BARRETT SMITH SCHAPIRO SIMON & ARMSTRONG

1201 PENNSYLVANIA AVENUE, N. W.

WASHINGTON, D. C. 20004

(202) 393-5024

CABLE: ROOTBAR WASHINGTONDC

WUI TELEX: 66420

26 BROADWAY

NEW YORK, N. Y. 10004

(212) 422-8180

CABLE: ROOTBAR

ROBERT F. AMBROSE
HAEL F. ARMSTRONG
J. BARRETT
D. BROWN III
LIAM C. CLARKE
WARREN H. COLODNER
KEVIN J. CURLEY
MICHAEL O. FINKELSTEIN
MAHLON M. FRANKHAUSER **
MORTON E. GROSZ
RANDALL D. HOLMES
CHARLES E. HORD III
RICHARD M. LEDER
LAWRENCE NIRENSTEIN
GERALD A. NOVACK
ALFRED T. OGDEN II
WILLIAM O. PURCELL
DONALD S. RICE
MARTIN F. RICHMAN *
CARL F. ROGGE, JR.
JACK B. SALWEN
DONALD SCHAPIRO
EDMUND R. SCHROEDER *
DAVID SIMON
W. MASON SMITH
ARTHUR D. SPORN
JOANNE W. YOUNG *

MEMBERS OF THE N. Y. BAR
*ALSO MEMBER OF THE D. C. BAR
**MEMBER OF THE D. C. BAR ONLY

OREN ROOT
V. HENRY ROTHSCHILD 2ND
COUNSEL

December 8, 1983

Act I CA-40
Section 17(f)
Rule
Public
Availability 5/21/84

Stanley B. Judd, Esq.
Deputy Chief Counsel
Division of Investment Management
Securities and Exchange Commission
450 5th Street, N.W.
Washington, D. C. 20549

Dear Mr. Judd:

We are requesting on behalf of our client, Z-Seven Fund, Inc. ("the Fund"), the advice of the Division that it would not recommend to the Commission that it take action if the Fund utilizes stock index futures contracts and options on futures contracts as outlined below. The Fund has filed a registration statement with the Commission which we hope will become effective approximately 30 days from filing.

The Nature of the Fund

The Fund will be a nondiversified, closed-end management investment company with a primary objective of long-term capital growth. A secondary objective is the preservation of capital. It's investments will be principally in common stocks and/or securities immediately convertible into common stocks.

A substantial portion of the Fund's portfolio will generally be committed to securities of "growth-type" companies. The portfolio will be determined by the investment advisor utilizing a highly disciplined and fundamental research appproach. It's methodology will eliminate new and unseasoned companies from portfolio consideration; will emphasize those companies which have demonstrated sustained growth over a reasonable period of time (at least six years) and have a solid financial base upon which to build future growth; and will have a current price/earnings multiple which will tend to indicate that the market price of shares will offer value regardless of the general market movement. See the enclosed preliminary prospectus at page 5 for a more detailed statement of the Fund's seven primary investment criteria. It is anticipated that these securities will be listed for trading on NASDAQ while some will be listed for trading on one or more securities exchanges.

The Fund has determined that stock index futures contracts ("index futures") and options on index futures both traded on national commodity exchanges and options on stock indexes traded on national securities exchanges provide a low cost and flexible mechanism for reducing the risks inherent in holding all securities as well as the systematic market risks. The Fund, subject to the limitations noted below, will sell index futures or options on index futures when the advisor anticipates a general market or market sector decline that may adversely affect the market values of the portfolio. It is anticipated that sales of these contracts would substantially reduce the risk to the portfolio of a market decline and, therefore, provide an alternate to rapid liquidation of the securities positions in the portfolio. Such transactions also may provide on some occasions an alternate to the liquidation of the securities resulting in savings in transaction costs. Index futures or related options contracts may be sold under the following circumstances:

1. When the market has risen to a point where the expected market value of the portfolio positions has been reached and/or surpassed, and liquidation of the portfolio has commenced but there is a substantial risk, in the advisor's opinion, of a major adverse price correction before liquidation of the portfolio positions can be completed; or

2. When several of the portfolio positions appear to represent such intrinsic value that the sale of such positions at that time would appear to be disadvantageous for the long

term because liquidation would forego possible price appreciation or make it extremely difficult to repurchase the portfolio positions if the advisor should be wrong on timing or the anticipated decline would be of such a short duration that the market price of these positions would be little affected; or

3. To close out any long contract positions.

In any event, the contract positions will not be maintained any longer than a maximum of three months.

