

# The Viability of Delaware Dynasty Trusts After the Kloiber Case

By Steven J. Oshins, Esq., AEP (Distinguished)

It's over! One of the highest-profile cases in the history of the estate planning industry, and one that was being monitored by estate planners all over the United States, has been settled. Delaware trust promoters had been holding their breath awaiting the result of the case that became the posterchild for jurisdiction selection and the importance of avoiding the use of a health, education, maintenance and support trust in a jurisdiction like Delaware that allows a divorcing spouse of a beneficiary to penetrate the trust.

No estate planning professional can “unsee” this result. No estate planning professional can disregard this result. No estate planning professional can choose not to draft around this result, whether the trust will be situated in Delaware or in any other jurisdiction that allows a divorcing spouse to pierce through the trust.

But let's back up and see how this case unfolded and then what to do about it if you do choose Delaware as your trust situs.

## How this Unfolded

The high-profile divorce between Kentucky residents Daniel (“Daniel”) and Beth (“Beth”) Kloiber took center stage in 2014 when their Unpublished jurisdictional decision (the “2014 Delaware Court Decision”) was released by the Court of Chancery of Delaware in the [\*Matter of Daniel Kloiber Dynasty Trust u/a/d December 20, 2002, 2014 WL 3924309 \(Del. Chan., Unpublished, August 6, 2014\)\*](#).

Daniel's father, Glenn had established a Delaware Dynasty Trust for the benefit of Daniel, Daniel's spouse (defined using a floating spouse definition that she be married to and



cohabitating with him to be a beneficiary) and Daniel's descendants. Glenn gifted approximately \$15,000 to the trust in 2002. In 2003, Dan sold 99.45% of his Extreme Software, Inc. shares to the trust for an unsecured promissory note with a face amount of \$6 million.

In June 2007, the trust sold approximately 80% of its Extreme Software, Inc. shares to an unrelated third-party company for approximately \$250 million. In March 2008, the trust sold its remaining stock to a different unrelated third-party company for approximately \$60 million. So there were big numbers involved and Beth understandingly wanted a piece of the trust in the divorce.

The biggest issue for the estate planning community was whether Beth's [\*Garretson v. Garretson\*](#) argument noted in that opinion would allow her to bust through the trust to claim some of the assets via the divorce.

## Delaware's Position on Divorcing Spouses and Spendthrift Provisions

Based on the *Garretson* case, Delaware doesn't consider a

divorcing spouse to be a creditor. Therefore, a spendthrift clause in a so-called support trust (like one with health, education, maintenance and support as the distribution standard) situated under Delaware law doesn't protect the trust assets from a divorcing spouse of a beneficiary.

This has been the law in Delaware since at least 1973 when the *Garretson* case was decided. This is nothing new. Yes, many practitioners have disregarded the problem, but that doesn't mean that the problem hasn't been there for decades. How many *Garretson*-motivated divorce settlements have we not seen over the years simply because they quietly happened because they weren't high-profile like *Kloiber*? What we don't see or hear about doesn't mean it hasn't been happening for decades.

### [Proposed] Order Severing Trust

The file-stamped e-filed [Proposed] Order Severing Trust, dated August 16, 2016, can be read at this [Link](#).

The [Proposed] Order refers to a Settlement Agreement entered into by Daniel and Beth in the divorce action which is "contingent upon the entry of an order in the Delaware Court of Chancery severing the Dynasty Trust to create a separate trust for the benefit of Beth to be funded with assets of the Dynasty Trust (the Severed Trust);"

The Delaware Court of Chancery employee with whom I spoke told me that the material items such as the dollar amount of assets transferred into Beth's Severed Trust were sealed and thus unavailable to the public.

However, I have since then discovered that at least one property worth close to \$30 million was transferred from the Delaware Dynasty Trust into an LLC controlled by Beth in her Severed Trust. The deed is at <http://www.oshins.com/images/KloiberDeed.pdf>.

### Drafting Around the Delaware Problem

Other than the lack of protection from divorcing spouses of the trust beneficiaries, Delaware would otherwise be one of the better trust jurisdictions, right up there with Nevada, South Dakota and Alaska. However, if you choose to use Delaware law, then you should draft the trust as a discretionary trust rather than a support trust since a discretionary trust doesn't need to rely on the spendthrift clause to protect the trust assets and thus is protected from divorcing spouses.

But if you prefer to use a trust with health, education, maintenance and support or another support standard for

distributions, then very simply you should not use Delaware or any other jurisdiction that subjects these trusts to divorcing spouses. And any existing Delaware support trusts need to be moved to a more protective jurisdiction unless the trust gives a trust protector or other independent party the power to modify the trust into a discretionary trust in which case it can remain in Delaware.

So, yes, Delaware trusts are still viable post-*Kloiber*. But not as health, education, maintenance and support trusts.

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### ABOUT THE AUTHOR

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