Date Filed: 11/10/2021

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

ON DIRECT APPEAL FROM THE UNITED STATES BANKRUPTCY COURT FOR THE NORTHERN DISTRICT OF TEXAS
BANKRUPTCY CASE NO. 19-34054-11 (SGJ)

REPLY BRIEF IN SUPPORT OF APPELLEE'S MOTION TO DISMISS APPEALS AS EQUITABLY MOOT

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CERTIFICATE OF INTERESTED PERSONS

The undersigned counsel of record certifies that the following listed persons and entities, as described in the fourth sentence of Rule 28.2.1, have an interest in the outcome of this case. These representations are made in order that the judges of this Court may evaluate possible disqualification or recusal.

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TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

CASES

STATUTES

Debtor-Appellee respectfully submits this Reply to opposition briefs of Appellants, the Advisors, Dondero, and Trusts ("Advisors Opp.") and the Funds ("Funds Opp.").

Appellants do not dispute that Debtor's reorganization plan (the "Plan") was substantially consummated after Appellants failed to obtain a stay. They nevertheless assert that the Plan can be unwound easily and without harm to third parties that have relied on the Confirmation Order. They are wrong. Appellants are also mistaken that equitable mootness never applies to bankruptcy appeals challenging exculpation and injunction provisions that are integral to a plan and its success.

1. The Plan Cannot Be Unwound.

Appellants mischaracterize Reorganized Debtor's post-Effective-Date transactions as having occurred only "on paper" and being reversible by the mere stroke of a pen. Nonsense. Trustee James Seery's Declaration details (at ¶11) the fully "funded" (*i.e.*, fully spent) $45 million exit facility from third-party Blue Torch Capital, the $5.2 million new note and $500,000 paid to third-party creditor Frontier, the $2.2 million paid to third-party creditor Acis, the $5.1 million (and counting) disbursed to numerous Class 7 creditors, as well as other disbursements made under the Plan. Those very real financial transactions indisputably involve the kind of innocent third parties not before the court that equitable mootness is designed to

protect from unwarranted harm. *See In re Idearc, Inc*., 662 F.3d 315, 320 (5th Cir. 2011); *In re Berryman Prods., Inc*., 159 F.3d 941, 946 (5th Cir. 1998); *In re Block Shim Dev. Company-Irving*, 939 F.2d 289, 291 (5th Cir. 1991).

If the Confirmation Order were to be reversed or vacated, the estate would have to seek creditors' disgorgement of $12+ million in payments. *See, e.g.*, *Berryman Prods.*, 159 F.3d at 946. Debtor's new lender, which had no role in the bankruptcy or prepetition business, would declare a default on its $45 million loan. And now-resolved third-party claims against the estate would be reinstated. The resulting disruption and expense of trying (and almost certainly *failing*) to restore the pre-confirmation *status quo* would be substantial. None of the affected third parties "assumed" that "risk" (Advisors Opp. 2) simply by knowing an appeal was pending even while the unstayed order went into effect. If that were enough to scuttle equitable mootness, then the doctrine would never apply.

The eggs are no less scrambled, and third parties are no less reliant on the Plan, just because orderly asset monetization is the Plan's goal. Appellants are wrong that equitable mootness "does not apply" to such a plan. Indeed, the Fifth Circuit dismissed, as equitably moot, a confirmation appeal challenging a plan that had as a core feature a liquidation trust. *In re Manges*, 29 F.3d 1034, 1037 (5th Cir. 1994). And other courts have rejected claims that they "may not—as a matter of law—invoke equitable mootness where a 'reorganization' in form nonetheless

functions as a liquidation." *In re Abengoa Bioenergy Biomass of Kan., LLC*, 958 F.3d 949, 956 (10th Cir. 2020) (citing *In re Superior Offshore Int'l, Inc.*, 591 F.3d 350, 353-54 (5th Cir. 2009) and cases from other circuits).

