

**UNITED STATES OF AMERICA**  
**Before the**  
**SECURITIES AND EXCHANGE COMMISSION**

**SECURITIES EXCHANGE ACT OF 1934**  
**Release No. 54993 / December 21, 2006**

**INVESTMENT COMPANY ACT OF 1940**  
**Release No. 27607 / December 21, 2006**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-12514**

**In the Matter of**

**DEUTSCHE BANK SECURITIES, INC.,**

**Respondent.**

**ORDER INSTITUTING  
ADMINISTRATIVE AND CEASE-AND-  
DESIST PROCEEDINGS, MAKING  
FINDINGS, AND IMPOSING  
REMEDIAL SANCTIONS AND A  
CEASE- AND-DESIST ORDER  
PURSUANT TO SECTIONS 15(b) AND  
21B OF THE SECURITIES  
EXCHANGE ACT OF 1934 AND  
SECTIONS 9(b) AND 9(f) OF THE  
INVESTMENT COMPANY ACT OF  
1940**

**I.**

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that public administrative and cease-and-desist proceedings be, and hereby are, instituted pursuant to Sections 15(b) and 21B of the Securities Exchange Act of 1934 (“Exchange Act”) and Sections 9(b) and 9(f) of the Investment Company Act of 1940 (“Investment Company Act”) against Deutsche Bank Securities, Inc. (“DBSI” or “Respondent”).

**II.**

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the “Offer”) that the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission or in which the Commission is a party, and without admitting or denying the findings, except those findings pertaining to the jurisdiction of the Commission over it and the subject matter of these proceedings, Respondent consents to the entry of this Order Instituting Administrative and Cease-and-Desist Proceedings, Making Findings, and Imposing Remedial

Sanctions and a Cease-and-Desist Order Pursuant to Sections 15(b) and 21B of the Securities Exchange Act of 1934 and Sections 9(b) and 9(f) of the Investment Company Act of 1940 (“Order”), as set forth below.

### III.

On the basis of this Order and Respondent’s Offer, the Commission finds<sup>1</sup> that:

#### Summary

1. This proceeding concerns late trading and deceptive market timing of mutual funds by a registered representative (“RR”) at DBSI. DBSI is a registered broker-dealer and a subsidiary of Deutsche Bank AG (“Deutsche Bank”), a German financial services and bank holding company.

2. Between March 2003 and September 2003, a DBSI RR defrauded mutual funds and fund shareholders by engaging in deceptive practices designed to mislead mutual funds as to the identity of his customers. For example, various mutual funds identified the RR’s customers as market timers, and funds rejected the customers’ trades. In response, the RR opened new accounts for the customers and then executed trades for the customers in the same mutual funds that had rejected the customers’ trades. The RR opened the new accounts to conceal the true identity of his customers and to mislead certain mutual funds into believing that the trades were coming from other DBSI customers, whose trading the funds had not blocked.

3. In total, the RR executed numerous market timing trades using deceptive means. The mutual funds would have rejected these trades had they known the RR’s customers’ true identities or trading strategies.

4. In addition, the RR entered late trades for at least one customer. The RR received and entered orders to purchase, redeem, or exchange mutual fund shares after the 4:00 p.m. Eastern Time market close, but entered the orders as if they had been received prior to 4:00 p.m. This enabled the customer to receive the share price based on the prior net asset value (“NAV”) determined as of 4:00 p.m. The RR entered the late trades on occasions when fund companies identified the customer as a market timer and blocked the customer’s original orders. On more than 55 occasions, the RR and DBSI received substitute orders after 4:00 p.m. ET, but treated them as though they had been received at the time of the original, rejected orders. This conduct violated Rule 22c-1(a) adopted pursuant to Section 22(c) of the Investment Company Act.

5. DBSI had no procedures and systems to prevent and detect the RR’s fraudulent conduct. DBSI also had no procedures and systems for monitoring whether employees submitted orders for processing at that day’s NAV only if they were received from customers before the market close.

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<sup>1</sup> The findings herein are made pursuant to the Respondent’s Offer and are not binding on any other person or entity in this or any other proceeding.

6. As a result of this conduct, the RR violated Section 17(a) of the Securities Act of 1933, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. DBSI violated Rule 22c-1, as adopted under Section 22(c) of the Investment Company Act, and the RR aided and abetted DBSI's violations of Rule 22c-1. In addition, DBSI failed reasonably to supervise the RR, with a view to preventing his violations of the antifraud provisions and Rule 22c-1 of the federal securities laws, pursuant to Section 15(b)(4) of the Exchange Act.

