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ATTORNEYS FOR THE DEBTORS

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

IN RE:	§	
	§	
VARTEC TELECOM, INC., *et al.,*	§	**CASE NO. 04-81694**
	§	
DEBTORS.	§	**(Chapter 11)**
	§	**(Jointly Administered)**

MOTION FOR AUTHORITY TO SELL ASSETS FREE AND CLEAR OF ALL LIENS, CLAIMS, RIGHTS, INTERESTS AND ENCUMBRANCES AND GRANT RELATED RELIEF (SHARES OF VARTEC EUROPE)

A HEARING WILL BE CONDUCTED ON THIS MATTER ON DECEMBER 17, 2004, AT 1:30 P.M. IN COURTROOM OF THE HONORABLE STEVEN A. FELSENTHAL, 1100 COMMERCE STREET, 14TH FLOOR, DALLAS, TEXAS. IF YOU OBJECT TO THE RELIEF REQUESTED, YOU MUST RESPOND IN WRITING, SPECIFICALLY ANSWERING EACH PARAGRAPH OF THIS PLEADING. UNLESS OTHERWISE DIRECTED BY THE COURT, YOU MUST FILE YOUR RESPONSE WITH THE CLERK OF THE BANKRUPTCY COURT WITHIN TWENTY (20) DAYS FROM THE DATE YOU WERE SERVED WITH THIS PLEADING. YOU MUST SERVE A COPY OF YOUR RESPONSE ON THE PERSON WHO SENT YOU THE NOTICE; OTHERWISE, THE COURT MAY TREAT THE PLEADING AS UNOPPOSED AND GRANT THE RELIEF REQUESTED.

TO THE HONORABLE STEVEN A. FELSENTHAL, UNITED STATES CHIEF BANKRUPTCY JUDGE:

The above-referenced debtors and debtors in possession (collectively, the "Debtors")[1] file this Motion for Authority to Sell Assets Free and Clear of All Liens, Claims, Rights, Interests and Encumbrances and Grant Related Relief (Shares of VarTec Europe) (the "Motion") and in support thereof the Debtors would show as follows:

INTRODUCTION

1. By this Motion, the Debtors seek entry of an Order authorizing the sale by VarTec Telecom International Holding Company (the "Seller") to Ventelo Sverige AB (the "Buyer"), or another bidder, of all of the outstanding ordinary shares of VarTec Telecom Europe Limited (the "Company") owned by the Seller and all of the outstanding ordinary shares of VarTec Telecom Belgium SPRL ("VarTec Belgium") owned by the Seller (collectively, the "Shares" or the "Assets") as set forth in that certain Share Purchase Agreement dated November 16, 2004 (the "SPA") by and among the Seller, the Buyer, the Company, and VarTec Telecom, Inc., pursuant to Bankruptcy Code § 363. A copy of the SPA is attached hereto as **Exhibit A**.

JURISDICTION AND PROCEDURAL BACKGROUND

2. The Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 1334 and 157. This Motion concerns the administration of the estate; and therefore, it is a core proceeding pursuant to 28 U.S.C. § 157(b)(2).

3. Venue is proper in this Court pursuant to 28 U.S.C. §§ 1408 and 1409.

[1] The Debtors include VarTec Telecom, Inc., Excel Communications Marketing, Inc., Excel Management Service, Inc., Excel Products, Inc., Excel Telecommunications, Inc., Excel Telecommunications of Virginia, Inc., Excel Teleservices, Inc., Excelcom, Inc., Telco Communications Group, Inc., Telco Network Services, Inc., VarTec Business Trust, VarTec Properties, Inc., VarTec Resource Services, Inc., VarTec Solutions, Inc., VarTec Telecom Holding Company, VarTec Telecom International Holding Company, and VarTec Telecom of Virginia, Inc.

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

5. Since the Petition Date, the Debtors have continued to operate and manage their businesses as debtors in possession pursuant to Bankruptcy Code §§ 1107(a) and 1108.

6. On November 9, 2004, the United States Trustee appointed the Official Committee of Unsecured Creditors (the “Committee”).

7. The Debtors’ Cases are jointly administered under Case No. 04-81694-SAF-11.

STATEMENT OF FACTS

VarTec and Its Business

8. VarTec Telecom, Inc., a Texas corporation, (“VarTec”) along with its sixteen direct and indirect domestic subsidiaries, each of which is a Debtor, and eighteen non-debtor direct and indirect foreign subsidiaries (collectively, the “VarTec Entities”), is among the largest privately held companies providing telecommunications services in North America and Europe. The VarTec Entities, founded in DeSoto, Texas in February 1989, with current employees totaling over 1,300 worldwide (including approximately 1,000 in the Dallas metroplex), sell a full range of telecommunication products and services to customers. In 2003, the VarTec Entities had revenues of approximately $1,260,000,000, and anticipate 2004 revenue in the approximate amount of $900,000,000. VarTec’s revenues have been derived primarily from three sale

distribution channels: (a) Direct Marketing; (b) Commercial Services; and (c) Multi-Level Marketing.

