UNITED STATES SECURITIES AND
EXCHANGE COMMISSION
Alan S. Maza
New York Regional Office
Brookfield Place, 200 Vesey St., Suite 400
New York, New York 10281
Phone: (212) 336-1100
Fax: (212) 336-1345

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISRICT OF NEW YORK

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In re	**Chapter 11 Case No. 19-22312 (RDD)**
WINDSTREAM HOLDINGS, INC., et al.,	**Jointly Administered**
Debtors.	**Objection Deadline: April 30, 2020** **Hearing Date: May 7, 2020**

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LIMITED OBJECTION OF THE U. S. SECURITIES AND EXCHANGE COMMISSION TO APPROVAL OF THE DISCLOSURE STATEMENT AND CONFIRMATION OF THE DEBTORS' JOINT PLAN OF REORGANIZATION

The U.S. Securities and Exchange Commission ("SEC" or "Commission"), a statutory party to these proceedings,[1] and the federal agency responsible for enforcement of the federal securities laws, objects to approval of the Disclosure Statement ("Disclosure Statement") and confirmation of the Chapter 11 Plan ("Plan") of Windstream Holdings, Inc. and its affiliated debtors (collectively, "Windstream" or the "Debtors"), dated April 1, 2020. In support of its limited objection, the Commission respectfully states as follows:[2]

1 As a statutory party in corporate reorganization proceedings, the Commission "may raise and may appear and be heard on any issue[.]" 11 U.S.C. § 1109(a).

2 Unless separately defined herein, capitalized terms have the meanings ascribed to them in the Plan.

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INTRODUCTION

As a general matter, nondebtor third party releases contravene Section 524(e) of the Bankruptcy Code, which provides that only debts of the debtor are affected by the Chapter 11 discharge provisions. Such releases have special significance for public investors because they enable nondebtors to benefit from a debtor's bankruptcy by obtaining their own releases with respect to past misconduct, including violations of the federal securities laws or breaches of fiduciary duty under state law. This concern is implicated here where the Debtors are seeking to bar public shareholders and various creditors, including public noteholders, from asserting claims against the released parties.

While such releases may be allowed in the Second Circuit in exceptional circumstances, those circumstances are not present here. *See In re Metromedia Fiber Network, Inc.,* 416 F.3d 136, 142 (2d Cir. 2005). In the absence of such exceptional circumstances, "[n]ondebtor releases may also be tolerated if the affected creditors consent." While the Debtors may claim that the inclusion of an opt-out provision renders the releases consensual, shareholder or creditor silence does not constitute "consent" to third party releases in the Commission's view. Here, the nonconsensual character of the releases is especially troubling because the releases contain no exception for gross negligence, willful misconduct or fraud.

We understand that this Court has previously relied on sections 1141(a) and (c) of the Bankruptcy Code to approve plans containing nonconsensual third-party releases. Section 1141, which provides a procedural framework for confirming a

plan to ensure that the plan is not subject to collateral attack from those who received proper notice, has no bearing on whether a nondebtor release is consensual. The issue of consent to a release is governed by contract law. The fact that a plan binds creditors and shareholders does not mean that a court should approve any term, no matter how egregious, simply because there was no objection. Indeed, the Court has an independent duty to ensure that the confirmation requirements of the Bankruptcy Code are met. Finally, we believe that, under the Supreme Court's ruling in *Stern v. Marshall*[3] the Bankruptcy Court lacks jurisdiction to approve non-consensual third party releases that involve state law claims between non-debtors.

BACKGROUND

On February 25, 2019 (the "Petition Date"), the Debtors filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code in the United States Bankruptcy Court for the Southern District of New York. On April 1, 2020, the Debtors filed the Plan and Disclosure Statement. The Debtors are a leading provider of advanced network communications, technology, broadband, entertainment, security, and core transport solutions to both consumer and business customers across the United States. (Discl. Stmt. at 18-19).

