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IN THE SUPREME COURT OF THE STATE OF DELAWARE

WELLS FARGO BANK, N.A., as Securities Intermediary, and BERKSHIRE HATHAWAY LIFE INSURANCE COMPANY OF NEBRASKA, Defendants/Appellants/Cross-Appellees, v. ESTATE OF PHYLLIS M. MALKIN, Plaintiff/Appellee/Cross-Appellant.	No. 172,2021 Certification of Questions of Law from the United States Court of Appeals for the Eleventh Circuit No. 19-14689 D.C. No. 1:17-cv-23136-MGC

ANSWERING BRIEF OF APPELLEE ESTATE OF PHYLLIS M. MALKIN TO OPENING BRIEF OF APPELLANT BERKSHIRE HATHAWAY LIFE INSURANCE COMPANY OF NEBRASKA

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NATURE OF THE PROCEEDINGS

In 2006, a senior citizen named Phyllis Malkin was victimized by a group of companies called "Coventry," which ran a stranger-originated life insurance ("STOLI") scheme and procured a $4 million life insurance policy (the "Policy") on her life. Coventry later sold the Policy to Berkshire Hathaway Life Insurance Company of America ("Berkshire"), which obtained the Policy's death benefit through its agent, Wells Fargo Bank, N.A. ("Wells Fargo"), upon her death.

In 2017, Ms. Malkin's estate (the "Estate") challenged this STOLI transaction. And in 2019, the United States District Court for the Southern District of Florida entered summary judgment for the Estate and against Berkshire and Wells Fargo, based on an undisputed factual record establishing that the Policy is a void *ab initio*, unconstitutional wager under Delaware's Insurable Interest Statute, 18 *Del. C.* § 2704(a). Ex. E.[1] The District Court also held that notwithstanding any purported affirmative defenses, the Estate is entitled to recover, under 18 *Del. C.* § 2704(b) ("Section 2704(b)"), the proceeds paid to Defendants because this is the chosen remedy in Delaware to ensure that unconstitutional wagers do not pay off. *Id*.

The United States Court of Appeals for the Eleventh Circuit affirmed the District Court in a published, precedential decision, finding as a matter of undisputed

[1] Exhibits A-F are attached to Berkshire's Opening Brief. Exhibit G is attached hereto.

fact and law that the Policy is a void *ab initio* wager. Ex. A. The Eleventh Circuit rejected Defendants' attempts to dispute the facts of this case, including Defendants' efforts to falsely claim (as they still do here) that Ms. Malkin somehow procured the Policy herself. The Eleventh Circuit also sought this Court's guidance on two sub-issues: whether Defendants can assert an affirmative defense under the Uniform Commercial Code ("UCC"), and whether Berkshire can retain from the Policy's death benefit the amount of premium Berkshire paid.

These Certified Questions directly implicate the Delaware Constitution's prohibition on wagers, and this Court's *en banc* 2011 decision in *PHL Variable Ins. Co. v. Price Dawe 2006 Ins. Trust*, 28 A.3d 1059, 1073 (Del. 2011), where this Court made crystal-clear that STOLI is nothing more than a wager on human life that is repugnant to Delaware's public policy and is in direct violation of Article II, Section 17 of Delaware's Constitution. Berkshire and Wells Fargo filed separate opening briefs on July 7, 2021, and three *amicus* briefs were filed on July 14, 2021. Remarkably, none mentions Delaware's Constitution even once.

SUMMARY OF THE ARGUMENT

The Estate responds to Berkshire's argument as follows.

1. Denied. Question 1 asks this Court whether the UCC allows Berkshire to override Section 2704 and cash-in completely on a human life wager that the Delaware Constitution prohibits. The answer must be "no."

First, because Section 2704 enforces Delaware's constitutional prohibition on wagering, it must be applied to all STOLI investors, without exception. Section 2704 works in two ways. If an insurer uncovers an insurable interest issue, it can invalidate the policy under Section 2704(a); but if the insurer pays the policy's benefits, Section 2704(b) deputizes the insured's family to recover those benefits from whoever received them. Thus, Section 2704 enforces the Constitution and protects the public by deterring human life wagers in the first instance and preventing them from coming to fruition when they are uncovered. In this way, Section 2704(b) serves as the final, constitutional backstop against STOLI.

Applying Section 2704(b) to all STOLI investors not only upholds the Constitution, but is consistent with 2704(b)'s plain language, which broadly applies to any "beneficiary, assignee, or other payee," thus plainly encompassing downstream investors. Like the Constitution, Section 2704(b) has no express or implied carve-out for bona fide purchasers. This is because Delaware's Constitution does not allow human life wagers to come to fruition, and no investor's personal

interests are above the public good. Thus, no one can use Delaware's insurance laws to gamble on human life, regardless of their alleged bona fides. The District Court was correct, therefore, to award the Policy's proceeds to the Estate.

Second, contrary to Berkshire's unsupported claim that a UCC Section 8-502 affirmative defense is available in every other context, the black-letter law is that affirmative defenses are typically unavailable for transactions that violate public policy. And, of course, the General Assembly lacks authority to enact legislation leading to unconstitutional results. This is clear from *Price Dawe* where this Court rejected the affirmative defense of incontestability in the face of a human life wager, even though that defense is otherwise mandated by Delaware's Insurance Code. 28 A.3d at 1065-68. Thus, a Section 8-502 defense cannot apply because, if proven, it would require a court to enforce an unconstitutional STOLI wager, which this Court has already held "[a] court may never" do. *Id*. at 1067.

Third, bona fide purchaser defenses only apply in actions to quiet title to actual property with merely voidable title. Section 8-502 requires an "adverse claim" to a "financial asset," narrowly defined as a claim concerning someone's "property interest in a financial asset." Like its common-law equivalents, Section 8-502 does not apply to void *ab initio* "property interests" that never existed. Because *Price Dawe* holds that STOLI transactions are void *ab initio*, no investor has a property interest in STOLI. *Id*. Berkshire attempts to tip-toe around this by claiming the

proceeds of the illegal wager are different than the Policy itself. But this argument lacks any support in law or logic and is undercut by the fact that, at the moment Berkshire claims it became a bona fide purchaser (when it bought the Policy in 2013), the Policy proceeds did not exist.

Fourth, Sections 2704(b) and 8-502 operate harmoniously: Section 2704(b) applies when a policy is void *ab initio* (a nullity) and its enforcement would violate Delaware's Constitution; whereas, Section 8-502 applies when there is a dispute over actual property with voidable title. In this way, both statutes respect legitimate property rights and do not require courts to enforce unconstitutional results. Berkshire, however, seeks a judicial expansion of the UCC beyond its plain terms, in a manner that would render the UCC unconstitutional because, if applied here, it would suddenly have the perverse effect of allowing unconstitutional wagers to pay off. This absurd result could not have been the General Assembly's purpose, nor is the General Assembly authorized to enact any statute, including a UCC provision, that would permit human life wagering. This could only be done with an amendment to the Constitution. And even if Section 8-502 could somehow apply in the context of an unconstitutional wager (it cannot), Section 2704(b) would control because its purpose is constitutional, and it is the more-specific and later-enacted statute with regard to insurable interest—a topic the UCC does not even purport to address.

Finally, even if Section 8-502 were applied here, Berkshire cannot meet the elements of that defense, including because when Berkshire purchased the Policy, it had notice that the Policy had serious insurable interest issues.

2. Denied. Although existing Delaware law concerning restitution in connection with illegal contracts supports the proposition that a party to a void *ab initio* contract can, depending on the facts and circumstances, recover the premiums it paid on a STOLI policy, the estate of a deceased insured is typically not the proper counterparty for such a claim. That claim must instead be pursued against the party with whom the STOLI investor was in contractual privity, which in this case was Coventry. Berkshire already sued Coventry under the contract between them and then settled its dispute, so Berkshire cannot now ask for additional relief against the Estate. Thus, the answer to Question 2 should be "no."

STATEMENT OF THE FACTS

A. The Policy was an illegal wager.

In 2006, two nearly-identical policies were procured on Ms. Malkin's life as illegal wagers through a notorious STOLI program operated by Coventry. Ex. E. The Policy at issue here was procured from American General, and the other STOLI policy on Ms. Malkin was procured from Sun Life.

