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A Solution for Drafting Errors in Post-December 31, 1978 Charitable Remainder Trusts: *State ex rel. Edmisten v. Sands*

Federal estate tax laws permit a deduction for transfers to charitable organizations.[1] Prior to 1969 estate planners frequently used split-interest gifts to obtain this deduction. Property would be transferred in trust for both a private and charitable use and the estate would deduct the present value of the charitable interest. In the Tax Reform Act of 1969 Congress reacted to a perceived abuse[2] of split-interest gifts by prohibiting deduction of the value of the charitable interest unless the transfer was in a prescribed form.[3] In *State ex rel. Edmisten v. Sands*[4] the testator's will attempted to establish a particular type of charitable remainder trust known as a charitable remainder unitrust.[5] During administration of the estate, it was discovered that the will lacked several administrative provisions that the Internal Revenue Service (IRS) requires in all instruments governing charitable remainder unitrusts.[6]

1. I.R.C. § 2055 (1982).

2. Congressional intent to correct past abuses is set forth in H.R. REP. No. 413, 91st Cong., 1st Sess. 58 (1969), *reprinted in* 1969 U.S. CODE CONG. & AD. NEWS 1645, 1704.

> The rules of present law for determining the amount of a charitable contribution deduction in the case of gifts of remainder interests in trust do not necessarily have any relation to the value of the benefit which the charity receives. This is because the trust assets may be invested in a manner so as to maximize the income interest with the result that there is little relation between the interest assumptions used in calculating present values and the amount received by the charity.

See also Ellis First Nat'l Bank v. United States, 550 F.2d 9, 15-16 (Ct. Cl. 1977); Gillespie v. Commissioner, 75 T.C. 374, 377-78 (1980).

3. I.R.C. § 2055(e)(2) (1982). The restrictions on the form of split-interest gifts produce a high correlation between the interest assumptions used in calculating the present value of the charitable interest and the amount received by the charity. Thus, the amount of the charitable deduction matches the amount the charity ultimately receives, eliminating the abuses discussed *supra* note 2. The following four types of split-interest gifts are allowed: (1) charitable remainder trusts, I.R.C. § 664(d) (1982); (2) pooled income funds, *id.* § 642(c)(5); (3) remainder interests in a farm or personal residence, *id.* § 170(f)(3)(B); and (4) guaranteed annuity interests, *id.* § 2055(e)(2)(B).

I.R.C. § 664(d) (1982) defines two types of charitable remainder trusts–charitable remainder annuity trusts and charitable remainder unitrusts. A charitable remainder annuity trust is defined in section 664(d)(1) as a trust that distributes at least 5% of the corpus at least once a year to a private beneficiary. The term may extend for the life of the private beneficiary or not more than 20 years. The remainder must go to charity. A charitable remainder unitrust as defined in section 664(d)(2) is similar, but the private beneficiary receives a fixed percentage of the fair market value of the corpus, valued annually.

A pooled income fund is a fund established by a charity to which donors contribute property for which they have retained income interests in a private beneficiary. The annual distribution to each private beneficiary is determined by the income of the pooled assets. Guaranteed annuity interests are deductible if the annual income distributed to the charity is either a sum certain or a fixed percentage of the trust assets. A discussion of pooled income funds, remainder interests in a farm or personal residence, and guaranteed annuity interests can be found in Moore, *Estate Planning Under the Tax Reform Act of 1969: The Uses of Charity*, 56 VA. L. REV. 565 (1970).

4. 307 N.C. 670, 300 S.E.2d 387 (1983).

5. *See supra* note 3. For a discussion of the charitable remainder unitrust provisions of the Internal Revenue Code, see *infra* text accompanying notes 9-16.

6. *See infra* notes 12-16 and accompanying text.

Consequently, the IRS denied the deduction claimed for the charitable remainder and proposed an increase in estate tax liability. The North Carolina Supreme Court, however, upheld an order construing the will and trust to include the requisite administrative provisions.[7]

This note examines *Sands* and other cases granting similar relief for defective instruments governing charitable remainder trusts, the effect on the IRS of construction orders made during the post-1969 Tax Reform Act transition period, and the public policy arguments favoring such construction orders. The note also analyzes the North Carolina Supreme Court's use of North Carolina General Statutes section 36A-53(a)[8] to uphold the construction order entered by the trial court in *Sands*.

