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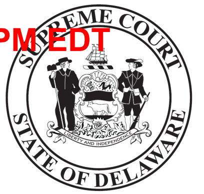

IN THE SUPREME COURT OF THE STATE OF DELAWARE

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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TABLE OF CONTENTS

INTRODUCTION 1

ARGUMENT 4

I. THE TRUST ACTION WAS NOT A SECURITIES CLAIM UNDER THE TRANSACTION OR VERIZON POLICIES 4

A. The Trust Action Was Not “Brought Derivatively on the Behalf of an Organization” 4

1. The Trust Action Was Not a Derivative Action as Understood in Corporate and Securities Law 4

a. The Securities Claim Definitions Track the Corporate- and Securities-Law Concept of a Derivative Action 4

b. The Trust Action Was Not a Derivative Action 9

2. The Trust Action Was Not a Derivative Action as Understood in Bankruptcy Law 15

B. The Trust Action Was Not “Brought … by a Security Holder” 19

II. AT A MINIMUM, THE TRUST ACTION WAS NOT A SECURITIES CLAIM UNDER THE VERIZON POLICY 22

A. The Trust Action Was Not “Brought Derivatively on the Behalf of [Spinco]” 22

B. Spinco Was Not an “Organization” When the Trust Action Was “Brought” 25

C. The Trust Action Was Not “Brought … by a Security Holder of [Spinco]” 31

CONCLUSION 33

TABLE OF AUTHORITIES

Cases

Allied Cap. Corp. v. GC-Sun Holdings, L.P.,
910 A.2d 1020 (Del. Ch. 2006)....................3, 23

Chi. Bridge & Iron Co. N.V. v. Westinghouse Elec. Co.,
166 A.3d 912 (Del. 2017)....................5

Cirka v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.,
2004 WL 1813283 (Del. Ch.)....................2, 18

Citigroup Inc. v. AHW Inv. P'ship,
140 A.3d 1125 (Del. 2016)....................*passim*

In re Cybergenics Corp.,
226 F.3d 237 (3d Cir. 2000)....................*passim*

In re Edwards,
2003 WL 22110778 (Bankr. E.D. Pa.)....................17

In re EPD Inv. Co.,
821 F.3d 1146 (9th Cir. 2016);....................10-11

IDT Corp. v. U.S. Specialty Ins. Co.,
2019 WL 413692 (Del. Super.)....................27

Lenois v. Sommers as Tr. for Erin Energy Corp.,
268 A.3d 220 (Del. 2021)....................17

Lewis v. Anderson,
477 A.2d 1040 (Del. 1984)....................24

MicroStrategy Inc. v. Acacia Rsch. Corp.,
2010 WL 5550455 (Del. Ch.)....................9

N. Am. Cath. Educ. Programming Found., Inc. v. Gheewalla,
930 A.2d 92 (Del. 2007)....................9

O'Brien v. Progressive N. Ins. Co.,
785 A.2d 281 (Del. 2001)....................7, 29

In re Patel,
2012 WL 2514891 (Bankr. D.N.M.)....................9

Premcor Ref. Grp., Inc. v. Matrix Serv. Indus. Contractors, Inc.,
2013 WL 6113606 (Del. Super.) 31

Prod. Res. Grp., L.L.C. v. NCT Grp., Inc.,
863 A.2d 772 (Del. Ch. 2004) 10

Sehoy Energy LP v. Haven Real Est. Grp., LLC,
2017 WL 1380619 (Del. Ch.). 13-14

Shiftan v. Morgan Joseph Holdings, Inc.,
57 A.3d 928 (Del. Ch. 2012) 29-30

Stillwater Mining Co. v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.,
289 A.3d 1274 (Del. 2023) 7

Stoms v. Federated Serv. Ins. Co.,
125 A.3d 1102 (Del. 2015) 29

Tooley v. Donaldson, Lufkin & Jenrette, Inc.,
845 A.2d 1031 (Del. 2004) 6, 7, 14

In re USA Gymnastics,
624 B.R. 443 (Bankr. S.D. Ind. 2021) 19

In re Verizon Insurance Coverage Appeal ("Idearc")
222 A.3d 566 (Del. 2019) 5, 6, 8, 28, 29

In re Wilton Armetale,
968 F.3d 273 (3d. Cir. 2020) 13, 16

Statutes

8 *Del. C.* § 259(a) 23

11 U.S.C. § 541(a)(1) 12

11 U.S.C. §§ 541(a)(3) 12

11 U.S.C. §§ 544(b) 12

11 U.S.C. § 550(a) 12, 15

N.C. Gen. Stat. § 39-23.4(c) 10

Rules

Fed. R. Bankr. P. 7023.1 15

Federal Rule of Civil Procedure 23.1 15

INTRODUCTION

Verizon is not entitled to coverage for its defense costs and settlement payments because the Trust Action was not a Securities Claim under the Transaction or Verizon Policies.[1] Under both policies, the Trust Action was not "brought derivatively on the behalf of an **Organization**" as understood in corporate and securities law, or even as understood in bankruptcy law. The Trust Action also was not "brought … by a security holder"—it was brought by the Trust, which held no securities. Furthermore, under the Verizon Policy, the Trust Action was not a Securities Claim for three additional reasons: (1) the 2011 Trust Action was not "brought derivatively on the behalf of [Spinco]," which dissolved in the 2008 Spinoff; (2) Spinco was not an "**Organization**" when the 2011 Trust Action was "brought"; and (3) the Trust Action was not "brought … by a security holder of [Spinco]" because the Notes were securities of FairPoint, not Spinco.

