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March 28, 1979

VIA EXPRESS MAIL

Mr. Joseph Mazella
Division of Investment Management
Securities and Exchange Commission
500 North Capitol Street
Washington, D. C. 20549

Re: Claremont Capital Corporation
No-Action Letter Request

Dear Mr. Mazella:

When we last spoke you indicated you wanted evidence in a Customer Agreement that a broker with whom Claremont Capital Corporation might do a margin or short sale business did not have the unfettered right to obtain securities held as collateral. We have finally completed our negotiations with Merrill Lynch and I am enclosing a copy of the current draft (Draft of 3/15/79) of the proposed form of Customer Agreement between Merrill Lynch and Claremont Capital Corporation. The section limiting the rights of Merrill Lynch to obtain custody of Claremont's assets is Section 3.B., at page 2, wherein it is stated that all securities, commodities and other property of Claremont shall be held in negotiable form in the possession of the custodian of Claremont's assets, but in a separate account in the name of Merrill Lynch. This section goes on to provide that Merrill Lynch agrees that the securities, commodities and other property will at all times be maintained with said custodian unless the same were released back to Claremont or sold or disposed of as permitted under the Customer Agreement. Further, you will note that at the time of directing any disposition of securities, commodities or property by Merrill Lynch, it must provide in the notice that all conditions precedent to the right to direct disposition have been satisfied.

We trust this is responsive to your inquiry and that you will now be in a position to give the no-action letter which we previously requested, at least with respect to an account with a single broker. Please contact the undersigned if you have any questions.

Very truly yours,

Paul A. Webber

encl

cc: Mr. Albert J. Stream
Mr. Erik E. Bergstrom
Mr. Martin Portnoy (w/encl)

RESPONSE OF THE OFFICE OF CHIEF COUNSEL
DIVISION OF INVESTMENT MANAGEMENT

Our Ref. No. 78-480-CC
Claremont Capital Corp.
File No. 811-1641-3

AUG 17 1979

Based on the facts and representations contained in your letters of May 19 and June 8, 1978, and March 28, 1979, but without necessarily agreeing with your legal analysis, we would not recommend action to the Commission under section 17(f) of the Investment Company Act of 1940 ("Act") if all securities, commodities and other property of Claremont Capital Corporation ("Claremont") in a margin account with a broker are held, in negotiable form, in the possession of the custodian of Claremont's other assets, but in a separate account in the name of the broker who has agreed that (1) the securities, commodities and other property in the account will at all times be maintained with the custodian unless released back to Claremont or sold or disposed of as permitted under Claremont's agreement with the broker and (2) in directing any disposition of the securities, commodities or property in the account, the broker must state that all conditions precedent to its right to direct disposition have been satisfied.

It does not seem that Claremont's entering into short sale transactions or purchasing securities on margin would violate section 12(a) of the Act in the absence of any rules thereunder, or that the proposed manner of compliance with section 18(a) of the Act would be inappropriate. If the Commission adopts rules under section 12(a) of the Act, Claremont, of course, will be expected to comply with them.

As we understand your proposal, the 300 percent test would be satisfied whenever a new margin transaction is entered into and whenever there is any increase over the last value, as opposed to value received when sold, in the total value of the securities sold short through any broker. In determining the value of total assets, securities purchased on margin will be valued at their current value, and in determining the indebtedness arising by reason of securities sold short, such securities will be valued at their current value.

You have withdrawn the question under section 18(c) of the Act since Claremont intends to use only one margin broker.

Claremont is a closed-end investment company and our response concerns only such companies and not open-end investment companies.

Stanley B. Judd
Assistant Chief Counsel

SBJ/mll

CC: SRO

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OF COUNSEL
GEORGE HERRINGTON
A. DOWNEY ORRICK
NATHAN D. ROWLEY

CABLE "ORRICK"
TELEX 34 0973

June 8, 1978

Investment Company Act
of 1940/Section 18(c)
(Your Ref. No. 78-480CC)

Office of the Chief Counsel
Division of Investment Management
Securities and Exchange Commission
500 North Capitol Street
Washington, D. C. 20549

Attn: Mr. Mike Lichtenthal

Re: Claremont Capital Corporation

Dear Sirs:

By letter dated May 19, 1978, we requested certain interpretive advice relating to proposed short selling and margin transaction activities of Claremont Capital Corporation (the "Company"). This letter is intended to supplement our earlier one and requests concurrence in our conclusion with one other aspect of the proposed activities. The description of the proposed activities of the Company is set forth in our May 19 letter which is hereby supplemented in the following respects.

