Nos. 22-631 and 22-669

In the Supreme Court of the United States

HIGHLAND CAPITAL MANAGEMENT, L.P., PETITIONER

v.

NEXPOINT ADVISORS, L.P., ET AL.

NEXPOINT ADVISORS, L.P., ET AL., PETITIONERS

v.

HIGHLAND CAPITAL MANAGEMENT, L.P., ET AL.

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE

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QUESTIONS PRESENTED

The petition in No. 22-631 presents the following question:

Whether the Bankruptcy Code authorizes a court to approve, as part of a plan of reorganization under Chapter 11 of the Bankruptcy Code, an exculpation clause that exempts from liability certain conduct by nondebtors, without the potential claimants' consent.

The petition in No. 22-669 presents the following questions:

1. Whether a bankruptcy court may approve, as part of a Chapter 11 reorganization plan, an exculpation clause that provides blanket immunity to certain nondebtors who are not bankruptcy trustees for any misconduct during the course of the bankruptcy process that does not rise to the level of gross negligence, on the theory that bankruptcy trustees have common-law immunity for such misconduct.

2. Whether a bankruptcy court may exculpate a debtor and certain nondebtors from liability for ordinary business conduct in operating the debtor's business after the confirmation date of a Chapter 11 reorganization plan.

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INTEREST OF THE UNITED STATES

This brief is filed in response to the Court's order inviting the Solicitor General to express the views of the United States in this case. In the view of the United States, the petitions for writs of certiorari should be held pending this Court's resolution of *Harrington* v. *Purdue Pharma L.P.*, cert. granted, No. 23-124 (oral argument scheduled for Dec. 4, 2023).

STATEMENT

1. "Congress' power under the [Constitution's] Bankruptcy Clause contemplates an adjustment of a failing debtor's obligations" and the distribution of "the

property of the debtor among his creditors." *Railway Labor Execs.' Ass'n* v. *Gibbons*, 455 U.S. 457, 466 (1982) (brackets, citations, and internal quotation marks omitted). Thus, this Court has explained that bankruptcy is the "subject of the relations between a[] * * * debtor and his creditors, extending to his and their relief." *Wright* v. *Union Cent. Life Ins. Co.*, 304 U.S. 502, 513-514 (1938) (citation omitted). The Bankruptcy Code seeks to give the honest but unfortunate debtor a "fresh start" while ensuring the maximum possible "equitable distribution" to creditors by exercising "jurisdiction over all of the debtor's property." *Central Va. Community College* v. *Katz*, 546 U.S. 356, 363-364 (2006); see *Stellwagen* v. *Clum*, 245 U.S. 605, 617 (1918).

Under the Code, a debtor seeking bankruptcy relief must shoulder a host of obligations. Those include the debtor's obligation to disclose all its creditors, its assets and liabilities, its current income and expenditures, and matters relating to its financial affairs. 11 U.S.C. 521(a). Absent the consent of individual creditors, 11 U.S.C. 1129(a)(7), a Chapter 11 debtor must then apply all its assets (with certain narrow exemptions for individual debtors, see 11 U.S.C. 522) to the satisfaction of its creditors' claims. In exchange, the debtor may receive a discharge of its debts, except for those that Congress deemed nondischargeable as a matter of public policy, such as an individual debtor's debts "for money * * * to the extent obtained by[] * * * fraud." 11 U.S.C. 523(a)(2)(A); see 11 U.S.C. 1141(d).

The Code "releases *a debtor* from personal liability with respect to any discharged debt by voiding any past or future judgments on the debt and by operating as an injunction to prohibit creditors from attempting to collect or to recover the debt." *Tennessee Student Assis-*

tance Corp. v. *Hood*, 541 U.S. 440, 447 (2004) (emphasis added). The discharge that a debtor can obtain is powerful: It "voids any judgment * * * , to the extent that such judgment is a determination of the personal liability of the debtor" with respect to a discharged debt; it "operates as an injunction against" any action "to collect, recover or offset any such debt as a personal liability of the debtor"; and, with certain exceptions, it "operates as an injunction against the commencement or continuation of an action, the employment of process, or an act, to collect or recover from, or offset against, [certain] property of the debtor * * * acquired after the commencement of the case." 11 U.S.C. 524(a). The Code expressly states that "discharge of a debt of the debtor does not affect the liability of any other entity on, or the property of any other entity for, such debt." 11 U.S.C. 524(e).