Verizon's responses fail on numerous grounds, but three errors permeate its arguments. First, Verizon argues that the Trust Action was a Securities Claim ***solely due to FairPoint's bankruptcy***. Although at times it suggests otherwise, Verizon ultimately concedes that, outside bankruptcy, fraudulent-transfer actions are direct, not derivative. A bankruptcy filing, however, cannot convert causes of action from

[1] Capitalized terms have the same meaning as in the Insurers' Corrected Opening Brief ("Br.").

direct to derivative. Verizon also argues that the Trust Action was brought "by a security holder" solely due to FairPoint's bankruptcy. Accordingly, while Verizon repeatedly cites the policies' Bankruptcy Provision and accuses the Insurers of improperly exploiting FairPoint's bankruptcy, it is actually Verizon that seeks to improperly use the bankruptcy to manufacture coverage not afforded by the policy language.

Second, Verizon mischaracterizes fraudulent-transfer actions. Verizon repeatedly asserts that fraudulent-transfer causes of action belong to the debtor and seek recovery on the debtor's behalf. That is wrong. Fraudulent-transfer actions are disputes between transferees (here, Verizon) and creditors (here, the Noteholders). The debtor's actions may be relevant, but the debtor—which made the challenged transfer—generally cannot recover. In the bankruptcy context, debtors-in-possession and their successors may bring fraudulent-transfer actions on behalf of the estate for the benefit of creditors, but that authority is a "legal fiction … that enables a debtor in possession to bring certain causes of action that actually belong to its creditors." *In re Cybergenics Corp.*, 226 F.3d 237, 241 (3d Cir. 2000). Fraudulent-transfer actions in bankruptcy thus are brought "on behalf of the [e]state only," "not … the debtor in possession." *Cirka v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, 2004 WL 1813283, at *1, *9 (Del. Ch.).

Third, in its arguments under the Verizon Policy, Verizon disregards the separate existences of Spinco and FairPoint. Even though the Spinco-FairPoint merger agreement provides that "the separate existence of Spinco shall cease," Verizon asserts that it is "incorrect" to state that Spinco "ceased to exist." Verizon's Corrected Answering Brief ("Opp."), at 9 n.4 (cleaned up). In Verizon's view, Spinco lived on post-merger as a nebulous "Spinco/FairPoint Entity." That is not just wrong, but antithetical to basic principles of Delaware law. "[O]ur corporation law is largely built on the idea that the separate legal existence of corporate entities should be respected …." *Allied Cap. Corp. v. GC-Sun Holdings, L.P.*, 910 A.2d 1020, 1038 (Del. Ch. 2006).

For all these reasons, the Trust Action was not "brought derivatively on the behalf of an **Organization** by a security holder of such **Organization**" under the Transaction or Verizon Policies. This Court should reverse.

ARGUMENT

I. THE TRUST ACTION WAS NOT A SECURITIES CLAIM UNDER THE TRANSACTION OR VERIZON POLICIES

The Trust Action was not a Securities Claim under the Transaction or Verizon Policies for two basic reasons—it was not "brought derivatively on the behalf of an **Organization**," and it was not "brought … by a security holder." If the Court rejects Verizon's arguments on either issue, the Insurers prevail. In fact, Verizon's arguments fail on both fronts.

A. The Trust Action Was Not "Brought Derivatively on the Behalf of an Organization"

The Trust Action was not a Securities Claim because it was not "brought derivatively on the behalf of an **Organization**" as understood in corporate and securities law. Contrary to Verizon's assertions, the Securities Claim definitions do not incorporate a special bankruptcy-based meaning, and even if they did, the Trust Action ***still*** was not a Securities Claim.

1. The Trust Action Was Not a Derivative Action as Understood in Corporate and Securities Law

a. The Securities Claim Definitions Track the Corporate- and Securities-Law Concept of a Derivative Action

The Transaction and Verizon Policies define a Securities Claim as a Claim "brought derivatively on the behalf of an **Organization** by a security holder of such **Organization**." A1706; 1783. Verizon does not dispute that that language naturally

includes the well-established concept of a derivative action as understood in the context of corporate and securities law. *See* Br. 2-3, 25-28; Opp. 27-28. The Securities Claim definitions thus undisputedly encompass lawsuits brought by a security holder to enforce a corporate right that an Organization is unwilling or unable to enforce itself.

Rather than disputing that the Securities Claim definitions encompass derivative actions as understood in corporate and securities law, Verizon argues that the definitions ***also*** encompass a very different category of lawsuits—fraudulent-transfer actions included in an Organization's bankruptcy estate. Opp. 27-30. Verizon thus attempts to engraft a special bankruptcy-based meaning onto the Securities Claim definitions solely for bankruptcy-related Claims. That interpretation contradicts the policy language in multiple ways.

To begin with, Verizon ignores that contract language must be "[v]iewed in proper context." *Chi. Bridge & Iron Co. N.V. v. Westinghouse Elec. Co.*, 166 A.3d 912, 916 (Del. 2017); *see* Br. 25-26, 34-35. As in *Idearc*, because "the words used in the definition[s] mirror those in a specific area of the law recognized as securities regulation," this Court must "start with a basic understanding … that the definition of a Securities Claim is aimed at a particular area of the law, securities law." *Idearc*, 222 A.3d 566, 573-74 (Del. 2019). Verizon attempts to distinguish *Idearc* on the ground that it involved the "regulating securities" part of the Securities Claim

definition, not the "brought derivatively" part at issue here, *see* Opp. 28-29, but that misunderstands *Idearc*'s analysis. As this Court explained, "the definition of a Securities Claim"—the ***entire*** definition—"is aimed at … securities law." 222 A.3d at 574. Here, the Securities Claim definitions in both policies are one sentence long and throughout include terms commonly employed in securities law. Indeed, the definitions' purpose is to define the term "***Securities*** Claim." The two parts of the definitions are set forth side-by-side, and even the part at issue here includes the term "security holder," thereby referring to "securit[ies]" directly. A1706; 1783.

Verizon disputes none of this. To the contrary, Verizon concedes that *Idearc* sets forth "interpretative guidance" that is relevant here. Opp. 28-29 (citation omitted). Verizon even observes that the Superior Court "[u]s[ed] the securities law context" in "determin[ing] that a Spinco Note is a 'security.'" *Id.* at 28 (citation omitted). But Verizon offers no reason this Court should ignore that same "securities law context" in construing the phrase "brought derivatively on the behalf of an **Organization**" within the same Securities Claim definitions.

