

**IN THE DISTRICT COURT OF THE VIRGIN ISLANDS
DIVISION OF ST. THOMAS AND ST. JOHN**

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In re CHARLES SCHWAB & CO.)

SECURITIES LITIGATION)

) CIV. NO. 1999-020

_____)

) CLASS ACTION

RE: ALL ACTIONS)

) JURY TRIAL DEMANDED

_____)

CONSOLIDATED AMENDED COMPLAINT

1. Plaintiffs, by their attorneys, allege for the Complaint, as follows against defendants Charles R. Schwab ("Charles"), Charles Schwab & Co., ("Schwab") and an affiliate of Schwab's corporate parent, Mayer & Schweitzer, Inc. ("M&S"). The allegations are based upon the investigation of their counsel, except as to the allegations specifically pertaining to plaintiffs and their counsel. Counsels' investigation conducted on plaintiffs' behalf, included, among other things: (i) an analysis of publicly-available news articles and reports; (ii) a review and analysis of public filings including, but not limited to, the M&S disciplinary files of the NASD and Schwab's annual and fiscal quarterly reports; (iii) press releases issued by defendants; and (iv) other matters of public record. The allegations as to all other matters are made upon information and belief and are based

upon, inter alia, an investigation made by plaintiffs' attorneys, which included among other things: direct and indirect contact with Schwab and its customers, and research of the applicable law with respect to the claims asserted herein.

NATURE OF CASE

1. This class action arises from defendants' unlawful and fraudulent conduct, in violation of Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act"), Rule 10b-5 promulgated thereunder ("Rule 10b-5"), and applicable regulatory and common law, to benefit themselves at the expense and to the detriment of plaintiffs, and other members of the Class, by refusing and failing to buy or sell securities at the best reasonably available prices. In particular, even though defendants knew that they could easily and inexpensively access a number of systems that frequently provide better prices for the execution of sell or buy orders, systems to which the defendants had access and routinely used in the everyday, ordinary course of business, defendants knowingly and/or with deliberate recklessness executed orders on behalf of Schwab customers, including plaintiffs and other members of the Class, at consistently disadvantageous prices. Not only did defendants fail to execute their customers' orders at the best available prices, which the defendants were obligated to do, they also executed orders for the same securities for their own accounts at superior prices to those obtained for their customers, thereby profiting themselves at the expense of Schwab customers. Defendants also fraudulently violated their obligations to plaintiffs and other members of the Class by "selling" customer orders, through M&S and otherwise, to other parties for execution pursuant to defendants' payment for order flow policy, knowing that such orders would not be executed at the best reasonably available prices. In connection with the foregoing purchases and sales of securities by plaintiffs and other members of the Class, defendants misrepresented material facts and omitted material facts, all in violation of applicable federal and common law.
2. Because defendants held themselves out as experienced, professionals ready, willing, and able to execute orders on behalf of retail customers, including plaintiffs and other members of the Class, they implicitly represented that they would deal fairly and professionally at all times with such retail customers and, inter alia, seek out and obtain the best available prices for orders given to them by checking all relevant and reasonably available bids and offers to, respectively, buy or sell such securities, including consummating transactions on the exchanges most advantageous to Schwab customers. Moreover, throughout the Class Period defined herein, defendants made public statements in newspaper advertisements, marketing solicitations and other public documents which touted their commitment to principles of fair dealing, including their purported "discounting of commissions" as compared to so-called "full-service" brokers. Defendants' image, skills, experience and manner of dealing with its customers were promoted by, inter alia, a Schwab publication entitled "The Essential Investor" in which Charles R. Schwab ("Charles") states boldly at page 3:

"When it comes to investing, there are some essentials that you -- and all investors -- want. You want a reliable source of information. . . . And, of course, you want to know you're getting a fair deal whenever you trade."

In furtherance of its image of putting its customers first, at page 14 of "The Essential Investor," Schwab maintains that "Schwab's everyday low commissions mean more of your money goes to work for you." Schwab's execution of customer orders at prices defendants knew were inferior for purposes of profiting themselves, without disclosing such practices to plaintiffs and other members of the Class, constituted fraudulent conduct and rendered defendants' implicit and explicit representation of fair dealing, "best execution" and "discounting" fraudulently false and misleading.

1. Similarly, a Schwab advertisement in the August 8, 1999 New York Times quoted defendant Charles on investing:

Despite this representation by defendant Charles concerning the absolute right of plaintiffs and other members of the Class to know and understand how their broker Schwab has been and is compensated, all the defendants violated the securities laws and engaged in other violations of

law by making material misstatements and omissions to plaintiffs and other members of the Class with regard to broker compensation and the economic impact of doing business with Schwab.

1. In accepting orders, defendants assumed an independent duty to disclose all conflicts of interest to plaintiffs and other members of the Class regarding transactions undertaken by defendants on behalf of plaintiffs and other members of the Class. Defendants' repeated knowing and/or deliberately reckless failure to seek out and obtain "best execution" prices for plaintiffs and the Class while secretly executing trades at prices more favorable to themselves and/or selling orders knowing that they would not be executed at the best available prices, were material conflicts of interest. Defendants' knowing and/or deliberately reckless failure to disclose such conflicts is actionable under Section 10(b), Rule 10b-5 and applicable common law.
2. The details of the wrongs alleged herein are not known to any of the plaintiffs personally upon actual knowledge and are of the type that are uniquely and exclusively within the knowledge of defendants and certain present and former customers and employees of the defendants who have uncovered such wrongdoing.

