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 C.A. No. 19-14689 D.C. No. 1:17-cv-23136-MGC

CORRECTED REPLY BRIEF OF APPELLANT BERKSHIRE HATHAWAY LIFE INSURANCE COMPANY OF NEBRASKA

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INTRODUCTION

The Estate has no answer to Berkshire's arguments that well-established principles of statutory construction compel the conclusion that an innocent, good-faith purchaser may assert a defense under Section 8-502 of the Delaware Uniform Commercial Code ("UCC") in an action under Section 2704(b) of the Delaware Insurance Code. That result is dictated by two straightforward points. First, the Estate's Section 2704(b) action seeks the policy's *proceeds*, and Section 8-502 indisputably protects the right of parties like Berkshire to retain such proceeds. The Estate almost entirely ignores that point, no doubt because it is fatal to the Estate's arguments. Second, recognizing a defense under Section 8-502 is entirely consistent with Section 2704(b). Doing so gives full effect to *both* statutes by permitting a subset of defendants in Section 2704(b) actions—downstream investors who purchased a policy for value and without notice of an adverse claim—to assert the Section 8-502 defense that is available *in every other commercial context*. Giving effect to both statutes respects the prohibition on policies lacking an insurable interest while furthering Delaware's equally important objective of fostering stability in commercial transactions.

Lacking any response to Berkshire's statutory-construction arguments, the Estate pivots to meritless arguments that the Delaware Constitution and public policy demand that an insured's estate receive the proceeds of a void policy *in all* *circumstances*, notwithstanding Section 8-502 and the statutory-construction principles governing its relationship with Section 2704(b). Those arguments are not merely baseless as a legal matter; they are premised on a misconceived and deeply misleading narrative. In the Estate's telling, Ms. Malkin and insureds like her were somehow "victimized" (Estate.Br.1)[1] by their counterparties in the original insurance transaction and by innocent investors in the life-settlement market. Not so: Ms. Malkin knowingly and willfully chose to purchase a policy for investment purposes. Ex. A,[2] at 4. While she ultimately was unable to profit from that investment due to market conditions, she lost nothing, and other insureds in her position did profit. Ms. Malkin thus was a full participant in the invalid transaction—and her Estate stands in her shoes. Once the Estate's significant mischaracterizations are corrected, the absurdity of its position becomes clear: the Estate urges this Court to hold that the prohibition on certain forms of wagering requires that a void policy's proceeds be taken from an innocent investor that engaged only in *lawful* conduct and handed over *to an essential party to the original*

[1] "Estate.Br." refers to the Estate's corrected Answering Brief to Berkshire's Opening Brief.

[2] This brief uses the defined terms and citation forms adopted in Berkshire's Opening Brief.

unlawful wager. There is no justification—and the Estate offers none—for such an inequitable result.

The Court therefore should answer the first certified question in the affirmative and hold that a party in Berkshire's position may assert an affirmative defense under Section 8-502. The Court also should answer the second certified question in the affirmative and hold that a party in Berkshire's position may seek restitution of premiums it paid, consistent with well-established equitable principles.

ARGUMENT

I. UCC SECTION 8-502 PROVIDES AN AFFIRMATIVE DEFENSE IN AN ACTION UNDER SECTION 2704(b).

A. The Estate's arguments that the Delaware Constitution and public policy preclude recognizing a Section 8-502 defense are meritless.

The Estate spends the vast majority of its brief arguing that the Delaware Constitution and free-floating policy considerations weigh against giving Section 8-502 the same effect in Section 2704(b) actions that it has in all other commercial contexts. Those arguments are meritless, and the Estate's position is irrational at its core. The Estate, which stands in Ms. Malkin's shoes, *Pierce v. Higgins,* 531 A.2d 1221, 1226 (Del. Fam. 1987), urges the Court to hold that a void insurance policy's proceeds must be awarded to the heirs of the insured *who actively helped procure that illegitimate policy* "no matter what" (Br.19)—notwithstanding the justified reliance interests of the innocent downstream investor that purchased the policy without notice of the alleged insurable-interest problem. That would disregard the UCC's important policy of promoting commercial stability and undermine the life-settlement market that Delaware has chosen to foster.

Perhaps recognizing that its position falls on the wrong side of the policy interests at stake, the Estate predicates its constitutional and policy arguments on fundamentally misleading accounts of both the underlying insurance transaction and the life-settlement market. The Estate misstates the record to portray Ms. Malkin—

who chose to obtain the Policy for investment purposes, planned to sell it for a profit, and ultimately lost nothing in the transaction—as the victim of a fraudulent scheme perpetrated by her counterparties in the transaction, and by Berkshire and the many investors in the life-settlement market. Nothing could be further from the truth.

