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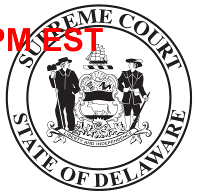

IN THE SUPREME COURT OF THE STATE OF DELAWARE

IN RE FAIRPOINT INSURANCE COVERAGE APPEALS	No. 478,2022 No. 479,2022 No. 480,2022 Court Below—Superior Court of the State of Delaware C.A. No. N18C-08-086 EMD (CCLD) (Davis, J.)

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NATURE OF PROCEEDINGS

This is the second recent appeal where Verizon Communications Inc. ("Verizon") has sought to expand the coverage that directors-and-officers ("D&O") insurance policies afford for "Securities Claims." In *In re Verizon Insurance Coverage Appeals ("Idearc")*, 222 A.3d 566 (Del. 2019), Verizon sought coverage for an underlying fraudulent-transfer action arising from the spinoff of its directories business. While the Superior Court found coverage, this Court reversed. The Court explained that the fraudulent-transfer action did not allege a violation of a law "regulating securities," as the unambiguous language of the Securities Claim definition required. *Id.* at 576. Here, Verizon again seeks coverage for an underlying fraudulent-transfer action arising from a spinoff. This time, Verizon invokes policy language defining a Securities Claim as a lawsuit "brought derivatively on the behalf of an **Organization** by a security holder of such **Organization**." A1706, 1783.[1] Under the unambiguous policy language, Verizon again is not entitled to coverage.

In March 2008, Verizon entered into a transaction (the "Spinoff") whereby it sold its New England landline business to FairPoint Communications, Inc. ("FairPoint"). Verizon did so by placing the relevant assets in a subsidiary called

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[1] Terms in **bold** appear as such in the original and are defined terms under the relevant policies. Citations to "A####" refer to the Joint Appendix filed herewith.

Northern New England Spinco Inc. ("Spinco"), which then merged into FairPoint and, as a result, ceased to exist. FairPoint later filed for Chapter 11 bankruptcy, and as part of its exit from bankruptcy, a litigation trust (the "Trust") was created. Authorized to pursue Spinoff-related causes of action on behalf of certain FairPoint creditors, the Trust brought a fraudulent-transfer action against Verizon (the "Trust Action") in October 2011. In the Trust Action, Verizon incurred $23.4 million in defense costs and ultimately settled for $95 million.

Verizon now seeks coverage for the Trust Action under two towers of D&O insurance. The first tower consists of a primary transaction-specific runoff policy (the "Transaction Policy"), plus two follow-form excess policies (collectively, the "Transaction Tower"). The second tower consists of a primary traditional annual policy (the "Verizon Policy"), plus two follow-form excess policies (collectively, the "Verizon Tower"). Under the Transaction and Verizon Policies, Verizon initially argued that the Trust Action was a Securities Claim under the same "regulating securities" language at issue in *Idearc*. But after this Court in *Idearc* held that a fraudulent-transfer action did ***not*** allege a violation of a law "regulating securities," Verizon began relying on a different part of the Securities Claim definitions instead. That part defines a Securities Claim as a "**Claim** … brought derivatively on the behalf of an **Organization** by a security holder of such **Organization**." A1706, 1783. By its plain meaning, that language refers to a

derivative action as understood in the context of corporate and securities law—a suit brought by a security holder to enforce a corporate right that the corporation is unwilling or unable to enforce itself. Under this Court's caselaw, however, fraudulent-transfer actions are direct, not derivative. Moreover, the Trust Action was not brought by a security holder—it was brought by a litigation trust. Furthermore, no derivative action possibly could have been brought on behalf of Spinco, as Verizon claimed, since Spinco ceased to exist during the Spinoff.

Nevertheless, the Superior Court found coverage. To begin with, Verizon moved for partial summary judgment, arguing that its defense costs were covered as a matter of law under the Transaction Tower. The insurers that issued the policies in both Towers (the "Insurers") cross-moved for judgment on the pleadings. In February 2021, the Superior Court granted Verizon's motion and denied the Insurers' motion. Under the Transaction Tower, the court reasoned that the Trust Action was "brought derivatively on the behalf of [FairPoint]" because it was "derivative as a matter of federal bankruptcy law." Ex. C, at 22, 24. The court also held that the Trust Action was "brought … by a security holder," even though, undisputedly, the Trust Action was brought by the Trust, and the Trust did not hold any securities. Finally, under the Verizon Tower, the court identified no ambiguity in the policy language, yet it still found material factual disputes regarding whether

"Verizon could have reasonably expected that any Spinco-related liabilities would be covered despite Spinco's divestiture and dissolution." *Id.* at 29-30.

After discovery, the Insurers and Verizon cross-moved for summary judgment, with Verizon now seeking coverage for the settlement under both Towers. To obtain coverage under the Verizon Tower, Verizon had to establish that the Trust Action was "brought derivatively on the behalf of an **Organization** by a security holder of such **Organization**" under the Verizon Policy. FairPoint, however, is not an "**Organization**" under the Verizon Policy—under that policy, "**Organization**" includes only Verizon or a Verizon subsidiary. But the entity Verizon pointed to—Spinco—was a ***former*** subsidiary that ***dissolved*** when it merged into FairPoint in 2008. Nevertheless, in October 2022, the court granted Verizon's motion and denied the Insurers' motion. Having previously held that the 2011 Trust Action was "brought derivatively on the behalf of [FairPoint] by a security holder of [FairPoint]," the court held that it was also "brought derivatively on the behalf of [Spinco] by a security holder of [Spinco]," which ***did not exist*** at the time. In so holding, the court referenced Verizon's reasonable expectations without finding the policy language ambiguous. The court also misconstrued an endorsement to the Verizon Policy as a grant of Spinoff-related coverage, when in fact it merely makes the Verizon Tower excess of the Transaction Tower.

The Superior Court's decisions ignore basic principles of Delaware corporate law, misapprehend bankruptcy principles, and contradict the plain meaning of the policy language. This Court should reverse.

SUMMARY OF ARGUMENT

1. The Superior Court erred in holding that the Trust Action was "brought derivatively on the behalf of an **Organization** by a security holder of such **Organization**" under the Transaction and Verizon Policies, for two reasons.

a. The Trust Action was not "brought derivatively on the behalf of an **Organization**." By its plain meaning, that language refers to derivative actions as understood in the context of corporate and securities law. Under this Court's caselaw, however, the Trust Action was not a derivative action. By their nature, fraudulent-transfer actions belong to and enforce the rights of a corporation's creditors, not the corporation itself. Similarly, fraudulent-transfer actions remedy harm to creditors, not the corporation, and relief goes to creditors, not the corporation. Tellingly, no participant in the Trust Action treated it as a derivative action at the time. The Superior Court erred in ignoring this Court's settled tests for distinguishing direct and derivative actions, and further erred in misapplying bankruptcy principles.

b. The Trust Action also was not "brought … by a security holder." The Trust Action undisputedly was brought "by" the Trust, and the Trust undisputedly did not "hold[]" any "security." That should end the matter. The Superior Court erred in failing to apply the plain meaning of the policy language.

2. At a minimum, the Superior Court erred in holding that the Trust Action was "brought derivatively on the behalf of an **Organization** by a security holder of such **Organization**" under the Verizon Policy, for three reasons.

a. The Trust Action was not "brought derivatively on the behalf of [Spinco]." Spinco merged into FairPoint and ceased to exist during the Spinoff in 2008, and the Trust Action was not "brought" until 2011. A lawsuit simply cannot be "brought derivatively on the behalf of" a nonexistent entity that dissolved in a merger. The Superior Court's reasoning would upend settled principles of derivative standing.

b. The Trust Action also was not "brought derivatively on the behalf of an **Organization**." Even if the Trust Action were deemed "brought derivatively on the behalf of [Spinco]," Spinco was not an "**Organization**" when the Trust Action was "brought." Under the Verizon Policy, a Verizon subsidiary "ceases to be an **Organization** when [Verizon] no longer maintains **Management Control** of [it]." A1791. When the Trust Action was brought in 2011, Spinco was a ***former*** Verizon subsidiary that no longer existed due to Spinco's 2008 merger into FairPoint. Spinco thus was not a Verizon "**Organization**" at the relevant time. The Superior Court's grounds for concluding otherwise ignore or distort the policy language.

c. Finally, the Trust Action was not "brought … by a security holder of [Spinco]." Indeed, Verizon is judicially estopped from arguing otherwise. Below,

Verizon successfully argued that the Trust Action was "brought … by a security holder of [FairPoint]" under the Transaction Policy. That is inconsistent with the Trust Action also being "brought by a security holder of [Spinco]" under the Verizon Policy. The relevant instruments were either securities of FairPoint or securities of Spinco; they cannot be both. Regardless, the Trust Action was not "brought … by a security holder of [Spinco]" on the merits. When the Trust Action was "brought" in 2011, Spinco did not exist, and the only obligor on the instruments was FairPoint. The Superior Court's reasoning misunderstands the Insurers' arguments.

STATEMENT OF FACTS

A. The Spinoff

On March 31, 2008, Verizon sold certain landline telephone assets in Vermont, New Hampshire, and Maine to FairPoint in the Spinoff. For tax reasons, the parties structured the Spinoff as a "reverse Morris Trust." In a reverse Morris Trust, a company selling assets places the assets in a subsidiary; the seller distributes the subsidiary's stock to the seller's own stockholders in a tax-free distribution; and the former subsidiary, newly independent, merges with the buyer in a tax-free reorganization. A322, 339-43, 378-79.