JURISDICTION AND VENUE

1. This action is brought pursuant to Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder on behalf of the plaintiffs and all other persons similarly situated. This action also contains pendent common law claims for violations of defendants' common law duties as agents and fiduciaries of plaintiffs and other members of the Class, and arising out of defendants' breaches of their contractual obligations to plaintiffs and the Class.
2. The Court has jurisdiction over the subject matter of plaintiffs' claims under the Exchange Act, pursuant to Section 27 of the Exchange Act, and jurisdiction over plaintiffs' common law claims pursuant to supplemental jurisdiction, 28 U.S.C. § 1367.
3. Venue is proper in this Court pursuant to Section 27 of the Exchange Act and 28 U.S.C. § 1391(b).
4. Many of the acts and transactions alleged and complained of herein, including the entry and execution of trades through Schwab and/or M&S, occurred or were initiated in the Virgin Islands. In addition, certain of the plaintiffs and other members of the Class reside in the Virgin Islands and defendants regularly do business with customers within the Virgin Islands.
5. In connection with the acts alleged in the Complaint, defendants, directly or indirectly, used the means and instrumentalities of interstate commerce, including the United States mails, telephone communications and facilities of national and regional securities exchanges.

THE PARTIES

A. Plaintiffs

1. Plaintiff Eva Cooper, a resident of St. Thomas, and a citizen of the United States Virgin Islands, placed buy and sell orders for stocks through her retail Schwab account during the Class Period as defined herein. Plaintiff, who also maintains a residence in New York, had a so-called "Schwab One Account" through which she has conducted transactions in securities listed on major stock exchanges and otherwise.
2. Plaintiff Philip T. Zuccala, a resident of New York, placed buy and sell orders for stocks through his retail Schwab account during the Class Period as defined herein. Plaintiff has maintained a so-called "Schwab One Account" through which he has conducted transactions in securities listed on major stock exchanges and otherwise for several years.
3. Plaintiff Nine Rodeo West Ltd. is a California Corporation that placed buy and sell orders for stocks through its retail Schwab account during the Class Period as defined herein. Plaintiff has maintained a so-called "Schwab One Account" through which it has conducted transactions in securities listed on major stock exchanges and otherwise for several years.

B. Defendants

1. Defendant Charles Schwab & Co., Inc. ("Schwab") is a Delaware corporation doing business throughout the United States and its territories, including within the Virgin Islands. Schwab is a subsidiary, indeed the "principal subsidiary," of Charles Schwab Corp. ("Corp."), according to Corp.'s SEC filings..
2. Schwab is a registered broker-dealer and is a member of the New York Stock Exchange ("NYSE"), the American Stock Exchange ("ASE"), the Philadelphia Stock Exchange, the Pacific Stock Exchange, other principal exchanges and the National Association of Securities Dealers ("NASD").
3. Schwab's customer assets were \$389.7 billion as of July 30, 1998. Corp.'s revenues for the 3rd quarter of 1998 were approximately \$700 million. The overwhelming majority of Corp.'s revenues and profits are derived from Schwab, its "principal subsidiary." Schwab has more than 260 offices located throughout the world, as well as a substantial "on-line" brokerage business which has been gradually overtaking Schwab's traditional brokerage business. Despite its role as a pioneer in the "discount" brokerage business, Schwab has lost substantial market share to lower-priced competitors including, more recently, "on-line" competitors. As recently as 1997, Schwab earned \$63 on every trade it handled, which average has fallen to \$53 or less. One means by which defendants have compensated for Schwab's revenue loss (from the increased competition which among other things lowered commission rates) was to engage in the illegal practices described herein which lowered Schwab's operating costs at the expense of its customers.
4. Defendant M&S is another subsidiary of Corp and an affiliate of Schwab.
5. M&S, also a registered broker-dealer, is one of the largest wholesale dealers on the NASDAQ market.
6. M&S previously has paid fines to settle charges that it did not seek out and obtain best execution for its clients and that it engaged in improper recordkeeping with respect thereto.
7. On or about October 21, 1997, M&S was fined \$200,000 as part of settling NASD charges (without admitting or denying the allegations) that it failed to provide the best execution possible for its customers on certain occasions from December 1995 through

June 1996 (which for the most part was during the Class Period herein); failed to establish, maintain and enforce written supervisory procedures to prevent these violations, and failed to maintain records of the time and manner in which M&S sent customer limit orders to other market makers for execution.

8. On March 20, 1996, M&S was fined \$75,000 as part of settling similar NASD charges (without admitting or denying the allegations) that it failed to provide best execution for its customers and that it engaged in "recordkeeping" violations.
9. M&S was also one of more than 30 broker-dealers which agreed to pay a total of \$910 million to settle antitrust price fixing charges related to illegally fixing the spread between the bid and asked price on NASDAQ securities, a substantial portion of which were sold and purchased through defendant Schwab.
10. In another settlement related to the price obtained for customers, M&S agreed to an Acceptance, Waiver and Consent ("AWC") with the NASD pursuant to which it was fined \$18,500, required to attend a compliance conference with NASDR staff, and required to conduct a rule education class for its traders. In the AWC, M&S agreed to the entry of findings (without admitting or denying the allegations) that it entered quotations in securities on the NASDAQ Stock Market that exceeded the parameters for maximum allowable spreads.
11. At least one or more of each of the plaintiff's trades with defendant Schwab as broker, were executed through Schwab or M&S at prices other than the most favorable ones available or where defendants did not provide fair dealing. Notwithstanding the events described in paragraphs 21-25, supra, the defendants conspired with one another to "conduct business as usual," thereby benefitting themselves at the expense of Schwab's unsuspecting retail customers.
12. Although Corp.'s SEC public filings indicate that M&S is a wholly-owned subsidiary of Corp., defendant Schwab in this action to date has asserted that "M&S is wholly owned by Schwab." Reply in Support of Charles Schwab & Co., Inc.'s Motion to Transfer Venue at 6.
13. In addition, defendant Schwab in this action to date has asserted that Schwab's firm-wide policies concerning order routing and order execution, which include those policies applicable to M&S, "are formulated at Schwab's headquarters in San Francisco, California. Such policies are generally set by Schwab's Vice Presidents and Senior Vice Presidents. These individuals work at Schwab's headquarters in San Francisco." Defendant Charles Schwab & Co., Inc.'s Motion to Transfer Venue, Jess Pearce Declaration ¶9; Defendant Charles Schwab & Co., Inc.'s Objections and Answers to Plaintiffs' First Set of Interrogatories, Answer No. 13.
14. As Corp.'s "principal subsidiary," Schwab, in its unilateral discretion, can formulate and implement policies for M&S and it can veto the implementation of any policy proposed by M&S.
15. Regardless of whether defendant M&S is or is not wholly-owned by Schwab, defendant Schwab at all relevant times was a "control person" of M&S pursuant to §20(a) of the Exchange Act.
16. Defendant Charles R. Schwab ("Charles") is Chairman of the Board of Directors of Schwab, and Chairman and Co-Chief Executive Officer of Corp. in which he has full responsibility and authority for the management of Corp. During most of the relevant time period, he was the sole Chief Executive Officer of Corp. At all relevant times, as

