DIVISION OF
INVESTMENT MANAGEMENT

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

July 7, 1995

ACT ICA of 1940
SECTION 17(a)
RULE
PUBLIC AVAILABILITY 7-7-95

Ms. Sarah E. Cogan
Simpson Thacher & Bartlett
425 Lexington Avenue
New York, NY 10017-3954

Re: Lehman Brothers Daily Income Fund

Dear Ms. Cogan:

Your letter of July 7, 1995 requests our assurance that we would not recommend that the Commission take any enforcement action under sections 17(a), 17(d) and 12(d)(3) of the Investment Company Act of 1940 ("1940 Act") and the rules thereunder if Lehman Brothers Daily Income Fund, a portfolio of Lehman Brothers Funds, Inc. ("Fund"), and Lehman Brothers Holdings Inc. ("LBH") effect the transaction summarized below and more fully described in the letter.

The Fund is a money market fund that seeks to maintain a stable net asset value per share of $1.00, and uses the amortized cost method of valuation in valuing its portfolio securities as permitted by rule 2a-7 under the 1940 Act. The Fund holds taxable notes issued by Orange County, California in the principal amount of $40 million (approximately 5.8% of net assets) that mature on July 10, 1995 ("Securities"). The Securities pay interest at a rate equal to one-month LIBOR, and the maximum interest rate is "capped" at 12%. As a result of the Orange County bankruptcy filing on December 6, 1994, the Fund was unable to obtain reliable market quotes for these Securities, and it determined the fair values of the Securities to be less than their amortized cost values.

In December 1994, LBH entered into an agreement with the Fund in order to avoid potential loss by shareholders of the Fund ("Arrangement").[1] Under the Arrangement, the Fund has the ability each day to require LBH to purchase at par plus accrued interest such portion of the Securities as may be necessary to result in the mark-to-market calculation of the Fund's price per share being not less than $0.997. Under the Arrangement, LBH is obligated to purchase the same portion of the principal amount of the Securities from the Fund on July 10, 1995 (the final maturity date of the Securities). The Fund continues to hold the Securities, and carries a portion of the Securities in an amount that reflects their amortized cost values (their par values plus accrued interest) based on the Arrangement. The Arrangement was entered into after the staff of the Division of Investment Management informed LBH and the Fund that it would not recommend to the Commission enforcement action against the parties if the Arrangement was effected.

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[1] You represented in your letter of December 9, 1994 that LBH had the highest ratings on its short-term debt obligations from the "Requisite NRSROs" (as defined in paragraph (a)(13) of rule 2a-7 under the 1940 Act).

The Fund has been informed that Orange County, in all likelihood, will not make the scheduled principal payment due on the Securities on July 10, 1995. Rather, Orange County has proposed, and the Bankruptcy Court has approved, an amendment, substitution or extension of the Securities ("Amendment") that would, among other things, extend the maturity date of the Securities to June 30, 1996 and contain certain other terms ("Amended Securities"). The interest rate on the Amended Securities would be equal to one-month LIBOR, plus 0.95% subject to a 12% "cap." A portion of the interest on the Amended Securities would be payable monthly, and a portion of the interest would be accrued and paid to the Fund at a later date.

As a result of these developments, you state that LBH will obtain a letter of credit from Chemical Bank ("Chemical Bank")[2] which is summarized below and more fully described in your letter of July 7, 1995 ("LOC"). The LOC will provide for the payment of $43 million to the Fund ($40 million attributable to principal and $3 million attributable to interest), and the Fund will have the unconditional right to draw on the LOC if scheduled interest and principal are not paid when due under any circumstances, including a repudiation by Orange County of its obligations under the Amended Securities. LBH will agree to reimburse Chemical Bank for any payments made to the Fund under the LOC. Under the LOC or pursuant to an agreement with LBH ("Agreement"), the Fund will receive the higher of (i) interest accrued at an annualized rate, reset monthly, of LIBOR plus 0.50% with no "cap" or (ii) interest accrued at the rate provided under the Amended Securities (interest accrued at an annualized rate, reset monthly, of LIBOR plus 0.95% subject to a 12% "cap"). Finally, LBH reserves the right under the Agreement to purchase the Amended Securities from the Fund at a price equal to the greater of their amortized cost values (par values plus accrued interest) or their market values.

