UNITED STATES BANKRUPTCY COURT
DISTRICT OF DELAWARE

In re	:	Chapter 11
	:	Case No.: 16-10386 (CSS)
PARAGON OFFSHORE PLC, *et al.*,	:	
	:	Jointly Administered
Debtors.	:	
	:	Related Docket No. 644

FINDINGS OF FACT AND CONCLUSIONS OF LAW DENYING CONFIRMATION OF THE AMENDED JOINT CHAPTER 11 PLAN OF PARAGON OFFSHORE PLC AND ITS AFFILIATED DEBTORS

As set forth in the Court's oral ruling on October 28, 2016, the question before the Court is simple - is the Debtors' plan feasible? It is not. Based upon the evidence before the Court, the Debtors' business plan, even under its Downside Sensitivity[1] analysis, is based upon unrealistic assumptions as to rig utilization and day rates and, thus, is not reasonable. Under the Debtors' proposed Modified Plan, the Debtors will either run out of cash altogether or, at best, breach their financial covenants under the reorganized debt – even though those covenants are lower than under the Original Plan. In addition, the Debtors have failed to establish that they will be able to refinance their debt when they meet their maturity wall in 2021.

[1] Capitalized terms shall have the meaning ascribed to them *infra*.

That is not to say the Debtors cannot reorganize. Indeed, the Debtors can and should be able to do so. It is also not to say that the Term Lenders' debt cannot be reinstated. It may, provided the Debtors can establish that the debt can be paid or refinanced at maturity, which is less than clear even if the Modified Plan is otherwise feasible. The main problem is that the Modified Plan, which is an improvement over the initial plan, still siphons $450 million in cash out of the estate, which is at least $150 to $200 million too much. That cash is needed for the Reorganized Debtors to be able to survive the challenging business environment of off-shore oil and gas production over the next several years and to be reasonably able to refinance their debt in 2021.

The Term Lenders make several arguments in opposition to the Modified Plan's feasibility. As noted, the Court finds that the arguments as to unreasonable rig utilization and day rates are valid. However, the Court rejects the argument that the Debtors' Modified Plan is not feasible because it underestimates future capital expenditures. The evidence supports management's estimates as to future capital expenditures as reasonable. In addition, the Court rejects the argument that the Modified Plan is not feasible as a matter of law because the Debtors would be balance sheet insolvent upon emergence. Balance sheet insolvency does not, *per se*, render a plan not feasible. Neither does balance sheet solvency guarantee feasibility. Whether a debtor is or is not balance sheet solvent upon emergence is a relevant but not controlling factor to consider in determining feasibility. In this case, the Term Lenders presented expert evidence that the Debtors will be balance sheet insolvent upon emergence, which the Debtors attempted to refute. This Court need not consider the merits of that evidence. Assuming, *arguendo*, that the Debtors would be balance sheet solvent upon emergence, the Modified Plan is nonetheless not feasible because the Business Plan is not reasonable and the Debtors will not be able to refinance their debt in 2021.

At the end of the day, these cases are all about liquidity. The Debtors' Modified Plan robs the businesses of too much cash and does not preserve sufficient liquidity to meet the challenges of the next several years. These businesses can and should reorganize and recover but not under the Modified Plan. Thus, the Court will deny confirmation for the reasons set forth herein.

I. INTRODUCTION AND PROCEDURAL HISTORY

1. On February 14, 2016 (the "**Petition Date**"), each Debtor commenced with the Bankruptcy Court a voluntary case under chapter 11 of the Bankruptcy Code (the "**Chapter 11 Cases**"). The Debtors are authorized to continue to operate their businesses and manage their properties as debtors in possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code.

2. No trustee or examiner has been appointed pursuant to section 1104 of the Bankruptcy Code. No statutory committee of unsecured creditors has been appointed pursuant to section 1102 of the Bankruptcy Code. Further, in accordance with an order of the Bankruptcy Court, the Debtors' cases are being jointly administered pursuant to Bankruptcy Rule 1015(b).[2]

[2] *Order Directing Joint Administration of Chapter 11 Cases Pursuant to Bankruptcy Rule 1015(b)* (Docket No. 69).

3. On April 19, 2016, the Debtors filed the *Second Amended Joint Chapter 11 Plan of Paragon Offshore plc and its Affiliated Debtors*, dated April 19, 2019 (Docket No. 318) (the "**Original Plan**") and *Disclosure Statement for Second Amended Joint Chapter 11 Plan of Paragon Offshore plc and its Affiliated Debtors*, dated April 19, 2016 (Docket No. 319) (the "**Disclosure Statement**"). On April 4, 2016, the Court entered an order approving the Disclosure Statement.[3]

4. Pursuant to the Original Plan, only holders of Claims in Class 3 (Revolving Credit Agreement Claims) and Class 5 (Senior Notes Claims) (together, the "**Voting Classes**") were entitled to vote. Holders of Claims in Class 1 (Priority Non-Tax Claims), Class 2 (Other Secured Claims), Class 4 (Secured Term Loan Claims), Class 6 (General Unsecured Claims), Class 7 (Intercompany Claims), Class 8 (Parent Interests), and Class 9 (Intercompany Interests) are unimpaired and, accordingly, are conclusively presumed to accept the Original Plan and are not entitled to vote on account of such Claims and Interests.

5. As set forth in the *Certification of James Lee with Respect to the Tabulation of Votes on Second Amended Joint Chapter 11 Plan of Paragon Offshore plc and its Affiliated Debtors* (Docket No. 433) (the "**Original Voting Certification**"), nearly 100 percent of the creditors in each of the Voting Classes voted to accept the Original Plan.

[3] *Order (I) Approving Proposed Disclosure Statement and Form and Manner of Notice of Disclosure Statement Hearing, (II) Establishing Solicitation and Voting Procedures, (III) Scheduling Confirmation Hearing and (IV) Establishing Notice and Objection Procedures for Confirmation of the Proposed Plan Pursuant to Sections 105, 502, 1125, 1126, and 1128 of the Bankruptcy Code and Bankruptcy Rules 2002, 3003, 3017, 3018, 3020, and 9006 and Local Rules 2002-1, 3017-1, and 9006-1* (Docket No. 248).

6. The following objections to confirmation of the Original Plan were filed: (i) *Alief Independent School District and Fort Bend Independent School District's Limited Objection to Confirmation of Second Amended Joint Chapter 11 Plan of Paragon Offshore plc and its Affiliated Debtors* (Docket No. 428) (the "**Texas Taxing Entities Objection**"), (ii) *Objection by the Internal Revenue Service to the Second Amended Joint Chapter 11 Plan of Paragon Offshore plc and its Affiliated Debtors* (Docket No. 429) (the "**IRS Objection**"), (iii) *Objection of Cypress-Fairbanks Independent School District, Fort Bend County, and Harris County to Debtors Second Amended Joint Chapter 11 Plan of Paragon Offshore plc and Its Affiliated Debtors* (Docket No. 430) (the "**Texas Taxing Authorities Objection**"), and (iv) *Objection of the Secured Term Loan Agent, on Behalf of the Secured Term Loan Lenders, to Confirmation of the Second Amended Joint Chapter 11 Plan of Paragon Offshore plc and its Affiliated Debtors* (Docket No. 438) (the "**Original Term Loan Agent Objection**"). The Texas Taxing Entities Objection, the IRS Objection, and the Texas Taxing Authorities Objection were resolved on the terms and conditions described on the record of the Initial Confirmation Hearing (as defined below).

7. On June 14, 2016, the Debtors filed: (i) the *Memorandum of Law in Support of Confirmation of Debtors' Second Amended Joint Chapter 11 Plan and Response to Certain Objections* (Docket No. 467) (the "**Original Confirmation Brief**"), and (ii) the *Declaration of Thomas B. Osmun in Support of Confirmation of Debtors' Second Amended Joint Chapter 11 Plan of Paragon Offshore plc and its Affiliated Debtors* (Docket No. 468) (the "**Original Osmun Declaration**").

8. The Confirmation Hearing on the Original Plan commenced on June 21, 2016 and continued on June 22, 23, 29 and 30, 2016 (the "**Initial Confirmation Hearing**"). The Debtors and the Term Loan Agent, collectively, called seven (7) witnesses at the Initial Confirmation Hearing: (i) Mr. David Kurtz from Lazard, the Debtors' investment banker; (ii) Mr. Randall Stilley, Paragon's CEO and President; (iii) Mr. David Pursell from Tudor Pickering Holt & Co., as an expert witness; (iv) Mr. Doug Fordyce from Lazard, as an expert witness; (v) Mr. Steven Manz, Paragon's Chief Financial Officer; (vi) Philip Verleger, an economist as an expert witness; and (vii) Paul Leand, the CEO of AMA Capital Partners.

9. On July 8, 2016, the Court conducted a chambers conference with representatives of Cortland, the lenders holding the revolving loan debt (the "**Revolver Lenders**"), the lenders holding the unsecured bond debt (the "**Noteholders**") and the Debtors (collectively, the "**Parties**"). (D.I. 547.) At the chambers conference, the Court communicated its concerns regarding the achievability of the Business Plan (also referred to herein as the "**Base Case**") and the feasibility of the Original Plan, including with respect to the achievability of the projected dayrates and rig utilization contemplated by the Base Case.

10. On August 15, 2016, the Debtors filed the *Modified Second Amended Joint Chapter 11 Plan of Paragon Offshore plc and its Affiliated Debtors*, dated August 15, 2016 (Docket No. 644) (as supplemented by the Plan Supplement (defined below), and as

otherwise amended in accordance with the terms thereof, the "**Modified Plan**").[4] In connection with the Original Plan and the Modified Plan, the Debtors filed various plan supplement documents (Docket Nos. 399, 470, 493 and 682) (together, as may be amended, supplemented, restated or modified from time to time, the "**Plan Supplement**").

11. On August 16, 2016, the Debtors filed the *Supplement to the Disclosure Statement for the Modified Second Amended Joint Chapter 11 Plan of Paragon Offshore plc and its Affiliated Debtors* (Docket No. 657) (the "**Disclosure Statement Supplement**"). The Disclosure Statement Supplement reflects updated Business Plan projections (the "**Business Plan,**" also referred to herein as the "**Base Case**"). The Disclosure Statement Supplement also included a downside scenario with respect to the Debtors' modified base case (the "**Downside Sensitivity**") (D.I. 657 at 2-3). On August 16, 2016, the Court entered an order approving the Disclosure Statement Supplement.[5]

12. The Modified Plan differs from the Original Plan in that it includes modifications to the treatment of Revolving Credit Agreement Claims and the Senior Notes Claims. Specifically, the Amended and Restated Credit Agreement was revised to reduce the minimum liquidity requirement from $110 million to $103 million. *Supplemental Declaration of Thomas B. Osmun in Support of Confirmation of Debtors' Modified*

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[4] Capitalized terms used but not otherwise defined herein shall have the meanings ascribed to them in the Modified Plan.

[5] *Order (I) Approving Proposed Supplement to Disclosure Statement and (II) Establishing Deadlines and Procedures for Changing Votes on the Debtors' Modified Plan Pursuant to Sections 105, 1125, 1126, and 1127 of the Bankruptcy Code and Bankruptcy Rules 2002, 3017, 3018, 3019, 3020, and 9006 and Local Rules 2002-1, 3017-1, and 9006-1* (Docket No. 655) (the "**Supplemental Disclosure Statement Order**").

Second Amended Joint Chapter 11 Plan of Paragon Offshore plc and its Affiliated Debtors (Docket No. 744) (the "**Supplemental Osmun Declaration**"), ¶ 9. The Debtors have no EBITDA-based covenants until 2019 and covenants for 2019 and beyond were relaxed further. *Id.* The treatment of Senior Notes Claims was modified to: (1) reduce the cash payment to be provided to the holders of Senior Notes Claims from $345 million to $285 million; (2) remove certain contingent payments from the package of consideration to the holders of Senior Notes Claims; (3) provide for the issuance of $60 million unsecured New Notes; and, (4) increase the number of Parent Ordinary Shares to be issued to the holders of Senior Notes Claims from 35 to 47 percent. *Id.*

13. The Voting Classes in the Modified Plan were the same as the Original Plan. *See supra* ¶ 4. As demonstrated in the *Certification of James Lee with Respect to the Tabulation of Votes on the Modified Second Amended Joint Chapter 11 Plan of Paragon Offshore plc and its Affiliated Debtors* (Docket No. 734) (the "**Supplemental Voting Certification**"), nearly 100 percent of the creditors in each of the Voting Classes voted to accept the Modified Plan.

14. On September 12, 2016, the Debtors filed the *Declaration of Todd D. Strickler in Support of Approval of the Noble Settlement Agreement Pursuant to Bankruptcy Rule 9019* (PGN 239) (the "**Strickler Declaration**").

15. On September 13, 2016, the Term Loan Agent filed its Objections to confirmation of the Modified Plan (D.I. 718).

16. On September 22, 2016, the Debtors filed the *Memorandum of Law in Support of Confirmation of Debtors' Modified Second Amended Joint Chapter 11 Plan* (Docket No. 743) (the "**Modified Confirmation Brief**") and the Supplemental Osmun Declaration.

17. The confirmation hearing on the Modified Plan began on September 27, 2016 and concluded on September 30, 2016 (the "**Second Confirmation Hearing**" and, together with the Initial Confirmation Hearing, the "**Confirmation Hearings**"). The Debtors and the Term Loan Agent, collectively, called five (5) witnesses at the Second Confirmation Hearing: (i) Mr. Randall Stilley, Paragon's CEO and President; (ii) Mr. Doug Fordyce from Lazard; (iii) Philip Burke, managing director of OGC Global Contracting Limited, (iv) Daniel Fischel, the Lee and Brena Freeman Professor of Law and Business Emeritus at The University of Chicago Law School and President of Compass Lexecon; and (v) Paul Leand, the CEO of AMA Capital Partners. The Court also reviewed deposition testimony from Andrew Tietz, Paragon's senior VP of Marketing and Contracts.

18. The sole remaining objector to the Modified Plan at the Second Confirmation Hearing was the Term Loan Agent (as defined *infra*). As discussed above, all other objections to the Original Plan and Modified Plan were resolved prior to the Second Confirmation Hearing.

II. BACKGROUND

A. Paragon's Business and Management

19. The Debtors are a global provider of offshore drilling rigs. 6/21/16 Hrg. Tr. at 134:24–135:12 (Stilley Test.). They principally operate standard specification rigs, which are generally used for "development drilling" on preexisting oil and gas fields. 6/23/16 Hrg. Tr. at 91:22–93:1 (Fordyce Test.). These rigs are also used for "workover," or fixing existing wells, as well as plugging and abandoning ("**P&A**") activities. 6/23/16

Hrg. Tr. at 90:6–93:1 (Fordyce Test.). Over the past three years, approximately eighty percent of Paragon's business has consisted of development drilling, workovers, re-entry and P&A work. 9/27/16 Hrg. Tr. at 97:3–13 (Stilley Test.); 9/30/16 Hrg. Tr. at 105:24–106:12 (Leand Test.); 9/30/16 Hrg. Tr. at 128:3–129:3 (Fordyce Test.).

