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
<u>TO OPENING BRIEF OF APPELLANT WELLS FARGO BANK, N.A.</u>

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NATURE OF THE PROCEEDINGS

Although Defendant Wells Fargo Bank, N.A. ("Wells Fargo") played an instrumental role in carrying out an unconstitutional wager on the life of Phyllis Malkin, Wells Fargo claims it cannot possibly be liable and should have been dismissed under Delaware's UCC because it was acting as a "securities intermediary." More than this, however, Wells Fargo brazenly seeks an even broader ruling that it (and other agents for STOLI investors) cannot even be *named* in future lawsuits because they have *absolute immunity from suit* under the UCC.

But like its co-defendant, Berkshire Hathaway Life Insurance Company of America ("Berkshire"), and like the *amici* that support Wells Fargo's position, Wells Fargo's opening brief *completely ignores* the most fundamental issue in this case: Delaware's Constitution prohibits wagering; this Court has held that STOLI is a form of human life wagering that "harm[s] the public" and is "a fraud on the court"; and STOLI is, therefore, prohibited by Delaware's Constitution. *PHL Variable Ins. Co. v. Price Dawe 2006 Ins. Trust*, 28 A.3d 1059, 1068-71 (Del. 2011).

So while Wells Fargo (and Berkshire and the *amici* for that matter) spill considerable ink arguing about the UCC and the mythical harm securities intermediaries might suffer if they are parties to STOLI lawsuits, they miss the dispositive point: Because STOLI is unconstitutional, no statute, including the UCC, can be interpreted as allowing the enforcement of a STOLI wager or protecting the strangers involved in that wager. And because this Court held that Delaware's Insurable Interest Statute, 18 *Del. C.* § 2704, upholds the Constitution's wagering prohibition, Section 2704(b) must be enforced by its plain terms. Here, that means Wells Fargo (the admitted "payee") is not immunized from a lawsuit in connection with its role in the STOLI scheme carried out on Ms. Malkin's life.

Nonetheless, while the UCC does not protect Wells Fargo from having to answer for its role in bringing about an unconstitutional human life wager, Wells Fargo is ultimately protected under basic principles of agency law and its own private contract with Berkshire. To that end, Wells Fargo will be discharged from all liability once its principal, Berkshire, satisfies the judgment entered in favor of Ms. Malkin's estate (the "Estate"). This result is not only provided for under black-letter agency law, but is guaranteed for Wells Fargo through its contract with Berkshire, which mandates that Berkshire indemnify Wells Fargo for any exposure in this case. Thus, in reality, Wells Fargo's UCC and other arguments in this proceeding are much ado about nothing because Wells Fargo is protected from ultimate liability here, but through a different path than the ones it suggests.

SUMMARY OF THE ARGUMENT

The Estate responds to Wells Fargo's summary of its argument as follows.

1. Denied. A Section 8-502 defense is not available to Wells Fargo for the same reasons it is not available to Berkshire. Section 2704(b)'s plain language authorizes families to recover STOLI proceeds from "the person so receiving them" (i.e., "the beneficiary, assignee, or other payee"). Interpreting Section 8-502 as providing a defense to a certain category of investors would (if proven) allow them to cash in on unconstitutional wagers and would require courts to enforce those unconstitutional wagers, something this Court has held "[a] court may never" do.

Thus, the UCC cannot be read as an exception to the Delaware Constitution's wagering prohibition, nor does the plain language of Section 8-502 support such a reading. Indeed, Section 8-502 only applies to an "adverse claim" to a "financial asset," narrowly defined as a claim concerning someone's "property interest." Because unconstitutional STOLI transactions are void *ab initio*, meaning they are deemed never to have happened, no investor has a property interest in its proceeds, and there is zero evidence even suggesting that the General Assembly intended Section 8-502 to breathe life into unconstitutional wagers, a result the General Assembly would have been powerless to effectuate had that been its purpose.[1]

[1] The Estate incorporates by reference herein its Answering Brief to Berkshire where this issue is discussed more fully.

2. Denied. A Section 8-115 defense is not available to Wells Fargo for the same reasons that a Section 8-502 defense is not available. Wells Fargo's primary objection is that Wells Fargo was acting solely as Berkshire's agent. But black-letter principles of agency law do not immunize agents from liability, especially where they act, as securities intermediaries do, on behalf of undisclosed principals. This is not to say, however, that securities intermediaries will ultimately have to satisfy Section 2704(b) judgments. Rather, the opposite is true. Wells Fargo will be discharged from liability once Berkshire satisfies the Estate's judgment, and Wells Fargo is otherwise fully protected by the terms of its commercial agreement with Berkshire, under which Berkshire has been indemnifying Wells Fargo all along. Thus, Wells Fargo and others like it are not in need of this Court's protection, nor would enforcing the law as written wreak havoc on Delaware's financial markets or on any Delaware institution. The only result that would obtain by the absolute "immunity from suit" sought by Wells Fargo would be the absurd result of allowing the *ultimate* payees of STOLI proceeds (i.e., investors like Berkshire) to remain nameless and unknown, and thus, for all practical purposes, free to cash in on human life wagers that violate Delaware's Constitution.[2]

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[2] Wells Fargo does not address the merits of Question 2, and instead adopts the positions stated in Berkshire's Opening Brief, so the Estate does not address Question 2 in this brief, and instead adopts its Answering Brief to Berkshire.

