Executive Summary

FINRA is issuing this Notice to allow member firms to exchange customer assets that are invested in the Reserve Primary Fund, the Reserve Yield Plus Fund, and the Reserve International Liquidity Fund (the Funds) in bulk for shares of another money market mutual fund or for deposits in an FDIC-insured bank without complying with all of the requirements of NASD Rule 2510(d), subject to certain conditions. In particular, firms may:

- Exchange shares of the Funds either for shares of another money market mutual fund or an FDIC-insured deposit account; and
- Conduct the bulk exchange prior to notifying customers, provided written notification is sent out promptly thereafter.

Questions concerning this Notice should be directed to Thomas M. Selman, Executive Vice President, at (202) 728-6977 or Joseph P. Savage, Vice President and Counsel, at (240) 386-4534.

Background & Discussion

NASD Rule 2510 imposes certain requirements on member firms and their associated persons that have discretionary power over a customer’s account, including prohibitions on excessive transactions, requirements for prior written customer consent as to the individuals possessing discretionary authority, and requirements related to the firm’s review and approval of discretionary orders.²
Rule 2510(d)(2) states that these provisions shall not apply to bulk exchanges at net asset value of money market mutual funds utilizing negative response letters sent to customers, provided certain conditions are met. In order to qualify for this exception:

- The bulk exchange must be limited to situations involving mergers and acquisitions of funds, changes of clearing members and exchanges of funds used in sweep accounts;
- The negative response letter must contain a tabular comparison of the nature and amount of the fees charged by each fund;
- The negative response letter must contain a comparative description of the investment objectives of each fund and a prospectus of the fund to be purchased; and
- The negative response feature must not be activated until at least 30 days after the date on which the letter was mailed.

On September 16 and 17, 2008, The Reserve announced that the net asset values of the Funds had fallen below $1.00 per share. Member firms have inquired whether they may make bulk exchanges of customer assets that are invested in the Funds, to either another money market mutual fund or deposits held at a bank insured by the Federal Deposit Insurance Corporation (FDIC) without complying with all of the requirements of Rule 2510(d)(2). Given the need to protect investors, and after consultation with the Securities and Exchange Commission (SEC) staff, FINRA has agreed to permit bulk exchanges of customer assets invested in the Funds to another money market mutual fund or an FDIC-insured bank account without compliance with all of the provisions of Rule 2510(d)(2), subject to certain conditions.

First, member firms may exchange customers’ assets from the Funds for either shares of another money market mutual fund whose net asset value is $1.00 per share and that is required to comply with Rule 2a-7 under the Investment Company Act of 1940, or for deposits in an FDIC-insured bank. Members must ensure that the money market mutual fund or bank deposit account into which it is moving customer assets is suitable for each customer based on the requirements of NASD Rule 2310.

Second, while member firms may exchange customers’ assets prior to sending out a notice of the bulk exchange, they must notify customers in writing promptly after the exchange. The notice must include the tabular comparison of the nature and amount of fees charged by each fund as required by Rule 2510(d)(2)(B) and the comparative description of the investment objectives of each fund and a prospectus of the new money market mutual fund as required by Rule 2510(d)(2)(C). If customers’ assets are being moved into an FDIC-insured bank account, the notice must include a description of the account, any fees associated with the account, and a listing of the account’s terms and conditions that the bank normally provides to customers opening such an account.
Endnotes

1 For purposes of this Notice, the term “bulk exchange” refers to both the movement of existing customer assets from the Funds to another money market mutual fund or bank account, and the redirection of future customer cash flows into the new fund or account.

2 See NASD Rule 2510(a), (b) and (c).

3 NASD Rule 2510(d)(2).


5 In the past, FINRA has issued guidance under Rule 2510 with regard to proposed bulk exchanges of customers’ money market mutual funds. See, e.g., Staff Interpretive Memo, “Use of a negative response process under NASD Rule 2510(d)(2)(D) to designate an alternative money market sweep fund when existing sweep fund closes with inadequate notice,” (May 15, 2008); Letter from Patricia Albrecht to George T. Simon (Jan. 26, 2005); Letter from Sarah J. Williams to Marc A. Cohn (Feb. 3, 2003). This Notice does not alter this guidance in any respect other than as expressly provided herein with regard to the Funds.

6 Customers who have consented to receiving communications from the member firm electronically may receive the notice in electronic form.

7 The SEC staff has asked FINRA to inform broker-dealers that, in structuring any bank sweep programs, broker-dealers should use the banking “brokered deposit” structure as a template for establishing the legal relationships between the broker-dealer, the bank and the customers.