UNITED STATES SECURITIES AND EXCHANGE COMMISSION
DIVISION OF ENFORCEMENT

--X

:

In the Matter of : File No. NY-7999

:

THE RESERVE FUND :

:

--X

WELLS SUBMISSION ON BEHALF OF BRUCE R. BENT, SR. AND BRUCE R. BENT II

WILMER CUTLER PICKERING
HALE AND DORR LLP
Robert B. McCaw
Lori A. Martin
Susan Schroeder
399 Park Avenue
New York, New York 10022
(212) 230-8800

James E. Anderson
Sarah Stafford
1875 Pennsylvania Avenue, NW
Washington, DC 20006
(202) 663-6000

Attorneys for Bruce R. Bent Sr. and Bruce R. Bent II

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

TABLE OF CONTENTS

Page

INTRODUCTION AND EXECUTIVE SUMMARY OF ARGUMENT 1

BACKGROUND 5

A. RMCI Background 5

B. RMCI Investments in Lehman 8

C. Deepening Liquidity Crisis and The Lehman Bankruptcy 13

D. Board Notification of Lehman Developments 15

E. The Bents' Efforts to Protect Investor Assets on September 15-16, 2008 17

F. The Money Fund Crisis Continues 19

ARGUMENT 21

I. The Bents' Statements to the Board Were Truthful and Complete 21

A. The Bents' Representations to the Board regarding Lehman Trading Activity and the Impact of Lehman Valuation on the Primary Fund and Yield Plus Fund Were Truthful 22

1. The Bents' Representations Relating to the Impact of Lehman Valuations on the NAV of the Primary Fund and the Yield Plus Fund 23

2. Disclosures Relating to Lehman Market Activity 26

B. The Bents' Representations to the Board Regarding Their Intentions to Support the NAV of the Primary Fund Were Truthful When Made 29

1. The Bents' Limited Understanding of Credit Support Agreements Shaped Their Expectations About the Arrangement for the Primary Fund 29

2. The Bents Did Not Have Detailed Information About the Terms of a Credit Support Agreement for the Primary Fund when They Met with the Board at 1:00 P.M. and, for that Reason, Did Not Conceal Material Terms of the Agreement from the Board 31

3. Bruce Sr.'s Statement That Sufficient Capital Could Be Made Available Was Truthful when Made, Did Not Deceive the Board, and Did Not Result in Any Different Action by the Board than It Would Otherwise Have Taken 34

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000247

4. Investment Advisers Are Not Legally Obliged to Support the NAV of Money Market Funds 37

C. The Bents Promptly Informed the Trustees That the Fund Had Overdrafts at State Street Bank 40

D. The Bents Were Under No Legal Obligation to Inform the Board That a Moody's Analyst Recommended That RMCI Create a Credit Support Agreement in the Event of a Credit Event 43

E. The Bents Had No Obligation to Disclose RMCI's Communications with the Rating Agencies to the Board 45

F. The Bents Were Under No Obligation to Disclose to the Board the Preliminary Discussions They Had with an Investment Banker Regarding a Possible Sale of the Adviser 46

II. RMCI Statements to the Public About the Bents' Intentions to Support the Primary Fund Were Not Fraudulent as They Were Accurate Statements of the Family's Intentions 47

A. Ledford's Unauthorized Statements to the Rating Agencies Did Not Deceive Those Agencies and Did Not Affect the Ratings for the Primary Fund 48

B. Bruce II's Expression of Commitment to the $1.00 NAV for the Primary Fund to Key Employees Was an Accurate Statement of His Support for the Fund and Was Not Intended to Defraud Investors 50

C. The Bents Are Not Liable for the Content of the Reserve Insights Publication That was Publicized Without the Bents' Approval, but Nonetheless Prepared in Good Faith by RMCI Employees 52

1. Statements Regarding the Maturation of the Lehman Debt 54

2. Statements Regarding the Credit Support Agreement 55

3. The Bents' Consultation with Counsel Regarding the Content of the Descriptions of the Proposed Credit Support Agreement Undercuts the Staff's Proposed Inference of Fraud 57

4. The Bents Cannot Be Liable for Aiding and Abetting Alleged Omissions or Misstatements by RMCI and Its Personnel 59

D. By September 16, Information that RMCI Was Not Supporting the Primary Fund's NAV Was Immaterial 60

Confidential Treatment Requested by WILMER CUTLER PICKERING HALE AND DORR LLP

III. The Creation of Receivables for Two Variable NAV Funds Was Not Fraudulent Where the Assistant Comptroller Created Them in Error and Without the Bents' Authorization 63

A. Description of the Receivables 63

B. The Bents Did Not Authorize the Creation of the Receivables 64

C. Reversal of the Receivables 66

D. Corroborating Evidence Supports Management's View That the Receivables Were Unauthorized 67

1. RMCI Refused to Issue Public Statements That It Intended to Support the NAV for the Yield Plus Fund or the International Liquidity Fund 67

2. Bruce II's Written Communications Confirm His Understanding That He Did Not Have a Commitment to Support the NAVs for the Yield Plus and International Liquidity Funds 68

3. After Informing the Board that the Yield Plus Fund Would Break the Buck if Lehman Was Priced at 80% of Par, the Bents Did Not Request Board Approval to Support the Fund's NAV or Notify the SEC of Any Intention to Do So 69

4. Lentinello's Conduct Suggests that There Was No Agreement to Backstop the NAVs for the Yield Plus and International Liquidity Funds 69

5. There is No Credible Evidence that The Bents Were Prepared to Spend More to Support Their Variable NAV Products than They Were Prepared to Support Their Flagship Money Fund 70

IV. The Bents Are Not Personally Liable for Delays in Obtaining Relief Under Section 22(e) of the Investment Company Act 71

V. The Bents Are Not Personally Liable for Books and Records Violations 73

A. Because the Facts Here Do Not Resemble Other Cases Involving Supervisory Liability, It Would Be Inappropriate to Charge the Bents for Books and Records Violations 73

B. The Bents Do Not Have Supervisory Liability for the Accounting-Related Functions Performed by the Finance Department and by the Company's Fund Accountant, State Street Bank, to Calculate the NAVs for the Funds 76

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

C. Because the Receivables Booked by Lentinello on September 15 Were Not Authorized, the Bents Should Not Be Charged for These Errors 77

D. The Bents Should Not Be Charged for Publication of the Reserve Insights Article 78

E. The Bents Also Are Not Liable as Aiders or Abettors for Books and Records Violations 79

Conclusion 80

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

TABLE OF AUTHORITIES

Page

Federal Cases

Basic Inc. v. Levinson,
485 U.S. 224, 231-32 (1988) 45, 47, 61

Burks v. Lasker,
441 U.S. 471, 482 n.10 (1979) 37

Carlin Equities Corp. v. Offman,
No. 07-Civ-359(SHS), 2008 WL 4387328, at *10-*11 (S.D.N.Y. Sept. 24, 2008) 47

Castellano v. Young & Rubicam, Inc.,
257 F.3d 171, 182 (2d Cir. 2001) 47

Ernst & Ernst v. Hochfelder,
425 U.S. 185, 206 (1976) 35, 51

Generic Comment Letter, SEC No-Action Letter,
1992 SEC No-Act. LEXIS 1120 at *6 (Jan. 17, 1992) 39

Hershfang v. Knotter,
562 F. Supp. 393, 399 (E.D. Va. 1983) 43

Howard v. SEC,
376 F.3d 1136, 1147 (D.C. Cir. 2004) 35, 59, 63

In re Apple Computer Sec. Litig.,
886 F.2d 1109, 1115 (9th Cir. 1989) 62

In re Clearly Canadian Sec. Litig.,
875 F. Supp. 1410, 1419 (N.D. Cal. 1995) 62

In re Peritus Software Servs., Inc. Sec. Litig.,
52 F. Supp. 2d 211, 227 (D. Mass. 1999) 33

Investors Research Corp. v. SEC,
628 F.2d 168, 178 (D.C. Cir. 1980) 59

Jones Mem'l Trust v. Tsai Inv. Servs., Inc.,
367 F. Supp. 491, 497, 500 (S.D.N.Y. 1973) 37

Markowski v. SEC,
34 F.3d 99, 105 (2d Cir. 1994) 52, 63

Monetta Fin. Servs., Inc. v. S.E.C.,
390 F.3d 952, 956-57 (7th Cir. 2004) 48

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

Monsen v. Consolidated Dressed Beef Co.,
579 F. 2d 793, 804 (3d Cir. 1978) 56

Novak v. Kasaks,
216 F.3d 300, 309 (2d Cir. 2000) 33, 36

Olkey v. Hyperion
1999 Term Trust, Inc., 98 F.3d 2 (2d Cir. 1996) 37

Resnik v. Swartz,
303 F.3d 147 (2d. Cir 2002) 36

Santa Fe Indus., Inc. v. Green,
430 U.S. 462, 472 n.11 (1977) 37

SEC v. Capital Gains Research Bureau, Inc.,
375 U.S. 180, 191-92 (1963) 37

SEC v. KPMG LLP,
412 F. Supp. 2d 349, 375-76 (S.D.N.Y. 2006) 49, 56

SEC v. Moran,
922 F. Supp. 867, 895-96 (S.D.N.Y. 1996) 48

SEC v. Snyder,
No. 07-20455, 2008 WL 4218781, at *13 (5th Cir. Sept. 16, 2008) 59, 63

SEC v. Texas Gulf Sulphur Co.,
401 F.2d 833, 851 (2d Cir. 1968) 47

SEC v. Treadway,
430 F. Supp. 2d 293, 338 (2006) 37

SEC v. Wolfson,
539 F. 3d 1249, 1260 (10th Cir. 2008) 56

Strougo ex rel. Brazil Fund v. Scudder, Stevens & Clark, Inc.,
964 F. Supp. 783, 797 (S.D.N.Y. 1997) 37

Sundstrand Corp. v. Sun Chemical Corp.,
553 F.2d 1033, 1045 n.19 (7th Cir. 1977) 36

Transamerica Mortgage Advisors, Inc. v. Lewis,
444 U.S. 11, 17 (1979) 37

TSC Indus., Inc. v. Northway, Inc.,
426 U.S. 438, 449 (1976) 61

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

Vacold LLC v. Cerami,
No. 00 Civ. 4024 (AGS), 2002 WL 193157, at *8 (S.D.N.Y. Feb. 07, 2002) 47

Wright v. Ernst & Young LLP,
152 F.3d 169, 175 (2d Cir. 1998) 56

Federal Statutes

15 U.S.C. § 78o(b)(4)(E) 73

15 U.S.C. §§ 80b-1 to -21 48

15 U.S.C. §78t(a) 52

15 U.S.C.A. § 77o 56

15 U.S.C.A. § 78t 56

Section 206. 15 U.S.C. § 80b-6 48

State Statutes

ICA Section 203(e)(6) 74

Other Authorities

Alvin W Gebhart, Jr., Exchange Act Release No.
34-58951, 2008 WL 4936788 (Nov. 14, 2008) 35

Arthur James Huff, Exchange Act Release No.
34-29017, 50 S.E.C. 524, 1991 WL 296561, at *4 (Mar. 28, 1991) 74

Back Bay Advisors, L.P., Investment Advisers Act Release No.
2070, 2002 WL 32101982 (Oct. 25, 2002) 74, 79

CancerOption.com, Inc., Exchange Act Release No.
34-43246, 2000 WL 1280326, at *2 (Sept. 6, 2000) 79

Chris Woessner, Initial Decisions Release No.
225, 2003 SEC LEXIS 646 (Mar. 19, 2003) 59

David B. Gosse, Exchange Act Release No.
34-45474, 2002 WL 261959, at *1 (Feb. 25, 2002) 79

Dean Witter Reynolds, Inc., Initial Decisions Release No.
179, 2001 WL 47244 (Jan. 22, 2001) 76

Edwin J. Pittock, Investment Company Act Release No.
20448, 1994 SEC LEXIS 2419 (Aug. 8, 1994) 72

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000253

Fundamental Portfolio Advisors, Inc., Exchange Act Release No.
34-48177, 2003 WL 21658248 (July 15, 2003) 42

Jay Houston Meadows, Admin. Proc. File No.
3-8257, 1994 SEC 2874 at *42 (Sept. 19, 1994) 36

John Christopher McCamey, Initial Decisions Release No.
230, 2003 WL 21396458 (June 17, 2003) 79

John H. Gutfreund, Exchange Act Release No.
31554, 1992 WL 362753, at *15 (Dec. 3, 1992) 74

Judy M. Rupay, Investment Company Act Release No.
25960, 2003 SEC LEXIS 506 (Mar. 4, 2003) 72

Kevin Hall, Initial Decisions Release No.
341, 2008 SEC LEXIS 82, at *65 (Jan. 15, 2002) 36

Massachusetts Financial Services Co., Investment Company Act Release No.
26409, 2004 WL 635594 (Mar. 31, 2004) 42

Nicholas-Applegate Capital Mgmt., Investment Advisers Act Release No.
1741, 1998 WL 466733 (Aug. 12, 1998) 74

Piper Capital Mgmt., Inc., Initial Decisions Release No.
175, 2000 WL 1759455 (Nov. 30, 2000)
aff'd Investment Company Release Act, 2003 WL 22016298 (Aug. 26, 2003) 74, 75, 76

Reserve Fund, Investment Company Act Release No.
28386, 2008 WL 4468809 (Sept. 22, 2008) 72

Reserve Fund, Investment Company Act Release No.
28465, 2008 WL 4826002 (Oct. 24, 2008) 72

Reserve Municipal Money-Market Trust, Investment Company Act Release No.
28466, 2008 SEC LEXIS 2396, at *9 (Oct. 24, 2008) 71

Scudder Kemper Investments, Inc.,
Investment Advisers Act Release No. 1848 (Dec. 22, 1999) 74

Temporary Exemption for Liquidation of Certain Money Market Funds, Investment Company Act Rel. No.
28487, 2008 SEC LEXIS 2629, at *6 (Nov. 20, 2008) 38

Vilis Pasts, Exchange Act Release No.
34-39074, 1997 WL 566807 (Sept. 15, 1997) 73

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000254

This Memorandum is respectfully submitted on behalf of Bruce R. Bent, Sr. ("Bruce Sr.") and Bruce R. Bent II ("Bruce II") (together, the "Bents"), in response to the Wells notices received from the Staff of the Division of Enforcement. The Staff has indicated that it intends to seek authorization to file a complaint alleging fraud and various additional violations of the Investment Advisers Act of 1940 and the Investment Company Act of 1940 in response to the Bents' actions on September 15 and September 16, 2008, when they experienced an unprecedented run on a $64 billion dollar money market fund (the "Primary Fund" or "Fund") advised by their company, Reserve Management Company, Inc. ("RMCI").[1] The run on the Fund was triggered by the Chapter 11 filing of Lehman Brothers Holdings, Inc., a company whose commercial paper and medium term debt constituted 1.2% of the Fund and which had been rated as A1 paper by Moody's and P1 by Standard & Poor's ("S&P") at the time that RMCI purchased the securities, and which maintained 2a-7 eligible ratings until after the Lehman bankruptcy filing.

INTRODUCTION AND EXECUTIVE SUMMARY OF ARGUMENT

The Staff's view of the collapse of the Primary Fund is based upon its arm-chair second-guessing of RMCI communications with the Fund's Board, the public, and RMCI sales and marketing personnel in the midst of an unanticipated and severe worldwide financial crisis. Notwithstanding the fact that every written communication to the public and the RMCI sales

[1] As demonstrated by the discussion below, the Staff's conclusions evidence a premature rush to judgment. The Staff issued its Wells notice on December 17, 2008, while its requests to interview and/or depose key witnesses, including RMCI's General Counsel and Chief Financial Officer, were still outstanding. Indeed, since issuing its Wells notice, the Staff has requested additional testimony from Bruce II after already drawing conclusions about his conduct. Since issuing its Wells notice, the Staff has also requested additional testimony from at least one other witness, Rose DiMartino, outside counsel to RMCI and certain registered investment companies advised by RMCI. In addition, the Staff's investigation has not been even-handed. For example, during Bruce Sr.'s testimony, the Staff played limited selections of audio tapes and excluded from the record additional portions of the tapes that directly refuted the Staff's factual conclusions. Although the Staff agreed to include full transcripts of the tapes in the record of Bruce Sr.'s testimony after counsel lodged a complaint, we understand that the complete audio tapes and transcripts were not provided to all witnesses.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

force was provided to RMCI's General Counsel for approval, and that RMCI's written disclosure, which is the subject of many of the Staff's allegations, was shared with RMCI's outside counsel for comment, the Staff attributes deficiencies in the written communications to an intention to deceive investors. The Staff similarly attributes the free flowing oral discussions with the Board – in the midst of an unprecedented market crisis and in the face of constantly changing circumstances – to an intention to deceive the Board. The Staff has no explanation for why RMCI senior management would have any motive to withhold important information from the Fund's Board, or more importantly, whether any more perfect communications strategy – crafted, as the Staff thinks was possible, once the financial crisis has long passed – would have resulted in any different decision by the Board, RMCI or the investing public. On September 16, 2008 – approximately 36 hours after Lehman filed for bankruptcy – the Primary Fund ceased to trade at $1.00 per share due to the collapse of Lehman, illiquidity in the credit markets, and investor panic. Even with the luxury of the Staff's second-guessing, a more perfect communications strategy would not have altered this unfortunate outcome, thus making imperfections in RMCI's public communications – by definition – immaterial.

The specific deficiencies in the Staff's view of the evidence and the law are as follows:

1. No fraud charges should be brought against RMCI and the Bents in connection with Bruce Sr. and Bruce II's oral reports to the Primary Fund Board of Trustees on September 15 and 16. Their reports were accurate, truthful and – in the context of fast-moving market developments – timely. The Bents called for an emergency Board meeting at 8:00 a.m. on September 15 and informed the Board about the valuation levels for Lehman that would cause the Primary Fund and the Yield Plus Fund to trade at less than $1.00 per share. They accurately reported market activity in Lehman debt; both the lack of trades as well as market gossip, such as

indications of interest. At a time when the Fund's Lehman securities did not result in a decline in NAV, they sought preliminary consent from the Board to pursue a credit support agreement for the Fund. The Staff has challenged other miscellaneous disclosures to the Board. The tapes of the Board discussions – and the minutes of the meetings – amply demonstrate that the Bents' reports to the Board were fulsome and did not deceive the Trustees.

2. No fraud charges should be brought against RMCI or the Bents in connection with RMCI's statements that it was committed to a $1.00 per share NAV. The statements were prepared in good faith by RMCI employees, and reviewed by RMCI's in-house and outside counsel. They accurately reflected the Bents' intentions at the time the statements were made, including the significant sacrifices that the Bents were prepared to make on behalf of Fund investors. Moreover, Bruce II expressly asked the SEC Division of Investment Management whether RMCI could inform investors that it intended to enter into a credit support agreement, and the SEC Staff expressly stated that they would not object if RMCI made this disclosure.[2]

3. No fraud charges should be brought against the Bents as a result of the unauthorized creation of receivables for the Yield Plus Fund or the International Liquidity Fund. RMCI's Assistant Controller, David Lentinello, created the receivables in error, having been asked only to prepare financial spreadsheets that would track the amount of capital required to support the funds' NAVs in the event the Bents reached a decision to support the funds. The Bents never agreed to take this action, did not discuss the requisite review of those arrangements with the Staff of the Division of Investment Management, did not execute support agreements for the funds, and did not agree to commit more money to support their variable NAV funds than they were prepared to commit to their flagship money market fund. When pushed by the

[2] Deposition of Bruce II, dated Nov. 3, 2008, at 145:1-146:4.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

Marketing Department to state that they were prepared to support the NAV for the Yield Plus Fund, Bruce II refused.

4. The Primary Fund did not violate Section 22(e); a 22(e) order was granted by the Commission, effective September 17, authorizing the suspension of the right of redemption and postponement of payment of redemption proceeds for more than seven days. Although several other RMCI-advised funds postponed the payment of redemption proceeds for more than seven days without obtaining an order under Section 22(e), they did so at the direction of the Board of Trustees of the Funds, and not at the direction of the Bents. Moreover, the delays occurred while representatives of the Funds negotiated in good faith with the Division of Investment Management to obtain an order under Section 22(e). When the Commission eventually granted those orders, it found that postponing the payment of redemption proceeds was necessary "to protect the Funds' security holders." In light of the Commission's own findings, any charges based on Section 22(e) are unwarranted.

5. No books and records charges should be brought against the Bents, who acted reasonably based on the facts as they understood them. The Company's auditor, KPMG, did not note any significant control deficiencies in its 2008 audit that would have put the Bents on notice of possible issues with the Company's books and records. The Bents reasonably relied on their CFO and the Company's Finance Department, as well as the Company's fund accountant, State Street Bank, to calculate the NAVs for the Primary Fund and the Yield Plus Fund. Finally, the Company had a long-standing review procedure for the drafting and approval of statements to the public, such as the *Reserve Insights* article that was published for less than three hours on the Company's website on the morning of September 16. The Bents reasonably assumed that the marketing staff would follow RMCI's vetting practices and procedures, which required written

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000258

approval by the Bents prior to publication. Because the Bents acted appropriately in exercising their supervisory responsibilities, they should not be charged for the violations of the books and records provisions of the federal securities laws.

For these reasons, as discussed in detail below, fraud charges are unwarranted. The Bents took reasonable steps to protect fund investors during an unprecedented run on the Primary Fund and in the midst of unprecedented market illiquidity. Despite the Staff's allegations that the Bents intended to deceive investors into maintaining their investments in the Fund, the record shows that the Bents worked diligently over two days to find liquidity to fill investor redemptions. The fact that the Primary Fund ultimately could not meet investors' redemption requests cannot be attributed to a desire to deceive investors or the Fund's Board.

BACKGROUND

A. RMCI Background

Bruce Sr., along with his then-partner, Henry Brown, formed RMCI in or about 1969 or 1970.[3] Shortly before they created the Company, Bruce Sr. and Brown developed the idea for a money market fund, whose investment objective was to enable moderately conservative investors to capture the yield difference between Treasuries and insured bank deposits. They filed registration papers for the first money market fund with the SEC in February 1970, and the fund went effective in October 1971.[4] It is now known as the Primary Fund.

Brown retired from the investment advisory business around 1991, and Bruce Sr. bought out Brown's partnership interest in RMCI in 1999. The Bent family now owns, either directly or through family trusts, 100% of RMCI, with beneficial interest shared among Bruce Sr. and his two sons, Bruce II and Arthur Bent ("Arthur"). The family also comprises the management

[3] Deposition of Bruce Sr., dated Oct. 29, 2008, at 10:16-20.

