The Safety of Customer Accounts Held at National Financial Services LLC

As a service provider to Commonwealth Financial Network,® Fidelity Institutional℠ [1] provides clearing, custody, and other brokerage services through National Financial Services LLC (NFS)[2] or Fidelity Brokerage Services LLC. As such, NFS provides trade execution, clearing, custody, and other related services for Commonwealth's customers' brokerage accounts. As registered broker/dealers, both Commonwealth and NFS are subject to the rules and regulations of the SEC, FINRA, and any other exchanges either firm is a member of, as well as of the Municipal Securities Rulemaking Board. Each of these regulatory organizations has certain rules and regulations regarding the safeguarding of customer assets, including, but not limited to, keeping accurate books and records, net capital requirements, and the Customer Protection Rule.

The Customer Protection Rule (Rule 15c3-3 of the Securities Exchange Act) generally requires a broker/dealer to (1) take physical possession or control of all fully paid securities and excess margin securities on its books and records; and (2) maintain with a bank a special reserve account for the exclusive benefit of its customers, containing the net funds it owes its customers. Under the Customer Protection Rule, our clearing firms are prohibited from pledging or borrowing a customer's fully paid (nonmargin account) securities in their proprietary business. The rule also limits the amount of a customer's securities a clearing firm can pledge to third-party lenders to support customer margin debt owed to the clearing firm.

[1] Fidelity Investments is an independent company, unaffiliated with Commonwealth. Fidelity Investments is a service provider to Commonwealth. There is no form of legal partnership, agency affiliation, or similar relationship between your financial advisor and Fidelity Investments, nor is such a relationship created or implied by the information herein. Fidelity Investments has not been involved with the preparation of the content supplied by Commonwealth and does not guarantee or assume any responsibility for its content. Fidelity Investments is a registered service mark of FMR LLC. Fidelity Institutional℠ provides clearing, custody, or other brokerage services through National Financial Services LLC or Fidelity Brokerage Services LLC, Members NYSE, SIPC. 815986.2.0

[2] The conclusions stated in this memo equally apply to Commonwealth's relationship with Pershing LLC, which provides clearing services on a minimal number of customer accounts.

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SIPC: Protecting Customers from Broker/Dealer Failure

Commonwealth and its clearing firms are members of the Securities Investor Protection Corporation (SIPC), which was created in 1970 as a nonprofit, nongovernment membership corporation funded by member broker/dealers. Its primary role is to restore funds to investors if the broker/dealer holding their assets fails financially. SIPC does not reimburse customers for market loss, investment fraud, or worthless securities; instead, it steps in to help individuals whose money, stocks, and other securities are at risk when a broker/dealer files for bankruptcy or becomes insolvent. The SIPC fund currently stands at just less than $4 billion, and it has borrowing power of up to $2.5 billion more from the U.S. Treasury through the SEC.[3]

It should be noted that, from the time SIPC came into existence through December 2020, SIPC has advanced $3.1 billion to make possible the recovery of $141.8 billion in assets for an estimated 773,000 investors. Not every investor is protected by SIPC, but SIPC estimates that, with its help, 99 percent of eligible people got their investments back in the failed brokerage firm cases it has handled to date.[4]

SIPC steps in when a firm has failed and filed for bankruptcy or is in danger of doing so. Upon either of these events, SIPC would request a federal court to issue a protective decree and appoint a trustee to liquidate the firm's assets.

For the purposes of a liquidation under SIPC, a firm's assets are divided into three categories: (1) securities (including stocks and bonds) registered in the customer's name, which are returned directly to the customer or transferred on behalf of the customer to another brokerage firm; (2) cash and other securities held for customers (including stocks, bonds, and money market funds that are invested in securities) in street name, which are divided pro rata among all customers; and (3) general assets of the firm, which are used to pay any remaining unsecured claims of customers (after SIPC payments discussed below) and expenses of the liquidation.

If the securities and funds in (1) and (2) above are insufficient to cover a customer's claims, SIPC will cover the remaining shortfall owed to the customer, up to $500,000 (including a maximum of $250,000, which a customer may have at the time held in cash with the firm). If there is any shortfall remaining after the SIPC payment, customers become general creditors of the firm.

To reiterate, if a broker/dealer fails and is subsequently liquidated under SIPC, any securities registered in a customer's name would be transferred to another firm. Cash and securities held in street name would be paid out to customers in a pro rata portion of the aggregate amount of the cash and securities actually held by the broker/dealer. Any remaining shortfall would be covered by SIPC, up to a maximum of $500,000, of which only $250,000 may be the recovery of cash held at the broker/dealer.

