IN THE UNITED STATES DISTRICT COURT

IN AND FOR THE DISTRICT OF DELAWARE

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PHL VARIABLE INSURANCE COMPANY, : CIVIL ACTION
:
Plaintiff, :
v :
:
ESF QIF TRUST, by and through its :
trustee, DEUTSCHE BANK TRUST COMPANY, :
INC., : NO. 12-317-LPS
Defendant. :

PHL VARIABLE INSURANCE COMPANY,
: CIVIL ACTION
Plaintiff, :
v :
:
ESF QIF TRUST, by and through its :
trustee, DEUTSCHE BANK TRUST COMPANY, :
INC., :
: NO. 12-319-LPS
Defendant.

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Wilmington, Delaware
Thursday, November 8, 2012
Oral Argument Hearing

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BEFORE: HONORABLE **LEONARD P. STARK**, U.S.D.C.J.

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APPEARANCES:

CONNOLLY BOVE LODGE & HUTZ, LLP
BY: CHAD S.C. STOVER, ESQ.

and

EDISON, McDOWELL & HETHERINGTON, LLP
BY: JARRETT E. GANER, ESQ., and
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(Houston, Texas)

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APPEARANCES: (Continued)

FARNAN, LLP
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and

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P R O C E E D I N G S

(REPORTER'S NOTE: The following oral argument hearing was held in open court, beginning at 2:36 p.m.)

THE COURT: Good afternoon.

(The attorneys respond, "Good afternoon, Your Honor.")

THE COURT: Let's have you put your appearances on the record for me, please.

MR. STOVER: Good afternoon, Your Honor. Chad Stover from Connolly Bove Lodge & Hutz for plaintiff. And with me today are Jarrett Ganer and Eunice Kuo from Edison, McDowell, and Hetherington in Houston, Texas.

THE COURT: And you are here for the plaintiff; correct?

MR. STOVER: Plaintiff, yes. Correct.

THE COURT: Thank you.

Mr. Farnan looks familiar.

MR. FARNAN: Good afternoon, Your Honor. Brian Farnan on behalf of ESF QIF. With me is Steven Sklaver from Susman Godfrey in Los Angeles, California.

THE COURT: Good afternoon to you as well. We are here on two different cases to hear argument on the plaintiff's motion to dismiss the counterclaims from the defendant. So we'll hear from the plaintiff first, please.

MR. GANER: Good afternoon, Your Honor. Jarrett Ganer with Edison, McDowell, and Hetherington.

Earlier this year, following last year's opinion by the Delaware Supreme Court in the *Price Dawe* case which reaffirmed that under Delaware law, an insurer can contest the validity of the life insurance policy even after the expiration of the policy's contestability period and setting out various factors to determine whether a policy was in fact issued in compliance with Delaware's insurable interest law or is an illegal and prohibited wage earner contract.

Following that decision, PHL Variable Insurance Company filed suits to seek to have a declaration that six insurance policies governed by Delaware law were void for lack of insurable interest. Two of those policies are involved, are owned by the defendant ESF QIF Trust, which I'm going to refer to as "the trust" today because those letters I can't quite keep straight, and were brought in two separate actions.

That trust responded by, in the Griggs action, filing a counterclaim seeking to expand the action to include 14 additional policies issued by PHL Variable Insurance Company purportedly also owned by the same trust that Phoenix has not sought to invalidate. Under all 14 of those policies, there are zero debts, zero claims submitted. There has been no representation by Phoenix that it intends to collect, that it intends to challenge the policies or that it will not pay the policies if a death claim is submitted. Quite simply, PHL Variable has taken no action with respect to those 14 policies.

Despite that fact, the trust seeks a declaration that the policies were issued in compliance with Delaware insurable interest law and that a death claim submitted in the future must be paid. This is an advisory opinion, pure and simple, and is simply a way to try to expand what is otherwise already a complicated action involving a $10 million death claim into a much larger case.

THE COURT: Do you acknowledge that if your client has no intention of paying on those policies that you're not providing insurance and you are not providing any benefit to whoever holds that policy?

MR. GANER: If my client had actually formed an intent and actually followed through with that intent, that is the key. Even if my client has an intent, until they actually get a claim and deny it, they have not failed to provide anything that they're contractually obligated to provide.

THE COURT: Is that quite true even if what you're providing is insurance? Let's just stipulate for the moment, let's take a hypothetical policy, your client has no intention of paying it today. They could change their mind tomorrow, but today they have no intention of paying it. What product or service are you providing at that point? Are you really providing insurance today if your intention is not to pay?