To qualify as a charitable remainder unitrust, the trust must distribute at least once a year to a private beneficiary a fixed percentage (at least five percent) of the fair market value of the trust assets, valued annually.[9] The trust term may extend for the life of the private beneficiary or for not more than twenty years.[10] Upon termination of these distributions, the trust must provide for transfer of the remainder interest to a charitable organization recognized by the IRS.[11] In addition to the rules limiting the dispositive terms of the trust, the regulations promulgated under section 664 by the Treasury Department require that the governing instrument contain certain administrative provisions.[12] The Code also includes prohibitions against self-dealing,[13] excess business holdings,[14] investments that jeopardize the charitable purpose of the trust,[15] and certain taxable expenditures.[16]

The 1969 revisions that contained the split-interest gift restrictions apply

7. *See infra* text accompanying notes 30-36.

8. N.C. GEN. STAT. § 36A-53(a) (Supp. 1983).

9. I.R.C. § 664(d)(2)(A)-(B) (1982).

10. *Id.* § 664(d)(2)(A).

11. *Id.* § 664(d)(2)(C).

12. *See* Treas. Reg. § 1.664-1(b) (1972) (noting the applicability of I.R.C. § 4947(a)(2) to charitable remainder trusts). I.R.C. § 4947(a)(2) (1982) subjects charitable remainder trusts to many of the private foundation rules. I.R.C. § 508(e) (1982) sets forth the rules relating to the required provisions in instruments governing private foundations and charitable remainder trusts under I.R.C. § 4947(a)(2) (1982). *See infra* text accompanying notes 13-16. Section 508(d)(2)(B) disallows a charitable deduction for transfers to trusts that do not contain provisions required under § 508(e).

13. I.R.C. § 4941 (1982). Acts of self-dealing as outlined in § 4941(d)(1) may include: (1) the sale, exchange, or leasing of property between a private foundation and a disqualified person; (2) the lending of money or other extension of credit between a private foundation and a disqualified person; (3) the furnishing of goods, services, or facilities between a private foundation and a disqualified person; (4) the payment of compensation by a private foundation to a disqualified person; (5) the transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a private foundation; or (6) the agreement by a private foundation to give money or other property to a government official. A disqualified person is defined in § 4946 and includes any manager of the foundation, anyone connected with a manager of the foundation, and anyone connected with the creator of the foundation.

14. *Id.* § 4943. A private foundation has excess business holdings if it and all disqualified persons own more than an aggregate 20% interest in a business.

15. *Id.* § 4944. Investments made without ordinary business care and prudence jeopardize the charitable purpose.

16. *Id.* § 4945. Taxable expenditures include amounts paid by a foundation: (1) to influence

to decedents dying after December 31, 1969.[17] The complexity of these restrictions, however, led to a series of transition rules allowing amendments to nonconforming instruments.[18] The present transition period covers instruments executed before December 31, 1978, and authorizes amendments through December 31, 1981.[19]

In *Sands*[20] the testator's will directed the executor to transfer the residue of the testator's estate to a charitable remainder unitrust. The trustee was instructed to distribute annually the lesser of the trust income or five percent of the fair market value of the trust assets,[21] valued annually, to the decedent's sisters for life. The trust was to terminate upon the death of the last surviving sister, with the remainder to pass free of trust to a local church. Clearly, the trust met the dispositive requirements of Internal Revenue Code section 664(d)(2),[22] but the will creating the trust failed to impose a prohibition against self-dealing and omitted several other required trust administration provisions.[23] Since the will was executed on August 23, 1979, more than seven months after the last grace period had expired, any reformation of the will would not have qualified for recognition under the transition rules.[24] The IRS disallowed the deduction of the charitable remainder because of the omission and proposed an increase in estate tax liability.

North Carolina's Attorney General, representing the charity and the public,[25] filed a complaint in superior court seeking an order construing the will to include the administrative provisions or, alternatively, an order retroactive to

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legislation; (2) to influence the outcome of a public election; (3) as a grant to an individual for travel, study, or other similar purposes; and (4) as a grant to an organization other than a charity.

