SCHWAB CHARLES CORP
Form 10-Q
May 07, 2014
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2014

Commission File Number: 1-9700

THE CHARLES SCHWAB CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	94-3025021
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

211 Main Street, San Francisco, CA 94105

(Address of principal executive offices and zip code)

Registrant's telephone number, including area code: (415) 667-7000

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company)	Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

1,301,140,339 shares of $.01 par value Common Stock

Outstanding on April 24, 2014

THE CHARLES SCHWAB CORPORATION

Quarterly Report on Form 10-Q

For the Quarter Ended March 31, 2014

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Part I – FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

THE CHARLES SCHWAB CORPORATION

Condensed Consolidated Statements of Income

(In Millions, Except Per Share Amounts)

(Unaudited)

	Three Months Ended March 31,	
	2014	2013
Net Revenues		
Asset management and administration fees	$ 611	$ 552
Interest revenue	579	497
Interest expense	(26)	(28)
Net interest revenue	553	469
Trading revenue	247	223
Other	68	56
Provision for loan losses	(1)	(6)
Net impairment losses on securities (1)	-	(4)
Total net revenues	1,478	1,290
Expenses Excluding Interest		
Compensation and benefits	528	536
Professional services	106	99
Occupancy and equipment	80	77
Advertising and market development	63	74
Communications	56	54
Depreciation and amortization	48	51
Other	75	68
Total expenses excluding interest	956	959
Income before taxes on income	522	331
Taxes on income	196	125
Net Income	326	206
Preferred stock dividends	8	8
Net Income Available to Common Stockholders	$ 318	$ 198
Weighted-Average Common Shares Outstanding — Diluted	1,311	1,282

Earnings Per Common Share — Basic	$ .24	$ .15
Earnings Per Common Share — Diluted	$ .24	$ .15

(1) There were no net impairment losses on securities for the three months ended March 31, 2014. Net impairment losses on securities include total other-than-temporary impairment losses of $0 million recognized in other comprehensive income, net of $(4) million reclassified from other comprehensive income, for the three months ended March 31, 2013.

See Notes to Condensed Consolidated Financial Statements.

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THE CHARLES SCHWAB CORPORATION

Condensed Consolidated Statements of Comprehensive Income

(In Millions)

(Unaudited)

	Three Months Ended March 31,	
	2014	2013
Net Income	$ 326	$ 206
Other comprehensive income, before tax:		
Change in net unrealized gain on securities available for sale:		
Net unrealized gain (loss)	159	(3)
Reclassification of impairment charges included in net impairment losses on securities	-	4
Other reclassifications included in other revenue	(1)	-
Other	-	1
Other comprehensive income, before tax	158	2
Income tax effect	(59)	-
Other comprehensive income, net of tax	99	2
Comprehensive Income	$ 425	$ 208

See Notes to Condensed Consolidated Financial Statements.

THE CHARLES SCHWAB CORPORATION

Condensed Consolidated Balance Sheets

(In Millions, Except Per Share and Share Amounts)

(Unaudited)

	March 31, 2014	December 31, 2013
Assets		
Cash and cash equivalents	$ 7,173	$ 7,728
Cash and investments segregated and on deposit for regulatory purposes (including resale agreements of $11,776 at March 31, 2014 and $14,016 at December 31, 2013)	20,548	23,553
Receivables from brokers, dealers, and clearing organizations	482	509
Receivables from brokerage clients — net	14,571	13,951
Other securities owned — at fair value	456	517
Securities available for sale	53,080	51,618
Securities held to maturity (fair value — $31,669 at March 31, 2014 and $29,490 at December 31, 2013)	32,123	30,318
Loans to banking clients — net	12,591	12,419
Equipment, office facilities, and property — net	820	790
Goodwill	1,227	1,227
Intangible assets — net	255	266
Other assets	740	746
Total assets	$ 144,066	$ 143,642
Liabilities and Stockholders' Equity		
Deposits from banking clients	$ 95,591	$ 92,972
Payables to brokers, dealers, and clearing organizations	1,918	1,467
Payables to brokerage clients	32,308	35,333
Accrued expenses and other liabilities	1,532	1,586
Long-term debt	1,902	1,903
Total liabilities	133,251	133,261
Stockholders' equity:		
Preferred stock — $.01 par value per share; aggregate liquidation preference of $885	870	869
Common stock — 3 billion shares authorized; $.01 par value per share; 1,487,543,446 shares issued	15	15

Additional paid-in capital	3,982	3,951
Retained earnings	9,492	9,253
Treasury stock, at cost — 186,648,711 shares at March 31, 2014 and 190,657,263 shares at December 31, 2013	(3,652)	(3,716)
Accumulated other comprehensive income	108	9
Total stockholders' equity	10,815	10,381
Total liabilities and stockholders' equity	$ 144,066	$ 143,642

See Notes to Condensed Consolidated Financial Statements.