In 2016, the District Court entered summary judgment in connection with the Sun Life policy, finding as a matter of Delaware law that "Coventry dictated every aspect of the transaction" and that Ms. Malkin "was simply the conduit" through which Coventry, along with a Florida STOLI producer called Simba, procured wagers. *Sun Life v. U.S. Bank*, 2016 WL 161598 (S.D. Fla. Jan. 14, 2016) ("*Sun Life*"). The Eleventh Circuit affirmed that decision in 2017 as "thorough and well-reasoned," declaring that the Sun Life policy was void *ab initio* under this Court's decision in *Price Dawe*. *Sun Life*, 693 Fed. Appx. 838 (11th Cir. 2017).

This case followed later that same year. In 2019, the Estate presented the District Court with a robust, uncontested record, complete with testimony from Simba that laid bare how the Policy was procured as a wager, including:

- Simba's business was "what's called stranger-owned life insurance." B079 ¶ 20 (Dkt. 135); B342 21:7-10 (Dep. P. Shapiro) (Dkt. 135-6).

- Insureds like Ms. Malkin had no ability to make decisions and were "part of the transaction only because [Simba] and [Coventry] were using their

body as the transaction." B082 ¶ 36 (Dkt. 135); B343 36:15-21 (Dep. P. Shapiro) (Dkt. 135-6).

- Simba did not give Ms. Malkin or other insureds full copies of documents, and just had them sign blank "signature pages." B083 ¶ 42 (Dkt. 135); B347-348 ¶ 14 (Statement of L. Bryan) (Dkt. 135-14).

- Before the Policy was even applied for, Coventry—and its captive buyer—received a life expectancy report on Ms. Malkin to assess how quickly she would die. B407 (Dec. 1, 2005 email to "Ken Zinn AIG Group") (Dkt. 135-21).

Berkshire had no contradictory evidence, but attempted to avoid summary judgment by making a string of false factual denials and by openly misstating the law. The District Court saw right through this and not only entered summary judgment for the Estate, finding the Policy was an illegal wager, but repeatedly admonished Berkshire. Ex. E, n.1 ("Berkshire has misused its [summary judgment] Response to 'dispute' virtually every factual point made by the Estate, without regard to whether those points are actually in controversy."); *id*. at 16 (admonishing Berkshire for "an outright misrepresentation of the record and holding in *Sun Life*").

In May 2021, the Eleventh Circuit affirmed the District Court's decision concerning the Policy through a published, precedential opinion finding that Ms. Malkin simply "did not procure the Policy" and that it was instead procured by Simba and Coventry, who "worked together to use the Malkins 'to do indirectly' what Delaware law prohibited them from doing directly." Ex. A at 14, 19.

In this proceeding, Berkshire continues to make the false assertion (Br. 1)[2] that "Ms. Malkin procured the Policy," ignoring not only what the District Court and the Eleventh Circuit held, but also the fact that every other judge analyzing Coventry's STOLI program, including Chief Judge Stark for the District of Delaware, has held as a matter of Delaware law that policies in this program were procured as wagers by Coventry and that the insureds were used merely as instrumentalities. *See, e.g.*, *Sun Life v. U.S. Bank*, 369 F. Supp. 3d 601, 617 (D. Del. 2019), *recon. denied* 2019 WL 2052352 (D. Del. May 9, 2019) ("*Sol*"); *U.S. Bank v. Sun Life*, 2016 WL 8116141 (E.D.N.Y. Aug. 30, 2016) ("*Van de Wetering*"), *R&R adopted by* 2017 WL 347449 (E.D.N.Y. Jan. 24, 2017).

Despite Berkshire's desire to present this Court with its own version of the facts and re-litigate whether the Policy was STOLI, that issue is not part of this proceeding and has already been decided. So the Estate focuses on what is actually at issue, namely whether Berkshire can assert an affirmative defense under Article 8 of the UCC, and thus be permitted to retain the proceeds of a STOLI wager, or whether Berkshire can seek to offset the amount of premiums it paid. The answer to both of these questions is "no."[3]

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[2] "Br." references Berkshire's Opening Brief.

[3] The undisputed facts proving the Policy was an illegal wager are detailed in the Estate's motion for summary judgment and related statement of undisputed facts.

B. When Berkshire bought the Policy, it knew the Policy was potentially STOLI.

The STOLI scheme that generated the Policy was the by-product of a 2001 "Origination Agreement" between Coventry and an American International Group, Inc. ("AIG") entity known as Lavastone, requiring Coventry to "originate" life insurance policies for resale to its captive buyer Lavastone. *Sun Life*, 2016 WL 161598, at *3; B076-B077 ¶¶ 1-8 (Dkt. 135). This is the same "non-recourse premium financing" STOLI scheme at issue in *Lavastone Capital LLC v. Estate of Beverly E. Berland*, Del. Supr. Ct., No. 75, 2021 ("*Berland*"), where Lavastone admitted that its "business rationale" was to "create new policies that . . . we [Lavastone] could [later] purchase." *Berland*, Estate's Ans. Br. 9-10, citing A216. In other words, this was a STOLI scheme. *See Price Dawe*, 28 A.3d at 1070 ("Virtually all jurisdictions . . . prohibit third parties from creating life insurance policies for the benefit of those who have no relationship to the insured. These policies, . . . known as . . . STOLI, lack an insurable interest and are thus an illegal wager on human life. . . . Securitization substantially increased the demand for life settlements, but did not affect the supply side, which remained constrained by a limited number of seniors who had unwanted policies . . . . STOLI promoters sought to solve the supply problem by generating new, high value policies.").

See B072, B440 (Dkt. 135, 138). That record demonstrates how seniors like Ms. Malkin were used as puppets by sophisticated financial entities to create wagers.

Far from being an "innocent" investor with no knowledge of the Coventry-Lavastone STOLI program, *Berkshire was a direct participant* with a significant financing stake in that program. To be sure, Berkshire admitted at deposition that during the mid-2000s, Berkshire [redacted]. B077 ¶ 9 (Dkt. 135); B335-B336 20:16-22:4 (Dep. M. Lawler) (Dkt.135-3). And in a prior matter, Lavastone admitted that Berkshire had actually "partner[ed] with" Lavastone. Ex. G at 341:15-342:6 (Dep. W. Taylor).

Additionally, by the time Berkshire acquired the Policy in 2013, there was extensive publicly-available information revealing that non-recourse premium financing programs like Coventry's were a marker for STOLI, including a well-publicized 2011 federal district court decision finding that a Coventry policy was STOLI. *See Berland*, Estate's Ans. Br. 41-44 (listing examples); *see* Estate's Ans. Br. to Wells Fargo Br. 22-28 (same). And for over a century, the common law has been clear that if an insurance company makes payment on a policy lacking insurable interest, the insured's family has a claim against the investor for the proceeds. *See, e.g.*, *Warnock v. Davis*, 104 U.S. 775 (1881). Since 1968, this has been the clear statutory rule in Delaware, through Section 2704(b).

It was against this backdrop that Berkshire purchased the Policy—*from Coventry itself*—in 2013. By that time, Coventry had placed the Policy in the hands

of one of its affiliates, LST Holdings ("LST"), and Berkshire entered a purchase agreement with Coventry/LST to buy a block of identically-procured policies. Highlighting the fact that Berkshire knew there were insurable interest concerns with the Policy and the others it was buying, Berkshire made Coventry/LST warrant that the policies were not "originated in connection with a STOLI transaction" and to indemnify Berkshire if this was false. A208 (Purchase and Sale Agreement).

Instead of investigating whether this bald claim by Coventry/LST was true, Berkshire admits it [redacted] B338 39:12-40:16 (Dep. M. Lawler) (Dkt.135-3). Berkshire further admits it conducted no due diligence and only [redacted]. B337-B340 33-48 (Dep. M. Lawler) (Dkt.135-3). Remarkably, Berkshire did not even take possession of the Policy file and instead left those documents in Coventry's possession. *Id*. Nor did Berkshire contact Simba, its principal Larry Bryan, or anyone else to ask even a single question. *Id*.