STATEMENT OF THE FACTS

The Estate adopts herein by reference the entirety of its Statement of Facts in its Answering Brief to Berkshire's Opening Brief (hereinafter, "Estate's Brief") which, among many other things, contradicts Wells Fargo's incorrect claim (Wells Fargo Br. 6) that Ms. Malkin procured the policy in question (the "Policy"). Indeed, both the District Court and the Eleventh Circuit held precisely the opposite. Ex. A, E.[3] The facts set forth below are particular to Wells Fargo and germane to the issues Wells Fargo presents in connection with Certified Question 1.

A. Since 2008, Wells Fargo was an intimate participant in the underlying Coventry STOLI program.

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 Lavastone. *Sun Life*, 2016 WL 161598, at *3; B077 ¶¶ 1-8 (Dkt. 135).

Beginning in 2008, Wells Fargo became a party to the Origination Agreement and other contracts under which it served in various roles for Coventry and Lavastone, including as fiscal agent, securities intermediary to both Coventry and Lavastone, and trustee of various trusts involved in the overall STOLI program.

[3] Citations to Exhibits A-F are those attached to Berkshire's Opening Brief.

B076-B077 ¶ 3 (Dkt. 135); B121-B122¶ 40 (*Lavastone v. Coventry* Compl.) (Dkt. 135-1); B264 ¶ 40 (*Lavastone v. Coventry* Ans.) (Dkt. 135-2). During its deposition in this case, Wells Fargo admitted that: (i) it entered into contracts with both Coventry and Lavastone (B439 29-30 (Dep. C. Young) (Dkt. 137-30)); (ii) Wells Fargo began its relationship with Coventry in 2008 because Wells Fargo's "client, AIG [Lavastone], was a purchaser of life insurance policies [and] Coventry at that time was a servicer of that portfolio and also an originator of policies in to that portfolio" (B438 27-28 (Dep. C. Young) (Dkt. 137-30)); and (iii) Wells Fargo operated on behalf of both Coventry and Lavastone through Wells Fargo's "Longevity Group" located in Minneapolis, Minnesota. B436-B437 9-14 (Dep. C. Young) (Dkt. 137-30).

B. With regard to the Policy, Wells Fargo first served as Coventry's agent, and later as agent to Berkshire.

The Policy on Ms. Malkin's life was procured by Coventry through its STOLI scheme in 2006. Wells Fargo's first direct involvement with this specific Policy was in 2012, when it became the nominal owner and beneficiary of the Policy on behalf of Coventry and a Coventry affiliate, LST Holdings ("LST"). B096 ¶¶ 134-35 (Dkt. 135); B408 (Am. Gen. Chng. Benef. and Owner) (Dkt. 137-25); A221 (Purchase and Sale Agreement); B410 (Purchaser's Sec. Acc. Cntrl Agreement) (Dkt. 137-27).

Through a Securities Account Control Agreement (the "Agreement"), dated June 17, 2013, Berkshire then engaged Wells Fargo to act as its agent concerning a block of policies (including the Policy) that Berkshire was purchasing from Coventry and LST. A182. In the Agreement, Wells Fargo identified itself as operating from its office in Minneapolis—through the same Longevity Group that had managed the Wells Fargo relationship with Coventry and Lavastone since 2008—and undertook the obligation to "establish and maintain" a "Securities Account" for Berkshire at that Minneapolis office. A183 §2(a).

Section 4 of the Agreement expressly: (i) limits Wells Fargo's duties; (ii) provides Wells Fargo with a broad "exculpation" for any "liability whatsoever for any actions or omissions hereunder except for any such liability arising out of or in connection with [Wells Fargo's] gross negligence or willful misconduct;" and (iii) requires that Berkshire indemnify Wells Fargo for "any and all claims, losses, causes of action, demands, damages, liability and expenses of every kind (including reasonable attorneys' fees and expenses) in any way relating to, growing out of or resulting from" Wells Fargo's actions as Berkshire's agent. A186-A187 §4(f).

When Berkshire finalized its purchase of the Policy from Coventry/LST, the Policy was transferred into the Securities Account Wells Fargo established for Berkshire in Minneapolis. A221 (Purchase and Sale Agreement). Wells Fargo then named itself the Policy's record owner and beneficiary by sending a change of ownership and beneficiary form to American General Life Insurance Company ("American General"), the issuer of the Policy. B408 (Am. Gen. Chng. Benef. and

Owner). Wells Fargo did not disclose to American General that it was acting for or on behalf of Berkshire, and did not otherwise disclose to American General Berkshire's role or involvement with the Policy. Nor was any of this information ever shared with Ms. Malkin or her family—who did not learn of Berkshire's involvement until after this lawsuit was filed in 2017.

C. Wells Fargo subjected itself to a claim under Section 2704(b) because it was the "beneficiary" and "payee" of the Policy's proceeds and the entity "receiving" those proceeds.

Since 1968, the Insurable Interest Statute has provided that "[i]f *the beneficiary, assignee or other payee* under any contract made in violation of this section [2704] *receives from the insurer* any benefits thereunder accruing upon the death . . . of the insured . . . his or her executor or administrator, as the case may be, may maintain an action to recover such benefits *from the person so receiving them*." 18 *Del. C.* § 2704(b) (emphasis added).

