



DEUTSCHE BANK SECURITIES INC.
(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Consolidated Statement of Financial Condition

December 31, 2010

(With Report of Independent Registered Public Accounting Firm Thereon)



KPMG LLP
345 Park Avenue
New York, NY 10154

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholder
Deutsche Bank Securities Inc.:

We have audited the accompanying consolidated statement of financial condition of Deutsche Bank Securities Inc. and subsidiaries (the Company), an indirect wholly owned subsidiary of Deutsche Bank AG, as of December 31, 2010, that you are filing pursuant to Rule 17a-5 under the Securities Exchange Act of 1934 and Regulation 1.10 under the Commodity Exchange Act. This consolidated statement of financial condition is the responsibility of the Company's management. Our responsibility is to express an opinion on this consolidated statement of financial condition based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the statement of financial condition is free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the statement of financial condition, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall statement of financial condition presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated statement of financial condition referred to above presents fairly, in all material respects, the financial position of Deutsche Bank Securities Inc. and subsidiaries as of December 31, 2010, in conformity with U.S. generally accepted accounting principles.

KPMG LLP

February 28, 2011

DEUTSCHE BANK SECURITIES INC.
(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Consolidated Statement of Financial Condition

December 31, 2010

(In thousands)

Assets

Cash and cash equivalents	\$	894,252
Cash and securities segregated for benefit of customers (includes securities at fair value of \$5,211,538)		10,247,177
Securities financing transactions:		
Securities purchased under agreements to resell (includes securities at fair value of \$39,192,437)		62,115,671
Securities borrowed (includes securities at fair value of \$37,039,880)		65,324,147
		127,439,818
Financial instruments owned, at fair value (includes securities pledged as collateral of \$69,789,055)		79,183,872
Receivables:		
Customers		2,970,201
Non-customers		30,585,467
Brokers, dealers, and clearing organizations		3,625,533
Other		7,000,000
		44,181,201
Property, plant, and equipment (net of accumulated depreciation of \$480,514)		634,766
Other assets		3,020,472
Total assets	\$	265,601,558

Liabilities and Stockholder's Equity

Securities financing transactions:		
Securities sold under agreements to repurchase (includes securities at fair value of \$96,376,173)	\$	130,752,458
Securities loaned (includes securities at fair value of \$674,622)		48,977,464
		179,729,922
Payables:		
Customers		10,679,182
Non-customers		6,197,006
Brokers, dealers, and clearing organizations		2,757,023
Other		12,320,800
		31,954,011
Financial instruments sold, but not yet purchased, at fair value		31,458,525
Other liabilities		4,308,393
Total liabilities		247,450,851
Commitments, contingencies and guarantees		
Subordinated liabilities		6,723,400
Stockholder's equity		11,427,307
Total liabilities and stockholder's equity	\$	265,601,558

See accompanying notes to consolidated statement of financial condition.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

(1) Organization

Deutsche Bank Securities Inc. (the Company) is a wholly owned subsidiary of DB U.S. Financial Markets Holding Corporation (the Parent), a wholly owned subsidiary of the Taunus Corporation, which is a direct subsidiary of Deutsche Bank AG (the Bank), a German corporation. The Company is a registered broker-dealer with the Securities and Exchange Commission (SEC) and is a member of the Financial Industry Regulatory Authority (FINRA), various exchanges, and the Securities Investor Protection Corporation (SIPC). As a futures commission merchant, the Company is registered with the Commodities Futures Trading Commission (CFTC), is a clearing member of the Chicago Board of Trade, Chicago Mercantile Exchange, New York Mercantile Exchange, ICE Futures U.S., and is a member of the National Futures Association.

The Company provides trade execution services for a broad range of domestic and international clients. It provides securities brokerage and investment advisory services to private clients and institutions and correspondent clearing services to broker-dealers. The Company provides a variety of capital raising, market making, and brokerage services for its government, financial institution, and corporate clients, including fixed income and equity sales and trading, emerging markets activities, equity market research and investment banking. The Company also executes trading and arbitrage strategies for its own account using debt, equity, and related derivative instruments.

The Company, like other securities firms, is directly affected by general economic and market conditions, including fluctuations in volume and price levels of securities, changes in interest rates, and demand for investment banking, securities brokerage, and other services, all of which have an impact on the Company's consolidated statement of financial condition as well as its liquidity.

(2) Significant Accounting Policies

(a) Basis of Presentation

The Company's consolidated statement of financial condition has been prepared in accordance with U.S. generally accepted accounting principles, which require management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated statement of financial condition. The most important of these estimates and assumptions relate to fair value measurements and the provision for potential losses that may arise from litigation and regulatory proceedings and tax audits. Although these, and other, estimates and assumptions are based on the best available information, actual results could be materially different from these estimates.

The consolidated statement of financial condition includes the accounts of the Company and its wholly owned subsidiaries and other entities in which the Company has a controlling financial interest. The Company's policy is to consolidate all entities in which it owns more than 50% of the outstanding voting stock unless it does not control the entity. The Company also consolidates any variable interest entities (VIEs) for which it is deemed to be the primary beneficiary. All material intercompany transactions and balances have been eliminated in consolidation.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

The consolidated statement of financial condition as of December 31, 2010 reflects \$8.4 billion of assets and liabilities attributable to the Company's subsidiaries as well as certain elimination and reclassification adjustments which are not reflected in the Company's unaudited statement of financial condition contained in Part II of SEC Form X-17A-5 which is prepared on an unconsolidated basis.

In the normal course of business, the Company's operations may include significant transactions conducted with affiliated entities. Such transactions are governed by contractual agreements between the Company and its affiliates.

At December 31, 2010, substantially all of the Company's assets and liabilities were carried at fair value or at amounts which approximate such values. Assets and liabilities recorded at fair value include cash equivalents, financial instruments owned, financial instruments sold, but not yet purchased and certain securities financing transactions. Assets and liabilities recorded at contractual amounts that approximate fair value include certain securities financing transactions, other receivables and payables and subordinated liabilities. The fair values of such items are not materially sensitive to shifts in market interest rates because of the limited term to maturity of many of these instruments and/or their variable interest rates.

(b) *Cash and Cash Equivalents*

The Company defines cash equivalents as short-term, highly liquid securities and interest-earning deposits with original maturities of three months or less, except for those used for trading purposes.

(c) *Cash and Securities Segregated for Benefit of Customers*

Cash and securities segregated for benefit of customers include cash and securities segregated in compliance with federal and other regulations and represent funds deposited by customers and funds accruing to customers as a result of trades or contracts. Also included are funds segregated and held in separate accounts in accordance with Section 4d(2) and Regulation 30.7 of the Commodity Exchange Act.

(d) *Financial Instruments*

The "Financial instruments owned, at fair value" and "Financial instruments sold, but not yet purchased, at fair value" amounts are reflected in the consolidated statement of financial condition at fair value on a trade-date basis.

(e) *Other Financial Assets and Financial Liabilities at Fair Value*

In addition to "Financial instruments owned, at fair value" and "Financial instruments sold, but not yet purchased, at fair value," the Company has elected to account for certain of its other financial assets and financial liabilities at fair value under Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 825-10 (Fair Value Option). The primary reasons for electing the fair value option are to reflect economic events in earnings on a timely basis, to mitigate volatility in earnings from using different measurement attributes and to address simplification and

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

cost-benefit considerations. Such financial assets and financial liabilities accounted for at fair value include certain securities financing transactions and the debt related to consolidated VIEs.

(f) Fair Value Measurements

The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (the exit price). Financial assets are marked to bid prices, and financial liabilities are marked to offer prices. Fair value measurements do not include transaction costs.

The fair value hierarchy under ASC 820 (Fair Value Measurement and Disclosures) prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below:

Basis of Fair Value Measurement

- | | |
|---------|---|
| Level 1 | Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities |
| Level 2 | Quoted prices in markets that are not considered to be active or financial instruments for which all significant inputs are observable, either directly or indirectly |
| Level 3 | Prices or valuations that require inputs that are both significant to the fair value measurement and unobservable |

A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement.

The Company defines active markets for equity instruments based on the average daily trading volume both in absolute terms and relative to the market capitalization for the instrument. The Company defines active markets for debt instruments based on both the average daily trading volume and the number of days with trading activity.

Credit risk is an essential component of fair value. Cash products (e.g., bonds and loans) and derivative instruments (particularly those with significant future projected cash flows) trade in the market at levels which reflect credit considerations. The Company manages its exposure to credit risk as it does other market risks and will price, economically hedge, facilitate and intermediate trades which involve credit risk.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

In determining fair value, the Company separates its “Financial instruments owned, at fair value” and its “Financial instruments sold, but not yet purchased, at fair value” into two categories: cash instruments and derivative contracts.

- *Cash Instruments* – the Company’s cash instruments are generally classified within Level 1 or Level 2 of the fair value hierarchy because they are valued using quoted market prices, broker or dealer quotations, or alternative pricing sources with reasonable levels of price transparency. The types of instruments valued based on quoted market prices in active markets include most U.S. government and sovereign obligations, active listed equities and certain money market securities. Such instruments are generally classified within Level 1 of the fair value hierarchy. Instruments classified within Level 1 of the fair value hierarchy are required to be carried at quoted market prices, even in situations where the Company holds a large position and a sale could reasonably impact the quoted price.

The types of instruments that trade in markets that are not considered to be active, but are valued based on quoted market prices, broker or dealer quotations, or alternative pricing sources with reasonable levels of price transparency include most government agency securities, most investment-grade corporate bonds, certain mortgage products and whole loans, certain bank and bridge loans, less liquid listed equities, state, municipal and provincial obligations, and certain money market securities. Such instruments are generally classified within Level 2 of the fair value hierarchy.

