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## **Schwab Managed Account Services™ for Clients of Investment Advisors**

**SEC File No. 801-29938   Disclosure Brochure**

This wrap fee program brochure provides clients of Investment Advisors with information about Charles Schwab & Co., Inc., the Managed Account Select® program and the Managed Account Access® program that should be considered before becoming a client of either of those programs. If you have any questions about the contents of this brochure, please contact us at 1-800-515-2157. This information has not been approved or verified by any governmental authority.

Additional information about Schwab is also available on the SEC's website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov).

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## Services, Fees and Compensation

This brochure describes the following managed account programs provided by Charles Schwab & Co., Inc. ("Schwab") for you as a client of your independent investment advisor, bank or trust company ("IA"): the Managed Account Select® program ("Select") and the Managed Account Access® ("Access") program (Select and Access are each referred to as a "program"). The programs allow you to select one or more Separate Account Managers ("MMs") with the assistance of your IA. In each program, an MM manages your investment portfolio on a discretionary basis pursuant to a stated investment strategy. The Select program consists of MMs that are unaffiliated with Schwab. These MMs are evaluated and monitored by Charles Schwab Investment Advisory, Inc. ("CSIA"), an affiliate of Schwab whose personnel were formerly in the division of Schwab known as the Schwab Center for Financial Research ("SCFR"), a division of Schwab, which began performing these functions for Select in 2008.

The Access program includes MMs that are unaffiliated with Schwab as well as two MMs that are affiliated with Schwab. The MM investment strategies in Access are not evaluated by Schwab, and there are no eligibility criteria.

**Fees.** Clients pay a single asset-based fee to participate in a program. The fee covers services provided by Schwab, including custody, execution of transactions in equity securities by Schwab and program administration, and the discretionary asset management services provided by the MMs. The fee does not cover trades executed by broker-dealers other than Schwab. In addition to the program fee, Schwab may receive separate compensation for some transactions and services as described below. The program fee is separate from the fee charged by your IA. Clients of the programs may include individuals, trusts, charitable organizations, pension and profit sharing plans, investment clubs, corporations and other business organizations.

The programs are sponsored by Schwab. In the Select program, CSIA assists with MM and strategy selection, monitors the MMs' performance periodically and provides MM research for use by your IA and you. In the Access program, any MM (including any MM affiliated with Schwab) is eligible to participate, and Schwab does not provide any MM evaluation or performance monitoring. Schwab provides custody, execution, reporting, program administration and related services for accounts under both programs; in rendering execution services, Schwab generally will route orders for equity securities to UBS Capital Markets, L.P. or UBS Securities LLC. Schwab is a full-service financial services company, offering securities and brokerage services, investment guidance and a full range of investment and financial products.

**Your IA's Role.** Your IA assists you in determining your investment objectives and asset allocation, and which MMs and strategies to select for your accounts in the programs. Your IA is also responsible for ongoing monitoring and review of each MM's performance, your asset allocation and your investment objectives. In both programs, your IA is responsible for reviewing the MM's investment strategy, performance, disciplinary record and other due diligence information.

### MM Asset Management Services

Your selection of an MM to manage your account is subject to the acceptance by the MM. An MM may decline to manage your account based on your investment objectives, financial situation, requested investment restrictions or other matters. If the MM accepts management of your account, the MM will provide discretionary investment advisory services and will be responsible for all investment decisions in your account. You authorize the MM you select to manage your assets on a discretionary basis by purchasing and/or selling individual stocks, bonds, money market instruments, money market funds, or other instruments as and when the MM sees fit without your approval of each transaction. In managing your account, the MM will employ the investment strategy you have chosen for your account. Each MM (and its investment strategies) is described in the MM's brochure, its MM Profile

(in the case of Select MMs—see "Information About MMs," below) and any other material the MM may give to you. The MM's discretionary authority will remain in full force and effect, even if you become incompetent or disabled, unless revoked or terminated by you in a written notice to Schwab. In your client account application, you agree not to effect trades in your account while an MM is managing the account, and you may be blocked from placing any trades in your account. MMs are not authorized to withdraw or transfer any money, securities, or property either in your name or otherwise, except as necessary to pay for or execute transactions in your account.

In filling out your client account application, you will provide information about yourself and your investment objectives. You will have the opportunity to impose reasonable restrictions on the management of your account. You may request that specified securities or categories of securities not be purchased for your account, but your MM may decline your requested restriction if your MM deems it unreasonable. You will not be able to impose restrictions on the management of a Fund. The MM managing your account is responsible for implementing and monitoring any restrictions you place on the management of your account. Schwab will forward to any MM you designate a copy of your client account application, as well as any restrictions you want to impose on your account. Accounts with investment restrictions may perform differently than accounts without restrictions; performance may be lower or higher for accounts with restrictions than those without restrictions. Since the MM's performance composite typically does not include accounts with restrictions, if your account has restrictions the performance of your account may be different than the MM's performance composite.

Working with your IA, you may have the opportunity to instruct the MM to realize gains or losses in your account for tax reasons. This may include the sale of positions with unrealized losses/gains above a certain amount or the sale of specified securities. The MM will use reasonable efforts to implement your request to harvest tax losses or gains.

Schwab will effect transactions in your account only as instructed by you, any MM appointed by you, or your IA (if you have granted your IA trading authority, your IA has agreed with Schwab not to effect trades in a managed account while an MM has discretionary authority over the account). In any and all transactions effected by or through Schwab in your account, Schwab is acting exclusively as a broker-dealer, and not as an investment advisor. Any MM you select is responsible for managing your account under the relevant program in a manner consistent with that MM's stated investment strategy, subject to any reasonable restrictions imposed by you. Schwab is not responsible for the MM's performance or adherence to its investment style, your investment objectives or your restrictions.

You may contact an MM directly, although it is generally expected that you will direct to your IA questions concerning your account. You may change MMs or investment strategies at any time by written notice to Schwab. An MM also may terminate a relationship with you at any time upon 30 days' notice to you, your IA and Schwab.

### IA Services and Responsibilities

Your IA assists you in determining whether a particular program is appropriate for you. Your IA will also assist you in determining your investment objectives and asset allocation, and which MMs and strategies to select for your accounts in the programs. Your IA is also responsible for ongoing monitoring and review of each MM's performance, your asset allocation and your investment objectives. In both programs, your IA is responsible for reviewing the MM's investment strategy, performance, disciplinary record and other due diligence information.

In the Select program, Schwab makes available to your IA CSIA research in the form of MM profiles and quarterly reviews to assist your IA in the due diligence process. In the Access program, neither Schwab nor CSIA evaluate the MMs or generate research regarding the MMs for use by

you or your IA. Currently, Schwab does make MM information available to your IA through a research and proposal generation system known as the Investment Proposal Center, described below under “Information About MMs.”

By recommending any program to you, your IA is responsible for determining that the particular program is appropriate for you. Schwab will not determine whether any program is appropriate for you. Your IA also is responsible for advising you on the selection of MMs to manage your accounts in the programs.

Although Schwab determines the MMs participating in the programs, the decision to select an MM is solely yours, with the advice of your IA. Schwab will not recommend MMs to you and is not responsible for your decision to participate in either program or for your choice of MM.

### **Change in Client Circumstances**

If material changes occur to your financial circumstances or investment objectives or you wish to impose or modify restrictions on the management of your account, it is your responsibility to promptly inform your IA. Your IA will respond to your questions and periodically discuss with you whether the management of your account continues to reflect your investment objectives and financial requirements. Your IA will communicate such information as necessary to the MM managing your account.

### **Schwab's Execution Services**

The program fee covers execution of equity orders by Schwab, as well as execution of fixed income orders by Schwab on an agency basis, but the program fee does not include execution of orders by Schwab as principal in fixed income securities (Schwab does not execute orders as principal for affiliated MMs in the Access program). “Principal trades” are trades in which a firm like Schwab sells securities from its own account to a client account or purchases securities for its own account from a client account. When Schwab or another firm acts as principal for its own account, it accepts the risk of market price and liquidity fluctuations when executing customer orders, and attempts to profit from the bid-ask spread for equity transactions and from dealer markups and markdowns for bond transactions.

#### **Execution of Transactions in Equity Securities**

Because the program fee covers execution of orders in equity securities only when executed through Schwab, MMs place most of their orders for the purchase or sale of equity securities, including exchange-traded funds (“ETFs”), with Schwab; for Access equity accounts managed by CSIM, you will agree in your account application that CSIM will only use Schwab to execute all brokerage transactions (which means you may not receive as high a quality of execution if CSIM used broker-dealers other than Schwab). Schwab generally will route orders for equity securities to UBS Capital Markets, L.P. or UBS Securities LLC (together, referred to as “UBS”), which are not affiliated with Schwab. Pursuant to an agreement between Schwab's parent company, The Charles Schwab Corporation (“CSCorp”) and UBS, UBS manages the execution of most types of equity, ETF and options trade orders for which customers have not provided specific instructions and order routing services for most types of directed orders.

Exchanges and broker-dealers frequently offer rebates for customer orders routed to them for execution. Although Schwab does not receive rebates or other payments from UBS, part of the consideration CSCorp received for the sale of its capital markets business to UBS in 2004 related to the services agreements with UBS and Schwab's commitments to route most types of equity, ETF and listed options orders through UBS.

UBS routing and execution services are subject to Schwab's execution quality standards for achieving best execution. In certain circumstances, Schwab itself may route orders directly to a market for execution. Schwab considers a number of factors in evaluating execution quality, including execution price and opportunities for price improvement, market depth and order size, the trading characteristics of the security,

speed and accuracy of executions, the availability of efficient and reliable order handling systems, and service levels and the cost of executing orders at a particular market or firm. Price improvement occurs when an order is executed at a price more favorable than the displayed national best bid or offer, and may be available for stocks and ETFs traded on the exchanges and in dealer markets, and for listed options. Schwab regularly monitors the execution quality provided by UBS and the various markets to which UBS and Schwab may route orders to help ensure orders are routed to markets that have provided high-quality executions over time.

#### **Execution of Transactions in Fixed Income Securities**

Fixed income securities generally trade in dealer markets, but some corporate bonds also trade on national securities exchanges. If a fixed income security is traded in the dealer markets, Schwab will generally execute an order as principal unless the MM directs Schwab to execute the order as agent. (Schwab will not execute principal transactions in fixed income securities for affiliated MMs in the Access program.) The principal transactions include a dealer markup or markdown by Schwab (not included in the program fee). If an MM places an order for fixed income securities with Schwab, Schwab will seek the best price reasonably available at that time by searching our Schwab BondSource® (“SBS”) electronic inventory and trading system. Schwab uses SBS except on rare occasions (e.g., for very large orders) in an effort to achieve a better price for clients. SBS accesses an extensive inventory of fixed income securities from Schwab, and a network of hundreds of other broker-dealers whose fixed income inventories are included in SBS.