[4] Deposition of Bruce Sr., dated Oct. 29, 2008, at 14:21-15:12.

Confidential Treatment Requested by WILMER CUTLER PICKERING HALE AND DORR LLP

RF-SEC-WH-00000259

structure of RMCI, with Bruce Sr. serving as President of the Company; Bruce II serving as Senior Vice President, Secretary and Assistant Treasurer; and Arthur serving as Senior Vice President, Chief Operating Officer, Treasurer, and Assistant Secretary.[5]

For the period covered by the Staff's investigation, the firm had seasoned and professional senior officers, including Chief Investment Officer Patrick Ledford, who has been an investment professional for 20 years, Chief Financial Officer Patrick Farrell, who is a certified public accountant and has served as a senior financial officer for 17 years, Managing Director of Marketing Eric Lansky, a professional with 15 years of marketing experience, Managing Director and Global Head of Sales John Drahzal, who has been a manager or sales professional for 20 years, and General Counsel Catherine Crowley, a 1978 graduate of Georgetown University Law Center and financial services lawyer with more than 22 years of experience advising banks and other financial services institutions.

RMCI also retained highly competent professional outside advisers. RMCI's outside counsel, who also served as counsel to the Primary Fund and to the Yield Plus Fund, were Joel H. Goldberg and Rose DiMartino, partners in the asset management group at Willkie Farr & Gallagher LLP ("Willkie"). Goldberg is a dean of the 1940 Act bar, with more than 20 years' experience advising mutual funds. He formerly served as the Director of the SEC Division of Investment Management. DiMartino is an expert on the Investment Company Act of 1940 and is ranked by Chambers (USA) 2008 as one of the leading individuals practicing in the area of registered funds. The Funds have retained KPMG LLP as their auditor. KPMG is a "Big Four Auditor" and one of the largest professional services companies in the world.

---

[5] Primary Fund Statement of Additional Information, dated Sept. 28, 2007, as supplemented through May 5, 2008, at 8-9.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

The Primary Fund grew from approximately $300,000 in assets in 1973 to $64 billion in assets by May 31, 2008.[6] The Fund is the oldest money market fund in the United States and, until Lehman filed for bankruptcy on September 15, had never incurred a credit default or other event that resulted in investor losses.Oversight for the management of the Primary Fund and the Yield Plus Fund is provided by a Board of Trustees, the majority of whom are independent – *i.e.*, not "interested persons" as defined in Section 2(a)(19) of the Investment Company Act of 1940. The Independent Trustees for the Primary Fund and the Yield Plus Fund are Edwin Ehlert, Jr., William J. Montgoris, Frank J. Stalzer, Ronald J. Artinian, Santa Albicocco, and Stephen P. Zieniewicz. The Trustees for the Primary Fund and the Yield Plus Fund have had distinguished careers in business and government, including, for example, serving as Chief Operating Officer of Bear Stearns, and Executive Vice President and Senior Managing Director of Smith Barney, and have provided attentive oversight to fund governance. The Boards for these funds met at least four times per year and diligently reviewed matters relating to investment process and performance. The counsel for the Independent Trustees is Stuart Strauss, a partner at Clifford Chance US LLP. Strauss' practice focuses on the Investment Company Act of 1940. He is well regarded in the 1940 Act bar and is the author of *A Practical Guide to the Investment Company Act* (Merrill/Magnus/1993). During the unprecedented events of September 15-16, the Board met eight times in less than 36 hours.

The Board of Directors for the International Liquidity Fund includes Bruce Sr., Bruce II and Arthur. The constituency of the Board is in accord with the laws of the British Virgin Islands.

[6] Primary Fund Annual Report, dated May 31, 2008 at 11.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000261

B. RMCI Investments in Lehman

The RMCI investment process has two components. First, the RMCI credit committee[7] reviews issuers for potential investment by a money market fund. RMCI creates and maintains a list of those issuers approved by the credit committee that satisfy the rigorous investment criteria of Rule 2a-7 of the Investment Company Act of 1940, as well as the adviser's own standards for creditworthiness.[8] Second, the Chief Investment Officer/portfolio manager for the money market funds considers whether investment in securities of a particular issuer is consistent with his own views about portfolio construction.[9]

The Primary Fund's investment in Lehman met these two criteria. At the time that RMCI selected Lehman securities for investment by its money funds, Moody's and S&P had rated Lehman's debt A1 and P1, respectively. The RMCI credit committee approved Lehman for inclusion on RMCI's approved list beginning in at least August 2005. Thereafter, Ledford made the following investments in Lehman securities for the Primary Fund: (1) on February 19, 2008, $250 million in medium term notes, maturing on March 20, 2009; (2) on February 28, 2008, $150 million in commercial paper, maturing on October 10, 2008; (3) on April 24, 2008, $185 million in commercial paper, maturing on October 29, 2008; and (4) on May 21, 2008, $200 million in commercial paper, maturing on October 28, 2008. RMCI disclosed the Lehman investments in the Primary Fund's Quarterly Schedule of Portfolio Holdings, which are filed with the SEC and, in accordance with the policies detailed in the Statement of Additional

[7] The Credit Committee consisted of Bruce Sr., Ledford and Damon Chan. *See* Deposition of Bruce Sr., dated Oct. 29, 2008, at 47:7-10, 51:8-10.

[8] Deposition of Bruce Sr., dated Oct. 29, 2008, at 44:10-47:6.

[9] Deposition of Bruce Sr., dated Oct. 29, 2008, at 46:10-47:6.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

Information, made portfolio holdings available on demand to fund investors.[10] The Primary Fund's prospectus expressly disclosed that the Fund could invest in commercial paper.[11]

At the time RMCI made these investments, the Lehman financial statements indicated that the Company's assets exceeded its liabilities. The market placed particular confidence in Lehman's financial statements because Lehman was one of five Consolidated Supervised Entities ("CSE") under heightened supervision by the SEC.[12] To become a CSE, Lehman had agreed to books and records examinations by the SEC, had regularly reported to the SEC on its financial and operational condition, and had maintained sufficient liquidity to meet expected cash outflows in a stressed liquidity environment. Lehman was particularly attractive because, as a CSE, the Commission was supposed to "monitor for, and act quickly in response to, financial or operational weaknesses in a CSE holding company or its unregulated affiliates that might place . . . the broader financial system at risk."[13] Indeed, after Lehman filed for bankruptcy protection, Lehman CEO Richard Fuld stated that regulators knew how Lehman was pricing its distressed assets and about its liquidity situation before its collapse. In testimony before the House Oversight and Government Reform Committee, Fuld stated that through 2008, the SEC and the Federal Reserve "actively conducted regular, and at times daily oversight of both our

---

[10] Primary Fund Statement of Additional Information, dated Sept. 28, 2007, as supplemented through May 5, 2008, at 7 ("A complete list of the portfolio holdings of each series of the Trust (the 'Funds'), as of the previous day if available, will be provided via facsimile by calling 800-637-1700. This information is available to any person or entity on request").

[11] Primary Fund Prospectus, dated Sept. 28, 2005 ("Primary Fund Prospectus"), at 3.

[12] SEC Office of Inspector General, *SEC's Oversight of Bear Stearns and Related Entities: The Consolidated Supervised Entity Program*, Report No. 446-A (Sept. 25, 2008) ("IG CSE Report"), at viii.

[13] *Id.* (internal citation omitted).

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000263

business and balance sheet." He added, "[Regulators] held regular price verification reviews. They were privy to everything as it was happening."[14]

At the time that the Primary Fund made its investments in Lehman, and indeed, on September 10, when the Trustees of the Primary Fund discussed the Primary Fund's holding of Lehman debt securities, the Bents, the Trustees and the investing public did not know that the SEC had defaulted on its obligation to oversee the financial risk posed by the then-undisclosed precarious financial condition of Lehman.[15] Had the SEC fulfilled its statutory responsibilities and taken steps to remedy or disclose Lehman's financial condition, the Reserve Funds likely would not have invested in Lehman or would have taken steps to protect Fund investors from a Lehman default.[16] In addition, the manner in which the SEC permitted or encouraged Lehman precipitously to file for bankruptcy without adequate preparation significantly increased investor losses.[17]

Although RMCI investment professionals believed that the Lehman investments were prudent and would mature at full value, the funds that purchased the Lehman securities were not insured against loss. The Primary Fund prospectus, for example, stated:

> An investment in the Fund is not insured or guaranteed by the U.S. government, FDIC or any other government agency. Although each Fund

---

[14] Richard S. Fuld, Jr., Statement before the U.S. House of Representatives Committee on Oversight and Government Reform (Oct. 6, 2008) at 6, *available at* http://oversight.house.gov/documents/20081006125839.pdf (last visited Jan. 20, 2009).

[15] *See* IG CSE Report at 2.

[16] For example, RMCI could have hedged its Lehman positions through credit default swaps.

[17] A three-month study by Lehman's restructuring advisor, conducted at the request of the Bankruptcy Court, determined that a more orderly liquidation would have preserved as much as $75 billion in value by enabling Lehman to unwind its derivatives position and sell some of its assets outside of bankruptcy-court protection. Stephen Foley, *Chaotic End to Lehman "Cost $75 billion in Value"; Bankruptcy of Bank Could Have Been Better Managed*, The Independent, Dec. 30, 2008, at 40; *see also* Susanne Craig, et al., *The Weekend That Wall Street Died --- Ties That Long United Strongest Firms Unraveled as Lehman Sank Toward Failure*, Wall St. J., Dec. 29, 2008, at A1; *see also* Jeffrey McCracken, *Lehman's Chaotic Bankruptcy Filing Destroyed Billions in Value*, Wall St. J., Dec. 29, 2008, at A10.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

seeks to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in a Fund.[18]

The Fund's Statement of Additional Information included similar disclosures.[19]

RMCI made Lehman investments in two additional funds for which they were also suitable – the Yield Plus Fund and the Reserve International Liquidity Fund Ltd. Although these two funds seek to maintain a stable $1.00 share price, neither of these funds is a money market fund. Indeed, the International Liquidity Fund is not a U.S.-registered fund. It is an offshore fund, registered in accordance with the British Virgin Islands Mutual Funds Act of 1996. The offering documents for both funds disclosed that the funds were not insured and that customers could lose money on their investment.[20]

Following its investment on behalf of the funds, RMCI continued to monitor the creditworthiness of Lehman. Although the financial sector experienced downward pressures throughout 2008, the market was optimistic about Lehman:

[18] Primary Fund Prospectus at 5.

[19] Primary Fund Statement of Additional Information, dated Sept. 28, 2007, as supplemented through May 5, 2008, at Table of Contents ("SHARES OF THE FUNDS ARE NEITHER GUARANTEED NOR INSURED BY THE U.S. GOVERNMENT, AND THERE CAN BE NO ASSURANCE THAT A FUND WILL BE ABLE TO MAINTAIN A STABLE NET ASSET VALUE OF $1.00 PER SHARE").

[20] The prospectus for the Yield Plus Fund, the sole series of Reserve Short-Term Investment Trust, for example, warns: "THIS FUND IS NOT A MONEY MARKET FUND. Investors can lose money by investing in the Fund .... WHILE THE FUND IS NOT A MONEY MARKET FUND, IT SEEKS TO MAINTAIN A STABLE $1.00 SHARE PRICE AND THERE CAN BE NO ASSURANCE THAT THE FUND WILL BE ABLE TO MAINTAIN A STABLE NET ASSET VALUE OF $1.00 PER SHARE .... Unlike the Fund, money market funds are subject to conditions in a Securities and Exchange Commission ("SEC") rule that are intended to stabilize a money market fund's net asset value at $1.00. These conditions are intended to limit risk in a money market fund's portfolio in the areas of credit quality, diversification and maturity of fund investments .... Although the Fund seeks to maintain a $1.00 share price, it is not required to comply with this SEC rule and therefore the Fund is a riskier investment than a money market fund." Yield Plus Fund Prospectus, dated July 29, 2008, as supplemented through Sept. 18, 2008, at 2. The International Liquidity Fund offering documents include similar disclosures, as required by the laws of the British Virgin Islands. *See* RF-SEC-WH 00000175-206, Reserve International Liquidity Fund Ltd. Offering Memorandum, dated Jan. 18, 2008, at 12-13 ("Although the Fund seeks to preserve the value of an investment at U.S. $1.00 per Share of each respective U.S.$ Share class, an investment in the Fund involves investment considerations and risk factors that prospective investors should consider before investing. It is possible to lose money by investing in the Fund .... While the Fund will strive to maintain a constant Share price, [various] factors could reduce the Fund's income level and/or Share price .... As a consequence of these basic risks . . . when you redeem your Shares in the Fund, they could be worth more or less than what you paid for them").

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

> The good news about Lehman Brothers Holdings Inc. is that it's no Bear Stearns. The firm won't disappear overnight . . . . Unlike Bear, Lehman has access to the Federal Reserve's discount window, allowing it to tap liquidity that wasn't available to investment banks back in March. Lehman also appears to have lengthened the terms of its collateralized borrowings, meaning it is less likely to face a debilitating run on the bank. Trading partners, while nervous, don't seem to be pulling business from the firm . . . . Credit markets haven't hit the panic button, in contrast to mid-March, when Lehman's debt dropped sharply in value. So Lehman may have some breathing room, perhaps even enough to allow Chief Executive Richard Fuld to continue fighting against a sale of the firm.[21]

Prior to the day that Lehman filed for bankruptcy protection, and throughout the period that the RMCI-advised funds held Lehman securities, Moody's, S&P, and Fitch maintained Rule 2a-7-eligible ratings for Lehman.

While financial services firms in general, and Lehman in particular, weakened throughout 2008, public information did not suggest that the Company would fail. By the first week of September 2008, the market speculated that Lehman might spin off its troubled mortgage assets to a new company, sell its investment management business, or sell part of itself to the Korea Development Bank.[22] Lehman's Chief Executive Officer, Richard Fuld, continued to reassure investors that Lehman's assets exceeded its liabilities. Fuld released Lehman's third-quarter earnings announcement ahead of schedule, and conducted an investor call before the market opened on Wednesday, September 10. During that call, Fuld stated that Lehman would spin off real estate assets, sell a majority of its investment management arm, reduce its dividend by 93%, and "emerge clean."[23] RMCI investment professionals were knowledgeable about these developments and conveyed Lehman's statements to the Board for the Primary Fund and the Yield Plus Fund, reporting that the Lehman holdings likely would mature at par:

---

[21] David Reilly and Peter Eavis, *Lehman's Holders in Pain – Shares May Not Get a Lift as Firm Seeks to Exit Rough Patch*, Wall St. J., June 13, 2008, at C14.

[22] Ben White and Jenny Anderson, *Lehman May Split Off Weak Holdings*, N. Y. Times, Sept. 5, 2008, at C1.

[23] Susanne Craig, *Lehman Struggles to Shore Up Confidence – Plan to Shrink Firm is Late, Critics Say; Fuld Fights Rumors*, Wall St. J., Sept. 11, 2008, at A1.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000266

> Mr. Montgoris asked Mr. Ledford whether the portfolio had any exposure to Lehman Brothers. Mr. Ledford told the Board that certain funds held Lehman debt and that the Primary Fund had approximately 1.1% of its assets in Lehman Brothers debt. A discussion followed regarding the nature of the position. The Trustees asked Mr. Ledford to comment on Lehman's current situation in comparison with that of Bear Stearns in March 2008. Mr. Ledford said that he had just listened to a telephone presentation regarding Lehman's financial situation and its future business plans. Mr. Ledford said that in his view, Lehman appeared to continue to have counterparties with which to deal whereas Bear Stearns had not under similar economic circumstances and that Lehman could have access to cash to meet its obligations under the Federal Reserve's lending program available to investment banks that was instituted shortly after Bear Stearns was acquired by J.P. Morgan. Mr. Bent stated that he agreed with that view.[24]

On September 15, Lehman declared bankruptcy. That same day, Merrill Lynch announced that it had agreed to be acquired by Bank of America. One day later on September 16, the federal government announced that it had agreed to support AIG, a private insurer. That same day, the Board of Trustees for the Primary Fund announced that the NAV of the fund had declined to $0.97 per share and that proceeds for redemptions from the Primary Fund would not be transmitted to redeeming investors for a period of up to seven calendar days.[25]

C. Deepening Liquidity Crisis and The Lehman Bankruptcy

Three events converged on September 15 and 16 to cause the Primary Fund to trade at less than $1.00 per share: a deepening worldwide liquidity crisis; the unanticipated bankruptcy filing of Lehman; and a panic-provoked run on the Primary Fund unlike anything previously experienced by a money market fund. Beginning in mid-2007, commercial banks began to report real estate investment losses, resulting in tightened lending standards and margins, forcing customer and counter-party sell-offs that depressed prices and tightened funding further. Among the many unprecedented actions taken by the federal government to stabilize the markets and ease constraints on credit were the following:

---

[24] RF-SEC-00178695.

[25] RF-SEC-0000003.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

- On August 9, 2007, the Federal Reserve injected $24 billion into the market,[26] and a week later, it expanded those efforts by (a) decreasing the discount rate by half a percentage point; (b) broadening the type of collateral banks could post; and (c) lengthening its lending horizon.[27]

- In September 2007, the Federal Reserve reduced both the federal funds rate and the discount rate by 50 basis points.[28]

- On December 12, 2007, the federal government announced the creation of the Term Auction Facility ("TAF"), which permitted banks anonymous access to governmental liquidity support.[29]

- On March 11, 2008, the Federal Reserve announced a $200 billion Term Securities Lending Facility, allowing investment banks to swap mortgage-related bonds for Treasury bonds for up to 28 days.[30]

Notwithstanding these extraordinary measures, significant and storied financial services companies collapsed in 2008:

- On March 13, 2008, Bear Stearns lost 80% of its available cash in one day and was on the brink of collapse.[31] The Federal Reserve intervened, providing an emergency loan facility (with J.P. Morgan Chase's commercial bank acting as conduit) to get Bear Stearns through Friday, March 14,[32] and then brokered the sale of Bear Stearns to JP Morgan. In order to generate further liquidity, the Federal Reserve cut its discount rate to 3.25% and, for the first time, opened its discount window to investment banks.[33]

- On July 11, 2008, a run on California regional savings and loan bank and mortgage originator, Indy Mac, prompted the FDIC to place the bank in conservatorship.[34]

---

[26] Carrick Mollenkamp, et al., *Global Scale: Impact of Mortgage Crisis Spreads*, Wall St. J., Aug. 10, 2007, at A1.

[27] Press Release, Federal Reserve (Aug. 17, 2007), *available at* http://www.federalreserve.gov/newsevents/press/monetary/20070817a.htm (last visited Jan. 20, 2009).

[28] Press Release, Federal Reserve (Sept. 18, 2007), *available at* http://www.federalreserve.gov/newsevents/press/monetary/20070918a.htm (last visited Jan. 20, 2009).

[29] Press Release, Federal Reserve (Dec. 12, 2007), *available at* http://www.federalreserve.gov/newsevents/press/monetary/20071212a.htm (last visited Jan. 20, 2009).

[30] Press Release, Federal Reserve (Dec. 12, 2007), *available at* http://www.federalreserve.gov/newsevents/press/monetary/20080311a.htm (last visited Jan. 20, 2009).

[31] Stephen Labaton, *Bear Stearns in the Committee Room*, N.Y. Times, Apr. 4, 2008, at C1.

[32] Landon Thomas, Jr., *Run on Big Wall St. Bank Spurs U.S.-Backed Rescue*, N.Y. Times, Mar. 15, 2008, at A1.

[33] Press Release, Federal Reserve (Mar. 16, 2008) *available at* http://www.federalreserve.gov/newsevents/press/monetary/20080316a.htm (last visited Jan. 20, 2009).

[34] Louise Story, *Regulators Seize Indy Mac After a Run on the Bank*, N.Y. Times, July 12, 2008, at C5.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000268

- On September 8, 2008, the government assumed control of mortgage giants Fannie Mae and Freddie Mac and placed them into conservatorship.[35]

Although the government anticipated that supporting Fannie Mae and Freddie Mac would "put a floor under the sagging housing market, which in turn would patch holes in the balance sheets of banks and brokerages that hold billions of dollars in mortgage-related securities on their books[,]"[36] financial services firms with significant exposure to the mortgage market continued to decline.

Against this background, on September 15, 2008, when Lehman filed for Chapter 11 protection, institutional investors panicked and sought to redeem their interests in the Primary Fund. They created a massive run on the Fund, exacerbated by frozen credit markets that impaired RMCI's ability to liquidate high quality positions in government agencies or commercial paper to satisfy client redemptions.

D. BOARD NOTIFICATION OF LEHMAN DEVELOPMENTS

In conformity with Investment Company Act rules, RMCI promptly notified the Primary Fund's Board of Trustees about Lehman's Chapter 11 filing and asked the Board, as it was required to do pursuant to Rule 2a-7 of the Investment Company Act of 1940, to consider a fair valuation for the Fund's Lehman debt. The Board met by telephone on September 15 at 8:00 a.m., 9:30 a.m. and 1:00 p.m.[37] At the 8:00 a.m. meeting, the Board preliminarily agreed to fair value the Lehman positions in the Fund, but asked RMCI management to provide it with

---

[35] Stephen Labaton and Edmund L. Andrews, *In Rescue to Stabilize Lending, U.S. Takes Over Mortgage Finance Titans*, N.Y. Times, Sept. 8, 2008, at A1.

[36] Walter Hamilton and Peter G. Gosselin, *Wall Street Scrambles as Banks Teeter*, Los Angeles Times, Sept. 15, 2008, at A1.

[37] On September 15 and 16, Bruce Sr. was in Italy. He flew to Italy on Sunday, September 14 (prior to Lehman's announcement that it was planning to seek Chapter 11 protection) in order to celebrate the 50th anniversary of the day he met his wife. He nonetheless participated by telephone in all of the board meetings on September 15 and 16. While in Italy, however, he did not have access to e-mails and did not review the draft RMCI communications relating to the Lehman bankruptcy. Deposition of Bruce Sr., dated Oct. 29, 2008, at 108:16-110:12.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

additional information about Lehman trading activity to inform the Board's valuation decision.[38] At the 9:30 a.m. meeting, the Board fair valued Lehman at 80% of par, and agreed to meet daily so that it could review the Lehman valuation as market conditions changed.[39] The Company notified the SEC immediately after the Board meeting.[40] At 1:00 p.m., RMCI asked for Board authorization to seek SEC no-action relief allowing RMCI to support the NAV of the Primary Fund. The Board provided its approval and Bruce II and counsel contacted the SEC.[41]

The following morning, September 16, at 10:00 a.m., RMCI informed the Trustees that redemptions had continued unabated and the Primary Fund had been unable to fill outstanding redemptions because of limitations the market and the Primary Fund's custodian bank, State Street Bank, had imposed on its liquidity. RMCI regretfully informed the Board that it would not be able to support the Primary Fund's NAV.[42] The Board met four more times on September 16 to review the adviser's efforts to find alternative sources of liquidity or support for the Fund. These meetings occurred at 12:00 p.m., 1:45 p.m., 3:45 p.m., and 4:15 p.m. At the noon meeting, Bruce II updated the Board on RMCI's efforts to obtain additional liquidity or to form a strategic partnership with a third party.[43] The Board considered further reducing the valuation of the Fund's Lehman securities, but adjourned without establishing a new price in hopes that the Federal Reserve would extend liquidity to the Primary Fund.[44] When the Board reconvened at 1:45 p.m., it joined RMCI on a telephone call with representatives of the Federal Reserve and asked for liquidity to allow the Primary Fund to meet existing redemptions, to prevent the Fund

---

[38] RF-SEC-00178716.