The Company contemplates that it would establish margin accounts with more than one broker-dealer and that there would be activity in each of such accounts concurrently. The principal reason for having multiple accounts opened and operating concurrently relates to the proposed short selling activity by the Company. In connection with a short sale, the broker through whom the trade is effected loans the securities sold short and must either take them from its own inventory or borrow them from a third party. No one broker will necessarily be able to borrow all of the securities which the Company may sell short nor would it have all such securities in inventory. Moreover, some brokers are in a better position than others to borrow specific securities sold short (or otherwise hold open a short position) for the periods of time necessary to accomplish the investment objective of the short seller. In other words, no one broker would necessarily be able to provide all execution and short sales support services which the Company hopes to obtain.

Accordingly, the Company proposes to execute customer agreements with a number of broker-dealers, and under its Custodian Agreement would transfer, into special segregated accounts with the Custodian, specific securities and cash to be held as collateral for margin transactions and short sales with each individual broker. It is not contemplated that securities and cash segregated to support margin transactions and short sales with a single broker-dealer would be commingled with any other securities or assets of the Company.

Supplemental Interpretive Advice Requested

We would appreciate your concurrence in our conclusion that the concurrent operation by the Company of multiple margin accounts, each of which would have separate cash and other collateral securing the same, would not constitute multiple classes of senior securities in violation of Section 18(c) of the Investment Company Act of 1940 (the "1940 Act").

Section 18(c)

Section 18(c) provides:

> "[It is unlawful] for any registered closed-end investment company to issue or sell any senior security representing indebtedness if immediately thereafter such company will have outstanding more than one class of senior security representing indebtedness,...except that (1) any such class of indebtedness...may be issued in one or more series: Provided, That no such series shall have a preference or priority over any other series upon the distribution of the assets of such registered closed-end company or in respect of the payment of interest... and (2) promissory notes or other evidences of indebtedness issued in consideration of any loan,... made by a bank or other person and privately arranged, and not intended to be publicly distributed, shall not be deemed to be a separate class of senior securities representing indebtedness."

We believe that pursuant to the second exception of Section 18(c) as interpreted by the Commission, the establishment of more than one margin account should not be deemed to be the issuance of separate classes of senior securities. Alternatively, we believe that all margin accounts are one class of indebtedness and that each separate account may be viewed as a series with no series having preference or priority over any other series within the meaning of the first exception of Section 18(c).

Second Exception

Since each of the margin accounts which the Company would maintain would be "privately arranged" and certainly not intended for public distribution, exception two on its face would seem to apply so that the existence of multiple accounts each of which had separate collateral would not seem to constitute separate classes of senior securities. This is also consistent with the conclusions reached by the Commission in Israel Development Corporation, Investment Company Act Release 3214 (March 16, 1961).

Israel involved the proposed public issuance by a closed-end investment company of debentures while private loans, secured by pledges of its portfolio securities, were outstanding. In the decision, the Commission interpreted the second exception of Section 18(c) to mean that a closed-end company could have outstanding both publicly distributed and privately arranged debt securities without the latter being deemed a separate class of senior securities, if there were no differences in the preferences as to assets and interest of any outstanding indebtedness. The Commission viewed Section 18(c) as a whole and concluded that the purpose of the section was to preclude the creation of multiple strata debt securities since this creates complexities and risks to public investors of a type which the 1940 Act was intended to prevent. Debt securities having different preferences make difficult appraisal by an investor of his own rights, and the use of preferences may impair his investment position. For these reasons the Commission concluded that exception two of Section 18(c) was intended only to make clear the factor of public or private issuance of debt, in and of itself, was not a separate basis for classification.