The Fund may also purchase index futures contracts or related options as a temporary substitute for the purchase of individual stocks when the advisor anticipates a significant market or market sector advance. The use of index futures contracts or related options in this situation affords a hedge against temporarily not purchasing securities for the portfolio. As purchases of securities are made, an amount of stock purchased would be liquidated by offsetting sales. When the advisor believes that the general market is about to make a sustained upside move, or is involved in an unusual (typically speculative) upside price move, index futures contracts may be purchased:

1. If the Fund is attempting to purchase equity positions in issues which it had or was having difficulty acquiring at prices considered fair value;

2. To close out any short contract positions.

It is not anticipated that portfolio risks can be fully hedged because of the imperfect correlation between the movements of the price of the index futures and the movements of the price of the securities in the Fund's portfolio. The securities to be hedged will not usually be the securities that make up the stock index which is the subject of the futures contract. To compensate for this imperfect correlation, the Fund may buy or sell index futures contracts or related options in a greater dollar amount than the dollar amount of the securities being hedged, if the historical volatility of the prices of such securities has been greater than the historical volatility of the index. This historical volatility relationship is referred to as the relationship of the portfolio's Beta value to the particular index's Beta value. On the other hand, the Fund may buy or sell fewer contracts if the historical volatility of the price of the securities being hedged is less than the historical volatility of the stock index.

The Fund may also purchase and sell (write) call and put options on stock indexes which are traded on national securities exchanges. These options may correlate more closely with the composition of the Fund's equity portfolio than indexes which are the subject of futures contracts. If the Fund determines that there is a closer correlation between options on a stock index than currently-traded futures contracts on indexes, and there is sufficient liquidity in the markets for those options, the advisor may recommend engaging in hedging transactions through the use of options on stock indexes in situations similar to those where the Fund may utilize index future contracts and options on futures contracts.

Limitations on the Purchase and Sale of Stock Index Futures

The Fund will engage in transactions in index futures solely as a hedge or a cross-hedge against the impact that changes in the general market conditions can have on the values of the securities held in the Fund's portfolio, or which it intends to purchase, and where the transactions are economically appropriate to the reduction of risks inherent in the ongoing management of the Fund. The Fund will not be long and short stock index futures contracts simultaneously. Nor will it maintain simultaneous open long and short options on stock index futures or long and short options on stock indexes.

The Fund will not maintain open short positions in stock index futures contracts, options written on stock index futures, and options written on stock indexes if, in the aggregate, the value of the open positions (marked to market) exceeds 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 index contracts (*i.e.*, the Beta volatility factor). To the extent the Fund has written call options on specific securities in its portfolio, the value of those securities will be deducted from the current market value of the securities portfolio. If this limitation should be exceeded at any time, the Fund will take prompt action to close out the appropriate number of open contracts to bring its open index futures and options position within its limitation.

When the Fund writes a call option on a stock index futures or on a stock index which is in the money at the time the call is written, the Fund will segregate with its custodian and/or in a special custodian account in which broker collateral deposits are maintained cash or U.S. Government securities equal in value to the amount by which the call is in the money times the multiplier times the number of contracts until the option expires or is closed out. In addition, at the time the Fund purchases stock index futures, an amount of cash and U.S. Government securities equal to the market value of the futures contracts, will be deposited in a segregated account with the Fund's custodian and/or in a special custodian account at the custodian in which broker collateral deposits are maintained.

In order to comply with the interpretations of the Commodity Futures Trading Commission that will exclude the Fund from the definition of "commodity pool" under the Commodity Exchange Act, the Fund has undertaken not to purchase or sell index futures contracts or purchase options in index futures contracts, if, immediately thereafter, the sum of the amount of the initial margin deposits on the Fund's open futures contracts and premiums paid for open options thereon would exceed 5 percent of the market value of the Fund's total assets. In addition, as noted above, the Fund's transactions in stock index futures contracts and options thereon will be made for traditional hedging purposes. As evidence of this hedging intent when it purchases such futures or options thereon to protect the Fund against an increase in the price of securities which it intends to purchase, the Fund has undertaken that approximately 75 percent of such securities will be purchased.