Certain cash instruments are classified within Level 3 of the fair value hierarchy because they trade infrequently and therefore have little or no price transparency. Such instruments include private equity and real estate fund investments, less liquid corporate debt securities and other debt obligations (including less liquid high-yield corporate bonds, distressed debt instruments and collateralized debt obligations (CDOs) backed by corporate obligations), certain whole loans and securities (backed by either commercial or residential real estate). The transaction price is initially used as the best estimate of fair value. Accordingly, when a pricing model is used to value such an instrument, the model is adjusted so that the model value at inception equals the transaction price. This valuation is adjusted only when changes to inputs and assumptions are corroborated by evidence such as transactions in similar instruments, completed or pending third-party transactions in the underlying investment or comparable entities, subsequent rounds of financing, recapitalizations and other transactions across the capital structure, offerings in the equity or debt capital markets, and changes in financial ratios or cash flows.

For positions that are not traded in active markets or are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or nontransferability. Such adjustments are generally based on available market evidence where available. In the absence of such evidence, management’s best estimate is used.

Recent market conditions have increased the level of management judgment required to value cash trading instruments classified within Level 3 of the fair value hierarchy. In particular,

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

management's judgment is required to determine the appropriate risk-adjusted discount rate for cash trading instruments with little or no price transparency as a result of decreased volumes and lower levels of trading activity. In such situations, the Company's valuation is adjusted to approximate rates which market participants would likely consider appropriate for relevant credit and liquidity risks. Due to the level of management judgment and estimate used in the valuation of cash instruments included within Level 3 of the fair value hierarchy, it is possible that other market participants could determine a materially different estimate of fair value for such instruments.

- *Derivative Contracts* – derivative contracts can be exchange-traded or over-the-counter (OTC). Exchange-traded derivatives typically fall within Level 1 or Level 2 of the fair value hierarchy depending on whether they are deemed to be actively traded or not. The Company generally values exchange-traded derivatives using models which calibrate to market-clearing levels and eliminate timing differences between the closing price of the exchange-traded derivatives and their underlying instruments. In such cases, exchange-traded derivatives are classified within Level 2 of the fair value hierarchy.

OTC derivatives are valued using market transactions and other market evidence whenever possible, including market-based inputs to models, model calibration to market clearing transactions, broker or dealer quotations, or alternative pricing sources with reasonable levels of price transparency. Where models are used, the selection of a particular model to value an OTC derivative depends upon the contractual terms of, and specific risks inherent in, the instrument as well as the availability of pricing information in the market. The Company generally uses similar models to value similar instruments. Valuation models require a variety of inputs, including contractual terms, market prices, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs. For OTC derivatives that trade in liquid markets, such as generic forwards, swaps and options, model inputs can generally be verified and model selection does not involve significant management judgment. OTC derivatives are classified within Level 2 of the fair value hierarchy when all of the significant inputs can be corroborated to market evidence.

Certain OTC derivatives trade in less liquid markets with limited pricing information, and the determination of fair value for these derivatives is inherently more difficult. Such instruments are classified within Level 3 of the fair value hierarchy. Where the Company does not have corroborating market evidence to support significant model inputs and cannot verify the model to market transactions, the transaction price is initially used as the best estimate of fair value. Accordingly, when a pricing model is used to value such an instrument, the model is adjusted so that the model value at inception equals the transaction price. The valuations of these less liquid OTC derivatives are typically based on Level 1 and/or Level 2 inputs that can be observed in the market, as well as unobservable Level 3 inputs. Subsequent to initial recognition, the Company updates the Level 1 and Level 2 inputs to reflect observable market changes, with resulting gains and losses reflected within Level 3. Level 3 inputs are only changed when corroborated by evidence such as similar market transactions, third-party pricing services and/or broker or dealer quotations, or other empirical market data. In

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

circumstances where the Company cannot verify the model value to market transactions, it is possible that a different valuation model could produce a materially different estimate of fair value.

When appropriate, valuations are adjusted for various factors such as liquidity, bid/offer spreads and credit considerations. Such adjustments are generally based on available market evidence. In the absence of such evidence, management's best estimate is used.

(g) *Securities Financing Transactions*

Securities financing transactions consist of the following:

- *Resale and Repurchase Agreements* – securities purchased under agreements to resell (reverse repurchase agreements) and securities sold under agreements to repurchase (repurchase agreements) are accounted for as collateralized financing transactions and are recorded at their contractual amounts, plus accrued interest. The Company's policy is to obtain possession of collateral with a market value equal to or in excess of the principal amount loaned under reverse repurchase agreements. To ensure that the market value of the underlying collateral remains sufficient, collateral is valued daily, and the Company may require counterparties to deposit additional collateral or return collateral pledged, when appropriate. Substantially all repurchase and reverse repurchase activities are transacted under master netting agreements that give the Company the right, in the event of default, to liquidate collateral held and offset receivables and payables with the same counterparty. Interest earned on reverse repurchase agreements and interest incurred on repurchase agreements are reported as interest revenues and interest expense, respectively.

As noted above, certain resale and repurchase agreements are carried in the consolidated statement of financial condition at fair value. Resale and repurchase agreements are generally valued based on inputs with reasonable levels of price transparency and are classified within Level 2 of the fair value hierarchy.

Reverse repurchase and repurchase agreements with common counterparties, along with their respective interest receivables and payables, are reported net by counterparty, when applicable, pursuant to the provisions of ASC 210-20 (Offsetting). At December 31, 2010, the Company's reverse repurchase and repurchase agreements reflected approximately \$30.9 billion of netting pursuant to ASC 210-20.

In accordance with ASC 860-30 (Secured Borrowing and Collateral), \$51.0 billion of U.S. government securities are pledged as collateral under repurchase agreements which the counterparty is permitted to sell or repledge. Additionally, \$110.6 billion of U.S. government and corporate securities have been pledged as collateral under agreements to repurchase for which the counterparty does not have the right to sell or repledge.

- *Securities Borrowed and Loaned* – securities borrowed and loaned transactions are recorded at the amount of cash collateral advanced or received. Securities borrowed transactions require

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

the Company to provide the counterparty with collateral in the form of cash, letters of credit, or other securities. The Company receives collateral in the form of cash or other securities for securities loaned transactions. On a daily basis, the Company monitors the market value of securities borrowed or loaned against the collateral value and the Company may require counterparties to deposit additional collateral or return collateral pledged, when appropriate.

As these arrangements generally can be terminated on demand, they exhibit little, if any, sensitivity to changes in interest rates. Certain securities borrowed and loaned transactions are recorded at fair value under the fair value option. These securities borrowed and loaned transactions are generally valued based on inputs with reasonable levels of price transparency and are classified within Level 2 of the fair value hierarchy.

(h) *Receivables and Payables – Customers*

Receivables from and payables to customers include amounts due on cash and margin transactions. Securities owned by customers, including those that collateralize margin or similar transactions, are not reflected on the consolidated statement of financial condition.

(i) *Receivables and Payables – Non-customers*

Receivables from and payables to non-customers include amounts due on cash and margin transactions of banks and broker dealers trading for their own account through the Company. These amounts represent transactions made predominantly with affiliates. Securities owned by non-customers, including those that collateralize margin or similar transactions, are not reflected on the consolidated statement of financial condition.

(j) *Receivables and Payables – Other*

Other receivables and payables, consisting primarily of loans receivable and payable, are presented on the consolidated statement of financial condition at their outstanding unpaid principal balances. These loans are predominantly made with affiliates. Interest revenue is accrued on the unpaid principal balance.

(k) *Foreign Currency Translation*

Assets and liabilities denominated in non-U.S. dollar currencies are translated into U.S. dollar equivalents using year-end spot foreign exchange rates.

(l) *Share-Based Compensation*

The Bank has a share ownership program granting certain employees of the Company special stock awards and incentives as part of their total compensation. The cost of employee services received in exchange for a share-based award is generally measured based on the grant-date fair value of the award in accordance with ASC 718. Share-based awards that do not require future service (i.e., vested awards, including awards granted to retirement eligible employees) are expensed immediately. Share-based employee awards that require future service are amortized over the

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

relevant service period. Expected forfeitures are included in determining share-based employee compensation expense.

(m) Exchange Memberships

Exchange memberships are recorded at cost, less impairment, and are included in other assets on the accompanying consolidated statement of financial condition.

(n) Property, Plant, and Equipment

Property, plant, and equipment are stated at cost less accumulated depreciation and amortization. Depreciation of furniture, fixtures, equipment, and computer software is computed using the straight-line method over their estimated useful lives of three to seven years. Buildings are depreciated on a straight-line basis over their estimated useful lives of 27 years. Leasehold improvements are amortized on a straight-line basis over the terms of the leases or the estimated useful lives of the improvements, whichever is shorter.

(o) Income Taxes

The results of the Company and its wholly owned subsidiaries are included in the consolidated U.S. federal income tax return, and certain combined and unitary state tax returns of its parent, the Taunus Corporation. Pursuant to a tax sharing agreement, income taxes are computed on a separate company basis. In addition, the Company files tax returns in certain states on a stand alone basis. Further, the Company is reimbursed on a current basis by its parent, the Taunus Corporation, for the value of any federal taxable losses of the Company.

The Company provides for income taxes on all transactions that have been recognized in the consolidated statement of financial condition in accordance with ASC 740 (Income Taxes). Accordingly, deferred taxes are adjusted to reflect the tax rates at which future taxable amounts will likely be settled or realized. The effects of tax rate changes on future deferred tax liabilities and deferred tax assets, as well as other changes in income tax laws, are recognized in the period during which such changes are enacted. Deferred tax assets are recognized subject to management's judgment that realization is more likely than not. Deferred tax assets and liabilities are included in other assets and liabilities, respectively, on the consolidated statement of financial condition.

ASC 740 clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements and prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Interpretation also provides guidance on derecognition, classification, interest and penalties, disclosure, and transition.

