

Joseph M. Coleman, SBT #04566100  
Joseph A. Friedman SBT #07468280  
Michael L. Scanlon, SBT #17707500  
**KANE RUSSELL COLEMAN & LOGAN, P.C.**  
3700 Thanksgiving Tower  
1601 Elm Street  
Dallas, Texas 75201  
Tel: 214-777-4200  
Fax: 214-777-4299

**SPECIAL COUNSEL TO THE DEBTORS**

**IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE NORTHERN DISTRICT OF TEXAS  
DALLAS DIVISION**

**IN RE:**

**VARTEC TELECOM, INC., *et al.*,**

**DEBTORS.**

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**CASE NO. 04-81694-SAF-11**

**(Chapter 11)  
(Jointly Administered)**

**DEBTORS' RESPONSE AND OBJECTION TO THE MOTION TO  
SHORTEN TIME PERIOD FOR THE DEBTORS TO ASSUME OR REJECT  
THE SBC TELCOS EXECUTORY CONTRACTS**

Vartec Telecom, Inc., *et al.* (the "Debtors"), file this Response and Objection to the Motion to Shorten Time Period for the Debtors to Assume or Reject the SBC Telcos Executory Contracts (the "Motion") and would respectfully show the Court as follows:

**I.  
PRELIMINARY STATEMENT**

1. The SBC Telcos seek to invoke this Court's discretion to reduce the time by which the Debtors may assume or reject unspecified and unidentified "SBC Telcos Executory Contracts." Failing to even identify the specific contracts at issue, the SBC Telcos also fail to explain why the issue is critical now, when it has not been critical for the eight months these cases have been pending before the Motion was filed. As set forth below, the Motion should be

denied because of (1) the significant harm to the Debtors' ability to maximize the value of its assets, protect the jobs of its employees, and the interests of creditors far outweighs the mere inconvenience imposed on the SBC Telcos by a delay on the decision to assume or reject the SBC Telcos Executory Contracts; (2) the SBC Telcos have already stipulated their interests are adequately protected under the terms of the Stipulation and Consent Order By and Among Certain Carriers and the Debtors Regarding Adequate Assurance/Adequate Protection of Future Payments (the "Carrier Stipulation") entered by this Court on or about December 2, 2004 [Docket No. 451]; (3) the Debtors will continue to pay for post-petition services provided by the SBC Telcos to the Debtors under various contracts with the SBC Telcos; and (4) regulatory approval must first be obtained before the Debtors can assume and assign many of the contracts in question and thus, the Debtors need to delay the decision to assume or reject in order to complete that process is neither prejudicial nor inequitable, but legally mandated.

## **II.** **RESPONSE TO MOTION**

2. The Debtors admit the allegation of jurisdiction and venue contained in paragraphs 1 and 2.

3. The Debtors admit paragraph 3.

4. The Debtors admit paragraph 4.

5. In response to paragraph 5, the Debtors admit that certain of the Debtors and the SBC Telcos have entered into approximately hundreds executory contracts relating to telecommunications services and facilities. The Debtors admit that as of the Petition Date the Debtors were delinquent in paying certain amounts due pre-petition as to some of these contracts. The Debtors deny any other allegations in paragraph 5.

6. The Debtors deny the characterization of the Debtors' witness' testimony as set forth in paragraph 6 and contend that the characterization is both over-generalization and simplification of such testimony. The Debtors expressly deny that all of the SBC Telcos Executory Contracts<sup>1</sup> are either inextricably intertwined or necessary to the Debtors' business.

7. The Debtors admit paragraph 7.

8. In response to paragraph 8, the Debtors maintain that the proposed Asset Purchase Agreement and Management Services Agreement speak for themselves, and deny the characterization of such terms set forth in paragraph 8.

9. In response to paragraph 9, the Debtors maintain that the terms of the Asset Purchase Agreement as its terms speak for themselves and deny the characterization of such terms contained in paragraph 9.

10. In response to paragraph 10, the Debtors admit that the SBC Telcos seek the relief set forth in paragraph 10, but deny that the SBC Telcos are entitled to such relief.

11. In response to paragraph 11, the Debtors admit that paragraph 11 purports to be a summary of the SBC Telcos' arguments, however, the Debtors deny such arguments are accurate or are legally valid. The Debtors deny any factual allegations contained in paragraph 11.

