June 18, 1981

Investment Company Act of 1940/Section 17(f); Rule 17f-2

Securities and Exchange Commission
500 North Capitol Street
Washington, D.C. 20549

Attention: Stanley B. Judd, Esq.
Assistant Chief Counsel
Division of Investment Management

Re: The Adams Company
File No. 811-2624

Gentlemen:

We are counsel to The Adams Express Company ("Adams"), a closed-end investment company registered under the Investment Company Act of 1940 ("1940 Act"). Reference is made to our letters to you of March 22, 1979 and July 13, 1979 in which we requested the advice of the staff of the Securities and Exchange Commission ("Commission") as to whether a "standby" letter of credit, issued under the circumstances described therein, could be used to collateralize a loan of portfolio securities...
by a registered investment company in compliance with Section 17(f) of the 1940 Act and Rule 17f-2 thereunder. In your response of September 20, 1979 (Reference No. 79-105-CC), you indicated that enforcement action would not be recommended if Adams accepted irrevocable letters of credit as collateral "under the terms and in the manner" described in our prior correspondence. Copies of our prior correspondence and your response thereto are enclosed herewith for your convenience.

Our prior correspondence indicated that Adams would not accept a letter of credit from an issuer proposed by a borrower unless Adams' Board of Directors had given its prior approval to such issuer and that only "banks which, at a minimum, satisfy the qualifications under Section 17(f) of the 1940 Act applicable to bank custodians of registered investment companies" would be eligible for consideration. A "bank" is defined under Section 2(a)(5) of the 1940 Act, in relevant part, as "(A) a banking institution organized under the laws of the United States . . . [or] (C) any other banking institution . . . doing business under the laws of any State or of the United States, a substantial portion of the business of which consists of receiving deposits . . . and which is supervised and examined by State or Federal
authority having supervision over banks . . . ." Pursuant to Section 17(f), a bank custodian must have the qualifications prescribed by Section 26(a) which requires that such bank at all times have "an aggregate capital, surplus, and undivided profits of . . . not less than $500,000 . . . ."

Adams has informed us that recently a major institutional borrower proposed to collateralize its securities loans with a letter of credit to be issued by the New York City branch of a bank organized under French law. Publicly available information indicates that the proposed issuing bank is one of three French banking subsidiaries of a Paris-based banking and financial holding company with total consolidated worldwide assets of approximately $53 billion. The bank is reported to be one of France's largest commercial and investment banks with approximately $18 billion in total assets, $18 million in retained earnings and $101 million in reserves at December 31, 1980 and net income of approximately $31.5 million for the year then ended. In its annual listing, the American Banker (July 25, 1980) reported that as of December 31, 1979 among world banks the French bank ranked 104th in terms of assets and 127th in terms of deposits and among French banks it ranked 7th in terms of deposits.
The New York City branch of the French bank is licensed pursuant to the New York State Banking Law to transact the business of "buying, selling, paying or collecting bills of exchange, or of issuing letters or credit or of receiving money for transmission or transmitting the same by draft check, cable or otherwise, or of making loans, or receiving deposits . . . ." Under New York law, the licensing of a branch of a foreign bank, which must be renewed annually, requires that such bank submit information as to its management, business and financial condition and the licensed branch is subject to extensive state regulation and examination, including compliance with applicable capital deposit and asset maintenance tests and financial reporting requirements. The French bank also operates a branch in Los Angeles, California and a subsidiary in Houston, Texas and is subject to regulation and supervision under the applicable banking laws of these states, in addition to regulation under the Bank Holding Company Act of 1956, as amended, 12 U.S.C. § 1841 et. seq., and the International Banking Act of 1978, 12 U.S.C. §§ 3101-3108 ("IBA").

We have been advised, however, in telephone conversations with personnel from the staff of the Commission's Division of Investment Management that the staff of the Division takes the position that a bank organized
under the laws of a foreign jurisdiction with domestically licensed branch or agency operations does not satisfy the definition of a "bank" under Section 2(a)(5), which would require that the "parent" bank itself be "organized" or "doing business" under state or Federal law. Thus, although the branch of the above-mentioned French bank which would issue the letter of credit is licensed, supervised and examined by the New York State Banking Department and the bank has other domestically licensed operations, the bank would be ineligible for consideration by Adams as an issuing bank under the eligibility criteria referred to above.

As a result of applying the technical definition of "bank" under Section 2(a)(5), if Adams adheres to its initial standard of eligibility a class of reliable and financially strong banking institutions will be eliminated as candidates for issuing letter of credit collateral. Because often there are established banking and other relationships between potential borrowers and certain banks, the ultimate effect may be to prevent Adams from entering into favorable lending arrangements, a result neither intended nor justified, as more fully explained below.

