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ATTORNEYS FOR THE OFFICIAL COMMITTEE OF EXCEL INDEPENDENT REPRESENTATIVES

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

_____	)	
In re	)	Chapter 11 Case
	)	
VARTEC TELECOM, INC., <u>et al.</u> ,	)	Case No. 04-81694-SAF-11
	)	
	)	Jointly Administered
Debtors.	)	
	)	Hearing Date and Time:
_____	)	[To Be Determined]

**MOTION OF THE OFFICIAL COMMITTEE OF EXCEL INDEPENDENT REPRESENTATIVES FOR RECONSIDERATION OF SALE ORDER DATED JULY 29, 2005 PURSUANT TO FED. R. BANKR. P. 9023 AND FED. R. CIV. P. 59**

TO: THE HONORABLE BANKRUPTCY JUDGE:

The Official Committee of Excel Independent Representatives (the “IR Committee”) appointed in the above-captioned jointly administered chapter 11 cases (the “Cases”) of VarTec Telecom, Inc. and its affiliated debtors (collectively, the “Debtors”) files this Motion (the “Motion”) pursuant to Rule 9023 of the Federal Rules of Bankruptcy Procedure (the “Bankruptcy Rules”) and sections 361 and 363 of title 11 of the United States Code (the “Bankruptcy Code”) for reconsideration of this Court’s Order (A) Approving the Sale Free and Clear of All Liens, Claims, Rights and Encumbrances to Comtel Investments LLC and (B)

**MOTION OF THE OFFICIAL COMMITTEE OF EXCEL INDEPENDENT REPRESENTATIVES FOR RECONSIDERATION OF SALE ORDER DATED JULY 29, 2005 PURSUANT TO FED. R. BANKR. P. 9023 AND FED. R. CIV. P. 59**

Granting Related Relief (Substantially all of the Debtors' Remaining Assets) dated July 29, 2005 [Docket No. 1663 ] (the "Sale Order"), and in support of this Motion, respectfully states as follows:

**PRELIMINARY STATEMENT**

1. This Motion is simple. Pursuant to Bankruptcy Rule 9023, the IR Committee respectfully requests reconsideration of the last sentence of paragraph 10 of the Sale Order, which decrees all net proceeds (the "Sale Proceeds") from the sale of substantially all of the Debtors' assets (the "Sale") to Comtel Investments LLC ("Comtel") shall be transferred by the Debtors to the Rural Telephone Finance Cooperative ("RTFC"). The Sale Proceeds are estimated at \$81.5 million, subject to adjustments.

2. Paragraph 10 of the Sale Order decrees, in pertinent part:

The Proceeds from the Sale shall be paid to the Sellers on the Closing Date and the Final Closing Date, as applicable, and the Net Proceeds (as defined in the First Amended and Restated Credit Agreement dated as of October 7, 2004, as amended ("DIPFA")) shall then be transferred by the Sellers to the RTFC and provisionally applied by the RTFC, all in accordance with the terms and provisions of DIPFA, as approved in the Final Order Authorizing Post-Petition Financing, Granting Senior Liens and Priority Administrative Expense Status, Authorizing Use of Cash

Sale Order, ¶ 10 (emphasis added).

3. The authority recited in paragraph 10 of the Sale Order for directing a transfer of the Sale Proceeds to the RTFC is this Court's Final Order Authorizing Post-Petition Financing, Granting Senior Liens and Priority Administrative Expense Status, Authorizing Use of Cash Collateral and Modifying the Automatic Stay dated January 12, 2005 [Docket No. 789] (the "DIP Financing Order") and the First Amended and Restated Credit Agreement dated as of October 4, 2004, as amended (the "DIPFA"). On the other hand, under the express terms of the

DIPFA Amendment dated on or about January 12, 2005 (the “DIPFA Amendment”), all payments and prepayments from asset sale proceeds (including the Sale Proceeds) on account of the RTFC’s *prepetition* loans (estimated at approximately \$256 million in the DIPFA) (the “Prepetition Loans”) are solely in the nature of “*adequate protection payments.*” See DIPFA Amendment, § 2.3.4(a) (emphasis added).

