EFiled: Mar 26 2018 05:11PM EDT
Filing ID 61842858
Case Number Multi-Case

IN THE SUPREME COURT OF THE STATE OF DELAWARE

IN RE TIAA-CREF INSURANCE APPEALS	) No. 478,2017 **PUBLIC VERSION**) No. 479,2017) No. 480,2017) No. 481,2017) Court Below–Superior Court of the) State of Delaware) C.A. No. N14C-05-178 JRJ (CCLD)))

ANSWERING BRIEF OF PLAINTIFFS BELOW / APPELLEES TIAA-CREF INDIVIDUAL & INSTITUTIONAL SERVICES, LLC; TIAA-CREF INVESTMENT MANAGEMENT, LLC; TEACHERS ADVISORS, INC.; TEACHERS INSURANCE AND ANNUITY ASSOCIATION OF AMERICA; AND COLLEGE RETIREMENT EQUITIES FUND REGARDING WHETHER TIAA-CREF SUFFERED COVERED "LOSS"

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Dated: March 9, 2018
Public Version: March 26, 2018

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NATURE OF THE PROCEEDINGS

TIAA-CREF,[1] the nation's leading provider of retirement investment services for people working in the academic and research fields, paid substantial premiums for a series of insurance policies to cover claims alleging errors and omissions in its business. It settled three such lawsuits, and even though the terms of its policies explicitly cover them, Insurers[2] refuse to pay, arguing that New York public policy prohibits insurance coverage for civil settlements relating to disgorgement.[3] There is no such established policy. To the contrary, New York's highest court in *J.P. Morgan Securities Inc. v. Vigilant Insurance Co.*, 992 N.E.2d 1076, 1081-82 (N.Y. 2013) ("*J.P. Morgan II*") reiterated that New York public policy poses only two exceptions to parties' freedom to contract for insurance: (1)

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[1] TIAA-CREF Individual & Institutional Services, LLC; TIAA-CREF Investment Management, LLC; Teachers Advisors, Inc.; Teachers Insurance and Annuity Association of America; and College Retirement Equities Fund ("CREF") are referred to herein as "Plaintiffs" or "TIAA-CREF."

[2] "Insurers" refers collectively to Defendants-Appellants Illinois National Insurance Company ("Illinois National"), ACE American Insurance Company ("ACE") and Arch Insurance Company ("Arch").

[3] *See* Opening Brief of Appellants Illinois National, ACE and Arch Regarding Whether TIAA-CREF Suffered Covered "Loss," dated January 26, 2018 ("Opening Brief"), at 4, 6, 18, 19, 21, 22, 23, 25, 26, 27, 29, 30, 39, 40, 45.

where coverage is sought for punitive damages; and (2) where it is established that the insured "acted with the intent to harm or injure others."

There has never been any dispute that the Underlying Actions[4] at issue here invoke neither coverage bar. Those Actions alleged negligent delays in TIAA-CREF's processing of transfer or withdrawal requests from participants' investment accounts. Although TIAA-CREF fully abided by contractual and legal requirements requiring it to value those accounts as of the date such requests were received, class plaintiffs claimed that they were entitled to any alleged appreciations in value after that date. Faced with the potential of significant class action costs and liabilities, TIAA-CREF settled and expressly disavowed any wrongdoing. Insurers denied coverage, asserting that the settlements constituted disgorgement, which they argue is uninsurable under New York law.

The Superior Court correctly held that those settlements fall within the definition of covered "Loss" in the insurance policies at issue, and were not uninsurable under any applicable public policy. This conclusion is supported by the policies' express mandate that there must be a "final adjudication" establishing

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[4] The "Underlying Actions" are *Rink v. CREF*, No. 07-CI-10761 (Ky. Cir. Ct.) (the "*Rink* Action"), *Bauer-Ramazani v. TIAA-CREF, et al.*, No. 1:09-cv-00190 (D. Vt.) (the "*Bauer-Ramazani* Action") and *Cummings v. TIAA-CREF, et al.*, No. 1:12-cv-93 (D. Vt.) (the "*Cummings* Action").

[redacted]

that TIAA-CREF was returning ill-gotten gains, before claims alleging disgorgement will be excluded from coverage. This conclusion is not inconsistent even with Insurers' cited authority, which bars coverage for disgorgement payments only when conclusively tied to a governmental order, judgment or finding that the policyholder had engaged in wrongful conduct. TIAA-CREF's civil settlements contain no such finding and thus do not implicate the public policies underlying those cases.

Finally, Insurers ignore the *J.P. Morgan* Court's recognition that, even if it had added "disgorgement" as a third category of uninsurable claims under New York law, which it did not, such a policy ban would not apply to funds that had not been retained by the policyholder but had gone to others. Here, as a matter of undisputed fact, the alleged investment gains at issue in the Underlying Actions did not reside with TIAA-CREF, but automatically flowed to non-withdrawing participants, as required by the at-cost agreements between TIAA-CREF and its accountholders.

[redacted]

SUMMARY OF ARGUMENTS

The Superior Court correctly entered summary judgment holding that the civil settlements of the Underlying Actions constitute covered losses under the insurance policies at issue and are not "uninsurable" under applicable law.

1. Denied. Although the Superior Court's ruling did not address or depend upon which party bears the burden of proof on the uninsurable Loss issue, that burden is on Insurers because: (1) as Insurers seek to apply the law of a state other than Delaware,[5] they bear the burden of proving the existence of a conflict of law; and (2) Insurers rely on a policy limitation or exclusion and therefore bear the burden of proof.
2. Denied. The New York Court of Appeals has expressly recognized that it has not yet adopted any public policy barring coverage for disgorgement claims, requiring rejection of Insurers' contention that such claims are "uninsurable" as a matter of New York law. The New York intermediate appellate cases on which Insurers rely are inapplicable, as they all involve governmental directives requiring disgorgement directly tied to findings of

[5] It is undisputed that Delaware has no public policy against insuring disgorgement payments. JA5224.

[redacted]

policyholder wrongdoing, while TIAA-CREF's civil settlements contain no such finding.

3. Denied. TIAA-CREF settled claims that it vigorously disputed for years and that were never adjudicated by any court or regulatory body. TIAA-CREF did not "agree[] to disgorge" gains that it "admittedly withheld" (Opening Br. at 7); the Underlying Action settlements were resolutions negotiated at arms-length, and TIAA-CREF paid significantly less than the original claims by reducing the size and scope of the settlement class. There is no applicable public policy prohibiting coverage for payments to settle contested civil claims merely alleging, but never proving, disgorgement. Alternatively, the Superior Court's ruling is supported by the New York Court of Appeals' determination in *J.P. Morgan II* that a settlement calling for the payment of monies that went to others does not constitute "disgorgement."

4. Denied. The insurance policies indisputably cover settlements of claims seeking a return of profits, absent a judgment or final adjudication establishing that TIAA-CREF was not legally entitled to those profits. There was no final adjudication here, only civil settlements expressly disavowing liability. Because the Superior Court's ruling involved the

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application of unambiguous policy language to the undisputed claims, proceedings and settlement terms in the Underlying Actions, there was no disputed issue of material fact requiring a jury trial.

