EFiled: Feb 28 2025 02:49PM EST
Filing ID 75741803
Case Number Multi-Case

IN THE SUPREME COURT OF THE STATE OF DELAWARE

IN RE AEARO TECHNOLOGIES LLC INSURANCE APPEALS	No. 381, 2024 No. 423, 2024 SUPERIOR COURT OF THE STATE OF DELAWARE C.A. No. N23C-06-255 SKR (CCLD)

REPLY BRIEF OF PLAINTIFFS-BELOW/APPELLANTS

OF COUNSEL
(*pro hac vice*):

Robin L. Cohen
Kenneth H. Frenchman
Orrie A. Levy
COHEN ZIFFER FRENCHMAN
& MCKENNA LLP
1325 Avenue of the Americas
New York, NY 10019
Telephone: (212) 584-1801
rcohen@cohenziffer.com
kfrenchman@cohenziffer.com
olevy@cohenziffer.com

Donald W. Brown
COVINGTON & BURLING LLP
415 Mission Street, Suite 5400
San Francisco, California 94105
Telephone: (415) 591-6000
dwbrown@cov.com

Rani Gupta
COVINGTON & BURLING LLP
3000 El Camino Real, 10th Floor
5 Palo Alto Square
Palo Alto, California 94306
Telephone: (650) 632-4700
rgupta@cov.com

Tyler Weinblatt
COVINGTON & BURLING LLP
One CityCenter
850 Tenth Street NW
Washington, DC 20001
Telephone: (202) 662-6000
tweinblatt@cov.com

Dated: February 28, 2025

BERGER MCDERMOTT LLP

David J. Baldwin (No. 1010)
Peter C. McGivney (No. 5779)
1105 North Market Street, 11th Floor
Wilmington, Delaware 19801
Telephone: (302) 655-1140
Facsimile: (302) 655-1131
dbaldwin@bergermcdermott.com
pmcgivney@bergermcdermott.com

Attorneys for Plaintiffs-Below/Appellants

TABLE OF CONTENTS

TABLE OF CITATIONS

Page(s)

Cases

Other Authorities

NATURE OF PROCEEDINGS

The Insurers' briefs fail to support their draconian and atextual reading of their Policies' self-insured retention ("SIR" or "retention") provisions. The Insurers do not identify a single case from any jurisdiction where an insurer even had the audacity to assert the position that such provisions preclude coverage for a wholly owned subsidiary that satisfies the SIR requirement through the offices of its parent, let alone a case endorsing that reading. This dearth of authority is no accident. It is common knowledge that companies routinely consolidate insurance functions in the parent entity, and that the parent typically manages claims and pays SIRs and defense costs for its various wholly owned subsidiaries without issue. Indeed, the structure and plain language of the Policies indicate to any reasonable reader that restrictions on *who* may pay an SIR prohibit, at most, payments by unaffiliated third parties that lack an identity of financial interest with the policyholder.

The Insurers' attempt to defend the Superior Court's reasoning that because the Policies' SIRs use the term "you," they require that the $250,000 SIR be paid from an account separately maintained by the Aearo insureds. But even the Insurers recognize that if their argument were taken to its logical conclusion, it would lead to absurd results given that the Policies use the word "you" throughout to describe functions that are commonly performed on behalf of an insured by a

parent entity or other related party. Thus, when the Policies are viewed as a whole, as is required, it is apparent that the Policies use the term "you" to distinguish conditions that are the insured's responsibility from those that are the insurer's.

Nor do the ACE and Twin City Policies' references to payments by "other" and "another" foreclose payments by 3M Company, the parent of the Aearo entities that are named insureds under the Policies, from satisfying the SIRs. In context, those provisions are most reasonably interpreted as prohibiting payments from non-affiliated entities such as other insurers from satisfying the SIR, as courts have interpreted these provisions.

Lacking support in relevant case law or the plain language of the Policies, the Insurers suggest that their policy language should be construed by relying on Aearo's separate bankruptcy case and precedent regarding corporate formalities, such as the veil piercing doctrine. But these corporate law doctrines say nothing about the relevant question here: Whether a reasonable policyholder would view 3M as sufficiently distinct from its wholly owned subsidiary such that it constitutes "another" entity for purposes of paying the SIRs.

The answer to that question is resoundingly no. No reasonable policyholder would conclude that it forfeits coverage when its own parent company—a co-defendant in the underlying litigation at issue—pays for a joint defense directly, rather than manufacturing a superfluous transaction whereby the parent funnels

those same funds through its wholly owned subsidiary's bank account so that the policyholder could itself nominally "pay" the same defense costs with the same funds. Nothing in the Insurers' briefs justifies imposing this requirement, much less demonstrates that the Insurers' novel and legally unprecedented interpretation is the *only* reasonable one, as required for them to prevail.

But even if the Insurers were somehow correct that their Policies' SIRs can *only* be exhausted through payment from an Aearo bank account, the "Savings Clauses" in each of the Insurers' Policies expressly preserve Aearo's coverage above $250,000 in the event of a failure and/or refusal to pay the SIR *for any reason*. The plain language of the Savings Clauses confirms that the draconian result the Insurers seek to achieve here is contrary to the Policies.

