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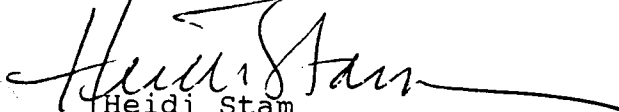
4 AUG 1994

RESPONSE OF THE OFFICE OF CHIEF COUNSEL
DIVISION OF INVESTMENT MANAGEMENT

Our Ref. No. 94-472-CC
PaineWebber Managed
Investments Trust
File No. 811-4040

By letter dated August 3, 1994, PaineWebber Capital Inc. ("PWC") and PaineWebber Managed Investments Trust (the "Trust"), of which PaineWebber Short-Term U.S. Government Income Fund (the "Fund") is a series, request our assurance that we will not recommend any enforcement action under Section 17(a) of the Investment Company Act of 1940 against PWC, the Trust, or the Fund as a result of the transaction described in the letter.

On the basis of the unusual facts and circumstances described in the letter, and the specific representations therein, we will not recommend enforcement action under Section 17(a). Our position applies solely to the transaction described in the letter. We take no position with respect to any other aspect of the underlying matter, including, but not limited to, the valuation of the securities that are the subject of the transaction. 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.


Heidi Stam
Assistant Chief Counsel

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August 3, 1994

1940 Act Section 17(a)

HAND DELIVERED

Heidi Stam, Esquire
Assistant Chief Counsel
Division of Investment Management
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

ACT ICA-40
SECTION 17(a)
RULE _____
PUBLIC _____
AVAILABILITY 8/4/94

Re: PaineWebber Managed Investments Trust:
PaineWebber Short-Term U.S. Government Income Fund

Dear Ms. Stam:

We are writing on behalf of PaineWebber Capital Inc. ("PWC") and PaineWebber Managed Investments Trust ("Trust"), an investment company registered under the Investment Company Act of 1940 ("1940 Act"), of which PaineWebber Short-Term U.S. Government Income Fund ("Fund") is a series, to seek your assurance that the staff of the Division of Investment Management ("Staff") will not recommend enforcement action under Section 17(a) of the 1940 Act against PWC, the Trust or the Fund if PWC purchases from the Fund two "structured floater" securities, as described below. PWC, the Trust and the Fund believe that the proposed sale of the securities is in the best interests of the Fund and its shareholders, that the sale would be consistent with prudent portfolio management of the Fund under the Fund's investment objective and policies, and that under the unusual and novel circumstances presented, a no-action position is appropriate in this matter.

I. Background on the Parties, the Structured Floaters, and the Proposed Transaction

PWC is a wholly-owned subsidiary of Paine Webber Group Inc., a publicly held financial services holding company. Mitchell Hutchins Asset Management Inc. ("MH"), a broker-dealer registered under the Securities Exchange Act of 1934 ("1934 Act") and an

investment adviser registered under the Investment Advisers Act of 1940, is a wholly-owned subsidiary of PaineWebber Incorporated ("PaineWebber"), another wholly-owned subsidiary of Paine Webber Group Inc. and a broker-dealer registered under the 1934 Act. MH serves as investment adviser and administrator of the Fund pursuant to a contract with the Trust. MH acts as the distributor of the shares of the Fund under separate distribution contracts with the Trust. Under separate exclusive dealer agreements between MH and PaineWebber, PaineWebber and its correspondent firms sell the Fund's shares.

The Trust was organized under Massachusetts law by a Declaration of Trust dated November 21, 1986. The Trust is a series mutual fund with six series, including the Fund. The Fund commenced operations on May 3, 1993. The Fund's investment objective is to achieve the highest level of income consistent with the preservation of capital and low volatility of net asset value. The Fund invests, under normal conditions, at least 65% of its total assets in U.S. government securities, including mortgage-backed securities issued or guaranteed by the U.S. government, its agencies or instrumentalities, other obligations issued or guaranteed by the U.S. government, its agencies or instrumentalities and repurchase agreements with respect to those securities. Up to 35% of the Fund's total assets may be invested in mortgage- and asset-backed securities that are issued by private issuers and that at the time of purchase have been rated AAA by Standard & Poor's Ratings Group or Aaa by Moody's Investors Service, Inc., have an equivalent rating from another nationally recognized statistical ratings organization or, if unrated, have been determined by MH to be of comparable quality.