(p) Variable Interest Entities (VIEs)

VIEs are entities that lack one or more of the characteristics of a voting interest entity. A controlling financial interest in a VIE is present when an enterprise has a variable interest, or a combination of variable interests, that provides the enterprise with (i) the power to direct the activities of the VIE

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

that most significantly impact the VIE's economic performance and (ii) the obligation to absorb losses of the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE. The enterprise with a controlling financial interest, known as the primary beneficiary, consolidates the VIE. The Company determines whether it is the primary beneficiary of a VIE by performing an analysis that principally considers: (i) the VIE's purpose and design, including the risks the VIE was designed to create and pass through to its variable interest holders, (ii) the VIE's capital structure, (iii) the terms between the VIE and its variable interest holders and other parties involved with the VIE, (iv) which variable interest holders have the power to direct the activities of the VIE that most significantly impact the VIE's economic performance, (v) which variable interest holders have the obligation to absorb losses or the right to receive benefits from the VIE that could potentially be significant to the VIE and (vi) related party relationships. The Company reassesses its initial evaluation of an entity as a VIE upon the occurrence of certain reconsideration events. The Company reassesses its determination of whether the Company is the primary beneficiary of a VIE upon changes in facts and circumstances that could potentially alter the Company's assessment.

(g) *Recent Accounting Developments*

Transfers of Financial Assets and Interests in Variable Interest Entities. In June 2009, the FASB issued amended accounting principles that changed the accounting for securitizations and VIEs. These principles were codified as Accounting Standards Update (ASU) No. 2009-16, "Transfers and Servicing (Topic 860) – Accounting for Transfers of Financial Assets" and ASU No. 2009-17, "Consolidations (Topic 810) – Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities" in December 2009. ASU No. 2009-16 eliminates the concept of a qualifying special-purpose entity (QSPE), changes the requirements for derecognizing financial assets, and requires additional disclosures about transfers of financial assets, including securitization transactions and continuing involvement with transferred financial assets. ASU No. 2009-17 changes the accounting and requires additional disclosures for VIEs. Under ASU No. 2009-17, the determination of whether to consolidate a VIE is based on the power to direct the activities of the VIE that most significantly impact the VIE's economic performance together with either the obligation to absorb losses or the right to receive benefits that could be significant to the VIE, as well as the VIE's purpose and design. Additionally, entities previously classified as QSPEs are now required to be evaluated for consolidation and disclosure as VIEs. Previously, QSPEs were not consolidated and not considered for disclosure as VIEs and the determination of whether to consolidate a VIE was based on whether an enterprise had a variable interest, or combination of variable interests, that would absorb a majority of the VIE's expected losses, receive a majority of the VIE's expected residual returns, or both. ASU Nos. 2009-16 and 2009-17 were effective for fiscal years beginning after November 15, 2009. Adoption of these amended accounting principles did not have a material impact on the Company's statement of financial condition.

Improving Disclosures about Fair Value Measurements. In January 2010, the FASB issued ASU No. 2010-06, "Fair Value Measurements and Disclosures (Topic 820) – Improving Disclosures about Fair Value Measurements." ASU No. 2010-06 provides amended disclosure requirements related to fair value measurements. Certain disclosure requirements of ASU No. 2010-06 were effective for the

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

Company beginning on January 1, 2010, while other disclosure requirements of the ASU are effective for financial statements issued for reporting periods beginning after December 15, 2010. Since these amended principles require only additional disclosures concerning fair value measurements, adoption did not and will not affect the Company's financial condition.

Balance Sheet Offsetting. In January 2011, the FASB and the IASB jointly issued an exposure draft of a proposed ASU, "Balance Sheet (ASC Topic 210), Offsetting". Under the proposal, an entity would be required to offset (that is, present as a single net amount in the statement of financial condition) a recognized eligible asset and a recognized eligible liability when it has an unconditional and legally enforceable right of offset and intends either to settle the asset and liability on a net basis or to realize the asset and settle the liability simultaneously. The proposal clarifies that the offsetting criteria would apply whether the right of setoff arises from a bilateral arrangement or from a multilateral arrangement (that is, between three or more parties). The proposal also requires that a right of offset must be legally enforceable in all circumstances (including default or bankruptcy of a counterparty) and that its exercisability must not be contingent on a certain event. The proposal would require an entity to disclose information about offsetting and related arrangements (such as collateral agreements) to enable users of its financial statements to understand the effect of those arrangements on its financial position. The proposal would replace the requirements for offsetting and the existing exceptions for derivatives and repurchase agreements. The comment period for the proposed standard will end April 28, 2011. The proposed guidance is expected to have a significant impact on the Company's consolidated statement of financial position.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

(3) Financial Instruments**(a) Fair Value of Financial Instruments**

The following table sets forth the Company's financial instruments owned, at fair value, including those pledged as collateral, and financial instruments sold, but not yet purchased, at fair value (in thousands):

	<u>Assets</u>	<u>Liabilities</u>
U.S. Treasury securities	\$ 18,365,509	16,877,502
U.S. Government Agency obligations (excluding MBS)	29,725,798	1,398,382
MBS issued or guaranteed by U.S. Government agencies	1,919,874	-
Other mortgage backed securities	902,050	-
Asset backed securities	3,268,645	5,659
Other structured financial products	14,518	-
Other debt securities	11,613,639	3,763,128
Equities	5,026,348	3,678,395
Contractual agreements:		
Interest rate contracts	4,925,054	5,006,143
Foreign contracts	-	-
Credit contracts	56,541	3,892
Equity contracts	1,533,774	717,521
Futures contracts	3,116	-
Commercial paper and money market funds	1,466,289	-
State and municipal bond obligations	362,717	7,903
Total	<u>\$ 79,183,872</u>	<u>31,458,525</u>

DEUTSCHE BANK SECURITIES INC.
(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition
December 31, 2010

(b) Fair Value Hierarchy

The following table sets forth by level within the fair value hierarchy “Financial instruments owned, at fair value,” “Financial instruments sold, but not yet purchased, at fair value” and other financial assets and financial liabilities accounted for at fair value under the fair value option as of December 31, 2010 (in thousands). Refer to note 2 for further information on the fair value hierarchy. Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

	Level 1	Level 2	Level 3	Counterparty and Cash Collateral Netting	Total
<u>Assets:</u>					
Cash equivalents	\$ 504,406	-	-	-	504,406
Cash and securities segregated for benefit of customers	-	5,211,538	-	-	5,211,538
Securities financing transactions	-	76,232,317	-	(30,892,073)	45,340,244
Financial instruments owned:					
U.S. Treasury securities	15,856,672	2,508,837	-	-	18,365,509
U.S. Government Agency obligations (excluding MBS)	-	29,679,443	46,355	-	29,725,798
MBS issued or guaranteed by U.S Government agencies	-	1,116,468	803,406	-	1,919,874
Other mortgage backed securities	-	821,143	80,907	-	902,050
Asset backed securities	-	2,859,938	408,707	-	3,268,645
Other structured financial products	-	-	14,518	-	14,518
Other debt securities	-	11,055,995	557,644	-	11,613,639
Equities	4,414,899	554,009	57,440	-	5,026,348
Contractual agreements:					
Interest rate contracts	-	4,427,228	497,826	-	4,925,054
Credit contracts	-	55,829	712	-	56,541
Equity contracts	3,454,242	9,234	4	(1,929,706)	1,533,774
Futures contracts	491	2,625	-	-	3,116
Commercial paper and money market funds	-	1,466,056	233	-	1,466,289
State and municipal bond obligations	6,195	283,233	73,289	-	362,717
Total financial instruments owned	23,732,499	54,840,038	2,541,041	(1,929,706)	79,183,872
Securities received as collateral	-	81,516	-	-	81,516
Total assets at fair value	\$ 24,236,905	136,365,409	2,541,041	(32,821,779)	130,321,576

DEUTSCHE BANK SECURITIES INC.
(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition
December 31, 2010

	Level 1	Level 2	Level 3	Counterparty and Cash Collateral Netting	Total
Liabilities					
Securities financing transactions	\$ -	97,050,796	-	(30,892,073)	66,158,723
Financial instruments sold, not yet purchased:					
U.S. Treasury Securities	16,176,608	700,894	-	-	16,877,502
U.S. Government Agency obligations (excluding MBS)	-	1,398,382	-	-	1,398,382
Asset backed securities	-	5,659	-	-	5,659
Other debt securities	4	3,761,327	1,797	-	3,763,128
Equities	3,306,479	371,070	846	-	3,678,395
Contractual agreements:					
Interest rate contracts	-	4,965,066	41,077	-	5,006,143
Credit contracts	3,803	-	89	-	3,892
Equity contracts	2,645,333	1,762	132	(1,929,706)	717,521
State and municipal bond obligations	119	7,784	-	-	7,903
Total financial instruments sold, not yet purchased	22,132,346	11,211,944	43,941	(1,929,706)	31,458,525
Obligation to return securities as collateral	-	81,516	-	-	81,516
Total liabilities at fair value	\$ 22,132,346	108,344,256	43,941	(32,821,779)	97,698,764

(c) Level 3 Financial Assets / Financial Liabilities

The table below presents additional information about Level 3 assets and liabilities measured at fair value on a recurring basis (in thousands). Level 3 instruments may be hedged with instruments classified in Level 1 and Level 2. As a result, the realized and unrealized gains and losses for assets and liabilities within the Level 3 category presented in the tables below do not reflect the related realized or unrealized gains and losses on hedging instruments that have been classified by the Company within the Level 1 and/or Level 2 categories. Additionally, both observable and unobservable inputs may be used to determine the fair value of positions that the Company has classified within the Level 3 category. As a result, the unrealized gains and losses for assets and liabilities within the Level 3 category presented in the tables below may include changes in fair value that were attributable to both observable (e.g., changes in market interest rates) and unobservable (e.g., changes in unobservable long-dated volatilities) inputs.