THE CHARLES SCHWAB CORPORATION

Condensed Consolidated Statements of Cash Flows

(In Millions)

(Unaudited)

	Three Months Ended March 31,	
	2014	2013
Cash Flows from Operating Activities		
Net income	$ 326	$ 206
Adjustments to reconcile net income to net cash provided by (used for) operating activities:		
Provision for loan losses	1	6
Net impairment losses on securities	-	4
Stock-based compensation	29	37
Depreciation and amortization	48	51
Premium amortization, net, on securities available for sale and securities held to maturity	27	44
Other	2	7
Net change in:		
Cash and investments segregated and on deposit for regulatory purposes	3,005	1,572
Receivables from brokers, dealers, and clearing organizations	29	(134)
Receivables from brokerage clients	(622)	1,003
Other securities owned	61	91
Other assets	(24)	(29)
Payables to brokers, dealers, and clearing organizations	293	84
Payables to brokerage clients	(3,025)	(3,442)
Accrued expenses and other liabilities	(81)	132
Net cash provided by (used for) operating activities	69	(368)
Cash Flows from Investing Activities		
Purchases of securities available for sale	(4,250)	(6,703)
Proceeds from sales of securities available for sale	1,285	-
Principal payments on securities available for sale	1,738	3,997
Purchases of securities held to maturity	(2,271)	(6,031)
Principal payments on securities held to maturity	520	1,279
Net increase in loans to banking clients	(171)	(530)
Purchase of equipment, office facilities, and property	(53)	(49)
Other investing activities	(8)	2
Net cash used for investing activities	(3,210)	(8,035)
Cash Flows from Financing Activities		
Net change in deposits from banking clients	2,619	3,047
Repayment of commercial paper	-	(300)
Repayment of long-term debt	(2)	(2)

Dividends paid	(100)	(98)
Proceeds from stock options exercised and other	65	25
Other financing activities	4	(1)
Net cash provided by financing activities	2,586	2,671
Decrease in Cash and Cash Equivalents	(555)	(5,732)
Cash and Cash Equivalents at Beginning of Period	7,728	12,663
Cash and Cash Equivalents at End of Period	$ 7,173	$ 6,931
Supplemental Cash Flow Information		
Cash paid during the period for:		
Interest	$ 40	$ 40
Income taxes	$ 51	$ 35
Non-cash investing activity:		
Securities purchased during the period but settled after period end	$ 158	$ -

See Notes to Condensed Consolidated Financial Statements.

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THE CHARLES SCHWAB CORPORATION

Notes to Condensed Consolidated Financial Statements

(Tabular Amounts in Millions, Except Per Share Data, Ratios, or as Noted)

(Unaudited)

1.Introduction and Basis of Presentation

The Charles Schwab Corporation (CSC) is a savings and loan holding company engaged, through its subsidiaries, in securities brokerage, banking, money management, and financial advisory services. Charles Schwab & Co., Inc. (Schwab) is a securities broker-dealer with over 300 domestic branch offices in 45 states, as well as a branch in each of the Commonwealth of Puerto Rico and London, England. In addition, Schwab serves clients in Hong Kong through one of CSC's subsidiaries. Other subsidiaries include Charles Schwab Bank (Schwab Bank), a federal savings bank, and Charles Schwab Investment Management, Inc. (CSIM), the investment advisor for Schwab's proprietary mutual funds, which are referred to as the Schwab Funds®, and for Schwab's exchange-traded funds, which are referred to as the Schwab ETFs™.

The accompanying unaudited condensed consolidated financial statements include CSC and its majority-owned subsidiaries (collectively referred to as the Company). Intercompany balances and transactions have been eliminated. These condensed consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States (U.S.), which require management to make certain estimates and assumptions that affect the reported amounts in the accompanying financial statements. Certain estimates relate to other-than-temporary impairment of securities available for sale and securities held to maturity, valuation of goodwill, allowance for loan losses, and legal and regulatory reserves. Actual results may differ from those estimates. These condensed consolidated financial statements reflect all adjustments that are, in the opinion of management, necessary for a fair presentation of the results for the periods presented. These adjustments are of a normal recurring nature. The Company's results for any interim period are not necessarily indicative of results for a full year or any other interim period. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013.

The Company's significant accounting policies are included in note "2 – Summary of Significant Accounting Policies" in the Company's Annual Report on Form 10-K for the year ended December 31, 2013. There have been no significant changes to these accounting policies during the first quarter of 2014.