Here, shortly before the Spinoff, Verizon incorporated Spinco as "a newly formed, wholly-owned, direct Subsidiary of Verizon." A520. During the Spinoff, Verizon transferred the relevant assets to Spinco in exchange for cash and debt securities (the "Notes"). Verizon then distributed Spinco's stock to Verizon's own stockholders, at which point Spinco was no longer a Verizon subsidiary. Finally, Spinco merged into FairPoint and ceased to exist. A384-85, 462-63, 520-21. The merger agreement provides that "Spinco shall be merged with and into [FairPoint] …, the separate existence of Spinco shall cease[,] and [FairPoint] shall continue as the surviving corporation of the Merger." A558. Delaware state records show that Spinco dissolved at 9:01 a.m. on March 31, 2008, as a "Non-Survivor" of a "Merger." A658-61.

As for the Notes, after Spinco issued them to Verizon, Verizon sold them to investment banks in exchange for outstanding Verizon commercial paper. The banks in turn sold the Notes to investors in a private offering. A384-85, 665-944. The original terms of the Notes were contained in an Indenture executed by Spinco as part of the Spinoff. That Indenture provided that, after Spinco's merger with FairPoint, FairPoint would "succeed to[] and be substituted for" Spinco as "the Issuer." A1016. Shortly thereafter, Spinco did merge with FairPoint. A464. Furthermore, "FairPoint executed a Supplemental Indenture and became the sole obligor on the Notes." A464; *see* A1071-87. FairPoint thus "became solely responsible for … repayment of the Notes," "assum[ing] the obligation of paying the interest and principal on the Notes as those payments came due." A384-85. Spinco "was … the obligor on the Notes for a matter of minutes on the day the [Spinoff] closed"—roughly "10 minutes." A463-64, 659-63. "[E]veryone who participated in the [Spinoff] understood that FairPoint—and not Spinco—… would be responsible to repay the … Notes." A464.

B. <u>The Transaction Tower</u>

In connection with the Spinoff, Verizon and FairPoint obtained the Transaction Policy from Appellant National Union Fire Insurance Company of Pittsburgh, Pa. ("National Union"). The Transaction Policy has a policy period of

March 31, 2008 to March 31, 2014, and has a limit of liability of $10 million excess of a $500,000 self-insured retention. A1698.

In addition to the Transaction Policy, Verizon and FairPoint obtained excess policies from Appellants XL Specialty Insurance Company and National Specialty Insurance Company. The XL and National Specialty policies "follow form" to the Transaction Policy, meaning that, unless otherwise provided, they incorporate that policy's terms and conditions, including the relevant terms discussed below. A151. The XL and National Specialty policies have a limit of liability of $10 million each. A151.

The Transaction Policy is a transaction-specific runoff policy affording coverage for FairPoint, Verizon, Spinco, their subsidiaries, and their individual directors and officers. The policy consists of a policy form—the "2/00" form—and several endorsements, including an endorsement entitled "Deal Specific Run-Off Multiparty Coverage" (the "Runoff Endorsement"). A1761-65. Under the Runoff Endorsement, the policy provides coverage under three Insuring Agreements. Two of those Insuring Agreements afford coverage for a "**Claim**"—defined to include a civil lawsuit—"made against an **Insured Person**"—defined to include individual directors and officers. A1703-06, 1761-62. Because the underlying lawsuit here was not brought against any individual, those two Insuring Agreements are not applicable.

The third Insuring Agreement affords narrower coverage for certain Claims brought against insured entities, including Verizon. Under the third Insuring Agreement, the Transaction Policy "shall pay the **Loss** of any **Organization** arising from a **Securities Claim** made against such **Organization** for any **Wrongful Act** of such **Organization** occurring on or prior to the **Effective Time**." A1762. "**Loss**" includes settlements and defense costs, and "**Organization**" includes FairPoint, Verizon, Spinco, and their subsidiaries. A1698, 1703-06, 1761. "**Effective Time**" is defined as "the effective time of the **Deal**," and "**Deal**" is defined as "the merger of [FairPoint] with [Spinco], currently a subsidiary of [Verizon], on March 31, 2008 while **Spinco** holds specified assets and liabilities that are used in **Verizon's** local exchange business and related activities in Maine, New Hampshire and Vermont." A1761. In other words, "**Deal**" means the FairPoint-Spinco merger in the Spinoff. "**Wrongful Act**" includes certain acts and omissions, but "solely in connection with or relating to the **Deal**." A1761, 1706-07; *see also* A1762 (providing that the Transaction Policy "shall not provide coverage for any **Wrongful Act** … occurring after the **Effective Time** or which are not in connection with or relating to the **Deal**").

Reading these provisions together, the relevant Insuring Agreement affords coverage for Verizon's defense costs and settlement payments arising from certain

Spinoff-related lawsuits, provided that the lawsuit constitutes a "**Securities Claim**." The Transaction Policy defines "**Securities Claim**" as follows:

> "**Securities Claim**" means a **Claim** … made against any **Insured**:
>
> (1) alleging a violation of any federal state, local or foreign regulation, rule or statute regulating securities (including but not limited to the purchase or sale or offer or solicitation of an offer to purchase or sell securities) …; or
>
> (2) brought derivatively on the behalf of an **Organization** by a security holder of such **Organization**.

A1706. As relevant here, "**Insured**" includes an "**Organization**." A1705. After this Court's decision in *Idearc*, Verizon abandoned reliance on prong (1) and now relies solely on prong (2).

The Runoff Endorsement also clarifies how the Transaction Tower relates to the Verizon Tower. In a section entitled "Primary to Traditional D&O Insurance," the Runoff Endorsement provides that the Transaction Tower is "intended to provide coverage which is primary to any [D&O] insurance program issued to Verizon." A1763-64.

C. <u>The Verizon Tower</u>

On an annual basis, Verizon obtained traditional D&O insurance, including the Verizon Policy issued by National Union. The Verizon Policy has a policy period of October 31, 2009 to October 31, 2010, and a limit of liability of $25 million excess of a $7.5 million retention. A1775, 2210-20. Verizon also purchased excess policies that "follow form" to the Verizon Policy, including policies issued by

Appellants AXIS Insurance Company and St. Paul Mercury Insurance Company with limits of $15 million each. A1941-68.

Like the Transaction Policy, the Verizon Policy consists of the 2/00 form with certain endorsements. It also contains three Insuring Agreements, two of which are not applicable because they afford coverage only for Claims made against individuals. Under the third Insuring Agreement, the Verizon Policy "shall pay the **Loss** of any **Organization** arising from a **Securities Claim** made against such **Organization** for any **Wrongful Act** of such **Organization**." A1779. The terms "**Claim**" and "**Loss**" have the same meaning as in the Transaction Policy. A1780, 1782. Unlike in the Transaction Policy, however, "**Wrongful Act**" is not limited to acts and omissions relating to the Spinoff. A1783-84.

The Verizon Policy also differs from the Transaction Policy in the definition of "**Organization**." In the Verizon Policy, "**Organization**" does not include FairPoint, and instead is limited to Verizon and any "**Subsidiary**." A1783. "**Subsidiary**" is defined to include "any for-profit entity of which [Verizon] has **Management Control** … on or before the inception of the **Policy Period**." A1810. "**Management Control**" is defined in relevant part as the power to designate a majority of a corporation's board of directors. A1782. But "**Organization**" does not include former Subsidiaries—the policy provides that a Subsidiary "ceases to be

an **Organization** when [Verizon] no longer maintains **Management Control** of [it].” A1791.

The definition of “**Securities Claim**” in the Verizon Policy is identical to the Transaction Policy. In both policies, the relevant portion defines a Securities Claim as a “**Claim** … brought derivatively on the behalf of an **Organization** by a security holder of such **Organization**.” A1706, 1783. But FairPoint is an “**Organization**” only under the Transaction Policy—not the Verizon Policy. Accordingly, under the Transaction Policy, a Securities Claim includes a “**Claim** … brought derivatively on the behalf of [FairPoint] by a security holder of [FairPoint],” but under the Verizon Policy, it does not.

Like the Transaction Policy, the Verizon Policy also clarifies the relationship between the Verizon Tower and the Transaction Tower. In an endorsement entitled “Excess To Deal Specific Program FairPoint and Verizon” (the “Excess Endorsement”), the Verizon Policy provides that, “[i]n the event of a **Claim** involving acts, errors or omissions in connection with or relating to the **Deal**, coverage as is afforded under this policy shall be specifically excess of valid and collectible insurance under [the Transaction Tower].” A1845. The definition of “**Deal**” in the Excess Endorsement is the same as in the Transaction Policy—“**Deal**” means the FairPoint-Spinco merger in the Spinoff. A1845. Thus, to the extent that

Spinoff-related Claims are covered under both Towers, the deal-specific Transaction Tower is primary, and the traditional Verizon Tower is excess.

D. FairPoint's Bankruptcy

On October 26, 2009, FairPoint and certain affiliates (not including Spinco, which did not exist) filed for bankruptcy under Chapter 11 of the Bankruptcy Code. A1969-99. Under the Bankruptcy Code, the commencement of a bankruptcy case "creates an estate." 11 U.S.C. § 541(a). As relevant here, the estate contains two types of property—(1) "all legal or equitable interests of the debtor in property," and (2) any property recovered by a representative of the estate in an avoidance action, including an avoidance action for a fraudulent transfer. *Id.* § 541(a)(1), (3); *see id.* §§ 544, 548, 550. FairPoint's estate thus included FairPoint's property and the proceeds of any fraudulent-transfer action.

During Chapter 11 proceedings, the debtor controls all estate property as the "debtor-in-possession" unless a bankruptcy trustee is appointed in the debtor's place. *See id.* §§ 1104, 1115(b); *see also id.* §§ 701-04 (governing appointment of bankruptcy trustee under Chapter 7). "[A]ppointment of a trustee is unusual in a bankruptcy filed under Chapter 11," *Cirka v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, 2004 WL 1813283, at *4 (Del. Ch.), and did not occur here. The commencement of a bankruptcy case also "operates as a stay" of any act to exercise control over estate property. 11 U.S.C. § 362(a). Accordingly, absent a bankruptcy-

court order to the contrary, the debtor-in-possession has the exclusive right to commence a fraudulent-transfer action "for the benefit of the estate," *id.* § 550(a)—creditors may not do so. Creditors may, however, file proofs of claim against the estate. *Id.* §§ 501-02. In FairPoint's bankruptcy, the Noteholders filed proofs of claim seeking payment of amounts due under the Notes. *See* A2056.

