Cincinnati Federal
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June 27, 2006

Federal Housing Finance Board
1625 Eye St. NW
Washington, DC 20006

Attention: Public Comments
FHFB Proposed Rule: Excess Stock Restrictions and Retained Earnings Requirement for FHLBs; RIN # 3069-AB30; Docket # 2006-03

Cincinnati Federal Saving and Loan Association is a member of the Federal Home Loan Bank of Cincinnati (FHLB-Cincinnati). We rely on the FHLB-Cincinnati for services, particularly the advance window, as the Cincinnati Bank is a primary source of liquidity for our Association. As an FHLB-Cincinnati stockholder, we also rely on a competitive rate of return on our Class B stock. We are extremely concerned that the proposed rule (noted above), is at best unnecessary, and potentially damaging to the FHLB-Cincinnati. For these reasons, we respectfully urge the Federal Housing Finance Board (FHFB) to withdraw the proposed rule.

The four main requirements of the proposed rule can be summarized as follows. It will: 1) limit the amount of stock the Federal Home Loan Banks (FHLBs) may carry, in spite of the fact that it is considered permanent capital under federal law; 2) prescribe a minimum amount of retained earnings, and doing so in a way that discriminates against and discourages advance borrowings and the successful mortgage purchase programs of the Cincinnati Bank; 3) limit the payment of dividends; and 4) preclude the payment of stock dividends, even though Federal law delegates that decision to the local banks. These requirements will be applied in a rigid, one-size-fits-all format, irrespective of the important differences among the various Home Loan Banks. When all four requirements are read together, it seems apparent that the FHFB has a goal of shrinking all the FHLBs and programs, including the FHLB-Cincinnati.

The proposed rule will <u>negatively impact and likely eliminate and/or greatly diminish housing programs.</u> Our Association supports the strong commitment to affordable housing that the FHLBs have demonstrated. The FHLB-Cincinnati has helped nearly 35,000 household within the Cincinnati district. The proposed rule will reduce FHLBs' profits and restrict the housing program funding for our communities.

For FHLB-Cincinnati, the new rules are <u>not necessary and may be harmful to its investment rating</u>. The FHLB-Cincinnati is a conservative, well-managed financial institution maintaining the highest Moody's and Standard and Poor's rating. The Bank is well-capitalized and is successfully operating under the capital plan approved in 2002. The rules that are proposed in the name of safety and soundness are unnecessary for the

FHLB-Cincinnati and may in fact lower the Bank's rating for several reasons. One, because excess capital must be redeemed under your proposal, the FHLB-Cincinnati will have less total capital. It is not relevant to the markets or rating agencies that the FHLB's capital account may have a higher percentage of retained earnings. Secondly, less capital will result in reduced services for our Association. For example, because the rule requires additional capital for non-advance assets, the FHLB may have to terminate or reduce mortgage purchase programs. Additionally, the Cincinnati Bank may not have the liquidity or flexibility to be able to continue offering same day advances. Thus, if services are reduced and dividends are slashed and made taxable as a result of the proposed rule, many shareholders will likely redeem their additional stock, again lowering overall capital. While this cannot be characterized as a run on the Bank's capital account, it is ironic that preventing accelerated redemptions in times of stress is one of the reasons justifying the proposed rule. Yet, an accelerated redemption is called for by redeeming excess stock within 60 days of enactment of this proposed regulation.

This rule will also <u>reduce liquidity</u>. Contrary to the Basel capital debate for banks and thrifts, the FHLBs will be required to hold the same capital to support cash and readily-marketable securities as for other mission-related assets. Given the scarcity of capital, it will simply be too expensive to maintain more than the absolute minimum amount of liquidity.

The proposed rule will cause our Association and other FHLB members to <u>pay additional taxes</u>. The current payment of stock dividends not only permits the FHLB-Cincinnati to retain capital to support housing and advance programs, but also permits FHLB shareholders to defer any taxation, as compared to regular dividends, which are immediately taxable. Also, if adopted in its current form, the proposed rule will require the FHLB-Cincinnati to redeem excess capital for cash within 60 days. This forced redemption will trigger our Association and other members to realize taxable gains with adverse tax consequences for all of us. Additionally, since credit union members do not pay taxes on the gains, this proposed rule will put us at a competitive disadvantage again.

For all these reasons, as a shareholder of FHLB-Cincinnati, we respectfully request that you withdraw the proposed rule.

Sincerely,

Joseph V Bunke

Joseph V. Bunke
President, Cincinnati Federal Savings & Loan