NATIXIS INVESTMENT MANAGERS | SOLUTIONS

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Tax trends and tactics: Section 351 exchanges, AI, and year-end planning



Section 351 exchanges: Incremental diversification without an immediate tax bill

One approach to managing appreciated stock positions that's gaining popularity is the Section 351 exchange. Instead of selling appreciated shares and recognizing capital gains, an investor may be able to contribute them in-kind to a newly forming ETF in exchange for shares of the ETF. If structured properly, the transaction is tax-deferred. The investor's cost basis carries over, leaving the ETF shares with the same amount of embedded gains.

As of mid-October, Tax Alpha Insider estimates that approximately 120 ETFs, representing $21 billion, have been launched this way. The contributed shares reportedly had a combined cost basis of $12 billion, allowing investors to further diversify their portfolios, rebalance, reduce fees, or simplify the number of individual holdings while deferring billions in unrealized capital gains.

By contributing appreciated shares alongside other investors interested in the ETF's objective, an investor gains exposure to the entire asset pool. For example, Investor A might have appreciated large-cap value stocks and want to add growth exposure without selling and realizing gains. And Investor B might hold large-cap growth stocks and want to rebalance toward value stocks. If they both find an attractive, newly forming large-blend ETF, each could contribute their stocks in exchange for ETF shares.

After inception, the ETF will trade like any other and new investors contributing cash allow the portfolio manager to move the fund closer to its target. Additional tax efficiency comes from the ETF's creation and redemption mechanism that allows appreciated shares to be redeemed in-kind, potentially reducing unwanted or overweight positions and reducing the chances the ETF has to distribute capital gains to shareholders at year end.

AI is quickly moving beyond simply helping advisors work faster and beginning to identify planning opportunities across a client's investments, taxes, and estate plan that may otherwise be difficult to spot.



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Diversification testing and the composition of the contributed basket matter, as does whether the securities are consistent with the ETF's strategy. If not, the ETF could reject them and the investor would have to look for a better fit elsewhere. The contributed portfolio must be sufficiently diversified to pass the 25/50 test. The test essentially prohibits concentrated stock positions from being transformed into a diversified ETF tax-free.

Even a diversified portfolio contributed could trigger tax. In September, the IRS released Revenue Ruling 2026-20[1] that found a 351 transaction failed based on legal principles of "substance over form" and the "step-transaction doctrine."

In this case, an investor contributed a diversified portfolio of appreciated securities to a newly formed ETF intended to qualify under Section 351. As part of the same plan, the ETF issued shares to an authorized participant (AP) in exchange for securities consistent with the ETF's investment strategy. Shortly after, the ETF redeemed the AP's shares in-kind using the appreciated securities originally contributed by the investor. After the transactions, the ETF held a portfolio consistent with its investment strategy but that was materially different from the portfolio originally contributed by the investor.

The ruling found that these transactions were part of a plan designed to enable the investor to exchange its appreciated portfolio for a materially different portfolio without recognizing any gains and ruled that it was a taxable transaction. The ruling raises questions about how quickly and how much of a contributed portfolio a manager can dispose of without jeopardizing 351 treatment.

One common use case is shifting from a separately managed account (SMA) of individual, appreciated stocks into an ETF clone. In early October, Natixis affiliate Harris Oakmark launched the Oakmark U.S. Concentrated ETF via Section 351 exchange. This new, actively managed ETF closely resembles an existing Harris concentrated equity SMA which made it a natural fit for existing investors looking for simpler ownership and easier charitable giving and estate planning.

A Section 351 exchange can be useful for investors with legacy, appreciated portfolios looking for incremental diversification, simplicity, professional management, or potentially lower fees, without first generating a large tax bill.

Artificial intelligence meets tax and financial planning tools

The AI wave reached the tax and financial planning world on February 10 when Altruist introduced a tax-planning agent for its Hazel AI platform. During the third quarter, Anthropic launched Claude for financial advisors and within the first week, it had been installed 30,000 times. The plugin integrates with major components of an advisor's tech stack including Charles Schwab, Envestnet, FactSet, Morningstar, and Salesforce.

Claude lets advisors run workflows to accomplish tasks, drawing information from connected programs to do so. It comes with several pre-built skills including pre-meeting preparation, portfolio review, and estate and tax brief. The estate and tax brief workflow checks for alignment among the estate plan, account titling, and designated beneficiaries and reviews the previous year's tax returns.

Holistiplan, a tax-planning software, also rolled out an AI tool that reads tax returns and generates potential tax savings actions for the advisors to consider with clients. Tax savings are classified as *true savings* like tax loss harvesting, *deferred savings* like Roth conversions, and *deferred cost* like traditional 401(k) contributions.

It's built to consider over two dozen tax-related strategies and assigns an estimated tax savings and confidence level to each. Many of the strategies we've discussed in Tax Trends and Tactics are included in Holistiplan's strategy library: tax loss harvesting, maximizing the 0% long-term capital gains bracket, mega backdoor Roth conversions, asset location optimization, maximizing HSA contributions, and gifting appreciated stock.

AI is quickly moving beyond simply helping advisors work faster and beginning to identify planning opportunities across a client's investments, taxes, and estate plan that may otherwise be difficult to spot. As AI becomes more deeply embedded in the advisor's tech stack, it has the potential to help advisors be more proactive and deliver personalized advice at scale.

Year-end planning: Three timely actions

As we approach year-end, we'd like to highlight three time-sensitive actions that can affect tax bills: tax loss harvesting, charitable giving, and gain harvesting.

When tax loss harvesting, don't forget to check fixed-income positions including individual bonds, ETFs, and mutual funds. At quarter end the 10-year Treasury yields around 5.25%, after being below 4% earlier this year, which may have resulted in unrealized losses. Be aware that harvesting a loss in a municipal bond may create unintended taxable income if the "de minimis" rule is violated when selecting a replacement security.

