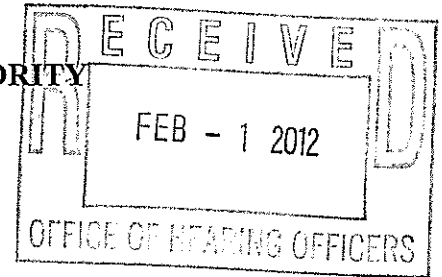


**FINANCIAL INDUSTRY REGULATORY AUTHORITY  
OFFICE OF HEARING OFFICERS**



Department of Enforcement,

Complainant,

v.

Charles Schwab & Company, Inc.  
(CRD No. 5393),

Respondent.

DISCIPLINARY PROCEEDING  
No. 2011029760201

**COMPLAINT AND REQUEST FOR  
EXPEDITED HEARING**

The Department of Enforcement alleges:

**SUMMARY**

1. In October 2011, Charles Schwab & Company, Inc. ("Schwab") amended its customer Account Agreement to include a Waiver of Class Action or Representative Action provision (the "Class Action Waiver"). The Class Action Waiver was part of the firm's predispute arbitration agreement and was sent to almost seven million Schwab customers.

2. The Class Action Waiver contained two provisions that violate NASD and FINRA rules. First, the Class Action Waiver improperly included language requiring customers to waive their right to bring or participate in class actions against Schwab. Second, the Class Action Waiver improperly included language requiring customers to agree that arbitrators have no authority to consolidate more than one party's claims.

3. The language in Schwab's Class Action Waiver purporting to waive a customer's right to bring or participate in class actions against Schwab violated NASD Rule 3110(f)(4)(C) for the period prior to December 5, 2011 and FINRA Rule 2268(d)(3) for the period from

December 5, 2011 to the present.<sup>1</sup> Those provisions prohibit member firms from placing “any condition” in a predispute arbitration agreement that “limits the ability of a party to file any claim in court permitted to be filed in court under the rules of the forums in which a claim may be filed under the agreement.”

4. By violating Rules 3110(f)(4)(C) and 2268(d)(3), Schwab also violated FINRA Rule 2010.

5. The language in the Class Action Waiver purporting to limit customers’ rights to bring or participate in class actions in any manner, and the language purporting to limit the ability of arbitrators to consolidate claims, violated NASD Rule 3110(f)(4)(A) for the period prior to December 5, 2011 and violated FINRA Rule 2268(d)(1) for the period from December 5, 2011 to the present. Those provisions prohibit member firms from placing “any condition” in a predispute arbitration agreement that “limits or contradicts the rules of any self-regulatory organization.”

6. By violating Rules 3110(f)(4)(A) and 2268(d)(1), Schwab also violated FINRA Rule 2010.

#### **REQUEST FOR EXPEDITED HEARING**

7. Schwab’s violative conduct is ongoing. Schwab continues to provide new customers with account agreements that contain the violative language described in this Complaint, and Schwab has done nothing to withdraw or modify the account agreements with that language that it has already provided to almost seven million customers.

8. The Class Action Waiver will likely lead millions of Schwab customers who have received the account agreements to incorrectly believe that they do not have the ability to bring

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<sup>1</sup> As part of the effort to create a consolidated rulebook for FINRA, NASD Rule 3110(f)(4) was converted to FINRA Rule 2268(d), effective December 5, 2011. No changes were made to the language of the rule in connection with the conversion.

or participate in class actions against Schwab, or to seek consolidation of their claims by an arbitration panel.

9. To address these widespread and ongoing violations in an effective and timely manner, the Department of Enforcement requests an expedited hearing in this matter.

#### **RESPONDENT AND JURISDICTION**

10. Charles Schwab & Company, Inc. is a member firm that has been registered with FINRA since 1970. Schwab maintains 340 offices nationwide and has more than 7,000 registered individuals.

11. In its membership application with FINRA (then known as NASD), and in subsequent amendments to that application, Schwab agreed to abide by and adhere to FINRA's rules.

#### **STATEMENT OF FACTS**

12. In October 2011, Schwab sent amendments to its account agreement to its customers, along with their September 2011 monthly account statements. Over 6.8 million copies of the amendments were sent by Schwab to its customers in the first week of October 2011. Under the terms of the account agreement, the amendments were effective upon notification to customers.