Corp.'s largest shareholder and Chairman and CEO/Co-CEO in charge of its management, and by virtue of his position as Chairman of Schwab, he was a "control person" of both Schwab and M&S pursuant to §20(a) of the Exchange Act.

17. Defendants Charles, Schwab and M&S are hereinafter collectively referred to as "defendants." The principal offices of defendant M&S is located in Jersey City, New Jersey and of Schwab and Charles in San Francisco, California.

CLASS ACTION ALLEGATIONS

1. Plaintiffs brings this action as a class action pursuant to Federal Rule of Civil Procedure 23 on behalf of all those persons ("the Class") who placed orders to purchase or sell shares of stock or other securities through retail (*i.e.*, non-institutional) accounts with Schwab between February 1, 1996 to the date of filing of the first of the Complaints in this consolidated action ("the Class Period") and were damaged by the conduct alleged herein. Excluded from the Class are defendants and any of their parents, subsidiaries, or affiliates (as those terms are used in the federal securities laws) as well as the directors and officers of and members of the immediate families, affiliates, successors and assigns of those directors and officers. Also excluded from the Class are those Schwab customers who received "Primary Market Prices" or "Primary Market Protection" from Schwab or who have already received refunds from Schwab of their damages. The definition of the Class is subject to change following discovery with respect thereto.
2. The members of the Class are so numerous that joinder of all members is impractical. While the exact number of Class members is unknown to plaintiffs at this time and can only be ascertained through appropriate discovery, plaintiffs believe there are at least many thousands of members of the Class. Members of the Class may be identified from trading records Schwab and M&S are required to maintain under the federal securities laws, and the rules and regulations of the NYSE, AMEX and NASD. The members of the Class may be notified of the pendency of this action by mail, using techniques and a form of notice similar to that customarily used in securities class actions arising under the federal securities laws.
3. Plaintiffs' claims are typical of the claims of the members of the Class. Plaintiffs and other members of the Class sustained damages arising out of defendants' wrongful conduct as described in detail herein.
4. Plaintiffs will fairly and adequately protect the interests of the Class. Plaintiffs have retained counsel competent and experienced in class, securities and/or other complex litigation.
5. A class action is superior to other available methods for the fair and efficient adjudication of this controversy since joinder of all members is impracticable. Furthermore, as the damages suffered by individual members of the Class may be relatively small, the expense and burden of individual litigation make it impracticable for the individual members of the Class to redress the wrongs done to them individually. There will be no difficulty in the management of this action as a class action.
6. Common questions of law and fact exist as to all Class members and predominate over any questions affecting solely individual Class members. Among the questions of law and fact common to the Class are:

(a) Whether defendants failed to fulfill their duty of fair dealing by failing to check alternate sources of price quotes before executing trades on behalf of plaintiffs and other members of the Class;

(b) Whether defendants failed to fulfill their duty of "best execution" by failing to check alternate sources of price quotes before executing trades, and by failing to provide best execution, on behalf of plaintiffs and other members of the Class;

(c) Whether defendants either through in-house matching of orders or through purchase or sale of the same securities on alternate execution sources such as Selectnet or Instinet appropriated an improper benefit in conflict with their duties to plaintiffs and other members of the Class;

(d) Whether defendants, without investigating other markets or market-makers, sold the order flow of plaintiffs and the Class to third parties in exchange for kickback payments while knowingly or with deliberate recklessness failing to know that such third parties would not obtain best execution for those trades;

(e) Whether defendants failed to adequately disclose such practices despite their implicit representation that they would deal fairly, honestly, and in the best interests of plaintiffs and the Class;

(f) Whether such practices and the lack of full and fair disclosure with respect thereto constituted violations of Section 10(b);

(g) Whether such practices and the lack of appropriate disclosure constituted breaches of fiduciary duties under common law in defendants' capacity as agents of plaintiffs and the Class;

(h) Whether such practices by defendants amount to a breach of Schwab's contractual obligations to plaintiffs and the Class; and

(i) Whether the Class has sustained damages and the extent of those damages caused by defendants' wrongful conduct.

FACTUAL BACKGROUND

1. The New York Stock Exchange is the oldest stock exchange in the United States. Securities listed for trading on the NYSE are typically larger, more seasoned companies than those which are traded on the much smaller ASE and otherwise.
2. The National Association of Securities Dealers ("NASD") is a voluntary trade association of securities brokers and dealers. Schwab is a member of the NASD as well as the NYSE and ASE.
3. NASDAQ, the acronym for the National Association of Securities Dealers Automated Quotation system, is the fastest growing stock market in America. In 1984, the share volume on NASDAQ was 159 million shares traded annually, as compared to a volume of 2.3 billion shares traded on the New York Stock Exchange ("NYSE"). By 1993, however, the share volume on NASDAQ was 63.5 billion shares traded annually, as compared to a volume of 66.9 billion shares traded on the NYSE. Moreover, in 1993, the volume of shares traded on NASDAQ was 15 times greater than the volume traded on the American Stock Exchange.
4. Prices for securities traded on the NYSE and ASE are determined on the trading floors of such exchanges. Quotes on the NASDAQ national market system are entered by approximately 500 market maker firms, including Schwab and its affiliate M&S, each of which trades shares of stock through computer and telephonic communications. Stock quoted on the NASDAQ trades "over-the-counter" or "OTC". NASDAQ price quotes are displayed on the "NASDAQ Level 2 Screen" (the "Level 2 Screen"). The Level 2 Screen is not an execution system and the quotes displayed on the Level 2 Screen do not list any quantity of stock available at quoted bid or asked prices.

