

**UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF NEW YORK**

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In re	:	Chapter 11
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PACIFIC DRILLING S.A., <i>et al.</i> , <sup>1</sup>	:	Case No. ___-____ (___)
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Debtors.	:	Joint Administration Pending
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**DECLARATION OF JAMES A. MESTERHARM  
IN SUPPORT OF FIRST DAY MOTIONS AND APPLICATIONS**

I, James A. Mesterharm, pursuant to section 1746 of title 28 of the United States Code, hereby declare that the following is true to the best of my knowledge, information and belief:

1. I am Managing Director of AlixPartners, LLP (“AlixPartners”) and the Co-Head of AlixPartners’ Turnaround & Restructuring Services Group in the Americas. AlixPartners has served as restructuring advisor to Pacific Drilling S.A. (“PDSA”), a Luxembourg public limited liability company (*société anonyme*), and each of the other above-captioned debtors and debtors-in-possession (collectively, the “Debtors”) since December 2016. I am familiar with the Debtors’ day-to-day operations, books and records, and business and financial affairs.
2. I have been a full time restructuring advisor for over 23 years. I received a B.S. in Accounting and Management in 1990 from Purdue University and a Masters of Business

<sup>1</sup> The Debtors in these chapter 11 cases and, if applicable, the last four digits of their U.S. taxpayer identification numbers are: Pacific Drilling S.A., Pacific Drilling (Gibraltar) Limited, Pacific Drillship (Gibraltar) Limited, Pacific Drilling, Inc. (1524), Pacific Drilling Finance S.à r.l., Pacific Drillship SARL, Pacific Drilling Limited, Pacific Sharav S.à r.l. (2431), Pacific Drilling VII Limited, Pacific Drilling V Limited, Pacific Drilling VIII Limited, Pacific Scirocco Ltd. (0073), Pacific Bora Ltd. (9815), Pacific Mistral Ltd., Pacific Santa Ana (Gibraltar) Limited, Pacific Drilling Operations Limited (9103), Pacific Drilling Operations, Inc. (4446), Pacific Santa Ana S.à r.l. (6417), Pacific Drilling, LLC (7655), Pacific Drilling Services, Inc. (5302), Pacific Drillship Nigeria Limited (0281) and Pacific Sharav Korlátolt Felelősségű Társaság.

Administration in Finance and Organizational Behavior in 1998 from Northwestern University's Kellogg School of Graduate Management, where I have been a guest lecturer on restructuring topics. I passed the Certified Public Accountant exam and am a Fellow of the American College of Bankruptcy. I have been employed by AlixPartners since September 1996. AlixPartners is a global independent restructuring consulting firm that has a wealth of experience in providing restructuring advisory services, and has assisted, advised, and provided strategic advice to debtors, creditors, bondholders, investors, and other entities in numerous chapter 11 cases of similar size and complexity to these chapter 11 cases. Since its inception in 1981, AlixPartners, its predecessor entities, and its affiliate, AP Services, LLC, have provided restructuring or crisis management services in numerous large cases. Some notable, publicly-disclosed restructuring assignments that I have personally led include the Gymboree Corporation, Linn Energy, Inc., Paragon Offshore PLC, Walter Energy, Inc., Nautilus Holdings Ltd., Eastman Kodak Company, General Growth Properties, Hilex-Poly, Silicon Graphics Inc., Parmalat USA, Safety-Kleen Corporation and Zenith Electronics Corporation.

3. I submit this declaration (this "Declaration") in support of the Debtors' petitions (the "Petitions") for relief under title 11 of the United States Code, 11 U.S.C. §§ 101 *et seq.* (the "Bankruptcy Code"), filed on November 12, 2017 (the "Petition Date") and the Debtors' related requests for initial relief in the form of motions and applications (the "First Day Motions"). I have reviewed the Debtors' Petitions and First Day Motions, or have otherwise had their contents explained to me, and it is my belief that the relief sought therein is essential to ensure the uninterrupted operation of the Debtors' business and the success of the Debtors' reorganization.

4. Additional information regarding the circumstances leading to the commencement of these reorganization cases pursuant to Chapter 11 of the Bankruptcy Code (the “Chapter 11 Cases”) and information regarding the Debtors’ business and capital structure is set forth in the *Declaration of Paul T. Reese Pursuant to Rule 1007-2 of the Local Bankruptcy Rules for the Southern District Of New York in Support of Chapter 11 Petitions and First Day Motions and Applications* (the “Reese Declaration”).<sup>2</sup>

5. Except as otherwise indicated, the facts set forth in this Declaration are based upon my personal knowledge, my review of relevant documents, my discussions with members of the Debtors’ senior management and other professionals, information provided to me by AlixPartners professionals working under my supervision or my opinion based upon experience, knowledge and information concerning the Debtors’ operations and their industry as a whole. I am authorized to submit this Declaration on behalf of each Debtor, and if called upon to testify, I would testify competently to the facts set forth herein.

6. On the Petition Date, the Debtors commenced the Chapter 11 Cases. The Debtors intend to operate their business in the ordinary course during the Chapter 11 Cases. I have reviewed the Debtors’ business plan and projected financial information, and the Debtors anticipate that cash on hand and revenue earned from postpetition operations will be sufficient to fund all payments contemplated by the Debtors’ First Day Motions and their postpetition operating and restructuring-related expenses.

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<sup>2</sup> Capitalized terms used but not defined herein have the meanings given to them in the Reese Declaration or the applicable First Day Motion.

**Relief Sought in the Debtors' First Day Motions**

7. To enable the Debtors to continue business operations without disruption and promote a smooth transition to chapter 11, the Debtors have requested various forms of relief in their First Day Motions. The First Day Motions seek authority to, among other things, preserve customer relationships, continue to pay employee obligations and ensure the continuation of the Debtors' cash management systems and other business operations without interruption. I have reviewed each of the First Day Motions and the facts set forth therein are true and correct to the best of my knowledge, information and belief. Moreover, I believe receiving court approval of the relief sought in the First Day Motions is essential to provide the Debtors an opportunity to work towards a successful restructuring that will benefit all of the Debtors' stakeholders.

8. Several of the First Day Motions request authority to pay certain prepetition claims that have not yet been invoiced. It is my understanding that Rule 6003 of the Federal Rules of Bankruptcy Procedure (the "Bankruptcy Rules") provides that to the extent "relief is necessary to avoid immediate and irreparable harm," a bankruptcy court may approve a motion to pay all or part of a claim that arose prior to the filing of a chapter 11 case within 21 days after the petition date.

A. Administrative Motions

- i. Motion for an Order (A) Authorizing Joint Administration of the Debtors' Chapter 11 Cases and (B) Waiving Requirements of Section 342(c)(1) of the Bankruptcy Code and Bankruptcy Rule 2002(n)

9. The Debtors are "affiliates" as defined in section 101(2) of the Bankruptcy Code. The Debtors therefore request that the Court jointly administer the Chapter 11 Cases. Joint administration will obviate the need for duplicative notices, motions, applications and orders, thereby saving considerable time for the Court and time and expense for the Debtors and

their estates. Furthermore, the Debtors also request a waiver of the requirements imposed by section 342(c)(1) of the Bankruptcy Code and Bankruptcy Rule 2002(n). The Debtors submit that the use of the proposed simplified caption without full tax identification numbers and previous names will ensure a uniformity of pleading identification. Such information is listed on each Debtor's petition which are publicly available. I believe that joint administration and a waiver of the requirements imposed by section 342(c)(1) of the Bankruptcy Code and Bankruptcy Rule 2002(n) will promote the fair and efficient administration of the Chapter 11 Cases, and accordingly, respectfully submit that this motion should be approved.

- ii. Motion for an Order (A) Authorizing the Debtors to Prepare a List of Creditors in Electronic Format in Lieu of Mailing Matrix, (B) Authorizing the Debtors to File a Consolidated List of Their 30 Largest Unsecured Creditors, (C) Authorizing the Debtors to Mail Notices Through Their Claims Agent, (D) Extending the Time to File Schedules and Statements and (E) Establishing Procedures for Notifying Parties of the Commencement of These Cases

10. The Debtors have requested that the Court authorize the Debtors to (a) prepare a list of creditors in electronic format, in lieu of submitting any required mailing matrix, (b) file a consolidated list of their 30 largest unsecured creditors, (c) mail notices through their claims and noticing agent, Prime Clerk LLC (the "Claims Agent"), (d) extend the 14-day period to file their schedules and statements and (e) establish procedures for notifying parties of the commencement the Debtors' chapter 11 cases.

11. The Debtors request authority to maintain a consolidated list of creditors in electronic format, in lieu of any required mailing matrix. This information exists in a reliable computerized form and I believe that converting the Debtors' computerized information into the required matrix format would be unduly burdensome and would increase the risk of error with respect to the transfer of this information from the computer systems maintained by the Debtors or their agents. The Debtors anticipate that, with the assistance of their Claims Agent, an

electronic consolidated list of their creditors will be completed within only 30 days of the Petition Date. The Debtors are prepared to make such list available in electronic form to any party-in-interest who so requests (or in non-electronic form at such requesting party's sole cost and expense) in lieu of submitting a mailing matrix.

12. Similarly, because many of the creditors are shared amongst certain of the Debtors and the Debtors operate as a single business enterprise, I believe that granting the Debtors authority to file a single, consolidated list of their 30 largest general unsecured creditors is appropriate under the circumstances.

13. The Debtors further request the authority to mail notices through their Claims Agent, whose services will streamline the notice process for all parties.

14. The Debtors also request that the Court extend the 14-day period to file their schedules of assets and liabilities, schedules of current income and expenditures and schedules of executory contracts and unexpired leases (collectively, the "Schedules") and statements of financial affairs (the "Statements") for an additional 30 days, for a total of 44 days. I believe that the size and complexity of the Debtors' business and the volume of material that must be compiled and reviewed by the Debtors' staff to complete the Schedules and Statements for each Debtor during the initial days of the Chapter 11 Cases provide ample "cause" for justifying the requested extension.

15. Further, an extension will permit the Debtors and their advisors to gather the necessary information in a manner that maximizes accuracy and avoids the necessity of subsequent corrections and amendments. All parties will benefit from the enhanced accuracy of the information-gathering process. Additionally, absent notice and a hearing, the Debtors do not

intend to sell their assets during this 44-day period, so no party-in-interest will suffer any adverse consequences as a result of the Debtors' requested extension.

16. Finally, the Debtors request that the Court approve the Debtors' procedures for providing notice of these chapter 11 cases. The Debtors request authority for the Claims Agent to provide notice of commencement of these chapter 11 cases by regular mail and by publication on a website maintained by the Claims Agent at <https://cases.primeclerk.com/PacificDrilling>. These proposed procedures will ensure that the Debtors' creditors receive prompt notice of the commencement of these chapter 11 cases. Accordingly, I respectfully submit that this motion is in the best interest of the Debtors and their estates and should be approved.

- iii. Motion for an Order (A) Enforcing Sections 362, 365(e)(1) and 525 of Bankruptcy Code and (B) Permitting the Debtors to Modify the Automatic Stay to Proceed with Certain Litigation Commenced Prepetition

17. The Debtors have requested that the Court enter a declaratory order enforcing and restating the automatic stay, *ipso facto* and anti-discrimination provisions under sections 362, 365(e)(1) and 525 of the Bankruptcy Code. The Debtors are a leading offshore drilling company and serve customers worldwide. As a result, the Debtors have many foreign creditors, contract counterparties and other parties-in-interest in various countries who may not be well versed in the protections and restrictions of the Bankruptcy Code. Some of these creditors do not transact business on a regular basis with companies that have filed for chapter 11, or are unfamiliar with the scope of a debtor-in-possession's authority to conduct its business. Such circumstances warrant an order apprising parties—especially non-U.S. customers, creditors and vendors—of sections 362, 365(e)(1) and 525 and the protections provided thereby.