### **Respondent**

7. **DBSI**, a Delaware corporation headquartered in New York, is a broker-dealer registered with the Commission pursuant to Section 15(b) of the Exchange Act. DBSI operated a number of branch offices, including an office located at 280 Park Avenue, New York, New York.

### **Facts**

#### **Background**

8. Market timing includes: (i) frequent buying and selling of shares of the same mutual fund or (ii) buying or selling mutual fund shares in order to exploit inefficiencies in mutual fund pricing. Market timing can harm other mutual fund shareholders because it can dilute the value of their shares. Market timing, while not illegal per se, can also disrupt the management of the mutual fund's investment portfolio and cause the targeted mutual fund to incur considerable extra costs associated with excessive trading and, as a result, cause damage to other shareholders in the funds. Market timing may be illegal, for example, if deception is used to induce a mutual fund to accept trades that it otherwise would not accept under its own market timing policies.

9. Rule 22c-1(a) adopted pursuant to Section 22(c) of the Investment Company Act requires registered investment companies issuing redeemable securities, principal underwriters and dealers, and any person designated in the fund's prospectus as authorized to consummate transactions in securities issued by the fund to sell and redeem fund shares at a price based on the current NAV next computed after receipt of an order to buy or redeem. Mutual funds generally determine the daily price of mutual fund shares as of 4:00 p.m. ET. Mutual funds' prospectuses generally state that orders received before 4:00 p.m. are executed at the price determined as of 4:00 p.m. that day, and that orders received after 4:00 p.m. are executed at the price determined as of 4:00 p.m. the next trading day.

10. "Late trading" refers to the practice of placing orders to buy, redeem, or exchange mutual fund shares after the time as of which mutual funds calculate their NAV, usually as of the close of trading at 4:00 p.m. ET, but receiving the price based on the prior NAV determined as of 4:00 p.m. Late trading violates Rule 22c-1(a) under the Investment Company Act.

11. DBSI entered into agreements with each of more than 100 mutual fund distributors or principal underwriters, which authorized DBSI to sell the particular company's mutual funds ("Dealer Agreements"). The Dealer Agreements typically required that shares of the company's mutual funds be sold in accordance with the federal securities laws and the terms of the funds' prospectuses. Further, the prospectuses for many mutual funds, including funds

covered by the Dealer Agreements, contained language prohibiting market timing. For example, some prospectuses prohibited frequent trading, while others contained limitations on the number of trades that an investor could make within a specific time period. In addition, the mutual fund prospectuses also typically required that orders to purchase, redeem, or exchange shares of a fund must be received no later than 4:00 p.m. ET to be effected at that day's NAV.

### **DBSI's RR Engaged In Deceptive Market Timing of Mutual Funds**

12. Beginning in March 2003 and continuing until September 2003, a DBSI RR, who worked at the firm's branch office at 280 Park Avenue, engaged in a fraudulent mutual fund trading scheme on behalf of certain customers, including an investment adviser to several hedge funds. The RR deceived mutual funds into accepting his customers' market timing trades, which the mutual funds would have rejected had they known the RR's customers' true identities or trading strategies.

13. More specifically, the RR deliberately employed deceptive practices that helped his customers hide their identities from mutual funds. These practices included opening new accounts when the customers' trades were blocked. In fact, the RR and his sales assistant prepared a daily "blocked list" identifying mutual fund families that had blocked a customer's account, which enabled the customer to place orders in the same mutual funds, but through new accounts. Additionally, the RR and his sales assistant journaled funds from a blocked account to a new account so the customers could continue to trade the same mutual funds.

14. For example, in March 2003, the RR opened six accounts for his investment adviser customer. The customer then used four of these accounts to engage in market timing.

15. Within a matter of weeks, mutual funds determined that the accounts were engaged in market timing, which the funds either prohibited or discouraged, and the mutual funds began to block certain accounts from future purchases of the funds' shares.

16. In response, beginning in April 2003, the RR directed his sales assistant to open additional accounts for the customer. The RR did this in order to misrepresent the customer's identity and to mislead mutual funds into believing that the purchases were coming from other DBSI customers, whose trading had not been blocked. The customer then continued market timing the same mutual funds until the mutual funds blocked the newly opened account.

