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Case No. 21-10449

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

In the Matter of: Highland Capital Management, L.P.,

Debtor.

NexPoint Advisors, L.P.; Highland Capital Management Fund Advisors, L.P.; Highland Income Fund; NexPoint Strategic Opportunities Fund; Highland Global Allocation Fund; NexPoint Capital, Incorporated; James Dondero; The Dugaboy Investment Trust; Get Good Trust,

Appellants,

v.

Highland Capital Management, L.P.,

Appellee.

REPLY BRIEF OF APPELLANTS NEXPOINT ADVISORS, L.P. AND HIGHLAND CAPITAL MANAGEMENT FUND ADVISORS, L.P.

Direct Appeal from the United States Bankruptcy Court for
the Northern District of Texas, the Honorable Stacey G.C. Jernigan

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REPLY BRIEF OF APPELLANTS NEXPOINT ADVISORS, L.P. AND HIGHLAND CAPITAL MANAGEMENT FUND ADVISORS, L.P.

NexPoint Advisors, L.P. and Highland Capital Management Fund Advisors, L.P. (the "Advisors"), two of the appellants in this bankruptcy appeal (collectively, the "Appellants"), hereby submit this *Reply Brief*.

I. SUMMARY

As it did below, the Debtor basically argues that all the appellants are vexatious, bad-faith litigants—despite being highly reputable entities that own and manage billions of dollars that others have entrusted to them—and that this somehow enabled the Bankruptcy Court to override the statutes, confer jurisdiction upon itself, disregard this Court's precedent, and basically do whatever the Debtor asked. Yet there is no proof of any vexatiousness in the record. There are no detailed findings of fact supporting any such argument. There is no history of past violations or sanctions. There are just the Debtor's histrionics, borne from the Advisors' refusal to submit to whatever demands the Debtor made. The Bankruptcy Court's real error was its failure to see through the Debtor's act.

But it is much simpler than that. The Plan's exculpation provisions are impermissible, the Plan violates the Absolute Priority Rule, and the Debtor failed to comply with Bankruptcy Rule 2015.3. None of these issues has anything to do with the Advisors. These are obligations the Debtor violated irrespective of any alleged vexatiousness or bad faith. Any alleged vexatiousness relates solely to the Plan's "gatekeeper" injunction, but that injunction too is impermissible because it effectuates a third-party release and because the record is devoid—as are the Bankruptcy Court's findings—of any fact justifying so extraordinary a sanction, even setting aside issues of the Bankruptcy Court's lack of jurisdiction.

At its core, though, the Debtor's argument is remarkably simple: effectuating its liquidation will be hard, expensive, and fraught with potential liability, and the Bankruptcy Court therefore has *carte blanche* authority to relieve the Debtor of these ills and duties. According to the Debtor, this even extends to exculpating the Debtor and myriad third parties from *future* liability as it manages more than $1 billion of other people's money. But where does it stop? If the Bankruptcy Court can ignore section 524(e) of the Bankruptcy Code, why not discharge anyone and everyone? If the Bankruptcy Court can disregard *Pacific Lumber*, then why not exculpate everyone for everything for all time? If the Bankruptcy Court is free to act outside the strict limits on bankruptcy jurisdiction, then why have principles of Federalism and Article III protections? And, if a bankruptcy court can protect a debtor post-confirmation, then why not stay in bankruptcy for perpetual Chapter 11 "protection?"

The Plan violates several key provisions of the statutes and this Court's precedent. It must be set aside. Doing so will not hamper the Debtor from otherwise liquidating its assets. It will not affect recoveries to creditors. It will not prejudice anyone. The Debtor must comply with the law like anyone else, whatever peculiar issues it may allege are unique to its case.