Verizon also ignores the implication of its position, which is that the policy language's meaning would change depending on the circumstances of the Claim at issue. *See* Br. 36. If a Claim arises in the corporate- and securities-law context, Verizon concedes that "brought derivatively on the behalf of an **Organization**" refers to derivative actions as described in cases like *Citigroup* and *Tooley*. *See*

Opp. 27-28. But if an Organization files for bankruptcy, Verizon contends that the same phrase changes meaning to encompass all causes of action that "attached before the bankruptcy was filed and were general to the estate," ***regardless*** of whether they are direct or derivative under *Citigroup* and *Tooley*. Opp. 25 (quotation marks omitted). The policy language, however, can have only "one meaning." *O'Brien v. Progressive N. Ins. Co.*, 785 A.2d 281, 291 (Del. 2001).

Verizon does not cite any case that has interpreted the same policy language to have different meanings contingent on a Claim's specific circumstances. In the choice-of-law context, this Court has rejected interpreting policies under a "claim-by-claim review," as that would "frustrate[] the intent of comprehensive insurance programs to have a single interpretive approach utilizing a single body of law." *Stillwater Mining Co. v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, 289 A.3d 1274, 1285 (Del. 2023) (quotation marks omitted). Even the Superior Court recognized that it would be untenable for the meaning of "derivatively on the behalf of an **Organization**" to be "dependent on whether a Claim is brought outside or inside bankruptcy." Ex. C, at 23. Yet that is precisely what Verizon advocates.

Verizon mistakenly asserts that the Insurers' interpretation would limit the Securities Claim definitions to "shareholder derivative suits," even though the policy language "uses the term 'security holder,' not 'shareholder.'" Opp. 27. That is incorrect. As the Insurers explained, the Securities Claim definitions encompass

derivative actions brought by stockholders ***or*** other security holders, such as LLC members, limited partners, or creditors of corporations that are insolvent. *See* Br. 27. Indeed, Verizon acknowledges that derivative actions as understood in corporate and securities law "can be brought by other security holders" beyond stockholders. Opp. 27 (quotation marks omitted).

Verizon also notes that the Transaction and Verizon Policies contemplate "coverage in both bankruptcy and non-bankruptcy contexts." Opp. 28. But that is irrelevant. Just because the policies cover certain Claims made after an Organization's bankruptcy does not mean that the phrase "brought derivatively on the behalf of an **Organization**" ***changes meaning*** depending on whether a Claim is asserted inside or outside bankruptcy. It certainly does not mean that ***all*** Claims included in an Organization's bankruptcy estate automatically are Securities Claims.

Indeed, the fact that the policies contain ***other*** provisions that are bankruptcy-specific shows that the parties "knew how" to tie coverage to bankruptcy concepts "when that was intended." *Idearc*, 222 A.3d at 578; *see* Br. 35. Verizon responds that the term "**Organization**"—used in the Securities Claim definitions—includes "(1) the **Named Entity**; (2) each **Subsidiary**, and (3) in the event a bankruptcy proceeding shall be instituted by or against the foregoing entities, the resulting debtor-in-possession." A1706; 1783; *see* Opp. 12. That language just reinforces the Insurers' point. The Organization definition has three prongs, two of which apply

generally, and one that applies "in the event a bankruptcy proceeding shall be instituted." That language "shows the parties knew how" to have a term carry a different meaning in the bankruptcy context "when that was their intent." *MicroStrategy Inc. v. Acacia Rsch. Corp.*, 2010 WL 5550455, at *7 (Del. Ch.). But the parties did ***not*** include such language in the Securities Claim definitions, which accordingly carry the same meaning ***regardless*** of whether an Organization filed for bankruptcy.

Contrary to Verizon's suggestion, the Insurers' interpretation would not "remove all [Securities Claim] coverage for derivative claims in the bankruptcy context." Opp. 30. A breach-of-fiduciary-duty action brought by creditors of an insolvent corporation, for example, could constitute a Claim "brought derivatively on the behalf of an **Organization**" as understood in corporate and securities law. *See N. Am. Cath. Educ. Programming Found., Inc. v. Gheewalla*, 930 A.2d 92, 101 (Del. 2007); Br. 27, 37. Creditors can and do bring such suits in bankruptcy. *E.g.*, *In re Patel*, 2012 WL 2514891, at *1 (Bankr. D.N.M.). The policies' coverage for derivative actions in bankruptcy thus is not illusory; it simply is limited to derivative actions as understood in corporate and securities law.

b. <u>The Trust Action Was Not a Derivative Action</u>

Under this Court's settled tests, the Trust Action was direct, not derivative. First of all, the Trust Action was direct under *Citigroup* because the causes of action

asserted could "not … plausibly belong to" FairPoint or Spinco. *Citigroup Inc. v. AHW Inv. P'ship*, 140 A.3d 1125, 1138 (Del. 2016). Rather, they "belong[ed] to" creditors, enforcing creditors' "own right[s]." *Id.* at 1138, 1140. Verizon does not dispute that "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) (emphasis added), that a fraudulent transfer "may be roughly defined as an infringement of the ***creditor's right*** to realize upon the available assets of his debtor," *Cybergenics*, 226 F.3d at 242 (emphasis added and citation omitted), or that North Carolina's fraudulent-transfer statute authorizes a "***creditor*** [to] mak[e] a claim for relief," N.C. Gen. Stat. § 39-23.4(c) (emphasis added); *see* Br. 29-33. Verizon also does not dispute that the Court of Chancery has repeatedly described fraudulent-transfer actions as direct, not derivative. *See* Br. 29, 37.