When Ms. Malkin passed away in 2014, Wells Fargo—in its own name—submitted a death claim to American General, asking American General to pay the Policy's death benefit to Wells Fargo. Again, Wells Fargo did not identify Berkshire. In October 2014, American General issued a check in the amount of $4,013,976.47 payable directly to Wells Fargo. A194.

There is no question, therefore, that Wells Fargo was "the beneficiary, assignee or other payee under" the Policy and that Wells Fargo also was "the person so receiving" the Policy's death benefit. Indeed, not only did Wells Fargo actually receive the STOLI proceeds from the Policy, but Wells Fargo purported to become a party to the Policy itself on behalf of an undisclosed principal. Wells Fargo also made premium payments to American General in its own name, and then claimed and received the Policy's death benefit in its own name.

In 2017, the Estate commenced suit against Wells Fargo under Section 2704(b), seeking a determination that the Policy was an illegal wager and that the proceeds paid to Wells Fargo must be turned over to the Estate. At the time, the Estate was not aware of Berkshire's involvement with the Policy; again, Berkshire's identity was only discovered after litigation was filed.

On summary judgment, the District Court held that the Policy was an illegal wager on the life of Ms. Malkin and that she was "used" as an instrumentality by investors to procure a STOLI policy through the well-oiled STOLI operation run by Coventry. Ex. E. In so doing, the District Court rejected Berkshire's and Wells Fargo's UCC defenses, holding, among other things, that the UCC could not trump Delaware's constitutionally-enshrined public policy against human life wagers, and thus could not be used to immunize those who receive illegal STOLI proceeds. The District Court also held, however, that "[t]o the extent that Wells Fargo, after receiving the Policy proceeds, merely passed them on in full to Berkshire, Wells Fargo would appear to have no liability." *Id*. at 22. The District Court then held that there were factual issues that remained about who had "custody and control" over the Policy's proceeds, and thus did not resolve this issue. *Id*.

In a precedential opinion issued in May 2021, the Eleventh Circuit affirmed the District Court's determination that the Policy was an unconstitutional human life wager. Ex. A. The Eleventh Circuit then certified two questions to this Court, the first of which deals with Defendants' UCC defenses and, as to Wells Fargo specifically, asks whether Wells Fargo "is entitled to assert a . . . securities intermediary defense under" Section 8-115 of Delaware's UCC, and the second of which deals with whether Section 2704(b) defendants are entitled to an offset of the premiums they paid. Berkshire filed a principal brief with this Court addressing Questions 1 and 2 as they pertain to STOLI investors like Berkshire; whereas, Wells Fargo filed a principal brief focusing on that portion of Question 1 pertaining to securities intermediaries acting as agents to STOLI investors.

D. Wells Fargo's request for absolute immunity in Section 2704(b) cases contradicts Wells Fargo's long and ongoing history of participating in STOLI litigation under Section 2704(a).

Contrary to Wells Fargo's arguments in this proceeding, the truth is that over the last decade, Wells Fargo has actively *commenced* lawsuits against a host of insurance companies arguing that the policies it owns in its name, always as a purported securities intermediary, are valid contracts because, Wells Fargo claims, those policies were issued with a valid insurable interest, including under Section

2704(a).[4] In those cases, Wells Fargo either names itself the plaintiff, or is sued as the defendant (and then asserts counterclaims), in its capacity as securities intermediary for an undisclosed and unknown principal. This is because even the insurers that have issued policies that later become owned by Wells Fargo, as a securities intermediary, are not told the names of the principals Wells Fargo is acting for, and deal with Wells Fargo alone as the counterparty to those policies.

Here, had American General challenged the Policy for lack of insurable interest, Wells Fargo would have been the counterparty to any such lawsuit. To be sure, not only has Wells Fargo been actively involved in that type of STOLI litigation for years, but Wells Fargo has never taken the position that the UCC somehow immunizes it from even being named as a defendant. Nor has Wells Fargo—a Minnesota securities intermediary working on behalf of investor clients across the country and the world—ever taken the position that the many STOLI lawsuits it has chosen to commence, and the many it has chosen to defend in its own name, have

[4] A partial list of Wells Fargo's extensive STOLI lawsuits include: *Sun Life v. Wells Fargo*, 3:14-cv-05789 (D.N.J. Sept. 17, 2014) ("*Bergman*"); *Sun Life v. Wells Fargo*, 3:17-cv-02679 (D.N.J. Apr. 19, 2017) ("*Klugman*"); *Sun Life v. Wells Fargo*, 1:17-cv-06588 (N.D. Ill. Sept. 12, 2017) ("*Corwell*"); *Wells Fargo v. Penn Mut. Life Ins. Co.*, No. 18-004704 (Fla. Circ. Ct. Feb. 28, 2018) ("*Roebuck*"); *Columbus Life Ins. Co. v. Wells Fargo*, 20-cv-833-MN-JLH (D. Del. June 22, 2020) ("*Snyder*"); *Wells Fargo v. Sun Life*, No. 1:21-cv-2984 (E.D.N.Y. May 26, 2021) ("*Fruchter*"); *Pruco Life Ins. Co. v. Brasner*, No. 9:10-cv-80804 (S.D. Fla. Jul. 9, 2010).

caused harm to the financial markets of Delaware or disrupted what Wells Fargo loosely refers to as Delaware's life settlement market.