Rev. Rul. 72-395, 1972-2 C.B. 340 gives examples of language that will satisfy the administrative provision requirements. *See also* Wren, *Charitable Remainder Trusts: Some Considerations to Draftmanship*, 8 U. RICH. L. REV. 25 (1973).

17. Tax Reform Act of 1969, Pub. L. No. 91-172, § 201(d), 83 Stat. 487, 580.

18. The Treasury Department granted the original transition period in Treas. Reg. § 1.664-1(f)(3) (1972). This regulation gave trusts created after July 31, 1969, but before December 31, 1972, until December 31, 1972, time to be amended. If the change resulted from judicial construction, Rev. Rul. 74-283, 1974-1 C.B. 283 provided that the construction would be effective as long as legal proceedings were initiated before December 31, 1972.

In 1974 Congress granted instruments executed after July 31, 1969, but before September 21, 1974, a grace period ending December 31, 1975, to amend nonconforming instruments or to initiate legal proceedings for construction. Act of Oct. 26, 1974, Pub. L. No. 93-483, § 3(a), 88 Stat. 1456, 1457-58 (codified as amended at I.R.C. § 2055(e)(3) (1982)). The Tax Reform Act of 1976, Pub. L. No. 94-455, § 1304(a), 90 Stat. 1520, 1715, expanded the transition period to cover instruments executed before December 31, 1977, and extended the cut-off date to December 31, 1977. The Revenue Act of 1978, Pub. L. No. 95-600, § 514(a), 92 Stat. 2763, 2883-84, extended the cut-off date to December 31, 1978. In 1980 Congress again amended § 2055(e)(3) to extend the cut-off date for instruments executed before December 31, 1978 to December 31, 1981. Act of Dec. 28, 1980, Pub. L. No. 96-605, § 301(a), 94 Stat. 3521, 3530.

19. I.R.C. § 2055(e)(3) (1982).

20. 307 N.C. 670, 300 S.E.2d 387 (1983).

21. Under Treas. Reg. § 1.664-3(a)(1) (1972), the lesser of the trust income or 5% of the fair market value of the assets, valued annually, is a permissible alternative for distribution.

22. *See supra* text accompanying notes 9-11.

23. *See supra* text accompanying notes 12-16.

24. *See supra* text accompanying notes 17-19.

25. N.C. GEN. STAT. § 36A-52(c) (Cum. Supp. 1983) grants the Attorney General power to enforce charitable trusts.

the decedent's death reforming the will to include the administrative provisions.[26] The trial court first noted the public policy of preserving charitable transfers whenever possible.[27] The court then reasoned that the failure to qualify the trust as a charitable remainder unitrust increased the estate tax liability and reduced the amount of the charitable bequest. According to the court, the testator intended to leave the maximum amount to charity and any reduction constituted a partial failure of the charitable bequest. The trial court concluded that this failure permitted it to invoke North Carolina General Statutes 36A-53(a), (b)[28] and order an administration of the trust in accordance with IRS requirements to fulfill the charitable intention of the testator.[29]

On appeal, the North Carolina Supreme Court[30] noted that section 36A-53(b)[31] applied only to instruments executed before December 31, 1978. The court rejected application of section 36A-53(b) as the basis for a construction or reformation order since the will had been executed on August 23, 1979, but upheld application of section 36A-53(a).[32] According to the court, a trust must meet the three following conditions to qualify for relief under this subsection: (1) it must be a charitable trust; (2) it must be impracticable of fulfillment; and (3) the testator must not have provided any alternate disposition of the property.[33] The court found that the trust in *Sands* met the first and last conditions.[34] The court also found that the second condition was fulfilled, because the phrase "impracticable of fulfillment," as used in section 36A-53(a) and defined in section 36A-53(d), includes the failure of a charitable remainder trust "expressly [to] include a provision prohibiting the trustee from engaging in any act of self-dealing."[35] The court reasoned that the legislature intended

26. *Sands*, 307 N.C. at 672, 300 S.E.2d at 389.