Defendants' Duties to Plaintiffs and Other Members of the Class

1. Defendants are brokers and dealers as those terms are defined within 15 U.S.C. §§ 78c(a)(4)-(5).
2. As broker-dealers, defendants Schwab and M&S each are subject to and must obey the securities laws of the United States of America, the rules and regulations of the Securities

and Exchange Commission, and the rules and regulations of the NYSE, the AMEX, the NASD and the other exchanges and Self-Regulatory Organizations of which each is a member.

3. In their capacity as broker-dealers, one of the rules and regulations which Schwab and M&S each must obey is that they have a duty to deal fairly with plaintiffs and other members of the Class.
4. In their capacity as broker-dealers, one of the rules and regulations which Schwab and M&S each must obey is the duty of "best execution" (and recordkeeping with respect thereto). This duty is applicable both to transactions on an exchange in listed securities and to transactions in unlisted securities on NASDAQ (which usually are made through market-makers). Pursuant to that duty, throughout the Class Period, when defendants received market orders (an order to buy or sell stock at the prevailing "market" price) or limit orders (an order to buy or sell a stock at a price specified by the customer) from plaintiffs and/or members of the Class, defendants were required to use reasonable diligence to obtain the best available market price for that order by checking all relevant sources and then ensure that its customers' orders are executed in the best market or by the best market-maker. This obligation constitutes one of the cornerstones of market integrity.
5. Concerning the NASD, as one example, NASD Conduct Rule IM-2310-2(a)(1), "Fair Dealing with Customers" states in relevant part:

Implicit in all member and registered representative relationships with customers and others is the fundamental responsibility for fair dealing. Sales efforts must therefore be undertaken only on a basis that can be judged as being within the ethical standards of the Association's Rules, with particular emphasis on the requirement to deal fairly with the public.

1. Similarly, NASD Conduct Rule 2320(a) states in relevant part:

In any transaction for or with a customer, a member and persons associated with a member shall use reasonable diligence to ascertain the best inter-dealer market for the subject security and buy or sell in such market so that the resultant price to the customer is as favorable as possible under prevailing market conditions.

1. Concerning the New York Stock Exchange, as one example, NYSE Rules 123A.41 and 123A.42 state:

Broker's Obligation in the Handling of Certain Orders

.41 Market orders.- A broker handling a market order is to use due diligence to execute the order at the best price or prices available to him under the published market procedures of the Exchange.

.42 Limited orders.- A broker handling a limited price order is to use due diligence to execute the order at the limit price, or at a better price, if available to him under the published market procedures of the Exchange.

1. Concerning the American Stock Exchange, as one example, AMEX Rules 156(a) and 156(b) state:

Market Order (a) A broker handling a market order is to use due diligence to execute the order at the best price or prices available to him under the published market procedures of the Exchange.

Limited price order (b) A broker handling a limited price order is to use due diligence to execute the order at the limit price, or at a better price, if available to him under the published market procedures of the Exchange.

1. A broker-dealer is required to periodically assess the quality of competing markets to ensure that its order flow is directed to markets providing the most advantageous execution for the customer's order.
2. A broker-dealer is required to periodically assess the quality of competing market-makers to ensure that its order flow is directed to market-makers providing the most advantageous execution for the customer's order.
3. Charles, as a registered person and as a registered principal, and as a senior corporate official and control person of M&S and Schwab, also is subject to and must obey the duties of fair dealing and best execution.
4. As brokers and dealers, throughout the Class Period, Schwab and M&S received tens of thousands of daily orders from Schwab customers, including plaintiffs and other members of the Class, to buy and sell tens of millions of shares of stock and other securities.
5. At relevant times, defendants served as agents to plaintiffs and other members of the Class in connection with the execution of orders placed with Schwab to buy or sell shares of stock or other securities. As agents, defendants also owed certain fiduciary duties to plaintiffs and other members of the Class, including the duties of care and loyalty. Those duties specifically included: (1) the obligation to act in the best interests of plaintiffs and the Class in a fully-informed manner; (2) the duty not to act adversely to plaintiffs and

the Class; (3) the duty to account for profits received in connection with transactions conducted on behalf of plaintiffs and the Class; and (4) the duty to fully disclose the nature and extent of any adverse interest to plaintiffs and the Class.

6. Throughout the Class Period, defendants (among other things) consistently breached their duty of best execution, violated Section 10(b) and Rule 10b-5, breached their common law fiduciary duties of care and loyalty and breached or caused the breach of Schwab's contractual obligations to plaintiffs and the Class, by buying and selling stock on behalf of Schwab's customers, including plaintiffs and other members of the Class, at prices defendants knew or with deliberate recklessness disregarded were inferior to those available from other sources, and by failing to disclose such conduct. By engaging in such practices, defendants not only robbed plaintiffs and other members of the Class of the best available prices for their buy and sell orders, but also generated huge, unjustified profits for themselves at the expense and to the detriment of plaintiffs and other members of the Class in the manner set forth herein.

