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May 16, 2008

SUBMITTED VIA EMAIL

Nancy M. Morris
Secretary
United States Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: File Number S7-10-00; Amendments to Form ADV

Dear Ms. Morris:

Charles Schwab & Co., Inc. ("Schwab") appreciates this opportunity to comment on the proposed amendments to Form ADV. Schwab strongly supports the Commission's goal of better plain-English disclosure with more effective delivery to customers. We also support the aspects of the rule proposal relating to electronic filing and clarification of record-keeping and filing requirements.

The Commission's re-proposal, however, does not sufficiently take into consideration recent developments reflecting the ongoing convergence of the investment advisory and broker-dealer regulatory models.[1] This results in two primary concerns.

First, the proposed Part 2B Brochure Supplement (The "Supplement") is duplicative of extensive regulatory disclosure already required under the Securities Exchange Act of 1934 and FINRA rules for dual registrants and their representatives. Through FINRA's BrokerCheck system, investors already have an easy way to receive a comprehensive report on their representative, whether that representative is providing an investment advisory or a brokerage service. The substantial additional burden and expense to track, compile, update, sort, and deliver essentially the same information in a

[1] The decision of the U.S. Court of Appeals for the D.C. Circuit in *Financial Planners Association v. Securities and Exchange Commission*, 482 F.3d 481 (2007) effectively abolished fee-based brokerage advice and led to dual-registrant firms offering their non-discretionary advice programs under the Advisers Act. The Commission recognized this significant change and the evolution of business trends over time with the adoption of final interim Temporary Rule 206(3)–3T, 72 Fed. Reg. 5502 (Sept. 28, 2007). As the SEC-commissioned RAND study recognized, the laws and regulations governing broker-dealers and investment advisers, respectively, "are based on distinctions between the two types of financial professionals that date back to the early 20th century and that . . . appear to be eroding today." Hung, Angela et al., *Investor and Industry Perspectives on Investment Advisers and Broker-Dealers* (2008) at 115 (RAND Study).

new format cannot be justified. Accordingly, the Commission should not adopt Part 2B or should exempt dual registrants or at least non-discretionary advisory programs whose representatives are already covered by BrokerCheck. As an alternative, the Commission should allow firms to include additional information in their firm disclosure brochure in lieu of the costly Supplement and to avoid the information overload investors already face.

Second, Form ADV Part 2A (the "Firm Brochure") and the annual and interim delivery obligations should be simplified. Nineteen categories of information are too many; resulting in a lengthy hard-to-read disclosure the RAND Study findings indicate investors won't read.[2] Given the RAND Study findings and the follow-up steps the Commission has promised, the Commission should refrain from adopting the current proposal and instead attempt to harmonize the key disclosure information for both broker-dealers and investment advisers in a shorter narrative format that would include notice of how to access additional, more detailed information online. The Commission's summary prospectus proposal and final rule for proxy delivery provide the right models to follow for Investment Advisers Act disclosures.

Below we discuss (1) the burdens of and alternatives to the Supplement, and (2) a unified, more effective and efficient notice and access disclosure model.

I. THE BURDEN OF THE SUPPLEMENT AND READY ALTERNATIVES FOR DUAL REGISTRANTS

A. <u>The Supplement Would Impose Substantial Unwarranted Costs and Burdens</u>

Schwab has estimated that it will cost us approximately $5 million to design, build and implement the systems necessary to comply with the Supplement requirement.[3] As detailed below, due to the complexity of preparing and delivering some 1600 different Supplements (one for each representative) in the right combinations to approximately 100,000 clients or households covering some 150,000 enrolled accounts, the price tag comes to about $3,125 per Supplement or $50 per Supplement package delivered to a

[2] RAND Study at 19, 117-118.

