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September 4, 2013

Office of the Secretary
of the Commission
U.S. Securities and Exchange Commission
c/o Elizabeth M. Murphy, Secretary
100 F Street, N.E.
Washington, D.C. 20549-4720

Re: Copley Fund, Inc: Application for Order for Exemptive Relief under Section 36 of the Securities Exchange Act; Rule 22c-1 Promulgated under the Investment Company Act of 1940 and Rule 4-01(a)(1) of Regulation S-X

Dear Commissioners:

This Firm represents Copley Fund, Inc. (“Copley” or the “Fund”) and on its behalf, submits this application for an Order for exemptive relief under Section 36 of the Securities Exchange Act of 1934 (the “Exchange Act”), 15 U.S.C. § 78mm, and 17 CFR 240.0-12.¹ Specifically, Copley requests an exemption from Rule 22c-1, promulgated under the Investment Company Act of 1940 (the “ICA”), and Rule 4-01(a)(1) of Regulation S-X that would permit Copley to alter the manner in which it currently accounts for deferred tax liability on unrealized gains. As a condition to, and limitation on, the requested exemption, Copley proposes to account for its deferred tax liability for unrealized gains by establishing a tax reserve based on a pre-set formula designed to present a more accurate and fairer disclosure to the investing public of the Fund’s invested assets and net asset value (“NAV”). The accounting method Copley proposes is virtually identical to that which Copley employed from 1992 to 2007, when the Division of Investment Management (the “DIM” or “Division”) demanded Copley abandon its proven and established method in favor of the full liquidation method for accounting for deferred tax liability generally required under GAAP.

¹ By letter dated August 2, 2013, the Division of Investment Management suggested that Copley may wish to pursue and to submit a request for exemptive relief pursuant to Section 36 of the Exchange Act for consideration by the Commission. See Exhibit A.

A. Summary of Argument

Rote and inflexible application of the rules from which Copley now seeks an exemption requires Copley to set a tax reserve for unrealized gains on the assumption of full liquidation, an inaccurate, “one shoe fits all” approach that is (a) misleading to investors because it substantially understates the Fund’s invested assets and NAV, while overstating its operating expenses, (b) inconsistent with Copley’s uninterrupted history and investment philosophy of reinvesting dividends and accumulating capital gains, and (c) incompatible with Copley’s unique structure and unusual tax issues (both of which the Commission has recognized). *See infra*, at 7. To address these circumstances, as discussed more fully below at pages 15 through 19, Copley presents two alternatively defined formulas for calculating the reserve and allowing pre-set means to sell securities in its portfolio to satisfy extraordinary redemptions if necessary. Additionally, Copley is also prepared to set forth a clearly defined disclosure of the disparate effects in NAV pricing when using the reserve and full liquidation value methods. Finally, Copley is prepared to convert to a Regulated Investment Company (“RIC”) by a pre-arranged commitment, essentially triggered by the unforeseen event of unusually high redemptions.

Pursuant to Section 36 of the Exchange Act, the Commission “may conditionally or unconditionally exempt” Copley from the above-referenced rules “to the extent that such exemption is necessary or appropriate in the public interest and is consistent with the protection of investors.” 15 U.S.C. § 78mm. *See also* 17 CFR 240.0-12 (requiring applicants for exemptive relief to “identify the anticipated benefits for investors and any conditions or limitations the applicant believes would be appropriate for the protection of investors.”) Copley respectfully submits that its proposals, which include (a) a pre-set reserve formula, (b) investor disclosures comparing this method to the full liquidation value method, and (c) Board preparations for RIC conversion (if necessary because of unforeseen events), provide greater benefit to investors than the full liquidation value method Copley is currently required to follow, accompanied by limitations and conditions that appropriately protect investors. Indeed, as set forth in detail in Sections C and D, *infra*, Copley’s proposals meet the Section 36 standard for granting of an exemption for the following reasons:

- Copley’s proposed pre-set formulas for calculating the reserve benefits current and future investors by accurately presenting the Fund’s NAV, as compared to the full liquidation value method, which understates the amount of invested assets under management on which gains or losses are actually realized and overstates the Fund’s operating expense ratio;

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- The Fund's unique structure and operations among open-ended mutual funds make the full liquidation value method particularly misleading to current and future investors by artificially depressing the value of the Fund and its NAV, particularly when the risk of the Fund incurring a tax liability in excess of the proposed pre-set reserve is exceedingly remote (and has never even remotely come close to occurring in the Fund's history of using a similar reserve methodology from 1992 to 2007);
- Copley's Board is prepared to make full disclosures of the Fund's NAV under both methodologies and has established a mechanism for conversion to a RIC in the event unforeseen circumstances were to cause gains to be realized that consumed the entire amount of accumulated deferred income taxes it has realized;
- As an additional benefit and basis for exemption, the proposed reserve methodology is consistent with the fundamental GAAP principles of revenue/realization recognition and matching, adequate disclosure, and that businesses will continue as going concerns. In contrast, as applied to Copley's unique circumstances, the full liquidation value method: (a) misleads investors by failing to accurately convey the true value of the Fund's shares, (b) assumes that the Fund will close, and (c) transforms a contingent liability into a full, current, realized liability while also failing to match current revenue and assets with correct, actual liabilities; and
- Exemption is warranted because the proposed reserve methodology (and associated measures designed to inform and protect investors) comport with the SEC's history of permitting certain flexibility to depart from a strict interpretation of GAAP or other tax accounting provisions where doing so would lead to more accurate reporting.