As MMs seek best execution based on net price and other factors, they have the ability to place orders for fixed income securities with dealers other than Schwab. Most MMs managing fixed income and bond ladder investment strategies have advised Schwab that they anticipate placing most of their fixed income orders with dealers other than Schwab, which may include a markup or markdown by those dealers (not included in the program fee).

When an MM buys a new bond issue for your account through Schwab acting as principal, Schwab receives a syndicate fee (also known as a dealer concession) which ranges from less than 0.01% to 2.0% of the par value, or face amount, of the bond, depending on the particular bond issue. The dealer concession is a standard custom and practice regarding payment to syndicate members for distributing, and for providing certain operational services associated with, new issues. Schwab as a dealer receives the same amount for any given new issue as other dealers participating in the same tier of the syndicate, and every new issue buyer (the customer) pays the same price no matter from which dealer a purchase is made.

#### **Execution of Transactions in Mutual Funds**

Schwab will execute all trades in mutual funds in your account. Mutual funds in a program strategy are limited to those fund families with which Schwab has an agreement pursuant to which Schwab renders administrative and shareholder services, including the funds in the Schwab Mutual Fund Marketplace®. Eligible mutual funds in the programs offer their shares to clients in the programs on a no-load or load-waived basis and may charge Rule 12b-1 (distribution) and/or shareholder servicing fees. Mutual fund shares are purchased at their current net asset value, which means the net asset value next computed after a fund receives an order. Although you will not pay any sales loads or transaction fees on the mutual fund shares purchased for your account, certain funds impose redemption fees if shares are not held for a minimum time period. If you fund your account with mutual fund shares, any mutual funds that are not consistent with the then-current selection of funds in your chosen strategy will be sold and any applicable redemption fees will be deducted from the proceeds, as stated in the prospectus for each fund. All investments in mutual funds are subject to the terms of the relevant fund's prospectus, including associated fees. You will receive prospectuses when the funds are initially purchased for your account.

### Trades Through Other Broker-Dealers

The program fee does not cover commissions for trades that an MM places with a broker-dealer other than Schwab, or markups or mark-downs charged by those other broker-dealers on principal trades. (The program fee does cover commissions for equity trades routed by Schwab to UBS.) MMs will have an incentive to execute most transactions in equity securities through Schwab. This incentive could, in some circumstances, conflict with an MM's duty to obtain best execution of transactions in your account. However, an MM (other than CSIM) may execute equity trades through other broker-dealers when required by applicable law or when an MM reasonably believes that another broker-dealer will provide better execution, net of any additional resulting transaction charges, than would be the case if the transaction were executed through Schwab. With regard to fixed income and bond ladder strategies, most MMs will generally place transactions with other dealers acting as principal. Such dealers will receive a markup or markdown that is not included in the program fee. Because such transactions would be subject to markups and markdowns outside of the program fee if placed through Schwab or another dealer, this conflict does not arise in connection with trades by these MMs.

In addition to cost considerations, an MM may consider various other factors in its best execution analysis as described in the MM brochure, including the liquidity of the security and the need for timely execution. Other broker-dealers may provide an MM with brokerage and research services, as disclosed in the MM brochure. To be eligible to receive a trade from an MM for your account, the other broker-dealer must have an agreement with Schwab under which Schwab will clear and settle transactions executed by that broker-dealer, or the MM must have agreed to use an electronic system to issue settlement instructions to Schwab for trades executed by other broker-dealers. This is described in more detail under the heading "Prime Brokerage, Step-In and Trade-Away Services" in your Schwab account application agreement.

### Aggregation of Transactions

Your MM may aggregate or bunch transactions for your account with transactions for other clients for execution purposes under appropriate circumstances. For these purposes, other clients may include other clients of the same MM under another Schwab bundled fee program. In addition, if an MM executes trades with another broker-dealer (as described above), other clients may include additional clients of the MM not participating in any Schwab program or service. This practice will not ordinarily affect or otherwise reduce the costs charged to your account for those transactions. The transactions (as well as any expenses incurred in transactions effected through other broker-dealers) will be allocated according to the MM's policies governing aggregation and allocation of transactions. These policies may require your MM to assign to your account the average price resulting from the aggregated trades. Partial fills of a block security transaction may be allocated by your MM among clients' accounts randomly, pro rata based on the size of the account, or under some other policy adopted by your MM. Your MM's trade allocation policies may result in certain clients paying higher or lower prices for securities than may otherwise have been obtained if the transactions had been executed separately. Additional information about an MM's policies for aggregation and allocation may be contained in the MM's Form ADV brochure ("MM brochure").

Transactions may be executed for your account through Schwab at different times, in different markets and at less advantageous prices than applicable to trades for other clients of your MM with the same investment strategy. An MM may have policies and procedures that determine when it will send trades in the Select or Access programs to Schwab in relation to sponsors of other separately managed account programs or other broker-dealers selected by the MM. The MM may include disclosure about its policies and procedures in the MM brochure.

Some MMs, such as the overlay manager for a Diversified Portfolio, may manage accounts based on recommendations or a model portfolio received from another money manager (the "model provider"). In such

cases, trades for your account may be placed by an MM at different times, and may be executed in different markets and at less advantageous prices, than applicable to accounts with the same investment strategy managed directly by the model provider. These differences may result from the application of the model provider's policies and procedures in addition to the MM's trading policies and procedures.

### Custody

Schwab acts as sole custodian for all assets in client accounts and performs all custodial functions customarily performed for securities brokerage accounts, including but not limited to crediting of interest and dividends on account assets. You will retain ownership of all cash, securities, and other instruments in your account. The program fee compensates Schwab for these services. If you have accounts and assets at Schwab that are not in the programs, any fees you are charged for the maintenance of such accounts, for custody of assets and for other account-related services will be separate from and in addition to your program fee.

### Reporting

Schwab will send you a monthly account statement detailing positions and activity in your account during the preceding month. The statement will include a summary of all transactions made on your behalf, all contributions and withdrawals made to or from your account, all fees and expenses charged to your account, and the value of your account at the beginning and end of the period. The statement may be based upon information obtained from third parties. Schwab believes that the data obtained from these third parties is accurate, but has no independent means of verifying and cannot guarantee such accuracy. You also will receive a separate confirmation of each transaction, unless you elect to receive a quarterly report containing confirmation information for trades occurring during that calendar quarter. By signing the Schwab account application, you authorize Schwab to provide trading and other information about your account to the MM managing your account, your IA and third parties designated by them. Schwab is not responsible for reviewing transactions in or the value of your account.

Schwab will make available to your IA information about your account, including positions and activity. In general, the information is intended to facilitate your IA's monitoring of your account, including the MM's performance. Performance information will be provided by a third party. Schwab believes that the data obtained from the third party is accurate, but does not independently verify, and is not responsible for, its accuracy. Your IA also may receive additional reports.

### Program Fee

Schwab charges an asset-based fee for the services provided under the programs by Schwab and the MMs. The maximum fee charged for the programs is set forth in the table below. The fees may be negotiable based on a number of factors that may result in a particular client paying a fee greater or less than the standard fees. The exact fee you will pay is specified in your Schwab account application. Schwab may change the actual fee charged to you by notice to you in accordance with your account application and your Schwab account agreement.

Dollar Value of Assets in Program Accounts	Equity Strategies (Excluding Index-Based) Annual Fee Schedule	Fixed Income (Non-Ladder) and Index-Based Strategies Annual Fee Schedule
First \$250,000	1.00%	0.65%
Next \$250,000	0.85%	0.65%
Next \$500,000	0.80%	0.60%
Next \$1,000,000	0.75%	0.55%
Next \$3,000,000	0.70%	0.50%
Over \$5,000,000	0.65%	0.45%

Dollar Value of Assets in Program Accounts	ETF Strategies Annual Fee Schedule	Bond Ladder Strategies Annual Fee Schedule
First \$500,000	0.75%	0.35%
Next \$500,000	0.65%	0.35%
Next \$4,000,000	0.50%	0.30%
Over \$5,000,000	0.50%	0.25%

Your account is assigned to a fee schedule based upon the type of investment strategy you have chosen for your account. Index-based equity strategies and preferred stock strategies are subject to the fixed income (non-ladder) fee schedule, and Diversified Portfolios and balanced strategies are subject to the equity fee schedule. The program fee is expressed as an annual rate. To calculate your program fee, Schwab multiplies the actual daily balance of your account by the daily pro rata portion of the annual rate and then adds together the fees for each day of the month. The program fee is billed to your account monthly, which may result in your paying a higher fee on an annual basis than the annual rate due to the effects of compounding. The program fee is blended—i.e., as the market value of your program account reaches a higher breakpoint, as set forth above, the assets within each breakpoint are charged a lower rate.

Effective April 1, 2011, Schwab will no longer charge a minimum fee on accounts in the programs.

If you have more than one account in either or both programs, your accounts may be “household” for purposes of calculating the fee. A “household” is generally a group of accounts having the same address of record or same Social Security number. Individual retirement accounts (“IRAs”), Simplified Employee Pension IRAs (“SEP-IRAs”), SIMPLE IRAs and other personal retirement accounts generally may be combined for householding purposes; however, other retirement plan accounts subject to ERISA and charitable remainder trusts may not be included. The accounts which may be householded are subject to negotiation (except for ERISA accounts) and Schwab’s approval. Schwab calculates your household fee by totaling the market value of your accounts under each strategy asset class (i.e., equity, fixed income [non-ladder], ETF or bond ladder) and charging your accounts according to the applicable fee schedule. The fee for each householded account within the following four categories is allocated on a pro rata basis to each account: regular equity, index-based equity, fixed income (non-ladder) and bond ladder. Each account’s pro rata amount is calculated by computing the market value of each account as a percentage of the total market value of all accounts in that category. If regular equity and index-based equity accounts are householded together, the market values of these assets are combined for purposes of determining applicable fee breakpoints, and Schwab charges the combined accounts in the following order according to the applicable fee schedule: (i) accounts with regular equity strategies; and (ii) accounts with index-based strategies.