SUBSTANTIVE ALLEGATIONS

1. Plaintiffs and other members of the Class placed orders to buy and sell securities through Schwab.
2. Schwab typically arranges for the execution of these orders, which may be "executed" in a choice of arenas. Unless the customer has directed that the transaction be executed on a particular exchange, Schwab chooses the arena (or market-maker) or market in which to execute the order.
3. As an example, an order to purchase AT&T Corp. may have been executed on the NYSE, the Philadelphia Stock Exchange, the Midwest Stock Exchange or the Pacific Stock Exchange. The quotation for the execution of the order will not automatically be the same on all of the exchanges. The NYSE and the ASE are referred to as primary markets upon which the transaction costs to Schwab are typically higher than in other markets. The other markets are referred to as "third markets."
4. Orders are also be executed outside of any exchange, such as on NASDAQ.
5. Orders are also "crossed" within house.
6. Although Schwab is required to seek out and obtain the best possible prices for its customers, it is not under an obligation to place transaction orders on any specific exchange or with any specific market-maker. Schwab, directly and/or through M&S, consistently places its orders where it obtains the lowest possible cost of execution or the most "reciprocal" orders or remuneration. Schwab's cost of execution of such transactions is based on volume.
7. Thus, a customer of Schwab could place an order to buy 100 shares of a stock at "the market." The price on the NYSE could be, for example, 34-1/4. Yet the market on the Philadelphia Stock Exchange could be 34-3/8. The stock trades during the day between 34 and 35. The customer believes he has received the best possible execution price but, in fact, has paid 1/8 of a dollar more per share if the order is directed to the Philadelphia Stock Exchange.
8. Schwab directly and/or through M&S primarily "places" its orders for listed securities on third markets. The probability of an execution more favorable to the customer is non-

existent -- although on paper this is a possibility -- since the executions are, if not equal to the primary exchanges, always at higher cost to Schwab's customers.

9. Similarly, with respect to orders on the NASDAQ, Schwab directly and/or through M&S placed limit orders for its customers (usually with market-makers).
10. A customer limit order, whether originating from a public customer or another market maker on behalf of a customer, is an order to buy or sell a stock at a price specified by the customer.
11. Schwab and/or M&S did not, with respect to NASDAQ limit orders which Schwab received from its customers, seek to obtain or obtain best execution in that, inter alia: (1) Schwab and/or M&S did not place the limit orders with the market-maker most suited to obtain best execution; (2) Schwab and/or M&S did not place the limit orders with any market-maker (having failed to transmit member-to-member customer limit orders for securities in which the firm did not make a market to another market-maker which could have filled the order); and (3) Schwab and/or M&S delayed execution of limit orders from Schwab customers (for example, with a sell limit order, until the highest bid from among the competing market-makers equaled the customer's limit price, thereby enabling the market-maker who resold the stock immediately to make the spread between the best bid and the lowest displayed asked price. For a limit buy order, a market-maker will delay executing the limit order until the inside offer drops to the limit order's price.).
12. In sum, although a Schwab customer believes he is saving money on a commission by using Schwab, in derogation of defendant Charles' purported principles as set forth in paragraphs 3 and 4, supra, he is, in fact, paying more because of (among other things) the failure to seek out and to obtain the best price and the costlier execution.
13. As a result of the foregoing practices, plaintiffs and other members of the Class have suffered substantial damages at the hands of the defendants.

Additional Scienter Allegations

1. Schwab and the senior officials in charge of Schwab, including defendant Charles, knew that Schwab was subject to and must conduct their business pursuant to the applicable law, rules and regulations governing the securities brokerage business, including that they must obey their duties of fair dealing and best execution with plaintiffs and other members of the Class.
2. Schwab, M&S, and the senior officials in charge of Schwab and M&S including defendant Charles, all knew that M&S was subject to and must obey the applicable laws, rules and regulations, including that they must obey their duties of fair dealing and best execution (and recordkeeping with respect thereto) with plaintiffs and other members of the Class.
3. Schwab also has compliance and other manuals which state that it and its employees including directors are subject to and must obey the applicable laws, rules and regulations, including their duties of fair dealing and best execution (and recordkeeping with respect thereto).
4. M&S also has compliance and other manuals which state that it and its employees including directors are subject to and must obey the applicable laws, rules and regulations, including their duties of fair dealing and best execution (and recordkeeping with respect thereto).

5. All employees of Schwab, including but not limited to Charles, are given a copy of Schwab's compliance manual.
6. Schwab's compliance and other manuals each require all Schwab employees, including but not limited to Charles, to read the manual and to follow the rules contained therein.
7. M&S's compliance and other manuals each require all M&S employees, including but not limited to Charles, to read the manual and to follow the rules contained therein.
8. As Chairman of Schwab, Charles is required to be a registered person, including a registered principal, in the securities industry.
9. In order to become a registered person and registered principal in the securities industry, an individual must take and pass certain industry examinations.
10. Charles has taken and passed the Series 7 and Series 24 examinations, making him a registered principal in the industry.
11. As Chairman of Schwab, and as a registered person and registered principal in the securities industry who has passed the required examinations, Charles knew that:

(a) Schwab, M&S and he were subject to and must obey the applicable laws, rules and regulations.

(b) He was required to follow the rules contained in Schwab's compliance and other manuals.

(c) He was required to follow the laws, rules and regulations, and the Schwab and M&S compliance and other manuals, all of which require fair dealing and best execution (and recordkeeping with respect thereto).

1. Upon information and belief, during part of the Class Period, a best execution exception report was routinely generated by Schwab and M&S, and disseminated to management.
2. The best execution exception report showed when Schwab and/or M&S was not obeying its duties of fair dealing and best execution with plaintiffs and the Class.
3. Schwab did not periodically assess the quality of competing markets and market-makers to ensure that its order flow was directed to markets and market-makers providing the most advantageous execution for customer orders.
4. M&S did not periodically assess the quality of competing markets and market-makers to ensure that its order flow was directed to markets and market-makers providing the most advantageous execution for customer orders.
5. Charles is a member of the Management Committee of both Schwab and Corp. and of the Customer Quality Assurance Committee of the Corp. Board of Directors.
6. The Management Committee of Schwab is responsible for and in charge of the management of Schwab.
7. Corp. is a holding company which engages in financial services businesses through its subsidiaries, with the principal subsidiary of Corp. being Schwab.
8. The Quality Assurance Committee of the Corp. Board of Directors monitored, with respect to all of Corp's subsidiaries, the service quality provided to customers, including Schwab's customers, which include plaintiffs and the Class.
9. Charles, by virtue of his senior management positions in both Corp. and Schwab, including but not limited to his position on the Quality Assurance Committee, and as a control person of M&S and Schwab, routinely received information concerning whether

Schwab and/or M&S was providing quality service to their customers, including plaintiffs and the Class.