DEUTSCHE BANK SECURITIES INC.
(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition
December 31, 2010

	Beginning Balance	Realized gains (losses)	Unrealized gains (losses)	Transfers in and/or out of Level 3	Purchases, sales, issuances and settlements, net.	Ending Balance
Assets:						
Financial instruments owned:						
US Treasury securities	\$ 21,315	-	-	(21,315)	-	-
US Government Agency obligations (excluding MBS)	32,722	-	(84,408)	486,549	(388,508)	46,355
MBS issued or guaranteed by US Government agencies	760,122	(14,484)	(60,728)	-	118,496	803,406
Other mortgage backed securities	529,511	-	2	(184,835)	(263,771)	80,907
Asset backed securities	1,011,518	5,420	5,206	(247,701)	(365,736)	408,707
Other structured financial products	16,398	-	250	-	(2,130)	14,518
Other debt securities	1,858,263	61,610	30,623	(906,520)	(486,332)	557,644
Equities	102,020	8,624	24,269	(4,122)	(73,351)	57,440
Contractual agreements:						
Interest rate contracts	2,983,319	-	(106,202)	(49,093)	(2,330,198)	497,826
Credit contracts	387,693	-	712	-	(387,693)	712
Equity contracts	-	-	-	-	4	4
Commercial paper and money market funds	5,429	-	(5,196)	-	-	233
State and municipal bond obligations	19,336	-	(759)	30,725	23,987	73,289
Total financial instruments owned	\$ 7,727,646	61,170	(196,231)	(896,312)	(4,155,232)	2,541,041
Liabilities						
Financial instruments sold, not yet purchased:						
Other debt securities	115,147	(17)	(12)	(100,064)	(13,257)	1,797
Equities	730	-	-	116	-	846
Contractual agreements:						
Interest rate contracts	-	-	-	41,077	-	41,077
Credit contracts	-	-	89	-	-	89
Equity contracts	4,000	-	-	-	(3,868)	132
Commodity contracts	-	-	-	-	-	-
Total financial instruments sold, not yet purchased:	\$ 119,877	(17)	77	(58,871)	(17,125)	43,941

There were no significant transfers between Level 1 and Level 2 of the fair value hierarchy during the period ended December 31, 2010.

(d) Financial Instruments not Measured at Fair Value

Certain of the Company's financial assets and liabilities are not measured at fair value on a recurring basis but nevertheless are recorded at amounts that approximate fair value due to their liquid or short-term nature.

(e) Derivative Activities

Derivative contracts (contractual agreements) are instruments, such as futures, forwards, swaps or option contracts that derive their value from underlying assets, indices, reference rates, or a combination of these factors. Derivative contracts may be privately negotiated contracts, which are often referred to as OTC derivatives, or they may be listed and traded on an exchange. Derivatives may involve future commitments to purchase or sell financial instruments, or to exchange currency or interest payment streams. The amounts exchanged are based on the specific terms of the contract with reference to specified rates, securities, currencies, or indices.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

Substantially all of the Company's derivative transactions are entered into for trading purposes, to facilitate customer transactions, to take proprietary positions or as a means of risk management. Risk exposures are managed through diversification, by controlling position sizes and by establishing hedges in related securities or derivatives. The Company does not apply hedge accounting under ASC 815 (Derivatives and hedging) to any of its derivative contracts.

The following table sets forth the fair value and the number of the Company's derivative contracts by major product type on a gross basis as of December 31, 2010. Gross fair values in the table below exclude the effects of both netting under enforceable netting agreements and netting of cash received or posted pursuant to credit support agreements, and therefore are not representative of the Company's exposure (in thousands, except number of contracts):

<u>Derivative contract type</u>	<u>Derivative Assets</u>	<u>Derivative Liabilities</u>	<u>Number of Contracts</u>
Contractual agreements:			
Interest rate contracts	\$ 14,812,268	14,893,357	73,151
Credit contracts	4,786,634	4,733,985	21
Equity contracts	1,533,774	717,521	3,906
Futures contracts	3,116	-	154
Subtotal	<u>\$ 21,135,792</u>	<u>20,344,863</u>	<u>77,232</u>
Counterparty netting (1)	(14,595,667)	(14,595,667)	
Cash collateral netting (2)	(21,640)	(21,640)	
Total fair value	<u>\$ 6,518,485</u>	<u>5,727,556</u>	

(1) Represents the netting of receivable balances with payable balances for the same counterparty pursuant to credit support agreements.

(2) Represents the netting of cash collateral received and posted on a counterparty basis pursuant to credit support agreements.

The Company generally enters into International Swaps and Derivative Association, Inc. master agreements or their equivalent with each of its counterparties, whenever possible. These master netting agreements provide protection in bankruptcy in certain circumstances and to further reduce default risk, the Company requires collateral, generally cash or securities in connection with its derivative transactions.

Credit Derivatives – The Company enters into credit derivatives, principally through credit default swaps, under which it provides counterparties protection against the risk of default on a set of debt obligations issued by a specified reference entity or entities. A majority of the Company's counterparties are banks, broker-dealers, insurance and other financial institutions, and monoline insurers. The table below summarizes certain information regarding protection sold through credit default swaps and credit-linked notes as of December 31, 2010 (in millions):

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

Credit ratings of the reference obligation	Protection sold				Fair value asset (liability) (1)
	Maximum potential payout/notional				
	Years to maturity				
	Less than 1	1 – 5	Over 5	Total	
Single-name credit default swaps:					
AAA	\$ —	—	62	62	(5)
AA	—	—	5	5	(1)
A	—	—	58	58	(8)
BBB	—	—	27	27	(5)
Noninvestment grade	—	4	713	717	(406)
	—	4	865	869	(425)
Multi-name credit default swaps:					
Noninvestment grade	—	675	11,473	12,148	(5,582)
	—	675	11,473	12,148	(5,582)
Total return swaps:					
Noninvestment grade	—	—	—	—	(1)
	—	—	—	—	(1)
Total protection sold	\$ —	679	12,338	13,017	(6,008)

(1) Fair value amounts are shown on a gross basis prior to cash collateral or counterparty netting.

The maximum potential amounts of future payments under credit derivatives contracts are based on the notional value of derivatives. The Company believes that the maximum potential amount of future payments for credit protection sold does not represent the actual loss exposure based on historical experience. In addition, the maximum amount of future payments for credit protection sold has not been reduced for any cash collateral paid to counterparties. Payments under credit derivative contracts would be calculated after netting all derivative exposures with that counterparty in accordance with a related master netting agreement. Due to such netting processes, determining the amount of collateral that relates to credit exposures only is not possible.

Single-name and multi-name credit default swaps – A credit default swap protects the buyer against the loss of principal on a bond or loan in case of a default by the issuer. The protection buyer pays a periodic premium (typically quarterly) over the life of the contract and is protected for the period. The Company in turn will have to perform under a credit default swap if a credit event as defined under the contract occurs. Typical credit events include bankruptcy, dissolution, or insolvency of the referenced entity; failure to pay; the obligations of the referenced entity and restructuring of the obligations of the referenced entity. In order to provide an indication of the current payment status or performance risk of the credit default swaps, the external credit ratings, primarily Moody's credit ratings, of the underlying reference entity of the credit default swaps are disclosed.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

Total return swaps – a total return swap transfers the risks relating to economic performance of a reference obligation from the protection buyer to the protection seller. Typically the protection buyer receives from the protection seller a floating rate of interest and protection against any reduction in fair value of the reference obligation, and in return the protection seller receives the cash flows associated with the reference obligation, plus any increase in the fair value of the reference obligation.

Purchased credit protection – For single-name credit default swaps and total return swaps, the Company has purchased protection with a notional amount of approximately \$19.2 billion, compared with a notional amount of approximately \$13.0 billion of credit protection sold with identical underlying reference obligations. The purchase of credit protection does not represent the sole manner in which the Company risk manages its exposure to credit derivatives. The Company manages its exposure to these derivative contracts through a variety of risk mitigation strategies. Aggregate market risk limits have been established for credit derivatives, and market risk measures are routinely monitored against these limits. The Company may also recover amounts on the underlying reference obligation delivered to the Company under credit default swaps where credit protection was sold.

Credit-Risk Related Contingent Features in Derivatives

For the Company's OTC derivative contracts that are with related parties, there are no credit-risk-related contingent features in these contracts with provisions that require the Company to either settle immediately, or post additional collateral if its credit rating, or the credit rating of its affiliates, is downgraded.

(4) Securities Pledged as Collateral and Obligations to Return Collateral

The Company pledges firm-owned assets to collateralize repurchase agreements and other secured financings. Pledged securities that can be sold or re-pledged by the secured party are parenthetically disclosed in financial instruments owned on the consolidated statement of financial condition.

In transactions where the Company acts as a lender in a securities lending agreement and receives securities that can be pledged or sold as collateral, it recognizes an asset on the consolidated statement of financial condition, representing the securities received, and a liability for the same amount, representing the obligation to return those securities. At December 31, 2010, included in other assets and other liabilities on the accompanying consolidated statement of financial condition was approximately \$81.5 million resulting from these transactions.

As of December 31, 2010, the Company has received collateral of \$97.0 billion and \$73.0 billion under agreements to resell and securities borrowed, respectively, of which \$86.0 billion and \$55.5 billion, respectively, has been re-pledged as collateral for repurchase transactions, securities lending transactions, to meet margin requirements at clearing organizations and to facilitate short sales of customer and non-customers.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

As of December 31, 2010, in the normal course of business, the Company was in possession of collateral in the amount of \$6.8 billion and \$62.9 billion from customers and non-customers, respectively, of which \$2.6 billion and \$43.6 billion, respectively, has been pledged for securities lending transactions, repurchase transactions and to facilitate short sales of customers and non-customers.

(5) Securitization Activities and Variable Interest Entities

(a) Securitization Activities

The Company engages in securitization activities related to commercial and residential mortgage loans and other types of financial assets. The Company may act as an underwriter of the beneficial interests that are sold to investors. The Company derecognizes financial assets transferred in securitizations, provided it has relinquished control over such assets. Transferred assets are accounted for at fair value prior to securitization. The Company generally receives cash in exchange for transferred assets. Net revenues related to underwriting activities are recognized in connection with the sales of the underlying beneficial interests to investors.

