

Compliance

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September 21, 2012

VIA EMAIL

Ronald W. Smith
Corporate Secretary
Municipal Securities Rulemaking Board
1900 Duke Street, Suite 600
Alexandria, VA 22314

RE: Comment Letter Regarding Concept Proposal to Strengthen Account Opening and Supervisory Practices of Dealers Effecting Online Municipal Securities Transactions with Individual Investors

Dear Mr. Smith:

Charles Schwab & Co. Inc. ("Schwab") appreciates the opportunity to comment on the Municipal Securities Rule Making Board's (the "MSRB") Notice 2012-41, which seeks comment on the MSRB's concept proposal to Strengthen Account Opening and Supervisory Practices of Dealers Effecting Online Municipal Securities Transactions with Individual Investors (the "Proposal").

Schwab's Position

Generally speaking, Schwab supports the stated intent of the Proposal, which as outlined seeks, "... [t]o improve the likelihood that individual investors who trade online would understand the features and risks of municipal securities and purchase securities that are appropriate based on their financial condition and risk tolerance." However, as explained below, we believe that certain key elements of the Proposal are not necessary to further the MSRB's stated intent or can be achieved more effectively and efficiently by alternate means.

Schwab requests clarification on the definition of Electronic Brokerage

Schwab understands that the definition of "electronic brokerage" is meant to encompass any dealer that effects online transactions in municipal securities with individual investors without any direct contact with a registered representative of the dealer, regardless of whether or not that same dealer also effects municipal securities transactions with individual investors via more traditional channels. As currently defined, the use of the term "solely" in the definition may lead the casual reader to assume that dealers that engage in municipal securities transactions with individual investors through multiple channels are excluded from the definition of "electronic brokerage."

Accordingly, we suggest deletion of the term "solely" from the "electronic brokerage" definition would serve to clarify the MSRB's intent.

Schwab supports making educational material available to investors, with the following modifications to the Proposal

Under the Proposal, dealers who operate an electronic brokerage would be required to deliver at account opening a municipal securities educational document to each individual investor containing important information about common features and risks of municipal securities.

Schwab believes investors should have the tools and resources available to make informed investment decisions.

While Schwab supports the MSRB's desire that individual investors have access to educational material related to municipal securities, requiring delivery of such documentation to clients within 10 days of account opening is impractical for the reasons stated below:

- It's Schwab's belief that the account opening process at most dealers does not require clients to inform the dealer of the channels they intend to use to effect securities transactions in the future. Furthermore, except for options accounts, dealers do not generally require clients to inform them of the types of securities in which they intend to invest. Under the Proposal, electronic brokerages would be required to deliver educational material to all clients who open accounts to ensure that anyone who might choose to transact in municipal securities online without direct contact with a registered representative in the future receives the required educational material. Requiring delivery of such material regardless of a client's future investment activity would likely render the material meaningless to the majority of clients who receive it, especially in light of all the other documentation that dealers are currently required to provide clients at account opening.

Schwab believes the following approach would achieve the MSRB's stated goal in a more efficient and effective manner:

- Schwab believes that it would be more effective to make such documentation available via a dealer's website and not subject to mandatory delivery by the dealer. Under this model, the availability of such documentation could be prominently displayed in a section of the dealer's site dedicated to municipal securities or investor education, and available to clients at all times. Clients who are interested in trading municipal securities online will have access to this material at any time, but more importantly during a time frame that is in close proximity to their municipal security trading activity.
- In addition, Schwab believes that in order to ensure that clients at all dealers have access to the same educational material; such documentation should be created by the MSRB and made available via the MSRB's Electronic Municipal Market Access (EMMA ®) website. Under this model, dealers would provide a direct hyperlink on their websites to EMMA where investors will be able to find not just educational material, but also ratings information, pricing history and material event disclosure documentation. It is Schwab's belief that most online investors are experienced users of the internet who prefer to access information online at a point in time when it is most useful. For clients who prefer to receive

a hard copy of the educational material, dealers can make this available upon request at no additional cost to the client.

Proposed requirement that electronic brokerages collect investment profile information for each individual investor unless they have determined that none of the municipal securities transactions executed with or on behalf of the customer would be recommended

Schwab believes that dealers should use reasonable efforts to obtain investor profile information prior to making a recommendation, regardless of the channel through which a recommendation is made. However, given rapid changes in technology and developments/enhancements in online brokerage, it would be difficult for a dealer engaged in electronic brokerage to determine at any point in time that none of its future online communications with a client will constitute a recommendation, especially if the communication is individually tailored. Accordingly, Schwab believes that each dealer should continue to have the flexibility to decide when, in view of the nature of its interactions with clients, it would need to collect sufficient investor profile information prior to making a recommendation.

Schwab also believes the MSRB should take this opportunity to harmonize the investor profile requirements of MSRB Rule G-19 and related interpretations with FINRA Rule 2111.

Proposed requirement that a municipal securities principal approve each new individual investor customer account prior to the first municipal securities transaction

Schwab does not believe that the proposal to have a municipal securities principal approve each new individual investor account prior to executing municipal securities transactions would further the MSRB's goal of investor protection. As noted above, clients are not generally required to inform dealers about their future investment plans at the time they open their accounts. Individual investors are required to provide dealers with certain information in order to meet basic account opening requirements. Subsequently, all such accounts are subject to supervisory review and approval prior to the commencement of trading. Since dealers do not generally know whether or not a client intends to trade municipal securities at the time of account opening, the only way to comply with this proposed requirement would be for dealers to subject all new accounts to approval by a municipal securities principal. Since all new accounts already are subject to a supervisory review and approval, it is not clear to Schwab what the added protection would be for the end client to require account approval by a municipal securities principal.