Berkshire applauds itself for its utter lack of diligence, and likes to say (Br. 11) that it also relied on a so-called specialist called Miravast that "detected no insurable-interest issues." But what Berkshire fails to explain is that Miravast was hardly a reliable or independent source, as it was run by the same former AIG/Lavastone employees who had been part of "AIG's Death-Bet Team" and were

themselves directly involved in the illegal origination of the policies Berkshire was buying—a fact Berkshire also knew.[4]

In summary, Berkshire ignored all of what it knew because the deal was too good to pass up. It paid $322,103 to Coventry/LST for the Policy; paid $137,194.20 to American General in premiums; and received $4,013,977.47 from American General (through Wells Fargo) when Ms. Malkin died 15 months later—for a net profit of $3,554,680.27 on Ms. Malkin's death. B098 ¶¶ 143-49 (Dkt. 135). Neither Ms. Malkin nor her family were paid anything.

In November 2017, after this case was commenced, Berkshire and Wells Fargo demanded indemnification from Coventry/LST. Among other things, they admitted that if the Policy was deemed void *ab initio* for lack of insurable interest, then Coventry/LST never had "good, valid and marketable title to [Policy]," "any subsequent property interests therein are similarly void and without effect," and "if a document purportedly conveying a property interest is void, ***it conveys nothing, and a subsequent bona fide purchaser or bona fide encumbrancer for value receives nothing***." B500-B501 ¶¶ 94-96 (Dkt. 146); B004-B005 at 4-5 (Dkt. 52-3); B039-B040 at 4-5 (Dkt. 52-4) (emphasis added). In other words, Berkshire and Wells Fargo admitted—in this case—that once the Policy was deemed void *ab initio*,

[4] *See* L. Scism, *AIG's Death-Bet Team Departs*, Wall S. J. (March 28, 2012), available at https://www.wsj.com/articles/SB10001424052702303404704577309840190718420.

their alleged bona fides would be irrelevant; the Estate would get the proceeds; and Berkshire's and Wells Fargo's only recourse would be against Coventry/LST.

When Coventry/LST refused to indemnify them, Wells Fargo (for itself and Berkshire) filed a third-party complaint against Coventry/LST, and then settled that claim on still-undisclosed terms.

ARGUMENT

I. Certified Question 1

A. Question Presented

If an insurance contract is void under Del. Code Ann. tit. 18, § 2704(a) and *PHL Variable Insurance Company v. Price Dawe 2006 Insurance Trust*, 28 A.3d 1059, 1073 (Del. 2011), is the party being sued under § 2704(b), as a third-party purchaser of the contract and holder of the proceeds, entitled to assert either a bona fide purchaser defense under Del. Code Ann. tit. 6, § 8-502, or a securities intermediary defense under Del. Code Ann. tit. 6, § 8-115?

B. Scope of Review

Question 1 presents an issue of statutory interpretation that this Court reviews *de novo*. *Price Dawe*, 28 A.3d at 1064.

C. Merits of Argument

The scourge of using life insurance to wager on strangers has been a problem for centuries, but peaked in the mid-2000s, when the securitization of high-value life insurance by investors substantially increased demand for policies insuring senior citizens. *Price Dawe*, 28 A.3d at 1070. Because the supply of valid policies was "constrained by a limited number of seniors who had unwanted policies of sufficiently high value," "STOLI promoters sought to solve the supply problem by generating new, high value policies" on the lives of seniors. *Id*. The result was

exactly what we see here: a policy created by and for strangers with no relationship to the insured, meant to end up in the hands of institutional investors like Berkshire.

STOLI, however, is a form of human life wagering that "harm[s] the public," is "a fraud on the court," and is prohibited by Delaware's Constitution. *Id.* at 1068-71. Thus, *Price Dawe's* core holding is that because human life wagering violates Delaware's Constitution, the Insurable Interest Statute, Section 2704, cannot be interpreted to allow STOLI policies to come to fruition. *Id.* at 1070-71, 1077-78.

The holding of *Price Dawe* dictates the result here: No provision of Delaware law can be interpreted to allow investors to cash-in on STOLI because doing so would allow an illegal wager to pay off, which would violate Delaware's Constitution and public policy. Accordingly, the private interests of any particular party are irrelevant. What matters is upholding Delaware's Constitution and public policy, even if that means the outcome may be unprofitable for STOLI investors like Berkshire. Thus, the answer to Question 1 must be "no."

1. Applying Section 2704(b) as written prevents unconstitutional human life wagers from coming to fruition.

In *Price Dawe*, this Court provided the Constitution-based analysis that must also be applied to Question 1 here. Specifically, the Court held that Article II, Section 17 of the "Delaware Constitution prohibits all forms of gambling unless it falls within one of the enumerated exceptions" and that "a life insurance policy procured or effected without an insurable interest is a wager on the life of the insured

the Delaware Constitution prohibits." 28 A.3d. at 1070-71. Thus, this Court held that it could not interpret any statute as permitting the very wagers the Constitution forbids, and any statute that could be read as allowing wagers is rendered ambiguous because it would create an absurd result not intended by the General Assembly. *Id*. at 1070 ("The plain language of 18 *Del. C.* § 2704(a) is ambiguous because a literal reading of the statute would permit wagering contracts, which are prohibited by the Delaware Constitution."); *id*. at 1071 ("Because a literal reading of the statute creates an absurd result not contemplated by the General Assembly, we must interpret the statute in conformity with both Delaware law and the General Assembly's intent.").

The same analytical framework controls here, meaning Section 2704(b) must be read as upholding the Constitution's prohibition on wagering, without exception. *See Op. of Justices*, 385 A.2d 695, 701 (Del. 1978). This is not difficult to do because the plain language of Section 2704(b) acts as a constitutional backstop that prevents the ultimate culmination of human life wagers by deputizing families to "recover . . . any benefits" paid under a STOLI policy from any "beneficiary, assignee, or other payee," or put differently, from "the person so receiving them." 18 *Del. C.* 2704(b). Consistent with Article II, Section 17 of Delaware's Constitution, Section 2704(b) does not contain any exception for downstream

purchasers of STOLI policies.[5] Thus, by its unequivocal terms, Section 2704(b) comports with the Constitution and precludes all strangers, without exception, from cashing-in on unconstitutional STOLI wagers.[6]

Section 2704(b) also comports with the common law it codified, which itself upholds the Constitution's ban on human life wagers. *See Price Dawe*, 28 A.3d. at 1073, n.59 (holding Section 2704 is founded on *Warnock*, 104 U.S. at 775, *Grigsby v. Russell*, 222 U.S. 149, 155 (1911), and *Balt. Life Ins. Co. v. Floyd*, 91 A. 653 (Del. 1914)). Under that common law, when a policy is procured as a wager, the entire transaction is void. *Floyd*, 91 A. at 656. So when investors like Berkshire buy policies on the lives of strangers, they do so knowing that if the policy was a wager to begin with, the assignment through which they received it is likewise void, and they have no rights to the policy or its proceeds. *See Grigsby*, 222 U.S. at 155.

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[5] The Act that amended the Delaware Insurance Code in 1968 (and enacted Section 2704(b)) states that it supersedes all prior law to the extent inconsistent, which would include the UCC bona fide purchaser defenses enacted in 1966. 56 Del. Laws c. 380, § 11 (1968); 55 Del. Laws c. 349, § 8-302 (1966). Moreover, the General Assembly's failure to provide a bona fide purchaser defense in Section 2704 appears intentional insofar as it *did* provide for such a defense in other parts of the very same Act amending the Insurance Code. *Compare* 56 Del. Laws c. 380, § 2704(b) (1968) (no exception for bona fide buyer), *with id.* § 5925(c) ("bona fide holder for value" defense available in connection with certain "voidable transfers").

[6] "The Delaware Constitution of 1897 contained a general prohibition against gambling. In 1973, Article II was amended to permit, among other exceptions, a state-operated Lottery." *Palese v. Del. Lottery Office*, 2006 WL 1875915, at *9 (Del. Ch. June 29, 2006). Had an exception been intended for downstream STOLI investors, it would appear in the Constitution. Because it does not, one cannot be implied.