Among the portfolio securities currently held by the Fund are two mortgage-backed securities commonly referred to as "structured floaters." The first of these structured floaters ("Security I") was purchased by the Fund on March 23, 1994. The second of these structured floaters ("Security II") was originally issued in July 1993, and was purchased by the Fund on March 29, 1994. Security I was issued by the Federal National Mortgage Association, and thus is a "government security," as defined in Section 2(a)(16) of the 1940 Act; Security II was issued by a private issuer and is rated AAA by Fitch Investors Service, Inc.

Over the past several months, the mortgage-backed securities markets have endured an unprecedented period of disruption. Dealers, hedge funds and other institutional investors have been forced to liquidate large holdings in mortgage-backed securities, resulting in severely depressed prices and, in some instances,

greatly reduced liquidity.^{1/} As a consequence of these events, by early June, the Fund's Valuation Committee had determined that the Securities were illiquid. These dramatically changing market conditions also had an adverse effect on the Fund, which experienced a decrease in its net asset value per share and a relatively rapid rate of net redemptions. The effect of the redemption rate was exacerbated when, starting on June 7, 1994, the Fund suspended sales of new shares pending court approval of the proposed settlement of certain class action litigation. The Fund's net assets were reduced from approximately \$1,029,000,000 on June 7 to approximately \$730,000,000 on July 27. During the month of July, the Fund experienced redemptions at a rate of approximately \$8 million per day.

As Fund redemptions have continued, the proportion of the Fund's assets represented by the Securities has increased. As of July 27, the Securities amounted to approximately 24% of the Fund's assets. As the Securities came to represent a larger and larger percentage of the Fund's assets (and with the prospect that this trend would only continue), the Securities presented certain portfolio management issues. For example, in the current rising interest rate environment, MH has sought to maintain a weighted average portfolio duration for the Fund of approximately 1.5 years, which is shorter than the duration of either of the Securities. Maintaining this duration while the Fund is holding its current large positions in the Securities becomes more difficult as the Fund's asset size shrinks. Moreover, adverse publicity regarding structured floaters in general (frequently referred to in the press as "kitchen sink" bonds),^{2/} and regarding the Fund's holdings of these securities in particular,^{3/} has created additional pressures on the Fund to dispose of the Securities.

In the absence of reliable and meaningful market quotations for the Securities, on June 27, the Fund's Valuation Committee determined that the Fund should utilize an alternative pricing

^{1/} See generally Jeffrey M. Laderman, What's a Security Worth?, BUSINESS WEEK, July 25, 1994, at p. 76 ("And now, says [Edward J.] Kohler, mortgage-backed securities are a 'dysfunctional market'"); Mortgage-backed Securities; Not for Widows, Orphans or Hedge Funds, THE ECONOMIST, July 9, 1994, at p. 81 (referencing "the recent distress in the [mortgage-backed securities] market").

^{2/} See, e.g., Richard Waters, No Longer as Safe as Houses: The Repercussions of Losses Made in the US Market for Securities Based on Home Loans, FINANCIAL TIMES, July 22, 1994, at 15; John Connor, Currency Comptroller Warns Banks About Investing in Structured Notes, WALL ST. J., July 22, 1994, at A4B.

^{3/} See, e.g., BARRON'S, July 4, 1994, at MW9.

methodology to value the Securities for purposes of calculating the Fund's net asset value.^{4/} Using the Fund's methodology, the fair values of Securities I and II were \$104,478,814 and \$75,846,663, respectively, on July 21, 1994. On that date, recognizing the nearly total absence of market demand at fair value for these instruments, PWC presented to the independent Trustees of the Trust, and the independent Trustees approved, a proposal whereby, subject to regulatory review, PWC would purchase the Securities at those July 21 prices. This PWC proposal was confirmed in a written bid (again subject to regulatory review) on July 22. The bid is revocable by PWC on 24 hours' notice, and PWC may need to exercise its right to revoke the bid if business considerations so require. PWC agreed as part of its proposal that if PWC sold or disposed of the Securities by July 22, 1996 (or if one or both of the Securities were unsold at the end of such two-year period and firm offers to purchase were available for the unsold Securities), PWC would pay to the Fund the amount, if any, by which such sale proceeds and/or firm offers to purchase exceeded PWC's purchase price plus its carrying costs for the Securities.^{5/}