Furthermore, Schwab does not believe that the risks associated with investing in municipal securities necessitate a different supervisory review process related to account opening than is currently imposed by either the Securities and Exchange Commission or FINRA for other fixed income products.

In proposing an account opening process for municipal securities similar to the one currently in place for options accounts, the MSRB appears to be equating the risks of investing in municipal securities to that of options. While there are inherent risks

associated with investing in municipal securities (just like all investment products), these risks do not approach the risks associated with certain options investment strategies, under which an investor can lose more than their initial investment.

Proposed requirement that dealers offer to enroll clients in the EMMA alert service

Schwab believes that giving clients access to continuing disclosures submitted to EMMA by issuers is a valuable tool that will enable them to further monitor their investments. However, we would not support a requirement that the electronic brokerage would be responsible for collecting email addresses and enrolling clients in the EMMA alert service.

Schwab believes that the infrastructure required to implement the proposal does not currently exist at most dealers, would be costly to establish, and would ultimately be an unnecessary administrative burden. In addition, as clients tend to move their assets from dealer to dealer, there is the possibility that the delivery of such alerts could be interrupted or discontinued should the client transfer their assets to another dealer. As most online investors are experienced users of the internet, Schwab believes that a more practical approach would be to allow dealers to inform their clients of the availability of such alerts and to direct them to EMMA where they can enroll in the service themselves.

Proposals related to the requirement that electronic brokerages have written supervisory procedures in place to address recommendations, delivery of material information, and fair pricing

Schwab believes that electronic brokerages should have a supervisory system in place that is reasonably designed to ensure that investors, regardless of the channel they choose to transact their business, have access to material event disclosures, receive access to prices that are fair and reasonable, and receive suitable investment recommendations.

In MSRB Notice 2002-30 (the 2002 Notice) which addressed the application of MSRB Rule G-19, on suitability of recommendations and transactions, to online communications, the MSRB stated that "[w]hether or not a particular transaction is in fact recommended depends on an analysis of all the relevant facts and circumstances."¹ The MSRB went on to say in the 2002 Notice that "[t]he 'facts and circumstances' determination of whether a communication is a recommendation requires an analysis of the content, context, and presentation of the particular communication or set of communications. The determination of whether a recommendation has been made, moreover, is an objective rather than a subjective inquiry." To the extent that an electronic brokerage is making recommendations, Schwab believes that current rules already require that their supervisory systems to address how the dealer is meeting its suitability obligations pursuant to MSRB Rule G-19. If a dealer has made the determination that transactions executed through its online channel are in fact not recommended based on the analysis referenced

¹ See MSRB Notice 2002, Notice Regarding Application Of Rule G-19, On Suitability Of Recommendations And Transactions, To Online Communications.

above, then there is no added benefit to require dealers to establish written supervisory procedures to delineate under what circumstances municipal securities transactions affected online would be recommended.

Additional Questions Posed by the Proposal

Schwab encourages the MSRB to expressly exclude municipal fund securities from any rule proposal applicable to the sale of municipal securities by electronic brokerages

Dealers in municipal fund securities are required under MSRB Rule G-32 to deliver 529 Plan official disclosure documents to investors no later than the settlement of the transaction, and in fact, most dealers in municipal fund securities ensure that the 529 offering documents are made available to investors well before the time of investment, both electronically and as part of marketing materials. The 529 Plan offering documents are generally written using plain English disclosures and are all made accessible to the public through EMMA.² Furthermore, it is unlikely that investors associate an investment in a 529 Plan with a municipal security, and it seems far more likely that general municipal securities disclosures sent to a 529 Plan investor would add to investor confusion, rather than improving an investor's understanding of the risks associated with investments in a 529 Plan.

Additional Comments

While Schwab appreciates the fact that the MSRB is seeking industry input on this Proposal, Schwab believes that the MSRB should also take this opportunity to revise its interpretation provided in the 2002 Notice regarding the application of Rule G-19, on suitability of recommendations and transactions, to online communications. The online marketplace for trading municipal bonds has evolved a great deal since the 2002 Notice. Yet, industry participants are navigating this marketplace with guidance that has not evolved at the same pace. For example, the 2002 Notice appears to put forth the notion that due to the fact that since no municipal securities dealer can offer the "wide universe" of municipal securities for sale or purchase that this would somehow limit the ability of the dealer to make municipal securities available through an online channel on anything other than a recommended basis.

While Schwab does not dispute the fact that dealers cannot offer access to the entire universe of municipal securities, today through multiple online platforms, dealers are able to offer investors access to tens of thousands of municipal securities from hundreds of dealers. Investors are able search for municipal securities by unique features, and through dealer websites or EMMA have access to educational material, ratings information, research, historical pricing and material events disclosures. With these tools and information, investors are able to do their own research and make their own decisions as to which municipal securities are appropriate for them based on their financial condition and risk tolerance, without the assistance of a registered representative of the dealer. Guidance from the MSRB that recognizes the changes in

² In connection with this, we note that not all 529 Plans are considered municipal fund securities. For example, the Private College 529 PlanSM was established and is maintained by a consortium of private colleges, and is not a municipal fund security subject to MSRB regulations.

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the online marketplace and the resources available to investors therein will go a long way to ensuring investor protection and strengthening the marketplace.

Thank you for your consideration of the points we have raised in this letter and we hope that our comments are useful. Please feel free to contact me at (415) 667-0866 if you have any questions.

Sincerely,

Michael D. Mora
on behalf of Bari Havlik

Bari Havlik
Senior Vice President, Chief Compliance Officer
Charles Schwab & Co., Inc.