13. The amendments included a provision entitled "Waiver of Class Action or Representative Action." That provision included the following language:

Neither you nor Schwab shall be entitled to arbitrate any claims as a class action or representative action, and the arbitrator(s) shall have no authority to consolidate more than one parties' [sic] claims or to proceed on a representative or class action basis.

You and Schwab agree that any actions between us and/or Related Third Parties shall be brought solely in our individual capacities. You and Schwab hereby waive any right to bring a class action, or any type of representative action against each other or any Related Third Parties in court. You and Schwab waive any right to participate as a class member,

or in any other capacity, in any class action or representative action brought by any other person, entity or agency against Schwab or you.

14. The Class Action Waiver was also included in account agreements for new accounts opened by Schwab on or after October 1, 2011. Moreover, Schwab continues to provide copies of the Class Action Waiver to all customers who open new accounts with the Firm. Since October 1, 2011, the Class Action Waiver has been included in accounts agreements for tens of thousands of new Schwab customers.

**FIRST CAUSE OF ACTION**  
**PLACING LANGUAGE IN PREDISPUTE ARBITRATION AGREEMENTS THAT LIMITS THE**  
**ABILITY OF CUSTOMERS TO FILE CLAIMS IN COURT**  
**VIOLATIONS OF NASD RULE 3110(f)(4)(C) AND FINRA RULES 2268(d)(3) AND 2010**

15. The Department realleges and incorporates by reference paragraphs 12 through 14 above.

16. NASD Rule 3110(f)(4)(C) and FINRA Rule 2268(d)(3) each prohibit member firms from including “any condition” in predispute arbitration agreements that “limits the ability of a party to file any claim in court permitted to be filed in court under the rules of the forums in which a claim may be filed under the agreement.” NASD Rule 3110(f)(4)(C) was effective at all times relevant hereto until December 4, 2011. FINRA Rule 2268(d)(3), which contains the same language that was contained in NASD Rule 2268(d)(3), became effective on December 5, 2011.

17. As set forth above, Schwab has placed language, and continues to place language, in its predispute arbitration agreements providing that customers waive their rights to file or participate in class actions against Schwab in court.

18. The FINRA Code of Arbitration Procedure makes clear that class actions are permitted under the rules of FINRA arbitration. For instance, Rule 12204 of the Code of Arbitration Procedure states that class action claims may not be arbitrated under the Code, sets

out a process for determining disputes as to whether a particular matter is part of a class action, and prohibits member firms and associated persons from enforcing arbitration agreements with respect to claims that are the subject of a certified or putative class action until certain events have occurred. For example, Rule 12204 (d) provides that a firm may not enforce an arbitration agreement “against a member of a certified or putative class action” until class certification is denied, the class is decertified, the member of the certified or putative class is excluded from the class, or the member of the certified or putative class elects not to participate or withdraws from the class.

19. FINRA Rule 2268 requires that the provisions set out in paragraph 18 regarding class actions be set forth in customer agreements. Schwab’s customer agreements contain those disclosures.

20. By attempting to limit customers’ ability to bring or participate in class action claims through the Class Action Waiver, Schwab violated NASD Rule 3110(f)(4)(C) from October 2011 until December 4, 2011 and violated FINRA Rule 2268(d)(3) from December 5, 2011 to the present. By virtue of those violations, Schwab violated FINRA Rule 2010.

**SECOND CAUSE OF ACTION  
PLACING LANGUAGE IN PREDISPUTE ARBITRATION AGREEMENTS  
THAT CONTRADICTS FINRA RULES  
VIOLATIONS OF NASD RULE 3110(f)(4)(A) AND FINRA RULES 2268(d)(1) AND 2010**

21. The Department realleges and incorporates by reference paragraphs 12 through 20 above.

22. NASD Rule 3110(f)(4)(A) and FINRA Rule 2268(d)(1) each prohibit member firms from including “any condition” in predispute arbitration agreements that “limits or contradicts the rules of any self-regulatory organization.” NASD Rule 3110(f)(4)(A) was effective at all times relevant hereto until December 4, 2011. FINRA Rule 2268(d)(1), which

contains the same language that was contained in NASD Rule 3110(f)(4)(A), became effective on December 5, 2011.

23. As set forth above, Schwab has placed language, and continues to place language, in its predispute arbitration agreements that requires customers to waive the right to bring or participate in any manner in class actions against Schwab.

