SCHWAB CHARLES CORP
Form 10-Q
August 07, 2017

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 June 30, 2017

Commission File Number: 1-9700

THE CHARLES SCHWAB CORPORATION
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	94-3025021 (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, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth 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
Emerging growth company	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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.
1,339,119,476 shares of $.01 par value Common Stock Outstanding on July 31, 2017

THE CHARLES SCHWAB CORPORATION

Quarterly Report on Form 10-Q
For the Quarter Ended June 30, 2017

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Part I – FINANCIAL INFORMATION

THE CHARLES SCHWAB CORPORATION
Management's Discussion and Analysis of Financial Condition and Results of Operations
(Tabular Amounts in Millions, Except Ratios, or as Noted)

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

INTRODUCTION

The Charles Schwab Corporation (CSC) is a savings and loan holding company engaged, through its subsidiaries (collectively referred to as the Company), in wealth management, securities brokerage, banking, asset management, custody, and financial advisory services.

Significant business subsidiaries of CSC include the following:

- Charles Schwab & Co., Inc. (Schwab), a securities broker-dealer;
- 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 (ETFs), which are referred to as the Schwab ETFs™.

The Company provides financial services to individuals and institutional clients through two segments – Investor Services and Advisor Services. The Investor Services segment provides retail brokerage and banking services, retirement plan services, and other corporate brokerage services. The Advisor Services segment provides custodial, trading, banking, and support services as well as retirement business services.
Schwab was founded on the belief that average Americans deserve access to a better investing experience. Although much has changed in the intervening years, the Company's purpose remains clear – to champion every client's goals with passion and integrity. Guided by this purpose and the aspiration of creating the most trusted leader in investment services, management has adopted a strategy described as "Through Clients' Eyes."

Under this approach, the Company's strategic goals are focused on putting clients' perspectives, needs, and desires at the forefront. Because investing plays a fundamental role in building financial security, the Company strives to deliver a better investing experience for its clients – individual investors and the people and institutions who serve them – by disrupting longstanding industry practices on their behalf and providing superior service. The Company aims to offer a broad range of products and solutions to meet client needs with a focus on transparency and value. In addition, management works to couple the Company's scale and resources with ongoing expense discipline to keep costs low and ensure that products and solutions are affordable as well as responsive to client needs. Finally, the Company aims to maximize its market valuation and stockholder returns over time.

Management estimates that investable wealth in the United States (U.S.) is currently well in excess of $30 trillion, which means the Company's $3.04 trillion in client assets represents a market share of less than ten percent, leaving substantial opportunity for growth. The Company's strategy is based on the principle that developing trusted relationships will translate into more assets from both new and existing clients, ultimately driving more revenue and, along with expense discipline, generating earnings growth and building long-term stockholder value.

This Form 10-Q is intended to provide an update on the activity and results of operations for the three and six months ended June 30, 2017 and should be read in conjunction with the 2016 Form 10-K. More information on the Company’s business operations, descriptions of revenue and expense categories, policies and procedures including the Company’s governance and monitoring programs is available in the 2016 Form 10-K. The Company’s recent annual reports on Form 10-K, quarterly reports on Form 10-Q, proxy statements, as well as other filings with the Securities and Exchange Commission (SEC), are available free of charge on the Company’s website, https://www.aboutschwab.com or by request via email (investor.relations@schwab.com), telephone (415-667-7000) or mail (Charles Schwab Investor Relations at 211 Main Street, San Francisco, CA 94105).

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FORWARD-LOOKING STATEMENTS

In addition to historical information, this Quarterly Report on Form 10-Q contains "forward-looking statements" within the meaning of Section 27A of the Securities Act, and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements are identified by words such as "believe," "anticipate," "expect," "intend," "plan," "will," "may," "estimate," "appear," "aim," "target," "could," "would," "continue," and other similar expressions. In addition, any statements refer to expectations, projections, or other characterizations of future events or circumstances are forward-looking statements.