Verizon attempts to distinguish these authorities because they supposedly "did not address derivative fraudulent transfer claims that a bankruptcy trustee controls as property of the debtor's estate." Opp. 36 n.23; *see* Opp. 34-35 (similar). But the Trust was not a "bankruptcy trustee" that controlled the debtor's estate; it was a litigation trust with circumscribed powers that was created upon FairPoint's ***exit*** from bankruptcy. *See* Br. 41. Verizon's argument also ignores cases holding that estate representatives bringing fraudulent-transfer actions "stand[] in the shoes of the creditors, not the debtors." *In re EPD Inv. Co.*, 821 F.3d 1146, 1152 (9th Cir.

2016); *see* Br. 30. As Verizon admits, the Trust itself alleged that it was asserting "'creditor' causes of action." Opp. 34; *see* Opp. 7 (similar).

Verizon's bankruptcy-focused argument also runs headlong into *Cybergenics*, which held that the inclusion of fraudulent-transfer causes of action in a bankruptcy estate does ***not*** transfer ownership over those causes of action from creditors to the debtor. In *Cybergenics*, the Third Circuit "consider[ed] whether certain fraudulent transfer claims arising from transfers made by Cybergenics Corporation were included in a sale of all assets of Cybergenics." 226 F.3d at 239. The court answered that question in the negative—even though the causes of action were part of Cybergenics's bankruptcy estate and Cybergenics controlled them as the debtor-in-possession. As the court explained, a debtor-in-possession's powers to pursue a fraudulent-transfer action "neither shift ownership of the fraudulent transfer action to the debtor in possession, nor are themselves a debtor's assets." *Id.* at 244. Fraudulent-transfer causes of action still "actually belong to … creditors." *Id.* at 241.

Verizon attempts to escape *Cybergenics* on the ground that it distinguished between "(1) a security holder's individual claim [and] (2) a derivative claim that becomes property of the estate." Opp. 35; *see* Opp. 3 (similar). That gets *Cybergenics* backwards. The central thrust of *Cybergenics* is that the nature of "a security holder's individual claim" ***does not change*** even if it "becomes property of

the estate." In the court's words: "Does this mean that the … 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.'" *Cybergenics*, 226 F.3d at 242-43.[2]

Verizon also suggests that, because the fraudulent-transfer causes of action were included in FairPoint's estate, they necessarily were "property of the debtor." Opp. 30-31, 36 nn.22-23, 48 n.29. But not all estate property is property of the debtor. As relevant here, a bankruptcy estate includes two categories of interests—(1) "all legal or equitable interests of the debtor in property," 11 U.S.C. § 541(a)(1), and (2) proceeds of fraudulent-transfer actions, *see id.* § 541(a)(3); Br. 16. Enumerating those two categories ***separately*** shows that fraudulent-transfer actions are ***not*** "interests of the debtor in property." *See Cybergenics*, 226 F.3d at 246. The inclusion of fraudulent-transfer actions in the estate thus is a "legal fiction … that enables a debtor in possession to bring certain causes of action ***that actually belong to its creditors***." *Id.* at 241 (emphasis added).

2 In a footnote, Verizon asserts that *Cybergenics* "concerned § 544(b)" and "did not address pre-petition fraudulent conveyance claims ... transferred to the debtor's bankruptcy estate." Opp. 36 n.22. That makes no sense—§ 544(b) empowers a debtor-in-possession to pursue "pre-petition fraudulent conveyance claims" that are included in "the debtor's bankruptcy estate." *See* 11 U.S.C. §§ 541(a)(3), 544(b), 550. The Trust invoked § 544(b) in the Trust Action. *See* A350-56.

While Verizon's arguments about the nature of fraudulent-transfer actions are wrong, they illustrate something important about Verizon's position. In particular, Verizon ultimately argues that the Trust Action was "brought derivatively on the behalf of an **Organization**" ***solely due to FairPoint's bankruptcy***. To be sure, Verizon repeatedly cites the Bankruptcy Provision, and at times it suggests that the relevant causes of action were derivative outside of bankruptcy and remained so inside bankruptcy. Opp. 25, 29-31, 36-37, 42. But when confronted with authorities showing that fraudulent-transfer actions are direct, not derivative, Verizon retreats, arguing that those authorities are inapposite because they did not consider the bankruptcy context. Opp. 35-37 & n.22-23. Furthermore, Verizon does not cite any case outside bankruptcy holding that a fraudulent-transfer cause of action was derivative. Instead, Verizon relies on cases like *In re Wilton Armetale*, 968 F.3d 273 (3d. Cir. 2020), which Verizon acknowledges are limited to "the insolvency and bankruptcy[ ]context." Opp. 26. Verizon thus effectively concedes that—outside bankruptcy—fraudulent-transfer actions are direct.

That concession is fatal to Verizon's position. A bankruptcy filing cannot convert a cause of action from direct to derivative. In Verizon's own words, "[s]imply because the cause of action was transferred to the estate in bankruptcy … does not change the nature of the claim." Opp. 42; *see* Opp. 3-4, 25 (similar). The Court of Chancery likewise has held that causes of action that are direct outside

bankruptcy remain so inside bankruptcy. *See Sehoy Energy LP v. Haven Real Est. Grp., LLC*, 2017 WL 1380619, at *9 (Del. Ch.).

Of equal weight, the Trust Action was direct under *Tooley* because creditors "suffered the alleged harm" and "would receive the benefit of any recovery." *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1033 (Del. 2004). Verizon acknowledges that the Superior Court refused to apply *Tooley*, Opp. 38 n.24, but nevertheless asserts that the Trust Action was derivative under *Tooley* because the "transfers at issue [allegedly] rendered Spinco[and] FairPoint … insolvent" in 2008, Opp. 37-38 (quotation marks omitted). But the Trust did not sue Verizon to redress the harm of rendering Spinco or FairPoint insolvent. Rather, the Trust sued Verizon to redress harm to ***creditors*** due to their inability to "realize upon the available assets of [their] debtor." *Cybergenics*, 226 F.3d at 242 (citation omitted). Far from being victims that suffered cognizable harm from a fraudulent transfer, Spinco and FairPoint were alleged ***perpetrators***, having transferred assets to Verizon that should have been available to creditors. Put another way, the question in the Trust Action was whether Verizon would keep the transferred assets or give some portion to the Noteholders and other Trust beneficiaries. In no circumstance would the assets return to FairPoint (or Spinco).

