No. 23-124

IN THE

# Supreme Court of the United States

WILLIAM K. HARRINGTON,
UNITED STATES TRUSTEE, REGION 2,

*Petitioner,*

v.

PURDUE PHARMA L.P., ET AL.,

*Respondents.*

**On Writ of Certiorari to the United States Court of Appeals for the Second Circuit**

## BRIEF FOR *AMICI CURIAE* NEXPOINT ADVISORS, L.P. AND NEXPOINT ASSET MANAGEMENT, L.P. IN SUPPORT OF PETITIONER


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NEXPOINT ASSET MANAGEMENT, L.P.
IN SUPPORT OF PETITIONER**

## INTEREST OF *AMICI CURIAE*[1]

*Amici Curiae* NexPoint Advisors, L.P. and NexPoint Asset Management, L.P. ("NexPoint") are registered investment advisers who participated in the Chapter 11

[1] Pursuant to this Court's Rule 37.6, *amici* state that no counsel for a party authored this brief in whole or in part, that no such counsel or party made a monetary contribution intended to fund the preparation or submission of the brief, and that no person other than *amici* and their counsel made such a monetary contribution.

reorganization of Highland Capital Management, L.P. ("Highland"). Two related petitions for a writ of certiorari arising from the Highland reorganization are currently pending before this Court. NexPoint respectfully submits this *amicus* brief, both to apprise the Court of its experience in the Highland reorganization and because the Court's decision on the third-party releases in this case will likely have a direct impact on the pending certiorari petitions in the Highland case.

In the Highland case, the bankruptcy court approved sweeping exculpations and injunctions in favor of a long list of third parties. The Fifth Circuit properly reversed that ruling in part, holding that Section 524(e) of the Bankruptcy Code prohibits courts from granting discharges to third parties who have not themselves declared bankruptcy. But it upheld third-party exculpations and injunctions with respect to certain parties, such as Highland's independent directors. See *In re Highland Cap. Mgmt., L.P.*, 48 F.4th 419, 435-440 (5th Cir. 2022).

Both Highland and NexPoint filed petitions for a writ of certiorari seeking review of the Fifth Circuit's decision. See *Highland Cap. Mgmt., L.P.* v. *NexPoint Advisors, L.P.*, No. 22-631 (filed Jan. 5, 2023); *NexPoint Advisors, L.P.* v. *Highland Cap. Mgmt., L.P.*, No. 22-669 (filed Jan. 16, 2023). Highland's petition claims that the Fifth Circuit erred by invalidating the third-party exculpations and injunctions as inconsistent with Section 524(e). NexPoint, by contrast, challenges the Fifth Circuit's decision to uphold certain third-party exculpations and injunctions. This Court called for the views of the Solicitor General in both cases on May 15, 2023. 143 S. Ct. 2454 (2023); 143 S. Ct. 2455 (2023). The Solicitor General has not yet filed a response.

Given NexPoint's role in that ongoing dispute, NexPoint has both unique insights into the issues presented in this case and a strong interest in the Court's decision. NexPoint has experienced, firsthand, the effect of third-party discharges in the reorganization process and their tendency to invite abuse. The Court's decision on the third-party releases in this case, moreover, will likely have a direct impact on the two petitions arising from the Highland reorganization. The third-party exculpations and injunctions there are invalid for the same reasons as the third-party releases here: Both are species of discharges, and Section 524(e) of the Bankruptcy Code makes clear that a discharge extends only to the debtor and not to third parties that have not themselves declared bankruptcy.

Highland's case arguably differs from this one with respect to the breadth of the provisions. Purdue's reorganization plan involves third-party *releases* that purport to eliminate third-party liability for a broad range of conduct, both pre- and post-petition. Highland's plan involves third-party *exculpations* that purport to relieve third parties from liability only for conduct relating to the bankruptcy proceeding, and only for claims short of gross negligence or willful misconduct. But that distinction between releases and exculpations should make no difference. Both are species of discharges. And Section 524(e) prohibits bankruptcy courts from granting any discharge to a third party, whether a court purports to release any and all claims or instead only certain categories of claims.

NexPoint therefore submits this brief to encourage this Court to issue a clear decision holding that Section 524(e) condemns all such provisions. Both third-party releases and third-party exculpations violate the express

terms of the Bankruptcy Code. There is no principled basis for distinguishing between them.

## SUMMARY OF ARGUMENT

Under the express terms of the Bankruptcy Code, a discharge affects only the debtor, not third parties who have not themselves declared bankruptcy. Bankruptcy courts cannot avoid that fundamental limitation by giving a discharge some different and broader effect. That principle applies equally whether a court purports to eliminate a party's liability entirely through a third-party release or instead merely to restrict the party's liability through a third-party exculpation.

I. A. Section 524 of the Bankruptcy Code limits the impact of a discharge to the debtor alone. Section 524(e) makes clear that the "discharge of a debt of the debtor *does not affect the liability of any other entity* on * * * such debt." 11 U.S.C. § 524(e) (emphasis added). Courts may not modify Congress's clear design by purporting to bestow a discharge with some broader effect.

B. Section 524(g) confirms that limitation by establishing an exception to Section 524(e) for a narrow category of cases. That provision states that, "[n]otwithstanding the provisions of section 524(e), * * * an injunction may bar any action directed against a third party" for certain asbestos claims. 11 U.S.C. § 524(g)(4)(A)(ii). That "notwithstanding" phrasing would make no sense if Section 524(e) did not already restrict courts' authority to grant third-party releases and exculpations.