Debtors may exit Chapter 11 proceedings by formulating a reorganization plan, which categorizes the claims against the estate into classes and addresses how the debtor will treat each class. 11 U.S.C. §§ 1122-23. Under a plan, the debtor may transfer estate property and may provide for the enforcement of a claim or interest by a representative of the estate. *Id.* § 1123(a)(5), (b)(3)(B). If a plan is confirmed, the reorganized debtor emerges "free and clear of all claims and interests of creditors." *Id.* § 1141(c).

Here, FairPoint and its affiliates exited Chapter 11 proceedings by formulating a joint reorganization plan, which the bankruptcy court confirmed on January 13, 2011. A2000-2166. In the plan, FairPoint agreed to satisfy the claims of the Noteholders and other unsecured creditors through the creation of the Trust—a litigation trust governed by an agreement under New York law. A2196. FairPoint then transferred to the Trust the right to litigate certain causes of action against Verizon arising from the Spinoff. A2173-74. The Noteholders and other creditors

received beneficial interests in the Trust in satisfaction of their claims against the estate. A2046.

E. <u>The Trust Action</u>

On October 25, 2011, the Trust brought the Trust Action against Verizon and three subsidiaries in North Carolina state court. *See* A196. Alleging that the Spinoff saddled FairPoint with excessive debt, the Trust asserted two fraudulent-transfer counts under the Bankruptcy Code and North Carolina's fraudulent-transfer statute. A313, 350. The Trust's operative complaint explained that it was "a successor of [FairPoint and its affiliated debtors] and a representative of their estates." A337. The Trust thus brought the Trust Action "on behalf of creditors," who would "receive[] the benefit of [any] recoveries." A313, 315.

Generally, "[t]wo types of fraudulent transfers have been historically subject to challenge: 1) transfers made with actual intent to hinder, delay, or defraud creditors, referred to as actual fraudulent transfers; and 2) transfers made for less than reasonably equivalent [value] when a debtor was in financial trouble, referred to as constructive fraudulent transfers." 2 Joan N. Feeney *et al.*, Bankruptcy Law Manual § 9:29 (5th ed. 2022). Here, after removal to federal court, Verizon successfully moved for summary judgment on the Trust's constructive-fraudulent-transfer cause of action. The court also granted partial summary judgment to Verizon on the Trust's actual-fraudulent-transfer cause of action, finding that, to the

extent FairPoint was the transferor, FairPoint lacked the requisite improper intent to defraud creditors. *See* A372.

In December 2013, the court held a bench trial on the Trust's actual-fraudulent-transfer cause of action with respect to Spinco as the transferor. *See* A372. Verizon argued that, like FairPoint, Spinco lacked the requisite improper intent to defraud creditors. A472. Alternatively, Verizon argued that FairPoint was the only relevant transferor, and therefore FairPoint's lack of improper intent was dispositive of the entire case. A472-73. On June 18, 2014, before the court could rule, the parties settled, with Verizon agreeing to pay the Trust $95 million. A2221-43.

F. <u>Procedural History</u>

Verizon notified the Insurers of the Trust Action shortly after it was filed. National Union responded by letter, explaining that the Trust Action related to a prior notice of a Claim first made during the policy period of the Verizon Policy, but was not covered because it was not a Securities Claim. A2210-20. The other Insurers adopted National Union's position. *See* Ex. C, at 10.

Years later, on August 10, 2018, after the Superior Court's decision in *Idearc*, Verizon sued the Insurers under the Transaction and Verizon Towers, seeking coverage for its defense costs and settlement payments from the Trust Action. A107-30. When the Insurers moved to dismiss or stay pending resolution of a parallel

action in New York state court, Verizon opposed in part on the ground that this case was controlled by the Superior Court's decision in *Idearc*. A157, 176-77. On April 26, 2019, the Superior Court denied the Insurers' motion. Ex. D. As to the Insurers' request for dismissal, the court held that Verizon breached the policies by filing suit before mandatory cooling-off periods expired, but the court nevertheless refused to dismiss, reasoning that the Insurers were required, but failed, to show that they were prejudiced by Verizon's breach. *Id.* at 17-21.[2]

On October 31, 2019, this Court issued its decision in *Idearc*, reversing the Superior Court and foreclosing Verizon's reliance on the first prong of the Securities Claim definitions here. Undeterred, Verizon began arguing that the Trust Action was a Securities Claim under the second prong. On March 6, 2020, before discovery, Verizon moved for partial summary judgment, seeking a ruling that its defense costs are covered under the Transaction Tower. A180-81. The Insurers then cross-moved for judgment on the pleadings, explaining that Verizon's defense costs and settlement payments are not covered under either Tower because the Trust Action was not a Securities Claim. A216-54.

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[2] While the Insurers are not, on this appeal, challenging the Superior Court's imposition of a prejudice requirement, the Insurers reserve the right to challenge that holding in the future. *See, e.g.*, *Fernstrom v. Trunzo*, 2017 WL 6028871, at *2-3 (Del. Ch.), *aff'd*, 198 A.3d 178 (Del. 2018); *Murphy Expl. & Prod. Co. Int'l v. Republic of Ecuador*, ICSID Case No. ARB/08/4, Award on Jurisdiction, ¶¶ 90-157 (Dec. 15, 2010).

On February 23, 2021, the Superior Court granted Verizon's motion and denied the Insurers' motion. Ex. C. As to the Transaction Tower, the court reasoned that the Trust Action was "brought derivatively" because "fraudulent transfer claims are derivative as a matter of federal bankruptcy law." *Id.* at 22. The court reasoned that the Trust Action was brought "on the behalf of [FairPoint]" because the Trust received its authority to sue from FairPoint. *See id.* at 24-28. The court further reasoned that, although the Trust did not hold any securities, the Trust Action was "brought … by a security holder of [FairPoint]" because—"read[ing] this phrase and those surrounding it with reference to the United State[s] Bankruptcy Code and Chapter 11 proceedings"—the Trust "stands in the shoes" of the Noteholders. *Id.* at 18-19. Finally, as to the Verizon Tower, the court identified no ambiguity in the policy language, but nevertheless found material factual disputes regarding "Spinco's role in the [Spinoff]" and whether "Verizon could have reasonably expected that any Spinco-related liabilities would be covered despite Spinco's divestiture and dissolution." *Id.* at 29-30.[3]

[3] The Superior Court also held that the Insurers forfeited the right to argue that Verizon's defense costs were not "reasonable and necessary," A1703, 1780, because they failed "to raise a fairness and reasonableness issue when they initially denied coverage." Ex. C, at 31 (brackets omitted). Again, while the Insurers are not challenging that ruling on this appeal, they reserve the right to do so in the future. *See, e.g.*, *Bantam v. New Castle Cnty. Vo-Tech Educ. Ass'n*, 21 A.3d 44, 50 (Del. 2011); *Martin v. Colonial Ins. Co. of Cal.*, 644 F. Supp. 349, 352 (D. Del. 1986).

On February 11, 2022, after discovery, the Insurers moved for summary judgment, explaining that, at a minimum, the Trust Action was not a Securities Claim under the Verizon Policy. A255-301. Verizon cross-moved for summary judgment, arguing the opposite. A2244-97. On October 18, 2022, the Superior Court granted Verizon's motion and denied the Insurers' motion, relying heavily on its earlier opinion. Ex. B. Despite having previously held that the Trust Action was "brought derivatively on the behalf of [FairPoint] by a security holder of [FairPoint]," the court held that the 2011 Trust Action simultaneously was "brought derivatively on the behalf of [Spinco] by a security holder of [Spinco]," even though Spinco had dissolved when it merged into FairPoint in 2008. *Id.* at 16-17. The court also relied heavily on the Excess Endorsement, which, as explained, simply provides that any Spinoff-related coverage under the Verizon Tower is excess of the Transaction Tower. The court, however, concluded that "the parties intended this endorsement to expand coverage to liabilities incurred in the [Spinoff] to a maximum extent" and that "the endorsement was added to ensure that Spinco's Deal-related liabilities would continue to be covered under Verizon's policies after the Deal." *Id.* at 19-20. The court also cited deposition testimony from Verizon's corporate representative as evidence that Verizon had "a reasonable expectation of coverage," *id.* at 20 (citation omitted), despite identifying no ambiguity in the policy language.

The court entered final judgment on November 29, 2022. Ex. A. The Insurers timely appealed. A2298-2320.

ARGUMENT

I. The Trust Action Was Not a Securities Claim Under the Transaction Policy or the Verizon Policy

A. Question Presented

Whether the Trust Action was "brought derivatively on the behalf of an **Organization** by a security holder of such **Organization**" under the Transaction and Verizon Policies. No. (Preserved at A239, 280.)

B. Scope of Review

This Court reviews the grant of summary judgment and the interpretation of an insurance policy *de novo*. *See Idearc*, 222 A.3d at 572.

C. Merits of Argument

The Trust Action does not fall within the Securities Claim definitions in the Transaction and Verizon Policies, for two reasons. First, the Trust Action was not "brought derivatively on the behalf of an **Organization**." Second, the Trust Action was not "brought … by a security holder." The Superior Court's contrary reasoning misconstrues the plain language of the Securities Claim definitions and misapprehends bankruptcy principles.

