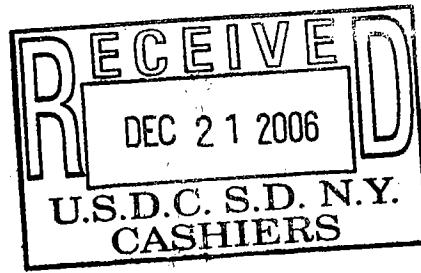


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UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK

Judge Pauley

06 CV 15345

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

-against-

MICHAEL G. VELASCO,

Defendant.

: 06 Civ. \_\_\_\_ ( )

: COMPLAINT

Plaintiff Securities and Exchange Commission ("Commission"), for its Complaint against defendant Michael G. Velasco ("Velasco" or the "Defendant"), alleges as follows:

**PRELIMINARY STATEMENT**

1. The Commission brings this enforcement action against Velasco, a former registered representative ("RR") at Deutsche Bank Securities, Inc. ("DBSI"), who deceptively market timed mutual funds.

2. From approximately March 2003 through September 2003, Velasco utilized deceptive practices to circumvent mutual funds' restrictions on his market timing customers' trading. For example, certain mutual funds identified Velasco's customers as market timers, and then rejected the customers' trades. In response to the mutual funds' efforts to block further

trading, Velasco opened new accounts for his customers, who then used the new accounts to continue market timing the same mutual funds that had previously rejected the customers' trades. Through this conduct, Velasco concealed the true identity of his customers and misled mutual funds into believing that the subsequent trades were for different DBSI customers whose trading had not been blocked. Mutual funds would have rejected these trades had they known Velasco's customers' true identities or trading strategies.

3. Velasco earned significant commissions from his customers who engaged in market timing. At the same time, these customers' market timing trading harmed the mutual funds in which they traded.

#### **VIOLATIONS OF FEDERAL SECURITIES LAWS**

4. Velasco, directly or indirectly, singly or in concert, has engaged in transactions, acts, practices, or courses of business that constitute violations of Section 17(a) of the Securities Act of 1933 ("Securities Act"), 15 U.S.C. § 77q(a), Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. § 78j(b), and Rule 10b-5, 17 C.F.R. § 240.10b-5.

#### **NATURE OF THE PROCEEDINGS AND RELIEF SOUGHT**

5. The Commission brings this action pursuant to the authority conferred upon it by Section 20(b) of the Securities Act, 15 U.S.C. § 77t(b), and Section 21(d)(1) of the Exchange Act, 15 U.S.C. § 78u(d)(1), and seeks a permanent injunction to enjoin Velasco from engaging in the transactions, acts, practices, and courses of business alleged herein. The Commission seeks a judgment ordering Velasco to disgorge his ill-gotten gains and to pay prejudgment interest thereon. The Commission also seeks the imposition of civil money penalties pursuant to Section 20(d) of the Securities Act, 15 U.S.C. § 77t(d), and Section 21(d)(3) of the Exchange Act, 15

U.S.C. § 78u(d)(3). Finally, the Commission seeks all other just and appropriate relief.

#### **JURISDICTION AND VENUE**

7. This Court has jurisdiction over this action pursuant to Sections 20(d) and 22(a) of the Securities Act, 15 U.S.C. §§ 77t(d) and 77v(a), and Sections 21(e) and 27 of the Exchange Act, 15 U.S.C. §§ 78u(e) and 78aa.

8. Venue lies in this District pursuant to Section 22(a) of the Securities Act, 15 U.S.C. § 77v(a), and Section 27 of the Exchange Act, 15 U.S.C. § 78aa. Certain of the transactions, acts, practices, and courses of business alleged herein occurred within the Southern District of New York. For instance, DBSI's headquarters are in New York, New York, and Velasco engaged in the conduct alleged herein while working at a DBSI office located in New York, New York.

9. Velasco, directly or indirectly, made use of the means or instrumentalities of interstate commerce, the means or instruments of transportation or communication in interstate commerce, and/or the mails, in connection with the transactions, acts, practices, and courses of business alleged herein.