MR. GANER: Well, you have to look at what the contract says. And the contract says that there is nothing that is actually due, there is no payment that is affirmatively due until the insurer's death.

What the company is providing, these are universal insurance policies so they're going to accumulate value based on the performance of the company. So there actually is, even if the company had an intent not to pay a death benefit

when it became due, there is still an accumulation of value and a savings component that is occurring within the policy. So even in that situation, there is still some value that is being transmitted, a service that is being provided.

THE COURT: What about this New York Supreme Court case? Doesn't that go against you on this very point?

MR. GANER: The lower court did go against Phoenix but it was a very different issue. The issue in that case was a discrete issue of whether or not Phoenix had the ability to challenge a policy after due to the fact that the contestability period had expired. In other words, the plaintiff came to Court and says I've got a policy that the contestability period has expired. There is a New York Superior Court opinion that says that an insurance company cannot challenge a policy even for lack of insurable interest after that.

I think Phoenix is going to do that based on the fact that they're doing that in these other cases, and I want a declaration that under this particular area of New York law and under this particular contestability statute that legally they don't have the right to do that. That is very different than here where they're coming in and saying here is 14 policies and I want an adjudication of whether all of these policies comply with Delaware insurable interest law and where Phoenix has taken no position to the

contrary with respect to any of those policies.

Then, of course, there is the much more similar opinion out of the Central District of California that was submitted as a supplemental briefing that was decided a day after this case, which is directly on point, which deals with a receiver trying to get an affirmation from Phoenix that Phoenix was going to pay for the policy and basically making the same allegations: that Phoenix has a pattern and practice of denying claims, challenging other policies. The Court there correctly held that all they were looking for was an advisory opinion and that Phoenix had taken no position to the contrary and indicated they weren't going to pay.

THE COURT: What about *Step-Saver*? You don't say much about that in your briefing.

MR. GANER: Well, we don't say much about *Step-Saver* within our initial brief. We do address it in our reply brief. Our initial brief relies on sort of the initial cases that underlie on *Step-Saver*.

But when you take a look at the *Step-Saver* factors, the first item is: adversity of interest.

They haven't shown adversity of interest here. They are saying that we believe our policies are valid and you have taken no opinion on the issue. Where is the adversity there? The adversity is, well, we think the

market is devaluing our policies and we think the market is doing that as a result of actions you are taking with other policies and just generally your business practices and your litigation practices. That is not a adversity of interest between the two parties on the subject matter they're trying to sue on.

THE COURT: Now, would you say that even if it were a fact that today your client does not intend to pay these policies upon death?

MR. GANER: If my client had communicated their intent. The fact that my client privately holds an intent that has been communicated to no one I think is completely irrelevant.

THE COURT: All right. Your client, of course, is an entity. What if there is an internal document from your client that says the following 14 policies will not be paid upon death? Do we have adversity yet?

MR. GANER: Not until they actually either communicate that to the party, to the other side. You know, my client is one side of a contract. Until we actually take some action that communicates our intentions to the other side of the contract, or they -- you know, that would actually be a communication towards them. That would put them on notice. That would create an adversity between the two parties.

THE COURT: What if it's not a communication directly to them but it sort of slips out and the newspaper gets ahold of it, so they learn of it but you didn't intend for them to learn of it?

MR. GANER: If my client has publicly disclosed it to the point where it has gotten into a newspaper, I think that would be a different story.

However, if it's just a matter of, well, there is other litigation going on and the newspapers are talking about your denial rates and it's nothing specific to where there is a newspaper article that says "here is this internal document," and it identifies these four policies, and it says at the bottom, "we will not under any circumstances pay these claims," and my client is essentially allowed that to become a press release, that is a different story.

Right now, all there is is there is speculation that my client has formed an internal intent that hasn't been disclosed or described to anyone.

THE COURT: And address the other factors on *Step-Saver*, please.

MR. GANER: Certainly. Conclusiveness.

Of course, this Court would have the ability to go through the *Dawe* factors and provide a conclusive opinion. I understand there are some technicalities of areas where if they didn't pay premiums, the way the

pleading is addressed, but I think those are more pleading deficiencies than anything else. Obviously, the Court would have the ability to provide a conclusive opinion.

The utility factor I think is very important in the broader context.