27. *See, e.g.*, N.C. GEN. STAT. § 36A-52(a) (Cum. Supp. 1983):

> Declaration of Policy.—It is hereby declared to be the policy of the State of North Carolina that gifts, transfers, grants, bequests, and devises for religious, educational, charitable, or benevolent uses or purposes . . . are and shall be valid, notwithstanding the fact that any such gift, transfer, grant, bequest, or devise shall be in general terms, and this section shall be construed liberally to affect the policy herein declared.

28. *Id.* § 36A-53(a)-(b). Section 36A-53(a) gives superior court judges the authority to order an administration if: (1) the testator manifested a general intention to devote the property to charity; (2) the trust has become illegal, impossible, or impracticable of fulfillment; and (3) no alternative disposition of the property was made. Section 36A-53(b) gives the court the authority to amend wills executed before December 31, 1978, so that charitable gifts will qualify for a federal estate tax deduction under the split-interest gift provisions of the Internal Revenue Code.

29. *Sands*, 307 N.C. at 672, 300 S.E.2d at 389.

30. *Sands* was certified for direct transfer to the North Carolina Supreme Court pursuant to N.C. GEN. STAT. § 7A-31 (1981 & Cum. Supp. 1983).

31. *See supra* note 28.

32. *See supra* note 28.

33. *Sands*, 307 N.C. at 675, 300 S.E.2d at 390.

34. *Id.* at 675, 300 S.E.2d at 391 ("Mr. Sands' intent [to provide scholarships for Methodist children] could hardly be more manifestly expressed . . . . [T]he will does not provide for an alternate disposition of the corpus in the event the trust fails as a charitable trust.").

35. *Id.* at 676, 300 S.E.2d at 391. N.C. GEN. STAT. § 36A-53(d) (Cum. Supp. 1983) defines "impracticable of fullfilment as:

> [T]he failure of any trust for charity, testamentary or inter vivos, (including, . . . charitable remainder trusts described in section 664 of the Internal Revenue Code of 1954 . . .) to include, if required to do so by section 508(e) or section 4947(a) of the Internal

section 36A-53(a) to apply whenever a charitable remainder trust failed to incorporate "the 'boilerplate' required by IRS regulations."[36] Thus, the application of section 36A-53(a) as a basis for relief was justified.

In fashioning an order to fulfill the testator's intent as directed by section 36A-53(a), the court noted that the IRS treats an instrument as speaking from its effective date.[37] A reformation order might be viewed to speak only from the date of entry,[38] and thus would not ensure favorable tax treatment of the trust. An order of construction, however, treats the instrument as if it had always contained the provisions, thus ensuring a charitable deduction and fulfillment of the trust purpose.[39] Consequently, the court affirmed the trial court's construction order and vacated the order of reformation. In evaluating the soundness of the court's holding, it is necessary to consider the background against which the case was decided.

Instruments drafted after the revision of the split-interest gift rules often proved defective because the complexity of the provisions led many drafters to omit language critical to favorable tax treatment of the charitable interest. State courts became an important vehicle for saving the charitable deduction, and orders construing or reforming charitable remainder trust instruments similar to that granted in *Sands* were common under the transition rules.[40] For example, in *Estate of Bird*,[41] a New York Surrogate's Court construed a trust that did not contain administrative provisions required by the regulations. A New York statute had obviated the need for amendment of trust instruments to preserve favorable tax status by providing for administration of private charitable trusts and split-interest trusts in accordance with federal requirements.[42] The New York court granted construction of the trust in *Bird* based on this statute. Other cases also have demonstrated the willingness of state courts to grant the relief sought, as long as the executor or trustee was seeking construction of administrative rather than dispositive provisions.[43]

These results were justified on public policy grounds. A construction or-

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Revenue Code of 1954 . . . , the provisions relating to governing instruments set forth in section 508(e) . . . .

Since the *Sands* trust was charitable and required by § 508(e) and § 4947(a) to include the provisions relating to governing instruments in § 508(e), *see supra* text accompanying notes 12-16, any failure to include the various administrative provisions made the trust "impracticable of fulfillment."

36. *Sands*, 307 N.C. at 676, 300 S.E.2d at 391.

37. *Id.* at 677, 300 S.E.2d at 392.

