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IN WASHINGTON  
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WASHINGTON, D.C. 20037  
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September 7, 1984

Investment Company Act  
Section 17(f)  
Section 18(f)

Act	I CA-40
Section	18(f)
Rule	
Responsibility	12/31/84

Stanley B. Judd, Deputy Chief Counsel  
Division of Investment Management  
Securities and Exchange Commission  
Judiciary Plaza  
450 Fifth Street, N.W.  
Washington, D.C. 20549

Re: Colonial Tax-Managed Trust File No. 2-62492  
Tax-Exempt Bond Index and Interest Rate Futures  
Contracts and Options on Such Futures Contracts

Dear Mr. Judd:

Colonial Tax-Managed Trust is a diversified open-end investment company which was established as a Massachusetts business trust under the laws of Massachusetts by an Agreement and Declaration of Trust dated August 19, 1978. A meeting of shareholders of Colonial Tax-Managed Trust will be held on September 18, 1984 for the purpose of, among other things, approving a change in its objective, policies and restrictions to convert Colonial Tax-Managed Trust into a mutual fund investing in tax-exempt high-yield securities. Upon shareholder approval of such change, Colonial Tax-Managed Trust's name will be changed to Colonial Tax-Exempt High Yield Trust (the "Trust"). Colonial Tax-Managed Trust has filed post-effective Amendment No. 11 to its 1933 Act Registration Statement and Amendment No. 9 to its 1940 Act Registration Statement, including a draft Prospectus and Statement of Additional Information, reflecting the anticipated conversion of Colonial Tax-Managed Trust into the Trust. Three copies of such Prospectus and Statement of Additional Information are enclosed. The Registration Statement provides that the

Stanley B. Judd,  
Deputy Chief Counsel

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Trust may not engage in tax-exempt bond index and interest rate futures contracts and related options transactions until it obtains a no-action letter under the Investment Company Act of 1940 (the "Act") (page 5 of the Prospectus). Similar no-action letters have been issued to Colonial Government Securities Plus Trust and Colonial Option Growth Trust (p.a.d. 6/15/84) and Colonial Option Income Trust--Portfolio II (not yet publicly available).

The Trust is seeking a no-action letter from the Commodity Futures Trading Commission ("CFTC") that it will not be a "pool" under Section 4.10(d) of the CFTC's Regulations and that the Trust will not be a "commodity pool operator" as defined in Section 2(a)(1)(A) of the Commodities Exchange Act ("CEA").

As stated in the enclosed draft Prospectus, the Trust's investment objective will be to provide a high yield, generally exempt from federal income taxes, by investing primarily in medium and lower quality bonds and notes issued by or on behalf of state and local governmental units whose interest is exempt from federal income tax. The Trust's secondary objective will be to preserve its capital. The Trust will be permitted to hedge its portfolio against interest rate changes through the use of tax-exempt bond index futures ("index futures") (when an active trading market in index futures develops) and financial futures contracts and related options. The Trust will be advised by Colonial Management Associates, Inc. (the "Adviser"). Colonial Investment Services, Inc. will be the Trust's Distributor of shares. Index and financial futures contracts and related options, and the commodities exchanges on which they are traded, are subject to regulation by the CFTC under the CEA. As stated in the Prospectus, the Trust may purchase and sell index and financial futures contracts; it may also purchase and write put options on index futures and on financial futures.

In connection with this "no-action" letter request the Trust represents as follows:

No consideration will be paid or received by the Trust upon the purchase or sale of a futures contract or upon the sale of a related option. Initially, the Trust will be required to deposit, for the account and in the name of the broker, in a segregated account with The First National Bank of Boston, its Custodian, an amount of cash or United States Treasury bills, which amount has not yet been determined in

