

**Item 1: Cover Page**

CHARLES SCHWAB INVESTMENT MANAGEMENT, INC.

211 Main Street  
San Francisco, CA 94105  
1-800-435-4000  
[www.CSIMfunds.com](http://www.CSIMfunds.com)

September 25, 2017

**This brochure provides information about the qualifications and business practices of Charles Schwab Investment Management, Inc. If you have any questions about the contents of this brochure, please contact us at 1-800-435-4000. The information in this brochure has not been approved or verified by the United States Securities and Exchange Commission (the “SEC”) or by any state securities authority. Registration with the SEC does not imply a certain level of skill or training.**

**Additional information about Charles Schwab Investment Management, Inc. is also available on the SEC’s website at [www.adviserinfo.sec.gov](http://www.adviserinfo.sec.gov).**

**Item 2: Summary of Material Changes** (As of March 30, 2017, since prior annual update on March 30, 2016)

- **Item 8.** CSIM has modified the discussion of certain risks currently disclosed in the brochure where CSIM believes that additional disclosure would be beneficial to investors in the current market environment.
- **Item 11.** CSIM has modified the discussion of its Code of Ethics currently disclosed in the brochure to incorporate certain changes that were made to the Code of Ethics.

### Item 3: Table of Contents

	Page
Item 1: Cover Page.....	1
Item 2: Material Changes.....	2
Item 3: Table of Contents.....	3
Item 4: Advisory Business.....	4
General.....	4
Managed Account Programs.....	4
Collective Trust Funds.....	5
Non-U.S. Fund.....	5
Item 5: Fees and Compensation.....	5
Item 6: Performance-Based Fees and Side-by-Side Management.....	6
Item 7: Types of Clients.....	6
Item 8: Methods of Analysis, Investment Strategies and Risk of Loss.....	7
Methods of Analysis and Investment Strategies.....	7
Material Risks.....	9
Item 9: Disciplinary Information.....	13
Item 10: Other Financial Industry Activities and Affiliations .....	15
Item 11: Code of Ethics, Participation or Interest in Client Transactions and Personal Trading.....	18
Code of Ethics.....	18
Participation or Interest in Client Transactions.....	19
Personal Trading.....	19
Item 12: Brokerage Practices.....	20
Selecting or Recommending Broker-Dealers.....	20
Directed Brokerage.....	22
Aggregation and Allocation of Securities Transactions.....	23
Item 13: Review of Accounts.....	24
Managed Account Programs.....	24
Collective Trust Funds.....	25
Non-U.S. Fund.....	25
Item 14: Client Referrals and Other Compensation.....	25
Item 15: Custody.....	25
Item 16: Investment Discretion.....	26
Item 17: Voting Client Securities.....	26
Item 18: Financial Information.....	28

## **Item 4: Advisory Business**

### General

Charles Schwab Investment Management, Inc., a Delaware corporation (“CSIM”), was founded in 1989 as a wholly-owned subsidiary of The Charles Schwab Corporation (“CSC”), a publicly held company.

CSIM provides advisory services to affiliated mutual funds, separately managed accounts participating in a wrap program, exchange-traded funds (“ETFs”), collective trust funds and one non-U.S. fund. As further described in Item 8, CSIM provides advice about a variety of investments, ranging from equity and fixed income to money market securities and also provides advice as to the selection of investment advisers and managed funds for certain clients.

As of December 31, 2016, CSIM managed approximately \$289,538,000,000 on a discretionary basis and approximately \$12,712,000,000 on a non-discretionary basis.

### Managed Account Programs

With respect to separately managed accounts, CSIM participates as an investment adviser in two managed account programs: the Managed Account Connection<sup>®</sup> program and the Managed Accounts Access<sup>®</sup> programs (collectively, the “Managed Account Programs”), sponsored by Charles Schwab & Co., Inc. (“Schwab”), an affiliate of CSIM. CSIM provides investment advice with respect to two equity strategies that are currently available to new clients: Large Cap Core Strategy and Dividend Equity Strategy.

As described further in Item 8, CSIM utilizes a disciplined quantitative and qualitative approach to identifying potential investments and uses Schwab’s proprietary stock research methodology as one of several inputs in the investment process to manage equity strategy client accounts; however, clients may request, subject to CSIM’s acceptance, that a particular security be excluded. Clients can also request that a particular security be sold in order to harvest capital gains or losses.

The strategies that CSIM uses to manage client accounts in the Managed Account Programs may also be used to manage mutual funds that CSIM advises. While CSIM advises certain mutual funds utilizing Schwab Equity Ratings similar to the strategies available in the Managed Account Programs, CSIM may rebalance the mutual funds’ holdings more frequently than those in the Managed Account Programs, which are generally rebalanced on a monthly basis, and such mutual funds are likely to have a greater number of holdings than strategies in the Managed Account Programs. Certain mutual funds have different comparative indices, which may result in a different universe of eligible securities. Furthermore, the mutual funds are registered under the Investment Company Act of 1940, as amended (the “1940 Act”), and CSIM must manage them within the limitations set forth by the 1940 Act. For example, mutual funds may be subject to industry concentration limits or issuer diversification requirements under the

1940 Act and diversification requirements under the United States Internal Revenue Code. By contrast an account managed for a Managed Account Program client may be significantly less diversified. As an investment adviser in the Managed Account Programs, CSIM receives a portion of the wrap fee that clients pay to Schwab for its services. Please see the disclosure brochure provided by Schwab for additional information about the wrap program.

#### Collective Trust Funds

CSIM provides non-discretionary investment management advice to Charles Schwab Bank (“CSB”), which is an affiliate of CSIM. CSB maintains and advises collective trust funds. CSIM makes recommendations to CSB on a non-discretionary basis relating to portfolio management, investment objectives and guidelines, asset allocation, sub-adviser selection, monitoring and termination, investing in underlying collective trust funds or mutual funds, broker selection and such other matters relating to the collective trust funds as CSB may request from time to time. As required by applicable law, CSB retains ultimate investment discretion over the collective trust funds and may follow or reject CSIM’s recommendations. CSIM tailors its recommendations to CSB based on a collective trust fund’s specific investment objectives and investment strategies as set forth in its governing and/or offering documents. A collective trust fund’s governing and/or offering documents may also impose restrictions on investing in certain securities or types of securities.

#### Non-U.S. Fund

CSIM also provides discretionary investment advisory services to Charles Schwab Asset Management (Ireland) Limited (“CSAMI”), an Irish limited liability management company under common control with CSIM, with respect to a non-U.S. investment vehicle managed by CSAMI. CSIM tailors its recommendations to the non-U.S. fund based on the non-U.S. fund’s specific investment objectives and investment strategies as set forth in its prospectus. The fund’s prospectus and applicable law may also impose restrictions on investing in certain securities or types of securities.

### **Item 5: Fees and Compensation**

As disclosed in Item 4, CSIM receives a fee from Schwab with respect to the advisory services CSIM provides as an investment adviser in the Managed Account Programs. Pursuant to an agreement between CSIM and Schwab, CSIM is entitled to receive an annual fee from Schwab, payable monthly, for assets managed under the Large Cap Core Strategy and Dividend Equity Strategy equal to 0.45% of such assets not in excess of \$100 million, 0.40% of such assets over \$100 million but not in excess of \$250 million, and 0.35% of such assets over \$250 million. As discussed in Item 4, CSIM manages certain mutual funds utilizing Schwab Equity Ratings similar to the strategies available in the Managed Account Programs. The total annual operating expenses for those mutual funds will generally be less for an investor than the total Managed Account Program annual fee.