Customers may increase their SIPC coverage by having multiple account registrations. A customer with an individual account, a joint account, an IRA, and a 401(k) plan account, for example, would be eligible for $500,000 coverage in each account, for a total of $2 million.

[3] SIPC Annual Report, 2020

[4] SIPC History and Track Record, www.sipc.org/about-sipc/history, as of 2020

Although most customers are eligible for SIPC assistance, SIPC's funds may not be used to pay claims of any failed brokerage firm customer who is also:

- A general partner, officer, or director of the firm
- The beneficial owner of 5 percent or more of any class of equity security of the firm (other than certain nonconvertible preferred stocks)
- A limited partner with a participation of 5 percent or more in the net assets or net profits of the firm
- Someone with the power to exercise a controlling influence over the management or policies of the firm
- A broker/dealer or bank acting for itself rather than for its own customer or customers

In addition, it should be noted that not all investments are protected by SIPC. In general, SIPC protects stocks, bonds, Treasury securities, certificates of deposit, money market funds invested in securities, mutual fund and other investment company shares, and other registered securities. It does not cover instruments such as unregistered investment contracts; unregistered limited partnerships; fixed annuity contracts; currency; and interest in gold, silver, or other commodity futures contracts or commodity options.

If a customer buys mutual funds through a brokerage account, those funds are protected by SIPC. If a customer buys mutual funds directly from the fund company, however, they aren't protected by SIPC because no protection is necessary. Every mutual fund is set up as a separate entity, apart from the investment advisor who manages the fund. The employees at a mutual fund company do not have direct access to customers' assets. Mutual fund assets, by law, are not held at the mutual fund, but rather are held in a trust account at a custodian bank. The trust account is not considered part of the bank's assets.

Although banks can and do fail, the mutual fund trust accounts are not involved in that failure.

After SIPC steps in, most customers can expect to receive their property in approximately one to three months after filing completed claim forms for brokerage firm liquidation.

Additional Customer Protection

In addition to SIPC protection, NFS provides for brokerage accounts additional "excess of SIPC" coverage. The excess of SIPC coverage will be used only when SIPC coverage is exhausted. Like SIPC protection, excess of SIPC protection does not cover investment losses in customer accounts due to market fluctuation. It also does not cover other claims for losses incurred while broker-dealers remain in business. Total aggregate excess of SIPC coverage available through NFS's excess of SIPC policy is $1 billion. Within NFS's excess of SIPC coverage, there is no per-customer dollar limit on coverage of securities, but there is a per-customer limit of $1.9 million on coverage of cash awaiting investment. This is the maximum excess of SIPC protection currently available in the brokerage industry.

For more details on SIPC or to request a SIPC brochure, visit www.sipc.org or call 202.371.8300.

Frequently Asked Questions

Q In the event Commonwealth fails, are my funds at risk?

No. As a fully introducing broker/dealer, Commonwealth does not have custody of client funds or securities.

Q In the event NFS fails, do general creditors share in the distribution of cash and securities of all client assets on hand?

No. Clients receive a preferential distribution of cash and securities equal in value to their pro rata share of all client assets on hand, in which general creditors do not share.

Q What is the limit of SIPC coverage?

SIPC coverage is limited to $500,000 per customer, including $250,000 for cash.

Q Is the $500,000 SIPC coverage for each account a customer has at NFS or for all the customer's accounts?

The limit is $500,000 per person, per account type. If an individual customer had two individual accounts in their name, for example, those accounts would be combined for SIPC purposes, and their total SIPC coverage would be $500,000. If a customer and spouse each had individual accounts, individual IRAs, 401(k) plan accounts, and a joint account, however, each account would be eligible for $500,000 of SIPC coverage.

Q Are margin accounts treated differently than other accounts?

No. You will receive your pro rata share of the net equity value of your account.

Q Are money market funds treated as securities or cash?

Money market funds are treated as securities and fall within the $500,000 securities maximum.

Q If I am not fully reimbursed from my pro rata share and my SIPC payment, is there any other source to make me whole?

Yes. To cover this exact possibility, NFS has arranged for additional protection beyond SIPC that covers both cash and covered securities.

Q Are there SIPC coverage exclusions?

Yes. SIPC does not cover commodity futures contracts, fixed annuity contracts, and currency, nor does it cover investment contracts, such as limited partnerships.

Q If NFS fails, how quickly will I get my investments back?

Historically, in cases where records are accurate and no fraud occurred, customers have generally received their property and payments one to three months after filing a completed claim form for brokerage firm liquidation.