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 Co. 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

1. Neither Section 8-502 nor Section 8-115 can be interpreted to allow unconstitutional human life wagers to come to fruition.

For the reasons explained in the Estate's Answering Brief to Berkshire, which is incorporated here by reference, a Section 8-502 defense is not available to either Wells Fargo or Berkshire, nor is a Section 8-115 defense available to Wells Fargo.

In summary, Section 2704(b)'s plain language deputizes families to recover STOLI proceeds from "the person so receiving them" (i.e., "the beneficiary, assignee, or other payee under" the policy). That obviously applies to securities intermediaries like Wells Fargo, who own STOLI policies on behalf of undisclosed principals, submit death claims on behalf of those undisclosed principals, and then actually receive and hold those proceeds of behalf of those undisclosed principals.

Interpreting either Section 8-502 or 5-115 as providing a defense to securities intermediaries like Wells Fargo would allow illegal human life wagers to pay off, a result Delaware's Constitution forbids. Not only is this interpretation of Section 8-502 and 8-115 compelled by Delaware's Constitution, but it is consistent with Section 8-502's and 8-115's plain language, both of which only apply to an "adverse claim" to a "financial asset," narrowly defined as a claim concerning someone's "property interest." Because unconstitutional STOLI transactions are void *ab initio*, meaning they are deemed never to have happened, no investor has a property interest in their proceeds. Moreover, there is no evidence that the General Assembly intended Sections 8-502 or 8-115 to provide a defense to a Section 2704(b) claim. Indeed, Section 2704(b) was enacted after the UCC's bona fide purchaser rules and is the more specific statute with respect to its subject matter. And, of course, the General Assembly is presumed not to intend outcomes that violate the Constitution.[5]

[5] Although Wells Fargo is correct that the 1997 amendments to Article 8 added provisions concerning securities intermediaries which were not defined as such in the prior-enacted version of Article 8, Article 8 already contained bona fide purchaser provisions and other protections for brokers and agents since 1966, and the mere fact that these provisions were redefined in the 1997 amendments is not enough for Wells Fargo to invoke the rule set out in *State v. Fletcher*, 974 A.2d 188, 193 (Del. 2009), which could not apply even if the 1997 amendments were truly new

Accordingly, neither Section 8-502 nor Section 8-115 are defenses to a Section 2704(b) claim, and the answer to Question 1 must be "no."

Regardless, to the extent this Court holds otherwise, Wells Fargo would bear the burden of proving these defenses. *Oscar Gruss & Son v. First State Bank*, 582 F.2d 424, 433 (7th Cir. 1978) ("[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."); *Marsh v. Marsh*, 261 A.2d 540, 542 (Del. Ch. 1970) (same under common law). But because of Wells Fargo's long and intimate relationship with, and the various roles its Longevity Group played in connection with, the underlying STOLI scheme, discussed *supra,* at 6-7 and *infra*, at 22-28, Wells Fargo would never be able to meet its burden, and these defenses would ultimately fail in any event. *See SEC v. Credit Bancorp, Ltd.*, 386 F.3d 438, 451-52 (2d Cir. 2004) (securities intermediary had notice, and was not a bona fide purchaser under Article 8, including because intermediary's officers and agents who conducted transaction saw press releases with allegations of short selling and failed to conduct investigation).

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because no one could plausibly argue that Section 8-115 is more specific than Section 2704, or that Section 2704 is merely a "general statute" on the issues central here. And, in any event, even if there was a conflict between Sections 2704(b) and 8-115, the UCC cannot be interpreted as providing a defense to an unconstitutional transaction.

2. Securities intermediaries have protection from ultimate liability in Section 2704(b) claims under black-letter agency law and through their contracts with their principals, so the mere fact that they cannot assert UCC defenses in STOLI cases will not negatively impact them.

The core of Wells Fargo's argument is that it should have been dismissed from this case because it was only acting as Berkshire's agent and followed Berkshire's instructions, and that if the Court does not interpret Sections 8-502 and 8-115 as providing *absolute* immunity to securities intermediaries *from suit*, the consequences to securities intermediaries will be "staggering." (Wells Fargo Br. 13). This hyperbole aside, Wells Fargo misses the point. Under basic principles of agency law, an agent can always be held liable to a third party even if the agent acts for and at the direction of its principal—especially where the principal is undisclosed, as Berkshire was. But if the principal satisfies the plaintiff's judgment, the agent is discharged from liability, which is exactly what will happen to Wells Fargo. Indeed, Wells Fargo's contract with Berkshire mandates that Berkshire satisfy the Estate's judgment, thus meaning Wells Fargo has no real exposure in this case, regardless of the fact that the UCC does not provide it a defense.

To be sure, Delaware follows the Restatement (Second) of Agency. *Doe v. Bicking*, 2020 WL 374677, at *7 n.32 (Del. Super. Ct. Jan. 22, 2020). Various provisions of the Restatement provide that an agent can be liable to a third party in a variety of contexts, but that the agent is discharged from liability once a judgment is obtained against, and satisfied by, the principal. In the context of a contract, for example, "[a]n agent who has made a contract on behalf of an undisclosed principal is not relieved from liability by the determination of the other party thereto to look to the principal alone for the performance of the contract. He is discharged from liability if the other obtains a judgment against the principal, or, to the extent that he is prejudiced thereby, if he changes his position in justifiable reliance upon the other's manifestation that he will look solely to the principal for payment." Restatement (Second) Agency § 337.