This case concerns provisions to relieve nondebtors from liability for actions taken after the commencement of a bankruptcy case. Only a single provision of the Code addresses such relief. Section 1125(e) provides that a person who, "in good faith and in compliance with the applicable provisions of [the Code]," "solicits acceptance or rejection of a plan" or participates in "the offer, issuance, sale, or purchase of a security, offered or sold" in connection with the plan "is not [thereby] liable * * * for violation of any applicable law * * * governing" those securities transactions. 11 U.S.C. 1125(e). The exculpation clause at issue here covers a broad range of conduct that does not fall within the terms of Section 1125(e).

2. a. In 2019, Highland Capital Management, L.P. (debtor) filed a Chapter 11 bankruptcy petition. 22-631

Pet. App. 4a.[1] Debtor is an investment firm co-founded by James Dondero. *Id.* at 2a. It sought bankruptcy protection due to a series of large judgments entered against it on various business litigation claims. See *id.* at 52a. At the time of debtor's bankruptcy filing, Dondero served debtor as a director and officer. See *id.* at 5a.

Despite allegations of management misconduct, debtor's bankruptcy "did not proceed under the governance of a traditional Chapter 11 trustee." Pet. App. 5a. Instead, the Unsecured Creditors' Committee negotiated an agreement with Dondero under which Dondero would "step[] down as director and officer of [debtor]" to serve as an "unpaid portfolio manager." *Ibid.* The creditors' committee then "selected a board of three independent directors to act as a quasitrustee and to govern" debtor. *Ibid.*

During the bankruptcy, Dondero proposed several reorganization plans that the creditors' committee and the independent directors opposed. Pet. App. 6a. When those plans failed, Dondero "began to frustrate the proceedings by objecting to settlements, appealing orders, seeking writs of mandamus, interfering with [debtor's] management, threatening employees, and canceling trades between [debtor] and its clients." *Ibid.* The bankruptcy court held Dondero in civil contempt and sanctioned him for his behavior. *Ibid.* Debtor's independent directors insisted that Dondero resign, and he did so in October 2020. *Ibid.*

In the meantime, the creditors' committee and the independent directors agreed on a proposed reorganization plan. Pet. App. 6a-7a. "Anticipating Dondero's

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[1] All citations to the petition appendix are to the one in case No. 22-631.

continued litigiousness," the proposed plan included provisions to shield from certain lawsuits debtor, its employees, general partner, and independent directors; the creditors' committee and successor entities; the oversight board; professionals retained in the bankruptcy case; and a broad universe of related persons. *Id.* at 8a; see *id.* at 8a-9a & nn.4-5. The confirmed plan permanently extinguished claims against the protected parties based on any conduct relating to "(1) the filing and administration of the [bankruptcy] case, (2) the negotiation and solicitation of votes preceding the Plan, (3) the consummation, implementation, and funding of the Plan, (4) the offer, issuance, and distribution of securities under the Plan before or after the filing of the bankruptcy, and (5) any related negotiations, transactions, and documentation." *Id.* at 9a. The exculpation clause did not extend to actions by debtor's general partner and its employees that predated the appointment of the independent directors, and it did not cover claims arising from "acts or omissions that constitute bad faith, fraud, gross negligence, criminal misconduct, or willful misconduct." *Ibid.* The plan's injunction provision enjoined individuals and entities that held claims against or equity interests in the debtor, and various other bankruptcy participants, from interfering with the implementation or consummation of the plan. *Id.* at 10a, 140a-143a.

The plan also included a gatekeeper provision. As to claims that are related to the bankruptcy case but not extinguished by the exculpation clause, the gatekeeper provision precludes the enjoined parties from filing the claim against a bankruptcy participant without first seeking leave to sue from the bankruptcy court and ob-

taining that court's determination that the "claim or cause of action is colorable." Pet. App. 10a.

