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

In re:	§	Chapter 11
HIGHLAND CAPITAL MANAGEMENT, L.P.,[1]	§	Case No. 19-34054-sgj11
Reorganized Debtor.	§	**Response Deadline: March 6, 2023 at 5:00 p.m. (CT)**

HIGHLAND CAPITAL MANAGEMENT, L.P.'S OBJECTION TO SCHEDULED CLAIMS 3.65 AND 3.66 OF HIGHLAND CLO MANAGEMENT, LTD.

Pursuant to sections 502(a)-(d) and 558 of title 11 of the United States Code (the "Bankruptcy Code") and Rule 3007 of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules"), the reorganized debtor in the above-referenced bankruptcy case, Highland

[1] Highland's last four digits of its taxpayer identification number are (8357). The headquarters and service address for Highland is 100 Crescent Court, Suite 1850, Dallas, TX 75201.

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Capital Management, L.P. (as temporally required, referred to as "Highland" (the entity that existed before the Petition Date) or the "Debtor" (the entity that existed from the Petition Date until the Effective Date) or "Reorganized Highland" (the entity that came into existence upon the Effective Date)), hereby objects to scheduled claim numbers 3.65 and 3.66 (together, the "HCLOM Scheduled Claim") carried on Schedule F of the Debtor's Amended Schedules [*see* Docket No. 1082] with respect to Highland CLO Management, Ltd. ("HCLOM").

Reorganized Highland respectfully submits that there are numerous bases for the disallowance of the HCLOM Scheduled Claim and represents as follows:

Preliminary Statement[2]

1. The HCLOM Scheduled Claim arises out of a note dated October 7, 2016 (the "Note") executed by Highland in favor of Acis Capital Management, L.P. ("Acis", and together with Highland and HCLOM, the "Parties"), then an affiliate of Highland, in the original amount of $12,666,446.00, which was then purportedly assigned to HCLOM. The HCLOM Scheduled Claim should be disallowed because HCLOM provided no consideration for the Note and otherwise materially breached the Parties' agreements, thereby relieving Highland of any obligation to perform under the Note.

2. The background facts are straight-forward. At all relevant times, Mr. Dondero controlled each of the Parties. Acis managed certain CLOs and received certain Servicer Fees in exchange. Since Acis had no employees of its own, Highland provided the services on behalf of Acis that enabled Acis to fulfill its obligations to the CLOs. In October 2016, Acis and Highland entered into the Purchase Agreement pursuant to which Highland tendered the Note to Acis in exchange for purported "Participation Interests" in Acis' Servicer Fees over a specified

[2] Capitalized terms not defined in this Preliminary Statement shall have the meanings ascribed to them below.

period, less certain expenses. Highland and Acis appeared to perform their respective obligations under the Purchase Agreement through early November 2017.

3. In November 2017 (immediately after the Joshua Terry arbitration award was issued but before the Acis involuntary), Highland purportedly notified Acis that it was unwilling to continue to support Acis' management of the CLOs, leaving Acis unable to fulfill its obligations as the CLOs' manager. HCLOM, a newly-formed entity created to replace Acis, purportedly offered to step into the breach and serve as Acis' Successor Manager in exchange for an assignment of the Note. On November 3, 2017, the Parties executed the Assignment pursuant to which, among other things, (a) HCLOM was to become the CLOs' Successor Manager, (b) Acis and HCLOM were to remit the Servicer Fees to Highland, and (c) the Note was assigned to HCLOM. Dondero executed the Assignment for both Highland and Acis. One of the Dondero entities' then-regular Cayman Islands directors, John Cullinane, executed the Assignment on behalf of HCLOM.

4. Notwithstanding the purported Assignment, HCLOM and Acis failed to perform their respective obligations under the Assignment and HCLOM never provided anything of value to Highland in exchange for the Note. HCLOM and Acis breached the Assignment by, among other things, failing to tender any Servicer Fees associated with the Acis Participation Interests and failing to "promptly pursue Successor Manager appointment . . . in respect of each CLO, including but not limited to achieving all conditions precedent required under the CLO Documents." (Assignment § 2).

5. Consequently, HCLOM never obtained an Appointment (defined in the Assignment as the "consummation of HCLOM's appointment as Portfolio Manager of a given CLO"), the entire purpose and purported *quid pro quo* of the Assignment. In fact, Acis has

continued to manage the CLOs, including during the first six months after the Assignment was executed while Mr. Dondero remained in control of Acis, but no Servicer Fees were paid to Highland. These failures (a) constituted material breaches of contract that relieved Highland of its obligations under the Note, both by the express terms of the Parties' agreements and also pursuant to applicable law; and (b) resulted in a complete failure of consideration under the Assignment, which had the effect of voiding the assignment of the Note.