We're dealing here right now with one defendant who is coming in and saying I want a declaratory judgment. I want to get damages based on this undisclosed intent on these 14 policies with $100 million in face value.

If the Court starts entertaining these type of challenges where anybody can just come in and start saying, hey, I'm in a contractual relationship with someone and they've been involved in other litigation and I just want the Court to weigh in on the validity of my contract, you are just opening the Court up to hundreds of policies being brought in and being litigated where there isn't actually any adversity of interest.

There is not actually a controversy. There is no actual dispute between the parties. One party just decides, hey, I want to go and get the Court to tell me my policy is okay. I just think that the utility of that under the grand scheme of things is negligible.

I didn't keep a real good eye on my time.

I think the claims in general in the broader context, outside of the fact that they're not ripe, the tort

claims all fall, have a fundamental flaw of not showing either a lack of duty or a lack of causation to the alleged damages.

This is essentially a case of someone who has alleged just a general diminution of value of an asset and looking for a cause of action, but they're saying, well, you sued on these other policies. You have had this litigation strategy. That is causing the market to interpret that data, and the market interpretation of that data is that my policy is not valuable anymore. That is the very idea of a proximate cause chain that is far too nebulous to actually be legally sufficient on probable -- on proximate cause.

There is also just no showing that my client has any duty or obligation to ensure that their policies are valuable on the secondary market, to assure that we don't take the litigation actions with respect to unrelated policies that might cause the market to have a different view of their other assets that we have taken no action on.

If I could reserve the rest of my time for a rebuttal.

THE COURT: I have some other questions for you.

MR. GANER: Okay.

THE COURT: On the analysis that the Delaware Supreme Court tells us to do as to the validity of these policies, of course, one of the issues is who paid the

initial premium; correct?

MR. GANER: That is one of the factors.

THE COURT: It is alleged in the counterclaims that the first premium payments were made by the individuals in the two different cases. Isn't it correct that that is alleged?

MR. GANER: That is alleged.

THE COURT: So I need to take that as true at this point; correct?

MR. GANER: Yes, Your Honor.

THE COURT: All right. So given that that is an important factor and that that is true for purposes of these motions, how can I grant all of the relief that you are asking for?

MR. GANER: Because, the *Dawe* factors, that is one of the *Dawe* factors. That is certainly not an exclusive listing of the *Dawe* factors. If you look through the *Dawe* opinion, the *Dawe* Court was emphatic that while that would provide strong evidence that the person actually intended to procure the policy for legitimate insurance purposes, it is that the policy needs to be procured not for wagering purposes but for legitimate insurance purposes; and there is no allegations within the complaint that would suggest that the policies were procured for legitimate insurance purposes other than that sole allegation related to the premiums.

And the fact that someone has paid the premiums, even if we were going to take that as true, is not dispositive of whether or not the policy was issued with an insurable interest.

THE COURT: So you acknowledge they have adequately alleged a strong factor; correct?

MR. GANER: Correct.

THE COURT: But that is just not enough, even on a motion to dismiss. That is your view; right?

MR. GANER: It's my view that simply alleging that the insured paid the initial premium would not allow the Court to find that an insurable interest existed. I think they need to satisfy all of the *Dawe* factors which included that the purpose for insurance was legitimate.

THE COURT: For purposes of this motion, I'm not finding whether there is an insurable interest. I'm finding whether you have persuaded me that they have failed to even adequately plead an insurable interest. Isn't that what I have to decide?

MR. GANER: Right. But even if you accept the fact that they have paid the first premium, even if you accept that as true, that fact alone would not be adequate to grant the relief that they had requested, which is that the policy be declared -- that it be declared that the policy was issued with a valid insurable interest. They

need to allege more.
It would be like if you allege fraud and you made a bunch of great arguments about what the person said wrong but you made no allegations related to duty. You have to make allegations, factual allegations if taken as true, would satisfy all of the factors of your cause of action or would allow the Court to look at the policy and say, okay, you have adequately alleged all of the factors that under *Dawe* would allow me to say the policy issued with an insurable interest. Just alleging factors relating to one of those factors is insufficient.
THE COURT: So you read *Dawe* as holding that it's never adequate to find insurable interest based solely on who paid the first premium. That is never going to be enough.
MR. GANER: No, the *Dawe* court requires that courts scrutinize the entire transaction. You can't look at one cancelled check and say that is enough to find that there is insurable interest. Absolutely not. You have to look at the entire transaction. You know, why was the insured paying that premium? Was the insured told, hey, I'm going to write you a check right now. You are going to deposit that into your account, and then you are going to write me a check right back out of that account, and that is going to be you paying the premiums, which is what happened