## MM Compensation

Under Schwab’s agreements with the MMs, each MM receives a portion of the program fee as compensation for the discretionary investment advisory services it provides. The fees paid by Schwab to MMs range between 0.20% and 0.40% of assets under management through the programs for ETF strategies, between 0.25% and 0.40% for index-based strategies, between 0.35% and 0.50% for equity investment strategies (excluding index-based), between 0.40% and 0.45% for Diversified Portfolios, between 0.25% and 0.40% for fixed income investment strategies (other than bond ladders) and 0.15% for bond ladder investment strategies. (In unusual cases, the MM’s fee rate for equity strategies in the Access program may be higher than 0.50%.) The MM’s fee rate will generally become lower as total program assets managed by the MM reach certain levels, although some MMs may be paid on a fee schedule that does not include breakpoints. MMs may pay Schwab to participate in seminars organized by Schwab and attended by Schwab

representatives, clients or IAs doing business with Schwab Advisor Services (“AS”), which serves independent investment advisors and includes the custody, trading and support services of Schwab. MM participation in these seminars is not required by Schwab.

## Services Covered by the Program Fee

The program fee covers the MM’s asset management services, as well as the following services provided by Schwab: (1) execution of transactions in equity securities, ETFs and agency transactions in fixed income securities; (2) custody of account assets; (3) program administration; and (4) monthly account statements.

The program fee covers trade execution for transactions in equity securities executed through Schwab. It does not include (1) execution of transactions in fixed income securities by Schwab as principal and (2) execution of transactions in securities by other broker-dealers.

## Other Charges and Compensation

Trades in fixed income securities executed by Schwab as principal and trades executed with other broker-dealers will involve transaction charges in addition to the program fee. When Schwab (in the case of fixed income securities) or another broker-dealer executes a trade as principal, Schwab or the other dealer will realize the customary dealer profits or losses on the trade. Schwab also will charge a markup or markdown on transactions executed as principal in fixed income securities in the Select program. When a trade is executed by your MM with another broker-dealer, you will pay additional compensation to that broker-dealer, which may include markups, markdowns, commissions, and dealer profits. Any dealer profit, commission, markup or markdown on principal trades will be separate from and in addition to, and will not reduce or otherwise offset, the program fee for your account.

The program fee does not cover certain costs or charges imposed by third parties, such as odd-lot differentials, third-party mutual fund transaction fees on mutual funds transferred into a program account and then liquidated, certain contingent short-term redemption fees, American Depositary Receipt fees, exchange fees, and transfer taxes mandated by law. Schwab also may impose additional charges for special services elected by you or an MM, including without limitation periodic distribution fees, electronic fund and wire transfer fees, certificate delivery fees, and reorganization fees. Schwab and CSCorp also may receive indirect economic benefits, in addition to the program fee, if assets in your accounts are held as cash balances earning Schwab One® taxable interest or if trades are executed by a market center in which CSCorp owns an interest.

If you choose a closed-end fund or ETF strategy (which may include mutual funds) (collectively, “Funds”), you may in effect be paying two fees for asset management or investment services. You will pay your pro rata share of a Fund’s fees. Funds pay investment advisory, administrative, distribution, transfer agent, custodial, legal, audit, and other customary fees and expenses. The Fund bears these fees but you ultimately bear your share of these fees as a Fund shareholder. Mutual fund fees are disclosed in the fund’s annual and semi-annual report or other materials, which may be available on the fund’s website or through your investment advisor. You also will pay the program fee on assets invested in closed-end fund or ETF strategies. The mutual funds available through strategies in the Access program may be available directly from the mutual funds pursuant to the terms of their prospectuses and without paying the program fee, and closed-end funds and ETFs are available outside of the Access program without paying the program fee, subject to applicable commissions and/or transaction charges.

MMs that have Affiliated Funds in their strategies may have a conflict of interest in deciding whether to purchase and hold shares of those Funds in client accounts, because MMs or their affiliates may earn fees from those Funds. MM Affiliated Funds may pay the MM and/or their affiliates for investment advisory, administrative and transfer agency

services, as well as shareholder and other Fund services (collectively, "Fund Services"). Certain MM Affiliated Funds developed for use with an MM's separate account strategies may have arrangements whereby they do not pay any advisory or administrative fees to the Fund manager or sponsor. Please refer to the Fund's prospectus and statement of additional information for more information on fees.

It is possible that MM strategies that use Funds may buy, hold or sell shares of Schwab Affiliated Funds, which may include mutual funds or ETFs that are affiliated with Schwab. (CSIM and Windhaven® will not buy ETFs affiliated with Schwab ("Schwab ETFs") for retirement accounts.) Schwab or its affiliates may receive fees and other compensation from Schwab Affiliated Funds for Fund Services. In addition, mutual funds that are available in the Schwab Mutual Fund Marketplace® (or their affiliates) pay Schwab fees for recordkeeping, shareholder services and/or other administrative services.

Even if you don't choose a closed-end fund or ETF strategy, it is possible that your MM may decide to buy an ETF for your account with cash that is awaiting investment. This might occur with a subsequent contribution by you to your account after account opening or during the 30-day wash-sale period with respect to sale proceeds resulting from a tax harvesting request.

The program fee also does not cover services provided by your IA. In your contract with your IA, you have agreed to pay a fee for the IA's services. The IA's fee is additional to and separate from the program fee, even though the IA's fee may also be paid from your account in the program.

### **Payment of Program Fees and Other Charges**

Program fees are deducted from your account in the month following the month for which the fees were incurred. Other charges are deducted from your account when they are incurred. The program fee and other charges are payable from free credit balances, if any, in your account. If there are no free credit balances in your account, Schwab may redeem money market fund shares in your account to cover the charges or notify you to deposit additional funds into your account. Schwab reserves the right to liquidate at any time a portion of the other assets in your account to cover the program fee or other charges. Liquidation may affect the relative balance of your account and also may have tax consequences. Schwab may withhold any tax to the extent required by law, and may remit the tax to the appropriate governmental authority.

### **Valuation**

For purposes of calculating the program fee, Schwab will value a security listed on a national securities exchange, as of the valuation date, at the closing or last sale price on the principal market where the security is traded. If you have an investment strategy that uses options, Schwab will not take into account any negative valuation arising from an option position held in your account. Schwab will value any other securities or investments in your account in a manner determined in good faith to reflect fair value. The actual prices at which you could buy or sell the securities may be different from the prices used to calculate the fee. Any such valuation is not a guarantee of the value of the assets in your account. In computing the value of securities in your account, Schwab may use a pricing service or other independent evaluator, as well as other independent sources. While Schwab believes these sources to be reliable, Schwab does not verify them or guarantee their accuracy.

### **Amount of Fees**

The program fee may be more or less than you would pay if you purchased separately the types of services included in the programs. You may be able to obtain some or all of the types of services available through the programs on a stand-alone basis through Schwab or other firms. For example, you could separately purchase execution services from Schwab, and you could choose to either pay a commission for each transaction or pay an asset-based fee that would cover all transac-

tions. Similarly, you could separately contract with an MM to manage your assets, although the MM's minimum account size for accounts outside the programs may be higher than the minimum for program accounts, and the MM may charge a different fee.

Depending upon the circumstances, the total of any separately paid charges may be higher or lower than the program fee. Factors that bear upon the cost of the programs in relation to the cost of the same services purchased separately include, among other things, the type and size of your account (and other accounts that you may be able to combine to determine fee breakpoints), the historical and expected size or number of trades for your account, and the number and range of supplementary advisory and other services provided to your account. The program fee also may be higher or lower than the fees charged by other firms for comparable services. An investment strategy available through the programs may be similar to a mutual fund managed by the same MM, and the operating expenses of such a mutual fund may be lower or higher than the program fee.

Schwab offers another managed account platform—the Managed Account Marketplace® ("Marketplace")—in which Schwab and the participating MMs each assess separate charges for their services rather than a bundled fee. The services of Schwab and the MMs in Marketplace may cost less (or more) in total than in the programs. Like the programs, Marketplace includes brokerage, custody and related services by Schwab, and discretionary management by an MM to accounts opened and maintained by Schwab. More MMs are available in Marketplace than in the programs. Schwab does not act as a program sponsor in Marketplace, which means, among other things, that you and your IA are responsible for negotiating your own fee and contractual arrangements with the MMs for the management of your account. Schwab does not screen or evaluate MMs in Marketplace.

MMs that have MM Affiliated Funds in their strategies may have a conflict of interest in deciding whether to purchase and hold shares of those Funds in client accounts, because MMs or their affiliates may earn fees from those Funds. See "Other Charges and Compensation" above.

### **Investment in Affiliated Money Funds**

In your account application you will have the choice of investing the cash in your account in a money market fund sponsored by Schwab, CSIM or another affiliate of Schwab (an "Affiliated Money Fund"), as long as the amount of cash to be invested satisfies the Affiliated Money Fund's minimum investment requirement. CSIM or another affiliate of Schwab serving as investment advisor to an Affiliated Money Fund will receive advisory fees from the Affiliated Money Fund as set forth in the Affiliated Money Fund's prospectus. CSIM or other affiliates of Schwab also may receive other compensation from the Affiliated Money Fund for shareholder servicing, accounting, recordkeeping, expense management and other administrative services (see the prospectus and statement of additional information for the Affiliated Money Fund for more information). If you have a retirement account managed by CSIM or Windhaven, effective April 30, 2012, Schwab will offset (reduce) the total Access program fee applicable to your account by an amount determined by multiplying the highest "Expense Ratio" for any Affiliated Money Fund (eligible for retirement accounts in Access) by the amount of assets in your account invested in your chosen Affiliated Money Fund. (The "Expense Ratio" for each Affiliated Money Fund is the ratio that results from dividing the amount of fees received by Schwab and its affiliates from the Affiliated Money Fund by the Affiliated Money Fund's total assets.) Prior to April 30, 2012, if you had a retirement account managed by CSIM, Schwab would have reduced the Access program fee applicable to any assets held in an Affiliated Money Fund by an amount at least equal to the amount of fees received by Schwab and its affiliates from the Affiliated Money Fund that was attributable to those assets. If you had a retirement account managed by Windhaven, prior to April 30, 2012, Schwab would not have charged the Access program fee on any assets held in an Affiliated Money Fund.



## Funds Awaiting Investment or Pending Distribution

Schwab earns interest, generally at money market rates, on aggregate cash balances held in Schwab's bank accounts, which include assets in accounts enrolled in Select or Access that are awaiting investment or pending distribution. Funds awaiting investment include both cash that you have deposited into your account and uninvested amounts held in your account as a result of an authorized transaction. Schwab may earn interest on such amounts through the beginning of the second business day following the deposit or transaction in question. Schwab may earn interest on assets pending distribution from your account beginning on the day the assets are debited from your account and continuing until the distribution check is presented for payment, the timing of which is beyond Schwab's control.