[3] If Schwab's estimated cost to compile 1600 individual Supplements is $5 million, the total cost to the industry with over 100,000 representatives covered by the rule change must be at least $100 million. The Commission's assumption that advisers will not "face substantial costs in gathering the required disclosure" (73 Fed. Reg. 13958, 13982, n. 271 (March 14, 2008)), fails to take account of the complexity of tracking, compiling, updating, sorting, and sending individualized information in one electronic database that today exists in diverse paper and electronic formats and files. Thus, the Commission's estimate of $21,981,182 in one-time first-year costs for preparing both the Firm Brochure ***and*** the Supplement ($14,723,982 in document preparation costs + $7,257,200 in outside legal fees) significantly underestimates the cost burden of the new Supplements. *See id.* at 13979, 13983.

client's household. In addition, there would be significant additional costs associated with the maintenance of the systems and the review of the disclosures.[4]

Schwab Private Client ("SPC") is Schwab's non-discretionary fee-based advisory service. Prior to October 2007 SPC was considered a fee-based brokerage program. Following the FPA vs. SEC decision, Schwab began delivering SPC under the Investment Advisers Act, although the program is essentially unchanged.

SPC clients are served by a team of three Schwab professionals: a local branch financial consultant; a centrally located portfolio consultant who helps implement the investment plan with individual buy and sell recommendations; and an associate portfolio consultant who meets day-to-day service needs but may make periodic trades. SPC clients seeking advice on individual fixed income securities may also receive recommendations from a member of a fixed income specialist team or a financial plan from a representative on a financial planning team. This team-based approach allows SPC clients to receive robust service and advice for an asset-based fee at 0.75% for equities and 0.50% for fixed income, with a reduced rate at higher asset levels.

SPC's team approach to advice delivery blends in-person local and national phone-based representatives. It was designed to create efficiencies for both Schwab and our clients. The approximately 1250 financial consultants, 200 portfolio consultants, and 140 associate portfolio consultants are organized into overlapping teams. For example, a financial consultant may have 70 of his clients enrolled in SPC and may have those clients assigned to 7 different portfolio consultants. Each portfolio consultant may service clients assigned to 20 different financial consultants. Add in the fixed income specialists and financial planners, and each client may have up to 5 different professionals on whom they rely for investment advice in this non-discretionary advice program.

As a result, there are ***thousands*** of team combinations of representatives serving clients in SPC, creating a tremendous challenge to collect, verify, update, organize, and distribute the right supplements to the right clients.[5] This would require 3 stages and three new or substantially redesigned systems.

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[4] We are assuming that the brochure supplement requirement for a supervised person who will "formulate investment advice for the client," proposed Rule 204-3(b)(2)(i), does not include representatives who perform basic asset allocation and recommend a managed account or a third-party adviser. It would be the money manager or third party adviser who would formulate the advice (i.e., buy-sell recommendations) and make discretionary investment decisions for the client in those advisory accounts – not the referring representative. Accordingly, it should be the money manager or third party adviser who provides a Supplement, not the referring representative. If our reading is not correct, the Commission should clarify, and the cost of complying with the Supplement requirement would increase significantly above what we detail in the discussion below.

[5] Given that the representatives covered by the Part 2B proposal number about 1600, it is impractical, likely more costly, and would defeat the purpose of good disclosure to create a single massive "supplement" to deliver to all clients.

Tracking. Although today's account records indicate which representatives are assigned to particular accounts, we will need to create a new electronic database system to facilitate the production of the 1600 unique Supplements. The system will need to capture new and changed account assignments for each representative who might provide advice to or interact with a particular client.

Compiling and Updating. Existing information on representatives currently compiled on employment applications and Forms U-4 and U-5 would need to be aggregated and stored in a database with an employee interface that allows periodic verification and updating of the information. In some respects each dual registrant firm would need to build on its own what FINRA already did for our industry. A second interface would need to be built to enable population of a Supplement template for each of the 1600 representatives. A method to review, proofread, and approve the 1600 Supplements on an ongoing basis would also be required.

Sorting and Sending. A third system would need to interface with the other two systems to select the correct Supplement bundle to be delivered to the correct clients. For most clients this could be 5 different Supplements, one for each of the representatives who might provide advice on the clients' enrolled accounts.

Actual mailing costs (around $150,000 for the initial mailing) would be trivial in comparison to the above systems work, which we estimate at approximately $5 million.[6] This does not include additional head count to administer the new systems, and review, proof and approve the 1,600 Supplements, which might be an additional 5 full-time employees at a cost of approximately $500,000 per year.

