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August 7, 2018

By E-Mail and Overnight Courier

Paul Cellupica, Esq.
Deputy Director and Chief Counsel
Division of Investment Management
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-0506

Re: *Securities and Exchange Commission v. Charles Schwab & Co., Inc., Case No. 4:18-cv-03942-KAW (N.D.Cal. July 9, 2018)*

Dear Mr. Cellupica:

We are writing on behalf of Charles Schwab & Co., Inc. ("CS&Co." or the "Firm"), the defendant in the injunctive action captioned above brought by the Securities and Exchange Commission (the "Commission"). CS&Co. seeks the assurance of the staff of the Division of Investment Management ("Staff") that it would not recommend enforcement action to the Commission under Section 206(4) of the Investment Advisers Act of 1940 (the "Advisers Act"), or Rule 206(4)-3 thereunder (the "Rule"), if an investment adviser registered or required to be registered pursuant to Section 203 of the Advisers Act pays CS&Co. or any of its associated persons, as defined in Section 202(a)(17) of the Advisers Act, a cash payment directly or indirectly for the solicitation of advisory clients, notwithstanding the entry of final judgment as to CS&Co. by the U.S. District Court for the Northern District of California on July 9, 2018 (the "Final Judgment"), as described below. While the Final Judgment does not prohibit or suspend CS&Co. or any of its associated persons from being associated with or acting as an investment adviser (except as provided in Section 9(a) of the Investment Company Act of 1940 (the "Company Act")),[1] and does not relate to solicitation activities on behalf of any investment

[1] Under Section 9(a) of the Company Act, CS&Co. and its affiliated persons will, as a result of the Final Judgment, be prohibited from serving or acting as, among other things, an investment advisor or depositor of any registered investment company or principal underwriter for any registered open-end investment company or registered unit investment trust. CS&Co. and affiliated persons of CS&Co. who act in the capacities set forth in Section 9(a) of the Company Act have filed an application under Section 9(c) of the Company Act (the "Section 9(c) Application") requesting the Commission to issue both temporary and permanent orders exempting them, and CS&Co.'s future affiliated persons should any of them serve or act in any of the capacities set forth in Section 9(a) in the future

adviser, the Final Judgment may affect the ability of CS&Co. and its associated persons to receive such payments.

The Staff in many other instances has granted no-action relief under the Rule in similar circumstances.

BACKGROUND

CS&Co. is dually registered with the Commission as a broker-dealer and investment adviser. CS&Co. is a wholly owned indirect subsidiary of The Charles Schwab Corporation ("CS").

The Commission filed a complaint in federal district court relating to the above captioned proceeding (the "Complaint") alleging violations of Section 17(a) of the Securities Exchange Act of 1934 (the "Exchange Act") and Rule 17a-8 thereunder. As discussed below, CS&Co. consented to the entry of the Final Judgment, without admitting or denying the allegations made in the Complaint.

According to the Complaint, CS&Co. failed to file Suspicious Activity Reports ("SARs") on suspicious transactions by independent, third party investment advisers ("Advisers") that CS&Co. terminated from its custodial platform in violation of Section 17(a) of the Exchange Act and Rule 17a-8 thereunder. Such Advisers were not affiliated or associated with CS&Co. CS&Co. terminated the Advisers for engaging in activity CS&Co. determined violated its internal policies and presented risk to CS&Co. or its customers. The Complaint alleges (1) that CS&Co.'s failure to file SARs during the 2012-2013 time period resulted from its inconsistent implementation of policies and procedures for identifying reportable transactions under the SAR Rule (31 C.F.R. § 1023.320(a)) when CS&Co. investigated and terminated Advisers from its custodial platform; (2) although CS&Co. took steps to investigate and terminate Advisers, CS&Co. did not have clear or consistent policies for the types of activities for which SARs

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(together, the "Covered Persons"), from the restrictions of Section 9(a). On the basis of the representations and conditions contained in the Application, the Commission issued a notice and temporary order exempting the Covered Persons from the prohibitions of Section 9(a) of the Company Act resulting from the Final Judgment.

The Final Judgment also disqualifies CS&Co. and certain of its affiliates from acting in certain capacities under certain provisions of the Securities Act of 1933 and the rules and regulations thereunder, including Rule 506 of Regulation D. CS&Co. obtained a waiver of the disqualification from relying on Rule 506 of Regulation D that may arise with respect to CS&Co. or any other person as a result of the Final Judgment.

needed to be filed; and (3) in a number of cases in which Advisers were terminated and there was reason for CS&Co. to suspect fraudulent activity, CS&Co. applied an unreasonably high standard for determining whether to file a SAR on the suspicious transactions.

CS&Co. submitted an executed Consent of the Defendant Charles Schwab & Co., Inc. to Entry of Final Judgment (the "Consent"), which was presented to the U.S. District Court for the Northern District of California when the Commission filed its Complaint. In the Consent, solely for the purpose of proceedings brought by or on behalf of the Commission or in which the Commission is a party, CS&Co. consented to the entry of the Final Judgment without admitting or denying the allegations made in the above-captioned proceeding (except as to personal and subject matter jurisdiction, which were admitted).

The Final Judgment permanently restrains and enjoins CS&Co. from violating Section 17(a) of the Exchange Act and Rule 17a-8 thereunder and ordered CS&Co. to pay a civil penalty in the amount of $2,800,000.