1. **<u>The Trust Action Was Not "Brought Derivatively on the Behalf of an Organization"</u>**

a. The Securities Claim Definitions Track the Concept of a Derivative Action

"[T]he scope of an insurance policy's coverage ... is prescribed by the language of the policy." *First Solar, Inc. v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, 274 A.3d 1006, 1013 (Del. 2022) (citation omitted). "[A]bsent ambiguity, Delaware courts interpret contract terms according to their plain, ordinary meaning." *Id.* (quotation marks omitted). It is the "insured's burden … to establish that a claim falls within the basic scope of coverage." *RSUI Indem. Co. v. Murdock*, 248 A.3d 887, 906 (Del. 2021).

Contract language also must be "[v]iewed in proper context." *Chicago Bridge & Iron Co. N.V. v. Westinghouse Elec. Co.*, 166 A.3d 912, 916 (Del. 2017). This Court has stressed the importance of context in interpreting the Securities Claim definition in a D&O policy. When construing the Securities Claim definition in *Idearc*, this Court began by noting that "the words used in the definition mirror those in a specific area of the law recognized as securities regulation." 222 A.3d at 573. The definition in *Idearc*, for example, referred to "the purchase or sale or offer … to purchase or sell securities," and "securities laws typically apply to the purchase or sale, or offer for sale of securities." *Id.* at 572-73 (quotation marks omitted). The definition also referred to a "'regulation, rule or statute regulating securities,'" and

"securities laws typically involve not only statutes, but also rules and regulations." *Id.* (quoting policy language). The Court thus "start[ed] with a basic understanding of the words used in the policy that the definition of a Securities Claim is aimed at a particular area of the law, securities law, and not of general application to other areas of the law." *Id.* at 574.

This Court's reasoning applies not just to the particular part of the Securities Claim definition at issue in *Idearc*, but to "the definition of a Securities Claim" generally. *Id.* Accordingly, while this case involves a different part of the Securities Claim definitions—defining a Securities Claim as a Claim "brought derivatively on the behalf of an **Organization** by a security holder of such **Organization**"—that language also must be read in the context of securities law. Indeed, the language at issue here is adjacent to the same language this Court considered in *Idearc*. *See id.* at 572-73; A1706; A1783. The language here also includes the term "***security*** holder." A1706 (emphasis added).

In that context, the phrase "brought derivatively on the behalf of an **Organization** by a security holder of such **Organization**" unambiguously refers to a derivative action. As this Court has explained, "[t]he derivative action developed in equity to enable shareholders to sue in the corporation's name where those in control of the company refused to assert a claim belonging to it." *Aronson v. Lewis*, 473 A.2d 805, 811 (Del. 1984), *overruled on other grounds by Brehm v. Eisner*, 746

A.2d 244 (Del. 2000). A derivative action accordingly "enables a stockholder to bring suit on behalf of the corporation for harm done to the corporation." *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1036 (Del. 2004).

Derivative actions typically are brought by stockholders, but they can be brought by other security holders as well. When a corporation is insolvent, derivative actions for breach of fiduciary duty can be brought by creditors, who "take the place of the shareholders as the residual beneficiaries of any increase in value." *N. Am. Cath. Educ. Programming Found., Inc. v. Gheewalla*, 930 A.2d 92, 101 (Del. 2007). Derivative actions also can be brought by LLC members, *see CML V, LLC v. Bax*, 28 A.3d 1037, 1041 (Del. 2011), or by limited partners, *see El Paso Pipeline GP Co. v. Brinckerhoff*, 152 A.3d 1248, 1260 (Del. 2016).

Regardless of the type of security holder suing, the basic doctrinal tests for distinguishing direct and derivative actions are well settled. Under *Citigroup Inc. v. AHW Investment Partnership*, 140 A.3d 1125 (Del. 2016), where a cause of action "belong[s] to the [security] holder[]" and could "not … plausibly belong to the issuer corporation," such that the plaintiff is plainly suing "based on the plaintiff's own right," the analysis is simple—the cause of action is direct. *Id.* at 1138-40. Under *Tooley*, a different analysis applies when the cause of action plausibly could belong to the security holder or the corporation, as when the corporation and stockholders both are owed fiduciary duties by the same directors. *See id.* at 1139-40. In that

circumstance, whether the cause of action is direct or derivative turns on "(1) who suffered the alleged harm …; and (2) who would receive the benefit of any recovery or other remedy"—"the corporation or the stockholders, individually." *Tooley*, 845 A.2d at 1033.

The distinction between direct and derivative actions is significant because derivative actions are subject to special requirements. For example, before commencing a derivative action, plaintiffs must make a demand on the board of directors or show that demand would be futile. *See* Ct. Ch. R. 23.1(a); 13 Fletcher Cyc. Corp. § 5963 (2022) ("Fletcher"). Similarly, settlements in derivative actions are subject to court approval and special notice requirements. *See* Ct. Ch. R. 23.1(c); 13 Fletcher § 6020.05. Finally, "[b]ecause a derivative suit is being brought on behalf of the corporation, the recovery, if any, must go to the corporation." *Tooley*, 845 A.2d at 1036; *see* 13 Fletcher § 6028.

b. The Trust Action Was Not a Derivative Action

Here, the Trust Action was not a derivative action as understood in the context of corporate and securities law, for three reasons.

First, the Trust Action was direct, not derivative, under *Citigroup*. The Trust's fraudulent-transfer causes of action "belong[ed] to" the Noteholders and enforced the Noteholders' "own right[s]" as creditors. *Citigroup*, 140 A.3d at 1138-40. The Trust's causes of action accordingly could "not … plausibly belong to" FairPoint (or

Spinco). *Id.* at 1138. Indeed, the Court of Chancery has repeatedly described fraudulent-transfer actions as direct, not derivative. *See Trenwick Am. Litig. Tr. v. Ernst & Young, L.L.P.*, 906 A.2d 168, 199 (Del. Ch. 2006) ("In a fraudulent conveyance suit[,] … the creditors … would have had direct standing …."), *aff'd*, 931 A.2d 438 (Del. 2007); *Quadrant Structured Prods. Co. v. Vertin*, 102 A.3d 155, 166 (Del. Ch. 2014) (describing "fraudulent transfer claims" as being brought "directly").

That fraudulent-transfer actions are direct, not derivative, follows from the "creditor focus of fraudulent transfers." *In re Cybergenics Corp.*, 226 F.3d 237, 242 (3d Cir. 2000). As a "well-known treatise" explains, "[t]he fraudulent conveyance, as known in our law, may be roughly defined as an infringement of the ***creditor's right*** to realize upon the available assets of his debtor." *Id.* (emphasis added) (citation omitted). Accordingly, "fraudulent transfer claims have long belonged to a transferor's *creditors*, whose efforts to collect their debts have essentially been thwarted as a consequence of the transferor's actions." *Id.* at 241 (emphasis original). As the Court of Chancery has observed, "the law of fraudulent conveyance exists specifically to protect creditors." *Prod. Res. Grp., L.L.C. v. NCT Grp., Inc.*, 863 A.2d 772, 777 (Del. Ch. 2004).

For this reason, courts have consistently held that, "[f]or the purpose of [fraudulent-transfer] claims," a representative of the estate "stands in the shoes of

the creditors, not the debtors." *In re EPD Inv. Co.*, 821 F.3d 1146, 1152 (9th Cir. 2016); *see In re Upper Crust, LLC*, 554 B.R. 23, 32-34 (Bankr. D. Mass. 2016) (similar); *In re LMI Legacy Holdings, Inc.*, 553 B.R. 235, 246 (Bankr. D. Del. 2016) (similar). The Superior Court acknowledged that an estate representative bringing a fraudulent-transfer action "stands in the shoes of the creditor." Ex. C, at 19 (quotation marks omitted). Likewise, the Trust expressly alleged that it sued "on behalf of creditors." A313. In a derivative action, by contrast, the security holder "stand[s] in the shoes of the corporation." 13 Fletcher § 5954.30; *see Schleiff v. Baltimore & Ohio R.R.*, 130 A.2d 321, 351 (Del. Ch. 1955).

That debtors-in-possession may bring fraudulent-transfer actions on behalf of a bankruptcy estate does not change the analysis. The power to bring fraudulent-transfer actions "simply enables a debtor in possession" to "maximize the bankruptcy estate for the benefit of creditors." *Cybergenics*, 226 F.3d at 243-44. "Does this [power] mean that the chapter 11 debtor in possession actually acquires its creditors' fraudulent transfer claims against third parties as a result of filing for bankruptcy? … [T]he answer is clearly 'no.'" *Id.* at 242-43. The "avoidance powers" granted to debtors-in-possession under the Bankruptcy Code "neither shift ownership of the fraudulent transfer action to the debtor in possession, nor are themselves a debtor's assets." *Id.* at 244.

North Carolina's fraudulent-transfer statute confirms that the Trust Action enforced the rights of the Noteholders, not FairPoint (or Spinco). That statute provides that a fraudulent transfer "is voidable as to ***a creditor***," and authorizes a "***creditor*** [to] mak[e] a claim for relief." N.C. Gen. Stat. § 39-23.4(a), (c) (emphasis added); *see id.* § 39-23.5(a), (c) (same). Furthermore, in a section entitled "Remedies of ***creditor***," the statute lays out relief that "a ***creditor*** … may obtain." *Id.* § 39-23.7(a) (emphases added). Plainly, fraudulent-transfer actions belong to and enforce the rights of creditors, not the debtor.

Second, the Trust Action was direct, not derivative, under *Tooley*. As to "who suffered the alleged harm," *Tooley*, 845 A.2d at 1033, fraudulent-transfer actions allege harm to creditors, who are injured when the debtor places assets beyond creditors' reach. *See Cybergenics*, 226 F.3d at 241-42. The "harm … in a fraudulent transfer" is "the debtor's alienation of an asset otherwise available to pay its debts." *Crystallex Int'l Corp. v. Petróleos De Venezuela, S.A.*, 879 F.3d 79, 85 (3d Cir. 2018). That harm is "visited upon creditors," not the debtor. *Id.*

As to "who would receive the benefit of any recovery or other remedy," *Tooley*, 845 A.2d at 1033, estate representatives may recover fraudulent-transfer proceeds only "for the benefit of the estate." 11 U.S.C. § 550(a). Chapter 11 debtors-in-possession therefore must bring fraudulent-transfer actions to "benefit the creditors, not the debtors themselves." *Cybergenics*, 226 F.3d at 244. As one treatise

explains, "fraudulent transfer law generally is not intended to aid the debtor-transferor to recover property; a transfer is generally valid as between the debtor and the transferee." 5 Collier on Bankr. ¶ 548.10[2] (16th ed. 2022).