II. REPLY

A. THE PLAN VIOLATES THE ABSOLUTE PRIORITY RULE

The Debtor accuses the Advisors of being "particularly disingenuous" by arguing the Absolute Priority Rule because they acquired unsecured claims after confirmation and because they are not in the lower-priority classes receiving unfair treatment. The Debtor misses the point entirely: the Plan clearly enjoins and prejudicially affects the Advisors and their past, present, and prospective rights and claims, and the Plan could not have been confirmed without violating the Absolute Priority Rule. As the Plan could not have been confirmed without violating the Absolute Priority Rule, the Advisors have every right to raise this element of confirmation in their attempt to set aside the Plan as, without the Plan, there are no exculpations and injunctions. And, there can be no question of the Advisors' standing to contest or to appeal the plan, which necessarily includes each sub-element that led to the Plan's confirmation.

The Debtor argues that what the Absolute Priority Rule requires is that each claimant in a dissenting class receive property of a value equal to the allowed amount of the claim and that the statute "does not require payment in full on the effective date." Appellee Brief at p. 59. But that is wrong in two ways. First, framing the issue in terms of "payment" is misleading because it implies payment in cash. The statute doesn't use the word "payment." Instead, the statute uses the word "property." Second, the value of that property, *measured as of the effective date*, must equal the amount of such creditor's claim. 11 U.S.C. § 1129(b)(2)(B)(i) ("property of a value, *as of the effective date of the plan*, equal to the allowed amount of such claim …." (emphasis added)). Here, the "property" that Class 8 received—*i.e.* trust interests in the claimant trust—was worth, at best, 71.32 percent of their claims. ROA.4158. Thus, there can be no dispute that the Plan fails to provide Class 8 with "property of a value, as of the effective date of the plan, equal to the allowed amount" of their claims.

It is this failure that triggers the Absolute Priority Rule, which provides that "the holder of any claim or interest that is junior to the claims of [Class 8] will not receive or retain under the plan on account of such junior claim or interest *any property*." 11 U.S.C. § 1129(b)(2)(B)(ii) (emphasis added). It is telling indeed that the Debtor never once cites this provision, even though the Advisors cited and addressed it extensively and even though this provision, not 1129(b)(2)(B)(i), constitutes the Absolute Priority Rule. The Debtor's focus on section 1129(b)(2)(B)(i) is simply an attempt to divert the Court and cloud the issues.

The only question, therefore, is whether junior classes "receive or retain under the plan . . . any property." As the Advisors pointed out in their opening brief, there can be no dispute here. The Plan gives holders of junior classes, representing limited partnership equity interests, contingent interests in the claimant trust, which may or may not pay in the future. Contingent trust interests are property: as a matter of law and as a matter of fact as conceded on the record by both the Debtor's Chief Restructuring Officer and its lead counsel. ROA.4393-94 (Tr. 177:10 – 178:25); ROA.4758 (Tr. 242:20-21). That they may have little to no value is irrelevant, as the Supreme Court has made clear. *See, e.g., Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 207-08 (1988).

Class 8 rejected the Plan. But the Plan does not provide Class 8 with property with a value equal to the allowed amount of their claims—*i.e.* Class 8 is not "paid" in full. Accordingly, no junior class could receive or retain any "property." Junior classes, however, receive contingent trust interests on account of their equity interests, which contingent trust interests are "property." This clearly violates the Absolute Priority Rule. The "work-around" adopted by the Bankruptcy Court and the court in *In re Introgen Therapeutics*, to the effect that these contingent trust interests cannot be paid unless and until Class 8 is paid in full, violates the express language of the Bankruptcy Code—the contingent trust interests are "property" regardless of when, how, and whether they are ever paid. That is all that matters, and it is for Congress, not the Bankruptcy Court, to rewrite the statute.

The Court should therefore vacate the Confirmation Order and render judgment that the Bankruptcy Court is to deny confirmation of the Plan because the Plan violates the Absolute Priority Rule and therefore fails the elements of confirmation required by sections 1129(a)(8) and 1129(b)(1) of the Bankruptcy Code.