## Negative Yield for Cash and Cash Investments

Please note that any cash or cash investments in your account will result in a negative yield to the extent the program fee exceeds the rates of return for Schwab One® interest or for an Affiliated Money Fund chosen as a cash sweep vehicle for your account. Please ask your IA about current rates on cash and cash investments for your account.

## Other Compensation

Schwab and its affiliates and their employees benefit from the compensation you pay to Schwab under the programs. To the extent that you use other products or services Schwab offers, Schwab benefits from this additional compensation.

Certain Schwab representatives may receive incentive compensation from Schwab based on the amount of net new assets that AS clients place into Schwab's managed account programs, including Access and Select. These Schwab representatives meet with AS advisors but do not meet with their clients. No compensation is paid to AS advisors under this arrangement.

Schwab may have business relationships with certain MMs and their affiliates outside of the programs in which Schwab receives direct or indirect compensation. Mutual funds that are affiliated with an MM may participate in Schwab's Mutual Fund Marketplace® or Mutual Fund OneSource® program, in which Schwab receives remuneration from the mutual funds (or their advisors) for shareholder servicing and other administrative services with respect to shares in those funds held at Schwab. Certain MMs or their affiliates may also have business relationships with AS in which these firms manage client assets outside of the programs; these relationships generate trading, margin and other revenue for Schwab in the normal course of its business as a broker-dealer. MMs may also receive (on behalf of clients or otherwise) research, execution, custodial, referral, pricing and other services offered by Schwab in the normal course of its financial services business.

The compensation Schwab pays to MMs with ETF strategies that include mutual funds may be based in part on Schwab's consideration of whether those mutual funds are in Schwab's Mutual Fund OneSource program, because Schwab receives remuneration from the mutual funds as described in the prior paragraph. To the extent Schwab pays an MM more than Schwab would if the MM did not use OneSource funds in its strategy, this could create an economic incentive for the MM to use OneSource funds instead of funds that are not in the OneSource program (e.g., transaction fee funds).

If you do not select a Schwab money market fund as the cash sweep feature for your account or do not meet the fund's minimum investment (see "Investment in Affiliated Money Funds" above), cash in your account will be held as a free credit balance with Schwab and you will receive Schwab One taxable interest. (Schwab money market funds are the only cash sweep features available to retirement accounts.) As a registered broker-dealer, Schwab may benefit from the possession or use of any free credit balances in your account, subject to restrictions imposed by law.

## Risk and Taxes

All investments involve the risk (the amount of which may vary significantly) that investment performance can never be predicted or guaranteed and that the value of your portfolio will fluctuate due to market conditions and other factors—see "Certain Risks" below. You should also understand that all or a portion of your securities may be sold either at the initiation of or during the course of the management of your account under the programs. You are responsible for all tax liabilities arising from such transactions, and you are encouraged to seek the advice of a qualified tax professional.

You may choose the cost basis method for calculating gains and losses on securities transactions in your account for tax purposes. If you do not choose the method, Schwab will calculate your gains and losses using the FIFO (First In, First Out) cost basis method for all securities except mutual funds, which means the first shares acquired of a particular security are the first shares that will be sold. The average cost method will be used for mutual funds, but even if it is applied, lots are sold in a FIFO manner. When an MM sells a security, the cost basis method used to calculate your gains and losses cannot be changed after your trade settles. Your MM's trading authorization includes the ability to select the tax lots they sell in your account. This is known as "versus purchase trading." When an MM places a trade and does not select a lot, the cost basis method listed on your account will be used to calculate your gain/loss.

## Termination of Participation in the Programs

You may terminate your participation in the programs at any time upon written notice to Schwab without penalty, subject to the payment of any fees incurred and allowing at least two business days for Schwab to process your termination instruction. Once your authorizations granted to your MM have been terminated, your account will be charged Schwab's then-current fees and other applicable charges for accounts managed by your IA at Schwab, and you and your IA will be responsible for managing your account. If you also terminate your authorizations granted to your IA, your account will become enrolled in the Schwab independent investor service and will be subject to the fees and commissions applicable to that service unless Schwab notifies you otherwise; you will then be solely responsible for managing your account.

If you terminate the MM for a managed account with a fixed income strategy that holds shares in a mutual fund developed for use with separate account strategies (such as Fixed Income Shares in the PIMCO Total Return Strategy), your shares in that mutual fund will be liquidated by the MM. You will not have the option of retaining those shares. If you terminate an account with a strategy that uses certain classes of no-load or load-waived shares, you may no longer be eligible to hold those shares, in which case your shares will be converted to an eligible share class that may have sales loads and/or transaction fees.

Depending on current market conditions, if you terminate an MM for a fixed income strategy and direct the sale of the bonds in your account, the MM may need additional time to sell your bonds (particularly municipal bonds). In this situation, your IA will inform you and give you the option of (1) allowing the MM to have additional time to sell your bonds, and the program fee will continue to apply to assets that remain in your account during this process; or (2) holding the bond in an account that is not managed by the MM and waiting until the bond matures or directing the sale of it yourself at some later date (without the MM's execution capabilities). There can be no assurance as to how long it might take to sell your bonds, and the sale price may be substantially lower than the price which you paid or the price at which the bond was previously traded.

Depending on the size of your account, some bonds may be purchased for your account by fixed income MMs in positions that are smaller than marketable round lots (sometimes called "odd lots"). If you have an odd lot bond, it may be more difficult to sell than a round lot, and the sale price may be substantially lower than the price which you paid or the



price at which the position previously was valued. If you decide to terminate your participation in a program and do not plan to hold the odd lot until maturity, it may be advisable for you to direct the sale of the odd lot when you terminate your program participation, as the MM may be able to obtain a better price for it than Schwab or another broker-dealer.

### **Funding and Adding Securities to Your Account**

You may fund your account with, and add to your account, cash, certain mutual fund shares, stocks or bonds to your account, but Schwab reserves the right to decline to accept particular securities or require you to wait a specific period before depositing certain securities. You cannot fund your account with certain securities, including foreign securities (other than American Depositary Receipts) or restricted securities. When funding your account with securities or depositing securities to your account, you should bear in mind that the MM you designate may decide to sell all or a substantial portion of such securities and that you will be responsible for any tax liabilities resulting from such transactions, as well as any contingent short-term redemption fees resulting from the sale of mutual fund shares you deposited in your account. Certain MMs will only accept certain types of securities for account funding, such as investment-grade municipal bonds for municipal bond ladder strategies.

### **Account Requirements and Types of Clients**

#### **Types of Clients**

The programs are intended for clients seeking discretionary management of their account for a bundled fee. Clients of the programs may include individuals, trusts, charitable organizations, pension and profit-sharing plans, investment clubs, corporations and other business organizations.

#### **Account Minimums**

Minimum account sizes apply to each investment strategy in the program and generally start at \$100,000 for equity strategies; the minimum account sizes for fixed income investment strategies (including bond ladder strategies) and for Diversified Portfolios are generally \$250,000 and \$350,000, respectively. Additional contributions to accounts managed by certain MMs may be subject to minimum amount requirements so that additional contributions of less than the minimum requirement will be held as cash or cash investments and earn interest or be invested in a money market fund as specified by you in your account application.

If the market value of your account falls significantly below the specified minimum due to your withdrawal of assets from the account, Schwab may require you to deposit additional money or securities to bring the account up to the required minimum, or Schwab reserves the right to close the account.

### **Portfolio Manager Selection and Evaluation**

#### **Select Services**

From the inception of the Select program in 2001 until the end of 2007, MM evaluation and research services were provided by Callan Associates Inc. ("Callan"), a consulting firm that is not affiliated with Schwab. Effective January 1, 2008, SCFR assumed responsibility for these functions, and effective January 1, 2010, CSIA assumed responsibility for these functions (on that date, the SCFR analysts performing these functions became part of CSIA). For purposes of this discussion, Callan, SCFR and CSIA are each referred to as the "Research Provider."

The MMs and investment strategies in the Select program have been determined by Schwab, with the Research Provider's assistance, to be appropriate for clients whose asset allocation, investment objectives, risk tolerance and time horizon, as determined with the advice of their IA, warrant the MM's investment strategy. You and your IA are respon-

sible for the determination of your asset allocation, investment objectives, risk tolerance and time horizon, as well as whether a particular MM (and their investment strategy) is suitable for you.

Before an MM and its investment strategy is selected to participate in the Select program, Schwab, with the Research Provider's assistance, performs a comprehensive review of the MM and its investment strategy, as more fully described below. To be included in Select, an MM must meet the program's business criteria, which include the program's MM fee structure, the program's account minimums, utilization by the MM of the program's portfolio management system, execution by the MM of Schwab's standard MM service agreement and other factors. Schwab's Advice Policy Committee (the "Committee") makes the final decision whether to include or keep an MM in the Select program, based upon the Research Provider's recommendation. The Committee consists of Schwab management personnel, and is also responsible for the selection of recommendable mutual funds in various lists maintained by Schwab.

In determining whether to recommend to the Committee that an MM's investment strategy be included in or terminated from Select, CSIA, as the current Research Provider, evaluates information from both quantitative and qualitative analyses. CSIA's review includes assessing information about the MM and its investment strategy collected from third party sources and information received directly from the MM through on-site visits, interviews or questionnaires. Schwab is not responsible for the performance of any MM under the Select program or any MM's compliance with applicable laws or regulations or other matters within the MM's control.

For its quantitative analysis, CSIA uses a proprietary scoring system that combines multiple characteristics into a single score which represents the expected future relative performance rank of the MM's investment strategy within its style category. The characteristics considered include (i) past performance adjusted for risk and style effects and measured over multiple, non-overlapping time horizons; (ii) assets under management; (iii) cash inflows; and (iv) a returns-based measure of active share, which is a measure of dissimilarity to a benchmark index. In its qualitative analysis, CSIA considers a variety of investment criteria, including:

- Historical style consistency
- Appropriateness of the strategy for the style category
- The MM's investment strategy and adherence to it
- Diversity of investment approach versus other strategies in Select
- Stability of management and ownership structure
- Governance program of the management company
- Quality of composite return information

CSIA evaluates each MM's investment strategy no less than quarterly based on the factors described above. Changes within an MM's organization or operations that, in CSIA's judgment, warrant review before the regular quarterly review will be reviewed at that time by CSIA. As a result of these reviews, an MM's investment strategy may be terminated from Select or put on a watchlist (which is available to your IA). If an MM's investment strategy is put on a watchlist, it will be monitored more closely over a specified time period; it will still be available for new accounts but may ultimately be removed from the program if no improvement occurs. Schwab reserves the right to terminate an MM's investment strategy from Select at any time for any reason.