[39] RF-SEC-00178717.

[40] RF-SEC-00178718.

[41] RF-SEC-00178719.

[42] RF-SEC-00178720.

[43] RF-SEC-00178723-24.

[44] RF-SEC-00178725.

Confidential Treatment Requested by WILMER CUTLER PICKERING HALE AND DORR LLP

from breaking the buck.[45] At 3:45 p.m., RMCI reported that the Federal Reserve had declined to provide any additional liquidity, and that redemption requests had reached approximately $40 billion, reducing the Primary Fund to approximately one-third of the assets it had held 36 hours previously. The Board concluded that the Primary Fund was no longer a going concern, and reduced the valuation of the Lehman securities to zero.[46] The Fund promptly issued a press release announcing that the NAV for the Primary Fund was $0.97 per share.[47]

E. The Bents' Efforts to Protect Investor Assets on September 15-16, 2008

The Bent family took extraordinary actions on September 15 and 16 to protect investors in the Primary Fund by seeking to create liquidity so that Fund investors could redeem, and by seeking a financial partner to provide NAV support for the Primary Fund. Bruce II's phone log and computer show that he received or sent 237 e-mails and participated in 96 calls on September 15 alone. (Between 9:00 a.m. and 5:00 p.m., Bruce II sent or received an e-mail on average every four minutes.) Among many actions, all compressed within the intense hours surrounding the eight Board meetings of September 15 and 16, RMCI management:

- Contacted the Federal Reserve Bank of New York on the 15th and 16th to request liquidity support for the Primary Fund and to warn it of the effects of potential problems of the bellwether Primary Fund on the $3 trillion money fund industry.[48]
- Sought approval from the Federal Reserve Bank of Boston for State Street to provide greater overdraft protection to the Primary Fund, whose assets were held at State Street Bank.[49]
- Committed personal funds to support the NAV of the Fund – and had been in discussions with the SEC on providing $10 million to support the Fund.[50]

---

[45] RF-SEC-00178725.

[46] RF-SEC-00178726.

[47] RF-SEC-00178726.

[48] Deposition of Bruce II, dated Nov. 25, 2008, at 101:12-20.

[49] RF-SEC-00162852.030; Deposition of Bruce II, dated Nov. 25, 2008, at 126:16-127:19.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000271

- Tried to negotiate a reverse repurchase agreement from either State Street or Barclays PLC so that the Primary Fund would have liquidity to meet investor redemptions.[51]

- Requested assistance from the Investment Company Institute in finding a buyer or consortium of buyers for the Lehman paper in the Primary Fund portfolio or other assistance.[52]

- Notified RMCI's investment bankers that the family would be willing to sell RMCI in an effort to support the Primary Fund's NAV.[53]

None of these measures proved successful and, around midnight on September 15, Bruce Sr. and Bruce II reluctantly concluded that RMCI could not support the Primary Fund's NAV.[54] At 7:00 a.m. on September 16, the Bents informed their counsel that they would not be able to support the NAV of the Primary Fund.[55] They called the SEC Division of Investment Management at 8:00 a.m. to inform the SEC Staff of overnight developments.[56] Throughout the day, rumors circulated that the Primary Fund would break the buck. Bloomberg, in fact, identified that *a source at the SEC* had informed its reporters that the Primary Fund was no longer valued at $1.00 per share.[57] Investor redemptions continued.[58] The Reserve's Board of

---

[50] RF-SEC-00178719; Deposition of Bruce Sr., dated Nov. 20, 2008, at 32:15-33:25; Deposition of Bruce II, dated Nov. 3, 2008, at 158:25-159:11.

[51] RF-SEC-00091442; RF-SEC-00107813-14; RF-SEC-00100008.

[52] RF-SEC-00178721; RF-SEC-00178724.

[53] Deposition of Bruce II, dated Nov. 3, 2008, at 163:16-24; Deposition of Bruce II, dated Nov. 25, 2008, at 103:10-105:20, 110:6-9; RF-SEC-00107903. Although Bruce II sent an e-mail to an investment banker stating that any potential buyer would not be legally obligated to support the NAV (RF-SEC-00038031), he explained in testimony that, in his efforts to find a strategic partner, he was trying to expand the number of potential venture partners and was eliminating conditions for engaging in discussions with buyers. *See* Deposition of Bruce II, dated Nov. 25, 2008, at 107:23-108:10. The Bents were willing to sell the company for "little to no compensation" to support the NAV. Deposition of Bruce II, dated Nov. 3, 2008, at 163:16-24.

[54] RF-SEC-WH-00000043-45; Deposition of Bruce II, dated Nov. 3, 2008, at 174:25-175:7; Deposition of Arthur Bent, dated Dec. 11, 2008, at 65:15-24.

[55] RF-SEC-00187438; Deposition of Bruce II, dated Nov. 3, 2008, at 180:12-181:2.

[56] RF-SEC-00187429-43, at RF-SEC-00187438.

[57] RF-SEC-00178890-92.

[58] RF-SEC-00162625.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

Trustees concluded that the Primary Fund appeared to be self-liquidating and, at 4:00 p.m., they announced that Fund's NAV was $0.97 per share.[59]

F. THE MONEY FUND CRISIS CONTINUES

Fallout from the Lehman bankruptcy has not been limited to RMCI; the events of September 15 triggered a broad dislocation across the money fund industry.[60] On September 16, the Bank of New York Mellon Corp.'s $22 billion BNY Institutional Cash Reserve Fund announced that its NAV had declined below $1.00 per share.[61] By mid-week, net outflows from money funds totaled over $140 billion, well in excess of the $7 billion outflows the prior week.[62] This investor exodus forced money funds into sell-offs as they scrambled for liquidity to meet redemptions.[63] On September 17, Putnam closed its Prime Money Market Fund because it could not meet redemptions.[64]

Concerned about potential spillover into the broader credit markets, the federal government once again intervened. On September 19, the Federal Reserve announced $230 billion in emergency loans to banks that agreed to purchase commercial paper from money

[59] RF-SEC-0000003.

[60] Daisy Maxey, *Sponsors to Back Some Lehman Exposure – Funds of Evergreen, Russell Investments To Receive Support*, Wall St. J., Sept. 17, 2008, at C19.

[61] Matthew Keenan and Christopher Condon, *BNY Mellon, Reserve Primary Rattle Fund Investors* (noting that the BNY Institutional Cash Reserve Fund was not a money fund but attempted to maintain a stable $1.00 NAV), Bloomberg News, Sept. 18, 2008, *available at* http://www.bloomberg.com/apps/ news?pid=20601087&sid=aLCm3FmG9zX4 (last visited Jan. 20, 2009).

[62] Deborah Solomon, et al., *Shock Forced Paulson's Hand – A Black Wednesday on the Credit Markets*, Wall St. J., Sept. 20, 2008, at A1.

[63] *Id.*; *see also* Shefali Anand and Diya Gullapalli, *The Financial Crisis: Bailout of Money Funds Seems to Stanch Outflow*, Wall St. J., Sept. 20, 2008, at A2.

[64] Diya Gullapalli, *Investors Flee Money Funds, Moving Cash to Safer Spots*, Wall St. J., Sept. 19, 2008, at C1.

Confidential Treatment Requested by WILMER CUTLER PICKERING HALE AND DORR LLP

funds.[65] At the same time, the U.S. Department of Treasury established a $50 billion guarantee program to ensure a $1.00 NAV for eligible money market funds.[66] The Treasury's guarantee is not available to money funds with NAVs below $0.995 as of September 19, 2008,[67] uniquely excluding only the shareholders of the Reserve's Primary Fund from the protection afforded to the rest of the industry.

Although the federal government's rescue efforts helped to ease some of the pressures on the money fund industry,[68] declining interest rates and Treasury yields make it nearly impossible for money fund advisers to cover their costs or generate a profit.[69] Evergreen Investments, Allegiant Funds, J.P. Morgan Chase, Vanguard, and Barclays have all closed their government and/or treasury funds to new investors.[70] Credit Suisse Asset Management exited the domestic money fund business altogether, liquidating three funds that totaled $8 billion.[71] Similarly,

---

[65] Press Release, Federal Reserve (Sept. 19, 2008), *available at* http://www.federalreserve.gov/newsevents/press/monetary/20080919a.htm (last visited Jan. 20, 2009); *see also*, Shefali Anand and Diya Gullapalli, *The Financial Crisis: Bailout of Money Funds Seems to Stanch Outflow*, Wall St. J., Sept. 20, 2008, at A2. The Federal Reserve subsequently augmented the initiative with the Money Market Funding Facility, which injected an additional $540 billion in liquidity to thaw short-term debt markets and enable money funds to satisfy redemption requests through selling assets. Press Release, Federal Reserve (Oct. 21, 2008), *available at* http://www.federalreserve.gov/newsevents/press/monetary/20081021a.htm (last visited Jan. 20, 2009); *see also* Neil Irwin, *Fed Prepared to Prop Up Money-Market Funds*, Washington Post, Oct. 22, 2008, at D1.

[66] Press Release, United States Department of the Treasury (Sept. 29, 2008) *available at* http://www.treas.gov/press/releases/hp1161.htm (last visited Jan. 20, 2009); Diana B. Henriques, *Rescue Plan for Funds Will Come at a Price*, N.Y. Times, Sept. 20, 2008, at C1.

[67] Press Release, United States Department of the Treasury (Sept. 29, 2008) *available at* http://www.treas.gov/press/releases/hp1161.htm (last visited Jan. 20, 2009).

[68] Shefali Anand and Diya Gullapalli, *The Financial Crisis: Bailout of Money Funds Seems to Stanch Outflow*, Wall St. J., Sept. 20, 2008, at A2; *see also*, Diya Gullapalli, *Crisis on Wall Street: Money Funds Feel the Pull of Fed's Moves*, Wall St. J., Dec. 18, 2008, at C2.

[69] Daisy Maxey, *Low Treasury Yields Buffet Money Funds – Some Managers Opt to Close Doors for a Bit*, Wall St. J., Dec. 11, 2008, at C11; Diya Gullapalli, *Crisis on Wall Street: Money Funds Feel the Pull of Fed's Moves*, Wall St. J., Dec. 18, 2008, at C2; Ian Salisbury, *Fed's Rate Cutting Puts Shine on CDs – Yields, Safety Give Edge Over Money Funds*, Wall St. J., Dec. 23, 2008, at C9.

[70] Daisy Maxey, *Low Treasury Yields Buffet Money Funds – Some Managers Opt to Close Doors for a Bit*, Wall St. J., Dec. 11, 2008, at C11.

[71] *Id.*

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000274

Dreyfus announced plans to liquidate its government money market fund at the end of January 2009.[72]

The pressures of the money fund crisis have been acutely experienced at RMCI. After RMCI announced that the Primary Fund could not meet redemptions and had been valued at $0.97, the Firm experienced massive redemptions from all of its funds. As of January 15, 2009, RMCI had liquidated 12 money funds, and is currently in the process of liquidating 17 more.[73] Once distributions to investors have been completed, and for the first time since Bruce Sr. registered the original money market fund in 1970, RMCI will not be the adviser to any money funds. RMCI and the Bents face an uncertain future in the investment advisory business.

ARGUMENT

I. THE BENTS' STATEMENTS TO THE BOARD WERE TRUTHFUL AND COMPLETE

In the Staff's view, Bruce Sr. and Bruce II were not truthful with the Board of the Primary Fund and the Yield Plus Fund. The Staff includes in its litany of alleged falsehoods or omissions the following: (i) information relating to trading activity in Lehman debt on the morning of September 15; (ii) the impact of Lehman's valuation on the NAV for the funds; (iii) the Bents' willingness to support the NAV of the Primary Fund; (iv) representations about the overdraft situation at State Street; (v) omissions relating to rating agency statements about the advisability of creating a Credit Support Agreement prior to a credit event in the Primary Fund; and (vi) omissions relating to the content of a single e-mail communication, dated September 16, 2008 between Bruce II and an investment banker regarding Bent family considerations with respect to a sale of RMCI.

---

[72] *Id.*

[73] http://www.ther.com/ReserveOnline/RSVYieldsHTML?info=yields (last visited Jan. 20, 2009).

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000275

Certain of the alleged falsehoods, as detailed below, are belied by the relevant audiotapes of the conversations prior to and during the Board meetings on September 15. The remaining omissions are immaterial at law and assume a legal obligation by the adviser to support the NAV of money funds that does not exist in the federal securities laws. A more considered and fair review of the evidence demonstrates that Bruce Sr. and Bruce II provided truthful information to the Board during a period of unprecedented market distress.

A. THE BENTS' REPRESENTATIONS TO THE BOARD REGARDING LEHMAN TRADING ACTIVITY AND THE IMPACT OF LEHMAN VALUATION ON THE PRIMARY FUND AND YIELD PLUS FUND WERE TRUTHFUL

We turn first to the Staff's claim that Bruce Sr. and Bruce II did not provide the Board of the Primary Fund and the Yield Plus Fund with accurate and timely information on the range of potential prices for Lehman between 8:00 a.m. and 10:00 a.m. on September 15, 2008 in connection with the Board's valuation of the Fund's Lehman holdings.[74] During the period in question – *i.e.*, in the first few hours following Lehman's bankruptcy announcement – there were no reported trades for Lehman debt.[75] The Board was fully aware of that fact, as well as the fact that any price below 55 cents per dollar would cause the Primary Fund's NAV to fall below $1.00 per share. The Staff's inferences to the contrary are not supported by the tapes of conversations among Bruce Sr., Bruce II, Ledford and the Board. We point to the following information:

[74] During the Wells call of December 17, 2008, the Staff appeared to suggest that Bruce Sr. and Bruce II were not truthful with the Board for the International Liquidity Fund. The Staff conducted no discovery on this issue and appears to have concluded, erroneously, that the Board for the Primary Fund and the Yield Plus Fund is also the Board for the International Liquidity Fund. This assumption is erroneous. As stated above, the International Liquidity fund's three-member Board of Directors consists of Bruce Sr., Bruce II, and Arthur.

[75] We note that Bruce Sr. took part in these calls a few hours after he had arrived in Italy following an overnight flight from the United States and at a time when he had no electronic access to market information, documents or e-mails.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

1. THE BENTS' REPRESENTATIONS RELATING TO THE IMPACT OF LEHMAN VALUATIONS ON THE NAV OF THE PRIMARY FUND AND THE YIELD PLUS FUND

The transcripts of Bruce Sr.'s discussions with the Board confirm that he promptly and truthfully informed the Board about the Lehman valuation levels that would cause the Primary Fund and the Yield Plus Fund to trade at less than $1.00 per share. RMCI called for a meeting of the Board of Trustees of both funds at 8:00 a.m. on September 15 to review the effect of the Lehman bankruptcy on the funds. In preparation for that meeting, Bruce II and Bruce Sr. consulted with the portfolio manager of the two funds, Ledford, regarding Lehman market activity and the potential Lehman valuations that would cause the Primary Fund's NAV to decline below $1.00 per share – information that an informed Board would expect the investment adviser to provide it in the event of a credit default of a significant position in a fund's portfolio.

In a 7:47 a.m. call with Ledford, Bruce Sr. and Bruce II asked Ledford to compile information about the impact of Lehman valuations on the NAV of the Primary Fund:

Bruce Sr.: Okay. We price the Funds each day and the variance of the value of the Fund relative to the market value is plus/minus $10 million, $30 million, whatever it is. The pricing sheet we get each day?

Ledford: Yes. Yes.

Bruce Sr.: Okay. Then what we have to do is figure out how much we have in Lehman. And assume the value of the other securities is going to be plus/minus whatever it was on Friday. And then we have to say, how much can the Lehman be marked down before we break the half-penny rule on each one of these funds.

Ledford: Okay. Alright. I can do that.

Bruce II: Okay. So you'll call me back when you have that Patrick?

Ledford: Yeah. I'll call you right back.[76]

[76] RF-SEC- 00162852.061.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

At 8:08 a.m., Bruce Sr. called Ledford and asked him to report on the impact of Lehman valuations on fund NAVs.[77] Ledford reported that the information had not yet been compiled. Bruce Sr. then asked Ledford to confirm basic, factual information about the funds' Lehman holdings from which he might compute this information for the Board. Ledford provided the following information about the two domestic funds that had Lehman exposure:

Bruce Sr.:	Okay. Let's go by the funds then. The thing that you came up with the other day – we have $67 billion in the Primary Fund?
Ledford:	That's correct. Uh huh.
Bruce Sr.:	Okay. And the Primary Fund is $750 million in Lehman?
Ledford:	Hang on. Let me get my sheet out. That is correct.
Bruce Sr.:	Okay.
Ledford:	It's like 1.18%.
Bruce Sr.:	Okay fine. Next fund that has Lehman is what?
Ledford:	Hang on, um Yield Plus.
Bruce Sr.:	Is that a '40 Act fund?
Ledford:	Um, no, that is no, so we don't have to worry about that.
Bruce Sr.:	How much money is in that? What's the percentage?
Ledford:	The total is $30 million.
Bruce Sr.:	$30 million in Lehman paper?
Ledford:	Yeah. $30 million in Lehman paper. Hang on. Let me get my sheet out here. Hang on a second, Mr. Bent. Let me get this out here. Okay, um, yeah. It's Yield Plus. Yield Plus is $1.1 billion or 2.6%.

The Bents and Ledford then joined the pre-scheduled 8:00 a.m. Board meeting and provided information about the impact of Lehman valuations on the funds' NAVs. Because the Finance

[77] RF-SEC-00178693.001.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

Department had not prepared the spreadsheet of the impact of Lehman's valuation on the Fund's NAV, Bruce Sr. performed his own rough calculation for the Board:

> Bruce Sr.: Okay, the half of one percent and the fair valuing. Let me, ah, I'll give you the statistics. We have $67 billion in the Primary Fund. A half of one percent of that would be $335 million. We've got $750 million in Lehman in the Primary Fund. If Lehman is marked to market at 55%, then we're at the half of one percent level. Now, I think the probabilities of that are zero. Nevertheless, what we want to do is get instructions from you people on the ability to go to fair value accounting.[78]

Contrary to the Staff's view that Bruce Sr. and Bruce II concealed from the Board the Lehman valuation levels that would cause the Primary Fund to trade at less than $1.00 per share, the transcripts confirm that Bruce Sr. provided the Board – at the very first Board meeting – with his best assessment that a 55% of par valuation for Lehman would cause the Primary Fund to trade at less than $1.00 per share.

He provided similar information to the Board about the impact of the Lehman valuation on the Yield Plus Fund. On this point, Bruce Sr. informed the Board that an 80% valuation of Lehman would cause the NAV of the Yield Plus Fund to decline below $1.00 per share:

> Bruce Sr.: To the extent that the Yield Plus amounts to more than a half of one percent, well that's really not party to this conversation, but anyhow, since they are here, we can put – we being RMCI – can put in a supplemental letter on that.[79]

The context of the discussion confirms that Bruce Sr. disclosed to the Board that valuation of Lehman at 80% would cause the Yield Plus Fund to trade at less than $1.00 per share and that RMCI would consider providing some form of credit support agreement – in his words, "a supplemental letter" – in order to protect the NAV of the Yield Plus Fund.

[78] RF-SEC-00178693.001.

[79] RF-SEC-00178693.004.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

2. Disclosures Relating to Lehman Market Activity

The audiotapes similarly confirm that Bruce Sr. and Bruce II did not deceive the Board of the Yield Plus and Primary Funds regarding market activity in Lehman debt. RMCI discussed Lehman valuations with the Board early on September 15, even before the market had opened. At the 8:00 a.m. meeting, the Board requested market data so that it could consider the fair valuation for Lehman. As reflected in the following exchange, Fund counsel concurred:

> Bruce Sr.: Okay, so this is not some sort of preemptory call? This is something we find out after the market opens.
>
> DiMartino: I would expect so.[80]

Bruce Sr., therefore, agreed – from Italy – to supervise the collection of Lehman market information to "see what happens in the marketplace. When we find out what happens in the marketplace, then we will reconvene the Board meeting and we will discuss with the board what we think is the best course of action at that point in time."[81]

Bruce Sr. followed through on his commitment to the Board and, in advance of the next-scheduled 9:30 a.m. Board meeting, spoke with Bruce II and Ledford about early market activity for Lehman paper. Ledford informed Bruce Sr. and Bruce II that there had been no actual trades of Lehman debt. In particular, and in response to Bruce II's question, "What are you going to recommend?" Ledford offered the following assessment:

> Ledford: A couple things. And this is very, very preliminary. It looks like the debt, regardless of the maturity, the senior debt is trading like at 30-40 cents on the dollar. But, none has actually traded.
>
> Bruce Sr.: 30-40 cents on the dollar?
>
> Ledford: Yeah, yeah. However, the preliminary valuations being done on the Street, it looks like what they're suggesting for the senior unsecured debt – 60-80 cents on the dollar would be recovered.

---

[80] RF-SEC-00178693.001.

[81] RF-SEC-00178693.001.

