



Online Investor Complaint Center

The original resource guide for the dissatisfied online investor

Schwab hit with class-action lawsuit over retroactive charges of mutual fund fees

By [Online Investor Complaint Center](#)

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An aggrieved customer of San Francisco-based Charles Schwab & Co. recently launched a class-action lawsuit against the firm, alleging that the nation's largest online and discount brokerage violated a contract, fiduciary duties to its customers, and statutory and regulatory obligations when it canceled and reprocessed previously confirmed mutual fund transactions to include omitted trading fees.

San Diego resident Tamara S. Ching, represented by San Diego law firm [Krause & Kalfayan](#), filed the class action on October 27, 2000, in San Diego County Superior Court.

Ching is suing on behalf of herself and more than 1,000 customers who sold mutual funds through Schwab's automated trading services during a six-month period last year.

According to the suit, which Schwab removed last month from state court to the U.S. District Court in San Diego, "Schwab unilaterally and retroactively canceled . . . and then reprocessed" customers' months-old mutual fund transactions to add previously uncharged short-term redemption fees.

The fee is a penalty—up to \$199 per trade via automated trading services or \$299 for broker-assisted trades—that Schwab charges short-term mutual fund investors who sell their shares within 180 days of the purchase date.

Schwab then issued new trade confirmations of the cancellations and reprocessed redemptions "with the original transaction dates," alleges the suit.

In the lawsuit, Ching charges that Schwab's reprocessed transactions and retroactive charges, which allegedly occurred on or around September 25, 2000, violated a Schwab account agreement and [Rule 10b-10](#) under the Securities Exchange Act of 1934. The plaintiff also charges



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that “Schwab knowingly and willfully” violated its “fiduciary duties of loyalty, honesty and due care.” The plaintiff further accuses Schwab of having engaged in “‘unfair,’ ‘unlawful,’ and ‘deceptive’” business practices in violation of Sections 17200 and 17500 of the California Business and Professions Code.

“We believe that this was a very shortsighted and ill-advised action by Schwab that illustrates a disturbing disregard for its customers’ rights and its own legal responsibilities,” Ralph Kalfayan, the plaintiff’s lead attorney, told the Online Investor Complaint Center.

“Schwab’s actions unjustly enriched itself at the expense of its clients in the amount of millions of dollars at a time when its clients were suffering from significant market declines,” the suit claims. The class action also alleges that “Schwab retroactively charged these transaction fees even if doing so threw their clients’ accounts into debt.”

The plaintiff is seeking compensatory and exemplary damages, full restitution and disgorgement of allegedly “ill-gotten gains,” a court order to prevent Schwab from “retroactively altering” previously completed and confirmed transactions, all legal fees, and “other appropriate relief.”

The class action stems from what a September 25, 2000 Schwab letter to customers referred to as “a processing error.” In the letter, Ron Carter, a Schwab senior vice president, told short-term mutual fund investors who had sold shares through Schwab’s automated services that the processing error had caused a failure to charge them short-term redemption fees between February 10, 2000, and August 28, 2000.

According to an [article](#) in the September 28, 2000 *Wall Street Journal*, Schwab blamed the six-month failure to charge customers on “a computer-processing error.”

As the Online Investor Complaint Center [reported](#) in an October 12, 2000 article, Schwab’s processing error was one in a [series](#) of many computer and trading system failures that have [plagued](#) Schwab and other major online brokers over the past few years.

In fact, the nation’s second-largest online broker—Menlo Park, California-based E-Trade Group Inc.—has itself been the target of [several](#) class-action lawsuits and [arbitration](#) claims by customers alleging money losses due to trading system glitches and disruptions.



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The U.S. General Accounting Office, the investigative arm of Congress, [focused](#) on these system problems of major online brokers in a May 2000 [report](#) on online trading and the protection of online investors.

The GAO recommended that the Securities and Exchange Commission require online brokers to keep “consistent records” of service failures and to warn investors about the risks of delays and outages. The GAO also recommended that the SEC monitor these records to better protect online investors.

Responding to the Ching class action against Schwab, Schwab spokesperson Morrison Shafroth said, “We believe the lawsuit is without merit, and we have filed a motion to dismiss it.”

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