The Company may have retained interests in transferred financial assets. These retained interests are classified as financial instruments owned in the consolidated statement of financial condition and are measured at fair value. The outstanding principal amount of the underlying collateral and fair value of retained interests transferred at December 31, 2010 were \$291.7 million and \$192.3 million, respectively.

The following table sets forth the weighted average key economic assumptions used in measuring the fair value of the Company's retained interests and the sensitivity of this fair value to immediate adverse changes of 10% and 20% in those assumptions at December 31, 2010 (in thousands):

	Mortgage- backed
Fair value of retained interests	\$ <u>192,304</u>
Constant prepayment rate	5.00%
Impact of 10% adverse change	\$ (1,151)
Impact of 20% adverse change	(2,332)
Anticipated credit losses	5.06%
Impact of 10% adverse change	\$ (1,125)
Impact of 20% adverse change	(2,258)
Discount rate	21.48%
Impact of 10% adverse change	\$ (7,607)
Impact of 20% adverse change	(14,591)

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

(b) Variable Interest Entities (VIEs)

The Company, in the ordinary course of business, creates or transacts with entities that are considered VIEs. The Company also purchases and sells variable interests in VIEs which primarily issue mortgage-backed and other asset backed securities in connection with its market making activities and making investments in VIEs that hold performing and nonperforming debt, equity and other assets. Substantially all of the consolidated assets of the VIE act as the collateral for the related consolidated liabilities.

The Company's variable interests in VIEs include senior and subordinated debt interests in mortgaged backed and asset backed securitization vehicles. The Company's exposure to the obligations of VIEs is generally limited to its interests in these entities. The Company has aggregated nonconsolidated VIEs based on the principal business activities. The following table sets forth (in thousands) the carrying amounts of assets in nonconsolidated VIEs in which the Company holds variable interests and the Company's maximum exposure to loss excluding the benefit of offsetting financial instruments that are held to mitigate the risks associated with these variable interests. In accordance with ASC 860 (Transfers and Servicing) and ASC 810 (Consolidations), the following table includes nonconsolidated VIEs in which the Company holds variable interests (and to which the Company sold assets and has continuing involvement as of December 31, 2010) that were formerly considered QSPEs prior to the adoption of these standards.

	Carrying value of variable interests held	Maximum exposure of debt interests
Residential mortgages	\$ 291,651	192,304
Commercial mortgages	1,525,941	1,525,941
Total	<u>\$ 1,817,592</u>	<u>1,718,245</u>

The following table sets forth the carrying amount (in thousands) and classification of the Company's assets and liabilities, excluding the benefit of offsetting financial instruments that are held to mitigate the risks associated with its variable interests, in consolidated VIEs. In accordance with ASC 810, the following table excludes VIEs in which the Company holds a majority of voting interest if the VIE meets the definition of a business as defined in ASC 805 and the VIE's assets can be used for purposes other than settlement of its obligations. The Company has aggregated consolidated VIEs based on principal business activity. Consolidated VIE assets and liabilities are presented after intercompany eliminations and include assets financed on a nonrecourse basis.

DEUTSCHE BANK SECURITIES INC.(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

	<u>Asset backed securities</u>
Assets	
Financial instruments owned	\$ 67,205
Other assets	979
Total assets	<u>\$ 68,184</u>
Liabilities	
Other payables	\$ 54,270
Other liabilities	892
Total liabilities	<u>\$ 55,162</u>

The Company's maximum exposure to loss presented in the preceding tables does not reflect the benefit of offsetting financial instruments that are held to mitigate the risks associated with these variable interests.

(6) Receivable from and Payable to Brokers, Dealers, and Clearing Organizations

Amounts receivable from and payable to brokers, dealers, and clearing organizations as of December 31, 2010 consist of the following (in thousands):

	<u>Receivable</u>	<u>Payable</u>
Securities failed to deliver/receive	\$ 2,098,458	1,989,551
Payable to clearing broker	—	109,776
Receivable from clearing organizations	1,403,381	—
Other	123,694	657,696
	<u>\$ 3,625,533</u>	<u>2,757,023</u>

The Company clears certain of its proprietary and customer transactions through other broker-dealers on a fully disclosed basis. The amount payable to the clearing broker relates, in part, to the above-mentioned transactions and is collateralized by securities owned by the Company.

(7) Receivables and Payables – Other

As of December 31, 2010, all of the Company's receivables, aggregating \$7.0 billion, were with affiliates, unsecured and were overnight or short-term.

The Company maintains an uncommitted bank loan facility whereby it may borrow funds on an unsecured or secured basis from the Bank at various rates approximating the Federal Funds rate of interest. At December 31, 2010, all but \$1.2 billion of the Company's borrowings, aggregating approximately \$12.3 billion, which are included in other payables in the accompanying consolidated statement of

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

financial condition were with affiliates and were unsecured. At December 31, 2010, the weighted average interest rate on these borrowings was approximately 0.86%. In addition, approximately \$11.1 billion of the borrowings were overnight or short-term.

(8) Related-Party Transactions

The Company is involved in significant financing and other transactions, and has significant related-party balances with certain of its affiliates. The Company generally enters into these transactions in the ordinary course of business and believes that these transactions are generally on market terms that could be obtained from unrelated third parties. Related party financing transactions are also discussed in notes 5 and 14.

(a) Related-Party Assets and Liabilities

The following table sets forth related-party assets and liabilities as of December 31, 2010 (in thousands):

Assets:

Cash and cash equivalents	\$ 693,329
Cash and securities segregated for benefit of customers	2,094,638
Securities purchased under agreements to resell	24,219,910
Securities borrowed	2,003,607
Financial instruments owned – contractual agreements	305,909
Receivable from customers	78,152
Receivable from non-customers	30,526,478
Receivable from brokers, dealers, and clearing organizations	2,456,381
Receivables – other	7,000,000
Other assets	1,197,038
	<u>\$ 70,575,442</u>

Liabilities:

Securities sold under agreements to repurchase	\$ 21,020,386
Securities loaned	45,620,470
Payable to customers	660,121
Payable to non-customers	6,153,523
Payable to brokers, dealers, and clearing organizations	525,766
Payables – other	12,015,301
Financial instruments sold – contractual agreements	251,309
Other liabilities	1,618,232
Subordinated liabilities	6,723,400
	<u>\$ 94,588,508</u>

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

(9) Categories of Risk

(a) Market Risk

Market risk is the potential loss the Company may incur as a result of changes in the market value of a particular instrument. All financial instruments, including derivatives and short sales, are subject to market risk. The Company's exposure to market risk is determined by a number of factors, including the size, duration, composition, and diversification of positions held, the absolute and relative levels of interest rates and foreign currency exchange rates as well as market volatility and illiquidity. For instruments such as options and warrants, the time period during which the options or warrants may be exercised and the relationship between the current market price of the underlying instrument and the option's or warrant's contractual strike or exercise price also affects the level of market risk. A significant factor influencing the overall level of market risk to which the Company is exposed is its use of hedging techniques to mitigate such risk. The Company manages market risk by setting risk limits and monitoring the effectiveness of its hedging policies and strategies.

(b) Credit Risk

The Company acts as a dealer of securities in the global capital markets and, consequently, has credit risk for the timely repayment of principal and interest regarding its holdings of securities. Credit risk is measured by the loss the Company would record if its counterparties failed to perform pursuant to the terms of their contractual obligations and the value of collateral held, if any, was not adequate to cover such losses. Specifically, the Company's potential credit loss exposure for contractual commitments is equal to the market or fair value of contractual commitments that are in a net asset position less the effect of master netting agreements. The Company has established controls to monitor the creditworthiness of counterparties, as well as the quality of pledged collateral, and uses master netting agreements whenever possible to mitigate the Company's exposure to counterparty credit risk. The Company may require counterparties to submit additional collateral when deemed necessary. The Company also enters into collateralized financing agreements in which it extends short-term credit, primarily to major financial institutions. The Company controls the collateral pledged by the counterparties, which consists largely of securities issued by the U.S. government or its agencies.

The notional amounts of contractual commitments do not represent exposure to credit risk. Credit risk associated with futures contracts is limited since all transactions are guaranteed by the exchange on which they are traded and daily cash settlements by all counterparties are required for changes in the market value of open contracts. The Company's purchased exchange issued options also possess low credit risk due to guarantee of performance by the issuing exchange. Negotiated contractual commitments, such as forwards, and certain OTC options possess greater exposure to credit risk since cash settlement is not normally required on a daily basis, and therefore, counterparty credit quality and the value of pledged collateral are essential elements in controlling the Company's risk.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

Concentrations of credit risk from financial instruments, including contractual commitments, exist when groups of issuers or counterparties have similar business characteristics or are engaged in like activities that would cause their ability to meet their contractual commitments to be adversely affected, in a similar manner, by changes in the economy or other market conditions. As a financial intermediary, the Company regularly transacts business with, and owns securities issued by, a broad range of governments, corporations, international organizations, central banks, and other financial institutions, which are economically and geographically diverse. The Company monitors credit risk on both an individual and group counterparty basis. The Company minimizes this risk through credit reviews, approvals, trading limits, and monitoring procedures.

(c) Operational and Support Risk

As a major intermediary in financial markets, the Company is directly exposed to market risk and credit risk which arise in the normal course of its business activities. Less direct, but of critical importance, are risks pertaining to operational and back-office support. This is particularly the case in a rapidly changing and increasingly global environment with increasing transaction volumes and an expansion in the number and complexity of products in the marketplace. Such risks include the following:

- i. Operational/settlement risk – the risk of financial and opportunity loss and legal liability attributable to operational problems such as inaccurate pricing of transactions, untimely trade execution, clearance and/or settlement, or the inability to process large volumes of transactions. The Company is subject to increased risks with respect to its trading activities in emerging markets securities, where clearance, settlement, and custodial activities continue to develop.
- ii. Technological risk – the risk of loss attributable to technological limitations or hardware failure that constrain the Company’s ability to gather, process, and communicate information efficiently and securely, without interruption, with customers, and in the markets where the Company participates. In addition, the Company must address the technological implications that will result from regulatory and market changes.
- iii. Legal/documentation risk – the risk of loss attributable to deficiencies in the documentation of transactions (such as trade confirmations) and customer relationships (such as master netting agreements) or errors that result in noncompliance with applicable legal and regulatory requirements.
- iv. Financial control risk – the risk of loss attributable to limitations in financial systems and controls; strong financial systems and controls ensure that assets are safeguarded, that transactions are executed in accordance with management’s authorization, and that financial information utilized by management and communicated to external parties, creditors, and regulators is free of material errors.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

(10) Commitments and Contingencies

(a) Commitments

Underwriting Commitments – in the normal course of business, the Company enters into underwriting commitments. Transactions relating to such underwriting commitments that were open at December 31, 2010, and were subsequently settled did not have a material effect on the consolidated statement of financial condition as of that date.