Windstream Holdings Inc. is a publicly-traded company that was traded on the NASDAQ Stock Market LLC under the ticker symbol "WIN" until March 6, 2019, when it was delisted by the NASDAQ and began trading on the OTC Markets. (Disclosure Statement at 21) As of the Petition Date, the Debtors had approximately

[3] *Stern v. Marshall,* 564 U.S. 462, 131 S. Ct. 2594,180 L. Ed. 2d 475 (2011)

$5.6 billion in aggregate funded-debt obligations including various series of publicly held secured and unsecured notes. (Discl. Stmt. at 20-21)

On April 1, 2020, the Debtors filed a plan of reorganization pursuant to a plan support agreement and global settlement of stakeholders, which provides for the transfer of the majority of the reorganized Debtors to its first-lien lenders and for distributions to holders of allowed claims in various classes, including those claims held by public noteholders. (Plan at 14) Windstream's public shareholders (Class 9) are deemed to reject the Plan and will not receive any distribution. (Plan at 21)

The Third Party Releases (the "Releases") provide releases in favor of: (a) the Consenting Creditors; (b) the Backstop Parties; (c) the Uniti Parties; (d) the indenture trustees and administrative agents under the Debtors' prepetition Secured credit agreement and Secured notes indentures; (e) the DIP Lenders; (f) the DIP Agent; and (g) with respect to each of the Debtors, the Reorganized Debtors, and each of the foregoing Entities in clauses (a) through (f), such Entity and its current and former Affiliates and subsidiaries, and such Entities' and their current and former Affiliates' and subsidiaries' current and former directors, managers, officers, equity holders . . . predecessors, successors, and assigns, subsidiaries, and numerous professionals, advisors and others who are not directly related to the bankruptcy case. (Plan at 10, defining the "Released Parties") The Releases are for any and all claims and causes of action and a wide range of other obligations and do not include a typical carve out for

liability for actions that constitute fraud, gross negligence or willful misconduct.[4] (Plan at 39)

The Releases bind holders of claims and interests who: (i) vote in favor of, or who are deemed to accept, the Plan; (ii) reject the Plan but fail to opt out of the Third Party Releases; (iii) abstain from voting on the Plan and fail to opt out of the Third Party Releases; or (iv) are deemed to reject the Plan, and fail to return the notice of nonvoting status affirmatively opting out of the Third Party Releases. (Plan at 10-11, defining the "Releasing Parties")

The Plan's exculpation provision provides that Exculpated Parties, including a wide range of non-debtors with no connection with the bankruptcy case, shall have no liability to creditors and interest holders for acts or omissions taken in connection with prepetition restructuring efforts, including pre-petition transactions related to the plan support agreement, and the bankruptcy case, although fraud or gross negligence are carved out. (Plan at 39-40).

DISCUSSION

I. Section 1141 Has No Bearing on Whether a Non-Debtor Third-Party Release is Permitted Under Section 524(e) or Applicable Law

A. Section 1141 Addresses Finality of a Plan

Bankruptcy Code section 1141(a) describes the effect of confirmation of a chapter 11 plan and states that the provisions of a confirmed plan bind the debtor, any entity issuing securities or acquiring property under the plan, and any creditor of, or

[4] The Debtors have agreed to incorporate in any modified Plan a government carve-out from non-debtor releases similar to that typically provided to the SEC in Chapter 11 cases. The SEC reserves its rights to object if the Debtors fail to incorporate an acceptable carve-out provision.

equity security holder in, the debtor. 11 U.S.C. § 1141(a). Section 1141(c) further provides that "after confirmation of a plan, the property dealt with by the plan is free and clear of all claims and interests of creditors, equity security holders, and of general partners in the debtor." 11 U.S.C. § 1141(c).

Thus, under Section 1141, a confirmed plan prevents parties from seeking to reopen issues post-confirmation where such issues were addressed under the plan. *See In re Arcapita Bank B.S.C.(c)*, 520 B.R. 15, 21 (Bankr. S.D.N.Y. 2014) citing *In re Indesco Int'l, Inc.,* 354 B.R. 660, 664 (Bankr.S.D.N.Y.2006) (bankruptcy court's "order of confirmation is treated as a final judgment with *res judicata* effect.")