4. As the Court is well-aware, “adequate protection” under sections 361 and 363 of the Bankruptcy Code is interim, not final, relief in a bankruptcy case and is subject to modification by the Court based upon the circumstances of each case and the alleged creditor’s need for adequate protection. Indeed, section 363(o)(2) of the Bankruptcy Code explicitly places the burden of proof on the issue of the validity, priority and extent of a prepetition secured claim squarely on the secured creditor seeking adequate protection.

5. Here, paragraph 9 of the DIP Financing Order provides: “Except for adequate protection payments of interest on the Pre-Petition Indebtedness as provided in the Budget, all payments to the Lender made as required under the DIP Loan Documents (unless otherwise expressly stated therein) *shall be credited against any post-petition obligations of the Debtors to the Lenders on account of the Loans.*” (emphasis added). The only reference to adequate protection of the Prepetition Loans is not in the DIP Financing Order but in Section 2.3.4(a) of the DIPFA Amendment, which provides that all payments or prepayments from sale proceeds on account of the Prepetition Loans are “adequate protection payments.”

6. Tellingly, the Court’s factual findings in paragraph C of the DIP Financing Order with respect to the validity, priority and extent of the RTFC’s Prepetition Loans were expressly subject to paragraph 19 of that order. Paragraph 19 explicitly preserved the rights of parties in interest to commence an adversary proceeding to challenge the RTFC’s Prepetition Loans and,

more importantly, expressly provided that such loans would constitute allowed claims for all purposes in the Cases only “[i]f no such adversary proceeding or contested matter is commenced as of such date[.]” (emphasis added).

7. In this case, the Official Committee of Unsecured Creditors (the “Creditors’ Committee”) timely filed a complaint and commenced an adversary proceeding against the RTFC in these Cases challenging the Prepetition Loans in accordance with paragraph 19 of the DIP Financing Order (the “Committee Action”). Accordingly, the Court’s findings of fact and conclusions of law in the DIP Financing Order that the RTFC’s liens and claims in respect of the Prepetition Loans are valid and enforceable are not binding on the Debtors’ estates as a result of the subsequently filed Committee Action and operation of paragraph 19 of the DIP Financing Order.

8. Notably, on the issue of adequate protection, paragraph 11 of the DIP Financing Order decrees: “Based upon the Lender’s consent, the adequate protection provided herein is reasonable and sufficient to protect the interests of the Lender *at the present time*, provided however nothing herein shall prejudice the Lender’s right to request or obtain modification of such adequate protection or the Debtors’ right to oppose such request.”

9. Simply put, pursuant to Bankruptcy Rule 9023, this Court should reconsider the last sentence of paragraph 10 of the Sale Order in light of the fact that the RTFC is statutorily required under section 363(o) of the Bankruptcy Code on the issue of adequate protection to meet its burden of proof as to the validity, priority and extent of its Prepetition Loans to be entitled to apply the Sale Proceeds to the Prepetition Loan as “adequate protection payments.” At the very least, the Court should include additional language expressly preserving the rights of parties in interest in these Cases (including the two statutory committees of creditors appointed

in these Cases, the Creditors' Committee and the IR Committee) to challenge the RTFC's entitlement to apply the Sale Proceeds under the DIPFA Amendment as "adequate protection payments" in accordance with sections 361 and 363(o) of the Bankruptcy Code and paragraphs 11 and 19 of the DIP Financing Order.

### **JURISDICTION AND VENUE**

10. This Court has jurisdiction to consider this Motion pursuant to 28 U.S.C. §§ 157 and 1334. This is a core proceeding pursuant to 28 U.S.C. § 157(b). Venue of this proceeding is proper in this district pursuant to 28 U.S.C. §§ 1408 and 1409. The statutory predicate for the relief sought herein is Bankruptcy Rule 9023 and sections 361 and 363 of the Bankruptcy Code.

### **PROCEDURAL BACKGROUND**

11. On or about November 1, 2004 (the "Petition Date"), each of the Debtors filed voluntary petitions for relief under chapter 11 of the Bankruptcy Code with this Court, commencing their respective Cases.

12. By order dated November 2, 2004, the Cases are being jointly administered. The Debtors are in possession of their property and operating their businesses as debtors and debtors-in-possession pursuant to sections 1107 and 1108 of the Bankruptcy Code.