Indeed, the longstanding majority rule is that if an insurer pays out the proceeds of a wagering policy, that money must be paid over to the insured's family so that, no matter what, the wager does not pay off. *Warnock*, 104 U.S. at 779-81. And even though *validly-procured* policies have been freely assignable at common law for over a hundred years, there was and is no exception at common law excusing downstream buyers from this rule or permitting them to retain wagering proceeds. *See Price Dawe*, 28 A.3d at 1072-73 ("The tenets of statutory construction require us to interpret statutes consistent with the common law unless the statutory language clearly and explicitly expresses an intent to abrogate the common law.").

Delaware is not alone on this issue. It is one of 29 states with a recovery statute like Section 2704(b), and consistent with the common law these statutes codify, the goal everywhere is the same: Deter STOLI from being created in the future and prevent already-made human life wagers from coming to fruition.[7] *See, e.g.*, *Beard v. Am. Agency Life Ins. Co*., 550 A.2d 677, 686 n.3 (Md. Ct. App. 1988) (identical Maryland statute is a "sanction to be imposed"); *Cundiff v. Cain*, 707 So.2d 187, 190 (Miss. 1998) (where policy lacks insurable interest, "[f]or all intents and purposes, there was no beneficiary at the time of [the insured's] death and the proceeds of the policy rightfully belong to his estate"); *Froiland v. Tritle*, 484

[7] *See* A529-30 (collecting statutes).

N.W.2d 310, 313 (S.D. 1992) (similar); *Tillman v. Camelot Music*, 2005 WL 3436484, at *2-5 (N.D. Okla. Dec. 14, 2005) (similar).

And applying Section 2704(b) to any "assignee" or "payee"—as the statute requires and the Constitution compels—is also consistent with the Insurable Interest Statute's overall purpose of "preventing speculation on human life." *Price Dawe*, 28 A.3d at 1074. No one disputes that Section 2704(b) does this by deterring STOLI from being created and preventing human life wagers from paying off. The District Court recognized this.[8] Judge Bibas's Certification Order in *Berland* recognized this.[9] And the *amici* recognize it too.[10]

This Court has repeatedly held that "[it] is not the function of a court to read into, or carve out, exceptions to a clearly-worded legislative or regulatory

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[8] Ex. E at 21-22 ("*Price Dawe* all but answers the question before this Court. While that case did not involve the specific statutory provision at issue here, the text of subsection (b) is entirely aligned with the spirit of *Price Dawe*. At its core, *Price Dawe* reaffirmed the unsavory truth about STOLI policies: they are nothing more or less than a bet on when a stranger will die. ***Price Dawe held that in Delaware, at least, such bets never pay off.*** Subsection (b) put that promise into effect under the circumstances presented here. . . . The provision makes no exception for 'payee[s]' who are bona fide purchasers, and this Court does not believe that the Delaware Supreme Court would fashion such an exception if given the opportunity. Based on *Price Dawe*, it appears that Delaware's highest court would hold that subsection (b) means exactly what it says: as between the insured's loved ones and the strangers who sought to profit from her death, the former have the better claim to the insurance money, regardless of the latter's status under the UCC.") (emphasis added).

[9] Ex. F at 4 ("Section 2704(b) ensures that a gamble made in violation of §2704(a) ***never pays off***.") (emphasis added).

[10] *E.g.*, Del. Banker's Ass'n. Br. 20.

enactment." *State Farm Mut. Auto. Ins. Co. v. Mundorf*, 659 A.2d 215, 220 (Del. 1995). And carving-out an exception from Section 2704(b) for downstream investors would frustrate the statute because, as this Court previously recognized, STOLI is created to meet the "demand" of downstream investors. *Price Dawe*, 28 A.3d at 1070 (noting that "STOLI promoters" create STOLI so that it can be "securitized and sold to investors"). By the time STOLI policies mature (and Section 2704(b) is triggered), they are naturally owned by the very downstream investors whose appetite drove their creation in the first place. Affording those investors complete immunity from Section 2704(b) would effectively mean that any STOLI policy not challenged by the insurer (which is most of them) would be allowed to come to fruition, which would send a clear message to STOLI promoters to target Delaware's markets with the next round of STOLI schemes.

Accordingly, the answer to Question 1 is already provided by *Price Dawe* and dictated by the Delaware Constitution: In no event can any stranger investor keep the proceeds of a human life wager because this would violate the Constitution and public policy. Any contrary holding would: (i) contravene Article 17, Section II of the Constitution by allowing a certain class of investors to make good on an unconstitutional wager, despite there being no such exception in the Constitution; (ii) effectively overturn *Price Dawe* by allowing courts to enforce human life wagers

and allow them to come to fruition; and (iii) re-write Section 2704(b)'s plain language to create an exception that does not exist and violates the Constitution.

To answer "no" to Question 1, this Court need only apply Section 2704(b) the same way it applied Section 2704(a) in *Price Dawe*—by rejecting any interpretation that would allow unconstitutional wagering. 28 A.3d at 1070-71; *see also Sun Life v. Wells Fargo*, 208 A.3d 839, 849 (N.J. 2019) ("*Bergman*") (citing *Price Dawe* and holding that under New Jersey law, "the insurable interest requirement is consistent with and helps enforce the Constitution's prohibition on gambling. By ensuring full compliance with the insurable interest statute, we can avoid an outcome that might run afoul of the Constitution.").

2. Section 8-502 cannot be interpreted to allow unconstitutional human life wagers to stand.

Remarkably, Berkshire's Brief never once mentions Delaware's Constitution, nor does Berkshire attempt to explain how a statute like Section 8-502 of the UCC—a generic statute with no specific application to life insurance—could possibly be used to enforce transactions the Constitution forbids. Instead, Berkshire argues (Br. 15, 28) that Section 2704(b) is "presumptively subject to defenses like that provided in Section 8-502" because affirmative defenses are, according to Berkshire, always available. This argument fails for two important reasons.

First, setting aside that there is no evidence that the General Assembly intended Section 8-502 to create an exception to the Constitution's wagering

prohibition, even if that had been its intent, it would have been meaningless because the General Assembly does not have the authority to enact unconstitutional legislation. *See Op. of Justices*, 385 A.2d at 707 (striking-down statute permitting wagering on jai-alai games as "an unconstitutional" violation of the Constitution's wagering prohibition). Section 8-502 cannot, therefore, be read as creating a wagering exception for any class of investor because doing so would lead to the same absurd result rejected in *Price Dawe*, namely that wagering would be permitted to pay off. *See Hazout v. Ting*, 134 A.3d 274, 278 (Del. 2016) ("[I]it is our obligation to give effect to the plain language of statutes to the extent we can do so without offending any supervening constitutional limits.").

Second, this Court has long held that many types of affirmative defenses cannot be invoked in connection with illegal or void subjects that violate public policy. *See*, *e.g.*, *Waggoner v. Laster*, 581 A.2d 1127, 1137 (Del. 1990) (estoppel inapplicable to void contract); *In re HealthSouth Corp. Shareholders Litig.*, 845 A.2d 1096, 1108 (Del. Ch. 2003), *aff'd* 847 A.2d 1121 (Del. 2004) ("Like its equitable counterpart the unclean hands doctrine, the *in pari delicto* defense will not be applied when its acceptance would contravene an important public policy.").

Thus, in *Price Dawe*, this Court rejected the same kind of argument Berkshire makes here by holding that an *otherwise effective* affirmative defense is *completely ineffective* against an unconstitutional policy void *ab initio* for lack of insurable

interest. 28 A.3d at 1064-68. There, the affirmative defense was based on Delaware's statutory requirement that all life policies contain an incontestability clause, preventing an insurer from contesting the "validity of a policy" after two years. *Id*. (citing 18 *Del. C.* § 2917). Notwithstanding that an incontestability defense is available in connection with merely voidable policies, this Court held that for void *ab initio* unconstitutional wagers, the defense does not exist and an insurer can challenge the validity of a policy for insurable interest reasons at any time. *Id*.