2.New Accounting Standard

New Accounting Standard Not Yet Adopted

In January 2014, the Financial Accounting Standards Board issued new guidance for creditors of consumer mortgage loans, which is effective January 1, 2015. The guidance clarifies when physical possession of a property underlying a consumer mortgage loan transfers to the creditor, and therefore when a loan receivable should be derecognized and the real estate property underlying the loan should be recognized. The adoption of this new guidance is not expected to have a material impact on the Company's financial position, results of operations, earnings per common share (EPS), or cash flows.

THE CHARLES SCHWAB CORPORATION

Notes to Condensed Consolidated Financial Statements

(Tabular Amounts in Millions, Except Per Share Data, Ratios, or as Noted)

(Unaudited)

3.Securities Available for Sale and Securities Held to Maturity

The amortized cost, gross unrealized gains and losses, and fair value of securities available for sale and securities held to maturity are as follows:

March 31, 2014	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Securities available for sale:				
U.S. agency mortgage-backed securities	$ 18,404	$ 168	$ 38	$ 18,534
Asset-backed securities	16,642	91	8	16,725
Corporate debt securities	9,043	53	9	9,087
U.S. agency notes	4,490	1	81	4,410
Certificates of deposit	3,424	4	2	3,426
Non-agency residential mortgage-backed securities	593	13	28	578
Non-agency commercial mortgage-backed securities	312	8	-	320
Total securities available for sale	$ 52,908	$ 338	$ 166	$ 53,080
Securities held to maturity:				
U.S. agency mortgage-backed securities	$ 31,066	$ 219	$ 627	$ 30,658
Non-agency commercial mortgage-backed securities	957	1	47	911
Other securities	100	-	-	100
Total securities held to maturity	$ 32,123	$ 220	$ 674	$ 31,669

December 31, 2013	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Securities available for sale:				
U.S. agency mortgage-backed securities	$ 18,554	$ 140	$ 49	$ 18,645
Asset-backed securities	15,201	42	37	15,206
Corporate debt securities	8,973	49	15	9,007
U.S. agency notes	4,239	1	104	4,136
Certificates of deposit	3,650	4	2	3,652
Non-agency residential mortgage-backed securities	616	11	34	593
Non-agency commercial mortgage-backed securities	271	8	-	279

Other securities	100	-	-	100
Total securities available for sale	$ 51,604	$ 255	$ 241	$ 51,618
Securities held to maturity:				
U.S. agency mortgage-backed securities	$ 29,260	$ 161	$ 921	$ 28,500
Non-agency commercial mortgage-backed securities	958	-	68	890
Other securities	100	-	-	100
Total securities held to maturity	$ 30,318	$ 161	$ 989	$ 29,490

Schwab Bank pledges securities issued by federal agencies to secure certain trust deposits. The fair value of these pledged securities was $131 million at March 31, 2014.

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THE CHARLES SCHWAB CORPORATION

Notes to Condensed Consolidated Financial Statements

(Tabular Amounts in Millions, Except Per Share Data, Ratios, or as Noted)

(Unaudited)

A summary of securities with unrealized losses, aggregated by category and period of continuous unrealized loss, is as follows:

March 31, 2014	Less than 12 months Fair Value	Unrealized Losses	12 months or longer Fair Value	Unrealized Losses	Total Fair Value	Unrealized Losses
Securities available for sale:						
U.S agency mortgage-backed securities	$ 6,119	$ 37	$ 176	$ 1	$ 6,295	$ 38
Asset-backed securities	1,887	5	769	3	2,656	8
Corporate debt securities	1,180	8	400	1	1,580	9
U.S. agency notes	3,909	81	-	-	3,909	81
Certificates of deposit	1,050	-	98	2	1,148	2
Non-agency residential mortgage-backed securities	59	1	352	27	411	28
Total	$ 14,204	$ 132	$ 1,795	$ 34	$ 15,999	$ 166
Securities held to maturity:						
U.S. agency mortgage-backed securities	$ 15,147	$ 438	$ 2,591	$ 189	$ 17,738	$ 627
Non-agency commercial mortgage-backed securities	444	23	338	24	782	47
Total	$ 15,591	$ 461	$ 2,929	$ 213	$ 18,520	$ 674
Total securities with unrealized losses (1)	$ 29,795	$ 593	$ 4,724	$ 247	$ 34,519	$ 840

(1) The number of investment positions with unrealized losses totaled 264 for securities available for sale and 154 for securities held to maturity.