12. The Debtors deny the allegations in paragraph 12.

13. In response to paragraph 13, the Debtors maintain that paragraph 13 purports to be a statement of the law that they are neither required to admit or deny. To the extent that paragraph 13 contains any factual allegations, the Debtors deny same.

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<sup>1</sup> Although used as a defined term in the Motion, the SBC Telcos never specify the actual contracts they assert are at issue.

14. In response to paragraphs 14 through 18, such paragraphs constitute legal argument that the Debtors are not required to admit or deny. To the extent that such paragraphs contain factual allegations, the Debtors deny same.

15. The Debtors deny paragraph 19.

16. The Debtors deny that the SBC Telcos are entitled to the relief requested in their motion.

### **III.** **OBJECTION**

A. SBC Telcos' Motion is Legally and Factually Flawed

17. The Bankruptcy Code provides that, with the exception of non-residential real property leases, a debtor in possession shall have until confirmation of the plan to assume or reject executory contracts or unexpired leases. 11 U.S.C. § 365(d)(2). “Permitting the debtor to make its decision as late as the plan confirmation date enables the debtor to carefully evaluate the possible benefits and burdens of an executory contract.” *In re Kmart Corp.*, 290 B.R. 614, 619 (Bankr. N.D. Ill. 2003); *see also In re Wheeling-Pittsburgh Steel Corp.*, 54 B.R. 385, 388 (Bankr. W.D. Pa. 1985). The clear policy of the Bankruptcy Code is to provide a debtor with breathing space following the filing of a bankruptcy petition, continuing until confirmation of the plan with in which to assume or reject executory contracts. *In re Enron Corp.*, 279 B.R. 695, 702 (Bankr. S.D.N.Y. 2002).

18. If a party to an executory contract is suffering economic losses while waiting for the debtor to assume or reject the contract it may move the court to set an earlier deadline for a debtor to assume or reject that contract. *See e.g. Memphis-Shelby County Airport Authority v. Braniff Airways, Inc. (In re Braniff Airways, Inc.)*, 783 F.2d 1283, 1285 (5th Cir. 1986); *Pub.*

*Serv. Co. of New Hampshire v. New Hampshire Elec. Coop., Inc. (In re Pub. Serv. Co. of New Hampshire)*, 884 F.2d 11, 15-16 (1st Cir. 1989).

19. When such a request is made, the bankruptcy court is called upon to exercise its discretion of what is a reasonable time within which a debtor should decide whether to assume or reject the contract in question in light of the particular circumstances of the case. *In re Enron Corp.*, 279 B.R. at 702 (Bankr. S.D.N.Y. 2002).

20. The SBC Telcos now contend that because all of the SBC Telcos Executory Contracts are allegedly essential to the Debtors' business, no further analysis or time is necessary for the Debtors to decide whether to assume or reject the SBC Telcos Executory Contracts. Ignoring the fact that the SBC Telcos have stipulated that on December 2, 2004 the Debtors' performance under the Carrier Stipulation adequately protects their interest, the SBC Telcos now assert they need an order compelling a decision on assumption or rejection of their contracts twenty-four (24) days after their Motion was filed.

21. The 7th Circuit rejected this "essential contract" argument twenty-two (22) years ago. *Data-Link Systems, Inc. v. Whitcomb & Keller Mortgage Co., Inc.*, 715 F.2d 375, 379 (7<sup>th</sup> Cir. 1983). The simple fact that services provided under executory contracts are essential to a Debtor is not sufficient cause to accelerate the Debtors' decision process. *Id.* at 379. Instead, the Debtors must be provided a reasonable time to determine whether assumption or assignment would be beneficial to the reorganization process. *Id.*

22. The 7<sup>th</sup> Circuit's analysis in *Data-Link* is consistent with that of a number of subsequent court decisions. For example, the Supreme Court has said that a court should interpret reasonable time consistent with the broad purpose of Chapter 11 in mind, which is "to permit successful rehabilitation of debtors." *NLRB v. Bildisco & Bildisco*, 465 U.S. 513, 104

S.Ct. 1188, 79 L.Ed 2d 482 (1984). *See also, In re G-I Holdings, Inc.*, 308 B.R. 196, 213 (D.N.J. 2004) (rehabilitation purpose most important factor under § 365(d)(2)) *citing, In re Dunes Casino Hotel*, 63 B.R. 939, 949 (D.N.J. 1986)).

