

October 27, 2011

Jennifer J. Johnson, Secretary      via email: [regs.comments@federalreserve.gov](mailto:regs.comments@federalreserve.gov)  
Board of Governors of the Federal Reserve System  
20<sup>th</sup> Street and Constitution Avenue, N.W.  
Washington, DC 20551

**Re: Comment on Interim Final Rule for Regulations LL and MM  
regarding Savings and Loan Holding Companies –  
Docket No. R-1429 RIN No. 7100 AD-80**

Dear Ms. Johnson:

These comments on the above-referenced Interim Final Rule are provided on behalf of Third Federal Savings and Loan Association of Cleveland, MHC (“Third Federal MHC”), a federally-chartered mutual holding company, TFS Financial Corporation (the “Company”), a federally-chartered mid-tier stock holding company and Third Federal Savings and Loan Association of Cleveland (“Third Federal Savings”), a federally chartered savings and loan association. Third Federal Savings began operations in 1938, was reorganized into a mutual holding company structure in 1997 and the Company completed a minority public offering of common stock in 2007. The Company is an approximately \$11 billion organization with over 16% capital, located in Cleveland, Ohio, and its minority stock (approximately 26% of the total outstanding) is traded on the NASDAQ market under the symbol TFSL.

Third Federal Savings is one of the leading mortgage lenders in Ohio and is committed to remaining an independent community bank dedicated to serving the banking and borrowing needs of its customers. We resisted the industry trend of converting to stock form in the 1980s and 1990s largely because the standard conversion model, which required a converting institution to sell 100% of its value in one transaction, had produced mixed results. Specifically, many converting savings institutions were simply not prepared for the immediate transition from mutual to full stock ownership and the challenge of prudently reinvesting the significant amount of capital raised. In our case, our bankers advised us that we would have had to sell as much as \$3.3 billion of common stock if we had pursued a standard full stock conversion. We would have been under significant pressure to reinvest the capital in a relatively short period of time to produce reasonable returns for our stockholders, or sell our bank. Instead, our board of directors elected to go public incrementally by selling 30% of the Company’s stock in a minority stock offering in 2007 that raised approximately \$1.0 billion. The board of directors and management of the Company believe that the minority stock offering was clearly the right choice for Third Federal Savings particularly in view of the collapse in the economy and mortgage markets that occurred subsequent to our offering. The former Office of Thrift Supervision (“OTS”) supported this mutual holding company (“MHC”) structure through its rules.

Provisions of proposed Section 239.8 of the Interim Final Rule exceed the parameters contemplated by Section 625 of the Dodd-Frank Act and place an undue burden on “Grandfathered MHCs” (OTS-chartered MHCs that were formed, sold stock and waived dividends prior to December 1, 2009). Section 625 of the Dodd-Frank Act, which was intended

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to preserve the existing rights of MHCs that had previously waived the receipt of dividends pursuant to OTS regulations and to continue to allow these MHCs to waive dividends without dilution of minority stockholders in the event of a second-step conversion to stock form. Grandfathered MHCs, like Third Federal MHC, have followed OTS dividend waiver rules from inception of their public offerings. The OTS rules allowed the boards of directors of MHCs to make dividend waiver decisions while considering, as required for all company matters, their fiduciary duties to the mutual members. These waivers were also subject to review by the OTS. Moreover, the Company's prospectus used to sell stock in its 2007 minority stock offering specifically stated that Third Federal MHC intended to waive the receipt of dividends subject to OTS approval. Proposed Section 239.8 questions the ability of MHC directors to make those fiduciary decisions and implies that they are incapable of making decisions that are in the best interest of an MHC and its members due to a perceived conflict of interest. Section 239.8 would require the board of Grandfathered MHCs to incur the unnecessary cost of soliciting proxies from mutual members to obtain the approval of a majority of the total eligible votes of members to approve dividend waivers. Moreover, it suggests that those MHC directors who happen to be stockholders of the subsidiary also should waive their individual right to receive a dividend. This is punitive and singles out MHC boards as being uniquely unqualified to address potential conflicts of interest in determining whether to waive the receipt of dividends. The member vote requirement is also contrary to the specific standards of Section 625 of the Dodd-Frank Act which provides that the Federal Reserve Board may not object to a dividend waiver if certain listed conditions (none of which include a member vote) are met. A member vote is a substantive change and contrary to the express language of the Dodd-Frank Act.