6. As set forth in more detail below, Reorganized Highland has no continuing liability under the Note and received nothing of value for the Note. The HCLOM Scheduled Claim should, therefore, be disallowed in its entirety. Alternatively, if Reorganized Highland is determined to have any continuing obligations under the Note, any such obligations would be subject to Reorganized Highland's rights of offset and recoupment for all amounts due from both Acis and HCLOM (*i.e.*, all covered Servicer Fees on the Acis CLOs from the date of the Note to present). On information and belief, such amounts exceeded the purported amount of the Note.

Jurisdiction

7. The Court has jurisdiction over this matter under the Bankruptcy Code and pursuant to 28 U.S.C. §§ 157 and 1334. This matter is a core proceeding within the meaning of 28 U.S.C. §§ 157(b)(2)(A), (B), and (L). Venue is proper in this District under 28 U.S.C. §§ 1408 and 1409.

8. The statutory predicates for the relief requested herein are 11 U.S.C. § 502(b)-(d), 11 U.S.C. § 558, and Federal Rule of Bankruptcy Procedure 3007.

Factual Background

9. On October 16, 2019 (the "Petition Date"), the Debtor filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code in the Bankruptcy Court for the District of Delaware, Case No. 19-12239 (CSS) (the "Delaware Court").

10. On December 4, 2019, the Delaware Court entered an order transferring venue of the Debtor's Bankruptcy Case to this Court [Docket No. 186].[3]

11. On February 22, 2021, this Court entered the *Order Confirming the Fifth Amended Plan of Reorganization of Highland Capital Management, L.P. (as Modified) and (ii) Granting Related Relief* [Docket No. 1943] (the "Confirmation Order"), which confirmed the *Fifth Amended Plan of Reorganization of Highland Capital Management, L.P. (as Modified)* [Docket No. 1808] (the "Plan").

12. The Plan became effective on August 11, 2021 (the "Effective Date") [Docket No. 2700].

The Note and Purchase Agreement

13. Prior to the Petition Date, Acis, using Highland employees, provided management services with respect to certain collateralized loan obligations ("CLOs") in exchange for management fees ("Servicer Fees") paid by the CLOs to Acis. Purportedly, because "cash flows from the Servicer Fees [we]re unpredictable," Acis sought to "obtain[] a guaranteed fixed amount of cash flow" in exchange for the Servicer Fees it earned from the CLOs. Purchase Agreement (as defined) at 102. In that context, Highland, as Purchaser, and Acis, as Seller, entered into the *Agreement for Purchase and Sale of CLO Participation Interests* dated October 7, 2016 (the "Purchase Agreement").

14. Pursuant to Section 1 of the Purchase Agreement, Acis agreed to sell to Highland "participation interests in the Servicer Fees (the "Acis Participation Interests") in an amount equal to . . . the total Servicer Fees paid to Seller [Acis] by each of the CLOs beginning in November 2016 and ending August 2019," less certain specified amounts. In exchange for the

[3] All docket numbers refer to the docket maintained by this Court.

Acis Participation Interests, Highland agreed to pay Acis $666,655 in cash and to execute the Note in favor of Acis as Payee. Thus, the Note was the primary form of consideration tendered by Highland to Acis in exchange for the Acis Participation Interests.

15. The Note and the Purchase Agreement were inextricably tied together as part of the purchase transaction. The Purchase Agreement attached a copy of the Note as an exhibit and made repeated references to the Note. Moreover, by its terms, the Note was to become effective only upon the effectiveness of the Purchase Agreement, which was executed contemporaneously by Highland and Acis. A condition precedent to the effectiveness of the Note provides:

> ***This Note shall not become effective and Payee shall have no obligation to make the advance hereunder until*** Payee has received each of the following in form and substance acceptable to Payee:
>
> . . . .
>
> (b) the Agreement for Purchase and Sale of CLO Participation Interests dated of even date herewith (the "Purchase Agreement"), by and between Maker and Acis Capital Management, LP, a Delaware limited partnership ("Highland") [*sic*], and copies of all agreements, documents and instruments executed or delivered in connection therewith and evidence that ***all conditions to the effectiveness of the Purchase Agreement have been or will be fulfilled contemporaneously with the initial advance under this Note***;

Note at 1 (emphases added).

16. Moreover, as highlighted above, Acis' obligation to remit the cash received with respect to the Acis Participation Interests to Highland was expressly incorporated into the terms of the Note through multiple references to the obligation of the Payee (*i.e.*, Acis) to make advances "hereunder" or "under this Note" to the Maker (*i.e.*, Highland). For example, as quoted above, the Note provides that "*Payee* shall have no obligation to make *the advance hereunder* until Payee has received" certain specified documents. Note at 1 (emphases added). The Note also

states that, in the event of a default by the Maker, the Payee may "terminate Payee's commitment to make any advances under this Note." Note at 3. The Note further provides:

> Notwithstanding any provision contained herein to the contrary, the total amount of interest that Maker is obligated to pay and Payee is entitled to receive with respect to this Note shall not exceed the amount calculated on a simple (i.e., non-compounded) interest basis at the maximum rate allowed by applicable law ***on principal amounts actually advanced hereunder to or for the account of Maker***.

