July 13, 2006

ATTN: Public Comments, Proposed Rule: Excess Stock Restrictions and Retained Earnings Requirements for FHLBanks
Federal Housing Finance Board
1625 Eye Street NW
Washington DC 20006

sent via email to comments@fhfb.gov

Dear Federal Housing Finance Board:

We appreciate the opportunity to comment on the proposed rules regarding changes to the capital structure of the FHLB system. In short, we believe that restricting the FHLB's ability to pay dividends seems somewhat arbitrary and could have long-term effects on the community banking system.

I represent a small community savings bank in Frankfort, Kentucky. In addition, I serve as President of Kentucky First Federal Bancorp under which is another small community savings institution in Hazard, Kentucky. I consider both banks to be heavy users of the FHLB of Cincinnati—we use transaction accounts and occasionally longer-termed deposit products, we are heavy users of advances, we often purchase and hold FHLB-issued securities, and we sell mortgages to the FHLB. Also, each bank owns a fairly large portion (relative to our size) of FHLB stock. We obviously have a vested interest in the FHLB's viability.

The short-term effects of the proposal would certainly have a detrimental effect on our return to our shareholders by both the reduction of the dividend rate and the payment of those dividends in cash rather than stock. Also detrimental is the possibility that excess stock, much of which has been accumulated in the form of stock dividends, would have to be redeemed and thus result in taxation. We understand that the FHLB is concerned that a reduction in the financial viability of FHLB may cause members to reduce their excess stock and to perhaps exit the system. Although we are extremely unlikely to renounce our FHLB membership, we have the same concerns and fear that a significant reduction in asset-size could compound the profitability issues by concentrating fixed costs on the remaining institutions and could imperil the FHLB's ability to attract personnel with the necessary high level of financial expertise needed. Further, accelerated redemption of FHLB stock either voluntarily or by function of the proposal, could result in a deterioration of the FHLB's financial position—causing their bonds to be downgraded and perhaps its stock to be impaired. Taken to the extreme, this could result in an industry-wide crisis in asset quality for community banks.

We are also concerned about the reduction in the ability of the FHLB to allocate to Affordable Housing Programs. We find their programs to be efficient and extremely helpful. Both of our institutions have partnered with the FHLB (and sometimes with other member banks) to facilitate low-income housing, which has greatly benefited our communities.

In closing, we do not believe that it has been demonstrated that the FHLB system as a whole or the FHLB of Cincinnati in particular is in any reasonable danger of insolvency. The FHLB system provides a variety of solutions that put our community banks in position to be competitive with larger financial institutions. An alteration or impairment of the FHLB of Cincinnati's ability to operate could result in significant damage to our banking system. We urge you to withdraw the proposal.

Sincerely,

Don Jennings
Executive Vice President, First Federal of Frankfort, KY
President, Kentucky First Federal Bancorp