Docket #1560 Date Filed: 05/31/2017

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE

In re:	:	Chapter 11
PARAGON OFFSHORE PLC, *et al.*,	:	Case No. 16-10386 (CSS) Jointly Administered
Debtors.	:	Re: D.I. 1459
	:	**Hearing Date: June 7, 2017, at 10:00 a.m.** **Obj. Deadline: May 31, 2017, at 12:00 p.m.**

OBJECTION OF THE UNITED STATES TRUSTEE TO CONFIRMATION OF THE FIFTH JOINT CHAPTER 11 PLAN OF PARAGON OFFSHORE PLC AND ITS AFFILIATED DEBTORS

Andrew R. Vara, Acting United States Trustee for Region 3 (the "U.S. Trustee"), through his undersigned counsel, hereby objects to the confirmation of the Fifth Joint Chapter 11 Plan of Paragon Offshore plc and Its Affiliated Debtors (D.I. 1459) (the "Plan"), and in support of his objection respectfully states as follows:

PRELIMINARY STATEMENT

The Plan should not be confirmed for three reasons: (1) its exculpation provisions are too broad; (2) it would discharge Debtors that are liquidating; and (3) it provides for the payment of an ad hoc committee's professional fees, without a predicate showing of substantial contribution. Unless these issues are corrected or the record is properly developed, confirmation should be denied.

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JURISDICTION

1. Pursuant to 28 U.S.C. § 1334, applicable order(s) of the United States District Court for the District of Delaware issued pursuant to 28 U.S.C. § 157(a), and 28 U.S.C. § 157(b)(2)(A), this Court has jurisdiction to hear and resolve this objection.

2. Pursuant to 28 U.S.C. § 586, the U.S. Trustee is charged with monitoring the federal bankruptcy system. *See United States Trustee v. Columbia Gas Sys., Inc. (In re Columbia Gas Sys., Inc.)*, 33 F.3d 294, 295-96 (3d Cir. 1994) (noting that 11 U.S.C. § 307 gives the U.S. Trustee "public interest standing"); *Morgenstern v. Revco D.S., Inc. (In re Revco D.S., Inc.)*, 898 F.2d 498, 500 (6th Cir. 1990) (describing the U.S. Trustee as a "watchdog").

3. The U.S. Trustee has standing to be heard on the Plan pursuant to 11 U.S.C. § 307.

BACKGROUND

4. On February 14, 2016, the above-captioned debtors (the "Debtors") filed chapter 11 petitions in this Court.

5. On March 29, 2016, an ad hoc committee of noteholders filed its Rule 2019 statement. *See* D.I. 196. The Rule 2019 statement discloses that the ad hoc committee of noteholders had five members, including Arosa Capital Management LP and Loomis Sayles & Company, L.P., and were represented by Paul, Weiss, Rifkind, Wharton & Garrison LLP ("Paul Weiss") and Young Conaway Stargatt & Taylor, LLP ("Young Conaway"). *See id.* The ad hoc committee filed subsequent supplements to its Rule 2019 statement. *See* D.I. 453 & 745.

6. On January 27, 2017, the U.S. Trustee appointed an official committee of unsecured creditors (the "Committee"). *See* D.I. 1059. The Committee was comprised of

Arosa Capital Management, L.P.; Loomis Sayles & Company, L.P.; and Angelo Gordon & Co, LP.

7. As of January 27, 2017, the ad hoc committee of noteholders ceased to exist, and counsel filed a notice of withdrawal of appearance a few days later. *See* D.I 1082.

8. On February 21, 2017, the Committee filed applications to retain Paul Weiss and Young Conaway. *See* D.I. 1141 & 1142. The applications include copies of proofs of claim that the firms filed for services rendered to the ad hoc committee of noteholders from the petition date through the date the Committee was appointed. Paul Weiss' proof of claim is for $1,596,217.56, and Young Conaway's proof of claim is for $299,408.44. *See* D.I. 1141 at Sch. 3 and D.I. 1142 at Exh. 2.