In selecting the criteria of "banks" qualifying under Section 17(f), Adams' objective was to set "high
standards of issuer eligibility" in order to minimize any risk of issuer insolvency and the standards applicable to custodians of registered investment companies appeared to be appropriate criteria. There was no intention, however, of eliminating the entire category of foreign banking institutions which could offer numerous candidates of established international banking reputation and financial strength equal if not superior to those domestic banks which could satisfy the technical definition of "bank" under Section 2(a)(5).

We note that the staff of the Commission has acknowledged that a foreign bank with domestically licensed subsidiary, branch or agency operations may be considered to have the essential attributes of a "bank" for purposes of determining the availability of the exemption from registration as an investment company under Section 3(c)(3) of the 1940 Act, which excludes "banks" from the definition of an investment company. In rendering no-action advice concerning the availability of the "bank" exemption in Bank Leumi le-Israel B.M. (available August 27, 1976), the staff of the Commission relied upon counsel's opinion that the Israeli bank, which was engaged in domestic banking operations through branches and subsidiaries doing business under the laws of New York, California and Florida, was
within the definition of Section 2(a)(5)(C) primarily because of the extent of the regulation and supervision of the bank's domestic activities under state law. See also Bank Leumi le-Israel B.M. (letter dated June 19, 1969); Israel Discount Bank Ltd. (letter dated November 7, 1969).

Similarly, the staff of the Commission frequently has relied on opinions of counsel that the nature and extent of the supervision and the manner of regulation of foreign bank branches and agencies under state law brought such "banks" within the registration exemption under Section 3(a)(2) of the Securities Act of 1933 available to securities "issued or guaranteed by any bank" (including letters of credit). Although Section 3(a)(2) applies to "any banking institution organized under the laws of any state ... the business of which is substantially confined to banking and is supervised by the State ... banking commission or similar official", because of the state's extensive regulatory oversight the staff permitted reliance on the exemption notwithstanding that licensing under state law was not "identical" to being "organized" thereunder. See, inter alia, Toronto-Dominion Bank (available January 12, 1981); The Mitsui Bank, Limited (available October 15, 1979); Barclays Bank International, Ltd. (available January 22, 1979). Of particular interest is a recent no-action inquiry, Societe
Generale-New York (Current) CCH Fed. Sec. L. Rep. ¶ 76,775 (available October 27, 1980), in which the staff of the Commission advised that it would not recommend enforcement action if a branch of a French bank, licensed to do business under the New York State Banking Law, issued irrevocable letters of credit to support industrial development bonds in reliance on the Section 3(a)(2) exemption. The staff specifically noted the "nature and extent of the supervision and regulation" of the domestic branch under the New York State Banking Law, as detailed in the no-action request, and relied upon the opinion of the bank's counsel that the foreign bank should be considered to be a "bank" for purposes of Section 3(a)(2).

We also note that as a result of enactment of the IBA, the degree of federal supervision and regulation over the operations of foreign banks has been significantly expanded and many of the operations of foreign banks are now subject to federal regulation and supervision. Prior to enactment of the IBA, the establishment of U.S. branches and agencies of foreign banks was subject solely to state law and state banking departments exercised exclusive supervisory authority over their operations, whereas now foreign banks have the option of establishing either federal or state branches or agencies. Such federal branches and agencies
are subject to examination and supervision by the Comptroller of the Currency and, in general, are subject to the same statutory and regulatory provisions applicable to national banks operating in the same location. Every branch or agency of a foreign bank must conduct its operations in compliance with the laws applicable to national banks or state-chartered banks doing business in the state in which such branch or agency is doing business. Although foreign branches and agencies are not required to become members of the Federal Reserve System, all foreign branches and agencies are subject to certain federal reporting requirements, the Federal and state branches of those foreign banks with worldwide consolidated assets in excess of $1 billion are subject to reserve requirements and FDIC insurance is generally mandatory for Federal branches engaged in the domestic retail deposit taking business.

As with any other investment decision, including investments in the securities of foreign issuers, Adams' management and its Board of Directors have ultimate responsibility for evaluating the relative risks and benefits of any proposed transaction. Accordingly, any "non-bank" issuer would be subjected to the same degree of scrutiny regarding its creditworthiness and financial strength as a "bank" issuer which satisfied the technical
definition of a "bank" under Section 2(a)(5). There appears to be little justification for eliminating foreign banks from consideration as eligible candidates if the principal concern in selecting an issuing bank is its financial strength and creditworthiness. While there are certain risks attendant to any international transaction, use of standby letters of credit as reliable mechanisms of international finance has been generally endorsed. See, \textit{inter alia}, Getz, "Enjoining the International Standby Letter of Credit: The Iranian Letter of Credit Cases", \textit{Harvard International Law Journal}, Vol. 21, No. 1 (Winter, 1980); "The Role of Standby Letters of Credit in International Commerce: Reflections After Iran", \textit{Virginia Journal of International Law}, Vol. 20, No. 2 (1980).

