

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

ROSE ST. JULIEN,	:	
Plaintiff,	:	
	:	CIVIL ACTION
	:	
v.	:	97-3290
	:	
CHARLES SCHWAB & COMPANY, and	:	
PRUDENTIAL INVESTMENTS,	:	
Defendants.	:	

MEMORANDUM

R.F. KELLY, J.

OCTOBER 6, 1998

Rose St. Julien ("Plaintiff") has brought this action against Charles Schwab & Company ("Schwab") and Prudential Investments ("Prudential") to recoup losses sustained in connection with a fraudulent investment scheme perpetrated by Michael Anthony Andrews ("Andrews").¹ Presently before this Court is Schwab's Motion to Dismiss and Motion to Stay and Compel Arbitration. For the reasons that follow, the Motion to Dismiss Count I is granted in part and denied in part, the Motion to Stay and Compel Arbitration is granted.

I. FACTS.

In January of 1995, Plaintiff sought advice on how to invest her assets. Plaintiff approached Michelle Greene, Esquire ("Greene"), her attorney, who referred Plaintiff to Andrews.

¹ Plaintiff previously sued Andrews, SEI Investments ("SEI"), and United Bank of Philadelphia ("United Bank") regarding the same fraudulent scheme. Plaintiff obtained judgment by default against Andrews for the full amount of her claim. All claims against SEI were dismissed by Memorandum and Order dated March 24, 1998 See, St. Julien v. Andrews, No. 97-2236, 1998 WL 134223 (E.D. Pa. 1998). Plaintiff reached a settlement with United Bank on the remaining claims.

Greene is also a financial planner but chose not to represent Plaintiff in both capacities.

Upon meeting Plaintiff, Andrews represented himself as having an affiliation with SEI. At Andrews' direction, Plaintiff partially filled out paper work with the SEI Investments logo. Andrews never submitted these documents to SEI. Plaintiff wrote several checks payable to "SEI." Plaintiff believed Andrews would open an account for her with SEI and invest her assets in their products. Unbeknownst to Plaintiff, Andrews proceeded to open an account with United Bank in the name of "SEI Company." Plaintiff's checks were deposited into that account.

Andrews recommended that Plaintiff liquidate her existing brokerage accounts and turn over the proceeds to him for investment with SEI. Plaintiff maintained two accounts with Schwab, a brokerage account and an IRA account. Plaintiff believed that Andrews would contact Schwab and, through the forms she signed, have the money transferred to either himself or SEI. In reality, Andrews opened a bank account in the name of Andrews Financial Services, forged Plaintiff's signature (spelled incorrectly as "St. Julian") on a document entitled "Account Authorization," and forwarded that document to Schwab. Pursuant to the forged "Account Authorization," Schwab transferred the contents of Plaintiff's accounts to the Andrews Financial Services bank account.

During 1996, Andrews told Plaintiff that he would be attending school in London. In reality, Andrews was serving time

in a federal minimum security correctional facility in New Jersey. Andrews escaped from that facility and has disappeared. The contents of the United Bank accounts have also disappeared.

In January of 1997, Plaintiff discovered that she had been defrauded by Andrews. This suit was instituted by Plaintiff against Schwab and Prudential to recover the funds stolen from Plaintiff's accounts. Plaintiff alleges that Schwab and Prudential's transfer of her funds pursuant to forged documents constitutes a violation of sections 15(c)(1) and 10(b) of the Securities Exchange Act, as well as corresponding Rules 15(c)-(5) and 10(b)-(5)(Counts I and II), negligence (Counts III and IV), breach of fiduciary duty (Counts V and VI), and that Defendants "gave substantial assistance or encouragement to Andrews in effecting the fraudulent fund transfer request" (Counts VII and VIII). (Pl.'s Compl. at ¶¶ 43-50). Schwab has filed a Motion to Dismiss Count I of Plaintiff's Complaint and a Motion to Stay the remainder of Plaintiff's Complaint and Compel Arbitration. Prudential has answered Plaintiff's Complaint.

II. STANDARD.

Under Rule 12(b)(6), the Court must determine whether the allegations contained in the complaint, construed in the light most favorable to Plaintiff, show a set of circumstances which, if true, would entitle Plaintiff to the relief she requests. Gibbs v. Roman, 116 F.3d 83, 86 (3d Cir. 1997)(citing Nami v. Fauver, 82 F.3d 63, 65 (3d Cir. 1996)). A complaint will be dismissed only if Plaintiff could not prove any set of facts

which would entitle her to relief. Nami, 82 F.3d at 65 (citing Conley v. Gibson, 355 U.S. 41, 45-46 (1957)).²

III. DISCUSSION.

A. Motion to Dismiss.

In Count I, Plaintiff seeks to hold Schwab liable for violations of Sections 10(b) and 15(c) of the Securities Exchange Act and Rules 10(b)-5 and 15(c)-5 promulgated thereunder. 15 U.S.C. §78t, 78j(b). Schwab seeks to dismiss Plaintiff's section 10(b) claims as filed beyond the statute of limitations and argues that no private cause of action exists under section 15(c).

