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IN THE SUPREME COURT OF THE STATE OF DELAWARE

IN RE VERIZON INSURANCE COVERAGE APPEALS	No. 558,2018 No. 561,2018 No. 560,2018 Court Below—Superior Court of the State of Delaware C.A. No. N14C-06-048 WCC (CCLD) **PUBLIC VERSION**

APPELLANT AND CROSS-APPELLEE ZURICH AMERICAN INSURANCE CO.'S REPLY BRIEF ON APPEAL AND ANSWERING BRIEF ON CROSS-APPEAL

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Introduction

Verizon devotes the majority of its Answering Brief to the Securities Claim issue. For the reasons explained in Illinois National Insurance Companyôs Reply Brief, Verizonôs arguments ignore both the plain meaning of the definition of ñSecurities Claimò in the Runoff Policies and the record in this case.[1] Zurich submits this separate brief to (1) respond to Verizonôs arguments regarding the trial courtôs blocking Zurich from litigating conditions to coverage and whether Zurich owes prejudgment interest, and (2) answer Verizonôs cross-appeal on when prejudgment interest began to accrue, assuming it began to accrue at all.

Verizon does not dispute that the Superior Court denied Zurich the ability to litigate whether Verizonôs $49 million in defense expenditures were reasonable and jointly incurred with John Diercksen so as to constitute covered ñLossò under the Runoff Policies. Instead, Verizon seeks to justify the trial courtôs about-face on bifurcation by misstating the law and ignoring the record on appeal. The Superior Court did not merely deny Zurich the opportunity to *conduct discovery* on the scope and nature of Verizonôs defense expenditures and whether Verizon had a covered ñLossò under the Policy, as Verizon asserts; it affirmatively *precluded*

[1] Zurich adopts and incorporates Illinois Nationalôs reply brief as it pertains to the meaning and definition of Securities Claim and why the Runoff Policies do not provide coverage to Verizon on the basis of that definition. Zurich does not incorporate Illinois Nationalôs other arguments, including without limitation its argument that the Superior Court correctly applied Delaware law to the issue of prejudgment interest. *See infra* n.5.

Zurich from litigating at all Verizonôs compliance with these conditions during Phase I of the case. The Superior Courtôs stay and bifurcation order prevented Zurich from developing these defenses, as well as from raising them at the summary judgment stage of Phase I, which the Superior Court strictly limited to one issue alone (an issue that was *not* the nature and scope of tens of millions of claimed defense costs sought by Verizon). By abruptly switching course and ending the case after its decision on that one issue, the Superior Court denied Zurich its due process right to challenge other coverage conditions at all. In this case, these additional coverage issues affected only Zurich and, if successful even in part, could well result in no exposure to Zurich here.

Verizonôs Answering Brief also ignores the history of the case, in which Zurich repeatedly identified these coverage conditions as outstanding defenses, and both Verizon and the Superior Court acknowledged them. Indeed, Verizon refused to produce discovery critical to assess these conditions expressly on the basis that it was outside the scope of the first phase of the litigation. Verizon cannot credibly argue that Zurichôs request to litigate coverage conditions is not timely after Verizon refused to provide the information necessary for Zurich to fully assess it.

Verizon also defends the Superior Courtôs decision to apply Delaware law and order Zurich to pay prejudgment interest. Verizonôs defense is not principled or credible, because Verizon has changed its position on which stateôs laws apply a

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whopping three times in this litigation. Consistent with two recent decisions of this Court, Delaware's choice of law principles mandate application of New York law to a nationwide insurance program like the Runoff Policies. Under New York law, the exhaustion provisions in the Zurich Policy plainly require that Verizon exhaust the limits of the underlying insurance policies by actual payment of Loss by the insurers before Zurich's policy is triggered.

If, however, this Court rejects all of Zurich's arguments on appeal and holds that Zurich must pay prejudgment interest, the Superior Court correctly determined that interest did not begin to accrue until Verizon demanded payment from Zurich and produced its invoices. Under both the plain language of the Runoff Policy and clearly-established legal principles, an insurer does not owe interest for expenses incurred until the insurer demands payment. Here, Verizon barely and rarely communicated with Zurich, a high layer excess insurer, about its defense of the *U.S. Bank* Action, let alone demanded payment or produced invoices. Accordingly, if this Court affirms the Superior Court's grant of final judgment, the decision on the accrual date of prejudgment interest should be affirmed.

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Answer to Verizon's Summary of Argument on Cross-Appeal

1. Denied. Assuming for purposes of the cross-appeal that the Superior Courtôs order granting Verizon prejudgment interest was not in error, the Superior Court correctly held that prejudgment interest did not begin to accrue until Verizon demanded payment from Zurich, rather than when Verizon purportedly began paying defense expenditures.