1. The Estate's constitutional and policy arguments are premised on mischaracterizations of the record and the life-settlement market.

The Estate mischaracterizes the circumstances of this case in important respects.

a. *The Policy's original procurement.* The Estate's constitutional and policy arguments begin from the false premise (Br.1) that Ms. Malkin was "victimized" by "a group of companies called 'Coventry'" when she applied for and obtained the Policy. The Estate relies on nothing other than its own characterizations, which the Eleventh Circuit's decision and the undisputed facts conclusively refute.

As the Eleventh Circuit explained, Ms. Malkin actively sought out life insurance broker Simba because she wanted to purchase insurance for investment purposes. Ex. A, at 4. Ms. Malkin decided to take advantage of a "risk free opportunity to make money" available to seniors "who did not wish to purchase life insurance for their own personal use, but who wanted to make money off of their life insurance capacity." *Id.* Far from lacking agency in the transaction, Ms. Malkin had a plan: to sell the Policy for a profit on the secondary market at the end of her loan term, using the proceeds to pay off the loan and pocketing the profit. A.166. The Estate has never contested that Ms. Malkin had that intent, and for good reason: Ms. Malkin memorialized her intent in a document drafted at her direction and expense by her personal estate-planning attorney, *id*., and Ms. Malkin's daughter—the Estate's representative—confirmed Ms. Malkin's plan in sworn deposition testimony, Dkt. 135-33, at 49. Ms. Malkin ultimately attempted to sell the Policy for a profit but was unable to do so, *id*.—unsurprisingly, given the recessionary downturn in the life-settlement market in 2008—and therefore relinquished her interest in the Policy to Coventry Capital as servicing agent for LaSalle Bank. Ex. A, at 7; A270 ¶ 121. Thus, although the "opportunity to make money," Ex. A, at 4, did not yield Ms. Malkin the profit she hoped for, nothing in the record suggests that she was a "victim[]" (Estate.Br.1) of anything other than poor market timing.

In holding that the Policy was void, the Eleventh Circuit did not question those undisputed facts or suggest that Ms. Malkin was somehow a victim of a scheme. The court explained that, under *Price Dawe*, the transaction was void for two reasons: (1) "either the person who is insured or the trustee must purchase the policy for lawful insurance purposes," and here Ms. Malkin never intended to keep the Policy as life insurance, Ex. A, at 16; and (2) Ms. Malkin did not pay premiums out-of-pocket, because the premiums were funded by a nonrecourse loan, and Ms.

Malkin was unable to sell the Policy for a sum that would have allowed her to repay the loan and keep the profit, *id*. at 18. For those reasons, the Eleventh Circuit held that, under *Price Dawe*, Coventry Capital—not Ms. Malkin—should be deemed as a matter of law to have procured the Policy, in violation of the insurable-interest requirement.[3] Ex. A, at 19; *PHL Variable Ins. Co. v. Price Dawe 2006 Ins. Tr., ex rel. Christiana Bank & Tr. Co.*, 28 A.3d 1059, 1075 (Del. 2011).

That determination does not even suggest, much less establish, that Ms. Malkin was somehow victimized in the transaction. Indeed, as *Estate of Beverly E. Berland v. Lavastone Capital LLC* demonstrates, insureds who entered into such transactions could and did sell their policies for a profit on the life-settlement market. *See* Ex. F. A transaction that contemplates that an insured can sell her policy for a profit might be void under *Price Dawe* (as the Eleventh Circuit held)—but it does not victimize the insured. To the contrary, the insured is a full and vital participant in the transaction. Thus, while the Estate (Br.5, 7-9) repeatedly characterizes the Policy's procurement as an "illegal wager," this Court should bear in mind that *Ms. Malkin herself* was an essential and willing party to that purported "wager."

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[3] Berkshire respectfully disagrees, and reserves the right to request reconsideration if appropriate in light of this Court's forthcoming decision in *Estate of Beverly E. Berland v. Lavastone Capital LLC*. Opening.Br.14 n.4.

b. *The life-settlement market*. The Estate's constitutional and policy arguments also depend on its repeated assertions (Br.12, 21, 25, 33) that downstream investors participating in the life-settlement market are somehow complicit in evading the insurable-interest requirement. Not so.

