

July 13, 2006

Federal Housing Finance Board
1625 Eye Street NW
Washington, DC 20006

Proposed Rule: Excess Stock Restrictions and Retained Earnings Requirements for
Federal Home Loan Banks

RIN Number 3069-AB30. Docket Number 2006-03

Ladies and Gentlemen:

MidFirst Bank is a federal savings association headquartered in Oklahoma City, Oklahoma, and is a member of the Federal Home Loan Bank (the "FHLB") of Topeka. MidFirst is pleased to offer the following comments in response to the Federal Housing Finance Board's (the "FHFB") proposed rule regarding retained earnings and excess stock as published in the *Federal Register* dated March 15, 2006, beginning on page 13306.

MidFirst believes the proposal contains the potential for unintended results that will likely impair the financial capacity of the FHLB System and therefore be detrimental to the member shareholders and the communities served by members. Minimum capital requirements and rules establishing effective safety and soundness parameters are important concepts the FHFB must promote, yet equally important is that such rules be balanced in approach without undue burden or unintended result. MidFirst encourages the FHFB to withdraw the proposal pending additional research on the topics proposed.

MidFirst shares many of the concerns outlined in comment letters from FHLB officials, other financial institutions, industry trade groups, and community groups that oppose the proposed rule. However, MidFirst focuses on the following:

1. The proposed one percent of assets limitation on excess stock is not appropriately outlined or justified. Without such justification, especially given the one case fits all approach, this concept should be eliminated. Certainly, the Finance Board recognizes that applying a once percent of asset limit for both 30-day Treasury Bills and 30-year fixed-rate mortgages is inconsistent and inappropriate. The proposal does not differentiate between risk characteristics of non-advance assets thereby encouraging a concentration of higher risk assets to improve the FHLB's return on equity.

2. Applying a fixed \$50 million retained earnings minimum for all FHLB's is inappropriate, given the variance in size of the institutions. For example, \$50 million of retained earnings equates to a capital ratio of well over 1 percent for the Des Moines FHLB while it equates to less than .25 percent for the San Francisco FHLB. This is extremely unfair to the smaller FHLB's and their shareholders that are required to fund the excess retained earnings percentage, especially when the fixed amount completely ignores the relative risk inherent in the FHLB's balance sheet.

3. Rather than establishing a minimum retained earnings requirement, regulatory efficiency and consistency would be achieved via a minimum total capital requirement approach. Granted the par value of stock has legal basis, but the cushion capital provides against loss and insolvency is the cushion regardless of the name assigned to the individual capital components. The important element is the level of total capital rather than the balances of individual capital components. Additionally, FHLB members are especially sensitive to conversion risk having experienced such Congressional action in 1987 and 1989 and given that 20 percent of FHLB's current retained earnings continue to pay REFCORP obligations. Finally, the minimum retained earnings requirement and resulting dividend restrictions will have a significant negative impact on many FHLB members as borrowing costs are increased which may cause larger members to leave the system in search of more favorable funding options. This in turn will diminish the FHLB's balance sheet and in turn shrink the income capacity of the FHLB's.

4. The proposed prohibition on stock dividends is not supported and will significantly impact the after-tax profitability of member institutions. If the Board sets a reasonable limit for excess stock, there is no additional benefit to elimination of stock dividends.

5. The proposal includes a restriction on excess stock that would limit the FHLB's flexibility and impair liquidity. Additional restrictions on a FHLB's ability to issue or to redeem stock could erode the confidence that member institutions have in FHLB Stock. Prior to the adoption of the Financial Institutions Reform Recovery and Enforcement Act of 1989, only financial institutions operating under the savings association charter could purchase FHLB stock. Since then, a savings association charter is not required for membership although savings association charters must be members. As a result, a majority of FHLB stockholders are now voluntary members, generally free to request stock redemption at any time, although it is widely understood that the FHLB's have the right to delay redemption of permanent stock for up to five years, if necessary. Of the approximate 900 members of the FHLB of Topeka, 43 are savings associations with headquarters in the four-state Topeka District.

6. A stated objective of the proposed rule is to minimize the "undue reliance on excess stock by a Bank to meet minimum capital requirements" [Federal Register page 13308]. The concern is that a significant volume of stock redemption requests by members would force the FHLB to liquidate assets thereby straining its financial capacity, ability to honor the stock requests, and impair future earnings capacity. However, the proposed rule may encourage optional shareholders to liquidate their investments thereby producing the exact effect the rule attempts to minimize.

7. Although drafted as a capital regulation, the purpose of the rule seems primarily designed to achieve investment and general safety and soundness objectives albeit in an indirect method. If the concern is indeed the volume and type of assets acquired, a risk weighted capital rule or a more direct restriction on non-advance assets would be more appropriate. If, as referenced on *Federal Register* page 13309, the FHFBS is concerned with FHLB's focusing on non-mission activities to produce arbitrage profits, the permissibility of non-mission activities should be the focus of a proposed rule. Agreed, higher risk activities warrant higher capital requirements, yet a more direct approach specifically addressing permissibility issues and FHLB investment powers would be more effective.

8. Should any concept of the proposed rule be adopted in a final form, an appropriate phase in period should be afforded to allow adequate time for both the FHLB's and the member institutions to adjust expectations and financial capacities to minimize the risk of unintended consequences and financial impairment.

In conclusion, MidFirst encourages the FHFB to reconsider the proposed rule as the dividend restrictions will thwart the FHFB's goal of actually reducing risk. MidFirst appreciates the opportunity to comment on the proposed rule. Should additional information be required, please advise.

Sincerely,

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Vice President and

Director of Regulatory Affairs

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