10. Quality Assurance issues necessarily would include, among other issues, fair dealing and best execution.
11. Each defendant has available to it and uses in the ordinary course of business real-time computer information about the securities markets and all of the thousands of individual securities traded thereon which includes but is not limited to: the name and symbol of the security, the price of the last executed transaction, the volume of the last transaction, the current bid and asked price and the number of shares available at that price, information by market-maker on NASDAQ securities and the total volume for the day of each security.
12. Each defendant routinely uses throughout the day, in the ordinary course of business, this real-time computer information.
13. Schwab and M&S each knew when they did not deal fairly with and/or provide the best execution to plaintiffs and the Class because (among other things): each defendant routinely used throughout the day the real-time computer information as part of their transactions; the best execution exception report provided such information; Schwab's payment for order flow policy; each defendant knew when it refused and failed (among other things) to make telephone call(s), as a regular and consistent business practice, to locate and check alternate sources of price quotes and execution and obtain the best execution prices; and the mandatory supervisory responsibilities of its senior managers, and their experience in the industry, including but not limited to Charles.
14. Charles knew when Schwab and/or M&S did not deal fairly with and/or provide the best execution to plaintiffs and the Class because of (among other things): the real-time computer information which he personally uses on a routine basis throughout the day; Schwab's payment for order flow policy; Charles' experience in the securities industry; his responsibilities as a registered principal; the positions and management authority he held in M&S, Corp. and Schwab, of which he was a control person; and the information which routinely was disseminated to him because of those positions, and the reports he received from his experienced senior managers.
15. Each defendant knew that it was required to follow applicable laws, rules and regulations concerning confirmation slips by having them include all material information, including but not limited to information related to best execution and payments for order flow.
16. Each defendant knew that Schwab, in return for directing transactions to certain third parties, received payments for order flow, and that as a result thereof plaintiffs and the Class were not treated fairly and did not receive best execution.
17. Each defendant knew that the computer software interface (which Schwab designed) used by plaintiffs and other members of the Class, for those of their securities transactions with defendants placed on the Internet, provided only certain transaction information so as to materially mislead plaintiffs and other members of the Class in order to conceal and facilitate defendants' fraudulent conduct.
18. Each defendant knew that by breaking the applicable laws, rules and regulations by (among other ways) not obeying its fair dealing and best execution obligations, they would obtain huge additional unlawful and otherwise unjustified profits.
19. Each of the defendants also acted with conscious misbehavior and deliberate recklessness concerning whether it obeyed their fair dealing obligations and sought and obtained the

best execution prices (and obeyed its recordkeeping obligations with respect thereto) as demonstrated by the following facts (among others): (a) each defendant knew the broker-dealer defendants regularly and consistently failed to locate and check alternate sources of price quotes and execution (including but not limited to failing to make telephone calls) and obtain the best execution prices; (b) each defendant knew the broker-dealer defendants did not use their real-time computer information to locate and check alternate sources of price quotes and execution and obtain the best execution prices; (c) each defendant knew that all defendants refused and failed to act upon the best execution exception reports which were routinely generated and disseminated within Schwab and/or M&S; (d) each defendant knew that the computer software interface used by plaintiffs and other members of the Class, for those of their securities transactions with defendants placed on the Internet, was designed by defendants to provide and provided only certain transaction information which would materially mislead plaintiffs and other members of the Class in order to conceal and facilitate defendants' fraudulent conduct; (e) each defendant knew the broker-dealer defendants did not include on the confirmation slips (or online versions thereof) sent to plaintiffs and the Class the required information which would have disclosed that Schwab was not obtaining best execution and, through M&S or otherwise, was knowingly receiving payments for order flow in return for which defendants would not seek to obtain best execution for plaintiffs and other members of the Class; (f) each defendant knew that each broker-dealer defendant, M&S and Schwab, did not periodically assess the quality of competing markets and market-makers to ensure that their order flow was directed to markets and market-makers providing the most advantageous execution for customer orders; (g) M&S had twice agreed to pay fines to settle NASD charges that, during the Class Period, it failed to obtain best executions for its customers, failed to establish, maintain and enforce written supervisory procedures to prevent these violations, and failed to maintain proper books and records; (h) each defendant knew of the settlements of the NASD charges; (i) the conduct embodied in the settlement of the NASD charges also constituted violations of, inter alia, Securities and Exchange Commission requirements and NYSE and AMEX rules and regulations; (j) defendants' conduct at issue in this Class Action also constitutes violations of, inter alia, SEC requirements and NYSE, AMEX and NASD rules and regulations; and (k) M&S paid substantial fines to settle NASD charges that it had violated best execution and related obligations and had been caught by regulatory authorities on not just one but on two occasions.

20. By engaging in these illegal activities, defendants sought to and did unlawfully and otherwise unjustifiably increase Schwab's and M&S' profit per trade in order to compensate for their lost revenue, declining profit and shrinking profit margin caused by an increase in lawful competition.
21. Unlike other executive officers of Corp., Charles is compensated based upon an employment agreement that was entered into between Charles and Corp.
22. Under this agreement, over 80 percent of Charles' compensation is his annual share of Schwab's and M&S' profits (the so-called "bonus"), which is compensation directly related to the financial performance of Corp.
23. Corp.'s "principal subsidiary" and the overwhelming majority of Corp.'s revenues and profits are generated by Schwab, with additional direct and indirect profits generated by M&S.

24. Charles' base salary is \$800,000 per year.
25. Under the employment agreement, Charles' total compensation is directly related to the financial performance of Schwab and M&S, including any illegally obtained profits, because he is eligible for incentive compensation based upon the attainment of pre-established performance targets relative to specified performance standards, including consolidated pretax profit margin and annual net revenue percentage growth of Corp. Under this agreement, Charles' annual "bonus," if any, is a multiple of his base salary.
26. For 1998 alone, Charles received a cash bonus of \$6,145,000, plus stock options on over one million shares of Schwab stock.
27. The amount of Charles' bonus for 1998 and prior years was directly related to the increased profits obtained from the unlawful scheme described herein.