Confidential Treatment Requested by WILMER CUTLER PICKERING HALE AND DORR LLP

Bruce II:	Where are you getting this from?
Ledford:	This is information from the dealer community. But, again, it's a moving target.
Bruce II:	So, what are you going to say? What are you going to recommend we price it at?
Ledford:	At somewhere between 60 and 80 cents on the dollar . . .
Bruce II:	It doesn't make any sense for us to price it between 60 and 80 cents. All you're doing is looking at the market. So, we're not going to do that. The market is too thinly traded.
Ledford:	Bruce, I agree. I agree completely.[82]

Bruce Sr., Bruce II and Ledford then joined the already convened 9:30 a.m. Board meeting. At the outset of the meeting, Bruce Sr. reported to the Board that he had discussed Lehman market information with Ledford:

Bruce Sr.:	Okay. Discussions with Patrick [Ledford] and Patrick's discussions with the marketplace. There is no valid market. The bids are being thrown out there anywhere from 45 to 80. Is that correct, Patrick?[83]
Patrick:	Yeah, that's correct.[84]

Moments after suggesting that there had been actual "bids" for Lehman, however, Bruce Sr. corrected his statement and observed: "I am sure that those are indications and no firm bids. Is that right, Patrick?"[85] Ledford agreed, stating, "That is correct. There is no actual trading being done."[86]

[82] RF-SEC-00178693.004.
[83] RF-SEC-00178693.004.
[84] RF-SEC-00178693.004.
[85] RF-SEC-00178693.004.
[86] RF-SEC-00178693.004.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

Based on the lack of actual trades, Bruce Sr. recommended that the Board value the Lehman holdings at par until "we get some sort of substance out of the marketplace."[87] The Board rejected Bruce Sr.'s recommendation. In accord with the recommendation of the counsel to the Independent Trustees, the Trustees applied their best efforts to "come up with a price that represents the value at which something could be sold at any particular day."[88] Recognizing that there were no market prices available for Lehman debt,[89] the Board considered the indications of market interest "anywhere from 40 to 90" as relevant data,[90] while recognizing also that "there is no, there's no trades out there, there is no transactions . . . ."[91] The Board then concluded: "given that the securities are illiquid and not paying interest on a current basis, the securities needed to be valued at less than par . . . . After consideration of all factors they considered relevant, the Trustees determined that the Lehman paper should be valued at a 20% discount to par."[92] Bruce Sr. was persuaded to follow this approach. The Board further agreed to reconvene, at least daily, to the extent there were "any material events during the day that management thinks impact on the values" that the Trustees selected.[93] General market conditions continued to deteriorate, and there were no reported trades in Lehman debt on September 15 and 16.

The complete transcripts of the Bents' discussions with the Board demonstrate that Bruce Sr. and Bruce II provided the Board with accurate information relevant to the Board's valuation of the Fund's Lehman holdings.

---

[87] RF-SEC-00178693.004.

[88] RF-SEC-00178693.004.

[89] RF-SEC-00178693.004 (Statements by Trustees included the following: "If you had no ready market for it, if you had no trading taking place in the securities, you would never have carried it at par . . . carrying a non-marketable security – where there is nobody making a market and no bids – at par is definitely the wrong answer"); *see also id.* ("Bruce basically came to us and Patrick, the market, and tells us there is no market for this paper right now, we've got indications, but no bids, no offers, but we've got indications that run anywhere from 40 to 90").

[90] RF-SEC-00178693.004.

[91] RF-SEC-00178693.004.

[92] RF-SEC-00178717.

[93] RF-SEC-00178693.005.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000282

B. THE BENTS' REPRESENTATIONS TO THE BOARD REGARDING THEIR INTENTIONS TO SUPPORT THE NAV OF THE PRIMARY FUND WERE TRUTHFUL WHEN MADE

We next address the Staff's claim that Bruce Sr. and Bruce II were not truthful with the Board regarding the extent of their willingness to support the NAV of the Primary Fund. As we understand its view of the evidence, the Staff believes that Bruce Sr. and Bruce II failed to disclose to the Board at the 1:00 p.m. meeting on September 15, 2008 that they had preliminarily capped the amount of their proposed support to the Primary Fund at $10 million. The Staff concludes, with no documentary support, that the Bents understood, as of the 1:00 p.m. Board meeting, that they would have to quantify their support for the Primary Fund upon the execution of a credit support agreement, that they had reached an agreed-upon view about the amount of their proposed support, and that the Bents were obliged to support the NAV of a money market fund. These conclusions are contradicted by the relevant evidence and applicable law.

1. THE BENTS' LIMITED UNDERSTANDING OF CREDIT SUPPORT AGREEMENTS SHAPED THEIR EXPECTATIONS ABOUT THE ARRANGEMENT FOR THE PRIMARY FUND

As of September 15, 2008, the Bents previously had supported the NAV of one, and only one, other fund – the Enhanced Cash Strategies Portfolio, LLC ("Enhanced Cash Fund").[94] The Enhanced Cash Fund is a Delaware limited liability company whose investment objective seeks to invest and reinvest the assets of each Series in investment securities and other property to achieve as high a level of current income as is consistent with the preservation of capital and liquidity. It is not a money market fund and the offering documents for the Enhanced Cash Fund disclose that its $1.00 share price may fluctuate. At or about the summer of 2007, and in part due to liquidity problems in the markets, the Enhanced Cash Fund began to have difficulty

[94] Deposition of Bruce II, dated Nov. 3, 2008, at 96:5-11.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

maintaining its $1.00 per share NAV.[95] The Bents believed that RMCI's reputation for managing funds with a stable $1.00 NAV could be injured if the Enhanced Cash Fund deviated from $1.00 per share. They, therefore, decided that they would support the NAV of the Fund.

RMCI's General Counsel Kate Crowley prepared the documentation for the credit support agreement. Crowley determined that, because the Enhanced Cash Fund was a private partnership, neither SEC nor board approval was required for the Bents to support the Fund's NAV. As drafted, the agreement did not require the creation of an escrow on behalf of the Fund, and it had no provision specifying the amount of support that the Bents would be expected to provide the Fund. Rather, the support obligation was at-will, "for as long as [the Bents] wanted to have it in place, and while it was in place, we were constantly committing further capital to support on an as-needed basis to protect the dollar."[96] Throughout the Fund's 2007 fiscal year, the Bents' commitment to the Fund was expressed in the form of a receivable, which fluctuated in size until the end of the fiscal year, at which point the Bents were required to make a cash payment to cover the Fund's realized losses. The Fund's accountant, KPMG, audited this contribution to the Enhanced Cash Fund and footnoted the Bents' contribution to the Fund in the Fund's financial statements.[97]

Because of their prior experience with the Enhanced Cash Fund, the Bents reasonably did not anticipate that they would have to quantify their support for the Primary Fund at the outset and had no expectations about the amount of their contribution until their counsel advised them that the credit support agreement would take the form of an escrow agreement, and conveyed that Robert Plaze, Associate Director for the SEC Division of Investment Management,

---

[95] Deposition of Bruce II, dated Nov. 3, 2008, at 96:12-98:8.

[96] Deposition of Bruce II, dated Nov. 3, 2008, at 98:18-99:5.

[97] As of December 31, 2007, the Bents agreed to reimburse the Enhanced Cash Fund in the amount of $6,510,592. Declaration of Bruce II, dated January 23, 2009, at ¶ 7.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000284

suggested inserting an escrow amount of $10 million, in the first instance, into the credit support agreement which would be used to support the Primary Fund NAV rather than the value of the Lehman debt.[98] Indeed, until the call with the SEC Division of Investment Management, the Bents were unaware that there were three alternative forms of support arrangements that the SEC Staff would approve.[99] For this, and the additional reasons discussed below, there is no factual basis for concluding that the Bents misrepresented the extent of their commitment to the Primary Fund at 1:00 p.m. on September 15, when they requested the Board's consent for RMCI to pursue a credit support agreement for the Primary Fund.

2. THE BENTS DID NOT HAVE DETAILED INFORMATION ABOUT THE TERMS OF A CREDIT SUPPORT AGREEMENT FOR THE PRIMARY FUND WHEN THEY MET WITH THE BOARD AT 1:00 P.M. AND, FOR THAT REASON, DID NOT CONCEAL MATERIAL TERMS OF THE AGREEMENT FROM THE BOARD

Late morning on September 15, with the Lehman holdings valued at 80% of par, the Primary Fund did not appear in immediate danger of trading at less than $1.00 per share. The Bents, however – aware of the unprecedented market conditions and extreme credit crunch – decided proactively to commit the resources of the management company to support the NAV of the Primary Fund.[100] The Bents delegated to RMCI's in-house counsel the responsibility for identifying the appropriate credit support arrangement for a money market fund.[101] Consistent

[98] *See* Section I.B.2, *infra*.

[99] Deposition of Bruce II, dated Nov. 3 2008, at 138:20-139:8; 153:21-155:6.

[100] RF-SEC-00187436; Deposition of Bruce Sr., dated Nov. 20, 2008, at 87:6-11; Deposition of Bruce II, dated Nov. 3, 2008, at 132:5-9; Deposition of Arthur Bent, dated Dec. 11, 2008, at 51:20-52:10.

[101] Deposition of Bruce II, dated Nov. 3, 2008, at 143:1-12 ("Q: You told us that in the course of the discussion with the SEC someone from the SEC said hey, there's different ways to structure a credit support agreement, right? A: Yes. Q: Okay. And the question I have is what prompted them to make that observation? Did somebody from The Reserve side say we're thinking generically about a credit support agreement? A: Essentially, yes. That was a big part of bringing it up with them was to...get details. And ultimately that was left with Kate to work directly with the SEC to figure out okay, exactly what do we want to do here").

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

with Section 17(b) of the Investment Company Act,[102] the Bents sought Board authorization to approach the SEC about supporting the Primary Fund's NAV.[103] RMCI promptly scheduled an emergency 1:00 p.m. Board meeting. The Trustees thereafter provided RMCI authorization to "contact the staff of the Commission *to inquire about implementing a credit support agreement for the Primary Fund*."[104]

At the 1:00 p.m. meeting, neither the Bents nor the Trustees discussed their expectations as to the content of a final credit support agreement. Instead, the Trustees conditioned their final approval for a support agreement on receipt of a final agreement that they determined would be in the best interests of the Fund's shareholders.[105] In other words, the Trustees authorized RMCI to pursue the *possibility* of a credit support agreement, while reserving their right to approve or disapprove of the final arrangement.

The Bents formulated their proposal to advance $10 million to support the NAV of the Primary Fund several hours after the 1:00 p.m. Board Meeting.[106] The following developments affected their proposal:

- At approximately 1:10 p.m., Bruce II, Goldberg, DiMartino, and Crowley called the SEC Division of Investment Management, whose Staff discussed the forms of credit support agreements that would be acceptable to the Division Staff.[107]

---

[102] Section 17(b) of the Investment Company Act provides that "Notwithstanding subsection (a) [setting forth prohibited transactions, including the loaning of money by an affiliated person of a registered investment company to that registered investment company], any person may file with the Commission an application for an order exempting a proposed transaction of the applicant from one or more provisions of that subsection."

[103] RF-SEC-00178718.

[104] RF-SEC-00178719.

[105] RF-SEC-00178719.

[106] Bruce Sr. did not have a good recollection as to how he came to agree that $10 million was the appropriate level of support for the agreement. Deposition of Bruce Sr., dated Oct. 29, 2008, at 76:1-22, 194:9-20; Deposition of Bruce Sr., dated Nov. 20, 2008, at 56:1-25. Bruce II's recollection was similarly vague. Deposition of Bruce II, dated Nov. 3, 2008, at 158:8-160:21. Documentary evidence confirming that the agreement would take the form of an escrow commitment suggests that the $10 million was formulated sometime in the afternoon on September 15. *See* RF-SEC-WH-00000003-13; RF-SEC-WH-00000014-18; RF-SEC-WH-00000019-20; RF-SEC-WH-00000049-56.

Confidential Treatment Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

- At 3:16 p.m. Robert Plaze, Associate Director for the SEC Division of Investment Management, sent RMCI's attorneys a template for an agreement that would require RMCI to contribute capital to an escrow account that would be accessed if the Fund recognized a loss on its Lehman securities.[108] In discussions relating to the escrow agreement, the Staff suggested that RMCI contribute $10 million to that escrow account.[109] RMCI's General Counsel informed Bruce II that the SEC Staff had proposed an escrow account and suggested $10 million in the first instance. Bruce II agreed that RMCI would fund the escrow account in that amount.[110]

- Between 4:30 p.m. and 7:30 p.m., Goldberg and DiMartino provided drafts of the Credit Support Agreement and drafts of the accompanying No-Action Letter to Crowley for review and approval.[111]

A close analysis of this chronology of the discussions among the Bents, their counsel, the Board, and the SEC Staff for the Division of Investment Management confirms that the Bents did not appreciate that a specific level of commitment would be required in a credit support agreement until hours after RMCI first presented the issue to the Board. The Bents' failure to discuss a particular level of commitment, in context, was not based on any intent to deceive the Board, but rather simply on the lack of knowledge that such specificity would be required.[112] The Bents cannot be liable for failing to disclose facts they did not know or reasonably appreciate.[113]

---

[107] Deposition of Bruce II, dated Nov. 3, 2008, at 138:20-139:1 ("[A]t some point after speaking with the trustees about the concept and after getting their permission and going to the SEC to discuss the concept further, we learned from the SEC that there were a few types of credit support agreements and they asked us which one we were interested in doing and we said we did not know and could they educate us on the different types").

[108] RF-SEC-WH-00000049-56.

[109] RF-SEC-WH-00000019-20.

[110] Deposition of Bruce II, dated Nov. 3, 2008, at 139:5-11.

[111] RF-SEC-WH-00000014-18; RF-SEC-WH-00000021-28.

[112] Similarly, the Bents did not fail to disclose to the Board that $10 million constituted the maximum amount they would contribute. Prior to 4:30 p.m., there is no indication that the Bents had contemplated a $10 million level of commitment. That number first appears in a draft of the no-action letter seeking exemptive relief more than three hours after the board meeting. RF-SEC-WH-00000014-18.

[113] *Novak v. Kasaks*, 216 F.3d 300, 309 (2d Cir. 2000) ("Corporate officials need not be clairvoyant; they are only responsible for revealing those material facts reasonably available to them."); *In re Peritus Software Servs., Inc. Sec. Litig.*, 52 F. Supp. 2d 211, 227 (D. Mass. 1999) ("The securities laws mandate disclosure — not clairvoyance.").

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

3. Bruce Sr.'s Statement That Sufficient Capital Could Be Made Available Was Truthful when Made, Did Not Deceive the Board, and Did Not Result in Any Different Action by the Board than It Would Otherwise Have Taken

We turn now to the Staff's claim that Bruce Sr. deceived the Board when he stated that his family could provide "sufficient capital" to support the NAV of the Primary Fund. Although there is no legal obligation to support the NAV of a money market fund, the Staff treats the Bents' failure to do so as a breach of fiduciary duty, and any statements about support that fall short of this supposed legal obligation as fraud. The Staff has no theory to explain why Bruce Sr. would have any motive to deceive the Fund's Board regarding the level of support he was financially able to contribute, or more importantly, whether the Trustees would have withheld their consent for RMCI to consult the SEC Division of Investment Management about a credit support agreement in the event that they better appreciated that the Bents eventually would agree to put $10 million in escrow to support the Primary Fund.

We note, firstly, that Bruce Sr.'s statement regarding the sufficiency of family capital to support the Primary Fund was truthful when he sought Trustee consent to support the NAV of the Primary Fund. As of 1:00 p.m., redemption volume did not pose an imminent threat to the Primary Fund's NAV. At the time, the Fund had a $13.5 billion redemption cushion before redemptions would cause the NAV of the Fund to decline below $1.00 per share.[114] The Bents were not aware of any problems filling redemptions, market developments continued to evolve, and management had pending requests for assistance to government agencies. Bruce Sr. had no reason to believe that circumstances would progress to the point where the capital required to

[114] Bruce Sr. testified that on the afternoon of September 15, with Lehman valued at $0.80, the Primary Fund could withstand $30 billion of redemptions before it broke the buck. *See* Deposition of Bruce Sr., dated Nov. 20, 2008, at 34:11-14 ("I did an analysis that if the Lehman value stayed at – did not go below 80 and the redemptions in the fund did not exceed 30 billion, we would not break the buck. That was a calculation that I did."). RMCI advised the Board of Trustees in the 1:00 p.m. meeting that as of the beginning of the meeting, redemption requests totaled approximately $16.5 billion. *See* RF-SEC-00178718.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

support the Primary Fund would exceed Reserve Management Corp.'s financial capability.[115] Nor were the Trustees deceived by Bruce Sr.'s characterization of his family resources. The Board received detailed financial statements from RMCI during each 15(c) review of the investment advisory agreements. The Board was sophisticated and informed about RMCI's financial resources, and had been for many years.[116] The Trustees could not have interpreted Bruce Sr.'s statement that RMCI could make sufficient capital available to provide credit support for the Primary Fund to imply an unconditional, limitless commitment up to and including the full $785 million par value of the Lehman holdings. Both the audience that received the statement, and the context in which Bruce Sr. briefly mentioned his willingness to provide capital support for the Primary Fund, confirm that Bruce Sr.'s statement was truthful and made in good faith.[117]

The Staff, at best, views the candor of Bruce Sr.'s statement about capital resources through the lens of hindsight, with full knowledge regarding redemption levels on the afternoon

---

[115] On September 15th and 16th, the Bents were prepared to commit far more than $10 million to save their business. Deposition of Bruce Sr., dated Nov. 20, 2008, at 81:21-23 (noting that $100 million could have been made available to support the Fund from personal and RMCI resources, depending on circumstances). Indeed, even when the $10 million threshold was established (hours after the Board Meeting), it was subject to enlargement at the Bents' discretion. Deposition of Bruce II, dated Nov. 3, 2008, at 158:25-159:4 ("I believe that if we hit that threshold [$10 million] then we would need to decide if we wanted to go further."). Furthermore, efforts were ongoing to seek governmental support and/or a strategic partner for the Fund, both of which would provide additional sources of liquidity for use in connection with the NAV backstop. Deposition of Bruce Sr., dated Nov. 20, 2008, at 92:15-93:14; Deposition of Bruce II, dated Nov. 3, 2008, at 141:1-10.

[116] Deposition of Bruce Sr., dated Nov. 20, 2008, at 79:13-17 ("The resources of the management company were well aware – the board was well aware of those resources. We had just gone through a management contract review. So what our earnings were, what our balance sheet was, they were aware of it").

[117] *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 206 (1976) (scienter requires conduct other than that made in good faith); *Howard v. SEC*, 376 F.3d 1136, 1147 (D.C. Cir. 2004) ("good faith [is] a relevant consideration in evaluating a defendant's scienter"); *Alvin W. Gebhart, Jr.*, Exchange Act Release No. 34-58951, 2008 WL 4936788 (Nov. 14, 2008) ("evidence of good faith [is] relevant to a determination of whether a respondent acted with the requisite state of mind").

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

of September 15, and continued deterioration of the credit markets. It is well established that hindsight does not amount to fraud.[118]

Second, there is no reason to believe that the Trustees would have withheld their consent from RMCI to consult the SEC Division of Investment Management about a credit support agreement in the event that they better appreciated that the Bents eventually would agree to put $10 million in escrow to support the Primary Fund.[119] As of 1:00 p.m., the Trustees, like the Bents, understood that neither redemption levels nor the price of Lehman had caused the Fund to trade at less than $1.00 per share. Even if the Bents had appreciated that they would be required to create an escrow account for the benefit of the Primary Fund, and further had agreed at 1:00 p.m. that they would be prepared to fund the account up to $10 million, it is highly unlikely that the Trustees would have rejected that offer. On behalf of Fund shareholders, the Trustees would not have refused to consent to RMCI's pursuit of a credit support agreement.

---

[118] *Novak v. Kasaks*, 216 F.3d 300, 309 (2d Cir. 2000) ("[W]e have refused to allow plaintiffs to proceed with allegations of 'fraud by hindsight' . . . . allegations that defendants should have anticipated future events and made certain disclosures earlier than they actually did do not suffice to make out a claim of securities fraud"); *Sundstrand Corp. v. Sun Chemical Corp.*, 553 F.2d 1033, 1045 n.19 (7th Cir. 1977) (whether a statement was made with the requisite intent "is an objective test although the circumstances must be viewed in their contemporaneous configuration rather than in the blazing light of hindsight"); *Kevin Hall*, Initial Decisions Release No. 341, 2008 SEC LEXIS 82, at *65 (Jan. 15, 2002) ("Respondents' conduct must be compared with actions a reasonable accountant would have taken at the time of the audit and review, without the benefit of hindsight"); *Jay Houston Meadows*, Admin. Proc. File No. 3-8257, 1994 SEC 2874 at *42 (Sept. 19, 1994) ("Fraud by hindsight, moreover, is not sufficient to establish the mental state required for a violation of Section 10(b)").

[119] Materiality is determined by the importance attached to the information by those who knew about it. *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 851 (2d Cir. 1968). Here, the Board voted to authorize RMCI to consult with the SEC about the possibility of executing a credit support agreement. Even if the Bents had known and disclosed that the credit support agreement would be limited to $10 million, it is unlikely that the Board would give weight to that limitation when deciding whether to authorize RMCI to enter into discussions with the SEC. Where allegedly omitted information would not assume actual significance in voting deliberations, it cannot be material. *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976) ("An omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote [in a proxy contest] . . . . [It requires] a showing of a substantial likelihood that, under all the circumstances, the omitted fact would have assumed actual significance in the deliberations of the reasonable shareholder."); *see also Resnik v. Swartz*, 303 F.3d 147 (2d. Cir 2002).

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000290

4. INVESTMENT ADVISERS ARE NOT LEGALLY OBLIGED TO SUPPORT THE NAV OF MONEY MARKET FUNDS

The Bents have explained that their reason for deciding to support the Primary Fund's NAV was not the result of any legal obligation, but rather their belief that a demonstration of their own commitment to the Fund would be meaningful to Fund investors confronted with a turbulent and uncertain market.[120] No legal obligation to support the Fund exists. While money market funds attempt to maintain a stable per share net asset value, such stability is not guaranteed, and the adviser is under no legal obligation to provide any financial support to maintain the fund's net asset value. An adviser's fiduciary duty neither dictates the steps an adviser must take to achieve stated investment objectives nor requires an adviser to reach specific investment results. An investment adviser has a fiduciary duty to exercise good faith and make full and fair disclosure of all material facts, and an affirmative obligation to employ reasonable care to avoid misleading its clients.[121] However, an adviser's fiduciary duty does not extend to the eventual success of its recommendations.[122] It is axiomatic that an adviser is not required to guarantee the net asset value of a money market fund – there is simply no authority for the proposition that RMCI violated section 36(a) of the Investment Company Act or Section

[120] *See, e.g.* Deposition of Bruce II, dated Nov. 25, 2008, 142:14-143:13 ("I thought that this would be something that would give them [institutional investors] confidence. Again, I'm under the impression this is not a credit problem, this is a crisis of confidence issue").