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Arguments on Appeal

I. In Arguing That the Superior Court Properly Denied Zurich the Opportunity to Litigate Coverage Conditions, Verizon Misstates Both the Standard of Review and the Trial Court Record

A. The Superior Court's Decision Barring Zurich From Challenging Coverage Conditions Is Reviewed *De Novo*, and in Any Event, the Court's Refusal to Allow ***Any*** Discovery Is an Abuse of Discretion.

Verizon incorrectly asserts that the Superior Courtôs refusal to allow Zurich to litigate the coverage conditions that Zurich raised at the outset of the case is a mere discovery ruling reviewed for abuse of discretion. VZ Br. at 70. To the contrary, the Superior Courtôs refusal to allow any discovery or any argument on coverage conditions that the court ï not Zurich ï deferred has deprived Zurich of its right to challenge Verizonôs compliance with such conditions, and is a denial of Zurichôs due process right to defend itself. Such a determination is reviewed *de novo*. *See, e.g.*, *In re Phila. Stock Exch., Inc.*, 945 A.2d 1123, 1135 (Del. 2008) (ñTo the extent this argument raises a due process question, that is an issue of law which this Court reviews *de novo*.ò); *Delle Donne & Assoc. v. Millar Elev. Serv. Co.*, 840 A.2d 1244, 1251 (Del. 2004) (waiver determination reviewed *de novo*).

Verizon argued before the Superior Court that Zurich waived its right to litigate both (1) the reasonableness of Verizonôs $49 million in defense expenditures and (2) whether those expenditures were ñjointly incurredò with Mr. Diercksen. JA5997-6000. Although the Superior Court expressly rejected

Verizonôs waiver argument, Zur. Br. at Ex. C p. 16-17, it nonetheless refused to allow Zurich and the other insurers the right to challenge coverage conditions, *id.* at 20-21; Zur. Br. at Ex. D; JA6476. While correctly holding that Zurich did not waive its defenses, the courtôs decision to enter final judgment on all issues and defenses ï not a Rule 54(b) judgment ï completely deprived Zurich of its right to litigate expressly preserved defenses to coverage, a due process violation of the right to defend itself. This is legal error, and it is subject to *de novo* review.

Regardless of the standard of review, however, the Superior Courtôs decision to end the case constitutes an unjustifiable abuse of discretion. Verizonôs brief ignores the fact that, at every appropriate stage of the trial court proceeding, Zurich asserted its right to challenge whether Verizon complied with conditions to coverage, and both Verizon and the court repeatedly recognized that right:

- August 27, 2014: Zurich asserted in its Answer to Verizonôs Complaint the conditions and defenses it now seeks to litigate. JA0256-0257.
- October 30, 2014: Zurich reiterated the same coverage conditions in its opposition to Verizonôs first motion for summary judgment. JA1864-1865.
- November 17, 2014: Verizon stated that its initial motion for summary judgment ñdoes not require the Court to determine at this time whether any portion of the fees incurred were unreasonable or unnecessary ï because if they were, then those costs are not ódefense Costs.ôò JA1926.
- December 4, 2014: Verizon reiterated to the court that the amount of covered Defense Costs is ñnot before this Court now.ò JA2251 at 7:13.

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- March 30, 2015: ***Verizon refused to answer discovery requests*** relating to the reasonableness of defense expenditures and whether they were jointly incurred on the grounds that the requests did not relate to whether the *U.S. Bank* Action constituted a Securities Claim. JA5910-5932.

- May 5, 2015: After instructing the parties in its March 20, 2015 to limit the first phase of discovery to the Securities Claim issue,[2] the Court formally bifurcated the case into two phases, with Phase I addressing only the Securities Claim issue, and Phase II addressing ñall remaining issues in the case.ò JA2267-2268.

- September 30, 2016: After oral argument on the Securities Claim issue, Verizon sent Illinois National a draft letter, which acknowledged that resolution of this Phase I issue would not end the entire case: ñ[If] the Court rules in Verizonôs favor on the óSecurities Claimô issue, the only ***remaining issue will be the 'reasonableness' of the defense costs that Verizon incurred***, which likely can be resolved on motion with minimal additional discovery.ò JA5857-5858 (emphasis added).

- March 24, 2017: Verizon produced 150 pages of invoices, totaling more than $560,000 in expenditures, ***for the first time in connection with its motion for final judgment***. JA5459 at ¶ 8. (Verizonôs brief incorrectly states that it produced these invoices in connection with a summary judgment motion. VZ Br. at 73 n.167.)

Verizon ignores entirely the procedural history of this case, and instead focuses solely on the fact that the insurers amended Verizonôs draft September 30, 2016 letter to the Superior Court. VZ Br. at 77. Verizonôs deflection misses the

[2] According to Verizon, the Superior Court stated in its March 20 opinion that a ruling in Verizonôs favor on the Securities Claim issue would effectively be a ñdirected verdict in Verizonôs favor.ò VZ Br. at 76. This misstates the Superior Courtôs decision, which merely opines that ñthe issue of allocation would appear to be mootò if the court rules for Verizon on the Securities Claim issue. Zur. Br. at Ex. A p. 10. And in any event, whether or not there is an allocation does not address the reasonableness of Verizonôs $49 million in defense expenditures.