COUNT I, Against Every Defendant
Violations of Section 10(b) and Rule 10b-5

1. Plaintiffs incorporate by reference and reallege paragraphs 1 through 106 as if fully set forth herein.
2. By virtue of its position as a broker-dealer and because it accepted orders to buy or sell shares of stock and/or other securities on behalf of plaintiffs and other members of the Class, Schwab made implicit and explicit representations that Schwab and its affiliate M&S would treat plaintiffs and the Class fairly and execute orders on their behalf only after taking all steps to seek out and obtain the best reasonably available transaction prices. Defendants were also obligated to disclose to plaintiffs and the Class: (a) all conflicts of interest relating to Schwab's executions of orders on behalf of plaintiffs and the Class; (b) all profits defendants obtained in executing orders on behalf of plaintiffs and the Class, and (c) all profits received by defendants "under the table" as a result of the sale of order flow, artificially low transaction costs of Class members and otherwise.
3. In derogation of those duties, and in violation of Section 10(b) and Rule 10b-5, defendants knowingly and/or with deliberate recklessness: (a) employed devices, schemes and artifices to defraud plaintiffs and the Class in connection with the purchase and sale of securities through Schwab; (b) made untrue statements of material fact and/or omitted to state material facts which, in light of the circumstances, were necessary to make the statements made not misleading; and (c) engaged in acts, practices and conduct which operated as a fraud and/or deceit upon plaintiffs and other members of the Class in connection with the purchase and sale of securities, as set forth above.
4. Defendants violated Section 10(b) and Rule 10b-5, among other ways, by engaging in and failing to disclose that they were not fulfilling their duties of fair dealing and of "best execution;" by refusing and failing to check alternate sources of price quotes and execution before executing orders on behalf of plaintiffs and other members of the Class; by refusing to use the best execution exception reports to obtain best execution for plaintiffs and the Class; by not providing best execution of orders on behalf of plaintiffs and other members of the Class, and by selling the order flow of plaintiffs and the Class to third parties in exchange for kickback payments while knowingly or with deliberate

recklessness failing to know that such third parties would not obtain best execution for those trades.

5. Plaintiffs reasonably relied upon defendants' false, misleading and incomplete representations (as set forth in paragraph 3, supra, and otherwise) that they would treat plaintiffs and the Class fairly, would seek out and obtain "best execution" of their buy/sell orders, and would disclose all conflicts with plaintiffs and the Class and profits obtained in connection with executing orders on behalf of plaintiffs and the Class.
6. Defendants' false, misleading and deceptive representations were material. If plaintiffs and the Class had known the true facts concealed by the defendants, they would not have placed their orders with Schwab and/or would have demanded "Primary Market Protection" and refunds, as some Schwab customers who learned of the defendants' illegal activities ultimately did.
7. As a direct and proximate result of defendants' wrongful conduct, plaintiffs and Class members were damaged by the defendants' violations of Section 10(b) and Rule 10b-5 as described herein in an amount which cannot presently be determined.

COUNT II, against Charles and Schwab

Pursuant to Section 20(a) of the Exchange Act

1. Plaintiffs incorporate by reference and reallege paragraphs 1 through 113 as if fully set forth herein.
2. This Count is asserted separately against individual defendant Charles and against Schwab and is based upon Section 20(a) of the Exchange Act.
3. Defendant Charles acted as a controlling person of both Schwab and of M&S within the meaning of Section 20(a) of the Exchange Act.
4. By reason of his positions as an executive officer, director, Management Committees member, and Board committees member, of Schwab and of Corp. as set forth herein, Charles participated in, and/or was aware of, the day-to-day operations of both Schwab and M&S, had intimate knowledge of the financial condition, finances and business practices of both Schwab and M&S, and was provided with or had unlimited access to information and internal reports with respect to the alleged unlawful conduct and copies of the press releases, public filings and other statements, of both Schwab and M&S alleged by plaintiffs to be false and misleading.
5. By virtue of his high-level positions, Charles had the power and authority to cause or to prevent the wrongful conduct complained of herein and he participated meaningfully in the fraud, including but not limited to: Charles had the power to influence and control and did influence and control, directly and indirectly, the decision-making of Schwab and M&S, including their conduct alleged to be unlawful and the content and dissemination of the various statements which plaintiffs contend are false and misleading; he had the ability to prevent the issuance of the statements or cause the statements to be corrected and, therefore, is presumed to have had and exercised the power to control or influence the particular transactions and events giving rise to the securities violations as alleged herein.
6. By reason of its ownership and/or control of defendant M&S, including but not limited to control on a day-to-day basis, Schwab had the power and authority to cause or to prevent

the wrongful conduct of M&S complained of herein. Schwab participated meaningfully in the fraud, including but not limited to: Schwab had the power to influence and control and did influence and control, directly and indirectly, the decision-making of M&S, including its conduct alleged to be unlawful and the content and dissemination of the various statements which plaintiffs contend are false and misleading; Schwab had the ability to prevent the issuance of the statements or cause the statements to be corrected and, therefore, is presumed to have had and exercised the power to control or influence the particular transactions and events giving rise to the securities violations as alleged herein.

1. Defendant Schwab, through its position of ownership and/or control as the principal subsidiary of Corp., had the power and authority to, and did, influence and control, directly and indirectly, the decision-making and conduct of M&S. By virtue of its position and power to control and influence M&S, Schwab was a "controlling person" of M&S within the meaning of section 20(a) of the Exchange Act and had the power and influence to direct the management of activities at M&S,
2. Pursuant to Section 20(a) of the Exchange Act, by virtue of his position as a controlling person of both Schwab and M&S, Charles is liable jointly and severally with and to the same extent as Schwab and M&S for each of their aforesaid violations of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder.
3. Pursuant to Section 20(a) of the Exchange Act, by virtue of its position as a controlling person of M&S, Schwab is liable jointly and severally with and to the same extent as M&S for its aforesaid violations of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder.
4. As a direct and proximate result of the wrongful conduct of defendant Charles and of defendant Schwab, plaintiffs and other members of the Class were damaged by each defendant's violations of Section 20(a) as described herein in an amount which cannot presently be determined.