With respect to the proposed multiple margin accounts of the Company (and multiple pledges to support the same), the evils perceived in Israel would not be present. First of all, there would be no confusion by public investors holding a different class of debt, since all of the margin accounts will be held by broker-dealers. (There would in fact be no publicly-held debt outstanding.) The financial statements of the Company would disclose the existence of margin account debts and that the same were secured by separate pledges. Further, since the Company is permitted by its fundamental investment policies to encumber its assets, the Company clearly could have a debt outstanding with a single financial institution, secured by a pledge, and that in and of itself would not create an 18(c) problem. Since this is the case, whether it creates one large debt with one large pledge with one broker, or a number of smaller pledges with a number of brokers, should create no different risk to a public investor. In addition, the brokers with whom margin accounts were opened would not be confused about their respective rights vis a vis the Company since they are sophisticated and able to fend for themselves. Further, since the margin accounts would not be with affiliated persons (and this will be the case), the risk for abuse is minimal or not existent.

Moreover, we do not believe that the import of Rule 18c-1 under the 1940 Act is inconsistent with Israel or with our conclusions. Rule 18c-1 provides that the issuance of multiple classes of debt securities by an SBIC is not prohibited by Section 18(c) so long as the SBIC does not have any public debt outstanding and all securities of the class are privately held by institutional investors. As originally proposed, Rule 18c-1 would have permitted an SBIC to have outstanding indebtedness to the Small Business Administration ("SBA") and other lenders so long as indebtedness issued to other lenders would not have preference over indebtedness issued to the SBA. As so proposed, the Rule would have allowed an SBIC to issue public debt securities, private unsecured debt securities and debt securities to the SBA which might have priority over the other two types of debt securities. Release No. 3324, Sept. 12, 1961. However, comments were received by the Commission regarding

the proposed Rule 18c-1 "which indicate[d] that it would be desirable to permit indebtedness to be issued to persons other than the SBA for which specific collateral would be pledged. The Rule as adopted permits this so long as no publicly held indebtedness is issued." Release No. 3361, Nov. 17, 1961.

The significance of the Rule in our view is found in its history rather than in its terms, and we believe it was intended to make clear that SBIC's could not have public and private debts outstanding at the same time, and to limit the holders of all private debt to institutional investors rather than any "person" as permitted under the second exception of 18(c). To conclude that the Rule has broader significance would render the second exception of 18(c) meaningless and would also be inconsistent with the Commission's interpretation thereof contained in Israel, i.e., that the exception is intended to make clear that "private versus public" was not a basis for separate classification.

Accordingly, we believe that the Company should be able to establish and maintain concurrently more than one margin account with more than one broker (each collaterized with separate cash and securities) without violating Section 18(c), in reliance on the second exception.

First Exception

Alternatively, establishment by the Company of more than one margin account should be viewed as being within the first exception of Section 18(c) as the issuance of one class of debt securities in more than one series with no series having preference over any other series. Although "class" is not defined in the 1940 Act, whether securities are of the same class depends upon whether they have the same preference or priority as to assets or in payment of interest.

While each margin account would be separately secured, the rights between margin accounts would be on a parity in that each would be looking to a separate pool

of assets (when imposing the mark-to-market requirements of the broker in question), and to the extent there were deficiency each such broker would be an unsecured creditor of the Company for any balance. Hence, none of the specific accounts would have priority over any other with respect to assets upon distribution since each should be viewed as being on a parity with the other with respect to the secured portion of the account and with respect to any unsecured deficiency each would also be on a parity.

Based upon the foregoing, we believe that the Company should be permitted to establish and concurrently maintain more than one margin (and short selling) account with more than one broker without violating multiple class limitations of Section 18(c) of the 1940 Act. Pursuant to Investment Company Act Release No. 6330, we are transmitting one signed and two additional copies of this letter.

Very truly yours,

Paul A. Webber

cc: Mr. Albert J. Stream
Mr. Erik E. Bergstrom
Mr. Boh A. Dickey
Mr. Stanley B. Judd

CONFORMED COPY

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May 19, 1978

Investment Company Act of
1940/Sections 12(a)(1),
12(a)(3), 17(f), 18(a)
and 18(c)

Office of Chief Counsel
Division of Investment Management
Securities and Exchange Commission
500 North Capitol Street
Washington, D.C. 20549

Re: Claremont Capital Corporation

Gentlemen:

Claremont Capital Corporation (the "Company") is a closed-end, management investment company registered under the Investment Company Act of 1940 (the "Act"). Its primary investment advisor is Claremont Advisers, Inc. At the Annual Meeting of its Stockholders held December 29, 1977 the Company's stockholders approved amendments to the Company's Fundamental Investment Policies to permit borrowing (including margin transactions and short selling). For your information a copy of the Notice of Annual Meeting of Stockholders and accompanying Proxy Statement is enclosed herewith. The vote in favor of such modification of the Company's Fundamental Investment Policies was 908,307 to 69,945; in terms of percentages 61.97% of the shares outstanding voted for the modification and only 4.77% voted against.

