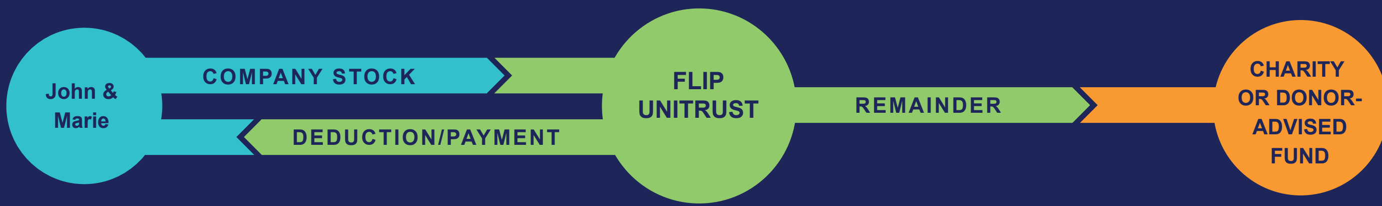
John & Marie Butte

Using a FLIP Unitrust to Diversify



John and Marie Butte, both age 58, plan to retire in five years. During his career, John has been granted (and exercised) stock options from the company where he works. The stock currently has a fair market value of $1 million and John's basis in the stock is $100,000. Even though they have other assets, John and Marie recognize that they will need to rely on this asset to produce a portion of their retirement income. With the fluctuation in the market, John and Marie have become concerned that a large portion of their wealth is tied up in one company. However, selling some of the stock would result in a significant capital gains tax.

The Buttes' financial advisor describes how a FLIP Charitable Remainder Unitrust (FLIP Unitrust) will permit them to diversify without incurring immediate capital gain tax and at the same time provide a steady cash flow stream during their retirement years. By contributing their stock to a "Flip Unitrust", they can achieve the following objectives:

1. Diversify and avoid the capital gain tax of approximately $206,000 on the sale of $1 million in company stock.
2. Obtain a current income tax charitable deduction in the amount of $195,000 for the present value of the remainder interest upon transfer of the stock to the FLIP Unitrust.
3. Minimize income for the first five years and allow the trust to appreciate.
4. After five years, take a steady cash flow stream from the CRT for retirement.

In this example, the defined triggering event is a date, specified in the trust document that corresponds with John's expected retirement. This will allow the trustees to invest the trust's assets to minimize the income earned and allow the trust corpus to appreciate during the initial phase (see the side-bar at right). Assuming the trust principal grows during the initial five year period, the annual income distributed to John and Marie will be enhanced at the end of the five year period when the trust "flips".

Benefits of Butte CRT	
Income Tax Deduction	$195,000
Before-Tax Lifetime Cash	$2,891,000
Donor-Advised Fund	$2,347,000
Capital Gain Taxes Deferred	$206,000

The FLIP Unitrust

The life cycle of a FLIP Unitrust is generally characterized by two phases. In the initial phase, a FLIP Unitrust only distributes the trust's net income. In the second phase, following the occurrence of a predetermined triggering event, the trust "flips" to pay out a fixed percentage of the trust's annual fair market value. The flip occurs on January 1st of the year following the triggering event. The triggering event must be defined in the trust document and is based on:

- A marriage,
- A divorce,
- A death,
- The birth of a child,
- The sale of an unmarketable asset or
- An uncontrolable event

Assumptions:

- Combined federal and state capital gains tax of 22.86%.
- CMFR of 2% and a payout rate of 6%.
- Distributions of 1% during the first 5 years and 6% thereafter. Assumes annual portfolio investment return of 8%.
- Based on a combined federal marginal income tax rate of 41.86% and an income tax deduction of $195,000.
- Taxable estate and a marginal estate tax rate of 40%.

This example is hypothetical and for educational use only. The situations, tax rates or return numbers do not represent any actual clients or investments. There is no assurance that the rates depicted can or will be achieved. Actual results will vary. Please consult with legal and tax counsel about the suitability.

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