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To whom it may concern,

As most of you are aware, the Federal Housing Board (FHFB) issued a proposed regulation on excess capital stock and retained earning on March 15, 2006. The proposed rule, if put into effect as is, would:

1. Limit the amount of excess capital stock an FHLBank may have outstanding to 1 percent of its total assets;
2. Prohibit the payment of stock dividends;
3. Establish a requirement to hold retained earning equal to $50 million plus 1 percent of non-advance assets (this is referred to as the retained earnigs minimum, or REM); and
4. Restrict dividends to 50 percent of quarterly income when an FHLBank is not in compliance with its REM.

This proposed rule has generated more heated discussion and consternation than any other FHFB action in recent memory. On May 2, 2006 the chairs and vice-chairs of all 12 FHFBanks sent a letter to the FHFB asking that the rule be withdrawn. The FHFB is accepting comments on the proposed regulation through July 13, 2006.

We urge each of you to review the proposed rule. It is available on the FHFB's site at www.fhfb.gov . At minimum, we believe it would be appropriate for you as a member of the FHFBank to make the following comments:

1. <u>Stock dividends should not be prohibited</u>. Stock dividends provide a tax benefit to members that should not be eliminated. Given the adoption of an apporpriate limit on the amount of excess stock, there is no basis to prohibit stock dividends. If an FHLBank controls the amount of excess stock outstanding, no regulatory objective is achieved by banning stock dividends.
2. <u>The limit on excess stock should be higher than 1 percent of assets</u>. While the preamble to the greater proposed egulation provided no explanation on how the 1 percent limit was determined, 1 percent

is too low. A higher limit would provide greater flexibility for the FHLBank to hold liquid assets and thereby maintain higher liquidity, increasing its ability to operate in a safe and sound manner and better serve its members'fluctuating advance needs.

3. <u>There should be a reasonable phase-in period the REM</u>. The proposed rule would limit dividends to 50 percent of net income immediately if the REM is not met when the regulation is effective. The 50 percent limitation is to sereve and restrictive and could significantly hurt a member's income. It is also unreasonable and unfair to impose a dividend restriction the day the rule becomes effective, There should be at least a three-year implementation period where dividend restrictions are not imposed if the FHLBank is making reasonable progress in meeting its REM.
4. <u>The REM applicable to money market assests should be reduced</u>. There is no justification for imposing the same retained earnings requirement on money market assets as is required for 30-year, fixed-rate mortgages. For example, it would not unduly complicate the rule to make the REM equal to $50 million plus ½ percent of money market assets and 1 percent of non-advance, non-money market assets.
5. <u>Once fully implemented, there should be some flexibility before divdend restrictions are imposed</u>. The proposed rule would impose the 50 percent limitation immediately when an FHLBank failed to meet its REM. This will effectively require an FHLBank to hold substanially more than its REM in order to prevent a violation through normal balance sheet volatility. For example, it would be preferable to impose divdend restrictions only in event that an FHLBank falls below 90 percent of its REM in a quater or fails to meet its REM for three consecutive quaters. Given that the current REM calculation is very conservative (relatively high level of retained earnings being required), the flexibility allowed before dividened restrictions are imposed would achieve the FHFB's objective while not being as operationally difficult for the FHLBank.
6. <u>Clarify that divdends paid and income earned in a quater are independent.</u> The proposed rule imposes limits on divdends based on a percentage of income in a quater. Standard corporate practice does not tie divdends to income earned in a period (except over the long term) and divdends are generally stable even though income is not. FHLBank members prefer a stable dividend policy, especially when income can be materially impacted in a single quater by gains and losses related to SFAS 133. While the imposition of dividend restrictions requires that dividends be related to income earned in a quater, any final rule should make clear that dividends need not be related to earnings in a certain time period if the FHLBank is in compliance with its REM The FHLBank need only have sufficient retained earning to meet its REM after payment of the dividend.

Regards,

Curt Coffman
President