Stanley B. Judd,  
Deputy Chief Counsel

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September 7, 1984

the case of an index futures contract and which amount is equal to approximately 1 1/2% of the contract amount in the case of a futures contract, or upon the sale of a put option on a financial futures contract, the amount of the option premium plus a specific dollar amount for each written put option. This amount is known as initial margin. The nature of initial margin in futures transactions and in written options on futures is different from that of margin in security transactions in that futures contract and written options margin does not involve the borrowing of funds by the customer to finance the transactions. The initial margin is in the nature of a performance bond or good faith deposit on the contract which is returned to the Trust upon termination of the futures contract, assuming all contractual obligations have been satisfied; or upon the closing of written options. Subsequent payments, called variation margin, to and from the broker, a process known as "marking to market," will be made on a daily basis as the price of the futures contract fluctuates, thereby making the long and short positions in the futures contract more or less valuable, or as the price of the written option fluctuates. Variation margin does not represent a borrowing of or loan by the Trust but is instead the daily settlement between the Trust and the broker of the amount one would owe the other if on such day the contract expired or if the written option were exercised. The broker has access to the amount of initial margin on deposit only if the Trust defaults in making payments of variation margin, and only after notice given by the broker to the Trust accompanied by the broker's statement to the Custodian that all conditions precedent to its rights to reach the initial margin have been satisfied.

The Trust undertakes that, on the occasions that it has the right to receive variation margin payments from the broker, it will promptly demand payment by the broker of such amounts upon notification by the broker that such amounts are payable. Any such funds received by the Trust will be held by the Trust's Custodian. At any time prior to expiration of the futures contract or the written option, the Trust may elect to close the position by taking an opposite position, which will operate to terminate the Trust's position in the futures contract or the written option. A final determination of variation margin will then be made, and if additional cash is required to be paid by or released to the Trust, the Trust will realize a loss or a gain.

Stanley B. Judd,  
Deputy Chief Counsel

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September 7, 1984

The Trust's futures contracts and related options contracts are governed by the terms and conditions of such contracts determined by the exchanges on which such contracts are traded, and its futures and related option positions are evidenced by confirmations of transactions received from the executing broker. The Trust undertakes that its Custodian will have copies of such exchange terms and conditions and that its Custodian will have possession of such confirmations.

The Trust represents that, in connection with its request to the CFTC that such agency take a no-action position that the Trust will not be within the definition of "commodity pool operator" and that the Trust will not be treated as a "pool" under the CEA, it has undertaken that its sales of futures contracts and its purchase of put options on futures contracts will be solely for purposes of protecting its portfolio against declines in value. The Trust will not engage in transactions in futures contracts or related options for speculation but only as a hedge against changes resulting from market conditions in the values of securities held by the Trust. Furthermore, the Trust would write put options on financial and index futures only to offset financial or index futures which it has sold. The Trust may not enter into any index or financial futures contract or related option if immediately thereafter, more than one-third of The Trust's net assets would be represented by futures contracts or related options. In addition, the Trust may not purchase or sell futures contracts or purchase related options if, immediately thereafter, the sum of the amount of margin deposits on the Trust's existing futures and related options positions and premiums paid for related options would exceed 5% of the market value of the Trust's total assets. In instances involving the purchase of futures contracts by the Trust, money market instruments equal to the market value of the futures contract (less any margin deposits thereon) will be earmarked in a segregated account with the Trust's Custodian to collateralize such long positions and thereby ensure that the use of such futures contracts is unleveraged. Such earmarked assets will not be used to support any other transactions which the Trust may engage in. The collateralization of futures contracts makes the use of such futures consistent with reverse repurchase agreements, standby commitments and other similar arrangements discussed in Investment Company Act Release No. 10666 (April 18, 1979) ("Release 10666").

Stanley B. Judd,  
Deputy Chief Counsel

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September 7, 1984

If, as assumed in previous interpretive releases, the Commission has jurisdiction over leveraged investments of registered investment companies generally pursuant to Section 18 of the Act, an index or financial futures contract or the sale of a related option may, because of the Trust's contingent obligation to pay variation margin during the life of the contract, constitute a "senior security" (as that term is defined in Section 18(g) of the Act), for the purpose of Section 18(f). Since such an obligation would not run to a bank, the purchase or sale of a futures contract or the sale of a related option thereon by the Trust may constitute the issuance of a senior security by the Trust in violation of Section 18(f)(1) of the Act. In addition, to the extent that variation margin payments to the Trust in connection with a futures contract or the sale of a related option are held overnight by a broker, the Trust may be unable to comply with the provisions of Section 17(f) of the Act.

The Trust requests your advice to the effect that the Division of Investment Management would not recommend enforcement action to the Securities and Exchange Commission under the provisions of Section 18(f)(1) and 17(f) of the Act with respect to the Trust's proposed transactions in index and financial futures contracts and related options.