As described in further detail in Schwab's disclosure brochure, the program fee for participation in the Managed Account Programs that clients pay to Schwab covers CSIM's asset management services. The fee also covers trade executions for transactions in equity securities executed through Schwab as agent. The program fee does not cover certain costs or charges imposed by third parties, including odd-lot differentials, American Depositary Receipt fees, exchange fees and transfer taxes mandated by law. Cash balances in Managed Account Connection are swept into a money market fund managed by CSIM. The program fee does not cover the expenses associated with an investment in the money market fund managed by CSIM; however, certain fees to which CSIM would be entitled as the investment manager to the money market fund may be rebated to certain clients to comply with the requirements of the Employee Retirement Income Security Act of 1974. CSIM does not provide any tax advice to any Managed Account Program clients.

Pursuant to an agreement between CSIM and CSB, CSIM is entitled to receive a fee from CSB based on the costs incurred by CSIM to provide the services, utilizing a cost allocation methodology agreed upon between CSIM and CSB. The fee is payable monthly to CSIM. Collective trust funds may incur custodian fees, brokerage fees and other transaction costs in connection with purchasing or selling securities recommended by CSIM and may also incur underlying fund expenses. CSIM's fees do not cover the costs of operating the collective trust funds in general, such as legal fees, audit expenses, and trustee's fees. Pursuant to an agreement between CSIM and CSAMI, CSIM is entitled to receive a fee based on a percentage of the assets under management for the non-U.S. fund. The non-U.S. fund will incur similar costs in connection with purchasing or selling securities and similar operating costs.

CSIM does not enter into agreements directly with Managed Account Program clients, collective trust funds or the non-U.S. fund and accordingly does not receive direct compensation from, or negotiate fees with, them.

For additional information relating to CSIM's brokerage practices, please see Item 12 below.

#### **Item 6: Performance-Based Fees and Side-by-Side Management**

Not applicable.

#### **Item 7: Types of Clients**

CSIM generally provides investment advice to individuals, non-profit organizations, pooled investment funds such as registered investment companies and non-U.S. funds, to trustees of collective trust funds, pension and profit sharing plans, retirement plans and business entities such as trusts, corporations and partnerships.

Managed Account Program clients must have a minimum account size of \$100,000 to participate in a CSIM managed equity strategy. This minimum is set by Schwab and not subject to waiver by CSIM.

## **Item 8: Methods of Analysis, Investment Strategies and Risk of Loss**

In managing discretionary client accounts and providing recommendations to non-discretionary clients, CSIM uses various investment strategies and methods of analysis, as described below. This Item also contains a discussion of the primary risks associated with these investment strategies, although it is not possible to identify all of the risks associated with investing and the particular risks applicable to a client account will depend on the nature of the account, its investment strategy or strategies and the types of securities held. Please refer to the applicable prospectus or other offering documents for a more detailed discussion of strategies and risks involved with your particular account.

While CSIM seeks to manage accounts so that risks are appropriate to the return potential for the strategy, it is often not possible or desirable to fully mitigate risks. Any investment includes the risk of loss and there can be no guarantee that a particular level of return will be achieved. Clients should understand that they could lose some or all of their investment and should be prepared to bear the risk of such potential losses.

Clients should be aware that while CSIM does not limit its advice to particular types of investments, mandates may be limited to certain types of securities (e.g., equities) or to the recommendation of investment advisers or managed funds and may not be diversified. The accounts managed by CSIM are generally not intended to provide a complete investment program for a client or investor and CSIM expects that the assets it manages do not represent all of the client's assets. Clients are responsible for appropriately diversifying their assets to guard against the risk of loss.

### Methods of Analysis and Investment Strategies

#### *Managed Account Equity Strategies*

For its Managed Account Program clients, CSIM uses a disciplined quantitative and qualitative approach to identifying potential investments and uses Schwab Equity Ratings®—Schwab's proprietary stock research methodology—as one of several inputs in the investment process. Schwab Equity Ratings represent Schwab's point-of-view on the 12-month performance outlook for approximately 3,000 of the largest (by market capitalization) stocks of issuers traded in the U.S. and headquartered or incorporated in the U.S. and in certain foreign nations where companies typically locate or incorporate for operational or tax reasons. Stocks are rated using a scale of "A," "B," "C," "D" and "F." Schwab's outlook is that "A" rated stocks, on average, will strongly outperform and "F" rated stocks, on average, will strongly underperform the equities market over the next 12 months. Schwab Equity Ratings are also available to Schwab brokerage account clients.

CSIM first identifies a universe of stocks based on the market capitalizations, sectors or other factors required by a particular strategy. Applying Schwab Equity Ratings, CSIM then typically purchases stocks rated “A” or “B” by Schwab Equity Ratings at the time of purchase. CSIM may purchase “C”-rated stocks for purposes of diversification or to help manage the volatility of the portfolio. Lower-rated securities may be purchased or held if CSIM believes it is necessary to continue holding the stock for purposes of diversification or to help manage the volatility of the portfolio. CSIM will consider the current market environment and any potential negative impact on the portfolio in determining when to sell a downgraded stock. Unrated stocks may also be purchased by CSIM to the extent it believes the purchases will help to manage the volatility of the portfolio or provide potential for capital appreciation. CSIM also takes into consideration other factors, such as sector and industry weightings, liquidity and turnover, seeking to construct a portfolio that it believes is appropriately diversified within the asset class represented by the strategy although, as discussed above, accounts may not be diversified across asset classes. CSIM continues to monitor and adjust the model portfolio while seeking to capture performance and manage overall risk. The model portfolio is generally rebalanced on approximately a monthly basis, which results in securities being bought or sold across all Managed Account Program client accounts.

#### *Collective Trust Funds*

CSIM provides non-discretionary investment advice to CSB with respect to collective trust funds that encompass a number of distinct investment strategies that are governed by each collective trust fund’s governing and/or offering documents. Such assistance includes periodic evaluation of the performance of third party sub-advisers to the collective trust funds, evaluation of compliance by the sub-advisers with any relevant policies and procedures, including best execution and other broker practices, and recommendations to select or terminate sub-advisers. When providing advice about the selection, monitoring and removal of sub-advisers to CSB, CSIM considers both qualitative and quantitative factors. Quantitative statistics considered include, but are not limited to, risk adjusted results over multiple time periods relative to peer groups and benchmarks, and return patterns in rising and falling markets. The qualitative review includes, but is not limited to, strategy philosophy and process, investment team, firm, institutional experience, portfolio characteristics, and fit with other sub-advisers in a portfolio context.

#### *Non-U.S. Fund*

In choosing securities for the Schwab U.S. Dollar Liquid Assets Fund, CSIM seeks to generate current income within the limit of the fund’s investment objective, credit, maturity, liquidity and diversification policies. CSIM’s credit research department analyzes and monitors the securities that the fund owns or is considering buying. CSIM may adjust the fund’s holdings or its average maturity based on actual or anticipated changes in interest rates or credit quality.