[121] *SEC v. Treadway*, 430 F. Supp. 2d 293, 338 (2006) (describing an adviser's fiduciary obligations under Section 206) (citing *SEC v. Moran*, 922 F. Supp. 867, 895-96 (S.D.N.Y. 1996), *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11, 17 (1979), *Burks v. Lasker*, 441 U.S. 471, 482 n.10 (1979), *Santa Fe Indus., Inc. v. Green*, 430 U.S. 462, 472 n.11 (1977), *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 191-92 (1963). *See also Strougo ex rel. Brazil Fund v. Scudder, Stevens & Clark, Inc.*, 964 F. Supp. 783, 797 (S.D.N.Y. 1997), *vacated in part on other grounds*, 282 F.3d 162 (2d Cir. 2002) (stating that "Section 36(a) embodies a Federal common law of fiduciary obligations").

[122] *See, e.g., Jones Mem'l Trust v. Tsai Inv. Servs., Inc.*, 367 F. Supp. 491, 497, 500 (S.D.N.Y. 1973) (stating that an adviser's fiduciary duty under Section 206 does not obligate an adviser to "prevent any decline in the client's portfolio").

In addition, in the context of shareholder fraud suits, federal courts have held that when the fund's disclosures sufficiently described the risks of investment, an adviser cannot be held liable for making investment decisions that in hindsight were simply not wise. *Olkey v. Hyperion 1999 Term Trust, Inc.*, 98 F.3d 2 (2d Cir. 1996).

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000291

206 of the Investment Advisers Act by failing to support financially the net asset value of the funds, and the Staff has cited none. In fact, both SEC pronouncements and the entire disclosure and regulatory regime for investment companies belie the existence of any such duty.

SEC Staff and Commission statements recognize that there is no legal obligation for an adviser to support a fund's net asset value. For example, in a recent SEC statement regarding the crisis facing money market funds, the Commission observed that financial support for money market funds from the adviser will occur only "in some cases."[123] Implicit in that statement is the absence of any legal requirement imposing a duty on advisers to support money market fund net asset values, and an acknowledgement that in many cases the adviser in fact will not provide financial support for money market funds. In 1997, the Director of the Division of Investment Management expressed concern regarding the growing misconception that an adviser will necessarily provide a cash infusion when a fund experiences a loss in its portfolio.[124] The Director noted that this expectation was in conflict with the SEC's required disclosures that investing in a money market fund involved an inherent risk that the net asset value per share could fall below $1.00.[125] Similarly, in its guidance regarding money market fund disclosures, the Staff previously had indicated that investors should be clearly warned that the stable net asset value of a money market fund is not assured. Specifically, in its 1992 Generic Comment Letter, the Staff stated that the following disclosure should be placed on the cover page of a money market fund's prospectus:

---

[123] *Temporary Exemption for Liquidation of Certain Money Market Funds,* Investment Company Act Rel. No. 28487, 2008 SEC LEXIS 2629, at *6 (Nov. 20, 2008) (indicating that "[t]he risk-limiting conditions built into rule 2a-7, together with the management skill and, ***in some cases***, the financial commitment of the advisers that sponsor money market funds, have contributed to the stability of money market funds for more than 30 years") (emphasis added).

[124] Barry Barbash, Director of the Division of Investment Management, SEC, Address at the 1997 Investment Company Institute General Membership Meeting (May 16, 1997), available at: http://www.sec.gov/news/speech/speecharchive/1997/spch158.txt (last visited Jan. 20, 2009).

[125] *Id.*

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000292

> If a registrant holds itself out as a money market fund, Item 1(a)(vi) of Form N-1A requires the outside cover page of the prospectus to contain a prominent statement that (A) an investment in the fund is neither insured nor guaranteed by the U.S. Government and (B) there can be no assurance that the fund will be able to maintain a stable net asset value of $ 1.00 per share (or, if other than $ 1.00, the applicable net asset value).[126]

Such prominent warnings would not be necessary if the adviser was under an obligation to guarantee the net asset value of each share.

Perhaps as equally telling as the affirmative statements of the Commission and its Staff is what the Commission and its Staff have *not* required. If a financial commitment by the adviser to support money market fund net asset values were required by law, it is implausible to believe that detailed prospectus disclosure about the scope, terms, and effect of the guarantee would not be required in money market fund prospectuses. Among other things, the adviser's own financial condition and ability to make good on such guarantees would be material disclosure items and would have to be included in money fund prospectuses. The current disclosure regime would be wholly inadequate if advisers were, in fact, required to support money fund net asset values.

Here, the money market funds advised by RMCI comply with applicable disclosure requirements, including the SEC Staff's prior pronouncements. The prospectuses and Statements of Additional Information expressly disclose the risk that shares in any of the funds could be worth less than $1.00 per share. For example, the Primary Fund Prospectus states:

> An investment in [The Primary] Fund is not insured or guaranteed by the U.S. government, FDIC or any other government agency. Although each Fund seeks to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in a Fund.[127]

---

[126] Generic Comment Letter, SEC No-Action Letter, 1992 SEC No-Act. LEXIS 1120 at *6 (Jan. 17, 1992) (emphasis added).

[127] Primary Fund Prospectus at 5.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000293

The Statement of Additional Information similarly discloses that "SHARES OF THE FUNDS ARE NEITHER GUARANTEED NOR INSURED BY THE U.S. GOVERNMENT, AND THERE CAN BE NO ASSURANCE THAT A FUND WILL BE ABLE TO MAINTAIN A STABLE NET ASSET VALUE OF $1.00 PER SHARE."[128]

For the foregoing reasons, Bruce Sr. and Bruce II were truthful with the Board regarding the extent of their willingness to support the NAV of the Primary Fund. Similarly, the Staff's assumption that the Bents were obliged to support the NAV of a money market fund is incorrect as a matter of law.

C. THE BENTS PROMPTLY INFORMED THE TRUSTEES THAT THE FUND HAD OVERDRAFTS AT STATE STREET BANK

In its next claim of alleged fraud, the Staff asserts that Bruce Sr. and Bruce II failed to provide real-time reports to the Board that the Fund had overdrafts at its custodian bank, State Street Bank. As is apparent in so much of the Staff's second-guessing of the Bents' response to an unprecedented crisis, the Staff assumes that management processes factual information instantaneously, and the Staff assumes further a legal obligation to provide reports to the Fund's Board at the moment of realization. Both assumptions are erroneous and provide no basis for asserting a fraud claim against the Bents. Bruce II received or sent 237 e-mails on September 15. On that same day, he attended more than three hours of Board meetings and provided concentrated attention between those meetings on efforts to enhance liquidity for Fund investors. The Staff's assumption that Bruce II read and contemporaneously synthesized all of the information provided to him by e-mail is contrary to human experience. Even assuming such perfect comprehension were possible, the timeline of the e-mails relating to overdrafts does not support the Staff's conclusion that Bruce II concealed information from the Board.

---

[128] Primary Fund Statement of Additional Information, dated Sept. 28, 2007, as supplemented through May 5, 2008, at Table of Contents.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000294

We address first the Staff's erroneous conclusion that Bruce II knew in advance of the 1:00 p.m. Board meeting on September 15 that State Street had stopped extending the Fund daylight overdraft protection. To the contrary, Bruce II did not learn that State Street had stopped extending daylight overdraft protection until several hours after the 1:00 p.m. teleconference with the Trustees. Sometime after 2:48 p.m., Bruce II received an e-mail that RMCI's Managing Director of Operations David Gareis and Drahzal needed to speak with him about the daylight overdraft situation.[129] During that discussion, Bruce II learned that RMCI had $8 billion in overdrafts at State Street and the bank was refusing to extend any further credit against the assets of the Primary Fund. As a result, State Street was no longer wiring cash to investors who had redeemed out of the Fund.[130] Having been uninformed about the situation prior to the 1:00 p.m. Board meeting, there is no support for the Staff's view that Bruce II concealed the development from the Board during the 1:00 p.m. call. The chronology, thus, does not support the Staff's conclusion that Bruce II withheld material information from the Fund's Board.

There is, however, ample evidence to suggest that Bruce II continued to manage State Street's refusal to send out customer wires. In particular, he sought additional overdraft protection at State Street – directly and through the Federal Reserve Bank of Boston – and explored alternative ways to ease the overdraft problem, including a reverse repurchase agreement with State Street.[131] Bruce II was diligently addressing the overdraft problem well

[129] RF-SEC-00099955; *see also* Deposition of Bruce II, dated Nov. 25, 2008, at 184:16-185:1. Bruce II testified that he became aware of the overdraft situation in the afternoon, and perhaps as late as the close of business on September 15. *See* Deposition of Bruce II, dated Nov. 13, 2008, at 175:8-23; Deposition of Bruce II, dated Nov. 25, 2008, at 184:16-185:1.

[130] Deposition of Bruce II, dated Nov. 25, 2008, at 184:15-185:1.

[131] *See, e.g.*, RF-SEC-00100004; RF-SEC-00099029-30; RF-SEC-00107587-89; *see also* RF-SEC-00107813.

Confidential Treatment Requested by WILMER CUTLER PICKERING HALE AND DORR LLP

after 6:00 p.m. on September 15.[132] Separately, Gareis continued to work with State Street as late as 7:45 p.m.[133]

Bruce II informed the Board about all of these efforts early in the morning on September 16:

> [Bruce] II informed the Trustees that from Monday morning through 9:00 AM on Tuesday morning, redemption requests from the Primary Fund totaled approximately $24.6 billion. The Primary Fund had been able to pay the proceeds of about $10.7 billion of that amount due to the illiquidity in the markets and the limits the Primary Fund's custodian put on overdrafts.[134]

In the face of prompt and detailed disclosure to the Board regarding overdrafts at State Street, the Staff maintains that a fraud charge is nonetheless appropriate because Bruce II's reports to the Board were not *contemporaneous* with his receipt of an e-mail (merely one of 237 e-mails that he sent or received on September 15) on the development of a fast-moving situation. The Staff cites no precedent supporting a requirement for instantaneous notification, and we are aware of none. To the contrary, in prior cases, charges involving alleged omissions to a fund board involved a protracted course of intentional conduct that impaired Board oversight over fund management over a period of years.[135] Here, by contrast, the Bents notified the Board about overdrafts at State Street at the next Board meeting, after the markets had next opened and less than 18 hours after Bruce II learned the information. Moreover, the Staff has no theory to explain how the timeliness of Bruce II's report to the Board affected any of the Board's decisions

[132] RF-SEC-00187438 (indicating that Bruce II spoke with Mr. Greene by telephone at 6:21 p.m.).

[133] RF-SEC-00060132-33.

[134] RF-SEC-00178720.

[135] *See, e.g., Massachusetts Financial Services Co.*, Investment Company Act Release No. 26409, 2004 WL 635594 (Mar. 31, 2004) (sanctioning fund investment adviser for failing to disclose to the fund board that the adviser had, for at least three years, allocated brokerage commissions in return for preferred treatment in promoting fund sales); *Fundamental Portfolio Advisors, Inc.*, Exchange Act Release No. 34-48177, 2003 WL 21658248 (July 15, 2003) (sanctioning investment adviser for failing to disclose to the fund board soft dollar arrangements that persisted for at least five years).

on September 15 and 16, or that the timing of Bruce II's report to the Board on the overdraft situation at State Street caused the Primary Fund to trade at less than $1.00 per share. Any failure by the Bents to provide real time reports to the Board is, therefore, immaterial in this context.

The Staff also asserts that the Bents failed to inform the Board that State Street had imposed a $1 billion overdraft limit on RMCI, and $9.5 billion of the overdraft protection it extended on the 15th was extended in error. We are not aware of any evidence that the Bents were aware that State Street took this position on September 16. The Bents cannot be liable for failing to disclose facts about which they were unaware.[136] Moreover, the Staff's conclusions about overdraft limitations at State Street are inconsistent with the Bents' understanding about the services provided by State Street. The reason that RMCI elected in the summer of 2008 to terminate its custody arrangement with JPMorgan Chase in favor of State Street is that State Street professed to have superior operational systems and bank officers represented that they would not impose a limit on daylight overdraft protection for a money market fund.

D. The Bents Were Under No Legal Obligation to Inform the Board That a Moody's Analyst Recommended That RMCI Create a Credit Support Agreement in the Event of a Credit Event

We next address the Staff's claim that the Bents deceived the Fund Board because they did not inform the Board that Henry Shilling of Moody's suggested in the summer of 2008 that RMCI create a credit support agreement in favor of the Primary Fund against the possibility of a future credit event. In the summer of 2008, the Bents met with Shilling and other Moody's representatives. Shilling requested the meeting, in part, to review RMCI's financial condition

---

[136] *Hershfang v. Knotter*, 562 F. Supp. 393, 399 (E.D. Va. 1983) ("defendants cannot be liable for not disclosing that which they could not possibly know . . . defendants can only be liable for not disclosing that which they should have known").

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000297

and to assess its credit processes in light of the Fund's increasing asset base.[137] Shilling asked the Bents to detail RMCI's resources for backstopping the NAV of a fund, in particular because RMCI did not have a corporate parent that might support the funds.[138] Although Bruce Sr. provided general information about his financial resources, he did not quantify the resources that RMCI would commit to the Primary Fund.[139] Indeed, Bruce Sr. made clear that any decision to support a fund's NAV would depend on the facts and circumstances.[140] With full knowledge that RMCI would not commit to fund a credit support agreement for the Primary Fund or Yield Plus Fund, Moody's did not downgrade the funds' ratings. The Bents did not report Shilling's proposal to the Board because they were under no obligation to do so where the discussions were not material to the Fund, as evidenced by Moody's maintenance of its previous rating.

The Staff's assertion that disclosure of the Shilling proposal was warranted appears based, in part, on the erroneous view that an investment adviser has a duty to support the NAV of the money market funds it manages. As discussed in detail above in Section B.4, investment advisers have no such duty. Moreover, we are unaware of any money market fund that has a pre-event credit support facility with its adviser. As a consequence, the assumption that the Bents had an obligation to inform the Board of the Shilling proposal because it would be material if RMCI was shirking a legal duty to support the Primary Fund NAV has no basis in law.

---

[137] Deposition of Bruce Sr., dated Oct. 29, 2008, at 57:15-59:1; Deposition of Bruce II, dated Nov. 3, 2008, at 108:12-18.

[138] Deposition of Bruce Sr., dated Oct. 29, 2008, at 64:22-66:11 ("The only thing that I think they persisted on was the fact that we're not Bank of America or equivalent"), 86:3-13; Deposition of Bruce Sr., dated Nov. 20, 2008, at 10:3-12:18, 26:6-8; ("I think the biggest concern [for Moody's] was that we didn't have a big parent"); Deposition of Bruce II, dated Nov. 3, 2008, at 111:4-23.

[139] Deposition of Bruce Sr., dated Nov. 20, 2008, at 10:3-14 ("We had a general discussion about the resources of Reserve Management and the Bent family. Specific plans, specific contract? No."); Deposition of Arthur Bent, dated Dec. 12, 2008, at 20:16-23 ("What was communicated was that we, we had some possibilities that could be considered but not that there were any, was anything that had been defined and clearly stated as something that was committed in the event of a liquidity event").

[140] Deposition of Bruce Sr., dated Nov. 20, 2008, at 16:3-15. Bruce Sr. declined to make any written or pre-emptive commitment of resources. *See id.* at 18:6-14.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000298

The Staff now seeks to bootstrap a conversation that proved immaterial to Moody's, into a material conversation that should have been disclosed to the Fund's Board. There is no legal basis for the Staff's position. The Board knew what resources were available to the Bents and that neither RMCI nor the Bents had entered into a pre-event credit support agreement. The fact that Moody's made such an inquiry and thereafter did not change the funds' rating or outlook despite the Bents' refusal to create a credit support agreement was immaterial to the Fund. Information about that discussion with Moody's would not have altered the "total mix" of information available to the Board. It was, thus, immaterial.[141]

E. THE BENTS HAD NO OBLIGATION TO DISCLOSE RMCI'S COMMUNICATIONS WITH THE RATING AGENCIES TO THE BOARD

The Staff contends that the Bents deceived the Trustees when they sought Board approval for RMCI to pursue a credit support agreement because they did not disclose that Ledford already had informed rating agencies that the adviser was planning to enter into credit support agreements. A fraud claim cannot be maintained on these facts because the Bents were unaware of the content of Ledford's statements. To the contrary, the rating agencies complained to Ledford that the Bents had not discussed a credit support agreement with them.[142]

Greater knowledge of Ledford's uninformed communications with the rating agencies would not, however, have altered the Bents' disclosures to the Board at the 1:00 p.m. meeting. Ledford acknowledged only that a credit support agreement was "in the works," had no detail as to the size of the agreement or its structure, and explained to the rating agencies that he was "not

[141] *Basic Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988) (information is material only where there is "a substantial likelihood that the disclosure of the . . . fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available") (quoting *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976)).

[142] The Bents had only one conversation with a rating agency representative prior to the 1:00 p.m. Board Meeting, at 9:16 a.m. on September 15. RF-SEC-00187437. Describing the call to Ledford less than an hour later, Shilling noted that "I suggested the Bents think about . . . a capital support agreement," and expressed concern that "while I think they [the Bents] understood what I was saying, there wasn't a sense of urgency there." RF-SEC-00162852.004.

necessarily in the loop."[143] The fact that Ledford had provided S&P limited, second-hand information about the contemplated credit support would have been immaterial to the Board. Indeed, the S&P representatives acknowledged the immateriality of Ledford's information, telling him that any ratings actions would focus on the agreement's details, including its form and the support level it provided, not the mere fact of its existence.[144]

F. THE BENTS WERE UNDER NO OBLIGATION TO DISCLOSE TO THE BOARD THE PRELIMINARY DISCUSSIONS THEY HAD WITH AN INVESTMENT BANKER REGARDING A POSSIBLE SALE OF THE ADVISER

The Staff is considering fraud charges because the Bents did not disclose all of the circumstances in which they might consider a sale of the Reserve advisory business to a hypothetical potential investor. The Staff points, in particular, to the content of an e-mail that Bruce II sent to his investment banker on September 16 stating that RMCI would not require buyers to support the NAV of the Primary Fund.[145] No charges should be brought because the information was immaterial at law. Bruce II had not identified any buyer on September 15 or 16, and had not set a price or conditions of sale. His correspondence with investment bankers who were trying to identify potential buyers was, at best, preliminary.

Although the preliminary nature of Bruce II's discussions with investment bankers did not require the Bents to notify the Fund Board, the Bents nonetheless disclosed their interest in finding a strategic partner. The Board minutes for the 10:00 a.m. meeting on September 16 report that the Bents had retained "an investment banker to try to find a strategic partner to acquire some or all of the assets of the Primary Fund or to purchase the adviser for negligible

[143] RF-SEC-001628252.015.

[144] RF-SEC-001628252.015 ("you're encouraged to send us [S&P] drafts . . . . You can check with specific criteria that may come up . . . . I don't want something to be signed sealed, delivered then have an issue with it").

[145] RF-SEC-00038031.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

consideration."[146] Details of the Bents' e-mail communications with their investment bankers were immaterial as a matter of law.[147]

II. RMCI STATEMENTS TO THE PUBLIC ABOUT THE BENTS' INTENTIONS TO SUPPORT THE PRIMARY FUND WERE NOT FRAUDULENT AS THEY WERE ACCURATE STATEMENTS OF THE FAMILY'S INTENTIONS

In the Staff's view, RMCI and the Bents made untruthful statements to investors and potential investors about the Bents' intentions to support the NAV of the Primary Fund. Among the alleged falsehoods or omissions are the following: (i) speculation from Ledford to the rating agencies that the Bents could pay hundreds of millions of dollars to support the Primary Fund NAV; (ii) an internal e-mail from Bruce II to key employees, including RMCI's general counsel, expressing RMCI's commitment to support the Primary Fund "to whatever degree is required"; and (iii) a draft statement for investors, called *Reserve Insights*, that RMCI senior executives did not approve for distribution. In our view, there is no basis for fraud charges because the Bents did not intend to deceive investors, sought legal advice with respect to RMCI's disclosures, and

[146] RF-SEC-00178721.

[147] With respect to contingent or speculative events, materiality depends on "a balancing of both the indicated probability that the event will occur and the anticipated magnitude of the event in light of the totality of the company activity." *Basic, Inc. v. Levinson*, 485 U.S. 224, 238 (1988) (quoting *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 849 (2d Cir. 1968)). Even though the possible sale of RMCI was an event of potentially large magnitude, on September 15 and 16 the likelihood of such a transaction was so remote as to be virtually insignificant within the total mix of information available to the Board. Indeed, Bruce II had not even identified a potential buyer or entered into any negotiations with one. *See Carlin Equities Corp. v. Offman*, No. 07-Civ-359(SHS), 2008 WL 4387328, at *10-*11 (S.D.N.Y. Sept. 24, 2008) (finding allegedly withheld information immaterial as a matter of law where defendant had no actual negotiations with potential buyers or investors, but one unsuccessful meeting with a potential buyer, two fruitless "sales calls" made through an investment banker, and a meeting with a potential replacement for the investment banker). While prior cases have held that even failed negotiations over a transaction may be material, *see, e.g., Castellano v. Young & Rubicam, Inc.*, 257 F.3d 171, 182 (2d Cir. 2001) (finding materiality an issue of fact where defendant had serious merger negotiations with third party and, after the negotiations failed, continued to pursue corporate restructuring options); *Vacold LLC v. Cerami*, No. 00 Civ. 4024 (AGS), 2002 WL 193157, at *8 (S.D.N.Y. Feb. 07, 2002) (materiality of negotiations undertaken between defendant and third party depended on "how close or how far apart the parties were"), here there were no negotiations. *See Carlin Equities Corp.*, 2008 WL 4387328, at *11.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

investors were in fact not deceived about the Bents' commitment to the Fund.[148] For these same reasons, the Bents cannot be personally liable for fraud or for aiding and abetting any alleged falsehoods or omissions by RMCI. We discuss each allegation below.

A. LEDFORD'S UNAUTHORIZED STATEMENTS TO THE RATING AGENCIES DID NOT DECEIVE THOSE AGENCIES AND DID NOT AFFECT THE RATINGS FOR THE PRIMARY FUND

We turn first to the Staff's claim that Ledford provided misleading statements to Moody's and S&P about RMCI's intention to enter into a credit support agreement. No fraud charges can be justified against the Bents for two reasons. First, Ledford's statements had no indicia of reliability, and the rating agencies were not deceived by them. Indeed, from his first call with S&P at 12:30 p.m. on September 15, 2008, S&P plainly understood that Ledford had no first-hand information about the content of the agreement. Second, there is no evidence that the Bents knew of Ledford's statements.

With respect to Ledford's statements, the following transcript is illustrative:

Ledford: The Bents are in the process of putting something together so they're gonna provide the backdrop . . . the backstop for our holdings. I'm not sure the vehicle they're going to use. But, that's definitely in the works right now.