Unlike Ms. Malkin, downstream investors like Berkshire are *not* parties to any "illegal wager." While Delaware law prohibits a third party from *procuring* a policy on the life of another, it expressly authorizes third parties to purchase *already-existing* life insurance policies, regardless of whether the third party has an insurable interest. 18 *Del. C.* §§ 2720, 2704; *see Price Dawe*, 28 A.3d at 1074. Investors who purchase policies are participating in a market that Delaware has chosen to promote, and that benefits insureds by enabling them to monetize unwanted policies. Opening.Br.7, 15. And an investor who satisfies the elements of the Section 8-502 defense necessarily has purchased its policy without notice of any allegation that the policy was procured illegitimately—which means the investor had no part in the policy's original procurement and no knowledge of or statutory duty to investigate a claim of invalidity. Thus, a downstream investor who satisfies Section 8-502 has engaged in precisely the type of legitimate commercial conduct Delaware has chosen to protect by enacting the UCC to promote reliance interests and commercial stability.

Attempting to justify disregarding those strong reliance interests, the Estate seeks to shift blame for invalid policies from the insureds and third parties who procure them to downstream investors who unknowingly purchase them. The Estate thus asserts (Br.21) that "STOLI [policies are] created to meet the 'demand' of downstream investors," whose "appetite drove their creation." But as *Price Dawe* makes clear, investor demand is for legitimate insurance policies, not illegitimate ones—the "STOLI" problem is a "supply side" phenomenon. 28 A.3d at 1069-70. That makes sense. No prudent investor would knowingly purchase a policy issued without a valid insurable interest, because the insurer would be entitled to refuse to pay the death benefit.[4] Investors like Berkshire do not set out to buy invalid policies; the attraction of life insurance policies as an investment is that they offer a predictable vehicle whose performance is not tied to the overall economy. Berkshire.Opening.Br.15. Claims that a policy is invalid undermine the very purpose of the investment by destroying predictability and imposing substantial transaction costs. Investors thus end up purchasing invalid policies only because detecting them, years after the initial transaction, is extremely difficult. Berkshire.Opening.Br.35.

[4] The Estate's assertion (at 21) that "most" invalid policies are not challenged by insurers is unsupported and is contradicted by the many cases the Estate cites involving insurers refusing to pay. Estate.Br.19, 22-26, 28-29.

c. *Berkshire's role in the transaction.* The Estate also claims (Br.11) that Berkshire itself was somehow complicit in the underlying void transaction, asserting for the first time that "Berkshire was a direct participant with a significant financing stake in" the "Coventry-Lavastone STOLI program." That is false—and if the accusation had even the slightest basis in fact, the Estate surely would have asserted it before now. The Estate (Br.11) egregiously misconstrues deposition testimony regarding an unrelated two-year arrangement between Berkshire and Lavastone (an AIG unit that purchased policies on the life-settlement market) to invest in legitimate life settlements. The Estate thus attempts to convey the misimpression that Berkshire funded premium payments on STOLI policies on behalf of individual insureds when the insureds still held the policies. In fact, Berkshire did no such thing, and it had no involvement in any "Coventry-Lavastone STOLI program." The testimony makes clear that Berkshire was simply involved in purchasing policies on the life-settlement market from licensed life settlement providers, and *then* paying premiums on the policies in order to eventually receive their proceeds. B336. That is entirely routine, lawful conduct that has no connection to this case, and the Estate's mischaracterization of it is beyond the pale.

Finally, in an effort to distract from the legal issues on which this case turns, the Estate attached to its Amicus Response Brief a press report regarding a confidential settlement between Berkshire and Coventry-affiliated entities concerning indemnification for the Estate's claim. Although the Estate has consistently alleged such an indemnification agreement and Berkshire has not denied it, the agreement is not part of the record because the district court correctly concluded that it is irrelevant to the legal issues. Dkt. 112. No element of the Section 8-502 defense turns on the absence of an indemnification arrangement. More generally, such arrangements with third parties are irrelevant to the proper resolution of the legal dispute between parties before the court, including because the rule announced by the court will apply even where no indemnification arrangement exists. *See, e.g.*, *JSI Commc'ns v. Travelers Cas. & Sur. Co. of Am.*, 807 F.3d 725, 729 (5th Cir. 2015) (rejecting argument that indemnification agreement with third party should affect how court should decide the dispute between the parties before it); *LeBlanc v. Glob. Marine Drilling Co.*, 193 F.3d 873, 876 (5th Cir. 1999); *Chem. & Fiberglass Corp. v. N. River Ins. Co.*, 908 F.2d 825, 833 (11th Cir. 1990). Indemnification should have no bearing on this Court's resolution of the legal questions presented.