For many years, Copley has presented multiple legitimate arguments in support of its position that the Fund and its investors have been treated unfairly given the Fund's acknowledged, unique circumstances. As set forth in the procedural history section below, despite a steady stream of letters exchanged between Copley and the DIM over this time, including the Division's interception of a letter from Copley directed to the Commissioners seeking their intervention in this matter, Copley has yet to receive any written substantive response to the Fund's multiple proposals and its conclusion that they would result in a more reasonable, accurate and equitable result for both Copley and its investors.

Because Copley has been forestalled from receiving a reasoned, final disposition of its requests from the Securities and Exchange Commission (the "SEC" or "Commission"), Copley has been stuck in a virtual administrative limbo, suffering economic harm because of the SEC's demands, but unable to obtain due process, let alone a remedy, through administrative channels.

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Indeed, given Copley's inability to obtain review from the Commission, it is faced daily with a Hobson's choice: (a) Copley can continue to report inaccurately its NAV based on an ill-fitting and inappropriate accounting method for its unique circumstances, or (b) the Fund can return to the more accurate accounting methodology it employed for fifteen years and face threatened enforcement action by the Commission.

This application for exemptive relief is Copley's ultimate opportunity and attempt to obtain a reasoned response and due process from the Commission through administrative channels to the multiple legitimate arguments Copley has presented to the SEC and the DIM over several years. Copley respectfully requests that the Commission issue a determination in response to this application for exemptive relief. *See* 17 CFR 240.0-12 (the Commission or Division Director "will issue an appropriate response" to an application for exemptive relief "and will notify the applicant.") (emphasis added). Absent notification from the Commission by **October 4, 2013**, that a final written order disposing of Copley's application will be issued, Copley will have no other recourse but to conclude that it has exhausted all available administrative remedies and, *sub silencio*, that the Commission's actions constitute a final Order denying its application on a full administrative record.

B. Procedural History of Copley's Pursuit of Relief through Administrative Channels

Since 1992, Copley has maintained that the accrual for unrealized capital gains taxes is best represented by a "reserve" established by its Board, rather than the use of a full liquidation value accrual to calculate the Fund's NAV. Until 2007, the SEC had never required that Copley change this methodology. It is this structure for which the Fund now seeks exemptive relief from Rule 4-01(a)(1) of Regulation S-X.

In August of 2007, the DIM for the first time took issue with Copley's accounting for, and disclosure of, tax reserves for unrealized appreciation in its financial statements filed for the year ended February 28, 2007. In a comment letter dated September 26, 2007 (the "Comment Letter"), the DIM asserted that Copley had failed to account properly for deferred tax liabilities and assets for the future tax consequences of events recognized in its financial statements, as required by FAS 109 and in violation of Rule 4-01(a)(1) of Regulation S-X, which provides that "financial statements filed with the Commission which are not prepared in accordance with generally accepted accounting principles will be presumed to be misleading or inaccurate, despite footnote of other disclosures, unless the Commission has otherwise provided." (A copy of the Comment Letter is annexed hereto as Exhibit B.) It is not clear from the DIM's

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correspondence what caused it to change its view in 2007 and suddenly to require Copley to change its methodology.

In the Comment Letter, the DIM noted that Copley has elected to operate as a subchapter C Corporation, and not a RIC, and that it was unaware of any other investment company that chose not to qualify as a RIC that did not accrue a deferred tax liability associated with its unrealized appreciation. (Ex. B at 3-4.) The DIM explicitly acknowledged Copley's willingness to convert to RIC status in the event unforeseen circumstances caused gains to be realized that consumed the entire amount of accumulated deferred income taxes that Copley had recognized. (*Id.* at 5-6.) It did not, however, address – and, to date, still has not addressed—whether conversion would satisfy the SEC's concerns regarding the Fund's tax accounting.

By letter dated November 30, 2007, the Division of Enforcement's Boston Regional Office expressed to Copley its intent to seek immediate injunctive relief against the Fund if it did not adjust its per share NAV to account for the full liquidation liability for tax on unrealized capital gains. (A copy of the November 30, 2007 Letter is annexed hereto as Exhibit C.) To avoid such injunctive litigation with the Commission, Copley's Board approved shortly thereafter an adjustment of the Fund's NAV using the SEC's preferred full liquidation value methodology.

On March 21, 2008, the Division of Enforcement informed Copley that it was conducting an informal investigation of the Fund into possible violations of the securities laws, and requested that the Fund provide certain information on a voluntary basis. The Commission apparently later converted the proceeding into a formal investigation against Copley and its CEO Irving Levine for potential violations of certain antifraud provisions, namely, Section 34(b) of the ICA, Rule 22c-1(a), promulgated under Section 22(c) thereunder, Section 17(a) of the Securities Act of 1933 (the "Securities Act"), and Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder; as well as a books and records violation under Section 204 of the Investment Advisors Act of 1940 and Rule 204-2 promulgated thereunder.² Copley fully cooperated with the investigation.