B. Plan's Impermissible Releases, Exculpation, and Injunctions

1. No Basis for Pre-Filing Injunction

Labeling someone a "vexatious litigant" is reserved for extraordinary cases, usually *pro se* litigants who are not bound by the lawyers' cannons of ethics. Courts have "no desire to deter any litigant from advancing any claim or defense which is *arguably* supported by existing law, or any reasonably based suggestion for its extension, modification, or reversal." *Farguson v. Mbank Houston*, *N.A.*, 808 F.2d 358, 359 (5th Cir. 1986) (emphasis added). "Positions thus taken cannot be considered as frivolous, although they may be unsuccessful and indeed may be given short shrift. But claims and defenses which fall outside of this broad umbrella may prove frivolous." *Id.* A vexatious litigant is not one who vigorously asserts legitimate rights, nor one who is simply annoying or an impediment to his adversary. *Id.* Indeed, a pre-suit injunction is a "drastic remedy" that "must be tailored to protect the courts and innocent parties, while preserving the legitimate rights of litigants." *Id.* at 360.

Nothing like that—nothing even close—is present here. The Advisors filed one motion in December, 2020 (represented by the highly reputable firm of K&L Gates) to restrict the Debtor from selling assets that were not property of the Debtor's estate but in which the Advisors' clients (publicly traded "retail funds" comprised of "mom and pop" investors) had an interest, which the Bankruptcy Court found to be frivolous—the only relevant finding with respect to the Advisors. The Advisors filed an administrative claim, which remains pending and has not been adjudicated. The rest of the Advisors' filings were done defensively in response to litigation initiated by the Debtor: one adversary proceeding and preliminary injunction request (based upon the aforementioned efforts to stop the Debtor from selling assets that were not property of the Debtor's estate); a second to collect on a promissory note against one of the Advisors; a third to collect on a promissory note against the other Advisor; and a fourth adversary proceeding seeking a mandatory injunction, which the Bankruptcy Court denied as moot. With the Plan, the Advisors objected, as is their right. That is it, and most of it is the Advisors acting defensively.

Indeed, in bankruptcy cases there is frequently an antagonist who contests many of the discrete motions and proceedings raised by a debtor. A secured creditor, for example, will frequently contest the use of cash collateral, will file administrative claims, may move to appoint a trustee or dismiss the case, may contest professional fees, may contest settlement motions, and is likely to contest a plan. While these positions may ultimately fail, they cannot be considered frivolous as long as they are arguably supported by existing law, or any reasonably based suggestion for its extension, modification, or reversal. *Farguson*, 808 F.2d at 359. Defending one's self in adversary proceedings commenced by a debtor, and contesting the confirmation of the debtor's plan or other motions in the bankruptcy case, does not rise to the level of vexatious litigation.

2. No Detailed Findings Supporting Anti-Filing Injunction

More to the point, the Bankruptcy Court did not make any of the underlying findings necessary to sustain a pre-filing injunction. A court may order a pre-filing injunction only "to deter vexatious, abusive, and harassing litigation." *Baum v. Blue Moon Ventures LLC*, 513 F.3d 181, 187 (5th Cir. 2008). The following four requirements are to be considered: "(1) the party's history of litigation, in particular whether he has filed vexatious, harassing, or duplicative lawsuits; (2) whether the party had a good faith basis for pursuing the litigation, or simply intended to harass; (3) the extent of the burden on the courts and other parties resulting from the party's filings; and (4) the adequacy of alternative sanctions." *Id*. at 189. A pre-filing injunction cannot extend to filings in state court: "those courts or agencies are capable of taking appropriate action on their own." *Id*. at 192 (internal quotation omitted).

An anti-filing injunction is a sanction. *See Qureshi v. United States*, 600 F.3d 523, 526 (5th Cir. 2010) ("a pre-filing injunction . . . falls within the same class as sanctions, costs, attorney's fees, and contempt remedies"). And, sanctions of this severe character require detailed findings of fact. *See, e.g., FDIC v. Calhoun*, 34 F.3d 1291, 1297 (5th Cir. 1994). Before a pre-filing injunction can be ordered, there should be an extensive history of prior vexatiousness, lesser sanctions, and warnings.