9. On May 2, 2017, the Debtors filed the Plan.

10. The Plan defines "Exculpated Parties" to mean:

> collectively, and in each case in their capacities as such: (a) the Debtors; (b) the Disbursing Agent; (c) the U.K. Administrators; (d) Deloitte; (e) the Creditors' Committee; (f) the Professional Persons; and (g) with respect to clauses (a) through (e), such entities' predecessors (other than the Non-Released Parties), professionals, successors, assigns, subsidiaries, affiliates, managed accounts and funds, current and former officers and directors (other than the Non-Released Parties), principals, shareholders, members, partners, managers, employees, subcontractors, agents, advisory board members, financial advisors, attorneys, accountants, investment bankers, consultants, representatives, management companies, fund advisors, and other professionals, and such entities' respective heirs, executors, estates, servants, and nominees, in each case in their capacity as such.

Plan at 6.

11. Article 10.7 of the Plan would exculpate the Exculpated Parties.

12. The Plan defines "Noteholders' Professional Fees" to mean:

> the reasonable and documented fees and expenses incurred by Paul, Weiss, Rifkind, Wharton & Garrison LLP, Young Conaway Stargatt & Taylor, LLP, and Ducera Partners LLC in their capacities as counsel and financial advisors, respectively, to an ad hoc group of Senior Noteholders as provided in that certain Plan Support Agreement (including all exhibits thereto), dated as of February 12, 2016, by and among the Debtors and the Consenting Creditors (as defined in the agreement).

Plan at 10.

13. Article 4.4(a) of the Plan provides that holders of class 4 claims would receive their pro rata share of "(ii) payment in full of the Noteholders' Professional Fees, *provided*, that the Noteholders' Professional Fees paid to Ducera Partners LLC shall be net of any and all fees and expenses paid to Ducera Partners LLC pursuant to the *Application for Order Authorizing the Employment and Retention of Ducera Partners LLC as Financial Advisor to the Official Committee of Unsecured Creditors of Paragon Offshore plc, et al., Nunc Pro Tunc to January 20, 2017* (Docket No. 1192); . . . ."

14. The payment of the Noteholders' Professional Fees as part of the treatment of class 4 claims was added to the pre-solicitation version of the Plan, dated May 2, 2017. *See* D.I. 1447.

15. Article 5.13(c) of the Plan provides:

> Following the Effective Date, each Liquidating Subsidiary shall be liquidated and dissolved in accordance with the applicable laws of the respective jurisdictions in which they are incorporated or organized (the "**Liquidating Subsidiary Wind-Down**"). The U.K. Administrators shall co-ordinate the Liquidating Subsidiary Wind-Down in accordance with their duties to the creditors of Paragon Parent under English law. If the liquidation or winding down of Paragon Parent results in the realization of any residual proceeds available for distribution to creditors of Paragon Parent then such residual proceeds shall be distributed to Reorganized Paragon and/or certain Transferred Subsidiaries pursuant to the terms of the U.K. Implementation Agreement.

16. The Plan defines "Liquidating Subsidiary" by referencing the defined term "Liquidating Debtor." *See* Plan at 8. "Liquidating Debtor" is defined to include more than half of the Debtors: "Paragon Parent, Paragon Offshore Finance Company, Paragon Holding SCS 2 Ltd., Paragon Offshore do Brasil Ltda., Paragon FDR Holdings Ltd., Paragon Asset (ME) Ltd., Paragon Offshore (Luxembourg) S.à r.l., Paragon Duchess Ltd., Paragon Offshore International Ltd., Paragon Leonard Jones LLC, Paragon Holding NCS 2 S.à r.l., Paragon Offshore Contracting GmbH, Paragon Holding SCS 1 Ltd., Paragon Drilling Services 7 LLC, and Paragon Offshore Leasing (Luxembourg) S.à r.l. (as such list may be further amended in the U.K. Implementation Agreement)." *Id.*