On July 18, 2008, Copley was required to restate its historical financial statements to account for the full liquidation value methodology required by the SEC and filed an amended Form N-CSR/A containing a Restated Annual Report to its shareholders. (A copy of that filing is annexed hereto as Exhibit D.) As set forth therein, this accounting change instantly reduced

² The Commission's request for information and its Formal Order of investigation are not being annexed hereto because they are non-public documents. Copley presumes that the Commission has access to those records.

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the Fund's per share value by \$13.89 by increasing a deferred tax liability to a level that would be realized only if the entire appreciated portfolio were liquidated. (*See* Ex. J., at 3.)

On or about November 19, 2008, in an effort to resolve the investigation, Thomas Henry, Esq., Copley's then-counsel, sent a letter to James S. Goldman, Esq., of the SEC's Boston Regional Office, enclosing a memorandum that described in detail the negative impact of the change in methodology and the reasons Copley's original reserve methodology was in the best interests of the shareholders (the "November 2008 Memo"). (A copy of the November 19, 2008 letter, with its enclosures, is annexed hereto as Exhibit E.) Among other things, the letter explained that Copley's change in methodology to a full liquidation value accrual in calculating the Fund's per share NAV had resulted in misleading and inconsistent financial statements that did not reflect the fair or accurate value of the Fund's shares. The letter also enclosed a proposed Prospectus Supplement that would provide disclosures to the shareholders necessary for their consideration of the risks associated with this methodology. We understand that correspondence was shared with the DIM.

Copley has not received a substantive response to the November 19, 2008 letter to Mr. Goldman. In February of 2009, Copley was informed by Mr. Goldman that the investigation of the Fund had been reassigned to Lawrence Pisto, Esq., also of the Boston Regional Office. Thereafter, the Division of Enforcement took testimony of, among others, Irving Levine and Copley's outside accountant, Roy Hale.

On October 5, 2009, Mr. Henry sent a letter to Mr. Pisto to follow up on a prior telephone conversation to inquire about the status of the investigation. With that letter, Mr. Henry re-submitted the November 2008 Memo and proposed Prospectus Supplement. (A copy of Mr. Henry's October 5, 2009 letter, with its enclosures, is annexed hereto as Exhibit F.) As detailed therein, Mr. Henry argued that a certain degree of flexibility is appropriate under GAAP and FAS accounting standards and under the SEC rules, and that such flexibility was warranted here. Further, Mr. Henry reiterated Copley's willingness to provide transparent disclosures to its investors and requested a meeting with the DIM.

Our understanding is that the requested meeting did not take place. Instead, in a December 2, 2009 letter, the DIM responded to Mr. Henry's October 5 letter and asserted that Copley had provided neither any new arguments not previously considered by the DIM, nor any "changes in the Company's circumstances that might cause reconsideration of [the DIM's] original position." (A copy of the December 2, 2009 letter is annexed hereto as Exhibit G.) In that letter, the DIM informed Copley that it would again recommend immediate enforcement

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action if Copley were to submit financial statements that did not comply with ASC 740 (which codified FAS 109) by using the methodology required by the DIM.

On March 5, 2010, Kevin Kelcourse, Esq., Assistant Regional Director from the Boston Regional Office, informed Mr. Henry by letter that the investigation of Copley and Mr. Levine was officially completed and that the Division of Enforcement would not recommend enforcement action. Thus, the investigation closed without any penalties. Nonetheless, Mr. Kelcourse's letter reiterated that if Copley did not comply with the requirements of FAS 109 and/or re-codified ASC 740, the Division of Enforcement would recommend enforcement action by the Commission. (*See Exhibit H.*)

Following the closing of the investigation, Copley and its counsel engaged in further communications with the DIM in an effort to reach a mutually acceptable resolution of this issue. For example, on July 15, 2010, Mr. Henry exchanged e-mails with Kevin Rupert of the DIM's staff concerning proposed modifications to Copley's financial statements. In that exchange, *Mr. Rupert acknowledged the unique structure of the Fund*, stating that, "While we have been firm on not permitting footnotes, *this fund has really unusual tax issues*, and for this reason an explanatory footnote *might* be permitted – but I make no promises." (Exhibit I (emphasis added).)³

On September 28, 2011, Copley, through its counsel, David Faust, Esq., sent the DIM the request for no-action assurance referenced earlier. The September 28 Letter explained in detail why the use of the DIM's full liquidation value methodology is inappropriate given the unique nature of the Fund, is inconsistent with its investment philosophy, policy and practice, has led to misleading financial statements and reporting that understates the amount of assets under management and does not represent the true value of the Fund's shares. (*See Exhibit J.*) Moreover, Mr. Faust explained that the Commission's refusal since 2007 to permit Copley's management to exercise any discretion with respect to deferred tax accounting differed from its treatment of Weyerhaeuser Corporation, which apparently had been permitted to depart from a literal reading of a required tax accounting provision. *Id.* Indeed, as more fully explained in the sections below, the Commission's position with respect to Weyerhaeuser and other similarly situated companies contradicts its position with respect to Copley.