In support of this requested "no-action" letter, the Trust believes that financial futures contracts and related options, are not "securities" for the purpose of the Act, and, thus, such contracts and options cannot constitute "senior securities" under Section 18(g) or be subject to regulation under Section 18(f)(1). Furthermore, even if such contracts and options are considered to be senior securities under the Act, the proposed use by and limitations on the Trust with respect to such contracts and options do not give rise to the speculative abuses which Section 18(f)(1) was designed to prevent. The limitations on the Trust's use of such contracts and options and the requirement, in connection with the purchase of a futures contract, that the Trust deposit in a segregated account cash or cash equivalents equal to the market value of such futures contract are, in fact, consistent with the procedures set forth in Release 10666 to minimize the speculative aspects of the leveraged investments which were the subject of Release 10666.

The Trust does not believe that index and financial futures contracts and related options are "securities" or

Stanley B. Judd,  
Deputy Chief Counsel

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September 7, 1984

that the legislative intent of the term "similar investments" reaches such contracts and options. In addition, the Trust believes separate custodian, safekeeping and procedural agreements among the Trust, its Custodian and the futures commission merchant, pursuant to which the Trust's margin deposits are held by the Custodian subject to disposition by the futures commission merchant in accordance with the CFTC Rules and the rules of the applicable commodities exchange, will be consistent with the provisions of Section 17(f).

Your advice is requested to the effect that the Division of Investment Management would not recommend enforcement action to the Securities and Exchange Commission under the provisions of Section 18(f)(1) and 17(f) of the Act with respect to the Trust's proposed transactions in index and financial futures contracts and related options.

If further information is required with respect to this request, would you kindly telephone the undersigned.

Very truly yours,

  
Peter MacDougall

PM/bmc

Enclosures

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November 6, 1984

Investment Company Act  
Section 17(f)  
Section 18(f)

Stephanie Monaco, Esq.  
Division of Investment Management  
Securities & Exchange Commission  
Judiciary Plaza  
450 Fifth Street, N. W.  
Washington, D. C. 20549

Re: Colonial Tax-Exempt High Yield Trust  
File No. 2-62492; Tax Exempt Bond Index  
and Interest Rate Futures Contracts and  
Options on Such Futures Contracts

Dear Ms. Monaco:

In accordance with our telephone conversation yesterday, I am furnishing this supplemental letter in connection with the no-action request dated September 7, 1984 by Colonial Tax-Exempt High Yield Trust (former name, Colonial Tax-Managed Trust) regarding its use of futures contracts and options thereon.

Enclosed is a copy of the letter from the Commodity Futures Trading Commission ("CFTC") dated November 1, 1984, granting certain no-action positions with regard to the proposed activities of the Trust. As indicated in note 2 on page 2 of that letter, the CFTC is not prepared at the present time to take a no-action position with regard to two proposed strategies. The first strategy is selling tax-exempt bond futures contracts (if and when approved) and buying U. S. Government bond financial futures contracts, or vice versa, to protect against shifts in value due to over-or-undervaluation of the tax-exempt bond market in relation to the taxable bond market-i.e., an intermarket

ROPES & GRAY

Stephanie Monaco, Esq.      -2-

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straddle position. The other strategy excepted by the CFTC's letter is writing put options on futures contracts the Trust has sold to offset the Trust's position in such futures contracts.

In light of the position taken by the CFTC, the Trust does not intend to engage in such strategies at the present time and accordingly hereby withdraws its no-action request to the Securities and Exchange Commission to the extent such no-action request covers the purchase of futures contracts or the writing of put options on futures contracts. We trust that this will answer any open questions regarding the Trust's no-action request and that a no-action letter regarding the Trust's selling of futures contracts and purchasing of put options on futures contracts may be issued in the near future. If you require any further information, please do not hesitate to call the undersigned.

Very truly yours,

  
Peter MacDougall

PM/dw  
Enclosure

FEDERAL EXPRESS





DIVISION OF  
TRADING AND MARKETS

COMMODITY FUTURES TRADING COMMISSION  
2033 K STREET, N.W., WASHINGTON, D.C. 20581

November 1, 1984

Peter MacDougall, Esq.  
Ropes & Gray  
225 Franklin Street  
Boston, Mass. 02110

Re: Colonial Tax-Exempt High Yield Trust --  
Regulation as a commodity pool operator.

