

# Futures Commission Merchant Firm Specific Disclosure Document

*Pursuant to CFTC Regulation 1.55(k)*

**(April, 2017)**

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## Disclosures

*(1) The futures commission merchant's name, address of its principal place of business, phone number, fax number, and email address.*

The name of the Futures Commission Merchant ("FCM") is optionsXpress, Inc. (referred to throughout as "optionsXpress," "the Firm," or "the FCM"). Its principal place of business is located at 150 S. Wacker Dr., 12<sup>th</sup> Floor, Chicago, IL 60606. Our telephone number for general inquiries is (888) 280-8020, and our facsimile number for general support services is (312) 629-5256. There is no general corporate email address, but email inquires can be submitted via an electronic form available at the "Contact Us" section of our public website ([www.optionsxpress.com](http://www.optionsxpress.com)).

*(2) The name, title, business address, business background, areas of responsibility, and the nature of the duties of each person that is defined as a principal of the futures commission merchant pursuant to Section 3.1 of Chapter I of Title 17 (Commodity Futures Trading Commission) of the Code of Federal Regulations.*

- a) Neesha Hathi, Executive Vice President, Investor Services, Charles Schwab & Co., Inc.<sup>1</sup>, 211 Main St, San Francisco, CA 94105. Ms. Hathi is a Director of optionsXpress, Inc. Ms. Hathi is the leader of digital platforms, including Schwab Intelligent Portfolios, and client experience for individual investors. Since joining Schwab, Ms. Hathi has held a range of leadership roles across the organization. She led Advisor Technology Solutions, delivering digital platforms and solutions to the over 7,000 registered independent advisors ("RIAs") that custody over \$1.1 trillion in client assets with Schwab, served as the COO of Schwab Performance Technologies®, and also led strategy and client experience teams that support Schwab's RIAs and other institutional clients. Prior to joining Schwab in 2004, Ms. Hathi led strategy, marketing and finance for various start-ups, including Enuvis, a developer of GPS technology for wireless devices and Kibu, a teen media company. She began her career in the field of investment banking, supporting the execution of initial and secondary public offerings and M&A transactions at PricewaterhouseCoopers and EVEREN Securities. Ms. Hathi earned a Bachelor's of Business Administration degree from the University of Michigan and a Master's of Business Administration degree from the Anderson School at the University of California, Los Angeles. She holds FINRA Series 7 and 24 licenses.
- b) Michael Canady, Senior Vice President, Finance, Charles Schwab & Co., Inc., 211 Main Street, San Francisco, CA 94105. Mr. Canady is a Director of optionsXpress, Inc. Mr. Canady oversees the financial results for Investor Services, Advisor Services, Retirement Plan Services, Client Solutions and support functions for the Firm. Prior to that he was the Chief of Staff for Charles M. Schwab, and also held roles in Investor Relations, Treasury, Corporate Development and Corporate Planning over the past 24 years with the Firm. Mr. Canady received a Bachelor of Arts degree from the University of California, Santa Barbara, majoring in Business Economics and Political Science. He also received an MBA from New York University with a double major in Finance and International Business. Mr. Canady holds a Series 27 license.
- c) Barry S. Metzger, Chief Executive Officer, optionsXpress, Inc., 150 S. Wacker Dr., 12th Floor, Chicago, IL 60606. As the CEO of optionsXpress, Mr. Metzger is responsible for both the

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<sup>1</sup> Charles Schwab & Co., Inc. ("Schwab") is an affiliated company of optionsXpress and is registered with the National Futures Association as an Introducing Broker for futures. Schwab is also a broker-dealer registered with the U.S. Securities and Exchange Commission, and a member of various securities exchanges and associations, including the Financial Industry Regulatory Authority, as well as the Securities Investor Protection Corp. ("SIPC").

ongoing operations of optionsXpress as well as the long-term, strategic development of Schwab's derivatives business. In addition, Mr. Metzger is responsible for the architecture and management of the corporate governance structure and is the liaison with the Schwab Institutional business. Mr. Metzger has been in this role since November 2014. Prior to this role, Mr. Metzger was the Chief Operating Officer of optionsXpress where he was responsible for the daily operations of the Firm, overseeing operations, futures, and international. Before that, Mr. Metzger was the CEO of brokersXpress, Inc., an affiliate of optionsXpress which was a broker-dealer that provided independent Registered Representatives, Financial Planners, and Registered Investment Advisors with a trading and clearing platform to service their clients. Prior to brokersXpress, Mr. Metzger worked in several roles at Morgan Stanley. Mr. Metzger is a graduate of the University of Illinois in Urbana-Champaign. He has an MBA degree from the Kellogg School of Management at Northwestern University. Mr. Metzger holds Series 7, 24, 27, 31, and 66 licenses.

