



Cracking Delaware's Notoriously Tough Trusts

Delaware's trust law makes the U.S. state an attractive jurisdiction for debtors to hold assets. Creditors therefore often may struggle when trying to access these trusts to recover assets. However, by deploying aggressive, multijurisdictional strategies, even Delaware's tough trusts can be cracked.

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Several features make Delaware's trust law attractive for debtors. The state allows individuals to shield assets through a domestic asset protection trust (DAPT), in which the trust's settlor is also the trust's beneficiary. There are various provisions that further protect the DAPT: for example, there are strict requirements for creditors to succeed on claims of fraudulent transfers to the trust. Broad powers for settlors make it difficult to claim that the trust is illusory. Delaware law also contains unique provisions that curtail attempts by courts outside of Delaware to apply non-Delaware law to matters involving Delaware DAPTs.

While attempting to access these Delaware trusts is challenging, aggressive multijurisdictional tactics can give creditors an edge:

Attack the validity of the trust. With such high walls, a Delaware trust might be best defeated by focusing firepower on its foundations. There are statutory requirements to establish a DAPT that, if violated, allow creditors to attack it as invalid. These include requirements that the trust must be irrevocable; that specific provisions must be included in the trust instruments; and that at least one trustee, part of the trust's administration, and some of the trust's assets, must be in Delaware.

Go through a creditor-friendly jurisdiction. Some U.S. states do not recognize DAPTs. If there is some connection between the trust and one of those states, a creditor can get the state's courts to reach the assets of a Delaware DAPT based on public policy or other reasons. Courts in Utah, Washington, and Illinois, for example, have done exactly that. This strategy can potentially overcome Delaware's attempt to restrict the reach of non-Delaware law.

Bring a fraudulent transfer claim anyway. The high barriers to bringing these claims may mean this attack is the least expected. Creditors will need to evaluate the likelihood the trustee would be entitled to use the trust assets to pay the costs of defending the DAPT, given that Delaware law gives them priority unless there is proof that the trustee acted in bad faith.

The attractiveness of Delaware's trusts makes the state a repository of debtor assets and a potential source of high returns for creditors. They should not be intimidated by the trust's fortress – a creative, multijurisdictional, and focused attack can lead creditors straight to the treasure trove behind the walls.

About Kobre & Kim

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Often working closely with lawyers in key markets around the world, our Delaware team:

- Consists of experienced trial litigators in the Delaware Court of Chancery and U.S. Bankruptcy Court for the District of Delaware who focus on complex commercial disputes;
- Has deep experience tracing, freezing and recovering misappropriated assets hidden in cross-border and offshore structures;
- Acts on behalf of creditors to monetize high-value judgments and arbitration awards, with most of our matters involving awards and judgments with face values of US \$100 million+ to several billion USD.