18. The Debtors also request the authority to modify the automatic stay in order to proceed with certain prepetition litigation. Specifically, on October 29, 2015, Debtor

Pacific Drilling VIII Limited (“PDVIII”) exercised its right to rescind a contract with Samsung Heavy Industries Co., Ltd. (“SHI”) for the construction and delivery of the drillship the *Pacific Zonda*, due to SHI’s failure to timely deliver the drillship in accordance with contractual specifications, and demanded that SHI refund the amount of its advance payments under the contract in the amount of approximately \$181 million, plus interest. PDVIII’s payment obligations under the contract were guaranteed by Debtor Pacific Drilling Services, Inc. (“PDSI”). SHI rejected PDVIII’s rescission, and on November 18, 2015, formally commenced an arbitration proceeding in London against PDVIII and PDSI (the “Zonda Arbitration”), seeking the final installment of the purchase price, which is close to \$350 million.

19. PDVIII made a demand under a third-party refund guarantee issued in connection with the SHI contract, seeking to collect its advance payments under the contract in the amount of approximately \$181 million, plus interest. PDVIII’s ability to collect under the refund guarantee is suspended until a decision is reached in the pending Zonda Arbitration. In addition to its demand under the refund guarantee, PDVIII also filed a counterclaim against SHI in the Zonda Arbitration seeking (a) to recoup its advance payments, (b) the return of its purchased equipment or the value of such equipment and (c) damages for wasted expenditures. In total, PDVIII is seeking close to \$350 million from SHI. As such, the outcome of the Zonda Arbitration could result in a sizeable claim either against or in favor of certain of the Debtors’ estates.

20. The Zonda Arbitration has been progressing in front of a panel of three experienced attorneys for almost two years. Each side has made numerous submissions to the panel, including voluminous evidentiary materials. A scheduled pre-trial hearing is set to take place shortly following the Petition Date, on November 21, 2017. A



hearing on the merits of the claims has been set for February 5, 2018, and is expected to last at least three weeks.

21. Authorizing the Debtors to modify the automatic stay and continue the arbitration would not interfere with the Chapter 11 Cases. An award in the Zonda Arbitration would fully resolve issues of liability thereunder; resolving the claims subject to arbitration would therefore assist in administering the Debtors' estates by providing finality to a contingent claim, and may result in an increase to the assets of certain of the Debtors' estates. Furthermore, a specialized tribunal has already been convened to hear the merits of the parties' claims. Last, PDVIII and SHI have prepared extensively for a hearing on the merits of the Zonda Arbitration and the interests of judicial economy weigh heavily in favor of allowing the parties to proceed. Accordingly, I respectfully submit that this motion should be approved.

iv. Application for an Order Appointing Prime Clerk LLC as Claims and Noticing Agent

22. The Debtors have numerous creditors and other parties-in-interest, many of whom are expected to file proofs of claim. As such, the Debtors respectfully submit that noticing parties and receiving, docketing and maintaining proofs of claim would impose heavy administrative and other burdens upon the Court and the Office of the Clerk of the United States Bankruptcy Court for the Southern District of New York. The Debtors propose to retain Prime Clerk LLC as their claims and noticing agent, to relieve the Court and the clerk's office of these burdens. Accordingly, I respectfully submit that this application should be approved.

B. Operational Motions

- i. Motion for Interim and Final Orders (A) Authorizing the Continued Use of the Debtors' Centralized Cash Management System, Bank Accounts and Business Forms, (B) Authorizing the Debtors to Make Intercompany Advances on a Secured Basis under Section 364(c) of the Bankruptcy Code, (C) Granting a Waiver of the Deposit Guidelines Set Forth in Section 345 of the Bankruptcy Code, and (D) Granting Related Relief

23. The Debtors have requested that the Court enter interim and final orders authorizing the Debtors to continue using their existing cash management system, bank accounts and business forms and to make intercompany advances a senior secured, superpriority basis, and granting a waiver of the deposit guidelines set forth in section 345 of the Bankruptcy Code. In furtherance of the Debtors' integrated global business operations, the Debtors utilize a centralized cash management system (the "Cash Management System") to collect, transfer and distribute funds generated by the Debtors' operations and to accurately record such collections, transfers and disbursements as they are made. I believe that the continued use of this Cash Management System is essential to the Debtors' reorganization. The Debtors filed the Chapter 11 Cases with over \$250 million in unencumbered cash, which they expect to use, together with revenue from operations, to fund their ongoing business operations, corporate needs and restructuring-related expenses. The majority of this unencumbered cash is held by Debtor Pacific Drilling (Gibraltar) Limited ("PDGL" or the "Pool Leader") in three accounts (the "Pool Leader Accounts"): (a) an investment account at Wells Fargo Securities, LLC ("Wells Fargo Securities"), which had a balance of approximately \$256 million as of the Petition Date, (b) a collections/payments account at Citibank, N.A. ("Citibank"), which had a balance of approximately \$600,000 as of the Petition Date, and (c) a payments account at Amegy Bank of Texas ("Amegy"), which had a balance of approximately \$2,700 as of the Petition Date.

Most of the Debtors' remaining cash is held by Debtor Pacific Drilling VII Limited ("PDVII") in a pledged account (the "SSCF Minimum Liquidity Account") at Wilmington Trust, National Association ("Wilmington"), which had a balance of approximately \$50 million as of the Petition Date. The Debtors' ability to successfully reorganize depends on their continued use of the Cash Management System described herein to collect and distribute cash and postpetition revenues to and from the various Debtors and their non-Debtor subsidiaries in a manner that is fair to all stakeholders.

24. The Cash Management System has several main components: (i) cash collection, including the collection of payments made to the Debtors from revenue generated in the ordinary course of business; (ii) cash disbursements to fund the Debtors' primary debt obligations and business operations, primarily consisting of payroll, maintenance costs and payments to vendors and service providers; and (iii) cash transfers among the Debtors and certain non-Debtor subsidiaries.

25. In connection with the Cash Management System, the Debtors maintain 38 bank accounts (the "Bank Accounts"), which include the Pool Leader Accounts, the SSCF Minimum Liquidity Account and various collections/payments accounts, payments accounts and payroll accounts. The majority of these Bank Accounts are located at Citibank, the collateral agent and a lender under the Debtors' Revolving Credit Agreement, and a lender under the Debtors' Senior Secured Credit Facility Agreement. The remainder of the Bank Accounts are located at Wilmington (the security agent under the Debtors' Senior Secured Credit Facility Agreement), Wells Fargo Securities, UniCredit S.p.A. ("UniCredit"), M&T Bank Corporation ("M&T"), Standard Chartered Bank ("Standard Chartered") and Amegy.

26. The Debtors and their non-Debtor subsidiaries receive funds from customers and pay funds to creditors by wire, ACH transfer, and occasionally check, and conduct transactions between and among themselves through wires, cash transfers and automated debits and credits. The Debtors also utilize a credit card account through Citibank to pay for travel and other business expenses of their employees (the “Credit Card Program”). There are currently 30 credit cards issued under this account. The ACH transfer program and Credit Card Program are secured by deposits of \$8 million and \$500,000, respectively, held in a Citibank Bank Account in the name of PDSA.

27. The Debtors utilize a cash-pooling system (the “Cash Pool”) with PDGL acting as Pool Leader, or the central intercompany “bank”, for all participants in the Cash Pool (the “Cash Pool Participants”). The Cash Pool allows for consolidated cash management and mitigates intercompany credit risks. When funds are received by the Cash Pool Participants—whether from drilling contracts, services agreements, third party and intercompany contracts or otherwise—the Debtors transfer such funds from the receiving account(s), directly or through one or more intercompany transfers, ultimately to the Pool Leader Accounts. Cash transfers to the Cash Pool Bank Accounts are typically effected within one day of receipt of funds, although the Debtors will occasionally leave funds in another Bank Account if a scheduled payment out of such Bank Account is approaching.<sup>3</sup> Each transfer of funds from a Cash Pool Participant to the Pool Leader is considered a loan from such Cash Pool Participant to the Pool Leader, which is interest free and payable on demand.

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<sup>3</sup> There is a related exception for local currency obligations in connection with operations in Nigeria. A portion of revenues earned by drillships operating out of Nigeria are denominated in Nigerian Naira and are deposited into a collections account held by non-Debtor Pacific International Drilling West Africa Limited (“PIDWAL”) at Guaranty Trust Bank plc (“GTB”), in accordance with Nigerian local content requirements. Nigerian employees are paid directly out of the PIDWAL GTB account, and a portion of the funds in this account are transferred to one of three additional PIDWAL accounts, to be used for operating disbursements.

28. The Debtors also use the Cash Pool to pay debt service and other expenses of the Cash Pool Participants. These payments are made either by a Cash Pool Participant using funds provided by the Pool Leader, or directly by the Pool Leader on a Cash Pool Participant's behalf. In each case, a transfer of funds from the Pool Leader to or on behalf of a Cash Pool Participant creates an intercompany loan from the Pool Leader to such Cash Pool Participant, which is also interest free and payable on demand.

29. The primary payments made through the Cash Pool system are allocated among the Cash Pool Participants as follows.

- *Debt Service Payments.* The cost of payments on the Prepetition Debt are ultimately allocated to the seven Drillship Subsidiaries that acquired and own the Debtors' drillships (the "Drillship Owners"). For the Ship Group A Debt, the Drillship Owners of the Pacific Bora and Pacific Scirocco first pay debt service on intercompany loans to PDOL, who then pays PDSA, and PDSA, as nominal borrower, pays the debt service to creditors. The Drillship Owners of the Pacific Santa Ana and Pacific Mistral first pay debt service on intercompany loans to PDSA, and PDSA as nominal borrower pays the debt service to creditors. For the Ship Group B Debt, the two Drillship Owners pay debt service directly, with the cost of debt service allocated equally between them. For the Ship Group C Debt, the single Drillship Owner pays debt service directly. In all these circumstances, debt service payments are funded by the Pool Leader and the account of the Drillship Owner as Cash Pool Participant is debited accordingly.
- *Support Services Fees.* Pursuant to intercompany support services agreements, Debtors PDSI and Pacific Drilling Operations Limited ("PDOL") provide support services to certain of the Debtors and their non-Debtor subsidiaries on an arms' length basis. These services include human resources, audit, regulatory compliance, environmental and safety support, legal, accounting, technical, engineering, logistics, supply chain, information technology, marketing, risk management and operational support services. PDSI and PDOL are reimbursed for their expenses and also earn a markup of between 5-10% (the "Support Services Fee") for certain of the services they provide, including human resources and executive services. Other services, such as treasury and accounting, are provided at cost, without any markup. Payments of any Support Services Fees to PDSI and PDOL are processed through the Cash Pool and paid with funds from the Pool Leader Accounts. The Support Services Fees

that are paid are ultimately allocated to the applicable Drillship Subsidiaries for whose benefit the services were provided, with the exception of certain corporate services allocated only to PDSA and subsidiaries that are not Drillship Subsidiaries. The Support Services Fees and related allocation methods represent arms' length transactions between and among the Debtors and their non-Debtor subsidiaries, conducted in accordance with the Debtors' established transfer pricing methods.

- *Payroll, Benefits and Operating Expenses.* Payroll, benefits and operating expenses are paid through the Cash Pool, either directly by the Pool Leader or through transfers from the Pool Leader to other Cash Pool Participants (both Debtors and non-Debtors). Payments to employees and third parties are generally made by one or more Debtor and non-Debtor subsidiaries (collectively, the "Service Entities") that provide labor and administrative services to other Debtors and non-Debtor subsidiaries. The Service Entities include Debtors PDSI, PDSA and PDOL, and non-Debtors Pacific Drilling International Ltd., Pacific Drilling Manpower Ltd., Pacific Deepwater Construction Limited and Pacific Drilling Manpower, Inc. Other than any Support Services Fees earned by PDSI and PDOL, the Service Entities are reimbursed only for their actual costs, and these costs are ultimately allocated in the same manner as the Support Services Fees described above.
- *Internal Charter Obligations.* As of the Petition Date, the *Pacific Sharav* is subject to an internal charter arrangement put in place in connection with its current long-term charter with a subsidiary of Chevron Corporation (the "Client"). Under this arrangement, one Drillship Subsidiary, Pacific Drilling Operations, Inc. (the "Internal Charterer") has entered into the contract with the Client, service arrangements with the applicable Service Entities and a "bareboat" charter with the Drillship Owner for the *Pacific Sharav*. Revenue from the contract with the Client is allocated among the Internal Charterer and the Drillship Owner in accordance with the bareboat charter. Both the Internal Charterer and the Drillship Owner have pledged substantially all of their property to secure the Ship Group B Debt.