Id. (emphasis added).

17. These repeated references to amounts to be advanced by the Payee to the Maker "under" the Note describe Acis's obligations to "remit" the cash received with respect to the Acis Participation Interests to Highland, as noted in Section 4 below.

18. Section 4 of the Purchase Agreement is titled "Covenants" and imposes several obligations on the parties to the Purchase Agreement. Section 4.1 of the Purchase Agreement includes the following covenant of the Seller (*i.e.*, Acis): "The Seller agrees to promptly remit, or cause to be promptly remitted, to the Purchaser the cash received with respect to the Acis Participation Interests." Purchase Agreement, § 4.1.

19. Section 3.6 of the Purchase Agreement further provides:

> Subject to Section 1.5, the Purchaser acknowledges and agrees that: (a) except as provided in Section 1.5, *should the Seller's rights with respect to the Servicer Fees be terminated, such termination shall not affect the Purchaser's obligations under the Note*; (b) except as provided in Section 1.5, ***the Seller may exercise all of its legal rights and remedies to enforce the Purchaser's obligations under the Note*** *even if the Acis Participation Interests are not paid, in full or part, by the CLO trustees for any reason, including the termination of the Seller as the manager, a hostile buyout of such CLO, or any other reason* ***(other than as a result of the Seller breaching its covenants under this Agreement or as a result of fraud or by willful misconduct of the Seller);*** and (c) Purchaser has had the opportunity to consult with its own legal counsel with respect to the purchase of the Acis Participation Interests. The Purchaser understands such actions could negatively impact the timing and amount of payment of such Acis Participation Interests during the pendency of such dispute by the trustee of such CLO. *The Purchaser bears the sole risk with respect to nonpayment of the Acis Participation Interests* ***(other than as a result of the Seller breaching its covenants under this Agreement or as a result of the fraud or willful misconduct of the Seller)***.

Purchase Agreement, § 3.6 (emphases added).

20. Thus, the Purchase Agreement is clear that, whereas Highland would remain obligated under the Note if Acis did not receive Servicer Fees from the CLO third parties, in the event that Acis breached its covenants under the Purchase Agreement to remit the cash received with respect to the Acis Participation Interests to Highland, Acis would forfeit the right to enforce the Note (subject to Section 1.5, which addresses a seizure or forfeiture of Servicer Fees due to governmental action, which did not occur here). In short, Highland's payment obligations under the Note were conditioned upon Acis' compliance with its own agreement to transfer to Highland the cash received with respect to the Acis Participation Interests pursuant to Sections 1 and 4.1 of the Purchase Agreement.

21. Section 5.7 of the Purchase Agreement provides Highland with the right to seek specific performance of the Purchase Agreement in the event of a breach by Acis:

> The Seller and the Purchaser agree that the rights created by this Agreement are unique and that the loss of any such rights is not susceptible to monetary quantification. Consequently, the Seller and the Purchaser agree that an action for specific performance (including for temporary and/or permanent injunctive relief) of the obligations created by this Agreement is a proper remedy for the breach of the provisions of this Agreement, and the Purchaser shall be entitled to such relief without the necessity of proving actual damages or posting a bond.

Purchase Agreement, § 5.7.

22. Both the Purchase Agreement and the Note are governed by Texas law.

The Purported Assignment of the Note to HCLOM

23. In November 2017, Highland (controlled by Mr. Dondero) notified Acis that it was "unwilling to continue to provide support personnel and other critical services to Acis with respect to the CLOs." Acis (also controlled by Mr. Dondero) then determined that it could no longer "fulfill its duties as portfolio manager of the CLOs" and needed to find a replacement,

and HCLOM (also controlled by Mr. Dondero) offered to fill the void. Assignment (as defined below) at 1.

24. To address the problem that Mr. Dondero manufactured, Highland, Acis, and HCLOM then entered into that certain *Assignment and Transfer Agreement* dated as of November 3, 2017 (the "Assignment"), the purpose of which was to have HCLOM replace Acis as the Successor Manager for the CLOs and assume all of Acis' rights and obligations under the Purchase Agreement and Note.

25. Thus, pursuant to the Assignment, (a) HCLOM agreed to act as Acis's Successor Manager, (b) Acis assigned to HCLOM all rights in the Note, (c) each of Acis and HCLOM agreed to transfer to Highland any Servicer Fees received by Acis and HCLOM, respectively, that Acis would have been required to remit to Highland pursuant to the Purchase Agreement, and (d) HCLOM agreed to execute a joinder to the Purchase Agreement.