C. Section 524(e)'s plain meaning reflects nearly two centuries of prior statutes that similarly limited the impact of a discharge to the debtor alone. Courts interpreted those prior statutes to bar third-party releases. Section 524(e) should be read the same way.

D. Sections 105(a) and 1123(b)(6) do not authorize third-party releases or exculpations. Those provisions by their terms do not apply. And even if they did, a court may not rely on general authorizations where a specific provision directly addresses an issue.

II. A. The foregoing principles apply both to third-party releases that eliminate a party's liability altogether and to third-party exculpations that eliminate only certain claims related to the bankruptcy itself. Section 524's text and structure apply equally to both types of provisions. And courts and the federal government have rejected efforts to distinguish between the two. Those courts that have treated releases differently from exculpations offer no persuasive basis for the distinction.

B. Third-party exculpations, no less than releases, invite abuse. Parties regularly propose reorganization plans with sprawling lists of exculpated parties and then fail to justify the breadth of the provisions. The plan that Highland proposed in NexPoint's case is a paradigmatic example.

This Court should reverse the Second Circuit's decision and reject the third-party releases in Purdue's plan. But the Court should avoid any rationale that would invite a distinction between releases and exculpations.

## ARGUMENT

The plain text of the Bankruptcy Code—like nearly two centuries of bankruptcy practice before it—precludes courts from granting discharges to third parties who have not themselves declared bankruptcy. Those provisions apply equally both to blanket releases and to more nuanced exculpations that merely eliminate liability for certain claims or conduct.

## I. SECTION 524 PROHIBITS THIRD-PARTY RELEASES AND EXCULPATIONS

The Bankruptcy Code makes clear that a discharge affects only liabilities of the *debtor*, not third parties. The statutory text is explicit. And the Code's historical backdrop confirms that the Code both says what it means and means what it says: Bankruptcy courts may only discharge debts of the debtor—not debts of third parties who have not filed for bankruptcy themselves.

### A. The Text and Structure of Section 524 Preclude Third-Party Releases and Exculpations

"The principal purpose of the Bankruptcy Code is to grant a 'fresh start' to the 'honest but unfortunate debtor.'" *Marrama* v. *Citizens Bank of Mass.*, 549 U.S. 365, 367 (2007). To that end, the Code provides for the discharge of the debtor's *own* liabilities. Confirmation of a Chapter 11 plan "discharges the *debtor* from any debt that arose before the date of such confirmation." 11 U.S.C. § 1141(d)(1)(A) (emphasis added).

Section 524 carefully describes the "[e]ffect" of that "discharge." 11 U.S.C. § 524. Section 524(a)(1) "voids any judgment * * * of the personal liability *of the debtor*." *Id.* § 524(a)(1) (emphasis added). And Section 524(a)(2) "operates as an injunction" against any effort to recover a debt as "a personal liability *of the debtor*." *Id.* § 524(a)(2) (emphasis added). Section 524(a) thus restricts the discharge to the debtor's *own* liabilities.

Section 524(e) makes that limitation explicit. "Except as provided in subsection (a)(3) of this section, 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) (emphasis added). That language could hardly be clearer. Except where Con-

gress explicitly says otherwise, the effect of the discharge is strictly limited to the debtor. Courts cannot evade that limit by granting releases or exculpations to parties other than the debtor who have not themselves declared bankruptcy. Congress defined the effect of a discharge and explicitly limited its impact to the debtor's own liabilities. A bankruptcy court cannot ignore Congress's judgment and decide to give a discharge some different and broader effect in a particular case instead.

Section 524(e)'s one textual exception—"[e]xcept as provided in subsection (a)(3)"—makes that limitation clearer still. Subsection (a)(3) addresses certain spousal community property (a type of property irrelevant to corporate reorganizations like this one). 11 U.S.C. § 524(a)(3). The need for that exception underscores Section 524(e)'s clear scope. Except where the Code says otherwise, a Chapter 11 discharge does not and cannot reach third-party liabilities. A statute's "enumeration of exemptions * * * confirms that courts are not authorized to create additional exceptions." *Law* v. *Siegel*, 571 U.S. 415, 424 (2014); see also *Hillman* v. *Maretta*, 569 U.S. 483, 496 (2013) ("[W]here Congress explicitly enumerates certain exceptions to a general prohibition, additional exceptions are not to be implied * * * ."). Congress's enactment of one specific exception for certain spousal property confirms that Congress did not envision that courts would dole out releases or exculpations to third parties whenever they considered it appropriate.

The Fifth and Tenth Circuits thus correctly recognize that the plain language of Section 524(e) prohibits courts from extending the impact of a discharge beyond the debtor's own liabilities. "[Section] 524(e) categorically bars third-party exculpations absent express authority in another provision of the Bankruptcy Code." *In re High-*

*land Cap. Mgmt., L.P.*, 48 F.4th 419, 436 (5th Cir. 2022), cert. pending, Nos. 22-631 & 22-669; see also *In re Pac. Lumber Co.*, 584 F.3d 229, 252 (5th Cir. 2009) (because "Section 524(e) only releases the debtor, not co-liable third parties," the Bankruptcy Code "foreclose[s] non-consensual non-debtor releases and permanent injunctions"). Simply put, "Congress did not intend to extend such benefits to third-party bystanders." *In re W. Real Est. Fund, Inc.*, 922 F.2d 592, 600 (10th Cir. 1990); see also *In re Lowenschuss*, 67 F.3d 1394, 1401 (9th Cir. 1995) (Section 524 "does not * * * provide for the release of *third parties* from liability"), cert. denied, 517 U.S. 1243 (1996).