2. The Delaware Constitution does not preclude recognizing the Section 8-502 defense in Section 2704(b) actions.

With the Estate's misstatements corrected, its constitutional and policy arguments fall apart. The Estate first contends that, if an insurer pays out the proceeds of a void policy, the Delaware Constitution *requires* that the "money must be paid over to the insured's family," Br.19, and that no other party, including an innocent downstream investor, may receive the death benefit, "without exception," Br.18. That is not only wrong; it leads to a perverse result. The Estate urges this Court to enforce the constitutional prohibition on wagers by holding that the proceeds must always be awarded to the estate that stands in the shoes of *one of the parties to the "wager*."

a. The Constitution does not require such a bizarre result. The provision on which the Estate relies—Article II, Section 17—is a general prohibition on gambling, with certain exceptions. Del. Const., art. II, § 17. *Price Dawe* explained that life insurance policies lacking an insurable interest fall within the constitutional provision on wagers. 28 A.3d at 1070-71, 1078. The Constitution therefore establishes that such policies are void. But it says nothing about the *consequences* of invalidity, or what should happen when an innocent downstream investor purchases such a policy, pays premiums, and receives the proceeds in return for value.

The Estate therefore argues (Br.16) that recognizing an innocent downstream investor's right under Section 8-502 to retain a void policy's proceeds would undermine the constitutional prohibition on wagers by "allow[ing] an illegal wager to pay off." That is wrong for at least two reasons. First, recognizing the Section 8-502 defense here does not require a court to *enforce* a void policy. In a Section

2704(b) suit, the contract necessarily has already been fully performed—the insurer has paid the proceeds, and the policy has terminated by its own terms. For the reasons explained in Berkshire's opening brief and below, *see* pp. 19-21, *infra*, holding that an investor in Berkshire's position has satisfied Section 8-502's elements does not in any way require a court to find that the underlying policy was lawful or to enforce any rights it purported to confer.

Second, as explained above, an investor entitled to avail itself of Section 8-502 is not a party to any "wager." An innocent downstream investor who purchases a void policy (potentially after it has changed hands multiple times, as here) does not become complicit in the original invalid transaction. The principles animating Section 8-502 and similar UCC protections reinforce that conclusion. Section 8-502 protects a purchaser who innocently acquires a financial asset even if the seller of the asset *stole* it from the original owner. 6 *Del C.* § 8-502 cmt. 3 ex. 2. The purchaser without notice is thus considered innocent of the initial wrongdoing, and Section 8-502 reflects the conclusion that protecting an innocent purchaser's right to an asset does not condone the original theft. So too here: permitting an innocent investor, rather than the Estate of the insured who entered into the "wager," to retain the Policy's proceeds does not allow an "illegal wager" to "pay off" (Estate.Br.16) or "create[] a wagering exception" for downstream investors (Estate.Br.22).

b. Even more to the point, the Estate's argument is nothing short of absurd. The Estate asks this Court, in the name of the constitutional prohibition against gambling, *to recreate the result of the original "wager"* by giving the death benefit over to the heirs of one of the two parties to that "illegal" transaction. As between the Estate—which stands in the shoes of Ms. Malkin, who chose to engage in the illegal transaction—and Berkshire—which lawfully purchased a policy it believed was valid after receiving warranties to that effect—the Estate suggests no good reason why the Constitution would require the proceeds to go to the Estate.

Of course, Section 2704(b) reflects a legislative judgment that an estate may seek a void policy's proceeds in some circumstances. But it does not reflect a judgment that Delaware's Constitution or public policy requires the counterintuitive result that the Estate seeks here. Statutes like Section 2704(b) apply to a broad range of situations having nothing to do with the life-settlement market, including those in which an insured actually is defrauded by a third party who procures an invalid policy on the insured's life without the insured's willing participation. The Estate's own cases (Br.19-20) prove that point. *See, e.g.*, *Cundiff v. Cain*, 707 So.2d 187, 190 (Miss. 1998) (statute used against beneficiary who forged insured's name on application); *Froiland v. Tritle*, 484 N.W.2d 310, 313 (S.D. 1992) (statute used against beneficiary who procured policy in agreement with insured but wrongfully attempted to keep full proceeds). Indeed, when Section 2704(b) was enacted, the life-settlement market did not yet exist.

c. Finally, the Estate asserts (Br.19) that the "longstanding majority rule" is that an estate must receive a void policy's proceeds, "no matter what." That, too, is wrong. The Estate does not identify a *single* case (and Berkshire is aware of none) in Delaware or any other State in which a statute like Section 2704(b) has been applied to permit the insured's estate to recover proceeds from an innocent downstream investor who satisfies the UCC's requirements. The cases on which the Estate relies (Br.19) merely allowed estates to recover proceeds from the wrongdoer who harmed the insured in the original unlawful insurance transaction.