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mark for two reasons. *First,* the draft letter evidences Verizonôs clear understanding, after the completion of Phase I, that there would be a Phase II. The fact that the draft letter was revised does not change Verizonôs contemporaneous understanding that there would be a Phase II. *Second*, contrary to the implication in Verizonôs brief, Zurich and the other insurers amended Verizonôs draft letter only because they did not want to represent to the court that the reasonableness of Verizonôs fees and costs was the only remaining issue or that it could be resolved by motion. JA5822 at n.8; JA6212 at 65:1-66:4. As a result, the parties agreed to a more general proposal ï namely, that they would meet and confer following the courtôs decision on summary judgment motions regarding a schedule ñfor the resolution of any remaining issues not disposed of by the Courtôs decision,ò including the reasonableness of defense expenditures and whether they were jointly incurred. VZ Br. at B5.

No matter the standard of review this Court applies, the Superior Courtôs refusal to allow Zurich to litigate conditions to coverage it repeatedly raised throughout the litigation ignores the clear record before the trial court, condones Verizonôs 180-degree turn on whether there would be a Phase II, and constitutes legal error. It should therefore be reversed.

B. Both the Superior Court and Verizon Denied Zurich Any Opportunity to Litigate Coverage Conditions That Are Likely to Substantially Affect Zurich's Coverage Obligations.

Although the Superior Court refused to even consider whether Verizonôs $49 million in defense expenditures were reasonable or ñjointly incurredò with Mr. Diercksen, Verizon argues that these conditions are ñmeritlessò and ñbelated,ò and that Zurich failed to preserve them. VZ Br. at 71-74 & n.170. Verizonôs arguments are premature, wrong and contradicted by the trial court record.

As to the reasonableness of Verizonôs defense expenditures, Verizon argues that Zurich is too late because Zurich has not yet identified costs that were unreasonable or unnecessary. VZ Br. at 72-74. But, as noted above and in Zurichôs Opening Brief, the parties were ordered to (and did) focus exclusively on the Securities Claim issue during Phase I of the litigation pursuant to the Superior Courtôs bifurcation order, and Verizon even rejected the insurersô discovery requests for additional information relating to the underlying *U.S. Bank* Action. JA5925-5928. To fully and fairly litigate this condition to coverage, Zurich is entitled to seek discovery and present expert testimony on the reasonableness of Verizonôs $49 million in expenditures, and Zurich has not yet been given an opportunity to do that.[3]

[3] Zurich retained an expert to review Verizonôs defense expenditures, JA6204 at 33:14-34:6, but the expert cannot complete its analysis until Verizon

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As to whether Verizonôs expenditures were ñjointly incurredò with Mr. Diercksen, Verizon does not even attempt to explain why it refused to produce any discovery relating to this coverage condition. Instead, Verizon leapfrogs to what it claims the Runoff Policies mean, VZ Br. at 71-72, an issue on which there has been no discovery and which the Superior Court never considered. Zurich vigorously disputes Verizonôs interpretation of the phrase ñjointly incurredò Defense Costs, as it renders other policy language ï *e.g.*, the requirement that Defense Costs be ñjointly made and maintainedò against both an Insured Person and an Organization ï superfluous. Zur. Br. at 31-32; JA6221. On remand, the parties should have an opportunity to conduct discovery on and fully brief this issue before the Superior Court in the first instance.

Moreover, Verizon fails to explain why the millions of dollars it appears to have spent on law firms and other professionals involved with the Idearc spin-off constitute ñjointly incurredò Defense Costs, given the provision in the Runoff Policy limiting indemnification coverage to an Organizationôs indemnification of only Insured Persons. JA1316 (End. 7, Cl. 1). Verizon again side-steps this issue,

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produces the additional discovery the insurers refused to produce, including without limitation: (1) the underlying file for the *U.S. Bank* Action; (2) communications concerning ñwho should be counsel for Mr. Diercksenò and the ñallocation of attorney fees, costs and expenses,ò JA5925-5928; as well as (3) information relating to Verizonôs indemnification agreements with third-party professionals involved with the Idearc spin-off.

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claiming it ñwas not raised and preserved below.ò VZ Br. at 74 n.170. But Zurich and the other insurers unquestionably did raise this issue, *see* JA6230 at n.10; JA6401, the Superior Court recognized that Zurich raised the issue, *see* Zur. Br. at Ex. C p. 18 & n.72, and the Superior Court failed to consider it.[4]

For the foregoing reasons and the reasons stated in Zurichôs Opening Brief, these two coverage conditions are likely to substantially reduce or eliminate entirely Zurichôs coverage obligations, and the Superior Courtôs refusal to allow the parties to litigate them is reversible error. These issues should be decided in the trial court, after discovery, on subsequent dueling motions for summary judgment or, if need be, a short trial.