### B. Section 524(g)'s Narrow Exception for Asbestos Claims Precludes Other Third-Party Releases and Exculpations

Another provision in the same section, Section 524(g), removes any doubt about Congress's design. Section 524(g) grants courts additional authority in bankruptcies involving "damages allegedly caused by the presence of, or exposure to, asbestos or asbestos-containing products." 11 U.S.C. § 524(g)(2)(B)(i)(I). In that one narrow context, Congress provided that, "[n]otwithstanding the provisions of section 524(e), * * * an injunction may bar any action directed against a third party" that is alleged to be liable as a result of its ownership or management of the debtor, its provision of insurance, or its role in a corporate restructuring. *Id.* § 524(g)(4)(A)(ii). Even then, the statute prescribes strict requirements, such as 75% voting support from the affected class of creditors. *Id.* § 524(g)(2)(B)(ii)(IV)(bb).

Section 524(g)'s phrasing makes clear that Section 524(e) otherwise prohibits third-party releases or exculpations. First, Section 524(g) states that an injunction in

an asbestos case may bar a claim against a third party "*[n]otwithstanding the provisions of section 524(e)*." 11 U.S.C. § 524(g)(4)(A)(ii) (emphasis added). That "notwithstanding" phrasing makes sense only if Section 524(e) otherwise prohibits such injunctions.

Second, Section 524(g)'s authorization of third-party injunctions in one specific context—asbestos cases—would be superfluous if bankruptcy courts could grant such protections in *any* context. This Court is "hesitant to adopt an interpretation of a congressional enactment which renders superfluous another portion of that same law." *Kawaauhau* v. *Geiger*, 523 U.S. 57, 62 (1998). Indeed, "[t]he canon against surplusage is strongest when an interpretation would render superfluous another part of the same statutory scheme." *City of Chicago* v. *Fulton*, 141 S. Ct. 585, 591 (2021). Section 524(g)'s specific authorization for certain third-party injunctions confirms Congress's understanding that courts did not already possess that authority. Otherwise there would have been no need to enact the provision.

Congress's careful limits on Section 524(g) strengthen that inference. While Section 524(g) prescribes an exception to Section 524(e), it sharply limits the third parties who may benefit from the injunctions it authorizes and the circumstances in which courts may grant such injunctions. Section 524(g) applies only to certain asbestos cases; it authorizes third-party injunctions only for particular types of liabilities; and it imposes strict requirements such as 75% approval by the affected creditors. 11 U.S.C. § 524(g)(2)(B), (4)(A)(ii). Those limitations would be meaningless if courts had general authority to grant third-party protections without regard to such limits. See Jonathan M. Seymour, *Against Bankruptcy Exceptionalism*, 89 U. Chi. L. Rev. 1925, 2008 (2022) (urging

that Section 524(g)'s "tightly constrained mechanism for channeling third-party liability only applicable in asbestos cases" "prohibits courts from authorizing third-party releases" in other contexts).

Section 524(g)'s enacting legislation does not say otherwise. In an uncodified provision, Congress included a "rule of construction" that states that "[n]othing in [Section 524(g)] shall be construed to modify, impair, or supersede any other authority the court has to issue injunctions in connection with an order confirming a plan of reorganization." Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 111(b), 108 Stat. 4106, 4117 (1994). That "rule of construction" is irrelevant here. Drawing reasonable inferences about Congress's understanding of existing law is not equivalent to "modify[ing], impair[ing], or superseding]" a court's authority. The point here is not that Section 524(g) *modified* courts' authority to issue injunctions. The point is simply that the way Congress phrased Section 524(g) shows that Congress understood that Section 524(e) would otherwise prohibit such injunctions.

### C. Longstanding Bankruptcy Practice Confirms Section 524(e)'s Plain Meaning

Section 524(e) follows nearly two centuries of bankruptcy tradition barring third-party discharges. There is no evidence that Congress sought to break from that tradition when it enacted the Bankruptcy Code in 1978. This Court has made clear that, "[w]hen Congress amends the bankruptcy laws, it does not write 'on a clean slate.'" *Dewsnup* v. *Timm*, 502 U.S. 410, 419 (1992). The Court "will not read the Bankruptcy Code to erode past bankruptcy practice absent a clear indication that Congress intended such a departure." *Hamilton* v. *Lanning*, 560 U.S. 505, 517 (2010). The Second Circuit's approval of third-party releases in this case represents a sharp break

from pre-Code practice without the slightest indication that Congress intended that departure.

