WISCONSIN BANKERS ASSOCIATION

July 11, 2006

VIA E-MAIL

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

RE: Proposed Rule on Excess Stock Restrictions and Retained Earnings Requirements for the Federal Home Loan Banks. RIN Number 3069-AB30. Docket Number 2006-03.

Dear Sirs and Madams:

The Wisconsin Bankers Association (WBA) is the largest financial institution trade association in Wisconsin, representing 310 state and nationally chartered banks, savings and loan associations, and savings banks located in communities throughout the state. WBA appreciates the opportunity to comment on the Federal Housing Finance Board's (FHFB) proposed rule regarding excess stock restrictions and retained earnings requirements for the Federal Home Loan Banks. WBA has several concerns with the proposed rule and in general, recommends that the proposed rule be withdrawn.

The proposed amendments would restrict the amount of excess stock that a Federal Home Loan Bank (Bank) could accumulate and keep outstanding, and would establish a required minimum level of retained earnings for each Bank. More specifically, the proposed rule would restrict the amount of dividends that a Bank could pay whenever the Bank is not in compliance with the minimum retained earnings requirements, and would prohibit the Banks from issuing dividends in the form of stock.

The "one-size fits all" approach set forth in the proposed rule is not appropriate to manage the capital issues raised by the FHFB and needlessly disadvantages certain Banks.

One fundamental flaw in the proposal is the across-the-board application of arbitrary formulas for retained earnings and excess stock. The FHFB's

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proposal is in total disregard for the Banks' capital and business plans that have been developed as required by the Gramm-Leach-Bliley Act. Each Bank should instead be allowed to present the FHFB with a retained earnings and excess stock plan based on the Bank's individual business plans. Furthermore, the Banks should be able to consider and adopt, if appropriate, alternative capital approaches, as opposed to only increasing retained earnings.

A majority of WBA members are also members of the Federal Home Loan Bank of Chicago and actively participate in the Mortgage Partnership Finance program offered by the Chicago Bank. This proposal needlessly places the Banks with mortgage purchase programs, like the Federal Home Loan Bank of Chicago, at a disadvantage. These mortgage purchase programs are mission-consistent and have fostered housing finance, at least in the Chicago district, by giving Bank members a competitive secondary market alternative. This proposal not only hurts the Banks' members, but will also ultimately reduce the funding available for such mortgage purchase programs, to the detriment of the families living in the communities served by these programs.

Moreover, there simply should not be an arbitrary ban on paying stock dividends. The restriction on the payment of stock dividends eliminates the tax-deferred benefit, which accrues to the membership. This is also contrary to the law which expressly authorizes the payment of stock dividends. Furthermore, elimination of stock dividends ignores the fact that cash dividends automatically reduce the capitalization of a Bank while stock dividends maintain capital levels. Capitalization is a key consideration by the independent ratings agencies when evaluating an organization's on-going credit rating. Each Bank should be permitted to pay dividends, in whatever form it chooses, unless a specific problem with this practice is identified at an individual Bank.

The proposed rule creates unintended consequences; therefore, it should be wholly withdrawn and replaced with an advance notice of proposed rulemaking.

In addition to WBA's concerns with the proposed rule described above, WBA is also concerned with the proposed rule's generic formula for calculating each Bank's minimum retained earnings requirements and the unintended consequences resulting from this. The proposal unnecessarily creates a higher retained earnings charge for having a Bank hold liquid assets, such as Treasury bills, agency securities, and cash. This is contrary to safety and soundness principles and the industry's need for immediate access to liquidity.

In addition, holding more retained earnings than needed from a risk perspective deleverages a Bank, reduces shareholder returns, and ironically may cause member withdrawal. The FHFB should instead adopt a risk-based approach tying the level of retained earnings to the risk on the balance sheet. This is more in line with the other federal banking regulators and the Basel capital studies.

The FHFB staff has acknowledged publicly that it is working on a new risk based capital model, consistent with the Basel II Accord for large financial institutions, and intends to have it ready in the next nine months. <u>Given this, the FHFB should withdraw the proposed rule and issue an advance notice of proposed rulemaking that solicits a broader range of comments on various approaches to Bank capital issues</u>.

If the FHFB does not withdraw the proposed rule, WBA again suggests at a minimum that the retained earnings minimum formula be adjusted to account for assets that do not present risk so that the Banks are not compelled to build retained earnings against cash and Treasuries held for liquidity purposes. In addition, the proposed rule's immediate effective date should be replaced with an appropriate transition period. In the Gramm-Leach-Bliley Act, Congress provided appropriate transition periods and a five-year redemption period for the Banks' Class B stock. A similar time frame for transition purposes would be appropriate here as well.

In conclusion, WBA believes that the best course of action is to withdraw the proposed rule and instead issue an advance notice of proposed rulemaking to foster better dialogue about the capital issues raised by the FHFB. WBA appreciates the opportunity to provide comments on the proposed rule and strongly urges the FHFB to give its concerns serious consideration. Thank you.

Sincerely,

Kurt R. Bauer
President/CEO