38. *Id.*

39. *Id.*

40. *See, e.g., In re* Estate of Burdon-Miller, 456 A.2d 1266 (Me. 1983); *In re* Estate of Barker, 82 Misc. 2d 974, 370 N.Y.S.2d 404 (Surr. Ct. 1975); *In re* Will of Hammer, 81 Misc. 2d 25, 362 N.Y.S.2d 753 (Surr. Ct. 1974); Estate of Bird, 69 Misc. 2d 1015, 332 N.Y.S.2d 85 (Surr. Ct. 1972).

41. 69 Misc. 2d 1015, 332 N.Y.S.2d 85 (Surr. Ct. 1972).

42. N.Y. EST. POWERS & TRUSTS LAW § 8-1.8 (McKinney Supp. 1983-84).

43. *See supra* note 40. *Cf.* Shriners' Hosp. for Crippled Children v. Maryland Nat'l Bank, 270 Md. 564, 312 A.2d 546 (1973) (reading the will as a whole testator would prefer enforcement of dispositive provisions to loss of the charitable deduction; court has no power to modify an instrument when the action would conflict with testator's intent).

der during the transition period preserved a charitable deduction for the estate. This decrease in the estate tax liability increased the amount ultimately available for charitable purposes, which furthered the policy favoring charitable contributions.[44] These orders also promoted the policy favoring enforcement of the Internal Revenue Code. Any relief, to be effective, had to order compliance with the 1969 Tax Reform Act and regulations. Thus, these orders helped prevent a recurrence of the earlier abuses of split-interest gifts. Construction orders also made charitable remainder trusts more available to people who could not afford an estate planning specialist. The complex 1969 revisions had removed drafting of charitable remainder trusts from the competency of general practitioners.[45] People unable to retain the services of an estate planning specialist might have avoided charitable remainder trusts. Construction orders, however, led more general practitioners to recommend charitable remainder trusts, since they knew that a minor drafting defect could be cured. In addition to the public policy favoring construction orders, several state legislatures explicitly granted relief guaranteeing charitable remainder trust status.[46] Orders construing wills to include the requisite provisions merely followed public policy and these statutes.

In nontransition-period cases it was uncertain whether state courts would display the same willingness to grant relief solely on public policy grounds. Some statutes obviating the need for trust amendments did not apply to nontransition cases.[47] Additionally, in *Commisioner v. Estate of Bosch*[48] the United States Supreme Court held that when federal estate tax liability depends on a state-created property right, the IRS is not bound by a state court determination of that right unless the state's highest court had ruled on the question. The IRS implicitly indicated that *Bosch* would apply to nonqualifying charitable remainder trusts when it suspended the application of *Bosch* in transition-period cases.[49] Thus, in deciding whether to grant a nontransition-period construction order, state courts had to balance public policy in favor of the order against the absence of a statute and the possibility that the order might be moot because the IRS would not be bound.

The first test of a court's willingness to grant relief in a nontransition-period case arose in *In re Will of Stalp*.[50] In *Stalp* the testatrix left property in

44. *See, e.g., supra* note 27. *See also* Keith v. Scales, 124 N.C. 497, 515, 32 S.E. 809, 812 (1899) ("Courts incline strongly in favor of charitable gifts, and take special care to enforce them.").

45. This problem with the 1969 revisions was identified in Pedrick, *And then to Charity: Charitable Remainder Trusts and the Federal Estate Tax*, 17 INST. ON EST. PLAN. §§ 303-07 (1983).

46. *See, e.g.*, CAL. CIV. CODE §§ 2271.1-2271.2 (West Supp. 1984); MD. EST. & TRUSTS CODE ANN. §§ 14-301 to -308 (1974 & Supp. 1983); N.C. GEN. STAT. § 36A-53(b) (Cum. Supp. 1983); N.Y. EST. POWERS & TRUSTS LAW § 8-1.8 (McKinney Supp. 1983-84).

47. *See, e.g.*, N.C. GEN. STAT. § 36A-53(b) (Cum. Supp. 1983) (applies only to wills executed before December 31, 1978).

48. 387 U.S. 456 (1967) (IRS not bound by state court's determination of the effect of an instrument releasing a general power of appointment).

