FINANCIAL INDUSTRY REGULATORY AUTHORITY
LETTER OF ACCEPTANCE, WAIVER AND CONSENT
NO. 20140428736

TO: Department of Enforcement
Financial Industry Regulatory Authority ("FINRA")

RE: Charles Schwab & Co., Inc., Respondent
Broker-Dealer
CRD No. 5393

Pursuant to FINRA Rule 9216 of FINRA's Code of Procedure, Charles Schwab & Co., Inc. ("Schwab" or the "Firm") submits this Letter of Acceptance, Waiver and Consent ("AWC") for the purpose of proposing a settlement of the alleged rule violations described below. This AWC is submitted on the condition that, if accepted, FINRA will not bring any future actions against the Firm alleging violations based on the same factual findings described herein.

I.

ACCEPTANCE AND CONSENT

A. The Firm hereby accepts and consents, without admitting or denying the findings, and solely for the purposes of this proceeding and any other proceeding brought by or on behalf of FINRA, or to which FINRA is a party, prior to a hearing and without an adjudication of any issue of law or fact, to the entry of the following findings by FINRA:

BACKGROUND

Schwab is a nationwide broker-dealer that has been registered with FINRA or one of its predecessors since 1970. The Firm is headquartered in San Francisco, California and has more than 7,400 registered persons in approximately 350 branch offices nationwide.

RELEVANT DISCIPLINARY HISTORY

During the past five years, the Firm has entered into a settlement with FINRA and the SEC to resolve allegations that the Firm lacked adequate policies and procedures with respect to certain areas of its business:

In early 2011, the Firm agreed to civil penalties and disgorgement in connection with allegations by the Securities and Exchange Commission ("SEC") and FINRA that Schwab and one of its affiliates made misleading statements regarding an ultra-short bond fund and failed to establish, maintain and enforce an

adequate supervisory system with respect to same. The Firm agreed to a civil penalty in the amount of $5 million with the SEC and a fine of $500,000 with FINRA in addition to disgorgement in the amount of $17.5 million. The SEC Order further required Schwab to retain an independent consultant to review and make recommendations about the Firm's policies and procedures to prevent the misuse of material, nonpublic information.

The Firm also has a disciplinary history in connection with the violation of Rule 15c3-3 of the Securities Exchange Act of 1934 ("SEA"):

In August 2000, the Firm consented to a $300,000 penalty by the New York Stock Exchange concerning its findings that from January 14 through January 29, 1999, Schwab failed to maintain customer reserves at required levels by amounts ranging from $45 million to $345 million in violation of SEA Rule 15c3-3.

OVERVIEW

On three dates between May 15 and July 1, 2014, Schwab did not maintain sufficient net capital to meet its obligations under the federal securities laws, which require broker-dealers to maintain certain levels of capital at all times to ensure the Firm can meet its obligations. On May 15, 2014, June 2, 2014, and July 1, 2014, Schwab made $1 billion transfers to its parent corporation, The Charles Schwab Corporation ("CSC"), for overnight investment with third-party investment counterparties, pursuant to a revolving loan agreement. As a result of the unsecured transfers, on those three dates, the Firm was net capital deficient by $612 million, $775 million and $287 million, respectively, in violation of SEA Rule 15c3-1(a). The Firm identified and self-reported the violation upon discovery to FINRA in July 2014.

These violations arose because the Firm failed to establish, maintain, and enforce an adequate supervisory system, including written procedures, reasonably designed to prevent Schwab's Treasury group from entering into intercompany transfers with Firm affiliates that could result in an unsecured receivable to the Firm under SEA Rule 15c3-1(c) and adversely impact the Firm's net capital position, in violation of NASD Rule 3010(a).

In addition to the above, the Firm failed to maintain an adequate process to ensure proprietary accounts of broker-dealers ("PAB") were categorized and coded in accordance with the 2014 amendments to SEA Rule 15c3-3(e). As a result of this coding issue, Schwab failed to maintain the appropriate level of reserves in its PAB Reserve account in violation of SEA Rule 15c3-3(e), and had a hindsight deficiency of at least $800,000.