23. Denying a motion to compel the assumption or rejection of an executory contract, the Kmart court noted,

Courts rarely force a debtor into assuming or rejecting a contract. *See* 734 F.2d at 1216 (to rush the debtor into what may be an improvident decision “to assume or reject an executory contract does not further the purposes of the reorganization provisions.”). **The reason for the reluctance is that the “interests of the creditors collectively and the bankruptcy estate as a whole will not yield easily to the convenience or advantage of one creditor out of many.”** *See In re Public Service Co. of New Hampshire*, 884 F.2d 11, 14-15 (1st Cir. 1989), *Wheeling-Pittsburgh*, 54 B.R. at 388, *see also In re Physician Health Corporation*, 262 B.R. 290 (D. Del. 2001) (denying motion compelling assumption or rejection of executory contract when bankruptcy case was only five months old) and *In re St. Mary Hosp.*, 89 B.R. 503, 513-14 (Bankr. E.D. Pa. 1988) (“the interests of the Debtor here in denying a precipitous assumption or rejection appear to us much greater than the interests of HHS in forcing a prompt resolution.”).

Kmart, 290 B.R. at 620 (*emphasis added*).

24. The SBC Telcos have shown no harm, much less manifest injustice or economic harm, they will suffer if the Debtors have until confirmation to assume or reject the Agreements. The right of the SBC Telcos to receive cure payments, if any, owed to them if their contracts are assumed, does not trump the interests of the Debtors’ creditors as a whole in a sale process that maximizes the value of the Debtors' estate. Assuming the cure amounts are at the levels the SBC Telcos allege, the Debtors are economically unable to satisfy the cure absent simultaneous assignment to the Buyer. The SBC Telcos never assert that assignment of the SBC Telcos Executory Contracts cannot occur prior to regulatory approvals. Accordingly, here the collective

interests of the Debtors' creditors should not be compromised by the convenience or advantage sought by the SBC Telcos.

25. The sale of substantially all of the Debtors' assets to a financially stronger operator, will save hundreds of jobs, and will allow services to millions of current and prospective consumers to continue uninterrupted, while also providing an opportunity for recovery for creditors.

26. As such, the issue of the Debtors' ability to make decisions about the SBC Telcos Executory Contracts because they are "essential" is a red herring. Instead, under the facts of this case, before the Debtors can decide to assume the contract, the ultimate purchaser<sup>2</sup> must make the decision of whether it wants to have the Debtors assign executory contracts to it.

27. The ultimate purchaser's decision in this regard will be influenced by, among other things, whether or not regulatory approvals can be obtained. While the Debtors and the current stalking horse purchaser estimate this process will only take six to seven months, in good faith, they have anticipated this process could take up to one year. The SBC Telcos do not suggest that regulatory approval could be obtained any faster, but instead simply ignore this component of the sale transaction in their Motion. When the Court examines the totality of the facts and circumstances surrounding the Debtors' case, the sale transaction, the need for regulatory approval and the controlling case law under § 365(d)(2), the Motion fails.

**B. Factors to Determine Reasonable Time to Assume or Reject**

28. Although the case law is clear that the paramount factor for the Court to weigh when considering the Motion is entirely of the Chapter 11 process, courts have also considered other factors when analyzing motions brought under § 365(d)(2), such as: (1) the nature of the

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<sup>2</sup> Although Leucadia is the stalking horse bidder, the ultimate purchaser will be determined at an auction on July 25, 2005, the same day the SBC Telcos have set a hearing seeking to compel the Debtors to make a decision.

interest at stake; (2) the balance of harms to the parties; (3) the good to be achieved; (4) the safeguards afforded to the litigants; (5) the Debtor's ability to satisfy post-petition delegations pending the decision; (6) the risk of the non-debtor suffering damages beyond compensation under the Bankruptcy Code; (7) the importance of the contracts to the Debtors' reorganization; and (8) whether there is sufficient time to make the decision on the contracts at issue. *See, e.g., In re Adelphia Communication Corp.*, 291 B.R. 283, 293 (Bankr. S.D.N.Y. 2003) (collecting cases and listing factors). Summarizing these factors, the Debtors believe case law requires a court to (1) balance the harms; (2) consider the protection in place or which could be put in place pending a decision to assume or reject at or prior to confirmation; and (3) consider the importance of the contracts and the reasons why the Debtors need the full amount of time allotted by the Bankruptcy Code to make their decisions. An examination of these factors weighs in favor of denying the Motion.