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[4] Verizon passingly states that Illinois National agrees with its position on what constitutes ñjointly incurredò Defense Costs. VZ Br. at 72. Illinois National is differently situated than Zurich on this issue because, unlike Zurich, Illinois Nationalôs sister company, National Union Fire Insurance Company of Pittsburgh, PA, another subsidiary of AIG, issued an E&O policy to Verizon (the ñVerizon Policiesò) that also provided coverage when the *U.S. Bank* Action was filed. JA2354. The Verizon Policies provided coverage excess to the Runoff Policies. JA2441. Unlike the Runoff Policies, the Verizon Policies provided coverage for Securities Claims brought against Verizon, even if Defense Costs were not ñjointly incurredò with an Insured Person. JA2358 (cov. B); JA5024 at 179:17-180:18. Thus, if Verizonôs Defense Costs were not ñjointly incurredò with Mr. Diercksen, those costs would not be covered under the Runoff Policies, but they may have been covered under the Verizon Policies. Because another AIG subsidiary is the primary insurer in the Verizon Policies, it is in Illinois Nationalôs financial interest to have all the Defense Costs be deemed ñjointly incurredò in order to insulate Defense Costs in the Verizon Policies Tower. *See* JA6224 at n.6. In short, correct or not, it is in Illinois Nationalôs financial interest here to join Verizon on this one issue because its affiliate *directly benefits by doing so* ï and for that reason alone.

II. Under New York Law, Zurich Does Not Owe Prejudgment Interest Unless and Until the Underlying Insurance Policies Are Exhausted By Actual Payment of Loss.

A. Verizon's Efforts to Apply Delaware Law to the Issue of Prejudgment Interest Are Baseless and Not Credible.

In arguing that Delaware law applies to the issue of prejudgment interest, Verizon inexplicably presents its third, contradictory position on this issue. In its first motion for partial summary judgment, Verizon argued that Delaware law applied, JA0381; JA1894 at n.7; in its motion for final judgment, Verizon argued that New York law applied, presumably in an effort to take advantage of New Yorkôs statutory rate of interest, which is higher than Delawareôs interest rate, JA5391; and now, in its brief on appeal to this Court, Verizon reverts back to Delaware law in an effort to avoid how the exhaustion provision in the Zurich Policy is interpreted under New York law, VZ Br. at 79-82. Not only is Verizonôs shifting position on choice of law not credible or principled, it also has no merit.

Verizon makes three arguments on appeal. *First*, Verizon argues that Zurich somehow ñconce[ded] that Delaware law governsò because the issue of prejudgment interest is a matter of substantive law. VZ Br. at 80. Zurich conceded nothing. To the contrary, Zurich has consistently argued since the outset of this litigation that New York law applies. JA1788 at n.9 (Illinois Nationalôs opposition to initial motion for summary judgment); JA1863 (Zurich joinder to

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Illinois Nationalôs opposition). The sole case cited in Verizonôs brief ï *Cooper v. Ross & Roberts, Inc.*, 505 A.2d 1305 (Del. Super. Ct. 1986) ï refutes Verizonôs argument. *Cooper* states: ñ[T]he substantive law ***selected by choice of law principles*** also determines the amount of damages.ò *Id.* at 1307 (emphasis added). As Zurich explained in its Opening Brief, because there was no conflict between Delaware and New York law on the threshold issue of whether the *U.S. Bank* Action constituted a Securities Claim, the Superior Court did not conduct a choice of law analysis, and instead defaulted to Delaware law. Zur. Br. at 35.

Second, after representing to the Superior Court that ñnothing in the Courtôs March 2 Order suggests that the Court made a choice of law decisionò so as to support the application of the law of the case doctrine, JA6009, Verizon now argues that ñthe application of Delaware law to the interest issue was separately supported as the law of the case,ò VZ Br. at 82. Verizonôs new argument is belied by Delaware law, which limits application of the law of the case doctrine to only when the choice-of-law analysis was squarely presented and decided by the trial court. Zur. Br. at 34. As Verizon previously explained when it was arguing for application of New York law, the Superior Court provided ñno discussion of the

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factors that would lead to the selection of one stateôs law over another,ò JA6009, and therefore it was legal error for the court to apply the law of the case doctrine.[5]

Third, Verizon incorrectly argues that Delawareôs choice-of-law principles mandate application of Delaware law. As an initial matter, because the Superior Court did not conduct a choice of law analysis, this Court should remand for the Superior Court to do so in the first instance. *See, e.g.*, *Ison v. E.I. DuPont de Nemours and Co., Inc.*, 729 A.2d 832, 844 (Del. 1999) (remanding for ñtrial court [to] consider afresh the choice of law questions on specific issues as the case develops and a full factual record is presentedò).