Schwab or an MM may remove the MM's investment strategy from a program under circumstances where that MM will no longer manage new accounts in the programs with that investment strategy. If this happens with an investment strategy that you have chosen, Schwab will inform you and your IA as soon as practicable. Your IA will advise you on whether to select a new investment strategy or MM that is available

through one of the programs, switch your account to an account outside the programs for management by the same MM (if that MM's investment strategy is available through one of Schwab's other managed account services), or take any other action. It is also possible that Schwab and an MM may agree to move a particular investment strategy from one program to the other. If this happens with an investment strategy you have chosen, Schwab will notify your IA but Schwab will not notify you. Your account will automatically become a managed account in the other program subject to the same fees with no action required on your part. If you want to know whether your strategy changes programs, you should ask your IA to keep you informed of any such changes. If your chosen investment strategy moves from Select to Access, Schwab will no longer provide research or other information regarding the strategy.

You also may have the option of keeping an existing account under the management of an MM that is not available to new client accounts under either program, subject to the agreement of that MM to continue providing its investment strategy under the program to existing clients and your agreement that Schwab is not responsible for monitoring that MM's performance or providing information on that MM. In that case, you would pay the same fees (unless the MM and Schwab agree to a change in fee schedule) and would receive many, but not all, of the same services as before. Schwab will not make information available to you or your IA about an MM's investment strategy that is no longer being offered to new accounts under the Select program and will not monitor the MM's performance. Schwab is under no obligation to provide this option to you.

### **Diversified Portfolios**

The Select program also includes Diversified Portfolios. A Diversified Portfolio strategy includes several investment strategies ("Combined Strategies"), such as large-cap equity, small-cap equity and fixed income strategies. You can have a Diversified Portfolio strategy in a single account, with a minimum account size (generally \$350,000, but the minimum may be as low as \$250,000 or as high as \$650,000) that is typically less than if you opened a separate account for each strategy. The Diversified Portfolio strategies currently have several different asset allocations composed of varying percentage allocations of the available Combined Strategies ("Asset Allocations"). Some of the Asset Allocations have bond holdings that are tax-exempt, and some have bond holdings that are taxable. SCFR developed these Asset Allocations to accommodate clients with different risk profiles, time horizons and tax status. Your IA will help you decide whether a Diversified Portfolio strategy is appropriate for you, and, if so, will help you choose which Asset Allocation is appropriate for you.

The structure of a Diversified Portfolio strategy typically involves an MM acting as "overlay manager," as well as other MMs who provide model investment portfolios or research for the Combined Strategies to the overlay manager ("Sub-MMs"). (The Sub-MMs may or may not be available on a stand-alone basis in Select.) The functions of an overlay manager will vary depending on the Diversified Portfolio strategy. Sometimes the overlay manager may have all the trading responsibility for all the Combined Strategies, sometimes the Sub-MMs may have all the trading responsibility (which is often the case with fixed income strategies), and sometimes the overlay manager and the Sub-MMs may allocate trading responsibility among themselves depending on the type of trading activity. Examples of the different trading activities which may be allocated among the overlay manager and the Sub-MMs include: initial implementation of your portfolio, subsequent changes to your portfolio based on changes to the Sub-MMs' model portfolios, re-balancing your portfolio to bring it within the guidelines of the Asset Allocation, trading caused by cash withdrawals initiated by you, tax harvesting requests initiated by you, and liquidations requested by you.

The overlay manager is authorized to make adjustments if one or more of the Combined Strategies in your portfolio become over- or under-weighted from the Asset Allocation as a result of market appreciation or depreciation. Such adjustments will generally be made by the overlay

manager when the proportion of equity securities to fixed income securities varies by five or more percentage points from the Asset Allocation and when the proportion of one of the Combined Strategies varies by more than 10 percentage points from the Asset Allocation. As a result of the possibility of allocation adjustments, the performance of a Combined Strategy in a Diversified Portfolio account may differ from the performance of that Combined Strategy in a separate account.

The overlay manager may also monitor your Diversified Portfolio account to make sure your investment restrictions are implemented across all Combined Strategies. For taxable accounts, the overlay manager will generally monitor and avoid wash sales.

The following overlay managers—Nuveen Investment Advisers Inc. ("Nuveen") and Parametric Portfolio Associates ("Parametric")—and the Sub-MMs for their Diversified Portfolio strategies were selected by Schwab for the Select program based on a number of factors, including the following: (i) the reputation, historical performance and organizational stability of the overlay managers and the Sub-MMs; (ii) the overall performance of the Diversified Portfolio strategies based on the combined performance of the Combined Strategies (calculated on a hypothetical basis); (iii) the fact that most of the Sub-MMs are affiliates of the overlay manager and have pre-existing working relationships with the overlay manager in other multi-strategy portfolios; (iv) most of the Sub-MMs for the Diversified Portfolio strategies were already in the Select program on a stand-alone basis and have already gone through the selection and review process described above under "Select Services"; and (v) the Sub-MMs and overlay managers met Schwab's business criteria for multi-strategy portfolios in the Select program, including the MM fee structure, account minimums, utilization of the program's portfolio management system and execution of Schwab's service agreement. If Schwab (with the Research Provider's assistance) had conducted a wider search for the Sub-MMs and Combined Strategies that comprise the Diversified Portfolio strategies, it is possible that other Sub-MMs or Combined Strategies may have been selected which would have been ranked higher by the Research Provider than those selected. The Research Provider has evaluated each Sub-MM and Combined Strategy based on factors such as investment performance, style adherence, and organizational stability, and will continue to evaluate the Sub-MMs and Combined Strategies on a quarterly basis.

A Sub-MM may be terminated and replaced by the overlay manager and Schwab without your approval. Similarly, Schwab and the overlay manager may also agree to change the percentages of the Asset Allocation without your approval. If you have a Diversified Portfolio account in which a Sub-MM is terminated and replaced, or if the percentages of the Asset Allocation are changed, you will be notified by Schwab as soon as reasonably practicable.

### **About Callan**

Callan provided MM research and performance evaluation services for the Select program until the end of 2007, at which time SCFR (now CSIA) began performing those services. Many of the MMs and investment strategies in the Select program were initially included in the Select program based on Callan's recommendation.

Callan received compensation from Schwab for Callan's services relative to the Select program based on the amount of assets in the program. MMs in the Select program may have paid Callan for strategic, communication and product consulting services, investment product analysis, research reports and software programs from Callan's Institutional Consulting Group or educational services from the Callan Investment Institute and Center for Investment Training. These payments may have given rise to potential conflicts of interest in Callan's recommendations of MMs for inclusion in the Select program and subsequent monitoring of those MMs. According to Callan, Callan managed these conflicts of interest with certain policies and a Code of Ethics designed to help maintain its independence, and its personnel that performed MM searches and evaluations were in a separate division from the areas in the firm that provide services to MMs.

## About CSIA

CSIA is an affiliate of Schwab that provides research and decision-making tools to Schwab for use by Schwab clients (and their advisors), including the *Mutual Fund OneSource Select List*®. CSIA personnel also act as portfolio managers for a mutual fund and ETF bundled fee program sponsored by Schwab. CSIA personnel were formerly part of SCFR. SCFR is still a division of Schwab that provides services such as Schwab Equity Ratings® and recommended asset allocations for investors within different risk categories.

## Access Services

Any MM is eligible to participate in the Access program, whether affiliated or unaffiliated with Schwab. Two affiliates of Schwab—Charles Schwab Investment Management, Inc. (“CSIM”) and Windhaven Investment Management Inc. (“Windhaven”)—are participating in Access as MMs.

The minimum account size for certain MMs is generally lower in the Access program than if you engaged the MM directly for discretionary investment management services. Unlike the Select program, neither Callan nor CSIA plays or has played a role in the Access program, and Schwab does not evaluate or monitor MMs in Access. There can be no assurance that the investment strategies in the Access program would be selected for the Select program if they were subjected to the Select screening process and were otherwise eligible (Schwab affiliates are not eligible to participate in the Select program). Schwab does not recommend or endorse any MMs in Access to you or your IA, whether affiliated with Schwab or not. Schwab does not offer IAs any incentive to allocate assets to an MM affiliated with Schwab.

The Access program includes municipal bond ladder strategies managed by Pacific Investment Management Co. LLC (“PIMCO”). In these strategies, PIMCO buys municipal bonds maturing over a designated period of years that are intended to be held until maturity. Retirement accounts are not permitted in these strategies. PIMCO will only accept cash or investment-grade municipal bonds to fund bond ladder strategies. When contributing investment-grade municipal bonds, you should be aware that PIMCO may, within five business days following notification of the securities to be contributed, determine to reject any security that is not consistent with the guidelines for the relevant ladder (e.g., because the bond is illiquid or subject to the federal alternative minimum tax). If PIMCO rejects a security, PIMCO may, at its option, either (i) liquidate the security and use the proceeds to fund purchases consistent with the strategy, in which case you may bear additional costs and consequences such as risk of adverse price movement, transaction costs and potential adverse tax consequences or (ii) inform Schwab that it will not accept the security, in which case Schwab will notify your IA to help you determine whether to liquidate the holding or to substitute cash or acceptable securities. If a rejection causes your account to fall below the minimum investment requirement, you may need to fund the account with cash or other investment-grade municipal bonds in order to enroll or stay enrolled in the strategy.

In addition to strategies that buy, hold and sell individual securities, the Access program includes MMs who create and maintain strategies that buy, hold and sell Funds for clients on a discretionary basis. These strategies may include mutual funds that are available through Schwab’s Mutual Fund MarketPlace® service; in addition, some of the Funds may be affiliated with the MM (“MM Affiliated Funds”) or Schwab (“Schwab Affiliated Funds”). See “Other Charges and Compensation.” With the exception of Windhaven®, MMs in Access that manage Fund strategies are not affiliated with Schwab, and Schwab does not influence their selection of Funds for client accounts.

Schwab makes no representation as to whether any MM or investment strategy in the Access program is appropriate for you. You and your IA are responsible for determining whether any investment strategy or any MM in the Access program is suitable for you in light of your asset allocation, investment objectives, risk tolerance and time horizon. You

and your IA are also responsible for the determination of your asset allocation, investment objectives, risk tolerance and time horizon.

There are no criteria for MMs to participate in the Access program, and Schwab does not monitor the style adherence or performance of MMs in the Access program. However, Schwab reserves the right to remove an MM or its investment strategy from the Access program at any time for any reason.

