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Delaware Bankruptcy Court Rebuffs U.S. Trustee Effort to Collect Statutory Fees from Litigation Trust Distributions

On June 28, 2021, in the chapter 11 cases of Paragon Offshore plc and certain of its affiliates (“Paragon” or the “Debtors”), the United States Bankruptcy Court for the District of Delaware denied the U.S. Trustee’s motion¹ to compel payment of \$250,000 in statutory fees assessed against litigation trust distributions. In its opinion, the Bankruptcy Court concluded that the U.S. Trustee had already collected all statutory fees due: first, when Paragon transferred its litigation claims to the litigation trust (the “Trust”) under its plan, and second, when the defendant in the Trust litigation, itself a chapter 11 debtor, later paid statutory fees in its own chapter 11 case based on, among other things, the cash settlement payment it made to the Trust. Finding the U.S. Trustee’s “attempt to double, or triple collect” the statutory fees “offensive,” the Bankruptcy Court held that the Trust’s payments of settlement proceeds to its beneficiaries were not “disbursements” made by or on behalf of the Debtors within the meaning of the U.S. Trustee fee statute, and as a result, that no such fees were payable.

Background

Congress intended that users of the bankruptcy system, rather than taxpayers, fund the U.S. Trustee program.² Section 1930(a)(6) of title 28 (the “Fee Statute”), accordingly, requires the payment of quarterly fees to the U.S. Trustee on “disbursements” made in bankruptcy cases.³ At issue in *Paragon* was whether payments made by a litigation trust created under a chapter 11 plan were “disbursements” within the meaning of the Fee Statute, thereby triggering the statutory fees.

On February 14, 2016, Paragon, an offshore drilling services company, filed for chapter 11 along with certain affiliates. Its chapter 11 plan (the “Plan”), which the Bankruptcy Court confirmed in June 2017, created the Trust to pursue certain litigation claims against Noble Corporation plc (“Noble”) and others related to Noble’s spin-off of Paragon in 2014 (the “Noble Claims”).⁴ The Trust assets consisted of all cash, proceeds, and other property received in connection with the prosecution, settlement or compromise of the Noble Claims.⁵ The Trust’s beneficiaries were former creditors of Paragon, who received their Trust interests pursuant to the Plan.⁶ Upon its transfer of assets to the Trust, Paragon ceased to have any interest in the Noble Claims. Paragon

¹ *In re Paragon Offshore*, Case No. 16-10386 (Bankr. D. Del. Jun. 28, 2021) [ECF No. 2257-1] (“Opinion”).

² H.R. REP. NO. 99-764 at 25 (1986), reprinted in 1986 U.S.C.A.N. 5227, 5238; *United States Trustee v. Gryphon at the Stone Mansion, Inc.*, 166 F.3d 552, 554 (3d Cir. 1999) (“Historically, § 1930(a)(6) set forth a scheme to impose the costs of the United States Trustee Program on its users.”)

³ 28 U.S.C. § 1930(a)(6).

⁴ Case No. 16-10386 (Bankr. D. Del. May 27, 2021) [ECF No. 2239] at 3 (“Trust Reply”).

⁵ *Id.* at 10.

⁶ *Id.* at 9.

paid to the U.S. Trustee the maximum statutory fees payable on disbursements for the quarter in which it distributed assets to the Trust.⁷

The Trust filed a complaint against Noble and others in December 2017.⁸ The parties engaged in active negotiations, and the Trust ultimately settled its claims against Noble for approximately \$90 million, including \$7.7 million from Noble.⁹ Like Paragon before it, Noble (which was a debtor in its own bankruptcy)¹⁰ paid the maximum fees on disbursements to the U.S. Trustee for the quarter in which it distributed assets to the Trust.¹¹

Following the Bankruptcy Court's approval of the Noble settlement, the U.S. Trustee moved to compel payment of quarterly fees on the Trust's distribution of the settlement proceeds to its beneficiaries. The U.S. Trustee argued that the Trust's distributions of the Noble settlement proceeds were Plan payments, that Plan payments were "disbursements" within the meaning of the Fee Statute, and that as a result, quarterly fees were due under the Plan and applicable law.¹² The U.S. Trustee urged the Bankruptcy Court to interpret the term "disbursements" broadly, arguing that Congress's failure to define the term intentionally placed no limitation on the source of "disbursements" made in a case, and that essentially all payments to third parties directly attributable to the existence of the bankruptcy case qualified.¹³

In response, the Trust argued that permitting fees on the Trust's disbursements would be the U.S. Trustee's third bite at the proverbial fee apple, and was inappropriate for multiple reasons.¹⁴ First, the Trust's payment of settlement proceeds was not a "disbursement" within the meaning of the statute because it was made by the Trust to its beneficiaries, and therefore, was not a payment "by or on behalf of the debtor" as the statute required. The Trust also argued that the Fee Statute does not impose liability for statutory U.S. Trustee fees on litigation trusts, and noted that the U.S. Trustee failed to cite a single case in which a court had imposed such fees on a litigation trust.¹⁵

Finding the U.S. Trustee's Attempts to "Double, or Triple Collect" its Fees "Offensive," the Bankruptcy Court Denies U.S. Trustee's Motion

The Bankruptcy Court recognized that the Fee Statute does not define the term "disbursements," but noted that courts have defined the term to mean "all payments by or on behalf the debtor," and that the word is commonly understood to mean payments made with funds generated from the liquidation of the debtor's assets.¹⁶

The Bankruptcy Court rejected the U.S. Trustee's position that "disbursements" should be so broadly interpreted as to include every payment made by or on behalf of a debtor, for any reason. Instead, it found that a "debtor [must have] had some interest in, or control over, the money disbursed" to trigger U.S. Trustee fees.¹⁷ Under this standard, the Bankruptcy Court held that the Trust's distributions of settlement proceeds to its beneficiaries were not payments on behalf of Paragon because, on the

⁷ Opinion at 3.

⁸ *Id.*

⁹ Trust Reply at 4.

¹⁰ *In re Noble Corporation plc*, No. 20-33836 (Bankr. S.D. Tex. July 31, 2020).

¹¹ *Id.* at 5.

¹² Case No. 16-10386 (Bankr. D. Del. June 4, 2021) [ECF No. 2244] at 1.

¹³ Case No. 16-10386 (Bankr. D. Del. May 12, 2021) [ECF No. 2231] at 11.

¹⁴ Trust Reply at 1.

¹⁵ *Id.* at 2.

¹⁶ Opinion at 4.

¹⁷ *Id.*

effective date of the Plan, Paragon transferred its ownership of the Noble Claims to the Trust in consideration for certain creditor releases. The Bankruptcy Court found that this transfer, which occurred in 2017, was the relevant “payment” made “by or on behalf of the Debtors” for purposes of the Fee Statute. Notably, the U.S. Trustee received its quarterly fees in connection with the disbursement at that time. The Trust’s payment of settlement proceeds to its beneficiaries—four years later—were by the Trust to its beneficial interest holders, and as such, were simply not payments by or on behalf of the Debtors.¹⁸

Conclusion

The Bankruptcy Court’s denial of the U.S. Trustee’s attempt to collect statutory fees from a plan-created litigation trust provides one clear demarcation of the type of payments that are not “disbursements” triggering U.S. Trustee fees in bankruptcy. Whether the U.S. Trustee will make similar attempts to collect statutory fees from what it considers plan-related distribution structures remains to be seen.

¹⁸ *Id.* at 6.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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