Discussion

A "stock index" assigns relative values to the common stocks included in that index (for example, the Standard & Poor's 500 Index of Composite Stocks or the New York Stock Exchange Composite Index), and the index fluctuates with changes in the market values of such stocks. A stock index futures contract is an agreement, depending on whether a contract is purchased or sold, to accept or make payment of an amount of cash equal to a specified dollar amount multiplied by the difference between the stock index value at the close of the last trading day of the contract, and the price at which the futures contract was originally purchased or sold. There is no physical delivery of the underlying stocks that make up the index.

The Fund will not engage in transactions in stock index futures contracts for speculation, but only as a hedge against the effect that changes in general market conditions may have on the values of securities held in the Fund's portfolio, or which it intends to purchase, and where the transactions are economically appropriate to the reduction of risks inherent in the ongoing management of the Fund. The Fund may also from time to time purchase and sell call and put options on stock index futures traded on a national commodity exchange solely as an alternative method of hedging market fluctuations.

Options on stock index futures gives the purchaser the right to assume a position in a stock index futures contract (a long position if the option is a call, a short position if the option is a put), at a specified exercise price at any time during the period of the option. Upon exercise of the option, the delivery of the futures position by the writer of the option will be accompanied by delivery of the accumulated balance in the writer's futures margin account representing the amount by which the market price of the stock index futures contract, at exercise, exceeds (in the case of a call) or is less than (in the case of a put), the exercise price of the option on the stock index futures. If an option is exercised on the last trading day prior to the expiration date of the option, the settlement will be made entirely in cash equal to the difference between the exercise price of the option and the closing level of the index on which the future is based on the expiration date.

An option on a stock index is a contract pursuant to which the purchaser of the option, in return for a premium payment, has the right to exercise the option at a specific exercise price ("strike price") at any time during the duration of the option. Upon such exercise, the purchaser will realize an amount equal to the difference between the strike price and the value of the securities comprising the stock index (in the case of a call option the purchaser receives the amount by which the value of the securities comprising the index exceeds the strike price; in the case of a put option the purchaser receives the amount by which the strike price exceeds the value of such securities). Exercise of options on stock indexes are effected with cash payments, and do not involve any delivery of securities.

Since the Fund will utilize options on a stock index when the index more closely correlates with the Fund's equity portfolio, an increase or decrease in the index on which the Fund has written a call or put option to the strike price level would normally correlate to an increase or decrease (but not necessarily to the same extent) in the value of the Fund's equity portfolio against which the option was written. Thus, any loss in the option transaction may be offset by an increase in the value of the equity portfolio to the extent the index correlates to the composition of that portfolio. The Fund may liquidate the call and put options it has purchased or sold by effecting a "closing sale transaction" (rather than exercise the option). This is accomplished by purchasing or selling an option of the same series as the option previously purchased or sold.

The Fund does not believe holding positions in index futures contracts, options on index futures contracts, or writing options on stock indexes constitute the issuance or sale of a senior security. It believes that such contracts will reduce the risks to the Fund and shareholders when utilized as a "hedge" as described above. However, as noted, the Fund's fundamental investment policies restrict the number of index futures contracts, options on index futures contracts and options on stock index positions under which the Fund may be obligated and require cash or cash equivalents to be segregated while call options written by the Fund and long futures contracts are open. Although the Fund believes the use of these contracts will reduce the Fund's risks, to the extent the staff believes index futures and related options may subject the Fund to additional "leveraged" obligations, restrictions imposed on their use are consistent with the underlying purposes of Section 18(c) of the Investment Company Act to preclude registered investment companies from becoming excessively "leveraged."