5. Denied. Insurers' argument against coverage because TIAA-CREF was obligated to allocate its Loss as an expense to the remaining participants in its retirement plans is contrary to the policy language and the law. Pursuant to the settlement agreements, TIAA-CREF remained contractually and financially liable to the underlying class plaintiffs to pay the amount of the settlement. Insurers' construction would impermissibly render any coverage for TIAA-CREF wholly illusory, as TIAA-CREF is always required to allocate such losses among accountholders, and thus could never suffer a Loss for any claim.

[redacted]

STATEMENT OF FACTS

A. TIAA-CREF's Operations

1. The Relevant TIAA-CREF Entities

TIAA-CREF is the principal retirement system for the nation's education and research communities and is one of the largest retirement systems in the world based on assets under management. JA1001; JA0934. It is made up of a family of not-for-profit companies and companies that provide their services "at cost" to certain investment products. JA0744-877; JA0881.

TIAA is a stock life insurance corporation organized under the New York Insurance Law and a wholly-owned subsidiary of the TIAA Board of Overseers (the "Board"), a New York not-for-profit corporation. JA0858-877; JA0881 at ¶ 3. TIAA, founded with a non-profit mission, offers investment options to participants, including the TIAA Real Estate Account (the "REA"). *Id.*; JA1002.

CREF is a New York nonprofit membership corporation and companion organization to TIAA. JA0743-760. Since its inception in 1952, CREF operates on an at-cost basis, has no employees and retains no earnings. JA0845-846; JA0881 at ¶¶ 4-6. CREF's only assets are the securities held in eight investment accounts through which it offers variable annuities (the "CREF Accounts"). JA0881 at ¶ 4.

[redacted]

TIAA and/or its affiliated companies, including Services and TCIM, provided investment advisory, administrative, distribution and/or management services on an at-cost basis to the REA and the CREF Accounts (the "At-Cost Accounts"). JA0743-0842; JA0881 at ¶ 6; JA0896; JA0922; JA935; JA1000; JA1003; JA1751 at 19:19-19:25; JA1737 at 25:1-26:4; JA1740 at 59:9-18; JA1724-26 at 114:5-115:17, 159:18-162:9, 165:1-20; JA1739-45 at 43:20-44:10, 63:10-66:7, 85:11-86:11; JA1176 at No. 8. Insurers refer to Services, a registered broker-dealer, as a "for-profit" entity. Opening Br. at 10. They ignore, however, that with respect to the transactions at issue, TIAA, Services and TCIM were contractually obligated to provide their services on an at-cost basis, charging the Accounts only for the expenses actually incurred in providing such services, without any profit (the "At-Cost Agreements"). *Id.*

2. TIAA-CREF's Calculation and Allocation of Transactional Fund Expense

At-Cost Account holders may request a transfer of their funds to another investment option, or request a withdrawal. Such a transfer or withdrawal requires, first, determination of the value of the units (or shares) for the Account in question as of the "Good Order Date," which is either the day that all documents needed to process the request have been received in good order, or an agreed-upon future

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business day. JA0976-977; JA1056-57; JA1750-51 at 17:19-18:2, 18:23-19:25; JA0882 at ¶¶ 9-10. The value of the redeemed unit(s) as of the Good Order Date is the price that the participant ultimately receives, whenever the actual payment is made.[6] *Id.*; JA1720-1723 at 58:20-60:24, 69:11-70:6; JA1740-41 at 61:20-62:24.

As a result of daily market fluctuations, the value of the units on the date the transaction is actually processed (the "Processing Date") may be different from the value on the Good Order Date. JA1740-41 at 61:20-62:9; JA0882 at ¶ 11. Any difference – positive or negative – in the value of the units on the Processing Date and the amount paid to the account holder is referred to as the "Transactional Fund Expense," or "TFE." JA0882-83 at ¶¶ 11-12; JA0896; JA0922; JA1749-50 at 12:21-13:9, 14:14-17. If the value of the units rises between the Good Order Date and the Processing Date, there is a TFE gain; if the value of the units falls, there is a TFE loss. JA1726-27 at 165:1-166:14; JA0882-83 at ¶¶ 11-12.

All TFE is recorded as one of many operational expenses on TIAA's general ledger, netted with other operational expenses and allocated to the At-Cost

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[6] This valuation process is driven by Rule 22c-1 of the Investment Company Act of 1940, and disclosed in the CREF Accounts prospectuses. JA0975-77.

[redacted]

Accounts and other investment options.[7] JA0883 ¶ 13; JA1751-53 at 20:2-22:6, 28:5-23; JA1739 at 43:20-44:10; JA1741-42 at 63:10-66:8; JA1744-45 at 85:11-86:11. TFE gains decrease total expenses, while TFE losses increase total expenses. TFE is a minor component of each investment option's overall expenses, measured in fractions of a basis point, and is immaterial with respect each investment option's net asset value. JA1727 at 167:21-22; JA1754 at 32:10-33:2; JA0883 at ¶ 14; JA1721 at 62:14-64:11; JA1726-27 at 165:1-167:19. Pursuant to the At-Cost Agreements, all expenses allocated to the At-Cost Accounts, including TFE, are passed through to current participants as a component of those Accounts' total expenses. JA1721 at 62:14-64:11; JA1726-27 at 165:1-167:19; JA0883 ¶ 13; JA1743 at 81:3-12.

B. The Underlying Actions and Settlements

The Underlying Actions involved civil claims relating to alleged delays in processing certain participants' transfer or withdrawal requests and the alleged failure to pay such participants any appreciation in the value of those accounts between the Good Order Date and the Processing Date. None of the cases resulted

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[7] The time by which Plaintiffs must process transactions involving sales of fund shares is governed by the federal securities laws (including Rule 15c6-1 of the Securities Exchange Act of 1934), and also disclosed in the CREF Accounts prospectuses. JA0925-1160.

[redacted]

in any finding in any form that TIAA-CREF acted improperly; to the contrary, in each case, either the court, the underlying plaintiffs, or both, acknowledged not only that TIAA-CREF had defended against the claims, but that they may have prevailed at trial on their defenses.

1. The *Rink* Action and Settlement

The *Rink* Action was filed on October 29, 2007. It alleged various state law claims against CREF for the failure to process transactions within a promised seven day period, and sought, among other relief, actual damages, as well as costs and attorneys' fees. JA1285-96. In December 2010, the court certified *Rink*'s proposed class after limiting it to participants whose CREF Accounts were governed by New York law. JA1352-1389.

Insurers erroneously imply that the *Rink* court rejected TIAA-CREF's defenses. Opening Br. at 34. To the contrary, in denying motions for summary judgment, the *Rink* court held that "the question is whether CREF breached that duty and, if so, to what extent did it profit or to what extent was Rink damaged by the alleged breach," which presented "just one example of the numerous issues pending in this matter" that made summary judgment inappropriate. JA2873.

[redacted]

In May 2012, shortly before trial, at which plaintiffs alleged they would be seeking [redacted] plus punitive damages (JA1465),[8] the *Rink* Action settled. JA0599-665. In exchange for limitations on the number of class members who would be entitled to payment, and thus a smaller total settlement payment, TIAA-CREF agreed to pay qualifying plaintiffs 100% of the TFE to which they claimed – and TIAA-CREF disputed – they were entitled. JA5671-74; JA0610 at III.A. As a "compromise on both sides," the parties "shortened the class period by many years," so a significantly smaller percentage of class members qualified for those payments. JA5673-74.