C. Balancing the Harms: Whose Ox is Being Gored?

29. The many factors listed above overlap into a consideration of balancing the harms or more colloquially: Whose ox is being gored?

30. In the instant case, if the Motion is not denied, the Debtors would suffer the loss of a substantial offer to purchase all of their assets, in that the current stalking horse offer is conditioned upon obtaining necessary regulatory approvals and the ultimate purchaser having sufficient time to obtain an understanding as to what executory contracts are ultimately desirable enough to justify paying cure costs. This, in turn, will either force the Debtors: (1) to abandon the sales process; (2) to accept an offer much lower than the one presently on the table, since the purchaser would have to make assumption decisions without adequate evaluation time; or (3) reject more contracts than it otherwise might since the buyer will not want to take on fixed cure obligations on the expedited schedule requested by the SBC Telcos.



31. The SBC Telcos, on the other hand, will only suffer a delay on the decision as to whether some or all of its contracts with the Debtors are assumed or rejected, a delay they have not previously complained about since the case was filed. The Debtors' non-payment of cure costs without an assumption and assignment is not the economic harm or manifest injustice contemplated by the Fifth Circuit in *Braniff Airways*. "The purpose of the Bankruptcy Code is to 'suspend the normal operation of rights and obligations between the debtor and his creditors,'" *Data-Link*, 715 F.2d at 379, quoting *Fontainebleau Hotel Corp. v. Simon*, 508 F.2d 1056, 1059 (5<sup>th</sup> Cir. 1975). The concept that the existence of a prepetition claim that needs to be cured prior to assumption justifies compelling a debtor to assume or reject an executory contract prior to confirmation would render Bankruptcy Code § 365(d)(2) meaningless (as well as Bankruptcy Code § 365(b)(1)). See *in re Physician Health Corp.*, 262 B.R. 290, 294 (Bankr. D. Del. 2001) ("[E]ven if the Debtors were in default of the [executory contract] pre-petition, it is not a legally cognizable reason to compel the Debtors to decide on an expedited basis whether to assume or reject that agreement."). If the SBC Telcos' position would be adopted, any debtor could be compelled to assume or reject virtually any of its executory contracts prior to the confirmation of a plan, denying a debtor the statutory "breathing spell" underlying Bankruptcy Code § 365(d)(2).

32. Moreover, as discussed in more detail below, the SBC Telcos have not and will not really "suffer" at all because they have already stipulated their interests are adequately protected under the Carrier Stipulation. As the *G-I Holdings* court recently observed, in denying a similar motion, "the only true concern here is the payment of money (which is relatively little in the context of ... net worth of the parties.)" 308 B.R. at 213.

33. In a staged process, transparently designed to maximize the value of the Debtors' assets, the Debtors have first sought Bankruptcy Court approval to auction their assets to the

highest bidder. The Debtors will then seek approval of that bid from the Court. The Debtors and the approved purchaser will then seek regulatory approvals of the sale. During the interim, and subject to the Debtors' ultimate control, the approved purchaser will assist the Debtors in managing the Debtors' business for the benefit of the estate and its creditors until regulatory approvals are obtained.<sup>3</sup> In the meantime, the SBC Telcos will continue to be adequately protected and adequately assured of payment under the Carrier Stipulation.<sup>4</sup>

D. The SBC Telcos are Fully Protected by the Carrier Stipulation

34. Another grouping of the factors courts focus upon is whether the non-debtor's position will deteriorate while the Debtors make their decisions on the executory contracts at issue.

35. The Carrier Stipulation by its very terms provides adequate assurance and adequate protection under any relevant SBC Telcos Executory Contract as stipulated to by the SBC Telcos themselves.

36. Thus, the SBC Telcos' interests are well safeguarded, there is little, if any, risk that the SBC Telcos will suffer damages for which they cannot be compensated.

E. The Contracts are Important and There is Good Reason to Permit the Purchaser Time to Make a Decision

37. The remaining factors focus on the relative importance of the contracts and the relative complexities the Debtors face in making their decision.

38. SBC views the decision to assume or reject contracts far too simplistically. While proclaiming the contracts to be "essential," the SBC Telcos ignore that the Asset Purchase

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<sup>3</sup> Among the benefits to the estate is the reduction in rejection damages in the event a particular contract is ultimately rejected.

<sup>4</sup> Given the terms of the Carrier Stipulation, the Debtors are unable to determine what unidentified "potentially significant costs and expenses" that the SBC Telcos claim in the Motion will be caused by a delay of the decision to assume or reject.