³ The DIM apparently did deviate from its normal practice of not permitting footnotes, as Copley's semi-annual shareholder report for the period ended August 31, 2010, includes footnotes to its financial statements clarifying the nature of the deferred tax liability. (*See Exhibit K.*)

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After Copley's letter of September 28, 2011, and subsequent discussions with DIM representatives failed to yield a written response from the DIM, Copley, through a 15-page letter to the division dated March 28, 2012, from its counsel, Blank Rome LLP, sought a continuation of its request for a written opinion from the DIM permitting the Fund to alter the manner in which it accounts for deferred tax liability for unrealized gains. (A copy of Blank Rome's March 28, 2012 letter to the DIM is attached hereto as Exhibit L.)⁴ As in this application for exemptive relief, Copley described in detail: (a) its past efforts to address the Commission's concerns; (b) arguments explaining why rote application of Rule 4-01(a)(1) of Regulation S-X yields inaccurate and misleading information to investors concerning the Fund's NAV; (c) relevant precedents showing the Commission's deviation from strict application of the rules in like circumstances; and (d) Copley's proposals for a structured reserve formula and conversion to a RIC should unforeseen circumstances so require.

Over a year later, the DIM responded to Copley's March 28, 2012 letter and denied its request for "No Action" relief in a brief letter dated April 5, 2013. (This letter is attached hereto as Exhibit M.) Despite Copley's attempt to engage the Division in an informed debate concerning Copley's unique circumstances and the Commission's deviation from routine application of the rules in similar circumstances, the DIM simply denied Copley's request because the Fund's proposals "would not comply with GAAP as it would result in Copley recognizing only a portion of the deferred tax liability required by ASC 740." (Ex. M at 2.) In other words, the DIM wholly failed to address the merits of Copley's arguments and instead merely recited the very requirements of the rules of general application from which Copley now seeks exemptive relief given its unique circumstances.

Having failed to receive a reasoned determination from the DIM, Copley next sought relief directly from the Commissioners in a letter dated April 12, 2013, in which Copley requested a full *de novo* review by the Commissioners of the DIM's April 5, 2013 denial of Copley's request for No-Action relief. (A copy of Blank Rome's April 12, 2013 letter to the Commissioners is attached hereto as Exhibit N.) Copley summarized therein for the Commissioners' benefit its arguments in support of its proposed reserve methodology, specifically, that it is more consistent with the assumptions, constraints and conventions underlying GAAP than the full liquidation value methodology, and that GAAP allows for flexibility where strict adherence to the principles of general application would be unreasonable. (See Ex. N at 2 through 4.)

⁴ The exhibits cited in Blank Rome's March 28, 2012 letter to the DIM are included with this application and are therefore omitted from Exhibit L.

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This letter, however, never reached the Commissioners. The DIM intercepted Copley's letter to the Commissioners and chose to "interpret[] [Copley's] request as being made pursuant to [Rule 202.1(d)], under which the DIM "may present a request for Commission review of a Division no-action response if it concludes that the request involves a matter 'of substantial importance and where the issues are novel or highly complex.'" (See DIM letter to Copley dated June 18, 2013 attached hereto as Exhibit O.) *Even though a Commission representative had previously acknowledged Copley's unique structure and unusual tax issues (see Ex. O), the DIM unilaterally decided to withhold Copley's request from consideration by the full Commission because it deemed Copley's request insufficiently important, novel, or complex. (See id.)*⁵

In a letter dated July 15, 2013, Copley responded to the DIM's foreclosure of the Fund's request for *de novo* review by the Commissioners. (See Exhibit P (attached)). Copley notified the DIM that it objected to its election to "interpret" Copley's letter as being made pursuant to Rule 202.1(d) and renewed its request for full *de novo* review of its No-Action application by the Commissioners.

Finally, the DIM informed Copley, in a letter dated August 2, 2013, that, based on its interpretation of the applicable rules, Copley's pursuit of No-Action relief was at an end and that Copley had no recourse to a full review by the Commissioners of the denial of No-Action relief. (See Ex. A.) The DIM volunteered, however, that, "[t]o the extent [Copley] seek[s] Commission consideration of [its] request," Copley could submit a request for exemptive relief pursuant to Section 36 of the Exchange Act. (See *id.*)

Based on the DIM's positions to date and suggestion, Copley now seeks review by the Commissioners of this application under Section 36 of the Exchange Act for exemptive relief from Rule 22c-1 promulgated under the ICA and Rule 4-01(a)(1) of Regulation S-X that would permit Copley to alter the manner in which it currently accounts for deferred tax liability.

C. Summary of Copley's Arguments

Below is a summary of the arguments Copley has previously presented to the DIM concerning its proposed method for accounting for deferred tax liability. Copley has yet to receive from the DIM or the Commissioners a substantive, reasoned response to its arguments in favor of altering its method of accounting for deferred tax liability in order to provide its current and future investors with a more fair and accurate presentation of its NAV.

⁵ Section C.1., *infra*, describes in detail Copley's uniqueness as compared to other U.S. open-end mutual funds.