## Material Risks

### *Risks Applicable to Equity and Fixed Income Investments*

- *Investment Risk.* Investing in securities is subject to a number of risks, any of which could cause a client to lose money and clients should be prepared to bear the risk of such loss.
- *Management Risk.* CSIM applies its own investment techniques and risk analyses in making investment decisions or recommendations for its clients, but there can be no guarantee that they will produce the desired results. In addition, there is no guarantee that a strategy based on historical information will produce the desired results in the future and, if market dynamics change, the effectiveness of the strategy may be limited.
- *Market Risk.* Financial markets rise and fall in response to a variety of factors, sometimes rapidly and unpredictably. As with any investment whose performance is tied to these markets, the value of an investment in a client account will fluctuate, which means that an investor could lose money over short or long periods.
- *Asset Allocation Risk.* Asset allocation risk is the risk that the allocation of a client's assets among the various asset classes and market segments will cause the client's account to underperform other accounts with a similar investment objective but different allocations.
- *Liquidity Risk.* Liquidity risk exists when particular investments may be difficult to purchase, sell or value, especially during stressed market conditions. The market for certain investments may become illiquid due to specific adverse changes in the conditions of a particular issuer or under adverse market or economic conditions independent of the issuer. In addition, dealer inventories of certain securities – an indication of the ability of dealers to engage in “market making” – are at, or near, historic lows in relation to market size, which could potentially lead to decreased liquidity. In such cases, a client account with limitations on investments in illiquid securities may decline in value, experience lower returns and/or be unable to achieve its desired level of exposure to a certain issuer or sector due to such limitations and may have difficulty in readily purchasing and selling such securities at favorable times or prices. Further, transactions in illiquid securities may entail transaction costs that are higher than those for transactions in liquid securities.
- *Frequent Trading Risk.* CSIM's equity strategies in the Managed Account Programs may result in a client's account buying and selling portfolio securities actively as accounts are rebalanced on a periodic basis. Similarly, CSIM's recommendations to CSB may result in frequent trading by a collective trust fund, depending on the particular fund's investment objective. To the extent a client

account or fund engages in frequent trading, its portfolio turnover rate and transaction costs will rise, which may lower performance and may have tax consequences unless the securities are held in a tax-exempt account.

- *Foreign Investment Risk.* Investments in securities of foreign issuers may involve certain risks that are greater than those associated with investments in securities of U.S. issuers. These include risks of adverse changes in foreign economic, political, regulatory and other conditions; possible seizure, nationalization or expropriation of foreign deposits; the imposition of economic sanctions or other government restrictions; changes in currency exchange rates or exchange control regulations (including limitations on currency movements and exchanges); differing accounting, auditing, financial reporting and legal standards and practices; differing securities market structures; and higher transaction costs. In certain countries, legal remedies available to investors may be more limited than those available with respect to investments in the United States. The securities of some foreign companies may be less liquid and, at times, more volatile than securities of comparable U.S. companies. A client account with foreign investments may also experience more rapid or extreme changes in value as compared to a client account that invests solely in securities of U.S. companies because the securities markets of many foreign countries are relatively small, with a limited number of companies representing a small number of industries. In addition, economic sanctions or other government restrictions may negatively impact the value or liquidity of such investments, and could impair a client account's ability to meet its investment objective or invest in accordance with its investment strategy. There also is the risk that the cost of buying, selling, and holding foreign securities, including brokerage, tax, and custody costs, may be higher than those involved in domestic transactions. During any period when foreign securities underperform other types of investments—U.S. securities, for instance—the performance of an underlying fund that focuses its investments in foreign securities will lag these investments. These risks may be heightened in connection with investments in emerging markets. In addition, sovereign risk, or the risk that a government may become unwilling or unable to meet its loan obligations or guarantees, could increase the credit risk of financial institutions connected to that particular country.

#### *Equity Securities Investment Risks*

- *Equity Risk.* 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.

- *Schwab Equity Ratings.* The quality of Schwab Equity Ratings depends on the accuracy of the financial data provided by third parties, including the companies rated through the approach. Any stock selection discipline has its limitations. Given that systematic stock selection approaches cannot capture all of the dynamics that affect individual stock returns, Schwab Equity Ratings may not capture more-subjective, qualitative influences on return and risk such as management changes and pending lawsuits. Furthermore, the ratings may not reflect the possible impact of late-breaking news. The portfolio optimization process used by CSIM for its Managed Account Program clients to assist in constructing a client's portfolio does not assure successful investment. Securities selected with the assistance of the process may be negatively impacted by factors or events not foreseen in developing the process. As a result, a client may have a lower return than if the account were managed using another process or strategy.
- *Market Capitalization Risk.* Securities issued by companies of different market capitalizations tend to go in and out of favor based on market and economic conditions. In addition, there may be less trading volume in securities issued by mid- and small-cap companies than those issued by larger companies and, as a result, trading volatility may have a greater impact on the value of securities of mid- and small-cap companies. Securities issued by large-cap companies, on the other hand, may not be able to attain the high growth rates of some mid- and small-cap companies. During a period when securities of a particular market capitalization fall behind other types of investments a client account's performance could be impacted.
- *Large-Cap Company Risk.* Large-cap companies are generally more mature than smaller companies. They also may have fewer new market opportunities for their products or services, may focus resources on maintaining their market share, and may be unable to respond quickly to new competitive challenges. As a result, the securities issued by these companies may not be able to reach the same levels of growth as the securities issued by small- or mid-cap companies.
- *Mid-Cap Company Risk.* Mid-cap companies may be more vulnerable to adverse business or economic events than larger, more established companies and their securities may be riskier than those issued by large-cap companies. The value of securities issued by mid-cap companies may be based in substantial part on future expectations rather than current achievements and their prices may move sharply, especially during market upturns and downturns.

#### *Fixed Income Investment Risks*

- *Interest Rate Risk.* Interest rates rise and fall over time. During periods when interest rates are low or there are negative interest rates, a client account's yield and total return also may be low or the client account may be unable to maintain positive returns. Changes in interest rates also may affect the account's value: a rise in interest rates could cause the account's value to fall. The risk is greater

when an account holds fixed income securities with longer maturities. An account may also lose money if interest rates rise. The longer the account's duration, the more sensitive to interest rate movements its value is likely to be. For example an account with a longer portfolio duration is more likely to experience a decrease in its share price as interest rates rise. Certain countries have recently experienced negative interest rates on certain fixed-income instruments. A change in a central bank's monetary policy or improving economic conditions may result in an increase in interest rates. Rising interest rates may decrease liquidity in the fixed income securities markets, making it more difficult for CSIM to sell a client account's fixed income securities holdings at a time when CSIM might wish to sell such securities. In addition, decreased market liquidity also may make it more difficult to value some or all of the client account's fixed income securities holdings. In general, changing interest rates, including rates that fall below zero, could have unpredictable effects on markets and may expose fixed-income and related markets to heightened volatility. To the extent that CSIM anticipates interest rate trends imprecisely, an account could miss yield opportunities or its share price could fall.