The Insurers' only retort is to try to limit these clauses to bankruptcy or insolvency, seemingly based on their headings. But that interpretation would render significant and material portions of the Savings Clauses meaningless, contrary to both Delaware and Indiana law. Specifically, the Savings Clauses apply *both* to bankruptcy/insolvency *and*, separately, to a failure and/or refusal to pay or the uncollectability of the SIRs *for any reason*. In both cases, they simultaneously prevent the Insurers from ever being required to pay the SIR while protecting Aearo from forfeiting coverage for amounts that exceed the SIR. If the Insurers intended to limit their Savings Clauses to instances of bankruptcy alone,

they were required to use different language to achieve that result. Instead, they used language expressly expanding their scope beyond the bankruptcy context.

Finally, the Insurers tie themselves into knots making contradictory arguments that the SIRs are somehow simultaneously conditions precedent to coverage *and* that they are not provisions that result in a forfeiture of coverage. But the defining feature of a condition precedent is that the failure to satisfy it results in forfeiture. Regardless, the Court does not need to resolve this internal inconsistency because the law in both Delaware and Indiana is clear: Courts will not interpret the failure to satisfy a condition to result in a forfeiture unless forfeiture is "expressly" or "explicitly" identified as the consequence of that failure—something these Policies glaringly fail to do with respect to restrictions on *who* may pay the SIR. Accordingly, any failure to comply with the SIRs in the Policies can *only* result in an offset, not a forfeiture of coverage.

For these reasons, this Court should reverse the relevant portion of the decision below and hold that payments by 3M satisfy the SIRs of the Policies, or that the Savings Clauses confirm that coverage is preserved in excess of $250,000 regardless of whether Aearo or its parent company, 3M, paid the SIR.

ARGUMENT

I. Payments Made by 3M Satisfy the Policies' SIRs

A. The Use of "You" in the Policies Supports Aearo's Construction

The Policies use the terms "we" and "you" to describe and distinguish between responsibilities falling on the Insurers ("we") and the insured, Aearo ("you"). For example, the Policies require that "you" provide notice of a claim, or that "you" maintain claim records—functions that are frequently performed on a policyholder's behalf, including by a parent company. Opening Br. at 20–21; Supp. Br. at 16–17; *see also Hugo Boss Fashions, Inc. v. Fed. Ins. Co.*, 252 F.3d 608, 623 n.15 (2d Cir. 2001) ("that the parent company, rather than the subsidiary, paid the costs" of defending the insured in underlying litigation "is of no moment").[1] Thus, consistent with the Policies' usage of the word "you" throughout, Aearo fulfilled its responsibility with respect to the SIRs when 3M, its 100% owner, satisfied the Policies' SIRs through payments made on Aearo's behalf.

Tellingly, Twin City does not even try to meaningfully defend the Superior Court's use of the word "you" in the SIRs to effectively exclude otherwise available coverage. *See* Twin City Br. at 15–16, 21; Ex. A at 13, 15–16. And for

[1] Contrary to Royal Surplus's contention, these conditions are not framed in terms of "you or your loss adjusting representative." *See* A00992 (listing eight conditions without such language).

good reason: No commercially reasonable person, insured or insurer, would interpret the word "you" in the SIR provision to prohibit Aearo's 100% parent from paying the SIR. That is likely why, prior to the Superior Court's decision here, *no* court had ever reached this conclusion.

Unlike Twin City, ACE and Royal Surplus attempt to defend the Superior Court's strained interpretation of the word "you," suggesting that such conditions may be performed by the insureds' agents, but for some reason not by its parent company. ACE/Royal Br. at 21. That distinction is unfounded and lacks any textual basis in the Policies. It is also inconsistent with reality. The Claims Manager in 3M's Insurance Department provided notice to the Insurers (on 3M letterhead) of the Earplug Litigation. A01450–A01452; A01454–01458. 3M's Insurance Department continued to communicate with the Insurers about the Earplug Litigation, who responded to 3M personnel. A03787–A03788; A03795–A03798; A03804–A03806.

Further, as 3M informed the Insurers, "3M's inside counsel" was "responsible for the handling and management of the Underlying Litigation" and provided numerous updates to the Insurers. A01457; A00933–A00934 ¶ 17. The Insurers never objected to such communications on the basis that they came from 3M rather than its wholly owned Aearo subsidiaries. *See, e.g.*, A03800–A03801; A01460–A01462. In fact, such practices were standard because Aearo did not

maintain separate insurance personnel or in-house litigation counsel after its 2008 acquisition by 3M—as is common in corporations. A00929–A00930 ¶¶ 2, 4; A03817–A03818 ¶ 3; United Policyholders *Amicus* Br., Appeal No. 381, 2024 (Dec. 10, 2024), at 11–15.

