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9 *Attorneys for Plaintiffs Phillip D. Reed and Pamela N. Reed*

10 SUPERIOR COURT OF THE STATE OF CALIFORNIA
11 FOR THE COUNTY OF SAN DIEGO

12 PHILLIP D. REED and PAMELA N.
13 REED,

14 Plaintiffs,

15 v.

16 CHARLES SCHWAB & CO., INC;
17 HIGHTOWER ADVISORS, LLC; and
18 DOES 1 through 10, inclusive,

19 Defendants.

Case No:

COMPLAINT FOR:

1. **Breach of Fiduciary Duty**
2. **Professional Negligence**
3. **Negligence**
4. **Breach of Contract**
5. **Breach of Implied Covenant of Good Faith and Fair Dealing**
6. **Promissory Estoppel**

DEMAND FOR JURY TRIAL

1 Plaintiffs PHILLIP D. REED and PAMELA N. REED, allege the following
2 against Defendants CHARLES SCHWAB & CO., INC. and HIGHTOWER
3 ADVISORS, LLC:

4 **INTRODUCTION**

5 1. Plaintiffs PHILLIP D. REED and PAMELA N. REED (collectively,
6 “PLAINTIFFS” or “The Reeds”) are the victims of a fraudulent scheme by which
7 unknown individuals stole nearly \$1 million of the Reeds’ retirement savings from
8 accounts held with Defendant CHARLES SCHWAB & CO., INC (“Schwab”) and
9 managed by Defendant HIGHTOWER ADVISORS, LLC (“Hightower”).

10 2. Between July 2022 and March 2023, dozens of suspicious and
11 unauthorized withdrawals depleted the Reeds’ accounts with Schwab. And, because
12 the perpetrators who unlawfully accessed the Reeds’ online Schwab account turned
13 off all electronic transaction notifications, the Reeds were unable to discover the
14 fraudulent account activity until it was too late.

15 3. Despite being paid to actively manage and monitor the Reeds’
16 investment accounts, Hightower never recognized a single suspicious transaction or
17 the rapidly declining balances in the Reeds’ accounts. And because the amount of
18 each unauthorized transaction fell just below Schwab’s threshold for heightened
19 scrutiny, Schwab never noticed or questioned any of the suspicious withdrawals. Nor
20 did Schwab fully honor its “Security Guarantee,” which purported to protect investors
21 against losses caused by the precise type of unauthorized activity that depleted the
22 Reeds’ retirement accounts.

23 4. The Reeds now seek damages for losses sustained as a result of Schwab
24 and Hightower’s breaches of their respective duties and contractual obligations.

25 **PARTIES, JURISDICTION, AND VENUE**

26 5. Plaintiff PHILLIP D. REED is an individual who resides in San Diego
27 County, California.

1 6. Plaintiff PAMELA N. REED is an individual who resides in San Diego
2 County, California.

3 7. Defendant CHARLES SCHWAB & CO., INC. (“Schwab”) is a
4 corporation organized and existing under the laws of the State of California. Schwab
5 operates as a broker-dealer registered with the Securities and Exchange Commission
6 and maintains its principal place of business in Westlake, Texas.

7 8. Defendant HIGHTOWER ADVISORS, LLC (“Hightower”) is a limited
8 liability company organized and existing under the laws of the State of Delaware.
9 Hightower operates as an investment adviser registered with the SEC. In July 2020,
10 Hightower acquired Frontier Investment Management Company. On information and
11 belief, Hightower operates under the business name of Frontier Investment
12 Management Company in certain jurisdictions, including California.

13 9. The true names and/or capacities, whether individual, corporate,
14 associate, partnership, or otherwise, of Defendants DOES 1 through 10, inclusive, are
15 currently unknown to Plaintiffs. Upon information and belief, Defendants DOES 1
16 through 10, inclusive, and each of them, is legally responsible in some manner for the
17 events and/or occurrences referred to herein, and legally caused injury and/or damage
18 to Plaintiffs as alleged herein. Plaintiffs reserve the right to amend this complaint to
19 identify the true names and/or capacities of each of the fictitiously named defendants
20 as soon as such names and/or capacities are ascertained.

21 10. Upon information and belief, at all relevant times, each of the
22 Defendants, including DOES 1 through 10, was the agent or employee of each of the
23 other Defendants, and at all times was acting within the scope and authority of their
24 agency or employment.

25 11. Venue is proper in this Court, pursuant to Code of Civil Procedure
26 Section 395(a), because both named Defendants contracted with and/or agreed to
27 provide services to Plaintiffs in San Diego County.
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1 **FACTUAL BACKGROUND**

2 12. The Reeds have maintained several investment accounts, including
3 retirement accounts, with Defendant Schwab since approximately 1991. Since 2020,
4 the Reeds' Schwab accounts have been actively managed by Hightower doing
5 business as Frontier Investment Management Company, an SEC-registered
6 investment adviser.