in a lot of these cases. That is not adequate under *Dawe*.
If the insured isn't actually paying that premium themselves, I'm digressing a little bit too much here I think, but there has to be a scrutiny of the factors. That one factor alone is not dispositive.
THE COURT: Do you object to the defendant's request that the Court take judicial notice of your client's filings of numerous other cases?
MR. GANER: I don't. My client has filed. It's all a matter of public record.
THE COURT: And it's alleged by the defendant that you request "judicial immunity from the equitable doctrines of waiver and estoppel;" is that correct?
MR. GANER: We don't request judicial immunity, we request that the Court acknowledge the holding of *Dawe,* which is that a court can never enforce an illegal criminal regardless of the intentions of the parties. That is what we're arguing. They've made an allegation that the court should enforce a contract even if it is illegal because they think my client has waived a right or should be equitably estopped from not participating in the payment on an illegal contract.
THE COURT: And the defendant asks that if I find any deficiencies, if I were thinking of granting your motion in any regard, that instead I should given them leave

to amend their counterclaims. Should I do that? And, if so, if not, why or why not?
MR. GANER: Well, Your Honor, I believe leave should be freely granted. I would not disparage you if you gave them leave to amend.
THE COURT: Okay. Well, you can reserve the rest of your time. Thank you very much.
MR. GANER: Thank you.
THE COURT: We'll hear from the defendant. Good afternoon.
MR. SKLAVER: Good afternoon. One moment while I set this up.
THE COURT: Certainly.
(Pause.)
MR. SKLAVER: May I approach, Your Honor?
THE COURT: You may. Do you have another copy of this?
MR. SKLAVER: I do.
THE COURT: We'll take two then. Thank you.
MR. SKLAVER: I apologize.
(Documents passed forward.)
THE COURT: Do you need help with that?
MR. SKLAVER: I may.
THE COURT: Ron?
The screen here came on. I do have it on my

screen. Can you see it on counsel table?
MR. FARNAN: Yes, Your Honor.
THE COURT: Okay. The big screen may come on. In fact, it looks like it is.
MR. SKLAVER: I may lose the jury on this one.
THE COURT: You may go ahead. We've all got it.
MR. SKLAVER: Thank you, Your Honor. Let me make start by making a concession. The trust is going to withdraw and dismiss without prejudice its Delaware Consumer Fraud Act claim. And while we seek leave amend in the alternative on the other claim, even if granted, we wouldn't seek to amend for that particular claim. So I just want to focus the Court at this point on the ripeness and tort claims.
THE COURT: Okay. Before you come to that, I think we saw enough in the briefing to know that you're also willing to dismiss or withdraw your declaratory judgment claim on validity of the policies, the one that is redundant of one of their claims; is that right?
MR. SKLAVER: Correct. With respect specifically to the Griggs policy and the Szalay policy.
THE COURT: Thank you. You may go ahead.
MR. SKLAVER: As for ripeness, the core of the trust counterclaims is the same as Phoenix claims: Phoenix through the trust in two different lawsuits here, five other

policies in Delaware, 25 plus other lawsuits across the country, that all raise the same issue. And if their claims are ripe, our claims are ripe. We seek the same thing. They want to have a policy declared void. We want our policies declared valid. And,

Under binding U.S. Supreme Court law, *Maryland Casualty*, the analysis is the same regardless of who brings the claim. That is the case we cite in our brief where the Court said: "It is immaterial that frequently, in the declaratory judgment suit, the positions of the parties in the conventional suit are reversed; the ripeness inquiry is the same in either case."

So what Phoenix is asking for here is an asymmetrical right where only they can come in and get the private contract rights adjudicated and we can't. And that causes harm that the CSSEL Bare Trust decision explained is ripe for adjudication, and it's ripe for two separate reasons. One is there is a present injury, and that is the impaired marketability of our policies. We're not just in the business as alleged in the complaint, of holding policies until maturity. We also are investors who sell it on a tertiary market. There is a secondary market and then a tertiary market.

Phoenix's only argument on the impaired marketability point is an argument about lack of causation.