The normal operation of the commodities marketplace will require the Fund to deposit with the futures commission merchants ("FCMs") through which the Fund effects index futures or related options transactions, the amount of cash or United States Treasury bills equal to approximately 5 to 7 percent of the contract value. This is known as initial margin, which is quite different from "margin" in securities transactions since it does not involve the borrowing of funds to finance the transactions. Rather, an initial margin is in the nature of a performance bond or good faith deposit on the contract, which is returned upon termination of the futures contract, assuming all contractual obligations have been satisfied. The initial margin may be retained by the FCM, only if the Fund defaults in making payment upon termination of the contract or in making the variation margin deposits. Variation margin deposits may be required to be made with the FCM subsequent to entering into the contracts as a result of marking the contracts to the market on a daily basis as the market in the contracts fluctuates. The variation margin also does not represent the borrowing or loaning of any funds, but instead consists of the daily settlement of the amount the Fund would owe or be owed if on that day the contract expired or was liquidated. The regulations of the Commodity Futures Trading Commission require FCMs to segregate all margin deposits they hold for customers.

The Fund will normally elect to close open index futures positions by taking an opposite position, which will operate to liquidate the Fund's position in the futures contract. A final determination of the variation margin is then made, cash may be required to be paid by or released to the Fund, and the Fund realizes a loss or a gain.

The Fund will enter into a separate special custodian agreement with its custodian bank and the FCMs which it uses, pursuant to which the Fund's margin deposits will be held by the custodian subject to the disposition by FCMs in accordance with the customer agreement with the Fund, CFTC rules and the rules of the applicable commodities exchange. In this connection, the only delivery or disposition of the initial margin for the benefit of the FCM, as opposed to that of the Fund, is in connection with a liquidation by the FCM on default by the Fund. In that case, the FCM will have to certify to the custodian and the Fund that pursuant to its customer's agreement with the Fund all conditions precedent to its right to give the custodian such an instruction have been satisfied. In addition, the Fund, when it has the right to receive variation margin payments from the FCM, will promptly demand such payments upon notification by the FCM that such amounts are payable. Any such funds received will be held by the Fund's custodian.

Despite the fact that the Fund believes index futures and options on index futures are not "securities" or "similar investments", the Fund will enter into this separate custodian agreement among it, its custodian bank, and the FCM through whom it will execute index futures or related options contracts. This will permit the Fund and its custodian to retain control of these funds and securities until liquidation of the contracts to which they apply and is consistent with the requirements of Section 17(f) of the Investment Company Act. Similarly, a separate custodian agreement between the custodian bank, the securities broker and the Fund will cover margin deposits required by the national stock exchanges on which the options on stock indexes written by the Fund are traded. Such deposits will be held by the custodian bank subject to disposition by the broker in accordance with the custodian agreement with the Fund. Delivery or disposition of these margin deposits would occur only upon exercise of the option and default by the Fund in making payment to the broker.

On the basis of the limitations imposed by the Fund's fundamental investment policies on the purchase and sale of index futures contracts and related options and the separate special custodial account agreement that will be utilized, we believe the Division should advise the Fund that it would not recommend to the Commission that it take action if the Fund proceeds with the transactions and procedures described herein.

If you have any questions concerning the Fund's limitations on the use of stock index futures, options on such futures, and options on stock indexes, please let me know immediately, since we are incorporating them into the registration statement which we hope will become effective next week. We, of course, request an early response to this letter so that we will be able to utilize these hedging instruments as soon as possible after the offering is completed.

Sincerely,

Mahlon M. Frankhauser

cc: Stephanie L. Monaco
Sheila Morgan Johnson

BARRETT SMITH SCHAPIRO SIMON & ARMSTRONG

1201 PENNSYLVANIA AVENUE, N. W.

WASHINGTON, D. C. 20004

(202) 393-5024
CABLE: ROOTBAR WASHINGTONDC
WUI TELEX: 66420

26 BROADWAY
NEW YORK, N. Y. 10004
(212) 422-8180
CABLE: ROOTBAR

December 12, 1983

Stanley B. Judd, Esq.
Deputy Chief Counsel
Division of Investment Management
Securities and Exchange Commission
450 5th Street, N.W.
Washington, D. C. 20549

Dear Mr. Judd:

This will confirm that my letter dated December 8, 1983, supercedes my earlier letter dated October 13, 1983 requesting on behalf of Z-Seven Fund, Inc., a no-action position from the Staff with respect to Sections 18(c) and 17(f) of the Investment Company Act of 1940. Accordingly, the October 13, 1983 letter should be deemed to have been withdrawn.