26. A recital to the Assignment provides: "HCLOM, a qualified Successor Manager, irrevocably commits to be appointed as Successor Manager ***in consideration of Acis assigning to it the Note***." Assignment at 1 (emphasis added).

27. Section 1 of the Assignment required Acis (again, then under Mr. Dondero's control) to "promptly provide the Controlling Class (as defined in the CLO Indentures) with notice requesting the appointment of HCLOM as Portfolio Manager pursuant to the requirements of the CLO Documents."

28. Section 2 of the Assignment provides that each of Acis and HCLOM would "promptly pursue Successor Manager appointment of HCLOM in respect of each CLO." Assignment, § 1.

29. Section 3 of the Assignment provides:

> **3. Assignment and Transfer of the Promissory Note; Stabilization Payments.**
>
> a. Effective immediately upon execution of this Agreement by the Parties, all right, title and interest of Acis under the Note, including the right to any and all Stabilization Payments[4] not yet paid to Acis, are hereby irrevocably assigned and transferred by Acis to HCLOM, it being understood that from the date of such assignment, HCLOM shall become the "Payee" thereunder.
>
> b. For so long as Acis shall receive Servicer Fees following the date hereof, Acis shall remit to HCM the HCM Stabilization Fees[5] pursuant to the Note Purchase Agreement.
>
> c. For so long as HCLOM receives any Servicer Fees following any Appointment, then HCLOM shall remit to HCM any portion of such fees that would otherwise have constituted HCM Stabilization Fees pursuant to the Note Purchase Agreement if Acis was the recipient of such fees.
>
> d. HCLOM shall sign a joinder to Note Purchase Agreement upon HCM's written notice thereof.

Assignment, § 3 (emphasis added).

30. Thus, the parties to the Assignment contemplated that HCLOM would assume Acis's rights under the Note, subject to HCLOM becoming the Successor Manager and to the continuing obligation of both Acis and HCLOM to remit Servicer Fees received by each entity to Highland.

31. Section 6.h of the Assignment contains a right of specific performance for breach and provides:

> The Parties agree that the rights created by this Agreement are unique and that the loss of any such rights is not susceptible to monetary quantification. Consequently, the Parties agree that an action for specific performance, including for temporary and/or injunctive relief) of the obligations created by this Agreement is a proper remedy for the breach of the provisions of this Agreement, and the Debtor shall be

[4] The term "Stabilization Payments" is defined in the Assignment to mean "cash flows from HCM," as set forth in the Note.

[5] The term "HCM Stabilization Fees" is defined in the Assignment to mean the "future Servicer Fees identified to be paid to HCM pursuant to the Purchase Agreement."

> entitled to such relief without the necessity of proving actual damages or posting a bond.

Assignment, § 6.h.

32. After the parties executed the Assignment, Acis and HCLOM failed to consummate the appointment of HCLOM as Successor Manager. Moreover, although Acis retained the benefit of the CLO servicer arrangements and received the Servicer Fees that were the subject of the Purchase Agreement and Assignment, neither Acis nor HCLOM made any further payments to Highland.

33. Following the commencement of the Acis bankruptcy, HCLOM and Highland released each other from the obligations under the Note and the Assignment.

Objection

A. Legal Standard

34. The Bankruptcy Code establishes a burden-shifting framework for proving the amount and validity of a claim. As the HCLOM Scheduled Claim was scheduled in the Debtor's schedules but was not scheduled as disputed, contingent, or unliquidated, the HCLOM Claim is deemed filed under section 501 of the Bankruptcy Code, notwithstanding that no proof of claim was filed by HCLOM. 11 U.S.C. § 1111(a). Furthermore, "[a] claim . . . , proof of which is filed under section 501 [of the Bankruptcy Code], is deemed allowed, unless a party in interest . . . objects." 11 U.S.C. § 502(a). "A proof of claim executed and filed in accordance with the [Bankruptcy Rules] shall constitute *prima facie* evidence of the validity and amount of the claim." FED. R. BANKR. P. 3001(f); *see also In re Armstrong*, 347 B.R. 581, 583 (Bankr. N.D. Tex. 2006). However, the ultimate burden of proof for a claim always lies with the claimant. *Armstrong*, 347 B.R. at 583 (citing *Raleigh v. Ill. Dep't of Rev.*, 530 U.S. 15 (2000)).

35. The HCLOM Scheduled Claim is based upon the Note. For the reasons described below, the Debtor is not liable on the Note. The HCLOM Scheduled Claim should, therefore, be disallowed in full.

B. Acis' Material Breaches of Contract Excused the Debtor's Performance under the Note

36. For the reasons discussed below, Acis' material breaches of the Purchase Agreement, the Note, and the Assignment relieved the Debtor from any purported payment obligations under the Note.