Pre-Code history makes clear that a bankruptcy discharge affects only the debtor's own liabilities and that courts may not discharge the debts of third parties. For two centuries, bankruptcy legislation has included language similar to Section 524(e) imposing that limitation. The original Bankruptcy Act of 1800 provided that "no such discharge of a bankrupt, shall release or discharge any person who was a partner with such bankrupt * * * or who was then jointly held or bound with such bankrupt for the same debt or debts." Act of Apr. 4, 1800, ch. 19, § 34, 2 Stat. 19, 31. The 1841 Act provided that "no discharge of any bankrupt under this act shall release or discharge any person who may be liable for the same debt as a partner, joint contractor, endorser, surety, or otherwise." Act of Aug. 19, 1841, ch. 9, § 4, 5 Stat. 440, 444. The 1867 Act stated that "no discharge granted under this act shall release, discharge, or affect any person liable for the same debt for or with the bankrupt, either as partner, joint contractor, indorser, surety, or otherwise." Act of Mar. 2, 1867, ch. 176, § 33, 14 Stat. 517, 533. And the 1898 Act stated that "[t]he liability of a person who is a co-debtor with, or guarantor or in any manner a surety for, a bankrupt shall not be altered by the discharge of such bankrupt." Act of July 1, 1898, ch. 541, § 16, 30 Stat. 544, 550. Congress thus followed an unbroken practice of limiting the impact of a discharge to the debtor itself.

Courts, moreover, interpreted Section 16 of the 1898 Act to prohibit third-party releases. In *In re Diversey Building Corp.*, 86 F.2d 456 (7th Cir. 1936), cert. denied, 300 U.S. 662 (1937), for example, the district court issued an injunction pursuant to a reorganization plan that "per-

petually restrain[ed] and enjoin[ed] [certain creditors] from instituting or further prosecuting any proceedings at law or in equity against the debtor, or against Fred Becklenberg," the debtor's guarantor. *Id.* at 456-457. The Seventh Circuit reversed. The reorganization plan, it held, was "too extensive in its scope" because "[i]t not only purported to reorganize the debtor's estate * * * but it also essayed to reduce the indebtedness of Becklenberg." *Id.* at 457. The court deemed its ruling "supported by section 16 of the Bankruptcy Act which provides that the liability of a person who is a co-debtor with, or guarantor, or in any manner a surety for, a bankrupt, shall not be altered by the discharge of such bankrupt." *Id.* at 458 (citation omitted).

Similarly, in *In re Bracy*, 449 F. Supp. 70 (D. Mont. 1978), a bankruptcy court issued an injunction that purported to restrain a creditor from pursuing claims in state court against both a discharged debtor and his insurer. *Id.* at 71. On appeal, the district court set aside the injunction to the extent it barred claims against the insurer. *Id.* at 71-72. The court observed that "Section 16 of the Bankruptcy Act provides that '[t]he liability of a person who is a codebtor with, or guarantor or in any manner a surety for, a bankrupt shall not be altered by the discharge of such bankrupt.'" *Id.* at 71 (citation omitted). As a result, "if an insurance company is as a matter of state law liable to a plaintiff in a personal injury action, subsequent discharge of the assured in bankruptcy does not alter the obligation of the insurance company." *Ibid.* "It seems clear that it is the policy of the law to discharge the bankrupt but not to release from liability those who are liable with him." *Ibid.*

Under the 1898 Bankruptcy Act, moreover, courts generally did not even have *jurisdiction* to issue third-

party releases or exculpations. In *Callaway* v. *Benton*, 336 U.S. 132 (1949), this Court explained that Congress's grant of "exclusive jurisdiction [over] the debtor and its property" did not encompass "exclusive jurisdiction over all controversies that in some way *affect* the debtor's estate." *Id.* at 142 (emphasis added). The Court set aside an injunction that purported to enjoin proceedings that would affect the debtor's reorganization but did not directly involve debtor property. *Id.* at 150-151. Other courts relied on the same jurisdictional limitation to reject third-party releases. See *Diversey*, 86 F.2d at 457-458 (no jurisdiction to enjoin claims against guarantor); *In re Nine N. Church St.*, 82 F.2d 186, 189 (2d Cir. 1936) (similar); Ralph Brubaker, *Nondebtor Releases and Injunctions in Chapter 11: Revisiting Jurisdictional Precepts and the Forgotten* Callaway v. Benton *Case*, 72 Am. Bankr. L.J. 1, 33 (1998) (noting that courts under the 1898 Act "rejected occasional efforts to obtain permanent nondebtor releases through a plan of reorganization").

Nothing in the Bankruptcy Code suggests that Congress departed from the traditional limits on discharges and authorized free-wheeling releases and exculpations for third parties. The Bankruptcy Code did, of course, expand federal jurisdiction to encompass claims that are merely "related to" a debtor's estate. 28 U.S.C. § 1334(b). But Congress did not expand the scope of a court's *discharge* authority. And the fact that jurisdictional limitations largely prevented this issue from even arising in pre-Code practice confirms that the plan provisions the Second Circuit endorsed would be a sharp departure from longstanding practice. This Court requires a "clear indication" from Congress before "read[ing] the Bankruptcy Code to erode past bankruptcy practice." *Hamil-*

*ton*, 560 U.S. at 517. The Bankruptcy Code contains no such indication, much less a clear one, here.