The Insurers next argue that "it was 3M's responsibility to ensure compliance with the Aearo Entities' legacy insurance program." ACE/Royal Br. at 28. But 3M did exactly that by providing notice, keeping the Insurers fully informed, and paying the SIRs hundreds of times over—as the Insurers sat by and said nothing. Compliance with the Policies does not, however, require 3M to maintain separate insurance personnel for Aearo LLC, Aearo Technologies, and each of the many other subsidiaries it acquires solely for the rare occurrence of communicating with insurers under a subsidiary's legacy insurance policy—any more than it requires 3M to deposit money in its subsidiary's bank account for the sole purpose of paying a $250,000 SIR.[2]

[2] Twin City falsely asserts that Aearo LLC contends that it was not "permitted" by 3M to open a bank account. Twin City Br. at 43 & n.15. Aearo simply submits that the Twin City Policy does not require Aearo LLC to open a bank account for the sole purpose of paying the SIR. Further, an accounting receivable on the books of Aearo LLC is not the equivalent of a bank account, as Twin City implies. *Id.* at 12. Nor do Aearo and 3M contend that subsidiaries "cannot" ever pay claim expenses. *See id.* at 23 n.8. Rather, the Policies do not condition coverage on such technical accounting measures.

B. The Insurers' Restrictive Reading of "Another" and "Other" Should Be Rejected

The Royal Surplus Policy has no additional policy language beyond "you" arguably governing who may pay the SIR; therefore, the Superior Court's ruling with respect to the Royal Surplus Policy should be reversed for the reasons stated in Section I.A alone. *See also* Supp. Br. at 15–17.

Further, the ACE policy language providing that the SIR "shall not be satisfied by payment … by any other insurer, person, or entity," and the Twin City policy language providing that the SIR "shall not be reduced by … any payment made … by another, including any payment from any other applicable insurance," does not require a different result. *See* ACE/Royal Br. at 16 (emphasis omitted); Twin City Br. at 10 (emphasis omitted).[3]

As discussed in 3M/Aearo's two opening briefs, the words "other" and "another," when read in context, focus on payments by non-affiliated third parties—not entities within the same corporate structure that share a complete financial interest with the policyholder with respect to the loss for which coverage is sought. Opening Br. at 22–24; Supp. Br. at 17–18. That is why the *only* example offered in the SIRs of the type of actual entity whose payment would not

[3] Twin City notes the irrelevant fact that many companies, including 3M, have captive insurers. Twin City Br. at 23–24. But this case does not present the issue of whether payments by a captive insurer would be affected by the "other applicable insurance" language in the SIR provision.

satisfy the retention is another insurer. The terms "other" and "another" in the policy language above do not include—much less unambiguously include—wholly related corporate entities with overlapping insurance and litigation functions, such as Aearo and 3M.

The Insurers cannot dispute that the plain meaning of the words "another" and "other" is "distinctly different," which 3M and Aearo are not for the purposes of paying the SIR. *American Heritage Dictionary of the English Language* 74 (5th ed. 2018); *see also* Opening Br. at 23; Supp. Br. at 18–19.[4] Aearo's loss is ultimately borne by its 100% owner, 3M. Whether 3M gives Aearo the funds to pay the SIR and Aearo then writes the check (which the Insurers concede would satisfy the SIR) or instead, 3M writes the check itself, the effect is one and the same. The Insurers' interpretation is thus contrary to the plain and ordinary meaning of these words and is commercially unreasonable. Opening Br. at 21–22 (citing cases); Supp. Br. at 16–17.

At the very least, a reasonable insured would not interpret the undefined words "other" and "another" so expensively that they vitiate coverage when its 100% parent—which performs insurance and litigation duties for its subsidiaries—

[4] Aearo's citation to *State of Minnesota v. Moore*, 2021 WL 4059689, at *3 (Minn. Ct. App. Sept. 7, 2021), Opening Br. at 23, was to emphasize the court's use of this dictionary definition, not to analogize to the facts of that case. *See* Twin City Br. at 17.

pays the SIR on its behalf. Thus, this interpretation controls. *Monzo v. Nationwide Prop. & Cas. Ins. Co.*, 249 A.3d 106, 118 (Del. 2021) (where "there is more than one reasonable interpretation of an insurance policy, Delaware courts apply the interpretation that favors coverage"); *Eli Lilly & Co. v. Home Ins. Co*., 482 N.E.2d 467, 470 (Ind. 1985) (same).[5]

C. The Insurers Misconstrue the Case Law

The Insurers do not identify any decision where a court interpreted this or similar policy language to preclude payment by the insured's corporate parent. And though the Insurers criticize Aearo for not identifying a specific case holding that a corporate parent's payment exhausts the SIR of its wholly owned subsidiary, that is only because Aearo has not been able to locate any decision where an insurer appears to have even *advanced* the extreme position taken by the Insurers here—not before any court in any jurisdiction.

The two cases the Insurers particularly rely on to suggest otherwise *actually* hold—consistent with Aearo's construction—that retentions could not be satisfied by unrelated additional insureds or other insurers, entities that are not corporate

[5] Twin City wrongly contends that Aearo waived an argument that the policy language is ambiguous. *See* Twin City Br. at 16. Both Aearo and the Superior Court cited the black-letter principle that ambiguities in an insurance policy are construed in favor of the insured. A00239; A03752; Ex. A at 12. In any event, an appellant can present an "additional reason in support of a proposition urged below." *Kerbs v. California E. Airways, Inc.*, 90 A.2d 652, 659 (Del. 1952).

affiliates of the named insured. *See Forecast Homes, Inc. v. Steadfast Ins. Co.*, 105 Cal. Rptr. 3d 200, 212–13 (Cal. Ct. App. 2010) (payment by contractor included as an additional insured in a subcontractor's policy does not satisfy the SIR); *Walsh Constr. Co. v. Zurich Am. Ins. Co.*, 72 N.E.3d 957, 958–59, 965 (Ind. Ct. App. 2017) (same).