In 2026, the rules governing charitable giving changed. For those itemizing deductions, only donations exceeding 0.5% of AGI are deductible. And the deduction is capped at 35% for taxpayers in the 37% bracket. Taxpayers who claim the standard deduction may deduct up to $1,000 (single) or $2,000 (married filing jointly) for direct cash gifts to qualified public charities. Gifts of household goods or securities, and contributions to a donor-advised fund, are ineligible.

Those 70½ or older also have the ability to direct up to $111,000 of their annual Required Minimum Distribution (RMD) from IRAs to a charity through a Qualified Charitable Distribution (QCD). A QCD is excluded from taxable income and counts toward the RMD, so it generally makes sense once living expenses are covered. Note that workplace 401(k)s and 403(b)s are ineligible for QCDs. And while the QCD satisfies the RMD, the taxpayer can't also claim a charitable deduction for the gift.

Gain harvesting is most effective when there's room in the 0% capital gains bracket. Because the wash sale rule applies to losses, not gains, an investor may repurchase the security immediately and reset the cost basis higher.

Tax loss harvesting	Charitable giving	Gain harvesting
Look to short-term losses before long-term losses as they offset more costly short-term gains first Don't repurchase the same stock within 30 days — the wash sale rule straddles the calendar year	Look to long-term capital gain property to fund charitable gifts to avoid paying capital gains tax and to get the market value deduction Short-term gains property can only be deducted to the extent of the cost basis	If you're in a temporary low tax bracket, consider harvesting long-term gains to fill up the lower tax brackets Don't forget UTMA/UGMA accounts to take advantage of the $1,350 kiddie tax threshold

Trump accounts auto enrollment

Recent conversations have revealed that many are still confused by these new types of retirement accounts. Most confusion comes from parents thinking their kids don't qualify for the $1,000 and therefore can't open an account. The one-time $1,000 contribution from the U.S. Treasury is available to children born between January 1, 2025, and December 31, 2028. But a parent or guardian can open an account for any child before their 18th birthday. In October, the U.S. Treasury automatically enrolled the remaining eligible children, about 60 million new accounts, and plans to continue auto enrolling newborns.

That means a child may have an account even if the parent never opened one. And given the potential for fraud, we think it makes sense for parents to "claim" the account via the Trump accounts app or website before someone else does. And private philanthropic commitments from the likes of Michael Dell and Ray Dalio may have already funded some children's accounts.

Winners and losers: S&P 500® performance through September

Through September, the S&P 500® returned 12.75%, led by energy, information technology, and healthcare. Utilities, consumer discretionary, and financials are all down for the year.

Approximately 225 stocks in the index had negative returns through September and nearly 180 fell by 5% or more – levels typically considered attractive for tax loss harvesting.

Natixis Direct Indexing portfolio managers have been busy this year, harvesting over $1 billion in tax losses for clients across 59,000 accounts. At the end of the third quarter, direct indexing assets totaled $38.8 billion.

Among the biggest movers: Sandisk is leading the way up (+630%) followed by Moderna (+550%) and Dell Technologies (+330%). A handful of names are down 50% or more, including Trade Desk Inc., Fair Isaac Corp, and Applovin, to name a few. The high-flying semiconductor names that had stellar returns in Q2 tended to give some of those gains back during Q3.

We commonly point out that tax loss harvesting opportunities exist in all market environments. Market volatility is the price of admission to the equity markets.

The third quarter's lesson is to check the details early. A conversation with clients in November leaves time to harvest losses, plan charitable gifts, claim a child's Trump account and, for anyone considering a Section 351 exchange, confirm the structure with a tax professional.

S&P 500® performance by sector (1/1/2026–9/30/2026)

YTD through September 2026	Average weight %	Total return %	Contribution to return %	Stocks up %	Stocks down %
Information technology	35.7	28.9	9.5	68	32
Financials	12.3	-1.3	-0.2	47	53
Communication services	10.4	3.4	0.5	40	60
Consumer discretionary	9.6	-5.8	-0.5	29	71
Healthcare	9.1	10.2	0.8	69	31
Industrials	8.7	8.6	0.9	61	39
Consumer staples	4.8	6.0	0.3	54	46
Energy	3.4	40.3	1.2	90	10
Utilities	2.2	-5.7	-0.1	29	71
Materials	1.9	8.8	0.2	72	28
Real estate	1.9	5.3	0.1	59	41
S&P 500®	**100.0**	**12.8**	**12.8**	**56**	**44**

Source: Natixis Investment Managers Solutions
Performance data shown represents past performance and is no guarantee of future results.

S&P 500® returns and maximum drawdown



Source: FactSet; Natixis Investment Managers Solutions
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Past performance is no guarantee of future results.

[1] Internal Revenue Service, irs.gov.

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Exchange-Traded Funds (ETFs) trade like stocks, are subject to investment risk, and will fluctuate in market value. Unlike mutual funds, ETF shares are not individually redeemable directly with the Fund, and are bought and sold on the secondary market at market price, which may be higher or lower than the ETF's net asset value (NAV). Transactions in shares of ETFs will result in brokerage commissions, which will reduce returns.

Tax liability is the total amount of tax debt owed by an individual, corporation or other entity to a taxing authority.

Tax loss harvesting is a strategy for selling securities that have lost value to offset taxes on capital gains.

Tax alpha considers how an investment performed relative to its benchmark on a pretax and after-tax basis.

Capital gain is a rise in the value of a capital asset (investment or real estate) that gives it a higher value than the purchase price.

Diversification does not guarantee a profit or protect against a loss.

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