Docket #0051 Date Filed: 3/15/2022

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF TEXAS

DALLAS DIVISION

IN RE HIGHLAND CAPITAL MANAGEMENT, L.P., Debtor.	(	3:21-CV-1895-D
HIGHLAND CAPITAL MANAGEMENT FUND ADVISORS, L.P., et al, Appellants	(	DALLAS, TEXAS
VS.	(	
HIGHLAND CAPITAL MANAGEMENT, L.P., Appellee.	(	JANUARY 25, 2022

TRANSCRIPT OF ORAL ARGUMENT VIA ZOOM

BEFORE THE HONORABLE SIDNEY A. FITZWATER

UNITED STATES DISTRICT JUDGE

A P P E A R A N C E S:

FOR THE APPELLEE: JEFFREY N. POMERANTZ
Pachulski Stang Ziehl & Jones LLP
10100 Santa Monica Blvd
13th Floor
Los Angeles, CA 90067
310-227-6910
Fax: 310-201-0760
Email: jpomerantz@pszjlaw.com

FOR THE APPELLANTS: DAVOR RUKAVINA
Munsch Hardt Kopf & Harr PC
500 N Akard St
Ste 3800
Dallas, TX 75201
214-855-7587
Email: drukavina@munsch.com

DOUGLAS DRAPER
Heller, Draper & Horn, L.L.C.
650 Poydras Street
Suite 2500
New Orleans, LA 70130
504-299-3300
Fax: 504-299-3399
Email: ddraper@hellerdraper.com

COURT REPORTER: PAMELA J. WILSON, RMR, CRR
pam_wilson@txnd.uscourts.gov
1100 Commerce Street, Room 1535
Dallas, Texas 75242
214.662.1557

Proceedings reported by mechanical stenography, transcript produced by computer.

ORAL ARGUMENT VIA ZOOM - JANUARY 25, 2022

P R O C E E D I N G S

THE COURT: The matter before the court is in re: Highland Capital Management bankruptcy appeal oral argument.

Before we begin I have some housekeeping matters to cover.

First of all, if at some point we lose the court reporter, obviously, we need to stop. I hope that will not happen, but if that occurs we will.

And if we have any technical difficulties that interrupt counsel's argument time, then I will add to your time so that you have your full allocated time.

The law clerk is aware of the time warnings that you want and I have advised him to interrupt you or interrupt me so that he can announce those time warnings as needed.

At this time then we'll begin with counsel for the appellants. I believe that's going to be divided time, so if you would proceed at this time.

MR. RUKAVINA: Your Honor, good morning.

Davor Rukavina of Munsch Hardt Kopf & Harr for two of the appellants we call the advisors. I'll be discussing the substance of the appeal, and my co-counsel, Douglas Draper, who represents the Dugaboy Trust, will be addressing the two motions to dismiss.

Your Honor, may it please the court.

Let me first reiterate what we argued in our brief, which is that this matter is very much a matter about substance. This is not a matter of procedure. This is not a case where -- where someone can say harmless error or where someone can say, okay, so what, the wrong procedure was followed. It is substance that goes to the core of the bankruptcy court's jurisdiction and what it does, because it deals with a confirmed plan. It is substance because the Bankruptcy Code has an express section dealing with plan modifications, if this is a plan modification.

THE COURT: Counsel, could I ask you a couple of questions before you continue on?

First of all, would you address the difference between indemnifying out of reserves and indemnifying out of the subtrust.

And second, would you address the assertion that the bankruptcy court order does not really add to the universe of entities who are eligible for indemnification.

MR. RUKAVINA: Thank you, Your Honor.

I think both of those questions revolve around the same answer, which is that the plan created originally three legal entities, the reorganized debtor, the litigation subtrust, and then the master claim and trust. Each of those entities was originally obligated to indemnify its own logistical and professionals. It's a little bit broader than that. There

was no cross indemnification. And it's my understanding that, yes, the claim and trust could reserve funds for the indemnification purposes. That is correct. But what the litigation trust or the claim and trust could reserve from its own funds on hand is different than what we have now. For example, we have a $22.5 million promissory note. That's not just reserving funds on hand. That is the future obligation that needs to be repaid before any creditors can be repaid.

But I think more importantly -- Your Honor, I apologize. Someone is typing and I can hear them and it's -- it's interfering with my ability to talk. But it might just be the court reporter, so I'll continue.

But, Your Honor -- and we have discussed this our reply brief in detail. There is no question that under this new order the claim and trust now is responsible for indemnifying people whom it was not responsible to indemnify in the beginning.