FACTS AND VIOLATIVE CONDUCT

The requirements of the net capital rule, SEA Rule 15c3-1(a), serve the important purpose of ensuring that every broker-dealer maintains sufficient liquidity to meet its obligations to customers, counterparties, and creditors at all times. The customer protection rule, SEA Rule 15c3-3(e), provides an additional layer of security for customers by mandating that customer assets be safeguarded with reserves at appropriate levels. This matter involves the Firm's violation of SEA Rule 15c3-1 with respect to its net capital deficiencies on three dates in 2014, and its violation of SEA Rule 15c3-3(e) in connection with the Firm's shortfall in its PAB Reserves.

1. Background

Schwab is a registered broker-dealer that as of December 31, 2014, held $2.46 trillion in client assets in 9.4 million active brokerage accounts. As part of the routine business of the broker dealer, customer activity such as settlements, deposits and wires received throughout the day result in increases in cash balances at the Firm. The Firm is permitted to invest overnight the cash it receives, provided that the Firm acts in accordance with SEA Rules 15c3-1 and 15c3-3. In 2014, Schwab had relationships with several investment counterparties for overnight investing purposes. In an effort to manage the risk of counterparty default, Schwab maintained internal investment limits with each institution. Generally, the Firm invested $1 billion or less in cash overnight, but on the three dates noted above, Schwab had in excess of $2 billion to invest.

The Firm's Treasury group oversees daily cash flows and provides forecasts of the Firm's daily cash position to other groups within the Firm. Based on these forecasts, the Capital Markets group determines whether cash should be invested overnight and if so, handles the overnight investments with the Firm's investment counterparties. Schwab's net capital calculation and regulatory reporting is handled by the Regulatory Reporting group, which is a separate group at the Firm.

In December 2006, the Firm and CSC entered into an Intercompany Revolving Promissory Note (the "Loan Agreement"), which allowed CSC to borrow up to $1 billion from Schwab for no more than 180 days. The Loan Agreement was effective through July 2014.

2. The Firm Failed to Maintain Net Capital at Required Levels on May 15, 2014, June 2, 2014 and July 1, 2014 in Violation of SEA Rule 15c3-1(a)

SEA Rule 15c3-1(a) requires that every broker-dealer have and maintain net capital at required levels at all times. The transfers made from Schwab to CSC in the form of unsecured loans on May 15, 2014, June 2, 2014, and July 1, 2014 resulted in net capital deficiencies on each of those dates and therefore the Firm

violated SEA Rule 15c3-1(a).

On May 15, 2014, the Firm held $2.4 billion in cash as a result of customer funds received late in the day. Schwab was unable to invest all of these funds with its approved investment counterparties. As a result, the Capital Markets group consulted with the Treasury group to determine whether $1 billion could be transferred to CSC for overnight investment. The Treasury group approved the transfer as an unsecured loan under the Loan Agreement, and Schwab transferred $1 billion to CSC. In approving the loan, the Treasury group did not communicate with anyone in the Regulatory Reporting group to consider whether an unsecured loan of $1 billion to CSC would impact the Firm's net capital position. CSC invested the cash overnight with its approved counterparties and the following morning transferred the cash back to Schwab in repayment of the loan. The loan reduced the Firm's tentative net capital, which resulted in undue concentration charges under Rule 15c3-1, and caused the Firm to be net capital deficient in the amount of $612 million.

On June 2, 2014, similar circumstances led to another $1 billion unsecured loan made from Schwab to CSC. Customer funds received late in the day resulted in $2.5 billion of cash at Schwab. Schwab again was unable to invest all of these funds with its approved investment counterparties, and the Treasury group approved a $1 billion transfer as an unsecured loan under the Loan Agreement from Schwab to CSC overnight. The Treasury group did not communicate with the Regulatory Reporting group to consider whether this loan would impact the Firm's net capital position. CSC invested the cash overnight and the following morning transferred the cash back to Schwab in repayment of the loan. The June loan reduced the Firm's tentative net capital, which resulted in undue concentration charges under Rule 15c3-1, and caused the Firm to be net capital deficient by $775 million.

On July 1, 2014, the Firm held $2.8 billion of cash as a result of customer funds received late in the day, and it was unable to invest all of these funds with the Firm's approved investment counterparties. The Treasury group approved another transfer as an unsecured loan under the Loan Agreement in the amount of $1 billion from Schwab to CSC. The Treasury group did not consult with anyone in the Regulatory Reporting group to consider whether this loan would impact the Firm's net capital position. Similar to the May and June loans, CSC repaid the loan the following morning. The July loan also reduced the Firm's tentative net capital, which resulted in undue concentration charges under Rule 15c3-1, and caused the Firm to be net capital deficient by $287 million.