Furthermore, Verizon concedes that "the proceeds from the [Trust] Action would be directed to the debt security holders and other creditors, not [FairPoint]."

Opp. 38. That should end the matter. While Verizon notes that the Trust sued "for the benefit of the estate," Opp. 38 (quoting 11 U.S.C. § 550(a)), that makes no difference, as creditors are the estate's principal beneficiaries. Debtors-in-possession thus bring fraudulent-transfer actions to "benefit the creditors, not the debtors themselves." *Cybergenics*, 226 F.3d at 244.

Finally, Verizon acknowledges that "the Trust made no attempt to comply with various requirements for derivative actions under … Federal Rule of Civil Procedure 23.1." Opp. 38-39. Verizon asserts that Rule 23.1 "govern[s] derivative actions outside the bankruptcy context, not … in the bankruptcy context," Opp. 39, but in fact it also "applies in adversary proceedings" in bankruptcy, Fed. R. Bankr. P. 7023.1. Regardless, the Trust Action was brought post-confirmation in a non-bankruptcy court. The Trust did not need to comply with Rule 23.1—entitled "Derivative Actions"—because the Trust Action was ***not*** a derivative action. Therefore, it was not a Securities Claim.

2. The Trust Action Was Not a Derivative Action as Understood in Bankruptcy Law

Even if the Securities Claim definitions could be stretched to incorporate a special bankruptcy-based meaning, the Trust Action still was not a Securities Claim, for two independent reasons.

First, the Trust Action was not "brought derivatively" under bankruptcy law. Verizon does not dispute that, in bankruptcy, "derivative standing" refers to the

ability of creditors to pursue avoidance actions in place of the bankruptcy trustee or debtor-in-possession. *See* Br. 37. Verizon also does not dispute that, in bringing the Trust Action, the Trust did not invoke derivative standing or meet the strict requirements for doing so. *See* Br. 38.

Instead, Verizon argues that the Trust Action was "brought derivatively" because the Trust asserted causes of action that, in bankruptcy, "can … only be asserted by the [bankruptcy] trustee" or debtor-in-possession—not by creditors, unless creditors obtain bankruptcy-court permission to invoke derivative standing. Opp. 31; *see* Br. 16-17, 37-38. But the Trust Action was ***not*** brought by creditors invoking derivative standing. It was brought by the Trust, which was granted authority to pursue the litigation by the debtor-in-possession. *See* Br. 17. Even if a hypothetical lawsuit brought by creditors invoking derivative standing could be said to be "brought derivatively," the Trust Action was not.

To be sure, bankruptcy cases sometimes use the word "derivative" to describe causes of action that may be brought only by an estate representative absent derivative standing. Verizon builds its brief around such cases—especially *Wilton*. *E.g.*, Opp. 2; *see* Opp. 32 (citing additional cases). As the Insurers explained, however, *Wilton* simply held that a Chapter 7 trustee had exclusive authority to bring fraudulent-transfer causes of action where the "theory of recovery [wa]s not personal, but derivative of harm to the estate." 968 F.3d at 283; *see* Br. 38-39. That

does not mean that all causes of action asserted by a bankruptcy estate representative are "brought derivatively." By analogy, in corporate and securities law, this Court often uses the word "derivative" to describe causes of action that cannot be asserted by security holders absent derivative standing. *E.g.*, *Citigroup*, 140 A.3d at 1126. That does not mean that causes of action asserted by a corporation itself or its successor are "brought derivatively." Rather, causes of action are "brought derivatively" only if they are brought by security holders invoking derivative standing to sue "on the corporation's behalf." *Id.* at 1139. Here, the Trust Action was brought by the Trust as an authorized representative of the estate, not a creditor invoking derivative standing. The Trust Action accordingly was brought "directly," not derivatively. *Lenois v. Sommers as Tr. for Erin Energy Corp.*, 268 A.3d 220, 236 (Del. 2021); *see* Br. 38-39.

Second, even if the Trust Action were "brought derivatively," it was brought on behalf of the estate, ***not*** "on the behalf of an **Organization**." Verizon does not dispute that the Trust Action was brought on behalf of the estate; it repeatedly argues as much. *E.g.*, Opp. 19, 25. Instead, Verizon asserts that "there is no practical difference between the 'estate' and the 'debtor.'" Opp. 41. The distinction between the estate and the debtor, however, "is a fundamental concept of bankruptcy law." *In re Edwards*, 2003 WL 22110778, at *3 (Bankr. E.D. Pa.). Furthermore, in the context of a D&O insurance coverage dispute, the Court of Chancery has expressly

held that, where an underlying suit is brought by creditors invoking bankruptcy-law derivative standing, that 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). *Cirka* is directly on point, but Verizon never addresses it.

Verizon's assertion that the Trust's complaint "treats 'estates' and 'Debtors' … interchangeably," Opp. 41, fares no better. The Trust's allegations cannot alter fundamental precepts of bankruptcy law. Moreover, even in the allegations Verizon quotes, the complaint mentions "the Debtors" and "their estates" separately, indicating that they are ***not*** interchangeable. *Id.* (quoting A316; 350-51). Verizon also notes that there is a "close connection between the estate and the debtor," Opp. 42, but that just underscores that the debtor and the estate are distinct. A "connection," after all, is a relationship between two ***separate*** things. The policies define a Securities Claim as a Claim "brought derivatively on the behalf of an **Organization**," not a Claim "brought derivatively on the behalf of an entity with a close connection to an **Organization**."

Contrary to Verizon's suggestion, Opp. 42-43, respecting the distinction between the estate and the debtor would not violate the policies' Bankruptcy Provision. That provision has nothing to do with whether a Claim is "brought derivatively on the behalf of an **Organization**." As many states require, the Bankruptcy Provision simply makes clear that, to the extent the policies impose

obligations on the Insurers, those obligations "continue[] even [if]" an Organization "file[s] a bankruptcy case." *In re USA Gymnastics*, 624 B.R. 443, 455 (Bankr. S.D. Ind. 2021); *see* Br. 35-36, 44-46. Here, the policies imposed no obligations on the Insurers in the first place because the Trust Action was not a Securities Claim.