1. Section 15(c) and Rule 15(c)-5.

Section 15(c) prohibits fraud and manipulation by broker-dealers involved in over-the-counter transactions and transactions on exchanges where the broker-dealer is not a member. 15 U.S.C. § 78t. Several Courts have held that no private cause of action exists under section 15(c). Fulton Bank v. McKittrick & Briggs Sec., Inc., Nos. 88-0144, 88-0882 1990 WL 126179 at *10 (E.D. Pa. August 27, 1990); Newfield v. Shearson Lehman Bros., 699 F. Supp. 1124, 1126 (E.D. Pa. 1988); Walck v. Am. Stock Exch., Inc., 565 F. Supp. 1051, 1059 (E.D. Pa. 1981), aff'd on other grounds, 687 F.2d 778 (3d Cir. 1982), cert.

² In deciding the present Motions, evidence submitted in connection with Plaintiff's first suit was considered, however, because those materials are "public records" the Motion to Dismiss will not be treated as a Motion for Summary Judgment. Oshiver v. Levin, Fishbein, Sedran & Berman, 38 F.3d 1380, 1384 n.2 (3d Cir. 1994).

denied, 461 U.S. 942 (1983). For this reason, Plaintiff's section 15(c) claim must be dismissed.

2. Section 10(b) and Rule 10(b)-5.

Actions brought pursuant to section 10(b) and Rule 10(b)-5 "must be commenced within one year after the discovery of the facts constituting the violation and within three years after such violation." Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson, 501 U.S. 350, 364 (1991), overruled in part by statute, 15 U.S.C. § 78aa-1 (preventing retroactive application of Lampf). Plaintiff commenced this action on June 25, 1998. The violation occurred March 25, 1996, when Schwab dispersed Plaintiff's funds to Andrews. Plaintiff filed this action within three years of the alleged violation, the issue is whether Plaintiff discovered facts constituting the violation prior to June 25, 1997.

Schwab contends that Plaintiff was aware that her funds were forwarded to Andrews rather than SEI on January 8, 1997, when she called the police to report Andrews. Plaintiff contends that she was unaware of Schwab's role until September to December 1997, when, through discovery in the first action, she received the forged "Account Authorization" form. I hold that Plaintiff had insufficient facts to discover Schwab's alleged violation of section 10(b) or Rule 10(b)-5 prior to June 25, 1997.

Plaintiff's January 8th, 1997 call to the police is only one instance which demonstrates her discovery of Andrews' fraud. Plaintiff testified that early in January 1997, she

visited United Bank and determined that Andrews was endorsing her checks made payable to SEI. (St. Julien Dep., 12/11/97, at 117-18). Plaintiff testified that also on January 8, 1997 she received a facsimile copy of a letter sent to Detective Shields, of the Philadelphia Police Department, by Derek Zeller, an employee of SEI, which unequivocally states that SEI never had an account in Plaintiff's name. (St. Julien Dep. at 81). Further, on January 17, 1997, Plaintiff wrote a letter to the Securities Exchange Commission requesting an investigation of Andrews because Plaintiff believed she had been defrauded. (St. Julien Dep. at 130).

While these actions compel the conclusion that Plaintiff knew she had been defrauded by Andrews as of January 1997, Plaintiff remained unaware that Schwab had transferred her funds pursuant to a forged authorization until she received that document through discovery in the prior litigation. For this reason, Count I of Plaintiff's Complaint as it pertains to section 10(b) and Rule 10(b)-(5) cannot be dismissed.

B. Motion to Stay and Compel Arbitration.

Schwab seeks to stay this action and compel arbitration pursuant to the Federal Arbitration Act ("FAA"). 9 U.S.C. §§ 3-4. Schwab points to four documents, signed by Plaintiff in connection with her accounts, which contain mandatory arbitration clauses. Specifically, Plaintiff signed an application prior to opening her brokerage account which provides:

I agree to settle by arbitration any controversy between myself and Schwab and/or any Schwab officers,

directors, employees, or agents relating to the Account Agreement, my Brokerage Account or account transaction, or in any way arising from my relationship with Schwab as provided in Section 16 of the Account Agreement.