20. In addition to providing rigs, the Debtors also operate the rigs on behalf of customers in the oil and gas industry. 6/21/16 Hrg. Tr. at 135:7–12 (Stilley Test.). The Debtors' customers include large national and international E&P companies, midsize E&P companies and smaller independent companies. 6/21/16 Hrg. Tr. at 134:24–135:6 (Stilley Test.). The Debtors have developed and maintained longstanding relationships with their customers located in geographically diverse regions. 6/21/16 Hrg. Tr. at 135:13–25 (Stilley Test.).

21. The Debtors have over 2,000 employees and are managed by a board of directors (the "**Board**") whose members have both expertise and managerial experience in the oil and gas industry. 6/21/16 Hrg. Tr. at 134:5–11 (Stilley Test.). The Debtors' senior management team is comprised of experienced professionals who have worked in the offshore drilling industry for decades. 6/21/16 Hrg. Tr. at 133:14–134:1 (Stilley Test.). For instance, senior management includes, among others, Mr. Randall Stilley (President and CEO), with over 40 years of experience, Mr. Andrew Tietz (Senior VP of Marketing and Contracts), with 25 years of experience, and Mr. Charlie Yester (Senior VP of Operations), also with over 40 years of experience. 6/21/16 Hrg. Tr. at 133:24–134:1 (Stilley Test.); TLA 620 (9/7/16 Depo. Tr. at 9:14–14:23 (Tietz Test.)). Furthermore, Paragon has management and employees dedicated to each of the markets in which the

Debtors operate, which enhances Paragon's relationships and communications with customers in its regions. 6/21/16 Hrg. Tr. at 135:13–25, 158:17–159:5 (Stilley Test.).

B. Paragon's Assets

22. The Debtors currently own 40 offshore drilling rigs (6/21/16 Hrg. Tr. at 132:20–21 (Stilley Test.)), including 34 jackup rigs (including two high specification, harsh environment jackups (6/21/16 Hrg. Tr. at 179:7–21, 183:23–184:21, 210:1–21 (Stilley Test.)), and six floating rigs (a/k/a "floaters," including three drillships and two semisubmersibles) (6/21/16 Hrg. Tr. at 141:1–5, 210:2–3 (Stilley Test.)). The Debtors also have an inventory of capital spares, or spare equipment, purchased before the Spinoff (as defined below) from Noble, and idle rigs that can also be used for parts in lieu of making capital expenditures. 9/27/16 Hrg. Tr. at 30:5–10, 44:18–22 (Stilley Test.).

23. As discussed in detail below, upon emergence from Chapter 11, the Debtors proposed to reduce their fleet to 23 rigs – 22 jackups (including the two Prospector rigs) and one semisubmersible. Under the Downside Sensitivity, the Debtors would operate 22 rigs.

C. Paragon's Markets

24. The Debtors currently operate in the North Sea, the Middle East, and India. 6/21/16 Hrg. Tr. at 132:22–133:4 (Stilley Test.). Up until just a few months ago, they were still operating in Brazil and West Africa, and they recently moved their final rig out of Mexico. 6/21/16 Hrg. Tr. (Stilley Test.) at 175: 21–25.

D. The Correlation Between Oil Prices and the Demand for Paragon's Rigs

25. Paragon acknowledges that Brent oil prices have a considerable knock-on effect on E&P companies and service providers, including Paragon. (TLA123 at PGN00027838; 6/22/2016 Hrg. Tr. 27:10-28:14 (Stilley Test.); 9/27/2016 Hrg. Tr. 69:25-70:7 (Stilley Test.); 9/28/2016 Hrg. Tr. 145:6-146:11; TLA422; 9/29/2016 Hrg. Tr. 150:8-151:14 (Leand Test.); TLA525.) Since March 2016, the price of oil has ranged between $30 to $60 a barrel, (TLA525), and projections for the future forecast only modest increases in the price of oil. (*Id.*; 9/28/2016 Hrg. Tr. 149:8-16, 149:22-150:7 (Leand Test.).)

26. Although Mr. Stilley told the Board in July 2016 that the supply-demand balance would occur in the second half of 2016, resulting in improved oil prices, oil prices have remained the same and have not improved. (9/27/2016 Hrg. Tr. 73:16-74:9 (Stilley Test.); TLA377 at 51.) Mr. Stilley also reported that producers' capital budgets were down 20 to 40% in 2016 and that 2017 spending is unknown. (TLA377 at 51.)

27. At the September 2016 Pareto Conference in Oslo, Norway, in his presentation to 1,000 bankers and analysts, Mr. Stilley noted that Brent crude oil prices "continue to be volatile" and that "4th quarter prices will be important factors for 2017 capital budgets" of producers. (TLA396 at 8.)

28. Daniel R. Fischel[6] opined that futures contract prices for oil are important because forecasts bake in analysis about what has happened in the past regarding oil

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[6] The Court accepted that Prof. Fischel is an expert in valuation, insolvency and economic analysis. (9/26/2016 Hrg. Tr. 132:21-23, 133:10-12 (Fischel Test.); *see also* TLA576.). However, the Court does not find Prof. Fischel to be an expert as to whether the Business Plan or the Modified Business Plan are reasonable or credible, and does not accept Prof. Fischel's testimony regarding the Debtors' projections.

prices in past cycles and can properly weigh the importance of past information. (TLA423; 9/28/2016 Hrg. Tr. 146:20-147:9, 147:14-21, 148:10-19 (Fischel Test.).) Prof. Fischel explained that the participants in the futures market have the ability to interpret past cycles and these people "are putting their money on the line and betting on what futures prices are going to be." (9/28/2016 Hrg. Tr. 147:5-9, 147:14-17 (Fischel Test.).) Prof. Fischel further explained that if participants believed the futures prices were too low, they could go long; and if enough participants took that position, future prices would rise. (*Id.* at 148:10-18.)

E. The Competitive Tendering Process

29. Contracts for offshore rigs such as the Debtors' rigs may be awarded through a direct negotiation or a competitive tender. (TLA621 at 38:18-13 (Tietz Dep.).) Philip Burke, the managing director of OGC Global Contracting Limited (which provides consulting services in procurement and contracting to oil and gas companies),[7] provided a thorough explanation of the process that oil companies and producers use in the current market environment to enter into contracts for offshore rigs. (9/29/2016 Hrg. Tr. 65:5-66:2, 79:23-80:19 (Burke Test.).)

30. Prior to 2015, when oil prices were high and rigs such as Paragon's rigs were in strong demand, it was not uncommon for rigs to be engaged on a single source or a negotiated basis, as opposed to a competitive tender. (9/29/2016 Hrg. Tr. 89:25-90:10 (Burke Test.); TLA621 at 39:14-40:6.) During the bullish market, rigs were snapped up

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[7] The Court accepted that Mr. Burke is an expert in the offshore drilling industry, including tendering and contracting for offshore rigs. (9/29/2016 Hrg. Tr. 80:20-81:2 (Burke Test.); TLA577.)

quickly and there was no time or choice to conduct competitive tendering. (9/29/2016 Hrg. Tr. 89:25-90:10 (Burke Test.).)

31. Following the downturn in oil prices and concomitant drop in demand for rigs, however, "almost … all" contracts are awarded now via tender. (9/29/2016 Hrg. Tr. 85:13-18, 90:12-16 (Burke Test.); TLA621 at 41:5-42:17; 9/27/2016 Hrg. Tr. 41:10-17 (Stilley Test.).) Oil companies "have a policy that everything unless under extreme extenuating circumstances will be the subject of a competitive tender." (9/29/2016 Hrg. Tr. 85:13-18 (Burke Test.).) Putting a bid out for auction improves performance, gets the best possible terms and rates, eliminates unnecessary costs, and makes economic sense. (6/29/2016 Hrg. Tr. 188:14-189:5 (Leand Test.); 9/29/2016 Hrg. Tr. 92:19-93:13, 101:9-13 (Burke Test.); TLA403.) Also the massive scandals over the past 12 to 18 months such as the significant bribery scandals in Brazil and Mexico have led the industry to favor the tendering method. (6/29/2016 Hrg. Tr. 188:14-189:5 (Leand Test.).) Mr. Stilley acknowledged that, "during a downturn [Paragon] probably responds to a greater percentage of tenders than [it would] during the times when business is better. . . ." (6/21/2016 Hrg. Tr. 160:1-5 (Stilley Test.).)

32. Even new contracts for 30 or 60 days in duration would be subject to competitive tendering because they represent a significant expenditure on behalf of the oil company in this market. (9/29/2016 Hrg. Tr. 92:9-18 (Burke Test.).) E&P companies are currently seeking to drive excessive costs out of the supply chain and are working to sustain this reduced cost environment to avoid over-inflation and "boom and bust principle" that has been seen in recent years and in the current cycle. (*Id.* at 84:18-85:10,

92:19-93:2.) Even if the price of oil recovers, oil companies are unlikely to return to past practices as opposed to competitive tendering because the vast oversupply of rigs will allow E&P companies to choose between multiple rigs for any one contract. (9/29/2016 Hrg. Tr. 93:14-20 (Burke Test.).) Furthermore, given the erosion of the balance sheets of oil companies in this downturn, oil companies would need to "see the oil price move in a period of stability," not just recover, before they would engage in less competitive tendering. (*Id.* at 93:14-94:4.)

33. There may be some exceptions to the use of competitive tendering, such as a need to extend contracts on rigs already under contract for a short period, when there is a short term requirement by an oil company for a particular short term piece of work, or when a rig is in the area or is moving through the area on its way to be stacked, but they are the exception and not the rule. (9/29/2016 Hrg. Tr. 90:17-91:22 (Burke Test.).)

34. Competitive tenders proceed in two stages. In the first, the prequalification stage, an oil and gas company approaches the market and solicits expressions of interest. The company screens out any rig companies that do not fulfill the key criteria that the tender will be evaluated on. (9/29/2016 Hrg. Tr. 95:21-96:9 (Burke Test.).) Factors that determine whether a rig company prequalifies include the financial condition of the rig company, and its safety record. (TLA621 at 53:8-54:8, 55:10-18 (Tietz Dep.).)

35. Those rig companies passing the pre-qualification stage (a "manageable" number of companies, *i.e.*, four or five) are included on the bid list and will be sent an invitation to tender, which states the scope of work for the contract and information the oil company expects to receive back from the rig companies in order to evaluate and make

a decision on who will be recommended for award. (9/29/2016 Hrg. Tr. 93:10-13, 96:4-18 (Burke Test.).)

36. Oil and gas companies evaluate a number of criteria in evaluating competitive tenders. These general factors are sometimes weighted differently in different situations, but are always applied. These factors include: financial stability, which is very important to oil and gas companies; health and safety statistics because "[t]he oil industry [is] very safety conscious;" an "individual company['s] processes and systems;" "the availability of the proposed rig for the particular schedule;" a "detailed review of the actual rig being proposed;" "[t]he equipment on the rig;" "[p]revious operational experience;" "[t]he key personnel that are being proposed;" "[t]he crew of the rig" and their "experience . . . working with a particular rig" which is important because of "learning curves involved with handling sophisticated pieces of equipment;' and "any of the alternative offers that the contractors may wish to propose." (9/29/2016 Hrg. Tr. 96:19-97:4, 97:24-99:2, 100:14-17, 102:5-9 (Burke Test.); TLA403.)

37. Alternative offers are a factor considered by oil and gas companies when evaluating a competitive tender. In a tender "bidders are encouraged to explore further opportunities that might result in a saving or cost-saving to the company." This may include "bundling services into the offer" "that may have previously been contracted separately. . . ." It could also involve "strategic thinking in terms of offering better value, in terms of deferred payment, possibly putting some profit at risk rather [than] providing a rig at a day rate." These alternative offers may "result in a bidder having an advantage [in the competitive tender process]." (9/29/2016 Hrg. Tr. 99:3-100:2 (Burke Test.).)

Paragon does not have a sufficient product mix or number of long-term expensive contracts to make such offers. (6/29/2016 Hrg. Tr. 171:9-173:2 (Leand Test.).)

38. After the pre-qualification phase, there are two methodologies for evaluating bids. (9/29/2016 Hrg. Tr. 107:10-11 (Burke Test.).) Under the first methodology, the "most economically advantaged bid" will win; meaning that the winner will be based on combined technical (*i.e.*, the key evaluation criteria) and commercial (*i.e.*, price) advantages of a bid. (*Id.* at 107:11-16.) Under the second methodology, which is used often, the oil company will award the contract to the "lowest price technically acceptable bidder." (*Id.* at 107:17-18.) Under this methodology, the "lowest normalized price" bidder that passes all of the technical criteria will receive the contract. (*Id.* 107:19-22.) The "lowest normalized price" will be determined depending on the efficiency of a rig's operations because oil companies look at the total cost of service and not just the dayrate; in other words, a lower specification lower efficiency rig may have to bid on a contract at a lower dayrate in order to win a contract over a higher specification higher efficiency rig that can perform the work in a shorter amount of time. (*Id.* at 107:24-108:20.)

39. It takes approximately five months from the time that the operator or oil company solicits bids until a rig can be put into the field and earn revenue; there will be an initial tender period; after the contract is awarded, the customer will inspect the rig; if the rig is stacked, the company will need to get a crew, arrange supply boats, other supporting equipment for the activity; the rig will need to be on location in time; and the

contract with the customer will need to be negotiated. (6/29/2016 Hrg. Tr. 155:23-156:9 (Leand Test.).)

F. The Supply Overhang of Jackup Rigs in the Offshore Industry

40. Mr. Stilley agreed that there are more jackup rigs in the marketplace looking for work than being used by customers for drilling activities. (TLA135 at PGN00045007; 6/22/16 Hrg. Tr. 40:13-42:2 (Stilley Test.); *see also* TLA529; TLA591; TLA609; TLA610; TLA611; 9/29/2016 Hrg. Tr. 155:14-156:17, 158:3-159:2, 160:15-166:24, 168:25-169:21 (Leand Test.); 9/30/2016 Hrg. Tr. 117:9-20 (Leand Test.) This "vast oversupply" of rigs is creating a "challenging commodity price environment" that is expected to last at least an additional 3.2 years, *i.e.*, throughout the duration of the Projection Period. (9/30/2016 Hrg. Tr. 110:1-25 118:9-119:15 (Leand Test.); TLA527; (TLA135 at PGN00045007; 6/22/16 Hrg. Tr. 40:13-42:20 (Stilley Test.); 6/23/2016 212:13-214:14 (Fordyce Test); PGN187 at p. 2.) Paragon itself acknowledges that the oversupply will last at least two or three years. (6/22/2016 Hrg. Tr. 42:21-44:1 (Stilley Test.); TLA135 at PGN00045007.) Paragon's senior VP of Marketing and Contracts, Mr. Tietz, further testified that over the course of the last year, utilization has decreased, creating more supply, less demand and dayrates have gone down. (TLA621 at 59:24-60:6 (Tietz Dep.).) The marketplace has continued to worsen over the course of 2016. (*Id*. at 59:12-16.) In mid-September 2016, Mr. Stilley told the Pareto Conference attendees that the offshore drilling market was "challenged" and that the "near-term outlook was uncertain." (TLA396 at 8; 9/27/2016 Hrg. Tr. 65:10-21, 67:8-16 (Stilley Test.).)

