

## U.S. SECURITIES AND EXCHANGE COMMISSION

Litigation Release No. 20500 / March 18, 2008

*Securities and Exchange Commission v. Tuco Trading, LLC, and Douglas G. Frederick, Case No. 08 CV 0400 DMS BLM (S.D. Cal.)*

### **Federal Court Permanently Enjoins Day-Trading Firm and Its Principal From Future Broker-Dealer Registration and Securities Fraud Violations**

The Securities and Exchange Commission announced today that on March 17, 2008, a federal court permanently enjoined Tuco Trading, LLC, an unregistered securities day-trading firm in La Jolla, California, and its principal, Douglas G. Frederick, from future violations of the broker-dealer registration and antifraud provisions of the federal securities laws. Tuco and Frederick consented to the entry of the permanent injunctions without admitting or denying the allegations of the Commission's complaint.

According to the Commission's complaint, the defendants provided securities day-trading capability to Tuco's over 250 traders who had approximately \$10.2 million in reported equity balances at Tuco. They permitted traders to day-trade securities in Tuco's own brokerage accounts at registered broker-dealers through sub-accounts created at Tuco for each trader. The complaint alleged that Tuco provided traders with services not permitted at a registered broker-dealer. As alleged in the complaint, the defendants allowed traders to day-trade without meeting the \$25,000 minimum equity requirement under NASD regulations for such trading. The complaint also alleges that for each \$1 in the trader's sub-account, Tuco and Frederick allowed the traders at Tuco to use up to \$20 of Tuco's equity, which had been invested by other traders, to purchase securities (20:1 buying power). NASD and NYSE regulations, however, only allow a day-trader to have 4:1 buying power.

The Commission's complaint also alleged that Tuco received transaction-based compensation for its traders' securities transactions, and Tuco's traders conducted substantial day-trading through Tuco's brokerage accounts both in dollar amounts and number of trades. As a result, Frederick earned substantial commissions on the trading as the registered representative for Tuco's main accounts at a registered broker-dealer. The complaint alleged that Frederick then used substantial amounts of his commissions to pay Tuco's operating expenses.

The complaint also alleged that the defendants' inaccurately reported to the traders their equity balances. Specifically, the complaint alleged that as of December 31, 2007, Tuco and Frederick had used about \$3.62 million of the traders' approximately \$10.2 million total equity to pay Tuco's expenses and to cover trader losses and that as of January 31, 2008, approximately a \$1.35 million shortfall remained. As alleged in the complaint, Tuco and Frederick failed to disclose those details or that the traders' recovery of the shortfall in the traders' equity was dependent on Frederick's efforts.

The judgment was entered by the Honorable Dana M. Sabraw, United States District Judge for the Southern District of California. The judgment permanently enjoins Tuco and Frederick from future violations of Sections 10(b) and 15(a) of the Securities and Exchange Act of 1934 and Rule 10b-5 thereunder. The judgment also freezes Tuco's assets, appoints a permanent receiver over Tuco, and prohibits the destruction of documents. The judgment further orders Tuco and Frederick to pay disgorgement with prejudgment interest and civil penalties in amounts to be determined. On March 5, 2008, the Court issued emergency orders appointing a temporary receiver to monitor Tuco, prohibiting destruction of documents, and expediting discovery. For additional information, see Lit. Rel. No. [20480](#) (Mar. 6, 2008)

<http://www.sec.gov/litigation/litreleases/2008/lr20500.htm>