We don't establish some link to their misconduct or alleged misconduct and the depressed value; and that is a fact question. We certainly do state in the complaint affirmatively, and it makes sense. You have got a party that sued not just us, they've sued us twice, they've sued the participants in our policy: Steven Lockwood, who is the broker on a lot of the policies; John Berck, the trustee; Lockwood Pension Services. They sued them for civil RICO violations and made statements in pleadings that these guys are essentially STOLI recidivists, some of the language they used, who are engaged in wagering of hundreds of millions of dollars of policies. So for Phoenix to say we have never taken a stand against these policies is really we think a linguistic game.

It is true they have not uttered this policy number in the same sentence that we're going to void the policy but they have made X or implicit threats related to the participants in the policies that, as we go through the *Step-Saver* factor, plainly establish that the claims are ripe.

THE COURT: Well, do you concede then that at least implicit threats, as you put it, are necessary in order for this to be redressable?

MR. SKLAVER: I concede they're sufficient. I don't think they're necessary.

So, for example, in the *Simmonds Accessories* case which is a Third Circuit case from 1958, that is a case that actually uses the language "implicit threats are sufficient to help establish adversity prong."

Here, under adversity, we have four factors in our favor. It's a factor-based test that obviously has some room in the joints to maneuver. But if you look at the factors, there is two STOLI lawsuits against my client; and we have cited the *Teva Pharmaceuticals v Novartis* case. It's a patent case from the Federal Circuit, but that stands for the proposition if you have similar litigation involving similar parties, and there it's similar technology, that is one factor that points to a likely imminent injury, that there is adversity between the parties.

You also have here 25 plus similar STOLI lawsuits that the Court can take judicial notice of.

And helpful on this fact is a Third Circuit case, I think it's called *Surrick v Killion*. That is the case where the Office of Disciplinary Counsel had brought a claim against a different lawyer, a nonparty to the litigation, and it had to do with he was disbarred in the state of Pennsylvania, and he wanted to open an office because he was still able to practice in federal court even though he was disbarred in state court. And the Office of Disciplinary Counsel said I never brought a claim against

this lawyer, this isn't ripe. The Court said let's look at all the factors. You don't disavow any intent to sue. I find that to be "significant." That is the language from the Third Circuit as part of the adversity prong. And you showed a tendency to enforce these type of claims by suing someone else.

Here, we don't even need to make that leap because this is not just that they sued other third parties, they sued the trust. So all four of these factors strongly point to a finding of adversity.

This sort of plays into the waiver point, the argument from opposing counsel. They are also arguing no matter how long they wait, no matter how long of a delay, the fact that they know that they are going to rescind these policies, they'll never waive a claim for lack of insurable interest. In fact, I think logically that applies that they stood up and said we will never sue the trust for lack of insurable interest. They can come back and say we can never waive a claim, the Court can't enforce a legal contract. All of that technique, all of these factors strongly point to finding of adversity.

And that is not only the *Surrick* case, there is a Supreme Court case, *Babbitt v Farm Workers* where the Attorney General there would not disavow any intent. There was a criminal statute to prosecute someone. Their only

position is that we haven't taken a position yet, but the fact that they won't disavow any intent is a strong factor. The conclusiveness factor --

THE COURT: So it follows in your mind, it doesn't matter what their intent is. If they do anything short of give you the express assurance you want, you think you have stated a claim that you can bring to federal court.

MR. SKLAVER: Well, fortunately in this case we have both. We have allegations based on strong circumstantial evidence that they already reached that intent internally. That they had the intent internally they're not going to pay these claims.

A good example of that or an inference that can be drawn for these purposes is the Fuld action. You have a case in Florida that we cite where they sued to rescind the policy and a disclosure of your counsel in that case and esteemed opposing counsel was counsel for Phoenix in that case in Florida. And in that case, they sued to rescind the life insurance Policy of Edward Fuld. They waited two more years, collected all their premiums on another policy on this gentlemen's life and sued in Delaware seeking the same type of relief.

By the way, one of the investors in the Fuld case was White Cliff who the counterclaim explained is an investor on four of the policies at issue on our

counterclaim.

So there is a strong inference that the Court can take now that Phoenix has reached a conclusion internally about what policies they're going to rescind and what they don't. They have internal tracking mechanisms or they have red flags where they know if a broker is involved, a trustee is involved, and all these policies match those characteristics which is on all fours with the CESSEL Bare case from the New York Supreme Court.

So the parties apparently have an agreement based on the oral argument on the conclusiveness factor. And I just want to highlight, since this is a factor-based test, and you look at all that, this is a unique case where all the facts exist. They're frozen in time in a box. The issue is was there an insurable interest at issuance five or six years ago?