41. Including newly built rigs in the shipyard, the total supply of jackup units is over 600. (TLA621 at 59:3-16 (Tietz Dep.).) The total rig supply, not including newbuilds, is 535 rigs. (9/29/2016 Hrg. Tr. 154:11-17 (Leand Test.); TLA527; TLA528.) Mr. Leand reviewed IHS Petrodata and found that there are 109 newbuild rigs, 100 of which are not contracted and 9 of which were being built for contracts. (9/29/2016 Hrg. Tr. 152:7-15 (Leand Test.); TLA527.) Mr. Stilley's presentation at the Pareto conference confirms Mr. Leand's testimony about the number of newbuild rigs. (TLA 396 at 15.) The number of current rigs under contract is 328 and the overall supply overhang (*i.e.*, uncontracted rigs) is 319 rigs. (9/29/2016 Hrg. Tr. 152:16-19 (Leand Test.); TLA527.) Not including newbuilds, there are 208 uncontracted rigs. (9/29/2016 Hrg. Tr. 154:18-19, 154:23-155:1 (Leand Test.); TLA527.) Based on this data, Mr. Leand opined that the market continues to be vastly oversupplied. (9/29/2016 Hrg. Tr. 152:20-24 (Leand Test.); TLA527.) The oversupply of rigs is "historical" even excluding newbuild rigs; and the only prior comparable downturn occurred in 1986, which had less of an overhang and did not have the additional newbuild overhang. (9/29/2016 Hrg. Tr. 157:15-158:2, 160:15-162:18 (Leand Test.); TLA609.)

42. Although Mr. Stilley stated during his direct examination that he did not agree that rigs in shipyards contributed to the oversupply, Mr. Stilley agreed that one of the reasons he believed market outlook was "uncertain" was due to shipyards full of uncontracted rigs under construction. (9/27/2016 Hrg. Tr. 51:16-52:2, 68:19-24, 69:5-10 (Stilley Test.); TLA396 at 8.) Mr. Stilley told Paragon's shareholders in the 2015 annual report that he believed that new builds will enter the market and add to the rig supply

overhang. (6/22/2016 Hrg. Tr. 42:21-43:11 (Stilley Test.); TLA135.) Mr. Leand explained that it did not matter whether the newbuild rigs were complete, sitting in the shipyards or under construction, the fact that they were being built and people believed that they would be built impacts market supply. (9/29/2016 Hrg. Tr.153:16-20 (Leand Test.).) Mr. Leand further explained that the newbuild rigs will likely come into the market over the next three years because of the capital spent to build the rigs and the need for the shipyards to monetize the rigs. (6/29/2016 Hrg. Tr. 161:7-162:2 (Leand Test.); 9/29/2016 Hrg. Tr. 159:18-160:2, 160:5-14 (Leand Test.).) The summer 2016 Morgan Stanley report, relied on by Mr. Leand, likewise envisioned newbuild rigs entering the market within the Projection Period. (9/30/2016 Hrg. Tr. 114:19-115:19 (Leand Test.); TLA540.)

G. The Debtors' Prepetition Indebtedness

43. On the Petition Date, the Debtors had approximately $1.43 billion of secured indebtedness and approximately $1.02 billion in unsecured indebtedness, substantially all of which was issued or guaranteed by the Debtors. Disclosure Statement at 12.

44. Paragon Parent and Paragon International Finance Company are borrowers under that certain Senior Secured Revolving Credit Agreement, dated as of June 17, 2014, by and among Paragon Parent and Paragon International Finance Company, as borrowers, the lenders and issuing banks party thereto (the "**Revolver Lenders**") from time to time, JPMorgan Chase Bank, N.A., as administrative agent, J.P. Morgan Securities LLC, Deutsche Bank Securities Inc. and Barclays Bank plc, as Joint Lead Arrangers and Joint Lead Bookrunners, and certain other parties thereto (as amended, restated,

modified, or supplemented from time to time, the "**Revolving Credit Agreement**"). *Id.*[8] The Revolving Credit Agreement provides for revolving credit commitments, including letter of credit commitments and swingline commitments, in an aggregate principal amount of $800 million (the "**Revolving Credit Facility**," and the amounts outstanding thereunder, the "**Loans**"). *Id.* at 12–13.

45. As of April 2016, the aggregate principal amount outstanding under the Revolving Credit Agreement was $708.5 million in unpaid principal, plus interest, fees, and other expenses, in addition to approximately $87.2 million of letters of credit. *Id.* The Loans bear interest, at Paragon Parent's option, at either (i) an adjusted LIBOR plus an applicable margin ranging between 1.50 to 2.50 percent, depending on the Leverage Ratio (as defined in the Revolving Credit Agreement), or (ii) a base rate plus an applicable margin ranging between 0.50 to 1.50 percent, depending on the Leverage Ratio. *Id.* The Revolving Credit Agreement originally was set to mature in July 2019. *Id.*

46. Paragon Offshore Finance Company is the borrower under that certain Senior Secured Term Loan Agreement, dated as of July 18, 2014, by and among Paragon Parent, as parent, Paragon Offshore Finance Company, as borrower, the lender parties thereto, and Cortland Capital Market Services LLC, as successor administrative agent (the "**Term Loan Agent**") (as amended, restated, modified, or supplemented from time to time, the "**Secured Term Loan Agreement**"). *Id.* The Secured Term Loan Agreement

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[8] PGN 22.

provided for a term loan in an aggregate principal amount of $650 million (the "**Secured Term Loan**"). *Id.*

47. As of April 2016, the aggregate amount outstanding under the Secured Term Loan Agreement was approximately $642 million in unpaid principal, interest, fees, and other expenses. *Id.* The Secured Term Loan bears interest at LIBOR plus 2.75 percent, subject to a minimum LIBOR rate of 1 percent or a base rate plus 1.75 percent at Paragon Offshore Finance Company's option. *Id.* The Secured Term Loan was set to mature in July 2021. *Id.*

48. Paragon Parent is party to that certain Senior Notes Indenture, dated as of July 18, 2014, by and among Paragon Parent, as issuer, each of the guarantors named therein, and Deutsche Bank Trust Company Americas, as trustee (the "**Notes Trustee**"), and the other parties thereto, pursuant to which the Debtors issued 6.75 percent Senior Notes due 2022 in the aggregate principal amount of $500,000,000 (the "**6.75% Senior Notes**") and 7.25 percent Senior Notes due 2024 in the aggregate principal amount of $580,000,000 (the "**7.25% Senior Notes**" and, together with the 6.75% Notes, the "**Senior Notes**"). *Id.* As of April 2016, the aggregate amount outstanding under the 6.75% Senior Notes was approximately $457 million in unpaid principal, plus interest, fees, and other expenses, and the aggregate amount outstanding under the 7.25% Senior Notes was approximately $527 million plus interest, fees, and other expenses. *Id.*

49. The obligations of Paragon Parent, Paragon International Finance Company, Paragon Offshore Finance Company, and the Debtor-guarantors, as applicable, under the Revolving Credit Agreement and the Secured Term Loan

Agreement are secured pursuant to that certain Guaranty and Collateral Agreement, dated as of July 18, 2014 (as amended, restated, modified, or supplemented from time to time, the "**Guaranty and Collateral Agreement**"). *Id*. at 14. Pursuant to the Guaranty and Collateral Agreement, each of the Debtors granted a first-priority lien on substantially all of its property other than "**Excluded Assets**," which include, among other things, any deposit accounts and securities accounts, any Capital Stock in Unrestricted Subsidiaries (as defined in the Revolving Credit Agreement and Secured Term Loan Agreement), and any owned or leased real property. *Id*. The collateral includes the Collateral Rigs (as defined in the Revolving Credit Agreement and Secured Term Loan Agreement), capital stock of (i) the owners of the Collateral Rigs, (ii) Paragon International Finance Company, and (iii) Paragon Offshore Finance Company and certain other property pledged under the Collateral Documents (as defined in the Revolving Credit Agreement and Secured Term Loan Agreement). In addition, certain guarantors under the Guaranty and Collateral Agreement executed mortgages for each of the Collateral Rigs. *Id*.

H. Hiring of Lazard and Consideration of Approach to Restructuring

50. In 2015, the Debtors engaged Lazard to provide financial advice and restructuring services. 6/21/16 Hrg. Tr. at 22:22–23 (Kurtz Test.); 6/23/16 Hrg. Tr. at 78:18–79:20 (Fordyce Test.); PGN 239 ¶ 34. Over the course of two months, Lazard engaged in an intensive due diligence process that included review of the Debtors' company documents, rigorous examination of the Debtors' financials and business plans,

and regular interaction with management, Board, and the finance and risk committee. 6/23/16 Hrg. Tr. at 79:8–83:22 (Fordyce Test.).

51. Prior to selecting the restructuring alternative embodied by the Original Plan and Modified Plan, the Debtors considered various alternatives, which were considered by the Board. The option which the Debtors ultimately pursued, was a plan that reinstated the Secured Term Loan, de-levered the Debtors' balance sheet, restructured financial covenants with the Revolver Lenders, and extended the maturity date of certain of their Loans. 6/21/16 Hrg. Tr. at 30:17–32:4 (Kurtz Test.).

I. Preparation of Business Plan

52. In the fall of 2015, over the course of several months, the Debtors initiated their annual budget process and began to prepare projections in connection with the restructuring options presented to the Board. 6/21/2016 Hrg. Tr. at 163:21–23 (Stilley Test.). The budgets are designed to balance capital expenditures with, among other things, risk-adjusted opportunities in the marketplace. 6/21/2016 Hrg. Tr. at 161:20–162:6 (Stilley Test.). The creation of the Debtors' budget is an iterative process that takes months to complete. 6/21/2016 Hrg. Tr. at 161:9–19 (Stilley Test.). Initially, the field operations group and shore-based groups, as well as the corporate group, developed individual budgets for their departments and locations. *Id.* at 161:9–13, 164:10–17. The Debtors' management team then reviewed individual department budgets to ensure that assumptions were reasonable and accurate (*id.* at 161:9–19, 164:18–25, 165:21–166:16), prior to presentation to the Board. *Id.* at 164:18–25.

53. In formulating the Business Plan, the Debtors took into account their current market position in each of the regions in which they anticipate operating (North Sea, Middle East, India, West Africa, and Mexico). 9/27/16 Hrg. Tr. at 37:24–38:10 (Stilley Test.); 6/21/16 Hrg. Tr. at 176:1–8 (Stilley Test.). Paragon also considered information received directly from customers, employees on the ground in each region, and their decades of experience in the oil and gas industry. 9/27/16 Hrg. Tr. at 37:24–38:10 (Stilley Test.).

54. The Debtors believe that they took a conservative approach in preparing the Business Plan. For instance, the Debtors assert that the Business Plan takes the "oversupply of rigs" into account, which is based on the expected marketed supply in each region. 6/21/2016 Hrg. Tr. 215:21–216:12 (Stilley Test.); 9/27/2016 Hrg. Tr. at 51:16–20 (Stilley Test.). The Business Plan also does not assume a significant improvement in oil prices. 9/27/16 Hrg. Tr. at 39:14–16 (Stilley Test.). Moreover, Mr. Stilley testified that he believes that the Debtors' budget accurately forecasts the capital expenditures needed to implement their Business Plan. 6/23/2016 Hrg. Tr. at 22:2–5 (Stilley Test.). He further testified that the dayrates and utilization assumptions built into the Business Plan are conservative. 6/21/2016 Hrg. Tr. at 199:19–24 (Stilley Test.)

55. The assumptions underlying the Business Plan were altered several times to reflect market changes and comments from the finance and risk committee in order to assess numerous possible scenarios. 6/21/16 Hrg. Tr. at 168:12–20 (Stilley Test.). After Paragon filed for bankruptcy, the market continued to worsen and customers began cutting their budgets for 2016 by as much as fifty percent. 6/21/16 Hrg. Tr. at 168:24–

169:5 (Stilley Test.). The Debtors also received feedback from customers that caused them to be concerned about their ability to meet the near-term timetables in their forecast. 6/21/16 Hrg. Tr. at 49:22–50:19 (Kurtz Test.); 6/21/16 Hrg. Tr. at 168:21–169:16 (Stilley Test.). As a result, the Debtors believed that the January business plan filed with the initial disclosure statement might need to be revised, especially for 2016, based upon changing information and market conditions. 6/21/16 Hrg. Tr. at 169:7 (Stilley Test.). In an effort to be prudent and conservative, the Debtors adjusted their projections. 6/21/16 Hrg. Tr. at 49:22–50:19 (Kurtz Test.); 6/21/16 Hrg. Tr. at 168:21–169:16 (Stilley Test.).

56. The Debtors' Business Plan going forward contemplates having 23 rigs, comprised of 22 jackups and one floating rig (a semisubmersible in the North Sea), 11 of which are already in operation. 6/21/16 Hrg. Tr. at 132:20–21, 145:3–6 (Stilley Test.). Mr. Stilley testified at the Initial Confirmation Hearing that the Debtors' 10 remaining rigs are certainly not "old and cold" and that the Debtors intend to bring them back into service within the next couple of years. 6/21/16 Hrg. Tr. at 145:13–146:13 (Stilley Test.). In fact, only two out of those 10 rigs are "cold-stacked," meaning there is nobody currently on the rig. 6/21/16 Hrg. Tr. at 145:13–146:13 (Stilley Test.). Moreover, the Debtors have experience with bringing cold-stacked rigs back into service. 6/21/2016 Hrg. Tr. at 146:14–25 (Stilley Test.). The Debtors estimate that it should not cost more than $3–$4 million to bring a "cold-stacked" rig back into service. 6/21/2016 Hrg. Tr. at 147:4–24 (Stilley Test.).

J. The Noble Settlement

57. The Debtors were spun-off from Noble in August 2014 (the "**Spinoff**"). PGN 239 ¶ 9. Paragon and Noble are party to several separation agreements executed in connection with the Spinoff including a tax sharing agreement dated as of July 31, 2014 (the "**Tax Sharing Agreement**"). 6/22/16 Hrg. Tr. at 5:3–4 (Stilley Test.); PGN 239 ¶ 10. Essentially, the Tax Sharing Agreement provides that Paragon assumed responsibility for certain tax liabilities for the Paragon entities, as well as for some of the Noble entities. 6/21/16 Hrg. Tr. at 217:13–21 (Stilley Test.); PGN 239 ¶ 17. Also on July 21, 2016, the Debtors executed a side letter with Noble which modified the Tax Sharing Agreement to allow Noble to manage certain tax claims in Mexico. 6/22/16 Hrg. Tr. at 4:24–5:2, 5:10–13 (Stilley Test.).

58. The Debtors were assessed a very significant tax liability in Mexico (the "**Mexican Tax Liabilities**"), arising from activities that occurred in 2010. 6/21/16 Hrg. Tr. at 39:3–8 (Kurtz Test.); PGN 239 ¶ 18. Mr. Kurtz testified that, at the time of the restructuring negotiations, the Mexican Tax Liabilities were estimated to be in the $190 million range, but could grow to approximately $300 million. 6/21/16 Hrg. Tr. at 39:9–12 (Kurtz Test.).