- d) Lynn M. Konop, Vice President, Compliance Department, Charles Schwab & Co., Inc., 12401 Research Blvd, Austin, TX 78759. Ms. Konop is the Chief Compliance Officer ("CCO") of optionsXpress, Inc. As the CCO, Ms. Konop is responsible for managing the development, implementation, maintenance and administration of reasonably designed and effective compliance programs that meet Corporate Compliance standards and the requirements of the functional regulators of optionsXpress, including, but not limited to, the U.S. Commodity Futures Trading Commission ("CFTC"), National Futures Association ("NFA"), U.S. Securities and Exchange Commission ("SEC"), and the Financial Industry Regulatory Authority ("FINRA"). Lynn attended St. Peter's College where she received a degree in Marketing with a minor in Economics. Ms. Konop holds Series 4, 7, 9/10[8], 23, and 24 licenses.
- e) Daniel E. O'Neil, Vice President, optionsXpress, Inc., 150 S. Wacker Dr., 12<sup>th</sup> Floor, Chicago, IL 60606. Mr. O'Neil is the head of the futures business at optionsXpress, and futures designated supervisory principal ("DSP") at the Firm. Mr. O'Neil is responsible for the strategic direction, growth, and business of the FCM. Previously, Mr. O'Neil was a founder and principal of Xpresstrade, LLC, one of the first online futures trading firms and which was acquired by optionsXpress in 2007, and then served as Executive Vice President responsible for futures and forex at optionsXpress. Mr. O'Neil began his career in financial services as an independent trader on the floor of the Chicago Mercantile Exchange and then at the Chicago Board Options Exchange ("CBOE"). He also served as a risk manager and client relationship manager at Anspacher & Associates, Inc., a Chicago-based futures brokerage firm. Mr. O'Neil earned an undergraduate degree from Middlebury College and an MBA from the University of Chicago and holds the Series 3, 4, 7, 24, and 63 licenses.
- f) Fred Schrick, Managing Director, Charles Schwab & Co., Inc. and optionsXpress, Inc. Mr. Schrick is currently the financial operations principal and Chief Financial Officer for optionsXpress with responsibilities including supervising the financial areas of the Firm and reporting applicable financial and regulatory information to the Firm's regulators. At Schwab and optionsXpress, Mr. Schrick oversees the accounting and financial regulatory reporting areas. He has a bachelor's degree in accountancy from the University of Notre Dame, is a Certified Public Accountant and holds the Series 27 license. Prior to Schwab and optionsXpress, Mr. Schrick worked as Vice President Reporting at Scottrade for five years and Finance Director at UBS Investment Bank for seven years.

*(3) The significant types of business activities and product lines engaged in by the futures commission merchant, and the approximate percentage of the futures commission merchant's assets and capital that are used in each type of activity.*

optionsXpress, Inc. is a wholly-owned subsidiary of optionsXpress Holdings, Inc. (“optionsXpress Holdings”), which in turn is a wholly-owned subsidiary of The Charles Schwab Corporation (“CSC”). The Firm provides internet-based option, stock, mutual fund, fixed income, and futures brokerage services to retail clients located throughout the United States (“U.S.”) and certain foreign countries. The FCM transacts business on an agency basis and does not take positions in securities or futures contracts, except to facilitate customer accommodations and/or correct error transactions. The approximate percentages of the Firm’s assets and capital that are used in its futures and securities activities are 25 and 75%, respectively.

*(4) The futures commission merchant's business on behalf of its customers, including types of customers, markets traded, international businesses, and clearinghouses and carrying brokers used, and the futures commission merchant's policies and procedures concerning the choice of bank depositories, custodians, and counterparties permitted transactions under Sec. 1.25.*

As an FCM, optionsXpress provides or arranges for execution and clearing services for futures and options on futures (collectively, “futures”) for its futures clients and the clients of its international affiliates, optionsXpress Australia, Pty Limited, and optionsXpress Singapore Pte. Ltd. The vast majority of the Firm’s futures clients are retail investors, who enter futures orders on a self-directed basis via one of our online portals (website, mobile device application or website, or downloadable trading software). The Firm does not transact on a principal basis with its clients. The business of the FCM is limited to exchange-listed futures, and it does not offer execution or custody services for over-the-counter derivatives such as commodity swaps. The majority of its clients’ futures transactions are executed on U.S. exchanges, but trading in some foreign futures markets is offered as well.

optionsXpress maintains futures trading accounts for its clients on a fully-disclosed basis, in which it records their futures transactions, the funds it receives from clients to margin and settle their transactions, gains and losses on their positions and other account activities. The Firm provides various back office functions for futures trading, including preparing client trade confirmations and account statements, performing designated cashiering functions, including the delivery and receipt of funds and securities to or from the client, possession or control of client assets, and safeguarding client funds and transmitting tax accounting information to the client and to the applicable tax authorities.

The FCM processes all of its futures transactions as a non-clearing Futures Commission Merchant through an omnibus account arrangement with its clearing Futures Commission Merchants (“clearing FCMs”). Currently, optionsXpress uses R.J. O’Brien & Associates LLC and ADM Investor Services, Inc. as its clearing FCMs, but reserves the right to use other clearing FCMs at some point in the future. As of April 2017, optionsXpress transmits orders via the clearing FCMs or through other executing FCMs to the following futures exchanges: Chicago Board of Trade (“CBOT”); CBOE Futures Exchange (“CFE”); Chicago Mercantile Exchange (“CME”); ICE Futures US (NY Board of Trade); Minneapolis Grain Exchange (“MGE”); New York Mercantile Exchange (“NYMEX”); Commodity Exchange, Inc., (“COMEX”); and European Exchange, AG, (“EUREX”). The clearing FCMs are responsible for settling futures transactions on the various futures exchanges with their associated clearinghouses. For example, the clearinghouse for futures transactions executed on the CBOT, CME, NYMEX and COMEX is CME Clearing. The Firm’s clearing FCMs are members of certain foreign futures exchanges and may trade directly on those exchanges. The clearing FCMs may also hold client funds and futures contracts directly at the designated clearinghouse for those foreign futures exchanges, and would be responsible for setting up client secured funds bank accounts in accordance with CFTC Regulation 30.7. In other cases, the clearing FCMs may not be a member of a foreign futures exchange or clearinghouse at which the Firm facilitates foreign futures trading. For those transactions, the clearing FCMs direct orders to a foreign clearing broker which is a member of those exchanges and clearinghouses for execution and custody.