1. The Fund is unique.

Copley is a C Corporation, and not a RIC. Although the Fund has some of the characteristics of a RIC, unlike one, up to 70% of the dividend income received, or 70% of the taxable income of the Fund, whichever is less, is exempt from federal taxation under the Internal Revenue Code. The remaining 30% of the Fund's income is taxable. Unlike most funds, the taxable income generated by the Fund is not passed on to the shareholders. Furthermore, contrary to most other funds, Copley has maintained a strategy of not distributing dividends and capital gains to shareholders, but rather, accumulating them within the Fund and then adding them to the value of each share on a daily basis. Shareholders, therefore, are able to defer dividend and capital gains taxes until redemption.

To the knowledge of Copley's management, it is the only U.S. open-end mutual fund that operates in this manner. As noted above, the DIM has, in fact, acknowledged the unique tax structure of the Fund. (*See supra* at 7 and Ex. I.)⁶ As a result of this method of operation, the risk of Copley incurring a tax liability in excess of the reserve established by the Board is exceedingly remote. Concomitantly, a strict application of FAS 109 to require a full liquidation value deferred tax liability affects the Fund disproportionately because, unlike a typical C Corporation whose shares are valued by the market, Copley is required to calculate its price daily with respect to its redeemable shares.

Thus, the full liquidation value methodology demanded by the DIM under the rules of general application puts Copley at a decisive disadvantage relative to its peer funds because it artificially deflates the Fund's NAV and thereby unfairly makes it appear to the investing public to be a less attractive investment opportunity compared to its competitor funds.

2. The full liquidation value methodology leads to misleading financial accounting.

Beginning in 1992, Copley implemented a policy of regularly monitoring the Fund's potential income tax liability on unrealized gains and accruing a reserve that corresponded with the anticipated actual liability. The estimate of the Fund's future liability was based on factors that included anticipated redemptions beyond the ability of the Fund to cover, the Fund's

⁶ Although in its 2007 Comment Letter (*see* Ex. B), the DIM referred to two other investment companies that have not elected RIC status but record a deferred tax liability, Tortoise Energy Capital Corp. and Kayne Anderson MLP Investment Company, as Copley explained in the November 2008 Memo, both are easily distinguishable from Copley because, among other things, they are closed-end funds. (*See* November 2008 Memo at Ex. E, p. 11, n. 4.)

investment strategy and track record of holding dividend paying stocks for the long term, and the fact that the entire deferred liability would be due only in the unlikely event the entire portfolio were liquidated. (See November 2008 Memo, at Ex. E, for a more detailed explanation of the reserve methodology.) *During the entire period in which the Board employed this methodology, the reserve was never used.* (See November 2008 Memo at 5.)

The Fund's use of the mandated full liquidation value methodology, under which it records the entire deferred tax liability, has led to a materially misleading reported NAV since 2007. This result derives from the facts that it (i) does not accurately reflect Copley's investment policy and practice of long-term holdings of its positions; (ii) understates the amount of invested assets actually under management on which gains or losses are actually realized; and (iii) overstates the Fund's operating expense ratio (by including as expenses deferred taxes, which are not actual or realized operating expenses). (See Ex. J at 2-4.)

Copley submits that it is in the best interests of the Fund's shareholders to reserve for deferred tax liability in a manner that allows the per share NAV to reflect better the true value of the Fund's shares. As Copley has always assured the DIM, if permitted to do so, it will provide full transparency to investors by, for example, including in its prospectus a clear explanation of the differing effects in pricing, as calculated using the reserve method and the full liquidation value methods. (See, e.g., Ex. E; Ex. F.)

Copley recognizes that the Commission may be reluctant to permit its management unfettered discretion to calculate the appropriate reserve and that it may have concerns that Copley, through its prior methodology, may have overstated the value of its shares. Without conceding the validity of those concerns, the Fund is prepared to address this issue and to propose an acceptable resolution. Accordingly, in Section D, below, Copley sets forth a new methodology, whereby the Fund will calculate the reserve using a pre-set formula that it believes will be acceptable to the Commission and should allay any of its concerns.

3. Copley is willing to convert to a RIC.

As explained in more detail in the memorandum initially provided to the DIM in November of 2008, Copley has informed the DIM of its willingness to convert to RIC status in the event unforeseen circumstances caused gains to be realized that consumed the entire amount of accumulated deferred income taxes it has recognized. (See Ex. B at 5-6; November 2008 Memo at Ex. E, pp. 6-8.) As discussed more fully, *infra*, at 18-19, conversion to a RIC would be

analogous to the restructure and tax treatment sanctioned by the Commission with respect to other entities.

4. Copley's "reserve" methodology is consistent with the ICA Rules.

Rule 22c-1 requires open-end funds to issue and redeem shares "at a price based on the current net asset value of such security...." In turn, the rules define "current net asset value" as the "amount which reflects calculations, whether or not recorded in the books of account, made substantially in accordance with the following, *with estimates used where necessary or appropriate.*" ICA Rule 2a-4 (emphasis added). As set forth in more detail in the September 28 Letter, these rules, when read together, do not require the price of the Fund's shares to be exactly the same as its NAV. (Ex. J at 2.) Copley's issuance and redemption of shares based on a NAV that reflects a management determined tax reserve, therefore, does not violate the ICA Rules.