17. In another instance, on May 12, 2003, a mutual fund sent a block letter to the RR. The letter advised DBSI that market timing was harmful to mutual funds and that the fund had rejected one of the RR's customer's market timing trades:

[Our] funds are intended for long-term investment. We believe that excessive trading in fund shares adversely affects fund expenses and investor returns. The prospectuses of each of [our] funds also state that the funds reserve the right to refuse any purchase request.

Please take this letter as your formal notification that, based on the pattern of short term trading in shares of [our] funds, [we have] determined that we must refuse the above-referenced transaction.

We regret the necessity of this action and trust that you appreciate that we are acting to help the funds avoid unnecessary or excessive portfolio turnover with the interests of all fund shareholders in mind.

18. Despite receiving this letter, the RR continued to execute market timing trades for his customer in these funds. On June 5, 2003, the RR's sales assistant opened two additional accounts, and transferred funds from the blocked accounts to the new accounts. The customer then continued market timing these mutual funds through one of the newly opened accounts. On July 2, 2003, the fund sent another block letter to the RR concerning trading in the new account.

19. This pattern of restricting accounts and opening new accounts continued through August 2003.

20. In total, the RR and his sales assistant opened 27 accounts for the investment adviser customer, 14 of which the RR's customer used to place mutual fund trades. By creating new accounts, the RR enabled his customer to evade restrictions that mutual funds' had placed on the customer's trading.

21. During the period from March 2003 through September 2003, at least 15 mutual fund families, representing hundreds of individual mutual funds, detected the RR's customers' market timing and sent block notices to DBSI, barring future purchases by those accounts.

22. From March 2003 through September 2003, the RR executed numerous market timing trades using deceptive means in various mutual funds for his customers.

23. DBSI earned over \$200,000 in fees from the RR's market timing customers.

### **The RR and DBSI Engaged in Late Trading**

24. The RR accepted substitution trades from his investment adviser customer after 4:00 p.m. ET, but the RR and DBSI executed the trades as if they had been received prior to the market close.

25. From March 2003 to September 2003, the RR and his sales assistant entered more than 50 mutual fund trades that his customer submitted after the 4:00 p.m. ET market close. In each instance, the trade the RR or his sales assistant entered was a replacement, or "substitution," for an order that the customer had placed before 4:00 p.m. but that the mutual fund had blocked because it had identified the customer as a market timer. After the RR or his sales assistant notified the customer that a trade had been blocked, they would allow the customer to trade shares of a different mutual fund. The RR and his sales assistant then entered the orders to trade a different mutual fund at that day's NAV, even though on numerous occasions they only received the substitution order after 4:00 p.m. ET.

26. During the same period, DBSI had in place a policy that provided that mutual fund orders received after 4:00 p.m. ET had to be executed at the next day's NAV.

### **DBSI failed to reasonably supervise the RR**

27. While the RR was engaged in the conduct described in paragraphs 12 through 26 above, DBSI had no procedures and systems in place to prevent and detect deceptive market timing engaged in by the RR or the RR's facilitation of late trading, which violated the federal securities laws.

28. For example, in 2001, DBSI had in place a Market Timing Policy that indicated that responsibility for policing market timing rested solely with the mutual funds, and that DBSI exercised "no control over the implementation of timing policies by a mutual fund company." DBSI, however, still had an obligation to sell mutual fund shares in accordance with the federal securities laws.

29. DBSI was aware that customers of the branch office at 280 Park Avenue were engaged in market timing.

30. Further, DBSI received numerous notices from mutual funds that they were blocking customers' trades for engaging in market timing. Many of these letters came to the attention of the DBSI branch management for the 280 Park Avenue office.

31. Despite this knowledge, DBSI failed to establish reasonable procedures designed to prevent and detect deceptive market timing. In particular, DBSI failed to have any procedures in place for identifying and responding to indicia of deceptive market timing, such as evidence indicating that an RR executed market timing trades for his customers in the mutual funds that had blocked his customers' trading because of market timing.

32. Beginning in March 2003, certain RRs were given direct desktop access to DBSI's order processing system for the purpose of entering mutual fund orders. (Previously, the RRs had been required to prepare order tickets and then have the orders manually entered into a software system that routed the orders to DBSI's clearing broker and then into DBSI's mutual fund processing system, which then cleared mutual fund purchases and redemptions through NSCC's FundServ clearance process. Because certain customers placed voluminous mutual fund orders, DBSI's branch management decided to give the RRs for these customers direct desktop access to DBSI's mutual fund processing system, as described above.) At the time, DBSI's principal means of monitoring purchases and redemptions of mutual fund shares consisted of relying on a computer software "rules engine," which required approval of trades within certain specified parameters. This software could automatically block further processing of trades exceeding share or dollar value limits. Thus, if a particular trade exceeded the share or dollar value limits (which was the case with many market timing trades), the trade would be blocked and a supervisor would have to review the trade. This process thus gave the supervisor the opportunity to review trades and should have enabled the supervisor to detect market timing trading, and more specifically, deceptive trading. This safeguard, however, was in place only on the manual software system, and not on the RRs' desktop system. Consequently, when branch management gave the RRs direct access to the mutual fund order processing system, this removed the market timing trades from being subject to the "rules engine" software. Thus, many market timing mutual fund trades were not submitted to branch management for approval prior to execution.