As an FCM, optionsXpress is subject to requirements under the Commodity Exchange Act (“CEA”) and regulations of the U.S. Commodity Futures Trading Commission (“CFTC”) regarding how it holds the

funds of its futures clients. Different rules apply with respect to customer funds for trading futures on U.S. exchanges and for trading futures on exchanges outside the U.S. The Firm is required to hold the funds that its futures clients deposit with it to margin and settle their futures transactions, along with any funds accruing on those transactions, on a segregated basis. That means, for example, the Firm cannot commingle those funds with its own operating funds, and holds those funds in accounts at a custodian bank or in omnibus accounts with a clearing FCM under account names indicating that the funds are held on behalf of the Firm's futures customers. The Firm's clearing FCMs are subject to the same regulatory requirements concerning the custody of client funds and assets, and are required to maintain adequate control over the futures contracts which they hold on behalf of the Firm's clients.

optionsXpress maintains client segregated funds accounts with major U.S. banking institutions to hold any uninvested funds of its futures clients that it has not pledged as collateral with the clearing FCMs to maintain client open positions. In a situation where optionsXpress clients hold open positions in futures contracts listed at exchanges outside the United States, the clearing FCMs, in turn, may be required to post collateral with correspondent clearing FCMs that are members of such foreign exchanges. Any proposed new bank relationships must be approved by Corporate Credit Research group of the Firm's Schwab affiliate. In evaluating a potential new banking relationship, the FCM (via the Schwab Corporate Credit Research group) would review the creditworthiness and reputation of the banking entity, as well as its operational abilities to deliver the type of banking services required and its agreement to abide by the terms of CFTC Regulations. The Corporate Credit Research group will evaluate factors such as the depository's capitalization, creditworthiness, operational reliability, and access to liquidity. The Corporate Credit Research group also monitors each approved depository on an ongoing basis to assess the depository's continued satisfaction of its criteria, including a thorough due diligence review at least annually. Various members of the Firm's management team would be required to approve the new relationship and counsel would review and approve the bank acknowledgement letter required by CFTC Regulations 1.20 or 30.7.

*(5) The material risks, accompanied by an explanation of how such risks may be material to its customers, of entrusting funds to the futures commission merchant, including, without limitation, the nature of investments made by the futures commission merchant (including credit quality, weighted average maturity, and weighted average coupon); the futures commission merchant's creditworthiness, leverage, capital, liquidity, principal liabilities, balance sheet leverage and other lines of business; risks to the futures commission merchant created by its affiliates and their activities, including investment of customer funds in an affiliated entity; and any significant liabilities, contingent or otherwise, and material commitments.*

optionsXpress believes that it has taken reasonable and adequate precautions to protect the funds of clients entrusted to the FCM. However, the Firm recognizes that it cannot eliminate all conceivable risks no matter how remote, particularly those which could arise from the actions or omissions of third parties such as futures exchanges, clearinghouses, bank custodians and other clearing or executing FCMs. The FCM has in place appropriate and effective policies and procedures to safely and reliably custody client assets deposited with it. Clients who deposit funds with optionsXpress are free to withdraw excess funds (to the extent that those funds are not collateralizing a futures position or other instrument) via customary and established processes such as check-writing, ACH requests and wire transfers. Nevertheless, funds entrusted by clients to the FCM would potentially be at risk in the unlikely event that the Firm becomes insolvent, particularly in a sudden and abrupt fashion. Theoretically, clients of the Firm are also subject to the indirect risk of the insolvency of a third-party with which the Firm transacts business, such as its clearing FCM or a foreign clearing broker used by the clearing FCM to execute and custody foreign futures contracts on behalf of the Firm's clients. Similarly, there is also a potential indirect risk to clients based on the insolvency of a futures exchange, clearinghouse, or bank which custodies client funds. An indirect risk to clients for a third-party insolvency exists largely to the extent that client funds entrusted to the third-party and which are not recoverable are of sufficient magnitude that the Firm cannot immediately make good on the obligations owed to clients. The FCM's policy is to perform appropriate due diligence

to the extent feasible of its third-party vendor relationships. Since these third-party vendors are independent actors, however, their conduct is normally outside of our control and therefore the Firm cannot guarantee that they perform their functions in an entirely risk-free manner. Moreover, certain entities with which the FCM conducts business, such as securities or futures exchanges, clearinghouses and market data providers, are centralized, mandatory counterparties in financial services transactions. The Firm has little or no ability to conduct due diligence of such entities or assess or impose controls on any risks inherent in their operations.

optionsXpress does not believe that a material risk of a sudden or unforeseen insolvency of the FCM exists. The Firm has a long history of profitability and does not risk its capital by engaging in proprietary trading activities. The FCM is part of the Charles Schwab family of companies, which share a similar history of profitability and are likewise risk-averse by nature. Moreover, the risk that clients would lose funds safeguarded by optionsXpress even in the circumstances of an insolvency proceeding of the Firm or its corporate affiliates is not material given the manner in which such funds are custodied. With the exception of warehouse receipts, funds deposited by clients with optionsXpress are custodied with major U.S. banking entities in segregated bank accounts in compliance with all applicable CFTC regulations. For these purposes, a segregated bank account means one which is specifically identified as being for the exclusive benefit of customers. Pursuant to CFTC Regulations, the bank holding funds in a client segregated funds account must agree in writing that funds in that account may not be used by the Firm for its own proprietary purposes, *e.g.*, to secure or obtain credit or to offset or be subject to a lien for Firm obligations or indebtedness. Additional CFTC rules and internal firm policies restrict the manner and type of investments of such funds to certain conservative investments (*See, Section 8, Investment Policy for Client Segregated Funds, infra*, for description of permitted investments). Thus, even in the unlikely event that the FCM, or its control affiliates, became insolvent, there does not appear to be a material risk that clients would lose the funds which they had deposited with the Firm. Since all future events cannot be foreseen, however, some risk of loss may exist.