Upon remand, Delawareôs choice of law principles mandate that New York law controls the issue of prejudgment interest for the reasons stated in Zurichôs Opening Brief. As Verizon emphasized when it was arguing for application of New York law, New York is Verizonôs principal place of business; other insurers in the Runoff and Verizon Policies are likewise based in New York; Zurich is a

[5] During the Superior Court proceeding, Illinois National also incorrectly argued for application of Delaware law based on the law of the case doctrine. JA5955 & JA5957 n.10. With respect to Illinois National, the primary carrier, the defenses that Zurich seeks to litigate during Phase II ï namely, the reasonableness of defense costs and whether those costs were ñjointly incurredò between Verizon and Mr. Diercksen ï will likely not help its coverage position. *See supra* n.4. Accordingly, regardless of the law or the merits, Illinois National would benefit from application of Delaware law because it provides a lower prejudgment interest rate than New York law, and Illinois Nationalôs affiliate financially benefits if Zurich loses on its own arguments.

New York corporation; and the insurance policies were negotiated in and delivered to Verizonôs broker in New York. Zur. Br. at 38-39; JA0204-0206; JA5391. Applying the factors in section 188 of the *Second Restatement*, as well as this Courtôs recent decisions in *Certain Underwriters at Lloyds, London v. Chemtura Corp.*, 160 A.3d 457 (Del. 2017), and *Travelers Indemnity Co. v. CNH Industrial America, LLC*, 191 A.3d 288 (Del. 2018), New York law clearly applies.

Verizon ignores both *Chemtura* and *Travelers Indemnity*, which provide clear guidance on which stateôs laws a court should apply when interpreting ñthe meaning of a contract that composed part of a comprehensive, nationwide insurance program.ò *Chemtura*, 160 A.3d at 459. These decisions assessed each of the section 188 factors, and focused in particular on the insuredôs principal place of business, because ña companyôs headquarters staff is usually heavily involved in managing insurance programs that cover the entire company.ò *Id.* at 470.

Like the policies at issue in both *Chemtura* and *Travelers Indemnity*, the Runoff Policies purportedly provided a comprehensive insurance program. As Verizon previously asserted: ñThe Idearc Runoff Policies were purchased expressly to [1] cover liabilities of both Verizon and its directors and officers that might arise from a series of securities-related transactions by which Verizon divested certain of its directories businesses to Idearc,ò and ñ[2] obtain the broadest coverage available for all liability arising from the Idearc-related transactions.ò

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JA2288; JA2295. For comprehensive policies like this, ñthe inquiry should center on the insurance contracts and not the underlying claims.ò[6] *Travelers Indem.*, 191 A.3d at *1. This is particularly true here, where the underlying actions for which Verizon sought coverage were filed across the country and asserted claims under the laws of several different jurisdictions.[7] For these reasons, on remand, the Superior Court should apply New York law to issues relating to prejudgment interest.

B. Zurich Does Not Owe Prejudgment Interest.

Under New York law, Zurich does not owe prejudgment interest. Presumably recognizing that, under New York law, exhaustion provisions like the

[6] Verizon instead summarily relies on two Superior Court decisions ï *Arch Ins. Co. v. Murdock*, 2018 WL 1129110 (Del. Super. Ct. Mar. 1, 2018), and *Mills Ltd. Partnership v. Liberty Mutual Ins. Co.*, 2010 WL 8250837 (Del. Super. Ct. Nov. 5, 2010). VZ Br. at 81. These decisions are neither relevant nor persuasive, because (1) the policies at issue were not intended to provide transaction-related coverage across the country, as the Runoff Policies purportedly did; and (2) they either predate or fail to acknowledge this Courtôs decisions in *Chemtura* and *Travelers Indemnity*. In any event, the *Murdock* decision is a misstatement of Delaware law and, barring other resolution in the trial court in the meantime, will surely end up in this Court for correction of the choice of law decision.

[7] *See* JA1647 (*U.S. Bank Nat'l Ass' v. Verizon*, No. 10-01842 (N.D. Tex.) ï asserted claims under Texas law, federal law and Delaware law); JA2635 (*Barnard v. Verizon*, No. 10-1304 (E.D. Pa.) ï asserted claims under multiple federal statutes and Pennsylvania law); JA2621 (*Talbot v. Idearc, Inc.*, No. 09-31828 (N.D. Tex.) ï request for appointment of trustee under federal bankruptcy laws); JA0202 (*U.S. Bank Nat'l Ass'n v. Coticchio*, No. 651132/2013 (N.Y. Sup. Ct.) ï writ of summons filed in New York).

one in the Zurich Policy require that the underlying insurers pay their policy limits before the excess carrierôs coverage obligations are triggered, Verizon relies on Delaware law. VZ Br. at 82-84. Verizon passingly attempts to distinguish the many cases applying New York law cited in Zurichôs Opening Brief, but its distinctions are either wrong or immaterial.