A memorandum sent to Insurers in June 2012 described TIAA-CREF's reasons for the settlement, including the "hostile" *Rink* court's "strong bias" for plaintiffs' counsel, plaintiffs' seeking [redacted] at trial plus punitive damages, the court's ordering of an overbroad and prejudicial class notice, and TIAA-CREF's expectation that it would take years to ultimately prevail on appeal. JA1465. In return, the memo noted that "through settlement the parties have agreed to sanitize the notice language *and drastically reduce the class size*," and that "the expected cost of settlement is low relative to the potential outcome of a

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[8] The *Rink* plaintiffs had previously calculated their damages and made a settlement demand for [redacted] JA1346-51.

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trial." *Id.* (emphasis added). Because not all eligible participants opted in, the *Rink* settlement resulted in payments of [redacted] JA2266.

The *Rink* settlement confirmed that CREF "expressly denie[d] any wrongdoing alleged in the pleadings and d[id] not admit or concede any actual or potential fault, wrongdoing or liability." JA0605 at I.J. It also contained a formal denial of liability:

> Defendant enters into this Agreement without in any way acknowledging any fault, liability, or wrongdoing of any kind. Defendant expressly denies that it has engaged in any misconduct, and agrees to settle to avoid the continued expense and distraction of litigation. Neither this Agreement, nor any of its terms or provisions, nor any of the negotiations or proceedings connected with it, will be construed as an admission or concession by Defendant of any of the allegations in the Action, or of any liability, fault, or wrongdoing of any kind on the part of Defendant.

JA0628 at § XIV.

Contrary to Insurers' assertions, that denial of liability was not a unilateral self-serving statement at odds with any ruling in the *Rink* Action. To the contrary, in their memorandum seeking court approval of the settlement, even the *Rink* plaintiffs acknowledged that "[a]t every stage of the litigation, Defendants asserted various legal and factual defenses, and expressed their belief that Plaintiffs could not and should not prevail on the claims asserted." JA2416. The *Rink* plaintiffs further asked the court to approve the settlement in part "[b]ecause of [the Class's]

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uncertainty of prevailing at trial or on appeal and the immediate and substantial benefits the settlement would provide the Class." *Id.*

2. The *Bauer-Ramazani* Action and Settlement

On August 17, 2009, named plaintiff Norman Walker (later replaced by intervenor Christine Bauer-Ramazani) filed the *Bauer-Ramazani* Action against all Appellees in Vermont federal court. JA1513-23; JA1549-1564. The *Bauer-Ramazani* complaint alleged various violations of the Employee Retirement Income Security Act of 1974 ("ERISA") and state law claims (later dismissed) arising from the alleged failure to pay participants' alleged appreciation in value between the Good Order Date and the Processing Date, regardless of the length of any processing delay. *Id.* As in the *Rink* Action, the *Bauer-Ramazani* plaintiffs sought both compensatory damages and attorney's fees and costs, among other relief on behalf of the putative class. JA1522; JA1562-64.

In May 2013, the court certified a class of participants whose transfer or withdrawal requests for their ERISA-governed variable annuity accounts were not processed within seven days, and who had not been paid any alleged appreciation in value between the Good Order Date and Processing Date. JA1636-55. In November 2013, the court dismissed the majority of *Bauer-Ramazani's* claims on

[redacted]

summary judgment and scheduled a trial for February 2014 on the sole remaining breach of fiduciary duty claim. JA1680-1702.

On January 31, 2014, TIAA-CREF settled the *Bauer-Ramazani* Action, agreeing to pay [redacted] on a pro-rata basis, representing approximately [redacted] of the TFE amounts allocable to the class members' transactions, and agreed to pay [redacted] in class counsel fees. JA0671-701 at ¶¶ 4, 30, 61, 69; JA2445; JA2452. As with *Rink*, class plaintiffs informed the court that the settlement was reasonable given the risk that TIAA-CREF would prevail at trial. JA2440 ("[b]ecause of the uncertainty of prevailing at trial or on appeal . . . this Settlement is an excellent result for the Class and the Settlement should be approved as fair, reasonable, and adequate").

TIAA-CREF entered into the *Bauer-Ramazani* settlement without any admission of liability, and under a settlement agreement that expressly provided that "this Settlement Agreement embodies a compromise settlement of disputed claims" and that "Defendants expressly deny any liability or wrongdoing with respect to the matters alleged in the Action [and] believe and assert that they acted

[redacted]

at all times reasonably, prudently, and loyally in compliance with ERISA and other laws." JA0695-96 at ¶ 84; *see also* JA0674.[9]

C. The Insurance Policies

Defendant Illinois National sold TIAA-CREF a primary [redacted] effective April 1, 2007 to April 1, 2008 (the "Primary Policy"). JA0348-404. The remaining Insurers each issued excess insurance policies during the 2007-2008 policy period, which followed form to the terms and conditions of the respective Primary Policy. JA0477-546

The Primary Policy's Insuring Agreement promises that Illinois National will "pay the Loss of the Insured . . . for any actual or alleged Wrongful Act of any Insured" in the rendering of or failure to render Professional Services. JA0352 at § I. "Loss" is defined as "judgments and settlements" and "any Defense Costs, *provided, however* that Loss shall not include: . . . (5) matters which may be deemed uninsurable under the law pursuant to which this policy shall be construed . . ." JA0353 at § II.5.

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[9] Coverage issues relating to the *Cummings* Action were excluded from trial by stipulation of the parties, and are not at issue on this appeal. TA0690. However, with respect to the Loss and disgorgement issues, there is no difference between the three Underlying Actions, and any ruling would apply equally to *Cummings*.

[redacted]

The Primary Policy also contains an exclusion for Claims "arising out of, based upon or attributable to . . . any gaining in fact by any Insured of any personal profit or advantage to which a judgment or final adjudication or an alternative dispute resolution proceeding adverse to the Insured establishes the Insured was not legally entitled" (the "Ill-Gotten Gains Exclusion"). JA0357 at § IV(h). There is no other provision that disclaims coverage for "disgorgement" or "restitution."

D. Insurers Dispute Coverage on the Grounds That the Underlying Actions Sought Disgorgement

Despite the fact that the Underlying Actions sought disgorgement, among other relief, for more than four years after receiving initial notice of those Actions, Illinois National never once suggested that any loss related to the Actions was uninsurable. JA1766 at 159:3-160:4. Rather, it reserved the right to deny coverage only under the Ill-Gotten Gains Exclusion, and then only in the event that there was a "final adjudication" against TIAA-CREF sufficient to trigger that Exclusion. JA1321-25.

When Illinois National finally did first raise the argument that TIAA-CREF's loss was uninsurable (*after* entry and approval of the *Rink* settlement), TIAA-CREF objected, noting that "CREF did not profit or otherwise benefit from" the conduct alleged in the *Rink* Action, so there was no disgorgement. JA1477.

[redacted]

Illinois National responded that that argument had been rejected by New York's Appellate Division in *J.P. Morgan Securities Inc. v. Vigilant Insurance Co.*, 936 N.Y.S.2d 102 (N.Y. App. Div. 2011) ("*J.P. Morgan I*"). JA1493. In 2013, the New York Court of Appeals reversed the decision in *J.P. Morgan I,* and held that a settlement related to funds that the insured had not retained, but instead passed on to its investors, was not uninsurable. When TIAA-CREF advised Illinois National that its principal authority had been reversed, Illinois National refused to reconsider – even though internally its employees appreciated the impact of the reversal. JA1499; JA1502.