Client funds may also be held by our clearing FCMs as security or collateral for open futures contracts carried by the clearing FCMs on behalf of the Firm's clients. The clearing FCMs may in turn pledge such funds as collateral for open positions at federally-licensed and regulated Designated Contract Markets. As a registered FCM, the clearing FCMs used by the Firm are also subject to the same CFTC rules regarding the segregation and investment of clients' funds. Assuming that the clearing FCMs comply with the CFTC regulations regarding the custody and investment of client funds, client funds held by the Firm's clearing FCMs should not be at a material risk of loss even if one or more of the clearing FCMs became insolvent. Unforeseen events or non-compliance with these regulations by the clearing FCM may, however, result in a risk of a loss in some circumstances. As noted above in Section (4), certain foreign futures transactions may be handled by foreign clearing brokers which may not be subject to CFTC regulations. While the Firm and its clearing FCMs would continue to be governed by CFTC Regulation 30.7 and would custody client funds in a secured bank account as appropriate, the conduct of foreign clearing brokers would be directed by the laws and regulations of the foreign jurisdiction and futures exchanges where the transaction was consummated. These laws and regulations may vary from country to country and exchange to exchange, and may not provide the same protections as under CFTC regulations. The Firm does not believe that any material risk to clients is presented by such arrangements, however, both the Firm and its clearing FCM remain obligated to clients based on the above-mentioned CFTC regulations on segregation of client funds entrusted to the Firm.

**CREDITWORTHINESS** – The investment activity of optionsXpress is conducted by the Firm's Finance Department and is governed by the Firm's Working Capital Portfolio Investment Policy. The Firm's principal investments consist of cash, cash equivalents, (which include highly liquid investments with original maturities of three months or less) and U.S. Treasury securities. The Firm's policies and procedures take into consideration the market, credit, counterparty, operational, and liquidity risks associated with such investments. The Firm has established policies and procedures setting forth the types of permitted investments, as well as credit standards and maturity guidelines (which vary depending

on the financial instrument). As of February 28, 2017, the weighted average maturity of the Firm's investments was 110 days. The Firm's investments were in U.S. Treasury bills, which are rated AAA and have no coupon rate. The Firm manages the permitted investments consistent with the objectives of preserving principal and maintaining liquidity.

The objective of the Working Capital Portfolio Investment policy is to ensure that the investments of the Firm's Working Capital portfolio are managed in a sound and prudent manner. Within this context, the primary investment considerations are to:

- ensure the safety and preservation of the Firm's capital;
- set forth permissible securities and investments for the Portfolio;
- provide adequate liquidity for optionsXpress to meet anticipated cash needs through maturing investments;
- provide adequate liquidity for the Firm to meet unanticipated cash needs through the selection of investments with liquid and efficient markets or investments for which an efficient repurchase market exists; and
- achieve an optimal rate of return consistent with the proper appraisal and control of credit and market risk, such that the Portfolio earnings are maximized consistent with prudent risk management.

Other assets of the Firm include receivables from brokerage clients, chiefly arising out of the extension of margin loans or other forms of credit in securities or futures transactions. The Firm's history is that such receivables are generally repaid in full by clients, although from time to time a small number of clients close or abandon their accounts without repaying in full the amounts loaned to them by the FCM. The Firm has been able to recover at least a portion of these debits in legal proceedings against the debtors.

Schwab's Corporate Risk Management ("CRM") group is responsible for the Firm's credit risk monitoring and reporting. Key activities and elements that are reviewed in order to provide insight and support for credit risk monitoring and reporting include issuer and counterparty exposure and bank loan portfolios. Issuer credit exposure monitoring includes initial CRM approvals and analysis, ongoing monitoring, and comprehensive annual reviews. In all cases involving counterparty and issuer credit exposures, credit limits are established and monitored. Collateral quality, in the case of counterparty exposures, and issuer credit quality in the case of unsecured exposures, is rigorously monitored. Credit exposures, including concentrations, are reported to various internal oversight committees. CRM performs monitoring of the monthly bank loan portfolio reports, reviewing key performance indicators to identify impacts of potential emerging risks and to take mitigating actions as appropriate.

As noted above, optionsXpress is an affiliate of CSC, a publicly traded holding company whose principal operating subsidiaries include Schwab, a registered broker-dealer, and the Charles Schwab Bank, a federally chartered thrift institution. In addition, the Firm has a \$200 million line of credit from CSC. Beginning in 2012, optionsXpress began enabling domestic clients to sweep excess funds held in brokerage accounts into deposit accounts at Charles Schwab Bank. In 2013, the Firm began borrowing securities from Schwab as part of its daily stock loan and financing activities.

**GENERAL CONTINGENCIES** – The Firm extends margin credit and leverage to its clients, which are subject to various regulatory and clearing firm margin requirements. Margin credit balances are collateralized by funds, securities and futures contracts in the clients' accounts. Leverage involves securing a large potential future obligation with a lesser amount of funds or securities. The risks



associated with margin credit and leverage increase during periods of volatile markets or in cases where leverage or collateral is concentrated and significant market movements occur. During such times, clients who utilize margin credit or leverage and who have collateralized their obligations with securities or futures may find that their positions have a rapidly depreciating value and may not be sufficient to cover their obligations in the event of liquidation. The Firm is exposed to credit risk when its clients execute transactions, such as short sales of options and equities or futures transactions that can expose them to risk beyond their invested capital. In addition, the Firm may be obligated for margin extended to the Firm's clients by its third-party clearing agent on futures positions.