The Estate also argues (Br.25-26) more generally that courts have disallowed affirmative defenses in cases involving policies lacking an insurable interest. But none of the Estate's cases involve affirmative defenses asserted by an innocent investor against an estate. Thus, in cases between two contractual counterparties (such as a policyholder and insurer), courts have declined to recognize defenses such as estoppel where doing so would require the court to *enforce* a void contract. Estate.Br.25-26 (citing cases). So too in *Price Dawe*, where this Court rejected an affirmative defense that required enforcing a void policy's incontestability clause. 28 A.3d at 1066-67. The principle that courts do not enforce void contracts is not implicated here. The Estate also cites (Br.23) cases involving equitable defenses whose *elements* require the court to assess the equities of the particular case. *See, e.g.*, *In re HealthSouth Corp. S'holders Litig.*, 845 A.2d 1096, 1108 (Del. Ch. 2003) (declining to apply unclean hands, which "is primarily a matter of public policy," where its application "would work an injustice"), *aff'd*, 847 A.2d 1121 (Del. 2004). Putting aside Ms. Malkin's participation in the "illegal" transaction, those cases do not suggest that courts may freely decline to recognize generally-applicable defenses for free-floating policy reasons. And in all events, cases involving common-law defenses with equitable elements are irrelevant to a statutory defense like Section 8-502, whose elements reflect a legislative determination as to when the defense is justified.

3. **The Section 8-502 defense may not be disregarded based on the Estate's meritless "public policy" arguments.**

The Estate's arguments (Br.23-26) that Section 8-502—which applies without exception in every other commercial context—"cannot be invoked" in *this* context as a matter of "public policy" are equally meritless. Section 8-502 and Section 2704(b)'s interaction is a matter of statutory construction, not of freewheeling policy analysis better suited to the General Assembly. But in all events, public policy considerations weigh decisively in Berkshire's favor.

a. As Berkshire explained (Opening.Br.28-29, 31-36), because statutory rights of action are presumptively subject to statutory defenses, the provision of a right of action has never been understood to reflect a policy judgment that plaintiffs should prevail on the merits in *all* instances. That is particularly true here. While Section 2704(b) does not reflect any legislative determination specific to the life-settlement market, *see* pp. 13-14, *supra*, Section 8-502 protects the rights and expectations of innocent participants in Delaware's life-settlement market. There is no conflict between the policies underlying Section 2704(b) and Section 8-502, properly understood.

The Estate nonetheless argues (Br.19) that public policy would be offended if, pursuant to Section 8-502, an innocent downstream investor was permitted to retain a void policy's proceeds. But the Estate offers no plausible explanation why public policy would favor the estate of an insured who was a full participant in, and planned to profit from, an invalid insurance transaction over an innocent downstream purchaser. Grasping at straws to explain why public policy would favor a good-faith purchaser over a party to an illegal wager, the Estate argues (Br.20-21) that downstream investors in the life-settlement market are somehow complicit in invalid transactions like the one into which Ms. Malkin entered. But that is wrong for the reasons stated above. *See* pp. 7-9, *supra*.

The Estate is also wrong in arguing that Section 2704(b) must categorically override Section 8-502 to deter investors from purchasing unlawful policies. Because it is difficult to detect invalid policies, abrogating Section 8-502 in Section

2704(b) suits—thereby imposing a strict-liability regime on downstream purchasers—would stifle demand for *all* policies by increasing transaction and litigation costs in the market as a whole. That would destabilize Delaware's life-settlement market, which would have severe negative consequences both for innocent investors and for innocent insureds who want to sell their policies. *See* Del. Bankers' Ass'n Br.6-10; Institutional Longevity Mkts. Ass'n ("ILMA") Br.7-12. The General Assembly did not choose to sacrifice the entire life-settlement market (worth billions of dollars) to stifle invalid life insurance transactions, and doing so would undermine Delaware's policies in favor of the market and the legitimate reliance interests of innocent participants in that market. And since the Estate's arguments for disregarding Section 8-502 could be made in virtually any other context, adopting its proposed rule could have severe negative consequences in other Delaware financial markets as well. *See* Del. Bankers' Ass'n Br.11-12.

Moreover, it is the *Estate's* position that encourages more invalid transactions. Under its view, an insured like Ms. Malkin may enlist a third party's aid in procuring a policy; knowingly and willfully enter into an illegal wagering transaction; sell the policy for a profit if possible (as in *Berland*), or relinquish it at no cost (as here); and rest assured that if the insurer pays the proceeds to the policy's ultimate purchaser, her heirs can use Section 2704(b) to obtain a multimillion-dollar windfall—even if the insured already profited from selling the policy, and even at the expense of an innocent market participant. That truly is a "risk free opportunity to make money," Ex. A, at 4—twice over—and sophisticated individuals will no doubt avail themselves of it. The Estate offers no reason whatsoever to think the General Assembly would reward insureds and their estates for helping create void insurance policies, while placing the economic risk of those policies squarely on secondary-market participants who engaged in no proscribed conduct. To the contrary, the legislature has made the opposite choice, by enacting the UCC.

