

Second Circuit Affirms Summary Judgment for Bona Fide Purchaser in STOLI Action

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In a June 8, ruling in *AEI Life v. Lincoln Benefit Life Co.*, the Second Circuit upheld the District Court for the Eastern District of New York's application of New York's two-year incontestability period to a STOLI policy. At issue in the litigation was a \$6,650,000 policy issued by Lincoln Benefit Life Company (Lincoln Benefit) and ultimately purchased by AEI Life LLC (AEI). AEI – deemed by both the district court and Second Circuit to be a bona fide purchaser, unaware of any fraud in the policy's procurement by the insured and initial policyholder – had sought a declaratory judgment that the policy was incontestable due to the lapse of the two-year contestability period.

In the district court, the central issue was whether New York or New Jersey law, and the states' respective rules as to incontestability, applied to the policy. While both states have two-year incontestability periods prohibiting insurers from successfully challenging the validity of life insurance policies after accepting premiums for two years or more, New Jersey's law, unlike New York's, contains an exception for fraudulent policies. The issue turned on whether the policy's "Conformity with State Law" clause, which stated that the policy was "subject to the laws of the state where the application was signed," governed as a choice of law provision. Lincoln argued that the application was signed in New Jersey and, therefore, New Jersey's incontestability law applied, along with its fraud exception. AEI, however, argued that the provision was not a choice-of-law clause and, in any event, that the application was signed in New York. The district court ultimately interpreted the conformity clause as a choice-of-law provision and applied New York substantive law, resulting in a grant of summary judgment for the plaintiff.

On appeal, while it disagreed with the district court's classification of the conformity clause as a choice of law provision, the Second Circuit affirmed summary judgment for AEI. Specifically, the circuit court found that the conformity clause was "not a choice-of-law clause [and was] instead, exactly what it is called in the policy: a conformity

clause [which] has the effect of excising a provision of an insurance policy that conflicts with or is voided by state law and replacing the provision with the prevailing state statute or judicial rule of law.”

It stated further that “[i]f the parties intended this provision also to act as a choice-of-law clause, we would expect it to bear a title that indicated it was serving both purposes.” The Second Circuit thus upheld the application of New York’s two-year incontestability law and found that Lincoln was precluded from contesting the policy’s validity.

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