**D. General Bankruptcy Code Provisions Do Not Justify Departing from Section 524(e)**

Despite Section 524(e)'s clear text and history, some courts have invoked other, general provisions of the Bankruptcy Code to uphold third-party releases and exculpations. In particular, Section 105(a) states that "[t]he court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title." 11 U.S.C. § 105(a). And Section 1123(b)(6) states that a Chapter 11 plan may "include any other appropriate provision not inconsistent with the applicable provisions of this title." *Id.* § 1123(b)(6). Neither provision authorizes third-party releases or exculpations.

Those provisions, by their terms, do not grant the authority claimed. Section 105(a) authorizes only orders "necessary or appropriate to carry out *the provisions of this title*." 11 U.S.C. § 105(a) (emphasis added). That section thus requires that an order implement another specific provision of the Bankruptcy Code, not merely a court's policy preferences or sense of fairness. See *In re Dairy Mart Convenience Stores, Inc.*, 351 F.3d 86, 92 (2d Cir. 2003) ("The equitable power conferred on the bankruptcy court by section 105(a) is the power to exercise equity in carrying out the *provisions* of the Bankruptcy Code, rather than to further the purposes of the Code generally, or otherwise to do the right thing.").

Similarly, Section 1123(b)(6) authorizes Chapter 11 plans to contain only "*appropriate* provision[s]" that are "*not inconsistent* with the applicable provisions of this title." 11 U.S.C. § 1123(b)(6) (emphasis added). Granting third-party releases or exculpations *is* "inconsistent with the applicable provisions of this title"—namely, Section

524's careful limitations on the effect of a discharge. And plan provisions plainly are not "appropriate" when they purport to give a discharge a broader effect than the one Congress prescribed.

Basic canons of construction foreclose expansive readings of Sections 105(a) and 1123(b)(6). "[I]t is a commonplace of statutory construction that the specific governs the general." *RadLAX Gateway Hotel, LLC* v. *Amalgamated Bank*, 566 U.S. 639, 645 (2012). Thus, where "a general authorization and a more limited, specific authorization exist side-by-side," the "terms of the specific authorization must be complied with." *Ibid.* Section 524 specifically addresses third-party protections and authorizes them only in one narrow context involving asbestos claims. Courts may not rely on more general provisions elsewhere in the Bankruptcy Code to issue such orders.

Nor may bankruptcy courts invoke their general equitable authority to approve third-party releases or exculpations. This Court has explained that "whatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code." *Norwest Bank Worthington* v. *Ahlers*, 485 U.S. 197, 206 (1988). "[A] court sitting in equity cannot 'ignore the judgment of Congress, deliberately expressed in legislation.'" *United States* v. *Oakland Cannabis Buyers' Coop.*, 532 U.S. 483, 497 (2001).

The Fifth and Tenth Circuits have thus correctly rejected attempts to rely on the Bankruptcy Code's general authorizations in Sections 105(a) and 1123(b)(6) to justify third-party releases or exculpations. "'[A] § 105 injunction cannot alter another provision of the code,'" and "the same logic extends to § 1123(b)(6), which allows a plan to 'include any other appropriate provision *not inconsistent with the applicable provisions of this title*.'" *Highland*

*Cap.*, 48 F.4th at 437; see also *W. Real Est.*, 922 F.2d at 601 ("[A] bankruptcy court's supplementary equitable powers [under Section 105(a)] may not be exercised in a manner that is inconsistent with the other, more specific provisions of the Code."); Ralph Brubaker, *Mandatory Aggregation of Mass Tort Litigation in Bankruptcy*, 131 Yale L.J.F. 960, 979 (2022) (Section 105 "is too weak a reed upon which to rest [delegation of] so weighty a power").

## II. SECTION 524(e)'S LIMITATIONS APPLY ACROSS THE BOARD TO BOTH THIRD-PARTY RELEASES AND THIRD-PARTY EXCULPATIONS

Some courts distinguish between third-party *releases* and third-party *exculpations*. Releases eliminate liability for a broad range of conduct before or after the bankruptcy petition; exculpations apply only to conduct related to the bankruptcy proceeding and typically exclude certain categories of claims, such as gross negligence or willful misconduct. See, *e.g.*, *Blixseth* v. *Credit Suisse*, 961 F.3d 1074, 1083-1084 (9th Cir. 2020) (distinguishing between exculpations and releases). Purdue's plan in this case involves third-party releases. Highland's plan at issue in the two pending petitions that NexPoint and Highland have filed (Nos. 22-631 and 22-669) involve third-party exculpations.

While that terminology may be useful to categorize the provisions, it does not justify treating them differently under Section 524(e). The Bankruptcy Code forecloses both third-party releases and third-party exculpations. Whether a plan purports to eliminate all claims against a third party or merely certain claims relating to certain conduct, the Bankruptcy Code does not authorize courts to discharge claims against third parties who have not themselves sought bankruptcy protection.

### A. Nothing in the Text of the Bankruptcy Code Supports a Distinction Between Releases and Exculpations

As explained above, the plain text of the Bankruptcy Code limits the effect of a discharge to the debtor itself and excludes any impact on third parties. Section 524(e) provides that the "discharge of a debt of the debtor *does not affect* the liability of any other entity on * * * such debt." 11 U.S.C. § 524(e) (emphasis added). That expansive language clearly encompasses exculpations no less than releases. Nothing in that language turns on the *extent* of the liabilities a court purports to eliminate. An exculpation clearly "affect[s]" a third party's liability, even if it does not eliminate all claims entirely.