7 13. Unbeknownst to the Reeds, their Schwab accounts were compromised
8 by unknown individuals at some point in 2022. On information and belief, beginning
9 on or about July 21, 2022, the perpetrators commenced a series of unauthorized
10 withdrawals from the Reeds' Schwab accounts that went undetected by either
11 Schwab or Hightower. The theft was accomplished through numerous internal
12 transfers from the Reeds' retirement accounts to their family trust cash account, and
13 subsequent transfers from the family trust account to an unknown account at Wells
14 Fargo Bank. On information and belief, each of the dozens of transactions fell below
15 the \$8,000 threshold amount that prompts additional scrutiny from Schwab.

16 14. In December 2022, before leaving on their three-month vacation, the
17 Reeds notified their primary contact at Schwab, William Gaston, that they would be
18 away for several months. On information and belief, by the time the Reeds left on
19 their vacation, the perpetrators had surreptitiously changed their Schwab account
20 notification preference from paperless to paper notifications.

21 15. As a result, the Reeds did not receive any electronic transaction
22 notifications while they were away. Instead, for the duration of the Reeds' extended
23 vacation, at which time the perpetrators apparently knew the Reeds would not be
24 home or able to review their mail, all Schwab account transactions were confirmed
25 exclusively through paper notifications sent via U.S. Mail.

26 16. Upon the Reeds' return from their vacation in March 2023, they
27 reviewed 42 paper account statements that had been delivered in their absence. Upon
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1 reviewing the statements, the Reeds’ noticed numerous unauthorized withdrawal
2 transactions that depleted their account balances by approximately \$982,000.00. The
3 Reeds notified Schwab shortly after discovering the unauthorized transactions.

4 **A. Schwab’s “Security Guarantee”**

5 17. During the time the Reeds maintained their retirement accounts with
6 Schwab, their funds were purportedly protected by a “Security Guarantee” promoted
7 by Schwab. According to Schwab, the Security Guarantee provides “automatic
8 protection” against losses caused by unauthorized activity. The only conditions of
9 Schwab’s Security Guarantee are that the account holder (1) not share account access
10 information, including login ID and password, with any third party; and (2) report
11 any unauthorized transactions to Schwab “as quickly as possible.”

12 18. The Reeds never shared their account access information and were not in
13 a position to discover the unauthorized transactions sooner because the perpetrators
14 turned off all electronic transaction notifications, such that the Reeds could not
15 discover the fraud until they returned home after their three-month vacation and
16 reviewed numerous items of mail from Schwab. In other words, the Reeds complied
17 with both conditions of Schwab’s Security Guarantee.

18 19. Although the Security Guarantee does not specify what “as quickly as
19 possible” means, Schwab declined to reimburse the full amount of the Reeds’ loss on
20 the ground that they failed to comply with this condition.

21 20. Ultimately, Schwab agreed to reimburse only \$196,400 of the Reeds’
22 losses pursuant to its “Security Guarantee.” That amount reflected 20 percent of the
23 \$982,000 total amount stolen.

24 **B. Schwab Breached a Duty of Care as the Reeds’ Broker-Dealer**

25 21. Because of Schwab’s long-standing relationship with the Reeds as their
26 broker-dealer and custodian of their retirement accounts, it owed a duty of care to the
27 Reeds. Schwab’s duty required, at a minimum, that it recognize dozens of red flags
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1 in the form of repeated and methodical withdrawals from retirement accounts in
2 amounts falling just below Schwab’s threshold for enhanced scrutiny. Even a
3 modicum of monitoring would have alerted Schwab to months of suspicious activity
4 warranting investigation, including dozens of transfers from the Reeds’ retirement
5 accounts to their family trust cash account. On information and belief, at the time of
6 the unauthorized withdrawals from the Reeds’ retirement accounts, Schwab had not
7 implemented adequate procedures and internal controls reasonably designed to
8 identify suspicious transactions.

9 22. Contrary to applicable regulatory guidelines, Schwab apparently
10 performed no monitoring, whatsoever, of the Reeds’ accounts. As a result, Schwab
11 failed to act as a reasonably careful broker-dealer would have acted under similar
12 circumstances. For example, applicable regulations and industry guidelines require
13 minimal safeguards to detect red flags and protect against fraud. But Schwab
14 overlooked myriad red flags and was unaware of the fraudulent scheme being
15 perpetrated in plain sight until it was notified by the Reeds. Schwab’s negligent
16 conduct was a substantial factor in causing the Reeds’ harm.