Appellants speculate (Advisors Opp. 17) that if confirmation is reversed, a hypothetical *new* plan could emerge that might provide certain creditors with the same payments that Debtor has made here, such that those payments could be retained. This Court rejected that precise argument in *Berryman*, 159 F.3d at 946. Indeed, it is possible no plan, or a very different one, would emerge on remand. Appellants—and only Appellants—would be perfectly happy with that result, and admit their preference that Debtor be pushed into a free-fall liquidation in a "different structure" outside of bankruptcy. Advisors Opp. 17.

Appellants also imply the Plan lacked broad creditor support because it was rejected by Class 8 general unsecured creditors. But the truth is that creditors holding 99.8% of the value of Class 8 claims voted *for* the Plan, which also had the support of the Unsecured Creditors' Committee. Class 8 voted against the Plan *by number only* because certain former employees (who now work for a Dondero-Related Entity) asserted spurious claims, which are subject to pending claim objections, that skewed that vote.

Additionally, Appellants do not deny the bankruptcy court's finding on the "remoteness" of their "economic interests" in this case, nor do they answer the

bankruptcy court's "serious questions" about whether they are pursuing challenges to the confirmed Plan "in good faith." Appellants label as "[b]reathless speculation" (Funds Opp. 12) the suggestion that they are merely trying to "burn the place down"—just as Dondero promised—but offer no other plausible explanation for their attacks on a Plan in which they have no meaningful stake. Nor is there any credence to the Funds' protestations that they should not be tainted by Dondero's actions. Neither their Opposition nor Reply on the merits addresses the evidence the bankruptcy court relied on to find that Dondero controls the Funds. *See* Appellee Br., 14 n.13, 53-54.

2. Equitable Mootness Applies to the Plan Protections.

Appellants also contend that equitable mootness can *never* require dismissal of a bankruptcy appeal challenging a confirmed plan's exculpation or injunction provisions. Advisors Opp. 4-5, 11-13. They draw that supposed prohibition from cases in which this Court held that challenges to releases did not meet the equitable-mootness standard on the facts of those cases. But none of those decisions established a *per se* rule that exculpations or injunctions can never be so integral to a reorganization that removing them would upend a consummated plan.

In each of Appellants' cited Fifth Circuit cases, in fact, the releases at issue were *not* integral to the consummated plans. They were, as even Appellants describe them (Funds Opp. 8), merely "peripheral" to those plans. In those very different

circumstances, this Court concluded that relief could be fashioned targeting only the tacked-on, unnecessary releases without undermining the rest of the plan.

In *In re Pacific Lumber*, this Court held that the releases at issue had merely been "purchased" by the plan sponsor, and "[n]othing in the record" suggested that those releases had any effect on the reorganization plan's success. 584 F.3d 229, 252 (5th Cir. 2009). Likewise, in *In re Hilal*, the appellant was not "appealing the entire confirmation order," and this Court found "no potential adverse effect on the plan or third parties" from appellant's request to modify the "scope" of a plan's release of the trustee and other bankruptcy professionals. 534 F.3d 498, 499-500 (5th Cir. 2008) (appeal ultimately denied on the merits as "border[ing] on frivolous").[1]

This case is different. Here, the bankruptcy court found—and Appellants do not challenge as clear error—that the Plan Protections are "integral" to the Plan's other terms and "necessary" to its success. ROA.51-52, ¶70. The Plan Protections are designed to safeguard key individuals and entities from the Dondero-Related Entities' vexatious litigation campaign and provide them the breathing space necessary to focus on maximizing value for all creditors. *Id.* After a two-day confirmation hearing, the bankruptcy court found that key individuals' willingness

[1] This Court's unpublished decision in *In re Thru, Inc.*, 782 F. App'x 339 (5th Cir. 2019) (*per curiam*), did not address whether appellant's challenge to release and exculpation provisions was equitably moot.

to work for the Reorganized Debtor, and to assist in winding down its complex assets, depended on those Plan Protections. ROA.51-58, ¶¶70-79. And Seery emphasized (Decl. ¶¶12-13) that he and others *continue* to rely on the Plan Protections and would not have accepted their positions without them. Excising those Plan Protections now would cause those key individuals to quit rather than face an onslaught of incessant litigation. That, in turn, would throw Debtor's reorganization into chaos, harm legitimate creditors as well as third parties who were never part of the bankruptcy, and potentially require appointment of a trustee or conversion of this case to a Chapter 7 liquidation.