At the time the Proxy Statement was submitted to the staff of the Securities and Exchange Commission (the "Commission") for review, the staff requested that the Company agree, as set forth on page 19 of the Proxy Statement, that even though no provision of the Act or any rule or regulation of the Commission adopted thereunder limits the extent to which closed-end investment companies may engage in purchases on margin and short selling activities, the Company would not commence margin purchases or short sales or encumber 100% of its assets until such time as interpretative advice or a formal order of the Commission were obtained to the effect that such activities are permitted under the Act. In accordance with that undertaking the following is submitted.

Description of Proposed Activities

To implement a margin transaction and short selling program, the Company proposes to amend its Custodian Agreement (by executing an amendment substantially in the form attached) to provide for the transfer, into a segregated account with the Custodian, of securities and cash to be held as collateral for margin transactions or short sales with a broker. As can be seen, from and after the time of the transfer into such account, the Custodian is directed to take instructions only from the beneficiary broker with respect to dispositions from such account. The Company would also enter into a customer agreement with a broker. Under such agreement, securities and cash held by the broker and belonging to the Company would be held in the possession of the Company's Custodian, and the broker would agree to leave the same in the possession of the Custodian until released or sold or otherwise disposed of in accordance with or under the terms of the customer agreement. Further, the broker would agree that such assets would not be pledged or encumbered by the broker, and that when requested by the Company the broker would cause the Custodian to release to the Company (to its general custodial account) securities, commodities and other property which is entitled to be released according to the terms of the customer agreement.

As indicated above, the Company has the power to encumber up to 100% of its assets. However, I have been advised by the Company that unless mandated by credit requirements of regulatory agencies, such as the Board of Governors of the Federal Reserve Board or exchanges, or by brokers or other lenders with which the Company might do business, the Company does not intend to encumber 100% of its assets, and, in any event, would not encumber assets in excess of what is reasonably necessary to accommodate its proposed credit transactions, with the caveat(s) that (a) it may encumber more than is absolutely necessary to avoid having to mark to market daily, and (b) in order to reduce administrative burdens and costs it would not attempt to retrieve

excess collateral on a daily basis but may leave the same in the segregated account to support future credit transactions.

Interpretive Advice Requested

We would appreciate your concurrence in our conclusions (a) that the implementation by the Company of either margin transactions or short sale transactions (against the box or otherwise) as described above, will not, as such, violate Sections 12(a), 18(a) or 18(c) of the Act, (b) that the contemplated method of effecting encumbered credit transactions will not violate Section 17(f) of the Act, and (c) that the method of computing the 300% asset coverage test described below is proper under Section 18(a).

Sections 12(a), 18(a) and 18(c) of the Act

Section 12(a) of the Act provides that registered investment companies may not purchase securities on margin or effect short sales in contravention of rules, regulations or orders of the Commission. The Commission has not adopted any rules, regulations or orders under Section 12(a). In Emerald Management Company (Available January 21, 1978 - Your reference 77-199CC), the staff indicated that while no rules have been adopted under Section 12(a) applicable to margin transactions or short sales, those activities may be limited by other provisions of the Act, including Section 18. The discussion in the staff response was similar to the discussion contained in the Guidelines For The Preparation of Form N-8B-1 ("Guidelines") (1940 Act Release No. 7221) in which it is stated under "Item 4(b) - The Borrowing of Money - Short Sales" and "Purchases on Margin" - that the staff interprets the prohibitions contained in Section 18(f)(1) of the Act against the issuance of senior securities by open-end companies (except in connection with bank borrowings) to limit short sales to ones involving 100% collateral, and to prohibit margin transactions. The Section 18(f) limitations do not apply to closed-end companies, such as the Company. The latter are not limited with respect to categories of

lenders, but rather are governed only by the 300% asset coverage test of Section 18(a) and by Section 18(c), which limits the classes of senior securities which may be issued by a closed-end company. Accordingly, in our view, so long as the 300% test is met at the time a margin transaction is effected and giving effect thereto, and with respect to short sales, as described below, the implementation of either conventional margin transactions or short sale transactions by the Company will not violate Sections 12(a), 18(a) or 18(c) of the Act.