The Insurers incorrectly describe *Forecast Homes* as "directly on point," mischaracterizing it as holding that "payments by the *'parent'* general contractor did not satisfy the retention because only payments by the insured would erode it." Twin City Br. at 26–27 (emphasis added). But the additional insured in *Forecast Homes* (a housing developer) was *not* the "parent" of the insured subcontractor and the word "parent" never even appears in the decision. 105 Cal. Rptr. 3d at 203–04. Rather, the policies were issued to wholly independent subcontractors required by hold harmless agreements to make Forecast an additional insured. *Id.* at 203. The court held that Forecast could tap into the subcontractors' policies only if Forecast requested that the subcontractor made payments pursuant to its hold harmless agreement with the developer, which would satisfy the SIR. *Id*. at 209. The court reasoned that the insured subcontractors "had sound reasons for wanting to control whether and when coverage under the policy would be triggered," including possibly wanting to "preserve the coverage" to pay for future claims. *Id.* at 213. *Forecast Homes* is therefore inapposite because the party that sought to pay the

SIR amount did so *on its own behalf* (***not*** to benefit the named insured) and was not only completely *unaffiliated* with the named insured but directly *adverse* to the policyholder.

Similarly, in *Walsh*, a general contractor (Walsh) sought coverage under its subcontractor's policy as an additional insured. 72 N.E.2d at 958. The subcontractor argued in support of the *insurer* that Walsh was *not* entitled to additional insured coverage at all. *See id.* at 962 n.3. Rejecting that argument, the court addressed the separate question whether an endorsement adding an SIR to the policy applied to the obligation to defend Walsh. Thus, the only issue was whether the SIR applied *at all* vis-à-vis an additional insured such as Walsh. The court never considered whether Walsh (rather than the named insured) might be able to satisfy the SIR itself as there was no suggestion in the opinion that Walsh paid the SIR amount or was prepared to do so. *Id.* at 963. *Walsh* is not instructive here.

D. The Purposes of SIR Provisions Support Aearo's Interpretation

The Insurers' arguments about the two core purposes of SIRs only confirm that Aearo's interpretation is correct. First, an SIR's main purpose is to relieve the insurer from managing and paying smaller claims—a plus for the insurer—thus reducing premiums, a plus for the insured. Twin City Br. at 32–34; ACE/Royal Br. at 21. That purpose is met if 3M (or anyone else) pays the first $250,000 in loss. Supp. Br. at 20.

Second, though the Superior Court relied on the "moral hazard" purpose of SIRs, the Insurers conspicuously ignore that the Superior Court and the Insurers acknowledged that if 3M deposited money in Aearo's bank account, Aearo could simply repay that money to defense counsel and satisfy the Policies' retentions under the Insurers' interpretation. Opening Br. at 30–32; A04740–A04741 at 62:11–63:4, Ex. A at 14–15 & n.65. But Aearo bears the same amount of risk in that situation as if 3M pays the retention directly, so the Insurers' interpretation furthers no moral hazard purpose. Supp. Br. at 19–20.[6]

The moral hazard rationale is further undermined by the fact that the "occurrence"-based Policies at issue here provide coverage for injury occurring in the applicable policy period: 1997–2000 for Royal Surplus, 2000–2001 for Twin City, and 2007–2008 for ACE. A00945; A00997; A01380. The moral hazard rationale is based on the idea that the insured will take less risky activity knowing that it (rather than the insurer) will be responsible for any resulting loss. Opening Br. at 30–31; Ex. A at 15 n.65. But during the period that Aearo was taking any actions for which it would be liable under the Policies, 3M was a "complete stranger" that had not yet acquired Aearo, such that the full risk relating to the loss

[6] Contrary to Twin City's argument, Aearo briefed the purpose of SIR provisions below and the Superior Court based its decision on this rationale. A04503; Ex. A at 15; *see also Kerbs*, 90 A.2d at 659 (appellant can present an "additional reason in support of a proposition urged below"); Del. Sup. Ct. R. 8 (permitting consideration of questions not presented below in interests of justice).

at issue here rested on Aearo during the relevant time period. ACE/Royal Br. at 31. It is unreasonable to believe that Aearo would be encouraged to act in a riskier manner in the late 1990s and 2000s based on the possibility that it might later be purchased and the responsibility for its SIR payments consolidated within a department of its parent company. Thus, there is no legitimate purpose served by the Insurers' interpretation.

E. That Aearo and 3M Are Separate Legal Entities Is Immaterial

Finally, the Insurers rely heavily on the uncontroversial fact that 3M and its Aearo subsidiaries are separate corporate entities, citing non-insurance cases about veil piercing and other corporate formalities doctrines.[7] None of these cases address the pertinent questions of insurance policy interpretation here.