30. While all of the Debtors participate in the Cash Pool, certain non-Debtor subsidiaries in Brazil and Nigeria maintain standalone accounts which are separate from the Cash Pool. To the extent necessary, the Debtors fund shortfalls in these accounts by creating an intercompany loan from the Pool Leader to such entities. The Debtors propose to make advances from the Pool Leader to these non-Debtor accounts during these chapter 11 cases so long as

aggregate amount in such accounts does not exceed \$10 million in U.S. Dollar equivalent at any time.

31. The Pool Leader has contractual netting and set off rights under prepetition documentation.<sup>4</sup> Advances between and among the Pool Leader and each Cash Pool Participant are typically netted by the Pool Leader on at least a monthly basis. This practice has the effect of rendering some Cash Pool Participants net lenders to and others net borrowers from the Cash Pool Leader, and the net position is carried on the books of the Pool Leader and each of the applicable Cash Pool Participants.

32. Although the mechanics have evolved over time to meet the Debtors' needs, the Cash Management System has been continuously utilized by the Debtors since 2013, and constitutes a customary and essential business practice.<sup>5</sup> This Cash Management System is similar to those commonly employed by companies comparable to the Debtors in economic scope and geographic reach. The Debtors maintain accurate and current records with respect to all transactions, whether transfers of cash, setoffs or otherwise, so that all transactions can be readily ascertained, traced and properly recorded. I believe that the interrelationships between the Debtors' operations and those of their subsidiaries, and the scope and breadth of their operations, mandates the use of the Cash Management System for a successful reorganization of the Debtors' business, as well as the preservation and enhancement of the Debtors' going

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<sup>4</sup> The Pool Leader's netting and set off rights are set forth in that certain Cash Pooling Agreement, dated as of June 10, 2015, by and among the Pool Leader and the Cash Pool Participants, as supplemented.

<sup>5</sup> In June 2015, the Debtors automated the Cash Pool, and all Cash Pool Bank Accounts other than the Pool Leader Account became zero balance accounts. The Debtors terminated this automated program in November 2016, and began once again to manually transfer funds between Bank Accounts in the Cash Pool. This system of manual transfers within the Cash Pool operates in substantially the same manner as it has since its inception in 2013. In addition, on February 3, 2017, Wilmington replaced DNB Bank ASA ("DNB") as collateral agent under the Senior Secured Credit Facility Agreement. As a result, several of the Debtors' accounts at DNB were replaced with newly-opened accounts at Wilmington.

concern value. Furthermore, preserving “business as usual” conditions and avoiding the enormous difficulties inevitably triggered by any substantial disruption of the Cash Management System will facilitate the stabilization of the Debtors’ postpetition business operations and assist the Debtors in their reorganization efforts.

33. The Debtors propose, subject to Court approval, to continue to use their Cash Management System during the Chapter 11 Cases in accordance with their historical practices, and also to make the following specific modifications that the Debtors believe are appropriate adjustments to historical practices in light of the Chapter 11 Cases, the requirements of the Bankruptcy Code and the interests of their diverse creditors. I have been informed that each of these modification is consistent with ordinary course practices.

34. *First*, the Debtors will follow appropriate procedures to ensure that intercompany claims arising prior to the Petition Date are not netted or set off against intercompany claims arising after the Petition Date except as ordered by the Court or otherwise permitted by the Bankruptcy Code.

35. *Second*, as described below, advances between the Pool Leader and each Cash Pool Participant arising from operation of the Cash Management System after the Petition Date will be entitled to administrative priority and, with respect to the net positive position in favor of each Cash Pool Participant from the Pool Leader from time to time, liens in favor of such Cash Pool Participant on all property of the Pool Leader other than the capital stock of the Ship Group B Drillship Subsidiaries.

36. *Third*, the Debtors will continue to allocate all corporate and support services costs and expenses during these chapter 11 cases in accordance with their prepetition past practices. In addition, to the extent authorized by the Court pursuant to the Debtors’ Cash



Collateral Motion<sup>6</sup>, payments of current interest and non-estate professionals' fees and costs related to specific Prepetition Debt will be allocated equally among the Drillship Owners to whom such Prepetition Debt is recourse.

37. *Fourth*, the Pool Leader will be authorized to take steps to avoid an unnecessary extension of credit by the Pool Leader to any Drillship Subsidiary within a Ship Group that is a net lender to the Pool Leader. Specifically, if any Drillship Subsidiary has made an advance to the Pool Leader after the Petition Date, the Pool Leader will be authorized to debit and reduce the amount of such advance by any payment made by the Pool Leader for the account of another Drillship Subsidiary in the same Ship Group in accordance with the Cash Management System.

38. *Fifth*, the Debtors may eliminate unnecessary interim transfers through bank accounts by directing third parties, Debtors and their non-Debtor subsidiaries to make payments of amounts otherwise payable to any Debtor directly to a Pool Leader Account for the benefit of such Debtor under the Cash Management System.

39. *Sixth*, upon entry of the Final Order, the balance in the SSCF Minimum Liquidity Account will be transferred to a Pool Leader Account and the owner of that account, PDVII, will be credited with a corresponding secured advance to the Pool Leader under the Cash Management System. The Debtors will not seek to transfer the balance in the SSCF Minimum Liquidity Account prior to the hearing on the Final Order.

40. I have reviewed the Debtors' current cash flow projections for the 13-week period beginning on November 13, 2017 and ending on February 9, 2018, prepared by

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<sup>6</sup> *Debtors' Motion For Interim and Final Orders (A) Authorizing the Use of Cash Collateral, (B) Granting Adequate Protection, (C) Modifying the Automatic Stay, (D) Scheduling a Final Hearing and (E) Granting Related Relief*, filed contemporaneously herewith and incorporated herein by reference.

members of my team at my direction and attached hereto as Exhibit A (the “13-Week Projections”), and discussed the same with the Debtors. The 13-Week Projections are based on the Debtors’ current expectations and are subject to change or update as assumptions change.

41. Over the period reflected in the 13-Week Projections, the Ship Group A Debtors, collectively, and the Ship Group C Debtors, collectively, are expected to be net consumers of cash from the Pool Leader under the Cash Management System, while the Ship Group B Debtors, collectively, are expected to be net contributors of cash to the Pool Leader under the Cash Management System. Specifically, during the entire period reflected in the 13-Week Projections, (i) the Pool Leader is expected to contribute \$36.1 million on a net basis to the Ship Group A Debtors and to contribute \$5.0 million on a net basis to the Ship Group C Debtors and (ii) the Ship Group B Debtors are expected to contribute \$36.7 million on a net basis to the Pool Leader. Similarly, during the first four weeks of this period, (i) the Pool Leader is expected to contribute \$10.2 million on a net basis to the Ship Group A Debtors and to contribute \$1.6 million on a net basis to the Ship Group C Debtors and (ii) the Ship Group B Debtors are expected to contribute \$22.1 million on a net basis to the Pool Leader. These amounts exclude the transfer to the Pool Leader of the approximately \$50 million in the SSCF Minimum Liquidity Account, which the Debtors will seek to transfer pursuant to a final order of the Court. Total cash in the Pool Leaders’ accounts at the end of the 13-Week Projections after giving effect to such transfer is forecasted to be \$311.4 million.

42. The Debtors also seek authority to honor postpetition intercompany obligations between and among the Debtors resulting from operation of the Cash Management System after the Petition Date, and to afford all claims on account of such obligations superpriority administrative expense status with priority over any and all administrative expenses

of the kind specified in sections 503(b) and 507(b) of the Bankruptcy Code. In addition, solely with respect to the net positive position in favor of each Debtor from the Pool Leader from time to time, the Debtors are requesting authority, pursuant to section 364(c) of the Bankruptcy Code, for the Pool Leader to grant each Debtor a senior lien to secure such superpriority administrative expenses.

43. The Debtors should be allowed to honor the postpetition intercompany obligations and afford all claims on account of such obligations superpriority administrative expense status, and to secure the net positive position in favor of each Debtor from the Pool Leader from time to time. *First*, I do not believe the Debtors could obtain from third parties the type of interest-free, covenant-free, revolving advances contemplated by the Cash Management System. Nor can the various Debtors, who are distinct entities with fiduciary duties to their individual estates, be expected to advance funds into the Cash Management System on an interest-free basis without confirmation of the superpriority administrative status of those advances and adequate assurance of repayment. It is the Debtors' business judgment that the granting of senior liens on the Pool Leader's unencumbered assets to secure the net positive position of the Debtors from the Pool Leader from time to time is reasonable and necessary to protect the Debtors and their estates. *Second*, I believe the continued transfer of funds between and among Debtors is necessary to preserve assets of the estates because so many Debtors must act in concert to operate and maintain the business of all the Debtors as a group. Without a corporate cash management system, excess cash would have to be maintained at individual Debtor entities, resulting in substantially higher liquidity costs and the risk of Debtor entities not having access to funds to pay necessary expenses. *Third*, I believe the terms of the intercompany transfers are fair and reasonable, as all postpetition intercompany loans will be

interest free, the net positive position in favor of each Debtor from the Pool Leader from time to time will be fully secured by senior liens and costs will be allocated in accordance with historical practices.

44. The Debtors also seek authority to continue to use the Pool Leader Account to fund shortfalls in the accounts of certain Nigerian and Brazilian non-Debtor subsidiaries that maintain standalone accounts separate from the Cash Pool, or to make payments directly on behalf of such non-Debtors, so long as the aggregate amount in such non-Debtor accounts does not exceed \$10 million in U.S. Dollar equivalent at any time. In the past, such payments were only occasionally made. I believe such payments may be necessary at times to maintain the Company's operations and should therefore be allowed to continue.

45. The Debtors also request that no bank participating in the Cash Management System (the "Cash Management Banks") that honors a prepetition wire or other item drawn on any account that is subject to this Motion (a) at the direction of the Debtors to honor such prepetition check or item, (b) in a good faith belief that the Court has authorized such prepetition wire or item to be honored or (c) as the result of a good faith error made despite implementation of customary item-handling procedures, be deemed liable to the Debtors or their estates on account of such prepetition wire or other item being honored postpetition. The Debtors believe that such flexibility accorded to the Cash Management Banks is necessary to induce the Cash Management Banks to continue providing cash management services without additional credit exposure.

46. In connection with their use of the Cash Management System, the Debtors incur periodic service charges and other fees to the Cash Management Banks for the maintenance of the Cash Management System (the "Bank Fees"). I have been informed that as of the Petition

Date there is approximately \$17,000 in unpaid prepetition Bank Fees, and the Debtors request authority to pay such unpaid prepetition Bank Fees. I believe payment of the prepetition Bank Fees is in the best interests of the Debtors, their estates and all parties-in-interest as it will prevent any disruption to the Cash Management System.

47. The Debtors also seek a waiver of the requirement of the Office of the United States Trustee for the Southern District of New York (the "U.S. Trustee") that existing bank accounts be closed and new postpetition accounts be opened. I believe that if enforced in the Chapter 11 Cases, these requirements would cause enormous disruption in the Debtors' business and would impair the Debtors' efforts to successfully reorganize. As described in detail above, the Debtors' Bank Accounts are central to an established Cash Management System that the Debtors need to maintain to ensure smooth collections and disbursements in the ordinary course of their business. For instance, any delays or disruption in the payment of wages and other employee-related expenses resulting from changing Bank Accounts would erode employee morale at this critical time, and would cause the Debtors' employees to suffer hardship. This, in turn, could result in their departure, an outcome which would severely hamper the Debtors' restructuring efforts. Furthermore, having to open new accounts as of the Petition Date would unnecessarily distract the Debtors' key accounting and financial personnel, whose efforts are more appropriately focused on assisting with the restructuring of the Debtors' business. Therefore, to avoid delays in paying debts incurred postpetition, and to ensure as smooth a transition into chapter 11 as possible, the Debtors should be permitted to continue to maintain their existing Bank Accounts and, if necessary, to open new accounts and close existing accounts in the normal course of the Debtors' operations. Accordingly, the Debtors request that their Bank Accounts be deemed to be debtor-in-possession accounts, and that their maintenance and

continued use, in the same manner and with the same account numbers, styles and document forms as those employed during the prepetition period, be authorized. If the relief requested by the motion is granted, I understand that the Debtors will implement appropriate mechanisms to ensure that no payments will be made on any debts incurred by them prior to the Petition Date, other than those authorized by the Court.