Nothing in the legislative history of 1141(a) or (c) addresses the issue of consent to third party releases under a plan. Rather, as discussed above, cases that involve Section 1141(a) and (c) address the binding nature of a confirmed chapter 11 plan, and hold that the provisions of such a plan, even if improper, may not be collaterally attacked in another forum. *See, e.g., In re Frontier Insurance Group, Inc.*, 585 B.R. 685, 693-694 (Bankr. S.D.N.Y. 2018), aff'd, 598 B.R. 87 (S.D.N.Y. 2019) (Transfer of property under chapter 11 plan upheld post confirmation.); *Wells Fargo Bank v. Morrill*, No. UWYCV176035159, 2019 WL 5068461, at 3 (Conn. Super. Ct. Sept. 6, 2019) (court held that confirmation of a plan is comparable to the entry of a final judgment in an ordinary civil litigation); *In re Winn-Dixie Stores, Inc.*, 414 B.R. 764, 768 (M.D. Fla. 2009), aff'd, 639 F.3d 1053 (11th Cir. 2011) (Bankruptcy court barred lessor from amending rejection claim by debtor-lessee based on provision of confirmed plan).

Before confirmation, a party may object to any provision of the Plan and the court should give due consideration to the raised objection. *See Trulis v. Barton*, 107 F.3d 685, 691 (9th Cir. 1995) citing 5 Collier on Bankruptcy ¶ 1141.01[1] ("[C]reditors who do not wish to release third party debtors pursuant to the principal debtor's plan of reorganization should object to confirmation of the plan on the ground that such a plan provision is violative of section 524 and not within the power, even jurisdiction, of the bankruptcy court.... *The point is that only a direct attack is available and collateral attack is unavailable")*(emphasis added).

Accordingly, before confirmation, the bankruptcy court should review objections to ensure that any contested provisions are appropriate under applicable law. *Id.*[5] *See e.g.*, *In re Young Broad, Inc.*, 430 B.R. 99, 139 (Bankr. S.D.N.Y. 2010) ("The Court . . . has an independent duty to ensure that the requirements of 11 U.S.C. §1129 are satisfied, even if no objections to confirmation have been made."). To hold otherwise, could result in a situation where parties are bound to any plan provision, no matter how outrageous, under Section 1141 in spite of validly raised objections to a plan's underlying terms.

B. *Metromedia* Addresses Consent

While case law focusing on Section 1141 sheds no light on when non-debtor third-party releases are permitted, the Second Circuit has spoken to this issue in *Metromedia*. Releases in favor of nondebtors have been allowed in this Circuit if the *Metromedia* factors have been met or if the affected parties have individually

[5] The SEC appears in this case as the statutory guardian of the investing public. *SEC v. Management Dynamics, Inc.,* 515 F.2d 801, 808 (2d Cir. 1975) (In performing its assigned duties, the SEC acts as a "statutory guardian charged with safeguarding the public interest in enforcing the securities laws.").

consented to them. *See In re Metromedia Fiber Network, Inc.,* 416 F.3d 136, 142 (2d Cir. 2005) ("[n]ondebtor releases may also be tolerated if the affected creditors consent.") *citing In re Specialty Equipment Cos.*, 3 F.3d 1043, 1047 (7th Cir. 1993).

In the Commission's view, the Releases here are not consensual because the Plan deems consent to the Releases to be established based on silence or a failure to opt out. With respect to creditors who vote to reject the Plan, but do not opt out of the Releases on their ballots, or creditors or shareholders who fail to return a ballot or notice of non-voting status opting out of the Releases, their silence should not constitute consent to the Releases. *See In re SunEdison*, *Inc.*, 576 B.R. 453, 461 (Bankr. S.D.N.Y. 2017) (court held creditor silence did not signify consent, because silence may have been due to meager recovery of less than 3%); *See also In re Specialty Equipment Cos.*, 3 F.3d 1043, 1047 (7th Cir. 1993) (the consensual release "binds only those creditors voting in favor of the plan of reorganization….a creditor who votes to reject the Plan or abstains from voting may still pursue any claims against third party nondebtors"); *In re Washington Mutual*, *Inc.*, 442 B.R. 314, 355 (Bankr. D. Del. 2011) ("Failing to return a ballot is not a sufficient manifestation of consent to a third party release"); *See Emerge Energy Servs. LP*, No. 19-11563 (KBO), 2019 WL 7634308, at *18 ("the Court cannot on the record before it find that the failure of a creditor or equity holder to return a ballot or Opt-Out Form manifested their intent to provide a release. ***Carelessness, inattentiveness, or mistake are three reasonable alternative explanations***")(emphasis added).