9. The Direct Marketing channel, managed by VarTec and certain of its subsidiaries offers telecommunications services to small business and residential consumers, including local and long distance telephone services, wireless telephone services, and internet access. VarTec pioneered the "10-10 dial-around" long distance market by offering customers the opportunity to access VarTec's discounted long distance services on a call-by-call basis by dialing "10-10" then a three-digit unique carrier access code. Under the "dial-around" model, a customer's long distance usage is billed on her local phone service provider's invoice, the local phone service provider collects the billed amounts, and the local phone service provider remits those collected amounts to VarTec.

10. While experiencing tremendous success with the "dial-around" model, VarTec began to offer other telecommunication services, including local and traditional long distance telephone services, wireless telephone service, and internet access, directly to small business and residential customers. VarTec is licensed to provide local and long distance telephone services in all fifty states, and markets its products and services through, among other means, direct mail and magazine insert campaigns composed of several hundred million items to persons in a targeted market each year. VarTec also uses outbound telemarketing for targeted campaigns to attract new customers of existing products and to offer new and/or additional products to existing customers.

11. The Commercial Services channel, managed by VarTec Solutions, Inc. (formerly known as eMeritus Communications, Inc.) and certain of its subsidiaries (collectively, "VarTec Solutions"), provides customized voice, data, and internet services to commercial and wholesale carrier customers throughout the U.S. VarTec Solutions' voice product offerings include switched and dedicated access, domestic and international toll-free service, calling cards, audio conferencing, and other specialized products. In addition, VarTec Solutions offers high-capacity data services that provide access to frame relay and IP networks. For carrier customers, VarTec Solutions offers the ability to co-locate their equipment inside carrier-class facilities, saving the cost and complications involved with building their own facilities.

12. Through the Multi-Level Marketing channel, which is managed by Excelcom, Inc. and certain of its subsidiaries (collectively, "Excel"), Excel offers telecommunications products and services to small business and residential consumers similar to those offered by VarTec to its customers. Excel, which was acquired by VarTec in 2002, has an international network of over 130,000 independent representatives who market Excel's products and services to small business and residential consumers and recruit new independent representatives to market such products and services. Each independent representative receives commissions and bonuses based on, among other things, the success of the independent representatives recruited and a portion of the success of their recruits (referred to as a "downline"), the usage of Excel products and services by customers of the independent representative and a portion of their downline. On November 1, 2004, the Debtors filed their motion to

reject agreements with these independent representatives. The hearing on that motion has been set for November 22, 2004.

Secured Debt

13. VarTec is a borrower and the other Debtors (except VarTec Telecom of Virginia, Inc. and Excel Telecommunications of Virginia, Inc.) are guarantors under that certain First Amended and Restated Credit Agreement with the Rural Telephone Finance Cooperative (the "RTFC"), pursuant to which the existing secured indebtedness owing to the RTFC was restructured in the form of a secured term loan and a secured line of credit to the Debtor.[2] The secured line of credit is in the form of a revolving credit facility, for the working capital, credit, and liquidity needed by the Debtor to conduct general business operations. As of the Petition Date, the total outstanding obligation to the RTFC consist of (a) a term loan of approximately $154,000,000 and (b) a revolving line of credit with a total commitment of $70,000,000.

The Industry

14. Prior to 1996, local telecommunications services were provided exclusively by traditional, monopoly providers, or incumbent local exchange carriers (the "ILECs"). Pursuant to the Telecommunications Act of 1996 (the "Telecommunications Act"), which was enacted to promote competition in the local telecommunications industry, ILECs were required to provide competitors, such as the Debtors, access to their networks to allow those competitive local exchange carriers (the "CLECs") to offer local telecommunications services. The terms, conditions, and prices charged by ILECs

[2] The capital stock of VarTec Telecom of Virginia, Inc. and Excel Telecommunications of Virginia, Inc. was pledged to the Rural Telephone Finance Cooperative under transactions completed in conjunction with the Credit Agreement.

to CLECs are provided in agreements – referenced as interconnection agreements – governed by rules and regulations promulgated by the FCC and various state agencies or public utility commissions. As consideration for relinquishing their monopoly positions, the ILECs were authorized to offer long distance telecommunications services, both out-of-region and in-region (where they were an ILEC) provided certain terms and conditions were satisfied.