Sincerely,

Mahlon M. Frankhauser

MMF/cla

BARRETT SMITH SCHAPIRO SIMON & ARMSTRONG

1201 PENNSYLVANIA AVENUE, N. W.

WASHINGTON, D. C. 20004

(202) 393-5024

CABLE: ROOTBAR WASHINGTONDC

WUI TELEX: 6971705

26 BROADWAY
NEW YORK, N. Y. 10004
(212) 422-8180
CABLE: ROOTBAR

ROBERT F. AMBROSE
MICHAEL F. ARMSTRONG
N J. BARRETT
D D. BROWN III
IAM C. CLARKE
WARREN H. COLODNER
KEVIN J. CURLEY
MICHAEL O. FINKELSTEIN
MAHLON M. FRANKHAUSER **
MORTON E. GROSZ
RANDALL D. HOLMES
CHARLES E. HORD III
RICHARD M. LEDER
THOMAS C. MERIAM
LAWRENCE NIRENSTEIN
GERALD A. NOVACK
ALFRED T. OGDEN II
WILLIAM O. PURCELL
DONALD S. RICE
MARTIN F. RICHMAN *
CARL F. ROGGE, JR.
JACK B. SALWEN
DONALD SCHAPIRO
EDMUND R. SCHROEDER *
DAVID SIMON
W. MASON SMITH
ARTHUR D. SPORN
JOANNE W. YOUNG *

MEMBERS OF THE N.Y. BAR
*ALSO MEMBER OF THE D.C. BAR
**MEMBER OF THE D.C. BAR ONLY

OREN ROOT
V. HENRY ROTHSCHILD 2ND
COUNSEL

March 30, 1984

Stanley B. Judd, Esq.
Deputy Chief Counsel
Division of Investment Management
Securities and Exchange Commission
450 5th Street, N.W.
Washington, D. C. 20549

Dear Mr. Judd:

This is the second amended letter requesting on behalf of our client, Z-Seven Fund, Inc. ("the Fund"), the advice of the Division that it would not recommend to the Commission that it take action if the Fund utilizes stock index futures contracts and options on futures contracts as outlined below. The original request letter was filed on October 13, 1983 with an amended letter filed December 8, 1983. The Fund's registration statement was declared effective on December 29, 1983 and the offering has been completed.

The Nature of the Fund

The Fund is a nondiversified, closed-end management investment company with a primary objective of long-term capital growth. A secondary objective is the preservation of capital. It's investments will be principally in common stocks and/or securities immediately convertible into common stocks.

A substantial portion of the Fund's portfolio will generally be committed to securities of "growth-type" companies. The portfolio will be determined by the investment advisor utilizing a highly disciplined and fundamental research appproach. It's methodology will eliminate new and unseasoned companies from portfolio consideration; will emphasize those companies which have demonstrated sustained growth over a reasonable period of time (at least six years) and have a solid financial base upon which to build future growth; and will have a current price/earnings multiple which will tend to indicate that the market price of shares will offer value regardless of the general market movement. See page 6 of the final prospectus for a more detailed statement of the Fund's seven primary investment criteria. These securities are listed for trading on NASDAQ and on a securities exchange.

The Fund has determined that stock index futures contracts ("index futures") and options on index futures both traded on national commodity exchanges and options on stock indexes traded on national securities exchanges provide a low cost and flexible mechanism for reducing the risks inherent in holding all securities as well as the systematic market risks. The Fund, subject to the limitations noted below, will sell index futures or options on index futures when the advisor anticipates a general market or market sector decline that may adversely affect the market values of the portfolio. It is anticipated that sales of these contracts would substantially reduce the risk to the portfolio of a market decline and, therefore, provide an alternate to rapid liquidation of the securities positions in the portfolio. Such transactions also may provide on some occasions an alternate to the liquidation of the securities resulting in savings in transaction costs. Index futures or related options contracts may be sold under the following circumstances:

1. When the market has risen to a point where the expected market value of the portfolio positions has been reached and/or surpassed, and liquidation of the portfolio has commenced but there is a substantial risk, in the advisor's opinion, of a major adverse price correction before liquidation of the portfolio positions can be completed; or

2. When several of the portfolio positions appear to represent such intrinsic value that the sale of such positions at that time would

appear to be disadvantageous for the long term because liquidation would forego possible price appreciation or make it extremely difficult to repurchase the portfolio positions if the advisor should be wrong on timing or the anticipated decline would be of such a short duration that the market price of these positions would be little affected; or

3. To close out any long contract positions.

In any event, the contract positions will not be maintained any longer than a maximum of three months.