59. Typically, taxes assessed by the Mexican government, including the Mexican Tax Liabilities, can be settled for "pennies on the dollar." 6/21/16 Hrg. Tr. at 39:13–23 (Kurtz Test.); PGN 239 ¶ 20. However, during the pendency of any such challenge, the Debtors would have been required to post a performance bond for the full amount of the assessment. 6/21/16 Hrg. Tr. at 39:13–23 (Kurtz Test.); PGN 239 ¶ 20.

Thus, the Debtors would have potentially had to post a bond of approximately $200 million, and potentially even more, over the course of the Business Plan. 6/21/16 Hrg. Tr. at 217:13–218:18 (Stilley Test.); 6/22/16 Hrg. Tr. at 212:8–11 (Stilley Test.); PGN 239 ¶ 21. Other than Noble, or utilizing cash collateral, the Debtors had no other source from which to obtain these funds. 6/22/16 Hrg. Tr. at 213:5–8 (Stilley Test.); PGN 239 ¶ 68. In addition, assuming a $300 million tax assessment, the Debtors could have been potentially liable for up to $45 million in fees associated with posting the bond. 6/23/16 Hrg. Tr. at 32:19–33:8 (Stilley Test.).

60. The term sheet for the Noble Settlement Agreement was executed in February 2016. PGN 14 at 6. The Noble Settlement confers two principal benefits on the Debtors: (i) it redistributes responsibility for the Mexican Tax Liabilities and related taxes levied on Noble entities in a manner more favorable to the Debtors; and (ii) it requires Noble to provide direct bonding for the Mexican Tax Liabilities, thereby permitting Noble and the Debtors to dispute the legitimacy of these claims without requiring the Debtors to collateralize the bond, and in turn freeing up nearly $200 million of the Debtors' cash. PGN 173 at 5; 6/22/16 Hrg. Tr. at 5:18–7:7 (Stilley Test.); 6/21/16 Hrg. Tr. at 39:3–40:11 (Kurtz Test); PGN 239 ¶¶ 60, 68, 69. Noble agreed to assume all of the Noble entities' liability for the Mexican Tax Liabilities, as well as half of any potential liability for the Paragon-related entities. 6/21/16 Hrg. Tr. at 218:21–219:12 (Stilley Test.); PGN 239 ¶¶ 68, 69. Noble has also agreed to manage the tax contesting process, ensuring that the Debtors do not have to devote people and resources to that process. 6/21/16 Hrg. Tr. at 219:10–12 (Stilley Test.); PGN 239 ¶ 69.

61. In exchange for the aforementioned benefits, the Debtors agreed to give up potential fraudulent conveyance claims that it had against Noble. 6/22/16 Hrg. Tr. at 7:8–11 (Stilley Test.); PGN 239 ¶ 54. At the Board's direction, the Debtors' advisors (Weil and Lazard) conducted an investigation of these potential claims by interviewing witnesses, reviewing financial statements and performing financial analyses to evaluate the strength of these potential claims. 6/22/16 Hrg. Tr. at 203:16–204:3 (Stilley Test.); PGN 239 ¶ 30. At a January 2016 Board meeting, the Debtors' advisors presented their findings to the Board. 6/22/16 Hrg. Tr. at 204:4–6 (Stilley Test.); PGN 239 ¶ 62. The Debtors' advisors explained that the pursuit of fraudulent conveyance claims against Noble would be expensive and the litigation could potentially take a number of months. 6/22/16 Hrg. Tr. at 209:11–24 (Stilley Test.); PGN 239 ¶ 62.

62. After extensive discussion, the Board determined that litigation with Noble would have an uncertain outcome, be expensive and time consuming, and that the Noble Settlement Agreement was in the best interest of the Debtors and their creditors. 6/22/16 Hrg. Tr. at 7:12–17, 8:5–9:2 (Stilley Test.); PGN 239 ¶ 64. Mr. Stilley explained that, absent the Noble Settlement Agreement, a settlement of the Mexican Tax Liabilities along with litigation over the fraudulent conveyance claims could have potentially cost the Debtors approximately $105 million. 6/23/16 Hrg. Tr. at 33:21–25 (Stilley Test.). More importantly, that course of action would have required the Debtors to bond up to $300 million in Mexican Tax Liabilities and could potentially have precluded the reorganization contemplated by the Modified Plan. 6/23/16 Hrg. Tr. at 34:1–4 (Stilley Test.); PGN 239 ¶ 68.

K. Negotiation of Original Plan

63. The Original Plan was the product of extensive, good-faith negotiations between the Debtors and the Plan Support Parties. Negotiations commenced in November of 2015, and on December 30, 2015, the Debtors reached a deal with the Ad Hoc Group of Senior Noteholders (the "**Ad Hoc Group**"), which included a $380 million cash payment. 6/21/16 Hrg. Tr. at 36:1–3, 41:3–8 (Stilley Test.). The deal with the Ad Hoc Group was conditioned upon entering into the Noble Settlement Agreement, which was reached in January of 2016. 6/21/16 Hrg. Tr. at 41:3–17 (Stilley Test.). Subsequently, the Debtors reached an agreement with the Revolver Lenders, which included a $165 cash payment and a two-year maturity extension. Given the cash payment to the Revolver Lenders, coupled with the Debtors' desire to only use up to approximately $500 million of cash in their restructuring, the Debtors subsequently renegotiated their agreement with the Ad Hoc Group and reduced their cash payment in exchange for an increased amount of equity in the Reorganized Debtors. 6/21/16 Hrg. Tr. at 42:20–44:18 (Stilley Test.).

L. Terms of the Original Plan

64. Under the Original Plan, approximately $985 million of Senior Notes were to be satisfied in exchange for $345 million in cash, 35 percent equity in the reorganized Paragon Parent and certain deferred cash payments up to $50 million to the Ad Hoc Group. PGN 212. In consideration of a $165 million principal payment, the Revolving Credit Agreement would be amended to include, among other things, new minimum liquidity covenant of $110 million (with a 60-day grace period where liquidity must

remain above $95 million), a leverage and interest coverage ratio covenant holiday through 2017, and an extended maturity date. PGN 213. The Original Plan also cured and reinstated the Secured Term Loan Agreement and incorporated the Noble Settlement Agreement (discussed below). 6/21/2016 Hrg. Tr. at 34:16–35:14, 51:16–52:17 (Kurtz Test.).

M. Updates to the Business Plan

65. Following the Initial Confirmation Hearing, the Debtors updated the Business Plan to reflect actual financial results through June 30, 2016, and to account for known changes in contract utilization, dayrates, and capital expenditures. PGN 178 (Business Plan forecast model).

66. The Debtors have outperformed their projections through June, with a net change in cash of $94 million above projections,[9] and an out-performance on expected EBITDA by $78 million.[10] 9/28/16 Hrg. Tr. at 32:21–33:13 (Fordyce Test.); 9/27/16 Hrg. Tr. at 4:16–23, 6:6–19, 7:3–22 (Stilley Test.); PGN 215. The Debtors' outperformance can be attributed to longer contracts, payment of receivables, and reduced costs. 9/28/16 Hrg. Tr. at 30:3–15 (Fordyce Test.); PGN 215. Paragon's contract drilling expenses were 20 percent lower than projected, a $55 million savings. 9/28/16 Hrg. Tr. at 30:11–15 (Fordyce Test.); PGN 215. At the same time, operating days for the first six months of

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[9] *Compare* PGN 10 at 50 (projecting $288 million in cash and $510 million to be paid to Ad Hoc Group and Revolvers upon emergence) *with* PGN 169 at 10 (form 10-Q demonstrating $892 million in cash at the end of second quarter 2016).

[10] *Compare* PGN 12 at 6 (projecting $104 million in adjusted EBITDA) *with* PGN 169 at 70 (demonstrating approximately $181 million adjusted EBITDA at the end of second quarter 2016).

2016 were only 5–6 percent below projections, demonstrating that the savings represent real cost control, not just reduced activity. 9/28/16 Hrg. Tr. at 94:7–14 (Fordyce Test.). As part of these efforts, Paragon negotiated very aggressively with its shipyards and suppliers to reduce costs. 9/27/16 Hrg. Tr. at 44:5–8 (Stilley Test.). The Debtors have also been successful at lowering stacking costs and "handrail" costs, which are operating costs required to operate the rigs while drilling. 9/28/16 Hrg. Tr. at 32:8–20 (Fordyce Test.). Such cost cutting is ongoing, and importantly, the benefits thereof have *not* been incorporated into the Business Plan or Downside Sensitivity. 9/28/16 Hrg. Tr. at 32:8–20, 94:1–23 (Fordyce Test.).

67. These first and second quarter results are reflected in the Business Plan. 9/27/16 Hrg. Tr. at 6:20–23 (Stilley Test.).

N. Preparation of Downside Sensitivity

68. After the Initial Confirmation Hearing, the Debtors and their advisors prepared a downside sensitivity analysis to the Debtors' Business Plan (the "**Downside Sensitivity**"). PGN 181 (Downside Sensitivity forecast model). The Downside Sensitivity is not a revised business plan and the Debtors believe that the Business Plan is still the best estimate of Debtors' expectations. 9/28/16 Hrg. Tr. at 15:22–16:8 (Fordyce Test.); 9/27/16 Hrg. Tr. at 8:6–8, 12:11–18 (Stilley Test.). The Downside Sensitivity was constructed in the same manner as the Debtors' Business Plan, but contains even more conservative inputs. 9/27/16 Hrg. Tr. at 12:11–18 (Stilley Test.); 9/28/16 Hrg. Tr. at 29:6–20 (Fordyce Test.); PGN 185. The Downside Sensitivity is essentially a "stress test" of Paragon's Business Plan that assumes a longer and more prolonged downturn and

slower recovery. 9/27/16 Hrg. Tr. at 7:3–8:5 (Stilley Test.); 9/30/2016 Hrg. Tr. at 133:21–22 (Fordyce Test.).

69. In formulating the Downside Sensitivity, Paragon's management team, including Randy Stilley, Steve Manz, Andrew Tietz, Blake Morris, and Todd Strickler, evaluated the current market and forecasted how a hypothetical downturn of an additional 12 to 18 months would impact Paragon's rigs in each region in which they operate. 9/28/16 Hrg. Tr. at 27:21–28:12 (Fordyce Test.); 9/27/16 Hrg. Tr. at 8:9–14, 10:7–25, 11:16–23, 128:6–12 (Stilley Test.). Considering that an additional 12 to 18 month delay would render this downturn the longest in the industry's history, the Debtors believe that these assumptions represent a very conservative approach. 9/27/16 Hrg. Tr. at 9: 22–10:6, 14:3–8 (Stilley Test.).

70. In putting together the Downside Sensitivity, the Debtors analyzed their current contractual situation in each region, their decades of industry experience, feedback from their employees on the ground in each region, and information received directly from their customers. 9/27/16 Hrg. Tr. at 12:19–25 (Stilley Test.).[11] The Debtors' assumptions were reviewed and tested by the Debtors' advisor, Lazard. Lazard reviewed the analysis rig by rig, market by market, and prodded management on the logic of their choices. 9/28/2016 Hrg. Tr. at 17:6–18 (Fordyce Test.). Lazard also participated in discussions with the Board and creditor groups to update the directors on the Debtors'

[11] As Mr. Stilley testified, the Debtors did not use third party analyst's input in developing their models, as they tend to be overly optimistic when the industry is doing well and overly pessimistic in downturns. 9/27/2016 Hrg. Tr. at 13:2–12, 125:12–23 (Stilley Test.).

potential future performance, and to negotiate additional cushion should the downside scenario actually occur. 9/28/16 Hrg. Tr. at 17:25–18:19 (Fordyce Test.).

71. The Downside Sensitivity made significant adjustments to dayrates,[12] utilization, and capital expenditures,[13] including adding increased costs for rigs that were out of service longer. PGN 178, 180, 181, 183; 9/27/16 Hrg. Tr. at 11:24–12:3 (Stilley Test.). In contrast to the Modified Plan, the Downside Sensitivity assumed that 17 of the Debtors' 23 rigs have dayrates reduced by approximately 20 percent, and that dayrates will start low and increase slowly. PGN 185; 9/28/16 Hrg. Tr. at 34:12–35:20 (Fordyce Test.); PGN 216–217 (demonstrative of dayrates and utilization assumptions). Further, 13 rigs had utilization negatively revised, including removal of the L1115 altogether. *Id.* The Debtors' utilization assumptions are significantly lower in the Downside Sensitivity than in the Business Plan, and remain lower for a longer period of time with a much slower recovery. 9/27/2016 Hrg. Tr. at 15:21–16:1 (Stilley Test.). Further, compared to the Modified Plan, the Downside Sensitivity assumes certain contracts will be canceled, and allows additional idle time in between rig contracts. PGN 185; 9/27/2016 Hrg. Tr. at 16:2–6 (Stilley Test.). The Debtors and Mr. Fordyce believe the reduced dayrates are a reasonable and conservative assumption. *See* 9/28/16 Hrg. Tr. at 29:6–20, 43:17–44:16 (Fordyce Test.).

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[12] PGN 185 (comparing utilization and dayrates in Business Plan and Downside Sensitivity).

[13] PGN 180 and 183 (comparing capital expenditures in Business Plan and Downside Sensitivity).

72. The Downside Sensitivity's revised assumptions result in $770 million less in aggregate projected revenue and $591 million less in aggregate adjusted EBITDA than the Business Plan, reductions of 26 percent and 54 percent, respectively. PGN 219; 9/28/16 Hrg. Tr. at 28:13–25 (Fordyce Test.); 9/27/16 Hrg. Tr. at 32:16–33:15 (Stilley Test.).[14] The revised assumptions do not include reduced operating costs per rig which would likely occur in the downside scenario, so the decrease in revenue greatly impacts EBITDA. 9/28/16 Hrg. Tr. at 42:11–43:16 (Fordyce Test.). As Mr. Fordyce testified, a 50 percent decrease in EBITDA is a conservative assumption in comparison with the reduction typically seen in other downside analyses he has undertaken (20–30 percent). 9/28/16 Hrg. Tr. at 29:6–20, 43:17–44:16 (Fordyce Test.). Significantly, the amount of cash on hand under the Downside Sensitivity—$177 million cash at end of projection period and $143 million cash at the end of 2018—is in excess of required covenants. PGN 222; 9/28/16 Hrg. Tr. at 46:11–48:10 (Fordyce Test.).

O. The Modified Plan

73. After developing and testing the Downside Sensitivity, Paragon approached the Revolver Lenders and the Ad Hoc Group to negotiate changes to the Original Plan. 9/27/16 Hrg. Tr. at 33:16–21 (Stilley Test.). Negotiations commenced in the middle of July through about the first week of August. 9/27/16 Hrg. Tr. at 33: 22–34:4 (Stilley Test.). The Debtors were able to negotiate with the Revolver Lenders to reduce the minimum liquidity covenant from $110 million to $103 million, lower the

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[14] These overall reductions are evidenced by comparing PGN 173 at 18 (projecting $3.4 billion in operating revenue in Business Plan) with PGN 220 ($2.6 billion in Downside Sensitivity).

corresponding 60-day grace period amount from $95 million to $88 million, and adjust covenant holidays so that Paragon has no EBITDA-based covenants until 2019. PGN 213; 9/28/16 Hrg. Tr. at 22:18–23:25 (Fordyce Test.); 9/27/16 Hrg. Tr. at 34: 24–35:11 (Stilley Test.). The Revolver Lenders also agreed to delay the testing of the maximum net leverage ratio and minimum interest coverage ratios until first quarter 2019, instead of in 2018. PGN 213; 9/28/16 Hrg. Tr. at 22:18–23:25 (Fordyce Test.); 9/27/16 Hrg. Tr. at 34: 24–35:11 (Stilley Test.).