December 31, 2013	Less than 12 months Fair Value	Unrealized Losses	12 months or longer Fair Value	Unrealized Losses	Total Fair Value	Unrealized Losses
Securities available for sale:						
U.S. agency mortgage-backed securities	$ 5,044	$ 47	$ 93	$ 2	$ 5,137	$ 49
Asset-backed securities	6,391	33	591	4	6,982	37

Corporate debt securities	1,802	14	499	1	2,301	15
U.S. agency notes	3,636	104	-	-	3,636	104
Certificates of deposit	-	-	299	2	299	2
Non-agency residential mortgage-backed securities	89	2	374	32	463	34
Total	$ 16,962	$ 200	$ 1,856	$ 41	$ 18,818	$ 241
Securities held to maturity:						
U.S. agency mortgage-backed securities	$ 19,175	$ 698	$ 2,345	$ 223	$ 21,520	$ 921
Non-agency commercial mortgage-backed securities	630	43	260	25	890	68
Total	$ 19,805	$ 741	$ 2,605	$ 248	$ 22,410	$ 989
Total securities with unrealized losses (1)	$ 36,767	$ 941	$ 4,461	$ 289	$ 41,228	$ 1,230

(1) The number of investment positions with unrealized losses totaled 273 for securities available for sale and 193 for securities held to maturity.

Non-agency residential mortgage-backed securities include securities collateralized by loans that are considered to be “Prime” (defined as loans to borrowers with a Fair Isaac Corporation (FICO) credit score of 620 or higher at origination), and “Alt-A” (defined as Prime loans with reduced documentation at origination). Management determined that it does not expect to recover all of the amortized cost of certain of its Alt-A and Prime residential mortgage-backed securities and therefore determined that these securities were other-than-temporarily impaired (OTTI). The Company does not intend to sell these

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Notes to Condensed Consolidated Financial Statements

(Tabular Amounts in Millions, Except Per Share Data, Ratios, or as Noted)

(Unaudited)

securities and it is not “more likely than not” that the Company will be required to sell these securities before anticipated recovery of the unrealized losses on these securities. The Company may recognize an impairment charge equal to the securities’ expected credit losses based on the Company’s cash flow projections for these securities. The expected credit losses are measured as the difference between the present value of expected cash flows and the amortized cost of the securities. There were no impairment charges recognized during the first quarter of 2014. Further deterioration in the performance of the underlying loans in the Company’s non-agency residential mortgage-backed securities portfolio could result in the recognition of impairment losses.

The following table is a rollforward of the amount of credit losses recognized in earnings for OTTI securities held by the Company during the period for which a portion of the impairment was recognized in or reclassified from other comprehensive income:

	Three Months Ended March 31,	
	2014	2013
Balance at beginning of period	$ 169	$ 159
Credit losses recognized into current period earnings on debt securities for which an other-than-temporary impairment was not previously recognized	-	-
Credit losses recognized into current period earnings on debt securities for which an other-than-temporary impairment was previously recognized	-	4
Balance at end of period	$ 169	$ 163

The maturities of securities available for sale and securities held to maturity at March 31, 2014, are as follows:

	Within 1 year	After 1 year through 5 years	After 5 years through 10 years	After 10 years	Total
Securities available for sale:					
U.S. agency mortgage-backed securities (1)	$ -	$ 1,005	$ 4,015	$ 13,514	$ 18,534
Asset-backed securities	-	1,513	4,109	11,103	16,725
Corporate debt securities	1,065	8,022	-	-	9,087

U.S. agency notes	-	4,410	-	-	4,410
Certificates of deposit	1,502	1,924	-	-	3,426
Non-agency residential mortgage-backed securities (1)	-	3	-	575	578
Non-agency commercial mortgage-backed securities (1)	-	-	-	320	320
Total fair value	$ 2,567	$ 16,877	$ 8,124	$ 25,512	$ 53,080
Total amortized cost	$ 2,560	$ 16,907	$ 8,047	$ 25,394	$ 52,908
Securities held to maturity:					
U.S. agency mortgage-backed securities (1)	$ -	$ 609	$ 13,036	$ 17,013	$ 30,658
Non-agency commercial mortgage-backed securities (1)	-	-	344	567	911
Other securities	100	-	-	-	100
Total fair value	$ 100	$ 609	$ 13,380	$ 17,580	$ 31,669
Total amortized cost	$ 100	$ 601	$ 13,717	$ 17,705	$ 32,123

(1) Mortgage-backed securities have been allocated to maturity groupings based on final contractual maturities. Actual maturities will differ from final contractual maturities because borrowers on a certain portion of loans underlying these securities have the right to prepay their obligations.