The Zurich Policy unambiguously provides that coverage attaches only after the underlying insurers have exhausted their policy limits through actual payment of loss: ñIn the event and only in the event of reduction or exhaustion of the Limit(s) of Liability of Underlying Insurance solely as the result of actual payment of loss covered thereunder.ò JA5868 at § III.B; *see also id.* § I. This provision is substantively identical to policy language which courts in both New York and elsewhere have held require the underlying insurers to pay their respective limits of liability before the excess insurerôs coverage is triggered.

For example, in *Forest Laboratories, Inc. v. Arch Insurance Co.*, 953 N.Y.S.2d 460, 462 (N.Y. Sup. Ct. 2012), a New York trial applying New York law interpreted the following exhaustion provision in an excess carrierôs policy as requiring payment of the limits of liability of the underlying insurers: ñ[I]t is agreed that in the event . . . of a reduction or exhaustion of the Underlying Limits of Liability, solely as a result of actual payment of a Covered Claim pursuant to the terms and conditions of the Underlying Insurance thereunder.ò *Id.* at 463. The

underlined language is the same as the language in the Zurich Policy. In fact, as the court in *Forest Laboratories* explained, the exhaustion provision in the Zurich Policy is even clearer in its requirement that the underlying insurers themselves pay the limits of liability, as it limits exhaustion to only the ñactual payment of loss or losses thereunder.ò *See id.* at 465 (stating that policy language nearly identical to Zurich Policy ñevince[s] a clarity unfortunately missing from the RSUI policy language [at issue in *Forest Laboratories*], but this does not render the RSUI policy language ambiguousò). This decision was affirmed by the Appellate Division of the Supreme Court. *See* 984 N.Y.S.2d 361 (N.Y. App. Div. 2014).

The United States Court of Appeals for the Fifth Circuit has also repeatedly found that policy language similar to that of Zurichôs requires payment by the underlying insurers of their policy limits before an excess carrierôs coverage is triggered. *See, e.g.*, *Martin Res. Mgmt. Corp. v. AXIS Ins. Co.*, 803 F.3d 766, 769 (5th Cir. 2015) (policy stating that ñinsurance afforded under this Policy shall apply only after all applicable Underlying Insurance . . . has been exhausted by actual payment under such Underlying Insuranceò was not triggered after insured settled with underlying insurer for less than policy limits); *Citigroup Inc. v. Federal Ins. Co.*, 649 F.3d 367, 373 (5th Cir. 2011) (Texas law) (policy providing that coverage attaches ñin the event of the exhaustion of all of the limit(s) of liability of such óUnderlying Insuranceô solely as a result of payment of loss

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thereunderò also precluded coverage after insured settled with underlying insurer for less than policy limits).

This Court has likewise interpreted substantially similar exhaustion provisions under the laws of other states, including New York, to require that the underlying insurers pay their limits of liability. *See In re TIAA-CREF Ins. Appeals*, 192 A.3d 554, at *5 (Del. 2018) (affirming Superior Courtôs holding that excess insurersô coverage obligations had not been triggered because (a) underlying insurers had not paid out policy limits and (b) obligations were uncertain) (New York law); *Intel Corp. v. Am. Guarantee & Liab. Ins. Co.*, 51 A.3d 442, 449 (Del. 2012) (holding that provision requiring exhaustion by ñpayments of judgments or settlementsò ñcannot be construed . . . to encompass an insuredôs own payment of defense costsò) (California law).[8]

Verizonôs attempt to distinguish *TIAA-CREF*, *Martin Resource*, and other cases with similar exhaustion language is unavailing. VZ Br. at 85 & n.194. As

[8] Other courts have interpreted this policy language in the same way. *See e.g.*, *JP Morgan Chase & Co. v. Indian Harbor Ins. Co.*, 98 A.D.3d 18, 21-22 (N.Y. App. Div. 2012) (policy providing that coverage attaches ñonly after all applicable Underlying Insurance with respect to an Insurance Product has been exhausted by actual payment under such Underlying Insuranceò precluded insured from settling with insurer for less than policy limits) (Illinois law); *Great Am. Ins. Co. v. Bally Total Fitness Holding Corp.*, 2010 WL 2542191, at *1, *5 (N.D. Ill. June 22, 2010) (excess policy applies only ñin the event of exhaustion of all of the limits of insurance of the Underlying Insurance solely as a result of actual payment of loss or losses thereunderò).