In cases involving similar judicial findings that plan protections were critical to a plan's success, other circuits have held that appeals attacking those plan protections would knock the props out from under the plans and are therefore equitably moot. The Second Circuit, for instance, dismissed an appeal challenging third-party releases because it concluded that those "releases were critical to the bargain that allowed [the debtor] to successfully restructure," and that "undoing them" would "cut the heart out of the reorganization." *In re Charter Communications, Inc.*, 691 F.3d 476, 496 (2d Cir. 2012). There, as here, "striking the releases[] would be no ministerial task," because "removing a critical piece" of the plan's underlying settlement "would impact other terms of the agreement and throw into doubt the viability of the entire Plan." *Id.* at 484-85.

Appellants also contend that any third-party reliance on the Plan Protections and resulting plan was unreasonable and so can be ignored in the equitable mootness analysis. Funds Opp. 9-10. But this Court and others have rejected that precise claim. This Court has explained, quoting the *en banc* Third Circuit: "to focus on the 'reasonableness' of [third-party] reliance, at least as measured by the likelihood of reversal on appeal, is necessarily a circular enterprise and therefore of little utility. Our inquiry should not be about the 'reasonableness' of the [third-parties'] reliance or the probability of either party succeeding on appeal." *In re GWI PCS 1, Inc.*, 230 F.3d 788, 801 (5th Cir. 2000) (quoting *In re Cont'l Airlines*, 91 F.3d 553, 565 (3d Cir. 1996)) (ellipsis omitted).

Finally, Appellants devote only scant attention to the equitable mootness of their challenge to the Plan's Gatekeeper Provision. That provision does not release, exculpate, or enjoin anything, and so Appellants' other arguments do not simply carry over to this separate plan term. The Funds briefly contend that the Gatekeeper Provision calls upon the bankruptcy court to screen claims "unrelated to the bankruptcy case," and therefore striking the provision "could not interfere with the plan's success." Funds Opp. 14. But the premise is mistaken. The Gatekeeper Provision requires any Enjoined Parties to seek the bankruptcy court's leave, upon showing an alleged claim is colorable, to pursue only claims having some

relationship to these proceedings.[2] Removing the Gatekeeper Provision would undoubtedly "interfere with the plan" by subjecting Protected Parties to the Dondero-Related Entities' frivolous litigation, siphoning resources away from the Reorganized Debtor's work of maximizing assets, and thereby diminishing creditor recoveries.

3. No "Fractional Relief" Is Possible.

Appellants fall back on proposing that, even if they cannot obtain the full reversal of the Confirmation Order they seek, this case is like others in which the possibility of "fractional relief" precluded equitable mootness. The analogy is inapt.

Each of the "fractional relief" cases Appellants cite involved bankruptcy appeals over how a plan distributed money. In those cases, this Court reasoned that *some* amount of money could be awarded to a successful appellant—even if well short of the full sum that appellant was seeking—that would not require the plan to be unwound. In *In re Texas Grand Prairie Hotel Realty L.L.C.*, 710 F.3d 324, 328 (5th Cir. 2013), this Court held that a secured creditor's appeal, seeking an 8.8% interest rate instead of a 5% interest rate, was not equitably moot because at least

[2] *See* ROA.150-51, Plan, Art. IX.F. (Gatekeeper Provision covers any claim "that arose or arises from or is related to the Chapter 11 Case, the negotiation of the Plan, the administration of the Plan or property to be distributed under the Plan, the wind down of the business of the Debtor or Reorganized Debtor, the administration of the Claimant Trust or the Litigation Sub-Trust, or the transactions in furtherance of the foregoing").