Here, moreover, FairPoint's reorganization plan and the Trust agreement both barred fraudulent-transfer proceeds from ***ever*** going to FairPoint (or Spinco, which did not exist). Under the plan, "[a]ny recoveries" by the Trust "shall be distributed to the holders of Litigation Trust Interests"—as relevant here, the Noteholders. A2047. Furthermore, once FairPoint transferred them to the Trust, "FairPoint … shall have no interest in or with respect to the Litigation Trust Assets or the Litigation Trust." A2048. Similarly, under the Trust agreement, "all net proceeds, income, and recoveries of or on account of" any causes of action asserted by the Trust "shall be transferred to the Litigation Trust to be distributed to the Litigation Trust Beneficiaries"—again, the Noteholders. A2176. Furthermore, "[i]n no event shall any part of the Litigation Trust Claims (including Litigation Trust Proceeds …) revert to or be distributed to FairPoint." A2173. Consistent with these provisions, the Trust alleged that "creditors" would "receive[] the benefit of recoveries from the causes of action asserted in [the Trust Action]." A313, 315. FairPoint (and Spinco) had no right or ability to receive ***any*** recovery from the Trust Action.

North Carolina's fraudulent-transfer statute is to the same effect. As explained, in a "Remedies of ***creditor***" provision, the statute sets forth relief that "a

creditor … may obtain." N.C. Gen. Stat. § 39-23.7(a) (emphases added). The remedies provision also states that creditors may obtain "[a]n injunction against further disposition [of property] ***by the debtor***." *Id.* § 39-23.7(a)(3)(a) (emphasis added). In other words, far from being the recipient of relief, the debtor may be the ***object*** of that relief.

Third, tellingly, no participant in the Trust Action treated it as a derivative action at the time. Verizon removed the Trust Action to federal court, and the Federal Rules of Civil Procedure impose pleading requirements on derivative actions to ensure compliance with the demand requirement. *See* Fed. R. Civ. P. 23.1(a). But the Trust's operative complaint, on its face, made no attempt to comply with those requirements, nor did Verizon or the court attempt to enforce them. *See* A311-58. Similarly, the Federal Rules impose requirements on derivative-action settlements, but the settlement of the Trust Action, on its face, did not comply with those requirements either. *See* Fed. R. Civ. P. 23.1(c); A2221-43. Finally, any recovery in a derivative action "must go to the corporation," *Tooley*, 845 A.2d at 1036, but Verizon made payment to the Trust, which distributed the funds to the Trust's beneficiaries, including the Noteholders, *see* A2224-25; A2180. No settlement funds went to FairPoint (or Spinco). While it was pending, the Trust, Verizon, and the court all treated the Trust Action as if it were ***not*** a derivative action. This Court should do the same.

c. The Superior Court Erred in Creating a Bankruptcy-Specific Interpretation of the Securities Claim Definitions

In holding that the Trust Action was "brought derivatively on the behalf of an **Organization**" under the Transaction and Verizon Policies, the Superior Court did not apply the tests from this Court's caselaw on direct and derivative actions in the context of corporate and securities law. Instead, the court purported to construe the Securities Claim definitions "with reference to the United State[s] Bankruptcy Code and Chapter 11 proceedings," ultimately concluding that "fraudulent transfer claims are derivative as a matter of federal bankruptcy law." Ex. C, at 18, 22. The court reached that conclusion under a "two-step analysis" drawn from bankruptcy law—it determined first whether "the claim attached before the bankruptcy was filed," and second "whether the claim [wa]s general to the [bankruptcy] estate or personal to the creditor." *Id.* at 21 (quotation marks omitted). That bankruptcy-based analysis was erroneous for multiple reasons.

First, the court ignored the context of the Securities Claim definitions. As explained in *Idearc*, "the definition of a Securities Claim is aimed at a particular area of the law, securities law." 222 A.3d at 574. Accordingly, "[v]iewed in proper context," *Chicago Bridge*, 166 A.3d at 916, the Securities Claim definitions must be given their ordinary meaning in the context of corporate and securities law. "Here, the controlling rule of construction is that a single clause or paragraph of a contract cannot be read in isolation, but must be read in context." *Stonewall Ins. Co. v. E.I.*

du Pont de Nemours & Co., 996 A.2d 1254, 1260 (Del. 2010) (quotation marks and brackets omitted).

Second, the structure of the Transaction and Verizon Policies confirms that the Securities Claim definitions do not have a bankruptcy-specific meaning. While the policies contain some bankruptcy-specific provisions, the Securities Claim definitions are not among them. For example, both policies contain an exclusion for certain Claims brought by one insured against another insured, and then provide an exception to that exclusion for Claims brought in a "bankruptcy proceeding." A1708; A1785. Both policies also contain a provision (the "Bankruptcy Provision") stating that the "[b]ankruptcy … of any **Organization** or any **Insured Person** shall not relieve the **Insurer** of any of its obligations hereunder." A1716; A1793. These provisions demonstrate that the parties "knew how" to tie coverage to the bankruptcy context "when that was intended." *Idearc*, 222 A.3d at 578.

The Superior Court acknowledged these bankruptcy-specific provisions, Ex. C, at 23-24, but drew the wrong conclusion from them. In the court's view, giving the Securities Claim definitions their plain meaning in the corporate- and securities-law context "would nullify the bankruptcy carve-outs in the [Transaction] Policy." *Id.* at 24. But those provisions do not guarantee coverage or alter the scope of the Securities Claim definitions. Nor would giving the Securities Claim definitions their plain meaning "relieve the Insurer[s] of any of [their] obligations."

Id. at 6. Rather, it would simply confirm that the Insurers have no obligation to cover the Trust Action in the first place. *See infra*, § I.C.2 (discussing the Bankruptcy Provision further).

Third, the Superior Court's reasoning would mean that the meaning of the Securities Claim definitions would depend on the circumstances where a Claim arises. Variants of the word "derivatively," after all, are used in many different areas of the law. If "derivatively" took its meaning from the circumstances where a Claim arises, it would have different meanings in different cases. The unambiguous policy language, however, can have only "one meaning." *O'Brien v. Progressive N. Ins. Co.*, 785 A.2d 281, 291 (Del. 2001).

The Superior Court recognized the problem with giving the same policy language multiple meanings. It acknowledged: "[T]he Securities Claim definition is not dependent on whether a Claim is brought outside or inside bankruptcy. The definition's unambiguous language does not make such distinctions." Ex. C, at 23. Nevertheless, the court's reasoning made precisely that distinction—because the Trust Action arose from a bankruptcy, the court applied a "two-step analysis" that is specific to, and makes no sense outside of, the bankruptcy context. *Id.* at 21-22.

Finally, the Superior Court incorrectly suggested that the Trust Action would have been derivative outside of bankruptcy. In the court's view, "creditors possess derivative standing to bring clawback actions on behalf of a corporation when that

corporation is insolvent," and "FairPoint's creditors thus could have brought fraudulent transfer claims derivatively outside bankruptcy." *Id.* at 23. That is wrong. While creditors of insolvent corporations may assert derivative causes of action for breach of fiduciary duty that they could not assert otherwise, *see Gheewalla*, 930 A.2d at 101, that does not mean that ***all*** causes of action asserted by creditors of insolvent corporations are derivative, or that ***fraudulent-transfer actions*** are derivative. To the contrary, the Court of Chancery has repeatedly described fraudulent-transfer actions as "direct[]." *Trenwick*, 906 A.2d at 199; *Quadrant*, 102 A.3d at 166.

d. The Trust Action Was Not a Securities Claim Under Bankruptcy Principles

Even if the Securities Claim definition were construed in light of bankruptcy-specific principles, the Trust Action still was not "brought derivatively on the behalf of an **Organization**." That is for two reasons.

First, the Trust Action was not "brought derivatively" under bankruptcy principles. In bankruptcy, "[t]he term 'derivative standing' … is used to refer to standing available to creditors … to pursue avoidance actions" in place of the bankruptcy trustee or debtor-in-possession. *Derivative Standing*, Norton Bankr. L. & Prac., Dict. Of Bankr. Terms, § D90 (3d ed. 2008). Derivative standing, however, "is the exception rather than the rule," and is permitted "only under strict conditions." *In re Balt. Emergency Servs. II, Corp.*, 432 F.3d 557, 561-62 (4th Cir.

2005). Creditors invoking derivative standing must obtain bankruptcy-court permission and make detailed showings specific to the particular litigation being pursued. *See In re Commodore Int'l Ltd.*, 262 F.3d 96, 99-100 (2d Cir. 2001).

Here, the Trust did not invoke such derivative standing. Indeed, courts have drawn a ***contrast*** between derivative standing and transferring causes of action to a litigation trust. *See In re Adelphia Commc'ns Corp.*, 544 F.3d 420, 425 (2d Cir. 2008) (explaining that a bankruptcy court "withdr[e]w" derivative standing when it authorized the estate to transfer causes of action "to a litigation trust"). The Trust never obtained bankruptcy-court permission to file the Trust Action, and it never showed that the Trust Action satisfied the strict requirements for derivative standing under bankruptcy law. That was unnecessary because FairPoint transferred litigation authority to the Trust as part of FairPoint's exit from bankruptcy. The Trust then brought the Trust Action directly, under its own authority, without any need for derivative standing.