74. The Debtors also negotiated with the Ad Hoc Group to reduce the cash payment to the Ad Hoc Group by $60 million, from $345 million to $285 million, and to remove the deferred cash payments that were contemplated by the Original Plan. PGN 212–214 (summarizing terms of Modified Plan); 9/27/16 Hrg. Tr. at 35:12–22 (Stilley Test.); 9/28/16 Hrg. Tr. at 21:12–22:16 (Fordyce Test.). As compensation for giving up $60 million in cash in connection with the Modified Plan and the right to contingent payments, the Ad Hoc Group received an increase in their pro forma ownership of common shares (from 35 to 47 percent) and issuance of $60 million in unsecured New Notes. PGN 212; 9/28/16 Hrg. Tr. at 21:12–22:16, 105:17–106:22 (Fordyce Test.); 9/27/2016 Hrg. Tr. at 35:12–22 (Stilley Test.).

75. Paragon also negotiated with Noble to receive reimbursement for amounts paid under the Noble Settlement Agreement with a $5 million note instead of cash (the "**Amended Noble Settlement**"). PGN 213; 9/28/16 Hrg. Tr. at 25:6–20 (Fordyce Test.); 9/27/16 Hrg. Tr. at 36:7–14 (Stilley Test.).

76. The results of these negotiations are cushions against the covenants in the Amended and Restated Credit Agreement. Under the Modified Plan, the Debtors project that they will have minimum 67 percent net leverage, 122 percent interest coverage, and 137 percent liquidity cushions. PGN 224; 9/28/16 Hrg. Tr. at 50:25–52:13 (Fordyce Test.). Under the downside scenario, if the Debtors met all of the requirements, the Debtors would have minimum 10 percent EBITDA and 39 percent liquidity cushions. PGN 225; 9/28/16 Hrg. Tr. at 52:14–24 (Fordyce Test.); 9/27/2016 Hrg. Tr. at 35:7–11 (Stilley Test.). Furthermore, the Debtors' asserted, under the Modified Plan, that the Debtors will be able to refinance debts by 2019, well before they will be required to do so in 2021, and will have leverage and coverage ratios in line with Moody's Baa-rated companies by 2018 and near investment grade metrics by 2019. PGN 226; 9/28/16 Hrg. Tr. at 52:25–54:2 (Fordyce Test.).

77. In sum, the Debtors' asserted that the Modified Plan de-leverages the Debtors by eliminating $1 billion in debt, converts the Revolving Credit Facility into a term loan and extends its maturity by two years, and reduces the Debtors' interest expense by approximately half. Pursuant to the Modified Plan, the Debtors asserted that Paragon will emerge with approximately $379 million in cash. PGN 214; 9/28/16 Hrg. Tr. at 27:9–16 (Fordyce Test.). The Debtors believe that the Modified Plan also provides the Debtors more flexibility, and incorporates Paragon's year-to-date performance, including the outperformance on EBITDA and cash, recent contract updates, which have been both positive and negative, and the results of further negotiations with the Debtors' stakeholders including, among others, additional cash from the Ad Hoc Group and

certain covenant holidays. 9/28/16 Hrg. Tr. at 10:16–11:4, 26:13–24 (Fordyce Test.). In addition, under the Modified Plan, if all the targets were met, Paragon would have $487 million in cash at end of the projection period and $694 million of net debt at the end of projection period, which is down from just under $1.1 billion at emergence, reflecting scheduled amortizations and repayments under cash flow sweeps. PGN 221; 9/28/16 Hrg. Tr. at 45:24–46:8 (Fordyce Test.).

P. Ad Hoc Group's Contribution

78. The Debtors began negotiating with the Ad Hoc Group in the fall of 2015, before filing for bankruptcy. 9/27/16 Hrg. Tr. at 60:8–11 (Stilley Test.). Throughout the entire process, the Ad Hoc Group continued to work with Paragon in developing a plan and negotiating with the Revolver Lenders. 9/27/16 Hrg. Tr. at 60:12–14 (Stilley Test.). Even after Paragon developed the Downside Sensitivity, the Ad Hoc Group agreed to forgo $60 million in cash and other items, including the right to receive two potential payments which had been contingent on the Debtors' EBITDA levels in 2016 and 2017. PGN 212; 9/27/16 Hrg. Tr. at 60:15–18 (Stilley Test.); 9/28/16 at 21:12–22:16 (Fordyce Test.). They also assisted in negotiating an advantageous settlement with Noble. 9/27/16 Hrg. Tr. at 60:21–25 (Stilley Test.).

III. CONFIRMATION OF THE MODIFIED PLAN

79. The Debtors' seek confirmation of the Modified Plan including the Amended Noble Settlement. The Term Loan Agent objects to confirmation of the Modified Plan, contending that: (i) the Modified Plan is not feasible; (ii) the Term Loan Lenders are impaired under the Modified Plan; (iii) the Debtors may not reinstate the

Secured Term Loan; (iv) the Modified Plan was not proposed in good faith; and (v) the Modified Plan improperly provides for the payment of the unsecured noteholders' professional fees. The Term Loan Agent has withdrawn its prior objection to the Amended Noble Settlement. For the reasons fully set forth below, the Court will deny confirmation of the Debtors' Modified Plan.

80. A debtor must prove a chapter 11 plan's feasibility by a preponderance of the evidence. *In re T-H New Orleans Ltd. P'Ship*, 116 F.3d 790, 801 (5th Cir. 1997) (*citing In re Briscoe Enter., Ltd. II*, 994 F.2d 1160, 1165 (5th Cir. 1993)); *see also In re W.R. Grace & Co.*, 475 B.R. 34, 114 (D. Del. 2012) ("The debtor bears the burden of proof on this inquiry, and must show by a preponderance of the evidence that a reorganization plan is feasible."). Section 1129(a)(11) of the Bankruptcy Code codifies the feasibility requirement, permitting confirmation of a plan if "[c]onfirmation of the plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or any successor to the debtor under the plan . . . ." 11 U.S.C. § 1129(a)(11).

81. Section "1129(a)(11) does not require a guarantee of the plan's success; rather the proper standard is whether the plan offers a 'reasonable assurance' of success." *In re Indianapolis Downs*, 486 B.R. 286, 298 (Bankr. D. Del. 2013); *see also In re W.R. Grace & Co.*, 475 B.R. at 115 ("In making this finding, the bankruptcy court need not require a guarantee of success, but rather only must find that 'the plan present[s] a workable scheme of organization and operation from which there may be reasonable expectation of success.'") (citations omitted). Speculative prospects of failure cannot defeat feasibility. *See In re Drexel Burnham*, 138 B.R. 723, 762 (Bankr. S.D.N.Y. 1992) ("The mere

prospect of financial uncertainty cannot defeat confirmation on feasibility grounds . . . .") (citing *In re U.S. Truck Co.*, 47 B.R. 932, 944 (E.D. Mich. 1985), *aff'd*, 800 F.2d 581 (6th Cir. 1986)).

82. Courts consider various factors in assessing the feasibility of a plan of reorganization, including: (i) the adequacy of the debtor's capital structure; (ii) the earning power of its business; (iii) economic conditions; (iv) the ability of the debtor's management; (v) the probability of the continuation of the same management; and (vi) any other related matters which determine the prospects of a sufficiently successful operation to enable performance of the provisions of the plan. *See In re Greate Bay Hotel & Casino, Inc.*, 251 B.R. 213, 226–27 (Bankr. D.N.J. 2000). The "Debtors are not required to view [their] business and economic prospects in the worst possible light." *In re Am. Consol. Transp. Companies, Inc.*, 470 B.R. 478, 491 (Bankr. N.D. Ill. 2012). Rather, "[w]here the projections are credible, based upon the balancing of all testimony, evidence, and documentation, even if the projections are aggressive, the court may find the plan feasible." *In re T–H New Orleans Ltd. P'ship*, 116 F.3d at 802.

a. Balance Sheet Solvency

83. Contrary to the Term Loan Agent's assertion, balance sheet solvency at emergence is not a feasibility requirement. Rather, solvency is merely a factor considered where relevant. *See In re W.R. Grace & Co.*, 475 B.R. at 163 n.137. However, it is not necessary for the Court to consider the extensive evidence submitted by the parties as to balance sheet solvency (or insolvency) in this case as the Court finds that, assuming the

Debtors were balance sheet solvent upon confirmation, the Modified Plan is not feasible for the reasons set forth below.

b. Capital Expenditure Assumptions are Reasonable

84. The Term Loan Agent argues that the capital expenditure assumptions contained in the Business Plan are unrealistic. The Debtors posit that the capital expenditures they have allotted in the Business Plan are reasonable, given the well-maintained current state of their rigs, their careful formulation and review of each potential upcoming project, and their recent track-record of keeping costs down. The Court has determined that the evidence presented at the Confirmation Hearings demonstrates that the Debtors' capital expenditure assumptions are well-reasoned and credible, and that such soundness further contributes to the feasibility of the Modified Plan.

85. The Debtors' management team spends considerable time managing capital expenditures throughout the year. 6/23/16 Hrg. Tr. at 11:13–25 (Stilley Test.). The evidence shows that Paragon's need for capital expenditures is highly dependent on the condition of each particular drilling rig, inventory of capital spares on hand, and the requirements of any particular customer for a specific new contract: all factors the Term Loan Agent's witnesses apparently disregarded. 9/27/16 Hrg. Tr. at 42:1–43:25, 49:11–19 (Stilley Test.). Unlike Mr. Leand, who arbitrarily tacked on an extra $10–$15 million in additional capital expenditures for each of Paragon's rigs (9/30/16 Hrg. Tr. at 92:18–94:22 (Leand Test.)), the Court finds that Paragon's management team

regularly projects its capital expenditures on a rig-by-rig basis and considered all relevant factors.

86. Moreover, the Court determines credible the evidence that the management team, along with the operations team and engineering group led by Mr. Charlie Yester, carefully formulates the capital expenditure budget and reviews each proposed capital expenditure project. 6/21/16 Hrg. Tr. at 213:9–18 (Stilley Test.); 9/27/16 Hrg. Tr. at 42:1–12 (Stilley Test.). For each rig, Paragon considers past expenditures, current conditions, idle time, and anticipated projects. 9/27/16 Hrg. Tr. at 42:1–12 (Stilley Test.). The Debtors have also included sufficient funds in the capital expenditure budget for reactivation costs. 6/23/16 Hrg. Tr. at 16:15–18 (Stilley Test.). In addition to the annual budgeting process, Mr. Stilley and Mr. Yester also review the capital expenditure budget on a monthly basis, and Mr. Stilley must personally approve any capital expenditures in excess of the budget. 6/23/16 Hrg. Tr. at 12:21–13:4 (Stilley Test.); 9/27/16 Hrg. Tr. at 42:13–21, 43:1–7 (Stilley Test.). Further, the Debtors have removed discretionary capital expenditures from their budget in 2016 and 2017 in order to reduce unnecessary capital expenditures, and have aggressively negotiated with shipyards and suppliers during the downturn in order to further reduce capital expenditures. 6/23/16 Hrg. Tr. at 19:19–23 (Stilley Test.); 9/27/16 Hrg. Tr. at 43:8–18, 44:3–9 (Stilley Test.). As a result of aggressive management, including the implementation of cost reduction and efficiency initiatives over the past 18 months (6/23/2016 Hrg. Tr. at 19:24–20:4 (Stilley Test.)), capital expenditures in 2015, and so far in 2016, were lower than expected. 6/23/16 Hrg. Tr. at 19:24–20:10 (Stilley Test.).

87. The Court finds that the projected capital expenditures in the Business Plan are not only supported by management's process, but also by empirical fact. From 2010 to 2014—a period in which Noble was preparing the rigs for potential sale or spin-off—Noble spent approximately $535.5 million on capital expenditures for the rigs that are in the Business Plan. 9/28/16 Hrg. Tr. at 56:5–59:21 (Fordyce Test.); PGN 228. For the period from 2015 to 2019, the Debtors anticipate spending approximately $496.4 million on the same rigs, only 7 percent lower than Noble spent during the years leading up to the Spinoff. 9/28/16 Hrg. Tr. at 56:5–59:21 (Fordyce Test.); PGN 228. This small reduction is reasonable and supportable by the availability of spare equipment, management's focus on eliminating discretionary capital expenditures, the condition of Debtors' rigs following the Spinoff, and lower steel and shipyard labor prices. 9/28/16 Hrg. Tr. at 56:18–25, 60:22–61:9 (Fordyce Test.). Moreover, the amount of money Noble spent during a prolonged upturn was unusually high, as it was preparing rigs for a potential sale. 9/27/16 Hrg. Tr. at 45:23–46:3 (Stilley Test.).

88. Because Noble already updated the rigs, including spending on long-lived capital equipment, Paragon will not have to spend as much money going forward. *Id*. at 46:4–12; 9/28 Hrg. Tr. at 56:21–23 (Fordyce Test.). The Debtors have chosen to reactivate their best-maintained rigs, *i.e.*, those that have been in the shipyard fairly recently, have been recently upgraded, or were operating most recently. 6/23/16 Hrg. Tr. at 18:5–18 (Stilley Test.). The Debtors' ample supply of spare equipment, including top drives, certified blowout preventers, and motors and generators, will also help reduce capital

expenditure outlays associated with reactivation. 6/23/16 Hrg. Tr. at 16:23–18:1 (Stilley Test.).[15]

89. The Court does not agree with the Term Loan Agent's arguments regarding capital expenditures. Indeed, the Court concludes that Mr. Leand did not inspect the Debtors' rigs (6/30/16 Hrg. Tr. at 143:11–12, 145:5–6 (Leand Test.)), did not take into account the Debtors' inventory of capital spares and other equipment (6/30/16 Hrg. Tr. at 18:24–19:1 (Leand Test.)), and failed, as described below, to calculate accurately the amounts budgeted for capital expenditures in the Debtors' projections by ignoring the amounts already included for capital spares allocations, and made other errors.

90. Mr. Leand alleges that the Debtors need to spend an additional $150 million already included in additional capital expenditures. 9/30/16 Hrg. Tr. at 77:21–78:2 (Leand Test.). Putting aside the fact that this assertion ignores the condition of the Debtors' rigs and existing inventory, the supposed gap is largely bridged by including the amounts the Debtors have already allocated in their Business Plan (and Downside Sensitivity) to other capital expenditures and capital spares. Mr. Leand admitted that, in calculating the difference between what he thought needed to be spent and the Debtors' budget for 2017, he failed to count a large portion, approximately $13 million, already included in the Debtors' Downside Sensitivity. 9/30/16 Hrg. Tr. at 97:20–100:1 (Leand

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[15] The Term Loan Agent argued that the Debtors' fleet is "old and cold" as the average age of each rig is approximately 34 years, and only the two Prospector rigs are relatively new. While the Court acknowledges that there may be some adverse effect to the age of a rigs, based on the type of work the Debtors perform, it is not of significant merit to impact the Debtors' Modified Business Pan beyond what is accounted for in the capital expenditure projections. *See, e.g.*, 6/21/16 Hrg. Tr. at 187:4–20 189:24–190:12 (Stilley Test.).