48. In addition, the Debtors request authority to preserve various reporting and accounting mechanisms, such as signatory authorizations and accounting systems central to the maintenance of the Bank Accounts. The interruption or termination of such reporting and accounting mechanisms would undermine the utility of the Bank Accounts. In accordance with existing practices, I am told that the Debtors will maintain strict records of all receipts and disbursements from the Bank Accounts during the pendency of the Chapter 11 Cases and will ensure that their records properly distinguish between pre and postpetition transactions.

49. The Debtors also request authorization to use their existing business forms. To minimize expenses to their estates, the Debtors request authority to continue to use all correspondence and business forms (including letterhead, purchase orders, invoices, etc.) as such forms were in existence immediately before the Petition Date, without reference to the Debtors' status as debtors-in-possession. It is my understanding that, upon depletion of the Debtors' business forms stock, the Debtors will obtain new business forms stock reflecting their status as debtors-in-possession.

50. By virtue of the nature and the scope of the Debtors' business operations and the number of suppliers of goods and services with whom the Debtors transact on a regular basis, it is important that the Debtors be permitted to continue to use their existing business forms without alteration or change, except as requested in the motion. Indeed, because parties

doing business with the Debtors undoubtedly will be aware of the Debtors' status as debtors-in-possession, I believe changing business forms is unnecessary and unduly burdensome.

51. The Debtors also request that a waiver of the requirements of section 345(b) of the Bankruptcy Code and permission to maintain their deposits in the Bank Accounts in accordance with their existing deposit practices. While the majority of the Debtors' Bank Accounts are located at Citibank, M&T and Amegy, which are either depository institutions on a pre-approved list issued by the U.S. Trustee ("Authorized Depository Institutions") or insured by the Federal Deposit Insurance Corporation, the following Bank Accounts are not held at Authorized Depository Institutions: (a) the primary Pool Leader Account at Wells Fargo Securities (the "Wells Pool Account"), (b) the three Bank Accounts at Wilmington (the "Wilmington Bank Accounts"), (c) the Bank Account at Standard Chartered (the "Standard Chartered Account") and (d) the Bank Accounts at UniCredit (the "Unicredit Accounts" and, together with the Wells Pool Account, Wilmington Bank Accounts and the Standard Chartered Account, the "Waiver Accounts"). For the reasons set forth below, the Debtors seek a waiver of the applicable requirements of section 345 of the Bankruptcy Code and U.S. Trustee Guidelines with respect to each of the Waiver Accounts.

52. As described above, the Debtors use the Wells Pool Account as one of their two primary accounts for collecting and warehousing funds. Accordingly, I believe the continued use of this Bank Account is central to the Debtors' Cash Management System and, therefore, the success of the Debtors' reorganization. I understand that Wells Fargo Securities is large, well known and well-capitalized. Therefore, the Debtors respectfully submit that cause exists to waive the applicable requirements of section 345 of the

Bankruptcy Code and the relevant provisions of the U.S. Trustee Guidelines with respect to the Wells Pool Account.

53. The Debtors maintain the Wilmington Bank Accounts in order to comply with requirements under the Senior Secured Credit Facility Agreement.

Wilmington is a financial institution that is acceptable to the applicable borrowers under the Senior Secured Credit Facility Agreement and I understand that is large, well known and well-capitalized. Accordingly, the Debtors respectfully submit that cause exists to waive the applicable requirements of section 345 of the Bankruptcy Code and the relevant provisions of the U.S. Trustee Guidelines with respect to the Wilmington Bank Accounts.

54. I understand the Debtors' Standard Chartered Account is inactive, currently only holds approximately \$300 and is in the process of being closed. Accordingly, the Debtors respectfully submit that cause exists to waive the applicable requirements of section 345 of the Bankruptcy Code and the relevant provisions of the U.S. Trustee Guidelines with respect to the Standard Chartered Account, to allow the Debtors to close this Bank Account in the ordinary course.

55. The Debtors do not maintain significant balances in the Unicredit Accounts, which are held in the name Pacific Sharav Korlátolt Felelősségű Társaság ("Pacific Sharav Kft"). I understand the average balance in these accounts has been less than \$13,000 for the 90 days prior to petition date. Regardless, I understand UniCredit is a well-capitalized bank and it is the only banking option for the Debtors in Hungary, where Pacific Sharav Kft is domiciled. Accordingly, the Debtors respectfully submit that cause exists to waive the applicable requirements of section 345 of the Bankruptcy Code and the relevant provisions of the U.S. Trustee Guidelines with respect to the Unicredit Accounts.



56. The debtors also request authority to continue to invest their funds in the Wells Pool Account pursuant to their investment guidelines. I believe that by investing pursuant to these guidelines, the Debtors will be able to earn a reasonable return on excess cash without incurring the administrative costs and compliance risk associated with managing a portfolio of direct purchases of U.S. government obligations.

57. The Debtors' current investment guidelines permit the Debtors to invest in cash or cash equivalents, and the Debtors believe that their investment guidelines provide the protection contemplated by Section 345(b) of the Bankruptcy Code. Through the Wells Pool Account, the Debtors invest in short term money market funds that invest in U.S. government obligations and also hold short term (90-day maturity or less) investment grade commercial paper from highly rated issuers. These investments provide a reasonable return for the Debtors while at the same time adequately providing for the safety and liquidity of such investments. I believe requiring the Debtors to change their investment procedures abruptly is therefore unnecessary and could result in harm to the Debtors, their estates and their creditors due to the disruption of their Cash Management System. If granted a waiver, I believe the Debtors will not be burdened with the significant administrative difficulties and expenses relating to opening new accounts in a manner that ensures all of their funds are invested strictly in accordance with the restrictions established by section 345 of the Bankruptcy Code.

- ii. Motion for Interim and Final Orders (A) Authorizing, But Not Directing, the Debtors to Pay Certain Prepetition Claims of Safety and Critical Vendors, (B) Approving Related Procedures and (C) Authorizing All Financial Institutions to Honor All Related Payment Requests

58. The Debtors have requested that the Court enter interim and final orders (A) authorizing, but not directing, the Debtors, in their sole discretion, to pay certain prepetition

claims of critical vendors (collectively, the “Critical Vendor Claims”) (B) approving related procedures and (C) authorizing all financial institutions to honor all related payment requests.

59. The Debtors’ primary business is the provision of drilling services for the exploration and production of oil and natural gas resources in ultra-deepwater areas. In the course of providing these offshore drilling services, the Debtors operate and maintain highly complex drilling units that conduct precise underwater operations in remote locations. Given the remote nature of the Debtors’ operations and the inherent risks in ultra-deepwater drilling, safety is a key concern for the Debtors. Incidents on drillships can involve loss of life, personal injury, environmental damage, shutting down of operations, loss of revenue, destruction of property, litigation and negative publicity. Indeed, I believe excellence in safety performance is a key factor for the Debtors’ success.

60. In order to operate their drillships in accordance with their exacting safety standards, the Debtors purchase specialized equipment, fuel and services from certain safety and critical vendors (collectively, the “Critical Vendors”). These Critical Vendors provide the Debtors with goods and services necessary to safely maintain their operations, including but not limited to parts, equipment, transportation of personnel and supplies, shipping, warehousing, communications, medical services, maintenance and repairs, janitorial services, financial and legal services, human resources, certifications and safety inspections.

61. The goods and services provided by Critical Vendors are necessary for the Debtors’ continued excellence in safety performance. A safety failure could result in loss of life, personal injury, environmental damage, shutting down of operations, loss of revenue, destruction of property, litigation and negative publicity. If the provision of goods and services from Critical

Vendors were interrupted, I believe the safety of the Debtors' employees and others could be compromised and the Debtors could be in violation of regulations or environmental laws.

62. The Debtors seek authority to pay, in their discretion, the prepetition claims of Critical Vendors that delivered goods or provided services to the Debtors prior to the Petition Date (the "Critical Vendor Payments"). The Debtors estimate that the Critical Vendor Payments will not be substantial and will not exceed approximately \$4.5 million in the aggregate.

63. The goods and services provided by the Critical Vendors are of paramount importance to the Debtors and their ability to maintain the highest safety standards. Disrupting the Critical Vendors' provision of essential goods and services would cause drilling operations to come to a halt and could lead to possible termination of customer contracts, as the Debtors' drillships cannot operate safely and efficiently without the goods and services provided by the Critical Vendors. A break in the Debtors' operations, even for just one day, could have disastrous consequences on the Debtors' business, both in terms of lost revenue from existing or anticipated customer contracts and by impeding the Debtors' ability to enter into new customer contracts.

64. Furthermore, some of the Critical Vendors are the sole source of their goods and services or are among a handful of such suppliers in the world or in those geographic regions in which the Debtors operate, and are likely to refrain from supplying goods and services essential for the day-to-day operations of the Debtors if they are not paid. Moreover, certain Critical Vendors are reliant upon the Debtors for the continued operation of their own businesses; without the Debtors' payments, several Critical Vendors would have little or no working capital, and may be forced to cease operations. Accordingly, it is imperative that the

Debtors maintain positive relationships with the suppliers of the goods and services essential to their operations throughout the course of the Chapter 11 Cases.

65. While the estimated total amount of Critical Vendor Claims is \$4.5 million, approximately \$1.5 million of those claims are for goods that were delivered with 20 day of the Petition Date and would therefore receive administrative expense priority. I believe that the payment of the Critical Vendor Claims is vital to the Debtors' ability to continue to operate safely and efficiently, and to their reorganization efforts generally. The Debtors cannot afford to have their major assets sitting idle because parts are not available, food stores are not delivered, maintenance has not been performed and/or labor has become unavailable. The Debtors cannot put their crews and their only assets at risk. I believe a failure to pay the Critical Vendor Claims would be detrimental to all stakeholders.

66. Furthermore, the maritime industry is almost unique in that it permits certain categories of claimants (for example, in respect of salvage, goods supplied to a drillship and, in certain circumstances, repairs) to enforce their claims *in rem*, as well as *in personam*. An *in rem* claim is enforced by way of "arrest" of the drillship in question and, in certain circumstances and jurisdictions, other drillships in common ownership or ultimately owned by the same person. In other words, a supplier of goods or services to a drillship will often be able to arrest that drillship (and certain other drillships) in order to enforce, or at least obtain security for, its claim. The arrest (generally obtained by court order) will remain in effect until the claim is satisfied, ultimately out of the sale proceeds of the drillship if no other source is available or until satisfactory security is provided for the claim (generally by way of bank letter of credit or guarantee).

67. Although some of the Critical Vendors generally waived their rights to assert liens against the Debtors' drillships when they agreed to provide prepetition goods, certain counterparties may fail to abide by the terms of their relationship with the Debtors. Thus, upon the Debtors' filing for chapter 11 relief, certain creditors of the Debtors may seek to arrest drillships in order to obtain security for their claims.

68. Accordingly, a salvor or supplier of goods or services who is owed money by the shipowner and who (rightly or wrongly) may seek an order for the arrest of a drillship. Such arrests almost inevitably have a ripple effect, as other creditors arrest further ships and insist that their claims be paid in full before the drillships are released. Such a scenario could put a severe cash strain on the Debtors since drillships under arrest will be unable to perform under the Debtors' drilling contracts (and may have their charters cancelled). This cash strain is only exacerbated by suppliers' customary requirement that a shipowner in financial difficulty be supplied goods on cash terms alone. Accordingly, I believe that the only means of avoiding such difficulties is to pay the Critical Vendor Claims in full at the time of filing, thus depriving potential claimants of the ability to arrest drillships.