- *Credit Risk.* A decline in the credit quality of a portfolio investment could cause a client's account to lose money or underperform. A client could lose money if the issuer or guarantor of a portfolio investment or the counterparty to a derivatives contract fails to make timely principal or interest payments or otherwise honor its obligations. The negative perceptions of an issuer's ability to make such payments could also cause the price of that investment to decline. The credit quality of a portfolio holding can change rapidly in certain market environments and any default on the part of a single portfolio investment could have a negative impact on the value of a client's account.
- *High Yield Risk.* High yield securities and unrated securities of similar credit quality (sometimes called junk bonds) are subject to greater levels of credit and liquidity risks. High yield securities are considered primarily speculative with respect to the issuer's continuing ability to make principal and interest payments. High-yield securities may be more volatile than higher-rated securities. An economic downturn or period of rising interest rates could adversely affect the market for these securities and reduce an account's ability to sell these securities (liquidity risk). If the issuer of a security is in default with respect to interest or principal payments, an account may lose its entire investment. Because of the risks involved in investing in high yield securities, an investment in an account that invests in such securities should be considered speculative.
- *Government Securities Risk.* Many U.S. government securities are not backed by the full faith and credit of the United States government, which means they are neither issued nor guaranteed by the U.S. Treasury. Certain issuers of securities such as The Federal National Mortgage Association (Fannie Mae), the Federal Home Loan Mortgage Corporation (Freddie Mac) Student Loan Marketing Association, Federal Home Loan Banks maintain limited lines of credit with the

U.S. Treasury. Securities issued by other issuers, such as the Federal Farm Credit Banks Funding Corporation, are supported solely by the credit of the issuer. There can be no assurance that the U.S. government will provide financial support to securities of its agencies and instrumentalities if it is not obligated to do so under law. Also, any government guarantees on securities an account owns do not extend to the account itself. Although the risk of default with U.S. government securities is considered unlikely, any default on the part of a portfolio investment could cause the account's yield to fall. On September 7, 2008, the U.S. Treasury announced a federal takeover of Fannie Mae and Freddie Mac, placing the two federal instrumentalities in conservatorship. The actions of the U.S. Treasury are intended to ensure that Fannie Mae and Freddie Mac maintain a positive net worth and meet their financial obligations, preventing mandatory triggering of receivership. No assurance can be given that the U.S. Treasury initiatives will be successful.

- *Prepayment and Extension Risk.* An investment in fixed income securities is subject to the risk that the securities may be paid off earlier or later than expected. Either situation could cause you to hold securities paying lower-than-market rates of interest, which could hurt an account's yield. In addition, rising interest rates tend to extend the duration of certain fixed income securities, making them more sensitive to changes in interest rates. As a result, in a period of rising interest rates, your account may exhibit additional volatility. This is known as extension risk. When interest rates decline, borrowers may pay off their fixed income securities sooner than expected. This can reduce the returns of an account because the account will have to reinvest that money at the lower prevailing interest rates. This is known as prepayment risk.
- *Counterparty Risk.* When CSIM enters into a repurchase agreement for a client account, the client's account is exposed to the risk that the other party (i.e., the counterparty) will not fulfill its contractual obligation. In a repurchase agreement, there exists the risk that, when the account buys a security from a counterparty that agrees to repurchase the security at an agreed upon price (usually higher) and time, the counterparty will not repurchase the security. These risks are magnified to the extent that a repurchase agreement is secured by collateral other than cash and government securities, such as debt securities and equity securities ("Alternative Collateral"). Alternative Collateral may be subject to greater price volatility and may be more volatile or less liquid than other types of collateral, increasing the risk that the account will be unable to recover fully in the event of counterparty's default.

## **Item 9: Disciplinary Information**

Charles Schwab & Co., Inc., Charles Schwab Investment Management, Inc. and/or Schwab Investments (together, "Schwab" for this Item 9 only) reached agreements with the United States Securities and Exchange Commission ("SEC"), the Financial Industry Regulatory Authority ("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 “Yield Plus Fund”) and/or Schwab Total Bond Market Fund (the “Bond Fund”).

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 Funds from 2005 through 2008. In particular, the SEC found that Schwab: (1) deviated from the Funds’ concentration policy with respect to investments in non-agency mortgage-backed securities, without shareholder approval; (2) made materially misleading statements and omissions about the Yield Plus Fund and its associated risks before and during the decline of its net asset value (“NAV”); (3) materially understated the Yield Plus Fund’s weighted average maturity (“WAM”) in certain instances; (4) willfully aided and abetted misstatements and omissions appearing in Yield Plus Fund sales materials and other documents; and (5) lacked policies and procedures reasonably designed to prevent the misuse of material nonpublic information about the Yield Plus Fund. Without admitting or denying these allegations, Schwab agreed to pay a total of approximately \$118,944,996 in disgorgement of fees, penalties and interest. The SEC settlement was approved by the U.S. District Court for the Northern District of California on February 16, 2011. As a result of the settlement with the SEC, Schwab retained an independent consultant to conduct a comprehensive review of Schwab’s policies, practices and procedures, including those related to material non-public information by or related to Schwab’s mutual funds. Schwab has taken a number of actions to improve its policies and procedures regarding, among other things, the protection of material non-public information related to Schwab’s mutual funds. Additionally, the SEC brought related complaints against two former employees of Schwab, and has reached settlements with both former employees.

The amount paid by Schwab pursuant to the SEC settlement includes approximately \$18,000,000 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 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 the maintenance of written procedures reasonably designed to comply with securities laws and regulations. The amounts paid to Illinois were included in the settlement with the SEC.

Schwab 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. The amounts paid to Connecticut were included in the settlement with the SEC.

Schwab and certain affiliated entities and individuals (the “Schwab Parties”) were named as defendants in a number of Yield Plus 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’ claim regarding changes to the investment policy of the Yield Plus 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 agreements.

#### **Item 10: Other Financial Industry Activities and Affiliations**

##### *Charles Schwab & Co., Inc.*

CSIM is under common control with Schwab, which is both a registered broker-dealer and a registered investment adviser. Schwab serves as the principal underwriter for certain mutual funds managed by CSIM but does not receive any compensation in that capacity. However, Schwab may receive recordkeeping, shareholder servicing and other administrative servicing fees from the mutual funds managed by CSIM.

In addition, as described in Items 4 and 5 above, Schwab is the sponsor of the Managed Account Programs for which CSIM serves as an investment adviser and CSIM receives fees from Schwab for its services. CSIM uses Schwab to execute all brokerage transactions in equity securities for its Managed Account Program clients. Schwab effects these transactions on an agency basis and generally routes orders for equity securities to other broker-dealers that are not affiliated with Schwab or CSIM. CSIM pays Schwab an annual fee to obtain the Schwab Equity Ratings used in its management of the equity strategies in the Managed Account Programs and for certain mutual funds. If the Schwab Equity Ratings were no longer available, CSIM would need to significantly alter its methods of analysis for these accounts.

Schwab, which is also an insurance agency, offers certain funds managed by CSIM as part of its insurance product offerings.

CSIM also pays Schwab for the services of certain employees and for the facilities and equipment necessary to enable it to provide advisory services to clients.