17. Article 10.3 of the Plan provides:

> Upon the Effective Date and in consideration of the distributions to be made under this Plan, except as otherwise provided in this Plan or in the Confirmation Order, each holder (as well as any trustee or agent on behalf of such holder) of a Claim or Interest and any successor, assign, and affiliate of such holder shall be deemed to have forever waived, released, and discharged the Debtors, to the fullest extent permitted by section 1141 of the Bankruptcy Code, of and from any and all Claims, Interests, rights, and liabilities that arose prior to the Effective Date. Except as otherwise provided in this Plan, upon the Effective Date, all such holders of Claims and Interests and their successors, assigns, and affiliates shall be forever precluded and enjoined, pursuant to sections 105, 524, and 1141 of the Bankruptcy Code, from prosecuting or asserting any such discharged Claim against or terminated Interest in any Debtor or any Reorganized Debtor.

ARGUMENT

A. Exculpation Is Too Broad

18. The definition of "Exculpated Parties" is too broad because it includes entities that are not estate fiduciaries. Exculpation "must be limited to the fiduciaries who have served during the chapter 11 proceeding: estate professionals, the Committees and their members, and the Debtors' directors and officers." *In re Washington Mutual, Inc.*, 442 B.R.

314, 350-51 (Bankr. D. Del. 2011). *See also In re Tribune Co.*, 464 B.R. 126, 189 (Bankr. D. Del. 2011) (same); *In re PWS Holding Corp.*, 228 F.3d 224, 246 (3d Cir. 2000) (Section 1103(c) "limits the liability of a committee to willful misconduct or *ultra vires* acts."); *In re PTL Holdings LLC*, 2011 WL 5509031 at *11-12 (Bankr. D. Del. 2011) (BLS) (exculpation "must be reeled in to include only those parties who have acted as estate fiduciaries and their professionals."); *In re Indianapolis Downs, LLC*, 486 B.R. 286, 306 (Bankr. D. Del. 2013) (exculpation "limited so as to apply only to estate fiduciaries" was consistent with applicable law).

19. The Plan's definition of "Exculpated Parties" goes beyond estate fiduciaries and would give protection to, for example, the Debtors' non-debtor affiliates, and directors and officers who served pre-petition. The U.S. Trustee respectfully submits that the definition of Exculpated Parties should be amended to provide:

> collectively, and in each case in their capacities as such: (a) the Debtors; (b) the Disbursing Agent; (c) the U.K. Administrators; ~~(d) Deloitte;~~ (e) the Creditors' Committee; (f) the Professional Persons; and (g) with respect to clauses (a) through (e), such entities' ~~predecessors (other than the Non-Released Parties), professionals, successors, assigns, subsidiaries, affiliates, managed accounts and funds,~~ current ~~and former~~ officers and directors (other than the Non-Released Parties), principals, ~~shareholders~~, members, partners, and managers, ~~employees, subcontractors, agents, advisory board members, financial advisors, attorneys, accountants, investment bankers, consultants, representatives, management companies, fund advisors, and other professionals, and such entities' respective heirs, executors, estates, servants, and nominees,~~ in each case in their capacity as such.

B. Liquidating Debtors' Eligibility for Discharge Not Established

20. The Plan provides for the liquidation of more than half of the Debtors. *See* Plan at 8 (defining "Liquidating Subsidiary" to include 15 of the 26 Debtors) and Article 5.13(c) ("Following the Effective Date, each Liquidating Subsidiary shall be liquidated and dissolved in accordance with the applicable laws of the respective jurisdictions in which they are incorporated or organized . . . ."). However, Article 10.3 of the Plan would give all of the Debtors, including the Liquidating Subsidiaries, a discharge.

21. The Debtors have not demonstrated that discharging the Liquidating Subsidiaries is permissible under Section 1141(d)(3). Section 1141(d)(3) of the Bankruptcy Code provides:

> The confirmation of a plan does not discharge a debtor if—
>
> (A) the plan provides for the liquidation of all or substantially all of the property of the estate;
> (B) the debtor does not engage in business after consummation of the plan; and
> (C) the debtor would be denied a discharge under section 727(a) of this title if the case were a case under chapter 7 of this title.