And another thing that I'll point out, Your Honor, with this indemnification subtrust, they're going to have to hold the $25 million until all possible indemnification claims are asserted and resolved. Under Texas law that's four years for breach of fiduciary duty.

So it's not a matter of the debtor's trustee in the exercise of his business judgment reserving some funds at any

given point to address conceived of or potential or threatened indemnification claims. It is a matter of tying up $25 million for years to come and by the claim and trust indemnifying people whom it alone -- or it itself was not indemnifying before.

Assume, Your Honor, arguendo, that -- that the litigation trust created under the plan didn't have the money to indemnify its personnel. That it -- it -- it ran through its seed money, it -- it-- it prosecuted litigation --

THE COURT: We've lost your sound.

(Pause.)

Now you're back on.

And I'll instruct the law clerk to add a minute to his time.

MR. RUKAVINA: Thank you.

Your Honor, what I was saying is that hypothetically the original litigation trust could just not have money to indemnify its personnel. Well, now, the claim and trust from its own funds, from it's $25 million, does so. So I hope I've addressed that portion of the court's question.

If I return to -- to what is a plan modification, Your Honor. Well, first, a plan is a contract. That's black letter bankruptcy law. The contract can be sued upon in state court. So I think Congress, just like fundamental contract law, they say a debtor can't unilaterally modify its

contract. No -- no contract party can just unilaterally modify a contract. So you have to follow the 1127(b) prescribed mechanism for a plan modification. And that has extreme safeguards. Your Honor, you have to have a disclosure statement that goes to all the creditors that discloses the economic impact in detail, the length, for example, I mentioned four years, that -- that tells the creditors and other parties in interest everything that the debtor knows in an approved format so that it's reasonably accurate for the creditors to make a decision.

That's the second point. A modification is voted upon. Here the creditors originally rejected the plan. We believe that they would likely reject the modification. But the creditor democracy is critical to Chapter 11 proceedings. The way that the bankruptcy court proceeded here, we didn't have that.

And third, and most importantly, this motion was approved under a very flexible, equitable, multifactor business judgment test. Section 1129 that governors confirmation has something like 14 elements, not factors, each of which must be proven with competent evidence.

And if the bankruptcy court proceeds on what's called cram down to confirm a plan that's been rejected, now you have two additional very heightened elements. That's what I mean that this is about substance.

And -- and we believe that if this proceeded as a plan modification it would have been rejected and denied.

Briefly, Your Honor, before I defer to Mr. Draper, we've briefed this at length, but a plan modification is something that changes a plan. We know that from U.S. Brass. In U.S. Brass the plan provided for litigation by trial of claims. It was changed later on to provide for litigation by arbitration. It didn't change the economics of the plan. It didn't change how much creditors were being paid. Yet the Fifth Circuit had no problem in -- in construing that as a plan modification, something that was prohibited in that case.

So the burden is pretty slight to find that a change to a plan is a plan modification. Again, because a debtor ought not to be able to unilaterally change its contract and creditor democracy in Chapter 11 is the key.

Here, Your Honor, there is no question that a new trust is being created, the indemnification subtrust. Your Honor, Chapter 11 trusts are created under plans. They're not created by motion. I would urge any -- any counsel who is a bankruptcy expert to give the court a single case where a trust was created by motion. That's a plan issue.

$25 million is potentially being removed from creditors. It may turn out to be a zero, that's true. But we won't know for many years to come. And in the meantime that $25 million

is tied up.

You have this increased indemnification of professionals by the creditor trust that you did not have before. There was no cross indemnification before. There was no guarantee under indemnification. And you have the fact that the plan expressly contemplated as a condition precedent DNO insurance, which could be waived, and they did waive it, but the plan required DNO insurance and now you're substituting that with this new trust. That, Your Honor, is a modification. It changes what is in the plan, both each of those things individually, and certainly I would argue in the totality of the circumstances.

Mr. Draper will now handle the motions to dismiss.

I would just point out as counsel for NexPoint that NexPoint did have five claims, known claims, when this appeal was commenced, and until recently NexPoint had the sixth claim, Hunter Covitz, which there was confusion internally at the HR department, but it always had that claim. That claim has been disallowed very recently. We are appealing that disallowance order because it was disallowed without a hearing and on negative notice, in violation of Rule 55.

And most importantly for standing, the plan requires the creditor -- creditor trust to reserve more than $200,000 for that claim until that claim is definitively and finally adjudicated by final order. We also have $14 million of

administrative claims that we're going to go to trial on probably now in April. They have not been disallowed. They have not been paid.