The independent Trustees' approval of the proposal was conditioned on the Fund being unable to sell the Securities in the market at the same or a higher price than would be paid by PWC following regulatory review. Thus, even though it was deemed highly unlikely that the condition would occur, prior to closing the purchase, the Fund would confirm that there was no interest in the market to buy either Security at a price equal to or higher

^{4/} Under this methodology, the Valuation Committee established a fair value for the Securities based on the discount from par that, when combined with the coupon interest on the securities, would produce a yield equal to the estimated market spread over LIBOR required by the market. LIBOR was utilized in this methodology because the Securities each pay a coupon rate of interest that is adjusted monthly based on one-month LIBOR. The estimated spread over LIBOR was initially determined by reference to the most recent dealer quotes on other structured floaters that were available to, and were considered reliable by, MH. The yield implicit in those quotes was then used to calculate the spread over LIBOR required by the market for instruments such as these. The difference between that market spread and the spread provided by the coupon rate of interest on each of the Securities was then used to derive a market price for each Security that was sufficiently discounted from par to produce a market yield. The market price so derived is then adjusted daily based on the actual changes in the market price of Treasury securities having approximately the same anticipated average lives as the respective Securities.

^{5/} The proposal was referenced in PaineWebber's press release containing its second quarter financial results, issued on July 22.

than the firm bids made by PWC. If a firm offer was made at such a price, the Fund would accept it. Further, as indicated above, the proposal by PWC was conditioned upon regulatory review by the Staff with respect to Section 17(a) issues. It is to remove the latter condition to the proposed transaction that PWC, the Trust and the Fund seek this no-action letter.

II. Analysis

Section 17(a) of the 1940 Act prohibits, among other things, an affiliated person of a registered investment company or an affiliated person of such person, acting as principal, from knowingly purchasing any security or other property from such registered investment company. Accordingly, Section 17(a) would proscribe the proposed transaction -- which involves a purchase of securities from the Fund by an affiliated person of an affiliated person of the Fund, acting as principal. We recognize that as a general matter, the Staff will not entertain no-action requests under Section 17(a).^{6/} As the Staff has recognized, however, no-action positions under Section 17(a) may be appropriate in "very unusual or novel circumstances."^{7/} Indeed, on a number of occasions, the Staff has taken no-action positions under Section 17(a), albeit under circumstances different than those here presented.^{8/}

^{6/} Section 17(b) of the 1940 Act provides a statutory mechanism for exemptive relief from the proscriptions of Section 17(a). Under Section 17(b), the Commission may exempt a proposed transaction from Section 17(a) upon application when it finds that (1) the terms of the proposed transaction, including the consideration to be paid or received, are reasonable and fair and do not involve overreaching on the part of any person concerned, (2) the proposed transaction is consistent with the policy of each registered investment company concerned, and (3) the proposed transaction is consistent with the general purposes of the 1940 Act.

^{7/} See Massachusetts Investors Trust, SEC No-Action Letter (Dec. 8, 1992).

^{8/} Thus, in dealing with defaulted securities held by money market funds, the Staff has taken no-action positions without requiring applicants to seek exemptive orders under Section 17(b), notwithstanding that the transactions clearly fall within Section 17(a)(2) of the 1940 Act. See, e.g., Liquid Green Trust, SEC No-Action Letter (Dec. 19, 1991) (Staff granted no-action request under Sections 17(a) and 17(d) to permit "purchase" by an adviser of defaulted commercial paper held by fund).

(continued...)

For the reasons indicated above, a no-action position enabling PWC to purchase the Securities on the terms proposed is urgently needed as a business matter. In the time that would be required for PWC and the Trust to file, and for the Commission to act upon, an exemptive application under Section 17(b), continued redemptions in the Fund -- perhaps exacerbated by the obstacles to effective management that could be presented as the Securities come to represent a still larger percentage of the Fund's total assets -- could reach a point such that MH's efforts to achieve the Fund's objective is severely impaired, thereby harming the Fund's remaining shareholders. The passage of time may also make it impracticable for PWC to purchase these securities as a business matter. Thus, a delay could simply foreclose the proposed transaction.^{9/} The proposed transaction is clearly in the best interests of the Fund and its shareholders, and the terms of the proposed transaction, including the consideration to be paid to the

^{8/}(...continued)