E. The Superior Court Rejects Insurers' Disgorgement Defense

Following discovery in this action, Insurers sought summary judgment that the Underlying Action settlements did not fall within the policy definition of "Loss" because they were disgorgement payments and thus "uninsurable" under New York law. TIAA-CREF sought summary judgment that the settlement payments constituted "Loss" and were not barred from coverage under any applicable public policy. On October 20, 2016, the Superior Court rejected Insurers' disgorgement defense, ruling that Plaintiffs' civil settlements constituted insurable Loss as a matter of law (the "Opinion"). JA5200-5244.

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The Court noted that Delaware has not articulated any public policy barring coverage for disgorgement claims, and held that it need not determine whether an actual conflict of laws existed because "the Court does not find that the settlement agreements in the Underlying Actions constitute uninsurable disgorgement under New York's public policy." Opinion at 22; JA5224. The Court held that, in each of Insurers' New York cases, there had been a consent judgment or governmental order finding that the policyholder had acted improperly, and a conclusive link between the disgorgement payment in question and the finding of wrongful conduct. Opinion at 24-25; JA5226-28. In contrast, the Court held that the undisputed record here, including the civil settlements of unresolved claims, provided no such "conclusive link" between the settlement payments and any wrongdoing on the part of TIAA-CREF:

> The facts here differ from those in *Credit Suisse*,[10] *Millennium*[11] and [*J.P. Morgan I*]. After lengthy litigation, TIAA-CREF settled, expressly denying any liability. Moreover, neither the SEC nor any other governmental entity was involved in the Underlying Actions. Defendants focus on *Credit Suisse's* language about "being ordered to

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[10] *Vigilant Ins. Co. v. Credit Suisse First Boston Corp.*, 2003 WL 24009803 (N.Y. Sup. Ct. July 8, 2003) ("*Credit Suisse I*"), *aff'd as modified*, 782 N.Y.S.2d 19 (N.Y. App. Div. 2004) ("*Credit Suisse II*").

[11] *Millennium Partners L.P. v. Select Ins. Co.*, 882 N.Y.S.2d 849 (N.Y. Sup. Ct. 2009) (*Millenium I*), *aff'd* 889 N.Y.S.2d 575 (N.Y. App. Div. 2009) (*Millenium II*).

[redacted]

> return funds." But, the *Credit Suisse* court noted, an order to return funds is different than a settlement, and "[a] different outcome [in which disgorgement payments are deemed insurable] might result when parties settle under different circumstances."
>
> *Credit Suisse, Millennium* and *J.P. Morgan* all involve conclusive links between the insured's misconduct and the payment of monies. Not so here. TIAA-CREF settled and expressly denied any liability. The Court finds no conclusive link between the settlements in the Underlying Actions and wrongdoing by TIAA-CREF that would render the settlement agreements uninsurable disgorgement.

Opinion at 27; JA5229 (footnotes omitted).

The Superior Court re-affirmed that holding on November 16, 2016 when it denied Insurers' request to certify an interlocutory appeal. TA0719-28. The Court confirmed that the settlements did not constitute uninsurable loss under TIAA-CREF's policies, and that, to the extent there was any public policy in New York against insuring disgorgement payments, it did not apply here. TA0721-22. The Court also dismissed Insurers' contention that it had overlooked certain authority, including *Reliance Group Holdings, Inc. v. National Union Fire Insurance Co. of Pittsburgh, PA,* 594 N.Y.S.2d 20 (N.Y. App. Div. 1993), *appeal denied,* 619 N.E.2d 656 (N.Y. 1993), noting that it had grounded its analysis in "more recent and germane cases," including that of New York's highest court in *J.P. Morgan II.* TA0725. Noting the trend among courts to narrow any disgorgement defense, the Court found that New York's cases did not stand for the "proposition that a civil

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settlement, free of any adjudication, finding or admission of wrongdoing, automatically comprises uninsurable disgorgement." TA0725-26. The Supreme Court also rejected Insurers' request for interlocutory appeal. TA0729-31.

ARGUMENT

I. THE SUPERIOR COURT CORRECTLY HELD THAT THE SETTLEMENTS OF THE UNDERLYING ACTIONS CONSTITUTE COVERED LOSS UNDER THE POLICIES AND THAT COVERAGE IS NOT BARRED BY ANY APPLICABLE PUBLIC POLICY

A. Counterstatement of the Question Presented

Did the Superior Court correctly determine as a matter of law that the Underlying Action settlements constitute covered Loss within the meaning of the insurance policies at issue and are insurable under the public policy of any potentially applicable jurisdiction? *See* JA0244-85; JA3194-3235, JA4797-98; JA5018-35; JA5067-75.

B. Standard and Scope of Review

The trial court's determinations of matters of law, including on a motion for summary judgment, are reviewed *de novo*. *In re Krafft-Murphy Co., Inc.,* 82 A.3d 696, 702 (Del. 2013). For decisions on cross-motions for summary judgment, the Court will review the record and draw its own conclusions as to the facts only "if the findings below are clearly wrong and if justice requires." *Fiduciary Tr. Co. of N.Y. v. Fiduciary Tr. Co. of N.Y.,* 445 A.2d 927, 930 (Del. 1982).

C. Applicable Law

To determine whether a conflict exists requiring a choice of law, a court must first "compare the laws of the competing jurisdictions to determine whether

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the laws actually conflict." *Mills Ltd. P'ship v. Liberty Mut. Ins. Co.*, 2010 WL 8250837, at *4 (Del. Super. Ct. Nov. 5, 2010) (citation omitted). If there is no actual conflict between Delaware law and that of another jurisdiction, "there is a 'false conflict,' and the Court should avoid the choice-of-law analysis altogether" by applying Delaware law. *Deuley v. DynCorp Int'l, Inc.*, 8 A.3d 1156, 1161 (Del. 2010) (citation omitted).[12]

Both Delaware and New York law enforce unambiguous contractual provisions as written and read contracts as a whole with effect given to every term.[13] While the parties agree that Delaware has no public policy barring coverage for disgorgement,[14] they disagree as to whether such a policy exists under

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[12] *See, e.g., Vichi v. Koninklijke Philips Elecs., N.V.*, 85 A.3d 725, 778 (Del. Ch. 2014); *Tyson Foods, Inc. v. Allstate Ins. Co.*, 2011 WL 3926195, at *5 (Del. Super. Ct. Aug. 31, 2011).

[13] *See Viking Pump, Inc. v. Century Indem. Co.*, 2 A.3d 76, 90 n. 38-40 (Del. Ch. 2009); *Lamberton v. Travelers Indem. Co.*, 325 A.2d 104, 106 (Del. Super. Ct. 1974), *aff'd*, 346 A.2d 167 (Del. 1975); *Kass v. Kass*, 696 N.E.2d 174, 181 (N.Y. 1998).