These substantial additional costs would place pressure on the very affordable pricing that makes available to many of our clients the additional advice and services in SPC. The proposing release did not examine this impact on a business model like Schwab's or the resulting effects on investor access to services and competition.

B. Supplement Would be Largely Redundant of FINRA's BrokerCheck, while other Relevant Information Could Be Included in the Firm Brochure.

The significant costs and burdens associated with a separate Supplement should be balanced by a commensurate benefit to clients. But the proposed disclosures: (1) are largely duplicative of publicly available information through BrokerCheck; (2) could easily be included in the Firm Brochure as applicable to all representatives; and (3) would add to the "information overload" investors already face.

[6] The mailing cost estimate is based on our experience mailing the SPC Disclosure Brochure to our clients when the program converted to Investment Advisers Act status following the FPA v. SEC decision.

1. FINRA's BrokerCheck Already Covers Most of the Supplement Information for Representatives of Dual Registrants

FINRA BrokerCheck presents information derived from FINRA's Central Registration Depository (CRD).[7] The CRD collects information in one database from registration forms including the U4 and U5. Information available to the public through BrokerCheck includes: registration with other firms; industry licenses held; investment adviser representative status in the various states; employment history; other business activities; and criminal, regulatory action, civil judicial, customer arbitration, and bankruptcy disclosures. The Commission approved this comprehensive investor disclosure regime, and FINRA has created an excellent and comprehensive tool for investors to easily search their representative and receive a printed report.

All 1600 Schwab representatives who help deliver investment advisory services to our clients are dually licensed as registered representatives and investment adviser representatives. They are already covered by BrokerCheck. To require a separate system under the Investment Advisers Act for representatives of dual registrants is redundant and unjustifiable, and has the potential of confusing investors by competing with BrokerCheck as a source of information. The Firm Brochure for dual registrants can simply direct an investor to BrokerCheck to learn more about the background of his or her representative.[8]

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[7] In the words of FINRA:

> FINRA BrokerCheck is a free online tool to help investors check the professional background of current and former FINRA-registered securities firms and brokers. It should be the first resource investors turn to when choosing whether to do business with a particular broker or brokerage firm.
>
> Features of FINRA BrokerCheck include:
>
> - Search capabilities for both a broker and brokerage firm
> - Online delivery of a report on a broker or brokerage firm
> - Explanatory information to help investors better understand the content, context and source of the information provided
> - Links to additional resources and tools
>
> The information made available through FINRA BrokerCheck is derived from the Central Registration Depository (CRD®), the securities industry online registration and licensing database, as reported on industry registration/licensing forms brokers, brokerage firms and regulators complete. BrokerCheck features professional background information on approximately 677,000 currently registered brokers and nearly 5,000 currently registered securities firms. Information is also available on thousands of formerly registered firms and brokers.

[8] This is consistent with NASD Rule 2280, which requires FINRA members to provide notice in writing once a year of FINRA's Public Disclosure Program hotline number, the FINRA website address, and the availability of an investor brochure that describes the Public Disclosure Program.

2. To the Extent BrokerCheck is Deemed Insufficient, Firms Should Be Able to Address Remaining Relevant Items in the Firm Brochure

Supplement Item 2: Educational Background and Business Experience

BrokerCheck lists the training of representatives in the form of industry licenses a representative holds, which at a minimum at Schwab is the Series 7 "General Securities Representative."[9] In addition, it is already the case that if a client asks a particular representative for his or her specific educational background and business experience, that representative has an obligation to answer truthfully. Given the burdens of the Supplement documented above, the Commission should refrain from over-regulating and mandating a universal requirement to repeat this information in a new document.

In terms of a non-discretionary advice service, clients are less dependent on the individual representative and therefore prior education and business experience is not as relevant. Clients who have chosen the non-discretionary model have explicitly reserved for themselves the final say over any decision pertaining to their accounts. At many firms, including Schwab, the recommendations that a representative makes are bound by advice policies and guidelines, including lists of recommendable securities in each investment category, subject to a supervised exception process. Such policies, guidelines, and recommendable lists are devised and approved by more senior firm executives whose backgrounds are already disclosed in the Firm Brochure.