49. Rev. Rul. 74-283, 1974-1 C.B. 157. *See also* Wissbrun, *Bosch and its Aftermath: The Effect of State Court Decisions on Federal Tax Questions*, 114 TR. & EST. 8 (1975).

50. 79 Misc. 2d 412, 359 N.Y.S.2d 749 (Surr. Ct. 1974).

trust to pay one hundred dollars a month to her aunt for life and the remainder to a hospital. The aunt's income interest did not comply with the required annual distribution of at least five percent of the trust corpus, as required in the charitable remainder trust rules.[51] The executor petitioned for a construction of the trust instrument to save the charitable deduction even though the action fell between amendments to the transition rules. The court granted relief by segregating the private annuity interest from the charitable interest, stating that public policy compelled the result notwithstanding its nonbinding effect on the IRS. The result in nontransition-period cases remained uncertain after *Stalp*, however, because the court seemed influenced by a pending amendment to the transition rules.[52]

Last Will and Testament of Kander,[53] however, resolved any remaining doubt, at least in New York, in favor of nontransition-period construction orders. In *Kander* the testator directed that ninety percent of the income and remainder from a trust established by his will be paid to charity. The remaining ten percent was devised to a private beneficiary and an unrecognized charity. Despite the absence of an applicable transition rule, the court ordered segregation of the two interests into two trusts so that the ninety percent interest would qualify for a charitable deduction. The court reasoned that any other result "would be inconsistent with reason and justice."[54]

The trial court's decision in *Sands* followed the view of the New York courts in *Stalp* and *Kander* that public policy[55] compels a construction order. The trial court also used the statutory authority in section 36A-53(a) to grant the construction order. But *Sands* presented an even stronger case for construction. Not only did public policy and section 36A-53(a) support construction, but the supreme court did not have to consider the decision's possible inconclusive effect on the IRS.[56] Viewed in this light, the North Carolina Supreme Court's decision in *Sands* was justified.

Arguably, however, section 36A-53(a) did not support the construction order in *Sands*. The words "illegal," "impossible," and "impracticable of fulfillment" used in section 36A-53(a) connote a total failure of a charitable gift rather than mere disqualification for a federal estate tax deduction. Disqualification of the trust in *Sands* would have reduced the amount available to the charity but would not have made the gift any less enforceable. A greater failure than that in *Sands* should be required to invoke the power granted in section 36A-53(a). Section 36A-53(b) strengthens this view because it specifically mentions the failure of a trust to qualify for a federal estate tax deduction

51. *See supra* text accompanying note 9.

52. *Stalp*, 79 Misc. 2d at 421, 359 N.Y.S.2d at 756. *See also In re* Will of Rayvid, 88 Misc. 2d 372, 388 N.Y.S.2d 211 (Surr. Ct. 1976) (later case granting similar relief decided between amendments).

53. 115 Misc. 2d 386, 454 N.Y.S.2d 229 (Surr. Ct. 1982).

54. *Id.* at 388, 454 N.Y.S.2d at 231.

55. *See supra* text accompanying notes 44-46.

56. Because the decision came from the state's highest court, the IRS had to accept the court's determination and allow the charitable deduction. *See supra* text accompanying notes 48-49.

under the charitable remainder trust rules.[57] If the legislature had wanted disqualification to invoke the authority in section 36A-53(a) it would have specifically mentioned it in that section or in the definition of impracticable of fulfillment.[58]

Moreover, the court was not without a statutory alternative. The Charitable Remainder Trusts Administration Act[59] states that:

> Notwithstanding any provisions in the laws of this State or in the governing instruments to the contrary, any charitable remainder annuity trust and any charitable remainder unitrust that cannot qualify for a deduction for federal tax purposes under section 2055 . . . of the Code in the absence of this Article shall be administered in accordance with this Article.[60]

The Act contains all of the administrative provisions necessary to qualify the trust as a charitable remainder trust.[61] This statute is more clearly applicable in *Sands* than is section 36A-53(a) because it specifically mentions failure to qualify for a deduction as a condition to its applicability. Moreover, the IRS has recognized this type of statute as effective to preserve a charitable deduction.[62] The trial court did not use the Act because it was not enacted until after the court had decided the case.[63] The Act was passed during the pendency of the appeal, however, and made retroactive to the creation date of the trust.[64] Given the Act's clearer applicability and its acceptance by the IRS, the supreme court in *Sands* should have considered employing its provisions instead of affirming the use of section 36A-53(a).