"Courts generally apply contract principles in deciding whether a creditor consents to a third party release." *In re SunEdison*, *Inc.*, 576 B.R. at 458 *citing In re*

Washington Mutual, Inc., 442 B.R. at 352; *In re Emerge Energy Services LP, et al.,* No. 19-11563 (KBO), 2019 WL 7634308, at *18 (Bankr. D. Del. Dec. 5, 2019) citing *Restatement (Second) of Contracts* § 19 (Am. Law Inst. 1981). Under New York law, "[a]n offeror has no power to transform an offeree's silence into acceptance when the offeree does not intend to accept the offer." *Id. quoting Karlin v. Avis*, 457 F.2d 57, 62 (2d. Cir. 1972) cert denied, 409 U.S. 849 (1972). The court in *In re SunEdison, Inc*., 576 B.R. at 461, held that creditor silence did not signify consent. In holding that the nonvoting creditors did not consent, the Court followed the ruling in *In re Chassix*, stating that "[c]harging all inactive creditors with full knowledge of the scope and implications of the proposed third party releases, and implying a 'consent' to the third party releases based on creditors' inaction, is simply not realistic or fair, and would stretch the meaning of 'consent' beyond the breaking point." *Id. (quoting In re Chassix Holdings*, 533 B.R. 64, 81).

None of the situations enumerated in the Restatement apply here. The Debtors cannot rely on the silence of the Windstream's public noteholders who reject or abstain from voting on the Plan but fail to opt out, and shareholders who fail to opt out on their notice of non-voting status, as a manifestation of their acceptance of the Releases. Indeed, there can be no contractual consent by silence because the Debtors are not offering anything of benefit to these parties. Rather, they are extinguishing a right these investors may have against non-debtor third parties unless they affirmatively object by submitting an opt-out form. This is a particularly onerous requirement to place on public investors, many of whom must rely on broker-dealer

intermediaries to deliver the appropriate forms and instructions to them.[6] Rather only those stakeholders who manifest an intent to be bound by the Releases through an opt in protocol should be deemed to consent to the Releases.

In addition, in the Commission's view, the exculpation clause in the Plan constitutes an impermissible non-debtor release and discharge since it limits the liability of various non-estate fiduciaries for conduct that occurred prior to the Chapter 11 case, and hence falls squarely within the scope of Section 524(e). *See Washington Mutual*, 442 B.R. at 350, *citing In re PWS Holding Corp., 228 F.3d 224, 246 (3d Cir. 2000)* (exculpations are limited to actions by estate fiduciaries in the bankruptcy case); *see also In re Aegean Marine Petroleum Network Inc.,* 599 B.R. 717, 721 (Bankr. S.D.N.Y. 2019) (proper exculpation provision is a protection not only of court-supervised fiduciaries, but also of court-supervised and court-approved transactions) *citing In re Granite Broad. Corp*., 369 B.R. 120, 139 (Bankr. S.D.N.Y. 2007) (approving exculpation provision that was limited to conduct during the bankruptcy case and noting that the effect of the provision is to require "that any claims in connection with the bankruptcy case be raised in the case and not be saved for future litigation.").

6 Windstream's shares continue to trade and, as a result, a buyer who purchases shares after the notice of non-voting status was distributed would not automatically receive that notice. The buyer would have to contact the broker-dealer to request the relevant forms. But such shareholder could nonetheless be bound by the Releases, which apply to conduct up to the Effective Date of the Plan (which will occur after plan confirmation). Similarly, many noteholders who are dependent on notices distributed by brokers of their public debt and indentures may not necessarily receive the forms necessary to opt out of the third party release. *See In re Hexcel Corp.,* 239 B.R. 564, 566 (N.D. Cal. 1999) (potential claimants must be given notice that their interests may be affected by the bankruptcy proceeding).

II. The Court lacks jurisdiction to approve the Releases

Bankruptcy courts are courts of limited jurisdiction. While the Releases appear to be intended to be limited to claims relating to the Debtors, that purported nexus alone is insufficient to grant the court the constitutional authority to approve the Releases under the Supreme Court's holding in *Stern v. Marshall,* 564 U.S. 462, 131 S. Ct. 2594,180 L. Ed. 2d 475 (2011) and Second Circuit case law holding that a bankruptcy court may lack subject matter jurisdiction to approve the Releases.