B. A party in Berkshire's position is entitled to the Section 8-502 defense in an action under Section 2704(b).

The Estate barely addresses the statutory-construction principles at the heart of this case. The entitlement of a party in Berkshire's position to assert a defense under Section 8-502 in an action under Section 2704(b) turns on two questions of statutory construction: first, whether a party like Berkshire satisfies the elements of Section 8-502, and second, whether, under the principles governing harmonization of two statutes, Sections 2704(b) and 8-502 both may be given full effect. The answer to both questions is yes.

1. A party in Berkshire's position satisfies the elements of the Section 8-502 defense.

The Estate contests Berkshire's satisfaction of the Section 8-502 defense in only two respects.

a. The Estate first argues (Br.26-31) that the Section 8-502 defense is not available because the Policy is void. The Estate does not explain, however, what element of Section 8-502 is negated in this case by the Policy's invalidity. Section 8-502 protects a party that received a security entitlement to a "financial asset" for value and without notice from "adverse claims." The "financial asset" at issue in this case is the $4,013,976.47 that represents the Policy's proceeds, not the Policy itself, *see* 6 *Del. C.* § 8-102(a)(9)(iii), and the Estate does not contend otherwise, Br.31. The proceeds unquestionably exist; the Policy has been reduced to proceeds and is no longer in effect. The Estate appears to contend (Br.30) that because Section 8-502 provides a defense against an "adverse claim"—defined as an assertion of a "property interest in a financial asset"—the provision does not "cover[]" a void policy. But an "adverse claim" is the property interest asserted by the *claimant*—here, the Estate. And the only property interest that Section 2704(b) permits the Estate to assert is in the Policy's "benefits." 18 *Del. C.* § 2704(b). The Estate thus attempts to have it both ways, seeking the proceeds while attempting to bootstrap the *Policy's* invalidity to avoid Berkshire's defenses with respect to those same *proceeds*.

In a footnote, the Estate protests (Br.31 n.13) that assessing the Section 8-502 defense as to the proceeds is "form over substance." It is anything but. Berkshire's focus on the proceeds is dictated by the *statutory text* of Section 8-502, which requires identifying the "financial asset" that Berkshire received and to which the Estate asserts a claim—here, indisputably, the proceeds—as well as by Section 2704(b) itself.

The Estate also argues (Br.31 n.13) that, because the Policy was invalid, Berkshire had no valid contractual right to receive the benefits from AIG, the insurer. Even if that is correct, it is irrelevant under Section 8-502, which does not examine whether the security entitlement holder (Berkshire) received the financial asset (the proceeds) through the performance of a valid contractual obligation; through the gratuitous performance of a void contract by the insurer, as happened here; or through some other means of acquisition. Rather, Section 8-502 requires only that Berkshire have acquired a security entitlement in the proceeds for value and without notice. Berkshire acquired a "security entitlement"—defined as rights *against the securities intermediary*, and therefore not contingent on the Policy's validity—when Wells Fargo, as securities intermediary, accepted the Policy's proceeds for credit to Berkshire's securities account. A183-184 § 2(c)-(d); A194-197; A89-90 ¶¶ 9-12; 6 *Del. C.* §§ 8-102(a)(9), 8-102(a)(17) & cmt. To acquire a security entitlement "for value," Berkshire need only have given "any consideration sufficient to support a simple contract"; it need not have done so pursuant to a *valid* contract. 6 *Del. C.* § 1-204. Berkshire's payment of the premiums (and purchase price) satisfies that element, and the Estate does not contend otherwise. Thus, no element of Section 8-

502 would require the Court to find the Policy valid or enforce its terms. Berkshire.Opening.Br.22-24.

Finally, the Estate relies (Br.26-29) on cases holding that bona fide purchaser principles do not enable a purchaser to claim a property interest when the deed purchased is void. Berkshire already has explained that those cases—none of which involve Section 8-502—are inapposite. The Section 8-502 defense is available if its statutory elements are fulfilled—as they are in this case. And in the Estate's cases, recognizing the bona fide purchaser's right to the property would require *enforcing* the void deed by upholding the purchaser's property rights as against others. That concern is not implicated here.