In fact, this is exactly what every single judge applying Delaware law has done post-*Price Dawe* when presented with affirmative defenses that might otherwise lead to the enforcement of a STOLI wager. *See, e.g.*, *Sun Life*, 2016 WL 161598 at 19-21 (as a matter of Delaware law STOLI investor could not recover death benefit through defenses such as misrepresentation, breach of contract, release, waiver, estoppel, ratification, unclean hands, and *in pari delicto*), *aff'd*, 693 Fed. Appx. 838, 840 (11th Cir. 2017); *Van de Wetering*, 2016 WL 8116141, at *19-20 (same), *adopted by* 2017 WL 347449 (E.D.N.Y. Jan. 24, 2017); *Sun Life v. Wilmington Trust*, 2018 WL 3805740 (Del. Super. Ct. Aug. 9, 2018) ("*De Bourbon*") (striking defenses of waiver, estoppel, and unclean hands); *Columbus Life v. Wilmington Trust*, 2021 WL 537117, at *6-10 (Del. Super. Ct. Feb. 15, 2021) ("*Kluener*") (striking defenses of estoppel, misrepresentation, unclean hands, and *in*

pari delicto); *Columbus Life v. Wells Fargo*, 2021 WL 106919, at *4-6 (D. Del. Jan. 12, 2021) ("*Snyder*") (striking defenses of estoppel, waiver, and unclean hands).[11/12]

The common rationale of these decisions is that investors are not allowed to have STOLI benefits, no matter their "innocence," and using affirmative defenses to avoid this rule "is, under the reasoning of *Price Dawe*, essentially the same thing as enforcing the policy, which the Delaware Supreme Court says courts cannot do" because it violates the Constitution. *Snyder*, 2021 WL 106919, at *16; *see also Sun Life*, 2016 WL 161598, at *20 ("Here, the immense public policy against wagering contracts clearly trumps any possible application of [unclean hands and *in pari delicto*]"); *Van de Wetering*, 2016 WL 8116141, at *19 (estoppel, ratification, *in pari delicto*, and unclean hands defenses "fail as a matter of law as they are inapplicable to a STOLI policy which has been declared void *ab initio*"); Ex. E at 20 ("As the Estate contends, the statute appears on its face to preclude[ ]—*without exception and*

[11] *See also Sol*, 369 F. Supp. 3d at 617 (declaring STOLI policy void *ab initio* notwithstanding investor's affirmative defenses); Proposed Jury Instr., *Sol*, 2019 WL 8353393, ECF 241 (investor requesting jury instruction on affirmative defenses), *with* Final Jury Instr., *Sol*, 2019 WL 8353393, ECF 267 (refusing jury instruction on affirmative defenses).

[12] Courts applying the law of other jurisdictions are in accord. *See, e.g.*, *Warnock*, 104 U.S. at 781-82 (rejecting investor's affirmative defenses and awarding STOLI policy proceeds to insured's estate despite contractual release and waiver from insured); *Bergman*, 208 A.3d at 846 (citing *Price Dawe* and rejecting incontestability defense); *Beard*, 550 A.2d at 688 (rejecting affirmative defenses of waiver, estoppel, and incontestability to illegal wagering policy).

as a matter of public policy—STOLI investors from retaining the death benefit of a life insurance policy manufactured through a STOLI scheme.").

Respectfully, the Delaware Constitution and well-settled statutory interpretation principles preclude any finding that the UCC provides an exception allowing human life wagers to pay off in Delaware. Indeed, if an incontestability clause mandated by the Insurance Code itself cannot protect STOLI investors, then a generic statute like the UCC cannot provide cover either. Holding otherwise would render Section 8-502 ambiguous and unconstitutional—a result that must be avoided. *See Terex Corp. v. S. Track & Pump, Inc*., 117 A.3d 537, 549 (Del. 2015) ("[W]here a possible infringement of a constitutional guarantee exists, the interpreting court should strive to construe the legislative intent so as to avoid unnecessary constitutional infirmities.").[13]

3. Bona fide purchaser defenses only apply to title disputes over property with merely voidable title, which is obvious from Section 8-502's own terms.

Delaware's constitutional prohibition on wagering compels this Court to decline Berkshire's invitation to interpret Section 8-502 as allowing certain unconstitutional wagers to pay off. The answer to Question 1 must be "no," and the

[13] The only Delaware case Berkshire cites to support its idea that affirmative defenses "presumptively apply" is a dog-bite case where the owner was permitted to assert that his veterinarian assumed the risk. Br. 28 (citing *Brady v. White*, 2006 WL 2790914, at *4 (Del. Super. Ct. Sept. 27, 2006). While troubling, dog bites are not unconstitutional, and *Brady* does nothing to advance Berkshire's position.

analysis need proceed no farther. Regardless, Berkshire's efforts to invoke a bona fide purchaser defense also fail under the plain language of Section 8-502.

The bona fide purchaser defense, whether under common law or UCC, only applies in title disputes over actual property with voidable title, not title that is deemed never to have come into existence. 77 Am. Jur. 2d Vendor & Purchaser § 361 ("Status as a bona fide purchaser is an affirmative defense to a title dispute. Accordingly, the defense of bona fide purchaser for value can be maintained only in favor of a title, though it may be defective, which a bona fide purchaser has, and it is not available for the purpose of creating a title."); *Taylor v. Just*, 59 P.3d 308, 313 (Idaho 2002) ("The doctrine of good faith purchaser for value is available to protect title obtained, not to acquire title."); *Madison v. Gordon*, 39 S.W.3d 604, 606 (Tex. 2001) ("Status as a bona fide purchaser is an affirmative defense to a title dispute.").

Indeed, counsel is not aware of *a single case* in the entire country where the bona fide purchase doctrine has been applied to rights allegedly springing from instruments so fundamentally flawed that they are deemed void *ab initio*. On the contrary, other UCC provisions provide that the bona fide purchaser concept only applies to claims about property with "voidable title." 6 *Del. C.* § 2-403 ("A person with voidable title has power to transfer a good title to a good faith purchaser for value."). This is consistent with the universal common law rule that when an instrument is void *ab initio*, even a truly innocent purchaser for value has nothing to

enforce. *See Faraone v. Kenyon* 2004 WL 550745, at *5-11 (Del. Ch. Mar. 15, 2004) (rejecting bona fide purchaser defense raised by lender where son tricked mother into signing a void *ab initio* deed to her home, procured a mortgage secured by a lien on the home, and squandered the proceeds, executor of mother's estate was entitled to restore title to the home without the lien because deed was *not* merely voidable).

When a grantor has no power to convey title because it is void *ab initio*, "it is immaterial whether the purchaser was a bona fide purchaser or not. In other words, if a document purportedly conveying a property interest is deemed void, it conveys nothing, and a subsequent bona fide purchaser or bona fide encumbrancer for value receives nothing." 77 Am. Jur. 2d Vendor & Purchaser § 363; *Trout v. Taylor*, 32 P.2d 968, 970 (Cal. 1934) ("[A]n instrument wholly void . . . cannot be made the foundation of a good title even under the equitable doctrine of bona fide purchase[r]."); *Kinwood Capital v. BankPlus*, 614 F.3d 140, 144 (5th Cir. 2010) (forged conveyance "is void *ab initio* and cannot pass title to a bona fide purchaser," whereas a fraudulent conveyance is merely voidable and thus "subject to the intervening rights of a bona fide purchaser for value without notice of the fraud").

Every court that has ever considered a bona fide purchaser defense in connection with a STOLI policy has, therefore, rejected it. *See, e.g.*, *Sun Life v. Conestoga Tr. Servs.*, 263 F. Supp. 3d 695, 703 (E.D. Tenn. 2017) (rejecting STOLI

investor's "innocent bona fide assignee" argument, holding "transferee's innocence or good faith will not revive a contract void from inception as an illegal wagering contract"); *Pruco Life Ins. Co. v. Brasner*, 2011 WL 13117063, at *10 (S.D. Fla. Nov. 14, 2011) ("[T]he bona fide purchaser for value defense fails because the policy is void *ab initio*," so that it "never [went] into effect" and the purported purchaser "never took valid title."), *vacated on other grounds sub nom*, *Pruco Life Ins. Co. v. Wells Fargo*, 846 F.3d 1188 (11th Cir. 2017).

