., In re Vel Rey Properties, Inc.*, 174 B.R. 859, 864 (Bankr. D.D.C. 1994) (trustee could not operate in violation of local housing regulations) *citing Gillis v. California*, 293 U.S. 62, 55 S.Ct. 4, 79 L.Ed. 199 (1934); *In re Murphy*, 34, B.R. 78, 80 (Bankr. D. Md. 1983) (“It would be improvident for this court to approve an illegal transaction.”). Therefore, the Court should condition any sale upon the assumption of all outstanding indebtedness for tariffed services consistent with TDS' tariffs.

5. Adoption of Additional Arguments.

In addition to the above, TDS adopts certain arguments raised by the RBOCs in their various Sale Procedures Objections. Specifically, TDS adopts the RBOC's arguments related to “assumption, assignment, and rejection of executory contracts and unexpired leases” as well as

⁵ TDS operates under the federal National Exchange Carrier Association Tariffs and also operates under tariffs with similar or identical language in 30 states.

⁶ In addition, with respect to the assumption of any TDS Contracts, it is difficult to imagine how Leucadia could provide adequate assurance of future performance if it intends to operate in a manner that violates the law.

the substantive objections to the Asset Purchase Agreement which, under the Procedures Order, were reserved for the hearing on the Sale Motion.⁷

B. The Debtors Should be Required To Immediately Assume or Reject the TDS Contracts.

As set forth in the Assumption Motions, telecommunications contracts are essential to the Debtors' operations. Thus, the decision whether to assume or reject such contracts should be part of typical due diligence on the part of any potential purchaser. The Debtors have been in bankruptcy for more than eight months and have had ample time to decide whether to assume or reject the TDS Contracts. *See, e.g., In re Travelot Co.*, 286 B.R. 462 (Bankr. S.D. Ga. 2002). The Debtors have proposed a transaction whereby Leucadia will receive the benefits of the contracts without assumption and assignment. As the Debtor has decided to sell its business and to grant Leucadia the benefits of the contracts, the Court should require the Debtor likewise to decide whether to assume the TDS Contracts. TDS also adopts the arguments raised by Verizon in its Assumption Motion in support of this request for relief.

⁷ In particular, TDS adopts the arguments raised in the following pleadings:

Objection of the Operating Telephone Company Subsidiaries of Verizon Communications, Inc. to Expedited Motion for Order (A) Approving Sale Procedures and Bid Protections in Connection with Sale of Certain Assets; (B) Scheduling an Auction and Hearing to Consider Approval of the Sale; (C) Approving Notice Relating to Sale and; (D) Granting Related Relief; Docket No. 1425;

Objection of SBC Telcos to Expedited Motion for Order (A) Approving Sale Procedures and Bid Protections in Connection with Sale of Certain Assets; (B) Scheduling an Auction and Hearing to Consider Approval of the Sale; (C) Approving Notice Relating to Sale and; (D) Granting Related Relief; Docket No. 1429;

Bellsouth's' Objection to Expedited Motion to Approve Sale Procedures; Docket No. 1430; and

Objection by Qwest Corporation and Qwest Communications Corporation to Expedited Motion for Order (A) Approving Sale Procedures and Bid Protections in Connection with Sale of Certain Assets; (B) Scheduling an Auction and Hearing to Consider Approval of the Sale; (C) Approving Notice Relating to Sale and; (D) Granting Related Relief; Docket No. 1438.

IV. Conclusion.

For the foregoing reasons, TDS respectfully requests that this Court enter an Order: (i) denying the Sale Motion; (ii) compelling assumption or rejection of the TDS Contracts in connection with the approval of any sale; (iii) and granting such further relief as is just and proper.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on this 19th day of July, 2005, a copy of the foregoing Objection was sent by overnight mail to:

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