See, e.g., Budri v. FirstFleet Inc., 2019 U.S. Dist. LEXIS 188250 at *13-*18 (N.D. Tex. 2019) (denying injunction "as not yet warranted" and issuing "formal reprimand and stern warning" instead). Likewise, "injunctions against filing future lawsuits without a prior warning are strongly disfavored." *McCampbell v. KMPG Peat Marwick LLP*, 982 F. Supp. 2d 445, 449 n. 6 (N.D. Tex. 1997).

To the extent that the Bankruptcy Court's power to enter an anti-filing injunction is the basis for the Plan's "gatekeeper" injunction, the Bankruptcy Court violated all of the foregoing requirements and principles.

First, there are no detailed findings of fact on issues related to any alleged vexatiousness of the Advisors: no prior finding of vexatiousness, no prior sanction, no repetitive assertion of rejected arguments, no pursuit of theories or claims in bad faith (*i.e.*, that are not arguably supported by existing law, or any reasonably based suggestion for its extension, modification, or reversal)—none of the "history of litigation" involving sanctionable conduct. Indeed, the Bankruptcy Court did not even find that the Advisors had ever acted vexatiously:

> Here, although I have not been asked to declare Mr. Dondero and his affiliated entities as vexatious litigants per se, it is certainly not beyond the pale to find that his long history with regard to the major creditors in this case has strayed into that possible realm, and thus this Court is justified in approving this provision.

ROA.4819.

The alleged "long history" of litigation did not involve the Advisors, and usually only involved "Mr. Dondero and his affiliated entities" as defendants. *See*

ROA.16354 (Mr. Dondero was a defendant in a case brought by Joshua Terry); ROA.16395 (Highland CLO Management, LLC was a defendant in a case brought by NWCC, LLC); ROA.16898 (the Debtor was a defendant in a case brought by UBS Securities); ROA.16926 (the Debtor was a defendant in another case brought by UBS Securities); ROA.16930 (the Debtor was a defendant in a case brought by Redeemer Committee of the Highland Crusader Fund); ROA.17027 (the Debtor was a defendant in a case brought by Patrick Daughtery).

Believing that "it is certainly not beyond the pale" that one individual "strayed into that possible realm" of vexatiousness, with vague examples in the record, is hardly the kind of extensive and specific factual finding required to enjoin someone's access to the courts.

Second, the extent of the Bankruptcy Court's findings of alleged vexatiousness (that Mr. Dondero was a serial filer or had litigated in bad faith) pertain only to Mr. Dondero. ROA.68-70 (¶¶ 77-79). These findings, themselves wrong, are directed at Mr. Dondero alone. The Confirmation Order contains no such finding regarding the Advisors. At most, there are generalized findings (conclusory findings, really) that entities affiliated with Mr. Dondero have also acted inappropriately in litigation. But so serious a sanction requires detailed findings, and there simply are none with respect to the Advisors: no finding of fact regarding prior vexatious, bad-faith filings of the Advisors; nor of any prior formal warning to the Advisors; nor any prior sanction, monetary or otherwise, on the Advisors.

Third, the justifications the Bankruptcy Court gave to explain its injunction do not support this extraordinary remedy. The Bankruptcy Court justified any pre-filing injunction as necessary to the Debtor's ability to obtain directors and officers insurance. ROA.70 (¶ 79). The Bankruptcy Court found that, without the injunction, Dondero and his related entities will "likely commence litigation . . . in jurisdictions other than the Bankruptcy Court in an effort to obtain a forum which Mr. Dondero perceives will be more hospitable to his claims." ROA.69 (¶ 78). The Bankruptcy Court found that, without the injunction, post-confirmation litigation "will impede efforts by the Claimant Trust to monetize assets for the benefit of creditors and result in lower distributions to creditors." *Id.* The need to obtain insurance, a desire to prevent lawful forum shopping, and a desire to help the claimant trust recover more money are simply not proper or just grounds to limit one's right to access the courts. On the contrary, these justifications are repugnant to any notion of equity or justice. And, as a severe sanction, an anti-filing injunction does not look to the *benefits* that may be conferred on the protected party but rather the need to *deter* improper litigation conduct by the offender.