These forward-looking statements, which reflect management's beliefs, objectives, and expectations as of the date hereof, are necessarily estimates based on the best judgment of the Company's senior management. These statements relate to, among other things, the following sections of this Form 10-Q:

- The Company's aim to maximize its market valuation and stockholder returns over time; and the Company's belief that developing trusted relationships will translate into more client assets which drives revenue and, along with expense discipline, earnings growth and stockholder value (see Introduction in Part I, Item 2);
- The expected impact of new accounting standards not yet adopted (see New Accounting Standards in Part I, Item 1, Financial Information - Notes to Condensed Consolidated Financial Statements (Item 1) – Note 2);
- The likelihood of indemnification and guarantee payment obligations (see Commitments and Contingencies in Item 1 – Note 8); and
- The impact of legal proceedings and regulatory matters (see Commitments and Contingencies in Item 1 – Note 8 and Legal Proceedings in Part II, Item 1).

Achievement of the expressed beliefs, objectives, and expectations described in these statements is subject to certain risks and uncertainties that could cause actual results to differ materially from the expressed beliefs, objectives, and expectations. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this Quarterly Report on Form 10-Q or, in the case of documents incorporated by reference, as of the date of those documents.

Important factors that may cause actual results to differ include, but are not limited to:

- General market conditions, including the level of interest rates, equity valuations and trading activity;
- The Company's ability to attract and retain clients, develop trusted relationships, and grow client assets;
- Client use of the Company's investment advisory services and other products and services;
- The level of client assets including cash balances;
- Competitive pressure on pricing;
- Client sensitivity to rates;
- Regulatory guidance;
- Timing, amount, and impact of migration of certain balances from brokerage accounts and sweep money market funds into Schwab Bank;
- Capital and liquidity needs and management;
- The Company's ability to manage expenses;
- The Company's ability to develop and launch new products, services and capabilities in a timely and successful manner;
- The effect of adverse developments in litigation or regulatory matters and the extent of any related charges; and
- Potential breaches of contractual terms for which the Company has indemnification and guarantee obligations.

Certain of these factors, as well as general risk factors affecting the Company, are discussed in greater detail in Part I – Item 1A – Risk Factors in the 2016 Form 10-K.

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OVERVIEW

Management focuses on several client activity and financial metrics in evaluating the Company's financial position and operating performance. For a discussion of the key metrics and a glossary of terms, refer to the Company's 2016 Form 10-K. Results for the second quarters and first halves of 2017 and 2016 are:

	Three Months Ended June 30,			Six Months Ended June 30,		
	2017	2016	Percent Change	2017	2016	Percent Change
Client Metrics:						
Net new client assets (in billions)	$64.5	$26.6	142 %	$103.4	$58.6	76 %
Core net new client assets (in billions)	$46.2	$26.6	74 %	$85.1	$58.6	45 %
Client assets (in billions, at quarter end)	$3,040.6	$2,622.0	16 %			
Average client assets (in billions)	$2,979.2	$2,585.4	15 %	$2,925.5	$2,515.4	16 %
New brokerage accounts (in thousands)	357	271	32 %	719	536	34 %
Active brokerage accounts (in thousands, at quarter end)	10,487	9,977	5 %			
Assets receiving ongoing advisory services (in billions, at quarter end)	$1,539.8	$1,315.5	17 %			
Client cash as a percentage of client assets (at quarter end)	11.5 %	12.6 %				
Company Financial Metrics:						
Net revenues	$2,130	$1,828	17 %	$4,211	$3,592	17 %
Expenses excluding interest	1,221	1,108	10 %	2,459	2,217	11 %
Income before taxes on income	909	720	26 %	1,752	1,375	27 %
Taxes on income	334	268	25 %	613	511	20 %
Net income	575	452	27 %	1,139	864	32 %
Preferred stock dividends and other	45	46	(2)%	84	66	27 %
Net income available to common stockholders	$530	$406	31 %	$1,055	$798	32 %
Earnings per common share – diluted	$.39	$.30	30 %	$.78	$.60	30 %
Net revenue growth from prior year	17 %	17 %		17 %	16 %	
Pre-tax profit margin	42.7 %	39.4 %		41.6 %	38.3 %	
Return on average common stockholders' equity	15 %	13 %		15 %	13 %	
Expenses excluding interest as a percentage of average client assets (annualized)	0.16 %	0.17 %		0.17 %	0.18 %	
Consolidated Tier 1 Leverage Ratio (at quarter end)	7.4 %	7.2 %				