69. Further, the Debtors request authorization to enter into vendor agreements, in substantially the form attached to the motion (each a "Vendor Agreement") when the Debtors determine, in the exercise of their reasonable business judgment, that is appropriate to do so; *provided* that the Debtors' decision not to enter into a Vendor Agreement will not prevent them from paying a Critical Vendor Claim when, in the exercise of their reasonable business judgment, such payment is necessary to the Debtors' reorganization. The Debtors propose that Vendor Agreements provide, among other things, that the Critical Vendor will continue to

provide trade terms consistent with the historical prepetition trade terms between the parties or on such other terms as the Debtors may approve in their sole discretion. In the event a Critical Vendor fails to comply with the terms and provisions of a Vendor Agreement, the Debtors also request authorization to, in their sole discretion, terminate such Vendor Agreement with such termination effective five business days after the date the Debtors provide written notice (with electronic mail being sufficient); *provided* that such Vendor Agreement may be reinstated if: (a) the Debtors' determination is reversed by the Court for good cause shown that the determination was materially incorrect after notice and hearing on a motion filed by the applicable Critical Vendor; (b) the underlying default under the Vendor Agreement is cured within five business days after the Debtors provide written notice of termination; or (c) the Debtors, in their sole discretion, agree to reinstate the Vendor Agreement.

70. The Debtors also request that all applicable banks and other financial institutions be authorized, when requested by the Debtors in their sole discretion, to receive, process, honor and pay any and all fund transfer requests made by the Debtors related to the Critical Vendor Claims so long as sufficient funds are available in the applicable accounts to make the payments.

71. In order to stabilize the Debtors' operations and to smoothly transition into chapter 11, I believe it is imperative that the Debtors normalize their vendor and supply relationships. Failure to do so would result in extremely adverse business effects given the current pressure on the Debtors' already strained supply chain. Under the Debtors' existing cash management system, wire and Automated Clearing House ("ACH") transfer requests can be readily identified as relating to an authorized payment made on account of the Critical Vendor Claims. Accordingly, I believe that wire and ACH transfer requests, other than those relating to

authorized payments, will not be honored inadvertently and that all applicable financial institutions should be authorized, when requested by the Debtors, to receive, process, honor and pay any and all fund transfer requests made by the Debtors related to the Critical Vendor Claims, so long as sufficient funds are available in the applicable accounts to make the payments. Any such financial institution may rely on the representations of such Debtors as to which wire or ACH transfers are made and authorized to be paid in accordance with the motion without any duty of further inquiry and without liability for following the Debtors' instructions.

Accordingly, I respectfully submit that this motion should be approved.

- iii. Motion for Interim and Final Orders (A) Authorizing, But Not Directing, the Debtors to Pay Prepetition Obligations Owed to Foreign Vendors and (B) Authorizing All Financial Institutions to Honor All Related Payment Requests

72. The Debtors have requested that the Court enter interim and final orders (A) authorizing, but not directing, the Debtors to pay prepetition obligations owed to foreign vendors and (B) authorizing all financial institutions to honor all related payment requests.

73. In the ordinary course of business, the Debtors incur various obligations to hundreds of foreign vendors that provide essential goods and services related to their business and the operation of their drillships (collectively, the "Foreign Vendors"). These Foreign Vendors include vendors located in jurisdictions throughout Africa, Asia, the Caribbean, Europe, the Middle East, Oceania, and South America. I have been informed that all or almost all of the Foreign Vendors do not have a presence in the United States. The Debtors estimate that the aggregate amount of ordinary course of business, prepetition obligations owed to Foreign Vendors is approximately \$1.7 million.

74. Certain Foreign Vendors provide crucial goods and materials to the Debtors, including fuel, hydraulic fluid, lube oils and greases, communication systems, drillship

positioning systems, drilling equipment, subsea equipment, topside equipment, tubulars, risers, safety equipment, power management systems, electrical equipment, contract cables, fingerboard latches, IT, controls, general consumables, foodstuffs and charts and publications necessary for the operation of the Debtors' drillships. In addition, given the Debtors' global footprint, there are many foreign service providers located in jurisdictions across the world that perform services vital to the Debtors' business. In certain jurisdictions outside of the United States, the Debtors rely on key foreign service providers to ensure their business operates efficiently and in accordance with applicable law. Services provided by Foreign Vendors include maintenance and repair services, labor, customs clearance and immigration services, safety inspections, waste management, storage and freight forwarding.

75. The goods and services provided by Foreign Vendors are necessary for the Debtors' continued excellence in safety performance. A safety failure could result in loss of life, personal injury, environmental damage, shutting down of operations, loss of revenue, destruction of property, litigation and negative publicity. If the provision of goods and services from Foreign Vendors were interrupted, I believe the safety of the Debtors' employees and others could be compromised and the Debtors could be in violation of regulations or environmental laws.

76. Significantly, all or almost all of the Foreign Vendors do not have a presence in the United States, and therefore may not consider themselves subject to the jurisdiction of the Court or provisions of the Bankruptcy Code that otherwise protect the Debtors' assets and business operations. Absent payment of prepetition amounts due to them, Foreign Vendors may commence arrest or insolvency proceedings in foreign jurisdictions, attempt to assert maritime liens on the Debtors' drillships, or otherwise attempt to seize the



Debtors' assets. In addition to the attendant costs, I believe foreign proceedings in the countries in which the Debtors operate would significantly impede the Debtors' operations and ability to generate revenues on an ongoing basis.

77. In many cases, the Foreign Vendors are the only source or the most preferred source from which the Debtors can procure certain goods and services within a timeframe and at a price that permit the Debtors to operate in the ordinary course. In addition to the risks of seizure and foreign proceedings, a failure to pay the prepetition amounts due to these Foreign Vendors would likely result in the need to obtain such goods and services elsewhere at a much higher price, if they can be obtained at all.

78. The Debtors are making every effort to avoid interruptions in their operations and the adverse effects that even a temporary break could have on their business. Even a short-term disruption in the Debtors' access to fuel or employment services from Foreign Vendors, for example, would give rise to instability and thus jeopardize the Debtors' ability to reorganize going forward. Because of the international and highly-specialized nature of the Debtors' business, Foreign Vendors may threaten that, unless their prepetition debts are paid, they will cease to supply with essential goods or services. To preserve the value of their assets, I believe the Debtors must have the ability to continue to pay their Foreign Vendors.

79. The Debtors also request that all applicable banks and other financial institutions be authorized, when requested by the Debtors in their sole discretion, to receive, process, honor and pay any and all fund transfer requests made by the Debtors related to Foreign Vendor Claims, so long as sufficient funds are available in the applicable accounts to make the payments.

80. In order to stabilize the Debtors' operations and to smoothly transition into chapter 11, it is imperative that the Debtors normalize their business. I believe failure to do so would result in extremely adverse business effects. Under the Debtors' existing cash management system, the Debtors represent that wire or ACH transfer requests can be readily identified as relating to an authorized payment made on account of Foreign Vendor Claims. Accordingly, it is my understanding that wire and ACH transfer requests, other than those relating to authorized payments, will not be honored inadvertently and that all applicable financial institutions should be authorized, when requested by the Debtors, to receive, process, honor and pay any and all fund transfer requests made by the Debtors related to Foreign Vendor Claims so long as sufficient funds are available in the applicable accounts to make the payments. Any such financial institution may rely on the representations of such Debtors as to which wire or ACH transfers are made and authorized to be paid in accordance with the motion without any duty of further inquiry and without liability for following the Debtors' instructions. Accordingly, I respectfully submit that this motion should be approved.

- iv. Motion for an Order Authorizing, But Not Directing, the Debtors to (A) Pay Certain Prepetition Compensation and Reimbursable Expenses, (B) Pay and Honor Benefits and Other Programs and (C) Continue Workforce Obligations

81. The Debtors have requested that the Court enter interim and final orders (A) authorizing, but not directing, the Debtors to (i) pay certain prepetition compensation and reimbursable expenses, (ii) pay and honor obligations relating to benefits and other programs and (iii) continue their Workforce Obligations (as defined below) on a postpetition basis and (B) authorizing, but not directing, financial institutions to receive, process, honor and pay all related payment requests solely to the extent the Debtors have sufficient funds standing to their credit with such financial institutions.

82. In the ordinary course of business, the Debtors engage the services of approximately 156 individuals (including full-time, part-time and temporary employees (collectively, the “Debtor Employees”), the Debtors’ directors (the “Board Members”) and temporary workers, who, together with any other service providers to the Debtors are the “Debtor Workforce”). The Debtor Workforce provides engineering, sales, management, legal, finance, accounting, administrative and other corporate services in Houston, Texas and internationally in Luxembourg. The Debtor Workforce’s skills, expertise and knowledge of the Debtors’ infrastructure and operations are essential to the ongoing operation of the Debtors’ businesses.

83. Additionally, the Debtors rely on the services of approximately 571 individuals engaged by certain non-Debtor subsidiaries of the Debtors to service the Debtors’ offshore drillships and provide support services. These non-Debtor subsidiaries (the “Non-Debtor Labor Subsidiaries”) employ 549 “commuter employees” to service the Debtors’ offshore drillships and 22 “non-commuter employees” to provide corporate support to the Debtors’ global operations (collectively, the “Non-Debtor Employees” and, together with the Debtor Employees, the “Employees”) and occasionally engage temporary workers (together with the Non-Debtor Employees, the “Non-Debtor Workforce”). The services of the Non-Debtor Workforce are critical to the Debtors’ ability to operate their drillships.

84. The Debtors pay the Debtor Workforce and generally provide employee health and other benefits to both the Debtor Workforce and Non-Debtor Workforce (together, the “Workforce”). Additionally, the Debtors fund their subsidiaries before those subsidiaries pay the Non-Debtor Workforce payroll. The obligations that the Debtors incur in compensating the Debtor Workforce and Non-Debtor Workforce for their services to the Debtors (collectively, the

“Workforce Obligations”) are described more fully below. The Debtors request the authority to honor the Workforce Obligations in the ordinary course of business prior to the Petition Date and to pay certain prepetition Workforce Obligations when they become due; provided that the Debtors are **not** requesting the authority at this time to (A) pay any severance to an insider<sup>7</sup> under the Severance Plan (as defined herein) that would exceed the limitations set forth in section 503(c) of the Bankruptcy Code, (B) pay any bonuses under the Performance Bonus Plan (as defined herein), (C) pay any Long-Term Incentives (as defined herein) in cash, or (D) award any new Long-Term Incentives.

85. Debtor Employee Payroll Obligations. The Debtors pay the Debtor Employees base salaries and overtime typically on a monthly or semi-monthly basis. The Debtors estimate that their monthly gross payroll to Debtor Employees is approximately \$1.6 million and that the aggregate gross amount of accrued and unpaid base salaries and overtime pay for the Debtor Employees as of the Petition Date is approximately \$15,000. The Debtors do not believe that any member of the Debtor Workforce is owed prepetition amounts that exceed the \$12,850 statutory cap provided by section 507(a)(4) of the Bankruptcy Code.

86. Additionally, in the ordinary course of business, the Debtors perform annual salary reviews to evaluate, and in some cases increase, the level of base salaries paid to their Debtor Employees to the extent necessary to bring the salaries in line with market level or to reflect increased responsibilities. Following the Debtors’ annual salary review in 2017, the Debtors’ estimated average salary will increase by 3%, effective January 1, 2018.

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<sup>7</sup> The Debtors’ insiders consist of the Debtors’ non-employee directors, all Employees designated as “senior management” in the Pacific Drilling S.A. Form 20-F in 2017, and all Employees who, as of the Petition Date or during these chapter 11 cases, occupy the positions listed as “senior management” in the Pacific Drilling S.A. Form 20-F in 2017.

87. Debtor Employee Deductions, Withholdings and Payroll Taxes. The Debtors are required by law to withhold from Debtor Employees' paychecks certain amounts related to taxes imposed by applicable law, to remit any such withheld amounts to the appropriate taxing authorities, and to make certain additional payments from their own funds in connection with such withholding taxes. The Debtors estimate that they withhold and contribute approximately \$420,000 per month in payroll taxes. In the ordinary course of processing payroll checks for Debtor Employees, the Debtors withhold approximately \$175,000 per month for other withholdings and deductions and remit those amounts to the appropriate third-party recipients. As of the Petition Date, the Debtors do not believe that they owe any amounts for unremitted payroll taxes and other withholdings and deductions.