Under Section 524(e), courts may not dole out blanket immunity to third parties for any and all claims. Nor may they dole out partial immunity for certain claims arising from the bankruptcy proceeding. Either type of immunity would disregard Congress's design by allowing third parties to claim the benefits of bankruptcy protection without subjecting themselves or their property to the bankruptcy process.

An exculpation, after all, *is* a release with respect to the claims that fall within its terms. A plan that limits a third party's liability to gross negligence or willful misconduct completely eliminates claims for ordinary negligence or strict liability. Whether one labels the provision an "exculpation" or a "release" makes no difference; the plan purports to eliminate certain claims. The impact can be particularly grave where a provision eliminates all liability short of gross negligence, leaving many claimants with no remedy or at least a burden that is much more difficult to overcome. See *Conway* v. *O'Brien*, 312 U.S. 492, 495 (1941) ("Gross negligence is substantially

and appreciably higher in magnitude and more culpable than ordinary negligence.”).

Section 524(g) does not support a distinction between releases and exculpations. That provision authorizes third-party protections in one narrow circumstance involving asbestos claims, subject to strict limitations and requirements. It does not authorize either releases or exculpations outside that context and without regard to those limitations and requirements. Nor do Sections 105(a) and 1123(b)(6) provide any greater authority for third-party exculpations. In short, all the textual arguments about the effect of Section 524 apply equally to both releases and exculpations.

Consistent with that analysis, the Fifth Circuit has repeatedly rejected the argument that courts should tolerate third-party exculpations even if they prohibit third-party releases. In *In re Pacific Lumber Co.*, 584 F.3d 229 (5th Cir. 2009), the court confronted a provision that “release[d] [certain parties] from liability—other than for willfulness and gross negligence—related to proposing, implementing, and administering the plan.” *Id.* at 251. The court explained that “the essential function of the exculpation clause proposed here is to absolve the released parties from any negligent conduct that occurred during the course of the bankruptcy.” *Id.* at 252. “The fresh start § 524(e) provides to debtors is not intended to serve this purpose.” *Id.* at 252-253. The court also invoked Section 524(g), which “suggests non-debtor releases are most appropriate as a method to channel mass claims toward a specific pool of assets,” not to limit parties’ liability for misconduct during the bankruptcy process. *Id.* at 252.

The Fifth Circuit reaffirmed that holding in NexPoint and Highland’s case. Highland urged the court to distin-

guish between "a concededly unlawful release of all non-debtor liability and the Plan's limited exculpation of non-debtor post-petition liability." *Highland Cap.*, 48 F.4th at 435. The Fifth Circuit rejected that "parsing between limited exculpations and full releases." *Id.* at 436. Section 524(e), the court held, "categorically bars third-party exculpations absent express authority in another provision of the Bankruptcy Code." *Ibid.*

The government has similarly rejected any distinction between exculpations and releases. In *In re Airadigm Communications, Inc.*, 519 F.3d 640 (7th Cir. 2008), the debtor's plan purported to "release[ ] the [debtor's] third-party financier * * * from liability for 'any act or omission arising out of or in connection with the * * * confirmation of this Plan * * * except for willful misconduct.'" *Id.* at 646-647. The Department of Justice filed a brief for the Federal Communications Commission opposing that provision. See FCC Br. in *In re Airadigm Commc'ns, Inc.*, No. 07-2212, 2007 WL 2216441, at 66-71 (7th Cir. July 27, 2007). The government urged that the exculpatory clause violated Section 524(e) because "plan provisions * * * effectively barring the litigation of claims against other parties are tantamount to a discharge of those claims, and a discharge of claims against parties other than the debtor is inconsistent with section 524(e)." *Id.* at 68. The provision's limitation to claims arising out of the bankruptcy process did not mitigate the problem. To the contrary, "the use of a release to extinguish claims arising out of the third party's conduct during the bankruptcy itself is particularly inappropriate." *Id.* at 71.

The U.S. Trustee has likewise objected to third-party exculpations no less than third-party releases. In Highland's bankruptcy, the U.S. Trustee objected to the exculpations. See U.S. Trustee Obj. in *In re Highland*

*Cap. Mgmt., L.P.*, No. 19-34054, Dkt. 1671 (Bankr. N.D. Tex. Jan. 5, 2021). It urged that the "plan contains nonconsensual third-party releases and exculpation in contravention of Fifth Circuit precedent." *Id.* at 4.

Even circuits that sometimes permit third-party releases recognize that releases and exculpations raise similar concerns. For example, in *In re Seaside Engineering & Surveying, Inc.*, 780 F.3d 1070 (11th Cir. 2015), cert. denied, 577 U.S. 823 (2015), the Eleventh Circuit confronted a provision that exculpated third parties "for any act, omission, transaction or other occurrence in connection with, relating to, or arising out of the Chapter 11 Case" except for "fraud, gross negligence or willful misconduct." *Id.* at 1076. The court held that such provisions "should be reserved for those unusual cases in which such an order is necessary for the success of the reorganization." *Id.* at 1078. The court directed bankruptcy courts to consider a list of factors that other courts had applied to third-party *releases*. *Id.* at 1079 (citing *In re Dow Corning Corp.*, 280 F.3d 648, 658 (6th Cir. 2002)). The Eleventh Circuit erred by permitting such provisions at all—but the court at least recognized that third-party exculpations and third-party releases are cut from the same cloth.