[14] Opinion at 22; JA5224 (Superior Court identified no case where Delaware court "has articulated [a] Delaware public policy regarding the insurability of disgorgement"); *see also U.S. Bank Nat'l Assoc. v. Indian Harbor Ins. Co.*, 2014 WL 3012969, at *4 (D. Minn. July 3, 2014) ("*U.S. Bank I*"), *aff'd*, 68 F. Supp. 3d 1044, 1049 (D. Minn. 2014) ("*U.S. Bank II*") (same); *Whalen v. On-Deck, Inc.*, 514 A.2d 1072, 1074 (Del. 1986) (Delaware public policy supports freedom to contract).

New York law. Opening Br. at 19. In light of the conclusion that the settlement agreements at issue did not constitute uninsurable disgorgement under New York law, the Superior Court did not reach the question of whether New York and Delaware law conflict. JA5224.

D. Merits of the Argument

1. Insurers Bear the Burden of Proving That the Settlements Are Uninsurable Under New York Law

The Superior Court did not address the question of burden, as it correctly held that there are no disputes of fact as to the terms of the settlements, the underlying claims or the policy language. To the extent relevant, however, Insurers bear the burden to prove that the settlements were uninsurable as a matter of New York law. As the proponent of the application of another state's law, Insurers bear the burden of proving a conflict requiring the application of substantive law other than that of Delaware. *See Sun-Times Media Grp., Inc. v. Royal & Sunalliance Ins. Co. of Canada*, 2007 WL 1811265, at *9 (Del Super. Ct. June 20, 2007); *see also Gallup, Inc. v. Greenwich Ins. Co.*, 2015 WL 1201518, at *8-9 (Del. Super. Ct. Feb. 25, 2015). Because the only purported conflict between New York and Delaware law is Insurers' claim that New York public policy bars coverage for the settlements at issue here, they properly bore the burden of proving the existence and applicability of such policy.

[redacted]

Furthermore, because carve-outs from the definition of "Loss" function as exclusions, Insurers accordingly bear the burden of proving that TIAA-CREF's loss falls solely and exclusively within the scope of that carve-out.[15] Accordingly, to the extent that the burden of proof is relevant to the determination at issue, it is borne by Insurers.[16]

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[15] *See, e.g.*, *Gallup,* 2015 WL 1201518, at *9-10 (insurer bore burden of establishing that claim was "uninsurable under the law" under Loss definition); *Planet Ins. Co. v. Bright Bay Classic Vehicles, Inc.*, 553 N.E.2d 562, 564 (N.Y. 1990) (when insurer's denial is based "on limiting language in the definition of coverage, the limiting language amounts to an exclusion"); *Hoechst Celanese Corp. v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, 1994 WL 721786, at *2 (Del. Super. Ct. Apr. 22, 1994) ("insurer should not be relieved of their burden of proof as to an exclusion simply because they have the tactical advantage of being able to place the exclusion within a coverage provision"); *Brown & Brown, Inc. v. Johnson*, 34 N.E.3d 357, 360 (N.Y. 2015) (burden on party seeking to invoke public policy exception to enforcement of choice-of-law contract provision).

[16] *Consolidated Edison Co. of N.Y., Inc. v. Allstate Insurance Co.,* 774 N.E.2d 687, 690 (N.Y. 2002) (*"Con Edison"*), the only authority cited by Insurers on this point (Opening Br. at 20 n. 57), is not to the contrary. The policyholder in *Con Edison* argued that the policy language limiting coverage to an accident or occurrence ***implied*** an exclusion for intentional wrongdoing as to which the insurer should bear the burden of proof. *Id.* at 690. Here, in contrast, the primary policy's "uninsurable" language is an *explicit* exception to – and thus, an exclusion from – what would otherwise constitute covered "Loss" under the policy, and thus, Insurers bear the burden of proof.

[redacted]

2. Settlements of Claims Seeking Disgorgement Are Not Uninsurable as a Matter of New York Public Policy

Insurers do not dispute that the only bar to coverage for the Underlying Action settlements is the "uninsurable" exception to "Loss." Accordingly, their position rests on the assertion that "New York courts have enunciated a clear public policy rationale prohibiting insurance coverage for disgorgement claims." Opening Br. at 22. In fact, however, the New York Court of Appeals expressly held in *J.P. Morgan II* that New York has recognized only two circumstances in which a countervailing public policy will override the otherwise dominant policy of the freedom to contract:

> Freedom of contract "is deeply rooted in public policy" . . . As a result, parties to an insurance arrangement may generally "contract as they wish and the courts will enforce their agreements without passing on the substance of them" . . . .
>
> Our cases, however, have recognized two situations in which a countervailing public policy will override the freedom to contract, thereby precluding enforcement of an insurance agreement. First, an insurer may not indemnify an insured for a punitive damages award, and a policy provision purporting to provide such coverage is unenforceable. . . . Second, as a matter of public policy, an insured may not seek coverage when it engages in conduct "with the intent to cause injury."

992 N.E.2d at 1081 (citations omitted). While the Court noted that some other states also barred coverage on the *separate* ground that coverage should not be available for disgorgement claims, the Court expressly noted that it "had not

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considered the issue." *Id.* at 1082.[17] Moreover, because the Court held that the underlying claims before it would not fall within such a policy if it existed, it did not need to determine whether to adopt such a policy or its scope.

That *J.P. Morgan II* did not expressly adopt a third exception to the freedom of insurance contracts is also reflected in the subsequent Appellate Division decision in *J.P. Morgan Securities Inc. v. Vigilant Insurance Co.,* 2 N.Y.S.3d 415 (N.Y. App. Div. 2015) ("*J.P. Morgan III*"), relied upon by Insurers. That decision did not address the application of a public policy disgorgement defense in the absence of allegations of intentionally harmful conduct. Rather, in that case, the

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[17] The Court referenced cases, including *Level 3 Communications, Inc. v. Federal Insurance Co.*, 272 F.3d 908, 911 (7th Cir. 2001), relied on by Insurers here for the proposition that a policyholder incurs no loss within the meaning of the insurance contract by being compelled to return property. However, *Level 3* and its progeny turned on the courts' interpretation of the word "loss" (sometimes undefined) to not encompass settlements of claims for disgorgement. *Id.* at 911-12 (declining to reach question of whether, if policyholder demonstrated that settlement reflected compromise of "groundless" claim, it would then be insurable under policy). In TIAA-CREF's policies, however, the inclusion of the Ill-Gotten Gains Exclusion (which requires a final adjudication of disgorgement to apply) necessarily implies that, absent a final adjudication of disgorgement, a settlement of such a claim is encompassed by "Loss." *See Gallup*, 2015 WL 1201518 at *9-10; *U.S. Bank II*, 68 F. Supp. 3d at 1049 (Delaware law) ("***even if restitution is not insurable***, the policies require the settlement ***to actually be – and not just allegedly be*** – restitution to be uninsurable") (emphasis added); *U.S. Bank I*, 2014 WL 3012969, at *3 ("[T]he policies exclude from coverage restitution resulting from a final adjudication and by implication include within coverage restitution stemming from a settlement.").