The Company experienced strong client engagement and demand for its contemporary approach to wealth management during the second quarter of 2017. Equity markets rose and volatility remained largely contained. While short-term interest rates increased, reflecting the Federal Reserve's March and June 2017 interest rate hikes, the longer end of the yield curve softened. Against this backdrop, clients opened more than 350,000 new brokerage accounts during the second quarter, bringing year-to-date new accounts to 719,000 – up 34% from a year ago. Heightened client engagement resulted in core net new asset growth of $46.2 billion in the second quarter of 2017, up 74% year-over-year, bringing total client assets to $3.04 trillion at June 30, 2017. Assets enrolled in some form of ongoing advisory service totaled $1.54 trillion at quarter-end, up 17% from a year ago.

The Company's financial model, with multiple revenue streams, operating leverage, and balance sheet strength resulted in a 27% increase in net income to $575 million in the second quarter of 2017, compared to the same period in 2016. Net income for the six months ended June 30, 2017 was $1.1 billion – an increase of 32% from the prior year. The pre-tax profit margins for the second quarter and first half of 2017 were over 40%, leading to a return on average common stockholders' equity of 15% for the second quarter and first half of 2017 compared to 13% for the same periods in 2016.

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RESULTS OF OPERATIONS

Net Revenues

Net revenues of $2.1 billion and $4.2 billion for the second quarter and first half of 2017, respectively, grew 17% from the prior year periods, reflecting significant improvements in both net interest revenue and asset management and administration fees. The following tables and sections present a comparison of the Company's major sources of net revenues:

Three Months Ended June 30,		2017		2016	
	Percent Change	Amount	% of Total Net Revenues	Amount	% of Total Net Revenues
Asset management and administration fees					
Mutual funds and ETF service fees	11 %	$513	24 %	$461	25 %
Advice Solutions	13 %	256	12 %	226	12 %
Other	9 %	76	4 %	70	4 %
Asset management and administration fees	12 %	845	40 %	757	41 %
Net interest revenue					
Interest revenue	34 %	1,127	52 %	840	46 %
Interest expense	76 %	(74)	(3)%	(42)	(2)%
Net interest revenue	32 %	1,053	49 %	798	44 %
Trading revenue					
Commissions	(25)%	142	6 %	190	10 %
Principal transactions	36 %	15	1 %	11	1 %
Trading revenue	(22)%	157	7 %	201	11 %
Other	7 %	75	4 %	70	4 %
Provision for loan losses	(100)%	—	—	2	—
Total net revenues	17 %	$2,130	100 %	$1,828	100 %

Six Months Ended June 30,		2017		2016	
	Percent Change	Amount	% of Total Net Revenues	Amount	% of Total Net Revenues
Asset management and administration fees					
Mutual funds and ETF service fees	16 %	$1,019	24 %	$876	24 %
Advice solutions	13 %	500	12 %	441	12 %
Other	7 %	149	4 %	139	4 %
Asset management and administration fees	15 %	1,668	40 %	1,456	40 %
Net interest revenue					
Interest revenue	32 %	2,182	52 %	1,650	46 %
Interest expense	61 %	(129)	(3)%	(80)	(2)%
Net interest revenue	31 %	2,053	49 %	1,570	44 %
Trading revenue					
Commissions	(21)%	320	7 %	405	11 %
Principal transactions	4 %	29	1 %	28	1 %

Trading revenue	(19	)%	349	8	%	433	12	%
Other	6	%	141	3	%	133	4	%
Provision for loan losses	—		—	—		—	—	
Total net revenues	17	%	$4,211	100	%	$3,592	100	%

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Asset Management and Administration Fees

The following tables present a roll forward of client assets for the Schwab money market funds, Schwab equity and bond funds and ETFs, and Mutual Fund OneSource®. The following funds generated 54% of the asset management and administration fees earned during the second quarter and first half of 2017, compared to 54% and 53% in the same periods in 2016:

	Schwab Money Market Funds		Schwab Equity and Bond Funds and ETFs		Mutual Fund OneSource®	
Three Months Ended June 30,	2017	2016	2017	2016	2017	2016
Balance at beginning of period	$162,887	$167,427	$139,412	$104,953	$204,887	$203,759
Net inflows (outflows)	(6,861)	(6,495)	8,086	3,572	(5,648)	(4,437)
Net market gains (losses) and other [1]	160	19	3,838	2,197	25,510	4,030
Balance at end of period	$156,186	$160,951	$151,336	$110,722	$224,749	$203,352

	Schwab Money Market Funds		Schwab Equity and Bond Funds and ETFs		Mutual Fund OneSource®	
Six Months Ended June 30,	2017	2016	2017	2016	2017	2016
Balance at beginning of period	$163,495	$166,148	$125,813	$102,112	$198,924	$207,654
Net inflows (outflows)	(7,585)	(5,243)	15,261	5,654	(10,239)	(9,179)
Net market gains (losses) and other [1]	276	46	10,262	2,956	36,064	4,877
Balance at end of period	$156,186	$160,951	$151,336	$110,722	$224,749	$203,352

[1] Includes transfers from other third-party mutual funds to Mutual Fund OneSource® in the second quarter of 2017.

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The following tables categorize asset management and administration fees, average client assets, and average fee yields by funds or revenue source:

Three Months Ended June 30,	2017			2016		
	Average Client Assets	Revenue	Average Fee	Average Client Assets	Revenue	Average Fee
Schwab money market funds before fee waivers	$158,974	$ 224	0.57 %	$163,929	$ 239	0.59 %
Fee waivers		(1)			(55)	
Schwab money market funds	158,974	223	0.56 %	163,929	184	0.45 %
Schwab equity and bond funds and ETFs	151,825	52	0.14 %	112,814	52	0.19 %
Mutual Fund OneSource®	220,680	179	0.33 %	201,034	169	0.34 %
Other third-party mutual funds and ETFs (1)	271,503	59	0.09 %	252,405	56	0.09 %
Total mutual funds and ETFs (2)	$802,982	513	0.26 %	$730,182	461	0.25 %
Advice solutions (2):						
Fee-based	$199,823	256	0.51 %	$175,973	226	0.52 %
Intelligent Portfolios	17,796	—	—	6,620	—	—
Legacy Non-Fee	18,340	—	—	17,015	—	—
Total advice solutions	$235,959	256	0.44 %	$199,608	226	0.46 %
Other balance-based fees (3)	406,307	64	0.06 %	338,529	58	0.07 %
Other (4)		12			12	
Total asset management and administration fees		$ 845			$ 757	

Six Months Ended June 30,	2017			2016		
	Average Client Assets	Revenue	Average Fee	Average Client Assets	Revenue	Average Fee
Schwab money market funds before fee waivers	$160,881	$455	0.57 %	$166,184	$485	0.59 %
Fee waivers		(9)			(152)	
Schwab money market funds	160,881	446	0.56 %	166,184	333	0.40 %
Schwab equity and bond funds and ETFs	145,363	107	0.15 %	108,103	103	0.19 %
Mutual Fund OneSource ®	211,548	349	0.33 %	197,839	333	0.34 %
Other third-party mutual funds and ETFs (1)	272,065	117	0.09 %	244,820	107	0.09 %
Total mutual funds and ETFs (2)	$789,857	1,019	0.26 %	$716,946	876	0.25 %
Advice solutions (2) :						
Fee-based	$195,791	500	0.51 %	$171,146	441	0.52 %
Intelligent Portfolios	16,020	—	—	5,868	—	—
Legacy Non-Fee	17,890	—	—	16,712	—	—
Total advice solutions	$229,701	500	0.44 %	$193,726	441	0.46 %
Other balance-based fees (3)	397,523	125	0.06 %	328,278	114	0.07 %
Other (4)		24			25	
Total asset management and administration fees		$1,668			$1,456	

(1) Includes Schwab ETF OneSource™.
(2) Average client assets for advice solutions may also include the asset balances contained in the mutual fund and/or ETF categories listed above.