Shaw: Some sort of capital support agreement?

Ledford: Yeah, exactly. Because we have to have that.[149]

Ledford acknowledged that he was "not necessarily in the loop," and, when asked to provide detail about the form and amount of the contemplated support, confessed: "I just don't know all the details."[150]

---

[148] In addition, the Bents could not be liable for alleged violations of Section 206 of the Investment Advisers Act by RMCI employees. The Investment Advisers Act does not contemplate control person liability for violations of Section 206. 15 U.S.C. § 80b-6. *See* 15 U.S.C. §§ 80b-1 to -21. Where control person liability might otherwise be appropriate, the SEC has attempted to rely on primary liability (*see, e.g. SEC v. Moran*, 922 F. Supp. 867, 897 n.23 (S.D.N.Y. 1996)) or aiding and abetting liability (*see, e.g. Monetta Fin. Servs., Inc. v. S.E.C.*, 390 F.3d 952, 956-57 (7th Cir. 2004)).

[149] RF-SEC-00162852.014.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000302

For their own part, the Bents did not discuss their intention to enter into a credit support agreement with the rating agencies until after the Trustees authorized RMCI to pursue an agreement, and after RMCI had obtained SEC authority to inform investors that they intended to enter into an agreement.[151] In this regard, Bruce II can be heard on the Ledford audiotape recordings as stating: "I have got another meeting with the Trustees in two minutes, then I'm gonna be with the SEC. And, provided that everything works out the way we'd like it to, then I will call S&P."[152]

Second, the Bents' lack of knowledge independently precludes the Staff's effort to impute personal liability to the Bents for Ledford's comments to the rating agencies. We note in this regard that there is no evidence that the Bents knew any details of Ledford's conversations with S&P. Indeed, in his e-mail to Bruce II, Ledford noted only that S&P had inquired about a capital support arrangement, without acknowledging that he had represented that the Bents were pursuing one.[153] There is no basis for imputing liability for statements that the Bents neither knew about nor authorized.[154]

---

[150] RF-SEC-00162852.014.

[151] While the Bents also spoke to a Moody's representative at 9:16 a.m., at that time, Shilling merely raised with the Bents the possibility of a credit support agreement, and did not elicit a commitment from them to implement one. *See* RF-SEC-162852.004 (Shilling "suggested the Bents think about . . . a capital support agreement"). Only later that morning did the Bents determine to pursue a credit support agreement, and only after discussing the issue with the Fund's Board and the S.E.C. did the Bents disclose their intent to the rating agencies. *See* RF-SEC-00162852.016 ("I cannot call S&P now actually . . . I have got another meeting with the Trustees in two minutes, then I'm gonna be with the SEC. And, provided that everything works out the way we'd like to, then I will call S&P"). *See also* RF-SEC-00187437 (phone records indicate 1:22 p.m. call with Moody's).

[152] RF-SEC-00162852.016.

[153] RF-SEC-00107152-53 ("I gave them [S&P] an update on our situation. Similar to Henry Shilling at Moody's, they are looking for some type of capital support facility to be [put] in place"). At 5:18 p.m. on September 15, Ledford told Bruce Sr., "The CSA, the capital support agreement that apparently, is going out though, all the institutional clients so that's gonna help tremendously and it also went out to Moody's and S&P so they're all set, they're fat and happy tonight." Bruce Sr. replied, "Okay, very good." RF-SEC-00000443.020. Ledford did not inform Bruce Sr. of the details of his conversations with the ratings agencies or provide any further information about what disclosures the ratings agencies had received.

[154] *SEC v. KPMG LLP*, 412 F. Supp. 2d 349, 375-76 (S.D.N.Y. 2006) (control person liability requires showing that "defendant was sufficiently responsible for the statement – in effect, caused the statement to be made – and knew or had reason to know that the statement would be disseminated to investors").

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000303

B. BRUCE II'S EXPRESSION OF COMMITMENT TO THE $1.00 NAV FOR THE PRIMARY FUND TO KEY EMPLOYEES WAS AN ACCURATE STATEMENT OF HIS SUPPORT FOR THE FUND AND WAS NOT INTENDED TO DEFRAUD INVESTORS

The Staff next claims that a draft e-mail that Bruce II prepared for consideration by his Directors of Sales and Marketing, and provided for review and legal advice to his in-house General Counsel, was intended to deceive investors in the Primary Fund. The draft e-mail cannot form the basis of a fraud charge as it accurately reflected the extensive support Bruce II was prepared to provide the Primary Fund, and further reflects consultation with counsel as to the propriety of the expression of his support.

The following e-mail, which Bruce II copied to his General Counsel, forms the basis of the Staff's claim for fraud:

> Re: Protecting NAV on Primary
>
> We (Reserve Management Company Inc.) intend to protect the NAV on the Primary fund to whatever degree is required. We have spoken with the SEC and are waiting [for] their final approval which we expect to have in a few hours. You may communicate this to clients on an as needed basis...[155]

This e-mail accurately reflects Bruce II's commitment to Primary Fund shareholders at the time he prepared it. As of 1:19 p.m. on September 15, the Primary Fund had no immediate need for capital support from the Bents. The Board had priced Lehman debt at 80% of par, a price which did not cause the NAV of the Fund to trade at less than $1.00 per share. Redemptions had not reached a level that would have caused the NAV to fall below $1.00. Thus, a capital support agreement – even at the $10 million level that the Bents eventually proposed – was sufficient to support the Fund's NAV at the time that Bruce II drafted his statement of intention.

We note, however, that the Bents' willingness to provide capital support for the Fund was only one form of financial support that RMCI was prepared to make on behalf of Fund

[155] RF-SEC-00203655.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000304

shareholders. A potentially larger financial contribution, of course, was the Bents' willingness to sacrifice strategic control of their Company – and perhaps sell the Company for much less than the $600 million that buyers previously had bid to the Bents[156] – so that the proceeds could be used to support the Fund's NAV.[157] That significant undertaking amply reflects Bruce II's commitment to support the Primary Fund "to whatever degree is required." The Staff's narrow focus on the eventual size of the credit support agreement – without regard to the amount of capital required at 1:00 p.m. *or* the Bents' willingness to sell their Company to support the Primary Fund's NAV – fails to capture the level of support that the Bents were prepared to make.[158]

Bruce II's consultation with Crowley on the language he used in his e-mail further refutes any intention to deceive. Crowley had been on the SEC call shortly after 1:00 p.m. on September 15, had legal responsibility to oversee the preparation of the credit support agreement, and was or subsequently became aware that the SEC had suggested RMCI enter into a credit support agreement that required it to fund an escrow account in a specific amount – for example, $10 million. Bruce II plainly sought Crowley's advice on the disclosure; indeed Crowley e-mailed Lansky and Drahzal ten minutes later, "We haven't entered into the agreements yet; that's why Bruce's e-mail said we intend to. We will submit a form of the agreement to the SEC this afternoon for its review and approval which we expect to obtain."[159] Moreover, Bruce II emphatically cautioned in a subsequent e-mail that Crowley was to review and approve public

---

[156] Deposition of Bruce Sr., dated Oct. 29, 2008, at 61:1-62:14 (noting that offers for the company had reached $600 million).

[157] Deposition of Bruce II, dated Nov. 3, 2008, at 163:16-24; Deposition of Bruce II, dated Nov. 25, 2008, at 103:10-105:20, 110:6-9; RF-SEC-00107903.

[158] Good faith is inconsistent with an intention to defraud. *See Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 206 (1976) ("There is no indication that Congress intended anyone to be made liable for [an alleged misstatement] unless he acted other than in good faith.").

[159] RF-SEC-WH-00000040-42.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

disclosures (in accordance with existing standard practice) before they were submitted for final approval.[160] Bruce II's practice of seeking out Crowley's advice, and relying on that advice, further evinces the good faith with which he wrote and disseminated an internal e-mail.[161]

We understand that the Staff believes that the RMCI sales force exaggerated the status of the credit support agreements.[162] There is no evidence that the Bents were aware of the exaggerated statements or approved them.[163]

C. THE BENTS ARE NOT LIABLE FOR THE CONTENT OF THE *RESERVE INSIGHTS* PUBLICATION THAT WAS PUBLICIZED WITHOUT THE BENTS' APPROVAL, BUT NONETHELESS PREPARED IN GOOD FAITH BY RMCI EMPLOYEES

The Staff has advised further that it is considering the recommendation of fraud charges against RMCI and the Bents in connection with the publication of the *Reserve Insights* publication, dated September 15, 2008, which was posted on the Company's website between 8:15 and 11:00 on the morning of September 16, 2008.[164] The Bents did not approve publication of the document and cannot be charged with fraud when an unapproved document later proves to be inaccurate. If marketing personnel had followed RMCI's reasonable procedures for the distribution of marketing materials to the public, the *Reserve Insights* piece clearly would not have been posted to the firm's website.

Prior to publication of the *Reserve Insights* piece on September 16, 2008, RMCI had a long-standing practice for review and approval of information provided to the public. As the

---

[160] Deposition of Bruce II, dated Nov. 3, 2008, at 138:20-140:25; Deposition of Bruce II, dated Nov. 25, 2008, at 140:14-141:9; *see also* RF-SEC-00203119.

[161] *Markowski v. SEC*, 34 F.3d 99, 105 (2d Cir. 1994) (finding that reliance on counsel defense applies where counsel provided advice that conduct was legal after complete disclosure, and client relies on that advice in good faith).

[162] *See, e.g.*, RF-SEC-00178682.137.

[163] *See Wright v. Ernst & Young LLP*, 152 F.3d 169, 175 (2d Cir. 1998); 15 U.S.C. §78t(a).

[164] The *Reserve Insights* piece was posted at 8:15 a.m. RF-SEC-0162771 (indicating article posted at 8:15 a.m.). It was removed at approximately 11:00, after DiMartino spoke with Robert Plaze at 10:57 a.m. and phoned Crowley at 10:58 a.m. RF-SEC-WH-00000046-48.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

Bents explained in their depositions, RMCI subjects public statements to a two-stage review process.[165] In the first stage, subject matter experts review and approve the content of information within their field of expertise. The subject matter experts for the *Reserve Insights* piece included RMCI's chief compliance officer, general counsel, the director of marketing, the director of sales and, with respect to the descriptions of the Lehman portfolio holdings, Ledford. Upon approval of all subject matter experts, a proposed publication proceeds to the second stage of review. In the second stage, Bruce Sr., Bruce II, Arthur, their in-house general counsel and the chief compliance officer review the content of a publication and, to the extent that they find it satisfactory, approve it for distribution. This two-stage process is documented on a review form, which includes the original signatures of all reviewers who approve distribution of RMCI's public statements and their express recommendation (reflected as "yes" or "no") as to whether the document is cleared for publication. All of the Bents consistently testified that they did not approve the *Reserve Insights* piece for distribution to the public.[166] They learned about the publication at about 11:00 a.m.[167] on Tuesday, September 16 when outside counsel told Crowley and Bruce II that the SEC Division of Investment Management had complained about the content of the publication, which reported that RMCI intended to enter into a credit support agreement that RMCI had informed both the SEC Staff and the Fund Board it was no longer pursuing.

The Staff appears to have focused on two types of statements in the *Reserve Insights* publication: (1) commentary regarding the impact of Lehman's bankruptcy on the maturation of the Lehman debt in the Fund; and (2) statements about RMCI's intention to enter into a support agreement. We address each of these statements below, and note further that the Bents had

[165] Deposition of Bruce II, dated Nov. 3, 2008, at 28:2-29:1; Deposition of Arthur Bent, dated Dec. 11, 2008, at 28:3-13; Deposition of Bruce Sr., dated Oct. 29, 2008, at 158:18-160:1.

[166] Deposition of Bruce Sr., dated Oct. 29, 2008, at 181:11-184:18; Deposition of Bruce II, dated Nov. 25, 2008, at 94:19-96:15; Deposition of Arthur Bent, dated Dec. 11, 2008, at 45:22-46:22, 47:9-14.

[167] RF-SEC-WH-00000046-48.

Confidential Treatment Requested by WILMER CUTLER PICKERING HALE AND DORR LLP

affirmatively rejected these descriptions on September 15 or 16, and had insisted that RMCI personnel subject any proposed publication to executive review, which would include approval by the in-house counsel and chief compliance officer.

1. STATEMENTS REGARDING THE MATURATION OF THE LEHMAN DEBT

We turn first to the following description of the Lehman exposure:

> The Reserve's exposure to Lehman debt in the Primary Fund is less than 1.2% .... The majority of the Lehman Brothers' senior debt will be coming due over the next several weeks. Based on current valuations of these holdings, we believe that the holdings will mature at par value. Due to the small exposure as well as par value at maturity, the NAV is not negatively impacted.[168]

The Bents consistently testified that the *Reserve Insights* piece had not cleared first stage review when marketing personnel arranged for the piece to be added to the Firm's website.[169] There is persuasive and corroborating evidence for this conclusion, not the least of which is the lack of a physical approval form for the *Reserve Insights* piece.[170] Moreover, the statement that the Lehman debt "will mature at par value" was inconsistent with statements that Bruce Sr. made to the Primary Fund's Board on September 15. In particular, in response to a Trustee's question as to whether the Lehman commercial paper would mature and be honored by the bankruptcy court, Bruce Sr. answered: "Everything is on hold." The Fund's counsel, DiMartino, concurred:

> Yeah. That's my understanding as well. They can't disburse any moneys out of the company without the consent of the bankruptcy court. So they file a petition today to allow them to continue operations and make payments in the ordinary course, like for example, to pay their employees so people don't quit. But other payments are not going to be made. They're suspended.[171]

---

[168] RF-SEC-00128452-53.

[169] Deposition of Bruce II, dated Nov. 25, 2008, at 94:19-96:15.

[170] RMCI created a sign-off sheet for preliminary review. RF-SEC-00162781-82. However, no form was created for executive review.

[171] RF-SEC-00178693.002.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

Having earlier rejected the characterization that Lehman would mature at par in conversations with the Fund Board, there is no evidence to support the Staff's view that the Bents approved *that same description* for publication to investors.

2. STATEMENTS REGARDING THE CREDIT SUPPORT AGREEMENT

We next address two obviously conflicting statements in the *Reserve Insights* publication regarding the Bents' intentions to support the Primary Fund's NAV. The first of these descriptions stated:

> The Reserve is committed to a $1.00 NAV for its Primary Fund. Reserve Management Company, Inc., (RMCI) intends to enter into support agreements with the Primary Fund to support the value of the Lehman credit held in the fund .... We have discussed with the SEC that our intent is to mitigate any decline in value of the Lehman debt so that it will not result in a decrease to the NAV of the Fund. We are submitting appropriate documentation to the SEC today, September 15, 2008.[172]

Later in the publication, *Reserve Insights* included the following sentence, on its face inconsistent with the forward-looking statement of intention that Crowley had proposed:[173] "Furthermore, our support agreements ensure the integrity of a $1.00 NAV."[174]

Here, again, there is ample corroborating evidence that the Bents neither reviewed nor approved this description for publication; notably, the absence of any review form evidencing the Bents' approving signatures. Moreover, a comparison of the various drafts of the *Reserve Insights* piece circulated among marketing personnel confirms that none of the marketing personnel provided the Bents with a draft of the publication containing the following statement: "Furthermore, our support agreements ensure the integrity of a $1.00 NAV."[175]

---

[172] RF-SEC-00128452-53.

[173] RF-SEC-WH-00000040-42.

[174] RF-SEC-00128452-53.

[175] *Compare* RF-SEC-00162775-76 and RF-SEC-00167706-08.

While the Staff appears to place great weight on the fact that marketing personnel provided portions of the *Reserve Insights* piece to Bruce II at various points on September 15, Bruce II's consistent and prior experience with the RMCI pre-publication review process reasonably led him to believe that the drafts he received would not be used before he (and other executives) authorized their publication in the executive review.[176] All of Bruce II's internal e-mails are consistent with this state of mind.[177] To the extent that marketing personnel departed from the Company's two-stage pre-publication review procedures, they did not inform Bruce II of their actions. Lansky did not, for example, copy Bruce II on his e-mail to marketing personnel reporting that materials relating to Lehman were subject to a "rush review[,]" which purportedly excluded Bruce Sr. and Arthur from executive review.[178]

In the absence of their review and approval of the *Reserve Insights* piece, and with no expectation that the publication could be released without their approval, the Bents cannot be found liable for alleged misstatements in that publication.[179]

Moreover, the conflicting reports of the status of the credit support agreement in the *Reserve Insights* publication – both that the Bents were awaiting approval for a credit support agreement from the SEC and the contrary statement that the agreement already had been

---

[176] Deposition of Bruce II, dated Nov. 25, 2008, at 148:7-16.

[177] *See, e.g.* RF-SEC-00203119-23 ("get approval from Kate first please, then show it to us").

[178] RF-SEC-00065810 (e-mail from Lansky (not copying the Bents) stating "assume what you will submit into review will be made available to all clients once given ok... For rush revie [sic] include [Managing Director, Global Head of Sales] john [Drahzal], [Director, Institutional Sales] Brandon [Semilof], [General Counsel] kate [Crowley] and [Bruce II]"; *see also* Deposition of Bruce II, dated Nov. 25, 2008, at 148:20-149:3.

[179] *Wright v. Ernst & Young LLP*, 152 F. 3d 169, 175 (2d Cir. 1998) ("[B]ecause §10(b) and Rule 10b-5 focus on fraud made in connection with the sale or purchase of securities, a defendant must know or should know that his representation would be communicated to investors." (internal quotation marks and citations omitted)); *SEC v. Wolfson*, 539 F. 3d 1249, 1260 (10th Cir. 2008) (citing *SEC v. Collins & Aikman Corp.*, 524 F. Supp. 2d 477, 490 (S.D.N.Y. 2007); *SEC v. Power*, 525 F. Supp. 2d 415, 420 (S.D.N.Y. 2007); *SEC v. KPMG, LLP*, 412 F. Supp. 2d 349, 375 (S.D.N.Y. 2006)). *See also Monsen v. Consolidated Dressed Beef Co.*, 579 F. 2d 793, 804 (3d Cir. 1978) ("[A] director may not be found liable [for the company's violations] unless he culpably participated in the controlled person's unlawful activity."); *see also* Securities Act of 1933, § 15, 15 U.S.C.A. § 77o; Securities Exchange Act of 1934, § 20, 15 U.S.C.A. § 78t.

approved by the SEC – were inconsistent with the Bents' disclosures to the Board and the SEC on the morning of September 16. In particular, Bruce II informed his outside counsel at 7:00 a.m. that the family did not believe that they could support the Primary Fund's NAV in light of the prior day's massive redemptions.[180] At 8:00 a.m., RMCI informed the SEC Division of Investment Management that the Bents could not support the NAV of the Primary Fund in the face of a significant loss of investor confidence.[181] At 10:00 a.m., the Bents informed the Fund's Board of Trustees that they regretfully had concluded that they were not able to support the Fund's NAV.[182] Having proceeded to make multiple and painful disclosures that they could not support the NAV of their flagship fund, and that the NAV of the Fund likely would fall below $1.00 per share (signaling a collapse of the money fund business the family had built over 40 years), it defies common sense to think that the Bents agreed to publish the *Reserve Insights* piece – with diametrically opposite representations about their intention to support the Fund's NAV – on the morning of September 16.

3. THE BENTS' CONSULTATION WITH COUNSEL REGARDING THE CONTENT OF THE DESCRIPTIONS OF THE PROPOSED CREDIT SUPPORT AGREEMENT UNDERCUTS THE STAFF'S PROPOSED INFERENCE OF FRAUD

Finally, the Bents' consultation with legal counsel in the review and approval of RMCI's public communications undercuts the inference of fraud that the Staff seeks to draw. The Bents and the marketing team consulted their in-house counsel on all of the draft marketing materials on September 15 and 16. Upon receipt of Bruce II's 1:19 p.m. e-mail announcing RMCI's intent to support the Primary Fund's NAV, for example, Lansky provided the following draft language to (among others) Crowley:

[180] RF-SEC-00187438 (phone records indicate an eleven minute call between Joel Goldberg and Bruce II at 7:03 a.m.); Deposition of Bruce II, dated Nov. 3, 2008, at 180:12-181:2.

[181] RF-SEC-00187438.

[182] RF-SEC-00178716-17.

RF-SEC-WH-00000311

Confidential Treatment Requested by WILMER CUTLER PICKERING HALE AND DORR LLP

> [H]ere is what [we] wish to state: The Reserve is committed to the $1 NAV of The Primary Fund. The Reserve has entered into support agreements which will support the value of the Lehman credit held in the fund. These agreements are intended to ensure that any decline in the value of the Lehman debt will not result in a decrease in the net asset value of The Reserve Primary Fund.[183]

Crowley clearly understood that the public communications required her approval and she provided commentary on the substance of the communications: "We haven't entered into the agreements yet; that's why Bruce's e-mail said we intend to. We will submit a form of the agreement to the SEC this afternoon for its review and approval which we expect to obtain."[184] When it appeared to Bruce II that marketing personnel were attempting to circumvent the approval process by providing draft correspondence directly to Bruce II for consideration, he directed them to obtain the General Counsel's approval before submitting documents to him for consideration.[185]

Crowley had available to her, as well, the sophistication and experience of the leading 1940 Act lawyers in the United States. In this regard, she asked Goldberg to review excerpts of the language that the Staff now challenges in the *Reserve Insights* publication:

> Joel:
>
> While Rose is busy drafting our SEC letter, can you take a quick look at our talking points below? They seem okay to me but given the time, I'm not comfortable with the representation that we expect SEC approval "in a few hours" although that was what Rick said in our first call. Let me know what you think. Thanks . . . .
>
> "While unprecedented events have unfolded over the past few days, The Reserve remains committed to providing money market funds and cash products based on thorough research, expertise and experience. We are confident in the underlying credit strength and quality of the securities in our money market funds. The Reserve intends to protect the NAV on the

[183] RF-SEC-00203127-28.

[184] RF-SEC-WH-00000040-42.