Nor would respecting the distinction between the estate and the debtor "nullify the Insured v. Insured Exclusion," as Verizon suggests. Opp. 43. The Insurers have not invoked that exclusion, making it irrelevant. The bankruptcy exception to that exclusion is even less relevant, as it merely reinstates part of the coverage the exclusion removes. *See* Br. 35-36. Neither the exclusion nor the exception has any bearing on whether a Claim is "brought derivatively on the behalf of an **Organization**" under the Securities Claim definitions. Because the Trust Action was not "brought derivatively on the behalf of an **Organization**" even under bankruptcy principles, it was not a Securities Claim.

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

The Trust Action independently was not a Securities Claim under the Transaction or Verizon Policies because it was not "brought … by a security holder." Verizon does not dispute (1) that the Trust Action was "brought … by" the Trust or (2) that the Trust held no securities. *See* Br. 42-43. Those concessions alone establish that the Trust Action was not a Securities Claim.

Verizon argues that, in addition to being "brought … by" the Trust, the Trust Action ***also*** was "brought … by" the Noteholders because the Trust was standing in the shoes of the Noteholders. In Verizon's view, "[a] claim brought by one 'standing in the shoes of' a debt security holder is equivalent to a claim brought by that debt security holder." Opp. 44. But the cases Verizon cites involve issues of standing, subrogation, and substitution. *See* Opp. 44 (citing cases). No case suggests that any lawsuit was "brought … by" a party other than the named plaintiff.

Verizon also ignores the policy language—specifically, its use of "by" and "on the behalf of." Contrary to Verizon's suggestion, Opp. 36-37, saying that the Trust was "standing in the shoes" of the Noteholders is simply another way of saying that the Trust was suing "on the behalf of" the Noteholders. Indeed, the Trust expressly alleged that it was suing "on behalf of creditors." A313. But the policy language says "***by*** a security holder," not "by ***or on the behalf of*** a security holder." In fact, the phrase immediately preceding "by a security holder" is "***on the behalf of*** an Organization," showing that the parties understood the difference between a Claim brought ***by*** a particular party and a Claim brought ***on the behalf of*** that party. *See* Br. 44. Verizon has no response.

Finally, Verizon again invokes the Bankruptcy Provision and the bankruptcy exception to the insured-v.-insured exclusion. Opp. 45. But those provisions are irrelevant for the reasons explained above. No provision of the policies purports to

convert a lawsuit brought by a litigation trust that holds no securities into a lawsuit brought by a security holder.

II. AT A MINIMUM, THE TRUST ACTION WAS NOT A SECURITIES CLAIM UNDER THE VERIZON POLICY

Under the Verizon Policy, the Trust Action was not a Securities Claim for three additional independent reasons: (1) the Trust Action was not "brought derivatively on the behalf of [Spinco]," (2) Spinco was not an "**Organization**" when the Trust Action was "brought," and (3) the Trust Action was not "brought … by a security holder of [Spinco]."

A. The Trust Action Was Not "Brought Derivatively on the Behalf of [Spinco]"

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 Insurers explained, Spinco ceased to exist as a legal entity when it merged into FairPoint in 2008. Consequently, when the Trust sued Verizon in 2011, the Trust could not have been suing "derivatively on the behalf of [Spinco]" because Spinco did not exist at that time. *See* Br. 48-50.

Remarkably, Verizon contends that "[the] Insurers' assertion that Spinco 'ceased to exist' is entirely incorrect." Opp. 9 n.4. In Verizon's view, "[t]he merger agreement provides that 'Spinco shall be merged with and into [FairPoint]' thus creating the Spinco/FairPoint Entity, and that the '*separate* existence of Spinco shall cease.'" *Id.* (emphasis by Verizon) (quoting A558). Verizon's suggestion that Spinco lived on post-merger as the "Spinco/FairPoint Entity" lacks any basis in fact

or law. There is no such thing as the "Spinco/FairPoint Entity." Northern New England Spinco Inc. ("Spinco") and FairPoint Communications, Inc. ("FairPoint") are the names of distinct legal entities.

The record is crystal clear that, when Spinco and FairPoint merged, FairPoint survived, but Spinco did not. As Verizon acknowledges, the merger agreement provides that "the separate existence of Spinco shall cease." A558. By italicizing "*separate* existence," Opp. 9 n.4, Verizon suggests that a corporation can have an existence other than a "separate existence," but that is incorrect. "Separate existence" is the standard language Delaware law uses to denote a corporation's existence as a legal entity. *See, e.g.*, 8 *Del. C.* § 259(a). Moreover, Delaware state records undisputedly show that Spinco dissolved at 9:01 a.m. on March 31, 2008. A658-61; *see* Br. 9. Even the Superior Court recognized that Spinco "ceased to exist" during the 2008 Spinoff. Ex. C, at 20 n.129. Post-Spinoff, FairPoint held assets and liabilities previously held by Spinco, but Spinco itself did not exist.

Verizon's argument conflicts with fundamental principles of Delaware law. "Our corporation law is largely built on the idea that the separate legal existence of corporate entities should be respected …." *Allied Cap.*, 910 A.2d at 1038. Verizon's contentions accordingly have implications far beyond insurance coverage disputes. This Court cannot endorse Verizon's arguments without destabilizing the very foundation of this state's corporate law.

In the context of the "continuous ownership rule," for example, this Court has long held that where one corporation merges into another, security holders of the non-surviving corporation "lose[] standing to continue a derivative suit." *Lewis v. Anderson*, 477 A.2d 1040, 1049 (Del. 1984). Verizon responds that the continuous ownership rule is inapposite because the Trust had standing "by operation of bankruptcy law." Opp. 48-49. That misses the point. The Insurers are not disputing the Trust's standing to sue. The point is that, if this Court were to hold that the Trust brought the Trust Action "derivatively on the behalf of" an entity that dissolved years earlier, it would throw the continuous ownership rule into doubt. If the Trust could bring a lawsuit derivatively on behalf of a nonexistent entity that dissolved in a merger, what prevents security holders of other non-surviving entities from doing the same thing? Verizon does not explain.