(3) Includes various asset-related fees, such as trust fees, 401(k) recordkeeping fees, and mutual fund clearing fees and other service fees. Beginning in the first quarter of 2017, a prospective methodology change was made to average client assets relating to 401(k) recordkeeping fees to provide improved insight into the associated fee driver, which resulted in an increase of approximately $25 billion. There was no impact to revenue or the average fee.
(4) Includes miscellaneous service and transaction fees relating to mutual funds and ETFs that are not balance-based.

Asset management and administration fees increased by $88 million, or 12%, and $212 million, or 15% in the second quarter and first half of 2017 compared to the same periods in 2016, as a result of further improvement in net money fund revenue from rising rates and growing balances in advised solutions, equity and bond funds, and ETFs. By quarter-end, the yields on all proprietary money fund portfolios were at or above their respective operating expense ratios fully eliminating yield-related fee waivers for the first time since 2008.

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Net Interest Revenue

The following tables present net interest revenue information corresponding to interest-earning assets and funding sources on the condensed consolidated balance sheets:

Three Months Ended June 30,	2017			2016		
	Average Balance	Interest Revenue/ Expense	Average Yield/ Rate	Average Balance	Interest Revenue/ Expense	Average Yield/ Rate
Interest-earning assets:						
Cash and cash equivalents	$8,562	$ 22	1.03 %	$10,888	$ 14	0.52 %
Cash and investments segregated	19,703	41	0.83 %	19,155	22	0.46 %
Broker-related receivables (1)	435	1	0.68 %	685	—	0.20 %
Receivables from brokerage clients	15,827	138	3.50 %	15,027	124	3.32 %
Available for sale securities (2)	48,154	177	1.47 %	71,431	211	1.19 %
Held to maturity securities	107,378	600	2.24 %	53,404	335	2.52 %
Bank loans	15,701	115	2.94 %	14,569	98	2.71 %
Total interest-earning assets	215,760	1,094	2.03 %	185,159	804	1.75 %
Other interest revenue		33			36	
Total interest-earning assets	$215,760	$ 1,127	2.10 %	$185,159	$ 840	1.82 %
Funding sources:						
Bank deposits	$163,711	$ 30	0.07 %	$136,009	$ 8	0.02 %
Payables to brokerage clients	26,125	3	0.05 %	25,302	1	0.01 %
Short-term borrowings	1,393	3	0.86 %	2,038	2	0.39 %
Long-term debt	3,518	31	3.53 %	2,876	26	3.64 %
Total interest-bearing liabilities	194,747	67	0.14 %	166,225	37	0.09 %
Non-interest-bearing funding sources	21,013			18,934		
Other interest expense		7			5	
Total funding sources	$215,760	$ 74	0.14 %	$185,159	$ 42	0.09 %
Net interest revenue		$ 1,053	1.96 %		$ 798	1.73 %

Six Months Ended June 30,	2017			2016		
	Average Balance	Interest Revenue/ Expense	Average Yield/ Rate	Average Balance	Interest Revenue/ Expense	Average Yield/ Rate
Interest-earning assets:						
Cash and cash equivalents	$8,803	$ 39	0.89 %	$10,820	$ 27	0.50 %
Cash and investments segregated	20,755	76	0.74 %	19,710	41	0.42 %
Broker-related receivables (1)	412	1	0.62 %	535	—	0.15 %
Receivables from brokerage clients	15,537	264	3.43 %	14,959	249	3.35 %
Available for sale securities (2)	59,728	428	1.45 %	69,797	409	1.18 %
Held to maturity securities	95,439	1,085	2.29 %	51,830	657	2.55 %
Bank loans	15,615	225	2.91 %	14,487	197	2.73 %
Total interest-earning assets	216,289	2,118	1.97 %	182,138	1,580	1.74 %
Other interest revenue		64			70	
Total interest-earning assets	$216,289	$ 2,182	2.03 %	$182,138	$ 1,650	1.82 %

Funding sources:						
Bank deposits	$163,696	$ 49	0.06 %	$133,814	$ 16	0.02 %
Payables to brokerage clients	26,892	5	0.04 %	26,015	1	0.01 %
Short-term borrowings	1,363	5	0.74 %	1,029	2	0.39 %
Long-term debt	3,305	59	3.60 %	2,877	52	3.63 %
Total interest-bearing liabilities	195,256	118	0.12 %	163,735	71	0.09 %
Non-interest-bearing funding sources	21,033			18,403		
Other interest expense		11			9	
Total funding sources	$216,289	$ 129	0.12 %	$182,138	$ 80	0.09 %
Net interest revenue		$ 2,053	1.91 %		$ 1,570	1.73 %

(1) Interest revenue or expense was less than $500,000 in the period or periods presented.