Your Honor, with that, I'll yield the balance of our 15 minutes to Mr. Draper.

MR. DRAPER: Your Honor, Douglas Draper.

Thank you very much for allowing this by zoom.

I'm going to address a few items that will be very quick and certainly things that are I believe lost in the pleadings and the papers that have been filed. The first one is citing Judge Jones in Pacific Lumber. Equitable mootness should be employed with a scalpel and not an axe. So it has to be narrow in its scope. I'd ask -- though we're talking about plan modifications, understand that the matter before you is not an appeal of the confirmation order. It is appeal of a separate order that is not the confirmation order.

And I'd ask the court to look at two cases, really three cases. Number 1 is the -- the concept of substantial consummation. And in U.S. Brass the Fifth Circuit held that substantial consummation was not a bar to a -- a equitable mootness and was not a cause for equitable mootness.

The next two cases are probably even more important. In Walker Hospital, which is in Sneed Shipbuilding, the Fifth Circuit expressly said equitable movements only applies to two types of orders: One an order confirming a plan, that's

not this case; and number two, an order under 363-M. This is not a sale order either.

So by virtue of the Fifth Circuit's express provisions in both Sneed and in Walker equitable mootness is not a -- is not a bar and should not be the cause of dismissal of this debtor's appeal.

The last issue I'd like to address, and I'd ask the court to take a look at, is a recent case out of the Eighth Circuit, which is VeroBlue. That is a very well-written opinion.

THE COURT: I think we've lost Mr. Draper's sound.

MR. DRAPER: Can you hear me?

THE COURT: Now I can. Okay. Go ahead, Mr. Draper. MR. DRAPER: Where did you lose me?

Was I mentioning VeroBlue?

THE COURT: You had started VeroBlue, yes, and then and turned to your right to get some papers.

MR. DRAPER: Okay. What I would ask you to look -- take a hard look at is VeroBlue, 6 Fed 4th 880, the court there did not uphold a dismissal on equitable mootness. Enormous distributions had been made. The plan had been virtually substantially consummated, but the court said, wait, we can -- we can fashion a relief here that is minimal and that is -- is not problematic.

Let's talk about what relief can be fashioned here. The

court can apply a scalpel and just go back and say, look, the parties who were originally covered by the indemnity are covered, anybody else who you just picked up is not covered.

And -- and the truth is when you look at the equitable mootness cases they fall into two categories. Category 1 is a creditor who had made concessions is now being asked to alter its treatment but still leave the concessions in place. That's not the case here. We don't have a creditor being asked to make a concession. In fact, the people now being covered by this had no expectation. In fact, the plan had no expectation of an indemnification. It was specific insurance coverage that, again, you can apply a scalpel and just go back to what the plan covered and limit it.

And number two is our third-party creditors before the court who were affected by the order. Well, that's not the case either, because the employees and the parties who were being covered by the indemnification are not before the bankruptcy, are not before the court here, were not creditors, who were not insiders. They were just outsiders who they're picking up.

Let me address now the -- the constitutional mootness. And I think there are a few issues here. The first is -- and when you look at it in their papers there's a footnote to a case where they cite that the Fifth Circuit says the -- the -- the -- the effect must be pecuniary. That's not true.

In CMS it's a footnote in the pleading that they filed on the 21st, the court there, and that's the Fifth Circuit, said a trustee who has no --

THE CLERK: Two minutes remain.

MR. DRAPER: -- who has no pecuniary interest in fact is -- it doesn't -- doesn't have to have one and can appeal.

Number two, Dugaboy has a real pecuniary interest. Though they have forgotten this, we are a contingent creditor under that plan. Simple mathematics says if the $20 million or $25 million is available for distribution to creditors my capability to being paid increases. The -- the test to whether I have a pecuniary interest is not a dollar test. It's a mathematical test. It's a pretty clear that this trust falls, or this trust is reduced to where it should be, my capability or my ability for my contingent interest is -- is increased.

Again, thank you very much. And, again, I would ask the court to look at the cases I've cited on the equitable mootness side because I think they are dispositive of the Fifth Circuit standing at issue.

THE COURT: Thank you, Mr. Draper.

And the appellants have reserved some time for rebuttal.

Mr. Pomerantz.

MR. POMERANTZ: Good morning, Your Honor.

Can you hear me?

THE COURT: I can.

MR. POMERANTZ: Thank you, Your Honor.

I will be focusing my comments this morning on the equitable mootness motion and the merits. We filed our reply in connection with the constitutional mootness motion and I'll largely stand on that unless Your Honor has any questions.