#### **DEFENDANT AND RELEVANT ENTITY**

##### **Defendant**

10. Velasco, age 45, is a resident of Basking Ridge, New Jersey. Velasco was a RR at DBSI from February 2001 until January 2004. Velasco worked at DBSI's branch office located at 280 Park Avenue, New York, New York.

##### **Relevant Entity**

11. DBSI is a Delaware corporation with its headquarters and principal executive offices in New York, New York. DBSI is a registered broker-dealer and registered investment

adviser. DBSI provides a comprehensive range of advisory, financial, and investment services to corporate and private customers. DBSI is a subsidiary of Deutsche Bank AG, a German financial services and bank holding company.

## **FACTS**

### **Market Timing**

12. “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.

### **DBSI Served as a Dealer in Mutual Funds**

13. DBSI entered into agreements with the distributors, or principal underwriters, of more than 100 mutual fund families. Each of these agreements, referred to as “dealer agreements,” authorized DBSI to serve as a dealer in a particular mutual fund family’s mutual funds, and thereby to sell the family’s mutual funds to DBSI’s customers.

14. The dealer agreements that DBSI typically entered into required DBSI to sell the fund families’ mutual funds in accordance with the federal securities laws and the terms of the mutual funds’ prospectuses.

15. Prospectuses for many mutual funds, including funds subject to the dealer

agreements DBSI entered into, prohibited 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.

#### **Velasco Sought Market Timing Customers**

16. In or around February 2003, Velasco solicited a hedge fund adviser to open accounts at DBSI to market time mutual funds.

17. When soliciting the hedge fund adviser, Velasco informed him that other customers at DBSI's New York office were market timing mutual funds.

18. The hedge fund adviser then agreed to open accounts at DBSI.

#### **Velasco Engaged In Deceptive Market Timing**

19. Beginning in March 2003 and continuing until September 2003, Velasco participated in a scheme to market time mutual funds with certain customers, including the hedge fund adviser.

20. Shortly after his customers began market timing mutual funds, Velasco received notices from mutual funds advising him that his customers' market timing was harming the mutual funds, and informing him that the customers' future trades would be blocked.

21. Despite receiving these block notices, Velasco and his customers took steps to circumvent the mutual funds' efforts to stop their market timing.

22. These practices included opening new accounts when the customers' trades were blocked, and then transferring funds from the blocked account to the new account so his customer could continue to trade the same mutual funds that had previously blocked the customer's trading.

23. Indeed, Velasco and his sales assistant prepared a daily "blocked list" identifying

mutual fund families that had blocked a customer's particular account. This enabled Velasco's customers to place orders in the same mutual funds, but through new or different accounts.

*Velasco Opened Multiple Accounts for a Hedge Fund Adviser  
to Circumvent Mutual Funds' Efforts to Block the Adviser's Accounts*

24. In or around March 2003, Velasco opened six accounts for his hedge fund adviser customer. Shortly thereafter, the customer began using these accounts to engage in market timing.

25. Within weeks, various mutual funds determined that the accounts were engaged in market timing. Because these mutual funds prohibited market timing, they began to block the customer's accounts from future purchases of the funds' shares.

26. In response, Velasco arranged to open additional accounts for the customer.

27. For example, on or about May 12, 2003, a mutual fund family sent a letter to Velasco that specifically stated that market timing was harmful to the fund family's mutual funds. Further, the letter indicated that the fund family had blocked Velasco's customer's trades. Specifically, the letter contained the following:

[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.

28. Following receipt of the May 12, 2003 letter, Velasco continued to execute market timing trades for his customer in the same mutual funds.

29. To carry out additional trades, however, Velasco had to conceal the customer's true identity from the fund family.

30. Consequently, in or around early June 2003, Velasco instructed his sales assistant to open additional accounts for the customer.