The few courts that have distinguished exculpations from releases offer no persuasive justification for the different treatment. Most prominently, in *Blixseth* v. *Credit Suisse*, 961 F.3d 1074 (9th Cir. 2020), cert. denied, 141 S. Ct. 1394 (2021), the Ninth Circuit upheld a third-party exculpation despite having invalidated third-party releases in several prior cases. *Id.* at 1081-1085. The Ninth Circuit failed to justify that departure from Section 524(e)'s clear strictures.

The Ninth Circuit reasoned that the exculpation was "narrow in both scope and time" because it covered only claims relating to the bankruptcy proceeding and excluded willful misconduct and gross negligence. 961 F.3d at 1081-1082. But the fact that an exculpation covers only *some* claims over *some* conduct does not reconcile it with the statutory text. Section 524(e) states that a discharge "does not affect" third-party liabilities. 11 U.S.C. § 524(e). It does not say that a court may discharge third parties for certain claims so long as it does not go too far.

The Ninth Circuit also reasoned that Section 524(e) did not apply because that provision addresses only third-party liability for "a debt of the debtor." 961 F.3d at 1082-1083 (quoting 11 U.S.C. § 524(e)). In other words, in that court's view, a bankruptcy court may not release a third party from liability for the *debtor's* debt, but it may release third parties from liability for *completely separate* debts for which the debtor is *not* liable. That is entirely backwards. Congress could not conceivably have intended to prohibit bankruptcy courts from granting third-party releases for debts on which the debtor is co-liable, while leaving courts free to release third-party debts with no connection to the debtor's estate at all. The obvious implication of Section 524(e) is that bankruptcy courts may not discharge third parties, period.[2]

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[2] The Ninth Circuit's reasoning is akin to reading the Takings Clause to impose no limits at all on takings for *private* use because the Clause states that "private property [shall not] be taken for *public* use, without just compensation." U.S. Const. amend. V (emphasis added). The obvious implication of that phrasing is that takings for private use are not permitted *at all*. See *Kelo* v. *City of New London*, 545 U.S. 469, 496 (2005) (O'Connor, J., dissenting) ("[W]e have read the Fifth Amendment's language to impose two distinct conditions on the exercise of eminent domain: '[T]he taking must be for

The Ninth Circuit finally emphasized the "highly litigious nature of Chapter 11 bankruptcy proceedings" and the desirability of allowing parties "to engage in the give-and-take of the bankruptcy proceeding without fear of subsequent litigation." 961 F.3d at 1084. That naked policy preference is no excuse for disregarding statutory text. Exculpation clauses relieve bankruptcy participants from the "fear of subsequent litigation" only by stripping other parties of otherwise valid claims. In any event, Congress is fully capable of authorizing third-party protections in contexts where it thinks there is too much litigation—as it did for asbestos claims. 11 U.S.C. § 524(g). Courts should not second-guess Congress's judgments by taking matters into their own hands.

Given the Ninth Circuit's dubious reasoning, it is no surprise that commentators have noted the tension between *Blixseth* and the Ninth Circuit's prior cases rejecting third-party releases. See, *e.g.*, Adam J. Levitin, *The Constitutional Problem of Nondebtor Releases in Bankruptcy*, 91 Fordham L. Rev. 429, 432 n.8 (2022); Caleb Downs, Note, *Without Exception? The Ninth Circuit's Evolving Stance on Nondebtor Releases in Chapter 11 Reorganizations*, 95 S. Cal. L. Rev. 953, 978 (2022). Neither *Blixseth* nor any other decision justifies treating third-party exculpations differently from third-party releases.

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a "public use" and "just compensation" must be paid to the owner.' "). Likewise here, the fact that Section 524(e) refers only to debts for which a third party is co-liable does not mean that courts may discharge a third party's independent debts with impunity. It confirms that courts may not discharge third-party debts *at all*.

### B. Third-Party Exculpations Invite Abuse

Experience has shown that third-party exculpations are a recipe for abuse. Debtors often propose sprawling exculpations that apply to a lengthy list of parties with little or no ascertainable justification.

In *Patterson* v. *Mahwah Bergen Retail Group, Inc.*, 636 B.R. 641 (E.D. Va. 2022), for example, the court rejected an exculpation that covered "all current and former employees, attorneys, accountants, managers, financial advisors and consultants of every party being exculpated." *Id.* at 702. The court faulted the provision for "extend[ing] beyond fiduciaries who have performed necessary and valuable duties" in the proceeding. *Ibid.*

In *In re Council of Unit Owners of 100 Harborview Drive Condominium*, 572 B.R. 131 (Bankr. D. Md. 2017), the court rejected an exculpation that applied to "any Affiliate [of the debtor] or any of their respective directors, officers, employees, members, attorneys, attorneys of the members, consultants, advisors and agents." *Id.* at 138-139. The court saw "no cogent reason * * * to impose such an onerous and possibly unconstitutional restriction" and rejected the provision for "broadly hindering and/or depriving [parties] of their legitimate rights to access to the courts." *Id.* at 139.