You represent that the board of directors of the Fund, including a majority of the directors who are not "interested persons" of the Fund as defined under section 2(a)(19) of the 1940 Act, has determined that it is in the best interests of the Fund and its shareholders not to require LBH to purchase the Securities on July 10, 1995 pursuant to the Arrangement, but, rather, to accept the Amended Securities subject to the LOC and the Agreement. This determination was based, in part, on an evaluation of the credit quality of Chemical Bank and the interest rate provided by the LOC or the Agreement. You also represent that the board of directors of the Fund has determined that the Amended Securities, together with the Agreement and the LOC, are "Eligible Securities" as defined in paragraph (a)(5) of rule 2a-7 under the 1940 Act, and present minimal credit risks as required by paragraph (c)(3) of that rule.[3] Finally, you state that the amount of the LOC

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2 You represent in your letter of July 7, 1995 that Chemical Bank currently has the highest ratings on its short-term debt obligations from the "Requisite NRSROs" (as defined in paragraph (a)(13) of rule 2a-7 under the 1940 Act).

3 We note that the Fund will hold more than five percent of its total assets in the Amended Securities. Rule 2a-7 under the 1940 Act generally prohibits a taxable money market fund from investing more than five percent of its total assets in securities issued by a single issuer, determined at the time the securities are acquired. See paragraph (c)(4)(i) of rule 2a-7. In your letter of July 7, you assert, and we agree, that the Fund is not required to treat its acceptance of the Amended Securities, subject to the LOC and the Agreement, as the acquisition of a new security for purposes of determining its compliance with the diversification standards of rule 2a-7.

attributable to interest is based on the interest rate projections of the Fund's investment adviser, Lehman Brothers Global Asset Management Inc., through the final maturity date of the Amended Securities.

On the basis of the facts and representations in your letter, we will not recommend enforcement action under sections 17(a), 17(d) and 12(d)(3) of the 1940 Act and the rules thereunder. You should note that any different facts or representations might require a different conclusion. Moreover, this response expresses the Division's position on enforcement action only and does not express any legal conclusions on the issues presented.

Sincerely,

Robert E. Plaze
Assistant Director

SIMPSON THACHER & BARTLETT

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July 7, 1995

Mr. Robert E. Plaze
Assistant Director
Office of Disclosure and
Investment Adviser Regulation
Division of Investment Management
Securities and Exchange Commission
450 Fifth Street, N.W.
Mail Stop 10-6
Washington, D.C. 20549

Dear Mr. Plaze:

We are writing on behalf of Lehman Brothers Holdings Inc. ("LBH"), an affiliated person of an affiliated person of Lehman Brothers Daily Income Fund (the "Fund"), a portfolio of Lehman Brothers Funds, Inc. (the "Company"). We seek assurance from the staff (the "Staff") of the Division of Investment Management that it will not recommend enforcement action to the Securities and Exchange Commission (the "Commission") under Sections 17(a), 17(d) or 12(d)(3) of the Investment Company Act of 1940, as amended (the "1940 Act"), or the rules thereunder, if the Fund and LBH enter into the transactions described below in place of certain existing arrangements.

The Fund is a diversified portfolio of the Company, which is registered with the Commission under the 1940 Act as an open-end management investment company. The Fund, a money market fund, seeks to maintain a stable net asset value per share of $1.00, and uses the amortized cost method of valuation in valuing its portfolio securities as provided for in Rule 2a-7 under the 1940 Act ("Rule 2a-7"). The Fund's investment adviser is Lehman Brothers Global Asset Management Inc. ("LBGAM"), a wholly-owned subsidiary of LBH.

The Fund holds in its portfolio taxable commercial paper (the "Notes") issued by Orange County on July 8, 1994, which matures on July 10, 1995. The Fund currently holds $40,000,000 in principal amount of the Notes, which represented approximately 5.8% of the Fund's portfolio as of the date hereof. On December 6, 1994, Orange County filed for relief under Chapter 9 of the United States Bankruptcy Code. Because of Orange County's bankruptcy and the resulting disruption of the municipal markets, LBH, on December 8, 1994, offered to enter into an arrangement with the Fund with respect to the Notes providing the Fund with the ability to cause LBH to purchase a portion of the Notes from the Fund at par plus accrued interest (amortized cost) for a ninety-day period. By letters dated December 9 and December 12, 1994, LBH requested that the Staff grant no-action relief with respect to the arrangement pursuant to Sections 17 and 12 under the 1940 Act. The Staff granted oral no-action relief. On March 1, 1995, the Staff granted additional oral no-action relief regarding the extension of the arrangement to the maturity of the Notes.