On July 2, 2014, the Treasury group raised the question of whether the above loans may have impacted the Firm's net capital position and contacted the Regulatory Reporting group. The Firm investigated the matter and self-reported the above net capital deficiencies to the Securities and Exchange Commission the same day.

3. The Firm Lacked Controls Reasonably Designed to Safeguard Its Moment to Moment Net Capital Obligations in Violation of NASD Rule 3010(a)

NASD Rule 3010(a) requires that the Firm establish and maintain a supervisory system, including written supervisory procedures, reasonably designed to achieve compliance with applicable securities laws and regulations. Because there was no supervisory system or written supervisory procedures in place from May 2012 through July 2014 to determine whether intercompany transfers to Firm affiliates made by the Treasury group could create an unsecured receivable under SEA Rule 15c3-1(c) and impact the Firm's net capital position, the Firm violated NASD Rule 3010(a) during that period.

During the above period, the Firm's Regulatory Reporting group was responsible for handling Schwab's net capital calculation. The Treasury group was responsible for managing the daily cash flows at the Firm and handling corporate wire transfers. As set forth in Section 2 above, on three occasions in 2014, the Treasury group made three unsecured loans to CSC under the Loan Agreement without consulting with the Regulatory Reporting group to consider whether the loans would impact the Firm's net capital position. As a result of additional haircuts and undue concentration charges, the Firm was net capital deficient on those three dates. In 2012, the Firm made two similar unsecured loans to CSC in the amounts of $18 million and $415 million. Although neither of these transfers caused the Firm to be net capital deficient, similar to the loans made in 2014, the Treasury group did not communicate with the Regulatory Reporting group to consider whether the loans would impact the Firm's net capital position.

There was no supervisory system or written supervisory procedures in place from May 2012 through July 2014 requiring the Treasury group to evaluate whether unsecured loans made from the Firm to CSC under the Loan Agreement, or other intercompany transfers with Firm affiliates, would create an unsecured receivable under SEA Rule 15c3-1(c) and impact the Firm's net capital position. There also was no system or practice in place requiring the Treasury group to communicate regarding such matters with the Regulatory Reporting group, which had the expertise in handling the Firm's net capital and reserves calculations, and the knowledge of the Firm's net capital position and how cash transfers would impact the Firm. Indeed, during the above period, the Firm had no controls in place to ensure that intercompany transfers to Firm affiliates made by the Treasury group would not create an unsecured receivable to the Firm and result in a net capital deficiency. Accordingly, the Firm lacked a supervisory system reasonably designed to achieve compliance with SEA Rule 15c3-1(a).

4. The Firm's Miscoding of Proprietary Accounts of Broker Dealers Resulted in a Deficiency in Required Reserves in Violation of SEA Rule 15c3-3(e)

SEA Rule 15c3-3(e), as amended in 2014, requires broker dealers to maintain a Special Reserve Bank Account for the proprietary accounts of broker dealers, known as a PAB Reserve Bank Account, which must be maintained at a certain level based on a statutory formula. The Firm violated SEA Rule 15c3-3(e) in 2014 by failing to properly identify and reserve for its PAB accounts.

During the Firm's 2014 cycle exam by FINRA's Office of Risk Oversight and Operational Regulation ("ROOR"), ROOR staff determined that the Firm had failed to maintain an adequate process to ensure that the Firm's PAB accounts were properly coded and sufficiently reserved. Specifically, in contravention of the 2014 amendment to SEA Rule 15c3-3(e), the Firm continued to classify certain broker dealer and mutual fund accounts as customer accounts instead of PAB accounts. Because these accounts were not properly coded as PAB accounts, the PAB Reserve account was underfunded by at least $800,000. The Firm conducted an independent review of its accounts to identify and resolve the coding errors, and at the outset of the process, deposited $20 million into its PAB Reserve account to cover any additional improperly coded PAB accounts.

OTHER FACTORS

With respect to the SEA Rule 15c3-1(a) and NASD Rule 3010 violations, the Firm identified and self-reported the unsecured loans and the resulting net capital deficiencies. The Firm also hired an independent external consultant to review the circumstances surrounding the violations and to make recommendations. After detecting the issue, the Firm promptly adopted remedial measures, which included terminating the Loan Agreement, establishing relationships with additional overnight investment counterparties, increasing limits with existing investment counterparties, and instituting a process requiring the Treasury group to assess whether cash transfers would impact the Firm's net capital position.