The Third Circuit's decision in *In re Wilton Armetale, Inc.*, 968 F.3d 273 (3d Cir. 2020), on which the Superior Court heavily relied, is not to the contrary. In *Wilton Armetale*, a Chapter 7 bankruptcy trustee abandoned a fraudulent-transfer action, lacking funds to pursue it. *Id.* at 279. Due to that abandonment, the Third Circuit held, the fraudulent-transfer action reverted to creditors, who owned the causes of action pre-bankruptcy. *Id.* at 277-78. In that context, the court used the

term “derivative” to explain why, between the bankruptcy filing and abandonment, the bankruptcy trustee had exclusive authority to pursue the fraudulent-transfer action. As the court explained, “[o]nly the trustee can pursue claims that rely on a derivative theory of recovery”—that is, claims that are “‘general’ to the estate” rather than “‘personal’ to a specific creditor.” *Id.* at 282. But the fact that, under Chapter 7, fraudulent-transfer actions generally must be brought by the bankruptcy trustee does not mean that such actions are always automatically “brought derivatively.” When brought by a bankruptcy trustee, a debtor-in-possession, or a successor thereof, fraudulent-transfer actions are brought directly, not derivatively. This Court recently observed that, when a Chapter 7 bankruptcy trustee sues on behalf of the estate, it proceeds “directly,” not derivatively. *Lenois v. Sommers as Tr. For Erin Energy Corp.*, 268 A.3d 220, 236 (Del. 2021).

Second, even if the Trust Action were “brought derivatively” under bankruptcy principles, it was not “brought derivatively on the behalf of” FairPoint (or Spinco). As explained, the Bankruptcy Code authorizes recovery of fraudulent-transfer proceeds only “for the benefit of the estate.” 11 U.S.C. § 550(a). The Superior Court acknowledged as much. *See* Ex. C, at 26. But if the Trust Action was brought on behalf of the estate, then it was not brought on behalf of FairPoint. The Court of Chancery has held under a D&O policy that, where a suit is brought by creditors invoking derivative standing in bankruptcy, the suit is brought “on behalf

of the [e]state ***only***"—"***not*** on behalf of the debtor in possession." *Cirka*, 2004 WL 1813283, at *1, *9 (emphases added).

The Superior Court's contrary holding reflects multiple errors. To begin with, the court improperly conflated the estate and the debtor. In the court's view, "in a Chapter 11 bankruptcy," "[t]he debtor exists temporarily as an estate until it reorganizes," and "there is no practical difference" between the two. Ex. C, at 27. That is incorrect. The Court of Chancery has rejected that notion, explaining that "[t]he [e]state … is a separate entity from the [d]ebtor in [p]ossession." *Cirka*, 2004 WL 1813283, at *7 n.52. One of the Superior Court's own cited authorities states: "That the debtor and the estate are distinct concepts is a fundamental concept of bankruptcy law that does not require elaboration." *In re Edwards*, 2003 WL 22110778, at *3 (Bankr. E.D. Pa.).

Furthermore, even under the Superior Court's view that the debtor and the estate are indistinguishable "until [the debtor] reorganizes," Ex. C, at 27, FairPoint reorganized in ***January 2011***. At that point, FairPoint was "free and clear of all claims and interests of creditors." 11 U.S.C. § 1141(c). When the Trust Action was filed nine months later, therefore, FairPoint and its estate were entirely distinct. Accordingly, even if the October 2011 Trust Action were deemed brought derivatively on behalf of ***the estate***, it was not brought derivatively on behalf of ***FairPoint*** (or Spinco).

The Superior Court also improperly conflated a Code-created bankruptcy trustee with a plan-created litigation trustee. FairPoint's Chapter 11 estate was administered by FairPoint as debtor-in-possession; no bankruptcy trustee was ever appointed. *See* A2016. As part of FairPoint's reorganization plan, however, FairPoint formed the Trust under New York law and transferred estate property to it. A2173, 2196. The Superior Court repeatedly described the Trust's trustee as if he were a statutory bankruptcy trustee appointed under 11 U.S.C. §§ 702 or 1104, which he was not. *See* Ex. C, at 24-27.

In so doing, the Superior Court overlooked that any proceeds the Trust recovered would be distributed solely in accordance with the plan and the Trust agreement. Under those January 2011 instruments, "FairPoint … shall have no interest in or with respect to" any fraudulent-transfer proceeds, and "[i]n no event shall any part of [such proceeds] revert to or be distributed to FairPoint." A2048; A2173-75. These provisions further refute any notion that the October 2011 Trust Action was brought derivatively on behalf of FairPoint (or Spinco).

Finally, the Superior Court misunderstood the nature of fraudulent-transfer actions. According to the court, "fraudulent transfers cause primary injury to the debtor that creates secondary harm to its creditors." Ex. C, at 25 (quotation marks omitted). On that basis, the court concluded that the Trust Action "asserted claims regarding 'injury' to FairPoint." *Id.* But as explained, fraudulent-transfer actions

do ***not*** seek redress for injury to the debtor. An estate representative bringing a fraudulent-transfer action "stands in the shoes of the creditors, not the debtor[]." *EPD*, 821 F.3d at 1152. Indeed, the debtor is a potential ***defendant*** in a fraudulent-transfer action. *See* N.C. Gen. Stat. § 39-23.7(a)(3). Under the plan and the Trust agreement, moreover, FairPoint had no right to ***any*** fraudulent-transfer proceeds. *See supra* § I.C.1.b.

Accordingly, the Trust Action was not a Securities Claim under corporate- and securities-law principles ***or*** bankruptcy-law principles. Under the unambiguous policy language, the Trust Action was not "brought derivatively on the behalf of an **Organization**."

2. The Trust Action Was Not "Brought … by a Security Holder"

Even if the Trust Action were "brought derivatively on the behalf of an **Organization**," it still was not a Securities Claim under the Transaction and Verizon Policies because it was not "brought … by a security holder." A civil lawsuit is "brought … by" the named plaintiff or petitioner. As one court explained in construing the phrase "claim brought by" in a D&O policy, "[b]y its plain and unambiguous meaning, the focus of the phrase is on who is bringing the claim." *In re Molten Metal Tech., Inc.*, 271 B.R. 711, 726 (Bankr. D. Mass. 2002). Here, the Trust Action was "brought … by" the Trust. *See* A312.

In addition, as the Superior Court acknowledged, "[a] holder is 'a person with legal possession of a document of title or an investment security.'" Ex. C, at 20 (quoting *Holder*, Black's Law Dictionary (11th ed. 2019)). Here, the Trust did ***not*** possess any securities of FairPoint or Spinco. *See* A2167-2209; Ex. C, at 19-20. That should end the matter. "[I]t is not the proper role of a court to rewrite or supply omitted provisions to a written agreement." *Cincinnati SMSA Ltd. P'ship v. Cincinnati Bell Cellular Sys. Co.*, 708 A.2d 989, 992 (Del. 1998).

In reaching a contrary conclusion, the Superior Court acknowledged the Insurers' argument that "only a Securities Claim brought by a true security holder qualifies for coverage," but was "not persuaded … on these facts." Ex. C, at 19-20. The court reasoned that, "in bankruptcy, FairPoint's debt security holders could not pursue claims related to their notes. Only the Trust[] could pursue those claims." *Id.* at 20. That is wrong on two levels. First, in fact, the Noteholders could have pursued Notes-related causes of action if the debtor-in-possession transferred that authority to them or they obtained bankruptcy-court permission to sue on the estate's behalf. Second, and more fundamentally, what the Noteholders "could" have done, hypothetically, does not matter. Under the policy language, what matters is what party actually "brought" the Claim at issue and whether that party was a "security holder."

The Superior Court's holding is simply incompatible with the policy language. The Superior Court effectively reasoned that the Noteholders were security holders of FairPoint, and it was close enough for the Trust Action to be brought ***on behalf of*** the Noteholders. But the policy language does not say "brought … by ***or on behalf of*** a security holder"; it says "brought … ***by*** a security holder." Indeed, the words immediately preceding "by a security holder" are "***on the behalf of*** an **Organization**." A1706, 1783 (emphasis added). The parties thus "knew how" to refer to a Claim brought ***by*** one party ***on behalf of*** another party "when that was intended." *Idearc*, 222 A.3d at 578.

The Superior Court also relied on the Bankruptcy Provision, which provides that the "[b]ankruptcy … of any **Organization** … shall not relieve the **Insurer** of any of its obligations hereunder." A1716, 1793. The court reasoned that applying the plain meaning of "brought … by a security holder" here "would, in fact, relieve [the Insurers] of their obligation to cover Securities Claims if FairPoint goes bankrupt." Ex. C, at 20. Not so. Nothing in the Bankruptcy Provision expands the Securities Claim definitions. The Bankruptcy Provision "simply means" that, to the extent the Insurers have obligations under the policies, those obligations "continue[] even [if]" FairPoint or Verizon "filed a bankruptcy case." *In re USA Gymnastics*, 624 B.R. 443, 455 (Bankr. S.D. Ind. 2021). Here, the Insurers are "not arguing that [their] obligations are relieved by [FairPoint]'s bankruptcy." *Eichler v. Twin City*

Fire Ins. Co., 2014 WL 12572922, at *2 n.3 (C.D. Cal.). "Rather, [they are] argu[ing]—correctly—that [their] obligations have not yet been triggered under the terms of the Polic[ies]," *id.*, because the Trust Action is not a Securities Claim.