Finally, Schwab sponsors, develops, coordinates the calculation of and maintains the Schwab 1000 Index. Pursuant to a licensing agreement between Schwab and CSIM, Schwab grants a license to a self-indexing ETF to use the Schwab 1000 Index and related

intellectual property at no cost to Schwab Strategic Trust or the self-indexing ETF. Schwab does not provide recommendations to the self-indexing ETF using the Schwab 1000 Index regarding the purchase or sale of specific securities. In addition, Schwab will not provide any information relating to changes to the Schwab 1000 Index methodology for the inclusion or exclusion of component securities or methodology for the calculation or the return of component securities to the self-indexing ETF, in advance of a public announcement of such changes by Schwab. The Schwab 1000 Index is used by another registered investment company managed by CSIM. The registered investment company, like the self-indexing ETF, seeks to track the performance of the Schwab 1000 Index by investing in the constituents of such index or a representative sample of such constituents of the index. Consistent with the self-indexing ETF's exemptive relief, the registered investment company will not engage in creation unit transactions with the self-indexing ETF.

Investment advisers recommended or selected by CSIM to act as sub-advisers for funds advised by CSIM, or investment advisers of mutual funds or ETFs in which the fund-of-funds that CSIM advises invest, may have a business relationship with Schwab whereby Schwab has agreed to make mutual funds advised by such advisers available through Schwab Mutual Fund OneSource platform and/or ETFs advised by such advisers available through Schwab ETF OneSource platform. Schwab receives fees from mutual funds, ETFs and/or their affiliates for the services Schwab provides in connection with Schwab Mutual Fund OneSource and Schwab ETF OneSource. CSIM does not take into consideration whether an adviser participates in these platforms when making its recommendations or selections. Schwab also makes available certain mutual funds and ETFs advised by CSIM through its Schwab Mutual Fund OneSource platform and Schwab ETF OneSource platform, respectively.

*Charles Schwab, Hong Kong, Ltd.*

Charles Schwab, Hong Kong, Ltd. has been appointed the Hong Kong representative of CSAMI and is authorized by CSAMI to receive requests from Hong Kong investors for subscriptions, redemptions and exchange of shares of the a non-U.S. fund advised by CSIM. Charles Schwab, Hong Kong, Ltd. is a registered securities dealer that is regulated by the Hong Kong securities and futures commission.

*Pooled Investment Vehicles*

CSIM provides investment advice to a number of registered investment companies, including mutual funds and ETFs, and a non-U.S. fund and may be deemed to control such funds, although CSIM disclaims any control relationship. CSIM also makes recommendations in connection with the management of certain collective trust funds although CSB retains ultimate investment discretion over those funds.

*Charles Schwab Investment Advisory, Inc.*

CSIM is under common control with Charles Schwab Investment Advisory, Inc., a



registered investment adviser (“CSIA”). CSIA participates as a portfolio manager in Schwab Managed Portfolios, a managed account program sponsored by Schwab. Pursuant to program parameters established by Schwab, CSIA establishes investment guidelines to create and manage portfolios of mutual funds and ETFs in several strategies. The model portfolios in this program include funds and/or ETFs managed by CSIM, for which CSIM receives investment advisory fees. Schwab, CSIM’s affiliate, has a financial interest in the funds and ETFs because it or its affiliates receive advisory and recordkeeping, shareholder servicing and other administrative servicing fees from the funds. Schwab also receives fees from third party funds (or their affiliates) in the model portfolios for record keeping, shareholder services, and other administrative services. The aggregate fees Schwab or its affiliates receive from the funds may be greater than the fees Schwab receives from third party funds. In connection with the Schwab Managed Portfolios program, CSIM provides Schwab and CSIA with composite performance reporting data resources and support, for which CSIM is paid a fee. CSIM pays CSIA an annual fee to obtain CSIA’s asset allocation models which are used in the management of certain mutual funds.

*Schwab Wealth Investment Advisory, Inc.*

CSIA provides portfolio management services to Schwab Intelligent Portfolios™ (“SIP”), an advisory program sponsored by Schwab Wealth Investment Advisory, Inc. (“SWIA”). CSIM is under common control with SWIA, a registered investment advisor and a wholly-owned subsidiary of The Charles Schwab Corporation. SIP offers clients investment strategies that consist of diversified portfolios of ETFs in a single account. Pursuant to asset allocations and ETF selection parameters established by SWIA, CSIA establishes investment strategies for SIP. SIP investment strategies may include ETFs managed by CSIM, for which CSIM receives investment advisory fees. SWIA also sponsors the Institutional Intelligent Portfolios™ (“IIP”), an automated investment management service. SWIA selects ETFs for use in IIP based on research and recommendations from CSIA, including ETFs managed by CSIM for which CSIM receives advisory fees.

*Windhaven Investment Management, Inc.*

CSIM is under common control with Windhaven Investment Management, Inc., a registered investment adviser (“Windhaven”). Windhaven manages portfolios comprised primarily of ETFs that are available as part of Schwab’s Managed Account Access wrap program. Further, Windhaven serves as an investment subadvisor to certain collective trust funds maintained and advised by CSB and monitored by CSIM. CSIM applies the same methods of analysis and standards in determining to recommend an affiliated investment adviser, such as Windhaven, as are applied when recommending an unaffiliated investment adviser.

*Charles Schwab Bank*

CSIM is under common control with CSB. As described above, CSIM provides

investment advice to CSB pursuant to an agreement between CSIM and CSB with respect to collective trust funds maintained and advised by CSB. CSB, however, retains the authority to accept or reject CSIM's recommendations. In addition, CSIM provides administrative services to, and receives compensation from, CSB. CSB provides custodial and other trust services to certain of Schwab's customers and affiliates. CSB provides directed trust and custody services to employee benefit or similar types of plans, and makes certain mutual funds advised by CSIM available to these clients.

#### *Charles Schwab Asset Management (Ireland) Limited*

As disclosed above, CSIM provides investment advisory services to, and receives compensation from CSAMI with respect to a non-U.S. investment vehicle managed by CSAMI.

### **Item 11: Code of Ethics, Participation or Interest in Client Transactions and Personal Trading**

#### Code of Ethics

##### *General*

CSIM has adopted a code of ethics (the "Code") pursuant to Rule 204A-1 under the Investment Advisers Act of 1940, as amended from time to time. The Code sets forth standards of business conduct that reflect CSIM's fiduciary obligations to its clients and requires CSIM employees to comply with all applicable laws, rules and regulations and promptly report any violation of the Code to a supervisor or CSIM's Chief Compliance Officer or his or her designee. The Code also requires CSIM's officers, directors, employees, contractors and any person who is determined to have access to nonpublic information regarding any client or CSIM ("access persons") to (i) report, and CSIM to review, personal securities transactions and securities holdings periodically, (ii) pre-clear transactions in covered securities, and (iii) confirm compliance with the provisions of the Code on a periodic basis. Covered securities do not include shares of registered non-affiliated open-end mutual funds (except for shares of ETFs), shares of non-affiliated unit investment trusts that invest exclusively in non-affiliated registered open-end investment companies (except those that trade as exchange traded products), direct obligations of the U.S. government, high quality short term debt instruments and affiliated money market funds. The Code may be changed as necessary to remain current with regulatory requirements and internal policies and procedures.

##### *Material Non-Public Information*

The Code prohibits access persons from disclosing portfolio transactions or any other material non-public information to anyone outside of CSIM, except as required to effect securities transactions for clients, and from using the material non-public information for personal profit or to cause others to profit. Employees are also prohibited from engaging in deceptive conduct in connection with the purchase or sale of securities for client

accounts.