[redacted]

court denied the plaintiff's motion to dismiss the insurer's affirmative defense based on "the doctrine precluding, on public policy grounds, insurance coverage for monies paid by the insured ***as a result of intentional harm to others***." *Id.* at 423 (emphasis added).[18] Contrary to Insurers' incorrect description of that case (Opening Br. at 29), it was in this context – where the public policy against intentional harm was at stake – that the court noted that findings of wrongful conduct in a government settlement order without a final adjudication could be considered as a basis to bar coverage.[19]

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[18] Insurers have never contended that the Underlying Actions involve or constitute claims of intentional harm to others under the standards of New York law. Indeed, the *Bauer-Ramazani* court held on summary judgment that TIAA-CREF's valuation practices were applied "evenhandedly" in increasing and decreasing markets, and thus, TIAA-CREF could not have known if any transaction might cause injury to a given participant. JA1680-1702. [redacted]

[19] In a later decision, the trial court granted summary judgment for the insured on the disgorgement defense, finding as a matter of undisputed fact after discovery that the payment Bear Stearns made to the SEC actually represented the gain of its customers, and thus was insurable, as there was no conclusive link between the disgorgement payment and improperly acquired funds in the hands of the insured. *J.P. Morgan Secs., Inc. v. Vigilant Ins. Co.*, 51 N.Y.S.3d 369, 373-76 (N.Y. Sup. Ct. 2017) ("*J.P. Morgan IV*"). To the extent that the trial court summarized the decision in *J.P. Morgan II*, the court merely quoted the Court of Appeals' discussion of *other courts'* rationales and holdings regarding when a disgorgement defense might otherwise apply, holdings not adopted by the Court of Appeals. *Id.* at 373 (quoting *J.P. Morgan II*, 992 N.E.2d at 1082).

[redacted]

In short, the *sine qua non* of Insurers' attack on the Superior Court's decision – their assertion that "[t]here was no legal basis for the Superior Court to conclude that the underlying settlements or disgorgement were insurable or covered as 'Loss'" (Opening Br. at 23) – is directly contradicted by the very *J.P. Morgan* decisions on which Insurers rely for that proposition. For that reason alone, the Opinion should be affirmed.

3. The Superior Court Correctly Held That the Cases Cited by Insurers Do Not Support Barring Coverage for Civil Settlements of Disgorgement Claims

Even if Insurers could appropriately rely on lower appellate court cases to establish a New York public policy the Court of Appeals has not expressly adopted, the Superior Court correctly held that those cases and any policy they advance do not support Insurers' effort to avoid coverage here. That is because, contrary to Insurers' descriptions of those cases, none involve civil settlements disavowing the allegations of the settled claim. To the contrary, they each address settlements in the wake of government orders, findings or consent decrees expressly ordering the insured to pay disgorgement damages as a direct result of *findings that the policyholder had willfully violated securities laws.*

The court in *Credit Suisse II*, for example, emphasized that in conjunction with the government consent order at issue there, the SEC had issued a "final

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judgment" that "expressly state[d] that the money ordered disgorged was 'obtained improperly by CSFB as a result of the conduct alleged in the Complaint.'" 782 N.Y.S.2d at 20. That decision, and the trial court decision it affirmed, were based on the fact that the final judgment "specifically links the disgorgement payment to the improper activity," as distinguished from "merely a case in which a party settled an action without admitting liability." *Credit Suisse I*, 2003 WL 24009803, at *4 (finding that Final Judgment was more like final adjudication after trial than settlement).[20] The court held that a "***different outcome might result when parties settle under different circumstances***." *Id.* (emphasis added).

Millennium II also involved a government decree with express findings linking an alleged disgorgement payment to violations of the securities laws:

> [T]he findings recited in the SEC's cease and desist order to which plaintiff consented and in the assurance of discontinuance it entered into with the Attorney General of the State of New York, which provided, inter alia, for the disgorgement by plaintiff of $148 million, 'conclusively link the disgorgement to improperly acquired funds'

889 N.Y.S.2d at *1 (internal citation omitted).[21]

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[20] *Credit Suisse* involved claims that CSFB had "coerced" certain clients into paying them a portion of their profits from flipping their IPO stock. *Credit Suisse I*, 2003 WL 24009803, at *1.

[21] The SEC order included express findings that that Millennium, a hedge fund, "generated tens of millions of dollars in profits through market timing trades of

[redacted]

J.P. Morgan I similarly arose in the wake of an SEC investigation and Order. After a lengthy investigation, the policyholder, Bear Stearns, settled with the SEC, which entered an Order directing that Bear Stearns disgorge $160 million. In its original decision, subsequently reversed by the Court of Appeals, the Appellate Division held that coverage was barred not merely because the claim involved an order of disgorgement, but because that disgorgement was conclusively tied to a finding of wrongdoing by the policyholder that could not be negated by the policyholder's denial of liability in the consent order:

> Here too [like *Millennium*], read as a whole, the offer of settlement [and] the SEC Order . . . are not reasonably susceptible to an interpretation other than that Bear Stearns knowingly and intentionally facilitated illegal late trading for preferred customers, and that the relief provision of the SEC Order required disgorgement of funds gained through that illegal activity.

936 N.Y.S. 2d at 106.[22]

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mutual fund shares;" and "devised and carried out a fraudulent scheme to avoid detection," including creating 100 legal entities and in excess of 1000 accounts to hide its improper activity. It further declared that Millennium's conduct violated the federal securities laws. *Millennium I*, 882 N.Y.S.2d at 851-52.

[22] As the Superior Court held, Insurers' citation to *Reliance,* 594 N.Y.S.2d at 20, ignores the evolution of New York law regarding insurance for claims of disgorgement as reflected in later cases from the same and higher courts in *Credit Suisse II* and *J.P. Morgan II.* TA0725. Furthermore, although *Reliance* involved a claim for coverage of a civil settlement, that settlement was concluded in the wake of findings by the court, in affirming the imposition of a constructive trust on $60

As the Superior Court correctly held, none of these cases is "on all fours" with the civil settlements at issue here, which involved neither an order or direction of disgorgement nor any finding or adjudication of wrongdoing by TIAA-CREF. Opinion at 23; JA5225; *see Reliance*, 594 N.Y.S.2d at 24 ("[O]ne may not insure against the risk of being ***ordered*** to return money or property that has been wrongfully acquired.") (citation omitted) (emphasis added); *Credit Suisse II*, 782 N.Y.S.2d at 20 ("The risk of being ***directed*** to return improperly acquired funds is not insurable.") (emphasis added). To the contrary, the undisputed facts establish only that: (1) TIAA-CREF faced civil claims that sought disgorgement among other relief; (2) TIAA-CREF disputed and vigorously defended the claims, repeatedly asserting that the procedures that resulted in TFE and its treatment were proper and lawful; (3) no court or governmental entity ever found to the contrary or ordered that TIAA-CREF make any payment in response to those claims;[23] and

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million in Reliance's greenmail profits, that the policyholder was required "to convey the [funds at issue] to another on the ground that [it] would be unjustly enriched if [it] were permitted to retain it." *Reliance,* 594 N.Y.S.2d at 25 (citation omitted).

[23] Insurers' attempt to turn the award of attorneys' fees in the *Rink* Action pursuant to Ky. Rev. Stat. Ann. ("KRS") § 412.070 into a "presumption" by the court that TIAA-CREF had, in fact, acted improperly ignores the plain language of that statute. (Opening Br. at 38). Under KRS 412.070, fees may be awarded "*[i]n actions for* . . . the recovery of money or property which has been illegally or

(4) TIAA-CREF settled the claims for far less than the amounts sought[24] while denying any liability. Insurers' recitation of the facts at issue is in perfect accord with the Superior Court's holding that on the undisputed record there was "no conclusive link between the settlements in the Underlying Actions and wrongdoing by TIAA-CREF that would render the settlement agreements uninsurable disgorgement." Opinion at 27; JA5229.