There are no further facts that can develop that will help that adjudication. But what makes this unique is actually the facts get worse, or the adjudication, the ability to adjudicate gets harder not just because memories fade over time but the insured dies.

Here, Roberta Griggs, on the $10 million claim, she is not going to be able to testify what her intent was when the policy was procured.

The last factor is utility.

The Third Circuit defines utility to mean, would a decision impact the parties plans of action? So, for example, in the *Surrick v Killion* case, you have a lawyer who said I would like to open an office in Pennsylvania. The Court said, you know, a ruling would affect that plan of action. That satisfies that test.

Or there is a case we cite, *Hurley v Minor* where you had someone who wanted to buy wine from an out-of-state winery directly via mail rather than through wholesalers. The Court said your intent to buy wine would be impacted if I issued a ruling that affects the parties plans of action.

There is *Lewis v Alexander* which is a reasonably recent Third Circuit case that came out in June where the Court said -- this decision had to do with complicated Medicaid regulations that impacted the administration of trusts. There, the Court held: If I issue a decision, it will impact how the trust administrators will work on the trust. It will actually impact administration of the trust.

We're the same thing. We want to know how we should handle our assets. Whether we can sell them? Could we resell them to investors, which is what we want to do, or if we can to keep paying premiums going forward, but we can't be stuck in this never-land of not knowing whether they're going provide coverage because we're prohibited from reselling them to investors.

THE COURT: Well, you say stuck, and I know it's advocacy, but in doing that, your client bought these policies in a free market. Didn't your client take certain risks that the policies were or were not valid?

MR. SKLAVER: Well, that is true. You always take a risk, but that argument would really overturn a substantial amount of ripeness jurisprudence. I will give you an example.

In the Supreme Court case, we cite, both parties cite *Village of Euclid* that talks about impaired marketability. There, you have a zoning ordinance that was passed that limited the ability of the land to be developed so that it couldn't be developed for industrial use. It could only be used for residential use. And the Court held that impaired the value of the property and so it's ripe for adjudication.

But if this logic applies you always take a risk and therefore you are subject to some impaired marketability were true, there wouldn't be ripeness in that case. And that is not how any of these cases come out. It is true there is risks when you make a position. That doesn't mean a claim isn't ripe for future adjudication when their conduct has caused us harm, and that is what we alleged.

Another case on that point is *SCA Services of Indiana* that we cite. That is from the Northern District of

Indiana. Where the EPA gave a score, kind of a score to a piece of property that essentially labeled it close to being hazardous dump based on their analysis of the environmental contaminants. Is there always a risk you get labeled a dump? Yes, it depends on what you do on the property, but the Court said that label diminished the value of the property and said the claim is ripe for adjudication.

THE COURT: What about, and I think counsel for the plaintiffs brought it up, conclusiveness? What is the practical risk to the Court that if we agree with you that we will be potentially flooded with claims of impaired marketability of various assets?

MR. SKLAVER: Well, the *Village of Euclid* decision about impaired marketability is from 1926. We sort of address this in our briefs. So we there is -- courts tend to be flooded anyway, but at least empirically we certainly have data to show that the court-clogging prediction is not really valid in this situation.

What is unique about this case are these factors about the same participants they have sued before for RICO violations involving STOLI: the broker Steven Lockwood, Lockwood Pension Services, John Berck, Robert Fink who they also sued. He was involved in the Fuld case. He was actually third party defendant in the case where Phoenix was as well as White Cliff. So that, really, if there is going

to be any of these public policy arguments about court clogging, this certainly makes that case unique.

THE COURT: By the way, your argument is impaired marketability. You don't contend that these assets are not marketable, do you?

MR. SKLAVER: We do. We actually state in our complaint that they are effectively destroyed. I guess I will, we do allege that the marketability has been destroyed. I think if we went back and pushed further through the documents, would someone be willing to buy that for $100 or something above zero? Realistically, that is right, but functionally it's been destroyed and it certainly is substantially impaired. The level of that impairment could be the subject of testimony and expert testimony, if necessary, but certainly on the pleadings we think we have sufficiently established it.

That is all I have on the ripeness issue.

As far as the Rule 8 issue involving declaratory judgment claim, we just respectfully disagree. We think we have adequately stated that the policy is supported by insurable interest. We point out that there was the recent *Rutgers* decision which was decided on a motion for summary judgment just in the last three months where the evidence was that the insured paid the first premium, and the Court said that is enough to get to a jury. So we think for the

same reason on the pleadings, the fact we made such an allegation is sufficient.