Whether the SIR provisions unambiguously prevent 3M's payments from satisfying the SIR is resolved by reference to the text of the Policies. The

[7] *See Wenske v. Blue Bell Creameries, Inc*., 2018 WL 5994971 (Del. Ch. Nov. 13, 2018) (vicarious liability, veil-piercing, and joint venture liability); *Buechner v. Farbenfabriken Bayer Aktiengesellschaft*, 154 A.2d 684 (Del. 1959) (creditor action); *New Empire Assocs. 14, L.P. v. Rich*, 292 A.3d 112 (Del. Ch. 2023) (fiduciary duty claims); *Culverhouse v. Paulson & Co.*, 133 A.3d 195 (Del. 2016) (investor standing for direct suit); *Manti Holdings, LLC v. Authentix Acquisition Co.*, 261 A.3d 1199 (Del. 2021) (stockholder appraisal action); *Cuppels v. Mountaire Corp.*, 2020 WL 3414848 (Del. Super. Ct. June 18, 2020) (agency liability); *Grasty v. Michail*, 2004 WL 396388 (Del. Super. Ct. Feb. 24, 2004) (veil-piercing and agency liability).

corporate law principles cited by the Insurers were never designed to alter the terms of an insurance policy, let alone restrict or forfeit coverage.

Nor is the dismissal of Aearo's bankruptcy case relevant. That dismissal was based on the bankruptcy court's factual findings that Aearo was not in "financial distress" due to the Earplug Litigation, and therefore did not make a showing of a valid reorganization purpose under the bankruptcy code, due to 3M's ongoing funding of Aearo's defense expenses. A01872. Contrary to Twin City's characterization, the bankruptcy court did not "expressly conclude[] that 3M was not passing along the costs of moral hazard (e.g., defense costs) along [*sic*] to Aearo." Twin City Br. at 20 n.7. The order does not mention "moral hazard" at all. The bankruptcy judge simply concluded that it was unlikely that 3M would stop paying Aearo's defense costs and therefore Aearo could not meet the requirements of Chapter 11. A01873.[8] This ruling does not affect the proper interpretation of the Policies.

[8] Instead of attempting to defend the Superior Court's reasoning, the Insurers attempt to a relitigate the factual issue of Aearo Technologies LLC's payment of more than $400,000 in defense expenses, which was not a basis of the decision below. Though Aearo Technologies LLC submitted unrebutted evidence from its controller that it paid $411,696.70 in legal fees (A00921–A00928), and the Insurers chose not to depose that witness (A04541 ¶¶ 17–18), the Insurers contested whether Aearo made these payments and contended (incorrectly) that Aearo was estopped from presenting such evidence. *See* A03763 & n.6. The Superior Court held that this was a disputed issue of fact that could not be resolved on summary judgment. Ex. A at 17. This Court should not resolve this factual dispute against Aearo and 3M for the first time on appeal.

Finally, the Insurers' unfounded insinuation that 3M is seeking coverage for its own liability in the Earplug Litigation under Aearo's Policies is incorrect. 3M and Aearo spent more than $370 million mounting a joint defense against the Earplug Litigation. The Superior Court did not decide the amount of those defense costs that were attributable to defending Aearo as compared to 3M. Ex. A at 21–22. That issue is currently being litigated in the Superior Court.

II. The Policies Provide Coverage for Losses Above $250,000 Even if Payments by 3M Did Not Satisfy the SIR

The Savings Clauses in each of the Twin City, ACE, and Royal Surplus Policies preserve coverage in instances where the SIR is not paid, so long as the insurer is not responsible for paying the $250,000 in covered losses within the SIR. None of the Insurers' arguments to the contrary is persuasive, especially because—as insurer-drafted language—those provisions must be read expansively in favor of coverage and against the insurer. *See Monzo*, 249 A.3d at 118; *Eli Lilly*, 482 N.E.2d at 470.

A. The Savings Clauses Are Not Limited to Bankruptcy or Insolvency

The Insurers' assertion that the Court should limit the Savings Clauses to the bankruptcy context disregards clear contrary language in the Policies. The Royal Surplus Policy states that if the SIR is "not available or collectible because of (a) the bankruptcy or insolvency of the named insured ***or*** (b) the inability or ***failure for any other reason*** of the named insured to comply with the provisions of the retention endorsement, then this policy should apply … as if such self insured retention were available and collectible." A00976 (End. 28) (emphasis added). Thus, the Savings Clause expressly separates inability to satisfy the SIR due to bankruptcy (subsection (a)), from any other "failure" to satisfy the SIR "for any other reason" (subsection (b)). *Id*. If the Savings Clause were limited to

bankruptcy alone, as Royal Surplus contends, subsection (b) would have no meaning.