Verizon also asserts that the Trust "said" that it was "acting on behalf of Spinco," Opp. 47, but that too is incorrect. While the Trust argued that "the relevant debtor … [was] *Spinco*," *id.* (emphasis by Verizon) (citation omitted), that simply meant that, in the Trust's view, Spinco's intent mattered, not just FairPoint's. *See* Br. 18-19. Contending that Spinco's intent was relevant does not mean that the Trust was suing "derivatively on [Spinco's] behalf." Similarly irrelevant is the Trust's statement that it had authority to "bring fraudulent transfer claims for pre-merger transfers made by [Spinco]." Opp. 47 (citation omitted). Challenging transactions

in which Spinco participated in 2008 does not mean that the Trust was suing "derivatively on the behalf of [Spinco]" in 2011. The Trust never argued that it was suing "derivatively on the behalf of Spinco"—nor could it have, because ***Spinco did not exist***. For that reason alone, the Trust Action was not a Securities Claim under the Verizon Policy.

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

The Trust Action also was not a Securities Claim because Spinco was not a Verizon "**Organization**" when the Trust Action was "brought." As the Insurers explained, while the term "**Organization**" includes "each **Subsidiary**" of Verizon, the Other Organizational Changes provision states that a Subsidiary "ceases to be an **Organization** when [Verizon] no longer maintains **Management Control** of [it]." A1783, 1791. Verizon does not dispute that it lost Management Control over Spinco in 2008. *See* Br. 51-52. Accordingly, the Trust Action was not "brought derivatively on the behalf of an **Organization**" in 2011.

Verizon responds that the Insurers "improperly insert[] a requirement that an entity qualifying as a Subsidiary must remain a Subsidiary when the underlying claim is made." Opp. 49. But that requirement is in the plain policy language. If a lawsuit is brought derivatively on behalf of an entity that is ***not*** an Organization at that time, it is not "brought derivatively on the behalf of an **Organization**."

Verizon's assertion that Spinco "meets the definition of 'Subsidiary,'" *id.*, also misses the mark. Again, the Other Organizational Changes provision states that a Subsidiary "ceases to be an **Organization** when [Verizon] no longer maintains **Management Control** of [it]." A1783, 1791. Verizon thus admits that "a Verizon subsidiary will cease to be covered under the [Verizon] Policies after Verizon no longer has management control over the entity." Opp. 14 n.6; *see* Opp. 6 (similar).

Verizon also asserts that the Verizon Policy covers "claims of Wrongful Acts that allegedly happened *while* an entity existed as Verizon's Subsidiary." Opp. 49 (emphasis original). That argument rests on a separate sentence of the Other Organizational Changes provision, which the Superior Court never mentioned. In relevant part, that sentence provides:

> In all events, coverage as is afforded under this policy with respect to a **Claim** made against any **Organization** … shall only apply for **Wrongful Acts** committed or allegedly committed after the effective time such **Organization** became an **Organization** …, and prior to the effective time that such **Organization** ceases to be an **Organization** ….

A1791 (underlined emphasis added). Verizon's brief misleadingly uses ellipses to omit the underlined portion of that sentence. Opp. 50-51. But as those underlined words make clear, the sentence applies only "with respect to a **Claim** made ***against*** any **Organization**" where "***such*** **Organization**" qualifies as an Organization at one time but not another. Here, the relevant Organization is Spinco. But the Trust Action was not a Claim made "against" Spinco; it was a Claim made against

Verizon. Indeed, Verizon's coverage theory rests on the notion that the Trust Action was brought ***on behalf of*** Spinco—on the plaintiff's side of the "v." in the caption, not the defendants' side. The first sentence of the Other Organizational Changes provision thus does not apply. "This Court can't buy into [Verizon]'s attempted rewrite of the policy's terms." *IDT Corp. v. U.S. Specialty Ins. Co.*, 2019 WL 413692, at *12 (Del. Super.).

Verizon's reliance on the Excess Endorsement is similarly misleading. Verizon asserts that the Excess Endorsement "identified Spinco as a 'current' subsidiary of Verizon," Opp. 50, omitting that the Endorsement actually describes Spinco as "currently a subsidiary … ***on March 31, 2008***," and even then, only "while **Spinco** holds specified assets and liabilities"—*i.e.*, before the Spinoff closed. A1761 (emphasis added); *see* Br. 52-53. Verizon also asserts that the Excess Endorsement "extended coverage for any 'acts, errors or omissions in connection with or relating to the Deal,'" but in fact, it does no such thing. 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 by this policy*** shall be specifically excess of [the Transaction Tower]." A1845 (emphasis added). That language simply takes whatever Spinoff-related coverage is afforded by the ***rest*** of the Verizon Policy—whether for Organizations ***or*** for individual directors and officers—and makes it excess of the Transaction Policy. The Excess Endorsement

thus does not create new coverage or alter the Securities Claim definition; it simply specifies, for Claims covered under both Towers, which Tower is primary (the Transaction Tower) and which Tower is excess (the Verizon Tower). *See* Br. 53-54. Verizon again has no response.

In another argument the Superior Court never adopted, Verizon relies on the Runoff Endorsement. *See* Opp. 50. But the Runoff Endorsement appears ***only*** in the Transaction Policy. Verizon never explains how it is relevant to the interpretation of the Verizon Policy. While the Runoff Endorsement in the Transaction Policy references Spinco, *see* Opp. 50, that says nothing about whether Spinco was an Organization under the Verizon Policy in 2011.