This is another insurmountable problem for both Defendants because they admitted, when they wrote to Coventry to demand indemnification, that "***if a document purportedly conveying a property interest is void, it conveys nothing, and a subsequent bona fide purchaser or bona fide encumbrancer for value receives nothing***." B500-B501 ¶¶ 94-96 (Dkt. 146); B004-B005 at 4-5 (Dkt. 52-3); B039-B040 at 4-5 (Dkt. 52-4) (Dkt. 52-4) (emphasis added). Moreover, Defendants admitted that if the Policy was void *ab initio*:

> [A]ny subsequent property interests therein are similarly void and without effect. Simply stated, at no time did LST have good, valid and marketable title to [the Policy and] LST actually had nothing to convey, and any purported property interest is and was void.

Id.

Defendants were correct then, and their arguments to the contrary now cannot be accepted. Not only is it clear from the common law and other UCC provisions

that bona fide purchaser defenses cannot apply in the face of illegal, void *ab initio* "assets," but this is also self-evident from Section 8-502's plain language, which merely provides protection from an "*adverse claim* to a *financial asset* . . . against a person who acquires a *security entitlement* under Section 8-501 for value and without notice of the adverse claim." 6 *Del. C.* § 8-502 (emphasis added).

"Adverse claims" are limited to situations where a claimant asserts a "*property interest* in a financial asset" and that its "*rights*" in that property were violated. 6 *Del. C.* § 8-102(a)(1) (emphasis added). Stated differently, "adverse claims" are claims about title to "property" where a claimant contends it has enforceable property "rights." *Id.* § 8-502 cmt. 1. Section 8-502 does not even suggest that it provides coverage over void *ab initio* property, or non-existent rights springing from void *ab initio* instruments, and reading it as such would expand the statute beyond comprehension. *See* 7 Hawkland UCC Series § 8-102:8 ("The concept of adverse claim is not, however, so broad as to reach all forms of assertions that a person acted wrongfully in transferring securities or other financial assets. *The first question that must be asked is whether the person asserting the claim has a property interest. That issue is determined under law other than Article 8.*") (emphasis added). Here, the "law other than Article 8" is the Delaware Constitution and *Price Dawe*, which clarifies that STOLI policies are unconstitutional, "harm the

public," are "a fraud on the court," and are "so egregiously flawed that they are void at the outset"—such that "a court may never enforce" them. 28 A.3d at 1067-68.

Likewise, to have a "financial asset" or a "security entitlement," Berkshire had to actually acquire "rights and property interests" in existing property. 7 Hawkland UCC Series § 8-102(a)(9), (17). Because STOLI policies violate Delaware's Constitution and public policy, they are a "nullity," meaning they "never came into existence." *Price Dawe*, 28 A.3d. at 1064-65. And because the Policy never existed, neither it nor its future proceeds could be "financial assets" or form the bases of a "security entitlement," rendering Section 8-502 inapplicable by its own terms.[13]

[13] Berkshire admits (Br. 24) that because no one could be a bona fide purchaser of a void *ab initio* STOLI policy, it had "no contractual right to have [American General] pay the [P]olicy's death benefit upon Ms. Malkin's death" and that it would not have had a UCC defense had American General challenged the Policy under Section 2704(a). Yet Berkshire claims (Br. 4, 5, 18) the UCC does somehow supply a defense to a Section 2704(b) claim because it supposedly bought the Policy's *proceeds* in 2013, and thus it is "*irrelevant*" that the Policy is void *ab initio*. This argument is pure form over substance. It is undeniable that Berkshire purchased the Policy in 2013; thus, at the moment Berkshire claims to have become a bona fide purchaser, the Policy proceeds did not even exist. Further, although Berkshire also purchased whatever rights Coventry/LST purported to have to the future death benefit, that purchase was itself a nullity because Coventry/LST had no rights to convey. And, of course, there is no authority making a distinction between a void *ab initio* contract and its fruits, and the case law rejects this novel argument. *See*, *e.g.*, *Faraone*, 2004 WL 550745, at *5-11. Regardless, this form-over-substance argument also ignores the reality that the end-game of a STOLI wager is the policy proceeds, and allowing Berkshire to keep the proceeds of the Policy would clearly violate the Constitution. *See Price Dawe*, 28 A.3d at 1071 (rejecting argument that

Against this stark legal backdrop, Berkshire and the *amici* argue that answering "no" to the first certified question will upset investors' commercial expectations and "breed uncertainty in the market," which would cause a "ripple effect" that would "extend far beyond the life-settlement industry, causing uncertainties and inefficiencies in Delaware's financial markets and casting doubt regarding Delaware's leading role in the U.S. financial services industry." Br. 32; Del. Banker's Ass'n. Br. 3. Respectfully, not only are these fear-mongering arguments wrong, they fundamentally misconstrue the narrow scope of the questions before this Court and ignore the fact that this Court's role is *not* to "rewrite[e] [a] statute to fit a particular policy position" of a litigant. *Taylor v. Diamond State Port Corp.*, 14 A.3d 536, 542 (Del. 2011).

Indeed, there is broad consensus that STOLI policies are not a legitimate part of the investor market. *See Price Dawe*, 28 A.3d at 1069-70. Investors like Berkshire choosing to invest in the market's illegitimate underbelly have known from the beginning that policies procured through non-recourse premium finance schemes like Coventry's were highly risky; that the proceeds of those human life wagers were subject to recovery by families under Section 2704(b); and that they

"would result in an illogical triumph of form over substance that would completely undermine the policy goals behind the insurable interest requirement").

needed to factor these risks into their purchase price.[14] Thus, answering "no" to the first certified question will not *upset* investors' expectation—it will *fulfill* them.

Nor is there any risk of "ripple effects" to legitimate markets or the financial system more generally. Not only is STOLI illegal (because it works a private harm), and not only is STOLI void *ab initio* (because it "harms the public"), but the most salient attribute of STOLI in Delaware is that it is unconstitutional. To answer "no" to the first certified question, this Court need only hold—consistent with *Price Dawe*—that Section 8-502 does not allow any stranger to retain STOLI proceeds because doing so would allow a Delaware human life wager to come to fruition, a result forbidden by Delaware's Constitution. This narrow holding would protect Delaware's strong stance against human life wagering without threat to any market other than the illegitimate market for unconstitutional wagers.[15]

4. There is no conflict between Sections 2704(b) and 8-502, but even if there were, Section 2704(b) would control because it is later-enacted and more specific.

Contrary to Berkshire's suggestion that enforcing Section 2704(b) as written creates a conflict with Section 8-502, these statutes apply in opposite situations. To

[14] *See, supra*, at 11-12; Estate's Ans. to Wells Fargo Br. at 22-28; *Berland*, Estate's Ans. to Amicus Br. 9-15 (citing sources).

[15] The Banker's Association argues that because goods acquired from a thief or a fraudulent fiduciary may be protected by Section 8-502, STOLI proceeds should be too. Del. Banker's Ass'n. Br. 10. This argument is irrelevant; although illegal, stealing and fiduciary fraud do not violate Delaware's Constitution like STOLI does.

be applicable, Section 2704(b) requires a finding that a policy is an unconstitutional, void *ab initio* wager, in which case Section 8-502 does not provide a defense. If a policy is found to have insurable interest, however, Section 8-502 would provide a defense to a title dispute regarding a merely voidable policy.

Assuming *arguendo* that Section 8-502 could apply in a STOLI case (it cannot), and further assuming Section 8-502 conflicted with Section 2704(b), Section 2704(b) nevertheless controls because it is obviously the more specific statute on insurable interest and was passed *after* Delaware adopted the bona fide purchaser rules in UCC Article 8. *State v. Fletcher*, 974 A.2d 188, 193 (Del. 2009) ("[T]he expression of legislative intent in a more specific and later-enacted statute controls the former, more general statute.").

