

**Steve Leimberg's Asset Protection Planning
Email Newsletter Archive Message #337**

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**Subject: Jocelyn M. Borowsky & Richard W. Nenno: Myths and Facts about
*Kloiber***

In [Asset Protection Planning Newsletter #332](#) and [Asset Protection Newsletter #336](#), **Steve Oshins** provided **LISI** members with his analysis of the *Kloiber* case. Now, **Jocelyn Borowsky** and **Richard Nenno** provide members with their perspective on *Kloiber*.

Jocelyn Margolin Borowsky is partner at **Duane Morris LLP** and a fellow of the American College of Trust and Estate Counsel. She practices in the areas of estate planning, estate and trust administration and fiduciary litigation in Delaware, New Jersey, and Pennsylvania. As an active Delaware practitioner, she routinely prepares, reviews and advises with respect to Delaware trusts. Jocelyn also represents fiduciaries and beneficiaries in trust and estate litigation, including matters in which she is engaged as an expert witness. She is AV® Preeminent™ Peer Review Rated by Martindale-Hubbell and an Accredited Estate Planner of The National Association of Estate Planners & Councils. Ms. Borowsky is a 1992 graduate of the University of Pennsylvania Law School and a graduate of New York University School of Law (LL.M. in Taxation, 1997) and the University of Texas (B.A., with highest honors, 1988), where she was elected to Phi Beta Kappa.

Richard W. Nenno is a Senior Managing Director and Trust Counsel at **Wilmington Trust Company**,ⁱ Wilmington, Delaware. He received his A.B. degree from Princeton University and his J.D. degree from Harvard Law School. Dick is a Fellow of the American College of Trust and Estate Counsel and a former member of the Council of the Real Property, Trust and Estate Law Section of the American Bar Association and has presented at many national conferences, including the Heckerling Institute, the Notre Dame Tax and Estate Planning Institute, the NYU Institute on Federal Taxation, and the AICPA Advanced Estate Planning Conference. He has written numerous articles and has authored or co-authored Tax Management Portfolios on Choosing a Domestic Jurisdiction for a Long-

Term Trust(TMP 867), Domestic Asset Protection Trusts (TMP 868), and State Income Taxation of Trusts (TMP 869).

Before we get to their commentary, members should note that a new 60 Second Planner by **Andy DeMaio** was just posted to the **LISI** homepage. In his commentary, Andy reviews *Estate of Baker* (No. 7143, 12/30/2016), where the Alaska Supreme Court held that a one-page document qualified as a holographic will. The text of the Alaska Supreme Court's opinion can be found at <http://tinyurl.com/zpr3y8l> and members should [click this link to listen to Andy's podcast](#).

Now, here is Jocelyn Borowsky and Richard Nenno's commentary:

EXECUTIVE SUMMARY:

Steve Oshins recently authored a **LISI** newsletterⁱⁱ about the recently settled *Kloiber* case,ⁱⁱⁱ in which he asserted that Delaware trusts are “susceptible to claims of divorcing spouses in a beneficiary’s divorce.” This is simply not factual. The case was settled, and the court never rendered a decision. What *Kloiber* actually teaches us about trusts in the context of divorce is the folly of transferring marital assets to a trust without full consideration while retaining the benefit of those assets.

FACTS:

Transfers Involving Marital Assets

Transferring marital assets to a trust without full consideration, while retaining the benefit of those assets, is inadvisable. This lesson holds true whether the trust is a third-party trust, as in *Kloiber*, or a self-settled trust as in *Dahl*^v, a case involving a Nevada asset protection trust. In *Dahl*, Charles Dahl (“Charles”) settled the trust for the benefit of himself, his spouse (then Kim Dahl), his issue and certain charitable organizations. Kim Dahl (“Kim”) brought an action seeking a declaration of her rights in the trust assets and requesting an accounting. Charles admitted that he had funded the trust with marital assets. Kim also had transferred marital property to the trust. One of Kim’s claims was that Charles retained the power to amend the trust, and that because of the power to amend, the trust was revocable.^v

The case was heard by courts in Utah, where the couple resided. After receiving adverse decisions in the lower courts, Kim appealed to the Utah

Supreme Court. On appeal, the Utah Supreme Court sided with Kim, holding that the trust was revocable.^{vi} The court further held that because Kim also was a settlor of the trust, her rights to trust property would be based on her contribution of property to the trust. The court remanded the case to the district court to, *inter alia*, “allow [Kim] to revoke the Trust with regard to the portion of the Trust property attributable to either her separate property or any marital property.”^{vii}

Kloiber, like *Dahl*, involved a husband, Dan Kloiber (“Dan”), who transferred marital assets to a trust during the marriage. Dan’s father settled a discretionary^{viii} trust for Dan, his wife and his descendants. Dan was a primary beneficiary of the trust. Dan sold his interest in his company, a marital asset, to the trust for \$6 million. The trust later sold the company interest for a sum in excess of \$300 million. Dan’s wife, Beth Kloiber (“Beth”), claimed that Dan’s transfer to the trust was a fraudulent transfer because he received only \$6 million in exchange for an asset worth in excess of \$300 million. As noted, the case was settled, and the trust was not pierced. Rather, the trust was divided into a share for Dan and a share for Beth, and each share continues to be held in further trust.