But I do want to highlight one point, Your Honor. Appellant's standing throughout the bankruptcy case has been an issue, so much so that Judge Jernigan issued an extraordinary order in June 2021 requiring NexPoint and other Dondero related entities to disclose all claims they had and all their relationships with the debtor. She entered the order so she could evaluate whether parties had standing to take positions before the bankruptcy court.

In July 2021 NexPoint filed their disclosure. They identified each employee claim by name, but they did not mention the COVID's claim. They had multiple chances to correct this error when its standing was questioned and many times after before the bankruptcy court.

Only now, after agreeing to withdraw all their other claims does the COVID's claim miraculously appear on the docket ten months -- ten months after it was transferred. Your Honor, they said confusion, there's a huge credibility

issue here, and the statement in the declaration that the transferred document was not backdated just doesn't cut it. In any event, Your Honor, that claim has been disallowed and can't support standing under the first and agreed standard.

Your Honor, with respect to equitable mootness the Fifth Circuit acknowledges that an appeal of a bankruptcy court order can become equitably moot. And appellants are incorrect are equitable mootness doesn't apply here.

First they argue that it doesn't apply because there is not a planned confirmation order, but the circuit has considered equitable mootness of orders other than confirmation orders. In GWI and in Skull Pack. And Sneed is not to the contrary. Sneed only stands for the proposition that a confirmed plan in the case is required, and we have that here.

Second, consistent with other circuits, the Fifth Circuit does not limit equitable mootness to the organizations as opposed to liquidations. Manges found equitable mootness in a litigation case as -- and also a litigation -- a liquidation was at issue in Superior Offshore.

Lastly, while the complexity of the case can be a factor, it's not a litmus test. Berryman found equitable mootness in a simple case. And while both Texas Prairie and Superior Offshore rejected equitable mootness, neither case

was complex and that didn't factor into the decision.

In any event, Your Honor, the asset monetization under this plan is complex and requires sophisticated management. As a result of serious allegations of mismanagement and fraud against Mr. Dandero, the bankruptcy court appointed Mr. Seery based upon his experience managing complex financial assets similar to the debtor in his work as a restructuring professional. He is the debtor -- reorganized debtor's CEO and the claimant trustee and his knowledge of the estate's assets the bankruptcy court found was vital to the plan success.

The assets consist of operating companies, undeveloped land, structured products, distressed debt, and other unique assets that will only deteriorate in value quickly if not managed effectively. Dismissal upon equitable mootness is appropriate under Manges if it effects either the rights of parties not before the court such that the court cannot order effective relief or the success of the plan, and we meet both, Your Honor.

Since the summer of 2020 Mr. Dandero and the other appellants have embarked on a litigation onslaught that's been designed to harass Mr. Seery and the other debtor representatives that has resulted in a TRO against Mr. Debtor -- Mr. Dandero, and a contempt order for violating the TRO.

Although the plan confirmed in February 2021, the effective date was conditioned upon obtaining acceptable DNO coverage. Why? Because Mr. Seery and the other post-confirmation management -- post effective date management was simply unwilling to accept their roles without a guarantee of their indemnification rights to protect against Mr. Dandero's attacks.

DNO coverage on an acceptable basis wasn't available because of Dandero, and the debtor and the committee pivoted to self-insurance and sought the court authority to implement the indemnity trust. Had the bankruptcy court not authorized the indemnity trust, the plan would not have gone effective, Highland would have remained in Chapter 11 without the ability to make distribution to creditors. But the bankruptcy court did approve the indemnity trust, management did rely on it, and the plan did go effective.

The court simply cannot order any effective relief in this appeal that would reinstate the status quo for the managers, and reinstatement of the status quo is a key that comes out of the cases. If the court reverses, management loses protection for their indemnification rights for actions taken after the August 11th effective date. And as the Dandero litigation onslaught has intensified post effective date and post confirmation, DNO insurance, not an option six months ago, will not be an option now. So security for the

indemnification rights, which was the only reason that the plan went effective, will no longer exist.

Reversal will not only pull out the rug from management but will also materially jeopardize the plan. Mr. Seery would resign if the order is reversed and believe the subtrust -- litigation subtrustee and the oversight members would follow suit. This a big deal. Mistake can't be easily replaced. As the court found in the confirmation order in the findings of fact, stripped of the ability to guarantee indemnification rights and without DNO coverage it would be impossible to find replacement managers with the sophistication necessary to monetize the assets, and the result would be a void in management, a likely default under the exit facility, and it would seriously jeopardize the plan's success.

