

UNITED STATES DISTRICT COURT FOR THE
SOUTHERN DISTRICT OF NEW YORK

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In re THE RESERVE FUND SECURITIES AND DERIVATIVE LITIGATION	09 MD. 2011 (PGG)
SECURITIES AND EXCHANGE COMMISSION, Plaintiff, v. RESERVE MANAGEMENT COMPANY, INC., RESRV PARTNERS, INC., BRUCE BENT SR., and BRUCE BENT II, Defendants, and THE RESERVE PRIMARY FUND, Relief Defendant.	ECF CASE 09 Civ. 4346 (PGG) <u>ORDER</u>

PAUL G. GARDEPHE, U.S.D.J.:

On November 25, 2009, this Court issued a Memorandum Opinion and an accompanying Order that, inter alia, provided for the pro rata distribution of the remaining assets of the Primary Fund and enjoined all claims against (1) Primary Fund assets, including shareholder claims against the Primary Fund; and (2) any of the Defendants and any of the Defendants' officers, directors, trustees, representatives, agents or employees to the extent that such claims are subject to indemnification by the Primary Fund.

The November 25 Opinion also provided that distributions made to "straddler" investors – those who were permitted to redeem a portion of their shares at a \$1.00 NAV on September 15, 2008 – "should be offset such that their total per share recovery does not exceed

that of any other investor participating in the final pro rata distribution. This offset is applicable only where the specific party that received payment on September 15, 2008, is identical to the party participating in the final distribution.” Nov. 25 Order ¶ 2(b) (Dkt. No. 202).

On December 11, 2009, this Court issued an Order setting forth its expectation, based on the representations of the parties, that \$3.4 billion of the \$3.5 billion remaining in the Primary Fund will be distributed to investors by the week of January 25, 2010. The Order further directed that if the parties encounter any obstacle to disbursing this amount by the week of January 25, they are directed to bring the issue to the Court’s attention immediately. (Dkt. No. 212)

On December 22, 2009, this Court received a letter from Christopher J. Clark, counsel for Defendants Reserve Management Company, Inc. (“RMCI”), Resrv Partners, Inc., Bruce R. Bent, Sr., and Bruce R. Bent II. (Dkt. No. 216) The December 22 letter outlined a number of issues that have arisen as RMCI prepares to implement the distribution of Primary Fund assets and made recommendations as to how these issues should be resolved. In response to this letter, the Court received submissions from the Commission and several claimants to Fund assets. On January 11, 2010, this Court issued an Order resolving all but one of the issues identified in the December 22 letter. (Dkt. No. 247)

The issue left open by the January 11 order was the treatment of straddler investors who are customers of omnibus retail brokers and banks. Defendants’ December 22 letter indicates that RMCI’s relationships as to such accounts are with the intermediary omnibus brokers or banks and not with the customers of these institutions. (Def. Dec. 22 Ltr. 2) Because all of RMCI’s account information is at the level of the intermediary, RMCI does not have a mechanism to determine which underlying individual account should be subjected to the

straddler offset. Id. Defendants propose to exempt omnibus accounts from the straddler offset and to permit all omnibus investors to recover a pro rata share of the distribution of Primary Fund assets. Id. at 2-3.

The Commission submitted a letter addressing this issue on December 31, 2009. The Commission argued that exempting omnibus accounts from the straddler offset would be inequitable and sought instead to apply the offset at the beneficial ownership level. (SEC Dec. 31 Ltr. 1-3) The Commission noted, however, that “[t]he critical inquiry at this stage is whether RMCI (or anyone else on the Primary Fund’s behalf) can create a reliable list of beneficial owners that can be used to carry out the Court’s Order as it pertains to straddlers, and, if so, at what cost and what delay.” Id. at 3. The Commission further stated that “[i]t may be that the costs involved in determining the beneficial owner straddlers would exceed the benefit achieved by offsetting their distribution by the amount they received.” This comment was in large part echoed by claimants IBM, Lazard Frères, Lazard Group, Qualcomm and FLO TV. (IBM et al Ltr. 2)

