Commonwealth

Step-Out Trading Disclosure

This document provides information to clients who are participating, or are considering participating, in the Preferred Portfolio Services® ("PPS") Direct SMA/UMA Program ("Program") sponsored by Commonwealth Financial Network® ("Commonwealth").

Best Execution Obligation

Money managers ("Managers") within the Program may select the broker/dealers that execute trade orders for client accounts. As an investment adviser, a Manager has an obligation to seek "best execution" for client trade orders. The Manager must place client trade orders with those broker/dealers that the Manager believes are capable of providing the best qualitative service, taking into account the full range and quality of the services offered by the broker/dealer, including, but not limited to, the broker/dealer's execution capabilities, the broker/dealer's financial stability, and the broker/dealer's responsiveness to the Manager. A Manager's best execution obligation does not require the lowest available cost to be obtained for trade orders. Clients should understand that Commonwealth does not evaluate whether a Manager is meeting its best execution obligations when trading away, as it is not a party to those transactions and is not able to negotiate the prices obtained or transaction-related charge(s) assessed between the Manager and the executing broker or dealer. The responsibility to determine whether to trade away arises out of a Manager's individual fiduciary duty to clients and its trading expertise.

Step-Out Trades

Managers may place client trade orders with a broker/dealer other than Commonwealth if they determine they must do so to comply with their best execution obligations. This practice is frequently referred to as "step-out trading."

Step-out trades may be executed without additional cost, but in certain instances, the executing firm may impose a commission, markup, markdown, or other charges for executing the transaction. If a Manager engages in a step-out trade and the executing broker/dealer assesses a commission or equivalent fee on the trade, the client will incur trading costs that are in addition to the annual and Program fees paid by the client to participate in the Program. In such cases, the net purchase or sale price reflected to the client will include the additional cost of the brokerage commissions or dealer markups/markdowns charged by the executing broker. Managers may reasonably believe that they are able to achieve better trading results by trading away.

Step-out trading practices differ from Manager to Manager. Some Managers do not engage in step-out trading, while others step out all transactions at no additional cost or for various additional costs. Managers who engage in step-out trades may be more costly to a client than Managers who do not engage in step-out trades. Clients should review the Manager's Form ADV Part 2A Brochure, inquire about the Manager's trading practices and associated trading costs, and consider this information carefully before selecting a Manager. Please note that this information reflects historical data and may not be indicative of the current frequency with which Managers trade away or the related costs of such trades. A Manager's past practice is not a guarantee that the Manager will follow the same practice in the future.

Included is a list of Managers who have informed Commonwealth that they engage in step-out trading; it provides information on the additional costs to clients for those trades. Clients should review these step-out trading practices and their affiliated costs (if any) with their advisor. Clients may also wish to contact their advisor to determine if other Managers on the platform provide a similar strategy at a lower cost. The information listed below does not reflect step-out trading practices in which Managers may engage when positions transfer in-kind to a new account within the Manager's program. In such cases, depending on the holdings, Managers may engage in step-out trading for the purpose of selling existing positions and reinvesting the proceeds into the trading strategy selected by the client.

Please note: This information was provided to Commonwealth by the respective Managers, but it has not been independently verified by Commonwealth. All data is for calendar year 2019.

Manager	Strategy	Step-Out Percentage[1]	Additional Cost[2]
Boyd Watterson	Managed Income Solution Managed Account	100%	$0.13 per trade
Boyd Watterson	High-Quality Intermediate Muni Managed Account	100%	$0.48 per trade
Eagle	Strategic Income Portfolio (Taxable) Managed Account	45%–55%	Fees vary[3]
GW&K	Core Bond Managed Account, Enhanced Core Taxable Managed Account, Intermediate Municipal Managed Account, Short-Term Taxable Managed Account, Total Return Taxable Managed Account	100%	Fees vary[4]
Lord Abbett	Intermediate Tax-Exempt Fixed Income Managed Account	100%	Fees vary[5]
Nuveen	Intermediate Muni Fixed Income Managed Account	99.6%	1–10 bps[6]
Pacific Income	Limited Duration MACS Managed Account	70.9%	0.1 bps[7]
Pacific Income	Market Duration MACS Managed Account	78.4%	0.1 bps[7]
Thornburg	Domestic Equity Managed Account	12%	$0.05 cps

[1] Step-out percentage refers to the most recent data provided by the Manager regarding the percentage of trades stepped out by the Manager.

