Best execution of equity securities

A solid understanding of how we seek to obtain Best Execution when you place an order to buy or sell stock is essential to being an informed investor. What follows is an overview of the firm’s approach to Best Execution, the factors that can affect the timing of an execution and the role market volatility plays in handling your order. Finally, we describe additional information that is made available to you on a quarterly basis to help you evaluate the firm’s Best Execution practices.

Our approach to Best Execution

UBS Financial Services Inc. seeks to obtain the most favorable terms reasonably available when executing your buy or sell order. To do this, we:

- Carefully consider the elements of order execution
- Employ sophisticated technology for routing, monitoring and executing orders
- Regularly and rigorously examine overall execution quality

The elements of Best Execution

Five main factors that are considered when assessing the best market for a security:

1. The character of the market for the security;
2. The size and type of transaction;
3. The number of markets checked;
4. The accessibility of the quotation; and
5. The terms and conditions of the order as communicated to the firm.
I. The execution process
UBS Financial Services Inc. evaluates three principal criteria to determine the best way to execute an order for a client:

1. Execution speed. This is particularly important in volatile markets. The impact of volatile markets on order execution is discussed in Section II. The firm seeks to provide customer orders with the fastest execution reasonably possible under the existing market conditions.

2. Price and size improvement. In equity markets in the United States and many other countries, firm quotations for stocks are published on a regular and continuous basis. The quotations consist of the prices and quantities at which market participants are willing to buy (bid) and sell (offer) stocks. The National Best Bid or Offer (NBBO) is the highest published bid and the lowest published offer for the quoted size (generally under 1,000 shares). UBS Financial Services Inc. seeks price and size improvement for its customers’ orders by routing orders to execution venues that may execute trades at prices or sizes better than the NBBO.

3. Overall execution quality. When determining how and where to route or execute an order, the firm draws on extensive experience with various markets, market makers and electronic communications networks (ECNs), focusing on prompt, reliable execution. UBS Financial Services Inc. uses automated systems to route and execute most customer orders. When a customer order is received, it is usually automatically routed to an execution center that UBS Financial Services Inc. (including UBS Securities LLC, an affiliate of UBS Financial Services Inc.) believes will provide the best execution.

Certain larger orders that require special handling may be routed to a market center for execution by the telephone.

UBS Financial Services Inc. regularly monitors other potential execution venues and may
route orders in exchange-listed or over-the-counter (OTC) securities to these other venues if it believes that such routing is consistent with Best Execution principles.

II. Review of execution quality
UBS Financial Services Inc. regularly and rigorously evaluates the overall quality of the executions received on its customers’ orders. The firm studies the quality of executions for listed and OTC retail market orders through the use of an independent outside service. The firm bases its decisions for its order routing practices on this regular evaluation of execution quality.

Price volatility
One factor that can affect order execution is volatility. When investors place a high volume of orders with brokers, order imbalances and backlogs can occur, requiring more time to execute orders. This is because of delays caused by the number and size of orders processed, the speed at which current quotations or last-sale information can be updated and system capacity constraints applicable to NASDAQ and the exchanges, as well as UBS Financial Services Inc. and other firms to which UBS Financial Services Inc. routes orders. Keep in mind that even electronic orders may not be executed instantaneously upon receipt and, thus, are also affected by volatility. When volatility is extreme, brokers may need to discontinue their usual automatic execution procedures and execute orders on a manual basis, leading to further delay.

Effects of volatility on order execution
Investors should be aware of the following risks associated with volatile markets, especially at or near the open or close of the standard trading session:

– An order may be executed at a substantially different price from the quoted bid or offer, or the last reported sale price at the time of order entry, or an order may be only partially executed or may be executed in several transactions at different prices.
Opening prices may differ substantially from the previous day’s close.
– Locked (the bid equals the offer) and crossed (the bid is higher than the offer) markets may prevent the immediate execution of customer trades.
– Increased price volatility may result from imbalances between buy and sell orders during initial public offerings (IPOs).

Types of markets available
Markets for different securities can vary dramatically, especially those instances where there is limited quotation and pricing information or foreign jurisdictions, away from U.S markets. Under these circumstances, UBS Financial Services Inc. will strive to determine the most favorable venue when routing orders for executions.

Orders and handling
You may wish to consider using different types of orders to limit risk and manage investment strategies, particularly when trading in volatile markets. You should discuss with your Financial Advisor the costs and benefits of different types of orders.

Bear in mind, if you provide a specific instruction on where to route your order, it may prevent us from following our execution process, designed to obtain the best overall result for the execution of orders on a consistent basis.

General order types and conditions
Market order. This is the simplest type of order. Here, an investor tells a broker to execute a trade of a certain size as promptly as possible at the prevailing market price. Firms are required to execute market orders without regard to price changes. Therefore, if the market price moves significantly during the time it takes to fill an investor’s order, the order will most likely be exposed to the risks outlined above, including execution at a price substantially different from the price when the order was entered.
Limit order. With a limit order, the investor sets the maximum purchase price, or minimum sale price, at which the trade is to be executed. If the market moves away from this price, the order will not be executed unless or until the market price returns to the limit price. Thus, the investor may not receive an execution of the order. Stop order. This type of order has a unique identifier that instructs the market center to hold such orders for execution until such time the “stopped” price is touched, at which point the market center handles the order as a market order. The prevailing market at the time the order is executed may not be the same as the stop price. Thus, for example, in a declining market, a sell stop order may be executed at a lower price than the stop price.

Stop limit order. This type of order combines the features of a stop order with those of a limit order. A stop limit order can only be executed at a specific price (or better) after a given stop price has been triggered. When the stop price is reached by the market, the stop limit order becomes a limit order to buy or sell at the limit price or better.

UBS Financial Services Inc. activates all Listed, NASDAQ and OTC stop and stop limit orders, excluding option orders and those with a special handling of “Not Held,” using a “transaction” at the stop price as the triggering event, depending on the marketplace to which the order is presented (effective January 21, 2013).

Not Held or Working order. “Not Held” is a special condition that a customer may place on a large order to provide the executing firm with greater discretion in handling that order.

The firm must continue to adhere to principles of Best Execution, but will be given additional discretion in handling the order and not be held to its normal responsibilities with respect to the time of execution and the price or prices of execution of such an order. You should discuss with your Financial Advisor the potential costs and benefits of placing a not held order.
Order duration types

Day—A day order is an order that automatically expires if not executed at the end of a trading day.

Good-Til-Cancelled (GTC)—A Good-Til-Cancelled (GTC) order is an order that lasts until the order is completed or cancelled.

Effective June 2, 2014: UBS Financial Services Inc. will automatically cancel all open Equity GTC orders that are in effect for a 6-month duration (Good for 6 months). Upon the opening of the next business day, these orders will be cancelled with immediate notification being sent via confirmation to the investor. This does not include any orders placed for Equity Plan Advisory Services (EPAS) clients or as part of a 10b5-1 trading plan.

Conclusion

Before placing orders, the firm encourages you to give careful thought to how the risks described in this document may affect an investment in volatile markets. There are several Internet resources available to help explain these and other risks in greater detail, including the websites of the Securities and Exchange Commission (www.sec.gov) and the Financial Industry Regulatory Authority (www.finra.org). You should also consider how different types of orders might help manage some of these risks. We encourage you to discuss these matters with your Financial Advisor.