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351 Exchange Overview

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Tax-Deferred Reallocation with 351 Exchanges

Section 351 of the Internal Revenue code allows investors to contribute appreciated assets into an exchange traded fund (ETF), in exchange for shares in the ETF, without triggering capital gains taxes. Exchanges are only available to U.S. persons, including individual and joint accounts, trusts, and S-corps. Partnerships and LLCs may qualify.

The exchange can only be used to transfer assets to a newly created ETF (called seeding) and must satisfy "25/50" diversification requirements under IRC §368(a)(2)(F). There are limitations as to what can be used as contributed property. Single stock positions and ETFs are eligible, and ETFs receive look-through treatment to the underlying positions. Mutual funds, limited partnerships, commodities, and other alternatives are not accepted.

Portfolios that (1) have a high tax cost for reallocating and (2) will experience a high expected benefit from reallocating are ideal candidates for a 351 exchange. Typical use-cases include ossified direct indexing accounts and reducing concentrated positions.

How does the exchange work, in practice?

Once a portfolio reallocation decision has been made and securities are identified, we will partner with the ETF sponsor to ensure the proposed securities meet all eligibility requirements.

Approximately one month before the exchange takes place, we will submit proposed contributions to the ETF sponsor for their evaluation. Once those checks and approvals have been satisfied, legal documents are signed and, in the days leading up to the ETF launch, the contributed assets will be transferred into the new fund. Following final compliance checks, the contributed assets are exchanged for shares in the new ETF and sent back to the custodian.

Investors generally see the new shares in their account within one or two days following the conversion date. The investor's previous tax basis is also transferred to the new ETF shares and communicated to the custodian, preserving future tax and estate planning opportunities.

One important note: the SEC requires that contributed securities align with the ETF's investment mandate, which means an investor can't contribute US stocks into an international equity ETF. However, US stocks can be contributed to an ETF with a global investment mandate.

What are the specific diversification rules for contributions?

Diversification rules apply on an investor-by-investor basis and broadly follow two guidelines. First, the 50% / top-five rule: The top five contributed securities cannot exceed 50% of the total portfolio value. Second, the 25% rule: No single security can comprise more than 25% of the contributed securities. Investors can include part of a concentrated position as long as portfolio of contributed securities meets the diversification requirements. The IRS would look unfavorably if the investor had used leverage to purchase securities to meet diversification requirements or if the investor contributed a previous 351 exchange into another 351 exchange in order to reduce the same concentrated position.

Near-term Opportunities

At the current time, most 351 exchanges are into ETFs targeting either indexed US large cap exposure or indexed global exposure. Some active fund companies have utilized 351 exchanges to seed new, actively managed ETFs. Index ETFs tend to have lower expense ratios (i.e. 0.25% or less), whereas actively managed ETFs can be more expensive.

US large cap mandate ETFs are seeded and launched every six months or so. These ETFs generally have low expense ratios and offer S&P 500-type exposure after launch.

It is more common for us to find investors that would prefer to use the 351 exchange to add international exposure to their portfolios. Fifteen years of US equity market outperformance has left many investors overweight US equities, but reallocating would otherwise come with a high tax cost.

We are currently diligencing, and expect our Investment Committee to ultimately approve, a global 351 exchange that is scheduled to close in mid-May 2026. It will target a global equity portfolio that is equally weighted to the largest 500 global companies by market cap (each stock will have a 0.2% weighting in the portfolio), will be rebalanced quarterly, and will be reconstituted annually. The ETF will have an expense ratio of 0.29%.

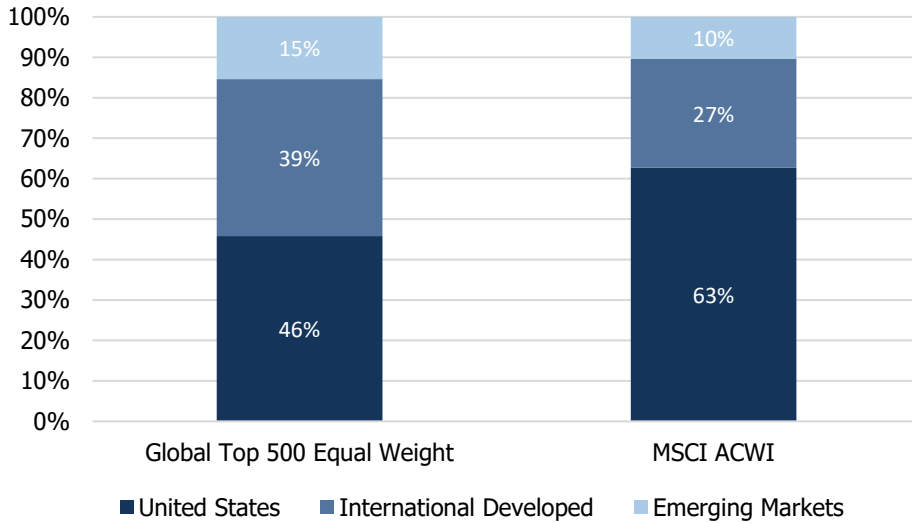
As of 12/31/2025, an equally-weighted portfolio of the largest 500 global companies has broader geographic exposure (Fig. 1), less sector concentration (Fig. 2), lower index valuations, a higher dividend yield, and an average market cap that is significantly lower than the market cap weighted MSCI All Country World Index (MSCI ACWI) (Fig. 3). Over the long term, the equally weighted strategy has slightly outperformed the MSCI ACWI, but with long, sustained cycles of out/under performance for each index (Fig. 4).