Agreement's bifurcation of the sale process and the assumption/rejection process is driven by the regulatory issues applicable to the Debtors' industry. To ignore regulatory demands makes no sense.<sup>5</sup>

39. The Debtors must conduct the administration of their estates in compliance with state and governmental regulations. *See* 28 U.S.C. § 959(b); *In re St. Mary Hospital*, 86 B.R. at 398 (inescapable conclusion that 28 U.S.C. § 959(b) requires a debtor to conform with applicable federal, state, and local law in conducting its business.); *In re Mirant Corp.*, 378 F.3d 511, 523 (5th Cir. 2004) (“The Bankruptcy Code clearly anticipates ongoing governmental regulatory jurisdiction while a bankruptcy proceeding is pending.” (citations omitted)); *In re Cajun Electric Power Coop., Inc.*, 185 F.3d 446, 453-54 (5th Cir. 1999) (noting that laws dealing with public safety and welfare are not be preempted by bankruptcy law).

40. The Debtors must obtain regulatory approval prior to the assignment of the Non-Transferred Assets portion of the Acquired Assets (as those terms are defined in the APA).<sup>6</sup> *See e.g., In re Southeast Community Media, Inc.*, 27 B.R. 834, 838 (E.D. Tenn. 1983) (explaining a purchase agreement where the transfer of assets and the assignment of agreements does not occur until after the FCC approves a radio license transfer); 28 U.S.C. § 959(b); *In re St. Mary Hospital*, 86 B.R. at 398; *In re Mirant Corp.*, 378 F.3d at 523; *In re Cajun Electric Power Coop., Inc.*, 185 F.3d at 453-54.

41. The FCC and the PUCs do not permit the transfer of control, without prior approval, of businesses subject to their jurisdiction that provide telecommunications common

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<sup>5</sup> Likewise, the SBC Telcos also make no sense when they argue that the stalking horse bidder's agreement to (1) buy the Debtors' assets now, and (2) make decisions as to what contracts to assume later, after securing regulatory approval is evidence that the stalking horse is prepared to make the decision to assume contracts now without obtaining regulatory approval for the purchase.

<sup>6</sup> While not specifically enumerated herein, the public utility and/or service commissions of the various states (the “PUCs”) have similar transfer and change in control provisions as the Federal Communication Commission (“FCC”) and thus the Debtors must seek PUC approval for the transaction contemplated in the APA.

carrier services. *See generally* 47 U.S.C. § 214; 47 F.R. §§ 63.04, 63.24. Accordingly, approval must be sought and such approval by the FCC and the PUCs will take time after any sale contemplated by the APA is approved by the Court.

42. While some of the SBC Telcos Executory Contracts are important to the Debtors' current operations, the SBC Telcos cannot make arguments that, and do not suggest: (1) the ultimate purchaser will find all of the SBC Telcos Executory Contracts to be essential; (2) all regulatory approvals can be obtained to transfer the Non-Transferred to the ultimate purchaser; or (3) the ultimate purchaser can assume the contracts without regulatory approval.

43. The SBC Telcos cannot make these arguments because the transactions contemplated by the APA necessarily require regulatory approval and no one can readily determine the timing and ultimate outcome of regulatory approvals.

44. The Debtor and the stalking horse purchaser have valid, unassailable reasons to bifurcate the timing of the sale process and the assumption and assignment of executory contracts. The SBC Telcos simply want to be paid sooner rather than later.

F. Sale of Assets and Management Agreement Not *De Facto* Assignment

45. The SBC Telcos' claim that it is wrong to delay the decision while the purchaser manages the Debtors' assets pending regulatory approvals is really nothing more than a complaint about the very process the Bankruptcy Code and regulations governing the Debtors' operations contemplate, and is not a basis to accelerate the timing of the Debtors' decision. The Management Services Agreement as defined by the APA does not and cannot transfer any form of control to the Buyer. FCC approval extends to both *de jure* transfers of control as well as *de facto* transfers of control. *See Fox Television Stations, Inc.*, 10 FCC Rcd 8452, 8513 (1995) (“As used in the Communications Act, control means every form of control, actual or legal, direct or indirect, negative or affirmative. We thus examine two types of control: *de jure* (control as a

matter of law) and *de facto* (actual control of the licensee).”) (internal quotation marks and citations omitted) (citing *Metromedia, Inc.*, 98 FCC 2d 300, 306 (1984); *WWIZ, Inc.*, 36 FCC 561, 579 (1954)). Thus, even where a *de jure* transfer has not taken place, it is still possible that, by ceding certain types of authority to a potential buyer over the operations of its business, a seller/licensee could be deemed by a regulatory agency to have engaged in an unauthorized *de facto* transfer of control.