Pursuant to the arrangement between the Fund and LBH, the amount of the Notes subject to the arrangement adjusts each day based on whether the Fund's mark-to-market calculation of the Notes (without giving effect to the arrangement) on a particular day together with the other securities in the Fund's portfolio would be less than 99.7%. The Fund has the ability each day to require LBH to purchase, at par plus accrued interest, such portion of the Notes as is necessary to result in the mark-to-market calculation of the Fund's portfolio being not less than 99.7%. If LBH's short-term debt securities are downgraded such that they are no longer rated "First Tier" (as defined in Rule 2a-7) by the "Requisite NRSROs" (as defined in Rule 2a-7), LBH is required to purchase that portion of the Notes necessary to maintain the mark-to-market calculation at not less than 99.7%. In addition, LBH is obligated to purchase a similar principal amount of the Notes from the Fund at maturity.

As stated above, principal with respect to the Notes is currently due on July 10, 1995. Interest with respect to the Notes is payable monthly at an annual rate equal to LIBOR, subject to a monthly reset and a maximum interest rate level or "cap" of 12%. While the County has made all interest payments with respect to the Notes to date, the County is not expected to pay the principal due on the Notes on July 10. On June 2, 1995, the County filed with the Bankruptcy Court a proposed stipulation and agreement (the "Extension Agreement") regarding an amendment, substitution or extension of the Notes (the "Amended Notes"). On June 27, the Bankruptcy Court approved the stipulation, as amended, and the Extension Agreement. Under the Extension Agreement, the maturity of the Notes will be extended to June 30, 1996. Interest on the Notes will continue to accrue based on the current formula rate. A portion of the monthly interest will be paid in cash based on a formula tied to the earnings on the repayment reserves for the Notes, with the remaining accruing portion payable at maturity. In addition, under the Extension Agreement the County will pay to the holders of the Notes at maturity an additional amount equal to .95% of the principal amount of the Notes held by each such holder, as compensation for the costs associated with the bankruptcy of the County. Under the Extension Agreement and the stipulation, the County has waived certain grounds for challenging the validity of the Notes while retaining certain other grounds, principally the allegation that the Notes were issued for an improper purpose and that the security interest in the reserves set aside to pay the Notes was not perfected.

In light of the Extension Agreement and the expectation that the maturity of the Notes will be extended, it is proposed that a third-party letter of credit (the "LOC") be obtained for the Fund from Chemical Bank ("Chemical Bank") to take the place of the Fund's current arrangement with LBH. The LOC would be in the amount of $43 million ($40 million attributable to principal and $3 million attributable to interest) and would guarantee the payment of all principal and interest due on the Notes up to the maximum amount of the LOC. Chemical Bank currently is rated First Tier by the Requisite NRSROs. The Fund would have the unconditional right to draw on the LOC if scheduled principal and interest payments were not made when due under any circumstances, including if Orange County repudiated its obligations under the Amended

Notes. Pursuant to an agreement between LBH and Chemical Bank, LBH would reimburse Chemical Bank for any payment to the Fund under the LOC.

Since the Notes are variable rate securities, the amount of the LOC attributable to interest has been based on LBGAM's interest rate forecast through the maturity of the Amended Notes. Pursuant to an agreement with the Fund (the "Agreement"), LBH will agree to pay any additional amounts in the event that the amount of the LOC is insufficient to pay all principal and interest on the Amended Notes when due. Further, LBH has agreed that the Fund will receive either pursuant to the Amended Notes or the Agreement the higher of (i) interest accrued at an annualized rate, reset monthly, of LIBOR plus .50%, with no "cap" on the rate or (ii) interest accrued at the rate proposed under the Amended Notes, which is an annualized rate, reset monthly, of LIBOR plus .95% with a "cap" of 12%. Pursuant to the Agreement, LBH would have the right to require the Fund, at any time prior to the June 30, 1996 maturity date of the Amended Notes, to sell some or all of the Notes to LBH at a price equal to the greater of par plus accrued interest or market.

The LOC and the Agreement have been approved by the Board of Directors of the Fund, including a majority of the Directors who are not "interested persons" of the Fund as defined under Section 2(a)(19) of the 1940 Act, subject to the receipt of appropriate relief from the Staff. In addition, the Board of Directors of the Fund has directed that the Fund from time to time exercise its rights under the LOC and the Agreement upon the occurrence of an event or events entitling it to payment thereunder.