The Fund may also purchase index futures contracts or related options as a temporary substitute for the purchase of individual stocks when the advisor anticipates a significant market or market sector advance. The use of index futures contracts or related options in this situation affords a hedge against temporarily not purchasing securities for the portfolio. As purchases of securities are made, an amount of stock purchased would be liquidated by offsetting sales. When the advisor believes that the general market is about to make a sustained upside move, or is involved in an unusual (typically speculative) upside price move, index futures contracts may be purchased:

1. If the Fund is attempting to purchase equity positions in issues which it had or was having difficulty acquiring at prices considered fair value;

2. To close out any short contract positions.

It is not anticipated that portfolio risks can be fully hedged because of the imperfect correlation between the movements of the price of the index futures and the movements of the price of the securities in the Fund's portfolio. The securities to be hedged will not usually be the securities that make up the stock index which is the subject of the futures contract. To compensate for this imperfect correlation, the Fund may buy or sell index futures contracts or related options in a greater dollar amount than the dollar amount of the securities being hedged, if the historical volatility of the prices of such securities has been greater than the historical volatility of the index. This historical volatility relationship is referred to as the relationship of the portfolio's Beta value to the particular index's Beta value. On the other hand, the Fund may buy or sell fewer contracts if the historical volatility of the price of the securities being hedged is less than the historical volatility of the stock index.

The Fund may also purchase and sell (write) call and put options on stock indexes which are traded on national securities exchanges. These options may correlate more closely with the composition of the Fund's equity portfolio than indexes which are the subject of futures contracts. If the Fund determines that there is a closer correlation between options on a stock index than currently-traded futures contracts on indexes, and there is sufficient liquidity in the markets for those options, the advisor may recommend engaging in hedging transactions through the use of options on stock indexes in situations similar to those where the Fund may utilize index future contracts and options on futures contracts.

Limitations on the Purchase and Sale of Stock Index Futures

The Fund will engage in transactions in index futures solely as a hedge or a cross-hedge against the impact that changes in the general market conditions can have on the values of the securities held in the Fund's portfolio, or which it intends to purchase, and where the transactions are economically appropriate to the reduction of risks inherent in the ongoing management of the Fund. The Fund will not be long and short stock index futures contracts simultaneously. Nor will it maintain simultaneous open long and short options on stock index futures or long and short options on stock indexes.

The Fund will not maintain open short positions in stock index futures contracts, call options written on stock index futures, and call options written on stock indexes if, in the aggregate, the value of the open positions (marked to market) exceeds 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 index contracts (*i.e.*, the Beta volatility factor). To the extent the Fund has written call options on specific securities in its portfolio, the value of those securities will be deducted from the current market value of the securities portfolio. If this limitation should be exceeded at any time, the Fund will take prompt action to close out the appropriate number of open contracts to bring its open index futures and options position within its limitation.

When the Fund writes a call option on a stock index futures or on a stock index which is in the money at the time the call is written, the Fund will segregate with its custodian and/or in a special custodian account in which broker collateral deposits are maintained cash or U.S. Government securities equal in value to the amount by which the call is in the money times the multiplier times the number of contracts until the option expires or is closed out. In addition, at the time the Fund purchases stock index futures, writes put options on stock index futures and put options on stock indexes, an amount of cash and U.S. Government securities equal to the market value of the futures contracts, will be deposited in a segregated account with the Fund's custodian and/or in a special custodian account at the custodian in which broker collateral deposits are maintained.