Moreover, in at least one response to a no-action request, the Staff has explicitly recognized that the "business urgency" of a proposed transaction may support a no-action position under Section 17. In Narragansett Capital Corporation, SEC No-Action Letter (Dec. 15, 1974), the Staff took a no-action position under Rule 17d-1(d)(5) before that rule was effective. The Staff noted that while it was usually unwilling to take a no-action position prior to a rule's effective date, especially in a situation that would otherwise require an application for exemption, it would take a no-action position, in part because of the "unique facts involved, including the business urgency of the transaction"

The Staff has also taken no-action positions without requiring applicants to seek exemptive orders under Section 17(b) for de minimis transactions. See National Aviation & Technology Corporation, SEC No-Action Letter (May 28, 1983) (no-action relief granted for purchase by investment adviser from affiliated fund of \$10,945 worth of office furniture and fixtures and a telephone system); Nelson Fund, Inc., SEC No-Action Letter (Dec. 15, 1975) (no-action relief granted in view of imminent liquidation of fund and de minimis financial impact of prohibited transactions involving assignment of "key man" insurance policy and sale of office equipment, furniture, fixtures and supplies to an affiliated person of the fund).

^{9/} Cf. Division of Investment Management, United States Securities and Exchange Commission, Protecting Investors: A Half Century of Investment Company Regulation 483 (1992) ("[B]ecause of the time and cost attendant to filing an application, it is probable that many transactions that do not involve overreaching are simply foregone; thus, the restrictions [of Section 17] also may impose opportunity costs on investment companies").

Fund, are reasonable and fair and do not involve overreaching on the part of any of the parties.

Even assuming that the Securities could be sold in the market, the price to be paid by PWC for the Securities will necessarily exceed what would be available elsewhere. This is because the Fund's independent Trustees, in approving the proposal as reasonable and fair, conditioned their approval on the Fund's being unable to sell the Securities in the market at the same or a higher price than would be paid by PWC following regulatory review. PWC's good faith with respect to the purchase price to be paid is evidenced by its further commitment to pay to the Fund the amount, if any, by which the price of the Securities sold or disposed of within two years of the purchase (or, if unsold at the end of the two-year period, the price at which firm offers to purchase, if any, are then available for the Securities) exceeds PWC's acquisition and carrying costs for the Securities.

The benefits to the Fund and its shareholders from the proposed transaction are clear. A delay until a normal market for the Securities is restored -- which restoration cannot be fairly predicted or guaranteed -- could have adverse consequences for the Fund. Prudent portfolio management of the Fund under its investment objective and policies would dictate reduction or elimination of the position as soon as possible. The possibility of a "fire sale" in the market, in which PWC would be disqualified from bidding for the Securities, could have more adverse consequences for the Fund than would simply having the Fund hold the Securities. A sale of the Securities to PWC at the price established by the Fund would not have these adverse consequences, and, indeed, would have the beneficial effect of providing cash to the Fund that could be redeployed in a manner most advantageous to shareholders.

The proposed transaction would not only enhance management of the Fund's portfolio but also would enhance liquidity for redeeming shareholders. Moreover, when the transaction is completed, PaineWebber and MH expect that the rate of redemptions will decline, thereby reducing the very pressures that currently are making it difficult for the Fund to achieve its objective. If the transaction is consummated, the Fund's investment adviser will be in a position to maintain a level of liquidity in the portfolio that should satisfy any level of redemption activity, and permit better management of the asset mix. Conversely, if the transaction is not completed promptly, the very problem now faced by the Fund -- illiquidity in the face of increasing redemptions and undue constraints on portfolio management -- may well be exacerbated.

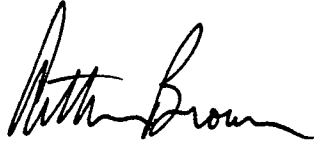
In conclusion, we believe that because the proposed transaction is fair and reasonable and in the best interests of the Fund and its shareholders, and because business exigencies and the potentially adverse effects of delay militate against undertaking

KIRKPATRICK & LOCKHART

a lengthy exemptive process, it is appropriate for the Staff to take the no-action position requested. We understand that the Staff is not taking any position on any other aspects of the underlying matter.

If you have any questions regarding this letter or require additional information, please contact the undersigned at the above number.

Sincerely,

A handwritten signature in cursive script, appearing to read "Arthur J. Brown".

Arthur J. Brown

cc: Theodore A. Levine, Esq.
Victoria E. Schonfeld, Esq.