The use of section 36A-53(a) instead of the Charitable Remainder Trusts Administration Act creates problems because the court had to specify the relief granted to save the charitable deduction.[65] The court's distinction between reformation and construction is not justified. Reformation has been defined as "a remedy to parties and the privies of parties to written instruments, to rectify them where they fail, through mistake or fraud, to conform

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57. N.C. GEN. STAT. § 36A-53(b) (Cum. Supp. 1983) provides:

> In the case of a will executed before December 31, 1978, . . . if a federal tax deduction is not allowed at the time of the decedent's death . . . any judge may . . . order an amendment to the trust so that the remainder interest is in a trust which is a charitable remainder [trust].

58. *See supra* note 35.

59. N.C. GEN. STAT. §§ 36A-59.1 to -59.7 (Cum. Supp. 1983).

60. *Id.* § 36A-59.2.

61. *Id.* §§ 36A-59.4 to -59.6.

62. As noted in *supra* note 12, charitable remainder trusts are subject to the governing instrument requirements of I.R.C. § 508(e) (1982). Treas. Reg. § 1.508-3(d)(1) (1972) states that governing instruments will be deemed to meet the § 508(e) requirements if valid provisions of state law either require the foundation to operate in conformity with the mandatory language (as in the Charitable Remainder Trusts Administration Act) or treat the language as being contained in the governing instrument. These rules apply without regard to any transition rules. *See also* Rev. Rul. 75-38, 1975-1 C.B. 161.

63. The Charitable Remainder Trusts Administration Act was enacted on June 18, 1982. The trial court entered its order on February 16, 1982.

64. Charitable Remainder Trusts Administration Act, ch. 1252, § 2, 1982 N.C. Sess. Laws 149 states that "this act relates back to the date of creation of the trust."

65. *See supra* text accompanying notes 37-39.

with the real agreement."[66] Construction, on the other hand, is "an effort to find the mind of the testator as expressed in the will."[67] In *Sands* the court added trust administration language that mistakenly had been omitted from the will, when it should have discerned the intended meaning of language contained in the will. This process falls within the definition of reformation, yet the court classified it as construction to save the charitable deduction.[68] Instead of using the two doctrines interchangeably, the court could have granted general relief under the Charitable Remainder Trusts Administration Act. This basis for relief would have preserved the charitable deduction[69] and the integrity of the two doctrines.

Whether based on the Charitable Remainder Trusts Administration Act or section 36A-53(a), the *Sands* decision probably will not lead to judicial construction of defective *private* trusts so that they too will qualify for favorable tax treatment. Although the policy that supports making tax favored trusts more available to the average taxpayer[70] also applies to private express trusts, no public policy favors these conveyances and no specific statutory authority to grant relief exists. Furthermore, the use of charitable remainder trusts is limited. Favorable construction of other trusts would result in increased judicial supervision of private express trusts. This might unduly burden the courts and probably would override any factors in favor of extending *Sands* to other trusts.

The North Carolina Supreme Court's construction of the will and trust in *Sands* certainly benefited the private income beneficiaries and the charitable remainderman. More importantly, the result demonstrated the court's willingness to forgive technical drafting errors that could jeopardize a charitable deduction. Yet given the somewhat strained application of section 36A-53(a), in future cases the courts of North Carolina should consider granting relief pursuant to the recently enacted Charitable Remainder Trusts Administration Act. Either alternative, however, should appeal to attorneys in North Carolina. Armed with a healthy respect for the complex charitable remainder trust rules and two avenues for correcting mistakes, practitioners should not hesitate to recommend these trusts to effect their clients' charitable aims.

DANIEL LOUIS JOHNSON, JR.

66. Henderson v. Henderson, 158 Tenn. 452, 453, 14 S.W.2d 714, 715 (1929).
67. Baker v. Edge, 174 N.C. 100, 102, 93 S.E. 462, 463 (1917).
68. *See supra* text accompanying notes 37-39.
69. *See supra* notes 61-64 and accompanying text.
70. *See supra* text accompanying note 45.