The U.S. Trustee has requested more information from the Debtors about the Liquidating Subsidiaries' assets and business operations after Plan consummation. Unless the Debtors demonstrate that all or substantially all of the Liquidating Subsidiaries' assets will not be liquidated under the Plan, and that the Liquidating Subsidiaries will engage in business after the Plan has been consummated, then the Liquidating Subsidiaries should not receive a discharge, pursuant to Section 1141(d)(3).[1]

[1] Section 1141(d)(3)(C) will be satisfied because the Debtors are corporations and as such would not be eligible for a discharge if they were chapter 7 debtors, pursuant to Section 727(a)(1). *See*,

C. Fees of Unofficial Noteholders' Committee Should Not Be Paid in Full Absent Showing of Substantial Contribution

22. Article 4.4(a) of the Plan would provide for payment of the fees and expenses incurred by Paul Weiss, Young Conaway, and Ducera Partners LLC in their capacities as counsel and financial advisors, respectively, to an ad hoc group of Senior Noteholders as provided in a plan support agreement that was filed earlier in these cases.

23. The standard applicable to the payment of an ad hoc committee's attorney and accountant fees and expenses is set forth in Section 503(b) of the Bankruptcy Code.[2] *See Davis v. Elliot Mgmt. Corp*. (*In re Lehman Bros. Holdings Inc*.), 508 B.R. 283, 290 (S.D.N.Y. 2014) (Section 503(b) is the exclusive avenue for payment of administrative expenses).

24. Section 503(b) of the Bankruptcy Code provides:

> After notice and a hearing, there shall be allowed administrative expenses, other than claims allowed under section 502(f) of this title, including—
>
> (3) the actual, necessary expenses, other than compensation and reimbursement specified in paragraph (4) of this subsection, incurred by . . .
>
> (D) a creditor, an indenture trustee, an equity security holder, or a committee representing creditors or equity security holders other than a committee appointed under section 1102 of this title, in making a substantial contribution in a case under chapter 9 or 11 of this title;
>
> (4) reasonable compensation for professional services rendered by an attorney or an accountant of an entity whose expense is allowable under subparagraph (A), (B), (C), (D), or (E) of paragraph (3) of this subsection, based on the time, the nature, the extent, and the value of such services, and the cost of comparable services other than in a case under this title, and reimbursement for actual, necessary expenses incurred by such attorney or accountant;

11 U.S.C. §§ 503(b)(3)(d) and 503(b)(4).

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e.g., *In re Flintkote Co.*, 486 B.R. 99, 129 n.80 (Bankr. D. Del. 2012)("Section 1141(d)(3)(C) is always satisfied for corporate debtors, as they cannot receive discharges in chapter 7.").

[2] As unsecured creditors, the noteholders are not entitled to the allowance or payment of their postpetition professional fees and expenses under Section 506(b).

25. Pursuant to Section 503(b), a party's right to payment is not automatic but "depends upon the requesting party's ability to show that the fees were actually necessary to preserve the value of the estate." *Calpine Corp. v. O'Brien Envtl. Energy, Inc.* (*In re O'Brien Envtl. Energy, Inc*.), 181 F.3d 527, 535 (3d Cir. 1999). A party must show it made a substantial contribution under Section 503(b)(3) as a prerequisite to getting attorney fees under section 503(b)(4). *See In re RS Legacy Corp.*, No. 15-10197, 2016 WL 1084400, at *3 (Bankr. D. Del. Mar. 17, 2016). The party's acts are analyzed in hindsight with particular scrutiny upon the actual benefits provided to the entire bankruptcy case. *See In re Worldwide Direct, Inc*., 334 B.R. 112, 121 (Bankr. D. Del. 2005).

26. A creditor makes a substantial contribution if its efforts provide an "actual and demonstrable benefit to the debtor's estate and the creditors." *Lebron v. Mechem Financial Inc.*, 27 F.3d at 943-44 (citation omitted) (quoting *In re Lister*, 846 F.2d 55, 57 (10th Cir. 1988)). *See also In re Worldwide Direct, Inc.*, 334 B.R. at 121.