Your Honor, equitable mootness cases involve an appellate trying to resolve its appellate rights which if successful will unquestionably enhance their rights. Courts have to balance the rights of the appellant to enhance their rights against parties' expectations and the success of the plan. But this is not the paradigm we have here.

Appellants filed this appeal in the name of unsecured creditors who they said were armed by the indemnity trust, but unsecured creditors were not armed by the indemnity trust. The committee, the statutory fiduciary for unsecured

creditors, supported the indemnity trust, and not one creditor with an allowed claim objected to it. The committee supported the order because they recognized protecting management, and having the plan go effective, a plan that was accepted by 99.8 percent in amount of unsecured creditors, was in the bankruptcy's word -- bankruptcy court's words a miracle. Voiding the trust, losing competent management, and jeopardizing success will significantly harm creditors.

Stripped of their unsecured claims appellant's motivation in this appeal becomes clear. It never had anything to do with protecting unsecured creditor's rights. They want to do everything they can to destroy the plan. That's not a basis for standing or a basis for allowing this court -- this appeal to continue. The court should dismiss the appeal as equitably moot.

Your Honor, turning to the merits, the indemnity trust order is not a plan modification because it did not alter the parties' rights, expectations, and obligations under the plan.

I want to spend a minute on the -- on the nature of appellant's interest, because it really goes to what their expectations could have been under the plan. NexPoint Advisors is owned and controlled by James Dandero. NexPoint along with appellant HCFMA (sic), also owned and controlled by Dandero, assert a $14 million administrative claim which

will be soon tried in the bankruptcy court. But any allowed administrative claim is not affected by the trust because it will be paid by the approximately 195 million that was available projected to be paid to junior unsecured creditors. There is no circumstance under which this claim will not be paid.

Appellants could not as trust beneficiaries have had any expectations of how indemnification claims would be paid under the plan because they were not trust beneficiaries at the time of confirmation. Their unsecured claims were acquired after confirmation.

Appellants are not like the creditors in U.S. Brass and the asbestos cases. In those cases the creditors withdrew their objections to the plan based upon changes specifically made in the plan to address their concerns and when post-confirmation the debtor tried to undo those changes. That's not what's happening here. Here, as I said, the committee and other creditors representing 99 percent in dollar amount of unsecured claims supported the plan. The committee actively participated in drafting the indemnity trust and supported the order which is being appealed, as it was the only way to protect the independent managers and have the plan go effective.

The only reason that the unsecured creditor class rejected the plan was because of a handful of votes of former

employees who were being terminated under the plan, who were Dandero loyalists, whose claims are disputed, and who now work for Dandero related entities, and none of whom objected to the plan.

Before I have turn to the merits on the indemnification, Your Honor, I want to describe the post-confirmation structure because I think it's very important. The debtor was reconstituted as the reorganized debtor, a limited partnership. Its limited partner is the claim and trust and its general partner is the corporate entity which is a subsidiary of the claim and trust. The reorganized debtor retained its management contracts with third-party funds and other related assets to avoid regulatory complications. The majority of the remaining assets were transferred to the claim and trust and Mr. Seery is the claim and trustee.

A litigation subtrust was created because the creditors wanted prosecution of claims separated from asset monetization and controlled by a different person. The claim and trust transferred litigation claims to the subtrust to be pursued by the litigation trustee, but proceeds generated by the reorganized debtor assets and the litigation --

THE COURT: I think we lost our sound just then, Mr. Pomerantz.

MR. RUKAVINA: Your Honor, what happened to Mr. Draper and I is somehow we were muted without pressing

the button. I don't know how. But perhaps Mr. Pomerantz has been also muted.

MR. DRAPER: If there could be a message to him to reengage his microphone it might work. That's what I did.

MR. POMERANTZ: Your Honor, can you hear me?

I'm not sure where you lost me, Your Honor.

THE COURT: All right.

MR. POMERANTZ: I was talking about the corporate structure of the three -- of the different entities.

THE COURT: Yes. You were just transitioning into that. And we'll add two minutes to your time.

MR. POMERANTZ: Okay, Your Honor. Sorry.

I talked about the general -- the -- the limited partnership and that the claim and trust is the limited partner and is the owner of the subsidiary who is the general partner. And the reorganized debtor remained -- retained its management contracts with third-party funds and other related assets to avoid regulatory complications.

The majority of the debtor's remaining assets were transferred to the claim and trust, and Mr. Seery is the claim and trustee. A litigation subtrust was created because creditors wanted prosecution of claims separated from asset monetization and controlled by a different person. The claim and trust transferred litigation claims to the subtrust to be pursued by the litigation trustee.