33. DBSI's decision to provide the RRs with direct access to DBSI's order processing system allowed the RR to enter substitution trades up until 4:30 p.m. ET, but receive the same day's NAV.

34. Finally, DBSI failed to have in place or adopt reasonable procedures for monitoring whether RRs submitted mutual fund orders for processing at that day's NAV only if they were received from customers before the market close.

35. If DBSI had had in place procedures and systems for identifying and responding to indicia of deceptive market timing by RRs and for monitoring whether RRs submitted for processing at that day's NAV only those mutual fund orders that were received from customers before market close, it is likely that DBSI could have prevented and detected the RR's deceptive market timing and the RR's facilitation of late trading.

### **DBSI's Remedial Efforts and Cooperation**

36. After DBSI learned of the SEC's inquiry into frequent trading by DBSI customers, DBSI conducted an independent internal investigation, sharing the results of that investigation with the Commission's staff, and implementing certain remedial measures.

### **Violations**

37. As a result of the conduct described in paragraphs 12 through 26 above, the RR violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5 thereunder.

38. Rule 22c-1 under the Investment Company Act provides that no registered investment company issuing any redeemable security, and no dealer in any such security shall sell, redeem, or repurchase any such security except at a price based on the current net asset value of such security which is next computed after receipt of a tender of such security for redemption or of an order to purchase or sell such security. DBSI, by virtue of dealer agreements with the mutual funds, was a dealer within the meaning of Rule 22c-1. DBSI, through the RR, regularly accepted and executed trades after the close of the U.S. equity markets at a price other than the current NAV which was next computed after receipt of a tender of such security for redemption or of an order to purchase or sell such security. As a result of the conduct described above, DBSI willfully<sup>2</sup> violated Rule 22c-1 under the Investment Company Act, and the RR aided and abetted these violations.

39. Section 15(b)(4)(E) of the Exchange Act provides for the imposition of a sanction against a broker or dealer who "has failed reasonably to supervise, with a view to preventing violations of the securities laws, another person who commits such a violation, if such other person is subject to his supervision." As a result of the conduct described in paragraphs 12

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<sup>2</sup> "Willfully" as used in this Offer means intentionally committing the act which constitutes the violation, *see* *Wonsover v. SEC*, 205 F.3d 408, 414 (D.C. Cir. 2000); *Tager v. SEC*, 344 F.2d 5, 8 (2d Cir. 1965). There is no requirement that the actor also be aware that he is violating one of the Rules or Acts.

through 35 above, DBSI failed reasonably to supervise the RR with a view to preventing his violations of the federal securities laws.

#### IV.

In view of the foregoing, the Commission deems it appropriate and in the public interest to impose the sanctions agreed to in Respondent's Offer.

Accordingly, it is hereby ORDERED that:

- A. Pursuant to Section 15(b)(4) of the Exchange Act, DBSI is hereby censured;
- B. Pursuant to Section 9(f) of the Investment Company Act, DBSI shall cease and desist from committing or causing any violations and any future violations of Rule 22c-1(a) as adopted under Section 22(c) of the Investment Company Act;
- C. DBSI shall, within 30 days of the entry of this Order, pay \$202,835 in disgorgement and \$37,284 in prejudgment interest, plus a civil money penalty in the amount of \$202,835, for a total of payment of \$442,954. Such payment shall be: (A) made by wire transfer, United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) wired, hand-delivered, or mailed to the Office of Financial Management, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, VA 22132; and (D) submitted under cover letter that identifies DBSI as a Respondent in these proceedings, the file number of these proceedings, a copy of which cover letter, wire transfer instruction, money order or check shall be sent to Mark K. Schonfeld, Regional Director, Securities and Exchange Commission, Northeast Regional Office, 3 World Financial Center, Room 4300, New York, New York 10281-1022.

By the Commission.

Nancy M. Morris  
Secretary