Likewise, in the context of torts, the rule is that "[a]n agent who does an act otherwise a tort is not relieved from liability by the fact that he acted at the command of the principal or on account of the principal[.]" *Id.* § 343; *see id*. § 344 ("An agent is subject to liability, as he would be for his own personal conduct, for the consequences of another's conduct which results from his directions if, with knowledge of the circumstances, he intends the conduct, or its consequences[.]") *id*. § 359B (Official Comment) ("If an agent commits a tort for which the principal is liable, both are tortfeasors. They may be equally liable or, as between the two, one may be primarily liable."); *id*. § 359C ("Principal and agent can be joined in one action for a wrong resulting from the tortious conduct of an agent or that of agent and principal, and a judgment can issue against each."); *see also id.* § 349 (similar).

Thus, both agent and principal can be sued in the same action. *See id.* § 210A ("A principal, initially undisclosed, and his agent can properly be joined in one action based upon a contract made by the agent; but if either defendant objects, the plaintiff can secure judgment only against the one whom he elects to hold."); *id.* § 217B ("Principal and agent can be joined in an action for a wrong resulting from the tortious conduct of an agent or that of agent and principal, and a judgment can be rendered against each."). Indeed, Delaware courts have followed these well-settled principles for many years. *See, e.g.*, *Metro Storage Int'l LLC v. Harron*, 2019 WL 3282613, at *25 (Del. Ch. Jul. 19, 2019) (citing *Verrastro v. Bayhospitalists, LLC*, 208 A.3d 720, 724-25 (Del. 2019)); *Kuhn Const. Co. v. Ocean and Coastal Consults.*, 723 F. Supp. 2d 676, 690 (D. Del. 2010); *First St. Staffing Plus v. Mont. Mut. Ins. Co.*, 2005 WL 2173993, at *10 (Del. Ch. Sep. 6, 2005); *Clark v. Brooks*, 377 A.2d 365, 370-71 (Del. Super. Ct. 1977), *aff'd Blackshear v. Clark*, 391 A.2d 747 (Del. 1979); *T.V. Spano Bldg. Corp v. Wilson*, 584 A.2d 523, 531 (Del. Super. Ct. 1990) (quoting Restatement (Second) Agency § 343)). Under basic agency law, therefore, any agent who collects STOLI proceeds on its principal's behalf is plainly subject to potential liability on a Section 2704(b) claim.

That is not to say, however, that a securities intermediary will actually be forced to pay a Section 2704(b) judgment. Rather, the rule is that a plaintiff can elect to hold the principal liable for the judgment, and the agent will be discharged from liability once the principal satisfies the judgment. *See, e.g.*, *Grinder v. Bryans Road Bldg. & Supply Co.*, 432 A.2d 453, 464 (Md. 1980) ("We hold that a creditor who contracts with the agent for an undisclosed principal does not obtain alternative liability, that he may proceed to judgment against both, but that he is limited to one satisfaction."); *id.* at 454; *see generally* Restatement (Second) Agency § 337 (agent is "discharged from liability if the other obtains a judgment against the principal")

Moreover, the sophisticated financial institutions that elect to serve as securities intermediaries for the sophisticated investors who trade in multi-million dollar policies insuring the lives of complete strangers obviously protect themselves contractually from the costs of suit and any theoretical agent liability by securing from their clients broad indemnification provisions. That is, of course, precisely what Wells Fargo did here. Section 4 of the Agreement between Wells Fargo and Berkshire expressly: (i) limits Wells Fargo's duties; (ii) provides Wells Fargo with a broad "exculpation" for any "liability whatsoever for any actions or omissions hereunder except for any such liability arising out of or in connection with [Wells Fargo's] gross negligence or willful misconduct;" and (iii) requires that Berkshire indemnify Wells Fargo for "any and all claims, losses, causes of action, demands, damages, liability and expenses of every kind (including reasonable attorneys' fees and expenses) in any way relating to, growing out of or resulting from" Wells Fargo's actions as a Securities Intermediary. A186-A187 §4. Wells Fargo failed to put forth any evidence in the record below to suggest that Berkshire has not lived up to its contractual indemnification obligation, and as the Estate understands it, Berkshire has actually been funding Wells Fargo's defense from the start and Wells Fargo has not gone out-of-pocket at all—nor will it.

In truth, this is exactly the same position Wells Fargo willingly puts itself in when it acts as both *plaintiff* and *defendant* in Section 2704(a) STOLI litigation between insurers and the principals for which Wells Fargo serves as a securities intermediary. In those cases, like here, Wells Fargo has absolutely no financial exposure because its efforts are directed by, and completely funded by, its principals.

Yet in the context of Section 2704(b) STOLI claims by the family of a deceased insured, Wells Fargo now contends it is not a proper defendant and should never even be named in such a suit. Of course, Wells Fargo does not even try to reconcile this position with it longstanding and ongoing role as a party in Section 2704(a) STOLI claims with insurers, and what is really going on here is plain from Wells Fargo's own brief: Wells Fargo is attempting to use the UCC to obtain (Wells Fargo Br. 12) absolute "immun[ity] . . . from suit" in Section 2704(b) cases so that estates are precluded from even *naming* securities intermediaries as defendants and must instead somehow name the undisclosed principals for whom securities intermediaries like Wells Fargo act, even though no one (including the insurer that paid out the proceeds) knows who those principals are.