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Proceeds and gross realized gains from sales of securities available for sale are as follows:

	Three Months Ended March 31,	
	2014	2013
Proceeds	$ 1,285	$ -
Gross realized gains	$ 1	$ -

4.Loans to Banking Clients and Related Allowance for Loan Losses

The composition of loans to banking clients by loan segment is as follows:

	March 31, 2014	December 31, 2013
Residential real estate mortgages	$ 8,050	$ 8,006
Home equity lines of credit	3,018	3,041
Personal loans secured by securities	1,536	1,384
Other	35	36
Total loans to banking clients (1)	12,639	12,467
Allowance for loan losses	(48)	(48)
Total loans to banking clients – net	$ 12,591	$ 12,419

(1) All loans are evaluated for impairment by loan segment.

The Company has commitments to extend credit related to unused home equity lines of credit (HELOCs), personal loans secured by securities, and other lines of credit, which totaled $5.9 billion and $5.7 billion at March 31, 2014 and December 31, 2013, respectively. All of the personal loans were fully collateralized by securities with fair values in excess of borrowings at March 31, 2014 and December 31, 2013.

Changes in the allowance for loan losses were as follows:

Three Months Ended	March 31, 2014			March 31, 2013		
	Residential real estate mortgages	Home equity lines of credit	Total	Residential real estate mortgages	Home equity lines of credit	Total
Balance at beginning of period	$ 34	$ 14	$ 48	$ 36	$ 20	$ 56
Charge-offs	(1)	(1)	(2)	(2)	(2)	(4)
Recoveries	-	1	1	1	-	1
Provision for loan losses	-	1	1	5	1	6
Balance at end of period	$ 33	$ 15	$ 48	$ 40	$ 19	$ 59

Included in the loan portfolio are nonaccrual loans totaling $40 million and $48 million at March 31, 2014 and December 31, 2013, respectively. There were no loans accruing interest that were contractually 90 days or more past due at March 31, 2014 or December 31, 2013. Nonperforming assets, which include nonaccrual loans and other real estate owned, totaled $46 million and $53 million at March 31, 2014 and December 31, 2013, respectively. Troubled debt restructurings were not material at March 31, 2014 or December 31, 2013.

Schwab Bank provides a co-branded loan origination program for Schwab Bank clients (the Program) with Quicken Loans, Inc. (Quicken® Loans®). Pursuant to the Program, Quicken Loans originates and services first lien residential real estate mortgage loans (First Mortgages) and HELOCs for Schwab Bank clients. Under the Program, Schwab Bank purchases certain First Mortgages and HELOCs that are originated by Quicken Loans. Schwab Bank sets the underwriting guidelines and pricing for all loans it intends to purchase for its portfolio. Schwab Bank purchased First Mortgages of $286 million and $1.3 billion during the first quarters of 2014 and 2013, respectively. Schwab Bank purchased HELOCs with commitments of

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Notes to Condensed Consolidated Financial Statements

(Tabular Amounts in Millions, Except Per Share Data, Ratios, or as Noted)

(Unaudited)

$172 million and $218 million during the first quarters of 2014 and 2013, respectively. The First Mortgages purchased under the Program are included in the First mortgages loan class in the tables below.

The delinquency analysis by loan class is as follows:

March 31, 2014	Current	30-59 days past due	60-89 days past due	>90 days past due and other nonaccrual loans	Total past due	Total loans
Residential real estate mortgages:						
First mortgages	$ 7,856	$ 6	$ 2	$ 25	$ 33	$ 7,889
Purchased first mortgages	155	1	-	5	6	161
Home equity lines of credit	3,004	3	1	10	14	3,018
Personal loans secured by securities	1,533	3	-	-	3	1,536
Other	35	-	-	-	-	35
Total loans to banking clients	$ 12,583	$ 13	$ 3	$ 40	$ 56	$ 12,639

December 31, 2013	Current	30-59 days past due	60-89 days past due	>90 days past due and other nonaccrual loans	Total past due	Total loans
Residential real estate mortgages:						
First mortgages	$ 7,808	$ 3	$ 4	$ 30	$ 37	$ 7,845
Purchased first mortgages	154	1	-	6	7	161
Home equity lines of credit	3,025	2	2	12	16	3,041
Personal loans secured by securities	1,384	-	-	-	-	1,384
Other	36	-	-	-	-	36
Total loans to banking clients	$ 12,407	$ 6	$ 6	$ 48	$ 60	$ 12,467

In addition to monitoring delinquency, the Company monitors the credit quality of residential real estate mortgages and HELOCs by stratifying the portfolios by the year of origination, borrower FICO scores at origination (Origination FICO), updated borrower FICO scores (Updated FICO), loan-to-value (LTV) ratios at origination (Origination LTV), and estimated current LTV ratios (Estimated Current LTV), as presented in the following tables. Borrowers' FICO scores are provided by an independent third party credit reporting service and were last updated in March 2014. The Origination LTV and Estimated Current LTV ratios for a HELOC include any first lien mortgage outstanding on the same property at the time of the HELOC's origination. The Estimated Current LTV for each loan is estimated by reference to a home price appreciation index.