Dear Mr. MacDougall:

This is in response to your letter dated September 7, 1984, as supplemented by the draft prospectus of September 1984 (the "Prospectus") enclosed therewith, in which you requested on behalf of your client, Colonial Tax-Exempt High Yield Trust (the "Trust"), our advice that we will not recommend that the Commission take any enforcement action against the Trust for failure to register as a commodity pool operator ("CPO") and to comply with the provisions of Subpart B of Part 4 of the Commission's regulations.

From the representations made in your letter, as supplemented, we understand the facts concerning the Trust's operations in general to be as follows: The Trust is a diversified open-end investment company which is registered under the Investment Company Act of 1940. Its primary investment objective is "to provide a high yield, generally exempt from federal income taxes," by investing primarily in certain debt securities of state and local governments. Its secondary investment objective is "to preserve its capital," by engaging in certain hedging transactions.

Included among the hedging transactions in which the Trust intends to engage are transactions involving commodity interests. Such transactions would, however, be subject to certain limitations. As the Prospectus, at pages 5 through 7, represents:

The Trust may enter into interest rate futures contracts ("financial futures") and tax-exempt bond index futures contracts ("index futures"), and options contracts on financial futures . . . and index futures to hedge against changes in the market value of tax-exempt bonds in the Trust's portfolio caused by

fluctuating interest rates, and to close out or offset its existing positions in futures contracts or options.1/

. . . .

The sale of financial futures is for the purpose of hedging the Trust's holdings of long-term debt securities. In the event of a rise in interest rates, the value of the Trust's financial futures would increase at approximately the same rate as the value of the long-term bonds in its portfolio would decline, thereby keeping the net asset value of the Trust from declining as much as it otherwise would have.

. . . .

The Trust also may purchase put options on financial futures which are traded on a U.S. exchange or board of trade and enter into closing transactions with respect to such options to terminate an existing position. The purchase of put options on financial futures is analogous to the purchase of put options on debt securities so as to hedge the Trust's portfolio of debt securities against the risk of rising interest rates.2/

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1/ We note, and as the Prospectus subsequently indicates, that as of this date the Commission has not approved for trading any such tax-exempt bond index futures contract or option thereon. We further note that in the event any such contract or option thereon is approved for trading, the gains or losses from such trading will not be exempt from Federal income taxation.

2/ The Prospectus further represents that "[t]he Trust's strategies in employing index futures will be similar to the strategies involved in financial futures transactions." Based upon such representation, the position we are taking herein also would be applicable to the Trust's trading in tax-exempt bond index futures contracts and in options thereon — if and when they are approved for trading by the Commission.

The Prospectus also discusses two other strategies, which we do not believe would result in "bona fide hedging transactions and positions" as contemplated by Rule 1.3(z)(1), 17 C.F.R. §1.3(z)(1) (1984). The first strategy is selling tax-exempt bond futures contracts (if and when approved) and buying U.S. Government bond financial futures contracts, "to protect against shifts in value due to over-or-under valuation of the tax-exempt bond market in relation to the taxable bond market" — i.e., an inter-market straddle position. The second strategy is writing put options on futures contracts the Trust has sold, to offset the

(Footnote Continued)

. . . .

The Trust will not engage in transactions in futures contracts or related options for speculative purposes but only as a hedge against changes resulting from market conditions in the values of securities in its portfolio. . . . In addition, the Trust will not purchase or sell futures contracts or purchase related options if immediately thereafter the sum of the amount of its margin deposits on its existing futures and . . . premiums paid for related options would exceed 5% of the Trust's total assets (taken at current value).