1. HCLOM and/or Acis' Breach of the Purchase Agreement Relieved the Debtor from any Purported Payment Obligations under the Note.

37. Pursuant to the terms of the Note, Highland was to make three payments to Acis. The first payment was scheduled to be made on May 31, 2017 in the amount of $3,370,694. The second payment was scheduled to be made on May 31, 2018 in the amount of $5,286,243, and the third payment was scheduled to be made on May 31, 2019 in the amount of 4,677,690. Highland made the first payment, but not the other two for the reasons set forth below.

38. As noted above, Acis agreed in Section 1 of the Purchase Agreement to remit to the Debtor the cash received with respect to the Acis Participation Interests through August 2019. Acis last remitted cash to Highland with respect to the Acis Participation Interests on November 1, 2017, before the Assignment was executed. Upon information and belief, the CLOs consistently paid the Servicer Fees to Acis on a regular basis. HCLOM and Acis breached their obligations under the Assignment by failing to remit to Highland any of the Servicer Fees related to the Acis Participation Interests (or any other amounts). The failure to remit such cash to Highland constituted a material breach of that agreement.

39. Pursuant to the express terms of the Purchase Agreement, HCLOM's and Acis' breach of their covenant to remit the cash received with respect to the Acis Participation Interests to Highland excused Highland's own performance under the Note. As explained above, Section 3.6 of the Purchase Agreement provides that Acis would retain the right to enforce Highland's obligations under the Note except where Acis' failure to transfer the cash received with respect to the Acis Participation Interests to Highland is "a result of [Acis] breaching its covenants under" the Purchase Agreement.

40. Upon information and belief, HCLOM and/or Acis apparently continued to receive Servicer Fees after November 3, 2017; they simply failed to remit those fees to Highland as the Purchase Agreement required. Since this failure to remit was due to a breach of the covenant to make such payments under the Purchase Agreement, Highland's obligation to pay any amounts under the Note was excused under Section 3.6 of the Purchase Agreement, and Acis (as well as any assignee) forfeited its rights to enforce Highland's obligations under the Note.

41. Indeed, even had Highland's obligations on the Note not been excused by the express terms of the Purchase Agreement, HCLOM's and Acis' material breaches would still have excused Highland's performance under applicable law. *See, e.g.*, *Allied Elevator, Inc. v. E. Tex. State Bank*, 965 F.2d 34, 38 (5th Cir. 1992) (holding that, if defendant had materially breached an agreement to procure life insurance, as required by the terms of a promissory note provided by plaintiff to the defendant in exchange for borrowed money, plaintiff would be excused from performing under the note, because "'[a] fundamental rule of contract law is that whenever a party to a contract … commits a material breach, the other party to that contract, at its election, is excused

from further performance'") (quoting *Bernal v. Garrison*, 818 S.W.2d 79, 83 (Tex. App. 1991); *see also MJR Corp. v. B & B Vending Co.*, 760 S.W.2d 4, 20-21 (Tex. App. 1988) ("It is fundamental that whenever one party to a contract commits a material breach, the other party, at its election, is excused from further performance") (citing *Mead v. Johnson Grp., Inc.*, 615 S.W.2d 685, 689 (Tex. 1981)).

2. HCLOM and Acis Breached the Note, Thereby Excusing the Debtor's Performance.

42. The failure by HCLOM and Acis to remit the requisite Servicer Fees to Highland resulted in a breach of the Note. As described above, the Note expressly requires Acis to make advances to Highland "under" the Note. The only advances that Acis committed to make to Highland in connection with the transactions that were the subject of the Purchase Agreement and the Note were those constituting the Servicer Fees received with respect to the Acis Participation Interests. By failing to honor the payment obligations under the Note, HCLOM and Acis materially breached their obligations under the Note.

43. Such material breach of the Note deprived Highland of the benefit of its bargain under that agreement in a manner that excused Highland's performance under the Note, which was given as the primary form of consideration provided in exchange for the Acis Participation Interests. *See, e.g.*, *Mustang Pipeline Co. v. Driver Co.*, 134 S.W.3d 195, 199 (Tex. 2004) (defendant's material breach of contract discharged plaintiff from its duties under the contract); *see also In re Dallas Roadster, Ltd.*, 846 F.3d 112 (5th Cir. 2017) ("A fundamental principle of contract law is that when one party to a contract commits a material breach of that contract, the other party is discharged or excused from any obligation to perform") (quoting *Hernandez v. Gulf Grp. Lloyds*, 875 S.W.2d 691, 692 (Tex. 1994)).

3. Alternatively, HCLOM's and Acis's Breach of the Purchase Agreement also Breached the Note, which Excused the Debtor's Performance under the Note.