Letters of Credit – the Company has an uncommitted facility with external banks permitting borrowing on an unsecured and secured basis for up to \$1.2 billion. As of December 31, 2010, \$789.0 million of this facility was utilized for letters of credit posted as margin to clearing organizations on an unsecured basis.

Forward Secured Financings – the Company had commitments to enter into forward secured financing transactions, including certain repurchase and reverse repurchase agreements and secured borrowing and lending arrangements of \$22.8 billion as of December 31, 2010.

Leases – the Company has entered into various noncancelable lease agreements for premises and equipment that expire through 2018. Certain agreements are subject to periodic escalation provisions for increases in real estate taxes and other charges. Future minimum rental commitments under noncancelable leases with initial or remaining terms exceeding one year as of December 31, 2010 are presented below (in thousands):

Year ending:		
2011	\$	20,896
2012		8,511
2013		7,781
2014		7,192
2015		2,795
2016 and thereafter		10,429
Total	\$	<u>57,604</u>

The minimum rental commitments shown above have not been reduced by approximately \$3.0 million of minimum sublease rentals to be received in the future under noncancelable subleases.

Other Commitments – commitments to invest and other compensation related commitments of the Company totaled approximately \$209.8 million as of December 31, 2010.

(b) Contingencies

The Company, together with various other brokers and dealers, corporations, and individuals, has been named as a defendant in various legal actions, including arbitrations, class actions, and other litigation arising in connection with the conduct of its business activities that allege violations of federal and state securities laws and claim substantial damages.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

In accordance with ASC 450-20 (Loss Contingencies), the Company will accrue a liability when it is probable that a liability has been incurred and the amount of the loss can be reasonably estimated. In many lawsuits and arbitrations, it is not possible to determine whether a liability has been incurred or to estimate the ultimate or minimum amount of that liability until the case is close to resolution, in which case no accrual is made until that time. In view of the inherent difficulty of predicting the outcome of such matters, particularly in cases in which claimants seek substantial or indeterminate damages, the Company cannot predict what the eventual loss or range of loss related to such matters will be. Subject to the foregoing, the Company continues to assess these cases and believes, based on information available to it, that the resolution of these matters will not have a material adverse effect on the financial condition of the Company. The actions against the Company include but are not limited to the following:

IPO Allocation Litigation

The Company and its predecessor firms, along with numerous other securities firms, have been named as defendants in over 80 putative class action lawsuits pending in the United States District Court for the Southern District of New York. These lawsuits allege violations of securities and antitrust laws in connection with the allocation of shares in a large number of initial public offerings (IPOs) by issuers, officers and directors of issuers, and underwriters of those securities. The Company is named in these suits as an underwriter. The securities cases allege material misstatements and omissions in registration statements and prospectuses for the IPOs and market manipulation with respect to aftermarket trading in the IPO securities. A related putative antitrust class action was finally dismissed in 2007. Among the allegations in the securities cases are that the underwriters tied the receipt of allocations of IPO shares to required aftermarket purchases by customers and to the payment of undisclosed compensation to the underwriters in the form of commissions on securities trades, and that the underwriters caused misleading analyst reports to be issued. In the securities cases, the motions to dismiss the complaints of the Company and others were denied on February 13, 2003. Plaintiffs' motion to certify six "test" cases as class actions in the securities cases was granted on October 13, 2004. On December 5, 2006, the U.S. Court of Appeals for the Second Circuit vacated the decision and held that the classes in the six cases, as defined, could not be certified. On March 26, 2008, the trial court granted in part and denied in part motions to dismiss plaintiffs' amended complaints. The extent to which the court granted the motions did not affect any cases in which the Company is a defendant. Following a mediation, a settlement was reached and approved by the trial court on October 6, 2009. On October 23, 2009, an objector filed a Rule 23(f) petition with the Second Circuit, seeking leave to appeal the trial court's certification of the settlement class in connection with all 310 cases, including the cases in which the Company was named as a defendant. The plaintiffs objected, and all the underwriter defendants responded to the petition on November 2, 2009. The petition was subsequently withdrawn and substituted with an appeal of the district court's order. The appeal is currently pending before the Second Circuit.

Tax-Related Litigation

The Bank, along with certain affiliates, including the Company, and current and/or former employees (collectively referred to as "Deutsche Bank"), have collectively been named as

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

defendants in a number of legal proceedings brought by customers in various tax-oriented transactions. Deutsche Bank provided financial products and services to these customers, who were advised by various accounting, legal and financial advisory professionals. The customers claimed tax benefits as a result of these transactions, and the United States Internal Revenue Service has rejected those claims. In these legal proceedings, the customers allege that the professional advisors, together with Deutsche Bank, improperly misled the customers into believing that the claimed tax benefits would be upheld by the Internal Revenue Service. The legal proceedings are pending in numerous state and federal courts and in arbitration, and claims against Deutsche Bank are alleged under both U.S. state and federal law. Many of the claims against Deutsche Bank are asserted by individual customers, while others are asserted on behalf of a putative customer class. No litigation class has been certified as against Deutsche Bank. Approximately 99 legal proceedings have been resolved and dismissed with prejudice with respect to Deutsche Bank. Approximately six other legal proceedings remain pending as against Deutsche Bank and are currently at various pre-trial stages, including discovery. Deutsche Bank has received a number of unfiled claims as well, and has resolved certain of those unfiled claims. Approximately five unfiled claims also remain pending against Deutsche Bank. Deutsche Bank does not expect these pending legal proceedings and unfiled claims to have a significant effect on its consolidated statement of financial condition.

The United States Department of Justice (DOJ) has been conducting a criminal investigation of Deutsche Bank's participation in tax-oriented transactions that were executed from approximately 1996 through early 2002. On December 21, 2010, Deutsche Bank resolved this investigation, entering into a non-prosecution agreement with the DOJ and a closing agreement with the Internal Revenue Service, pursuant to which Deutsche Bank paid \$553.6 million to the United States government and, among other things, agreed to retain an independent expert to evaluate the implementation and effectiveness of various compliance measures that Deutsche Bank has implemented.

Adelphia Communications Corporation

The Bank and certain of its affiliates, including the Company, were among numerous financial institutions and other entities named as defendants in two adversary proceedings commenced in 2003 by a creditors committee and an equity committee of Adelphia Communications Corporation. In October 2007, the Adelphia Recovery Trust filed an amended complaint consolidating the two adversary proceedings, which was amended again in February 2008. The consolidated suit named more than 700 defendants and sought to avoid and recover certain loan payments, including approximately \$50 million paid to the Company in connection with margin loans, and sought affirmative damages from all defendants collectively based on common law tort claims. The bank defendants filed several motions to dismiss the consolidated complaint, which were granted in part and denied in part. The claims that remained pending in the district court against the Company included common law tort claims and an avoidance claim relating to the margin loans. In October 2010, a settlement was reached in which all but one of the bank defendants resolved all outstanding claims against them in the adversary proceeding in exchange for a total payment of \$175 million by those bank defendants collectively. The settlement has been approved by the court, and the matter has been dismissed with prejudice as against the settling defendants, including the Company. In

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

addition to the lawsuit brought by the Adelpia Recovery Trust, the Company was one of the underwriters named in several actions brought by investors alleging federal securities law violations and common law claims. Those cases have largely been resolved by settlement or dismissal upon the defendants' motions. An amended complaint was filed in one case that was previously disposed of on a motion to dismiss. The Company filed a motion to dismiss the amended complaint as to some plaintiffs in that case. That motion is fully briefed and remains pending.

Asset Backed Securities Matters

The Bank and its affiliates, including the Company (collectively referred to as Deutsche Bank), have received subpoenas and requests for information from certain regulators and government entities concerning its activities regarding the origination, purchase, securitization, sale and trading of asset backed securities, asset backed commercial paper and credit derivatives, including, among others, residential mortgage backed securities, collateralized debt obligations and credit default swaps. Deutsche Bank is cooperating fully in response to those subpoenas and requests for information. Deutsche Bank has also been named as defendant in various civil litigations (including putative class actions), brought under federal and state securities laws and state common law, related to residential mortgage backed securities. Included in those litigations are (1) a putative class action pending in California Superior Court in Los Angeles County regarding the role of the Company, along with other financial institutions, as an underwriter of offerings of certain securities issued by Countrywide Financial Corporation or an affiliate (Countrywide), as to which there is a settlement agreement that has been preliminarily but not yet finally approved by the Court, and a putative class action pending in the United States District Court for the Central District of California regarding the role of the Company, along with other financial institutions, as an underwriter of offerings of certain mortgage pass-through certificates issued by Countrywide; (2) a putative class action pending in the United States District Court for the Southern District of New York regarding the role of the Company, along with other financial institutions, as an underwriter of offerings of certain mortgage pass-through certificates issued by affiliates of Novastar Mortgage Funding Corporation; (3) a putative class action pending in the United States District Court for the Southern District of New York regarding the role of the Company, along with other financial institutions, as an underwriter of offerings of certain mortgage pass-through certificates issued by affiliates of IndyMac MBS, Inc.; (4) a putative class action pending in the United States District Court for the Northern District of California regarding the role of the Company, along with other financial institutions, as an underwriter of offerings of certain mortgage pass-through certificates issued by affiliates of Wells Fargo Asset Securities Corporation; and (5) a putative class action in the United States District Court for the Southern District of New York regarding the role of a number of financial institutions, including the Company, as underwriter, of certain mortgage pass-through certificates issued by affiliates of Residential Accredited Loans, Inc., which the Company was dismissed from on March 31, 2010 and then reinstated as a defendant on December 21, 2010; (6) a lawsuit filed by the Federal Home Loan Bank of San Francisco (FHLB SF) pending in the San Francisco Superior Court regarding the role of a number of financial institutions, including certain affiliates of Deutsche Bank as issuer and the Company as underwriter of certain mortgage pass-through certificates purchased by FHLB SF; (7) a lawsuit filed by the Federal Home Loan Bank of Seattle (FHLB Seattle) pending in the Washington

