



KTBS Law Case Alert by Sasha M. Gurvitz: *In re Paragon Offshore, PLC*, Case No.: 16-10386 (Bankr. D. Del. June 28, 2021)

On June 28, 2021 Chief Judge Christopher S. Sontchi of the Delaware Bankruptcy Court issued a decision rejecting the imposition of U.S. Trustee fees in connection with distributions made by a post-confirmation litigation trust in *In re Paragon Offshore, PLC*.

In the *Paragon* case, as in so many other chapter 11 cases, the debtors confirmed a plan establishing a litigation trust to pursue claims against third parties and make distributions to creditors, who, under the plan, received interests in the litigation trust in satisfaction of their claims against the debtors. The debtors' plan provided that the causes of action transferred to the trust would be transferred "fee and clear," and thereafter the debtors disclaimed any interest in or with respect to any of the trust assets—including those assigned causes of action.



When the debtors initially transferred their assets to the trust, the debtors paid U.S. Trustee fees in accordance with 28 U.S.C. § 1930(a)(6)(A), which provides that in each case under Chapter 11 (other than a Subchapter V case), a quarterly fee shall be paid to the U.S. Trustee until such case is converted or dismissed, whichever occurs first. The amount of the fee is tied to the amount of "disbursements" made by the debtor. Accordingly, for the quarter in which the debtors first disbursed the assets to the litigation trust, the debtors paid the corresponding fee to the U.S. Trustee (notably, the fee was in the maximum amount set forth under the statute at that time, based on the significant dollar value of the assets disbursed to the trust).

Years later, the trust recovered and distributed to the holders of the litigation trust interests the proceeds of certain causes of action that had been assigned to the trust by the debtors. The U.S. Trustee filed a motion to compel the debtors and the trust to pay quarterly fees to the U.S. Trustee in connection with the disbursement to the trust's beneficiaries of the proceeds of the litigation. Judge Sontchi denied the U.S. Trustee's motion, on the basis that section 1930 provides only for the payment of quarterly fees in connection with "disbursements." Surveying the case law, Judge Sontchi interpreted the term "disbursements" in this context to refer to payments made with funds generated by the liquidation of the *debtor's* assets or payments made by or on behalf of the *debtor*, and noted that the common thread among the cases was that the *debtor* had some interest in or control over the funds disbursed. By contrast, the litigation proceeds disbursed in this case were derived from assets of the *trust*, assets in which the debtors had expressly disclaimed any interest whatsoever, and the distributions were made by or on behalf of the *trust*. In further support of his conclusion, Judge Sontchi cited language in the confirmed plan and the litigation trust agreement that made clear that the trust assets belonged to the trust, not the debtors, and that the trust was solely responsible for making distributions from such assets on behalf of the trust to the holders of litigation trust interests on account of those interests.



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Moreover, Judge Sontchi noted that the U.S. Trustee had already received payment of quarterly fees on account of these assets when the debtors initially transferred those causes of action to the litigation trust, and explained that he viewed the U.S. Trustee's motion as an attempt to impose a second tax on the same assets. The Court emphasized in a footnote, "I cannot stress enough how offensive I find the OUST's attempt to double, or triple collect its 'tax.' ... What is reprehensible is attempting to take money out of the pockets of creditors, which are already receiving a small recovery on their claims, multiple times for the same distribution." As such, Judge Sontchi concluded, "the notion that the Trust's 'final distribution to Litigation Trust Beneficiaries on account of their Litigation Trusts Interests' is, in fact, a 'disbursement' on behalf of the Debtors cannot be squared with the law, the Plan, nor the Litigation Trust Agreement," and thus the Court denied the U.S. Trustee's motion for imposition of the statutory fee.

Judge Sontchi's decision provides bankruptcy practitioners (at least in Delaware cases) with a useful roadmap for strengthening the argument that distributions from a post-confirmation trust should not constitute disbursements for purposes of imposition of the U.S. Trustee's quarterly fees. Among other things, practitioners can attempt to clarify in the relevant documents that trust assets should be considered property of the trust, with no residual interest held by the debtors, and that distributions from the trust are distributions to creditors by or on behalf of the trust on account of the creditors' interests in the trust. The decision is a positive development for creditors, as the double counting of U.S. Trustee fees, first upon funding of the trust and again upon distribution, can otherwise erode creditor recoveries.

For more information, or to speak with the author of this alert, please contact Sasha Gurvitz at 310-407-4032 or sgurvitz@ktbslaw.com.

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