Verizon also invokes Endorsement 15 of the Verizon Policy, which provides that "the Definition of Subsidiary in this policy shall not include (1) Verizon Directories Disposition Corp. aka Idearc Inc.; and (2) Verizon Information Services aka Idearc Information Services Inc." A1821; *see* Opp. 51. The Superior Court never mentioned this endorsement, but Verizon asserts that it "shows that Insurers knew how to exclude a spun-off entity from the 'Subsidiary' definition when it was their intent." Opp. 51. The fact that "**Subsidiary**" does ***not*** include two Idearc entities, however, does not demonstrate *ipso facto* that it ***does*** include Spinco. Furthermore, contrary to Verizon's suggestion, Endorsement 15 is not duplicative of the Other Organizational Changes provision—Endorsement 15 provides that the

Idearc entities do not qualify as Subsidiaries at ***any*** time, whereas the Other Organizational Changes provision established only that they ceased to be Organizations after Verizon lost Management Control.

Verizon also ignores that there were good reasons to clarify the status of the Idearc entities. First and foremost, the Idearc entities continued to exist post-spinoff. *See* A1821; *Idearc*, 222 A.3d at 569. Spinco, by contrast, ceased to exist when it merged into FairPoint. Endorsement 15's discussion of the Idearc entities thus sheds no light on Spinco.

Finally, Verizon cites extrinsic evidence purportedly showing "Verizon's reasonable expectation that Spinco would be treated as a Subsidiary for any claims alleging Wrongful Acts relating to the [Spinoff]." Opp. 53. "[T]he reasonable expectation doctrine," however, "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); *see* Br. 55. This Court has warned against finding insurance policies ambiguous, *see O'Brien*, 785 A.2d at 288, and has consistently found D&O Securities Claim definitions to be unambiguous, *e.g.*, *Idearc*, 222 A.3d at 572.

Regardless, Verizon's reasonable-expectations argument fails on its own terms. Verizon cites no contemporaneous evidence from before the Verizon Policy incepted, instead relying on deposition testimony from its corporate representative

and broker voicing their "subjective, unexpressed views" during this litigation. *Shiftan v. Morgan Joseph Holdings, Inc.*, 57 A.3d 928, 935 (Del. Ch. 2012). Even that testimony concerns a predecessor policy, not the Verizon Policy, and it indicates that Verizon's coverage expectations were generalized at best. The testimony does not demonstrate that Verizon even contemplated the possibility of a fraudulent-transfer action like the Trust Action, much less expected that it would be covered as a Securities Claim. *See* B1093-95, B1003.[3]

Verizon also fails to mention its own contrary statements about Spinco's insurance coverage at the time of the Spinoff. In the Verizon-Spinco distribution agreement, Verizon agreed that Spinco "will have no rights with respect to" Verizon's then-existing insurance policies—including the relevant predecessor to the Verizon Policy. B231-32. Verizon also told its stockholders that, "[f]ollowing the spin-off, FairPoint"—not Verizon—"will be responsible for obtaining and maintaining its own insurance coverage with respect to the Spinco business." AR124. Verizon's arguments thus contradict its own contemporaneous statements.

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[3] Verizon also cites testimony from National Union's corporate representative, Opp. 53, but his views (1) were "general" in nature, (2) were never discussed during the negotiation of the Verizon Policy, and (3) concerned policy provisions governing coverage for individual directors and officers, not Organizations. B1120-21. That testimony provides no insight into Verizon's purported expectations for organizational coverage when the Verizon Policy incepted.

C. The Trust Action Was Not "Brought … by a Security Holder of [Spinco]"

Finally, the Trust Action was not a Securities Claim because it was not "brought … by a security holder of [Spinco]." As the Insurers explained, Spinco was the obligor on the Notes for only a matter of minutes, and all Spinoff participants "understood that FairPoint—and not Spinco—… would be responsible to repay the … Notes." A464; *see* Br. 10, 58.

Verizon objects to the Insurers' citations to Verizon's proposed factual findings in the Trust Action, Opp. 17, but "[w]hen reviewing a duty to indemnify under a settlement, the Court must look at the facts as established … before the settlement," *Premcor Ref. Grp., Inc. v. Matrix Serv. Indus. Contractors, Inc.*, 2013 WL 6113606, at *5 (Del. Super.). Verizon's own proposed findings obviously shed light on what the evidence in the Trust Action established. Moreover, the Trust never disputed that Spinco was an obligor on the Notes only for a brief moment, or that Spinoff participants understood that that would be the case. Instead, the Trust argued that Spinco was "the true 'debtor' for purposes of the asserted fraudulent transfer claims." Opp. 55. As explained, that argument concerned whether Spinco's intent at the time of the Spinoff mattered. It has no bearing on whether the Notes were securities "of [Spinco]" or "of [FairPoint]" after the Spinoff closed.

Verizon also argues that the Notes were securities "of [Spinco]" because they were "issued by Spinco." Opp. 54. But that ignores the original indenture, which

provided that, upon Spinco's merger into FairPoint, FairPoint would "succeed to[] and be substituted for" Spinco as "the Issuer." A1016. A supplemental indenture then confirmed that, post-merger, FairPoint was "the sole obligor on the Notes." A464. Furthermore, the merger agreement provided 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.

Finally, Verizon fails to explain how, having persuaded the Superior Court that the Notes were securities "of [FairPoint]" under the Transaction Policy, it is not judicially estopped from arguing that they were securities "of [Spinco]" under the Verizon Policy. In a footnote, Verizon asserts that it has argued consistently that the Trust was "standing in the shoes of the *Spinco* Noteholders." Opp. 55 n.31. But that is nonresponsive. Verizon successfully argued that the Trust was a "security holder of [FairPoint]," only to turn around and argue that it was a "security holder of [Spinco]." The February 2021 opinion Verizon procured contains an entire section with the heading, "The Trustee was a 'Security Holder' of FairPoint." Ex. C, at 18. Verizon never explains how it can consistently maintain that the Trust was a "security holder of [FairPoint]" ***and*** a "security holder of [Spinco]" simultaneously.

CONCLUSION

The judgment of the Superior Court should be reversed.

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