Fourth, the Bankruptcy Court also failed to consider any less severe alternative. Again, the Advisors had not been sanctioned before, so the normal progression of sanctions and warnings under Rule 11 and section 1927 was not even given a chance (not that there was any need for it). The Advisors are large and reputable business entities with professional and capable counsel. There is no indication that the normal tools that protect the integrity of the system would be insufficient. There is no indication that the Advisors or their counsel would not be able to pay any monetary sanction, if they violate any rule. Only where "monetary sanctions are ineffective in deterring vexatious filings" would "enjoining such filings [] be considered." *Farguson v. MBank Houston NA*, 808 F.2d 358, 360 (5th Cir. 1986). The Bankruptcy Court's findings of fact are silent on these important points.

Fifth, the pre-filing injunction applies to all courts, including state courts and courts outside of this Circuit. As this Court has previously held, however, these courts are capable of protecting themselves and litigants before them. *Baum*, 513 F.3d at 192. If the Bankruptcy Code stays or prohibits litigation (such as with a discharge), then the Bankruptcy Court can enjoin filings in other courts. But that is not the case here. The "gatekeeper" injunction admittedly applies to many claims and persons not protected by the Debtor's discharge.

Finally, and this point should not be lost, the "gatekeeper" injunction applies not only to past and present claims and causes of action, but also to any that may arise in the future. Nor does it apply only to claims against the Debtor. The list of "protected parties" is boundless. This is unprecedented. How can the Bankruptcy Court possibly conclude that any filing by the Advisors in the future based on potential future violations of the law by any of the "protected parties" would be vexatious, harassing, or brought in bad faith?

3. No Jurisdiction to Enjoin Future Actions

The Debtor argues that this Court, in *Villegas*, held that "the bankruptcy court can act as a gatekeeper even if does not have jurisdiction to adjudicate the underlying dispute." Appellee Brief at p. 29 (citing *Villegas v. Schmidt*, 788 F.3d 156 (5th Cir. 2015)). The Advisors have closely reviewed *Villegas*, in particular the pinpoint citation given by the Debtor (at pages 159-59) and find nothing in *Villegas* addressing or supporting the Debtor's contention. Rather, *Villegas* holds that the Barton Doctrine (inapplicable in Chapter 11) continues to apply post *Stern v. Marshal* (an opinion concerning the Constitutional authority of the bankruptcy court) even if the bankruptcy court lacks jurisdiction over the underlying dispute.

In fact, *Villegas* is highly instructive for a different reason, because the Court held that "[i]f a bankruptcy court concludes that the claim against a trustee is one that the court would not itself be able to resolve under *Stern*, that court can make the initial decision on the procedure to follow." *Id*. at 158-59 (emphasis added). What the Bankruptcy Court did here, however, is far different and differs from anti-injunction cases where leave from the court is required prior to commencing suit.

Here, the Bankruptcy Court required, as a *substantive* requirement for such leave, that the movant prove the existence of a "colorable" claim. This is not merely a "procedural" hurdle as contemplated in *Villegas*. No known anti-injunction or Barton case requires parties to prove a colorable claim. An anti-filing injunction is a personal sanction against a party. It is logical that the party must demonstrate its good faith before receiving leave to proceed. But that is far different from a substantive filter, which is what a "colorable claim" standard imposes, much like Rule 12(b)(6).

The Bankruptcy Court will be the sole and exclusive court to determine whether a colorable claim exists based on future post-confirmation actions against non-debtors having nothing to do with the bankruptcy case, the Plan, or the discharge. That involves more than merely granting leave to proceed. This is a substantive determination. If the Bankruptcy Court determines that a claim is not "colorable," then that is it: a court that clearly has no subject matter jurisdiction over the dispute will have fully disposed of a cause of action. This amounts a massive usurpation of jurisdiction by the Bankruptcy Court, to the exclusion of all other courts. Neither *Villegas*, the Barton Doctrine, nor any known anti-filing-injunction case supports that outcome; they all contradict it. And, this massive appropriation of jurisdiction eviscerates principles of federalism, the necessities of the federal courts' limited jurisdiction, and the dictates of Article III of the Constitution.