On the waiver issue, really conceptually we think the argument is pretty simple. Phoenix is coming to court seeking equity. They want a declaratory judgment that the policies are deemed void. And when you come to Court in equity, you are subject to equitable defenses.

It is our position that alleged carrier misconduct is not immune from these defenses just because their claim is that the contract is illegal. And the trust alleges it is an innocent purchaser and that Phoenix's misconduct started years ago before they acquired the policies, when it knowingly encouraged agents to write these alleged STOLI policies. And whether Phoenix is or is not more culpable than the trust is a fact question that should be decided on summary judgment or trial, not on the pleadings. And we cite some cases on this proposition.

It is true there is language in the *Dawe* decision that Phoenix quotes that says void policies are never enforced, but the issue is not squarely before the Court about whether or not it is subject to waiver or estoppel-type defenses. When that issue is squarely before the Court -- we cite two cases from Pennsylvania; one from the Supreme Court, one from a lower court; and one from Oregon.

It's the Oregon case that is pretty strong. That's the *Hammond v Oregon & California Railroad Company*. In that case, you have a plaintiff who bought some railroad land from a defendant. And it turned out that was an illegal contract because there was a federal law that prohibited that transfer based on that price. So the plaintiff had to pay the government some money to clear up title and then sued the defendant. And the defendant said, look, that is an illegal contract. It was in violation of the law here, and it should be deemed void. Therefore, we don't have to pay for those damages. And the Court said, look, in this situation, I'm going to look at who was the more innocent party even though it's a void contract and unless the parties are in pari delicto or accomplices in the crime -- the language there is, I can't remember the Latin phrase, but percipius preminus (phonetic). Unless they're in pari delicto and percipius preminus, I'm going to give relief to the more innocent party.

We alleged that we're the more innocent party and therefore the waiver and estoppel defenses are claimed. We have an estoppel claim and a waiver defense as part of our declaratory judgment claim, should exist.

Unless the Court has other questions?

THE COURT: Do you admit that there were misrepresentations made on the applications for these

insurance policies?
MR. SKLAVER: No.
THE COURT: That's denied at this point.
MR. SKLAVER: Well, let me just -- on the policies at issue, there is one thing that needs to be clear. On all 15 policies, they're incontestable, and so issues of misrepresentation shouldn't be relevant at least for some type of fraud.
THE COURT: The contestability period has run.
MR. SKLAVER: Right. That doesn't bar the insurable interest challenge, that is what *Dawe* held, but it does bar claims of misrepresentation. We haven't done our full investigation on what was said on the application. They are signed by the insured, that is not my client. They are signed by the broker, that is not my client. The broker who they sued for RICO violation.
Right now, in our answer to their claim, I think we either denied it or stated that we don't have enough information right now to reach a conclusion.
THE COURT: Thank you very much.
Is there any rebuttal?
MR. GANER: I'll try to be brief, Your Honor.
I just want to respond very briefly to the allegation that we're playing coy, that we will not disavow intent to sue. My client has never been asked to disavow an

intent to sue. We were served with a counterclaim in our lawsuit. It would have been inappropriate for my client to affirmatively state what its intentions were in moving to dismiss that complaint. Just simply, the question has never been asked: What are your intentions with respect to these policies?
THE COURT: It was certainly argued about in the brief. Are you saying your client is prepared to represent whether it intends to sue on the other 12 or 13 policies?
MR. GANER: I do not know that, one way or the other. My client has no present intent to sue on any of those policies. I don't believe my client has any intent with respect to them as we sit here today.
But, once again, I think that is getting too much into a fact issue. That they have alleged we have this intent, we're going to deny we had this intent if we have to answer the complaint. But the idea that we're playing coy by not affirmatively disavowing this, we have never been asked to affirmatively disavow it outside of the litigation. You can't file a piece of litigation and then say, well, you have never affirmatively disavowed this, so therefore there is a case in controversy. There has to be an actual dispute ahead of time. And,
There is an actual dispute from Phoenix's side. Phoenix is a party to a contract. Phoenix is standing up