5. Copley's "reserve" methodology is permissible under GAAP.

The reserve methodology Copley proposes is more consistent with the assumptions, constraints and conventions underlying GAAP than the currently mandated full liquidation value methodology. For example, under GAAP, there is an assumption that a business will continue to operate as a going concern. (*See, e.g., Accounting Research Bulletin 43, Chapter 3: Working Capital, Section A, stating "It should be emphasized that financial statements of a going concern are prepared on the assumption that the company will continue in business."*). The liquidation value method, by contrast, assumes the Fund will close, be sold or entirely liquidated *en masse*. The use of the liquidation value method also contradicts the principles of realization/revenue recognition and matching by effectively transforming a contingent liability into a full, current, realized liability and failing to match current revenue and assets with correct, actual liabilities. Lastly, the use of the liquidation value method is contrary to the principle of adequate disclosure underlying GAAP, in that it presents financial statements that are effectively misleading because they do not accurately convey the true value of Copley's shares. (*See November 2008 Memo, at Ex. E, p. 10.*)

Even assuming, *arguendo*, that the Fund's proposed reserve methodology would depart from ASC 740, GAAP does allow for certain flexibility where, for instance, the strict adherence to GAAP appears unreasonable under the circumstances and/or would produce unjustifiable results. The Commission has appropriately recognized this concept. (*See November 2008 Memo at Ex. E, p. 11, n.5, citing the Commission's issuance of rules even for the use of non-GAAP financials, Release No. 33-8176, 34-17226 (January 22, 2003).*) Further, as discussed in

Copley's October 5, 2009 letter to Mr. Pisto (Ex. F), the Commission submitted to Congress in 2008 a report on mark to market accounting in which it presented recommendations that suggested the appropriateness of discretion and flexibility, including the application of "judgment" in making market price decisions. Here, the use of the full liquidation value method has produced a skewed and unreasonable result – Copley's per share NAV does not reflect the realistic value of the Fund – and, therefore, such flexibility is warranted.

6. The Commission has permitted management discretion with respect to GAAP and tax accounting provisions.

We understand from prior correspondence that the DIM apparently has adopted the position that ASC 740 does not allow for *any* discretion or flexibility with respect to accounting for deferred tax liability. There is, however, evidence to the contrary, as the SEC has permitted certain flexibility to depart from a strict interpretation of GAAP or other tax accounting provisions where doing so would lead to more accurate reporting.

First, we are aware of at least two entities – Weyerhaeuser and American Tower Corp. – that converted from C Corporations into real estate investment trusts ("REITs") and, in doing so, have exercised discretion with respect to accounting for deferred tax liabilities.⁷ Upon conversion to REIT status, those entities would be subject to a tax on any "built-in gains" that had accrued as of the conversion date if they recognized gains on the disposition of any assets owned at the time of the conversion during the 10-year period following the conversion. Nonetheless, both Weyerhaeuser and American Tower have not accounted for deferred tax liabilities associated with such "built-in gains" – presumably concluding that their likelihood of disposing of such assets within the 10-year recognition period is exceedingly remote. (*See also* discussion of Weyerhaeuser in the September 28 Letter at Ex. J, pp. 7-8.)

To our knowledge, the Commission has not challenged the approaches of either Weyerhaeuser or American Tower. Notably, the conversions to REITs by Weyerhaeuser and American Tower took place in 2010 and 2012, respectively – years *after* the Commission mandated that Copley *not* exercise any management discretion with respect to its deferred tax liability accounting. Although the Fund's situation is not entirely equivalent to that of Weyerhaeuser and American Tower, it is sufficiently analogous because like those entities, Copley is seeking to exercise discretion not to account for the full amount of liabilities that are contingent and exceedingly remote. Copley does not understand the Commission's justification

⁷ Additional examples, based on reviews of publicly filed 10-K's, include Cyrus One, Penn National Gaming, Empire State Realty, CoreSight, and Ryman Hospitality.

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for prohibiting it from exercising similar management discretion, but later permitting Weyerhaeuser and American Tower to do so. Put differently, Copley submits that the Commission's interpretation of ASC 740 as applied to the Fund is fundamentally inconsistent with the deferred tax liability accounting of these two REITs.

Second, in at least one instance, the Commission has granted no-action relief permitting an investment company to present its financial statements in a manner that would have been prohibited under a strict interpretation of GAAP. In April of 2008, the Division assured Fidelity Investments that it would not recommend enforcement action against a Fidelity registered investment company called the Gold Portfolio if it consolidated its financial statements with those of its subsidiary, Fidelity Select Gold Cayman Ltd. *See* Response of the Office of Chief Accountant of the Division of Investment Management to Fidelity Investments, 2008 SEC No-Act. LEXIS 459 (Apr. 29, 2008).