In *In re SunEdison, Inc.*, 576 B.R. 453 (Bankr. S.D.N.Y. 2017), the court invalidated an exculpation that applied to an even lengthier list of parties:

> (a) the Debtors and all of the Debtors' and Reorganized Debtors' (1) current financial advisors, attorneys, accountants, investment bankers, representatives, and other professionals * * * ; (2) current employees, consultants, Affiliates, officers and directors, * * * (3) Existing Directors, (b) the Origi-

> nal DIP Agents, (c) the Original DIP Lenders and all other Original DIP Secured Parties, (d) the Replacement DIP Agents, (e) the Replacement DIP Lenders, (f) the Supporting Second Lien Parties, (g) all Professionals * * * , (h) the Creditors' Committee and each of its members * * * , (i) the Indenture Trustees, (j) the Second Lien Collateral Trustee, (k) the Second Lien Agents, (*l*) any underwriters, arrangers, or placement agents in respect of the Second Lien Senior Notes, (m) the Prepetition First Lien Secured Parties, (n) the Prepetition First Lien Agents, (o) the Applicable Issuers, and (p) with respect to each of the above-named Entities * * * , such Entity's current and former affiliates, subsidiaries, advisors, principals, partners, managers, members, employees, officers, directors, representatives, financial advisors, attorneys, accountants, investment bankers, consultants, agents, and other representatives and professionals * * * .

576 B.R. at 456. While the debtors tried to justify that clause on the basis of purported indemnification obligations, they could not "point[ ] to any indemnification obligation running in favor of these unidentifiable Released Parties." *Id.* at 463.

The government has explained why "the use of a release to extinguish claims arising out of [a] third party's conduct during the bankruptcy itself is particularly inappropriate." FCC Br. in *In re Airadigm Commc'ns, Inc.*, No. 07-2212, 2007 WL 2216441, at 71 (7th Cir. July 27, 2007). "If a [third party], in the course of maximizing its own economic advantage, unlawfully infringes the interests of other claimants in the case, then it should be held accountable through ordinary legal process, not released from all liability." *Ibid.* "Bankruptcy is intended

to afford a measure of fairness to creditors as well as the debtor. It does not give third parties *carte blanche* to engage in whatever conduct furthers their own economic interests so long as it also facilitates the debtor's reorganization. Nor does it authorize the bankruptcy court to immunize a third party from liability for conduct that harms other parties in the case." *Ibid.*

NexPoint's own case is a paradigmatic example of abuse. Highland's reorganization plan includes a sweeping exculpation clause that applies to "(i) the Debtor and its successors and assigns, (ii) the Employees, (iii) [the Debtor's general partner] Strand, (iv) the Independent Directors, (v) the Committee, (vi) the members of the Committee (in their official capacities), (vii) the Professionals retained by the Debtor and the Committee in the Chapter 11 Case, (viii) the CEO/CRO, and (ix) the Related Persons of each." Pet. in No. 22-669, at 7. "Related Persons" include all "present, future, or former officers, directors, employees, managers, managing members, members, financial advisors, attorneys, accountants, investment bankers, consultants, professionals, advisors, shareholders, principals, partners, subsidiaries, divisions, management companies, heirs, agents, and other representatives." *Ibid.*

The exculpation clause also covers a broad range of claims. It applies not only to claims arising out of the bankruptcy proceeding, but also to "the implementation of the Plan." Pet. in No. 22-669, at 7-8. Because Highland's reorganization plan contemplated that the company would continue to operate its business for three years or longer while it gradually wound down operations, the exculpation sweeps in a broad range of post-discharge conduct. *Id.* at 8. The related injunction and gatekeeping provision similarly prohibits claims over "the wind down

of the business of the Debtor or Reorganized Debtor" unless the bankruptcy court "first determin[es] * * * that such claim or cause of action represents a colorable claim." *Ibid.* The plan thus grants broad immunity for ordinary business activities years after the bankruptcy ends.

The bankruptcy court tried to justify those broad provisions based on the parties' "litigious conduct." Pet. App. in No. 22-669, at 125a-126a. But alleged litigiousness cannot justify rewriting a statute to grant authority Congress withheld. And as NexPoint has observed, "one party's 'litigiousness' is another party's diligent protection of its legal rights." Cert. Reply in No. 22-669, at 10. In one instance, for example, the bankruptcy court tried to insulate a contempt ruling from review by stating that it would "add on a sanction of $100,000 for each level of rehearing, appeal, or petition for [certiorari] that the Alleged Contemnors may choose to take with regard to this Order, to the extent any such motions for rehearing, appeals, or petitions for certiorari are not successful." *Charitable DAF Fund LP* v. *Highland Cap. Mgmt. LP*, No. 3:21-cv-01974, Dkt. 49 at 13 n.62 (N.D. Tex. Sept. 28, 2022), appeal pending, No. 22-11036 (5th Cir.). Highland did not even defend that novel ruling on appeal, and the district court vacated it. *Id.* at 13.

The Fifth Circuit properly rejected the plan's exculpations with respect to most of the third parties. See *Highland Cap.*, 48 F.4th at 435-440. Because Highland's and NexPoint's petitions are pending before this Court, however, the fate of Highland's plan remains uncertain. For the reasons above and those in the government's brief, the Court should reverse the Second Circuit's decision upholding the third-party releases in Purdue's plan. The Court should adopt a clear holding that avoids any

suggestion that its rationale would not apply equally to third-party exculpations too.

## CONCLUSION

The court of appeals' judgment should be reversed.

Respectfully submitted.


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