24. This language is contrary to the provisions of the Code of Arbitration Procedure. Rule 12204(d) of the Code provides:

A member or associated person may not enforce any arbitration agreement against a member of a certified or putative class action with respect to any claim that is the subject of the certified or putative class action *until*:

- The class certification is denied;
- The class is decertified;
- The member of the certified or putative class is excluded from the class by the court; or
- The member of the certified or putative class elects not to participate in the class or withdraws from the class according to conditions set by the court, if any.

[Emphasis added]

25. Thus, under the Code of Arbitration Procedure, customers can bring and participate in class actions in the manner set out in Rule 12204. Schwab's Class Action Waiver limits and contradicts the provisions of Rule 12204 by requiring customers to waive the right to bring or participate in any manner in any aspect of a class action against Schwab.

26. By placing language in its predispute arbitration agreements that limits and contradicts Rule 12204(d) of the FINRA Code of Arbitration Procedure, Schwab violated NASD Rule 3110(f)(4)(A) from October 2011 until December 4, 2011 and violated FINRA Rule 2268(d)(1) from December 5, 2011 to the present. By virtue of those violations, Schwab violated FINRA Rule 2010.

**THIRD CAUSE OF ACTION  
PLACING LANGUAGE IN PREDISPUTE ARBITRATION AGREEMENTS  
THAT CONTRADICTS FINRA RULES  
VIOLATIONS OF NASD RULE 3110(f)(4)(A) AND FINRA RULES 2268(d)(1) AND 2010**

27. The Department realleges and incorporates by reference paragraphs 12 through 26 above.

28. NASD Rule 3110(f)(4)(A) and FINRA Rule 2268(d)(1) each prohibit member firms from including “any condition” in predispute arbitration agreements that “limits or contradicts the rules of any self-regulatory organization.” NASD Rule 3110(f)(4)(A) was effective at all times relevant hereto until December 4, 2011. FINRA Rule 2268(d)(1), which contains the same language that was contained in NASD Rule 3110(f)(4)(A), became effective on December 5, 2011.

29. As set forth above, Schwab has placed language, and continues to place language, in its predispute arbitration agreements that purports to limit the ability of arbitrators to consolidate claims of more than one party.

30. This language is contrary to the provisions of the Code of Arbitration Procedure. Rule 12312(a) of the Code of Arbitration Procedure provides that “one or more parties may join multiple claims together in the same arbitration” under certain circumstances. Rule 12312(b) states:

After all responsive pleadings have been served, claims joined together under paragraph (a) of this rule may be separated into two or more arbitrations by the Director before a panel is appointed, or by the panel after the panel is appointed. *A party whose claims were separated by the Director may make a motion to the panel in the lowest numbered case to reconsider the Director's decision.* [Emphasis added]

31. Rule 12312(b) thus provides that arbitrators have the authority to consolidate claims. Schwab's Class Action Waiver contradicts that rule by providing that the parties agree that arbitrators have no such authority.

32. By placing language in its predispute arbitration agreements that contradicts Rule 12312(b) of the FINRA Code of Arbitration Procedure, Schwab violated NASD Rule 3110(f)(4)(A) from October 2011 until December 4, 2011 and violated FINRA Rule 2268(d)(1) from December 5, 2011 to the present. By virtue of those violations, Schwab violated FINRA Rule 2010.

#### **RELIEF REQUESTED**

WHEREFORE, the Department respectfully requests that the Panel:

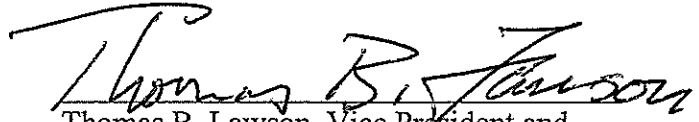
- A. make findings of fact and conclusions of law that Respondent committed the violations charged and alleged herein;
- B. order that Respondent cease from further violating FINRA Rule 2268;
- C. order that one or more of the sanctions provided under FINRA Rule 8310(a), including monetary sanctions, be imposed;
- D. order that Respondent(s) bear such costs of proceeding as are deemed fair and appropriate under the circumstances in accordance with FINRA Rule 8330; and
- E. impose any other fitting sanction.



FINRA DEPARTMENT OF ENFORCEMENT

Dated: Feb. 1, 2012

Respectfully submitted,



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FINRA Department of Enforcement

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