In order to comply with the interpretations of the Commodity Futures Trading Commission that will exclude the Fund from the definition of "commodity pool" under the Commodity Exchange Act, the Fund has undertaken not to purchase or sell index futures contracts or purchase options in index futures contracts, if, immediately thereafter, the sum of the amount of the initial margin deposits on the Fund's open futures contracts and premiums paid for open options thereon would exceed 5 percent of the market value of the Fund's total assets. In addition, as noted above, the Fund's transactions in stock index futures contracts and options thereon will be made for traditional hedging purposes. As evidence of this hedging intent when it purchases such futures or options thereon to protect the Fund against an increase in the price of securities which it intends to purchase, the Fund has undertaken that approximately 75 percent of such securities will be purchased.

Discussion

A "stock index" assigns relative values to the common stocks included in that index (for example, the Standard & Poor's 500 Index of Composite Stocks or the New York Stock Exchange Composite Index), and the index fluctuates with changes in the market values of such stocks. A stock index futures contract is an agreement, depending on whether a contract is purchased or sold, to accept or make payment of an amount of cash equal to a specified dollar amount multiplied by the difference between the stock index value at the close of the last trading day of the contract, and the price at which the futures contract was originally purchased or sold. There is no physical delivery of the underlying stocks that make up the index.

The Fund will not engage in transactions in stock index futures contracts for speculation, but only as a hedge against the effect that changes in general market conditions may have on the values of securities held in the Fund's portfolio, or which it intends to purchase, and where the transactions are economically appropriate to the reduction of risks inherent in the ongoing management of the Fund. The Fund may also from time to time purchase and sell call and put options on stock index futures traded on a national commodity exchange solely as an alternative method of hedging market fluctuations.

Options on stock index futures gives the purchaser the right to assume a position in a stock index futures contract (a long position if the option is a call, a short position if the option is a put), at a specified exercise price at any time during the period of the option. Upon exercise of the option, the delivery of the futures position by the writer of the option will be accompanied by delivery of the accumulated balance in the writer's futures margin account representing the amount by which the market price of the stock index futures contract, at exercise, exceeds (in the case of a call) or is less than (in the case of a put), the exercise price of the option on the stock index futures. If an option is exercised on the last trading day prior to the expiration date of the option, the settlement will be made entirely in cash equal to the difference between the exercise price of the option and the closing level of the index on which the future is based on the expiration date.

An option on a stock index is a contract pursuant to which the purchaser of the option, in return for a premium payment, has the right to exercise the option at a specific exercise price ("strike price") at any time during the duration of the option. Upon such exercise, the purchaser will realize an amount equal to the difference between the strike price and the value of the securities comprising the stock index (in the case of a call option the purchaser receives the amount by which the value of the securities comprising the index exceeds the strike price; in the case of a put option the purchaser receives the amount by which the strike price exceeds the value of such securities). Exercise of options on stock indexes are effected with cash payments, and do not involve any delivery of securities.

Since the Fund will utilize options on a stock index when the index more closely correlates with the Fund's equity portfolio, an increase or decrease in the index on which the Fund has written a call or put option to the strike price level would normally correlate to an increase or decrease (but not necessarily to the same extent) in the value of the Fund's equity portfolio against which the option was written. Thus, any loss in the option transaction may be offset by an increase in the value of the equity portfolio to the extent the index correlates to the composition of that portfolio. The Fund may liquidate the call and put options it has purchased or sold by effecting a "closing sale transaction" (rather than exercise the option). This is accomplished by purchasing or selling an option of the same series as the option previously purchased or sold.

The Fund does not believe holding positions in index futures contracts, options on index futures contracts, or writing options on stock indexes constitute the issuance or sale of a senior security. It believes that such contracts will reduce the risks to the Fund and shareholders when utilized as a "hedge" as described above. However, as noted, the Fund's fundamental investment policies restrict the number of index futures contracts, options on index futures contracts and options on stock index positions under which the Fund may be obligated and require cash or cash equivalents to be segregated while put options written by the Fund and long futures contracts are open. Although the Fund believes the use of these contracts will reduce the Fund's risks, to the extent the staff believes index futures and related options may subject the Fund to additional "leveraged" obligations, restrictions imposed on their use are consistent with the underlying purposes of Section 18(c) of the Investment Company Act to preclude registered investment companies from becoming excessively "leveraged."