(Def.'s Mot. to Dismiss and to Stay and Compel Arbitration Ex.

C). Section 16 of Schwab's "Brokerage Account Agreement" states in relevant part:

Arbitration Agreement: You agree to settle by arbitration any controversy between you and us and/or any of our officers, directors, employees, or agents relating to the Account Agreement, your Brokerage Account or account transaction, or in any way arising from your relationship with us.

Such arbitration will be conducted by, and according to the securities arbitration rules then in effect of, the American Arbitration Association, the National Association of Securities Dealers, the New York Stock Exchange or any other U.S.-based national securities exchange registered with the U.S. Securities and Exchange Commission. Either of us may initiate arbitration by serving or mailing a written notice to the other. The notice must specify which forum will hear the arbitration. This specification will be binding on both of us.

(Def.'s Mot. to Dismiss and to Stay and Compel Arbitration Ex.

C). Plaintiff's IRA Account application and agreement contain substantially similar mandatory arbitration clauses. (Def.'s Mot. to Dismiss and to Stay and Compel Arbitration Ex. E, F).

"A threshold inquiry under the Federal Arbitration Act is to determine, under recognized principles of contract law, the validity of, and the parties bound by, the arbitration agreement." First Liberty Inv. Group v. Nicholsberg, 145 F.3d 647, 649 (3d Cir. 1998)(citing In re Prudential Ins. Co. of Am. Sales Practice Litig. All Agent Actions ["Prudential Agents"], 133 F.3d 225, 227 n.1 (3d Cir. 1998), petition for cert. filed,

66 U.S.L.W. 3783 (U.S. May 29, 1998)(No. 97-1911). "[T]he next step in the analysis is to identify the nature of the dispute at issue and the scope of the arbitration clause." Prudential Agents, 133 F.3d at 230.

Plaintiff does not contest the validity of the arbitration agreement or that it binds her, but argues that this matter is outside the scope of the arbitration clause for three reasons. First, Plaintiff contends that because she used her Schwab account to hold money, rather than purchase securities, the arbitration clause does not apply. Second, Plaintiff contends that there is no "controversy" between the parties because it is undisputed that Schwab transferred Plaintiff's funds pursuant to a forgery. Finally, Plaintiff contends that she was not informed that she was giving up her right to seek judicial redress for Schwab's "actionable negligence." (Pl.'s Reply in Opp'n to Def.'s Mot. to Dismiss at 8).

Each of Plaintiff's arguments must fail. The arbitration agreement clearly covers Plaintiff's claims against Schwab. Nothing contained in the application or agreement for either of Plaintiff's Schwab accounts provides an exception for accounts used to hold money rather than purchase securities.

A "controversy" does exist between the parties. This suit was filed to resolve that "controversy": whether or not Schwab handled Plaintiff's accounts in a reasonable manner. It is immaterial to the applicability of the arbitration clauses that the facts surrounding this "controversy" are undisputed. An

arbitration panel must determine the legal ramifications of those undisputed facts pursuant to the terms of the agreements.

Finally, Plaintiff was specifically informed that she was waiving her right to seek judicial redress in the account agreements. The agreements provide in relevant part:

(2) The parties are waiving their right to seek remedies in court, including the right to a jury trial.

(Def.'s Mot. to Dismiss and to Stay and Compel Arbitration Ex. D F). Plaintiff is bound by the terms of her agreement with Schwab.

In sum, Plaintiff has not convinced this Court that the mandatory arbitration clauses are inapplicable to this matter. Pursuant to section 3 of the FAA, this Court must stay this matter pending arbitration. 9 U.S.C § 3. Further, because Plaintiff has refused to submit this matter to arbitration as is required under the agreements, Schwab is entitled to an Order compelling arbitration pursuant to section 4 of the FAA. 9 U.S.C § 4. Such an Order follows.

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CHARLES SCHWAB & COMPANY, and	:	
PRUDENTIAL INVESTMENTS,	:	
Defendants.	:	
_____	:	

ORDER

AND NOW, this 6th day of October, 1998, upon consideration of Defendant, Charles Schwab & Company's Motion to Dismiss Count I and Motion to Stay and Compel Arbitration, and Plaintiff's Response thereto, it is hereby ORDERED that said Motion to Dismiss Count I is GRANTED in part and DENIED in part. It is further ORDERED that Plaintiff's Motion to Stay and Compel Arbitration is GRANTED. This matter shall be STAYED pending arbitration before the National Association of Securities Dealers.

BY THE COURT:

Robert F. Kelly, J.