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A flip charitable remainder unitrust with a makeup provision ("unitrust”) is a gift plan defined by federal tax law that allows a donor to provide income to herself and/or others while making a generous gift to charity. The income may continue for the lifetimes of the beneficiaries, a fixed term of not more than 20 years, or a combination of the two.

The donor irrevocably transfers property, for example illiquid assets such as real estate, to a trustee of choice, such as a bank trust department. The donor receives an income tax deduction equal to the trust's remainder value to the charity, subject to IRS 30%/50% limitations. The remainder value to charity must be at least 10% of the funding amount.

During the unitrust's term, the trustee invests the unitrust's assets. Each year, the trustee distributes to the income beneficiaries a fixed percentage of between 5% and 50% of the unitrust's value, as revalued annually. Payments may be made annually, semiannually, quarterly, or monthly.

Each year, the trustee makes payments to the income beneficiaries. The method used to determine the amount of these payments "flips" upon the occurrence of an event stipulated in the trust instrument. Allowable triggering events are the sale of unmarketable assets held by the trust, the arrival of a specific date, or a single event whose occurrence is not within the control of the trustee or anyone else, such as a marriage, divorce, death, or birth of a child.

Prior to the flip, the trustee pays the beneficiaries the fixed percentage the unitrust is supposed to distribute or the income earned by the trust, whichever is less. This "net income" feature guarantees that trust principal is not invaded to make a distribution during the time the funding asset is held in the trust. If the trust earns more than the fixed percentage during a later year within the pre-sale period, the unitrust will make up its earlier shortfall to the extent that its earned income exceeds its fixed percentage.

After the year in which the flip is triggered, the trustee pays the beneficiaries the unitrust's fixed percentage, regardless of the income earned by the trust. This "flip" in how payment amounts are determined allows the trustee to invest for growth or for income after the funding asset is sold without limiting income payments.

After the flip, if the unitrust's value goes up from one year to the next, its payout increases proportionately. If the unitrust's value goes down from one year to the next after the flip, however, the amount it distributes also goes down. For this reason, it may be to advantageous to choose a relatively low payout percentage so that the unitrust assets can grow, which in turn will allow the unitrust's yearly payments to grow.

When the unitrust term ends, the unitrust's principal passes to charity, to be used for the purpose the donor designates. The donor may add funds to her unitrust whenever she likes.

Flip trust final regulations (Treasury Decision 8791)

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