As you are aware, on February 2, 1984, the Commission issued proposed Rule 4.5, which would exempt certain otherwise regulated persons from registration as a CPO and from the provisions of Subpart B of Part 4 of the Commission's regulations.<sup>3/</sup> See 49 Fed. Reg. 4778 (February 8, 1984), 49 Fed. Reg. 6910-11 (February 24, 1984). Based upon our review of the representations made in your letter, as supplemented, it appears that the Trust would be eligible for this proposed exemption inasmuch as the Trust: (1) is among the persons and qualifying entities covered by the proposal — i.e., a registered investment company; (2) will engage in commodity interest transactions solely for bona fide hedging purposes; (3) will not deposit as initial margin or premiums for its commodity interest transactions more than 5% of its total assets; (4) will not be, and has not been, marketed as a commodity pool or otherwise as a vehicle for trading in the commodity interest markets; and (5) will disclose in writing to its prospective participants the purpose of and the limitations on the scope of its commodity interest trading.<sup>4/</sup>

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(Footnote Continued)

Trust's positions in such futures contracts. Notwithstanding the fact that this strategy may not increase the Trust's risks as a participant in the commodity interest markets, it would not result in a bona fide hedging position. Moreover, this strategy cannot be considered as merely effecting an offsetting position, because such offset will only occur if and when the holder of the option exercises the option. Accordingly, the position we are taking herein presumes that the Trust will not engage in either of these strategies.

<sup>3/</sup> Section 4m(1) of the Act, 7 U.S.C. §6m(1) (1982), requires each person who comes within the CPO definition to register as a CPO with the Commission. The provisions of Subpart B of Part 4 concern the operational, disclosure, reporting and recordkeeping requirements of registered CPOs. See 17 C.F.R. §§4.20-4.23 (1984).

<sup>4/</sup> In this connection, we believe that prior to trading in any tax-exempt bond index commodity interest, the Trust should disclose that the gains or losses from such trading will not be exempt from Federal income taxation.

Accordingly, this Division will not recommend that the Commission take any enforcement action against Colonial Tax-Exempt High Yield Trust for failure to register as a CPO or to comply with the provisions of Subpart B of Part 4 of the Commission's regulations.<sup>5/</sup> This position is, however, subject to the condition that the Trust will comply with Rule 4.5 as adopted by the Commission or with any other such rule that the Commission may adopt to exempt certain otherwise regulated persons from regulation as a CPO.<sup>6/</sup> Therefore, this position will cease upon the effective date of Rule 4.5 or of such other rule.

In this connection, we note that previously we have issued opinions to certain registered investment companies that they would not be pools within the meaning and intent of Rule 4.10(d) based upon representations similar to those made by the Trust.<sup>7/</sup> However, in light of the Commission's proposal in this area, we believe that such a "no-action" position is the appropriate relief that should be afforded at this time. We further note that with respect to such investment companies and the filing of certain notices proposed in Rule 4.5, the Commission has stated:

[We do] not believe that it should be necessary for the recipients of such interpretative letters to, in effect, "re-submit" an application for exemption -- i.e., to file an initial notice of eligibility -- in the event the proposal is adopted. However, to insure that these persons (and entities) would be in compliance with the requirements of the proposed rule, the Commission intends to take the position that such persons must file supplemental notices in the event that any of the representations they previously had

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- <sup>5/</sup> Inasmuch as proposed Rule 4.5 would provide exemption for a registered investment company and any principal or employee thereof, the position we are taking herein also would apply to any principal or employee of the Trust -- e.g., its officers.
- <sup>6/</sup> For example, the rule as adopted may or may not contain the same standards and indicia of bona fide hedging transactions and positions contained in the rule as proposed. Moreover, to the extent that the rule as adopted is less restrictive than the rule as proposed -- with respect to the standards and indicia of bona fide hedging transactions and positions or to any other aspect of the proposal -- the Trust would be able to trade commodity interests subject to such other restrictions provided, of course, that such trading is conducted in accordance with the rule as adopted.
- <sup>7/</sup> See Pension Hedge Fund Inc., Comm. Fut. L. Rep. (CCH) ¶21,908 (available November 3, 1983); SteinRoe Bond Fund, Inc., Comm. Fut. L. Rep. (CCH) ¶21,906 (available October 21, 1983); Prudential-Bache Option Growth Fund, Inc., Comm. Fut. L. Rep. (CCH) ¶21,905 (available September 13, 1983). See also Piedmont Income Fund, Inc., Comm. Fut. L. Rep. (CCH) ¶21,910 (available November 21, 1983).

made to the Commission changed or that, to the extent that the proposal would require any additional representations, they were not in compliance with them. This position would ensure equal treatment of all persons claiming exemption under the rule. 49 Fed. Reg. 4778 at 4782-83.