44. It is a general rule of contract interpretation under Texas law that "separate instruments or contracts executed at the same time, for the same purpose, and in the course of the same transaction are to be considered as one instrument, and are to be read and construed together." *Jones v. Kelley*, 614 S.W.2d 95, 98 (Tex. 1981); *see also Vista Dev. Joint Venture II v. Pac. Mut. Life Ins. Co.*, 822 S.W.2d 305, 307 (Tex. App. 1992) (applying rule to promissory note and deed of trust).

45. The Note was unquestionably an integral part of the Purchase Agreement. It was tendered by Highland as the primary form of consideration in exchange for the Acis Participation Interests, it was executed at the same time as the Purchase Agreement, and the Purchase Agreement attached a copy of, and made repeated references to, the Note. Similarly, the Note is conditioned on the effectiveness of the Purchase Agreement. The Purchase Agreement and the Note should, therefore, "be considered as one instrument, and . . . be read and construed together." *See Kelley*, 614 S.W.2d at 98.

46. When considered as part of the Purchase Agreement, HCLOM's and Acis' material breach of the Purchase Agreement excused Highland's obligations under the Note. *See, e.g.*, *Fitzpatrick v. Animal Care Hosp., PLLC*, 104 A.D.3d 1078 (N.Y. App. Div. 2013) (where promissory note executed contemporaneously with purchase agreement represented partial consideration for the purchased assets and the purchase agreement specifically referred to the note, the court concluded that the parties' rights and obligations set forth in the note and purchase agreement were inextricably intertwined and one party's breach of the purchase agreement permitted the other party to offset its obligations due under the promissory note against any damages caused by the breach); *see also Ingalsbe v. Mueller*, 257 A.D.2d 894 (N.Y. App. Div.

1999); *A+ Assocs. v. Naughter*, 236 A.D.2d 655 (N.Y. App. Div. 1997); *Windmill Run Assocs. v. Fannie Mae (In re Windmill Run Assocs.)*, 566 B.R. 396, 444 (Bankr. S.D. Tex. 2017) (applying Texas law; "[s]eparate documents executed at the same time, for the same purpose, and in the course of the same transaction are to be construed together.... The note, the deed of trust, and the RRSA [replacement reserve and security agreement] were executed contemporaneously. The court concludes that these documents form the contract between the parties"); *Rieder v. Woods*, 603 S.W.3d 86, 94 (Tex. 2020) ("We construe a contract in a manner that gives 'effect to the parties' intent expressed in the text,' but we may also take into account 'the facts and circumstances surrounding the contract's execution.' In that vein, Texas courts have long recognized that, under appropriate circumstances, 'instruments pertaining to the same transaction may be read together to ascertain the parties' intent, even if the parties executed the instruments at different times and the instruments do not expressly refer to each other.' Where appropriate, 'a court may determine, as a matter of law,' that multiple separate contracts, documents, and agreements 'were part of a single, unified instrument.' In determining whether multiple agreements are part and parcel of a unified instrument, a court may consider whether each written agreement and instrument was 'a necessary part of the same transaction'" (footnotes and citations omitted)); *Nat'l City Bank of Ind. v. Ortiz*, 401 S.W.3d 867, 884 (Tex. App. 2013) ("National City's [noteholder] claims for breach of contract and judicial foreclosure cannot be parsed fairly into claims under the Note and claims under the Deed of Trust. Because the two documents form a single contract, both the Note and the Deed of Trust must be considered on remand in relitigating these claims"); *Wasaff v. Lipscomb*, 713 S.W.2d 730, 732 (Tex. App. 1986) ("We hold that the 'Trusteeship Agreement,' the promissory note and the deed of trust securing same must be read together and that when so read together, they permit the trustee to conduct the sale").

47. Notably, the Purchase Agreement expressly provides for specific performance and injunctive relief in the event of a breach by Acis. Because the Note and the Purchase Agreement must be construed together, absent strict performance by HCLOM and Acis of their obligations under the Purchase Agreement, Reorganized Highland cannot be compelled to honor any obligations under the Note.

4. The Note Is Unenforceable Due to a Failure of Consideration

48. The Note is unenforceable because there was a failure of consideration provided by HCLOM or Acis to support the Note. "Failure of consideration generally 'occurs when, because of some supervening cause after an agreement is reached, the promised performance fails.'" *Ropa Expl. Corp. v. Barash Energy*, No. 02-11-00258-CV, 2013 Tex. App. LEXIS 7290, at *15 (Tex. App. June 13, 2013) (quoting *US Bank, N.A. v. Prestige Ford Garland Ltd. P'ship*, 170 S.W.3d 272, 279 (Tex. App. 2005). "[F]ailure of consideration may result as a consequence of one party's failure to perform its obligations under the agreement, resulting in the other party's failure to receive the consideration set forth in the agreement." *City of The Colony v. N. Tex. Mun. Water Dist.*, 272 S.W.3d 699, 733 (Tex. App. 2008). The defense of failure of consideration "challenges the agreement as a whole." *Doskocil Mfg. Co. v. Sang Nguyen*, No. 02-16-00382-CV, 2017 Tex. App. LEXIS 5961, at *15 (Tex. App. June 29, 2017).