[185] Deposition of Bruce II, dated Nov. 3, 2008, at 138:20-140:25; Deposition of Bruce II, dated Nov. 25, 2008, at 140:14-141:9; *see also* RF-SEC-00203119.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

> Primary fund to whatever degree is required. As a result, The Reserve will enter into agreements which will support the value of the Lehman securities held in our fund. We have spoken with the SEC and are awaiting their final approval which we expect to have in a few hours. These agreements are intended to ensure that any decline in the value of the Lehman debt will not affect the $1 NAV of the Reserve Primary Fund. As of September 15, 2008, Lehman debt constitutes less then 1% of The Reserve's money fund assets. All of those assets are senior debt maturing and the majority will mature by the end of October . . ."[186]

Their consultation and reliance upon experienced and informed counsel underscores that the Bents acted in good faith, and refutes the Staff's conclusion that the Bents intended to defraud investors.[187]

4. THE BENTS CANNOT BE LIABLE FOR AIDING AND ABETTING ALLEGED OMISSIONS OR MISSTATEMENTS BY RMCI AND ITS PERSONNEL

The Bents are not liable for fraud or aiding and abetting for alleged omissions or misstatements by RMCI and its personnel. To establish aiding and abetting liability under the securities laws, the SEC must demonstrate: (1) a securities violation committed by another party; (2) knowledge by the aider and abettor that his actions were part of the improper activity; and (3) proof that the aider and abettor knowingly and substantially assisted in the primary violation.[188] Even where the primary violation does not require a finding of scienter, the Commission has determined that aiding and abetting liability cannot be established without a finding of scienter.[189] Acting in good faith precludes such a finding.[190] For the reasons discussed above, including the good faith demonstrated by the consultation with counsel, the Bents lacked the requisite scienter to be liable under theories of aiding and abetting.

---

[186] RF-SEC-WH-00000001-02.

[187] *Howard v. SEC*, 376 F.3d 1136, 1147 (D.C. Cir. 2004); *SEC v. Snyder*, No. 07-20455, 2008 WL 4218781, at *13 (5th Cir. Sept. 16, 2008) (reliance on counsel is "a means of demonstrating good faith and represents possible evidence of an absence of any intent to defraud").

[188] *Investors Research Corp. v. SEC*, 628 F.2d 168, 178 (D.C. Cir. 1980).

[189] *Chris Woessner*, Initial Decisions Release No. 225, 2003 SEC LEXIS 646 (Mar. 19, 2003) (evaluating aiding and abetting liability under the Investment Advisers Act).

[190] *Id.* at *29 (citing Kingsley, Jennison, McNulty & Morse Inc., 51 S.E.C. 904, 911 (1993)).

D. BY SEPTEMBER 16, INFORMATION THAT RMCI WAS NOT SUPPORTING THE PRIMARY FUND'S NAV WAS IMMATERIAL

We now turn to the Staff's claim that the Bents misled investors because they did not make a corrective disclosure on September 16, stating that they could not support the NAV of the Primary Fund before the Fund announced shortly after 5:00 p.m. that it no longer traded at $1.00 per share.[191] There is little factual basis for the Staff's claim that investors were deceived about the state of the Fund on September 16. The market knew from disclosure of the Fund's holdings that it held $785 million (out of $62 billion) in Lehman securities as of the opening on September 15.[192] Any investor could calculate that a valuation below roughly 55 cents per dollar would cause the Fund to break the $1.00 per share NAV and that redemptions would lead to the same result at higher valuations. It was also widely known that Lehman debt was not trading, and that liquidity for other securities was severely diminished.[193] On September 16, there was also significant market speculation, including statements attributed to the SEC, that the Primary Fund would likely break the buck.[194] Further reports that the Bents could not support the NAV of the Primary Fund were immaterial in this context. In addition, as of September 16, the Bents relied entirely upon counsel regarding their disclosure obligations and what duty, if any, they had to make corrective disclosures to Fund investors.

---

[191] Deposition of Bruce II, dated Nov. 25, 2008, at 167:6-9.

[192] The Fund's portfolio assets, including its Lehman holdings, were disclosed in its Annual Report, filed with the SEC on Aug. 8, 2008.

[193] *See, e.g.* RF-SEC-00178693.004 ("none [of the Lehman debt] has actually traded . . . . This is information from the dealer community"); RF-SEC-00178693.004 ("There's no transactions taking place in Lehman paper and there's very, very few transactions taking place in any paper"); RF-SEC-00178718 ("Mr. Bent discussed the unprecedented illiquidity in the markets").

[194] *See, e.g.* notes 196-200, *infra.*

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000314

The chaotic market events of September 16 are discussed earlier in this submission, and we limit our discussion to the total mix of information available to investors on that date.[195] As of September 16, the market included ample indicia that the Primary Fund was likely to fail. Consider the following:

- During RMCI's 8:00 a.m. conference with the SEC Division of Investment Management, the Staff suggested that RMCI contact the Investment Company Institute ("ICI") for assistance.[196] Before RMCI could place the call, however, ICI's general counsel called Crowley and Goldberg, stating that she "[understood] you're in the thick of things"[197] and the ICI was "willing to help."[198]

- At 1:29 p.m., the *Wall Street Journal* asked RMCI to comment on reports that the Primary Fund would cease to trade at $1.00 per share.[199]

- At 3:00, a reporter from Bloomberg News e-mailed RMCI's public relations director, claiming that "*we have a source at the SEC* telling us the fund has broken the buck."[200]

- Sometime between 3:00 and 4:00 p.m., the Chief Compliance Officer for JPMorgan Chase Asset Management called DiMartino, telling her that she had heard from industry groups that the Primary Fund had broken the buck.

Even if the Bents had issued a corrective statement earlier on September 16, that statement would not have altered the total mix of information available to investors – the market understood that the Primary Fund was in danger. The omission of such publicly available

---

[195] Information is material if there is a "substantial likelihood" that the reasonable investor would view it "as having significantly altered the 'total mix' of information made available." *See Basic, Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988) (quoting *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976)).

[196] RF-SEC-00178721.

[197] RF-SEC-WH-00000031.

[198] RF-SEC-WH-00000030.

[199] RF-SEC-00001946-47; RF-SEC-00001950-51.

[200] RF-SEC-00132092 (emphasis added).

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

information for a few hours in the midst of a financial crisis cannot be the basis of securities fraud.[201]

Equally importantly, on September 16, all facets of RMCI's communications with the public were reviewed by in-house counsel and, for some communications, the adviser's outside counsel. Seasoned legal professionals both inside and outside the adviser affirmatively recommended that RMCI not issue disclosure about its intentions with respect to the Primary Fund's NAV before the official announcement at 5:00 p.m. that the Primary Fund was no longer trading at $1.00 per share. Counsel's advice to say nothing is reflected in the numerous e-mail communications between the marketing department and Crowley. For example:

- At 9:33 a.m., RMCI sales personnel asked Crowley what they should tell investors about the continued vitality of the credit support agreement.[202] Although she participated in RMCI's reports to the Board and the SEC that the Bents could not support the Fund's NAV, she did not tell them that corrective disclosure was required.

- At 12:08 p.m., shortly after the *Reserve Insights* publication was removed from the Company's website, Lansky asked Crowley for an explanation.[203] In her response of 1:23 p.m., she advised John Drahzal that the sales force should stop referencing the statement.[204]

- Before the 5:00 p.m. press release, which disclosed that the NAV of the Fund was $0.97 per share, Crowley and RMCI's outside counsel advised RMCI to maintain their silence about the credit support agreement, with Goldberg expressly stating that he would prefer that RMCI not disclose its intention to make an announcement later that day.[205]

---

[201] *In re Apple Computer Sec. Litig.*, 886 F.2d 1109, 1115 (9th Cir. 1989) ("the defendant's failure to disclose material information may be excused where that information has been made credibly available to the market by other sources"); *In re Clearly Canadian Sec. Litig.*, 875 F. Supp. 1410, 1419 (N.D. Cal. 1995) ("If a disclosure by the defendants would not have altered this total mix of information, it cannot be material and is therefore not actionable.").

[202] RF-SEC-WH-00000029.

[203] RF-SEC-WH-00000032.

[204] RF-SEC-WH-00000033-35.

[205] RF-SEC-WH-00000036-39.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RMCI's reliance on this advice is well-documented. As Bruce II explained to Lansky: "I'm sorry, we are handling everything from a legal perspective all statements to the media will be coming from our legal department and nobody else."[206] On this record, the Staff's perception that RMCI and the Bents' intended to defraud investors is unsupportable. To the contrary, the Bents' reliance on counsel confirms their "good faith" and "represents possible evidence of an absence of any intent to defraud."[207]

III. THE CREATION OF RECEIVABLES FOR TWO VARIABLE NAV FUNDS WAS NOT FRAUDULENT WHERE THE ASSISTANT COMPTROLLER CREATED THEM IN ERROR AND WITHOUT THE BENTS' AUTHORIZATION

We next address the Staff's claim that the Bents created receivables in the Yield Plus Fund and the International Liquidity Fund for the ostensible purpose of misleading investors of variable NAV products that the NAV of their funds was actually valued at a stable $1.00. As of the December 17 Wells call, the Staff had taken no testimony regarding the creation of the receivables, including from such central witnesses as Lentinello, who instructed State Street to create the receivables, Farrell, who was Lentinello's supervisor and the Chief Financial Officer of the firm, or Bruce II, whom the Staff assumes instructed Lentinello to create the receivables. Although the Staff seems to have formulated its negative views in the absence of even a modestly complete investigation on the issue, there is ample documentary and other evidence that Lentinello created the receivables in error and without the Bents' authorization. We detail that evidence below.

A. DESCRIPTION OF THE RECEIVABLES

On September 15, Lentinello instructed State Street to record receivables in the Yield Plus Fund and the International Liquidity Fund. As discussed above at page 11, unlike money

[206] RF-SEC-00201138-41.

[207] *SEC v. Snyder*, No. 07-20455, 2008 WL 4218781, at *13 (5th Cir., Sept. 16, 2008); *Markowski v. SEC*, 34 F.3d 99, 105 (2d Cir. 1994); *Howard v. SEC*, 376 F.3d 1136, 1147 (D.C. Cir. 2004).

market funds, which are intended to have a stable $1.00 NAV, both of these funds have variable NAVs, and neither invests in accordance with Rule 2a-7. The receivables for the Yield Plus Fund and the International Liquidity Fund totaled $1,462,927 and $14,870,300, respectively.[208] As computed by Lentinello, the receivables had the effect of keeping the NAV of both funds from dropping below $0.995 per share on September 15 (and the NAV for the International Liquidity Fund, as computed by Lentinello, exceeded $1.00 per share on September 16). Even after Lentinello created the receivables, the NAVs for the Yield Plus Fund and the International Liquidity Fund declined below $1.00 as a result of the Board's decision to value the Yield Plus Fund's Lehman holdings at zero on the afternoon of September 16.[209]

B. THE BENTS DID NOT AUTHORIZE THE CREATION OF THE RECEIVABLES

There is very little about Lentinello's account regarding the creation of the receivables with which the Bents agree. Their only common ground is this: on September 15, Bruce II called Lentinello to request his assistance in preparing the financial documents that would permit the Bent family to review the financial impact of supporting the NAVs of the Yield Plus Fund and the International Liquidity Fund.[210] Although Bruce II had little experience working directly with Lentinello, a member of the Finance Department two reporting levels junior to Bruce II, RMCI's Chief Financial Officer was out of the office on business travel. In Farrell's absence, Bruce II asked Lentinello to prepare calculations similar to those the Bents had used to assess RMCI's daily capital support of the Enhanced Cash Fund.[211] Bruce II understood that the process of tracking the Bents' capital obligations to the Enhanced Cash Fund was manual and

---

[208] RF-SEC-00204898.

[209] Although RMCI was not obliged to price the Lehman debt in the International Liquidity Fund at the same fair valuation that the Primary Fund and Yield Plus Fund Boards had determined, the adviser utilized the same valuation for all of the Lehman debt owned by RMCI's advisory clients. *See* RF-SEC-00205588 (Lentinello circulates a snapshot report "adjusted for Lehman price of 80% for Yield Plus, Primary and Int'l Liquidity").

[210] Declaration of Bruce II, dated Jan. 23, 2009, at ¶ 8.

[211] Declaration of Bruce II, dated Jan. 23, 2009 at ¶ 8.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000318

time-consuming, and that certain processes needed to be in place in the event the Bents elected to provide similar support to the Yield Plus and International Liquidity Funds.[212]

The Bents reject entirely, however, Lentinello's claim that Bruce II asked the Finance Department to do more than marshal resources in order to track the Bent family's potential capital obligations to the Yield Plus Fund and International Liquidity Fund. Bruce II did not request that Lentinello create receivables, and he did not request that Lentinello commit the Bent family's personal capital of an unspecified amount, pursuant to a formula that Lentinello did not share with Bruce II.[213] Indeed, Lentinello's written correspondence on September 15 provided the Bents with no indication that he had interpreted Bruce II's request so broadly. The 11:52 a.m. snapshot report is illustrative.[214] That report documents the Bents' capital obligations to the Enhanced Cash Fund, valued at $3,399,114 as of September 12, 2008. The report contains no reference to any capital obligations for the Yield Plus Fund or International Liquidity Fund.

To the extent that Lentinello's written e-mails refer to the creation of receivables for the Yield Plus and International Liquidity funds, there is no evidence that the Bents were aware of them. In particular, Lentinello did not copy the Bents on the following instructions to State Street:

- The 1:54 p.m. direction to "See calc to book receivable from RMC."[215]
- Instructions to book a receivable for the Primary Fund, along with a formula for computing that receivable.[216] Although no receivable was ever created for the Primary Fund, Lentinello's erroneous directions to State Street were completely at odds with the discussions that Bruce II and his counsel were having with the SEC Division of Investment Management about the creation of an escrow agreement on behalf of the Primary Fund.

[212] Declaration of Bruce II, dated Jan. 23, 2009, at ¶¶ 8-9.

[213] Declaration of Bruce II, dated Jan. 23, 2009, at ¶ 9.

[214] RF-SEC-00201563-64.

[215] RF-SEC-00137280.

[216] RF-SEC-WH-00000003-13; RF-SEC-WH-00000014-18; RF-SEC-WH-00000021-28.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000319

- Instructions to State Street to finalize the value of any Yield Plus receivable after State Street struck an NAV for Yield Plus at the end of the day; thus, creating a single one-day liability for the Bents that potentially exceeded in total the amount that the Bents had contributed to the Enhanced Cash Fund over a period of a year.[217]

C. Reversal of the Receivables

Bruce II learned about the creation of the receivables on September 16, upon receipt of a daily snapshot report stating: "Due to the Lehman write-down and large redemptions in the Funds, receivables from RMCI were booked in Yield Plus and International Liquidity Fund in the amounts of $1.7 million and $14.8 million respectively."[218] Bruce II was surprised to see that Lentinello had created the receivables and immediately informed Lentinello that he had made a mistake and should not have done so.[219] Lentinello assured Bruce II that the erroneous receivables could be corrected by way of a reversal.[220] Bruce II made a similar request to Farrell who, by September 16, had returned to the office.[221]

Although we understand that Farrell and Lentinello both acknowledge that Bruce II directed them to correct the erroneous entry of the receivables, neither acted promptly to address the error and the receivables remained on the books of both funds well after September 16. In follow-up inquiries by Bruce II, Lentinello attributed the ongoing error to State Street's failure to follow his instructions. Regardless of his explanation to Bruce II, Lentinello's written

[217] Lentinello sent an e-mail to various State Street employees, including Darin Mcinnis, R. Wallace, A. Eugley, and Jay Stratton, cc-ing John Plange and Patrick Farrell at 1:54 p.m. on Sept. 15, 2008. RF-SEC-00137280-86 ("This is just a snapshot at 1:30 and not [the] final numbers").

[218] RF-SEC-00204898. Bruce Sr. and Arthur did not learn about the erroneous receivables until November 25, 2008, following an inquiry by a court-appointed Temporary Supervisor for the International Liquidity Fund into the $14.8 million receivable recorded for that fund on September 15, 2008. Deposition of Arthur Bent, dated Dec. 11, 2008, at 98:19-99:4, 110:21-111:25; Declaration of Bruce II, dated Jan. 23, 2009, at ¶ 14. At approximately 5:26 p.m. on Monday, November 24, 2008, Dana Dalle Molle of AlixPartners, the Temporary Supervisor in a case captioned *Caxton Int'l Ltd. v. Reserve Int'l Liquidity Fund, Ltd.*, No. 08/602875 (N.Y. Sup. Ct.), asked Lentinello the purpose of a debit for $14,913,152 on September 15, 2008 and credit for the same on October 3, 2008. RF-WH-SEC-00000170-174.

[219] Declaration of Bruce II, dated Jan. 23, 2009, at ¶ 12.

[220] Declaration of Bruce II, dated Jan. 23, 2009, at ¶ 12.

[221] Declaration of Bruce II, dated Jan. 23, 2009, at ¶ 13.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

communications with State Street suggest that he delayed asking State Street to reverse the receivables until September 24. On that date, Lentinello sent an e-mail to State Street, writing: "[F]or today, 9/24/08, please reverse all receivables from RMC for the following funds: Enhanced Cash Fund $3,376,758[;] Yield Plus $1,706,980[;] International Liquidity $14,870,300."[222] Lentinello does not appear to have taken any action to monitor whether State Street complied with his direction, as the receivables continued to be recorded for the funds as late as September 29. At this point, Farrell asked Lentinello to explain why the receivables continued to be recorded on the Funds' records. Lentinello responded: "These were all reversed last week on EC[,] YP and IL. Let's discuss."[223]

The funds' records indicate that the receivables were reversed on or about October 3, 2008.[224] Consistent with management's view that the receivables were not authorized, no amount of the receivables has been contributed to the Yield Plus Fund or International Liquidity Fund.

D. CORROBORATING EVIDENCE SUPPORTS MANAGEMENT'S VIEW THAT THE RECEIVABLES WERE UNAUTHORIZED

However honestly Lentinello held the belief that Bruce II instructed him to create the receivables, the corroborating evidence confirms that Lentinello's creation of the receivables was unauthorized.

1. RMCI REFUSED TO ISSUE PUBLIC STATEMENTS THAT IT INTENDED TO SUPPORT THE NAV FOR THE YIELD PLUS FUND OR THE INTERNATIONAL LIQUIDITY FUND

There is a tension between the Staff's view that RMCI publicized its commitment to the Primary Fund NAV to dissuade investors from redeeming out of the fund (or, alternatively, to entice investors to invest in the fund) and the Staff's claim that the Bents concealed the declining

[222] RF-SEC-00211485.

[223] RF-SEC-00211497.

[224] Declaration of Bruce II, dated Jan. 23, 2009, at ¶ 14.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

NAV for the Yield Plus and International Liquidity funds through the use of receivables. The institutional investors in the Yield Plus and International Liquidity funds – like the investors in the Primary Fund – were knowledgeable about the funds' Lehman exposure and understood that Lehman could impair the value of the funds' NAVs. In this regard, Lansky repeatedly asked Bruce II for a statement regarding whether RMCI would support the Yield Plus Fund's NAV.[225] Notwithstanding investor interest, Bruce II refused to provide any assurances that RMCI intended to protect the NAV of their funds. Bruce II's response to Lansky's suggestion to include Yield Plus in the *Reserve Insights* draft is illustrative. In response to Lansky's request: "[D]o you want us to include [Y]ield [P]lus as well in the doc[?]" (and his supplemental suggestion, "[I]f wish to state protection for YP we will simply update doc"), Bruce II responded "[N]o we don't need to do that right now."[226] In this context, anonymous receivables would have done nothing to quell investor concern and it seems highly improbable that Bruce II authorized their creation under the circumstances that Lentinello has described.

2. BRUCE II'S WRITTEN COMMUNICATIONS CONFIRM HIS UNDERSTANDING THAT HE DID NOT HAVE A COMMITMENT TO SUPPORT THE NAVS FOR THE YIELD PLUS AND INTERNATIONAL LIQUIDITY FUNDS

On September 17, Bruce II took affirmative action to conclude his support obligation for the Enhanced Cash Fund. In particular, in a 3:56 p.m. e-mail to Farrell, Bruce II instructed that "as of today we are no longer protecting the NAV on the Enhanced Cash Strategies Portfolio."[227] There is no comparable communication with respect to the Yield Plus or International Liquidity Funds. If Bruce II believed that the Bents had outstanding a similar commitment to protect the Yield Plus and International Liquidity Funds, he would have sent a similar e-mail rescinding

[225] RF-SEC-00179026-33; RF-SEC-00203105-12.

[226] RF-SEC-00179026-33; RF-SEC-00203105-12.

[227] RF-SEC-00330232-33.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000322

those commitments as well. The absence of any document terminating a support obligation for those funds corroborates Bruce II's understanding that he did not have support obligations for the funds.

3. AFTER INFORMING THE BOARD THAT THE YIELD PLUS FUND WOULD BREAK THE BUCK IF LEHMAN WAS PRICED AT 80% OF PAR, THE BENTS DID NOT REQUEST BOARD APPROVAL TO SUPPORT THE FUND'S NAV OR NOTIFY THE SEC OF ANY INTENTION TO DO SO

As discussed above, at the 9:30 a.m. Board meeting on September 15, RMCI informed the Board that the Yield Plus Fund would cease to trade at $1.00 per share when Lehman was valued at 80% of par.[228] However, the minutes of the Board meetings do not indicate that the Bents sought Trustee approval to support the Yield Plus Fund either at the 9:30 a.m. or 1:00 p.m. Board meetings.[229] Nor did the Bents advise the SEC Division of Investment Management, in their subsequent conversations on September 15, of any intention to support the NAV of the Yield Plus Fund. These facts suggest that the Bents understood they were prepared to let a variable NAV fund fluctuate from $1.00 per share.

4. LENTINELLO'S CONDUCT SUGGESTS THAT THERE WAS NO AGREEMENT TO BACKSTOP THE NAVS FOR THE YIELD PLUS AND INTERNATIONAL LIQUIDITY FUNDS

Lentinello's actions suggest that he understood that the Bents did not agree to backstop the NAVs for the Yield Plus and International Liquidity Funds. He did *not*, for example, recalculate the receivables after the Trustees reduced the fair value of the Lehman securities to zero on September 16. In the event that Lentinello believed a backstop obligation was in place, the receivables should have been increased to cover the decline in Lehman valuation. The books

[228] Although the Bents considered supporting the NAV of the Yield Plus Fund (*see* RF-SEC-00178693.0004 ("To the extent that the Yield Plus amounts to more than a half of one percent, well that's really not party to this conversation, but anyhow, since they are here, we can put – we being RMCI – can put in a supplemental letter on that.")), the minutes do not reflect that they sought Board approval to pursue a support arrangement, and they did not discuss support of that Fund with the SEC Division of Investment Management.

[229] RF-SEC-00178716-19.

Confidential Treatment Requested by WILMER CUTLER PICKERING HALE AND DORR LLP

and records for the Yield Plus and International Liquidity funds instead indicate that the value of the receivables remained constant between September 15, when Lentinello created them, and September 24, when he instructed State Street to reverse them.