13. On November 8, 2004, the Office of the United States Trustee (the "U.S. Trustee") appointed the Creditors' Committee pursuant to section 1102 of the Bankruptcy Code.

14. On December 8, 2004, the U.S. Trustee appointed the IR Committee.

15. On January 12, 2005, the Court entered the DIP Financing Order.

16. On June 10, 2005, the Creditors' Committee filed the Committee Action.

17. On July 29, 2005, the Court entered the Sale Order.

## RELIEF REQUESTED

18. Bankruptcy Rule 9023 makes Rule 59 of the Federal Rules of Civil Procedure (the “Federal Rules”) applicable to contested matters. Reconsideration of an order under Federal Rule 59(e) and Bankruptcy Rule 9023 is appropriate where the bankruptcy court has made a clear error of law or fact. See Fed. R. Bankr. P. 9023 (“Any motion to alter or amend a judgment shall be filed no later than 10 days after entry of the judgment.”) See also Trust Co. Bank v. U.S. Gypsum Co., 950 F.2d 1144, 1147 (5th Cir. 1992).

19. The Sale Order fails to address the legal issue of adequate protection raised in the DIP Financing Order and the DIPFA Amendment and, thereby, creates an unnecessary ambiguity that requires clarification with respect to the application of the Sale Proceeds.

20. “Adequate protection is a device intended to provide additional protection against loss to a secured creditor....” Memphis-Shelby County Airport Authority v. Braniff Airways, Inc. (In re Braniff Airways, Inc.), 783 F.2d 1283, 1286 (5th Cir. 1986). Section 363 of the Bankruptcy Code provides that adequate protection is appropriate in certain circumstances as a result of a sale of a debtor’s assets:

(e) Notwithstanding any other provision of this section, at any time, on request of an entity that has an interest in property used, sold, or leased, or proposed to be used, sold, or leased, by the trustee, the court, with or without a hearing, shall prohibit or condition such use, sale, or lease as is necessary to provide adequate protection of such interest. This subsection also applies to property that is subject to any unexpired lease of personal property (to the exclusion of such property being subject to an order to grant relief from the stay under section 362).

...

(o) In any hearing under this section--  
(1) the trustee has the burden of proof on the issue of adequate protection; and

(2) the entity asserting an interest in property has the burden of proof on the issue of the validity, priority, or extent of such interest.

11 U.S.C. § 363 (emphasis added).

21. Section 361 of the Bankruptcy Code sets forth various means of providing adequate protection:

When adequate protection is required under section 362, 363, or 364 of this title of an interest of an entity in property, such adequate protection may be provided by—

(1) requiring the trustee to make a cash payment or periodic cash payments to such entity, to the extent that the stay under section 362 of this title, use, sale, or lease under section 363 of this title, or any grant of a lien under section 364 of this title results in a decrease in the value of such entity's interest in such property;

(2) providing to such entity an additional or replacement lien to the extent that such stay, use, sale, lease, or grant results in a decrease in the value of such entity's interest in such property; or

(3) granting such other relief, other than entitling such entity to compensation allowable under section 503(b)(1) of this title as an administrative expense, as will result in the realization by such entity of the indubitable equivalent of such entity's interest in such property.

11 U.S.C. § 361.

22. Adequate protection is “a flexible concept, which can be molded to meet the peculiar facts and circumstances of each particular case....Consequently, even after [an order on adequate protection] is entered, the order is subject to change, if the circumstances upon which it was premised also change.” In re Lafayette Dial, Inc., 92 B.R. 798, 799 (denying modification of adequate protection agreement, because the evidence and arguments advanced by the debtor were not premised upon any change in circumstances); see also Braniff, 783 F.2d at 1287

(“adequate protection provided to creditors by Chapter 11 is generally considered interim relief.”).