Dondero and several other interested parties objected to the plan, including to the exculpation, injunction, and gatekeeper provisions. Pet. App. 7a. Among the objectors were two entities owned or controlled by Dondero: NexPoint Asset Management, L.P.—formerly known as Highland Capital Management Fund Advisors, L.P.—and NexPoint Advisors, L.P., respondents in No. 22-631 and petitioners in No. 22-669 (collectively, NexPoint). The United States Trustee also objected to the exculpation clause and injunction, explaining that those provisions constituted an impermissible nonconsensual release of nondebtors' claims against other nondebtors that extended beyond the parties protected by common-law immunity. See Bankr. Ct. Doc. 1671, at 4 (Jan. 5, 2021); Pet. App. 7a, 68a.[2]

b. The bankruptcy court confirmed the plan, as modified in respects that are not material here. See Pet. App. 39a-160a. The court concluded that the exculpation clause was justified by Dondero's "prior litigious conduct." *Id.* at 111a. In particular, the court found that the "costs [that] the [Exculpated Parties] might incur defending against" the claims covered by the provisions "are likely to swamp either the Exculpated Parties or the reorganization." *Ibid.* (citation omitted; brackets in original). The court also observed that the

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[2] The United States Trustee is a Department of Justice official, appointed by the Attorney General, 28 U.S.C. 581(a)(6), whose role includes "serv[ing] as [a] bankruptcy watch-dog[] to prevent fraud, dishonesty, and overreaching in the bankruptcy arena." H.R. Rep. No. 595, 95th Cong., 1st Sess. 88 (1977). By statute, "[t]he United States Trustee may raise and may appear and be heard on any issue in any case or proceeding under [the Code]." 11 U.S.C. 307.

exculpation clause was consistent with Fifth Circuit decisions recognizing a limited form of qualified immunity for creditors' committee members and bankruptcy trustees. *Id.* at 108a-111a. In approving the exculpation and gatekeeper provisions in their entirety, the court invoked general provisions of the Code recognizing bankruptcy courts' residual equitable authority over bankruptcy proceedings. *Id.* at 112a, 116a-117a.

3. On direct appeal from the bankruptcy court to the court of appeals under 28 U.S.C. 158(d)(2), the court of appeals vacated in part the plan's nondebtor exculpation clause. Pet. App. 1a-38a.[3] The court upheld the remainder of the plan, including the plan's injunction and gatekeeper provisions. See *id.* at 35a-37a.

With respect to the exculpation clause, the court of appeals reaffirmed circuit precedent holding that Section 524(e) of the Bankruptcy Code "categorically bars third-party exculpations absent express authority." Pet. App. 30a. The court then rejected debtor's argument that, as some other courts of appeals have found, the requisite authority is provided by 11 U.S.C. 105(a) and 1123(b)(6). Pet. App. 29a, 31a-32a. The court explained, however, that the "limited qualified immunity" that it viewed as applying to "creditors' committee members for actions within the scope of their statutory duties" and to "bankruptcy trustees unless they act with gross negligence" could provide a "source[] of authority" for exculpating nondebtors. *Id.* at 32a.

Consistent with that reasoning, the court of appeals vacated the exculpation clause to the extent that it protected entities beyond "the debtor, the creditors' committee and its members for conduct within the scope of

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[3] All references to the opinion of the court of appeals are to the opinion as modified on panel rehearing. See Pet. App. 2a.

their duties," and "the [bankruptcy] trustees within the scope of their duties." Pet. App. 33a. The court also determined that, although debtor's estate was not governed by a bankruptcy trustee, the independent directors—who were "appointed to act together as the bankruptcy trustee for [debtor]"—"are entitled to all the rights and powers of a trustee," including "limited qualified immunity for any actions short of gross negligence." *Ibid.*

As for the injunction and gatekeeper provisions, the court determined that bankruptcy courts have authority to enjoin conduct with respect to the narrowed group of exculpated parties. Pet. App. 35a-36a. And the court held that the gatekeeper provision was lawful under the "*Barton* doctrine," named after this Court's decision in *Barton* v. *Barbour*, 104 U.S. 126 (1881), which allows a bankruptcy court to require parties to "obtain leave of the bankruptcy court before initiating an action in district court when the action is against the trustee or other bankruptcy-court-appointed officer, for acts done in the actor's official capacity." Pet. App. 36a-37a (citation omitted); see *Barton*, 104 U.S. at 128.