DISCUSSION

Rule 206(4)-3 prohibits an investment adviser that is required to be registered under the Advisers Act from paying a cash fee, directly or indirectly, to any solicitor that has been permanently or temporarily enjoined by an order, judgment, or decree of a court of competent jurisdiction (among other disqualifying events) from engaging in or continuing any conduct or practice in connection with the purchase or sale of any security. The Final Judgment causes CS&Co. to be disqualified under the Rule, and accordingly, absent no-action or other relief, CS&Co. and its associated persons are unable to receive cash payments for the solicitation of advisory clients. In addition, because the Final Judgment is not a Commission order, CS&Co. cannot rely on the Staff's no-action letters, dated March 26 and July 3, 2003, to Dougherty & Company, LLC.

In the release adopting the Rule, the Commission stated that it "would entertain, and be prepared to grant in appropriate circumstances, requests for permission to engage as a solicitor a person subject to a statutory bar."[2] We respectfully submit that the circumstances present in this case are precisely the sort that warrant a grant of no-action relief.

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[2] *See Requirements Governing Payments of Cash Referral Fees by Investment Advisers*, Release No. IA-688 (July 12, 1979), 17 S.E.C. Docket (CCH) 1293, 1295, at note 10.

The Rule's proposing and adopting releases explain the Commission's purpose in including the disqualification provisions in the Rule – namely, to prevent an investment adviser from hiring as a solicitor a person whom the adviser would not be permitted to hire as an employee, thus doing indirectly what the adviser could not do directly. In the proposing release, the Commission stated that:

> [b]ecause it would be inappropriate for an investment adviser to be permitted to employ indirectly, as a solicitor, someone whom it might not be able to hire as an employee, the Rule prohibits payment of a referral fee to someone who . . . has engaged in any of the conduct set forth in Section 203(e) of the [Advisers] Act . . . and therefore could be the subject of a Commission order barring or suspending the right of such person to be associated with an investment adviser.[3]

The Final Judgment does not bar, suspend, or limit CS&Co. or any person currently associated with CS&Co. from acting in any capacity under the federal securities laws (except as provided in Section 9(a) of the Company Act).[4] CS&Co. has not been sanctioned for conduct in connection with the solicitation of advisory clients for investment advisers nor was any such activity at issue. Accordingly, consistent with the Commission's rationale in proposing and adopting the Rule, there is no reason to prohibit any investment adviser from paying CS&Co. or its associated persons for engaging in solicitation activities under the Rule.

In addition, the need for the no-action relief requested is neither theoretical nor speculative, but instead is concrete. CS&Co. is currently contractually entitled to receive cash compensation from certain investment advisers in connection with its solicitation of advisory clients for those advisers. The Staff previously has granted numerous requests for no-action relief from the disqualification provisions of the Rule to individuals and entities found by the Commission to have violated a wide range of federal securities laws and rules thereunder or permanently enjoined by courts of competent jurisdiction from engaging in or continuing any conduct or practice in connection with the purchase or sale of any security.[5]

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[3] *See Requirements Governing Payments of Cash Referral Fees by Investment Advisers*, Release No. IA-615 (Feb. 2, 1978), 14 S.E.C. Docket (CCH) 89, 91.

[4] *See supra* note 1.

[5] *See, e.g., Macquarie Capital (USA) Inc.*, SEC No-Action Letter (Jun. 1, 2017); *Stifel, Nicolaus & Company, Inc.*, SEC No-Action Letter (Dec. 6, 2016); *F. Porter Stansberry and Stansberry & Associates Investment Research LLC*, SEC No-Action Letter (Sept. 20, 2015); *JPMorgan Chase & Co.*, SEC No-Action Letter (May 20, 2015); *Royal*

UNDERTAKINGS

In connection with this request, CS&Co. undertakes that:

1. It, directly or indirectly, will conduct any cash solicitation arrangement entered into with any investment adviser registered or required to be registered under Section 203 of the Advisers Act in compliance with the terms of Rule 206(4)-3 as if CS&Co. were not a disqualified person for purposes of Rule 206(4)-3 by virtue of the Final Judgment;

2. The Final Judgment does not bar, suspend or limit CS&Co. or any person currently associated with CS&Co. from acting in any capacity under the federal securities laws (except as provided in Section 9(a) of the Company Act);

3. It has complied and will continue to comply with the terms of the Final Judgment, including, but not limited to, the Injunction and the payment of the civil monetary penalty; and

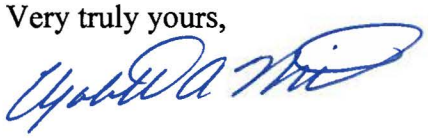
4. For ten (10) years from the date of the entry of the Final Judgment, CS&Co. and any person through whom CS&Co. directly or indirectly conducts its solicitation activities or any investment adviser with which it or any such person has a solicitation arrangement subject to Rule 206(4)-3 will disclose the Final Judgment in a written document that is delivered to each person whom CS&Co. or such persons solicit (a) not less than 48 hours before the person enters into a written or oral investment advisory contract with the investment adviser, or (b) at the time the person enters into such a contract, if the person has the right to terminate such contract without penalty within five business days after entering into the contract.

Bank of Canada, SEC No-Action Letter (Dec. 19, 2014); *Bank of America, N.A. and Merrill Lynch, Pierce, Fenner & Smith Incorporated*, SEC No-Action Letter (Nov. 25, 2014).

CONCLUSION

We respectfully request the Staff to advise us that it will not recommend enforcement action to the Commission if an investment adviser that is required to be registered with the Commission pays CS&Co. or its associated persons a cash payment for the solicitation of advisory clients, notwithstanding the Final Judgment.

Very truly yours,



Elizabeth A. Marino