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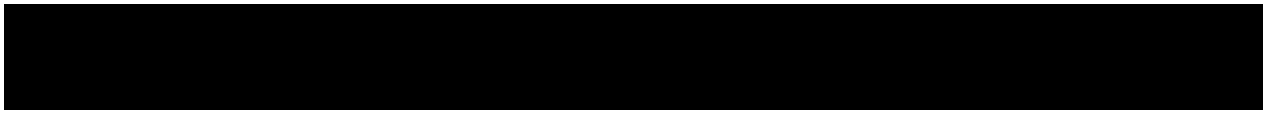
the New York court found in *Forest Laboratories, Inc.*, an exhaustion provision need not have the magic words ñunderlying insurersò to unambiguously require that the insurers themselves pay their policy limits before an excess policy attaches. *See* 953 N.Y.S.2d at 462. The policy at issue in *Martin Resource*, for example, required exhaustion ñby actual payment under such Underlying Insurance,ò rather than by ñactual payment of loss covered thereunderò as the Zurich Policy requires. 803 F.3d at 769; *see also* VZ Br. at 85 n.194. The Fifth Circuit nonetheless emphasized that the exhaustion provision presented ñlanguage closest to theò language at issue in *Citigroup*, which is substantively identical to the Zurich Policy, and the court accordingly required exhaustion of the underlying insurance through actual payment by the insurers. *See Martin Res.*, 803 F.3d at 769. In other words, in requiring the underlying insurers to pay their policy limits before an excess carrierôs coverage was triggered, *Martin Resource* relied on the exhaustion provision language in the Zurich Policy.[9]

In sum, the exhaustion provision in the Zurich Policy unambiguously requires that the underlying insurers pay their respective policy limits before

[9] Verizon also misstates the Second Circuitôs decision in *Ali v. Federal Insurance Co.*, 719 F.3d 83, 94 (2d Cir. 2013). VZ Br. at 85 n.193. The courtôs holding simply required actual ñpayment of losses,ò rather than ñthe accrual of liability,ò to trigger excess coverage, and the court expressly did not rule ñon whether the underlying insurers, in particular, were required to make paymentsò because that was not at issue in the litigation.



Zurichôs coverage obligations are triggered. As this Court has previously explained, the ñplain policy language on exhaustionò controls. *Intel Corp.*, 51 A.3d at 450. For this reason, even if this Court affirms the Superior Courtôs final judgment, the decision requiring Zurich to pay prejudgment interest should be reversed. At a minimum, the issue should be remanded for the Superior Court to consider the issue under New York law and apply the correct law to the issue.

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Arguments on Cross-Appeal

I. Assuming for Purposes of Verizon's Cross-Appeal That the Superior Court Did Not Err in Awarding Verizon Prejudgment Interest, the Court Correctly Held that Interest Began to Accrue When Verizon Demanded Payment From the Insurers.

A. Question Presented

Assuming the Superior Courtôs decision to award Verizon prejudgment interest was not in error, did the Superior Court err in holding that prejudgment interest began to accrue when Verizon demanded payment from the insurers, rather than when Verizon purportedly began accruing defense expenditures. Exs. C & D (Raised below at JA5840.)

Suggested Answer: No.

B. Standard and Scope of Review

A trial courtôs determinations relating to the award of prejudgment interest are reviewed *de novo*. *See Chrysler Corp. v. Chaplake Holdings, Ltd.*, 822 A.2d 1024, 1037 (Del. 2003).

C. Merits of Argument

For the reasons stated above and in Zurichôs Opening Brief, Zurich does not owe prejudgment interest because its Policy has not yet attached, and it will not attach until the underlying insurers exhaust their respective policy limits through ñactual payment of loss covered thereunder.ò JA5868 at § III.B. But even if the Court were to agree with Verizonôs interpretation of the Policyôs exhaustion

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provision, prejudgment interest did not begin to accrue until Verizon produced invoices for its purported defense expenditures and demanded payment from Zurich. Verizonôs argument that prejudgment interest should begin to accrue when Verizon made payment is inconsistent with both the Runoff Policy and clearly established legal principles.

The Runoff Policy states: ñ[T]he Insurer shall advance, excess of any applicable retention amount, covered Defense Costs no later than ninety (90) days *after the receipt by the Insurer of such defense bills*.ò JA1282 (emphasis added). In March 2014, Verizon produced for the first time invoices to Zurich, JA1930-1931 at ¶ 4, and it did not finish producing invoices until March 2017, when it filed its Motion for Final Judgment, JA5459 at ¶ 8. Under the plain terms of the Runoff Policy, interest therefore could not begin to accrue until production of the invoices.

The cases Verizon cites on pages 86 and 87 of its brief further support the Superior Courtôs decision. In *Metropolitan Mutual Fire Insurance Co. v. Carmen Holding Co.*, 220 A.2d 778, 782 (Del. 1966), this Court explained that where a policy requires ñpayment within [a certain number of] days after the filing of a proof of loss,ò as the Runoff Policy required here, interest starts from ñthe end of that period.ò In *Rexnord Industries, LLC v. RHI Holdings, Inc.*, 2009 WL 377180 (Del. Super. Ct. Feb. 13, 2009), the Superior Court held that interest begins to accrue when payment is due because, unlike the Runoff Policy at issue here, the

indemnification provision expressly stated that defendants were obligated to pay ñas sums for such Losses ***become due and payable***.ò *Id.* at *9 (emphasis added). Because the Runoff Policy did not require the insurers to advance defense expenditures until they received invoices, Zurich does not owe prejudgment interest until Verizon complied with this condition.