## Information About MMs

Each MM’s Form ADV disclosure brochure (“MM brochure”) provides information about that MM. For each of your accounts, you will receive the brochure of the MM you designate to manage that account before the MM begins managing it. The MM has discretion as to whether or not to accept the management of your account.

Additional information about an MM in the Select program and its investment strategy is available in its MM Profile; MM Profiles are not available through Schwab for MMs in the Access program, although Schwab does make available a brochure from PIMCO describing its bond ladder strategies and may in the future make available a profile from Windhaven. CSIA prepares the MM Profiles for strategies in Select based on information obtained from the MMs and third-party sources. The MM Profile describes the MM, its investment strategy and past performance information. MM Profiles are available to your IA. The accuracy and completeness of the MM data contained in the MM Profiles are the responsibility of the MM. CSIA will update the MM Profiles for Select strategies quarterly based on information obtained from the MMs and third-party sources.

Schwab makes MM information available to your IA through a research and proposal generation system known as the Investment Proposal Center (“IPC”). The IPC is provided by Informa Investment Solutions, Inc. (“Informa”), an independent financial services firm and a wholly owned subsidiary of Informa Financial Information, Inc. Schwab licenses the IPC from Informa; Schwab and Informa are not affiliated. The IPC allows your IA to research MMs who provide performance and other information to Informa, including MMs available in the programs. The IPC also allows your IA to create a client proposal or report that includes MM information, and it is possible that you will receive a report from your IA that was generated from the IPC. Schwab may discontinue making the IPC available to your IA at any time, and the IPC may not provide information on all strategies in the programs.

Schwab does not independently verify or guarantee the accuracy or completeness of (i) the information available through the IPC, (ii) the information in the MM Profiles or (iii) any information provided by the MM directly to you or your IA. Any MM past performance information contained in any source is not verified or audited by Schwab. There can be no assurance that the MM performance information available to you is calculated on a uniform or consistent basis. Past MM performance is no guarantee of future results.

## Non-Exclusive Relationship

Schwab and its affiliates may perform, among other things, research, brokerage, asset management, and similar services for other clients and receive asset-based fees for such services. The advice given and the actions taken for a particular client may differ from the advice given or the timing and nature of action taken for other clients’ accounts. Transactions in a specific security may not be accomplished for all clients’ accounts at the same time or at the same price. In managing your account, an MM may purchase or sell securities in which the MM, Schwab, or their officers, directors, employees or representatives, directly or indirectly, have or may acquire a position or interest.

CSIM also manages mutual funds that use Schwab Equity Ratings, but CSIM will not adjust the model portfolio it uses for its Access strategies as frequently as the mutual funds’ portfolios and, therefore, the time and market price at which one of those mutual funds buys or sells a specific security may vary from the time and price at which CSIM buys

or sells the same security for an Access account. Further, the price at which CSIM buys or sells the security for an account in Access may reflect market activity resulting from purchases and sales by the mutual funds and Schwab clients who acted on changes to the Schwab Equity Ratings® before CSIM acted for accounts in the Access program.

In managing your account, an MM may purchase or sell securities in which the MM, Schwab or their officers, directors, employees or representatives, directly or indirectly, have or may acquire a position or interest. In addition, it is possible (although unlikely) that a mutual fund managed by CSIM could have a short position in a stock owned by clients in the Access program, meaning that the CSIM mutual fund portfolio manager expects that the price of the stock held short will go down, even though the CSIM portfolio manager for the Access strategy has caused Access client accounts to buy that stock.

The MMs, Schwab or their affiliates may, in the course of business, obtain material nonpublic or other confidential information that, if disclosed, might affect an investor's decision to buy, sell or hold a security. The MMs, Schwab, and their affiliates are restricted from disclosing or using this information under applicable law, and are under no obligation to disclose the information to any client or use it for any client's benefit.

### **Client Information Provided to Portfolio Managers**

By signing the Schwab account application, you authorize Schwab to provide trading and other information about your account to the MM managing your account and third parties designated by the MM. In addition, your IA will communicate such information as necessary to the MM managing your account. Examples of information communicated by your IA to your MM may include investment restrictions, tax harvesting instructions and updates to the information you provide in your account application.

### **Client Contact With Portfolio Managers**

You may contact an MM directly, although it is generally expected that you will direct questions concerning your account to your IA. You may change MMs or investment strategies, or switch an account from one program to another, at any time by submitting the form prescribed by Schwab for that purpose. An MM also may terminate a relationship with you at any time upon 30 days' notice to you and Schwab.

### **Additional Information**

#### **Disciplinary Information**

The SEC and other regulatory agencies and organizations have, in the past, taken certain disciplinary actions against Schwab for violations of investment-related statutes, regulations and rules. The matters have been settled, and Schwab has paid fines with respect to certain violations.

1. Schwab entered into a consent order with the State of Nevada on November 2, 2011, in which Schwab was fined \$10,000 for failing to detect the lack of Nevada state registration of a non-employee investment advisor. Schwab was found to have violated its own procedures and Nevada Administrative Code Section 90.321 for failing to determine that the non-employee was acting as a professional investment advisor at the time the accounts were set up or during the course of his management of the accounts at issue.
2. A disciplinary action initiated by the Financial Industry Regulatory Authority ("FINRA") asserted that Schwab violated Municipal Securities Rulemaking Board Rule G-14 by: (1) failing to report required information about certain municipal securities transactions to the Real-Time Transaction Reporting System ("RTRS") within 15 minutes of trade time; and (2) failing to report the correct trade execution time to the RTRS for some of these transactions. Without admitting or denying these assertions, Schwab consented to a censure and a fine of \$12,500 on June 17, 2011.

3. Schwab and CSIM have reached agreements with the United States Securities and Exchange Commission ("SEC"), FINRA, the Illinois Secretary of State, Securities Department ("Illinois"), and the Connecticut Department of Banking, Securities and Business Investments Division ("Connecticut") to settle matters related to the Schwab YieldPlus Fund® (the "Fund"). For purposes of this discussion of matters related to the Fund, Schwab and CSIM are collectively referred to as "Schwab."

As part of the SEC settlement, the SEC found that Schwab violated certain investment-related laws and regulations related to the offer, sale and management of the Fund from 2005 through 2008. In particular, the SEC found that Schwab: (1) deviated from the Fund's concentration policy with respect to investments in non-agency mortgage-backed securities, without shareholder approval; (2) made materially misleading statements and omissions about the Fund and its associated risks before and during the decline of its net asset value ("NAV"); (3) materially understated the Fund weighted average maturity ("WAM") in certain instances; (4) willfully aided and abetted misstatements and omissions appearing in Fund sales materials and other documents; and (5) lacked policies and procedures reasonably designed to prevent the misuse of material nonpublic information about the Fund. Without admitting or denying these allegations, Schwab agreed to pay a total of approximately \$118,944,996 in disgorgement of fees, penalties and compensation to investors. As part of the settlement with the SEC, Schwab will also take a number of actions to improve procedures and reinforce Schwab's commitment to its clients. These actions include retaining an independent consultant to conduct a comprehensive review of Schwab's policies, practices and procedures designed to prevent the misuse of material, nonpublic information by or related to Schwab's mutual funds. The SEC settlement was approved by the U.S. District Court for the Northern District of California on February 16, 2011. Additionally, the SEC has brought related complaints against two former employees of Schwab.

The amount to be paid by Schwab pursuant to the SEC settlement includes approximately \$18,000,000 to be paid by Schwab in settlement of the FINRA matter in which FINRA made related factual allegations against Schwab and found that Schwab's conduct violated FINRA's just and equitable principles of trade and its rules pertaining to communications with the public and supervision.

Schwab has also agreed to pay approximately \$8,567,364 in settlement of the Illinois matter in which Illinois made related factual allegations against Schwab and found that Schwab's conduct violated Illinois Securities Law provisions relating to supervision of securities and advisory activity by employees and to maintenance of written procedures reasonably designed to comply with securities laws and regulations.

Schwab has also agreed to pay an amount not to exceed \$2,800,000 in settlement of the Connecticut matter in which Connecticut made related factual allegations against Schwab and found that Schwab violated applicable Connecticut laws and regulations by failing to reasonably supervise its employees.

Schwab and certain affiliated entities and individuals (the "Schwab Parties") were named as defendants in a number of Fund-related class action lawsuits filed in the United States District Court for the Northern District of California in 2008. These lawsuits were consolidated into a single class action complaint that alleged violations of state law and federal securities law similar to those described above. On March 30, 2010, the court granted plaintiffs' motion for summary judgment holding defendants liable for plaintiffs' state law claim regarding changes to the investment policy of the Fund, which plaintiffs alleged were made without shareholder approval in violation of the Investment Company Act of 1940. Although the judgment was subject to a potential appeal and further proceedings on damages, the Schwab Parties entered into a settlement agreement to settle the plaintiffs' federal securities law claims for approximately

\$200,000,000 and the plaintiffs' California law claims for approximately \$35,000,000. On April 19, 2011, the court entered an order granting plaintiffs' and defendants' motions for final approval of the settlement agreement.