Test.) (discussing PGN 181 at 156:7 (showing total capital expenditures for 2017 and the subset of capital expenditures used by Mr. Leand)). Extrapolating that error for the entire Business Plan projection period (2016–2019), Mr. Leand fails to account for approximately $60 million already included in the Debtors' Business Plan for capital expenditures. PGN 228 (calculating total Capital Spares/Other for 2016–2019 shown in red box). Having failed to take already budgeted amounts into consideration, in addition to his failure to account for spares in inventory (6/30/16 Hrg. Tr. at 18:24–19:1 (Leand Test.)), the Court determines Mr. Leand's assumption that it is necessary to add $10–$15 million to the capital expenditure budget for each rig is not supported by the evidence and is not credible.

91. Mr. Leand also added $10–$15 million to the Debtors' projected capital expenditure estimates for special surveys and $3 million for intermediate surveys. 6/30/2016 Hrg. Tr. at 135:21–136:5 (Leand Test.). However, the Court does not believe that such significant capital expenditures will be required to perform the SPS surveys, because it agrees with the evidence presented at the Confirmation Hearings that the Debtors' rigs have been properly maintained. 6/23/2016 Hrg. Tr. at 15:25–16:9 (Stilley Test.). The Court notes that the Debtors have also been conservative in their SPS survey estimates and the Debtors' budget sets aside sufficient funds for SPS surveys. 6/21/2016 Hrg. Tr. at 211:24–212:4, 213:6–8 (Stilley Test.).

92. The Court also does not find support in the record for Mr. Leand's assertion that 10 rigs need to be scrapped because the Debtors lack adequate capital to keep them in service. The Debtors have set forth sufficient evidence to prove that those rigs have

been thoroughly assessed and capital expenditures have been budgeted accordingly. 6/21/2016 Hrg. Tr. at 206:22–207:17 (Stilley Test.); 9/27/2016 Hrg. Tr. at 43:17–25 (Stilley Test.). Further, Mr. Stilley testified that the Debtors have sufficient capital to put these rigs back to work. 6/21/2016 Hrg. Tr. at 209:5–16 (Stilley Test.); 9/27/2016 Hrg. Tr. at 43:9–16 (Stilley Test.).

93. The Debtors perform both routine maintenance and preventative maintenance on an ongoing basis. 6/21/2016 Hrg. Tr. at 147:25–148:13 (Stilley Test.). Five years prior to the Spinoff, Noble invested $1.8 billion in upgrades and maintenance for its rigs, approximately $536 million of which was spent on rigs that will form the basis of the Debtors' fleet going forward. 6/21/2016 Hrg. Tr. at 149:2–9, 152:11–13 (Stilley Test.). The Court finds that, as both Mr. Stilley and Mr. Fordyce have testified, the Debtors' capital expenditure numbers are conservative and include adequate allotments of capital for spending throughout the projection period. 9/27/16 Hrg. Tr. at 44:9–22, 50:8–14 (Stilley Test.); 9/28/16 Hrg. Tr. at 61:10–16 (Fordyce Test.); PGN 238 (comparing historical and projected capital expenditures by rig); PGN 228 (showing historical capital expenditures of Noble-era rigs). Thus, based on the Debtors' processes, the condition of the Debtors' rigs, the capital spares inventory on hand, and the budget set aside for the rigs in the future, the Debtors are more than capable of maintaining the rigs under the Business Plan, thereby supporting the feasibility of the Modified Plan.

B. The Downside Sensitivity Is Not Achievable Because Projected Utilization and Dayrates Are Not Achievable; Paragon Will Run Out of Cash

a. The Adverse Effect of the Oversupply of Rigs

94. The current market environment of an overhang of rigs has put downward pressure on current and future dayrates. (TLA219; 6/29/2016 Hrg. Tr. 207:8-16, 212:11-17 (Leand Test.).) Both the supply of rigs and the price of oil[16] correlate with dayrates: dayrates are generally historically inversely correlated with an over-supply of rigs, meaning that if the market has an over-supply of rigs, dayrates fall; the price of oil is generally historically positively correlated with dayrates, meaning that as the price of oil falls, dayrates fall. (6/29/2016 Hrg. Tr. 206:13-207:7 (Leand Test.); 9/29/2016 Hrg. Tr. 162:25-165:22 (Leand Test.); TLA609; TLA610; 611.) However, both rig utilization (*i.e.*, whether there is an over-supply of rigs) and oil prices historically work together to

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[16] During the Confirmation Hearing, the Court heard testimony from two economists regarding the price of oil:

Mr. David Pursell from Tudor Pickering Holt & Co., a private energy-focused investment bank, forecasted West Texas Intermediate prices above $80/bbl for 2017 through 2020. (PGN135 at ¶ 26-27). At the time of his testimony, Mr. Pursell projected that oil would be approximately $80/bbl in the fourth quarter of 2016. (6/23/2016 Hrg. Tr. 52:10-55:11 (Pursell Test.)).

Philip Verleger, an economist who writes frequently about oil prices and is one of the regular contributors of forecasts for oil prices to the publication Energy and Metals Consensus Economic forecast, reached the same conclusion about the price of oil in future years as Prof. Fischel did (that oil would be in a range of $50 to $55 per barrel), based on the econometric model that Dr. Verleger uses to forecast price. (6/30/2016 Hrg. Tr. 202:20-203:1 (Verleger Test.); TLA308 ¶36; PGN121; TLA270; TLA271.) At the time of his testimony, Dr. Verleger projected that oil would remain at approximately $50/bbl through the end of 2017. (6/30/2016 Hrg. Tr. 172:25-173:6 (Verleger Test.).)

Although both experts use sophisticated methodologies, the Court is not optimistic that oil prices will reach these projections. The Court believes that oil prices are crucial to the recovery of the off-shore drilling business. To date, oil prices remain below the more conservative forecast set forth by Dr. Verleger. *See* http://oilprice.com/. More specifically, on November 15, 2016, Brent Crude Oil opened at $44.70. http://oilprice.com/commodity-price-charts?1&page=chart&sym=CB*1. At the least, however, the Court finds Dr. Verleger's conservative projections to be more persuasive than Mr. Pursell's self-described outlier projections.

influence dayrates; one has to look at both oil prices and rig supply dynamics together when considering the health of the offshore drilling market in terms of expected dayrates. (9/29/2016 Hrg. Tr. 165:23-166:24 (Leand Test.); TLA609; TLA610; TLA611.) In light of the vast oversupply of rigs in the market at this time (*see* paragraphs 49-51, *supra*), the market in which Paragon operates will "continue to be a challenging market for a longer period of time." (9/29/2016 Hrg. Tr. 166:25-167:24 (Leand Test.); TLA525; TLA609; TLA610; TLA611; TLA619.) Indeed, operators are going to cash-flow break even dayrates to keep their rigs operating. (6/29/2016 Hrg. Tr. 205:13-17 (Leand Test.); *see* TLA396 at 11.)

95. Paragon believes a recovery will begin in 2017 due to the highly cyclical nature of the offshore drilling industry. (9/27/2016 Hrg. Tr. 8:15-25 (Stilley Test.). Mr. Stilley believes that flat dayrates are not possible due to this "extreme cyclicality," but fails to consider the supply overhang. (6/21/2016 Hrg. Tr. 206:6-15 (Stilley Test.).) Mr. Stilley acknowledged that utilization of marketed rigs (excluding newbuilds) is 64.7%, and he does not expect a decrease in the supply of rigs over the next 12 months. (9/27/2016 Hrg. Tr. 77:22-78:5, 79:23-80:1, 81:12-15 (Stilley Test.).) Mr. Leand's analysis of the supply/demand imbalance shows that it will likely take 38 months to absorb the oversupply of rigs, meaning that it will take 3.2 years from when the recovery begins before the oversupply is ended. (9/30/2016 Hrg. Tr. 118:5-119:16 (Leand Test.); TLA607; TLA609; TLA610; TLA611; TLA619.) Given the current and ongoing rig imbalance, there is no reason to believe that dayrates will increase. (9/29/2016 Hrg. Tr. 209:2-13, 211:1-4 (Leand Test.).) Therefore, Mr. Leand holds dayrates flat not because he believes that they

will be purely flat, but because the market is so vastly oversupplied that it makes sense to hold dayrates flat. (*Id.* at 162:25-164:11, 211:5-212:2 (Leand Test.); TLA610.) Furthermore, Mr. Leand reviewed third party analyst reports to test that opinion, and none of those analysts called for dayrates to rise. (9/29/2016 Hrg. Tr. 212:10-213:11 (Leand Test.); TLA549; TLA551; TLA546; TLA351 at p. 47.)

96. New rigs also create price ceilings for old rigs. A new rig coming onto the market and dropping their day rates to get business creates a ceiling for Paragon's rigs dayrates. (6/22/2016 Hrg. Tr. 44:3-45:17 (Stilley Test.).)

97. Paragon has acknowledged the downward trend of dayrates. Paragon's 10-K acknowledges that there is a risk that an oversupply of jackup rigs and floaters may lead to a reduction in dayrates and demand for their rigs, which could have a material adverse impact on their profitability. (6/29/2016 Hrg. Tr. 205:23-206:3 (Leand Test.).) Mr. Fordyce's notes from a March 2016 meeting acknowledge that "more rigs [are] now competing[,] rates down." (TLA294; 6/23/2016 Hrg. Tr. 160:10-161:1 (Fordyce Test.).)

b. Paragon Is Not Presently Achieving its Downside Dayrates

98. In Paragon's Downside Sensitivity, Paragon revised its projected utilization and dayrates. Nevertheless, Paragon's dayrate and utilization assumptions in the Downside Sensitivity are aggressive and not-achievable. (9/29/2016 Hrg. Tr. 86:6-21 (Burke Test.).) Paragon's Downside Sensitivity assumes rising dayrates throughout the Projection Period, and although the rise varies by region, an increase is being projected across the board. (9/29/2016 Hrg. Tr. 206:1-8 (Leand Test.); TLA601A.)

99. For example, C463 is projected to have dayrate increases over 40 percent during the Projection Period, starting at $85,000 per day, rising to $100,000, $115,000 and then $120,000. (9/29/2016 Hrg. Tr. 206:9-22 (Leand Test.); TLA601A.) The Downside Sensitivity also projects increasing dayrates for short-term duration contracts, which Mr. Leand opined are too aggressive based on market dynamics. (9/29/2016 Hrg. Tr. 206:23-207:8 (Leand Test.); TLA601A.) Mr. Leand observed that, based on his review of Paragon's bid-log reports with respect to tendering activity, the dayrates that Paragon tendered were actually lower than those projected in the downside. (9/29/2016 Hrg. Tr. 208:17-209:1 (Leand Test.); PGN185.)

100. In fact, during trial, Paragon admitted that they were bidding for projects below the dayrates suggested in the Downside Sensitivity. (9/27/2016 Hrg. Tr. 118:24-119:9, 119:14-20, 136:2-15 (Stilley Test.); TLA621 at 129:19-130:5 and 200:23-201:18 (Tietz Dep.); TLA310 at 65; TLA353.)

101. Mr. Leand also opined that Paragon's step-up assumptions on dayrates in the Downside Sensitivity could not be achieved because the difficult market would continue with an oversupply of rigs. (9/29/2016 Hrg. Tr. 209:2-13 (Leand Test.).) Furthermore, based on Mr. Leand's analysis of the market, Paragon should have taken a more conservative approach to dayrates and that parts of the projections did not make sense. (9/29/2016 Hrg. Tr. 209:14-20 (Leand Test.).)

102. Neither Paragon nor Lazard reviewed any third party reports corroborating Paragon's outlook on dayrates assumptions for the Downside Sensitivity. (6/22/2016 Hrg. Tr. 177:4-8 (Stilley Test.); 9/28/2016 Hrg. Tr. 66:21-67:7 (Fordyce Test.).) Nor has

Paragon conducted an analysis or reviewed any analysis explaining how the supply overhang would disappear after 2017 causing dayrates to recover. (6/22/2016 Hrg. Tr. 175:2-13 (Stilley Test.).) Lazard did not review the average dayrates or projected dayrates for 2016 through 2018 that were available in the four-page excerpt from the Morgan Stanley report that Mr. Fordyce purportedly relied on. (PGN034; 6/23/2016 Hrg. Tr. 176:16-178:7 (Fordyce Test.).) Mr. Fordyce did not conduct this exercise in connection with the Downside Sensitivity, even though he was challenged during his testimony in the First Confirmation hearings for his failure to do so. (9/28/2016 Hrg. Tr. 85:17-88:17 (Fordyce Test.).)

103. When evaluating dayrates coming out of past downturn cycles, Mr. Fordyce did not examine the supply/demand imbalance for jackups at the trough prices, the supply/demand balance for oil at trough prices, nor the status of producers' explorations and productions at the trough date, despite the fact that Mr. Tietz looks at supply and demand data all the time. (9/28/2016 Hrg. Tr. 117:1-25 (Fordyce Test.); PGN 227; TLA621 at 57:3-19 (Tietz Dep.).) Nor did Mr. Fordyce examine any economic factors to see how the current market compared to past downturn markets other than the price of oil in conducting his analysis. (9/28/2016 Hrg. Tr. 118:1-119:5 (Fordyce Test.); PGN 227.)