(2) Amounts have been calculated based on amortized cost.

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Net interest revenue increased $255 million, or 32%, and $483 million, or 31%, in the second quarter and first half of 2017 compared to the same periods in 2016 due to higher interest margins and interest-earning assets driven by growth in bank deposits. As of June 30, 2017 net interest revenue represented 49% of total net revenues, growing from 44% in the same period in the prior year.
Higher short-term interest rates reflecting the Federal Reserve's March and June 2017 interest rate hikes, coupled with growth in interest-earning assets, have resulted in a 23 and 18 basis point improvement in net interest margins to 1.96% and 1.91% during the second quarter and first half of 2017, respectively, compared to the same periods in 2016.
Compared to the prior year, the Company has grown bank deposits through a combination of:

- Gathering additional assets from new and current clients;
- Transferring uninvested cash balances in certain client brokerage accounts to Schwab Bank; and
- Establishing the Schwab Bank sweep feature as the default investment option for uninvested cash balances within all new brokerage accounts as of June 2016.

While there has been significant growth in bank deposits and average interest-earning assets compared to the prior year periods, balances declined from the first quarter due to clients investing more of their cash into the markets.

In March 2017, the Company transferred $24.7 billion of debt securities from the available for sale (AFS) category to the held to maturity (HTM) category. The transfer had no effect on the overall net interest margin. For additional information on the transfer, see Item 1 – Note 3.

Trading Revenue
The following table presents trading revenue and the related drivers:

	Three Months Ended June 30,			Six Months Ended June 30,		
	2017	2016	Percent Change	2017	2016	Percent Change
Daily average revenue trades (in thousands)	311	279	11 %	314	303	4 %
Clients' daily average trades (in thousands)	589	518	14 %	587	566	4 %
Number of trading days	63.0	64.0	(2)%	125.0	125.0	—
Average revenue per revenue trade	$7.96	$11.27	(29)%	$8.91	$11.36	(22)%
Trading revenue	$157	$201	(22)%	$349	$433	(19)%

During the first quarter of 2017, the Company announced two trading price reductions which lowered standard equity, ETF, and option trade commissions from $8.95 to $4.95 and lowered the per contract option fee from $.75 to $.65. Trading revenue decreased by $44 million, or 22%, and $84 million, or 19%, in the second quarter and first half of 2017, respectively, compared to the same periods in 2016, primarily due to these pricing reductions. These reductions in commission rates reflect both the Company's belief that trade pricing should never be an obstacle for choosing Schwab and the Company's commitment to share the benefits of its scale with clients. With these changes, trading revenue represented 8% of total net revenues through the first half of 2017 compared to 12% for the same period in 2016.

Other Revenue

Other revenue increased by $5 million, or 7%, in the second quarter of 2017 compared to the second quarter of 2016 largely due to an increase in realized gains on available for sale securities. Other revenue increased $8 million, or 6%, in the first half of 2017 compared to the same period in 2016, primarily due to the sublease of office space in San Francisco, a gain on the sale of a building in Indianapolis, and an increase in realized gains on available for sale securities.

Order flow revenue was $26 million and $25 million during the second quarters of 2017 and 2016 and $53 million and $52 million during the first halves of 2017 and 2016, respectively.

THE CHARLES SCHWAB CORPORATION
Management's Discussion and Analysis of Financial Condition and Results of Operations
(Tabular Amounts in Millions, Except Ratios, or as Noted)

Expenses Excluding Interest
The following table shows a comparison of expenses excluding interest:

	Three Months Ended June 30,				Six Months Ended June 30,			
	2017	2016	Percent Change		2017	2016	Percent Change	
Compensation and benefits								
Salaries and wages	$371	$339	9	%	$738	$675	9	%
Incentive compensation	191	166	15	%	393	339	16	