88. Non-Debtor Labor Subsidiaries' Payroll Obligations. The Debtors fund the amounts to be paid by the Non-Debtor Labor Subsidiaries to the Non-Debtor Workforce in advance of each Non-Debtor Labor Subsidiary's monthly or semi-monthly payroll. In October 2017, the Debtors' aggregate monthly payment to the Non-Debtor Labor Subsidiaries in respect of the Non-Debtor Workforce was approximately \$6.9 million. The Debtors do not believe that, as of the Petition Date, any prepetition amounts are due to the Non-Debtor Labor Subsidiaries in respect of the Non-Debtor Workforce but estimate that approximately \$1.9 million has accrued in respect of Non-Debtor Workforce prepetition services. No member of the Non-Debtor Workforce has accrued prepetition amounts that exceed the \$12,850 statutory cap provided by section 507(a)(4) of the Bankruptcy Code.

89. Health and Welfare Plans. The Debtors offer eligible Debtor Employees and Non-Debtor Employees benefits under three medical plans worldwide, a U.S. dental plan and a vision plan. The Debtors estimate that their average monthly cost under the medical plans

is \$427,000, under the dental plan is \$30,000 and under the vision plan is \$6,000. The Debtors also provide life, accidental death and dismemberment, short-term disability and long-term disability insurance benefits and an employee assistance program. As of the Petition Date, the Debtors estimate that they owe approximately \$61,000 on account of these welfare plans.

90. Vacation, Paid Time Off and Leaves of Absence. The Debtors provide eligible Employees with certain paid leave benefits, including medical, vacation and holiday leave. As of the Petition Date, the Debtors estimate that the aggregate value of accrued and unused paid leave benefits was approximately \$1.0 million.

91. Retirement Programs. In the ordinary course of business, the Debtors provide defined contribution retirement benefits to Employees (the “Retirement Program”). The Debtors estimate that their October 2017 aggregate monthly matching contributions to the Retirement Program were approximately \$250,000. As of the Petition Date, the Debtors estimate that the aggregate amount owed in respect of the Retirement Program is approximately \$50,000.

92. Severance Plan. PDSI sponsors the Pacific Drilling Severance Plan (the “Severance Plan”), pursuant to which all full-time Employees are eligible for severance benefits on an involuntary termination of employment other than for “cause” (as defined in accordance with the Severance Plan). As of the Petition Date, the Debtors do not believe that any prepetition severance is owed to non-insider or insider Employees.

93. Travel and Reimbursable Expenses. The Debtors pay approximately \$100,000 per month to Global Transportation Limited for travel for their Debtor Workforce<sup>8</sup> and reimburse approximately \$20,000 per month in respect of business expenses directly to the

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<sup>8</sup> Travel expenses incurred by the Non Debtor Workforce are included in the cost of retaining the Non Debtor Workforce, which the Debtors fund to the Non-Debtor Labor Subsidiaries as described herein.

Debtor Workforce. As of the Petition Date, the Debtors estimate that approximately \$100,000 is owed in respect of prepetition travel expenses and approximately \$40,000 is owed on account of prepetition reimbursable expenses.

94. Expatriate Expenses. The Debtors provide expatriate Debtor Employees certain benefits in connection with their foreign assignment. The Debtors estimate that they pay, on average, approximately \$50,000 per month directly to the Debtor Workforce in respect of these expenses. As of the Petition Date, the Debtors estimate that approximately \$20,000 is owed in respect of expatriate expenses.

95. Employee Incentive Programs. The Debtors historically have maintained an entirely performance-based annual incentive plan (the "Performance Bonus Plan") and have provided a portion of certain Debtor Employees' total annual target compensation opportunity in the form of long-term incentive awards (the "Long-Term Incentives"). As discussed above, the Debtors are **not** requesting the authority at this time to (A) pay any bonuses under the Performance Bonus Plan, (B) pay any Long-Term Incentives in cash, or (C) award any new Long-Term Incentives.

96. Third Party Providers. The Debtors engage with third-party service providers for various services, including payroll processing; the provision of welfare and retirement benefits under the Debtors' plans; Workforce training; managing employee-related protection and indemnity claims relating to the Debtors' drillships; hiring; and administrative services (collectively, the "Third Party Providers"). The Debtors pay approximately \$384,500 per month to the Third Party Providers. As of the Petition Date, the Debtors estimate that approximately \$383,000 is accrued in respect of prepetition services by the Third Party Providers.

97. Targeted Retention Awards to Non-Insiders. From time to time, the Debtors have granted retention awards to key Employees (the “Non-Insider Retention Awards”) in order to incentivize those Employees to remain employed with the Debtors. All such awards are subject to the Employee’s continued employment or an earlier termination of employment without “cause.” Currently, 122 Employees, none of whom are insiders, have outstanding retention awards with an aggregate value of approximately \$3.3 million (for 103 Debtor Employees) and approximately \$1.7 million (for 19 Non-Debtor Employees).

98. Contract Worker Obligations. From time to time and in the ordinary course of business, the Debtors contract with independent contractors and third-party labor staffing agencies (collectively, the “Third Party Staffing”) to engage contract workers to provide temporary corporate support services and supplemental labor to certain Debtor drillships in operation. As of October 31, 2017, the Debtors had contracted for approximately 22 contract workers. The Debtors estimate that the aggregate gross amount of accrued and unpaid obligations owed to the Third Party Staffing on account of contract workers is approximately \$270,000.

99. Director Compensation. PDSA’s Board is comprised of eight Board Members.<sup>9</sup> Each Board Member receives a \$192,000 annual cash retainer. In addition, the Chairman of the Board receives a \$76,000 annual retainer and the Vice Chairman of the Board receives a \$60,000 annual retainer. For their services to the Debtors in leading Board committees, the chair of each of the audit and compensation committees receives an additional \$32,000 annual retainer and the chair of the nominating committee receives an additional

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<sup>9</sup> Three of these Board Members are affiliated with PDSA’s majority shareholder, Quantum Pacific (Gibraltar) Limited. The retainers and fees (as described herein) due to those Board Members are paid directly to Quantum Pacific (Gibraltar) Limited.



\$16,000 annual retainer. For their work on Board committees, Board Members also receive a \$180,000 annual retainer as a member of the restructuring committee, a \$16,000 annual retainer as a member of each of the audit and compensation committees and a \$8,000 annual retainer as a member of the nominating committee. These retainers are paid on a quarterly basis and a portion of amounts payable are withheld and remitted to Luxembourg tax authorities. The other Debtors are governed by boards of directors in accordance with local law requirements. The estimated aggregate annual fees paid in respect of such directors' service on the Debtors' various boards are approximately \$75,000<sup>10</sup> (all retainers and fees paid to the Board Members and directors of the Debtors, the "Director Compensation"). As of the Petition Date, the Debtors estimate that the aggregate gross amount of accrued and unpaid amounts owed in respect of prepetition Director Compensation is approximately \$300.

100. I believe the Workforce constitutes one of the Debtors' most fundamental and valuable assets and is essential to the successful operation of the Debtors' business and to the Debtors' successful reorganizations. Absent an order granting the requested relief, many members of the Workforce will suffer undue hardship and, in many instances, face serious financial difficulties, as the payments and benefits in question may be needed to enable certain Workforce members to meet their own personal obligations. Moreover, an inability to pay the Workforce in the ordinary course may irreparably undermine the stability of each and all of the Debtors' ongoing operations and prevent their successful reorganizations.

101. I have no doubt that the Debtors' ability to preserve their business and assets and to maximize value through these chapter 11 cases will be adversely affected if the

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<sup>10</sup> One Debtor, Pacific Sharav Korlátolt Felelősségű Társaság, was recently formed and appointed a new director whose compensation for future services will be determined in the ordinary course of business.

Debtors are unable to retain a dedicated and loyal Workforce. Accordingly, it is critical that the hardship and disruption caused by the commencement of these chapter 11 cases be minimized in order to preserve morale and to maintain the Workforce's engagement. I believe that the relief requested is in the best interests of the Debtors' estates and will enable the Debtors to continue to operate their businesses during these chapter 11 cases without disruption so as to avoid immediate and irreparable harm to the Debtors' estates. Accordingly, I respectfully submit that interim and final orders granting the requested relief in the motion should be issued.

- v. Motion for Interim and Final Orders (A) Authorizing, But Not Directing, the Debtors to Pay Prepetition Taxes and (B) Authorizing All Financial Institutions to Honor All Related Payment Requests

102. The Debtors have requested that the Court enter interim and final orders (A) authorizing, but not directing, the Debtors, in their sole discretion, to pay prepetition taxes as they become due and (B) authorizing all financial institutions to honor all related payment requests.

103. In the ordinary course of business, the Debtors incur certain taxes and fees relating to the operation of their business and drillships, including (a) Income Taxes, (b) Franchise Taxes, (c) Property Taxes and (d) Miscellaneous Taxes and Fees (each as defined below, and collectively (a) through (d), the "Taxes") that are payable directly to taxing, registration and regulatory authorities (collectively, the "Taxing Authorities") as such payments become due. The Debtors' operations require them to pay Taxes with respect to each of their drillships to Taxing Authorities in the United States, Luxembourg, Nigeria, Liberia and Brazil.<sup>11</sup> In addition, the Debtors continue to seek out and enter into new drilling contracts in new

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<sup>11</sup> Out of an abundance of caution, the Debtors seek authority to pay Taxes in Nigeria. Although the Debtors do not currently owe Taxes in Nigeria, the Debtors may incur Taxes in Nigeria in the future.

locations, including recent contracts in the Republic of Guinea and Mauritania, and may therefore be required to pay Taxes to Taxing Authorities in those and other jurisdictions.

104. As a result of their operations throughout the world, the Debtors incur income tax liabilities in various jurisdictions (collectively, "Income Taxes"). The Debtors estimate that their prepetition liability for United States Federal Income Taxes is approximately \$1,300,000, due on December 15, 2017. In addition, the Debtors estimate that their prepetition liability for Luxembourg corporate and municipal Income Taxes is approximately \$3,200,000.

105. The Debtors are also required to pay taxes assessed for the privilege of doing business within a particular jurisdiction ("Franchise Taxes"). Franchise Taxes are paid annually to Taxing Authorities in Texas and Delaware. The Debtors estimate that their prepetition liability for Franchise Taxes is approximately \$300,000.

106. The Debtors own certain personal property in Texas that is subject to local property taxes ("Property Taxes"). Additionally, the Debtors may incur Property Taxes for the storage of certain equipment. The Property Taxes are assessed in estimated amounts at the beginning of the year, and the Debtors remit payments on such estimated amounts to the appropriate Taxing Authority on an annual basis. The Debtors estimate that their prepetition liability for Property Taxes is approximately \$40,000.

107. Finally, the Debtors also incur and pay in the ordinary course of operating their business certain value added taxes, regulatory assessments, drillship registration fees, permitting fees, licensing fees, levies, seaman credentials and other miscellaneous Taxes (collectively, "Miscellaneous Taxes and Fees").<sup>12</sup> Although the Debtors pay certain

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<sup>12</sup> Out of an abundance of caution, the Debtors wish to make clear that the Miscellaneous Taxes and Fees include, but are not limited to, annual registration fees owed to the Republic of Liberia and fees owed to the Liberian International Ship & Corporate Registry Seafarer's Identification and Certification Division.

Miscellaneous Taxes and Fees directly to the appropriate Taxing Authority, the Debtors, when required by local law, withhold certain Miscellaneous Taxes and Fees from payments to vendors and remit to the appropriate Taxing Authority. I believe that the continued payment of Miscellaneous Taxes and Fees, including any such taxes due and owing on account of prepetition Miscellaneous Taxes and Fees, are a necessary cost of continuing to operate their business. Accordingly, the Debtors request authority to pay any such amounts, including Miscellaneous Taxes and Fees that accrued prepetition, as they come due in the ordinary course of business.

108. Although I have been informed that the Debtors are current on all of their Taxes that have become due as of the Petition Date, a lag between the time when the Debtors incur an obligation to pay the Taxes and the date such Taxes become due and payable may exist. As a result, some Taxing Authorities may have claims against the Debtors for Taxes that have accrued but remain unpaid as of the Petition. Furthermore, the Debtors may be subject to an audit of any open tax year, which could result in additional Tax liabilities. Out of an abundance of caution, to the extent that the Debtors have (i) miscalculated the amounts due on account of Taxes, (ii) paid an amount that was less than is actually owed for any prepetition Tax, or (iii) made any payments of Taxes prepetition that were rejected, lost, or otherwise not received in full by any Taxing Authority, the Debtors request authority to pay any additional amounts for Taxes that may become due during the pendency of the Chapter 11 Cases.