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improperly collected, withheld or converted." The statute does not limit awards of fees to actions in which there has been a finding of wrongdoing, but only where the action "is for" – *i.e.* seeks damages due to an allegation of – wrongdoing. In fact, the sole case cited by Insurers on this point, *Reid v. Allinder,* 504 S.W.2d 706, 707 (Ky. 1974), held that an award of fees was not warranted because the funds at issue were not being withheld and the suit in question was not prosecuted "for the benefit of all taxpayers." Unlike the SEC orders and findings in *Credit Suisse* and *Millennium,* an award of fees to class counsel under KRS 412.070 is in no way inconsistent with the defendant's agreement to settle without admitting wrongdoing.

[24] The *Rink* Settlement substantially reduced the size and scope of the settlement class, and thus TIAA-CREF's total payment. JA5673-74; JA1465. And, even Insurers admit that the *Bauer-Ramazani* settlement payment totaled only [redacted] of the total amount that TIAA-CREF had allegedly "withheld" from the underlying plaintiffs' distributions in that case. Opening Br. at 13-14.

[redacted]

4. Alternatively, the Superior Court's Decision Should Be Affirmed on the Ground That the Monies Sought in the Underlying Actions Cannot Be Conclusively Linked to Funds Retained by TIAA-CREF; the TFE Gains Went to Others

Even if the New York Court of Appeals in *J.P. Morgan II* adopted disgorgement as a third New York public policy exception to freedom of contract (it did not), such policy would not have applied in any event to the facts of that case. That same conclusion applies to the undisputed facts here, and provides an alternate basis for affirming the decision of the Superior Court holding that the Underlying Action settlements constituted insurable "Loss."[25]

Bear Stearns, the policyholder in *J.P. Morgan*, argued that any rule barring insurance coverage for disgorgement "should apply only where the insured requests coverage for the disgorgement of its ***own*** illicit gains." 992 N.E.2d at 1082 (emphasis added). The Court of Appeals agreed and held that there could be no bar to coverage where the funds allegedly subject to disgorgement were actually retained by Bear Stearns' clients. *Id.* at 1083. As the court explained:

> Moreover, the cases upon which the Insurers rely are distinguishable. . . .In each, the insured was barred from obtaining coverage for SEC-

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[25] *See In re Santa Fe Pac. Corp. S'holder Litig.*, 669 A.2d 59, 67 (Del. 1995) (appellee may offer "an alternative ground, fairly raised below," to support affirmance of decision appealed from).

[redacted]

> ordered disgorgement because the SEC's findings "conclusively link[ed]" the disgorgement payment to improperly acquired funds in the hands of the insured. . . . In this case, in contrast, Bear Stearns alleges that it is not pursuing recoupment for the turnover of its own improperly acquired profits and, therefore, it would not be unjustly enriched by securing indemnity. The Insurers have not identified a single precedent, for New York or otherwise, in which coverage was prohibited where, as Bear Stearns claims, the disgorgement payment was (at least in large part) linked to gains that went to others.

Id.

Insurers do not dispute that both TIAA and CREF operate pursuant to their not-for profit charters, or that the TFE gains associated with the At-Cost Accounts were not retained by TIAA-CREF (as proscribed by the At-Cost Agreements).[26] Rather, TFE gains, like TFE losses, are necessarily passed back to the remaining participants in those Accounts as a component of total expenses. Under the standards set forth in *J.P. Morgan II*, TIAA-CREF had nothing to "disgorge" because the funds allegedly subject to disgorgement in the Underlying Actions were ultimately "held" by the remaining plan participants. Accordingly, even if the Court of Appeals had, in fact, adopted a public policy against coverage for

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[26] Indeed, Insurers argue that TIAA-CREF is not entitled to coverage for the amount of the Underlying Action settlements precisely because such amounts were passed on to the remaining plan participants. Opening Br. at 42-45.

disgorgement – which it did not – on the undisputed record here, the Underlying Action settlement amounts would still constitute covered Loss.

5. No Material Disputes of Fact Warrant Remand

Finally, contrary to Insurers' belated arguments, there is no material dispute of fact on this record which barred entry of summary judgment. Insurers' failure to fairly present to the Superior Court any argument that questions of fact existed precludes them from raising such an argument for the first time in this Court under Supreme Court Rule 8.[27] However, that argument also fails on its merits, as neither the nature of the claims and proceedings in the Underlying Actions, nor the terms of the settlements are disputed. The Superior Court properly applied those undisputed facts to unambiguous policy language. *See, e.g., Alstrin v. St. Paul Mercury Ins. Co.,* 179 F. Supp. 2d 376, 388 (D. Del. 2002).

Insurers cite no authority for their assertion that, on this undisputed record, the Superior Court should have "left it for the jury to decide" the legal issue of "whether the settlements were for uninsurable disgorgement," (Opening Br. at 41),

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[27] Notably, Insurers did present to the Superior Court the same "record evidence" they address in section I(C)(3) of their Opening Brief – but argued that this evidence showed there was no dispute of fact that the exclusionary language in the definition of Loss barred coverage for the Underlying Action settlements. JA4881-85; JA5225 n.104 (Superior Court noting that Insurers argued below that underlying settlements only resolved claims for disgorgement).

[redacted]

nor is there any such authority. As discussed above, settled civil "disgorgement" claims are not uninsurable under New York law. Further, Insurers did not show, and still have not shown, the existence of any question of fact from which a reasonable jury could conclude that TIAA-CREF caused intentional harm to the underlying class plaintiffs – the correct measure of "uninsurability" under New York law. Finally, the Superior Court did not "create[] a presumption of coverage" for disgorgement claims or base its decision "entirely upon the fact that TIAA-CREF summarily denied liability in the settlement agreements." Opening Br. at 40. Rather, it correctly held that, unlike in the cases cited by Insurers, there was no countervailing governmental finding or order sufficient to create a material fact dispute as to whether TIAA-CREF's settlements could be conclusively linked to monies belonging to others.[28] Accordingly, the Superior Court correctly entered

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[28] For that reason, the New York Appellate Division's decision in *J.P. Morgan III* does not support Insurers' belated claim that fact questions barred summary judgment on the "uninsurability" issue. In *J.P. Morgan III,* unlike here, the consent order with the SEC and settlement with the NYSE contained specific findings of intentional wrongdoing by the policyholder, including that it had operated a "late trading and market timing scheme" and taken "affirmative steps" to help its clients evade trading restrictions set up by various mutual funds, including assignment of "multiple account numbers to customers so that mutual funds could not identify them as customers." 2 N.Y.S.3d at 417. Those findings created a question of fact as to whether the policyholder had acted with the intent to harm others sufficient to bar coverage.

summary judgment that the coverage claim did not invoke any New York public policy that would render the claim uninsurable as a matter of law.

6. Even If the Settlements Are Not Insurable, TIAA-CREF's Defense Costs and Class Counsel Fees Are Covered Under the Policies

Even if coverage for the settlements was properly barred – which it is not – Insurers still would be required to cover the Defense Costs and class counsel fees paid by TIAA-CREF. First, neither of those costs or fees are even arguably other people's money that TIAA-CREF is returning. This renders inapplicable any public policy articulated by Insurers, which only applies to the return of ill-gotten gains – not to insurance for litigation costs.