17 **C. Hightower Breached a Duty of Care as the Reeds’ Fiduciary**

18 23. Hightower’s Form ADV Part 2A Brochure confirms that it is an SEC-
19 registered investment adviser held to the standards of a fiduciary. Furthermore, the
20 Brochure of Frontier Management Company provided to the Reeds states, among
21 other things, that Frontier/Hightower performs (1) “ongoing portfolio *monitoring*,
22 evaluation and rebalancing,” and (2) “account reviews” on an “ongoing basis.”
23 Accordingly, Hightower expressly undertook to monitor the accounts from which the
24 Reeds’ retirement savings were stolen.

25 24. As a paid investment advisor tasked with monitoring the Reeds’
26 retirement accounts, Hightower’s conduct failed to comply with applicable regulatory
27 guidelines, industry custom and practice, or the Reeds’ reasonable expectations.
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1 25. At a minimum, Hightower should have questioned numerous transfers
2 from retirement accounts that directly contradicted Hightower’s advice. For example,
3 despite advising the Reeds to avoid withdrawing funds from their retirement accounts
4 without first consulting Hightower to address tax consequences and potential
5 alternatives, Hightower overlooked dozens of such transactions without making any
6 effort to verify whether the Reeds had, in fact, authorized such transactions without
7 notifying Hightower. In light of Hightower’s specific warnings to the Reeds to avoid
8 withdrawing funds from their retirement accounts, a reasonably prudent investment
9 advisor would have identified the suspicious transactions and contacted the Reeds to
10 confirm their knowledge of and intent to execute such transactions.

11 26. Despite charging fees to actively manage the Reeds’ accounts, and
12 executing other transactions within those same accounts during the same time period,
13 Hightower never noticed any of the unauthorized withdrawals or the rapidly declining
14 balances in the accounts it was managing for the Reeds. Nor did Hightower ever seek
15 to confirm a single transaction with the Reeds.

16 27. On the other hand, the Reeds relied on certain statements they received
17 from Hightower, which reflected purchases and sales of securities the Reeds believed
18 had been directed by Hightower as part of its management of the affected accounts.

19 28. The Reeds had no idea Hightower was asleep at the wheel and had not
20 authorized, or even noticed, dozens of transactions that amounted to hundreds of
21 thousands of dollars over the course of roughly eight months. It was not until the
22 Reeds returned from a three-month overseas vacation in late March 2023 that *they*
23 finally discovered the fraud and immediately notified Schwab and Hightower.

24 29. When the Reeds notified Hightower, its manager initially rejected the
25 suggestion that the affected account balances could possibly have declined so
26 dramatically without detection. But after reviewing and confirming the account
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1 activity himself, the manager acknowledged incredulously what had transpired on
2 Hightower's watch.

3 30. As a result of Hightower's professional negligence and breach of
4 fiduciary duty, the Reeds were damaged through the loss of a large portion of their
5 retirement savings.

6 **FIRST CAUSE OF ACTION**

7 **Breach of Fiduciary Duty**

8 **(Against Defendant Hightower Advisors, LLC)**

9 31. Plaintiffs repeat the allegations of all preceding paragraphs of this
10 Complaint and incorporate the same by reference.

11 32. Defendant Hightower is and at all relevant times was an SEC-registered
12 investment adviser. Hightower's status as a registered investment adviser renders it a
13 fiduciary of the Reeds. In addition, the Reeds placed trust and confidence in
14 Hightower as their investment adviser in connection with their retirement investments
15 and Hightower voluntarily accepted a fiduciary role with respect to the Reeds.

16 33. Defendant Hightower's fiduciary responsibilities include the obligation
17 to act with due care in managing the Reeds' investment accounts.

18 34. Defendant Hightower failed to exercise due care in managing the Reeds'
19 investment accounts in that it neglected to monitor the Reeds' accounts or recognize
20 dozens of suspicious withdrawal transactions, including transactions that directly
21 contradicted Hightower's advice to the Reeds. As such, Hightower failed to act as a
22 reasonably careful investment adviser would have under the same or similar
23 circumstances.

24 35. As a direct result of Defendant Hightower's failure to act as a reasonably
25 careful investment adviser, the Reeds were harmed.

26 36. Defendant Hightower's conduct was a substantial factor in causing the
27 Reeds' harm.

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SECOND CAUSE OF ACTION

Professional Negligence

(Against Defendant Hightower Advisors, LLC)

37. Plaintiffs repeat the allegations of all preceding paragraphs of this Complaint and incorporate the same by reference.