The normal operation of the commodities marketplace will require the Fund to deposit with the futures commission merchants ("FCMs") through which the Fund effects index futures or related options transactions, the amount of cash or United States Treasury bills equal to approximately 5 to 7 percent of the contract value. This is known as initial margin, which is quite different from "margin" in securities transactions since it does not involve the borrowing of funds to finance the transactions. Rather, an initial margin is in the nature of a performance bond or good faith deposit on the contract, which is returned upon termination of the futures contract, assuming all contractual obligations have been satisfied. The initial margin may be retained by the FCM, only if the Fund defaults in making payment upon termination of the contract or in making the variation margin deposits. Variation margin deposits may be required to be made with the FCM subsequent to entering into the contracts as a result of marking the contracts to the market on a daily basis as the market in the contracts fluctuates. The variation margin also does not represent the borrowing or loaning of any funds, but instead consists of the daily settlement of the amount the Fund would owe or be owed if on that day the contract expired or was liquidated. The regulations of the Commodity Futures Trading Commission require FCMs to segregate all margin deposits they hold for customers.

The Fund will normally elect to close open index futures positions by taking an opposite position, which will operate to liquidate the Fund's position in the futures contract. A final determination of the variation margin is then made, cash may be required to be paid by or released to the Fund, and the Fund realizes a loss or a gain.

The Fund will enter into a separate special custodian agreement with its custodian bank and the FCMs which it uses, pursuant to which the Fund's margin deposits will be held by the custodian subject to the disposition by FCMs in accordance with the customer agreement with the Fund, CFTC rules and the rules of the applicable commodities exchange. In this connection, the only delivery or disposition of the initial margin for the benefit of the FCM, as opposed to that of the Fund, is in connection with a liquidation by the FCM on default by the Fund. In that case, the FCM will have to certify to the custodian and the Fund that pursuant to its customer's agreement with the Fund all conditions precedent to its right to give the custodian such an instruction have been satisfied. In addition, the Fund, when it has the right to receive variation margin payments from the FCM, will promptly demand such payments upon notification by the FCM that such amounts are payable. Any such funds received will be held by the Fund's custodian.

Despite the fact that the Fund believes index futures and options on index futures are not "securities" or "similar investments", the Fund will enter into this separate custodian agreement among it, its custodian bank, and the FCM through whom it will execute index futures or related options contracts. This will permit the Fund and its custodian to retain control of these funds and securities until liquidation of the contracts to which they apply and is consistent with the requirements of Section 17(f) of the Investment Company Act. Similarly, a separate custodian agreement between the custodian bank, the securities broker and the Fund will cover margin deposits required by the national stock exchanges on which the options on stock indexes written by the Fund are traded. Such deposits will be held by the custodian bank subject to disposition by the broker in accordance with the custodian agreement with the Fund. Delivery or disposition of these margin deposits would occur only upon exercise of the option and default by the Fund in making payment to the broker.

On the basis of the limitations imposed by the Fund's fundamental investment policies on the purchase and sale of index futures contracts and related options and the separate special custodial account agreement that will be utilized, we believe the Division should advise the Fund that it would not recommend to the Commission that it take action if the Fund proceeds with the transactions and procedures described herein.

We, of course, in all our earlier letters requested an early response so that we would have been able to utilize these hedging instruments as soon as possible. We review those requests.

Sincerely,

Mahlon M. Frankhauser

cc: Stephanie L. Monaco

PUBLIC

APR 20 1984

RESPONSE OF THE OFFICE OF CHIEF COUNSEL
DIVISION OF INVESTMENT MANAGEMENT

Our Ref No. 83-443
Z-Seven Fund, Inc.
File No. 811-3877

We would not recommend that the Commission take any enforcement action under sections 18(c) and 17(f) of the Investment Company Act of 1940 against Z-Seven Fund, Inc. (Fund), a registered closed-end management investment company, if the Fund proceeds as described in your letters dated December 8, 1983, and March 30, 1984. Our position is based on the facts and representations contained in those letters as well as the oral representation made on April 5, 1984, by Mahlon M. Frankhauser of your office to me that when the Fund writes put options on stock index futures and put options on stock indexes, the Fund will segregate with its custodian cash and cash equivalents equal to the market value of the written put options and will maintain this account while the put options are open.

Stephanie M. Monaco
Attorney/Adviser

SEF