Verizonôs argument also contradicts well-established legal principles. ñFor insurance claims, interest accumulates from the date a party actually demands payment.ò *Stonewall Ins. Co. v. E.I. Du Pont De Nemours & Co.*, 996 A.2d 1254, 1262 (Del. 2010). ñWhere the underlying obligation to make payment arises *ex contractu*,ò as it does with insurance policies, this Court ñlook[s] to the contract itself to determine when interest should begin to accrue.ò *Hercules, Inc. v. AIU Ins. Co.*, 784 A.2d 481, 508 (Del. 2001). Until an insured demands payment and the insurer denies coverage, a cause of action does not exist and, accordingly, interest cannot accrue.[10] *See, e.g.*, *AGCS Marine Ins. Co. v. World Fuel Servs.,*

[10] The cases on which Verizon relies are either easily distinguishable or support the Superior Courtôs decision. *See Brandywine Smyrna, Inc. v. Millennium Builders, LLC*, 34 A.3d 482, 487 (Del. 2011) (highlighting that plaintiff ñdid not delay its demand for paymentò); *Citadel Holding Corp. v. Roven*, 603 A.2d 818, 826 (Del. 1992) (ñUnder this contractual scenario, Roven is entitled to interest computed from the date of demand.ò); *Wayman Fire Prot., Inc. v. Premium Fire & Sec., LLC*, 2014 WL 897223 (Del. Ch. Mar. 5, 2014) (holding that, for tort and statutory claims, not contract claims like those at issue here, interest accrued when injury took place).

Inc., 220 F. Supp. 3d 431, 442-43 (S.D.N.Y. 2016) (setting accrual date for prejudgment interest to be thirty days after insured provides proof of loss, consistent with policy language).

Here, Verizon inexplicably waited to demand payment from Zurich until January 2014, when it requested mediation. Prior to that date, Verizon communicated regularly with Illinois National, the primary insurer, about its fees. JA5817-5818. But Verizon never communicated with Zurich about its fees or provided defense invoices; it waited a year to even forward Illinois Nationalôs coverage position to Zurich, JA5902; and it left Zurich off its correspondence with Illinois National about whether the *U.S. Bank* Action constitutes a Securities Claim. To be sure, Verizon provided Zurich with general updates on the status and purported costs of the underlying action, JA6033-6077, but as this Court held in *Hercules*, such ñnoticesò do not constitute ña request for payment of any sum.ò *Hercules, Inc.*, 784 A.2d at 508 (holding that notices which ñprovide updates on pending litigation and provide cost estimatesò and ñstate that there is órеason to believe the claims were of such a magnitude that your policies could be implicatedôòò do not constitute requests for payment so as to trigger the accrual of prejudgment interest).[11]

[11] Recognizing that this Courtôs decisions in *Hercules* and *Stonewell* flatly refute Verizonôs argument that it is entitled to prejudgment interest before it

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Awarding an insured prejudgment interest years before it demanded reimbursement of that payment from its insurer would create the perverse incentive for insureds to delay issuing a formal demand and providing proof of loss in an effort to capitalize on above-market prejudgment interests rates. Delaware courts should not incentivize such gamesmanship. *See, e.g.*, *Village of Ilion v. Cty. of Herkimer*, 23 N.Y.3d 812, 821 (N.Y. 2014) (ñCalculating interest on a municipalityôs debt from the time of demand was developed as a means to deter opportunistic creditors from buying up small claims against municipalities and waiting to demand payment until the statute of limitations has nearly expired in order to reap the benefits of the statutory interest rate.ò).

For these reasons, assuming for purposes of this cross-appeal that the Superior Court correctly awarded prejudgment interest to Verizon, such interest did not begin to accrue until at least January 2014, when Verizon formally demanded payment of its defense expenditures from Zurich pursuant to its mediation request.

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demands payment, Verizon attempts to distinguish them on the grounds that those cases involved general liability policies. *See* VZ Br. at 88. The distinction is legally irrelevant on this point. In fact, Verizonôs assertion that ñit was unclear [in *Hercules* and *Stonewall*] when the excess insurersô payment obligations were triggeredò applies equally here ï Zurich did not know of Verizonôs belief that Zurichôs payment obligations were triggered until Verizon requested mediation, because Verizon never informed Zurich of its coverage position.

Conclusion

The Superior Courtôs judgment denying Zurich an opportunity to litigate conditions to coverage that Zurich timely raised at the outset of this litigation, and its determination that Zurich is liable for prejudgment interest before the underlying insurers exhausted their policy limits through actual payment of covered loss, constitute legal error. Zurich therefore respectfully requests that this Court reverse the Superior Courtôs final judgment and remand for further proceedings. However, if this Court finds that Zurich currently owes prejudgment interest, it should affirm the Superior Courtôs determination that interest did not begin to accrue until January 2014, when Verizon demanded for the first time its defense expenditures from Zurich.

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