In connection with its approval, the Board of Directors of the Fund, upon the representations and recommendations of LBGAM, determined that, if this were a new investment decision, the Amended Notes, the LOC and the Agreement, combined, would result in an investment by the Fund in an "Eligible Security" (as defined under Rule 2a-7) presenting minimal credit risk; and determined that it was in the best interest of the Fund and its shareholders not to require LBH to purchase the Notes under the current arrangement, but, rather, to accept the Extension Agreement, the Amended Notes, the LOC and the Agreement. With respect to the diversification requirements under Rule 2a-7(c)(4)(i), the Fund will not treat the extension of the maturity of the Notes as an acquisition of a new security. It is our understanding that the Staff is in accordance with this view.

As indicated above, LBH is obligated to pay the amount of any shortfall in the amount of the LOC covering interest payments. In view of the terms of the LOC, including the amount of the LOC attributable to interest, reliance upon the creditworthiness of LBH is an insignificant aspect of this transaction.

As indicated above, LBH is an "affiliated person" of an "affiliated person" of the Fund under Section 2(a)(3) of the 1940 Act since, as described above, LBGAM is the investment adviser of the Fund. The proposed transaction may fall within Section 17(a)(1) of the 1940 Act, which makes it unlawful for any affiliated person of a registered investment company or any affiliated person of such person acting as principal to knowingly sell any security or other property to the investment company. In addition, the transaction may fall within Section 17(a)(2) of the 1940 Act, which makes it unlawful for any affiliated person of a registered investment company or any affiliated person of such person acting as principal to knowingly purchase any security or other property from the investment company. The proposed transaction may also fall within Section 17(d) of the 1940 Act, which generally prohibits investment companies and their affiliates, or affiliates of affiliates, from engaging in "joint transactions."

The Fund and LBH believe that the LOC and the Agreement are in the best interest of the Fund and its shareholders. LBH and the Fund hereby request that the Staff give its assurance that it will not recommend that the Commission take enforcement action against LBH or the Fund under Sections 17(a) or 17(d) if LBH and the Fund enter into the Agreement and the Fund obtains the LOC, and if the parties engage in the transactions contemplated thereby. To the extent that the foregoing arrangements may raise issues under Section 12(d)(3) of the 1940 Act, we also request assurance that the Staff will not recommend that the Commission take enforcement action against LBH or the Fund under such provision of the 1940 Act.

If you have any questions or other communications concerning this matter, please call Sarah E. Cogan at 212-455-3575 or James J. Burns at 212-455-7083.

Very truly yours,

Simpson Thacher & Bartlett

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FREEDOM OF INFORMATION ACT
CONFIDENTIAL TREATMENT REQUESTED

December 9, 1994

Via Facsimile

Kenneth J. Berman
Deputy Office Chief
Office of Disclosure and Investment
Adviser Regulation
Division of Investment Management
U.S. Securities and Exchange Commission
450 Fifth Street, N.W.
Mail Stop 10-6
Washington, D.C. 20549

Re: Lehman Brothers Daily Income Fund

Dear Mr. Berman:

We are writing on behalf of Lehman Brothers Holdings Inc. (the "Affiliate"), an affiliated person of an affiliated person of Lehman Brothers Daily Income Fund (the "Fund"), a portfolio of Lehman Brothers Funds, Inc. (the "Company"). We seek assurance from the staff (the "Staff") of the Division of Investment Management (the "Division") that it will not recommend enforcement action to the Securities and Exchange Commission (the "Commission") under Section 17(a) of the Investment Company Act of 1940, as amended (the "1940 Act"), or the rules thereunder, if the Fund and the Affiliate enter into the transactions described below.

The Fund is a diversified portfolio of the Company, which is registered with the Commission under the 1940 Act as an open-end management investment company. The Fund's investment adviser is Lehman Brothers Global Asset Management Inc. (the "Adviser"), a wholly owned subsidiary of the Affiliate. The Fund, a money market fund,

CONFIDENTIAL TREATMENT WAIVED
BY COUNSEL.
NOTATION BY THE DIVISION OF
INVESTMENT MANAGEMENT 7/25/95.

seeks to maintain a stable net asset value per share of $1.00, and uses the amortized cost method of valuation in valuing its portfolio securities as provided for in Rule 2a-7 under the 1940 Act ("Rule 2a-7"). Approximately 6% of the Fund's net assets as of the date hereof consist of certain debt securities (the "Securities") as more fully described below. As a result of the Orange County, California bankruptcy, the Fund has experienced difficulties in obtaining reliable market quotes for the Securities. The Securities consist of $40,000,000 in principal amount of taxable commercial paper issued by Orange County and purchased by the Fund on July 24, 1994. The Securities mature on July 10, 1995. The CUSIP number of the Securities is 684201EL6.