COUNT III, Against Charles and Schwab
For Breaches of Fiduciary Duty
(Common Law)

1. Plaintiffs incorporate by reference and reallege paragraphs 1 through 123 as if fully set forth herein.
2. Schwab acted as agent for plaintiffs and other members of the Class in accepting market orders from plaintiffs and other members of the Class. Further, Schwab and the other defendants assumed a fiduciary duty to be careful, skillful, diligent and loyal in conducting business on behalf of plaintiffs and the Class. Schwab also had a fiduciary duty to account and disclose to plaintiffs and the Class all profits received in connection with executing their orders at prices other than those to which they were entitled. By personally advertising and promoting Charles himself in advertisements, TV commercials and otherwise, defendant Charles knew that potential and existing Schwab customers

would place their trust in him. As such, to the extent he did not otherwise have it, Charles accepted a fiduciary responsibility to plaintiffs and other members of the Class.

3. Schwab, aided and abetted by the other defendants, violated those duties by, inter alia, not fulfilling their duties of fair dealing and "best execution" by refusing and failing to check alternate sources of price quotes and execution before executing orders on behalf of plaintiffs and other members of the Class, and by selling the order flow of plaintiffs and the Class to third parties in exchange for kickback payments while knowingly or with deliberate recklessness failing to know that such third parties would not obtain best execution for those trades, and/or intentionally doing so while obtaining for Schwab and M&S lower operating costs and higher profits.
4. Moreover, defendants violated their fiduciary duties to plaintiffs and the Class by failing to disclose to them, at any time, any of the foregoing wrongful conduct. Plaintiffs and the Class were not informed prior to entering into an agency and fiduciary relationship with Schwab that they would conduct themselves in such a manner to the economic disadvantage and detriment of the plaintiffs and the other members of the Class.
5. Plaintiffs and other members of the Class were injured as a direct and proximate result of defendants' misconduct in an amount which cannot presently be determined, and they are entitled to recover damages from defendants for defendants' misconduct.

COUNT IV, Against Every Defendant
Unjust Enrichment
(Common Law)

1. Plaintiffs incorporate by reference and reallege paragraphs 1 through 128 as if fully set forth herein.
2. By virtue of their fiduciary duties to plaintiffs and other members of the Class, defendants were obligated not to unjustifiably obtain any profits or benefits at the expense of plaintiffs and the Class in connection with executing orders on their behalf in the manner described herein.
3. As described herein, defendants were unjustly enriched because they wrongfully appropriated for themselves profits and benefits properly belonging to plaintiffs and the Class by not fulfilling their duties of fair dealing and "best execution" by refusing and failing to check alternate sources of price quotes and execution before executing orders on behalf of plaintiffs and other members of the Class, and by selling the order flow of plaintiffs and the Class to third parties in exchange for kickback payments while knowingly or with deliberate recklessness failing to know that such third parties would not obtain best execution for those trades, and/or intentionally doing so.
4. Plaintiffs and other members of the Class were injured as a direct and proximate result of defendants' misconduct and are entitled to receive from defendants the value of their unjust enrichment.

COUNT V, against Schwab
Breach of Contract

1. Plaintiffs incorporate by reference and reallege paragraphs 1 through 132 as if fully set forth herein.
2. Schwab had as an implicit provision of its contract to buy and sell securities on behalf of plaintiffs and the Class the obligation to seek out and to obtain the "best execution" prices for plaintiffs and other members of the Class.
3. Schwab breached such contractual obligations to plaintiffs and the Class by not seeking and/or obtaining the "best execution" prices available.
4. Plaintiffs and other members of the Class were injured as a result of defendants' breach of contract and are entitled to be compensated for their damages.

PRAYER FOR RELIEF

WHEREFORE, Plaintiffs, on behalf of themselves and the Class, pray for judgment against defendants, as follows:

- A. Declaring this action to be a proper class action, the plaintiffs to be adequate Class representatives and their counsel to be appropriate Class counsel;
- B. Declaring that defendants violated Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder;
- C. Declaring that defendant Charles was a control person of M&S and Schwab pursuant to, and that Charles violated, Section 20(a) of the Exchange Act;
- D. Declaring that defendant Schwab was a control person of M&S pursuant to, and that Schwab violated, Section 20(a) of the Exchange Act;
- E. Declaring that defendants breached their fiduciary and contractual obligations to plaintiffs and the Class;
- F. Ordering defendants to fulfill their duty of "best execution" in executing customer orders to buy or sell shares of stock and/or other securities;
- G. Ordering defendants to account to plaintiffs and the Class for all undisclosed profits and benefits defendants obtained in connection with executing orders on behalf of plaintiffs and other members of the Class during the Class Period in the manner described herein;
- H. Awarding plaintiffs and the Class compensatory damages in an amount to be proven at trial;
- I. Awarding plaintiffs and the Class punitive and exemplary damages;
- J. Awarding plaintiffs and the Class pre-judgment and post-judgment interest as well as their reasonable attorneys' fees, expert witness fees and other disbursements and Court costs; and
- K. Such other and further relief as the Court may deem just and equitable.

JURY DEMAND

Plaintiffs, by their counsel, each hereby request a trial by jury on all matters triable by jury.

Dated: September 17, 1999

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158605-7

Certificate of Service

I, _____, hereby certify, under the penalty of perjury pursuant to 28 U.S.C. §1746, that I caused to be served Plaintiffs' Consolidated Amended Complaint, by first class mail, postage pre-paid, upon Campbell, Arellano & Rich, No. 4A & B Kongens Gade, Charlotte Amalie, St. Thomas, United States Virgin Islands, and upon Bruce E. Coolidge, Esq., Wilmer, Cutler & Pickering, 2445 M Street, N.W., Washington, D.C. 20037, counsels for defendants.