In connection with SEA Rule 15c3-3, the Firm performed an internal review of its PAB accounts to ensure such accounts were properly coded and adjusted its PAB Reserve account to resolve the deficiency.

The sanction reflects the Staff's consideration of the above actions taken by the Firm.

B. The Firm also consents to the imposition of the following sanctions:

- A censure; and
- A fine of $2 million

The Firm agrees to pay the monetary sanction upon notice that this AWC has been accepted and that such payment is due and payable. The Firm has submitted an Election of Payment form showing the method by which the Firm proposes to pay the fine imposed.

The Firm specifically and voluntarily waives any right to claim that it is unable to pay, now or at any time hereafter, the monetary sanction imposed in this matter.

The sanctions imposed herein shall be effective on a date set by FINRA staff.

II.

WAIVER OF PROCEDURAL RIGHTS

The Firm specifically and voluntarily waives the following rights granted under FINRA's Code of Procedure:

A. To have a Complaint issued specifying the allegations against the Firm;

B. To be notified of the Complaint and have the opportunity to answer the allegations in writing;

C. To defend against the allegations in a disciplinary hearing before a hearing panel, to have a written record of the hearing made and to have a written decision issued; and

D. To appeal any such decision to the National Adjudicatory Council ("NAC") and then to the U.S. Securities and Exchange Commission and a U.S. Court of Appeals.

Further, the Firm specifically and voluntarily waives any right to claim bias or prejudgment of the Chief Legal Officer, the NAC, or any member of the NAC, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including acceptance or rejection of this AWC.

The Firm further specifically and voluntarily waives any right to claim that a person violated the ex parte prohibitions of FINRA Rule 9143 or the separation of functions prohibitions of FINRA Rule 9144, in connection with such person's or body's participation in discussions regarding the terms and conditions of this AWC, or other consideration of this AWC, including its acceptance or rejection.

III.

OTHER MATTERS

The Firm understands that:

A. Submission of this AWC is voluntary and will not resolve this matter unless and until it has been reviewed and accepted by the NAC, a Review Subcommittee of the NAC, or the Office of Disciplinary Affairs ("ODA"), pursuant to FINRA Rule 9216;

B. If this AWC is not accepted, its submission will not be used as evidence to prove any of the allegations against the Firm; and

C. If accepted:

1. this AWC will become part of the Firm's permanent disciplinary record and may be considered in any future actions brought by FINRA or any other regulator against the Firm;

2. this AWC will be made available through FINRA's public disclosure program in accordance with FINRA Rule 8313;

3. FINRA may make a public announcement concerning this agreement and the subject matter thereof in accordance with FINRA Rule 8313; and

4. The Firm may not take any action or make or permit to be made any public statement, including in regulatory filings or otherwise, denying, directly or indirectly, any finding in this AWC or create the impression that the AWC is without factual basis. The Firm may not take any position in any proceeding brought by or on behalf of FINRA, or to which FINRA is a party, that is inconsistent with any part of this AWC. Nothing in this provision affects the Firm's: (i) testimonial obligations; or (ii) right to take legal or factual positions in litigation or other legal proceedings in which FINRA is not a party.

D. The Firm may attach a Corrective Action Statement to this AWC that is a statement of demonstrable corrective steps taken to prevent future misconduct. The Firm understands that it may not deny the charges or make any statement that is inconsistent with the AWC in this Statement. This Statement does not constitute factual or legal findings by FINRA, nor does it reflect the views of FINRA or its staff.

The undersigned, on behalf of the Firm, certifies that a person duly authorized to act on its behalf has read and understands all of the provisions of this AWC and has been given a full opportunity to ask questions about it; that the Firm has agreed to its provisions voluntarily; and that no offer, threat, inducement, or promise of any kind, other than the terms set forth herein and the prospect of avoiding the issuance of a Complaint, has been made to induce the Firm to submit it.

Date: 8.4., 2015

Charles Schwab & Co., Inc.

By: _____

Name: Marie Tellini

Title: SVP & Deputy General Counsel

Reviewed by:

_____

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Counsel for Charles Schwab & Co., Inc.

Accepted by FINRA:

8/24/15

Date

Signed on behalf of the
Director of ODA, by delegated authority

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