Because of the Orange County bankruptcy and the resulting disruption of the municipal markets, the Affiliate, on December 8, 1994, offered to enter into an agreement with the Fund with respect to the Securities providing the Fund with the ability to put a portion of the Securities to the Affiliate at par plus accrued interest (amortized cost) for a ninety-day period. The amount of the Securities subject to the put adjusts each day based on whether the Fund's mark-to-market calculation of the Securities (without giving effect to the put) on a particular day together with the other securities in the Fund's portfolio would be less than 99.7%. The Fund will have the ability each day to require the Affiliate to purchase at par plus accrued interest such portion of the Securities as may be necessary to result in the mark-to-market calculation of the Fund's portfolio being not less than 99.7%. For example, assume that the aggregate amortized cost of the Fund's portfolio were $645 million (which includes the Securities at their amortized cost value of $40 million). If the Securities were marked-to-market at 90% of amortized cost, their market value would be $36 million. Assume that there were no deviation from amortized cost with respect to the remaining portion of the portfolio. The total market value of the portfolio would thus be $641 million, and the mark-to-market value of the portfolio versus amortized cost would be 99.379845%. In order to maintain a mark-to-market calculation not less than 99.7% of amortized cost, an additional $2,065,000 in value would need to be added to the portfolio through the put, by bringing a portion of the Securities to a value of 100. Given that the Securities were priced at 90, $20,650,000 worth of Securities would be subject to the put.

Certain features discussed with the Staff have been included in the put. The Affiliate's short-term securities currently are rated "First Tier" by the Requisite NRSROs (as defined in Rule 2a-7). The put is required to be exercised in the event that the Affiliate's short-term securities are no longer rated First Tier by the Requisite NRSROs. In addition, the portion of the put, if any, that remains outstanding on the 90th day (assuming the put has not been exercised, extended or terminated) is required to be exercised at that point. The Fund understands that the Staff may be willing to consider a further extension of the put beyond the 90th day, but that any such extension would require further review by the Staff.

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The Board of Directors of the Fund has reviewed the terms of the transaction, including the provisions of the put that require its mandatory exercise in certain circumstances. The independent directors were advised by separate counsel. As was indicated in our telephone conversations yesterday, determination of the value of securities for which market quotes are not readily available, including the Securities, will be made by a pricing committee appointed by the Board of Directors, which currently includes any one of the Fund's independent directors and any one of certain designated officers of the Fund or the Adviser. Valuation determinations by the committee will require unanimity. Valuation determinations by the committee will be reviewed by the full Board at the next regular meeting of the Board.

The Affiliate is an "affiliated person" of an "affiliated person" under Section 2(a)(3) of the 1940 Act since the Affiliate is the parent company of the Adviser. The transaction may fall within Section 17(a)(1) of the 1940 Act, which makes it unlawful for any affiliated person of a registered investment company or any affiliated person of such person acting as principal to knowingly sell any security or other property to the investment company. In addition, the transaction falls within Section 17(a)(2) of the 1940 Act, which makes it unlawful for an affiliated person of a registered investment company or any affiliated person of such person acting as principal to purchase any security or other property from the investment company.

The Fund and the Affiliate believe that the acquisition of the put from the Affiliate as well as any subsequent acquisition of the Securities by the Affiliate pursuant to exercise of the put by the Fund is in the best interests of the Fund's shareholders. Any of the Securities that are actually put to the Affiliate would be acquired at par plus accrued interest. On behalf of the Fund and the Affiliate, we hereby request that the Staff give its assurance that it will not recommend that the Commission take enforcement action against the Fund or the Affiliate under Section 17(a) of the 1940 Act in connection with the acquisition of the put by the Fund and any subsequent purchase by the Affiliate of the Securities pursuant to the terms of the put as described above.

If you have any questions or other communications concerning this matter, please call George R. Krouse, Jr. at (212) 455-2730, Sarah E. Cogan at (212) 455-3575 or James J. Burns at (212) 455-7083.

Very truly yours,

Simpson Thacher & Bartlett

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