Furthermore, policy language must be "[v]iewed in proper context," *Chicago Bridge*, 166 A.3d at 916, and the context of the Bankruptcy Provision is that it has long been mandated by statute in "a number of states." Patricia A. Bronte, *'Pay First' Provisions and the Insolvent Policyholder*, 3 Ins. Coverage L. Bull., no. 5, 2004, *available at* https://bit.ly/3vXVpE5. Before those statutes, "recovery by an injured party could be defeated by the technical interpretation of the insurance policy as indemnifying the insured against only loss[,] i.e., payment." *175 E. 74th Corp. v. Hartford Acc. & Indem. Co.*, 416 N.E.2d 584, 586 (N.Y. 1980). "The insolvency or bankruptcy of an insured, which prevented payment, necessarily relieved the insurer of any obligation to the insured[,] and the injured party was left without a source of recovery." *Id.* The statutes thus were "enacted to meet the situations … where it was held that there was no loss until payment of liability, and consequently in cases of bankruptcy there was no loss and no right of recovery." *Gen. Acc. Assur. Co. v. Caldwell*, 59 F.2d 473, 474 (9th Cir. 1932). Critically, these statutes "were enacted for the benefit of injured parties," not insureds, and "do not enlarge or extend the insurer's liability." *Gen. Acc. Fire & Life Assur. Corp. v. Aetna Cas. & Sur. Co.*, 158 S.E.2d 750, 753 (Va. 1968).

Here, the Insurers have not argued that FairPoint's bankruptcy prevented payment by Verizon and therefore precluded coverage. The Bankruptcy Provision and the statutes that mandate it are therefore inapposite. The Trust Action was not "brought … by a security holder," and accordingly was not a Securities Claim under the Transaction and Verizon Policies.

II. At a Minimum, the Trust Action Was Not a Securities Claim Under the Verizon Policy

A. Question Presented

Whether the Trust Action was "brought derivatively on the behalf of an **Organization** by a security holder of such **Organization**" under the Verizon Policy. No. (Preserved at A280-90.)

B. Scope of Review

This Court reviews the grant of summary judgment and the interpretation of an insurance policy *de novo*. *See Idearc*, 222 A.3d at 572.

C. Merits of Argument

Even if the Trust Action somehow were deemed a Securities Claim under the Transaction Policy, it was not a Securities Claim under the Verizon Policy. As explained, while the Securities Claim definitions in the two policies are identical, "**Organization**" has a different meaning under the two policies. Under the Transaction Policy, "**Organization**" includes FairPoint, while under the Verizon Policy, "**Organization**" includes only Verizon and any "**Subsidiary**," but undisputedly does ***not*** include FairPoint.

Verizon's theory under the Verizon Policy is that the relevant "**Organization**" is Spinco. To meet its burden under the Verizon Policy, therefore, Verizon had to make three showings: (1) that the Trust Action was "brought derivatively on the behalf of [Spinco]," (2) that Spinco was an "**Organization**" when the Trust Action

was "brought," and (3) that the Trust Action was "brought … by a security holder of [Spinco]." But Verizon could not make any of those showings because, when the Trust Action was brought in 2011, Spinco did not exist, and all its rights and obligations had been acquired by FairPoint. The Superior Court's reasoning contradicts the Verizon Policy's plain terms.

1. <u>**The Trust Action Was Not "Brought Derivatively on the Behalf of [Spinco]"**</u>

The Trust Action was not a Securities Claim under the Verizon Policy because it was not "brought derivatively on the behalf of [Spinco]." As the Superior Court acknowledged, the phrase "on the behalf of" means "in the name of, on the part of, as the agent or representative of." Ex. C, at 24 (quoting *On behalf of*, Black's Law Dictionary (11th ed. 2019)). That meaning necessarily implies taking action in the name of, on the part of, or as the agent or representative of a person or entity ***that exists***. A nonexistent entity lacks capacity to act, or for anyone to act on its behalf.

This Court has addressed this issue in the context of "the continuous ownership rule." *Brookfield Asset Mgmt., Inc. v. Rosson*, 261 A.3d 1251, 1262 n.35 (Del. 2021). Under that rule, "[a] plaintiff who ceases to be a shareholder, whether by reason of a merger or for any other reason, loses standing to continue a derivative suit." *Lewis v. Anderson*, 477 A.2d 1040, 1049 (Del. 1984). In a merger, any derivative causes of action, as assets of the corporation, "pass[]" to the surviving corporation. *Id.* at 1050. At that point, if a derivative action is to be brought, it must

be brought on behalf of the surviving corporation by a security holder of the surviving corporation. No cause of action can be brought derivatively on behalf of a nonexistent entity that dissolved in a merger. *See id.* at 1049-50. This is a basic principle of Delaware corporate law. *See, e.g.*, *El Paso*, 152 A.3d at 1265; *Ark. Tchr. Ret. Sys. v. Countrywide Fin. Corp.*, 75 A.3d 888, 894 (Del. 2013); *Brokerage Jamie Goldenberg Komen Rev Tru U/A 06/10/08 Jamie L Komen Tr. for Komen v. Breyer*, 2020 WL 3484956, at *7, *14 (Del. Ch.).

Here, when the Trust Action was "brought" in 2011, Spinco did not exist as a legal entity. During the Spinoff in 2008, it was agreed that "Spinco shall be merged with and into [FairPoint] …, [and] the separate existence of Spinco shall cease." A558. The Superior Court acknowledged that Spinco "ceased to exist" and "dissolved" during the Spinoff. Ex. C, at 20 n.129; Ex. B, at 7, 17. Because Spinco did not exist when the Trust Action was brought three and a half years later, the Trust Action could not possibly have been brought "on the behalf of" Spinco.

The Superior Court reached a contrary conclusion on the ground that "Spinco's causes of action automatically passed to 'new' FairPoint in the Merger, so 'new' FairPoint—and the Trustee later appointed in 'new' FairPoint's bankruptcy—could assert those causes of action on Spinco's behalf." Ex. B, at 17. But the fraudulent-transfer causes of action the Trust asserted were not "Spinco's causes of action." In 2008, the fraudulent-transfer causes of action belonged to

creditors; in 2009, authority to assert the causes of action passed to FairPoint as debtor-in-possession; and in 2011, litigation authority passed to the Trust. These causes of action were ***never*** held by Spinco.

Furthermore, even if "Spinco's causes of action" existed in 2011, Spinco ***itself*** did not. Spinco dissolved in the Spinoff in 2008, and all its assets—including its legal rights and causes of action—became assets of FairPoint. As the merger agreement provides, "all the property, rights, privileges, powers and franchises of [FairPoint] and Spinco shall vest in [FairPoint]." A558; *see* A1016 (similar in Indenture). The Insurers are not aware of any case where any other court has held that lawsuit was "brought derivatively on the behalf" of an entity that did not exist at the time the lawsuit was filed due to a merger. Numerous cases hold the opposite. *E.g.*, *Breyer*, 2020 WL 3484956, at *7, *14.

More broadly, the Superior Court's two decisions together held that the Trust Action was brought on behalf of ***four*** separate parties. In the court's view, the Trust Action was brought on behalf of the Noteholders, FairPoint's estate, FairPoint itself, and Spinco. Ex. C, at 24, 27; Ex. B, at 17. That is untenable. The phrase "derivatively on the behalf of" cannot possibly refer to all those different things simultaneously. Because the Trust Action was not "brought derivatively on the behalf of [Spinco]," it was not a Securities Claim under the Verizon Policy.

2. Spinco Was Not an "Organization" When the Trust Action Was "Brought"

Even if the Trust Action were deemed "brought derivatively on the behalf of [Spinco]," it still was not a Securities Claim under the Verizon Policy because Spinco was not a Verizon "**Organization**" when the Trust Action was "brought." Under the Verizon Policy, "**Organization**" includes "each **Subsidiary**," which in turn includes "any for-profit entity of which [Verizon] has **Management Control** … on or before the inception of the **Policy Period**." A1783; A1810. In a provision entitled "Other Organizational Changes," however, the Verizon Policy provides that "**Organization**" does not include ***former*** Subsidiaries. In particular, a Subsidiary "ceases to be an **Organization** when [Verizon] no longer maintains **Management Control** of [it]." A1791. In general, that provision benefitted Verizon, as it ensured that Verizon's current D&O insurance would not be eroded by Claims made against Verizon's former Subsidiaries.

Here, Verizon had Management Control over Spinco until March 31, 2008. During the Spinoff, however, Verizon lost Management Control when it distributed Spinco's shares to Verizon's own stockholders. Verizon's loss of Management Control then was reinforced when Spinco merged into FairPoint—an independent company that is not an Organization under the Verizon Policy—and ceased to exist. Because Verizon lost Management Control over Spinco on March 31, 2008, Spinco "cease[d] to be an **Organization**," A1791, at that time. Spinco therefore was not an

Organization when the Trust Action was brought three and a half years later in October 2011.

In concluding that the Trust Action was "brought derivatively on the behalf of an **Organization**" under the Verizon Policy, the Superior Court never squarely addressed the Other Organizational Changes provision. Instead, the court offered rationales that failed to interpret the policy "as a whole" and impermissibly rendered critical policy language "illusory or meaningless." *Murdock*, 248 A.3d at 905 (citation omitted).

The Superior Court noted, for example, that the Subsidiary definition "include[s] entities over which Verizon has Management Control 'on or before … the Policy Period,'" and "Verizon owned 100% of Spinco 'before' the Policy Period." Ex. B, at 19 (quoting A1810); *see* Ex. C, at 28 (same). But that ignores the Other Organizational Changes provision, which provides that a Subsidiary "ceases to be an **Organization** when [Verizon] no longer maintains **Management Control** of [it]." A1791.

The court also relied on the Excess Endorsement to the Verizon Policy, improperly transforming it into an expansive grant of Spinoff-related coverage. The court focused on that Endorsement's definition of the term "**Deal**," which provides that "'**Deal**' means the merger of [FairPoint] with [Spinco], currently a subsidiary of [Verizon], on March 31, 2008 while **Spinco** holds specified assets and liabilities

that are used in **Verizon**'s local exchange business and related activities in Maine, New Hampshire and Vermont." A1761. In the court's view, that definition "expressly recognizes Spinco as a subsidiary of Verizon at the time of the Deal." Ex. B, at 19 (citing Ex. C, at 28). That characterization is misleading. The definition recognizes Spinco as being a Verizon subsidiary on the date of the Spinoff, but ***only*** "while **Spinco** holds specified assets and liabilities"—i.e., before the Spinoff closed. After the Spinoff closed, Spinco no longer held ***any*** assets or liabilities; it no longer existed.