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(Tabular Amounts in Millions, Except Per Share Data, Ratios, or as Noted)

(Unaudited)

	Residential real estate mortgages			
March 31, 2014	First mortgages	Purchased first mortgages	Total	Home equity lines of credit
Year of origination				
Pre-2010	$ 818	$ 53	$ 871	$ 2,246
2010	479	7	486	189
2011	694	36	730	151
2012	2,333	26	2,359	157
2013	3,304	36	3,340	239
2014	261	3	264	36
Total	$ 7,889	$ 161	$ 8,050	$ 3,018
Origination FICO				
<620	$ 10	$ 1	$ 11	$ 1
620 – 679	94	13	107	19
680 – 739	1,361	32	1,393	571
>740	6,424	115	6,539	2,427
Total	$ 7,889	$ 161	$ 8,050	$ 3,018
Updated FICO				
<620	$ 54	$ 5	$ 59	$ 38
620 – 679	188	8	196	111
680 – 739	1,017	27	1,044	447
>740	6,630	121	6,751	2,422
Total	$ 7,889	$ 161	$ 8,050	$ 3,018
Origination LTV				
<70%	$ 5,352	$ 111	$ 5,463	$ 2,017
>70% – <90%	2,521	45	2,566	977
>90% – <100%	16	5	21	24
Total	$ 7,889	$ 161	$ 8,050	$ 3,018

March 31, 2014	Balance	Weighted Average Updated FICO	Utilization Rate (1)	Percent of Loans that are on Nonaccrual Status
Residential real estate mortgages:				
Estimated Current LTV				
<70%	$ 6,742	776	N/A	0.06 %

>70% – <90%	1,140	765	N/A		0.28	%
>90% – <100%	77	739	N/A		2.53	%
>100%	91	728	N/A		11.43	%
Total	$ 8,050	774	N/A		0.24	%
Home equity lines of credit:						
Estimated Current LTV						
<70%	$ 2,146	774	36	%	0.06	%
>70% – <90%	651	764	47	%	0.28	%
>90% – <100%	116	754	59	%	0.47	%
>100%	105	743	61	%	2.23	%
Total	$ 3,018	770	39	%	0.20	%

(1) The Utilization Rate is calculated using the outstanding HELOC balance divided by the associated total line of credit.

N/A Not applicable.

THE CHARLES SCHWAB CORPORATION

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	Residential real estate mortgages			
	First	Purchased first		Home equity
December 31, 2013	mortgages	mortgages	Total	lines of credit
Year of origination				
Pre-2010	$ 859	$ 55	$ 914	$ 2,304
2010	503	7	510	191
2011	733	38	771	155
2012	2,403	26	2,429	162
2013	3,347	35	3,382	229
Total	$ 7,845	$ 161	$ 8,006	$ 3,041
Origination FICO				
<620	$ 10	$ 1	$ 11	$ -
620 – 679	96	14	110	20
680 – 739	1,352	32	1,384	576
>740	6,387	114	6,501	2,445
Total	$ 7,845	$ 161	$ 8,006	$ 3,041
Updated FICO				
<620	$ 50	$ 5	$ 55	$ 42
620 – 679	209	10	219	106
680 – 739	1,012	29	1,041	453
>740	6,574	117	6,691	2,440
Total	$ 7,845	$ 161	$ 8,006	$ 3,041
Origination LTV				
<70%	$ 5,306	$ 110	$ 5,416	$ 2,040
>70% – <90%	2,523	45	2,568	977
>90% – <100%	16	6	22	24
Total	$ 7,845	$ 161	$ 8,006	$ 3,041

December 31, 2013	Balance	Weighted Average Updated FICO	Utilization Rate (1)	Percent of Loans that are on Nonaccrual Status
Residential real estate mortgages:				
Estimated Current LTV				

<70%	$ 6,649	775	N/A		0.05	%
>70% – <90%	1,181	763	N/A		0.34	%
>90% – <100%	86	732	N/A		4.77	%
>100%	90	730	N/A		10.50	%
Total	$ 8,006	772	N/A		0.26	%
Home equity lines of credit:						
Estimated Current LTV						
<70%	$ 2,127	773	36	%	0.13	%
>70% – <90%	664	762	48	%	0.22	%
>90% – <100%	127	752	59	%	1.22	%
>100%	123	743	63	%	1.34	%
Total	$ 3,041	769	39	%	0.24	%

(1) The Utilization Rate is calculated using the outstanding HELOC balance divided by the associated total line of credit.