We believe, and intend to recommend, that the Commission should take this same position with respect to the Trust.<sup>8/</sup>

You should be aware that the position we have taken in this letter does not excuse the Trust from compliance with any otherwise applicable requirements contained in the Act or in the Commission's regulations thereunder. For example, it remains subject to the anti-fraud provisions of Section 40 of the Act, 7 U.S.C. §60 (1982), and to the reporting requirements for traders set forth in Parts 15, 18 and 19 of the Commission's regulations, 17 C.F.R. Parts 15, 18 and 19 (1984).

The position we have taken herein is based upon the representations that have been made to us. Any different, changed or omitted facts or conditions might require us to reach different conclusions. In this connection, we request that you notify us immediately in the event the Trust's operations and activities change in any way from that as represented to us.

Very truly yours,

  
Andrea M. Corcoran  
Director

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<sup>8/</sup> We historically have treated registered investment companies and their officers and directors as those persons subject to CPO regulation. In the unlikely event that Rule 4.5 or any other such rule as the Commission adopts includes investment advisers to and broker-dealers of registered investment companies among the persons who could be considered to be CPOs but does not also include provision for exemption from regulation as a CPO for such persons, the Division will not recommend that the Commission take any enforcement action against the Trust's adviser, distributor, or any officer, director or employee thereof, pending such persons' compliance with such requirements as the rule may impose. Of course, this position assumes that such persons will endeavor to achieve such compliance as promptly as possible.

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November 27, 1984

Investment Company Act  
Section 17(f)  
Section 18(f)

Stephanie Monaco, Esq.  
Division of Investment Management  
Securities & Exchange Commission  
Judiciary Plaza  
450 Fifth Street, N. W.  
Washington, D. C. 20549

Re: Colonial Tax-Exempt High Yield Trust  
File No. 2-62492; Tax Exempt Bond Index  
and Interest Rate Futures Contracts and  
Options on Such Futures Contracts

Dear Ms. Monaco:

This will confirm our recent discussions in connection with the no-action request dated September 7, 1984 by Colonial Tax-Exempt High Yield Trust (former name, Colonial Tax-Managed Trust) regarding its use of futures contracts and options thereon, as supplemented by my letter of November 6, 1984.

The representation contained in the fourth sentence of the second paragraph on page 4 of the September 7, 1984 letter that the Trust will not enter into any index or financial futures contract or related option if immediately thereafter more than one third of the Trust's assets would be represented by futures contracts or related options is hereby withdrawn. In place thereof the Trust hereby represents as follows:

The Trust will not maintain open short positions in financial or index futures contracts if, in the aggregate, the value of the open positions (marked to market) exceeds

Stephanie Monaco, Esq. -2-

November 27, 1984

the current market value of its securities portfolio plus or minus the unrealized gain or loss on those open positions, adjusted for the historical volatility relationship between the portfolio and the financial and index futures (i.e., the Beta volatility factor). If this limitation should be exceeded at any time, the Trust will take prompt action to close out the appropriate number of open contracts to bring its open financial and index futures position within this limitation.

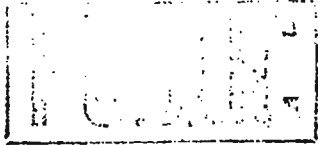
We trust that this will answer any open questions regarding the Trust's no-action request and that a no-action letter regarding the Trust's selling of futures contracts and purchasing of put options on futures contracts may be issued in the near future. If you require any further information, please do not hesitate to call the undersigned.

Very truly yours,

  
Peter MacDougall

PM/dw  
Enclosure

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NOV 29 1984

RESPONSE OF THE OFFICE OF CHIEF COUNSEL  
DIVISION OF INVESTMENT MANAGEMENT

Our Ref. No 84-297-CC  
Colonial Tax-Exempt High  
Yield Trust  
File No. 811-2865

We would not recommend any enforcement action to the Commission against the Colonial Tax-Exempt High Yield Trust ("Trust") for violations of sections 17(f) and 18(f) of the Investment Company Act of 1940 if the Trust proceeds as described in your letter of September 7, 1984, as supplemented by your letters of November 6 and 27, 1984. Our position is based on the facts and representations contained in those letters.

  
Stephanie M. Monaco  
Attorney