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

Superior Court regarding the role of certain affiliates of Deutsche Bank as issuer and the Company as underwriter of a mortgage pass-through certificate purchased by FHLB Seattle; and (8) a lawsuit filed by Cambridge Place Investments Management Inc. (Cambridge) pending in the Massachusetts Superior Court regarding the role of a number of financial institutions, including certain affiliates of Deutsche Bank as issuer and the Company as underwriter of certain mortgage pass-through certificates purchased by Cambridge. In addition, the Company has been named as a defendant in an action filed by Assured Guaranty Municipal Corp. pending in California Superior Court regarding the Company's role as underwriter of certain mortgage pass-through certificates issued by affiliates of IndyMac MBS, Inc. Also, certain affiliates of Deutsche Bank, including the Company, have been named in a putative class action pending in the United States District Court for the Eastern District of New York regarding their roles as issuer and underwriter of certain mortgage pass-through securities. Each of the civil litigations is in its early stages.

Auction Rate Securities

The Bank and the Company are the subjects of a putative class action, filed in the United States District Court for the Southern District of New York, asserting various claims under the federal securities laws on behalf of all persons or entities who purchased and continue to hold auction rate preferred securities and auction rate securities (together ARS) offered for sale by the Bank and the Company between March 17, 2003 and February 13, 2008. On December 9, 2010, the court dismissed the putative class action with prejudice. Plaintiff has filed a notice of appeal of the dismissal. The Bank and the Company, including a division of the Company, have also been named as defendants in 17 individual actions asserting various claims under the federal securities laws and state common law arising out of the sale of ARS. Ten of the individual actions are pending, and seven of the individual actions have been resolved and dismissed with prejudice.

The Bank and the Company have also been the subjects of proceedings by state and federal securities regulatory and enforcement agencies relating to the marketing and sale of ARS. In August 2008, the Bank and its subsidiaries, entered into agreements in principle with the New York Attorney General's Office (NYAG) and the North American Securities Administration Association (NASAA), representing a consortium of other states and U.S. territories, pursuant to which the Bank and its subsidiaries agreed to purchase from their retail, certain smaller and medium-sized institutional, and charitable clients, ARS that those clients purchased from the Bank and its subsidiaries prior to February 13, 2008; to work expeditiously to provide liquidity solutions for their larger institutional clients who purchased ARS from the Bank and its subsidiaries; to pay an aggregate penalty of \$15 million to state regulators; and to be subject to state orders requiring future compliance with applicable state laws. On June 3, 2009, the Company finalized settlements with the NYAG and the New Jersey Bureau of Securities that were consistent with the August 2008 agreements in principle, and the Company entered into a settlement with the SEC that incorporated the terms of the agreements in principle with the states. The Company has since received proposed settled orders from a number of state and territorial agencies pursuant to which those agencies have claimed their respective shares of the \$15 million penalty. The Company expects to finalize those settled orders and pay the requisite shares of the penalty to the requesting states over the next several months.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

Trust Preferred Securities

The Bank and certain of its affiliates and officers, including the Company, are the subject of a consolidated putative class action, filed in the United States District Court for the Southern District of New York, asserting claims under the federal securities laws on behalf of persons who purchased certain trust preferred securities issued by Deutsche Bank and its affiliates between October 2006 and May 2008. Claims are asserted under sections 11, 12(a)(2), and 15 of the Securities Act of 1933. An amended and consolidated class action complaint was filed on January 25, 2010. There is a motion to dismiss pending.

Short-Selling Litigations

The Company has been named as a defendant in various civil litigations asserting claims relating to short selling. These litigations include: (i) a lawsuit pending in California state court by alleged shareholders of Novastar Financial, Inc. (Novastar) against the Company and other financial institutions alleging that the defendants have manipulated the price of Novastar securities in connection with short sale transactions; (ii) a lawsuit pending in the United States District Court for the Northern District of Georgia, Atlanta Division, by TASER International, Inc. (TASER) and alleged TASER shareholders against the Company and other financial institutions alleging that the defendants have manipulated the price of TASER securities in connection with short sale transactions; and (iii) a lawsuit which was pending in California state court as of December 31, 2010 by Signalife, Inc., also known as Hearttronics, Inc. or Heart Tronics, Inc. (Signalife), against the Company and other financial institutions alleging that the defendants have manipulated the price of Signalife securities in connection with short sale transactions. The Novastar litigation is in the discovery stage. The Company and the plaintiffs in the TASER litigation have agreed to a confidential settlement of that litigation pursuant to which the case will be dismissed with prejudice as against the Company. The plaintiffs in the Signalife litigation filed a request for voluntarily dismissal without prejudice as against the Company on or about January 10, 2011. In addition, on or about December 29, 2010, a lawsuit which was pending in California state court by Overstock.com, Inc. (Overstock.com) and alleged Overstock.com shareholders against the Company and other financial institutions alleging that the defendants have manipulated the price of Overstock.com securities in connection with short sale transactions was dismissed with prejudice as against the Company pursuant to a confidential settlement.

Aravali

The Company has been named as a respondent in twenty arbitrations seeking damages allegedly sustained from investments in the Aravali Fund (Aravali), a third-party hedge fund sold by the Company to retail clients. Aravali used a high degree of leverage in investing in municipal bonds to generate return and income, leverage that led to the collapse of the fund when the municipal bond market suffered a decline in the fall of 2008. Ten of the arbitrations are pending, and ten of the arbitrations have been resolved and dismissed with prejudice.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

Themis

The Company has been named as a respondent in fifteen arbitrations seeking damages for losses sustained through a put spread options investment strategy directed by an independent registered investment advisor, Themis Asset Strategies LLC (Themis), whose principal Derek Clark was a client advisor at the Company from 2002-2005. Claimants include direct clients of Themis, for whom the Company performed execution and custody services; customers of the Company, who participated in the trading program through the Company's referral program; and a non-customer whose trades were executed through the Company's options desk and delivered to another firm. The put spread options strategy experienced a severe decline during the market turmoil of October 2008, and the Company discontinued its referral arrangement with Themis in November 2008. Ten of the arbitrations are pending and four have been resolved and dismissed with prejudice.

M&T Bank

The Company is a defendant in an action brought by M&T Bank (M&T) in New York State Supreme Court. The suit seeks compensatory and punitive damages in connection with M&T Bank's March 2007 purchase of approximately \$82 million in notes issued by Gemstone VII CDO, which was collateralized by subprime residential mortgage-backed securities. M&T alleges that the Company misrepresented and did not disclose the impairment of the underlying collateral for the Gemstone VII CDO; that the Company's level of due diligence in the selection and monitoring of the underlying collateral was deficient; and that the Company withheld from the rating agencies information regarding the deteriorating quality of the collateral. M&T asserted numerous causes of action under New York state law, including among others, fraud, negligent misrepresentation, rescission, breach of contract, and violations of New York's consumer protection statute. All claims against the Company, except for the fraud and rescission claims, have been dismissed. The Company and M&T are currently engaged in discovery.

(11) Obligations under Guarantees

The Company has obligations under certain guarantee arrangements, including contracts and indemnification agreements that contingently require a guarantor to make payments to the guaranteed party based on changes in an underlying measure (such as an interest or foreign exchange rate, security or commodity price, an index or the occurrence or nonoccurrence of a specified event) related to an asset, liability or equity security of a guaranteed party. Also included as guarantees are contracts that contingently require the guarantor to make payments to the guaranteed party based on another entity's failure to perform under an agreement, as well as indirect guarantees of the indebtedness of others.

The Company enters into certain derivative contracts that meet the accounting definition of a guarantee under ASC 460 (Guarantees). Such derivative contracts include certain written options, contingent forward contracts and credit default swaps. Although the Company's derivative arrangements do not specifically identify whether the derivative counterparty retains the underlying asset, liability or equity security, the Company has disclosed information regarding all derivative contracts that could meet the accounting definition of a guarantee. In order to provide information regarding the maximum potential

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

amount of future payments that the Company could be required to make under certain derivative contracts, the notional amount of the contracts has been disclosed.

The Company records all derivative contracts at fair value. Aggregate market risk limits have been established, and market risk measures are routinely monitored against these limits. The Company also manages its exposure to these derivative contracts through a variety of risk mitigation strategies, including, but not limited to, entering into offsetting economic hedge positions. The Company believes that the notional amounts of the derivative contracts generally overstate its exposure.

The Company also provides guarantees to securities clearinghouses and exchanges. Under the standard membership agreement, members are required to guarantee the performance of other members. Under the agreements, if another member becomes unable to satisfy its obligations to the clearinghouse, other members would be required to meet shortfalls. The Company's liability under these arrangements is not quantifiable and could exceed the cash and securities it has posted as collateral. However, the potential for the Company to be required to make payments under these arrangements is remote. Accordingly, no contingent liability is carried on the consolidated statement of financial condition for these transactions.

In connection with its prime brokerage business, the Company provides to counterparties guarantees of the performance of its prime brokerage clients. Under these arrangements, the Company stands ready to meet the obligations of its customers with respect to securities transactions. If the customer fails to fulfill its obligation, the Company must fulfill the customer's obligation with the counterparty. The Company is secured by assets in the customer's account as well as any proceeds received from the securities transaction entered into by the Company on behalf of the customer. No contingent liability is carried on the consolidated statement of financial condition as the Company believes that potential for loss under these arrangements is remote.