So the way these assets work together is proceeds generated by the reorganized debtor's assets and the litigation subtrust claims are upstreamed to the claim and trust for distribution to trust beneficiaries along with the proceeds of claim and trust assets. They work together as a symbiotic group to upstream these assets. All of the preconfirmation debtor assets are -- end up being upstreamed to the claim and trust after expenses are paid.

Your Honor, turning to the merits, the appellant's principal argument is that the indemnity --

THE LAW CLERK: 10 minutes remaining.

MR. POMERANTZ: Thank you.

Turning to the merits, the principal argument is that the indemnity trust expanded the people who were to be indemnified by the claim and trust to include people indemnified by the litigation subtrust of the reorganized debtor.

Your Honor, first, under the Fifth Circuit's McKenzie decision and Your Honor's All Track Transportation decision, the appellant's have waived this argument by not making it in their pleadings or in the argument below. Even if not waived, Your Honor, the argument mischaracterizes the indemnity trust and the provisions of the plan and its implemented documents.

As a threshold matter, Your Honor, neither the indemnity

trust order or the indemnity trust create any obligations to any party. The turn sheet attached to the motion states that the purpose of the trust is to provide collateral security supporting the indemnification obligations created under the claim and trust agreement, the litigation subtrust agreement, and the reorganized debtor limited partnership. The indemnity trust is only a mechanism to satisfy the indemnity claims that become due under the various plan documents and which are not satisfied first by the claim and trust, the litigation subtrust, and the reorganized debtor. It does not create any new indemnification obligations. Rather, the indemnity obligations are created under the plan documents. 8.2 of the claim and trust, 8.2 of the litigation trust, and Section 10 of the reorganized debtor limited partnership.

Therefore, the real question, Your Honor, is whether the funding of the indemnification trust is consistent with the plan, and that the answer is yes. The indemnification trust was to be funded with two and a half million dollars of cash, of debtor cash upon inception, and a 22 and a half million dollar note. The claim and trust, the litigation subtrust, and the reorganized debtor are all co-obligors under the 22 and a half million dollar note. The assets of all those entities will fund the note.

Appellants dismiss the claim and trust ability to create reserves and -- and obligation to fund litigation subtrust

expenses and the right to contribute capital to the reorganized debtor to preserve its value. Various provisions of the plan and its implementing documents provide the claim and trust with such authority, discretion, and obligation.

In addition to the cases cited in our brief, Your Honor, I direct the court's attention to Article 4, Capital A and B of the plan, and Section 3.3(b)(vi) of the claim and trust agreement.

The bankruptcy court also ruled correctly that the creation of the indemnity trust to securitize plan approved indemnification obligations was an action to implement the plan authorized by Article 4(d) of the plan.

So several principals flow from these provisions.

First, the plan authorized the claim and trust and other post-effected date entities to complete reserves and fund expenses of all post-confirmation entities.

Second, claim and trust beneficiaries were only entitled to the proceeds net after all expenses were paid and reserved for.

Third, the debtor was authorized to take actions to implement the terms of the plan and supporting documents.

Fourth, as the bankruptcy court found, nothing in the plan prohibits self-insurance through the creation of the indemnity trust in lieu of DNO insurance.

And, last, the structure was consistent with creditor

expectations key for the plan modification argument. Asset proceeds would flow up to the claim and trust, go and distribute the net proceeds to creditors after payment of all expenses relating to the asset monetization process.

Appellants argue in their briefing that the creditors' rights were fundamentally changed because while the plan created discretion to set reserves, the indemnity trust transformed that discretion into a legal obligation. But appellants are wrong for two reasons.

First, the indemnity trust authorized the creation of the indemnity -- the order authorized the creation of the indemnity trust. It did not become a legal obligation unless and until the claim and trust oversight board authorized the execution of the indemnity trust agreement. The claim and trust board actually did authorize the execution of the indemnity trust on August 11th, the effective date of the plan. So the premise of the argument that the indemnity trust order took away discretion is not correct. The claim and trust oversight board retained such discretion -- discretion and exercised it.

Moreover, Your Honor, under the plan all creditors seated decision-making authority to the claim and trust and the oversight board over administration of the trust, including the discretion of whether to create reserves to fund litigation trust expenses and reorganize debtor

expenses, the amount of those reserves, how much money could be spent on DNO coverage. All that discretion was given to those -- those governing bodies. Because no creditor influenced how the claim and trust was administered, the fact --

THE CLERK: Five minutes remain.