In this way, Wells Fargo seeks to use its agency status to immunize not only itself, but the hidden STOLI investor principals for whom it works. The practical impact of the rule Wells Fargo (improperly) seeks to create is that almost no one would ever be able to commence a Section 2704(b) claim, because, without litigation, almost no one would ever be able to identify the actual principal for whom the securities intermediary acted. This would gut Section 2704(b) of its efficacy, allow STOLI wagers to come to fruition without challenge, and transform Delaware into a STOLI safe haven.

Respectfully, this Court should reject Wells Fargo's attempt to create such a rule, especially when, for all practical purposes, Wells Fargo's appeal is much ado about nothing. Once the District Court's judgment is affirmed, the Estate will elect to enforce its judgment against Berkshire, and once satisfied, Wells Fargo will be discharged from liability. Meanwhile, Wells Fargo has been indemnified by Berkshire all along, and faces no actual financial impact. Accordingly, the District Court's decision below was entirely correct: Wells Fargo was a proper defendant under Section 2704, even though it will be discharged of any liability to the Estate once Berkshire satisfies the judgment.

3. Wells Fargo is wrong when it baldly suggests a finding in favor of the Estate will have a material negative impact on the investor market.

Wells Fargo, along with Berkshire and the *amici*, argue that allowing estates to recover under Section 2704(b) against downstream investors is unfair because it will somehow upset the investor market's supposed expectations.[6] This argument is untethered from reality, however, because the market has been on notice from the very beginning, and certainly by the 2013 purchase date for the Policy, that policies procured through non-recourse premium financing programs like Coventry's were highly risky, particularly in states like Delaware with strong anti-STOLI laws, and that families could challenge these policies and recover the proceeds.

Consider, for example, the following non-exhaustive information available in the public domain:

- At least as early as 2005, industry commentators were advising that "non-recourse premium financing" is "***a thinly disguised attempt to skirt state insurable interest laws***"[7] and that "[w]hen looking below the surface of a ***non-recourse premium financing transaction***, a thorough review of the mechanics of the transaction may uncover undocumented or ignored elements that may (1) ***constitute a violation of state insurance law or regulations*** [and] (2) raise significant securities regulation and litigation issues."[8]

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[6] Wells Fargo Br. 9-10, 13-16; Berkshire Br. 4-5, 32, 34-36; Del. Banker's Ass'n. Br. 1, 3, 6, 18, 20; ILMA Br. 2, 6; Taiwanese Banks Br. 13-14.

[7] Steven R. Leimberg, *Stranger-Owned Life Insurance: Killing the Goose that Lays Golden Eggs!*, Tax Analysts, at 811 (May 2005) (emphasis added).

[8] R. Marshall Jones, et al., *'Free' Life Insurance: Risks and Costs of Non-Recourse Premium Financing*, 33 Estate Planning 7, at 3 (July 2006) (emphasis added).

- At least as early as 2006, large fund managers were disclosing the risks of non-recourse premium financed policies to prospective investors. For example, one large fund manager warned its potential investors that "[t]he U.S. Congress, U.S Treasury Department and various state insurance regulators have recently begun examining whether the ***financing of newly-issued life insurance policies by persons*** . . . ***violates state life insurance insurable interest laws***," focusing on financing that "is ***nonrecourse to the proposed insured***," and stating that if a court were to determine that premium financed policies are void, it would have "***a material adverse effect on your investment***."[9]

- At least as early as 2008, the life settlement industry's only trade journal published an article discussing ***a legal action brought by an insured's family*** to recover a $10 million death benefit that had been paid out by the insurer to an investor on a STOLI policy, stating that the case "***may have wide-ranging repercussions for the industry as a whole***, legal experts and others say."[10]

- In April 2009, the U.S. Congress heard testimony that mirrored these concerns: ***"[C]reative premium financing transactions*** are used to fund the purchase of high value life insurance policies. ***Seniors are being offered 'free' or low cost premium financing for the first two years of the policy term***. Often, the free or low cost financing term coincide with the state holding period for a life insurance policy before it is eligible to be sold in a viatical transaction. At the end of the free or low cost financing period, the senior is offered a chance to pay for the policy. Often, the accumulated premium and finance charges are so high that is cost-prohibitive for the senior to continue with the transaction. The fine print of the financing documents allows for the finance company to maintain the life insurance policy or sell it to a third party. ***Thus a STOLI is born***."[11]

- At least as early as 2010, the significant risks associated with investing in non-recourse premium financed polices was being reported in the mainstream media.

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[9] Genesis Voyager Equity II Corp, *Confidential Preliminary Private Offering Memorandum*, at 8-9 (Oct. 10, 2006) (filed in *SEC v. Private Equity Management Group, Inc.*, 2:09-cv-02901, Doc. 43-28 (May 7, 2009)) (emphasis added).

[10] *New York Trust Case May Impact Settlement Industry*, The Deal's Life Settlement Report, dated Feb. 6, 2008 (emphasis added).