"partial relief" such as a "slightly higher" interest rate or "small money judgment" would not "disturb[] the reorganization." Likewise, in *In re Scopac*, 624 F.3d 274, 282 (5th Cir. 2010), the Court held that even if the debtor lacked the liquid assets to pay appellant's claim in full, the possibility of partial payment meant the appeal was not equitably moot.[3]

These appeals, however, do not involve a dispute over money. Nor do Appellants explain what kind of fractional relief they could plausibly seek and obtain that would not require rewriting (and reconfirming) Debtor's consummated Plan. If the Plan Protections are illegal (they aren't), then other Plan terms to which those safeguards are "integral" and "necessary" must also be revisited and revised. If contingent trust interests granted to Classes 10 and 11 violate the absolute priority rule (they don't), then adjusting those classes' potential recovery (and directing it elsewhere) would require a new plan.[4] And what "fractional relief" could possibly be available on Appellants' all-or-nothing requests to deny Debtor a discharge and

[3] Appellants' reliance on *Texas Grand Prairie Hotel*, *Pacific Lumber*, and *Scopac* is also unavailing because (unlike here) those appeals were brought by secured creditors. This Court takes an especially narrow view of equitable mootness when it is asserted against secured creditors. *See Tex. Grand Prairie Hotel*, 710 F.3d at 328; *Pac. Lumber*, 584 F.3d at 234-50, *Scopac*, 624 F.3d at 322.

[4] Advisors (Opp. 7-8) mischaracterize Debtor's 11 U.S.C. §1127(b) argument. The point is *not* that section 1127(b), by precluding plan modification after substantial consummation, prevents all appellate review of confirmation orders. Rather, section 1127(b) provides that, once a plan has been substantially consummated, the plan cannot be modified piecemeal without a new confirmation process involving all stakeholders. Nothing in *In re Blast Energy Services*, 593 F.3d 418 (5th Cir. 2010), is to the contrary.

re-do plan confirmation with additional Debtor financial disclosures? There is no realistic fractional relief available to save these appeals from equitable mootness.

4. Direct Appeal Does Not Abrogate Equitable Mootness.

Appellants contend (Advisors Opp. 18-19; Funds Opp. 5-6) that the direct-appeal statute, or something in the parties' joint certification that the direct-appeal criteria were met in this case, prevents Debtor from obtaining dismissal on equitable-mootness grounds. Not so. When Congress provided for direct appeal from the bankruptcy court to the court of appeals, it did not modify the substantive law—including the equitable-mootness doctrine—that applies to such appeals. 28 U.S.C. §158(d)(2). While the Debtor certified that direct appeal would materially advance the progress of this case, it did so because any party that lost on appeal in the district court was "virtually certain" to appeal to this Court. Advisors Opp. Ex. A ¶13. That was true regardless of whether a district court dismissed the appeal as equitably moot or decided it on the merits. Indeed, the irrelevance of Debtors' support for direct appeal is in stark contrast to the clear relevance of Appellants' directly contradictory statements when seeking a stay that the Plan's substantial consummation would result in the equitable mootness of these appeals. *See* Mot. 6.

5. Other Issues on Appeal Are Equitably Moot.

Finally, Appellants do not specifically address the equitable mootness of their claims seeking reversal of the confirmed Plan for its supposed violations of the

absolute priority rule, disclosure requirements, and discharge limits. The equitable mootness of such appeals seeking to eviscerate consummated plans and restart a confirmation process from scratch is well-established. *See* Mot. 16.[5]

CONCLUSION

The consolidated appeals should be dismissed as equitably moot.

[5] The Funds contend that their request for this Court to strike certain findings of fact (supported by uncontroverted testimony) from the Confirmation Order is not equitably moot because excising those findings would not harm third parties. Fair enough. But that aspect of the Funds' appeal fails on the merits for the same reason—it seeks no relief *from the judgment* that would affect *anyone* (parties or third-parties alike). *See* Appellee Br. 53-54.

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CERTIFICATE OF SERVICE

I hereby certify that on November 10, 2021, the attached Reply Brief was electronically filed using the appellate CM/ECF system. I further certify that all participants in this case are registered CM/ECF users and that service will be accomplished via CM/ECF.

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