The ACE Policy likewise preserves coverage "[i]n the event of bankruptcy or insolvency of any insured, ***or the inability, failure, or refusal to pay*** the "Self Insured Retention," utilizing the disjunctive "or." A05267 (End. 16 § IV.I.1) (emphasis added). Like Royal Surplus, ACE attempts to read the second part of the sentence out of its Savings Clause, which expressly extends the scope of the clause beyond "bankruptcy or "insolvency" to the "failure" or even "refusal" to pay the SIR. ACE's contrary interpretation of the scope of its Savings Clause is contrary to its plain terms, let alone the only reasonable reading.

Royal Surplus and ACE argue that this Court should ignore the bolded and italicized language quoted above because the headings of each of these provisions include the word "bankruptcy." ACE/Royal Br. at 43. But neither heading is limited to the word "bankruptcy." Rather, both headings include language confirming that the provisions are *not* limited to bankruptcy—consistent with the full text of the endorsements.[9]

[9] The Royal Policy provision is titled "Non Drop Down Bankruptcy or Insolvency of the Named Insured," A00976 (End. 28), while the ACE Policy's Savings Clause is titled "Bankruptcy; Payment of Self Insured Retention," A05267 (End. 16 § IV.I.1).

In any case, courts do not interpret headings to override the actual policy language. *See, e.g., Jordan v. Marion Tech. Coll.*,1991 WL 217662, at *2 (Ohio Ct. App. Aug. 15, 1991) ("Section headings in a contract are not binding provisions. They merely guide the reader to certain provisions."); *Comstock Dairy Enters, Inc. v. W. Nat'l Mut. Ins. Co.*, 662 N.W.2d 679 (Wis. Ct. App. 2003) ("Insurance policies should not be construed based on titles or headings."); *Kemper Nat'l Ins. Cos. v. Heaven Hill Distilleries, Inc.*, 82 S.W.3d 869, 873 (Ky. 2002) ("The caption or title of an endorsement cannot override the provisions below it.").

Finally, Twin City fails to address the language in its Savings Clause that expressly extends its scope beyond instances of bankruptcy or insolvency, preserving coverage where the SIR is "invalid, suspended, unenforceable or uncollectable ***for any reason***, *including* bankruptcy or insolvency." A01015 (§ IV.9) (emphasis added). Though Twin City argues earlier in its brief that the word "including" denotes a "broad class" beyond the example provided, *see* Twin City Br. at 22, Twin City conveniently forgets that argument a few pages later when it attempts to read the word "including" out of its Savings Clause. At base, Twin City cannot escape the conclusion that "for any reason" means for any reason, including (but not limited to) bankruptcy or insolvency.

B. Aearo Did "Maintain" the SIR Under the Twin City Policy

Twin City argues that its Savings Clause (which it calls a "Maintenance Clause") does not apply, grasping onto the Superior Court's rationale that Aearo LLC was required to "maintain" the SIR by establishing a separate bank account to pay the SIR. Twin City Br. at 38–39; Ex. A at 16. But nothing in that phrase or the word "maintain" specifies *how* the SIR must be "maintain[ed]," let alone requires that Aearo LLC (the insured under Twin City's Policy) do so by depositing $250,000 in any particular bank account. Rather, the word "maintain" is reasonably construed as being satisfied where a parent or wholly owned subsidiary of the named insured, Aearo LLC, stands ready, willing, and able to furnish "sufficient funds" as needed. *See* Opening Br. at 37–38.

This interpretation is supported by the use of the word "maintain" elsewhere in the Twin City Policy. Specifically, the Policy provides that if a claim or suit is brought against any insured, "You … must … [*m*]*aintain* adequate 'claim' records and supporting data." A01014 (§ IV.5.c.(7)) (emphasis added). Even Twin City cannot reasonably dispute that if 3M "maintain[ed]" these records in its offices on behalf of Aearo LLC, this requirement would still be satisfied.

C. The Savings Clauses Preserve Coverage in Excess of $250,000

The Insurers next argue that even if their Savings Clauses are triggered, their Policies still would not provide coverage above the $250,000 retention. Twin City

Br. at 40–42; ACE/Royal Br. at 42–43. The Insurers' reading is contrary to the policy language and must be rejected.

The Royal Surplus Policy expressly provides that in the event of the "failure" to comply with the retention endorsement "for any other reason," "***this policy should apply*** … as if such self insured retention were available and collectible." A00976 (End. 28) (emphasis added). Ignoring this clear language, Royal Surplus argues—based on the words "Non Drop Down" in its heading—that this provision should be read merely to confirm that its policy "does not 'drop down' below the limit set by the SIR." ACE/Royal Br. at 42. But the reference to "Non Drop Down" in the heading simply confirms that—even when the Savings Clause is triggered and coverage is preserved—Royal Surplus will not pay for the defense expenses from the first dollar to $250,000. The "Non Drop Down" reference in the heading is immaterial here because Aearo only seeks coverage from Royal Surplus for expenses in excess of $250,000 and Royal Surplus is not being asked to "drop down."

