

Enhance Tax Efficiency for Your Portfolio

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Polen Welcomes 351 Exchange Discussions

Benefits of a 351 ETF Exchange:

- **Tax Deferral:** Transfer securities into an ETF without triggering immediate capital gains taxes.
- **Diversification:** Help reduce single-stock and/or concentrated exposure by moving into a diversified vehicle (e.g., an ETF).
- **Implementation / Transition tool:** Can facilitate moving from legacy holdings into a new allocation with less “tax friction.”
- **Carryover Basis and Holding Period:** Maintain your original cost basis and holding period in the new ETF shares.
- **Potential ETF tax efficiency thereafter:** Once in an ETF, investors may benefit from tax-efficient ETF mechanics.

Why Consider a 351 ETF Exchange?

ETFs have gained popularity for their intraday liquidity, low fees, and tax efficiency. However, investors may hesitate to sell appreciated legacy stock positions due to capital gains taxes. A Section 351 tax-free exchange allows investors to efficiently move these low-basis holdings into an ETF without triggering immediate tax consequences, subject to certain applicable criteria.

ETFs are generally more tax-efficient than SMAs, private funds, or mutual funds in taxable accounts because their in-kind creation and redemption process avoids most capital gains inside the fund. Under Section 852(b)(6), ETFs can prevent capital gains distributions, allowing investors to defer taxes until ETF shares are sold.

In short, a Section 351 exchange potentially allows for the avoidance of capital gains, while preserving the original tax basis.

What is a 351 ETF Exchange?

Section 351 of the Internal Revenue Code allows investors to transfer appreciated assets, like stocks, into an ETF without triggering capital gains taxes—similar to a 1031 exchange in real estate. Investors can diversify by contributing a portfolio of securities to a new ETF in exchange for ETF shares, deferring taxes on unrealized gains.

To qualify, the portfolio must be diversified, and investors must control at least 80% of the ETF immediately after the exchange. Additional requirements include:

- No single issuer's securities may exceed 25% of the contributed portfolio's value.
- The top five issuers' securities may not exceed 50% of the portfolio's value in total.
- ETFs are “looked through” for diversification testing.
- Contributed positions must align with the ETF's investment mandate (e.g., only US equities for a US equity ETF).

How Section 351 Exchanges Affect Taxes

The ETF and its investors will recognize no taxable gain or loss in the transaction. Both will receive a carryover basis and holding period—with the ETF's based on the original assets' acquisition date, and investors' based on their prior assets.

1. Requirements

Investors may transfer a diversified securities portfolio to a new ETF and receive ETF shares tax-free if IRS rules are met. No single stock may exceed 25% of the portfolio; the top five stocks together must not exceed 50%. Contributing investors must control at least 80% of the ETF after the exchange.

2. Eligible Securities

Allowed: Stocks, ETFs and ADRs

Not Allowed: Mutual funds, cryptocurrency, options, private investments, restricted stocks, and closed-end funds.

3. Minimum Contribution

\$500,000 per investor

4. Conversion Process

1. Submit interest and portfolio details to Polen.
2. Polen and our Service Providers review for IRS eligibility.
3. If approved, sign paperwork (KYC, tax opinion, rep letter, custodian forms); submit documents and tax lot info two weeks before launch.
4. Shares are transferred to the ETF two days before launch, valued at the prior day's closing price; ETF shares are issued on launch day.
5. Cost basis and holding period are transferred to the ETF shares post-launch.

5. Diversification Rules

- **Individual:** No position >25%; top 5 positions ≤50%.
- **Fund:** Combined contributions must also meet RIC guidelines: no position >25%, positions >5% together ≤50%.

6. Tax Consequences Post-Conversion

No taxable gain or loss for the ETF or investors. Both receive a carryover cost basis and holding period. Capital gains tax applies only when ETF shares are ultimately sold.

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Portfolios that Qualify:

- An investor wants to contribute a portfolio consisting of 20% Nvidia stock and 80% assorted stock holdings, each representing approximately 1% of the positions.
- An investor wants to contribute a portfolio consisting of 100% SPY ETF.
- An investor with a 20-stock portfolio that is roughly equally weighted.

Portfolios that DO NOT Qualify:

- An investor with a Schwab brokerage account wants to contribute a portfolio consisting of 50% Nvidia stock and 50% cash.
- An investor with a portfolio of mutual funds.
- An investor with a portfolio of DogeCoin.



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