4. A disciplinary action initiated by the New York Stock Exchange ("NYSE") asserted that Schwab: (a) submitted inaccurate electronic blue sheets in violation of NYSE Rules 410A and 401; and (b) failed to properly supervise the preparation of its electronic blue sheets in violation of NYSE Rule 342. Effective January 5, 2006, the NYSE approved a stipulation of facts and consent to penalty ("Stipulation") between Schwab and the NYSE Division of Enforcement. Without admitting or denying guilt, Schwab consented to the Stipulation that it violated the foregoing rules and regulations. As part of the Stipulation, Schwab consented to a censure and a fine of \$300,000. Schwab also agreed to conduct a validation of all required blue sheet data elements and notify the NYSE in writing that it has completed the validation.
5. A disciplinary action initiated by the NYSE asserted that Schwab: (a) violated NYSE Rules 342(a) and (b) in that Schwab failed to establish and maintain appropriate procedures for supervision and control, including a separate system of follow-up and review, with respect to certain business activities relating to protection of customer assets in accounts managed by non-employee investment advisors and carried by Schwab; and (b) violated Section 17(A) of the Securities Exchange Act of 1934 ("Exchange Act") and Rules 17A-4(b)(4) and 17A-4(f) thereunder and NYSE Rule 440 by failing to preserve and maintain certain electronic communications in the required format and for the required retention periods. Effective October 17, 2005, the NYSE approved a stipulation of facts and consent to penalty ("2005 Stipulation") between Schwab and the NYSE Division of Enforcement. Without admitting or denying guilt, Schwab consented to the 2005 Stipulation that it violated the foregoing rules and regulations. As part of the Stipulation, Schwab consented to a censure and a fine of \$1,000,000. Schwab also undertook: (a) to retain an outside consultant to conduct a review of its policies and procedures with respect to the disbursement of funds from accounts managed by investment advisors; (b) to have the consultant provide a report to the NYSE's Division of Enforcement within 120 days of the date the decision becomes final; and (c) to submit to the NYSE a written representation setting forth the implementation of the recommendations contained in the consultant's report within 60 days of the report's issuance.
6. On September 14, 2004, the SEC issued an order instituting public administrative and cease and desist proceedings pursuant to Sections 15(b) and 21B of the Exchange Act and Sections 9(b) and 9(f) of the Investment Company Act of 1940 ("Investment Company Act") making findings, imposing remedial sanctions and issuing a cease-and-desist order as to Schwab ("Order"). Schwab consented to entry of the order without admitting or denying the SEC's findings made in the Order. The SEC found that from at least January 2001 through October 2003, Schwab engaged in a practice that enabled certain mutual fund shareholders to place mutual fund orders after the time the funds calculated their net asset values ("NAV") for that day. Specifically, Schwab allowed clients of investment advisors to place substitute mutual fund orders after 4:00 p.m. Eastern Time ("ET"), the time as of which those funds calculated their NAV. The order substitutions were permitted when one of these client's original pre-4:00 p.m. ET mutual fund orders was rejected by Schwab's computer system because it could not be processed as submitted. The SEC found that this practice violated Rule 22c-1(a) under the Investment Company Act and Schwab's own internal policy requiring any orders Schwab received after 4:00 p.m. ET to get the next day's fund price. These substitute orders were not made pursuant to any improper agreements between Schwab personnel and the investment advisor or the investment advisor's clients. The SEC imposed on Schwab the following sanctions: (1) that Schwab cease and desist from committing or causing any violations and any future violations of Rule 22c-1(a) under the Investment Company Act; (2) censure of Schwab; and (3) a civil money penalty payable by Schwab in the amount of \$350,000.
7. A disciplinary action initiated by the NYSE asserted that during the time period between approximately February 1997 and September 2003, Schwab: (a) violated NYSE Rule 346(f) by having persons associated with it (without permission of the NYSE) that Schwab knew, or through the exercise of reasonable care should have known, were subject to statutory disqualification; (b) violated NYSE Rule 351(a)(5) by failing to promptly report to the NYSE certain arrests, arraignments, indictments, convictions, guilty pleas and/or no contest pleas to criminal offenses, other than minor traffic violations of employees; (c) violated NYSE Rule 342 by failing to reasonably supervise its business in order to ensure compliance with federal securities laws and NYSE rules relating to associations with statutorily disqualified individuals and reporting to the NYSE of events related to employee criminal matters. Effective July 8, 2004, the NYSE approved a stipulation of facts and consent to penalty between Schwab and the NYSE Division of Enforcement. Without admitting or denying guilt, Schwab consented to the stipulation that it violated NYSE rules. As part of the stipulation, Schwab agreed to censure and a fine of \$250,000. Schwab also agreed (a) to retain an outside consultant within 30 days of the decision to perform a review and prepare a report; (b) have the consultant provide a report to the NYSE's Division of Enforcement and Schwab's Board of Directors within 120 days from the date the decision becomes final; and (c) submit to the NYSE a written representation setting forth the implementation of the recommendations contained in the report within 60 days of the report's issuance.
8. A disciplinary action initiated by the National Association of Securities Dealers ("NASD") asserted that: (a) during the period August 14, 2002, through March 25, 2003, Schwab violated Municipal Securities Rule Making Board Rules G-17 and G-30(a) when it relied solely on the bids provided by a broker's broker to determine the fair market value in the liquidation of six municipal security positions for customers; (b) the prices paid to the customers and received by Schwab were below the fair market value for the security in amounts ranging from 6.57% to 38.57%; and (c) Schwab failed to ensure that the transactions were executed at aggregate prices that were fair and reasonable. Effective June 28, 2004, the NASD approved a letter of acceptance, waiver and consent ("AWC") from Schwab. Without admitting or denying guilt, Schwab agreed to censure and a fine of \$30,000 and was required to pay \$30,869.25 plus interest in restitution to the customers. Schwab agreed to provide a copy of its updated written supervisory procedures as they relate to the determination of the fair market value of municipal securities being bought or sold from a public customer to the NASD within 90 days of the acceptance of the AWC.

## Account Review

Your IA is responsible for ongoing monitoring of your asset allocation and investment objectives, and each MM's performance. Schwab does not conduct periodic reviews of client accounts. If material changes occur to your financial circumstances or investment objectives, or you wish to impose or modify restrictions on the management of your account, you should promptly notify your IA.

MMs monitor and review their clients' accounts pursuant to their own compliance and supervisory systems of account review. Schwab does not participate in and is not responsible for such review.

## Other Financial Industry Activities and Affiliations

Schwab is primarily engaged in business as a broker-dealer and spends most of its time on that business. Schwab is registered as a broker-dealer under the Securities Exchange Act of 1934 and is a member of the Financial Industry Regulatory Authority ("FINRA"). Schwab provides brokerage services to clients located throughout the United States and, in some circumstances, outside the United States. Incidental to our broker-dealer business, we offer our clients a variety of investment information services and products, including seminars, periodicals, reports, guides, planning tools, brochures and other publications about securities and investment techniques. We also provide certain online data and financial reporting services.

Schwab is also registered as an investment advisor under the Investment Advisers Act of 1940. As sponsor of the Select and Access programs, Schwab is acting as both a registered investment advisor and broker-dealer. Schwab provides investment advisory services outside of the context of the Select and Access programs. With Schwab Advisor Network®, Schwab makes referrals of investment advisors to investors who are looking for assistance in managing their assets and/or other financial planning activities. Advisors participating in Schwab Advisor Network are independent and not affiliated with Schwab. Investment advisors pay a fee to participate in the Schwab Advisor Network program.

Schwab also acts as a registered investment advisor for other programs, including Schwab Managed Portfolios™ (a mutual fund and ETF wrap fee program) and Schwab Private Client™ (investment advisory and brokerage services), and when we provide financial planning services through the Schwab Personal Financial Plan™ Schwab Retirement Consultation, and Schwab Equity Compensation Consultation.

Schwab does not trade futures and is not a Futures Commission Merchant. However, for our customers that have a desire to trade futures, we have a referral relationship with a company that is not affiliated with Schwab. Per the terms of the referral relationship, Schwab receives a portion of the commissions that Schwab clients pay to that company.

### **Schwab Affiliates**

Schwab is a wholly owned subsidiary of CSCorp, a Delaware corporation that is publicly traded and listed on the NASDAQ (symbol: SCHW).

Other wholly owned subsidiaries of CSCorp are engaged in investment advisory, brokerage, trust, custody or banking services. CSIM, in addition to providing MM services in the Access program and the Managed Account Connection™ program (a wrap fee program available to Schwab retail clients) ("Connection"), provides advisory and administrative services to certain proprietary mutual funds marketed under the Schwab Funds® name and under the Laudus® name. Windhaven® is an affiliate of Schwab that provides MM services in the Access and Connection programs as well as MM and investment advisory services to other clients. CSIA is an affiliate of Schwab that is described above under the heading "About CSIA."

In addition, Schwab has several affiliates and/or units engaged in various aspects of the retirement plan business. The Charles Schwab Trust Company ("CSTC"), a California-chartered trust company, provides custodial and other trust services to Schwab customers and affiliates in relation to retirement plans, including 401(k) plans. The Schwab Corporate & Retirement Services division provides custodial services and administrative and recordkeeping support to Schwab corporate customers and their employees in connection with retirement and stock option plans and the monitoring of trading in employee accounts.

CSIA is a registered investment advisor and an affiliate of Schwab that provides research and decision-making tools to Schwab for use by Schwab clients, including the *Mutual Fund OneSource Select List*®. In addition to providing MM research and evaluation services for the Select program, CSIA personnel also act as portfolio managers for Schwab Managed Portfolios™ which is a mutual fund and ETF wrap-fee program sponsored by Schwab.

Charles Schwab Bank ("Schwab Bank") is a subsidiary of CSCorp that offers deposit accounts, mortgage and home equity line of credit lending products, and credit card products to both Schwab brokerage clients and other clients who have no relationship with Schwab.

### **Code of Ethics, Participation or Interest in Client Transactions and Personal Trading**

#### **Code of Ethics**

Schwab has various ethical standards, including a code of ethics adopted pursuant to SEC Rule 204A-1 under the Investment Advisers Act of 1940 (the "Code"). The Code is intended to reflect fiduciary

principles that govern the conduct of Schwab and its supervised persons in those situations where Schwab acts as an investment adviser as defined under the Investment Advisers Act of 1940 in providing investment advice to clients. As a general matter, the Code requires that Schwab's supervised persons comply with applicable federal securities laws, report violations of the Code, and (for supervised persons who are deemed "access persons" by virtue of their involvement in providing investment advice or access to certain related information) report their personal transactions and holdings in certain securities periodically and get pre-clearance before buying certain securities, including an initial public offering or private offering. The Code is subject to change as necessary to remain current with regulatory requirements and internal business policies and procedures. A copy of Schwab's Code is available on request.

Schwab has imposed policy restrictions on all personnel with respect to transactions for their own accounts and accounts over which they have control or a beneficial interest. These include restrictions on employee purchases of stocks on the "Restricted List," which includes securities for which Schwab is engaged in certain activities involving public offerings. Employee trading restrictions also prohibit unacceptable trading practices such as front running, crossing trades with customers, and insider trading.

#### **Schwab's Participation or Interest in Client Transactions**

Consistent with applicable law and regulation, Schwab may execute principal trades for fixed income securities in the programs; Schwab will not execute equity trades as principal and will not execute fixed income trades as principal for accounts managed by affiliated MMs. Schwab will execute principal transactions for your fixed income account only when an MM believes you will receive at least as favorable execution as would be the case were the transaction executed through another dealer. Schwab executes orders in fixed income securities from MMs as principal. Schwab may receive compensation in connection with such transactions in the form of a dealer markup or markdown. Such compensation is separate from and in addition to, and will not reduce or otherwise offset, the program fee for your account. Please refer to "Schwab's Execution Services" under "Services, Fees and Compensation" above for more information.