Relatedly, the Estate contends (Br.29) that Berkshire "admitted" that a void policy conveys "nothing" in seeking indemnification. But Berkshire simply restated an undisputed legal point: a valid policy conveys a *right* to have the insurer pay the death benefit, and a void policy does not. Again, that has nothing to do with the Section 8-502 defense.

b. The Estate also argues (Br.35-36) that Berkshire cannot invoke the Section 8-502 defense because it had notice of the Estate's adverse claim. While ordinarily that argument might raise a factual question, it does not here. "Notice" is defined as actual knowledge, or deliberate avoidance of actual knowledge, "of the adverse claim"—that is, the claim that the Estate asserts *in this suit*—or a violation of a statutory or regulatory duty to investigate. 6 *Del. C.* § 8-105(a) & cmt. 3. The Estate has never argued that Berkshire possessed any of those forms of knowledge. To the contrary, the Estate forfeited the issue of notice by contending at summary judgment that whether Berkshire had notice was "irrelevant" and by failing to make any substantive argument as to notice, *see* Dkt. 147, at 16; Berkshire 11th Cir. Resp. & Reply Br.42 n.15. In any event, undisputed facts establish that Berkshire lacked the required notice of the Estate's claim, which it first asserted in 2017, when Berkshire received a security entitlement in the Policy's proceeds in 2013. Berkshire received representations and warranties when it purchased the Policy that there was no insurable-interest issue,[5] and the Estate did not assert its claim by filing suit until years *after* Berkshire received the Policy's proceeds. Nor has the Estate ever identified any statutory or regulatory duty to investigate.[6]

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[5] Remarkably, the Estate invokes (Br.35-36) the purchase agreement's representation that none of the policies Berkshire purchased "originated in connection with a STOLI transaction," A208 § 4.08(c), as evidence that "Berkshire obviously knew" that the opposite was true. That is not how warranties work. And in its response to the amicus briefs (at 26 n.15), the Estate argues that the *lack* of warranties in *other* institutions' purchase agreements is evidence that those institutions "knew" the policy was invalid. The Court should reject both arguments.

[6] In *SEC v. Credit Bancorp*, the court held that a securities intermediary had notice of certain adverse claims because its agent had reviewed press releases that *expressly asserted the adverse claims* and announced the filing of two corresponding lawsuits. 386 F.3d 438, 451-52 (2d Cir. 2004) (cited in Estate.Br.36). That is actual knowledge of the adverse claim asserted.

Instead, citing no authority, the Estate attempts to redefine "notice" as encompassing mere awareness that *other* policies in *other* cases had been challenged as lacking an insurable interest. But Section 8-502 defines notice as "notice of *the* adverse claim"—that is, the specific claim asserted here. 6 *Del. C.* § 8-502 (emphasis added). And, as the Estate acknowledges (Br.35), its argument would render Section 8-502 unavailable to "the entire market" of life-settlement purchasers. The Estate's argument is thus another attempt to nullify the Section 8-502 defense entirely.

The Estate also makes (Br.12) a number of baseless allegations—without citation to the record—that Berkshire "knew" various purported facts, such as that the company that reviewed the policies Berkshire purchased for insurable-interest issues was not "reliable." Putting aside the unsupported and improper nature of these allegations, they are irrelevant, as they do not suggest that Berkshire had the required notice of the Estate's adverse claim.

Finally, the Estate argues (Br.36 n.17) that it needs more discovery to investigate whether Berkshire had notice. The Estate forfeited that argument: if it believed that it needed further discovery to contest Berkshire's summary judgment motion on the UCC, it should have requested it, rather than contending only that notice was irrelevant. *See* Dkt. 147, at 16.

2. **Based on well-established principles of statutory construction, Section 8-502 should be given full effect in <u>Section 2704(b) actions.</u>**

The Estate devotes less than a page of its answering brief (at 34) to the core statutory-construction question that controls this case: whether Sections 2704(b) and 8-502 can both be given full effect. As Berkshire's opening brief explained (at 27-31), the two statutes are not in conflict, and can be harmonized, because Section 8-502 merely gives *some* Section 2704(b) defendants an affirmative defense. Besides incorrectly asserting that affirmative defenses are not available in cases involving void policies, *see* pp. 14-15, *supra*, the Estate does not challenge the proposition that causes of action can be subject to defenses without creating any statutory conflict. Berkshire.Opening.Br.28-29 (citing cases); *cf*. Estate.Br.26 & n.13.