49. Highland tendered the Note to Acis in exchange for the Acis Participation Interests and Acis' obligation to remit the related cash received with respect to such interests. HCLOM's and Acis' failure to honor the obligation to remit those amounts after the Assignment was executed deprived Highland of its bargained-for consideration. Because the performance promised by Acis failed, the Note is unenforceable, including by Acis' assignees.

C. Material Breaches of the Assignment by HCLOM and Acis Excuse the Debtor's Performance under the Note

1. HCLOM's Failure to Perform under the Assignment Resulted in the Note Being Unenforceable Due to a Failure of Consideration.

50. The Parties purportedly entered into the Assignment because:

> (a) Highland sent the Notification (as defined in the Assignment) to Acis pursuant to which Acis was informed that Highland was "unwilling to continue to provide support personnel and other critical services to Acis with respect to the CLOS,"
>
> (b) Acis determined that in light of the Notification, it could not "fulfill its duties as portfolio manager of the CLOs," and
>
> (c) HCLOM "irrevocably commit[ted] to be appointed as Successor Manager [as defined in the Assignment] in consideration of Acis assigning to it the Note."

Assignment at 1.

51. Thus, the whole purpose of the Dondero-engineered Assignment was to have HCLOM step into Acis' shoes as the Successor Manager of the CLOs. Assignment §§ 1, 2. Until the Appointments (as defined in the Assignment) were consummated, Acis agreed to remit to Highland the "HCM Stabilization Fees pursuant to the Note Purchase Agreement" (to the extent Acis received Servicer Fees). After the Appointments (as defined in the Assignment) were consummated, HCLOM agreed to remit to Highland the any portion of such Fees that would have constituted HCM Stabilization Fees had they been received by Acis. *Id*. § 3(b), (c).

52. Although the Note was purportedly assigned to HCLOM, HCLOM never succeeded to Acis' role as the Successor Manager, no Appointments were ever consummated, and, therefore, HCLOM never transferred any Servicer Fees to Highland. In short, because the intent of the Assignment was never realized, HCLOM cannot receive all of the benefits of the transaction – *i.e.*, the Note – without accepting any of the burdens or providing anything of value in exchange for the Note or payments thereunder.

53. The total failure of consideration provided by HCLOM to support the Assignment, to which Highland was a party, renders the Assignment unenforceable as against Reorganized Highland. As described above, "failure of consideration may result as a consequence of one party's failure to perform its obligations under the agreement, resulting in the other party's failure to receive the consideration set forth in the agreement." *City of The Colony*, 272 S.W.3d at 733. HCLOM agreed in the Assignment to assume certain rights and obligations then held by Acis, including the obligation to transfer Servicer Fees to Highland. The assumption of those obligations constituted the consideration provided by HCLOM in exchange for the right to receive an assignment of the Note and to receive payments from Highland under the Note. Indeed, Highland consented to the Assignment only because HCLOM agreed to perform in accordance with its agreements under the Assignment.

54. HCLOM's failure to succeed to Acis as Successor Manager meant that HCLOM never assumed any servicer obligations, controlled any Servicer Fees, or transferred any Servicer Fees to Highland; indeed, HCLOM completely failed to perform under the Assignment as the parties intended. As a result, Highland never received any of the consideration for which it bargained under the Assignment. The total failure of performance by HCLOM under the Assignment renders the Note unenforceable by HCLOM.

2. Alternatively, HCLOM's Breach of the Assignment Excused the Debtor's Performance under the Note.

55. Even if the Assignment is not rendered unenforceable for failure of consideration, HCLOM's failure to comply with its obligations constituted material breaches thereof. Specifically, HCLOM breached the Assignment by failing to: (a) "provide the Controlling Class (as defined in each of the CLO Indentures) with notice requesting the appointment of HCLOM as Portfolio Manager," as required by Section 1 of the Assignment; (b) "promptly pursue

Successor Manager appointment," as required by Section 2 of the Assignment; (c) "achiev[e] all conditions precedent required by the CLO Documents," as required by Section 2 of the Assignment; and (d) execute a joinder to the Purchase Agreement, as required by Section 3.d of the Assignment.

56. HCLOM's material breaches of the Assignment excused Highland's obligations under the Note. *See, e.g.*, *Mustang Pipeline Co.*, 134 S.W.3d at 199 (defendant's material breach of contract discharged plaintiff from its duties under the contract).

D. Any Obligations that May Be Due under the Note Are Subject to Highland's Rights of Offset and Recoupment

57. Even if Reorganized Highland's remaining obligations under the Note are not excused, Reorganized Highland's rights of setoff and recoupment would reduce those obligations by an amount that is not less than the amount of unpaid Servicer Fees that should have been remitted to Highland through August 2019 by Acis and HCLOM. On information and belief, that amount exceeds the face amount of the Note.