46. When questions as to *de facto* transfer of control arise, the FCC examines the facts of each case. In doing so, it applies the criteria set forth in the case of *Intermountain Microwave*, 12 FCC 2d 559 (1963). In that case, the FCC held that its licensees must “at all times retain exclusive responsibility for the operation and control of the facilities” used to provide common carrier services. *Id.* at 560. According to the FCC, the “normal minimum incidents” of such control include:

unfettered use of all facilities and equipment used in connection therewith; day to day operation and control; determination of and the carrying out of policy decisions, including the preparation and filing of applications with this Commission; employment, supervision, and dismissal of personnel; payment of financial obligations including expenses arising out of operation; and the receipt of moneys and profits derived from the operation of the . . . facilities.

*Id.*

47. Therefore, under the FCC’s *Intermountain* criteria, it is essential that the Debtors continue to be responsible for the payment of all financial obligations and that it receive all monies and profits from the operation of its business until the necessary regulatory approvals for the sale are received. To meet its obligations under the Bankruptcy Code and its obligations as regulated entities, the APA precludes the Debtors from transferring its necessary working capital, operating assets (including at least some of the SBC Telcos Executory Contracts) and facilities

until regulatory approvals are obtained and the Final Closing (as defined by the APA) is consummated.

48. The sale obligates the Buyer to provide the Debtors with certain services as an independent contractor under the Management Services Agreement (subject to the Debtors maintaining ultimate control over the business) prior to the receipt of regulatory approvals and the Final Closing Date (as defined by the APA). The only benefit the Buyer gets from the Management Service Agreement is a management fee.

49. The SBC Telcos Executory Contracts will not be assigned to the Buyer during this interim period when the Management Services Agreement is in place. The assignment of the SBC Telcos Executory Contracts to the Buyer would result in the transfer of responsibility for the payment and collection of monies to the assignee. Thus, if the Debtors were to assign any SBC Telcos Executory Contracts that are essential to the operation of its business to the Buyer prior to obtaining regulatory approvals, they would cede to the Buyer the Debtors' authority over the payment and collection of monies relating to the business – an important indicia of de facto control under *Intermountain*. Such an assignment would be a clear violation of *Intermountain*, and thus, cannot be accomplished prior to the receipt of regulatory approvals, despite the SBC Telcos requesting such relief.

#### **IV.** **CONCLUSION**

The Debtors' sale of their assets must comply with both the Bankruptcy Code and the federal and state regulations outside the Bankruptcy Code that govern such transactions. While the SBC Telcos ignore this fact, the Court should not. The SBC Telcos simply cannot have what they want because, in addition to the Court's approval of the sale, regulatory approvals must also be obtained. The Debtor cannot decide today, tomorrow or at any point earlier than when

regulatory approvals are secured, what SBC Telcos Executory Contracts to assume or reject. Pending those events occurring the SBC Telcos' interests are adequately protected by the Carrier Stipulation.

WHEREFORE, the Debtors request the Court deny the Motion.

Dated: July 25, 2005.

Respectfully submitted,

**KANE RUSSELL COLEMAN & LOGAN, P.C.**  
3700 Thanksgiving Tower  
1601 Elm Street  
Dallas, Texas 75201  
Tel: 214-777-4200  
Fax: 214-777-4299

By: /s/ Joseph A. Friedman  
Joseph M. Coleman, SBT #04566100  
Joseph A. Friedman SBT #07468280  
Michael L. Scanlon, SBT #17707500

**SPECIAL COUNSEL TO THE DEBTORS**

**CERTIFICATE OF SERVICE**

This is to certify that on July 25, 2005, a copy of this *Debtors' Response and Objection to the Motion to Shorten Time Period for the Debtors to Assume or Reject the SBC Telcos Executory Contracts* was served by the Electronic Case Filing System for the United States Bankruptcy Court for the Northern District of Texas. A separate certificate of service shall be filed with respect to those parties on the Master Service List that do not receive electronic e-mail service.

/s/ Joseph A. Friedman  
Joseph A. Friedman