Berkshire attempts to invoke *Fletcher* in its favor (Br. 30-31), but fails to argue that Section 8-502 is "more specific" than Section 2704 on any "common subject matter," let alone insurable interest issues. Nor could it, as the UCC is a general statute with no bearing on life insurance, whereas that is all Section 2704 is about. And, in any event, an essentially identical bona fide purchaser rule has been part of Article 8 of Delaware's UCC since 1966, two years before Section 2704(b) was enacted in 1968.[16] A544 (1966 UCC). *Supra*, at n.5.

[16] Moreover, as noted *supra*, at n.5, when the General Assembly passed the Act rewriting the Delaware Insurance Code (including Section 2704), it enacted

5. Even if Section 8-502 provides an affirmative defense, Berkshire cannot meet its burden of proof.

"[T]he cases are virtually unanimous in concluding that a party claiming the benefit of the status of a bona fide purchaser under Article 8 of the UCC . . . bears the burden of proving that he acted without notice and in good faith." *Oscar Gruss & Son v. First State Bank*, 582 F.2d 424, 433 (7th Cir. 1978); *Marsh v. Marsh*, 261 A.2d 540, 542 (Del. Ch. 1970) (same under common law). Berkshire consistently took the position below that it would have had notice—and thus no UCC defense—if Berkshire had "*notice of a potential insurable interest problem*" with the Policy when it bought it in 2013. A392 (emphasis added). The facts establish that Berkshire had this level of notice—and much more.

Among other things, Berkshire was directly involved with the Coventry/Lavastone STOLI scheme for years and knew full-well how and why Coventry was procuring policies on strangers. By 2013, when Berkshire bought the Policy, Berkshire (and the entire market) was on notice that non-recourse premium finance deals like Coventry's were markers for STOLI, and that at least one court had already declared a nearly-identical Coventry policy to be STOLI. And, of course, Berkshire obviously knew the Policy had insurable interest problems

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provisions making exceptions for bona fide holders; thus, the decision to omit such a carve out in Section 2704(b) was intentional and should be respected.

because it made Coventry/LST represent in its 2013 purchase agreement that if the Policy was STOLI, Coventry/LST would indemnify Berkshire. *Supra*, at 12.

No rational factfinder could conclude that Berkshire was a bona fide purchaser, including because Berkshire knew it was buying a block of policies that had "insurable interest problems" but didn't care because the potential reward was worth the risk of being caught.[17] *See SEC v. Credit Bancorp*, 386 F.3d 438, 451-52 (2d Cir. 2004) (securities intermediary had notice, and was not bona fide purchaser under Article 8, where its agents saw press releases but failed to conduct investigation).

[17] Berkshire suggests that if this Court holds that the UCC provides a *possible* defense, it should also find as a matter of fact that Berkshire proved this defense. Not so. Berkshire did not even plead its UCC defense until after fact discovery closed. So even if Section 8-502 is somehow interpreted to provide a *possible* defense (and it should not be), the Estate would be entitled to discovery to uncover even more evidence establishing that Berkshire cannot meet its burden of proof.

II. Certified Question 2

A. Question Presented

If an insurance contract is void under Del. Code Ann. tit. 18, § 2704(a) and *PHL Variable Insurance Co. v. Price Dawe 2006 Insurance Trust, ex rel. Christiana Bank & Trust Co.*, 28 A.3d 1059, 1073 (Del. 2011), can the party that is being sued under § 2704(b) recover premiums it paid on the void contract?

B. Scope of Review

Question 2 presents an issue of statutory interpretation that this Court reviews *de novo*. *Price Dawe*, 28 A.3d at 1064.

C. Merits of Argument

Under basic principles of Delaware law, a STOLI investor may pursue a restitution claim against an appropriate defendant in an appropriate case. The Estate, however, is not such a defendant, nor is this such a case. Here, Berkshire conferred benefits on Coventry, sued Coventry for indemnification, and reached a confidential settlement. Berkshire's legal claim to recover expenses was against Coventry, not the Estate. This result is consistent with Section 2704(b)'s language, principles of equity, and Delaware's constitutional interest in deterring human life wagers.

1. An investor in Berkshire's position has a restitution claim, but only against the party with whom it was in contractual privity.

As Berkshire explains (Br. 40-41), in the context of insurable interest claims between a life insurance company and a STOLI investor where those litigants are

"contractual counterparties" (albeit under a void contract), certain Delaware courts have recognized that a STOLI investor can seek to prove an entitlement to restitution from the insurer for the premiums that the investor paid towards a STOLI policy.

But even in that context, the Superior Court has correctly rejected the argument that downstream STOLI investors are *automatically* entitled to a premium refund upon a STOLI finding, and has instead held that a STOLI investor seeking a refund of the premium it paid must prove the exception set forth at Restatement (Second) Contracts § 198. *Brighthouse Life Ins. v. Geronta Funding*, 2019 WL 8198323, at *2-3 (Del. Super. Ct. 2019) ("*Seck*"), *inter. cert. denied*, 2019 WL 8198324, at *2-3 (Del. Super. Ct. 2019), *appeal refused* 207 A.3d 579 (Del. 2019).[18] Berkshire fairly summarizes this exception (Br. 41) as whether the STOLI investor "was reasonably unaware of the insurable-interest problem."

This is also consistent with the way the New Jersey Supreme Court recently addressed the issue in a STOLI case under New Jersey law. *See Bergman*, 208 A.3d at 859 (STOLI investor can try to prove entitlement to refund of the premium it paid; trial court should "develop a record and balance the relevant equitable factors,"

[18] This theory of restitution is presented by STOLI investors as an exception to Delaware's general rule that "[o]rdinarily . . . neither party [to an illegal agreement] has a remedy to any extent against the other." *Della Corp. v. Diamond*, 210 A.2d 847, 849 (Del. 1965).

including "a party's level of culpability, its participation in or knowledge of the illicit scheme, and its failure to notice red flags.").

But this restitution theory does not apply to a Section 2704(b) claim between an estate and a STOLI investor because the plain language of Section 2704(b) provides that an estate should recover "any benefits" paid under a STOLI policy, not "net benefits."[19] *See Tillman*, 2005 WL 3436484, at *4-5 (applying identical Oklahoma recovery statute and refusing to allow the investor-defendant a set-off for the premium it paid by reasoning that "the plain language of the statute—which is 'benefits thereunder accruing upon the death . . . .' plainly means death benefits under the policy. Further, it does not state 'net benefits,' or 'profit,' or 'gain'").

Moreover, as Berkshire admits (Br. 38), the idea behind a restitution claim in connection with illegal transactions is to prevent unjust enrichment. But "[i]n order for a claim of unjust enrichment to withstand a motion to dismiss, there must be allegations of 'some direct relationship' . . . between a defendant's enrichment and a plaintiff's impoverishment. In other words, there must be 'a showing that the defendant was enriched unjustly by the plaintiff who acted *for* the defendant's benefit." *Anguilla Re v. Lubert-Adler Real Estate Fund IV, L.P.*, 2012 WL 5351229, at *6 (Del. Super. Ct. Oct. 16, 2012) (original emphasis). An unjust enrichment

[19] The Delaware Banker's Association's argument that, at common law, family actions to recover STOLI proceeds only recovered the death benefit net of premiums is, if true, irrelevant because Section 2704(b)'s plain language is more forceful.

claim also fails where there is an adequate remedy at law. *Total Care Physicians v. O'Hara*, 2002 WL 31667901, at *10 (Del. Super. Ct. Oct. 29, 2002).

Here, Berkshire and Ms. Malkin were not parties to any contract; Berkshire never paid any money to Ms. Malkin; Berkshire was not acting for Ms. Malkin's benefit; and Berkshire otherwise did not confer a direct benefit on Ms. Malkin. Rather, Berkshire perpetuated an illegal human life wager on Ms. Malkin's life in the hopes of profiting from her premature death. And the Estate's entitlement to the Policy's proceeds does not arise from any benefit Berkshire conferred on Ms. Malkin or the Estate, but rather stems from Delaware's common law and Section 2704(b), both of which uphold the Constitution's wagering prohibition. Moreover, Berkshire already exercised its actual remedy at law against Coventry, when it sued Coventry for selling it a STOLI policy—in violation of Coventry's contractual promise that the Policy was not STOLI. That claim was resolved pursuant to a confidential settlement, the terms of which Berkshire refuses to disclose. Thus, Berkshire has no unjust enrichment claim against the Estate.