It is simply unprecedented, unsupportable, and dangerous for a bankruptcy court to order that a party must come before it, eventually even in a closed bankruptcy case where reopening the case itself is discretionary, and prove that a colorable claim under non-bankruptcy and potentially state law, including torts and personal injury, exists for future actions and claims. It is the kind of monarchical power that our Constitution protects against.

4. <u>Issues of Vexatiousness Do Not Permit Exculpation</u>

In addition to the gatekeeper provision, the Plan includes a broad, impermissible, and unprecedented exculpation provision that not only exculpates the Debtor, but the same extensive list of "protected parties." The Debtor attempts to bootstrap its "vexatious litigant" argument to justify the exculpation provision, but (as detailed above) there has not even been a proper finding of vexatiousness against the Advisors (and certainly not the unknowing third parties, such as the investors whose funds the Debtor manages, who are also bound by its releases). But none of that empowers the Bankruptcy Court to exculpate anyone. If one receives exculpation in the first place, then a "gatekeeper" injunction is irrelevant because there is no "colorable" claim *a priori*. Exculpation, which is valid as against the world, has nothing to do with anyone's alleged vexatiousness or anyone's alleged bad faith litigation motives.

The fundamental problem with the Debtor's argument is the same as the Advisors raised in their opening brief: what portion of the Bankruptcy Code authorizes exculpation? The Debtor seeks to cloud this simple question by micro-analyzing precedent to argue that exculpation is not prohibited by that precedent, but that is the second step. The first step remains the one the Debtor did not take: what portion of the Bankruptcy Code authorizes exculpation? None. On the contrary, as *Pacific Lumber* expressly recognizes, the Bankruptcy Code makes clear that a debtor's discharge does not discharge or release anyone but the debtor. *See* 11

U.S.C. § 524(e). And, as this Court has repeatedly made clear, the Bankruptcy Court's broad equitable powers under section 105(a) of the Bankruptcy Code do not empower the Bankruptcy Court to override or contradict an express provision of the Bankruptcy Code. *See, e.g., Southmark Corp. v. Grosz (In the Matter of Southmark Corp.)*, 49 F.3d 1111, 1116 (5th Cir. 1995).

The Debtor again relies on the Barton Doctrine. The Advisors have explained why *Barton* has no application to Chapter 11 or the facts of this case and why *Barton* conflicts with the express provisions of the statute. *See* 28 U.S.C. § 959(a). But, assuming that *Barton* applies, all that it holds is that a plaintiff must obtain leave from the appointing court before a receiver (and by extension a trustee) may be sued. *See Barton v. Barbour*, 104 U.S. 126 (1881). It does not exculpate anyone. It does not impose a "colorable claim" requirement prior to suit.

Finally, none of the Debtor's arguments, nor any reported opinion authorizing exculpations, authorizes the Bankruptcy Court to exculpate the myriad persons, professionals, and entities, including non-debtors, that this one does—especially not for <u>future</u> actions, omissions, and liabilities. It really is a "get out of jail free card" that is unprecedented and that the Bankruptcy Court has no jurisdiction, power, or authority to bestow—if indeed any court in our democratic and just system has.[1]

[1] A court may immunize its own agents, for limited, known, and discrete things, such as the U.S. Marshals executing a writ. That is far different from an Article I court immunizing various highly-paid people who are not its agents as they operate a business into the future.

C. <u>The Debtor's Violations of Bankruptcy Rule 2015.3 Prevented Confirmation of the Plan</u>

The Debtor concedes that it utterly failed to comply with Bankruptcy Rule 2015.3, but the Debtor contends that denying confirmation based on this failure "would fall within the absurdity doctrine." Appellee Brief at p. 63. This is a remarkable argument, as a debtor has many obligations, reporting or otherwise, under the Bankruptcy Code. There are consequences for failing to comply with those obligations, particularly when a debtor utterly fails to provide basic financial reporting and information concerning hundreds of millions of dollars in property it indirectly owns through subsidiaries. Or, is there no consequence for failing, for eighteen months, to comply with a mandatory "shall" requirement in the Bankruptcy Rules? That is the absurd argument.