[11] U.S. Sen. Sp. Cmte. On Aging, *Betting on Death in the Life Settlement Market: What's at Stake for Seniors*, No. 111-4 (Apr. 29, 2009) (emphasis added).

The Wall Street Journal, for example, published an article discussing litigation risk on "financed policies" and how the market was "so ripe for fraud."[12]

- In July 2010, the SEC convened a Life Settlements Task Force, whose report explicitly identified "***non-recourse premium financing***" as an "***indicator of a STOLI transaction***," referenced "***approximately 300 STOLI cases in active litigation***" and noted that "these cases are brought by insurance companies and ***parties such as family members***."[13]

- Later in 2010, the Federal Deposit Insurance Corporation ("FDIC") warned banks of the litigation risk in "Senior Life Settlements" based on practices designed to skirt insurable interest laws, expressly discussing the "**Litigation Risk** . . . ***that the insured's family members (heirs) . . . will file legal action*** and the potential financial impact to the investor."[14]

- Throughout this time period, large fund managers continued to warn of the risks of investing in non-recourse premium financed policies. In August 2011, for example, another large fund manager (Fortress)[15] sought to securitize its portfolio

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[12] *The Pros and Cons of Betting on Death*, W.S. J., April 12, 2010, available at https://www.wsj.com/articles/SB10001424052748703909804575123960669921740.

[13] Staff Report to the SEC Commission, Jul. 22, 2010 at 14, available at https://www.sec.gov/files/lifesettlements-report.pdf.

[14] *Senior Life Settlements: A Cautionary Tale*, Supervisory Insights, Winter 2010 at 29, 31, available at https://www.fdic.gov/regulations/examinations/supervisory/insights/siwin10/siwinter10-article3.pdf (emphasis added and in original).

[15] Fortress is the same STOLI investor that unsuccessfully lobbied the Delaware General Assembly and Delaware Department of Insurance for many years to consider legislation that would have automatically returned all premiums to STOLI investors whose policies were invalidated for lack of insurable interest. *See* Delaware Dep't of Insurance, *Secondary Market for Life Insurance Policies: Report to Delaware State Senate*, Dec. 28, 2016 at 12-13, available at https://insurance.delaware.gov/wp-content/uploads/sites/15/2017/01/sr19report-2016-1228-final.pdf (hereinafter, "Delaware DOI Report"). None of these bills were successful. *See* Del. S.B. 220, 146th Gen. Assem. (2012); Del. H.B. 87, 147th Gen. Assem. (2013); Del. S.B. 71, 148th Gen. Assem. (2015). Fortress also tried (again unsuccessfully) to get the Delaware Department of Insurance to recommend this legislation. Delaware DOI Report at 12-13. But the Delaware DOI also rejected

of policies, many of which had been procured through non-recourse premium finance. In so doing, the fund publically filed with its regulators a "Listing Particulars," which discussed ***the insurable interest risk inherent in non-recourse premium financed policies*** at length, including the ability of ***the insureds' family members to sue*** to recover STOLI death benefits paid to investors, and noted that such legal challenges "***could materially and adversely affect***" the investment.[16]

- And, of course, in 2011, this Court issued its seminal decision in *Price Dawe*, which clarified, among other things, that STOLI is "a fraud on the court"; that policies must be procured in "good faith" for a legitimate insurance purpose as part of a "bona fide" transaction and not as a "cover for a wager"; and that investors cannot use insureds to "generate" polices for investors. 28 A.3d at 1068 n.25, 1070-73, 1078. This Court also observed that "STOLI schemes are created to feign technical compliance with insurable interest statutes" and that courts must therefore "scrutinize the circumstances under which the policy was issued" and refuse to allow "an illogical triumph of form over substance that would completely undermine the policy goals behind the insurable interest requirement." *Id.* at 1071, 1074, 1076.

- In so doing, this Court relied considerably on a law review article by Professor Martin, which specifically identified policies procured through ***non-recourse lending programs as classic examples of STOLI*** and which warned that families could bring suits to recover those proceeds under Section 2704(b). *See, e.g.*, Susan Lorde Martin, *Betting on the Lives of Strangers: Life Settlements, STOLI, and Securitization*, at 12, 24, 29, 31, 32 (Fall 2010), *cited with approval by Price Dawe*, 28 A.3d at 1069 n.27, 1070 n.33.

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these efforts out of concern that accepting them would cause Delaware to be targeted for STOLI and potentially become a "haven for STOLI." *Id.* at 18.

[16] Note Offering, Aug. 12, 2011 at 27-29, available at https://ise-prodnr-eu-west-1-data-integration.s3-eu-west-1.amazonaws.com/legacy/ListingParticulars_501e5b69-c72e-41cb-8ac7-9e0338e5653e.PDF (emphasis added).