MR. POMERANTZ: Excuse me?

THE COURT: I think the clerk said five minutes remain.

MR. POMERANTZ: Okay. Thank you.

Because no creditor could influence how the claim and trust was administered, the fact that the claim and trust and the oversight board could reserve and fund expenses as they deemed appropriate was within creditors' expectations under the plan and did not change the legal relationship between the debtor and its creditors thereby requiring a plan modification.

I want to briefly mention the issue of DNO coverage, Your Honor. The plan effective date was contingent upon obtaining acceptable DNO insurance. As I said, the condition was essential, because Seery and the other managers would not agree to serve without protection. The debtor could not have found post-confirmation effective date management without it, and though the -- the condition was waivable, unfortunately acceptable insurance was not available because of Dondero's

threats and litigation onslaught, but rather than not going effective, the debtor made -- decided to self-insure.

And who objects to the self-insurance?

Appellants. Who did not hold general unsecured claims of confirmation, who are not trust beneficiaries now, notwithstanding Mr. Draper's comments of this contingent right, that's clearly not sufficient under the Fifth Circuit standing to be a person aggrieved, who are the reason acceptable DNO insurance cannot be obtained and really who have no legitimate basis to contest the indemnity trust, other than to be, in the words of the bankruptcy court's confirmation order, disrupters.

The indemnity trust is the functional equivalent of DNO coverage. Both are designed to secure indemnity obligations under the plan. The cost of DNO insurance reserves are claim and trust expenses or expenses otherwise necessary to preserve the value of the reorganized debtor and are senior to the payment of trust beneficiaries.

And while payment of DNO premiums are some costs never to be recovered and potentially distributed to beneficiaries, any funds from the indemnity trust may be freed up to pay trust beneficiary claims if no indemnity claims are asserted.

Appellants argument that the change to an indemnity trust modified the prayer's rights, obligations, and expectations, is not supported by the plan or any of the

documents executed in support of the plan, and it's not supported by the case law.

The parties have briefed the leading cases of what constitutes a plan modification, and they don't support appellant's argument. In the Fifth Circuit's Brass case, Your Honor, the debtor modified a plan prior to confirmation to resolve an insurance company's plan objection. The change provided that future disputes would be resolved by litigation and not arbitration. That change was critical to the insurance company. Why? Because it believed arbitration could result in conducive settlements detrimental to its coverage defenses.

When post-confirmation the debtor through a settlement agreement tried to change the way in which the claims would be resolved through arbitration, the insurance company objected. Because this change modified a fundamental plan provision, which the insurance company relied upon in withdrawing its objection to confirmation, the Fifth Circuit easily found it to be a plan modification.

THE LAW CLERK: Two minutes remain.

MR. POMERANTZ: Thank you.

This is nothing like what's going on in here.

In the Second Circuit's Joint Asbestos case the plan carefully created a priority and distribution mechanism to satisfy asbestos claims against the post-confirmation trust.

Post confirmation the trust became insolvent and could not satisfy its plan obligations. Certain parties agreed to modify the trust to change the payment timing, the priority scheme, and how claims would be resolved. The Second Circuit found that this restructuring of the trust was a plan modification. As with U.S. Brass this case is stark -- in stark contrast to what's going on here.

In conclusion, Your Honor, this appeal is nothing but a continuation of James Dandero and his related entities' efforts to throw every roadblock into the debtor's restructuring process. The indemnity order did not alter appellant's expectations of their treatment under the plan. How could it? They didn't have any unsecured claims when the plan was confirmed. Nor does it modify the rights or treatment of creditors' claims or effect the relationship in any way. The plan board fall contemplated asset proceeds being upstream to the claim and trust who would fund those expenses, create reserves, and distribute the remaining to the trust beneficiaries. The indemnity trust is entirely faithful to this principle.

Thank you, Your Honor.

THE COURT: Thank you, Mr. Pomerantz.

Rebuttal?

MR. RUKAVINA: Yes, Your Honor. Can the court hear me?

THE COURT: Very well.

MR. RUKAVINA: Thank you.

Your Honor, in U.S. Brass the Fifth Circuit rejected the very argument just made, which is that, well, under the plan the debtor had the discretion to compromise claims, so switching from litigating them to arbitration was no harm, no foul. So that argument is not a sound argument. Nor is the no harm, no foul argument. The bankruptcy code provides for a mechanism and that mechanism must be complied with. I took Your Honor's questioning of me earlier to -- to go to that argument, no harm, no foul. Respectfully, they are changing a plan, whether it's actually no harm, no foul doesn't matter. That's an argument to be made at the new confirmation hearing.