N/A Not applicable.

5.Commitments and Contingencies

The Company has clients that sell (i.e., write) listed option contracts that are cleared by the Options Clearing Corporation – a clearing house that establishes margin requirements on these transactions. The Company partially satisfies the margin requirements by arranging unsecured standby letter of credit agreements (LOCs), in favor of the Options Clearing Corporation, which are issued by multiple banks. At March 31, 2014, the aggregate face amount of these LOCs totaled $240 million. There were no funds drawn under any of these LOCs at March 31, 2014. In connection with its securities lending activities, the Company is required to provide collateral to certain brokerage clients. The Company satisfies the collateral requirements by providing cash as collateral.

The Company also provides guarantees to securities clearing houses and exchanges under 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 houses and exchanges, other members would be required to meet shortfalls. The Company’s liability under these arrangements is not quantifiable and may exceed the cash and securities it has posted as collateral. However, the potential requirement for the Company to make payments under these arrangements is remote. Accordingly, no liability has been recognized for these guarantees.

Legal contingencies: The Company is subject to claims and lawsuits in the ordinary course of business, including arbitrations, class actions and other litigation, some of which include claims for substantial or unspecified damages. The Company is also the subject of inquiries, investigations, and proceedings by regulatory and other governmental agencies.

The Company believes it has strong defenses in all significant matters currently pending and is contesting liability and any damages claimed. Nevertheless, some of these matters may result in adverse judgments or awards, including penalties, injunctions or other relief, and the Company may also determine to settle a matter because of the uncertainty and risks of litigation. Described below are certain matters in which there is a reasonable possibility that a material loss could be incurred or where the matter may otherwise be of significant interest to stockholders. With respect to all other pending matters, based on current information and consultation with counsel, it does not appear that the outcome of any such matter could be material to the financial condition, operating results or cash flows of the Company. However, predicting the outcome of a litigation or regulatory matter is inherently difficult, requiring significant judgment and evaluation of various factors, including the procedural status of the matter and any recent developments; prior experience and the experience of others in similar cases; available defenses, including potential opportunities to dispose of a case on the merits or procedural grounds before trial (e.g., motions to dismiss or for summary judgment);

the progress of fact discovery; the opinions of counsel and experts regarding potential damages; potential opportunities for settlement and the status of any settlement discussions; and potential insurance coverage and indemnification. Often, as in the case of the Auction Rate Securities Regulatory Inquiries and Total Bond Market Fund Litigation matters described below, it is not possible to reasonably estimate potential liability, if any, or a range of potential liability until the matter is closer to resolution – pending, for example, further proceedings, the outcome of key motions or appeals, or discussions among the parties. Numerous issues may have to be developed, such as discovery of important factual matters and determination of threshold legal issues, which may include novel or unsettled questions of law. Reserves are established or adjusted or further disclosure and estimates of potential loss are provided as the matter progresses and more information becomes available.

Auction Rate Securities Regulatory Inquiries: Schwab has been responding to industry wide inquiries from federal and state regulators regarding sales of auction rate securities to clients who were unable to sell their holdings when the normal auction process for those securities froze unexpectedly in February 2008. On August 17, 2009, a civil complaint was filed against Schwab in New York state court by the Attorney General of the State of New York (NYAG) alleging material misrepresentations and omissions by Schwab regarding the risks of auction rate securities, and seeking restitution, disgorgement, penalties and other relief, including repurchase of securities held in client accounts. As reflected in a statement issued August 17, 2009, Schwab has responded that the allegations are without merit, and has been contesting all charges. By order dated October 24, 2011, the court granted Schwab's motion to dismiss the complaint with prejudice. The NYAG appealed, and in a decision issued August 29, 2013, the Appellate Division reinstated two of the NYAG's four causes of action. A petition by the NYAG for reconsideration of part of the Appellate Division's decision was denied, and the NYAG has now filed notice with the trial court of its intention to proceed on the remaining two causes of action.