Schwab also may effect agency cross trades with accounts in the programs (except Access accounts managed by CSIM and Windhaven) to the extent permitted by applicable law and regulations and Schwab's internal policies. "Agency cross trades" are transactions in which Schwab acts as broker for the parties on both sides of the transaction. Schwab may receive compensation from the client on the other side of the transaction (the amount of which may vary). Thus, Schwab may have a potentially conflicting division of loyalties and responsibilities. If Schwab effects an agency cross transaction for your account, the confirmation for the transaction will disclose that Schwab acted as agent for both buyer and seller in the transaction. The compensation received by Schwab from the other client is in addition to the program fee described above. While such compensation, in theory, could create a potentially conflicting division of loyalties and responsibilities, all transactions under the programs are directed by either you or the MM (or the IA if you have granted the IA trading authority), and Schwab will be acting solely as a broker-dealer in connection with such trades.

If your MM buys new-issue bonds through Schwab acting as a dealer, Schwab receives a customary selling concession for providing distribution and operational services, which ranges from less than 0.01% to 2% of the par value, or face amount, of the bond, depending on the product. The percentage rate of the selling concession may differ not only between different new-issue offerings, but also between different series and bond maturities within a single offering.

Schwab has entered into a fixed income dealer agreement with J.P. Morgan Securities Inc. ("J.P. Morgan") to purchase from J.P. Morgan, and sell to our clients acting as principal, certain new-issue fixed income securities from offerings in which J.P. Morgan acts as an underwriter or

a selling group member. Pursuant to this agreement, Schwab receives a portion—and, in some cases, all—of the relevant selling concession. The percentage of the selling concession received by Schwab depends upon the type of offering, the type of security, and the underwriting syndicate's arrangement with the issuer. Although Schwab's aggregate compensation for a particular offering increases with the number of securities in the offering that Schwab sells to its clients, the portion of the selling concession Schwab receives in an offering does not vary based upon the number of securities sold to its clients.

Schwab may offer discounts or preferential prices on materials and services ordinarily offered by Schwab through the programs or in its capacity as a broker-dealer to IAs whose clients are brokerage customers of Schwab.

Additionally, from time to time, Schwab offers certain of its employees the option of participating in incentive programs relating to referrals of potential investors to investment management firms which have participated or are participating in Schwab Advisor Network®, which may include IAs or MMs participating in the programs.

### Certain Risks

Investments in securities, both generally and in the context of the investment strategies available through the Select and Access programs, involve various risks, including those summarized below. In addition, each MM's investment style may involve risks different from or in addition to those summarized below. The profile for each Select MM includes several measures of volatility and other risk factors for that MM based on its past management of accounts; these may not necessarily indicate future risks. Please review the brochure and, for Select MMs, the MM Profile for each MM that you are considering for additional relevant disclosures.

### Equity Risks

**General.** The prices of equity securities rise and fall daily. These price movements may result from factors affecting individual companies, industries or the securities market as a whole. Individual companies may report poor results or be negatively affected by industry and/or economic trends and developments. The prices of securities issued by such companies may suffer a decline in response. In addition, the equity market tends to move in cycles which may cause stock prices to fall over short or extended periods of time.

**Large- and Mid-Cap Risk.** Investment strategies that focus on large- and/or mid-cap segments of the stock market involve the risk that these types of stocks tend to go in and out of favor based on market and economic conditions. However, stocks of mid-cap companies tend to be more volatile than those of large-cap companies because mid-cap companies tend to be more susceptible to adverse business or economic events than larger, more established companies. During a period when large- and mid-cap U.S. stocks fall behind other types of investments—bonds or small-cap stocks, for instance—the performance of investment strategies focused on large- and/or mid-cap stocks will lag the performance of investments in bonds or small-cap stocks.

**Small-Cap and International Risk.** Historically, small-cap and international stocks have been riskier than large- and mid-cap stocks. Stock prices of smaller companies may be based in substantial part on future expectations rather than current achievements and may move sharply, especially during market upturns and downturns. Small-cap companies themselves may be more vulnerable to adverse business or economic events than larger, more established companies, and international companies may be more vulnerable to geopolitical factors than U.S. companies. During a period when small-cap and/or international stocks fall behind other types of investments—bonds or large-cap stocks, for instance—the performance of investment strategies focused on small-cap or international stocks will lag the performance of bonds or large-cap stocks.

**Management Risk.** MMs generally make investment decisions for particular investment strategies using historical information. There is no guarantee that an investment strategy based on historical information will produce the desired results in the future. In addition, if market dynamics change, the effectiveness of that kind of strategy may be limited. Either of these risks may cause the investment strategy of a particular MM to underperform its benchmark or similar investment strategies managed by different MMs.

### Fixed Income Risks

**General.** Bond markets rise and fall daily, and fixed income investments are subject to various risks, including changes in interest rates. As with any investment whose performance is tied to these markets, the value of a managed account fixed income portfolio will fluctuate, which means that you could lose money.

**Interest Rate Risk.** When interest rates rise, bond prices usually fall, and with them the value of your portfolio. A fall in interest rates could hurt your portfolio by lowering its yield.

**State and Regional Factors.** To the extent that your fixed income portfolio is invested in securities from a given state or geographic region, its value and performance could be affected by local, state and regional factors, including erosion of the tax base and changes in the economic climate. National governmental actions, such as the elimination of tax-exempt status, also could affect performance. In addition, your portfolio may be more sensitive to adverse economic, business or political developments if a substantial portion of it is invested in municipal securities that are financing similar projects. Your portfolio may also have more exposure to the risks of a given issuer than a diversified bond fund.

**Credit Risk.** A decline in the credit quality of a fixed income investment could cause the value of your fixed income portfolio to fall. Your portfolio could lose money if the issuer or guarantor of a portfolio investment fails to make timely principal or interest payments or otherwise honor its obligations. The emphasis of a fixed income strategy on quality and preservation of capital also could cause your portfolio to underperform certain other types of bond investments, particularly those that take greater maturity and credit risks. Municipal securities may have greater risks than taxable bonds.

**Maturity Risk.** The MM's duration and maturity decisions will affect the value of your fixed income portfolio. To the extent that the MM anticipates interest rate trends imprecisely, your portfolio could miss yield opportunities or its value could fall.

**Tax Risk.** If tax-exempt securities purchased in your portfolio are later deemed to be taxable, a portion of your portfolio's income could be taxable. Any defensive investments in taxable securities could generate taxable income. Also, some types of municipal securities produce income that is subject to the federal alternative minimum tax (AMT). You should consult your tax advisor about the potential effects of the AMT on your tax situation.

**Liquidity Risk.** Some bonds, particularly municipal bonds, may be difficult to sell, and the last quoted price for a bond may be based on the last price at which the bond was traded, which may not accurately reflect the current market price. If you are enrolled in a fixed income strategy and are terminating your account, withdrawing funds from your account or otherwise taking action that may require the sale of one or more bonds in your account, the MM may need additional time to sell your bonds, especially if you own a small amount of bonds of one or more issuers. There can be no assurance as to how long it might take to sell your bonds, and the sale price may be substantially lower than the price you paid or the price at which the bond was previously traded.

**Default risk.** A bond issuer may be unable to make interest or principal payments, thereby resulting in a default. If this happens, the bond may have little or no value.



## Municipal Bond Ladder Strategy Risks

Municipal bond ladder strategies are generally subject to the same risks as listed under “Fixed Income Risks” above. In addition, depending on the types and amounts of securities within your ladder, a municipal bond ladder strategy may not ensure adequate diversification of your investment portfolio. If you include callable bonds within your ladder, these bonds may be called prior to maturity and you may be unable to reinvest the principal in a similar bond issue. A called bond may alter the schedule of principal and interest payments within your ladder. You and your IA must evaluate whether a municipal bond ladder and the securities held within it are consistent with your investment objectives, risk tolerance, and financial circumstances.

## ETF Strategy Risks

Shares of ETFs trade on the secondary market, and cannot be directly purchased from or redeemed by the Fund. Shares of ETFs may trade above or below their NAV. The per share NAV of an ETF is generally calculated at the end of each business day, and will generally fluctuate with changes in the market value of the ETF's holdings. The market prices of shares of ETFs, however, will generally fluctuate continuously throughout the trading day in accordance with the relative supply of, and demand for, the shares on the exchange on which such shares are listed, which may not correlate with NAV. The trading price of shares of an ETF may deviate significantly from the ETF's per-share NAV during periods of market volatility. Price differences may be due to the fact that supply and demand forces at work in the secondary trading market for shares of an ETF are closely related to, but not identical to, the same forces influencing the prices of the securities held by the ETF. ETFs are subject to secondary market trading risks. Shares of an ETF will be listed for trading on an exchange; however, there can be no assurance that an active or liquid trading market for them will develop or be maintained. There can be no assurance that the requirements of the exchange necessary to maintain the listing of the ETF shares will continue to be met or will remain unchanged.

Generally ETFs are created using direct exposure to the securities in the index (stocks, bonds, etc.). However, some ETFs provide market exposure through indirect means such as futures, options or structured products. In the case of a structured product, there may be counterparty risk associated with the issuers of the product.

## Windhaven® Strategy Risks

**Systematic or market risk:** Windhaven strategies are invested in the global capital markets and are exposed to these markets. This exposure includes a large number of asset classes with varying risk profiles. Windhaven applies a systematic risk management discipline based on the application of the Windhaven Global Asset Allocation Model to construct investment strategies that provide the balance between risk and return appropriate to three categories of risk tolerance. However, the individual securities in accounts managed by Windhaven are subject to the market risk associated with the asset class they represent. In addition, since Windhaven's strategies use exchange-traded products (“ETPs”) for exposure to the asset classes, it is possible that an ETP fails to track the underlying index properly.

**Model risk:** As mentioned above, the Windhaven Global Asset Allocation Model is a key component of the risk management discipline described above. The model will determine which asset classes are overweight in the strategies. Since no model is a perfect predictor of future market behavior, it is possible that the overweight positions may fail to add value to a portfolio for a period of time. If this turns out to be the case, the strategies could decline or rise despite the overweight holdings, since Windhaven strives to maintain some exposure to stocks, bonds, hard assets and currencies.

**Counterparty risk:** Windhaven invests primarily in ETFs and, on occasion, exchange-traded notes (“ETNs”). ETFs are subject to the same risks described under “ETF Strategy Risks” above. To the extent that Windhaven uses an ETN, accounts managed by Windhaven are exposed to the credit risk of the issuer.

Schwab Advisor Services™ serves independent investment advisors and includes the custody, trading, and support services of Charles Schwab & Co., Inc. Independent investment advisors are not owned by, affiliated with, or supervised by Schwab.