23. The last sentence of paragraph 10 of the Sale Order, however, the Court appears to require the transfer by the Debtors of the Sale Proceeds to the RTFC, without addressing the adequate protection issue. Specifically, paragraph 10 of the Sale Order decrees, in pertinent part:

The Proceeds from the Sale shall be paid to the Sellers on the Closing Date and the Final Closing Date, as applicable, and the Net Proceeds (as defined in the First Amended and Restated Credit Agreement dated as of October 7, 2004, as amended ("DIPFA")) shall then be transferred by the Sellers to the RTFC and provisionally applied by the RTFC, all in accordance with the terms and provisions of DIPFA, as approved in the Final Order Authorizing Post-Petition Financing, Granting Senior Liens and Priority Administrative Expense Status, Authorizing Use of Cash

Sale Order, ¶ 10 (emphasis added).

24. Importantly, however, payments to the RTFC from asset sale proceeds in respect of the Prepetition Loans are solely “adequate protection payments” under the express terms of the DIPFA Amendment. See DIPFA Amendment, § 2.3.4(a). Specifically, section 2.3.4(a) of the DIPFA Amendment provides:

Section 2.3.4. (a) is amended in its entirety to read as follows: (a) Lender will apply all payments and prepayments (i) first to accrued interest on the Post-Petition Debt, (ii) then to the Post-Petition Principal Debt until it is reduced to zero, and (iii) then as adequate protection payments in respect of the Pre-Petition Debt (as provided in the Authorizing Order), to be applied first to Revolving Principal Debt, and then to the Term Loan.

(emphasis added).

25. Section 363(o) of the Bankruptcy Code requires the RTFC to meet its burden of proof in these Cases on the validity, priority and extent of the Prepetition Loan to be entitled to adequate protection. Specifically, paragraph C of the DIP Financing Order contains factual findings in favor of the RTFC, including as to its entitlement to adequate protection (C.ix), but

expressly provides that such findings are “subject to the limitations thereon described below in decretal Paragraph 19 below[.]” Paragraph 19 of the DIP Financing Order provides that the findings and other provisions of that order are binding and that the Prepetition Loan “shall constitute allowed claims for all purposes in the Cases” *unless* a timely action challenging the Prepetition Loan is brought by a party in interest. In this case, the Committee Action constitutes a timely action challenging the RTFC’s Prepetition Loan in accordance with paragraph 19 of the DIP Financing Order.

26. In sum, the statutory burden of proof of establishing the validity, priority and extent of its Prepetition Loan rests squarely with the RTFC under section 363(o) of the Bankruptcy Code for purposes of adequate protection. By virtue of paragraph 19 of the DIP Financing Order and the Committee Action, that burden continues to remain with the RTFC and has not been met to justify any adequate protection payments. Accordingly, the IR Committee respectfully requests that the last sentence of paragraph 10 of the Sale Order be stricken.

27. Alternatively, at the very least, the last sentence of paragraph 10 of the Sale Order should be modified to reflect the fact that parties in interest retain the right to seek modification of the RTFC’s entitlement to adequate protection in light of the changed circumstances in these Cases as recognized by the Fifth Circuit in Braniff. Indeed, paragraph 11 of the DIP Financing Order (entered in January 2005 – well-prior to the Sale and the Committee Action) expressly recognizes that adequate protection in favor of the RTFC in these Cases may be modified as appropriate in the future. DIP Financing Order, ¶ 11 (“Based upon the Lender’s consent, the adequate protection provided herein is reasonable and sufficient to protect the interests of the Lender *at the present time*, provided however nothing herein shall prejudice the Lender’s right to request or obtain modification of such adequate protection or the Debtors’ right to oppose such

request.”) (emphasis added). Such reservation of rights language should be added to paragraph 10 of the Sale Order.

WHEREFORE, the IR Committee respectfully requests that the Court enter an order (i) pursuant to Bankruptcy Rule 9023 and Federal Rule 59, amending paragraph 10 of the Sale Order by deleting the last sentence thereof or, alternatively, adding reservation of rights language with respect to the issue of adequate protection, and (ii) granting such other and further relief as is just and proper.

Dated: August 8, 2005  
Dallas, Texas

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-and-

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REPRESENTATIVES

**CERTIFICATE OF SERVICE**

The undersigned hereby certifies that on this 8<sup>th</sup> day of August 2005, he caused a true and correct copy of the foregoing document to be served on the parties and in the manner set forth in the Certificate of Service filed contemporaneously herewith.

/s/ Craig H. Averch \_\_\_\_\_  
Craig H. Averch