2. To the extent Berkshire can seek restitution from the Estate, Berkshire cannot meet the elements of that claim.

Assuming *arguendo* that this Court finds a restitution claim can be pursued against the Estate, Berkshire cannot meet its burden of proof. As Berkshire admits (Br. 41), it would need to prove its own clean hands and that "it was reasonably unaware of the insurable-interest problem" with the Policy.

But in addition to Berkshire's long involvement with Coventry and Lavastone and its actual knowledge of STOLI issues with the Policy before it bought it from Coventry in 2013, any investor employing even minimal diligence in 2013 would have known that buying a Delaware non-recourse premium finance policy originated by Coventry presented substantial insurable interest problems. *See, supra*, n.14. This is, after all, why Berkshire required Coventry/LST to baldly promise that the Policy was not STOLI and to indemnify Berkshire if this was false. *Supra*, at 12.

Accordingly, even if Berkshire could seek a premium offset against the Estate, Berkshire could never meet the elements of that claim here. Instead, as the District Court held, Berkshire's only recourse was against Coventry/LST. Ex. D at 19.

CONCLUSION

Respectfully, this Court must uphold Delaware's constitutional prohibition on human life wagering, reject Berkshire's attempt to create the absurd situation where a stranger STOLI investor can subvert the Constitution, and hold that when an insured's estate establishes that a policy violated Section 2704(a), it is entitled to recover from the investor all benefits paid to it in connection with a STOLI policy. Further, this Court should hold that to the extent a STOLI investor has any recourse for the premium payments it made towards a STOLI policy, it is against the person or entity with whom it was in contractual privity, and not against the estate of an insured who was used as an instrumentality in a STOLI scheme.

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Dated: August 6, 2021

Exhibit G

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

----------x

LAVASTONE CAPITAL, INC.

Plaintiff, Action No.

vs. 14-CV-7139 (JSR)

COVENTRY FIRST LLC, et al.,

Defendants.

----------x

** CONTAINS ATTORNEYS' EYES ONLY PORTIONS **

DEPOSITION OF WILLIAM TAYLOR

New York, New York

April 15, 2015

Reported by:

MARY F. BOWMAN, RPR, CRR

JOB NO. 92025

MS. LEVIN: Objection.

A. I would say no.

Q. Did you expect Coventry First or any of its affiliates to sacrifice their own interest to further AIG's interests?

A. I'm sorry, can we go back to that previous question? I apologize.

You said direct in any way? Yes. If I saw a policy that I really did not want, I think I could tell Reid, walk away from that policy, let's walk away from that situation. Maybe you could say he had to agree with it, but I can't tell you I never directed him to do anything because I think I probably did on a rare occasion.

Now, go to your next question, go ahead now.

Q. Well, now I have another question. Subject to that possible exception, did AIG have the power to direct the activities of Coventry First in any respect?

A. In general, no, not at all.

Q. My next question was, did you expect Coventry First or LST to sacrifice

their own interests to further AIG's interests?

A. No, I did not expect that.

Q. So let me give you a hypothetical. Let's say Coventry First looked at two policies in the marketplace but could only buy one. The first policy, once you factor in all origination fees and incentive fees and all of the other economics, yields more profit for Coventry and less for AIG. So first policy is better for Coventry. Second policy is the opposite.

Factoring in origination fees, incentive fees and all other economics, the second policy yields less profit for Coventry and more profit for AIG. Which one would you expect Coventry First to buy?

MS. LEVIN: Objection.

A. If it was in the box, I would expect them to give due consideration to the one that would give us the better yield. If it was out of the box, I had no such expectation, and that's not to say that they were obligated to do that.

Q. Were they obligated to do that in your view?

A. No. I don't believe they were obligated to do that.

Q. Do you know what a fiduciary is?

A. I do not necessarily -- I'm not an expert in the legal definition of the term "fiduciary." My understanding of fiduciary is that the person has a responsibility to act in the best interests of the other party that they are the fiduciary of.

Q. Did you understand Coventry First or its affiliates to be AIG's fiduciary?

MR. BRODSKY: Objection, form.

Q. Based on your definition?

A. Based on my understanding, not the legal definition, no, I did not.

Q. Now, Mr. Brodsky asked you certain questions about whether Coventry and AIG were partners or were in a partnership. Do you recall some of those questions?

A. Yes.

Q. Did you have an understanding -- strike that.

And you, yourself wrote some e-mails that used those terms, partner and partnership, correct?

A. I did.

Q. Were you using those words in the legal sense?

A. I don't know what the legal sense is. The answer is no.

Q. How did you mean them?

A. I meant we were working together to grow and form a beautiful business for AIG and for Coventry. So we were working closely together. We were partnering to do this.

Q. Are there other entities with whom AIG did business that you thought of as your partner?

A. I thought of Wells and U.S. Bank as our partner in this business also, not a key partner, not as key as Coventry. When I had reinsurers and there was a time when Hanover Re were partnering with us and investing their money alongside of us and providing medical underwriting to us, I thought of them as our partners. And there was a time when

Berkshire was partnering with us because they were buying some of the policies. So there were other times when there were other key, significant, what I would consider to be partners in the business.

Q. Was it generally your sense, when you're doing business with someone else, they are your partner?

A. No.

MR. BRODSKY: Objection.

A. No, that is not my general sense.

Q. Well, what would make somebody your partner in your view?

A. At AIG, we sell insurance to a lot of people. I -- we do that all day and night and that's the transaction we do and I don't consider our insureds partners.

So -- but within risk financial, we do funky kind of things -- and I'm sorry for using that term, I don't know what a better way is. There was a fair number of transactions we did when we were partnering with other organizations to do something.

Q. Got it.

Did you ever hear anyone at Coventry refer to AIG as a partner?

A. Yes.

Q. And did you take that to mean a legal partnership?

A. No, when I heard that we were good partners, I did not take it to mean we were good legal partners. I just thought we were working together in selling the business. I'm sorry, I don't mean to chuckle.

Q. That's OK.

A. You asked a good question. I'm sorry. I didn't mean to laugh.

Q. That's OK.

Did AIG take steps to prevent Coventry from having too much leverage in the parties' relationship?

MR. BRODSKY: Objection, form.

A. Without going through a lengthy definition of leverage, I would say yes.

Q. What steps did it take?

A. We set up relationships with other parties to do other kinds of business.

Q. And why did AIG do that?

A. Because there was a feeling that at the AIG management level, that we were too -- we were -- we were subject to something going wrong at Coventry. So for example, when Elliot Spitzer did something, it occurred to us that, well, maybe we need to branch out and form some broader relationships just to sort of make sure that we aren't totally leveraged, as you put it, with our relationship with Coventry.

Q. I am going to mark -- OK, we will mark this as WT20.

(Exhibit 20, document Bates stamped LAV 2895180 through 90 plus attachment marked for identification, as of this date.)

Q. Mr. Taylor, you're free to review as much of this document as you wish. But my question concerns the top paragraph on page 6.

I'm sorry, let me make sure that you're looking at the right -- forgive me, it is the page number 6 at the bottom of the page, and it has the words

background/situation over at the top. Do you see that?

A. I see that page. What question do you want to ask me?

Q. So do you see the third sentence starts with, "Risk finance has approximately," do you see that?

A. Yes.

Q. I'm just going to read a couple of sentences and my question at the end is going to be, do you agree with what I've read. OK? Risk -- this document says -- and for the record, this document is WT20, and it is starts with the Bates stamp LAV 02895180. And I'm asking about the document Bates stamped LAV 02895186, and it states, "Risk, risk finance has approximately 30 full-time equivalent professionals dedicated to its life settlements business, including a staff of 15 medical underwriters who perform risk finance's own internal mortality analysis. Through December 2010, Chartis had acquired approximately 6,600 life insurance policies on approximately 5,400 lives totalling over