Your Honor, we're not talking about stripping Mr. Seery of indemnification. The allegation that he and the others will resign, it's baseless. They can set aside several million dollars -- they have indemnification rights under the plan. We're not challenging that. They can set aside millions of dollars for themselves. For the notion that reversing this order will defeat the plan because the professionals will quit is not supported by the record and it's certainly not a logical one.

But most importantly, what I take real exception with is, and I'm quoting "the Dandero litigation onslaught". Your

Honor, my two clients represent thousands of investors who have trusted them with billions of dollars. We're not some cowboys litigating with everyone. In fact, we are not taking offensive litigation to the bankruptcy case. We are not Mr. Dondero. We have not been sanctioned. If the -- if the debtor is concerned, the debtor has Rule 11 rights. The debtor has Section 1927 rights.

We are the defendants in multiple lawsuits filed by the debtor. In one lawsuit, Your Honor, we had a final trial on six days notice on a mandatory injunction the debtor sought against us. And they lost. The bankruptcy court denied them that.

I am -- I -- I hear my clients being maligned nonstop, but listen to what they're saying. They're saying James Dondero. They're saying James Dondero was sanctioned. Whatever the merits of those arguments are, they simply do not apply to my clients. My clients are enjoined by the plan. They're enjoined from properly representing their constituents. That is why we are appealing the plan to the Fifth Circuit. That is why we are involved in this bankruptcy case. As we said at the confirmation hearing, don't enjoin us and we'll go home.

So -- so the allegation that we are picking this fight, that we are cowboy litigants, that we are vexatious, is not in the record, Your Honor, and again it shouldn't matter for

purposes of this appellant argument.

Also not in the record is what Mr. Pomerantz was talking about, the terms of the promissory note here. I just had my associate look and he could not find it and I don't remember it. It's part of the problem, Your Honor. If this had been handled as a plan modification with a disclosure statement, all of these documents that have now been signed would have been public, would have been -- would have been known by everyone. That's, again, the whole point that the -- the democracy, not only of the creditors in a Chapter 11, Your Honor, but all the other parties in interest, and certainly my clients are parties in interest, were alleged to owe tens of millions of dollars to the debtor. We're -- we're subject to final and permanent injunctions in the plan.

We've also made that argument on standing, Your Honor. The record is clear that the plan itself would not have gone effective but for this order. My client right now, and Mr. Dondero -- I'm sorry, Mr. Draper's client right now would not be looking down a permanent injunction and exculpations of their claims and releases of their claims without this order. It takes multiple orders to get to an effective plan in Chapter 11, Your Honor, disclosure statement, plans estimation, plan confirmation, et cetera. This is merely the last link in that chain. Whether the court agrees with me or not that we have creditor standing, we have standing --

THE CLERK: One minute remains.

MR. RUKAVINA: Thank you.

-- because the plan would not be effective.

Your Honor, very quickly, this court I submit has a duty to supervise the Article I bankruptcy court. That's the whole point of Northern Pipeline -- Northern Marathon. We have cited and quoted Stern v. Marshall, a recent Supreme Court case, where the Supreme Court says, "Any party may appeal those determinations to the Federal District Court where the Federal District Judge will review them," et cetera. The bankruptcy jurisdictional system does not work if this court can't review it. And your law clerk can find it for you, Your Honor. It came out yesterday. It's a Second Circuit opinion. It's case number 20-2548. In that Second Circuit opinion standing was iffy. The Second Circuit didn't find standing under traditional notions, but it says, "But the fact that this case is a one-off --

THE CLERK: Time.

THE COURT: All right. Thank you, counsel.

All right. Thank you, counsel for your arguments.

I'm going to ask that you remain on the link after I leave the courtroom in case the court reporter has any questions about any portion of your argument or any cases that you cited. Sometimes she does, sometimes she doesn't. And then once that process is completed then you're welcome

to sign-off.

At this time the court takes the appeal under submission and will issue its ruling.

Thank you, counsel.

The court will stand in recess.

(End of proceedings.)

INDEX - ORAL ARGUMENT

C E R T I F I C A T I O N

I, PAMELA J. WILSON, CSR, certify that the foregoing is a transcript from the record of the proceedings in the foregoing entitled matter.

I further certify that the transcript fees format comply with those prescribed by the Court and the Judicial Conference of the United States.

This the 15th day of March, 2022.

s/Pamela J. Wilson
_____
PAMELA J. WILSON, RMR, CRR
Official Court Reporter
The Northern District of Texas
Dallas Division