38. Defendant Hightower is and at all relevant times was an SEC-registered investment adviser.

39. As part of its engagement by the Reeds, Defendant Hightower agreed to perform ongoing portfolio monitoring, evaluation and rebalancing, as well as account reviews on an ongoing basis. Hightower had a duty to act with reasonable care in monitoring the Reeds’ investment accounts for which it was responsible.

40. Defendant Hightower failed to exercise due care in managing and monitoring the Reeds’ investment accounts in that it neglected to recognize dozens of suspicious withdrawal transactions, including transactions that directly contradicted Hightower’s advice to the Reeds. As such, Hightower failed to act as a reasonably careful investment adviser would have acted under the same or similar circumstances.

41. As a direct result of Defendant Hightower’s failure to act as a reasonably careful investment adviser, the Reeds were harmed.

42. Hightower’s conduct was a substantial factor in causing the Reeds’ harm.

THIRD CAUSE OF ACTION

Negligence

(Against Defendant Charles Schwab & Co., Inc.)

43. Plaintiffs repeat the allegations of all preceding paragraphs of this Complaint and incorporate the same by reference.

44. Defendant Schwab was negligent in that it failed to act as a reasonably careful broker-dealer would have acted under the same or similar circumstances in

1 overseeing the Reeds' investment accounts. For example, Schwab neglected to
2 recognize dozens of suspicious transactions, some of which occurred at times during
3 which Schwab had been specifically advised the Reeds would be away from home.

4 45. As a direct result of Defendant Schwab's failure to act as a reasonably
5 careful broker-dealer, the Reeds were harmed.

6 46. Schwab's conduct was a substantial factor in causing the Reeds' harm.

7 **FOURTH CAUSE OF ACTION**

8 **Breach of Contract**

9 **(Against Defendant Charles Schwab & Co., Inc.)**

10 47. Plaintiffs repeat the allegations of all preceding paragraphs of this
11 Complaint and incorporate the same by reference.

12 48. Plaintiffs performed all conditions, covenants, and promises required on its
13 part to be performed in accordance with the terms and conditions of Defendant
14 Schwab's Security Guarantee.

15 49. Defendant Schwab breached its contractual obligation to reimburse
16 Plaintiffs for their losses caused by the unauthorized withdrawals from their Schwab
17 accounts by failing to reimburse all such losses, as promised.

18 50. Plaintiffs have been damaged in an amount to be proven at trial, which
19 amount includes their unreimbursed losses caused by the unauthorized withdrawals
20 from their Schwab accounts.

21 51. Defendant Schwab's above-referenced breach of contract was a
22 substantial factor in causing Plaintiffs' harm.

23 **FIFTH CAUSE OF ACTION**

24 **Breach of Implied Covenant of Good Faith and Fair Dealing**

25 **(Against Defendant Charles Schwab & Co., Inc.)**

26 52. Plaintiffs repeat the allegations of all preceding paragraphs of this
27 Complaint and incorporate the same by reference.

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1 53. In every contract or agreement there is an implied promise of good faith
2 and fair dealing. This implied promise means that each party will not do anything to
3 unfairly interfere with the right of any other party to receive the benefits of the
4 contract. Good faith means honesty of purpose without any intention to mislead or to
5 take unfair advantage of another. Generally speaking, it means being faithful to one's
6 duty or obligation. However, the implied promise of good faith and fair dealing
7 cannot create obligations that are inconsistent with the terms of the contract.

8 54. The Reeds and Defendant Schwab entered into a contract that included
9 Schwab's Security Guarantee.

10 55. Plaintiffs did all, or substantially all of the significant things that the
11 contract required Plaintiffs to do under the terms and conditions of Defendant
12 Schwab's Security Guarantee.

13 56. Defendant Schwab's failure to honor its Security Guarantee prevented
14 Plaintiffs from receiving benefits to which they were entitled under the contract.

15 57. By failing to fully honor its Security Guarantee, Defendant Schwab did
16 not act fairly and in good faith.

17 58. Plaintiffs have been damaged in an amount to be proven at trial, which
18 amount includes losses from the unauthorized withdrawals that Schwab has failed to
19 reimburse, as promised.

20 **SIXTH CAUSE OF ACTION**

21 **Promissory Estoppel**

22 **(Against Defendant Charles Schwab & Co., Inc.)**

23 59. Plaintiffs repeat the allegations of all preceding paragraphs of this
24 Complaint and incorporate the same by reference.

25 60. Defendant Schwab made a clear promise through its Security Guarantee
26 to protect the Reeds' against losses caused by unauthorized account activity – that is,
27 Schwab promised to reimburse Plaintiffs for any such losses.
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