In a January 4, 2010 letter, the Defendants responded by outlining the “enormous logistical problems” that would result from attempting to apply the straddler offset to shareholders who invested through omnibus accounts. (Def. Jan. 4 Ltr. 2) RMCI would, they contend, be required to “determine which of its customers are holding shares for other beneficial owners” and to “obtain information from each bank and broker sufficient to not only identify the beneficial owner, but also to track and analyze all transactions (including those relating to stocks, bonds, dividends, etc.) undertaken by that beneficial owner.” Id. at 2-3. This process could, Defendants estimate, take as long as five to six months and cost “many hundreds of thousands, if not millions of dollars.”

In its January 11 Order, this Court directed Defendants to provide additional information about the feasibility of applying the straddler offset to customers of omnibus retail brokers and banks at the beneficial ownership level. Since that time, Defendants have worked diligently with the Commission and the Court in an effort to resolve this issue and to determine the cost and delay associated with such an effort. This Court conducted telephone conferences concerning these issues on January 15, January 20 and January 21, 2010.

On the basis of these conferences and the submissions concerning this issue, the Court has determined that RMCI lacks the information necessary to identify straddler investors who are customers of omnibus retail brokers and banks at the beneficial ownership level. The Court has further determined that any effort to identify such customers at the beneficial ownership level would be costly and would significantly delay the distribution of \$3.4 billion planned for this week. As a result, Defendants' proposal to exempt omnibus account holders from the straddler offset is the most efficient approach to ensure that the bulk of the remaining Primary Fund assets are distributed to investors as expeditiously as possible.

Some omnibus account holders may not be identified as such in RMCI's records. For example, the Commission has indentified BMO Nesbitt Burns Corporation as an omnibus account holder that would, under the terms of the November 25 Opinion and Order, be classified as a straddler. (SEC Dec. 31 Ltr. 2) This entity, however, is not registered as an omnibus account holder with RMCI. (Def. Jan. 4 Ltr. 2 n. 1) As a result of such discrepancies, it is possible that some accounts might be subjected to the straddler offset that ought to be exempt pursuant to the omnibus account exception. Accordingly, any account holders who believe that the straddler offset was improperly applied to their account will be given an opportunity, as set forth below, to make that argument to the Court and to obtain their full pro rata share of the

distribution if appropriate. Based on the parties' representations, the Court expects that the funds being held back from the pro rata distribution to be carried out this week should be more than sufficient to satisfy these potential claims.¹

Accordingly, it is hereby ORDERED that all accounts designated as omnibus accounts in RMCI's internal records or otherwise known by RMCI to be omnibus accounts shall be exempt from the straddler offset provided for in Paragraph 2(b) of the November 25 Order.

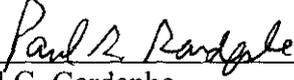
It is further ORDERED that RMCI shall send contemporaneous notice by first class U.S. Mail to account holders whose holdings were subjected to the straddler offset informing the account holders that: (1) their account was subjected to the straddler offset; and (2) if they believe that application of the straddler offset was improper — because their account should have been classified as an omnibus account — they may seek a full pro rata share of the distribution by making application to this Court.

¹ The November 25 Opinion and Order provided for the creation of an Expense Fund to be held back from the pro rata distribution and to be used to satisfy claims for management fees and expenses and for indemnification expenses. The Opinion and Order further provided that any funds remaining in the Expense Fund once these claims have been resolved will be distributed to investors on a pro rata basis. On January 11, 2010, the Defendants, the Relief Defendant and the Independent Trustees submitted various claims for management fees and expenses and indemnification expenses. The Commission estimates that if all of the claims submitted on January 11 were paid in full, \$40 million would remain in the Expense Fund. According to the parties, this amount is more than sufficient to address any potential claims alleging a misapplication of the straddler offset, and these funds will be used for this purpose if necessary.

It is further ORDERED that any such application to this Court must be made by March 1, 2010, and must be supported by evidence sufficient to establish omnibus account status.

Dated: New York, New York
January 26, 2010

SO ORDERED.



Paul G. Gardephe
United States District Judge