The absurdity doctrine requires that the "result must be preposterous, one that no reasonable person could intend." *Tex. Brine Co. LLC v. Am. Arbitration Ass'n*, 955 F.3d 482, 486 (5th Cir. 2020). It can hardly be said that no reasonable person could conclude that a debtor, who has utterly failed to comply with a disclosure and reporting requirement the law imposes on it, should be able then to freely obtain confirmation without proving significant excusable neglect and without taking immediate corrective action—neither of which occurred here. Instead, the Debtor cavalierly said 'whoops,' informing the Bankruptcy Court that, despite almost 18 months and tens of millions of dollars in professional fees, "it fell through the cracks." ROA.1564 (Tr. 49:5-21). Never mind that the Debtor was providing the same information to the Committee behind closed doors on a weekly basis. *See* ROA.15323-25 (protocols requiring weekly reporting); ROA.15336 (order approving protocols).

The Debtor also argues that its failure to comply with Bankruptcy Rule 2015.3 does not mean that it failed to "compl[y] with the applicable provisions of this title" as required by section 1129(a)(2) of the Bankruptcy Code. Here, the Debtor argues that this provision has been limited to requiring compliance with "the disclosure requirements of section 1125." Appellee Brief at p. 62. There are certain lower court opinions that agree with the Debtor. But the Debtor and these opinions are wrong and, as pointed out by the Advisors, other opinions hold otherwise. *See In re Seatco, Inc.*, 257 B.R. 469, 479 (Bankr. N.D. Tex. 2001) (holding that section 1129(a)(2) applies to reorganization provisions[2]).

Section 1125 already provides that no plan may be solicited without an approved disclosure statement. *See* 11 U.S.C. § 1125(b). There is no need to limit section 1129(a)(2) to providing the same. Section 1129(a)(1) requires that a plan comply with all applicable provisions, thus already providing a remedy if section 1125 is violated. *See* 11 U.S.C. § 1129(a)(1). And what about non-section 1125 issues? What if a debtor fails to pay a filing fee, fails to file schedules and

[2] Bankruptcy Rule 2015.3 is undoubtedly a reorganization provision, as it expressly applies only to Chapter 11 cases.

statements, violates the prohibition on using cash collateral or obtaining debt without court approval, or one of the myriad other requirements, limitations, and obligations under the Bankruptcy Code? Should all that be forgotten at confirmation? Of course not; a debtor cannot ignore its own obligations and sweep all of its violations away by confirming a plan—especially over the votes of its creditors. But agreeing with the Debtor's reasoning would provide a perverse incentive to mischievous debtors to do precisely that.

Rather, when section 1129(a)(2) requires compliance with "the applicable provisions of this title," it merely recognizes that the Bankruptcy Code has multiple chapters and types of proceedings. There is a Chapter 7 liquidation, a Chapter 9 municipality case, a Chapter 13 consumer reorganization, a Chapter 12 farmer reorganization, and a Chapter 15 cross-border case. "Applicable" provisions therefore means those provisions applicable to a Chapter 11 case, as opposed to a different type of case, and "applicable" means those provisions which apply to the plan's proponent, as opposed to some other bankruptcy participant who may have violated its own obligations. Bankruptcy Rule 2015.3 is certainly and expressly applicable to Chapter 11. *See* FED. R. BANKR. P. 2015.3(a).

Finally, the Debtor argues that the Bankruptcy Court had the ability to vary Rule 2015.3's reporting requirements, which the Debtor argues the Bankruptcy Court did when it approved certain protocols between the Debtor and the Committee. Remarkably, the Debtor argues that:

> The operating protocols entered as part of the Governance Settlement served this function and provided the information and protections concerning Highland's operations, subsidiaries, and affiliates that would have been provided by the Rule 2015.3 reports.

Appellee Brief at p. 63.