58. As discussed above, Highland became obligated to Acis under the Note in exchange for Acis' simultaneous commitment to transfer Acis Participation Interests to Highland. Acis assigned its interests in the Note to HCLOM on the condition that HCLOM share Acis' payment obligations to Highland. Both Acis and HCLOM failed to transfer any cash received with respect to the Acis Participation Interests to Highland from and after November 3, 2017.

59. As summarized by the Texas appellate court:

> "Recoupment" allows a defendant to reduce the amount of a plaintiff's claims by asserting a counterclaim which arose out of the same transaction. There are two general requirements for recoupment: (1) some type of overpayment must have been made, and (2) both the creditor's claim and the amount owed the debtor must arise from a single transaction. . . .
>
> . . . .

> The right of setoff allows entities that owe each other money to apply their debts to each other. Where setoff is allowed, there are mutual debts arising from different transactions, which contrasts with the single transaction required in recoupment.

Sommers v. Concepción, 20 S.W.3d 27, 35 (Tex. App. 2000) (citing *Matter of Kosadnar*, 157 F.3d 1011, 1013 (5th Cir. 1998)).

60. Because Highland's obligations under the Note arose from the same transaction as Acis' payment obligations under the Purchase Agreement, Highland's obligations must be reduced under a theory of recoupment by the amount of Acis' obligations to Highland. Similarly, since Highland's consent to the assignment of the Note by Acis to HCLOM was conditioned on the agreement by both Acis and HCLOM to continue making payments to Highland under the Purchase Agreement, Reorganized Highland's obligations must be reduced under a theory of recoupment by the amount of HCLOM's obligations to Highland.

61. Alternatively, even if Highland's obligations under the Note are not viewed as arising under the same transaction as Acis' or HCLOM's respective obligations to Highland, Reorganized Highland's obligations must be reduced under a theory of setoff by all amounts owed by Acis and HCLOM to Highland, which include all unpaid obligations of those entities under the Purchase Agreement and the Assignment.

E. Reservation of Rights

62. Reorganized Highland reserves its right to supplement, amend, or modify this Objection based on facts adduced in discovery or otherwise, including to assert further objections, defenses or arguments in support of the disallowance of the HCLOM Scheduled Claim.

[REMAINDER OF PAGE INTENTIONALLY BLANK]

WHEREFORE, Reorganized Highland respectfully requests (i) that the HCLOM Claim be disallowed in its entirety, and (ii) for such other and further relief as this Court may deem just and proper.

Dated: February 2, 2023

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

In re:	§	Chapter 11
HIGHLAND CAPITAL MANAGEMENT, L.P.,[1]	§	Case No. 19-34054-sgj11
Reorganized Debtor.	§	

ORDER SUSTAINING
HIGHLAND CAPITAL MANAGEMENT, L.P.'S OBJECTION TO
SCHEDULED CLAIMS 3.65 AND 3.66 OF HIGHLAND CLO MANAGEMENT, LTD.

Upon consideration of the *Objection to Scheduled Claims 3.65 and 3.66 of Highland CLO Management, Ltd.* [Docket No. __] (the "Objection")[2] filed by Highland Capital Management, L.P., the reorganized debtor (as temporally required, the "Debtor" or "Reorganized Highland") in the above-captioned chapter 11 case (the "Bankruptcy Case"), and the Court (1) having considered the Objection and (2) finding that (a) notice of the Objection was good and sufficient upon the particular circumstances and that no other or further notice need be given, (b) the Objection is a

[1] The last four digits of the Reorganized Debtor's taxpayer identification number are 8357. The headquarters and service address for the Reorganized Debtor is 100 Crescent Court, Suite 1850, Dallas, TX 75201.

[2] Capitalized terms not otherwise defined in this Order shall have the meanings ascribed to them in the Objection.

core proceeding under 28 U.S.C. § 157(b), (c) the Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334, (d) venue is proper pursuant to 28 U.S.C. §§ 1408 and 1409, and (e) Highland CLO Management, Ltd. ("HCLOM") was properly and timely served with the Objection and the notice of hearing on the Objection, and good and sufficient cause appearing therefor,

it is **HEREBY ORDERED THAT**:

1. The Objection is **SUSTAINED**.

2. The HCLOM Scheduled Claim is **DISALLOWED** with prejudice.

3. To the extent applicable, the official claims register in the Debtor's Bankruptcy Case will be modified in accordance with this Order.

4. Reorganized Highland is authorized and empowered to take any action necessary to implement and effectuate the terms of this Order.

5. The Court shall retain jurisdiction over all disputes arising out of or otherwise concerning the interpretation and enforcement of this Order.

###END OF ORDER###