Maryland Bankers Association

KATHLEEN M. MURPHY
PRESIDENT & CEO

July 10, 2006

Federal Housing Finance Board
1625 Eye Street, N.W.
Washington, D.C. 20006
Attention: Public Comments

Re: Federal Housing Finance Board. Proposed Rule: Excess Stock Restrictions and Retained Earnings Requirements for the Federal Home Loan Banks. RIN Number 3069-AB30. Docket Number 2006-30

Dear Madam or Sir:

The Maryland Bankers Association ("MBA"), representing Maryland's financial services industry and more than 100 member-owners of the Federal Home Loan Bank of Atlanta, appreciates the opportunity to comment on the proposed rule by the Federal Housing Finance Board (the "Finance Board") relating to excess stock and retained earnings at the 12 Federal Home Loan banks ("FHLBs") (the "Proposal").[1] The Proposal would establish a minimum level of retained earnings for each FHLB, restrict dividend payments until a FHLB achieves the required minimum level of retained earnings, and impose new restrictions on excess stock. For the reasons set forth below, we believe the Proposal should be withdrawn and replaced with an advanced notice of proposed rulemaking ("ANPR"). This will enable more careful consideration of the important issues raised by the Finance Board in the Proposal.

As cooperative owners of the FHLB System, MBA members share the Finance Board's goal of insuring its ongoing viability, and support efforts to address legitimate safety and soundness concerns. Nevertheless, we believe the Proposal fails to adequately address any stated safety and soundness concerns, but will have significant unintended consequences. If adopted, the MBA believes the Proposal poses an even greater risk to the FHLBs, member-owners and their communities.

Rather than strengthening the FHLB system, the Proposal threatens to undermine the cooperative nature of the Federal Home Loan system along with each FHLB's critical role in

[1] 71 Fed. Reg. 13306 (March 15, 2006).

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helping its member financial institutions serve their customers and growing communities. MBA members' concerns with the Proposal include:

- A reduced availability of member advances;
- The financial impact on MBA members from reduced dividends and delayed payments;
- The particularly negative effects on community bank FHLB member-owners;
- The lack of a risk-based retained earnings formula; and
- An absence of a reasonable transition period for achieving the minimum level of retained earnings.

Reduced Availability of Member Advances: The MBA believes the Proposal will significantly reduce the availability of FHLB advances, a key source of cost-effective funding for FHLB member-owners in Maryland. As a result of the new restrictions, some FHLBs would be less able to meet the demand for member advances. Any reduction in funding availability from the FHLB Atlanta would negatively impact our member institutions, their customers and the communities they serve across Maryland. For many FHLB member-owners, there are few alternative sources of funding liquidity.

Financial Impact of Dividend Restrictions: The anticipated dramatic reduction in dividends will reduce an important source of income for MBA member-owners of the FHLB Atlanta. This will increase our members' total cost of obtaining member advances to support lending activities in their communities, which ultimately impacts consumers. The dividend restriction under the Proposal also is troubling because a FHLB investment often is one of the largest assets on a member-owner's balance sheet.

Separately, the Proposal would change the FHLB Atlanta's well-established dividend payment schedule, which will unnecessarily disrupt member-owners' financial planning. Currently, FHLB Atlanta member-owners receive dividend payments on the first day following completion of a calendar quarter. This dividend payment is based on actual net income results from the first two months of that calendar quarter and the last month of the previous quarter. The Proposal would require the FHLB Atlanta to alter its dividend payment schedule without any corresponding increase in safety and soundness.

Negative Impact on Community Banks: MBA members believe that community bank FHLB member-owners particularly would bear the brunt of increased costs and reduced capacity that flow from the Proposal as larger member-owners, with more funding options, could choose to redeem their stock and terminate their membership. Any significant level of stock redemption could result in some FHLBs shrinking, which would further erode their ability to meet demands for member advances and other important programs, such as the Affordable Housing Program.

Lack of Risk-Based Retained Earnings Formula: Under the Proposal, all FHLBs would be required to achieve and maintain a minimum level of retained earnings equal to $50 million plus one percent of all non-advance assets. The MBA believes this "one size fits all" retained earnings formula does not enhance the safety and soundness of the FHLBs because it fails to account for varying credit and market risks among different categories of assets. The FHLB Atlanta already has in place a strong, risk-based retained earnings policy that was developed in accordance with the Finance Board's existing guidance, and which accounts for different risk profiles among its assets. In the MBA's view, the Proposal would replace this careful, risk-based approach with a single formula that does not promote safety and soundness. In fact, the Proposal's formula would tend to penalize those FHLBs with less risky asset portfolios.

Absence of Reasonable Transition Period: The Proposal fails to include a transition period that would allow each FHLB to continue to set its own dividend policies without any restrictions, provided the FHLB was on target to meet its minimum retained earnings target. The MBA believes a reasonable transition period is essential for any changes to the capital structure of the FHLBs in order to minimize disruption to the member-owners.

Based on the foregoing, the MBA urges the Finance Board to withdraw the Proposal and replace it with an ANPR. Issuing an ANPR would ensure the Finance Board has the opportunity to receive critical input from all stakeholders as it considers capital changes to such a vital component of housing finance. We believe this is particularly important because of the critical stake our members have in the FHLB system. In addition, an ANPR also would allow the Finance Board to coordinate this rulemaking with its ongoing review of risk-based capital standards, which is essential given the significant effort and expense associated with the development and recent implementation of revised capital plans by the FHLBs.

Thank you for the opportunity to comment on this important matter. The MBA and its members look forward to working with the Finance Board to insure a safe and strong FHLB system.

Sincerely,

Kathleen M. Murphy
President & CEO