This is a remarkable argument because it admits that the Debtor had all the necessary information and had prepared all the necessary reports, meaning that it could have easily complied with Bankruptcy Rule 2015.3. Compliance with that Rule would not have been "difficult" as the Debtor testified. ROA.1564 (Tr. 49:5-21). Nor do the protocols live up to the rule's spirit when they left nearly all creditors in the dark. Why not then simply file the information and make it available to all creditors and other parties-in-interest, as opposed to sharing it in secret with the Committee?

The argument also implies that the Debtor always understood and intended for the "protocols" somehow to supplant or replace the requirements of Bankruptcy Rule 2015.3. But this, of course, belies the Debtor's own testimony that such compliance was an oversight and that "it feel through the cracks." *Id.* And, if there really was any such intent, then why did the Bankruptcy Court not so clarify in its ninety (90) pages of written findings and conclusions or its fifty (50) pages of oral findings and conclusions, instead of wholly omitting any discussion of the issue?

The Court should therefore see the Debtor's argument for what it is: an after-the-fact, contrived argument bearing no relation to the facts or to anyone's actual intentions. Rather, although the Bankruptcy Court had the authority to "vary" the requirements of Bankruptcy Rule 2015.3 "after notice and a hearing," the Debtor never requested that it do so—not even after the fact, *nunc pro tunc*—and the Bankruptcy Court never entered an order granting any such relief.

The fact remains that the Debtor failed to comply, for eighteen (18) months, with a fundamental and critical rule of bankruptcy disclosure, and that it has offered no satisfactory or credible explanation for this failure either then or now. The fact remains that this failure concerned hundreds of millions of dollars of assets and value, information about which the Debtor kept from its creditors and parties in interest. The fact remains that the Debtor had this information at its fingertips and could easily have filed it—including in redacted format if needed—yet did not do so. And, the fact remains that the Plan was a hotly contested plan where the class of unsecured creditors rejected confirmation by a wide margin (27 rejecting and only 17 accepting, and the Bankruptcy Code requiring a 2/3d affirmative vote). ROA.4202. This is not the case to sweep this serious violation of the Bankruptcy Rules under the rug.

The Court should therefore vacate the Confirmation Order and render judgment that the Bankruptcy Court enter an order denying confirmation of the Plan because the Debtor failed to comply with Bankruptcy Rule 2015.3, and therefore that it failed to comply with sections 704(a)(8), 1106(a)(1), and 1107(a) of the Bankruptcy Code, meaning that it failed to comply with all applicable provisions of the Bankruptcy Code as required for confirmation by section 1129(a)(2) of the Bankruptcy Code. There is nothing absurd about such a result. Instead, such a result would be a lesson to other debtors to take their reporting requirements seriously and to comply with their bankruptcy duties. After all, debtors obtain massive benefits from Chapter 11. It is not too much to ask that they at least report in detail the required financial information regarding their assets and their subsidiaries.

III. CONCLUSION

The Plan violates the Absolute Priority Rule. The Plan contains sweeping, broad, prospective, and unprecedented exculpations prohibited by the Bankruptcy Code and *Pacific Lumber*. The Plan contains a "gatekeeper" injunction without basis in fact or in law. The Debtor violated Bankruptcy Rule 2015.3. Each of these issues individually mandated a denial of confirmation of the Plan. Taken collectively, and especially given that the large majority of Class 8 unsecured creditors *rejected* the Plan, the Plan violates the Bankruptcy Code in some of its most important respects, as well as the rights of the Advisors and many others. This Court should forcefully vacate the Confirmation Order and render judgment that the Plan be denied confirmation.

RESPECTFULLY SUBMITTED this 27th day of October, 2021.

MUNSCH HARDT KOPF & HARR, P.C.

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that, on this the 27th day of October, 2021, a true and a correct copy of the foregoing document was served on the counsel of record listed below via electronic service.

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CERTIFICATE OF COMPLIANCE WITH RULE 32(a)'s TYPE-VOLUME LIMITATION, TYPEFACE LIMITATION, AND TYPE-STYLE REQUIREMENTS

1. This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) because this brief contains 5,528 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

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Dated: October 27, 2021.

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