In connection with its securities clearing business, the Company performs securities execution, clearance and settlement services on behalf of other broker-dealer clients for whom it commits to settle, with the applicable clearinghouse, trades submitted for or by such clients; trades are submitted either individually, in groups or series or, if specific arrangements are made with a particular clearinghouse and client, all transactions with such clearing entity by such client. The Company's liability under these arrangements is not quantifiable and could exceed any cash deposit made by a client. However, the potential for the Company to be required to make unreimbursed payments under these arrangements is remote due to the contractual requirements associated with clients' activity and the regular review of clients' capital. Accordingly, no contingent liability is carried on the consolidated statement of financial condition for these transactions.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

The table below summarizes certain information regarding the Company's derivative contracts that meet the definition of a guarantee and certain other guarantees as of December 31, 2010 (in millions):

Type of guarantee	Maximum potential payout/ notional years to maturity				Carrying amount (asset/ liability)	Collateral/ recourse
	Less than 1	1 – 5	Over 5	Total		
Notional amount of derivative contracts	\$ —	679	12,338	13,017	(6,008)	—
Standby letters of credit	1,200	—	—	1,200	(792)	—

(12) Retirement Plans

(a) Defined Benefit Pension Plan

Along with other affiliates of Deutsche Bank Americas Holding Corp. (DBAH), the Company participates in the DBAH Cash Account Pension Plan. The plan is a tax-qualified, noncontributory defined benefit cash account pension plan that covers substantially all employees who have completed one full year of service and were hired on or before December 31, 2004. An employee's pension account is credited each year with 6.5% of base pay plus bonus amounts up to 75% of base pay up to IRS limits. Accounts are also credited each year with an interest credit equivalent to the annual rate of interest of 30-year U.S. Treasury securities. The funding policy has been to contribute at least the amount required to satisfy the Employee Retirement Income Security Act of 1974 minimum funding requirements.

The plan was closed to new participants effective December 31, 2004.

(b) Postretirement Welfare Plan

The Company participates, together with other affiliates of DBAH, in an unfunded contributory postretirement health care plan. The plan pays stated percentages of most necessary medical expenses of retirees after a stated deductible has been met.

(c) Defined Contribution Plan – Matched Savings Plan

The Company participates, together with other affiliates of DBAH in a tax-qualified 401(k) plan. Employees are able to contribute from 1% to 20% of their eligible compensation on a before-tax or after-tax basis, up to IRS limits. For employees hired before January 1, 2005, after a participant has completed six months of service, the Company matches dollar for dollar up to 5% of eligible compensation, up to a maximum of \$4,000 per year.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

Effective January 1, 2005, the plan was amended for employees hired on or after January 1, 2005. Participants who have completed six months of service receive a matching contribution from the Company of up to 4% of eligible compensation. In addition, participants employed less than ten years receive a Company fixed contribution equal to 4% of the first \$100,000 of eligible compensation. Participants employed ten or more years receive a Company fixed contribution equal to 6% of the first \$100,000 of eligible compensation.

(d) *Share-Based Compensation Plans*

The Company participates in various share-based compensation plans of the Bank, including the DB Share Scheme and the Restricted Equity Units Plan where the Bank grants employees of the Company deferred share awards which provide the right to receive common shares of the Bank at specified future dates. The vesting period of the awards is generally from one to five years. The Bank discontinued the Global Share Plan in 2010.

The Bank adopted the guidance in ASC 718 effective January 1, 2006. For transition purposes, the Bank elected the modified prospective application method. Under this application method, ASC 718 applies to new awards and to awards modified, repurchased, or canceled after the required effective date. Awards are expensed on a straight-line basis over the vesting period, which is generally from three to five years.

The Bank enters into certain derivative contracts indexed to its common shares in order to hedge the overall cost associated with employee share-based compensation awards. For the year ended December 31, 2010, the Company was allocated approximately \$19.0 million related to its portion of the overall gain realized by the Bank that was attributable to share-based awards granted to the Company's employees. This amount has been reflected as an adjustment to the Company's additional paid-in capital.

(e) *Cash Retention Plan*

The Company participates in cash retention plans of the Bank, including the DB Restricted Cash Plan and the DB Restricted Incentive Plan. As a rule of the DB Restricted Cash Plan the awards are only paid out to the employee if there is a non-terminated employment relationship between the employee and Deutsche Bank at the respective vesting date. The award consists of three tranches each amounting to one third of the original grant volume. The first tranche vested in early 2010 and was paid out, net of any forfeiture during the course of 2009 according to the terms and conditions of the plan. The two remaining tranches vest in early 2011 and early 2012, respectively. Each tranche is expensed over its vesting period.

The DB Restricted Incentive Plan consists of three tranches each amounting to one third of the grant volume. The tranches vest in early 2011, 2012 and 2013. Each tranche is expensed over its vesting period. In line with regulatory requirements this plan includes performance-indexed clawback rules for the most senior employees. Thus, there is the possibility that parts of the awards will be subject to forfeiture in the event of non-achievement of defined targets, breach of policy or financial impairment.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

(13) Income Taxes

Significant components of the Company's deferred tax assets and liabilities as of December 31, 2010 were as follows (in thousands):

Deferred tax assets:	
Deferred compensation	\$ 716,545
State and local tax net operating losses	1,635
Deferred book gain	177,559
Capital loss carryforward	12,145
Depreciation	62,343
Litigation and other reserves	42,148
Pension and post retirement benefits	22,398
Other	225,337
	<hr/>
Gross deferred tax assets	1,260,110
Valuation allowance	(17,116)
	<hr/>
Deferred tax assets, net of valuation allowance	1,242,994
	<hr/>
Deferred tax liabilities:	
Other	(95,650)
	<hr/>
Gross deferred tax liabilities	(95,650)
	<hr/>
Net deferred tax assets	\$ 1,147,344
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The Company believes it is more likely than not that the results of future operations will generate sufficient taxable income to realize the net deferred tax assets. The realization of the Company's net deferred tax assets are also impacted by the Bank's various strategic initiatives.

In accordance with ASC 740, a reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

Balance at January 1, 2010	\$ 63,350
Additions based on tax positions related to the current year	
Additions for tax positions of prior years	144,997
Reductions for tax positions of prior years	(4,287)
Settlements	—
	<hr/>
Balance at December 31, 2010	\$ 204,060
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The effect of the unrecognized tax benefits of \$204.0 million, if recognized, would impact the effective tax rate of the Company.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

The Company and its subsidiaries remain subject to income tax examinations in certain U.S. state and local jurisdictions for years after 2001, and the U.S. federal jurisdiction, for years after 2003.

Pursuant to ASC 718, excess tax benefits are recognized as additional paid-in capital in the period the benefit is realized. The write-off of a deferred tax asset related to a tax deficiency is first offset against any existing additional paid-in capital that resulted from previously realized excess tax benefits from previous awards accounted for in accordance with ASC 718. During 2010, a tax shortfall of \$18.4 million occurred, which was the result of the tax deduction being less than the cumulative book compensation cost. This is reflected as a decrease in stockholder's equity and the Company's pool of tax benefits (APIC pool).

(14) Subordinated Liabilities

The Company has an \$8.0 billion revolving note and cash subordination agreement with Deutsche Bank Trust Corp., an affiliated entity. The agreement has a maturity date of November 15, 2011 and at December 31, 2010, approximately \$6.7 billion of the facility was outstanding, all of which is approved by FINRA and qualifies as regulatory capital for the purpose of computing net capital under the Uniform Net Capital Rule of the SEC. To the extent that the outstanding subordinated liabilities are required for the Company's continued compliance with its regulatory net capital requirements, the subordinated liabilities may not be repaid.

The Company's subordinated revolving note and cash subordination agreement requires the payment of interest at floating rates based on the London Interbank Offered Rate plus 30 basis points. At December 31, 2010, the interest rate on this facility was .56%. The Company must obtain the approval of FINRA prior to any additional subordinated borrowings or repayments.

(15) Regulatory Requirements

The Company is subject to the SEC's Uniform Net Capital Rule (15c3-1), which requires the maintenance of minimum net capital.

The Company has elected to use the alternative method, permitted by the Rule, which requires that it maintain minimum net capital, as defined, equal to the greater of \$1.5 million, 2% of aggregate debit balances arising from customer transactions, as defined, or the CFTC minimum net capital requirement, as defined. Additionally, equity capital may not be withdrawn or cash dividends paid if resulting net capital would be less than 5% of aggregate debits. As of December 31, 2010, the Company had net capital of approximately \$6.0 billion, which was 95.86% of aggregate debit balances, and approximately \$5.4 billion in excess of required minimum net capital.

As a clearing broker and in accordance with SEC Rule 15c3-3, the Company computed a reserve requirement for the proprietary accounts of introducing broker-dealers (PAIB). As of December 31, 2010, securities aggregating \$1.4 million were segregated on behalf of introducing broker-dealers.

DEUTSCHE BANK SECURITIES INC.

(A Wholly Owned Subsidiary of
Deutsche Bank AG)

Notes to Consolidated Statement of Financial Condition

December 31, 2010

The Company is also subject to the SEC's Customer Protection Rule (15c3-3) which requires, under certain circumstances, that cash or securities be deposited into a special reserve bank account for the exclusive benefit of customers. As of December 31, 2010, the Company had \$3.9 billion of cash and \$2.1 billion of U.S. Government securities segregated in the special reserve bank account.

The Company, in accordance with the Commodity Exchange Act, is required to segregate and hold in separate accounts all monies, securities, and property received to margin and to guaranty or secure the trades or contracts of customers in regulated commodities. As of December 31, 2010, segregated funds exceeded such requirement by \$401.8 million. In addition, pursuant to Regulation 30.7 of the CFTC, the Company had secured funds held in separate accounts for foreign denominated positions that exceeded such requirements by \$201.2 million.