Under a technical reading of the ICA, the subsidiary might not have been considered an investment company because it was only invested in commodities, which are not considered "securities." *Id.* at *10. Therefore, the Gold Portfolio technically was not permitted to consolidate its financial statements with the subsidiary, pursuant to GAAP and Rule 6-03(c)(1) of Regulation S-X, which preclude consolidation by a registered investment company with an entity that is not an investment company. *Id.* at *4-*5. The DIM, however, accepted Fidelity's argument that notwithstanding those regulations, it would be appropriate to consolidate the financial statements of the subsidiary into the Gold Portfolio because it would give shareholders a "more accurate picture" of the portfolio and its structure. Specifically, the subsidiary was authorized to invest in securities, would operate as an investment company for all relevant purposes, and was established to act as an investment vehicle for the Gold Portfolio. *Id.* at *5, *15. Copley, likewise, should be permitted flexibility to depart from a strict interpretation of GAAP by formulating a reserve for deferred tax liability that leads to a per share NAV that better, and more accurately, reflects the true value of the Fund's shares to the investing public.

For all of the reasons summarized here (and others more fully articulated in the attached Exhibits) Copley requests that the Commission issue a final Order granting Copley a limited exemption from Rule 22c-1 promulgated under the ICA and Rule 4-01(a)(1) of Regulation S-X that would permit Copley to account for its deferred tax liability for unrealized gains in the manner set forth in the section below.

D. Copley's Proposal for Accounting for Deferred Tax Liability on Unrealized Gains

As a limited and structured exemption to the foregoing rules, Copley submits the following proposals relating to its accounting for deferred tax liability on unrealized gains, which would result in a fairer and more accurate disclosure to the investing public, together with a more equitable outcome.

1. Reserve Formula

The Fund proposes to accrue a deferred tax liability that fairly and accurately reflects a realistic tax liability, and which addresses the issues regarding the ability to meet redemptions at a NAV that does not include a tax reserve that assumes full liquidation. Accordingly, the Fund proposes to accrue a defined tax liability using one of the following two formulas, each of which is fully transparent.

(a) Alternative 1

- At the end of each calendar quarter, the Fund will calculate its average historical turnover rate over the previous five, or even ten, years. In calculating its NAV on a daily basis, Copley will use a tax reserve calculated at a tax rate equal to a percentage of the statutory corporate tax rate determined at four times the average historical turnover rate. The historic, average five-year turnover rate of the Fund for the period from February 29, 2008 through February 29, 2012 was 2.31%; the average ten-year turnover rate is 2.28%. (See Portfolio Turnover Rate chart annexed hereto as Exhibit Q.) Thus, for example, if the unrealized gain at the close of business is \$50,000,000, the deferred tax liability under the full liquidation value approach would be \$17,500,000. Under either the historical, five-year rate of 2.31% or the historical ten-year rate of 2.28% (both rounded to 2.5%), Copley would set a reserve at four times that 2.5%, or 10%, of the \$17,500,000, *i.e.*, \$1,750,000. Based on these actual average historical rates, Copley respectfully submits that any multiple of four times allows for a reasonable and adequate tax reserve.
- This formula obviously would be independent of any unfettered discretion of the Fund's management. Rather, it would reflect, in a most conservative manner, the average historical turnover rate of the Fund and, therefore, the lack of need for – or propriety of – a “full” or “liquidation based” tax reserve.

- Under this scenario, the Fund would ensure that even if it receives requests on any given day which would require sales of investment assets at a rate *four times* in excess of its historical rates – a high number based on a 20-year historical track record – it will be able to accommodate such requests.

(b) Alternative 2

- At the end of each trading day, the Fund will determine the highest daily redemption of its shares (as a percentage of shares outstanding) during the previous five years. In calculating its NAV on a daily basis, Copley will use a tax reserve calculated at a tax rate equal to a percentage of the statutory corporate tax rate determined at four times the highest daily redemptive rate. For example, if the unrealized gain at the close of business is \$50,000,000, the deferred tax liability under the full liquidation value approach would be \$17,500,000. If the historically highest daily redemptive rate of the Fund were 2%, Copley would set a reserve at four times that 2%, or 8%, of the \$17,500,000, *i.e.*, \$1,400,000. This formula, likewise, would be totally independent of the unfettered discretion of the Fund's management. It would reflect, in a most conservative manner, the historically low redemptive rate of the Fund and, therefore, the lack of need for – or propriety of – a “full” or “liquidation based” tax reserve.
- To put this alternative into perspective, the highest daily redemption in the history of the Fund since inception was \$1,000,000, which represented approximately 23,260 shares or approximately 1.6% of the total outstanding shares on the date of redemption. The redemptions were effected with no problem.
- Under this scenario as well, the Fund would insure that even if it receives redemption requests on any given day that are *four times* greater than its historically highest redemption – an inconceivably high number based on a 20-year historical track record – it will be able to accommodate such redemptions.

Either alternative will assure investors in the Fund the ability to redeem their shares at the stated, accurate NAV, thus addressing any concerns that the Commission may have previously harbored.

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(c) Further Conditions to Protect Investors

As a condition to the requested exemption and to provide full disclosure and protection to investors, the Fund is prepared to present in its public disclosures appropriate charts that compare the Fund's NAV under the proposed reserve methodology to the full liquidation value method under the GAAP rules of general application. Such disclosures should appropriately alleviate the SEC's concerns respecting any misleading statements and compliance with GAAP.