104. Yet, third party analyst reports, such as the August 2016 Tudor Pickering Holt report, whose analysis Mr. Fordyce "particularly like[s]", and on which Mr. Leand relied (among numerous reports) in his analysis of Paragon's dayrates and assumptions, have stated that dayrate momentum was "a long way away" and showed "no signs of

notable sustained recovery." (9/29/2016 Hrg. Tr. 212:10-18 (Leand Test.); 6/23/2016 Hrg. Tr. 139:16-19 (Fordyce Test.); TLA549.) Increase in drilling activity, tendering activity or tendering for more long-term contracts has not yet occurred. (6/29/2016 Hrg. Tr. 207:17-208:5 (Leand Test.).) Mr. Leand also relied on the June 2016 Nordea report which stated that dayrates would "continue to decline" until "oversupply" was "resolve[d]." (9/29/2016 Hrg. Tr. 212:19-23 (Leand Tr.); TLA551.) The D&B Markets report from August 2016, which was relied on by Mr. Leand, found that dayrates were continuing a downward trend due to the oversupply, they "would not be surprised to see rates deteriorate further towards operating cash break even," that "depressed dayrates and low utilization" were likely to continue, the "the significant oversupply will not improve in the next three years," and dayrates would remain under pressure. (9/29/2016 Hrg. Tr. 212:24-213:11 (Leand Test.); TLA546.) Mr. Fordyce admitted that, like Mr. Leand, Morgan Stanley was holding dayrates flat through 2018. (9/28/2016 Hrg. Tr. 88:18-89:17 (Fordyce Test.); TLA351 at p.47.) Other consensus analysists including Arctic Clarkson, D&B, Nordea and Pareto are also predicting flat dayrates. (6/29/2016 Hrg. Tr. 208:6-210:7; Leand Test); TLA219.) Mr. Leand agreed with the analysts' views of dayrates and found that there was a "consistent view throughout the market." (9/29/2016 Hrg. Tr. 212:12-15 (Leand Test.).) Mr. Leand testified that he looked and did not find a single analyst that took a contrary view. (*Id.* 212:16-18.)

c. Paragon's Utilization Assumptions Are Too Aggressive

105. As of the second quarter of 2016, utilization of effective supply is 64.7 percent,[17] with 177 standard jackups, 205 high specification jackups, 118 jackups scheduled for delivery, and a spare capacity of 63 standard jackup rigs and 66 high specification jackup rigs. (9/27/2016 Hrg. Tr. 77:10-13, 77:22-78:21, 79:23-80:1 (Stilley Test.); TLA377 at 34.) More than one-third of standard spec jackups are unutilized. (9/27/2016 Hrg. Tr. 78:18-21 (Stilley Test.).) The contracted supply of rigs with future contracts is at 40 percent. (9/27/2016 Hrg. Tr. 78:22-79:17 (Stilley Test.); TLA377 at 34.) Any rigs coming off contract in 2017 will become part of the supply of rigs searching for new business. (9/27/2016 Hrg. Tr. 80:5-23 (Stilley Test.); TLA377 at 34.) Moreover, Mr. Stilley agreed that the supply of rigs will not decrease over the next year. (9/27/2016 Hrg. Tr. 81:12-15 (Stilley Test.).)

106. At the First Confirmation Hearing, Mr. Stilley testified that the market was "definitely at the trough," very close to turning around, and Paragon's customers were discussing starting delayed projects. (6/21/2016 Hrg. Tr. 192:12-13, 192:17-193:1.) Since that time, Paragon's fleet utilization declined to 38 percent for the second quarter of 2016, compared to 53 percent for the first quarter of 2016. (9/28/2016 Hrg. Tr. 98:15-98:21 (Fordyce Test.); TLA392.) Utilization of Paragon's marketed floating rig fleet declined to 35 percent in the second quarter of 2016, compared to the 68 percent utilization achieved in the first quarter of 2016. The decrease in marketed utilization reflected the reduced

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[17] Effective supply means rigs that are in the market place, not rigs that are sitting in the shipyard waiting to be completed. (9/27/2016 Hrg. Tr. 78:1-5 (Stilley Test.).)

number of operating days for MSS1 and MSS2, which completed contracts during the second quarter. (9/28/2016 Hrg. Tr. 99:19-100:5 (Fordyce Test.); TLA392.) Utilization of Paragon's marketed jackup rig fleet declined to 39 percent in the second quarter of 2016, compared to the 51 percent utilization achieved in the first quarter of 2016. (9/28/2016 Hrg. Tr. 100:20-101:6 (Fordyce Test.); TLA392.)

107. In its Q-2 2016 earnings call, Paragon stated "the industry dynamic has continued to worsen for offshore drillers. During the quarter, there were additional contract cancellations among our competitors and very few new contracts. This is not surprising, as capital spending for E&P is still contained." (9/28/2016 102:3-103:1 (Fordyce Test.); TLA393.)

108. At the June Confirmation Hearing, Mr. Stilley stated that the market had hit bottom and Paragon's customers were "optimistic." (6/22/2016 Hrg. Tr. 142:2-10 (Stilley Test.).) On July 28, 2016, Mr. Tietz made a presentation to the Board about the state of the jackup market utilization, backlog and supply and demand. (TLA377 at 34.) As of June 2016, one third of the standard spec jackups did not have contracts, were not working and were either warm or cold stacked. (9/27/2016 Hrg. Tr. 78:12-17 (Stilley Test.); TLA377 at 34.)

109. Paragon noted that, according to Wells Fargo, global jackup utilization was down to 70% in October 2015. (6/22/2016 Hrg. Tr. 91:21-92:3 (Stilley Test.); TLA045.) According to IHS Petrodata—which Mr. Tietz described as "an expert" in rig activity and whose information he had "no reason to doubt" is correct – total utilization for jackups worldwide decreased by one percent in July to an average of 60 percent. (TLA621 at

63:19-24, 65:23-25, 68:6-15 (Tietz Dep.); TLA342.) As of July, 179 newbuild rigs were on order, planned and under construction worldwide, including 114 jackups. (TLA621 at 68:17-25 (Tietz Dep.); TLA342.) Only 25 percent of the newbuilds have contracts already in place, and only 11 percent of the newbuild jackups have a future commitment. (TLA621 at 69:1-18 (Tietz Dep.); TLA342.) Mr. Tietz acknowledged that IHS Petrodata reported jackup utilization in July 2016 was 71.6 percent compared to 82.5 percent in July 2015. (TLA621 at 64:19-65:25 (Tietz Dep.); TLA342.)

110. Despite the slowdown, under the Downside Sensitivity, Paragon assumes that utilization will be in excess of 94% throughout the Projection Period. (9/29/2016 Hrg. Tr. 195:23-196:9 (Leand Test.); TLA601A.) The Downside Sensitivity projections assumes a win rate in excess of Paragon's prior performance and the market overall. (9/29/2016 Hrg. Tr. 195:23-196:9 196:10-16 (Leand Test.).)

111. Mr. Leand reviewed and analyzed the total marketed utilization rates in the June 25, 2016 Morgan Stanley report, which projected floater and jackup utilization has fallen to levels not seen since the 1980s, with floater utilization at a trough of 65% in 2016 and 2017 and 70% in 2018, and jackup utilization falling to 69% in 2016 followed by an uptick to 74% in 2017 and 2018. (9/29/2016 Hrg. Tr. 196:17-197:10, 197:12-17 (Leand Test.); TLA540 at p. 5.) Mr. Leand saw that the report had an underlying supply element and their utilization calculation included a number of rigs leaving the market which would impact utilization. (9/29/2016 Hrg. Tr. 197:19-198:3 (Leand Test.); TLA540.) Mr. Leand reviewed estimates prepared by Morgan Stanley which estimated that total marketed utilization for 2016 at 69% and projected total marketed utilization at 74% from

2017 through 2019. (9/29/2016 Hrg. Tr. 198:24-199:7 (Leand Test.); TLA540 pp. 5, 41.) Mr. Leand opined that Morgan Stanley's report likely reflected the analyst consensus views of the market, which was also consistent with Leand's view. (9/29/2016 Hrg. Tr. 199:24-200:7 (Leand Test.).)

112. Mr. Leand also analyzed other analyst utilization projections from 2016 to 2018, which showed utilization as relatively flat at 62 to 65 percent. (9/29/2016 Hrg. Tr. 213:19-214:1, 214:11-14 (Leand Test.); TLA562.) These analysts were not projecting anywhere close to the nearly 100% utilization Paragon is projecting for its fleet. (9/29/2016 Hrg. Tr. 214:24-215:1 (Leand Test.); TLA562.)

113. Under the Downside Sensitivity, Paragon expects to continue working in the North Sea, the Middle East, India, West Africa, and Mexico.

114. **The North Sea:** Under the Downside Sensitivity, Paragon projects that it will operate almost half their rigs in the North Sea, despite the fact that the region lost two rigs over the period. (9/29/2016 Hrg. Tr. 156:24-157:5 (Leand Test.); TLA529.) Paragon projects nine rigs will secure contracts in the North Sea by 2018. (9/29/2016 Hrg. Tr. 200:10-18 (Leand Test.); TLA601A.) Yet, Mr. Leand opined that Paragon will have difficulty meeting this projection in this market, given that there is not much growth in demand anticipated. (9/29/2016 Hrg. Tr. 198:6-7, 198:12-23, 200:10-18 (Leand Test.); TLA540 p. 41; TLA601A.) Moreover, dayrates for jackups have fallen in the North Sea. (TLA621 at 60:7-10 (Tietz Dep.).) There are "very few" long-term jackup contracts in the North Sea. (6/21/2016 Hrg. Tr. 160:20-161:2 (Stilley Test).)

115. Paragon's projections in the North Sea are aggressive. Based on a historic analysis, as well as the current status of Paragon's rigs, there's no reason to believe that Paragon is going to be able to outperform the market. (TLA152; 6/29/2016 Hrg. Tr. 192:17-194:11 (Leand Test.).)

116. **The Middle East:** The Middle East comprises of Qatar and the UAE. (6/29/2016 Hrg. Tr. 197:21-23 (Leand Test.).)[18] The Middle East typically requires performance bonds for contracts. (TLA621 at 92:7-12 (Tietz Dep.).)

117. The Middle East market is vastly over-supplied and has a lot of attention from many drilling companies. The supply issues will continue to linger there and be a very competitive market. (TLA197; 6/29/2016 Hrg. Tr. 200:9-16 (Leand Test.).) For example, at the First Confirmation Hearing, Mr. Leand testified that 19 rigs were not contracted for in the Middle East as of May 2016 and that this number will increase to 32 by the end of 2017. (TLA197; 6/29/2016 Hrg. Tr. 198:25-199:7 (Leand Test.).) Out of 90 rigs that obtained contracts since June 2014, only three of them went to idle rigs that were built post-1986, and only one went to an idle rig that was built pre-1986. (TLA299; 6/29/2016 Hrg. Tr. 137:9-139:1 (Leand Test.).)

118. Paragon has five rigs in the Middle East, with three projected to have contracts throughout virtually the entire Projection Period under the Downside Sensitivity. (PGN 185.)

[18] Saudi Arabia is not within Paragon's operating plan. (6/29/2016 Hrg. Tr. 197:24-198:4 (Leand Test.).)

119. The Morgan Stanley four page excerpt on which Mr. Fordyce relied shows that the rig count in the Middle East will stay flat in 2016, increase by one rig in 2017 and then flat again in 2018. (PGN34; 6/23/2016 Hrg. Tr. 181:23-182:9 (Fordyce Test.).) Lazard did not speak with anyone in the Middle East about Paragon's prospects for contracts and relied on general discussions with senior management. (6/23/2016 Hrg. Tr. 167:16-21 (Fordyce Test.).) Nor did Lazard look at any IHS Petrodata figures or data about the competitive environment or relationship with customers. (*Id*. at 168:9-15.)

120. Paragon's projections for the Middle East are also too aggressive, as they fail to account for the competition in that marketplace and the limited growth expected to occur there.

121. **India:** Paragon's current customer in India is Dynamic Drilling, which contracts out Paragon's rigs to ONGC; British Gas is a potential customer. (TLA621 at 45:10-19 (Tietz Dep.).) Paragon currently has three rigs working in India on long term contracts. (6/21/2016 Hrg. Tr. 189:22-190:3 (Stilley Test.).) No new contracts are projected through July 2017. (6/29/2016 Hrg. Tr. 203:5-13 (Leand Test.).) As of September 27, 2016, Paragon received no tenders for India. (9/27/2016 Hrg. Tr. 94:4-15 (Stilley Test.).)

122. **West Africa:** The West Africa region comprises of the entire coast to South Africa. (6/29/2016 Hrg. Tr. 200:17-19 (Leand Test.).) At the First Confirmation Hearing, Mr. Leand testified that the utilization for pre-1990 jackups is approximately 33%. (TLA199; 6/29/2016 Hrg. Tr. 201:1-3 (Leand Test.).) As of May 2016, there were 15 uncontracted rigs in West Africa. The number will increase to 20 by the end of 2017.

(TLA199; 6/29/2016 Hrg. Tr. 201:14-19 (Leand Test.).) Most of the tender activities have been pushed into the second part of 2017. (TLA199; 6/29/2016 Hrg. Tr. 201:20-23 (Leand Test.).) Since June 2016, two rigs became uncontracted West Africa, showing some degradation in the market over the period from June through September. (9/29/2016 156:3-12 (Leand Test.); TLA529.)

123. Paragon projections in West Africa are unrealistic because it is a difficult market for customers due to the political environment and taxes. (6/21/2016 Hrg. Tr. 190:13-21 (Stilley Test.).) It is an extremely difficult and competitive operating environment. (TLA199; 6/29/2016 Hrg. Tr. 201:24-202:7 (Leand Test.).)

124. There is not a reasonable likelihood that Paragon will obtain two contracts in West Africa within the next year. (TLA152; 6/29/2016 Hrg. Tr. 202:14-203:4 (Leand Test.).) Mr. Stilley agrees that the overcapacity remains in Africa. (9/27/2016 Hrg. Tr. 94:25-95:4 (Stilley Test.).) "The jackup sector [in West Africa] continues to stagnate with . . . further rigs becoming available in the already oversaturated market," and Mr. Tietz has not "seen a contract award in West Africa . . . ." (TLA621 69:19-70:8 (Tietz Dep.); TLA 342.)

125. **Mexico:** In July 2016, the total rig supply in Mexico was 45 rigs, with 29 contracted. (TLA621 at 66:25-67:11 (Tietz Dep.); TLA342.) At the First Confirmation Hearing, Mr. Leand testified that by the end of 2016, 25 units will not be contracted in Mexico. 35 units will not be contracted by the end of 2017, including new builds. (TLA195; 6/29/2016 Hrg. Tr. 195:3- 196:4 (Leand Test.).) Since June 2016, six rigs became

uncontracted, showing some degradation in the market. (9/29/2016 156:3-17 (Leand Test.); TLA529.)

126. Paragon has needed to post performance bonds in Mexico. (9/27/2016 Hrg. Tr. 102:12-15 (Stilley Test.).)

127. PEMEX is the Mexican state oil company. (6/29/2016 Hrg. Tr. 196:10-11 (Leand Test.).) PEMEX mandated that it will not take rigs that are more than 10 years old, although may potentially make exceptions; given PEMEX's position, Paragon's projections are unreasonable. (6/29/2016 Hrg. Tr. 196:12-197:3 (Leand Test.).) Furthermore, PEMEX views itself as over supplied and is doing whatever they can to shed tonnage/assets. (*Id.* at 197:10-18.) PEMEX focused almost entirely on Mexican companies to be the supplier of the rigs. (*Id.* at 197:18-20.)

128. Paragon projects getting contracts in the Mexican market in 2017. Based on the competitive demands of that market, however, it is unlikely that Paragon will be able to obtain three rig contracts as projected.

129. Given the supply overhang, current and projected market conditions, age and idleness of the Paragon fleet, nature of Paragon's business, nature of the contracts they were receiving and pitching, and capital expenditure needs, Mr. Leand opined that Paragon's Downside Sensitivity projections for 2019 are too aggressive and would not be achievable. (9/29/2016 Hrg. Tr. 204:19-205:2; 210:12-15 (Leand Test.); TLA601A.)

C. Ability to Refinance

130. Under the Downside Sensitivity, Paragon has three different debt obligations totaling approximately $1.3 billion that come due in 2021 and will have to be

refinanced in that year or earlier: the term loan debt, the revolver debt and new notes being issued to the noteholders. (9/28/2016 Hrg. Tr. 105:4-16, 107:11-18 (Fordyce Test.); 9/29/2016 Hrg. Tr. 136:13-20 (Leand Test.).) Additionally, capital leases on Paragon's Prospector rigs need to be addressed in 2020. The amount of that obligation is approximately $89 million, though a $40 million dollar cash reserve will come with that, meaning that, on a net basis, the obligation is about $50 million. (9/28/2016 Hrg. Tr. 107:22-108:11 (Fordyce Test.).)