31. On or about June 5, 2003, Velasco's sales assistant opened two additional accounts.

32. The sales assistant then transferred funds from the accounts that the fund family had blocked to the new accounts.

33. The customer then continued market timing the fund family's mutual funds through one of the newly opened accounts.

34. The customer's market timing through the new account continued until the fund family blocked the new account in or around early July 2003 for engaging in market timing.

35. Through his conduct, Velasco was able to conceal from the mutual funds the identity of his hedge fund customer. Further, Velasco was able to mislead mutual funds into believing that the purchases were coming from different DBSI customers whose trading the mutual funds had not already blocked.

#### **Velasco Profited from His Customers' Market Timing While Mutual Funds Suffered Harm**

36. During the period from March 2003 through September 2003, Velasco earned ill-gotten gains through this fraudulent market timing scheme.

37. In particular, DBSI earned fees from Velasco's market timing customers, and DBSI paid a portion of those fees to Velasco.

38. For instance, DBSI received a "wrap fee" of 1.25% of the money it managed for Velasco's hedge fund adviser customer.

39. DBSI earned approximately \$202,835.21 in fees from the hedge fund adviser customer, and DBSI paid approximately \$60,824.26 of this amount to Velasco.

40. At the same time, Velasco's customers' market timing caused harm to the mutual funds.

41. Among other things, Velasco's customers' market timing diluted the value of the mutual fund shares and increased the transaction costs associated with the management of the timed mutual funds.

### **CLAIM FOR RELIEF**

#### **Violations of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act, and Rule 10b-5**

42. Plaintiff repeats and realleges paragraphs 1 through 41 above.

43. Velasco directly and indirectly, singly or in concert, by use of the means or instrumentalities of interstate commerce, or of the mails, in the offer and sale, and in connection with the purchase or sale, of securities, knowingly or recklessly: (a) employed devices, schemes or artifices to defraud; (b) obtained money or property by means of, or otherwise, made untrue statements of material fact, or omitted to state material facts necessary in order to make statements made, in light of the circumstances under which they were made, not misleading; and/or (c) engaged in transactions, acts, practices and courses of business which operated or would have operated as a fraud or deceit upon purchasers of securities and upon other persons.

44. As part and in furtherance of the violative conduct, Velasco participated in a fraudulent scheme to market time mutual funds. For instance, after receiving block notices from the fund companies, Velasco misrepresented the identities of his market timing customers so that they could continue to market time these mutual funds.

45. Velasco misrepresented, and failed to disclose, material information to mutual funds to induce them to accept his customers' trades in the mutual funds. For instance, the fund companies would not have processed the orders submitted by Velasco on behalf of his market timing customers had Velasco disclosed their identities or identified his customers as market timers.

46. Velasco knowingly or recklessly engaged in the fraudulent conduct alleged above.

47. By reason of the foregoing, Velasco, directly or indirectly, violated and, unless enjoined will again violate, Section 17(a) of the Securities Act, 15 U.S.C. § 77q(a), Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5, 17 C.F.R. § 240.10b-5.

**PRAYER FOR RELIEF**

**WHEREFORE**, the Commission respectfully requests a Final Judgment:

**I.**

Permanently enjoining Velasco, his agents, servants, employees, attorneys, and all persons in active concert or participation with him who receive actual notice of the injunction by personal service or otherwise, and each of them, from future violations of Section 17(a) of the Securities Act, 15 U.S.C. § 77q(a), Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5, 17 C.F.R. § 240.10b-5.

**II.**

Ordering Velasco to disgorge the ill-gotten gains he received as a result of his violations of the federal securities laws and to pay prejudgment interest thereon.

**III.**

Ordering Velasco to pay civil money penalties pursuant to Section 20(d) of the Securities

Act, 15 U.S.C. § 77t(d), and Section 21(d)(3) of the Exchange Act, 15 U.S.C. § 78u(d)(3).

IV.

Granting such other and further relief as the Court may deem just and proper.

Dated: New York, New York  
December 21, 2006



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