### *Gifts and Business Entertainment*

CSIM access persons may not give or accept gifts or business entertainment that create a conflict of interest or the appearance of impropriety.

A client or prospective client may obtain a copy of CSIM's Code without charge by calling CSIM at (415) 667-7238.

### Participation or Interest in Client Transactions

CSIM or Schwab may recommend that a client purchase securities of CSC, the parent company of both CSIM and Schwab. Certain funds managed by CSIM may purchase securities in an underwriting in which Schwab participates, to the extent consistent with the 1940 Act and the rules and regulations thereunder. Schwab, as an insurance agency, may offer to advisory clients of CSIM insurance products that offer funds managed by CSIM as part of the insurance product offerings.

Certain mutual fund clients to which CSIM provides investment advice are fund-of-funds. Consistent with the funds of funds' investment objectives and strategies, CSIM may recommend that these funds allocate a portion of their portfolios to other funds advised by CSIM for which CSIM receives investment advisory fees. CSIM has policies and procedures in place to establish appropriate controls to identify, and to limit use and distribution of, confidential information about the firm, its businesses and its clients. CSIM does not receive investment management fees from many of the registered fund-of-funds that it manages. For those funds-of-funds that do pay CSIM an investment management fee, the Board of Trustees of such funds meets annually to determine that the amount of the fee is appropriate given the services provided by CSIM. Similarly, CSIM may recommend that certain collective trust funds advised by CSB invest in other collective trust funds advised by CSB.

### Personal Trading

Schwab, a related person of CSIM, is a registered broker/dealer that effects securities transactions for its brokerage customers. Schwab may act as a principal or agent in these transactions. Pursuant to agreements between Schwab and clients participating in the Managed Account Programs, Schwab may effect equity securities transactions for such clients but will only do so on an agency basis. Compensation Schwab receives from Managed Account Program clients is the wrap fee the clients pay to participate in the program. In the normal course of the conduct of its business as a broker/dealer, Schwab may enter into purchase and sale transactions in securities that CSIM has recommended to its clients.

CSC, Schwab and CSB may invest for the benefit of their own accounts in the same securities that CSIM recommends to its clients. These affiliates may buy or sell securities at the same time that CSIM clients are buying or selling the same security and

may take positions that are the same or contrary to one that CSIM has recommended. In addition, directors, officers and employees of CSIM may buy or sell for themselves (through personal accounts or through accounts of which they are direct or indirect beneficiaries) securities that are also recommended to, or purchased or sold on behalf of, clients.

CSIM and its affiliates have established policies and procedures designed to prevent the exchange of information between employees at each organization relating to securities holdings and possible trades. Additionally, the personal securities transactions of CSIM's access persons are subject to the Code, which is designed to detect and mitigate or prevent conflicts of interest and unlawful practices that may arise in connection with an access person's personal securities transactions. For example, as described above, the Code requires periodic reporting and review of personal securities transactions and securities holdings. Furthermore, the Code requires access persons to obtain prior approval from CSIM compliance prior to engaging in a security transaction except for certain types of transactions deemed not to present conflicts of interest with CSIM's advisory activities on behalf of its clients ("Exempted Transactions"), such as purchases pursuant to an automatic investment plan. Access persons are restricted from executing personal transactions in securities, except for Exempted Transactions, when they know or should have known at the time that there is a pending "buy" or "sell" order in the same security for any client account. Portfolio managers, research analysts and credit analysts are subject to a blackout period of 7 calendar days for both when a security is traded, or is expected to be traded on behalf of a client account and after a security has been traded on behalf of a client. In addition, certain access persons are prohibited from realizing a profit from purchasing and selling, or selling and purchasing, the same security on a short term basis. All access persons are also restricted from executing a personal transaction in securities when the access person has material non-public information regarding the security or issuer, including affiliated money market funds. Certain personal transactions in securities may be subject to further review by CSIM's Chief Compliance Officer or his or her designee.

## **Item 12: Brokerage Practices**

### Selecting or Recommending Broker-Dealers

With the exception of the assets under the management of sub-advisers and Managed Account Program clients, CSIM is responsible for selecting brokers or dealers to execute transactions for client accounts. Brokerage for the portion of the collective trust funds' assets under the management of a particular sub-adviser is allocated by that sub-adviser, although the sub-advisers are subject to the oversight of CSIM. CSIM provides assistance to CSB with respect to policies and procedures relating to the selection and monitoring of collective trust fund brokers; however, the sub-advisers to the collective trust funds make the actual broker recommendation to CSB with respect to any particular transaction. With respect to its Managed Account Program clients, clients direct CSIM to only use Schwab to execute transactions in equity securities. Schwab generally routes the

orders for equity securities in the Managed Account Programs to other broker-dealers that are not affiliated with Schwab or CSIM.

CSIM seeks to obtain best execution for its clients' portfolio transactions. CSIM may take a number of factors into account in selecting brokers or dealers to execute these transactions. Such factors may include, without limitation, the following: execution price; brokerage commission or dealer spread; size or type of the transaction; nature or character of the markets; clearance or settlement capability; reputation; financial strength and stability of the broker or dealer; efficiency of execution and error resolution; block trading capabilities; willingness to execute related or unrelated difficult transactions in the future; order of call; ability to facilitate short selling; or provision of additional brokerage or research services or products. CSIM does not take into consideration sales of funds advised by CSIM when selecting a broker to effect a portfolio transaction; however, CSIM may execute through brokers that sell shares of funds advised by CSIM. In addition, CSIM may execute through Authorized Participants (institutional investors who have entered into an authorized participant agreement with the Schwab ETFs) for the Schwab ETFs or through Authorized Participants' affiliated broker-dealers.

CSIM generally will not enter into soft-dollar arrangements with brokers to obtain brokerage or research services in exchange for brokerage commissions paid by advised accounts. However, CSIM does receive various forms of eligible proprietary research that is bundled with brokerage services at no additional cost from certain of the brokers with whom CSIM executes equity or fixed income trades. These services or products may include: company financial data and economic data (e.g., unemployment, inflation rates and GDP figures), stock quotes, last sale prices and trading volumes, research reports analyzing the performance of a particular company or stock, access to websites that contain data about various securities markets, narrowly distributed trade magazines or technical journals covering specific industries, products, or issuers, seminars or conferences registration fees which provide substantive content relating to eligible research, discussions with research analysts or meetings with corporate executives which provide a means of obtaining oral advice on securities, markets or particular issuers, short-term custody related to effecting particular transactions and clearance and settlement of those trades, lines between the broker-dealer and order management systems operated by a third party vendor, dedicated lines between the broker-dealer and CSIM's order management system, dedicated lines providing direct dial-up service between CSIM and the trading desk at the broker-dealer, and message services used to transmit orders to broker-dealers for execution. CSIM may use research services furnished by brokers or dealers in servicing all client accounts, and not all services may necessarily be used in connection with the account that paid commissions or spreads to the broker or dealer providing such services.

CSIM does not currently cause a client to pay a higher commission in return for brokerage or research services or products to obtain research or other products or services. If CSIM elected to do so, CSIM would receive a benefit because it would not have to produce or pay for the research, products or services. Consequently, this would

create an incentive for CSIM to select or recommend a broker-dealer based on its interest in receiving the research or other products or services.