131. In analyzing whether Paragon has the ability to refinance its debt, Lazard did not directly address the fact that "$110 billion of debt associated with severely strained oilfield services and drilling (OFS) companies will mature or expire over the next five years." (9/28/2016 Hrg. Tr. 108:22-110:1 (Fordyce Test.); TLA 598.) Lazard did not consider that Paragon's debt was issued in 2011 through 2015, when energy prices were high. Yet, since WTI crude is down 50 percent from 2014, Moody's expects the industry's EBITDA to be down 30 to 40 percent in 2016. Nor did Lazard consider the fact that Moody's does not expect the sector to begin to recover before mid-2017. Rather Mr. Fordyce simply assumed that the "leveraged finance market . . . would be a functioning market" when Paragon's debt comes due. (9/28/2016 Hrg. Tr. 110:2-20 (Fordyce Test.); TLA 598.) Nor did Mr. Fordyce consider all the different companies with debt similar to Paragon's coming due in the 2020 to 2021 timeframe. (9/28/2016 Hrg. Tr. 111:7-112:11 (Fordyce Test.); TLA 598.) Finally, Mr. Fordyce did not analyze what the credit markets will be like when Paragon's debt comes due under the Downside Sensitivity. (9/28/2016 Hrg. Tr. 112:12-113:8 (Fordyce Test.).)

132. Prof. Fischel criticized Mr. Fordyce for his purported ability to predict what Paragon's debt rating would be in 2019, closer to when it would need to refinance its debt, when Mr. Fordyce was either unable or unwilling to determine what Paragon's debt rating would be at emergence. (9/28/2016 Hrg. Tr. 202:23-203:15 (Fischel Test.).) Mr. Fordyce is not a credit ratings expert and simply made observations based on guidelines from a credit rating memorandum. (*Id*. at 112:24-113:8, 114:13-15.)

133. Mr. Fordyce projected a "B" rating under the Downside Sensitivity and projects that Paragon's credit rating from Moody's in 2019 would be "solidly in the non-investment grade range." (6/23/2016 Hrg. Tr. 113:19-114:12 (Fordyce Test); PGN146; 9/28/2016 Hrg. Tr. 53:3-54:22 (Fordyce Test.); PGN 226.) His conclusion is based exclusively on looking at two EBITDA-based metrics. (9/28/2016 Hrg. Tr. 38:7-39:25, 114:13-18 (Fordyce Test.); PGN146.)

134. Mr. Leand disagreed with Mr. Fordyce's opinion that the sole metric for refinancing is whether debt-to-EBITDA meets Moody's criteria for B-rated companies because, based on his experience, while that may be one consideration, it has never been a driving factor for potential underwriters. (9/29/2016 Hrg. Tr. 137:18-25 (Leand Test.).) The most important factors to potential underwriters are backlog, collateral value, customer base, quality and diversity of its customer base and fleet. (9/29/2016 Hrg. Tr. 138:1-7 (Leand Test.); 6/30/2016 Hrg. Tr. 156:1-8 (Leand Test.).)

135. Mr. Leand testified that he did not believe Paragon could refinance the debt in 2021 under the Downside Sensitivity. (9/29/2016 Hrg. Tr. 136:21-25 (Leand Test.).) Mr. Leand explained that, based on his adjustments, Paragon could breach the liquidity

covenants and run out of cash prior to maturity. (*Id.* at 137:1-5.) Even if that liquidity event did not occur, Mr. Leand did not believe Paragon's profile would be sufficient to allow it to raise capital in the market. (*Id.* 137:6-9.) Factors affecting Paragon's credit profile would include collateral value, contract backlog, its customer base (including quality and diversity), the fleet and its credit ratings. (*Id.* 137:10-17.)

136. Mr. Stilley claims Paragon does not pay attention to backlog. (9/27/2016 Hrg. Tr. 126:24-127:4, 128:13-17 (Stilley Test.).) However, in the presentation made to the Term Loan Lenders in 2014, Paragon emphasized its $2.7 billion backlog, a $3.4 billion asset value compared to a $1.345 billion debt (2.5x coverage) and highlighted that it served approximately 16 customers in 12 countries on 5 contents and emphasized that these were diversified, long-tendered clients. (TLA599; 9/29/2016 Hrg. Tr. 140:22-141:9 (Leand Test.); TLA317 at 11; 9/27/2016 Hrg. Tr. 129:12-17, 129:24-130:22 (Stilley Test).) Paragon's backlog, collateral value and quality of customer base described in 2014 do not currently exist. Further, when Mr. Leand reviewed Paragon's 2014 presentation, he did not see any mention of Mr. Fordyce's metric of debt-to-EBITDA. (TLA599; 9/29/2016 Hrg. Tr. 141:10-16 (Leand Test.).) And Paragon performed no analysis of its backlog in taking the position it will be able to refinance. (9/27/2016 Hrg. Tr. 131:19-22 (Stilley Test.).)

137. By December 31, 2015, Paragon's Form 10-K showed that Paragon's contract backlog was $1 billion. (9/29/2016 Hrg. Tr. 138:15-139:2 (Leand Test.); TLA502 p. 6.) At this time, Paragon is now a regional player at best in a specific market as opposed to a broader asset base in a broader market, and has a much smaller and diminishing

backlog, and the assets are "nowhere near" what they were when the notes were first issued. (9/29/2016 Hrg. Tr. 147:12-23 (Leand Test.).)

138. Mr. Tietz's July 28, 2016 presentation to the Board showed that backlog per rig has been steadily declining. (9/27/2016 Hrg. Tr.77:5-21 (Stilley Test.); TLA377 at 34.) The backlog for Paragon's standard spec jackups has decreased from $1.7 billion in Q3 2015 to half a billion in Q4 2015 and decreased to $315 million as of the Second Confirmation Hearing. (9/27/2016 Hrg. Tr. 81:16-82:15 (Stilley Test.); 9/29/2016 Hrg. Tr. 139:8-11, 140:6-10 (Leand Test.); TLA377 at 35.) Paragon's backlog has decreased faster than its competitors because its rigs are primarily jackups on short-term contracts. (6/23/2016 Hrg. Tr. 94:4-19 (Fordyce Test.); PGN40.)

139. As of the commencement of the Second Confirmation Hearing, Paragon's contract backlog was approximately $315 million. (Leand Direct 9/29 139:8-11, 140:6-11.)

140. Mr. Leand's opinion is partly based on his review of the Transocean Offering Memorandum, dated July 6, 2016, which Transocean issued in connection with a bond offering, and in which Transocean highlighted as its competitive strength their significant asset base, a fleet of 60 rigs, a $14.6 billion backlog, a blue chip customer base, a strong equity position and a global footprint. (TLA397; 9/29/2016 Hrg. Tr. 9/29 141:17-142:7, 142:22-143:3 (Leand Test.).) These factors highlighted by Transocean are consistent with the factors highlighted by Paragon in 2014, and, based on Mr. Leand's review of the document and his experience in the industry, are key drivers to potential lenders and underwriters. (9/29/2016 Hrg. Tr. 9/29 143:4-14 (Leand Test.).) Mr. Leand observed that

the Transocean Offering Memorandum never mentions debt-to-EBITDA. (9/29/2016 Hrg. Tr. 145:9-13 (Leand Test.); TLA397.)

141. Mr. Leand reviewed and relied on the various Pareto Conference presentations in which Transocean highlighted a $13.7 billion backlog, Shelf Drilling highlighted a $2 billion backlog and their highly diversified customer base, and Songa Offshore highlighted a $4.9 billion backlog extending into 2024. (9/29/2016 Hrg. Tr. 146:1-18 (Leand Test.); TLA580; TLA581; TLA582.)

142. Mr. Fordyce refused to even speak to what Paragon's backlog might look like in 2021, stating it would be a "guess." (9/28/2016 Hrg. Tr. 62:22-63:13 (Fordyce Test.).)

143. The offshore drilling industry is predominantly dominated by asset-based lenders looking to the value of Paragon's assets. (6/30/2016 Hrg. Tr. 155:18-25 (Leand. Test.).) As to collateral value, Mr. Leand reviewed the expert report that the Debtors had Ulrik Engelschion prepare. Mr. Engelschion valued Paragon's rigs at between $2 and $15 million, which would make collateral value of the jackup fleet at approximately $315 million, plus an estimated value of the MSS1 as the only floater. (9/29/2016 Hrg. Tr. 146:19-147:11 (Leand Test.).) Mr. Leand opined that this collateral value is insufficient to support a refinancing, and together with other factors, demonstrate that Paragon today is simply not the company Paragon was when it raised debt at the time of the spinoff from Noble, which fact will further impact Paragon's ability to refinance its debt. (9/29/2016 Hrg. Tr. 147:12-23 (Leand Test.).)

144. Paragon will also have competition in the refinancing market in 2021. (9/29/2016 Hrg. Tr. 147:24-148:1 (Leand Test.).) According to Mr. Leand, Moody's identified maturities coming due in the offshore drilling space with the "vast majority" or "at least half" of the total $110 billion maturing in 2020 and 2021. (9/29/2016 Hrg. Tr. 148:3-14 (Leand Test.); TLA598.)

145. Mr. Leand did not agree with Mr. Fordyce's testimony that there was a $1 trillion E&P market and financing would always be available. (9/29/2016 Hrg. Tr. 148:15-20 (Leand Test.).) Although Mr. Fordyce's overall description of the market was "probably right," the market for "asset-based" financing for drilling companies was a smaller, more-specific market, and the characteristics of that market had "changed drastically" over the prior two years because historical capital used to support the market was no longer there. (9/29/2016 Hrg. Tr. 148:20-149:2. (Leand Test.)) If oil prices remained flat, the market would continue to be "under stress" and "difficult." (*Id.* at 149:3-7.)

146. Mr. Leand also did not agree with Mr. Stilley and Mr. Fordyce that backlog was not relevant because one of the first things industry participants highlight on their websites is backlog. (9/29/2016 Hrg. Tr. 145:3-8 (Leand Test.).) Mr. Stilley's and Mr. Fordyce's testimony is also contradicted by Paragon's own 10-K as well as the 2014 lender presentation.

147. Mr. Fordyce's opinion about Paragon's ability to refinance its debt in 2021 is not reliable, as it is based on a superficial analysis and does not take account market factors relevant to Paragon's ability to refinance its debt. On the other hand, Mr. Leand's

opinions and conclusions are reliable. As Mr. Leand opines, it is unlikely that Paragon will be able to refinance its debt in 2021.

D. Paragon Will Run Out of Cash and Breach Financial Covenants

148. Under its covenants with the Revolver Lenders, Paragon is required to maintain certain liquidity levels. In addition, in order to run its business, Paragon needs sufficient working capital.

149. Mr. Leand evaluated Paragon's projections, and concluded that Paragon will run out of cash and breach its liquidity covenant with the Revolver Lenders as early as 2018. (9/29/2016 Hrg. Tr. 136:21-137:5, 217:15-18 (Leand Test.).) Mr. Leand created a model with two scenarios, although the Court will only consider the first, as the Court finds that the Debtors' capital expenditure analysis is reasonable. Under Mr. Leand's scenario, dayrates were held flat and no other adjustments were made to the Downside Sensitivity. Paragon breached its financial covenants and liquidity covenants and ran out of cash before the end of the Projection Period. (9/29/2016 Hrg. Tr. 216:4-13 (Leand Test.).) Mr. Leand explained that, in this scenario, Paragon would run out of cash "just into 2019." (*Id.* 217:10-14; TLA536.)

150. Mr. Leand's model shows that Paragon will fail the leverage covenant in the scenario where the dayrates were held flat. (9/29/2016 Hrg. Tr. 217:21-218:3 (Leand Test.); TLA536.) Mr. Leand's model also shows that Paragon would fail the interest coverage ratio if, as under Mr. Leand's scenario, the dayrates are held flat. (9/29/2016 Hrg. Tr. 218:4-10 (Leand Test.); TLA537.)

151. Mr. Leand's ultimate conclusion was that Paragon would not be able to achieve the Downside Sensitivity and that it was not feasible. (9/29/2016 Hrg. Tr. 219:7-11 (Leand Test.).)

152. Mr. Leand testified that based on the scenarios he ran, Paragon would be out of cash and in breach of its covenants before its debt matured; therefore, refinancing would only become a hypothetical at that point. (9/29/2016 Hrg. Tr. 219:12-17 (Leand Test.; TLA536.) Mr. Leand explained that "irrespective" of whether Paragon runs out of cash or meets its covenants, in 2021, Paragon will have no appreciable backlog and will not have the same characteristics that it had in 2014 when it was able to borrow initially. (9/29/2016 Hrg. Tr. 219:18-220:8 (Leand Test.).)

153. Because Mr. Leand's opinions regarding the Downside Sensitivity are reliable, his opinions regarding Paragon's liquidity and his conclusion that Paragon will run out of working capital in 2018 are reliable.

E. The Amended Noble Settlement

154. As the Noble Settlement is part of the Modified Plan and as confirmation of the Modified Plan is being denied, the Court need not discuss or rule upon the Amended Noble Settlement.

IV. CONCLUSIONS OF LAW DENYING CONFIRMATION OF THE MODIFIED SECOND AMENDED JOINT CHAPTER 11 PLAN

155. The Debtors have the burden of proving that each of the requirements of Section 1129(a) of the Bankruptcy Code is satisfied with respect to the Modified Plan, including that the Modified Plan has been proposed in good faith as required by Section

1129(a)(3) and that the Modified Plan is not likely to be followed by the liquidation or the need for further financial reorganization of the Debtors as required by Section 1129(a)(11).

156. The Debtors have failed to meet their burden of proving that the Modified Plan complies with the requirements of each of Section 1124(2) and 1129(a)(11) of the Bankruptcy Code.

157. The Modified Plan is likely to be followed by the liquidation or the need for further financial reorganization of the Debtors and the Modified Plan accordingly does not comply with the requirement of Section 1129(a)(11) of the Bankruptcy Code because: (i) the assumptions underlying the Debtors' Downside Sensitivity and the Modified Base Case are not reasonably achievable, and the Debtors are likely to run out of cash and therefore breach their financial covenants and be unable to pay their debts; and (ii) the Debtors are unlikely able to refinance their indebtedness to the Term Lenders, the Revolver Lenders and the Noteholders at or prior to maturity.

158. As the Court finds that the Modified Plan is not feasible, the Court finds that the claims of the Secured Term Loan Lenders may not be reinstated under Section 1124 of the Bankruptcy Code.[19]

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[19] The Court limits its ruling on reinstatement of the Secured Term Loan Agreement to the terms of the Modified Plan. The Court makes no ruling on whether the Term Loan Agreement may be reinstated under the terms of another plan.

V. CONCLUSION

159. For the reasons set forth above, the Court DENIES confirmation of the Modified Plan. IT IS SO ORDERED.

Dated: November 15, 2016

Christopher S. Sontchi
United States Bankruptcy Judge