and saying this contract is not valid. We're seeking a declaratory judgment that the contract is not valid. If they came in and said we agree with you the contract is not valid, there is no case or controversy. That is a different story. It's not two sides of the same coin.
THE COURT: What if they refuse to take a position?
MR. GANER: If they refuse -- they have to answer the lawsuit or they have to move to dismiss. They're the ones that are sending in premium payments. They're the ones that are the party to the contract.
It's a different story when one party stands up and says we're a party to this contract and I am affirmatively stating this contract does not exist. I want a declaration this contract is void. That is different than someone standing up and saying I want a declaration that this contract is valid. It's just it's two different. They're related but they're not the exact flip side. And,
With the Griggs case, there was a claim for death benefits submitted so there is definitely a dispute as to whether or not Phoenix is going to pay a death benefit. They have asked for us to pay a death benefit and we have refused, and we paid to file this lawsuit.
With respect to the allegation that Phoenix has been involved in litigation with Mr. Berck, with

Mr. Lockwood, with Mr. Fink. Yes, we have. So have numerous other carriers. Mr. Berck is involved in a lot of litigation, most of which, many of which are cited within Phoenix's -- within, I'm sorry, the trust's opposition. Mr. Berck is involved in this litigation with Lincoln, with Penn Mutual, with the Pruco Insurance Company. This isn't a Phoenix specific issue. You know, I'm sure Your Honor is aware there is litigation. I think Lincoln is party to about a dozen cases in this District, as is Phoenix, as are other insurance carriers.
This is a much broader issue if you allow any of these investors to come in and say, well, I've got some policies and, you know, Lincoln has filed some lawsuits so I want to have these hundred policies declared valid, well, Penn Mutual filed some lawsuits, I want to have these 50 policies declared valid when there has been no express repudiation as to any of those particular contracts.
All of the impaired marketability cases that were cited, all of those involve an action taken by some party towards the other. They involve an action taken by an environmental regulatory group saying this property is a dump, and you are saying, well, you have impaired my marketability with respect to this action with respect to me. The allegations here are that we impaired the marketability by filing lawsuits against unrelated parties.

Even the lawsuits we filed against ESF, against this trust, they're alleged to not have been involved in either the initial purchase of the policies from Phoenix or the initial resale of those purchases or the beneficial interest in the trust that own these policies onto the secondary market. They bought the policies years later and they have, the policies have varied background. So, unlike with the Lockwood case, the CSSEL Bare case, all of those policies came through one program and were all involved in one very narrow, very specific issue.

These policies are varied. They're from different producers. There is some overlap in trustees, there is some overlap in producers, but there is nothing that says that all of these policies that they own that they bought at different times from different areas are all part of something that Phoenix is definitely going to challenge.

As far as the equity waiver issues, I'm not saying that my client wouldn't be subject to some type of liability if they had done something wrong. All I'm saying is that on the very narrow issue of whether the relief is that despite the fact this is an illegal contract, this Court is going to enforce it, that's not permitted. If my client has done something wrong, they would certainly be subject to some type of claim if they have actually done all these bad things. I don't know what exactly what the form

of that is, but it might be that it would be a claim for damages, that you have caused damages. You have done something to me that caused damages. That would be the remedy. It wouldn't be the Court enforcing an illegal contract. That is a much narrower issue.

I am not saying they wouldn't be without redress in this hypothetical situation that ten years down the line, my client sues to rescind one of these policies, these 14 unrelated policies, that they wouldn't be subject to some type of claim for damages. But that is, again, a hypothetical situation. If my client ever actually denied a claim, that would be a different story, but that is not the factual situation we have.

THE COURT: Do you agree that the contestability period is over on all of these policies?

MR. GANER: Yes, all of the policies are past the contestability period. In the Griggs and Szalay cases, my client has not moved to void the policies due to misrepresentations. We have moved to have the policies declared void due to lack of insurable interest. I think that misrepresentation with fraud that happened in the applications certainly can be relevant. And,

With respect to the sort of passage of time argument, my client has the burden of proof to declare all of these policies are invalid and that they lacked an

insurable interest. Letting time go past is not helpful to me. It's much easier if I have a live insured I can go talk to than if I am trying to circumstantially prove the circumstances related to a transaction where the insured is dead. The passage of time makes it much harder for me to get rid of a policy than it does for them to keep one on the books.

THE COURT: Thank you very much.

MR. GANER: Thank you, Your Honor.

THE COURT: I appreciate the argument. We'll take it under advisement. We will be in recess.

(Oral argument hearing ends at 3:22 p.m.)

I hereby certify the foregoing is a true and accurate transcript from my stenographic notes in the proceeding.

/s/ Brian P. Gaffigan
Official Court Reporter
U.S. District Court

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