Lentinello's conduct after September 16 is more generally in accord with the conclusion that the Bents had not committed to support the Yield Plus and International Liquidity Funds. On September 17, for example, when Farrell forwarded to Lentinello the statement that the Bents were "no longer protecting the NAV on the Enhanced Cash Strategies Portfolio"[230] he responded simply, "Okay [State Street Bank] knows."[231] Had Lentinello still believed by this time that the Bents had committed to protecting the NAV of the Yield Plus and International Liquidity Funds, surely he would have inquired as to whether those commitments were also rescinded. But he did not, suggesting that he understood that the Bents had never agreed to support the NAVs for those funds.

5. THERE IS NO CREDIBLE EVIDENCE THAT THE BENTS WERE PREPARED TO SPEND MORE TO SUPPORT THEIR VARIABLE NAV PRODUCTS THAN THEY WERE PREPARED TO SUPPORT THEIR FLAGSHIP MONEY FUND

As discussed earlier in this memorandum, the Bents were prepared to place $10 million in escrow to support the NAV of their flagship money market fund, the Primary Fund, a $62 billion fund. The receivables that Lentinello created, by contrast, totaled in aggregate $16.5 million, a number far disproportionate to the significance of two small variable NAV funds with aggregate assets of approximately $4.7 billion. The Staff has no credible basis for concluding that the Bents would support these smaller funds over their flagship Primary Fund,

---

[230] RF-SEC-330215-16.

[231] RF-SEC-330227-28.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000324

the oldest money market fund in the country. That Lentinello created the receivables in these circumstances suggests that he misunderstood the Bents' instructions on September 15.

IV. THE BENTS ARE NOT PERSONALLY LIABLE FOR DELAYS IN OBTAINING RELIEF UNDER SECTION 22(E) OF THE INVESTMENT COMPANY ACT

The Staff maintains that the Bents should be liable for delays in obtaining relief under Section 22(e) of the Investment Company Act in circumstances where the Commission itself has determined that suspension of the right of redemption was in shareholders' interests. As discussed in detail in the Wells memorandum for RMCI, incorporated herein by reference, there simply is no justification for penalizing the technical violation of Section 22(e) while RMCI sought the requisite orders to suspend redemptions. To the contrary, the Commission found in granting those orders that postponing the payment of redemption proceeds was necessary "to protect the Funds' security holders."[233] Moreover, there simply is no legal basis to impose personal liability on the Bents for the Funds' technical violation of Section 22(e), nor is there any compelling policy interest served given that the decisions that were made by the Board were necessary for the protection of the Funds' investors and the investing public as a whole.

The Bents did not cause the funds to violate Section 22(e). Rather, State Street, without notice to RMCI or the Funds, unilaterally suspended redemptions in the Primary Fund. When Bruce II learned of the suspensions, he took reasonable, albeit unsuccessful, steps to find the liquidity to enable State Street to resume redemptions. The independent Board of each fund made the determination that postponing payment of redemption proceeds was in the best interest of the shareholders. The liquidity problems which led the Boards to postpone payments for each fund were caused by the unprecedented run on the money market industry and a collection of unforeseeable and extraordinary events in the financial industry that culminated in the collapse

---

[233] *Reserve Municipal Money-Market Trust*, Investment Company Act Release No. 28466, 2008 SEC LEXIS 2396, at *9 (Oct. 24, 2008).

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000325

of Lehman Brothers and widespread panic in the market.[234] The Boards' decision to postpone payment of redemption proceeds was not caused by specific actions the Bents either took or failed to take. In fact, throughout September and early October, the Bents regularly provided the Boards with information regarding the continuing liquidity crisis and the status of redemption requests so that the Boards could determine that postponing redemption payments was necessary for the protection of investors. The fact that the Boards, and not the Bents, made the decision to postpone payment of redemption proceeds obviates any possible personal liability on the part of the Bents.

Although there are no adjudicated cases against investment advisers under Section 22(e), the conclusion that the Bents are not personally liable is consistent with the limited number of settled administrative proceedings under Section 22(e). Investment advisers have incurred liability for 22(e) violations only in instances where the adviser took specific, and at times fraudulent, actions which led to inaccurate valuation or illiquidity triggering the delay in payment of redemption proceeds or suspension of redemption rights.[235] Here, the Board's decision to postpone payment of redemption proceeds was not caused by the Bents. Rather, as the Commission recognized in its 22(e) Order, postponing payments was necessary due to the continued high rates of redemption requests in the midst of the unprecedented market turmoil.[236]

---

[234] *See* Background Section C, *supra.*

[235] *See e.g.*, *Edwin J. Pittock,* Investment Company Act Release No. 20448, 1994 SEC LEXIS 2419 (Aug. 8, 1994) (finding that the adviser caused the fund to loan money in contravention to its stated investment policies, impairing the fund's ability to timely meet redemption requests); *see also Judy M. Rupay,* Investment Company Act Release No. 25960, 2003 SEC LEXIS 506 (Mar. 4, 2003) (finding that the adviser knowingly recorded a receivable on the fund's books when it had no reasonable basis to believe the receivable could be collected, causing the fund to redeem shares at inflated prices and ultimately suspend redemptions due to the resulting liquidity problems).

[236] *Reserve Fund*, Investment Company Act Release No. 28386, 2008 WL 4468809 (Sept. 22, 2008); *Reserve Fund*, Investment Company Act Release No. 28465, 2008 WL 4826002 (Oct. 24, 2008) (providing that the circumstances required immediate action to protect the Funds' investors).

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

V. THE BENTS ARE NOT PERSONALLY LIABLE FOR BOOKS AND RECORDS VIOLATIONS

The Staff contends that because RMCI and the Bents are subject to the record-keeping requirements of the Investment Advisers Act and Investment Company Act, the Bents should be charged for RMCI's allegedly false, misleading and inaccurate records concerning: (1) the calculation of the NAVs for the Primary Fund and the Yield Plus Fund; (2) the nature of receivables on the Funds' books; and (3) RMCI's communications to investors on September 15 and 16, 2008. The Staff proposes to bring charges under Section 204 of the Investment Advisers Act, specifically Rule 204-2, and Section 22(c), Rule 22c-1, Section 31(a) and Rule 31a-1 of the Investment Company Act.

A. BECAUSE THE FACTS HERE DO NOT RESEMBLE OTHER CASES INVOLVING SUPERVISORY LIABILITY, IT WOULD BE INAPPROPRIATE TO CHARGE THE BENTS FOR BOOKS AND RECORDS VIOLATIONS[237]

The facts demonstrate that the Bents met their supervisory responsibilities and that charging them for books and records violations here would be inconsistent with Commission precedent. As discussed below, The Reserve had in place supervisory procedures that could reasonably be expected to prevent and detect violations of the securities laws, and the Bents reasonably discharged their duties and obligations as supervisors that flowed from those

[237] The standard for supervisory liability under Section 203(e)(6) of the IAA is the same as the standard under the Exchange Act. *See* Exchange Act Section 15(b)(4)(E), 15 U.S.C. § 78o(b)(4)(E); *see also Vilis Pasts*, Exchange Act Release No. 34-39074, 1997 WL 566807 (Sept. 15, 1997) ("Under Sections 203(e) and 203(f) of the Advisers Act, the Commission may seek sanctions where an investment adviser or an associated person has failed reasonably to supervise, with a view to preventing violations of the federal securities laws and rules thereunder, another person subject to the investment adviser's or associated person's supervision who commits such violations. Sections 15(b)(4) and 15(b)(6) of the Exchange Act provide similar authority with respect to registered broker-dealers and associated persons of such broker-dealers.").

procedures.[238] Federal securities law requires only *reasonable efforts* to discharge the obligations imposed and does not demand a guarantee against violations.[239]

The appropriate test for whether an individual has discharged his or her responsibility "is not whether, in hindsight, violations could have been better prevented by any other course of conduct," but instead "*whether the actions taken represent a reasonable response based on the information available at the time*."[240] The conduct at issue here, which occurred during an extraordinary market-wide two-day crisis, is strikingly different from the months or years of repeated violations in prior cases alleging supervisory liability. Rather than involving supervisors who failed to detect patterns of violations that had occurred for months or years,[241] the books and records issues alleged here occurred over two days. Moreover, during the two

[238] *John H. Gutfreund*, Exchange Act Release No. 31554, 1992 WL 362753, at *15 (Dec. 3, 1992), ("determining if a particular person [with compliance responsibilities] is a 'supervisor' depends on whether, under the facts and circumstances of a particular case, that person has a requisite degree of responsibility, ability or authority to affect the conduct of the employee whose behavior is at issue").

[239] *See* ICA Section 203(e)(6) (providing safe harbor for supervisor who, assuming procedures are in place to reasonably prevent and detect securities violations, has "reasonably discharged the duties incumbent upon him by reason of such procedures and system without reasonable cause to believe that such procedures and system were not being complied with."); *Dean Witter Reynolds, Inc.*, Initial Decisions Release No. 179, 2001 WL 47244 (Jan. 22, 2001) (finding that company met safe harbor because adequate supervisory procedures were in place and were reasonably followed by compliance department and branch manager).

[240] Commissioner Mary L. Schapiro, *Remarks at the National Association of Securities Dealers, Inc. Sixth Annual Educational Seminar*, New York, N.Y. (Oct. 5, 1993) (emphasis added), at 16-17, *available at* http://www.sec.gov/news/speech/1993/100593schapiro.pdf (last visited Jan. 20, 2009); *Arthur James Huff*, Exchange Act Release No. 34-29017, 50 S.E.C. 524, 1991 WL 296561, at *4 (Mar. 28, 1991) (Opinion of Commission reversing ALJ decision and finding that compliance officer Huff exercised reasonable supervision "under the attendant circumstances"); *see also Piper Capital Mgmt., Inc.*, Initial Decisions Release No. 175, 2000 WL 1759455 (Nov. 30, 2000) (rejecting Division's failure-to-supervise charge against CEO of mutual fund adviser because adequate procedures were in place and CEO had reasonably delegated responsibility and made "systematic and reasonable" efforts to ensure that supervisors fulfilled their obligations and that procedures were followed), *aff'd on other grounds*, Investment Advisers Act Release No. 2163, 2003 WL 22016298 (Aug. 26, 2003); *Dean Witter Reynolds, Inc.*, Initial Decisions Release No. 179, 2001 WL 47244 (Jan. 22, 2001) (alleged deficiencies in respondent's supervisory procedures "cannot be judged in hindsight or with information learned long after the events in question occurred").

[241] *See, e.g., Back Bay Advisors, L.P.*, Investment Advisers Act Release No. 2070, 2002 WL 32101982 (Oct. 25, 2002) (registered investment adviser sanctioned for failure to adequately supervise investment staff who facilitated 65 illegal cross trades over five-year period); *Scudder Kemper Investments, Inc.*, Investment Advisers Act Release No. 1848 (Dec. 22, 1999) (investment adviser and direct supervisor sanctioned where trader executed more than 100 unauthorized derivatives transactions over 15-month period.); *Nicholas-Applegate Capital Mgmt.*, Investment Advisers Act Release No. 1741, 1998 WL 466733 (Aug. 12, 1998) (investment adviser sanctioned for failing to supervise head trader/portfolio manager who engaged in undisclosed fraudulent trades over two-year period).

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000328

days in question, the Company faced an extraordinary crisis due to the Lehman collapse and subsequent unprecedented redemptions in The Reserve's funds. The Bents respectfully submit that charging supervisory liability here would be a notable departure from SEC precedent.[242]

The Bents were not on notice of any books and records issues as of September 2008, and they should not be charged with supervisory liability. As of KPMG's September 10, 2008 report to the Audit Committee, no pending significant internal control deficiencies had been identified by KPMG.[243] To the extent KPMG had identified minor issues relating to State Street's calculation of subscriptions and redemptions, management had already addressed them.[244] Furthermore, when KPMG had noted control deficiencies prior to September 2008, the Company took action to correct them and KPMG had not noted the deficiencies again.[245] RMCI utilized both an internal audit team and a Chief Compliance Officer, and its holding company, Reserve Management Corp., had successfully completed a SAS-70 audit in August 2006 in which the auditor found reasonable assurance that the daily NAV for each fund was calculated appropriately.[246] Because the Bents were not on notice of any control deficiencies existing as of

[242] *See, e.g.*, *Piper Capital Mgmt., Inc.*, Initial Decisions Release No. 175, 2000 WL 1759455, *aff'd* Investment Company Release Act, 2003 WL 22016298 (Aug. 26, 2003) (noting "extraordinary confluence of events" on first day of crisis and finding that no violations arose from fund managers' initial efforts to determine fair value prices in order to calculate fund's NAV).

[243] RF-SEC-WH-00000057-169.

[244] RF-SEC-WH-00000057-169 (noting that The Reserve management had corrected "certain deficiencies in internal control that [KPMG had] not considered to be significant deficiencies or material weaknesses" relating to the calculation of gross, rather than net, subscriptions and redemptions by the funds' transfer agent and fund accountant, *i.e.*, State Street).

[245] RF-SEC-WH-00000057-169. To the extent that KPMG identified issues with the CFO's finance team, those issues — which do not relate to the books and records issues alleged here — were promptly addressed. For example, in May 2006, KPMG noted a significant control deficiency, noting that the Yield Plus Fund's financial reporting process "as observed was not efficient and relied too heavily on higher-level managerial reviews to identify and correct simple reporting mistakes..." Management responded that the new CFO was "reviewing the process and [was] modifying procedures so as to streamline the report preparation to ensure higher quality in the statement generation process." After the Company implemented new procedures, this issue was not cited by KPMG in any subsequent audit.

[246] RF-SEC-WH-00000207-42.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000329

September 15, 2008, they should not be charged with books and records violations in connection with the events of September 15 and 16.[247]

B. The Bents Do Not Have Supervisory Liability for the Accounting-Related Functions Performed by the Finance Department and by the Company's Fund Accountant, State Street Bank, to Calculate the NAVs for the Funds

The Bents appropriately relied on Farrell and the Finance Department to calculate the NAVs for the Funds on September 15 and 16. Delegation of this responsibility was reasonable given the Bents' knowledge of Farrell's qualifications and experience, as well as assurances that Farrell made to the Bents.[248]

In his first conversation with the Bents mid-morning on September 15, Farrell offered to monitor the NAVs of the funds, and he told the Bents that he would be able to do so.[249] Farrell also informed the Bents that he was in contact with Lentinello regarding accounting matters for the Primary Fund.[250]

Over the course of Farrell's three-year tenure at the Company, the Bents had learned that they could depend upon his expertise and good judgment. They also knew that Farrell could be counted on to supervise Lentinello in calculating NAVs and performing other accounting functions for the Funds. As Bruce Sr. testified:

> Mr. Lentinello has a long history in the mutual fund business, he is supervised by our CFO, Patrick Farrell, who is a CPA who's got twenty or

[247] In *Piper Capital Mgmt.*, 2000 WL 1759455, the administrative law judge rejected the Division's failure-to-supervise charge against the CEO of a mutual fund management company, noting that the CEO had established a "multi-layered and integrated internal supervisory system" consisting of "(1) [the management company's] Operations Department; (2) a Risk and Control Committee; (3) an Audit Committee; and (4) the Board of Directors." The Reserve also had similar supervisory elements in place, which included a Credit Committee, an Investment Policy Committee, and a Valuation Committee. Deposition of Bruce Sr., dated Oct. 29, 2008, at 29:2-30:17, 44:10-48:8, 84:6-21.

[248] *Dean Witter Reynolds Inc.*, 2001 WL 47244 (Jan. 22, 2001) (alleged deficiencies in supervisory procedures "cannot be judged in hindsight").

[249] Deposition of Arthur Bent, dated Dec. 11, 2008, at 60:6-61:10.

[250] Deposition of Arthur Bent, dated Dec. 11, 2008 at 60:6-61:10.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000330

> more years in the mutual fund business and these are things that they do on a regular basis. They're experienced people and we rely on them to do their work.[251]

The Bents further understood that the Finance Department would keep them informed about the NAVs of the funds.[252]

However, on September 16, the Primary Fund's NAV was computed on the basis of prices for portfolio holdings that did not take into account the previous day's write-down of all of the Fund's Lehman securities. Neither Farrell nor Lentinello identified the mistake on September 16, and, as a result, the NAV for the Primary Fund fell below $1.00 per share several hours earlier than the Fund reported that day.[253]

The Bents are not personally liable for these inadvertent errors in the midst of extraordinary circumstances. The managers responsible for the computation of the NAV made an honest mistake, and there is no indication that Bruce Sr. and Bruce II were aware of the mathematical error. To the contrary, when the Trustees valued the Lehman debt at zero, and the Bents understood that the Fund was no longer trading at $1.00 per share, they supported disclosure of the event to the market.

C. Because the Receivables Booked by Lentinello on September 15 Were Not Authorized, the Bents Should Not Be Charged for These Errors

As explained *supra* at Section III, Bruce II notified Lentinello on September 15 that there might be a need to set up receivables for funds that held Lehman debt.[254] Although Lentinello was never authorized to book the receivables, he sent an e-mail mid-morning on September 16,

---

[251] Deposition of Bruce Sr., dated Nov. 20, 2008 at 144.

[252] Deposition of Arthur Bent, dated Dec. 11, 2008, at 84-85 (Farrell was "well aware" that he should inform the Bents if the Primary Fund ceased to trade at $1.00 per share; Lentinello knew to contact them directly if he could not reach Farrell).

[253] Deposition of Bruce Sr., dated Nov. 20, 2008, at 142:20-144:23.

[254] Declaration of Bruce II, dated Jan. 23, 2009, at ¶ 8.

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

indicating that he had done so.[255] Receivables in the amounts of $1.7 million for the Yield Plus Fund and $14.8 million for the International Liquidity Fund had been booked the day before, on September 15.[256] Bruce II directed that the erroneous receivables should be corrected as soon as he learned of them on September 16,[257] but they were not reversed until September 24.[258] Because Lentinello exceeded the scope of his authority in booking the $16.5 million in receivables, the Bents should not be held accountable for his error.[259]

D. THE BENTS SHOULD NOT BE CHARGED FOR PUBLICATION OF THE *RESERVE INSIGHTS* ARTICLE

As explained *supra* at Section 2(D), RMCI's marketing professionals unilaterally bypassed the Company's established review procedures and made inaccurate disclosures, including the *Reserve Insights* article. Until this aberration occurred, the marketing staff had always obtained approval from Bruce Sr. and Bruce II of the final version of all investor communications.[260] Nor did the Bents rely solely on past practices and procedures, as Bruce II instructed Lansky via e-mail that "*if [he] wants to put something on the website [Bruce II] need[s] to see language for approval first*[.]"[261] The article was posted for less than one day –

---

[255] RF-SEC-00204898.

[256] The $240,000 receivable purportedly booked on September 1, 2008 appropriately includes over accrued interest from State Street. In any event, there has been no suggestion that this receivable should have put the Bents on notice of any issues with receivables in the funds, and KPMG did not note any issues with receivables in its September 10, 2008 audit report.

[257] Declaration of Bruce II, dated Jan. 23, 2009, at ¶ 12-13.

[258] RF-SEC-00211484.

[259] For the same reasons, the Bents should not be charged for the Company's failure to report that the Yield Plus Fund had broken the buck on September 15. *See* Deposition of Arthur Bent, dated Dec. 11, 2008, at 97:10-20 (regarding effect of receivables on calculation of NAVs for funds).

[260] Deposition of Bruce Sr., dated Nov. 3, 2008, at 27:20-32:12 (describing process for vetting and approval of written communications to shareholders and testifying that he does not know why Reserve Insights piece did not go through entire process); Deposition of Bruce II, dated Nov. 25, 2008, at 95:17-97:7 ("I don't believe [the article] was ever approved to be released.").

[261] RF-SEC-00201159 (emphasis added).

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

from 8:15 a.m. until later that morning.[262] Once the mistake was realized, DiMartino contacted Crowley and Bruce II to ensure that the article was removed from the website immediately.[263] In contrast, the Commission usually pursues charges only when such misstatements have remained uncorrected for months.[264] Because the *Reserve Insights* article was posted in error, then taken down within hours, the Commission should decline to pursue charges on this basis.

E. THE BENTS ALSO ARE NOT LIABLE AS AIDERS OR ABETTORS FOR BOOKS AND RECORDS VIOLATIONS

Aider and abettor liability requires a higher level of awareness than does supervisory liability.[265] Because there is no basis to find even supervisory liability here, the Bents should not be charged for books and records violations as aiders or abettors.

Accordingly, we strongly believe that no action of any kind against the Bents is warranted or justified.

---

[262] RF-SEC-00162771 (indicating the article was posted at 8:15 a.m.); RF-SEC-00001955-1956 (11:46 a.m. e-mail from Lansky to Hatch notes "will find out about insights piece, but for now, don't send anything until find out why taken down").

[263] RF-SEC-WH-00000046-48.

[264] *See David B. Gosse,* Exchange Act Release No. 34-45474, 2002 WL 261959, at *1 (Feb. 25, 2002) (links to false press releases remained on company website for several months); *John Christopher McCamey*, Initial Decisions Release No. 230, 2003 WL 21396458 (June 17, 2003) (false and misleading statements posted on broker-dealer website for several-week period); *CancerOption.com, Inc.*, Exchange Act Release No. 34-43246, 2000 WL 1280326, at *2 (Sept. 6, 2000) (false analyst reports posted on company's website for six months).

[265] Aiding and abetting liability requires proof of "(1) a primary securities law violation; (2) that the aider and abettor knowingly and substantially assisted the conduct that constitutes the violation, and (3) awareness or knowledge by the aider and abettor that his or her role was part of an overall activity that was improper." *Back Bay Advisors, L.P.*, Investment Advisers Act Release No. 2070, 2002 WL 32101982, at *6 (Oct. 25, 2002) (internal citations omitted).

CONCLUSION

For the foregoing reasons, as well as the reasons set forth in the submission of RMCI, to the extent applicable, the Commission should not commence any proceeding against the Bents regarding their response to an unprecedented run on The Primary Fund on September 15 and 16, 2008.

Dated: New York, New York
January 23, 2009

WILMER CUTLER PICKERING
HALE AND DORR LLP

By:

Robert B. McCaw
Lori A. Martin
Susan Schroeder
399 Park Avenue
New York, New York 10022
(212) 230-8800

James E. Anderson
Sarah Stafford
1875 Pennsylvania Avenue, NW
Washington, DC 20006
(202) 663-6000

Attorneys for Bruce R. Bent, Sr. and Bruce R. Bent II

Confidential Treatment
Requested by
WILMER CUTLER PICKERING
HALE AND DORR LLP

RF-SEC-WH-00000334