The court of appeals also noted that the independent directors, their agents, advisors, and employees, and the debtor's CEO in his official capacity, are exculpated to the extent provided in two earlier bankruptcy court orders because those orders had become final and the court of appeals "lack[s] jurisdiction to consider [a] collateral attack[] on final bankruptcy orders even when it concerns whether the court properly exercised jurisdiction or authority at the time." Pet. App. 34a n.15.

DISCUSSION

The principal question presented in this case is whether the Bankruptcy Code authorizes a court to ap-

prove, as part of a plan of reorganization under Chapter 11 of the Bankruptcy Code, an exculpation clause that exempts from liability certain conduct by nondebtors, without the potential claimants' consent. In *Harrington* v. *Purdue Pharma L.P.*, cert. granted, No. 23-124 (oral argument scheduled for Dec. 4, 2023) (*Purdue*), this Court is considering the question whether the Bankruptcy Code authorizes a court to approve, as part of a Chapter 11 plan of reorganization, a release that extinguishes claims held by nondebtors against nondebtor third parties, without the claimants' consent. The Court should hold this case pending resolution of *Purdue*.

1. As applied to nondebtors, exculpation clauses are a type of third-party release contained in a plan of reorganization that pertains to nondebtor conduct that occurs after the filing of a bankruptcy petition. Exculpation clauses generally address conduct that occurs during the bankruptcy itself to prevent relitigation of issues resolved in the bankruptcy court. See, *e.g.*, *In re LATAM Airlines Grp. S.A.*, No. 20-11254, 2022 WL 2206829, at *50 (Bankr. S.D.N.Y. June 18, 2022). Some exculpation clauses also address conduct that happens after plan confirmation, including conduct or transactions relating to the implementation, consummation, or execution of the plan. See, *e.g.*, *In re Voyager Digital Holdings, Inc.*, 649 B.R. 111, 136-137 (Bankr. S.D.N.Y. 2023), appeal pending, No. 23-cv-2171 (S.D.N.Y. Mar. 14, 2023); *In re Aegean Marine Petroleum Network,* 599 B.R. 717, 721 (Bankr. S.D.N.Y. 2019). Exculpation clauses also differ with respect to the scope of third parties they purport to protect. Some apply only to bankruptcy fiduciaries, such as the bankruptcy trustee, a creditors' committee, or the committee's members. See,

e.g., *In re Pacific Lumber Co.*, 584 F.3d 229, 253 (5th Cir. 2009) (creditors' committee members); *In re Hilal*, 534 F.3d 498, 501 (5th Cir. 2008) (bankruptcy trustees). Some reach more broadly and purport to release any number of other third parties from liability, including persons associated with the debtor. See, *e.g.*, *Blixseth* v. *Credit Suisse*, 961 F.3d 1074, 1082 (9th Cir. 2020) ("various participants in the Plan approval process," including a lender who was the debtor's biggest creditor), cert. denied, 141 S. Ct. 1394 (2021).

In the absence of a valid exculpation clause barring suit, other protections may be available to bankruptcy fiduciaries sued for their conduct during a bankruptcy case. For instance, a common-law immunity might be available as an affirmative defense to certain conduct. See, *e.g.*, *In re Mailman Steam Carpet Cleaning Corp.*, 196 F.3d 1, 8 (1st Cir. 1999) ("[A] trustee acting with the explicit approval of a bankruptcy court is entitled to absolute immunity, as long as there has been full and frank disclosure to creditors and the court."), cert. denied, 530 U.S. 1230 (2000); *Yadkin Valley Bank & Trust Co.* v. *McGee*, 819 F.2d 74, 76 (4th Cir. 1987) ("[I]f a trustee is acting under the direct orders of the court, there is immunity."); *In re Castillo*, 297 F.3d 940, 951 (9th Cir. 2002), as amended (Sept. 6, 2002) (recognizing a "quasi-judicial immunity" for "those functions essential to the authoritative adjudication of private rights to the bankruptcy estate"). Courts also have inherent power to dismiss actions brought by litigants that they deem to be acting vexatiously or in bad faith and to impose sanctions on such litigants. See, *e.g.*, *In re Carroll*, 850 F.3d 811, 815 (5th Cir. 2017) (per curiam); Pet. App. 38a n.19 (explaining that "[n]othing in this opinion should be construed to hinder the bankruptcy court's power to