In the very least the Commission should allow a burden-saving alternative under which a firm could disclose minimum educational and business experience requirements for representatives in the Firm Brochure, in lieu of the cost and trouble of creating and updating hundreds of individually-tailored Supplements.

Item 3: Disciplinary Information

As noted above, for representatives of a dual-registrant firm like Schwab this information is already available through BrokerCheck. Instead of the Supplement, the Commission could require dual registrants to note in their Firm Brochures information about FINRA BrokerCheck, including the web address.

Item 4: Other Business Activities
Item 5: Additional Compensation

BrokerCheck covers most of these topics as well. In terms of Item 4B, some firms do not allow their investment adviser representatives to engage in outside business

[9] The proposing release states that "the U.S. federal securities laws do not prescribe minimum experience or qualification requirements for persons providing investment advice." 73 Fed. Reg. 13958, 13958 (March 14, 2008). This appears to be the reason to include Supplement Item 2. Representatives of dual registrants, however, do have minimum qualification requirements administered by FINRA: the Series 7 General Securities Representative examination, and the Series 66 (or 65) Investment Adviser examination. Successful completion of both examinations is noted in BrokerCheck.

activities that provide a "substantial source of" income" or involve a "substantial amount" of representatives' time, away from the firm's advisory or brokerage activities. If so, a disclosure to that effect in the Firm Brochure should be sufficient. In terms of other registrations (one aspect of "other business activities"), a high percentage of representatives in our industry have dual registration (broker-dealer and investment adviser) and already disclose this fact on business cards and in written correspondence. It would be unnecessary and duplicative to require a separate Supplement to state it again.

How a representative is compensated is material (including whether compensation comes from third parties) and could give rise to conflicts of interest. But firms that already disclose their compensation plan elements and practices in the Firm Brochure should not be required to state it again in a Supplement.

Item 6: Supervision

The Supervision policy disclosures are also of questionable value or interest, especially to non-discretionary advisory clients. Requiring such a policy narrative would be inconsistent with the Commission's sensible decision elsewhere in the Release to omit disclosure of specific "Policies and Procedures" designed to address conflicts of interest. As the Release acknowledges in that context, a narrative description of such policies is likely either to be perfunctory or "lengthy, technical in nature, and difficult to read."[10] The same would be true in the case of supervisory policies.

A reasonable alternative is to require in the Firm Brochure a short explanation of how the firm supervises its representatives who deliver the advisory service. In terms of identifying the particular supervisor, for large firms like Schwab including a telephone number to call to obtain the name and phone number of the supervisor would be a reasonable approach that would avoid the burdens of tens of thousands of Supplements (industry-wide) each with a different supervisory phone number that would need to be updated on a frequent basis with job shifts and personnel changes.

3. Information Overload

Under the proposed rule, the Firm Brochure will consist of 19 general categories of information with a number of sub-parts. The Firm Brochure is already long under the existing rule. For example, at Schwab the SPC Disclosure Brochure is 14 double-columned pages. Even if plain-English, it is a lot of information for a typical investor to digest. On top of receiving and hopefully reading this information, an investor would also confront the Supplement with its additional 6 categories of information (with subparts), making the total package of disclosure even longer.

Schwab strongly agrees with the Commission's acknowledgement that lengthy and complex disclosures, even if accurate and well-written, do not always serve clients' interests. Any new set of disclosures, particularly disclosures in a separate new

[10] 73 Fed. Reg. 13958, 13960 (March 14, 2008).

document, therefore, should pass a strict test of real-world usefulness. A disclosure that does not pass this test only contributes to clutter, and to the discouraging observation from the RAND Study: "Few investors actually read" even the currently required disclosures.[11]

As detailed above, the Supplement fails this test.