109. Failure by the Debtors to pay applicable Taxes may result in, among other things, the imposition of maritime liens on the Debtors' property for any accrued and unpaid amounts. Any such liens potentially entitle the relevant Taxing Authorities to a secured claim against property of the relevant Debtor's estate. Paying such Taxes will therefore affect only the timing of the payments, and not the amounts that the Debtors would ultimately have to pay.

110. Unpaid Taxes may also result in the invalidation of a drillship's certificate of registry as well as other penalties against the Debtors, disrupting the Debtors' ability to operate their drillships, use property of their estates and otherwise conduct business in the ordinary course. By paying prepetition Taxes as they become due, I believe the Debtors will avoid unnecessary disputes and possible litigation with the Taxing Authorities, and avoid the expense and distraction of attending to these and other consequences of failing to pay applicable Taxes as they become due.

111. The Debtors also request that all applicable banks and other financial institutions be authorized, when requested by the Debtors in their sole discretion, to receive, process, honor and pay any and all fund transfer requests made by the Debtors related to prepetition Taxes, so long as sufficient funds are available in the applicable accounts to make the payments.

112. In order to stabilize the Debtors' operations, and to smoothly transition into chapter 11, I believe it is imperative that the Debtors normalize their business. Failure to do so would result in extremely adverse business effects. Under the Debtors' existing cash management system, the Debtors represent that wire and ACH transfer requests can be readily identified as relating to an authorized payment made on account of prepetition Taxes. Accordingly, I have been informed that wire and ACH transfer requests, other than those relating to authorized payments, will not be honored inadvertently and that all applicable financial institutions should be authorized when requested by the Debtors, to receive, process, honor and pay any and all fund transfer requests made by the Debtors related to prepetition Taxes so long as sufficient funds are available in the applicable accounts to make the payments. Any such financial institution may rely on the representations of such Debtors as to which wire and ACH

transfers are made and authorized to be paid in accordance with the motion without any duty of further inquiry and without liability for following the Debtors' instructions.

113. Accordingly, I believe that the Debtors should be authorized to make payments to the relevant Taxing Authorities for any accrued and unpaid prepetition Taxes, as and when they become due, in the ordinary course of business, and the Debtors' financial institutions should be authorized to honor all related payment requests.

- vi. Motion for Interim and Final Orders (A) Authorizing, But Not Directing, the Debtors to Continue Prepetition Insurance Policies and Pay Prepetition Obligations Relating Thereto, (B) Authorizing All Financial Institutions to Honor All Related Payment Requests and (C) Modifying the Automatic Stay to Permit the Debtors' Employees to Proceed with Workers' Compensation Claims

114. The Debtors have requested that the Court enter interim and final orders (A) authorizing, but not directing, the Debtors, in their sole discretion, to continue to administer their prepetition insurance policies and to pay prepetition obligations relating thereto, including brokers' fees arising thereunder or in connection therewith, to the extent the Debtors determine that such payments are necessary or appropriate to maintain adequate insurance coverage for the Debtors' estates and assets, (B) authorizing financial institutions to receive, process, honor and pay all related electronic payment requests, solely to the extent the Debtors have sufficient funds standing to their credit with such financial institutions and (C) modifying the automatic stay to permit the Debtors' employees to proceed with Workers' Compensation Claims (as defined below).

115. In the ordinary course of their business, the Debtors maintain an insurance program (the "Insurance Program") that provides millions of dollars of coverage for the Debtors' operations around the globe. The Insurance Program includes a marine insurance program, protection and indemnity insurance policies, a management liability program and an onshore

liability program (collectively, the “Insurance Policies”). As of the Petition Date, the Debtors are current on their premiums and there are no outstanding premiums due that have not been paid.

116. The premiums the Debtors pay to procure and maintain the Insurance Program consist of certain premiums that are fixed at the beginning of the period during which the Debtors are insured (the “Policy Period”) and other premiums that can be renegotiated during the Policy Period at the Debtors’ sole election. In addition, certain premiums are estimated and adjusted based on losses incurred in previous Policy Periods.

117. In 2017, the Debtors paid premiums on Insurance Policies of approximately \$11.6 million in the aggregate. These include \$3.0 million of advance annual or semi-annual premiums, \$7.8 million of annual quarterly or four month installment premiums and \$800,000 of other premiums. The Debtors are currently negotiating several Insurance Policies that will provide coverage in 2018, but expected to pay approximately the same amount in premium payments in the next 12 months. As of the Petition Date, the Debtors do not believe that there are any amounts due to Carriers on the Insurance Policies.

118. The Debtors’ Insurance Program is managed through four insurance brokers: McGriff Seibels & Williams (“McGriff”), Lloyd & Partners (“Lloyd”), JLT Specialty Bermuda (“JLT”) and YOA Insurance Broker Limited (“YOA”, and collectively with McGriff, JLT and Lloyd, the “Brokers”). The Brokers assist the Debtors in determining the appropriate types and amounts of insurance coverage for their business and assets and then negotiate with insurance companies on the Debtors’ behalf to procure the optimal policies. In addition,

premiums are generally paid to the Brokers who then remit such payments to the Carriers.<sup>13</sup> The Brokers receive an annual brokerage fee. For the current year, which runs April 1, 2017 through March 31, 2018, an annual brokerage fee in the amount of approximately \$76,500 was paid to YOA. Annual fees of approximately \$320,000 and \$200,000 are being paid in quarterly installments to McGriff and Lloyd, respectively, in 2017.

119. Certain of the Insurance Policies provide coverage to both the Debtors and the Debtors' non-debtor subsidiaries and their assets. PDSA and PDSI, a subsidiary of PDSA and a Debtor in the Chapter 11 Cases, are the named parties on the majority of the Debtors' Insurance Policies. PDSI maintains, among others, workers' compensation coverage ("Workers' Compensation Insurance"), employer liability, general liability, foreign liability, non-owned automobile, non-owned aviation and other Insurance Policies which benefit non-debtor subsidiaries. The Debtors are required to maintain Workers' Compensation Insurance under the laws of the states and localities in which they have onshore employees, and such insurance provides the Debtors with coverage for onshore employees' claims arising from or related to employment by the Debtors ("Workers' Compensation Claims"). In addition, the Debtors maintain protection and indemnity Insurance Policies to cover similar claims brought by offshore crew members.

120. The Debtors, in the ordinary course of their business, pay the required premiums and account for their non-debtor subsidiaries' share of the shared Insurance Policies' premiums through the creation of intercompany obligations owed to a Debtor by the relevant

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<sup>13</sup> Some exceptions exist. For example, the Debtors pay premiums directly to the Carrier of their U.S. Workers' Compensation insurance.



non-debtor subsidiary.<sup>14</sup> By obtaining the required insurance coverage for Debtors and non-debtor subsidiaries on a combined basis, the Debtors have been able to realize substantial savings and efficiencies in the cost of their Insurance Program. In the areas that these Insurance Policies cover it would not be feasible to separate out the Debtors' operations and other insurance needs from those of their non-debtor subsidiaries and to obtain new separate insurance coverage for the Debtors and their non-debtor subsidiaries, respectively, at a reasonable cost or within a reasonable time frame without exposing the Debtors and their operations to significant risk of disruption and increased expense from any material disruption of the Insurance Program.

121. In many cases, the coverage provided by the Insurance Policies is required by various regulations, laws and contracts that govern the Debtors' business conduct under applicable non-bankruptcy law. In addition, the terms of the Debtors' financing documents require the Debtors to maintain adequate insurance coverage. Such coverage could not be provided without the continuation of the entire Insurance Program.

122. I believe failure to pay premiums when due may harm the Debtors' estates in several ways. First, the Carriers may refuse to renew the Debtors' Insurance Policies, which will require the Debtors to obtain replacement policies and possibly to reconfigure their risk management program. This in turn would require the commitment of significant resources and could result in less favorable coverage or terms from the Debtors' insurers. Second, the Carriers could attempt to terminate the Debtors' existing Insurance Policies, which could create uncertainty as to the Debtors' ability to continue operating their business given the myriad

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<sup>14</sup> In addition, in certain instances, the Debtors pay the premiums on certain Insurance Policies that provide coverage exclusively to the Debtors' non-debtor subsidiaries. An intercompany payable is created on account of the Debtors' payments in these instances. For the avoidance of doubt, I wish to make clear that the motion seeks the authority to allow the Debtors to continue paying premiums on account of their non-debtor subsidiaries' Insurance Policies.

regulatory and contractual requirements imposed on the Debtors to maintain specific amounts and types of insurance coverage. Any purported termination of the Debtors' Insurance Policies and any material change in the terms thereof would place additional risk on the Debtors and other parties who benefit from the Debtors' Insurance Policies.

123. I believe the Insurance Policies are essential to the preservation of the value of the Debtors' business, properties and assets, and their ability to successfully prosecute the Chapter 11 Cases. The Insurance Policies protect the Debtors and other parties in interest from losses caused by casualty, natural disaster, fraud or another unforeseen event. Therefore, it is in the best interests of the estates to continue to maintain the Insurance Policies and to pay any outstanding prepetition insurance premiums necessary to do so, as well as to revise, extend, supplement or change insurance coverage, as necessary. Accordingly, I believe that the Debtors should be authorized to continue to maintain the Insurance Policies and to pay any outstanding prepetition insurance premiums necessary to do so, as well as to revise, extend, supplement or change insurance coverage, as necessary.

124. I have been informed that cash reserves and cash flows from operations will be sufficient to pay postpetition obligations related to the Insurance Policies. Also, under the Debtors' existing cash management system, the Debtors represent that wire and ACH transfer requests can be readily identified as relating to an authorized payment made on account of the Insurance Policies. Accordingly, I have been informed that wire and ACH transfer requests, other than those relating to authorized payments, will not be honored inadvertently and that all applicable financial institutions should be authorized when requested by the Debtors, to receive, process, honor and pay any and all wire transfer or ACH transfer requests with respect to the Insurance Policies, solely to the extent the Debtors have sufficient funds standing to their credit

with such financial institutions. Any such financial institution may rely on the representations of such Debtors as to which wire and ACH transfers are made and authorized to be paid in accordance with the motion without any duty of further inquiry and without liability for following the Debtors' instructions.

125. In addition, the Debtors request that Court modify the automatic stay to permit the Debtors' employees to proceed with Workers' Compensation Claims. If the Debtors' employees hold valid Workers' Compensation Claims, the Debtors seek authority, under section 362(d) of the Bankruptcy Code to permit those employees to proceed with their Workers' Compensation Claims, each in the appropriate judicial or administrative forum; *provided, that* employees may only pursue their claims in accordance with the terms of the Debtors' prepetition Workers' Compensation Insurance policies. There is cause to modify the automatic stay because staying the Workers' Compensation Claims could cause employee departure or otherwise harm employee morale, which could severely disrupt the Debtors' business and prevent a successful reorganization. Accordingly, I believe the Court should (a) modify the automatic stay as it relates to valid Workers' Compensation Claims to allow any such claims to proceed to resolution and (b) waive the corresponding notice requirements under Bankruptcy Rule 4001(d). The Court should also grant the Debtors authority, if required by law or under the Workers' Compensation Insurance, to pay all or part of a claim related thereto directly to an employee, any of his or her medical providers, or any of his or her heirs or legal representatives, as set forth in the applicable law or policy.

126. The Debtors also request that all applicable banks and other financial institutions be authorized, when requested by the Debtors in their sole discretion, to receive, process, honor and pay any and all fund transfer requests made by the Debtors related to the

Insurance Policies, so long as sufficient funds are available in the applicable accounts to make the payments.