It is our opinion that investors shouldn't base their allocation decision on whether the equally-weighted index will outperform the market cap weighted index, and we did not select this strategy with a high conviction of outperformance. Instead, the equally-weighted index provides more "bang-for-the-buck" for investors seeking additional international exposure, and future performance should be viewed in the portfolio context of that allocation shift, not against the ACWI index or the strategy that funded the exchange.

Conclusion

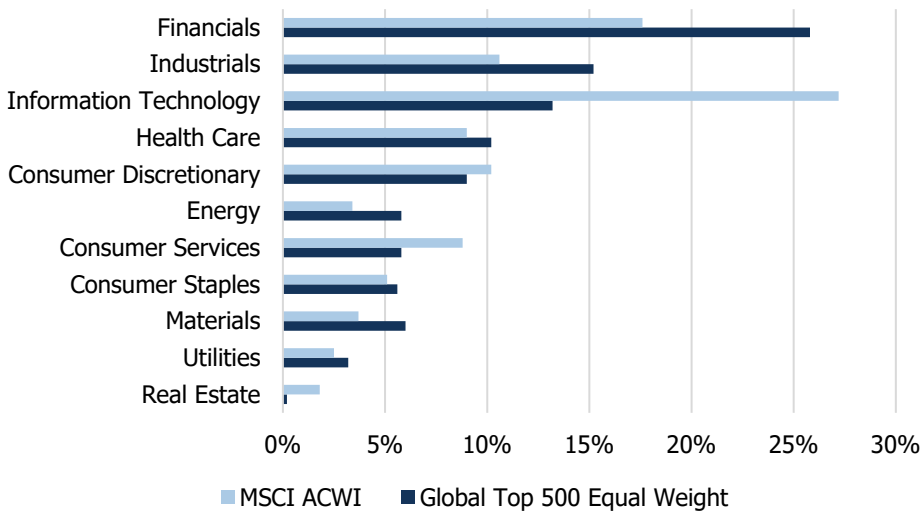
Section 351 exchanges are best suited for investors that would benefit from reallocation within their equity portfolios and face a high tax cost from the reallocation. There are constraints in regard to the investors that can participate, the types of property that are accepted, and the available investment mandates, but 351 exchanges can be very useful tools for investors that fit the appropriate criteria.

Fig. 1: Geographic exposure comparison



Source: Cambria, Bloomberg, Mill Creek. As of 12/31/2025.

Fig. 2: Sector exposure comparison



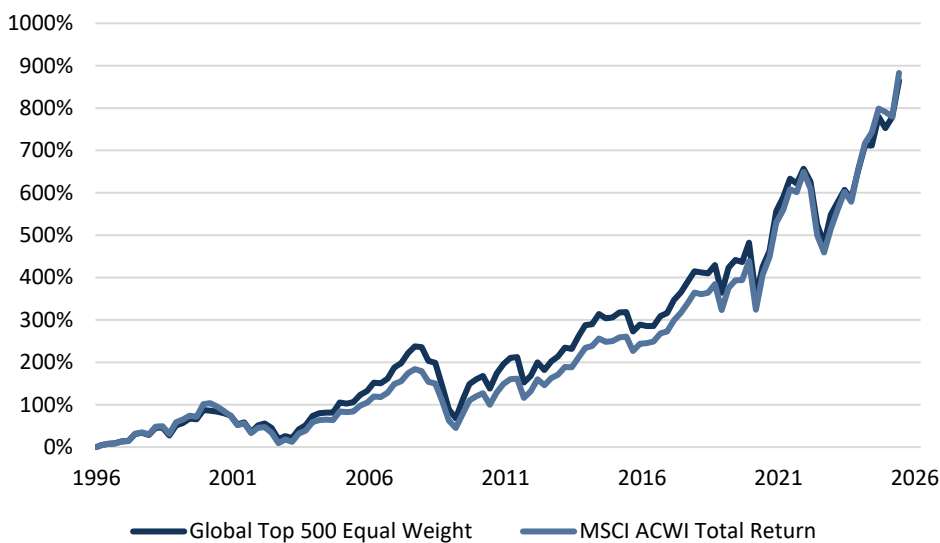
Source: Cambria, Bloomberg, Mill Creek. As of 12/31/2025.

Fig. 3: Index characteristics

	Global Top 500 Equal Weight	MSCI ACWI
Number of Constituents	500	2246
Average market cap (billions)	187.2	948.9
Weight of top 10 constituents	2.0%	24.5%
P/E	20.2	24.2
P/B	2.8	3.6
Dividend Yield	2.30%	1.80%

Source: Cambria, Bloomberg, Mill Creek. As of 12/31/2025.

Fig. 4: Long-term performance



Source: Source: Cambria, Bloomberg, Mill Creek. As of 12/31/2025.

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An index is unmanaged and unavailable for direct investment. The Global Top 500 Equal Weight Index is a rules-based equity index that tracks the performance of 500 of the largest global companies, with each constituent assigned an equal weight at periodic rebalancing, rather than weights based on market capitalization. The MSCI ACWI Total Return Index is a market capitalization-weighted index designed to measure the performance of large- and mid-cap equities across developed and emerging markets globally, with dividends reinvested.

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