Section 17(f) of the Act

Section 17(f) requires the assets of an investment company be held by a bank custodian except for certain exceptions not applicable to the Company's proposed program. However, previous interpretive advice letters of the staff, as well as the Guidelines, indicate that in interpreting this provision the proposed arrangements of the Company satisfy Section 17(f).

In the Guidelines, under the caption "Item 4(b) - The Borrowing of Money - Short Sales", it is stated that while a short position is open, proceeds of any short sales are ordinarily held by the broker, i.e., someone other than the registered investment company. Clearly, this contemplates by inference the propriety of such proceeds being held by someone other than the registered investment company in question. Similarly, in The Bank of New York (Available March 16, 1977 - Your Reference No. 76-681CC), the staff indicated that it would not recommend action under Section 17(f) of the Act if the covered call mechanism outlined in the letter of the bank's counsel (dated December 20, 1976) were followed. In that letter, under Section III, it was indicated that once a registered investment company had written a covered call option, the underlying securities would be held by the custodian bank subject to the rights

of the holder of the call; in other words, at least in part for the benefit of someone other than the registered investment company. With respect to the Company's proposed transactions, while its collateral to support margin transactions and short sales (as well as proceeds of short sales) would be held by its Custodian for the benefit of a broker, this is not dissimilar to what was contemplated in The Bank of New York. In both instances, the assets remain with the custodian under circumstances where the registered investment company would not have unrestricted access to the same.

Another letter in which encumbering assets and Section 17(f) were considered by the staff is Stagecoach Fund, Inc. (Available April 13, 1973). While the staff did not agree that the proposed encumbering of 100% of the investment company's assets complied with Section 17(f), in our view the staff clearly suggested that encumbering assets, as such, was not inconsistent with Section 17(f). Rather, what the staff viewed as not permissible was encumbering 100% of the assets of an investment company without there being a compelling business reason to do so.

We believe that the purpose of Section 17(f) is to provide security for the assets of a registered investment company, and in our view this purpose is fulfilled by requiring that incident to margin and short sales transactions the participating broker leave the collateral with the custodian as contemplated above.

300% Asset Coverage Test

As indicated above, the Company is a closed-end company and as such is subject to the debt limitation provisions of Section 18(a)(1) of the Act. Under this limitation, the Company may not issue a senior security which is debt if after giving effect thereto the aggregate amount of senior securities is more than one-third of the assets of the Company (less liabilities exclusive of senior securities) The test is applied at the time of a borrowing which results in the creation of a senior security. It is not a limitation

which applies continuously as is the case for open-end companies under Section 18(f)(1). In applying this test with respect to margin transactions and short sale transactions in which the Company may engage, we believe the appropriate methods of measuring asset coverage to be as follows:

1. Conventional Margin Transactions. These transactions involve an extension of credit by a broker. Once the credit is extended (absent a new or additional credit transaction) the amount is fixed even though the borrower may have to meet margin calls by virtue of marking to market. However, the marking to market will not affect the amount of the debt, but merely the value of the security therefor. Accordingly, we believe that the Company need apply the 300% asset coverage test in the case of a conventional margin transaction only at the time of effecting the same (giving effect thereto).

2. Conventional Short Sales (Not Including Sales "Against the Box"). In these transactions, the "debtor" is borrowing securities rather than a finite sum, and the value of the securities can fluctuate. Accordingly, the securities borrowed would be marked to market by the Company. Hence, the market price of such securities (computed in a conventional manner employed by the investment companies) would be the amount of the "debt" for purposes of the 300% asset coverage test, and would therefore be measured more frequently than at the opening of a short sale.

The Company is most anxious to implement its margin and short selling program, and we stand ready to provide you promptly with any additional information which you believe is necessary. If you have any questions, please call the undersigned at (415) 392-1122. Pursuant to Investment Company Act Release No. 6330, we are transmitting one signed and six additional copies of this letter.

Very truly yours,

PAUL A. WEBBER

Paul A. Webber

encl

cc: Albert J. Stream
Erik E. Bergstrom