The margin and leverage requirements that the Firm imposes on its client accounts meet or exceed those required by various regulatory requirements and Regulation T of the Board of Governors of the Federal Reserve. The amount of this risk is not readily quantifiable since the risk is dependent upon analysis of a potential significant and undeterminable rise or fall in securities or futures prices. As a result, the Firm is exposed to significant off-balance sheet credit risk in the event client collateral is not sufficient to fully cover losses that clients may incur. In the event clients fail to satisfy their obligations, the Firm may be required to purchase or sell financial instruments at prevailing market prices to fulfill the clients' obligations.

**COLLATERAL MANAGEMENT** – The Firm borrows or lends securities temporarily from other broker-dealers in connection with its broker-dealer business. The Firm deposits funds as collateral for the securities borrowed. Decreases in securities prices may cause the market value of the securities borrowed to fall below the amount of cash deposited as collateral. In the event the counterparty to these transactions does not return the cash deposited, the Firm may be exposed to the risk of selling the securities at prevailing market prices. The Firm seeks to manage this risk by requiring credit approvals for counterparties, by monitoring the securities values on a daily basis, and by requiring additional collateral as needed. Securities borrowed require the Firm to deliver cash to the lender in exchange for securities. For securities loaned, the Firm receives collateral in the form of cash in an amount equal to or greater than the market value of securities loaned. The market value of securities borrowed and loaned is monitored, with additional collateral obtained or refunded to ensure full collateralization. All of the Firm's securities lending transactions are subject to enforceable master securities lending agreements with other broker-dealers.

**LEGAL CONTINGENCIES** – In the ordinary course of business as an FCM and securities broker-dealer, the Firm may be subject to lawsuits, arbitrations, claims, and other legal proceedings. The FCM cannot predict with certainty the outcome of pending or threatened legal proceedings. A substantial judgment against the Firm or other resolution regarding the proceedings could have a material adverse effect on the Firm's financial condition.

**GUARANTEES** – The FCM clears its clients' futures transactions on an omnibus basis through one of its clearing FCMs. The Firm has agreed to indemnify its third-party clearing FCMs for losses that it may sustain in the handling of orders, instructions and transactions for the FCM's clients or the failure of the FCM's clients to meet obligations owed in connection with their trading of futures contracts, such as meeting margin calls or paying amounts due. In connection with its securities brokerage activities, the Firm provides guarantees to its clearing organizations and exchanges under their standard membership agreements, which require members to guarantee the performance of other members. Under the agreements, if another member becomes unable to satisfy its obligations to the clearing organization or exchange, other members would be required to meet shortfalls. The Firm's liability under these arrangements is not quantifiable and may exceed the cash and securities it has posted as collateral. However, the Firm believes that it is unlikely that it will have to make any material payments under these arrangements.

(6) *The name of the futures commission merchant's designated self-regulatory organization and its Web site address and the location where the annual audited financial statements of the futures commission merchant is made available.*

The designated futures self-regulatory organization for optionsXpress is the NFA. The address of the NFA's public website is <http://www.nfa.futures.org/>. The annual audited financial statement of optionsXpress can be found on its public website at [http://www.optionsxpress.com/security\\_risks/financial\\_statement.aspx](http://www.optionsxpress.com/security_risks/financial_statement.aspx) or by following the link titled "Financial Statements" on the optionsXpress home page.

(7) *Any material administrative, civil, enforcement, or criminal complaints or actions filed against the futures commission merchant where such complaints or actions have not concluded, and any enforcement complaints or actions filed against the futures commission merchant during the last three years.*

There are no proceedings against optionsXpress acting in its capacity as an FCM which were filed in the last three years. Other proceedings against the Firm arising out of its activities as a securities broker-dealer in the last 3 years include the following:

- a) *In re: optionsXpress, Inc.*, Letter of Acceptance, Waiver and Consent ("AWC") No. 2014041865201 (Sept. 19, 2016). In a settled matter, the Firm consented to entry of an Order finding that in 29 instances it routed agency orders to the BATS Exchange and executed them by pairing them with principal orders without first exposing them to the market for at least one second, in violation of BZX Rule 22.12. The Firm was censured and fined \$60,000.
- b) *In re: optionsXpress, Inc.*, AWC No. 2013038427401 (July 22, 2015). In a settled proceeding, FINRA found that the Firm failed to adjust the price or share quantity on open good-till-cancelled ("GTC") orders in violation of FINRA Rules 3220 and 5330, and related supervisory violations. Without admitting or denying the findings, the Firm consented to a censure and monetary fine of \$165,000.
- c) *In re: optionsXpress, Inc.*, File No. 15-0073 (July 7, 2015), the CBOE instituted a settled disciplinary proceeding against the Firm for failing to obtain and review the outside brokerage account statements for certain of its associated persons, as well as for failing to adequately enforce its policies and procedures related to its insider trading program. Without admitting or denying the findings, the Firm consented to a censure and fine of \$20,000.
- d) *In re: optionsXpress, Inc.*, AWC No. 2013038709001 (Apr. 29, 2015). In a settled proceeding, FINRA found that the Firm submitted erroneous short interest position reports in violation of FINRA rules, and associated supervisory violations. Without admitting or denying the findings, the Firm consented to a censure and fine of \$12,500.
- e) *In re: optionsXpress, Inc.*, AWC Nos. 2010023686101 and 2012031310901 (March 20, 2015). In a settled proceeding brought on behalf of the Nasdaq Options Market, LLC ("NOM"), FINRA found that the Firm violated FINRA and NOM rules regarding Large Option Position Reporting ("LOPR") by failing to report or failing to accurately report a significant number of LOPR submissions, and associated supervisory violations. Without admitting or denying the findings, the Firm consented to a censure and fine of \$2,400,000, and committed to future undertakings to engage an outside consultant to review and report to FINRA on the accuracy of its LOPR reporting.
- f) *In re: optionsXpress, Inc.*, AWC No. 2012034190001 (March 17, 2015). In a settled proceeding, FINRA found that the Firm violated FINRA rules regarding supervision of accounts in connection