In *Stern*, the Supreme Court held that Article III of the Constitution requires that bankruptcy courts enter final judgments only on claims that "stem from the bankruptcy itself or would necessarily be resolved in the claims allowance process"; otherwise, the bankruptcy court must submit proposed findings to the district court. *Stern*, 564 U.S. at 499. Therefore, to the extent that the jurisdictional statute permits a bankruptcy court to enter final judgment as to a claim that falls outside this boundary, the statute is unconstitutional as applied. *Id*. at 482. Here, the non-debtor claims purported to be released by the Releases neither stem from the bankruptcy itself nor have any connection to the claims allowance process.

In applying *Stern* to nonconsensual third party releases, the Third Circuit recently held that such releases could be approved by a bankruptcy court where the releases were "integral to the restructuring of the debtor-creditor relationship." *In re Millennium Lab Holdings II, LLC*, 945 F.3d 126, 137 (3d Cir. 2019). The Third Circuit held that the releases in that case were integral to the restructuring of the debtor-creditor relationship because, without the releases, the released parties would not have made contributions under the plan that were necessary to the feasibility of

the plan and without which the "Debtors would likely have shut down." *Id.* Here, there can be no argument that the Releases granted to numerous non-debtors with tenuous relationships to the Debtors are an integral part of the restructuring of the debtor-creditor relationship. Thus, the Court lacks the constitutional authority to approve them.

In addition to the constitutional problem under *Stern*, it is not even clear if the Court can be said to have statutory "related to" jurisdiction for purported releases with such a tenuous connection to the Debtors or bankruptcy estate. Specifically, courts in the Second Circuit have concluded that bankruptcy courts lack jurisdiction to enjoin claims that are not against an asset of the bankruptcy estate and that do not affect the estate. *See In re Aegean Marine Petroleum Network Inc.,* 599 B.R. 717, 723 (Bankr. S.D.N.Y. 2019) citing *Johns-Manville Corp. v. Chubb Ind. Ins. Co. (In re Johns-Manville Corp.*), 600 F.3d 135, 153-154 (2d Cir. 2010) (holding that a bankruptcy court did not have in rem jurisdiction over a third party's direct claims against a non-debtor insurer); accord *In re Dreier LLP*, 429 B.R. 112, 132 (Bankr. S.D.N.Y. 2010) (court lacks subject matter jurisdiction to enjoin claims that do not affect the property of the estate or the administration of the estate); *see also In re Tronox Inc.,* 855 F.3d 84, 101 n.22 (2d Cir. 2017) ("[A] bankruptcy court is without jurisdiction to enjoin claims against nondebtors that are not derivative of the debtor's wrongdoing."); *see also In re Metcalfe & Mansfield Alternative Invs*., 421 B.R. 685, 695 (Bankr. S.D.N.Y. 2010).

Accordingly, the bankruptcy court may lack both constitutional authority and statutory jurisdiction to bind Windstream's creditors and shareholders under Section 1141, or any other bankruptcy provision, to the Releases prescribed in the Plan.

CONCLUSION

For all of the foregoing reasons, the SEC requests that the Court deny approval of the Disclosure Statement and confirmation of the Plan unless the Plan is amended to provide: (i) that either (a) the Releases are deleted from the Plan or (b) that the holders of interests in Windstream and claims of impaired classes be required to "opt in" to the Releases in order to be bound and that the Releases should be amended to include a carve-out for gross negligence, willful misconduct or fraud; and (ii) that the exculpation clause be narrowly tailored to cover only estate fiduciaries and to exclude prepetition conduct.

Dated: New York, New York
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

By: /s/ Alan S. Maza
Alan S. Maza
Senior Bankruptcy Counsel
New York Regional Office
200 Vesey St., Suite 400
New York, New York 10281
Phone: (212) 336-1100
Fax: (212) 336-1348
Mazaa@sec.gov

Of Counsel: Alistaire Bambach
Morgan Bradylyons
Neal Jacobson