Next, Insurers would like to treat the "uninsurable" exception to Loss as if it were an actual exclusion of a claim, applying to all Loss arising therefrom. But, because Insurers' position is based on an exception to what is otherwise covered Loss, other Losses that do not fall within the exception (like insurable portions of any "settlements" and "any Defense Costs") are not similarly excepted. *See UnitedHealth Grp. Inc. v. Hiscox Dedicated Corp. Member Ltd.*, 2010 WL 550991, at *10-12 (D. Minn. Feb. 9, 2010) (applying New York law) (even though settlement not covered because it fell within exception to "damages" definition, attorneys' fees paid to underlying plaintiffs as part of same lump-sum settlement

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could still be covered).[29] Here, because there is no exclusion applicable to the Underlying Actions – the claims themselves ***are*** covered by the Policies – only so much of TIAA-CREF's Loss that is uninsurable will be excepted from covered Loss. Nothing in the Policies consolidates the various types of Loss arising out of one Claim for purposes of evaluating any exception thereto, nor should Insurers be permitted to rewrite the Policies to expand the Loss exception beyond what they bargained for.

Other Policy provisions are in accord. The Policies define Defense Costs as the "reasonable and necessary fees, costs and expenses" incurred in defending a Claim. JA0353. This does not require that any judgment or settlement of such a Claim include insurable Loss for Defense Costs to be recoverable. By contrast, the primary case Insurers relied on for this point involves materially different policy language. *See also* Opening Br. at 28-29. In *Millennium I*, Defense Costs were defined to mean "***that part of Loss*** consisting of costs, charges and expenses incurred in the defense of Claims." 882 N.Y.S.2d at 851 (emphasis added). Because the policy incorporated the concept of "Loss" into the definition of

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[29] *See also Burks v. XL Specialty Ins. Co.*, 543 S.W.3d 458, 467 (Tex. Ct. App. 2015) (even if disgorgement uninsurable, loss definition does not exclude advancement of defense expenses).

[redacted]

Defense Costs, it was appropriate to link Loss and Defense Costs together for purposes of evaluating coverage for Defense Costs. That link does not exist here.

II. INSURERS MAY NOT AVOID THEIR COVERAGE OBLIGATIONS ON THE BASIS THAT THE COSTS OF THE UNDERLYING SETTLEMENTS WERE ULTIMATELY BORNE BY THE REMAINING PARTICIPANTS IN THE AT-COST ACCOUNTS

A. Counterstatement of Question Presented

May Insurers evade coverage on the ground that TIAA-CREF was required to pass on the costs of litigation and settlement to account holders, particularly where to do so would render the coverage sold to TIAA-CREF illusory? JA4888; JA5049-56; JA5245-50.

B. Standard and Scope of Review

The meaning and application of language in an insurance policy is appropriately a question of law for the Court and thus subject to *de novo* review. *See, e.g.*, *Krafft-Murphy,* 82 A.3d at 702; *Alstrin*, 179 F. Supp. 2d at 388.

C. Merits of the Argument

As a last-ditch effort to avoid the Superior Court's ruling, Insurers latch on to a single sentence in their briefs below and a passing reference at oral argument to claim that TIAA-CREF is not entitled to coverage because the remaining participants in the At-Costs Accounts bore the costs of the Underlying Actions. JA4888; JA5049-56. That argument fails under the policy language and applicable law.

[redacted]

The Opening Brief does not identify any policy language that supports Insurers' effort to avoid coverage based on the fact that TIAA-CREF allocated their losses in connection with the Underlying Actions to the various account holders as an expense. However, at oral argument below, Insurers purported to base that claim on the fact that the definition of "Loss" excludes "any amount for which the insureds are not financially liable, or which are without legal recourse to the Insureds." JA5049-50 at 38:6-39:17; JA5056 at 45:2-10.

The court in *Cirka v. National Union Fire Insurance Co.,* 2004 WL 1813283 (Del. Ch. Aug. 6, 2004) rejected a virtually identical construction of the Loss definition. The policyholder in *Cirka* had entered into an agreement in the underlying action limiting its liability to the coverage available under the insurance policy. The insurer argued that, as a result of that agreement, the policyholder faced no actual financial liability for any judgment or settlement, and that therefore there was no "Loss" within the meaning of the policy. The court held that the cited limitation was "simply inapplicable" because "while National Union may be the sole source to which the [underlying plaintiff] may look for recovery, [the policyholder] is still very much a defendant in these claims." *Id.* at *2 n.4. Similarly, here, the TIAA-CREF defendants in the Underlying Actions faced direct

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liability while those Actions were pending, and were financially liable *to the class* for the settlement payments.

Moreover, TIAA-CREF was not "indemnified" for its losses in connection with the Underlying Actions; rather, as required by its operating structure, it allocated those losses among the remaining accounts as an expense. Thus, accepting Insurers' arguments on this point would preclude coverage whenever a policyholder passed increased litigation costs on to customers in the form of higher prices or shareholders in the form of reduced dividends or earnings. Nothing in the policy language allows the insurers to evade coverage based on such recoveries.

For TIAA-CREF in particular, equating the required allocation of losses among participants with an alternate source of "indemnification" would ensure that TIAA-CREF could *never* suffer a covered "Loss" for any type of claim. Based on its At-Cost business model, all expenses are necessarily passed through to its account holders as an expense. Courts will not adopt an interpretation of policy terms which thus renders the promise of coverage illusory. *See, e.g.*, *First Bank of Del., Inc. v. Fid. & Deposit Co. of Maryland,* 2013 WL 5858794, at *9 (Del. Super. Ct. Oct. 13, 2013) (although exclusion unambiguously barred coverage, it would not be applied as written because "a grant of coverage should not be swallowed by an exclusion"); *Thomas J. Lipton, Inc. v. Liberty Mut. Ins. Co,* 34

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N.Y.2d 356, 361 (1974) (rejecting insurer interpretation of ambiguous phrase because it would "exclude what, as a practical matter, would usually be some of the largest foreseeable elements of . . . damage [and thus] would render the coverage nearly illusory").

Finally, the very same operating parameters that required allocation of the Underlying Action losses to the TIAA-CREF account holders also will require the allocation of any insurance recovery to those participants. Accordingly, unlike the inapposite "authority" on which Insurers rely,[30] TIAA-CREF neither seeks nor will obtain any "double recovery" if Insurers are held to their promise of coverage for the precise type of losses at issue in the Underlying Actions.

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[30] *See Pan P. Retail Props., Inc. v. Gulf Ins. Co.*, 471 F.3d 961, 974 (9th Cir. 2006) (cited in Opening Br. at 44 n.129).

[redacted]

CONCLUSION

For the reasons set forth above, TIAA-CREF respectfully requests that this Court affirm the Superior Court decision and order to the extent that it (1) granted TIAA-CREF's motion for summary judgment that the civil settlements of the Underlying Actions do not constitute uninsurable disgorgement under the insurance policies; (2) granted TIAA-CREF's motion for summary judgment that coverage is not barred by any public policy against disgorgement; and (3) denied Insurers' motions for summary judgment that the settlement payments constitute uninsurable loss.

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Dated: March 9, 2018
Public Version:
March 26, 2018

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