C. Conclusion

The Commission should not adopt the Supplement requirement because it is not justified on a cost-benefit basis, or the Commission should adopt an exemption for dual registrants or at least for non-discretionary advisory programs. Alternatively, the Commission should allow dual registrant firms to rely on BrokerCheck and otherwise disclose general information in their Firm Brochure instead of mandating Supplements.[12]

II. A UNIFIED NOTICE AND ACCESS APRROACH WOULD BETTER INFORM INVESTORS, REDUCE BURDENS, AND BE MORE CONSISTENT WITH OTHER RECENT ACTIONS BY THE COMMISSION

The proposal essentially maintains the current disclosure system. This ignores key trends that the Commission itself has recognized: (1) the ongoing convergence of the investment advisory and brokerage industries leading to questions about how to harmonize the regulatory approach to assure fairness and investor choice and protection; (2) the RAND Study's findings that investors do not read today's current long disclosures that are written to comply with SEC requirements and avoid liability rather than to inform investors; and (3) "current levels of access to the Internet merit adoption of the notice and access model as an alternative."[13]

Although a narrative disclosure, as proposed, holds the promise of providing more meaningful plain-English information compared to a check-the-box government form, this is not necessarily the case. Under Rule 204-3 today, Firm Brochures are already too long. If the Commission were to consider a "Form BD Part 2" as part of harmonizing the regulatory schemes, the Form ADV Part 2 would not be the model to emulate. This warrants the Commission taking a fresh look at the scope of required content and its method of presentation and delivery and awaiting decisions on staff recommendations on options based on RAND Study findings before proceeding with a final rule.

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[11] RAND Study at 19.

[12] The Commission should also consider the potential for investor confusion, with disclosures about representatives through BrokerCheck being very similar to, but not quite the same, as the disclosures in the proposed Supplement (e.g., the respective time periods for which disciplinary events must be disclosed).

[13] Internet Availability of Proxy Materials, Release No. 34-55146, 72 Fed. Reg. 4148, 4149 (Jan. 29, 2007).

In terms of approach to content, the SEC's recent summary prospectus proposal, with its seven categories of information and 4 pages in length, is more effective.[14] Key to the summary prospectus is the ability to incorporate by reference a fuller disclosure statement available online. In the Investment Advisers Act context, a Summary Disclosure could contain a description of advisory services provided, the direct and indirect fees and compensation, and conflicts of interests. Additional items and details could be provided in the complete Firm Brochure.

At the point of sale (i.e., at the initiation of the advisory contract and relationship), investors generally would be more likely to read a concise Summary Disclosure, while those interested in the lengthier complete Firm Brochure could access it online or ask for a paper copy. For the annual delivery obligation, instead of the proposed step backward that would require industry-wide mailing of millions of additional lengthy documents each year, the Commission should adopt the notice and access approach it adopted a year ago for proxy materials. Recognizing widespread Internet availability and access, the Commission opted for the notice and access approach in the interest of cost-efficient disclosure.[15] The same rationale should apply here.

This approach would be both consistent with and enhance today's requirement that an adviser offer the Firm Brochure once a year. An amendment to Rule 204-3(c) could require firms to provide a notice once a year that an updated Firm Brochure is available on the firm's website, and include the web address along with a phone number to call to receive a free paper copy. The notice and access approach would also be sufficient to notify clients of any interim changes to disciplinary history.[16]

[14] Enhanced Disclosure and New Prospectus Delivery Option for Registered Open-End Management Investment Companies, Release No. 33-8861, IC-28064, 72 Fed. Reg. 67790 (Nov. 30, 2007).

[15] *See supra* note 13.

[16] Any material change to the investment advisory program itself would be handled by notice and delivery of an amendment to the investment advisory contract, with the further "backstop" of the Section 206 fiduciary and anti-fraud protections requiring disclosure of material facts regardless whether a specific rule requires it.

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Thank you for your consideration of the points we have raised in this letter. Please feel free to contact me to discuss them in more detail.

Very truly yours,

Christopher Gilkerson

cc: Chairman Christopher Cox
Commissioner Paul Atkins
Commissioner Kathleen Casey
Andrew Donohue, Director, Division of Investment Management
Robert Plaze, Associate Director, Division of Investment Management
David Blass, Assistant Director, Division of Investment Management
Daniel Kahl, Branch Chief, Division of Investment Management
Vivien Liu, Senior Counsel, Division of Investment Management