Similarly, the ACE Policy provides that ACE will "not be liable under the policy ***to any greater extent than we would have been liable had the*** insured not become bankrupt or insolvent or had such inability, ***failure or refusal not occurred***." A05267 (End. 16 § IV.I.1) (emphasis added). ACE argues that this language somehow does not mean that its policy will remain in force even if the

SIR is not paid by the policyholder. But if failing to pay the SIR relieves ACE of coverage entirely (even when the Savings Clause applies), then ACE's liability could never be "greater" than had the policyholder paid the SIR. In that case, there would be no liability (much less the opportunity for "greater" liability). This language would be entirely superfluous under ACE's reading. Because ACE effectively reads the Savings Clause out of its policy, its interpretation must be rejected. *In re Shorenstein Hays-Nederlander Theatres LLC Appeals*, 213 A.3d 39, 56–57 (Del. 2019).[10]

Twin City, meanwhile, rests its argument on the purported difference between a deductible and an SIR. Twin City Br. at 41. But any differences are irrelevant here because the Savings Clause includes clear language preserving coverage when it is triggered. Similar to the ACE Policy, Twin City's Savings Clause provides that if the SIR is "uncollectable for any reason," Twin City "***shall be liable only to the extent we would have been had such 'self-insured retention' remained in full effect***." A01015 (§ IV.9) (emphasis added). Much like ACE,

[10] Unsurprisingly, ACE does not cite any case law supporting its interpretation given that, to Aearo's knowledge, no court has adopted this reading of the policy language. To the contrary, courts have recognized that this language means exactly what it says. *See Phillips v. Noetic Specialty Ins. Co.*, 919 F. Supp. 2d 1089, 1098 (S.D. Cal. 2013) ("[P]olicy language stating that the insolvency of the insured 'will not increase our obligations under the policy' suggests that [the insurer] has an immediate duty under the policy to indemnify its insured for any losses incurred during the policy period *regardless* of the status of the SIR.") (emphasis in original).

Twin City's interpretation fails to give this policy language any meaning because if failure to pay the SIR would relieve Twin City of its contractual obligations entirely, Twin City would have no liability at all, not only to the same "extent" as had the SIR remained in full effect.

Finally, this Court should reject Twin City's unsupported argument that an SIR amounts to a different layer of primary insurance. Twin City Br. at 34. An SIR is not a separate insurance policy. *See, e.g.*, *Montgomery Ward & Co. v. Imperial Cas. & Indem. Co.*, 81 Cal. App. 4th 356, 370 (2000) ("we see no basis in the insurance contracts, or in applicable law, from which to conclude … SIRs are the equivalent of policies of primary insurance"); *Cone Mills Corp. v. Allstate Ins. Co.*, 443 S.E.2d 357, 360 (N.C. Ct. App. 1994) (an SIR "does not constitute a primary policy"); *William Powell Co. v. OneBeacon Ins. Co*., 162 N.E.3d 927, 943 (Ohio Ct. App. 2020); *Lamorak Ins. Co. v. Kone, Inc.*, 147 N.E.3d 132, 138 (Ill. Ct. App. 2018). Nor does Twin City cite any case law suggesting that this characterization is relevant to the interpretation of the Savings Clauses at issue here.

D. The SIR Payment Provisions Are Not Conditions Precedent

For the reasons stated above, this Court may reverse without reaching the question of whether the Policies' various restrictions on *who* may satisfy the SIR are conditions precedent to coverage. But to the extent that this Court reaches the

issue, those restrictions are not conditions precedent to coverage, the breach of which could result in forfeiture. The Insurers' contrary arguments do not clear the high bar required by both Delaware and Indiana law to read a condition precedent resulting in forfeiture into an insurance policy.

First, ACE and Royal Surplus describe at length other policies that used clear "condition precedent" language in connection with their SIR provisions but cannot point the Court to any similar language in their own Policies. *See* ACE/Royal Br. at 35–39. The ACE Policy promises to pay "those sums that the insured becomes legally obligated to pay as damages … *in excess of the 'Self Insured Retention'*." A05265 (End. 16 § I.I.1.a) (emphasis added). The Royal Surplus Policy states that its "obligation … to pay damages on your behalf applies only to that amount of damages *in excess of the 'Retained Limit*.'" A00981 (End. 33(2)) (emphasis added). This language requires only that the policyholder incur liability in excess of the SIR to trigger ACE's payment obligation, not the exhaustion of the SIR amount by payment (let alone from any particular party).

Neither Policy states that the additional payment restrictions contained in later parts of the Policy (which the Insurers contend details *who* must pay the SIR) are conditions precedent to coverage or are otherwise necessary to trigger the Insurers' payment obligations. *See Lasorte v. Those Certain Underwriters at Lloyd's*, 995 F. Supp. 2d 1134, 1143 (D. Mont. 2014) (holding that while insurer's

liability to pay under the policy was not triggered until SIR "exhausted", the further requirement of payment of the SIR in "cash" was not a condition precedent to coverage; if "the insurer intends to make actual payment in cash of the Self Insured Retention a condition precedent to liability on its policy, then it can include specific language to that effect in the policy"). That other insurers expressly designate their SIR payment restrictions as "condition[s] precedent" undermines rather than supports the Insurers' position. *See, e.g., Walsh*, 72 N.E.3d at 964 (expressly identifying all requirements in separate SIR endorsement as "conditions precedent"). Unlike those insurers, ACE and Royal Surplus did not use the "express[]" or "explicit[]" language required to overcome Delaware and Indiana law's disfavor of conditions precedent. Opening Br. at 33–34 (collecting cases).