Moreover, by the 2013 purchase date of the Policy in this case, there had long been reports in the public domain that *Coventry in particular* was generating STOLI policies through non-recourse premium financing. For example:

- In 2005, the Wall Street Journal published an article where Coventry's CEO admitted to arranging "non-recourse premium financing," which article explained that critics viewed this practice as merely feigning compliance with insurable interest laws wherein "[o]utside investors are (not so) indirectly buying life insurance on the life of a stranger."[17]

- In 2007, the industry's trade publication (Life Settlements Report) reported on a lawsuit where an insurer alleged that Coventry procured a policy that "looked like an ordinary life insurance transaction on the surface," but was instead "designed to circumvent insurable interest laws" through a non-recourse premium finance loan where the insured paid no premiums and the investors were the intended beneficiaries.[18]

- In 2008, a lawsuit was filed alleging that Coventry engaged in a "scheme" to "circumvent the laws of the State of Florida with regard to insurable interest" through a "sham transaction" that used a 2-year non-recourse finance loan to obtain and control a $10,000,000 policy.[19]

- In 2011, a court declared a Coventry-generated and Wells Fargo-held policy void *ab initio* under Florida law based on the fact that Coventry controlled the transaction; the insured neither wanted nor needed insurance; the insured did not pay any premiums, which were instead funded through a non-recourse loan hidden in a sub-trust, which the producer testified was "smoke and mirrors," and which policy the court concluded was not "procured in good

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[17] *Letting an Investor Bet on When You'll Die—New Ins. Deals Aimed at Wealthy Raise Concerns; Surviving a Two-Year Window*, Wall Street J., May 26, 2005.

[18] *New York Life Sued Over Rescission of Policy*, The Deal's Life Settlements Report, July 4, 2007, available at *h*ttps://pipeline.thedeal.com/article/27q2l56p1s1f 47qj6m0w0/deal-news/new-york-life-sued-over-rescission-of-policy.

[19] Compl., *Dulaw Mgmt. v. PHL Var. Ins. Co.*, 09-08028-610 (Fla. 17th Jud. Cir. June 23, 2008) ¶¶ 7, 13-15, *available* at 08-cv-61167, D.I. 2 (S.D. Fla. July 24, 2008).

faith."[20] The impact of this decision on the investor community was widely reported, both in the Wall Street Journal[21] and the Life Settlements Report.[22]

And these are only *some* of the many facts that were (and are) available in the *public domain*. Thus, by the time Well Fargo was working with Berkshire to acquire the Policy in 2013, the sophisticated, multi-billion dollar investor market knew full-well that non-recourse financed policies like the Policy had massive insurable interest problems. And Wells Fargo knows full-well from *its own STOLI investor clients* that they factor this insurable interest risk into the price they are willing to pay to acquire those policies on the secondary and tertiary markets. *See, e.g.*, *Sun Life v. Wells Fargo*, 1:17-cv-06588, Doc. 166-3 at 107:8-108:17, 178:4-179:7,

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[20] *Pruco Life Ins. Co. v. Brasner*, 2011 WL 13117063, at *1-3, 7-9 (S.D.Fla. Nov. 14, 2011). The result in this case was overturned years later when the Florida Supreme Court held that, even though the policy was "STOLI," mere technical compliance with Florida's insurable interest statute was enough to comply with Florida's then-existing law. *Wells Fargo v. Pruco Life Ins. Co.*, 200 So.3d 1202, 1206 (Fla. 2016). That approach was, of course, the exact opposite of what this Court held in *Price Dawe*—that feigned technical compliance was unconstitutional and not enough under Section 2704(a)—and Florida's legislature later corrected Florida law to align with Delaware law. In any event, it remains that even the Florida Supreme Court found the Coventry scheme was STOLI.

[21] *Prudential Wins Ruling Over $10 Million Life-Settlement Case*, Wall Street, J., Dec. 12, 2011 (ruling is "particularly troubling to the investment community").

[22] *Florida Judge Lets Pruco Void Policy, Keep Premiums in $10M STOLI Case*, The Deal's Life Settlements Report, Nov. 17, 2011, available at https://pipeline.thedeal.com/article/27q2lwj0fm4tf75xqzqps/deal-news/federal-judge-allows-counterclaim-against-prudential-to-proceed (explaining that Coventry loan had been described as "smoke and mirrors").

273:5-24 (Dep. of Wells Fargo's tertiary market client, Vida Capital June 12, 2019) (conceding same in connection with Coventry policy).[23]

Thus, Wells Fargo is completely off base when it asserts that a finding in favor of the Estate will have a material negative impact on the investor market. The truth is that answering the certified questions in the Estate's favor will not *upset* the market's expectations; it will *fulfill* them by confirming what the market has known from the beginning: Policies originated through non-recourse premium financing programs like Coventry were wagers on human life and, if challenged, either by an insurer or an estate under Delaware law, those policies would be void *ab initio* and the wager would never pay off.

For all of these reasons, the answer to Question 1 must be "no."

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[23] This Coventry-procured policy was later held void *ab initio* for lack of insurable interest under Illinois law. *Corwell*, 2020 WL 1503641 (N.D. Ill. March 30, 2020).

CONCLUSION

This Court should uphold Delaware's clear constitutional prohibition on human life wagering and reject Wells Fargo's attempt to create absolute immunity from suit for itself and other agents like it who choose to serve those who invest in illegal wagers. Adopting the untenable rule suggested by Wells Fargo would subvert the Constitution by creating the absurd situation where a STOLI investor can use an agent to collect STOLI proceeds and hide itself from judicial scrutiny, thus effectively immunizing the STOLI investor in the process. This would do nothing to further Delaware's Constitution and public policy, and this Court should instead find that agents like Wells Fargo, who obtain STOLI proceeds for others, can be held liable for Section 2704(b) claims under normal agency principles.

<u>*/s/ Donald L. Gouge, Jr. (#2234)*</u>
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Dated: August 6, 2021