with the transmittal of funds from customer brokerage accounts to outside bank accounts. Without admitting or denying the findings, the Firm consented to a censure and fine of \$150,000 and agreed to implement improved review procedures.

- g) *In re: optionsXpress, Inc.*, AWC No. 20130364136 (June 23, 2014). In a settled proceeding brought on behalf of the International Securities Exchange, Inc. ("ISE"), FINRA found that the Firm violated ISE Rule 1400(a) by failing to make and keep certain text messages from firm-issued cellular devices, and associated supervisory violations. Without admitting or denying the findings, the Firm consented to a censure and fine of \$125,000.
- h) *In re: optionsXpress, Inc.*, Letter of Acceptance, Waiver and Consent ("AWC") No. 2012030742601 (May 21, 2014). In a settled proceeding, FINRA found that the Firm violated FINRA rules regarding supervision of activities and the contents of communications with clients and prospects in connection with the Firm's arrangements with a third-party educational service provider. The AWC order also found that the Firm engaged in a retail foreign exchange business prior to receiving approval from FINRA to do so. Without admitting or denying the findings, the Firm consented to the entry of an Order which censured the Firm and imposed a fine of \$275,000.
- i) *In re: optionsXpress, Inc., and Jonathan Feldman*, Exchange Rel. No. 78621, AP File No. 3-14848 (Aug. 18, 2016). On appeal from the decision of the SEC Administrative Law Judge in 2013, the full Commission found that optionsXpress violated Rules 204 and 204T of Regulation SHO by failing to close out a number of fail-to-deliver short positions. optionsXpress was ordered to cease and desist from violating Rules 204 and 204T, make disgorgement of \$1,574,599, plus interest, and pay a civil monetary penalty of \$2,000,000.

*(8) A basic overview of customer fund segregation, futures commission merchant collateral management and investments, futures commission merchants, and joint futures commission merchant/broker dealers.*

Funds and other assets segregated and on deposit for regulatory purposes include interest-bearing cash deposits from clients' securities accounts held in a special reserve bank account according to Rule 15c3-3 of the Exchange Act, and interest-bearing cash deposits, including open trade equity and cash deposits with a clearing FCM, that have been segregated or secured for the benefit of futures clients according to the regulations of the CFTC governing a futures commission merchant.

Pursuant to CFTC regulations, funds of clients are maintained in a segregated bank account. As noted above, the bank holding these assets is required to keep them in a separate account which is specifically identified as being for the exclusive benefit of the Firm's customers. CFTC Regulations require that any custodial bank agree in writing that it will not permit those funds to be used to pay, offset or secure any obligation or indebtedness of the Firm. Client funds deposited in the Segregated Funds account are permitted to be commingled with funds deposited by other customers of the Firm. Net additions or subtractions to the Segregated Funds Account are based on changes in clients' margin requirements. The Firm's Finance Department will determine the required minimum balance to be maintained in the account and direct the Cash Management Department to make any required deposit or withdrawal not for the benefit of customers.

Pursuant to futures industry regulations, the Firm is required to maintain a residual interest consisting of its own proprietary funds in the client segregated funds accounts. The Firm's residual interest must exceed the "undermargined amount" of clients' futures accounts as defined by CFTC Regulation 1.22 (basically, the amount, if any, by which the total amount of collateral required to support the futures positions in clients' accounts exceeds the value of futures clients' funds in the futures account, calculated

daily at the end of the business day). The Firm may not withdraw proprietary funds in the clients' segregated funds accounts beyond its residual interest. Furthermore, under NFA rules, the FCM must ensure that management properly authorizes any withdrawal of more than 25% of its targeted residual interest from the clients' segregated funds accounts not for the benefit of customers, and immediately notifies the NFA of the withdrawal.

## Investment Policy for Client Segregated Funds

The objective of the Firm's Investment Policy is to ensure that the investments of the Special Reserve ("15c3-3") portfolio ("Special Reserve Portfolio" or "Portfolio") and the Segregated/Secured ("CFTC Regulations 1.20 and 30.7") Portfolio ("Segregated Portfolio") are managed in a sound and prudent manner. Within this context, the primary investment considerations are to safeguard excess customer credit balances, ensure the safety and preservation of the FCM's capital and principal, set forth permissible securities and investments for the Special Reserve Portfolio, provide adequate liquidity for the Firm to meet anticipated cash needs through maturing investments, provide adequate liquidity to meet unanticipated cash needs through the selection of investments with liquid and efficient markets or investments for which an efficient repurchase market exists, achieve an optimal rate of return consistent with the proper appraisal and control of credit and market risk, such that portfolio earnings are maximized consistent with prudent risk management, and take into account regulatory capital haircuts applied on investments in the portfolio.