27. A benefit that the estate receives as an incident to a creditor's protecting its own interests is not substantial. *See Lebron v. Mechem Financial Inc*., 27 F.3d at 944.

28. Creditors are presumed to act in their own interest "until they satisfy the court that their efforts have transcended self-protection." *Lebron v. Mechem Financial Inc.*, F.3d 937, 944 (3d Cir. 1994) (citations omitted). The activities that a Section 503(b)(3)(D) applicant has engaged in are "presumed to be incurred for the benefit of the engaging party and are reimbursable if, but only if, the services 'directly and materially contributed' to the reorganization." *Lebron v. Mechem Financial Inc.*, 27 F.3d at 943-44 (citation omitted).

29. Applicants must prove by a preponderance of the evidence that they made a substantial contribution. *See In re Buckhead America Corp.*, 161 B.R. 11, 15 (Bankr. D. Del.

1993). When determining if an applicant has met its burden, courts consider whether the services provided—

1) were only for the benefit of the client or were for the benefit of all parties in the case;
2) directly, significantly and demonstrably benefited the estate; and
3) were duplicative of the services provided by attorneys for the committee, the committees themselves, or the debtor and its attorneys.

See In re Worldwide Direct, Inc., 334 B.R. at 122 (citing *In re Buckhead America Corp.*, 161 B.R. at 15).

30. Extensive participation in a case is not enough to justify a substantial-contribution award. *See In re Worldwide Direct, Inc.*, 334 B.R. at 123 (citing *In re Granite Partners*, 213 B.R. at 445); *see also In re Summit Metals, Inc.*, 379 B.R. at 53.

31. A substantial contribution applicant has the burden of establishing that a "causal connection" exists between service provided and contribution to the estate. *See In re Worldwide Direct, Inc.*, 334 B.R. at 121-22.

32. The plan proponents have not demonstrated that the ad hoc noteholders' committee made a substantial contribution in these cases. It is not apparent that the ad hoc noteholders' committee did anything beyond seeking to protect its own interests. The plan support agreement to which the ad hoc noteholders' committee was a party was not approved by the Court or performed. *See* D.I. 794. Further, a global plan resolution was not reached until months after the ad hoc noteholders' committee had ceased to exist. *See* D.I. 1082. Unless the plan proponents demonstrate that the ad hoc noteholders' committee made a substantial contribution in these cases, the payment of the Noteholders' Professional Fees should be denied. *See In re Lehman Bros. Holdings Inc.*, 508 B.R. at 288-294 (administrative

expenses are post-petition expenses that receive special treatment of payment priority and incentivize certain parties to take on difficult work that benefits estate as a whole. "A plan provision cannot short-circuit the process by effectively deeming an entity to have made a substantial contribution." *Id.* at 294).

33. Assuming *arguendo* that the Noteholders' Professional Fees could be evaluated and paid as a general unsecured claim, then the plan proponents would need to demonstrate why a recovery on Noteholders' Professional Fees claims of 100% is fair, when other general unsecured creditors are receiving projected recoveries in the range of 30-35%, and shareholders are receiving nothing.

CONCLUSION

34. The U.S. Trustee reserves any and all rights, remedies and obligations to complement, supplement, augment, alter and/or modify this objection, file an appropriate motion or conduct any and all discovery as may be deemed necessary or as may be required, and to assert such other grounds as may become apparent upon further factual discovery.

WHEREFORE, the U.S. Trustee respectfully requests that the Court deny confirmation of the Plan unless (1) the definition of "Exculpated Parties" is limited to estate fiduciaries; (2) the Debtors demonstrate that the Liquidating Subsidiaries are eligible for a discharge; and (3) the payment of Noteholders' Professional Fees is conditioned on a showing that those entities made a substantial contribution under Section 503(b)(3)(D).

Dated: May 31, 2017
Wilmington, DE

Respectfully submitted,

ANDREW R. VARA
ACTING UNITED STATES TRUSTEE,
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By: */s/ Benjamin Hackman*

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