[2] Additional cost represents the average additional cost that clients pay for the Manager's step-out trades. Additional costs expressed as percentages are percentages of the total dollar value of the transaction; "CPS" denotes "cents per share." The following hypothetical examples are provided for illustrative purposes only. Actual costs may be higher or lower than those illustrated.

- If a Manager executes a step-out trade on a $10,000 transaction with an average additional cost of 0.1451 percent, the client would see an additional cost of $14.51 for the transaction.
- If a Manager executes a step-out trade on a transaction of 1,000 shares with an average additional cost of $0.05 cps, the client would see an additional cost of $50 for the transaction.

[3] For fixed income step-out trades, clients receive institutional execution where there is an institutional bond spread but no additional cost, except for certain types of trades done on electronic trading platforms (i.e., MarketAxess, Tradeweb, Liquidnet, TMC). Each platform has its own range of fees.

- **MarketAxess Open Trading:** The fee is from 0 to 1.5% bps to counterparty depending on size and maturity.
- **Tradeweb Corporate Trading:** The fee is 0.6 bp to the liquidity provider.
- **Tradeweb Direct:** Liquidity provider pays a fee, based on a pricing grid depending on maturity and size, $0.10–$3 per bond.
- **Liquidnet:** Fee is 1 bp all in.
- **Trumid:** Anonymous 18 months–5Y = 1 bp, 5y–10y = 0.8 bp, Old Long (Treasury) Bond (OLB) = 0.6 bp all in.
- **TMC (The Muni Center):** For Munis, the seller pays a fee depending on maturity in size ranging from a minimum of $0.10[1] and a maximum of $10 per bond. For Corporates and Agencies, a fee of $0.50–$1 per bond is charged to liquidity providers.
- **Arbor:** Ticket fee is $0.03125–$0.0625.

[4] The following disclosure of additional costs has been provided by GW&K:

"For municipal bond strategies, under normal market conditions: While the diversity of municipal markets and the sheer number of issuers makes it difficult to give general perspective on potential markup and markdown assessed by our trading partners, we believe those impacts to be typically between 0 and ½-point (dollar) markup or markdown trade by trade, with a weighted average of approximately ⅛-point (dollar).

For taxable bond strategies, under normal market conditions:

- Investment-grade corporate bonds are typically quoted within a 10-basis-point bid/ask spread but generally trade within a 5-basis-point markup/down if riskless.
- High-yield bonds are typically quoted within a one-point bid/ask spread but generally trade within ¼ point, or approximately a 5–10-basis-point markup/down, if riskless.
- MBS bonds are typically quoted with a ⅛-point bid/ask spread but generally trade within 1⁄16 point, or approximately a 5-basis-point markup/down if riskless.
- Treasury bonds typically trade within a 1⁄16-point markup/down.
- Taxable munis are comparable to investment-grade credit spreads."

[5] Lord Abbett has provided the following disclosure of additional costs:
"Trades away from Commonwealth do not incur any additional costs and typically provide the opportunity to reduce transaction costs. For selling bonds, each year we complete trades with over one hundred dealers, so we can put them in competition to produce the best bid rather than relying on just one firm to provide liquidity. Similarly, when we buy bonds we have access to the same number of dealers, so we are able to select from the full range of new issues and bonds offered in the secondary market. Lord Abbett does not mark up or charge commission for trades, so we do not collect any profits from completing the transactions. The dealers we trade with include the size of their commission in the net price they are paying us, so we do not control their markup but are able to monitor them through market data in order to make sure they are fair. Commissions are typically smaller for larger institutional size trades and when dealers are put in competition for business, but we review the net prices to determine if the bid or offer is attractive for our clients. Any commissions that are charged generally come from the client's custodian, if they are charged at all."

[6] For secondary market trades, dealer trading mark-ups can range from just a few cents to several dollars per bond depending on several factors, including position size, market strength or weakness, and holding period, among others. For primary market (new issue) trades, there are no additional trading costs.

[7] If step-out trades are performed over the phone, there is no additional cost. If the step-out trades are done using electronic trading platforms such as Tradeweb or MarketAxess, the average cost is approximately 0.1 bps.