enjoin and impose sanctions on Dondero and other entities by following the procedures to designate them vexatious litigants"). And courts may be able in certain circumstances to adopt gatekeeper provisions, which require leave of the court before a court-appointed trustee can be sued for certain acts done in the trustee's official capacity. See *Barton* v. *Barbour*, 104 U.S. 126, 128-129 (1881); 28 U.S.C. 959.

An exculpation clause is a particular type of third-party release. While a third-party release often purports to extinguish pre-petition liability of nondebtors, an exculpation clause addresses the liability of nondebtors for post-petition conduct. See Pet. App. 29a; *In re PWS Holding Corp.*, 228 F.3d 224, 246-247 (3d Cir. 2000). Nonetheless, outside of narrow circumstances inapplicable here, no provision of the Code expressly authorizes either exculpation clauses or third-party releases, and many of the arguments on which courts have relied in assessing the permissibility of exculpation clauses are similar to those on which they have relied in assessing third-party releases more generally. Accordingly, many exculpation clauses raise significant concerns similar to those posed by nonconsensual third-party releases, including that exculpation clauses lack express authorization under the Code; that they secure outcomes that conflict with the text, structure, and purposes of the Code; and that they purport to extinguish claims of both individuals and sovereigns without consent. See Gov't Br. at 19-48, *Purdue*, *supra* (No. 23-124); see also *Voyager Digital Holdings*, *supra*.

2. In urging review on the question presented in debtor's petition (No. 22-631) regarding the statutory authority for exculpation clauses, the parties on both sides invoke a circuit conflict that largely overlaps with

the one that the Court is currently considering in *Purdue*. See 22-631 Pet. 13-18; 22-631 Resp. Br. 8-9 (agreeing with petitioner about the existence and contours of the circuit conflict); see also 22-631 Pet. 13-14 (invoking *Purdue*, then pending before the Second Circuit, and suggesting that *Purdue* implicates the same "long-standing conflict among the Circuits" as this case) (citing *In re Purdue Pharma, L.P.*, 635 B.R. 26, 89 (S.D.N.Y. 2021), rev'd and remanded, 69 F.4th 45 (2d Cir. 2023), cert. granted, No. 23-124 (oral argument scheduled Dec. 4, 2023)).

The two questions presented in NexPoint's petition (No. 22-669) are dependent on the question in debtor's petition. To the extent they are fairly presented in this case, but see 22-669 Br. in Opp. 11-19, they arise only to the extent that the court of appeals was correct in concluding that broader exculpation clauses would not be authorized by the Bankruptcy Code, and they do not appear independently worthy of review. See 22-669 Pet. 15 (urging that review of the two questions is "particularly imperative if the Court is inclined to grant [debtor's] petition"); 22-631 Resp. Br. 8 (NexPoint describing the questions in its petition as "intertwined" and "related" to the question presented in debtor's petition).

This Court's decision in *Purdue* is likely to shed light on considerations relevant to the question presented in debtor's petition in this case. In addition, it is possible that the reasoning of the *Purdue* decision will shed light on considerations relevant to the questions presented in NexPoint's petition. Both petitions in this case should therefore be held pending the Court's decision in *Purdue*, and then disposed of as appropriate in light of that decision.

CONCLUSION

This Court should hold the petitions for writs of certiorari in this case pending disposition of *Harrington* v. *Purdue Pharma L.P.*, *supra* (No. 23-124), and then dispose of the petitions as appropriate in light of the Court's disposition in that case.

Respectfully submitted.

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