CSIM may purchase for clients new issues of securities in a fixed price offering. In these situations, the seller may be a member of the selling group that will, in addition to selling securities, provide CSIM with research services, in accordance with applicable rules and regulations permitting these types of arrangements. Generally, the seller will provide research “credits” in these situations at a rate that is higher than that which is available for typical secondary market transactions.

CSIM may place orders directly with electronic communications networks or other alternative trading systems. Placing orders with electronic communications networks or other alternative trading systems may enable clients to trade directly with other institutional holders. At times, this may allow clients to trade larger blocks than would be possible trading through a single market maker.

CSIM has established a Trade Management Policy Oversight Committee (“TMPOC”) to oversee trading practices, and has established policies and procedures applicable to best execution, soft dollars and other client commissions practices. The policies and procedures require CSIM portfolio management to obtain approval from the TMPOC for certain arrangements with a broker to obtain a research product or brokerage services. During its last fiscal year, CSIM did not pay commissions to a particular broker-dealer in return for brokerage and research services but, as noted above, may have executed through “full service” broker dealers at a rate higher than might otherwise be available.

In determining when and to what extent to use Schwab or any other affiliated broker-dealer as a broker for executing orders for clients, CSIM follows procedures that are designed to assure that affiliated brokerage commissions (if relevant) are reasonable and fair in comparison to unaffiliated brokerage commissions for comparable transactions.

#### Directed Brokerage

Clients with separate accounts under the Managed Account Programs agree in their account agreements with Schwab that all brokerage transactions for equity securities will be executed by Schwab. As a result, a client may not always obtain as favorable a price or execution as might have been available through another broker-dealer. Not all investment advisers require their clients to direct brokerage. Because Schwab receives a portion of the wrap fee for its brokerage and other services in the Managed Account Programs, CSIM and its affiliates may make more money than if CSIM provided its investment advisory services outside of the Managed Account Programs. Clients should consider that, depending upon the level of the wrap fee charged by Schwab, the amount of portfolio activity in the client’s account, the value of custodial and other services provided by Schwab, the wrap fee may or may not exceed the aggregate cost of such services if they were to be provided separately and if CSIM negotiated commissions and sought best price and execution on a transaction by transaction basis.

## Aggregation and Allocation of Securities Transactions

In certain market circumstances, CSIM may determine that its clients, which include registered investment companies and other advisory clients, are best served by placing one order on behalf of several of them. CSIM will not aggregate transactions if it determines that to do so (i) would be unfair or inequitable in the circumstances; (ii) is impractical; or (iii) is otherwise inappropriate in the circumstances. For Managed Account Program clients, CSIM will only block equity orders with equity orders for other clients in the Managed Account Programs and will not block such orders with clients outside of these programs. Clients may pay higher brokerage costs or otherwise receive less favorable prices or execution if CSIM does not aggregate trades when it has an opportunity to do so.

CSIM's aggregation and allocation guidelines are intended to ensure that trade allocations are timely, that no set of trade allocations is accomplished to unfairly advantage or disadvantage particular clients or types of clients and that, over time, client accounts are treated fairly and equitably, even though a specific trade may have the effect of benefiting one account against another when viewed in isolation. In connection with the aggregation of purchase and sale orders for two or more client accounts, the following requirements must be met:

- (1) CSIM shall not receive additional compensation or remuneration of any kind as a result of aggregating transactions for clients.
- (2) CSIM, for each client, must determine that the purchase or sale of each particular security involved is appropriate for the client and consistent with its investment objectives and its investment guidelines or restrictions.
- (3) Each client that participates in a block trade will participate at the average security price with all transaction costs shared on a pro-rata basis.
- (4) Client account information at CSIM must separately reflect the securities that have been bought, sold and held for each client.

For equity transactions, CSIM's portfolio management and trading departments determine whether aggregation is appropriate for orders received on the trading desk. Generally, mutual fund trade orders received at a contemporaneous point in time that contain the same security trading in the same direction (buy/sell) and which utilize the same trading strategy are candidates for aggregation. However, such trades will only be aggregated if the portfolio manager and trader believe that such aggregation is necessary and consistent with CSIM's duty to seek best execution. Portfolio managers and traders may determine other circumstances where it may be appropriate to aggregate trades across multiple fund accounts. Portfolio managers and traders may elect to aggregate orders not meeting the above criteria provided that such aggregation is determined to be in the best interest of each client account and consistent with CSIM's duty to seek best execution. Adjustments to the pro-rata allocation may be made to avoid having odd lots

of shares held in any client account, or to avoid conflicts with limitations established for a client.

CSIM portfolio management personnel are responsible for placing orders for fixed income securities transactions with broker-dealers. When orders for the same fixed income security for different client accounts are aggregated, they are generally allocated after execution. For fixed income and money market fund accounts that have similar strategies, allocations are determined with the general purpose of achieving, as nearly as possible, performance and portfolio characteristic parity/proportionality among such accounts over time. In addition to performance (gross yield), factors considered in making allocations may include, but are not limited to: (i) duration; (ii) sector weights relative to benchmarks; (iii) capacity available for a particular name or sector; (iv) cash flow / liquidity; (v) portfolio yield; and (vi) weighted average maturity or weighted average life. Similar money market fund accounts furthest from achieving performance and portfolio characteristic parity typically receive priority in allocations. For fixed income and money market fund accounts that do not have similar strategies, portfolio management personnel document target ranges for significant portfolio characteristics (“Target Ranges”) and allocations among such accounts are determined in accordance with the Target Ranges in effect at the time of the trade. Portfolio management personnel may give priority to a particular account in circumstances where the transaction is necessary to meet that account’s investment objective, and may consider additional factors including, but not limited to: (i) the factors set forth for similar client accounts; (ii) alternative minimum tax; (iii) issuing state; (iv) tax exempt versus taxable income status of the security; and (v) portfolio characteristics of client accounts.

Any trade allocations in a manner other than as described above, other than adjustments to equity pro rata allocations to avoid odd lots or partial executions, must be made in accordance with CSIM’s policies and procedures.

### **Item 13: Review of Accounts**

#### **Managed Account Programs**

CSIM will review, at least quarterly, the performance of clients’ separate accounts measured against their appropriate benchmarks, including the account composite. Schwab will contact clients participating in the Managed Account Connection program, and a client’s investment adviser will contact clients participating in the Managed Account Access program, at least annually to determine whether there have been any changes in the client’s financial situation or investment objectives and whether the client wishes to impose any reasonable restrictions on the management of the account or reasonably modify existing restrictions. For clients participating in the Managed Account Connection program, Schwab will communicate this information to CSIM’s portfolio managers as necessary for the management of the account. For clients participating in the Managed Account Access program, the investment adviser will communicate this information to CSIM’s portfolio managers (or Schwab will relay it to CSIM) as necessary



for the management of the account. CSIM may also review client accounts as a result of market events or vendor errors.

### Collective Trust Funds

A team of investment professionals are responsible for overseeing the sub-advisers to collective trust funds maintained and advised by CSB. The team monitors each collective trust fund for asset allocation, sub-adviser performance and sub-adviser exposure as compared to the fund's guidelines on a daily basis, with additional meetings or reviews on monthly basis. CSIM meets with CSB at least quarterly to review sub-adviser performance, provide updates relating to general economic conditions and matters related to the collective trust funds and to recommend changes when deemed appropriate. CSIM portfolio managers also perform reviews on an as needed basis such as to conduct new asset class or sub-adviser searches.