In any event, under Section 22(e) of the ICA, the Fund need not redeem all such shares on the day such requests are received, but instead has seven days to redeem them. The Fund has never failed to redeem on the day requests are made. Although the Fund expects to continue to honor all redemption requests on the day requested, it notes that Section 22(e) provides an additional safety valve.

Copley does not believe it is a cogent objection to its proposal to say that if more than 8% of the shares are redeemed on one day, then the NAV will somehow be overstated due to an insufficient deferred tax liability. In such case, the Fund would seek relief from the DIM and/or could postpone some redemptions to the next day, or for several more days, or for an appropriately longer period, in which case the NAV on those later days would be adjusted to reflect any updated deferred tax liability. Again, the Fund would be following traditional and accepted industry practice, since hundreds or thousands of funds would in fact defer some redemptions if these requests reached 8%. If they did not, they would have to dispose of assets at a material discount, resulting in an apparently overstated NAV. As discussed above, a fund is presumed under GAAP to be a going concern that will continue in business. (*See* ARB 43.) In other words, the regulatory framework of the fund industry, which promises investors liquidity at a stated NAV, is founded on the premise that there will be an orderly process for large redemptions all at once.

For example, if all the investors in Vanguard's S&P 500 Index requested redemptions at the same time, they would, even with a wait of seven days, receive a fraction of their expected NAV, if a distressed liquidation were mandated. Of course, either Vanguard would implement gating procedures or the Commission would be expected to provide relief by allowing for a more orderly liquidation in such instance; the core point regarding the assumptions of the regulatory scheme still holds.

Copley believes that such a sophisticated approach is appropriate given the unique status and history of the Fund and, in particular, given the treatment apparently afforded to Weyerhaeuser, American Tower, and others, all of which have excluded deferred tax liabilities

relating to assets whose sale is considered remote. Copley's alternative rational formulas similarly take into account the fact that the accrual of the full deferred tax liability under the liquidation value methodology would be exceedingly remote. The Fund believes that the Commission has a regulatory obligation to provide Copley with equal treatment.

To date, neither the Commission nor the DIM has addressed the issue of this disparate treatment. If the DIM's response to the Fund in its September 26, 2007 letter were applied to Weyerhaeuser and American Tower, those companies would have to accrue a deferred tax liability calculated by assuming a liquidation of all their assets. These companies are not special purpose vehicles restricted by covenants designed to limit borrowings ("bankruptcy remote vehicles"). Thus, for example, they may borrow, become overleveraged and have to sell assets. Additionally, they may encounter environmental or other operating liabilities, be subject to large legal claims and be forced to sell assets. Nonetheless, the Commission apparently has taken the position that the prospect of such a disposition of assets is sufficiently remote to warrant a deferred tax liability that assumes there will be no such sale. The Fund respectfully submits that it is likewise entitled to such treatment.

2. Board Resolution to Convert to RIC Status

As discussed above, the Fund has long contemplated conversion to a RIC in the event unforeseen circumstances caused gains to be realized that consumed the entire amount of accumulated deferred incomes taxes it has recognized. To ensure that this occurs as first contemplated by the Board years ago, the Fund enacted Board resolutions confirming its intent and detailing how and when this RIC conversion shall occur. A redacted copy of the Board minutes adopting the Resolutions, on March 23, 2012, is annexed hereto as Exhibit L.

The resolutions (Ex. L) provide that if the deferred tax liability, as computed under the proposal described above, reaches an amount equal to 10% of Pre-Tax NAV, defined as the NAV of the Fund plus an amount equal to Copley's deferred tax liability as of the end of such trading day, the Fund will convert to a RIC for tax purposes. Upon such conversion, there would be a further parallel with Weyerhaeuser and American Tower, since those companies have converted from C Corporation to REIT status and have assumed they will not sell assets so as to recognize built-in gain for 10 years, and the Fund will be making the same (or a parallel) conversion and assumption. The Fund, however, will continue to accrue a deferred tax liability in excess of the assumptions employed by Weyerhaeuser and American Tower, as certain asset sales sufficient to support redemptions of the Fund's shares will be assumed. The Fund, unlike Weyerhaeuser and American Tower, does have explicit restrictions on its permitted leverage under the ICA, and is, for all practical purposes, a bankruptcy remote vehicle. Thus, if anything,

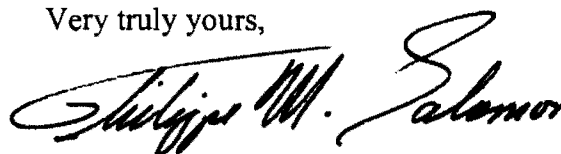
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the Fund's tax accrual proposal is far more conservative than the practices of Weyerhaeuser and American Tower that are currently sanctioned by the Commission.

* * * * *

We look forward to your final written Order in response to Copley's request for exemptive relief. If you have any questions, or if we can be of further assistance, we would welcome the opportunity to discuss these issues further with you.

Very truly yours,



PHILIPPE M. SALOMON

Enclosures

cc: David I. Faust, Esquire (w/attachments)