If Adams were not limited to the technical definition of a "bank" under the 1940 Act, it would be expected that the nature and extent of the supervision and regulation of a foreign banking institution's activities by domestic authorities would be a significant factor taken into account by Adams' Board of Directors in evaluating potential issuers. Other relevant inquiries might include the scope of the bank's domestic business activities, its international banking reputation, and the nature and extent of the banking regulation to which it is subject under the laws of its home country.
Insofar as financial standards are concerned there can be little question that under present day standards, the financial qualifications of custodian banks required by Section 17(f) are not an adequate measure of financial strength for issuers of letters of credit in the face amount required to collateralize Adams' securities loans.

Because the factors relevant to an evaluation of the creditworthiness and financial strength of any particular banking institution, and the relative weight to be accorded such factors, are more appropriately determined in each individual case with regard to the size and nature of the loan transaction involved, we believe that in granting its prior approval to proposed issuers of letter of credit collateral, Adams' Board of Directors should exercise its business judgment without the limitations of prescribed definitions or financial standards, which may impose artificial and ineffectual constraints on the Board's judgment.

We would appreciate your advice as to whether you concur in our views set forth herein. Because Adams is currently considering entering into a loan arrangement collateralized by a letter of credit issued by the French bank referred to above, we would appreciate your prompt response to our inquiry. If any further informa-
Securities and Exchange Commission

June 18, 1981

If additional information is needed or if we can be helpful in any other way, please contact the undersigned or, in my absence, Mary Ellen Pindyck of this office, by collect telephone (212-541-5800).

Very truly yours,

[Signature]

Robert R. Hamas
Effective May 17, 1982, the Board of Governors of the Federal Reserve System ("Board") amended 12 CFR 220.6(h) to permit brokers and dealers to borrow and lend securities against, among other things, letters of credit issued by a bank insured by the Federal Deposit Insurance Corporation, or by a foreign bank that has filed a Form F.R. T-2 with the Board agreeing to comply with the same rules and regulations applicable to U.S. banks in securities credit transactions. Only foreign banks with branches or agencies that are supervised and examined by State or Federal banking authorities are eligible to file such a form. Based on this amendment and the representations in your letters of June 18, 1981, and February 12, 1982, we would not recommend that the Commission take any enforcement action under section 17(f) of the Investment Company Act of 1940 or rule 17f-2 thereunder if The Adams Express Company ("Adams") accepts, as collateral for the loan of Adams' portfolio securities, irrevocable letters of credit issued by an eligible foreign bank which has filed a form F.R. T-2 with the Board. However, this Division expresses no view on whether the letter of credit of such a bank could be provided to Adams as collateral by a broker or dealer. See Securities Exchange Act Rule 15c3-3(b)(3)(iii).

Stanley B. Rudd
Deputy Chief Counsel
February 12, 1982

Mrs. Elizabeth Tsai
Securities and Exchange Commission
Division of Investment Management
500 North Capitol Street
Washington, D.C. 20549

Re: Reference No. 81-425-CC

Dear Mrs. Tsai:

Reference is made to our recent telephone conversation regarding the status of the above-referenced request for advice, submitted on behalf of our client The Adams Express Company ("Adams"), concerning securities loans collateralized by a letter of credit issued by a foreign bank through its domestically licensed branch. You have requested that we provide you with supplemental information concerning the legal status of holders of letters of credit under applicable foreign law in the event of the bankruptcy of the foreign issuing bank, which may involve considerable additional legal research.

As you are aware, the Board of Governors of the Federal Reserve System has proposed an amendment to Regulation T which authorizes broker/dealers to collateralize securities loans with letters of credit issued by a "bank insured by the Federal Deposit Insurance Corporation." In its presently proposed form, this would not authorize collateralization with letters of credit issued by foreign banks. As I mentioned to you, we have been advised by the staff of the Board of Governors that it has received a
number of comments on the proposed amendment objecting to this limitation and urging that broker/dealers should be permitted to use letters of credit issued by foreign banks, directly or through a domestic branch. We were also informed that the staff has not yet determined whether to recommend deletion of the FDIC limitation.

As you are aware, if the amendment to Regulation T is adopted as presently proposed, this would eliminate Adams' interest in pursuing the broad authority for acceptance of foreign banks' letters of credit as collateral. Accordingly, we believe it inappropriate at this time to furnish supplemental information with respect to foreign banks' letters of credit.

We continue to believe that there is no practical or legal justification for prohibiting the use of letter of credit collateral issued by a foreign bank through its domestic branch if, in the judgment of Adams' Board of Directors, such bank has the financial strength and creditworthiness equivalent to a domestic bank which technically satisfies the definition of "bank" under Section 2(a)(5) of the Investment Company Act of 1940. Under the circumstances, however, we suggest that any response by the staff of the Securities and Exchange Commission to our above-referenced letter be deferred until definitive action has been taken by the Board of Governors of the Federal Reserve System on this matter.

Very truly yours,

Mary Ellen Pindyck

cc: Stanley B. Judd, Esq.