15. ILECs, CLECs, and long distance carriers utilize each other's networks to transmit the voice and data traffic of their customers. The framework and pricing of the exchange of voice and data traffic between ILECs and CLECs, on the one hand, and long distance carriers, on the other hand, is governed by multiple laws, regulations, tariffs, and interconnection agreements. For example, if an ILEC or a CLEC's customer originates a call that is carried to its destination by one of the Debtors, the respective Debtor will bill the CLEC or ILEC on a minute of use basis; if a customer of one of the Debtors originates a call that is carried to its destination by an ILEC or a CLEC, the ILEC or CLEC will bill the respective Debtor on a minute of use basis. This is known as reciprocated or intercarrier compensation.[3]

16. To effectuate the billing, collection, and maintenance of account information, the Debtors often entered into agreements with various ILEC and CLEC, under which such ILEC or CLEC bills customers for the services provided by the Debtors, collects the billed amount for the Debtors, and pays or remits to the Debtors the collected amounts periodically.

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[3] A long distance carrier can also be an ILEC or a CLEC.

17. The deregulation of local and long distance telecommunication services pursuant to the Telecommunications Act resulted in increased competition and decreased local and long distance rates. Despite successfully competing in the telecommunications industry for almost fifteen years, (i) VarTec's lack of brand name recognition comparable to some of its competitors in the more intensively competitive telecommunications market, (ii) customer attrition exacerbated by aggressive customer win-back campaigns by the dominant telco providers, and (iii) the margin compromises caused by increasing wholesale rates while retail rates are suffering, have all made it difficult for VarTec to maintain its historical revenue and profitability levels.

Challenges

18. In the weeks preceding the Petition Date, several ILECs, CLECs, and long distance carriers with whom the Debtors have interconnection or access agreements have (i) threatened to terminate services provided to the Debtors, (ii) requested security deposits, and/or (iii) offset amounts owed to the Debtors. The actions of the ILECs, CLECs, and long distance carriers have impaired the Debtors' liquidity.

19. In addition to the matters discussed above, because of various disputes[4] with Teleglobe Inc. ("Teleglobe") regarding VarTec's acquisition of certain of the companies now associated with Excel and VarTec Solutions (the "Acquired Companies"), VarTec has had to spend millions of dollars in the past several years supporting the Excel companies (for which it had anticipated reimbursement), which has financially weakened the Debtors.

[4] Such disputes have spawned considerable litigation, including an arbitration between VarTec and Teleglobe's bankruptcy estate.

20. The combination of these economic and financial events has impaired the Debtors' liquidity and compelled the Debtors to commence these Cases in order to maximize the value of their assets for the benefit of their creditors and other constituencies under chapter 11 of the Bankruptcy Code.

Proposed Sale of VarTec Europe

21. The Seller, a Debtor in these Cases, owns all of the outstanding ordinary shares of the Company and 1% of the outstanding ordinary shares of VarTec Belgium. The remaining 99% of the outstanding ordinary shares of VarTec Belgium are owned by the Company.

22. Under the SPA, the Buyer agrees to purchase the Assets for consideration in the approximate amount of $6,500,000.

23. Contemporaneous herewith, the Debtors filed their Motion for Order (A) Approving Sale Procedures and Bid Protections in Connection with Sale of Certain Assets Owned by the Debtors, (B) Scheduling an Auction and Hearing to Consider Approval of the Sale; (C) Approving Notice of Certain Dates, Times and Places; and (D) Granting Related Relief (Shares of VarTec Europe) (the "Sale Procedure Motion").[5]

RELIEF REQUESTED

24. Pursuant to Bankruptcy Code §§ 105(a) and 363, the Debtors seek authority to sell the Assets to the Buyer, or an alternate offerer who submits a higher and better offer at the Auction and/or Sale Hearings, free and clear of liens, claims and encumbrances (except that the Seller's Shares of VarTec Belgium shall be subject to

[5] Capitalized terms not defined herein shall have the meaning giving to them in the Sale Procedure Motion.

the lens of Barclays Bank PLC) (the "Sale") with such liens, claims and interests to attach to the proceeds of the Sale.

25. Bankruptcy Code § 363(f) provides, in pertinent part:

> (f) The trustee may sell property under subsection (b) or (c) of this section free and clear of any interest in such property of an entity other than the estate, only if –
>
> (1) applicable nonbankruptcy law permits sale of such property free and clear of such interest;
>
> (2) such entity consents;
>
> (3) such interests is a lien and the price at which such property is to be sold is greater than the aggregate value of all liens on such property;
>
> (4) such interest is in bona fide dispute; or
>
> (5) such entity could be compelled, in a legal or equitable proceeding, to accept a money satisfaction of such interest.

11 U.S.C. §363(f); *Pelican Homestead v. Wooten (In re Gabel)* 61 B.R. 661, 667 (Bankr. W.D. La. 1985) (stating that a trustee may sell property of the estate for purposes other than in the ordinary course of business free and clear of all existing liens and encumbrances provided that any one of the conditions of § 363(f) are met).