Investments for the Special Reserve (15c3-3) portfolio and Segregated (CFTC Regulation 1.25) portfolio will be limited to the following classes of securities, which are all permissible under SEC Rule 15c3-3 and CFTC Regulation 1.25:

- Direct U.S. Government obligations in the form of bills, notes, bonds and STRIPS and other instruments explicitly guaranteed by the U.S. Government;
- Participation Certificates or Mortgage-Backed Securities guaranteed by the Government National Mortgage Association ("GNMA"), including GNMA REMIC Collateralized Mortgage Obligations;
- Certificates of Deposit of approved U.S. Banks and Thrifts (as defined by Section 3(a)(6) of the Exchange Act) up to Federal Depository Insurance Corporation's ("FDIC") insured maximum issued by any one institution. Investments in CDs greater than the FDIC insured maximum are permissible if aggregate investments from that institution do not exceed the lesser of 50% of the excess net capital of the broker dealer or 10% of the bank's equity capital;
- Reverse Repurchase Agreements collateralized by any of the above, subject to certain repurchase transaction requirements;
- Money Market Deposit Accounts ("MMDA") as defined under Regulation D of the Federal Reserve System provided that the deposit is with a U.S. bank or thrift (as defined by section 3(a)(6) of the Exchange Act) in accordance with the requirements of Rule 15c3-3 (e) and (f). The total deposit with any one bank must not exceed 50% of the broker-dealer's excess net capital and must not be greater than 10% of the bank's equity capital; and
- Cash or Trust Deposit accounts.

Prior to establishing any omnibus account on behalf of a Special Reserve Portfolio, the custodian bank ("Bank") must execute an acknowledgement letter which provides that the Bank will hold the funds in a separate account titled for the exclusive benefit of customers of the FCM and by which the Bank agrees not to use the funds in the account to secure or guarantee any obligation of the FCM to the Bank or

assert any right of offset or lien for any indebtedness, obligation or liability of the FCM owed to the Bank, as required by applicable law. U.S. Government and Agency-backed investments do not require prior credit approval; all other investment and counterparties can only be made subject to approved credit limits.

*(9) Information on how a customer may obtain information regarding filing a complaint about the futures commission merchant with the Commission or with the firm's designated self-regulatory organization.*

Information for optionsXpress customers about how to file a complaint with the CFTC or the NFA can be found at the public website for each respective organization by searching the term "File a Complaint."

*(10) The following financial data as of the most recent month-end when the Disclosure Document is prepared:*

*(i) The futures commission merchant's total equity, regulatory capital, and net worth, all computed in accordance with U.S. Generally Accepted Accounting Principles and Sec. 1.17, as applicable.*

Equity: \$349,407,570  
Net capital: \$273,595,457  
Net worth: \$349,407,570  
(as of January 31, 2017)

*(ii) The dollar value of the futures commission merchant's proprietary margin requirements as a percentage of the aggregate margin requirement for futures customers, Cleared Swaps Customers, and 30.7 customers.*

Not applicable.

*(iii) The smallest number of futures customers, Cleared Swaps Customers, and 30.7 customers that comprise 50 percent of the futures commission merchant's total funds held for futures customers, Cleared Swaps Customers, and 30.7 customers, respectively.*

As of December 31, 2016, our 285 largest accounts represent 50% of the total funds we hold for futures clients in our Segregated futures balance. With regard to our 30.7 (Secured) balance, our 21 largest accounts constitute 50% of the total funds we hold for clients. The Firm does not engage in swaps trading activity and therefore has no Cleared Swaps customers or funds.

*(iv) The aggregate notional value, by asset class, of all non-hedged, principal over-the-counter transactions into which the futures commission merchant has entered.*

The Firm does not enter into any principal over-the-counter transactions.

*(v) The amount, generic source and purpose of any committed unsecured lines of credit (or similar short-term funding) the futures commission merchant has obtained but not yet drawn upon.*

As noted above, the Firm has a \$200 million line of credit from CSC.

*(vi) The aggregated amount of financing the futures commission merchant provides for customer transactions involving illiquid financial products for which it is difficult to obtain timely and accurate prices.*

Except in highly unusual circumstances and/or temporary periods of extreme volatility or market disruption which are difficult to anticipate or quantify, the exchange-traded products offered by the Firm are not illiquid to the extent that it is difficult to obtain timely and accurate prices.

*(vii) The percentage of futures customer, Cleared Swaps Customer, and 30.7 customer receivable balances that the futures commission merchant had to write-off as uncollectable during the past 12-month period, as compared to the current balance of funds held for futures customers, Cleared Swaps Customers, and 30.7 customers.*

The total amount of balances which were written-off as uncollectable between February 1, 2016 and February 28, 2017 and that are attributable to futures losses is \$172,876. This includes all write-offs in excess of \$100. As of February 28, 2017, the current balance of funds held for futures customers was \$138,956,707 (Segregated assets) and \$2,622,163 (Secured assets).

*(11) A summary of the futures commission merchant's current risk practices, controls and procedures.*

As noted above, the FCM is part of The Charles Schwab Corporation corporate hierarchy. As such, it benefits from the risk management framework of this network of companies. For example, many of the support services discussed below are provided by Schwab employees or departments or by using Schwab systems and control processes. optionsXpress leverages the existing risk management control structure at Schwab, supplemented by systems and activities of optionsXpress and its personnel, as described herein.