### Non-U.S. Fund

The portfolio managers and officers of CSIM review the performance of the non-U.S. fund at least quarterly and report on performance to the board of directors of the non-U.S. fund. These reviews and reports include analysis of adherence to the fund's objective and policies, fund performance and other matters relating to CSIM's management of the fund. In addition, CSIM provides information to CSAMI on a monthly basis, including a compliance checklist and performance summary, that is included as part of CSAMI's monthly management report to the board of directors.

## **Item 14: Client Referrals and Other Compensation**

As described in Item 5 above, CSIM receives payments from Schwab in connection with managing separate accounts under the Managed Account Programs. Schwab pays certain of its employees compensation based on the value of certain client or shareholder assets invested during a specified period of time in separate accounts and registered investment companies managed by CSIM. Consequently, these employees may have an incentive to recommend CSIM advised registered investment companies and programs over other types of accounts.

## **Item 15: Custody**

Managed Account Program clients receive quarterly (or more frequent) account statements from Schwab detailing account positions and activities during the preceding period. Account statements will include a summary of all transactions made on behalf of the account, all contributions and withdrawals made to or from the account, all fees and expenses charged to the account, and the value of the account at the beginning and end of the period. Managed Account Program clients should carefully review any account statements they receive from Schwab.

## **Item 16: Investment Discretion**

As described in Item 4, subject to CSIM's acceptance, a Managed Account Program client can request that a particular security be excluded. Managed Account Program clients may also elect to retain proxy voting authority for their accounts. Managed Account Program clients appoint CSIM as the money manager for their accounts in their Schwab Managed Account Services account application. By signing the application, clients designate CSIM to manage their accounts according to the terms and conditions set forth in the Account Application Agreement, which includes trading authority over their accounts, voting proxies, investment restrictions and taking other actions regarding investments held in their accounts. Clients wishing to retain the ability to vote proxies must submit a separate form to Schwab that may be obtained from their Schwab Financial Consultant who then communicates this to CSIM. As described in Item 12, all transactions in equity securities for a Managed Account Program client must be executed through Schwab and CSIM does not have discretion to use another broker.

CSIM has investment discretion over the non-U.S. fund pursuant to an investment management agreement between CSAMI and CSIM. As described in Item 4, CSIM manages the fund in accordance with its prospectus. CSAMI and/or the board of directors of the fund may also place additional restrictions on CSIM's investment discretion.

## **Item 17: Voting Client Securities**

The following is a summary of CSIM's Proxy Voting Policy and Procedures (the "Procedures") concerning proxies voted by CSIM on behalf of each investment advisory client who delegates voting authority to CSIM ("Delegating Client"). The Procedures may be changed as necessary to comply with regulatory requirements and internal policies and procedures and are designed to ensure that proxies are voted in the best interest of clients and to reduce potential conflicts of interest. As described in Item 16, Managed Account Program clients may choose to retain the authority to vote proxies with respect to their accounts.

It is CSIM's policy to vote proxies in the manner that CSIM and CSIM's Proxy Committee (the "Committee") believe will maximize the value of the Delegating Clients' investments by protecting the long term best interests of Delegating Clients. CSIM believes that directors, as shareholders' elected representatives, are best positioned to oversee the management of companies in which its clients invest, thereby promoting and protecting its clients' long term interests. Therefore, CSIM will generally support a board of directors' recommendations unless concerns arise, such as the board's performance, accountability or management of conflicts of interests. CSIM invests on behalf of its clients in companies domiciled all over the world. Since corporate governance standards and best practices differ by country and jurisdiction, the market context is taken into account in the analysis of proposals. Furthermore, there are instances where CSIM may determine that voting is not in the best interests of its Delegating Clients (typically due to costs or to trading restrictions) and will refrain from submitting votes.

To assist CSIM and the overall proxy voting process, CSIM has elected to retain an unaffiliated third party proxy voting service as an expert in the proxy voting and corporate governance area (the “Service”). The services provided by the Service include in depth research, global issuer analysis and voting recommendations, as well as vote execution, reporting and record keeping. CSIM may also retain additional experts in the proxy voting and corporate governance area. CSIM reviews and evaluates the Service’s written proxy voting policies and procedures (the “Service’s Proxy Guidelines”). CSIM has adopted guidelines on key proposals, including election of directors, ratification of auditors, classified boards, majority/cumulative voting, proxy access, independent chair, executive compensation, equity compensation plans, employee stock purchase plans, shareholder rights plans, supermajority voting, preferred shares, mergers and acquisitions, environmental and social proposals, and political contributions. In circumstances other than key proposals, CSIM will utilize the Service’s Proxy Guidelines to vote proxies.

From time to time, client accounts may hold securities issued by a fund advised by CSIM (an “Affiliated Fund”) or securities issued by The Charles Schwab Corporation (“CSC”), CSIM’s parent company. Because CSIM has an inherent conflict of interest with respect to such proxies, the Committee will “echo vote” proxies solicited by an Affiliated Fund or by CSC, unless otherwise required by law. When required by law or applicable exemptive order, the Committee will also “echo vote” proxies of an unaffiliated mutual fund or ETF. Echo voting means that proxies for CSIM clients will be voted in the same proportion as proxies are voted by all of the other shareholders of the relevant issuer. Echo voting allows shares held by CSIM to count towards any necessary quorum without otherwise influencing the outcome of a proxy measure.

Except as described above for proxies solicited by Affiliated Funds or CSC and CSIM’s guidelines on key proposals, proxy issues that present material conflicts of interest between CSIM and/or any of its affiliates, and its clients, will be voted by the Service in accordance with the Procedures.

Voting proxies with respect to shares of foreign securities may involve significantly greater effort and corresponding cost than voting proxies with respect to domestic securities, due to the variety of regulatory schemes and corporate practices in foreign countries with respect to proxy voting. In consideration of the foregoing issues, the Service uses its best-efforts to vote foreign proxies. As part of its ongoing oversight, the Committee will monitor the voting of foreign proxies to determine whether all reasonable steps are taken to vote foreign proxies. If the Committee determines that the cost associated with the attempt to vote outweighs the potential benefits clients may derive from voting, the Committee may decide not to attempt to vote. To preserve liquidity and freedom of action, CSIM will not vote proxies solicited by foreign issuers in countries that impose restrictions on the sale of securities for a period of time before or after a shareholder meeting.

Where CSIM has delegated day-to-day investment management responsibilities to a sub-adviser, CSIM generally does not delegate proxy voting responsibility to the sub-adviser. However, each sub-adviser to whom proxy voting responsibility has been delegated will be required to review all proxy solicitation material and to exercise the voting rights associated with the securities it has been allocated in the best interest of each mutual fund or ETF and its shareholders, or other client. Prior to delegating the proxy voting responsibility, CSIM will review each sub-adviser's proxy voting policy to determine whether it believes each sub-adviser's proxy voting policy is generally consistent with the maximization of the value of CSIM's clients' investments by protecting the long term best interests of such clients.

A client may obtain a copy of CSIM's Procedures, or information regarding how his or her securities were voted, by calling CSIM at (415) 667-7238.

**Item 18: Financial Information**

Not applicable.