The Superior Court also reasoned that the Excess Endorsement "provide[s] coverage for 'a Claim involving acts, errors or omissions [in connection] with or relating to the Deal,'" from which the court inferred that "the parties intended this endorsement to expand coverage to liabilities incurred in the [Spinoff] to a maximum extent." Ex. B, at 19 (quoting Excess Endorsement); *see* Ex. C, at 28-29 (same). In fact, the Excess Endorsement does nothing of the sort. The Endorsement states: "In the event of a **Claim** involving acts, errors or omissions in connection with or relating to the **Deal**, coverage ***as is afforded under this policy*** shall be specifically excess of [the Transaction Tower]." A1845 (emphasis added). While that language recognizes the possibility of Spinoff-related Claims, all such Claims are ***not*** automatically covered. To the contrary, the language confirms that the only Spinoff-related coverage the Verizon Policy affords is "coverage ***as is afforded under this***

policy"—i.e., coverage that is already available under the policy's other terms and conditions. In other words, whatever Spinoff-related coverage the rest of the Verizon Policy affords, if any, that coverage is excess of the Transaction Tower.

Other language in the Excess Endorsement reinforces that it does not alter the Verizon Policy's scope of coverage. The Endorsement provides that "[c]overage under this policy shall be subject to all of its terms, conditions, retentions, exclusions and other limitations." A1845. The Endorsement further provides that the ***only*** change it effects is to insert language into the "Other Insurance and Indemnification" section of the policy, and "ALL OTHER TERMS, CONDITIONS AND EXCLUSIONS REMAIN UNCHANGED." A1845.

The Superior Court also reasoned that "Verizon undisputedly controlled Spinco until the Transaction and all alleged Wrongful Acts took place on or before the Transaction." Ex. B, at 20. That, too, is irrelevant. Regardless of when Verizon's alleged Wrongful Acts took place, Spinco "cease[d] to be an **Organization**" in 2008, A1791, and therefore was not an Organization when the Trust Action was "brought" in 2011.

Finally, the Superior Court cited evidence purportedly showing that Verizon had "a reasonable expectation of coverage for a lawsuit like the [Trust] Action." Ex. B, at 20 (citation omitted). In particular, the court referenced deposition testimony about the meaning of the term "**Subsidiary**" from Verizon's corporate

representative. *See id.* Under longstanding interpretive principles, however, "the reasonable expectation doctrine" "applies only after a determination that an insurance contract is ambiguous." *Stoms v. Federated Serv. Ins. Co.*, 125 A.3d 1102, 1108 (Del. 2015) (quotation marks omitted). Here, the Superior Court never determined that any term in the Verizon Policy is ambiguous. To the contrary, the court itself described the policy language as "unambiguous." Ex. C, at 23.

In *IDT Corp. v. U.S. Specialty Insurance Co.*, 2019 WL 413692 (Del. Super.), the Superior Court rejected an argument similar to Verizon's argument here. The D&O policy in *IDT Corp.* provided that "[a]n entity ceases to be a **Subsidiary** when [IDT] ceases to own more than 50% of its issued and outstanding securities representing the right to vote for the election of such entity's directors or managers." *Id.* at *11 (quoting policy language). "IDT d[idn]'t deny that it ceased to hold 'more than 50% of the voting rights' of [the relevant entity] after [a] Spinoff," but it argued that "a former subsidiary of IDT is within the meaning of 'Subsidiary' … so long as the former subsidiary's role is purportedly pivotal to the Underlying Complaint." *Id.* at *12. The court rejected that argument, explaining that it "c[ould]n't buy into IDT's attempted rewrite of the policy's terms." *Id.* The "policy language," the court explained, "provides that an entity qualifies as a Subsidiary under the policy if IDT owns more than 50% of its voting rights." *Id.* "The 'Subsidiary' definition in no

way … allows a former subsidiary to continue to constitute a Subsidiary under any other circumstances." *Id.*

The same reasoning applies here. The Other Organizational Changes provision states that a Subsidiary "ceases to be an **Organization** when [Verizon] no longer maintains **Management Control** of [it]." A1791. Spinco thus ceased to be an Organization on March 31, 2008, and was not an Organization when the Trust Action was brought in October 2011. Accordingly, even if the Trust Action somehow were deemed "brought derivatively on the behalf of [Spinco]," it was not "brought derivatively on the behalf of an **Organization**." This Court should reject Verizon's "attempted rewrite of the policy's terms." *IDT Corp.*, 2019 WL 413692, at *12.

3. <u>The Trust Action Was Not "Brought … by a Security Holder of [Spinco]"</u>

Even if the Trust Action were deemed "brought derivatively on the behalf of [Spinco]" and Spinco were deemed an "**Organization**" in 2011, the Trust Action still was not a Securities Claim under the Verizon Policy because it was not "brought … by a security holder of [Spinco]." Verizon's theory is that the Trust effectively held the Notes, and the Notes were securities of Spinco. But the Notes were not securities of ***Spinco***. They were securities of ***FairPoint***.

Indeed, Verizon is judicially estopped from arguing that the Trust Action was "brought … by a security holder of [Spinco]." The doctrine of judicial estoppel

"protect[s] the integrity of … judicial proceedings" by "preclud[ing] a party from asserting a position inconsistent with a position previously taken in the same or earlier legal proceeding." *Motorola Inc. v. Amkor Tech., Inc.*, 958 A.2d 852, 859 (Del. 2008). As relevant here, judicial estoppel has two requirements—(1) "the litigant's [position] contradicts another position that the litigant previously took" and (2) "the [c]ourt was successfully induced to adopt [that position] in a judicial ruling." *Id.* at 859-60.

Both of those requirements are met here. First, in its initial motion for partial summary judgment under the Transaction Policy, Verizon argued that the Trust Action was "brought by a security holder of [FairPoint]." In Verizon's view, because the Trust was suing on behalf of the Noteholders, and the Noteholders were security holders of FairPoint, the Trust was a security holder of FairPoint. *See* A209. Second, the Superior Court adopted Verizon's argument. The court's February 2021 opinion has a three-page section captioned, "The Trustee was a 'Security Holder' of FairPoint." Ex. C, at 18.

Verizon's successful argument below that the Trust Action was "brought … by a security holder of [FairPoint]" is inconsistent with any argument here that the Trust Action was "brought … by a security holder of [Spinco]." The phrase "security holder of" cannot allow the Trust or the Noteholders to be security holders

of ***both*** FairPoint ***and*** Spinco simultaneously. At the relevant time, the Notes were either securities of FairPoint or of Spinco. Verizon cannot have it both ways.

Regardless, the Notes were not securities of Spinco on the merits. After the Spinoff closed, the only obligor on the Notes was FairPoint. The original Indenture provided that, upon Spinco's merger into FairPoint, FairPoint would "succeed to[] and be substituted for" Spinco as "the Issuer." A1016. Minutes later, Spinco in fact merged into FairPoint, with the merger agreement providing that "the separate existence of Spinco shall cease," that FairPoint "shall … be subject to all the obligations of Spinco," and that "all the debts, liabilities, duties and obligations of … Spinco shall become the debts, liabilities, duties and obligations of [FairPoint]." A558. FairPoint also signed a Supplemental Indenture making FairPoint solely responsible for all payments under the Notes. A1071-87. A party cannot possibly be a "security holder of" a nonexistent entity that has no obligations for the relevant security.

Everyone involved understood that, after the Spinoff, the Noteholders were creditors of FairPoint, not Spinco. In the Spinoff, "everyone who participated in the [Spinoff] understood that FairPoint—and not Spinco—… would be responsible to repay the … Notes," and "regulators and potential investors all evaluated the financial wherewithal of FairPoint—and not Spinco." A464. Similarly, in FairPoint's bankruptcy, the Noteholders filed proofs of claim because they were

creditors of the debtor, FairPoint—not Spinco, which was not a debtor in the bankruptcy because it did not exist. When the FairPoint action was brought in 2011, the Noteholders were security holders only of FairPoint.

The Superior Court rejected the Insurers' arguments without addressing their substance. In ruling on the parties' second round of cross-motions, the court reasoned that the Insurers were "attempting to revive an argument the [c]ourt rejected in its previous decision—that 'only a Securities Claim brought by a true security holder qualifies for coverage.'" Ex. B, at 16 (quoting Ex. C, at 19). That is mistaken. In the first round of cross-motions, the Insurers explained that the Trust Action was not a Securities Claim because it was brought by the Trust, which was not a "security holder of" FairPoint ***or*** Spinco because the Trust did not hold any securities at all. *See supra*, § I.C.2. In the second round of cross-motions, the Insurers explained that, even if the Trust were a "security holder of [FairPoint]" under the Transaction Policy, it was not a "security holder of [Spinco]" under the Verizon Policy because the Notes were securities of FairPoint, not Spinco. These are independent arguments, and the Superior Court erred in conflating them.

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The Superior Court's decisions were mistaken on numerous levels. For all the foregoing reasons, the Trust Action was not "brought derivatively on the behalf of an **Organization** by a security holder of such **Organization**" under the

unambiguous terms of Transaction and Verizon Policies. The Trust Action therefore was not a Securities Claim, and Verizon's defense costs and settlement payments are not covered.

CONCLUSION

The judgment of the Superior Court should be reversed.

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Aaron M. Nelson, Esquire, hereby certifies that, on March 3, 2023, the foregoing Corrected Joint Appellants' Opening Brief was served electronically upon the following:

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