127. In order to stabilize the Debtors' operations and to smoothly transition into chapter 11, it is imperative that the Debtors normalize their business. Failure to do so would result in extremely adverse business effects. Under the Debtors' existing cash management system, the Debtors represent that wire and ACH transfer requests can be readily identified as relating to an authorized payment made on account of the Insurance Policies. Accordingly, the Debtors believe that wire and ACH transfer requests, other than those relating to authorized payments, will not be honored inadvertently and that all applicable financial institutions should be authorized, when requested by the Debtors, to receive, process, honor and pay any and all fund transfer requests made by the Debtors related to the Insurance Policies, so long as sufficient funds are available in the applicable accounts to make the payments. Any such financial institution may rely on the representations of such Debtors as to which wire or ACH transfers are made and authorized to be paid in accordance with this Motion without any duty of further inquiry and without liability for following the Debtors' instructions.

- vii. Motion for Interim and Final Orders (A) Authorizing, but not Directing, the Debtors, in their Sole Discretion, to Pay for Certain Future Utility Services, (B) Prohibiting Utility Providers from Altering or Discontinuing Service on Account of Outstanding Prepetition Invoices, (C) Establishing Procedures for Determining Adequate Assurance of Payment for Future Utility Services and (D) Authorizing All Financial Institutions to Honor All Related Payment Requests

128. The Debtors have requested that the Court enter interim and final orders (A) authorizing, but not directing, the Debtors, in their sole discretion, to pay for certain future utility services, (B) prohibiting utility providers from altering or discontinuing service on

account of outstanding prepetition invoices and (C) establishing procedures for determining adequate assurance of payment for future utility services.

129. To operate their business and manage their properties in the ordinary course, the Debtors incur utility expenses for telecommunications and other utility services (collectively, the “Utility Services”)<sup>15</sup> from approximately 12 providers (collectively, the “Utility Providers”). A nonexclusive list of Utility Providers that provide Utility Services to the Debtors as of the Petition Date is attached to the motion as Exhibit C (the “Utility Services List”). The Debtors pay these Utility Providers on a monthly basis.

130. It is my understanding that Debtors have a good historical payment record with the Utility Providers and there are no material defaults or significant arrearages for the Debtors’ undisputed invoices for prepetition Utility Services, other than payment interruptions that may have been caused by the commencement of the Chapter 11 Cases. Based on a monthly average for July through September of this year, the Debtors estimate that their cost of Utility Services for the next 30 days will be approximately \$92,090.

131. Uninterrupted Utility Services are essential to the Debtors’ ongoing operations (including the safety and security of their personnel) and, therefore, the success of the Debtors’ reorganization. Should any Utility Provider alter, refuse, or discontinue service, even for a brief period of time, the Debtors’ business operations could be severely disrupted. The Debtors operate a complex global business with significant operations in numerous countries around the world. Interruption of the Utility Services provided at any of their locations would

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<sup>15</sup> In addition to the Utilities Services charged directly to the Debtors, the Debtors also receive water, steam, sewage, waste disposal, gas, electricity and ventilation services as part of their lease of office space in Houston, Texas. Since the providers of these utility services do not contract directly with the Debtors, these services are not included in the relief sought through the motion.

disrupt necessary communication and coordination between the Debtors' employees, vendors, customers, and various regulatory authorities, and would prevent the provision of necessary support to these same parties. Such interruption would negatively impact the Debtors' reorganization efforts and all parties in interest.

132. The Debtors intend to pay postpetition obligations owed to the Utility Providers in a timely manner. The Debtors expect that cash reserves and cash flows from operations will be sufficient to pay postpetition obligations related to their Utility Services. Furthermore, to reassure Utility Providers of the Debtors' ability and willingness to pay for future Utility Services, the Debtors propose to deposit \$46,045 (the "Adequate Assurance Deposit") into a segregated, interest-bearing bank account within five business days of the entry of an Interim Order with respect to the motion. This amount represents a sum equal to the cost of two weeks' worth of the estimated aggregate annual amount of Utility Services provided by all of the Utility Providers set forth on the Utility Services List. The Debtors submit that the Adequate Assurance Deposit, in conjunction with the Debtors' cash flow from operations and cash on hand, demonstrates the Debtors' ability to pay for future Utility Services in the ordinary course of business (together, the "Proposed Adequate Assurance"). Notwithstanding the Proposed Adequate Assurance, if any Utility Provider believes additional adequate assurance is required, it may request such assurance pursuant to the procedures described in the motion (the "Adequate Assurance Procedures").

133. The proposed Adequate Assurance Procedures are necessary for the Debtors to carry out their reorganization efforts. If they are not approved, the Debtors could be blindsided by a Utility Provider unilaterally deciding—on or after the 30th day following the Petition Date—that it is not adequately protected and discontinuing service or making an

exorbitant demand for payment to continue service. Such discontinuation of Utility Services could put the Debtors' reorganization efforts in jeopardy.

134. The Debtors also request that all applicable banks and other financial institutions be authorized, when requested by the Debtors in their sole discretion, to receive, process, honor and pay any and all fund transfer requests made by the Debtors related to the Utility Services, so long as sufficient funds are available in the applicable accounts to make the payments.

135. In order to stabilize the Debtors' operations and to smoothly transition into chapter 11, it is imperative that the Debtors normalize their business. Failure to do so would result in extremely adverse business effects. Under the Debtors' existing cash management system, the Debtors represent that wire and ACH transfer requests can be readily identified as relating to an authorized payment made on account of the Utility Services. Accordingly, the Debtors believe that wire and ACH transfer requests, other than those relating to authorized payments, will not be honored inadvertently and that all applicable financial institutions should be authorized, when requested by the Debtors, to receive, process, honor and pay any and all fund transfer requests made by the Debtors related to the Utility Services, so long as sufficient funds are available in the applicable accounts to make the payments. Any such financial institution may rely on the representations of such Debtors as to which wire or ACH transfers are made and authorized to be paid in accordance with this Motion without any duty of further inquiry and without liability for following the Debtors' instructions.

136. The relief requested in the motion will ensure that the Debtors' operations will not be disrupted by the termination of vital Utility Services or the requests

by Utility Providers of unnecessarily large deposits that could endanger the Debtors' liquidity. In addition, I believe that the relief requested provides the Utility Providers with a fair and orderly procedure for determining requests for additional adequate assurance. Accordingly, I believe the Court should prohibit Utility Providers from altering, refusing or discontinuing the Debtors' Utility Services, and approve the Debtors' Proposed Adequate Assurance and Adequate Assurance Procedures.

I declare under penalty of perjury that the foregoing is true and correct.

Date: November 12, 2017

/s/ James A. Mesterharm

Name: James A. Mesterharm

Title: Managing Director of AlixPartners, LLP  
and the Co-Head of AlixPartners' Turnaround &  
Restructuring Services Group in the Americas



**EXHIBIT A**

**13-Week Projections**

Pacific Drilling  
 Consolidated Cash Forecast  
 (\$000's)

Forecast Week	Weekly Forecast													Weekly Total
	1	2	3	4	5	6	7	8	9	10	11	12	13	
Week Beg (Mon)	13-Nov	20-Nov	27-Nov	4-Dec	11-Dec	18-Dec	25-Dec	1-Jan	8-Jan	15-Jan	22-Jan	29-Jan	5-Feb	
Week End (Fri)	17-Nov	24-Nov	1-Dec	8-Dec	15-Dec	22-Dec	29-Dec	5-Jan	12-Jan	19-Jan	26-Jan	2-Feb	9-Feb	
Receipts	\$ 18,249	\$ -	\$ -	\$ 17,994	\$ -	\$ -	\$ -	\$ 15,675	\$ -	\$ -	\$ -	\$ -	\$ 19,434	\$ 71,352
Operating Disbursements														
Rig Operations	314	792	1,166	2,880	876	344	556	2,453	1,424	1,257	1,585	1,626	3,544	18,817
Payroll	-	-	6,113	-	1,478	-	1,275	4,838	-	1,478	-	4,396	-	19,578
Insurance	-	-	-	-	-	-	-	2,002	-	-	-	-	-	2,002
Shorebase	125	315	463	1,144	348	137	221	974	566	499	629	655	1,429	7,504
Overhead	112	282	415	1,025	312	122	198	873	507	447	564	646	1,408	6,909
Total Operating Disbursements	551	1,389	8,157	5,049	3,014	603	2,249	11,140	2,497	3,681	2,778	7,323	6,381	54,811
Debt Service	3,112	5,185	-	-	-	-	2,045	369	-	-	2,045	-	-	12,756
Professional Fees	-	-	-	-	-	-	-	-	1,413	-	-	707	-	2,120
Capital Expenditures	150	300	450	638	750	750	750	81	81	81	81	81	101	4,293
Tax	-	-	-	983	-	-	-	450	-	-	-	-	306	1,739
Net Cash Activity from Vessel Operations	\$ 14,436	\$ (6,874)	\$ (8,607)	\$ 11,324	\$ (3,764)	\$ (1,353)	\$ (5,045)	\$ 3,635	\$ (3,990)	\$ (3,762)	\$ (4,903)	\$ (8,110)	\$ 12,647	\$ (4,368)
Corporate Disbursements														
Corporate G&A	121	241	362	513	603	603	603	491	491	491	491	491	614	6,116
Professional Fees	-	-	-	-	-	99	-	-	2,022	165	-	810	-	3,096
Total Corporate Disbursements	121	241	362	513	603	702	603	491	2,513	656	491	1,301	614	9,212
<b>Net Cash Activity</b>	<b>\$ 14,315</b>	<b>\$ (7,115)</b>	<b>\$ (8,969)</b>	<b>\$ 10,811</b>	<b>\$ (4,367)</b>	<b>\$ (2,055)</b>	<b>\$ (5,648)</b>	<b>\$ 3,144</b>	<b>\$ (6,503)</b>	<b>\$ (4,418)</b>	<b>\$ (5,395)</b>	<b>\$ (9,411)</b>	<b>\$ 12,033</b>	<b>\$ (13,579)</b>
<b>Cumulative Net Cash Balance</b>	<b>\$ 339,315</b>	<b>\$ 332,200</b>	<b>\$ 323,231</b>	<b>\$ 334,042</b>	<b>\$ 329,675</b>	<b>\$ 327,619</b>	<b>\$ 321,971</b>	<b>\$ 325,115</b>	<b>\$ 318,612</b>	<b>\$ 314,193</b>	<b>\$ 308,799</b>	<b>\$ 299,388</b>	<b>\$ 311,421</b>	<b>\$ 311,421</b>
Silo A	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Silo B	50,000	50,000	50,000	50,000	-	-	-	-	-	-	-	-	-	-
Silo C	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Pool Leader	289,315	282,200	273,231	284,042	329,675	327,619	321,971	325,115	318,612	314,193	308,799	299,388	311,421	311,421
<b>Cumulative Net Cash Balance</b>	<b>\$ 339,315</b>	<b>\$ 332,200</b>	<b>\$ 323,231</b>	<b>\$ 334,042</b>	<b>\$ 329,675</b>	<b>\$ 327,619</b>	<b>\$ 321,971</b>	<b>\$ 325,115</b>	<b>\$ 318,612</b>	<b>\$ 314,193</b>	<b>\$ 308,799</b>	<b>\$ 299,388</b>	<b>\$ 311,421</b>	<b>\$ 311,421</b>
Memo: Ship Group A net post-petition balance with cash Pool Leader	\$ (406)	\$ (3,374)	\$ (8,803)	\$ (10,196)	\$ (11,678)	\$ (12,383)	\$ (15,361)	\$ (23,095)	\$ (25,463)	\$ (27,081)	\$ (30,895)	\$ (35,619)	\$ (36,099)	\$ (36,099)
Memo: Ship Group B net post-petition balance with cash Pool Leader	\$ 14,925	\$ 11,213	\$ 8,777	\$ 22,110	\$ 20,124	\$ 19,681	\$ 17,857	\$ 30,204	\$ 29,006	\$ 27,096	\$ 26,297	\$ 23,192	\$ 36,736	\$ 36,736
Memo: Ship Group C net post-petition balance with cash Pool Leader	\$ (83)	\$ (277)	\$ (1,019)	\$ (1,635)	\$ (1,931)	\$ (2,137)	\$ (2,380)	\$ (3,357)	\$ (3,782)	\$ (4,016)	\$ (4,306)	\$ (4,587)	\$ (5,004)	\$ (5,004)