Total Bond Market Fund Litigation: On August 28, 2008, a class action lawsuit was filed in the U.S. District Court for the Northern District of California on behalf of investors in the Schwab Total Bond Market Fund™ (Northstar lawsuit). The lawsuit, which alleges violations of state law and federal securities law in connection with the fund's investment policy, names Schwab Investments (registrant and issuer of the fund's shares) and CSIM as defendants. Allegations include that the fund improperly deviated from its stated investment objectives by investing in collateralized mortgage obligations (CMOs) and investing more than 25% of fund assets in CMOs and mortgage-backed securities without obtaining a shareholder vote. Plaintiffs seek unspecified compensatory and rescission damages, unspecified equitable and injunctive relief, costs and attorneys' fees. Plaintiffs' federal securities law claim and certain of plaintiffs' state law claims were dismissed in proceedings before the court and following a successful petition by defendants to the Ninth Circuit Court of Appeals. On August 8, 2011, the court dismissed plaintiffs' remaining claims with prejudice. Plaintiffs have again appealed to the Ninth Circuit, where the case is currently pending.

Other Regulatory Matters: A subsidiary of optionsXpress Holdings, Inc. (optionsXpress) and an individual employee are respondents in a pending regulatory matter which predates the Company's acquisition of optionsXpress. On April 16, 2012, optionsXpress, Inc., a securities broker-dealer and wholly-owned subsidiary of optionsXpress, was charged by the SEC in an administrative proceeding alleging violations of the firm's close-out obligations under Regulation SHO (short sale delivery rules) in connection with certain customer trading activity. Following trial, in a decision issued June 7, 2013, the judge held that optionsXpress, Inc. violated Regulation SHO and aided and abetted fraudulent trading activity by its customer, and ordered the firm to pay disgorgement and penalties. The Company continues to dispute the allegations and is appealing the decision. The Company has a contingent liability associated with this matter, which was not material at March 31, 2014.

6.Fair Values of Assets and Liabilities

For a description of the fair value hierarchy and the Company's fair value methodologies, including the use of independent third-party pricing services, see note "2 – Summary of Significant Accounting Policies" in the Company's Annual Report on Form 10-K for the year ended December 31, 2013. There were no significant changes in these methodologies during the quarter ended March 31, 2014. The Company did not transfer any assets or liabilities between Level 1 and Level 2 during the quarter ended March 31, 2014, or the year ended December 31, 2013. In addition, the Company did not adjust prices received from the primary independent third-party pricing service at March 31, 2014 or December 31, 2013.

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Financial Instruments Recorded at Fair Value

The following tables present the fair value hierarchy for assets measured at fair value. Liabilities recorded at fair value were not material, and therefore are not included in the following tables:

March 31, 2014	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at Fair Value
Cash equivalents:				
Money market funds	$ 1,037	$ -	$ -	$ 1,037
Commercial paper	-	14	-	14
Total cash equivalents	1,037	14	-	1,051
Investments segregated and on deposit for regulatory purposes:				
Certificates of deposit	-	3,493	-	3,493
U.S. Government securities	-	925	-	925
Total investments segregated and on deposit for regulatory purposes	-	4,418	-	4,418
Other securities owned:				
Schwab Funds® money market funds	208	-	-	208
Equity and bond mutual funds	200	-	-	200
State and municipal debt obligations	-	33	-	33
Equity, U.S. Government and corporate debt, and other securities	1	14	-	15
Total other securities owned	409	47	-	456
Securities available for sale:				
U.S. agency mortgage-backed securities	-	18,534	-	18,534
Asset-backed securities	-	16,725	-	16,725
Corporate debt securities	-	9,087	-	9,087
U.S. agency notes	-	4,410	-	4,410
Certificates of deposit	-	3,426	-	3,426
Non-agency residential mortgage-backed securities	-	578	-	578

Non-agency commercial mortgage-backed securities		-		320		-		320
Other securities		-		-		-		-
Total securities available for sale		-		53,080		-		53,080
Total	$	1,446	$	57,559	$	-	$	59,005

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December 31, 2013	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at Fair Value
Cash equivalents:				
Money market funds	$ 1,141	$ -	$ -	$ 1,141
Commercial paper	-	22	-	22
Total cash equivalents	1,141	22	-	1,163
Investments segregated and on deposit for regulatory purposes:				
Certificates of deposit	-	2,737	-	2,737
U.S. Government securities	-	2,539	-	2,539
Total investments segregated and on deposit for regulatory purposes	-	5,276	-	5,276
Other securities owned:				
Schwab Funds® money market funds	261	-	-	261
Equity and bond mutual funds	208	-	-	208
State and municipal debt obligations	-	32	-	32
Equity, U.S. Government and corporate debt, and other securities	1	15	-	16
Total other securities owned	470	47	-	517
Securities available for sale:				
U.S. agency mortgage-backed securities	-	18,645	-	18,645
Asset-backed securities	-	15,206	-	15,206
Corporate debt securities	-	9,007	-	9,007
U.S. agency notes	-	4,136	-	4,136
Certificates of deposit	-	3,652	-	3,652
Non-agency residential mortgage-backed securities	-	593	-	