26. The RTFC asserts a lien on 65% of the Seller's interest in the Assets. Upon information and belief, the RTFC will either consent to the sale or they may be compelled, in a legal or equitable proceeding, to accept a money satisfaction of their interest.

27. Pursuant to Bankruptcy Code § 105(a), a bankruptcy court "may issue any order, process or judgment that is necessary or appropriate to carry out the provisions of [the Bankruptcy Code]." *See* 11 U.S.C. §105(a). Bankruptcy Code § 363(b)(1)

provides, "The trustee, after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate." 11 U.S.C. §363(b)(1). The proposed use, sale or lease of property of the estate may be approved under Bankruptcy Code § 363(b) if it is supported by sound business justification. *See e.g. In re Terrace Gardens Park Partnership*, 96 B.R. 707, 714; *see also In re Crutcher Resources Corp.*, 72 B.R. 628, 631 (Bankr. N.D. Tex. 1987) ("A Bankruptcy Judge has considerable discretion in approving a § 363(b) sale of property of the estate other than in the ordinary course of business, but the movant must articulate some business justification for the sale") (Bankr. W.D. Tex. 1989); *see also The Institutional Creditors of Continental Air Lines, Inc. v. Continental Air Lines, Inc. (In re Continental Air Lines)*, 780 F.2d 1223, 1226 (5th Cir. 1986) ("for a debtor-in-possession or trustee to satisfy its fiduciary duty to the debtor, creditors and equity holders, there must be some articulated business justification for using, selling, or leasing the property outside the ordinary course of business"); *see also Myers v. Myers (In re Marlin)*, 91 F.3d 389, 395 (3rd Cir. 1996); *In re W.A. Mallory Company, Inc.*, 214 B.R. 834, 836 (Bankr. E.D. Va. 1997) (with respect to pre-confirmation asset sales, "great deference is given to a business to determine its own best interests."); *see also In re Delaware & Hudon Ry. Co.*, 124 B.R. 169, 176 (D. Del. 1991) (outlining requirements for sale of assets pursuant to section 363); *In re Phoenix Steel Corp.*, 82 B.R. 334, 335-36 (Bankr. D. Del. 1987) (stating that judicial approval of a section 363 sale requires a showing that the proposed sale is fair and equitable, a good business reason exists for completing the sale and that the transaction is in good faith); *Committee of Equity Sec. Holders v. Lionel Corp. (In re Lionel Corp.)*, 722 F.2d 1063, 1070 (2d Cir. 1983); *Stephens Indus., Inc. v. McClung*, 789 F.2d 386, 389-90 (6th Cir. 1986). Further, in reviewing a proposed sale of assets, a bankruptcy court should give deference to the business judgment of a debtor in possession when it deems the sale to be appropriate. *See Esposito v. Title Ins. Co. (In re Fernwood Mkts.)*, 73 B.R. 616, 621 n.2 (Bankr. E.D. Pa. 1987).

28. The Debtors have determined in the exercise of their business judgment that the Sale is in the best interest of their estates and creditors.

29. Bankruptcy Code § 363(m) states, in relevant part:

> The reversal or modification on appeal of an authorization under subsection (b) or (c) of this section of a sale or lease of property does not affect the validity of a sale or lease under such authorization to an entity that purchased or leased such property in good faith, whether or not such entity knew of the pendency of the appeal, unless such authorization and such sale or lease were stayed pending appeal.

11 U.S.C. § 363(m).

30. The Sale and SPA are the result of an arm's-length, good-faith negotiation between the Debtors and Buyer. Both the Debtors and Buyer have retained legal counsel and have conducted due diligence, negotiations, and revisions of the SPA, as necessary under the circumstances. The Debtors believe the Buyer is a "good-faith" purchaser within the meaning of Bankruptcy Code § 363(m). Accordingly, at the Sale Hearing, the Debtors will request findings and protections pursuant to Bankruptcy Code § 363(m).

WAIVER OF 10-DAY STAY

31. Bankruptcy Rule 6004(g) provides, "An order authorizing the use, sale, or lease of property other than cash collateral is stayed until the expiration of 10 days after entry of the order, unless the court orders otherwise." FED. R. BANKR. P. 6004(g).

Because the parties intend to close the Sale of the Assets as soon as practicable after the entry of an Order approving the Sale, the Debtors request that the Court waive the 10-day stay provided in Bankruptcy Rule 6004(g).

PRAYER

The Debtors request that this Court enter an Order approving the Sale and granting them such other and further relief, both general and specific, to which they may be justly entitled.

Dated: November 16, 2004.

Respectfully submitted,

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