Transfers Not Involving Marital Assets

The *Kloiber/Dahl* facts lie in stark contrast to a typical discretionary trust, settled by a third party (e.g., a parent or grandparent) for a beneficiary who never transfers any property to the trust. As to a typical discretionary trust, Delaware law stands firm against claims of the beneficiary’s creditors. Its creditor protection statute^{ix} has been revised multiple times over the years. It has been transformed from a basic statute precluding access to creditors of a beneficiary, to a comprehensive one. It now provides, in pertinent part, that a trust shall be exempt from:^x

execution, attachment, distress for rent, foreclosure, garnishment and from all other legal or equitable process or remedies instituted by or on behalf of any creditor, including, without limitation, actions at law or in equity against a trustee or beneficiary that seeks a remedy that directly or indirectly affects a beneficiary's interest such as, by way of illustration and not of limitation, an order, whether such order be at the request of a creditor or on the court's own motion or other action, that would:

- (1) Compel the trustee or any other fiduciary or any beneficiary to notify the creditor of a distribution made or to be made from the trust;

- (2) Compel the trustee or beneficiary to make a distribution from the trust whether or not distributions from the trust are subject to the exercise of discretion by a trustee or other fiduciary;
- (3) Prohibit a trustee from making a distribution from the trust to or for the benefit of the beneficiary whether or not distributions from the trust are subject to the exercise of discretion by a trustee or other fiduciary; or
- (4) Compel the beneficiary to exercise a power of appointment or power of revocation over the trust.

COMMENT:

Delaware's creditor protection statute is a formidable firewall against creditor claims, even in the context of divorce. No Delaware case holds otherwise. As Jennifer Wallace and Jocelyn explained in an earlier [LISI](#) newsletter,^{xi} in *Garretson*,^{xii} a case Mr. Oshins frequently cites, the couple was still married in the eyes of the court, and the husband had abandoned the wife. Because the couple was still married, the husband was obligated to support his wife. The Delaware Supreme Court then acknowledged that once spouses are divorced, they can become creditors of one another.^{xiii} Delaware's modern creditor protection statute provides in this regard that "the creditors of a beneficiary shall include, but not be limited to, any person that has a claim against the beneficiary, the beneficiary's estate, or the beneficiary's property by reason of any forced heirship, legitime, marital elective share, or similar rights."^{xiv}

Creditor protection statutes are often invoked following a divorce, when one spouse has failed to pay his or her divorce obligations. Before a divorce order is entered, a family court will determine, among other things, whether or not trust property is marital property, community property or separate property, and will divide the property accordingly, based on equitable principles. What *Dahl* and *Kloiber* demonstrate is that at the property division stage, the court is likely to treat trust property as marital property where [i] during the marriage, a spouse transferred the property to the trust either gratuitously or without receiving full consideration for the property; and [ii] the spouse is a trust beneficiary. In both *Dahl* and *Kloiber*, the divorce proceedings were heard by the family court or divorce court in the state where the couple resided, which, in *Kloiber*, was a non-asset protection state. What these cases do not address is whether an asset protection state court will enforce a family court order and compel a trustee

to distribute the marital assets from the trust. The *Dahl* court, which circumvented that situation by finding the trust to be revocable, observed that, had it found the trust to be irrevocable, “it would create a serious conflict between trust law and divorce law in Utah. The question of whether a spouse could create an irrevocable trust in which he or she placed marital property, thereby frustrating the equitable distribution of the property in the event of a divorce, is not before us in this case. Accordingly, we take no position on a likely outcome of such conflict. Rather, we bring the potential pitfalls to the Legislature’s attention.”^{xv}

Conclusion

To avoid such potential pitfalls, estate planners should discourage clients from transferring marital assets while retaining the benefit of those same assets unless they receive full consideration. While some asset protection states have laws which purport to protect self-settled trusts funded during a marriage, such laws are on a collision course with equitable principles in divorce.

HOPE THIS HELPS YOU HELP OTHERS MAKE A POSITIVE DIFFERENCE!

Jocelyn Borowsky
Richard Nenno

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ⁱⁱ *Steve Oshins on the Kloiber Case: Delaware Dynasty Trust Broken into Pieces by Beneficiary's Divorcing Spouse*, [Asset Protection Planning Newsletter #332](#) (October 24, 2016); See also *Steve Oshins on Kloiber: The Aftermath*, [Asset Protection Newsletter #336](#) (December 7, 2016).

ⁱⁱⁱ *IMO Daniel Kloiber Dynasty Trust U/A/D, December 20, 2002*, C.A. No. 9685-VCL.

^{iv} *Dahl v. Dahl*, 345 P.3d 566 (Utah 2015); See *Steve Oshins & Jeremy Spackman on Dahl v. Dahl: Utah Supreme Court Rules Trust Not a Domestic Asset Protection Trust!*, [Asset Protection Planning Newsletter #283](#) (February 12, 2015), at www.leimbergservices.com.

^v *Id.*, 345 P.3d at 579, n. 8.

^{vi} *Id.*, 345 P.3d at 580.

^{vii} *Id.*, 345 P.3d at 582.

^{viii} Delaware does not treat discretionary trusts which include an ascertainable standard as “support trusts.” 12 *Del. C.* § 3315(b) (“A beneficiary eligible to receive distributions from a trust in the trustee's discretion has a discretionary interest in the trust.”).

^{ix} 12 *Del. C.* § 3536.

^x 12 *Del. C.* § 3536(a).

^{xi} *Jocelyn Borowsky and Jennifer Wallace on In re Garretson*, [Asset Protection Planning Newsletter #221](http://www.leimbergservices.com) (February 28, 2013), at www.leimbergservices.com.

^{xii} *Garretson v. Garretson*, 306 A.2d 737 (Del. 1973).

^{xiii} *Id.*, 306 A.2d at 742.

^{xiv} 12 *Del. C.* § 3536(a).

^{xv} *Dahl v. Dahl*, 345 P.3d at 582, n. 13.