Even if there were an irreconcilable conflict, Section 8-502 prevails as the later-enacted statute. The Estate contends (Br.34) that Section 2704(b) "controls because it is obviously the more specific statute on insurable interest." But a statute providing a cause of action could always be characterized as more specific *about the cause of action itself*. If that were enough to warrant setting aside generally applicable affirmative defenses, no statutory cause of action would ever be subject to such defenses. In any event, to control in the event of a conflict, Section 2704(b) would also have to be the later-enacted statute, *State v. Fletcher*, 974 A.2d 188, 193

(Del. 2009), and it is not. Section 8-502 is the later-enacted statute for harmonization purposes because it was reenacted in a 1997 "major revision" that substantially broadened the Section 8-502 defense.[7] Del. Code Ann. tit. 6 art. 8, Refs & Annos, Prefatory Note; *see Bash v. Bd. of Med. Prac.*, 579 A.2d 1145, 1151 (Del. Super. 1989); Berkshire.Opening.Br.30 n.7. The Estate's erroneous characterization of Section 8-502 as "essentially identical" to its predecessor (Br.34) is yet another mischaracterization.

[7] Contrary to the Estate's contention (Br.18 n.5, 34 n.16), 18 *Del C.* § 5925(c), which concerns bankrupt insurers' fraudulent transfers of property, does not suggest legislative consideration of innocent-purchaser principles in any context relevant here.

II. EVEN IF THE ESTATE WERE ENTITLED TO THE PROCEEDS, BERKSHIRE WOULD BE ENTITLED TO RECOVER THE PREMIUMS IT PAID.

As the Estate concedes (at 37-39), courts uniformly have held that, to prevent unjust enrichment, restitution is available to recover the premiums paid on a policy later deemed void for lack of an insurable interest. That conclusion flows from well-established equitable principles, including in cases where an insured's heirs sought to recover the death benefit of a policy lacking an insurable interest from the wrongdoing third party that procured the policy. Berkshire.Opening.Br.38-42; Del. Bankers' Ass'n Br.13 & n.5 (citing cases). Those principles counsel even more strongly in favor of recognizing an unjust enrichment counterclaim here, where the insured's heirs seek recovery from an *innocent* third party. The Estate briefly offers a few responses, all unavailing.

First, the Estate argues (Br.39) that Section 2704(b) provides that an estate may recover "any benefits" paid, not "net" benefits. But as Berkshire explained, Opening.Br.42-44, that the statute provides a right of action to recover "any benefits" does not "plainly or clearly manifest[]" a legislative intent to displace the common law's restitutionary offset. *A.W. Fin. Servs., S.A. v. Empire Res., Inc.*, 981 A.2d 1114, 1122 (Del. 2009); *Pierson v. Ray*, 386 U.S. 547, 554 (1967). The Estate's contrary argument relies solely on an unreported district court case holding that the term "benefits" in an Oklahoma statute did not itself provide authority to set off policy proceeds against premiums paid. *Tillman v. Camelot Music, Inc.*, 2005 WL 3436484, at *2 (N.D. Okla. Dec. 14, 2005). As the court there took care to note, no unjust-enrichment or other equitable set-off claim was at issue. *Id*. Here, Berkshire does assert an equitable counterclaim, and it is undisputed that there is ample authority under Delaware law permitting a set-off for unjust enrichment to recover the premiums paid on a void policy.

Second, the Estate argues (at 39-40) that its purported entitlement to the proceeds is unrelated to Berkshire's payment of premiums. But as Berkshire explained, the two are directly related because, but for Berkshire's payment of premiums, the Policy would have lapsed, the insurer would not have paid a claim, and there would be nothing for the Estate to recover. Opening.Br.39-40.

Third, the Estate contends (at 40-41) that even if a restitutionary set-off is available, Berkshire has not met its "burden of proof." That factual contention, based on the Estate's erroneous arguments about notice, *see* pp. 21-24, *supra*, is irrelevant. The issue having been decided on a motion to dismiss, Berkshire had only to plead the elements of its unjust-enrichment claim, which it did. Berkshire.Opening.Br.38-40.

Finally, the Estate (at 40-42) argues that Berkshire can pursue a claim only against the party with which it was in "contractual privity." But an unjust enrichment claim does not require a contractual relationship between the parties, *see Schock v.*

Nash, 732 A.2d 217, 232 (Del. 1999), or any net financial loss, *see Nemec v. Shrader*, 991 A.2d 1120, 1130 n.37 (Del. 2010). And where a party is unjustly enriched, equity does not permit that party to retain its unjust gains by redirecting the aggrieved party's demand for recompense to an indemnitor or other third party. *See Metcap Sec. LLC v. Pearl Senior Care, Inc.*, 2009 WL 513756, at *6 (Del. Ch. Feb. 27, 2009); *Mort v. United States*, 86 F.3d 890, 892 (9th Cir. 1996).

CONCLUSION

For the foregoing reasons, this Court should hold that the UCC Section 8-502 defense is available to defendants in a Section 2704(b) action and that a party in Berkshire's position may be entitled to offset any award to the estate by the amount of premiums it paid.

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