As part of The Charles Schwab Corporation family of companies, optionsXpress is committed to the highest standards of ethical conduct. The Code of Business Conduct and Ethics ("Code") applies to an individual's service as a director, officer, or employee of CSC and its subsidiaries and affiliates. The Code outlines ethical conduct in several key areas:

- Ethical behavior and legal compliance;
- Conflicts of interest;
- Confidentiality of information;
- Employment practices;
- Business practices; and
- Compliance and reporting

While the Code outlines key areas of ethical conduct, more detailed information is set forth throughout the Compliance Manual applicable to the Firm, policies and procedures for individual business units, and policies with which employees must comply as a condition of employment with the Firm (collectively referred to as "company policies"). Employees are responsible for reviewing the Code and company policies that apply to them and their business unit and are expected to act in compliance with the Code and company policies in their daily activities.

The FCM has adopted a Risk Management Program pursuant to CFTC Regulation 1.11 which is designed to help the Firm identify risks and set reasonably appropriate risk tolerance limits across a number of areas, such as Market, Operational, Technology, Legal, Liquidity, Foreign currency, Segregation, Settlement, Credit, and Capital risk. The departments overseeing functional areas of the

Firm's business are responsible for monitoring and managing relevant risks to the Firm. In addition, these departments are expected to maintain procedures and systems which are reasonably designed to comply with this Policy. Such procedures must include the following essential elements:

- Description of applicable risks in the functional areas or business activities overseen by the department, along with specific risk tolerance limits;
- Methodology for monitoring these risks and the risk tolerance limits;
- A process for detecting breaches of these tolerance limits and alerting the appropriate members of the Firm's senior management, the appropriate optionsXpress oversight committee(s), and the Firm's Risk Management Unit in the event of breaches;
- Policies for determining when exceptions to the risk tolerance limits are allowed, and a process for seeking and receiving approval for any such exceptions; and
- Quarterly reports to the appropriate optionsXpress oversight committee and the Firm's Risk Management Unit.

The risk management process at the Firm is delivered through three lines of defense, with clearly defined responsibilities at each level. The first level of risk management lies with the employees and managers of the FCM. Working with staff, management has the ownership, responsibility, and accountability for identifying, assessing, controlling, and mitigating risks in accordance with corporate standards, vision, values and strategy. Each business unit within the Firm has an appropriate business leader, who is responsible for designing, maintaining, and testing a system of staff-level and supervisory processes and procedures to comply with applicable laws and regulations, as well as company policies. Known risk events of sufficient magnitude are required to be escalated to Management, as well as the Supervision & Controls team.

The second level of risk management consists of the regular oversight of its business activities. Responsibility for this function has been delegated to a series of governance committees of the FCM. The senior governance committee in this hierarchy is the Executive Committee. Other committees include the Development Committee; Operational Risk Committee; New Products and Services Review Council, Pricing and Margin Committee; Treasury, Capital and Finance Committee; and Trading and Execution Risk Committee. These committees report to the Executive Committee. In general, the governance committees work to manage risk by setting standards, monitoring the risk management practices, and reporting on risk activities and emerging risks. These committees meet periodically throughout the year to review the Firm's activities in their respective areas of responsibility and make decisions on the future direction of the Firm.

Additionally, each committee below the Executive Committee receives and reviews a Risk Exposure Report ("RER") from the various operational units of the Firm within its purview. The RERs are generated from the Firm's Risk and Control Self-Assessment ("RCSA") Process. The RCSA process is a risk management framework used by Schwab and optionsXpress to disclose current risk exposures generally within the firm and the current strength of the control activities in place to mitigate those risks. RERs are issued no less than quarterly. The RERs will set forth all applicable risk exposures of the Firm, current risk tolerance limits, may recommend changes to the Risk Management Program for the business unit to address or mitigate such risks, and review the status of any previously recommended changes. The Firm's Risk Management Unit Steering Committee, which is composed of persons with sufficient authority and qualifications who are independent of the Business Unit of the Firm, reviews the RERs and discusses the material aspects of the reports with the Firm's Executive Committee on at least a quarterly basis. The Program also specifies that the FCM's Executive Committee will review and approve the risk tolerance

limits described in the RERs quarterly and that the Firm's Board of Directors will review and approve such risk tolerances annually.

At both levels, management and the various optionsXpress committees are supported by a number of units and advisors. Some of these support personnel work directly for the Firm, while others provide these services through one of its corporate affiliates. Examples of these advisory units include Corporate Legal Services, Compliance, Supervision and Controls, Human Resources, Vendor Management Organization, Anti-Money Laundering Office, Global Security Organization and Fraud Prevention Departments. In addition, there also are a number of Schwab oversight bodies whose scope includes the activities of optionsXpress. These committees include the Global Risk Committee, Credit and Market Risk Oversight Committee, Order Routing Committee (a joint Schwab-optionsXpress committee), Investment Product Review Council, Information Security and Privacy Security Committee, Model Governance Committee, Operational Risk Oversight Committee, and Integration Oversight Committee. These Schwab committees do not report to the FCM's Executive Committee

The final level of risk management consists of the review by Schwab's Internal Audit department of the policies and procedures of the Firm, including the consistent application and compliance with those policies and procedures. Findings and recommendations made by Internal Audit are provided to appropriate members of the Firm's management and staff for implementation. Internal Audit tracks the resolution of its recommendations and reports on progress to optionsXpress management and the Audit Committee of Schwab. Additional audits and reviews of the Firm may be performed from time to time by the Firm's Compliance Department. The Firm's financial statements are audited by an independent, third-party auditor (currently, Deloitte & Touche).

optionsXpress' Risk Management Program must be reviewed and independently tested by the Schwab Internal Audit Department on at least an annual basis, or more frequently upon any material change in the Firm's business that is reasonably likely to alter its risk profile. The annual review will include an analysis of adherence to, and the effectiveness of, the Firm's policies and procedures required by this Policy and any recommendations for changes or enhancements.

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