



fixing a broken charitable remainder trust

MSK Client Alert

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Correcting Errors in CRT Agreements

Most charitable remainder trusts are created, funded, and operated in a routine manner. On rare occasions, however, errors are made. For example, a CRT may be mistakenly created as a unitrust instead of as an annuity trust or the payout rate inserted into the CRT agreement may not be what the trustor expected. When these types of errors are made, can the "defective" CRT be fixed? The answer depends upon the type of error that is made.

As a general rule, CRTs are irrevocable and not subject to amendment. Therefore, when an error is discovered after the CRT agreement has been signed, it can pose a significant problem. In certain situations, however, the IRS adopts the "no harm, no foul" approach and allows the mistake to be corrected without disqualifying the CRT if the error can be classified as a "scrivener's error." Whether an error is, in fact, a mere scrivener's error and, therefore, correctable will depend upon the underlying facts.

IRS Private Letter 200649027

The IRS recently issued a private letter ruling that provides guidance as to when an error in the drafting of a CRT may be considered to be a scrivener's error and, therefore, correctable. In PLR 200649027 (12-8-06), a CRT was created by two trustors. According to the trustors, the CRT agreement mistakenly included a net income limitation. The trustors filed a petition in the state court having jurisdiction over the CRT to obtain its consent to amend the CRT and remove the net income limitation. The court issued an order reforming the CRT. The order, however, was contingent upon the trustors obtaining a private letter ruling from the IRS confirming that the reformation would not cause the CRT to violate the Internal Revenue Code or the applicable Regulations.

It's the Lawyer's Fault

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practice areas

nonprofit organizations



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According to the trustors, the attorney who drafted the CRT failed to advise them that the CRT could have been created as a "standard" CRT, i.e. one that did not contain a net income limitation. In addition, the trustors asserted that the "investment climate" had changed subsequent to the CRT's creation. This change caused an unexpected result - namely that the CRT earned less interest income than anticipated. According to the trustors, this frustrated one of the principal purposes of the CRT, to provide the trustors with a "suitable" annual income.

Can't be Fixed if it's not a Scrivener's Error

After reviewing the requirements imposed on CRTs by the Internal Revenue Code and the Regulations, the IRS concluded in PLR 200649027 that the purported error was not a scrivener's error. Therefore, the CRT instrument could not be amended without disqualifying the CRT.

Prior IRS Rulings

In trying to make sense of the IRS' decision in PLR 200649027 and determine what type of error may be considered to be a scrivener's error, a brief review of some of the prior private letter rulings that the IRS has issued concerning this topic is useful.

In PLR 9822041, the drafting attorney inadvertently inserted a net income limitation in the CRT agreement. The trustors were told that the CRT would be a standard CRT and would not contain a net income limitation. The trustors signed the CRT agreement without realizing that it contained this limitation. The IRS determined that this was a scrivener's error and could be corrected.

In PLR 9833008, the drafting attorney mistakenly neglected to include a provision in the CRT agreement to allocate post-contribution capital gain attributable to the CRT's assets to income. The trustors were told that the CRT agreement would contain this language. The IRS concluded that that mistake was a scrivener's error and could be corrected.

In PLR 200002029, despite advising the trustors that the CRT agreement would be drafted so as to allow the trustors to select a private foundation as a charitable remainderman, the drafting attorney mistakenly inserted language in the CRT agreement limiting the charitable remaindermen to public charities. The IRS determined that this was a scrivener's error and its correction would not cause disqualify the CRT.

In PLR 200251010, despite advising the trustors that the CRT would be a unitrust, the drafting attorney mistakenly inserted language in the CRT agreement causing it to be an annuity trust. The trustors did not notice this mistake until after the CRT agreement was signed. The IRS determined that this was a scrivener's error and could be corrected.

In PLR 200441019, the IRS determined that an error made in listing a CRT payout rate was a scrivener's error and could be corrected without disqualifying the CRT. The trustors were told that the CRT payout rate would be 5%. After the CRT agreement was signed, it was determined that 7% was mistakenly inserted into the agreement.



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Making Sense of the Rulings

In trying to reconcile what appears to be a fairly open-minded view of the IRS in allowing CRT drafting errors to be corrected (as set forth in the several rulings cited above) with the negative (from the trustor's perspective) conclusion reached in PLR 200649027, a few observations can be made.

When analyzing whether an error may be classified as a scrivener's error, it is important to distinguish between an omission or error that is made during the pre-drafting discussion phases leading up to the drafting of the CRT agreement and one that is made during the actual drafting of the CRT agreement after all of the terms of the CRT have been agreed to by the trustor. The latter may generally be regarded as a scrivener's error while the former may not be.

For example, if, as in PLR 200649027, an attorney fails to discuss the various options that are available to a trustor such that the trustor is not aware of the choices that he or she may have in creating a CRT, that is an omission or mistake by the attorney in the CRT's pre-drafting phase. It is likely, however, that this error may not be corrected because it is not a scrivener's error i.e. it does not relate to an omission or mistake that was made by the drafter between the time that the CRT's terms were decided upon by the trustor and the actual drafting of the CRT agreement.

This situation may be contrasted with one where a trustor is advised (and decides) that his CRT will contain certain provisions, such as the agreed upon payout rate. If a mistake is made during the actual drafting of the agreement such that the expected payout rate is not inserted, this type of error is likely to be considered to be a scrivener's error and correctable.

As stated, in PLR 200649027 the error was made by the attorney in the pre-drafting discussion period. The error was an omission by the attorney in that the attorney did not provide the trustors with a complete description of their options. This is distinguishable from an error that is made during the drafting of the CRT agreement (for example, by not inserting a previously agreed upon term).

The Moral of the Story

Although a potential trustor of a CRT should be able to rely on the advice of counsel, it is important for the trustor to become as knowledgeable as possible during the pre-drafting discussions concerning the CRT provisions. Moreover, it is important that the trustor make an effort to take an active role in structuring the CRT prior to the drafter putting pen to paper (digits to keyboard). This will help increase the chances that the trustor is as informed as possible about the different types of CRTs, the options that he may have, and the type of CRT that will work best for him. As shown, errors or omissions that are made in the formative stages of a CRT's life can have severe (and irreparable) consequences.

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