Second, unlike the ACE and Royal Surplus Policies, the Twin City insuring agreement states that that its coverage applies only after "damages are in excess of the 'self insured retention' that has been exhausted solely by the payment of 'claim expenses' … ." A01004 (§ I.1.a.); A01017 (§ V.8.a). But this language still does not identify *who* must exhaust the SIR as a condition precedent to coverage, merely that the SIR must be exhausted. The further provision that the SIR cannot be paid by "another" comes later in the Twin City Policy, A01020 (§ V.26.b), with no language tying it to when Twin City pays (or otherwise identifying it as a

condition precedent), let alone providing for forfeiture. Had Twin City intended that further restriction to qualify as a condition precedent that could result in *forfeiture*, it was required to say so. Supp. Br. at 26–27. Having failed to do so, Twin City cannot rely on the SIR to effect a forfeiture of coverage.

ACE and Royal Surplus additionally argue that they are *not* seeking forfeiture as a remedy. ACE/Royal Surplus Br. at 40. But forfeiture of otherwise available coverage is *exactly* what they are seeking here: to deprive Aearo of coverage for losses that otherwise fall squarely within their Policies simply if the SIR was paid by 3M, rather than from a separate bank account maintained by Aearo.

Indeed, that the Insurers are trying to recast their argument as something other than forfeiture tacitly admits that forfeiture is not available to them. The law "abhors forfeiture where to do so would deny the insured the very thing paid for." *Med. Depot, Inc. v. RSUI Indem. Co.*, 2016 WL 5539879, at *11 (Del. Sept. 29, 2016), *abrogated on other grounds by First Solar, Inc. v. Nat'l Union Fire Ins. Co. of Pittsburgh, PA*, 274 A.3d 1006 (Del. 2022). "If the language does not clearly provide for a forfeiture, then a court will construe the agreement to avoid causing one." *Nucor Coatings Corp. v. Precoat Metals Corp.*, 2023 WL 6368316, at *11 (Del. Super. Ct. Aug. 31, 2023). This requirement is taken so seriously that Delaware courts have elevated it to a "public policy against forfeitures of insurance

contracts ….” *Annestella v. Geico Gen. Ins. Co.*, 2015 WL 4400198, at *2 (Del. Super. Ct. June 15, 2015). Indiana law is in accord. *See, e.g., Champlain Cap. Partners, L.P. v. Elway Co., LLP*, 58 N.E.3d 180, 197, 199 (Ind. Ct. App. 2016) (similar).

Thus, the Insurers’ effort to secure the remedy of forfeiture fails under black letter law—regardless whether they mischaracterize their requested relief as something besides forfeiture.

CONCLUSION

Aearo and 3M respectfully request that this Court reverse the Superior Court’s order granting Twin City’s motion for partial summary judgment, reverse the portion of the Superior Court’s order holding that payments by 3M could not satisfy the SIRs of the Royal Surplus and ACE Policies, and remand to the Superior Court for further proceedings.

[Signature on next page.]

OF COUNSEL (*pro hac vice*):

Robin L. Cohen
Kenneth H. Frenchman
Orrie A. Levy
COHEN ZIFFER FRENCHMAN & MCKENNA LLP
1325 Avenue of the Americas
New York, NY 10019
Telephone: (212) 584-1801
rcohen@cohenziffer.com
kfrenchman@cohenziffer.com
olevy@cohenziffer.com

Donald W. Brown
COVINGTON & BURLING LLP
415 Mission Street, Suite 5400
San Francisco, California 94105
Telephone: (415) 591-6000
dwbrown@cov.com

Rani Gupta
COVINGTON & BURLING LLP
3000 El Camino Real, 10th Floor
5 Palo Alto Square
Palo Alto, California 94306
Telephone: (650) 632-4700
rgupta@cov.com

Tyler Weinblatt
COVINGTON & BURLING LLP
One CityCenter
850 Tenth Street NW
Washington, DC 20001
Telephone: (202) 662-6000
tweinblatt@cov.com

Dated: February 28, 2025

Respectfully submitted,

BERGER MCDERMOTT LLP

/s/ David J. Baldwin
David J. Baldwin (No. 1010)
Peter C. McGivney (No. 5779)
1105 North Market Street, 11th Floor
Wilmington, Delaware 19801
Telephone: (302) 655-1140
Facsimile: (302) 655-1131
dbaldwin@bergermcdermott.com
pmcgivney@bergermcdermott.com

Attorneys for Plaintiffs-Below/Appellants

Multi-Case Filing Detail: The document above has been filed and/or served into multiple cases, see the details below including the case number and name.

Transaction Details

Court: DE Supreme Court

Document Type: Reply Brief

Transaction ID: 75741803

Document Title: Appellants' Reply Brief (eserved) (jkh)

Submitted Date & Time: Feb 28 2025 2:49PM

Case Details

Case Number	Case Name
381,2024C	In Re Aearo Technologies LLC Insurance Appeals
423,2024C	In Re Aearo Technologies LLC Insurance Appeals