Our legal counsel, Luse Gorman Pomerenk & Schick, through a separate comment letter, has provided a comprehensive legal analysis of the logic of following existing rules and allowing all MHCs (including non-Grandfathered MHCs) to waive the receipt of dividends without dilution of minority stockholders in the event of a second-step conversion to stock form. We don't intend to repeat those legal arguments here, but certainly we agree with and support their logic. Our major concern with the Interim Final Rule revolves around the presumption of an "inherent conflict of interest" on the part of the MHC board of directors who are also stockholders of the dividend paying subsidiary. The fiduciary duties of the MHC board of directors align with the mutual members. The mutual members benefit from a strong, stable financial institution. The initial reason for establishing the MHC structure was to provide a vehicle that would allow savings associations to raise capital and grow responsibly. As noted above, in many instances, the conversion of a mutual to a full public stock organization can result in a surplus of capital that may lead to unsafe investment and growth decisions. By allowing a "partial conversion" using the MHC structure, the smaller capital raise allows measured growth which does not put the insured institution at risk. Having the ability to raise additional capital, either through another incremental stock offering or in a full conversion, provides a recapitalizing mutual organization with much needed flexibility, particularly in troubling economic times such as now. However, a minority stock offering will raise more capital and be attractive to investors only when minority stockholders have the ability to achieve a return on their investment. Since minority stockholders do not have a controlling vote and there is limited potential for capital appreciation from a sale of control of an MHC, a dividend

provides for a tangible return for the real capital and risk they have invested. Most, if not all (as was the case with the Company's offering in 2007), of initial stockholders who invest in an MHC minority stock offering are depositors of the thrift. A dividend paying stock also attracts more investors and enhances the interest in, and market valuation of, future capital raises. (We note that if an MHC cannot waive dividends, the value of the subsidiary bank or mid-tier holding company's stock would be less compared to the value of stock sold in a standard conversion to stock form.) A strong, flexible organization aligns perfectly with the long term interests of mutual members. The ability of MHC directors, through a dividend waiver, to allow capital to remain in the organization and provide a reasonable return to minority stockholders enhances future capital raising flexibility and fully supports the long term interests of the mutual members. Without the ability to waive dividends, two options exist: (i) either dividends will be paid from the mid-tier public company to the MHC and become subject to various levels of taxation and lost value; or (ii) no dividends will be paid to any stockholders, which reduces the demand for minority shares and the current and future valuations of the mid-tier holding company stock. Both options reduce the ability of a mid-tier holding company to be a source of strength to the insured institution.

When looking at the perceived conflict of interest, the actual overall economic impact in each case needs to be considered. The directors of Third Federal MHC beneficially own less than 1.5% of the Company's publicly traded shares. The decision of Third Federal MHC to waive its receipt of dividends surely is not designed to benefit its directors. However, the ability to pay a dividend without dilution does benefit the other 98.5% of our public stockholders, including more than 10,000 stockholders who were depositors and mutual members who bought stock in our initial public offering, the Third Federal Foundation, which provides a tremendous service to the community, and the Third Federal Employee Stock Ownership Plan, which benefits Third Federal Savings and approximately 1,000 of our employees by making them co-owners of our organization. To imply that MHC directors who are also stockholders are not acting prudently and unable to make fiduciary-guided decisions is a discredit to those directors. MHCs are not unique in this regard from other fully stock companies, as public company directors are frequently required to make decisions that involve actual or perceived conflicts of interest. Going to the other extreme and requiring that MHC directors not own any shares of their mid-tier company or bank subsidiary is contrary to the belief that directors should have a shared interest in the company they serve. In addition, we note that it is often preferable to have the same individuals serve on the board of each entity in the MHC structure, as they have the greatest understanding of the operations of the overall organization and multiple different boards may be confusing and disruptive to the efficient operation of a banking organization.

The Interim Final Rule requires directors of Grandfathered MHCs to document how they have addressed the conflict of interest. We don't feel there is a conflict that cannot be addressed by having directors exercise their normal fiduciary responsibilities. But suggesting that directors who have demonstrated their support for an organization, such as Third Federal Savings, by investing personal resources in its capital stock, must waive their right to receive dividends paid to all stockholders is punitive, contrary to the interests of an MHC and its members, and contrary to best corporate practices.

The proposed language will require a yearly vote of the MHC members in order to qualify for a dividend waiver. We understand that the Federal Reserve Board would not allow "running proxies" to be used to obtain member approval, so approval of a majority of members eligible to vote would be needed each year. This poses a huge burden on the MHC and again, questions the ability of the MHC directors to make business decisions that benefit the organization as a whole. Requiring an annual positive vote of the majority of those members eligible to vote establishes an ongoing requirement normally reserved for a major organizational decision. Third-party proxy solicitors would be necessary to obtain the vote, causing the MHC to incur unnecessary annual expenses, which is in no one's best interest. We are not aware of any mutual member being adversely affected by the numerous MHC dividend waivers that have occurred over the years. The members do not have an ownership interest or stake that is akin to that of stockholders, and consequently simply don't care about this issue. The conflict of interest issue identified in the Interim Final Rule is difficult to identify and to understand even for those directly involved in regulating or evaluating MHC dividend waivers, and members of an MHC would be hard pressed to understand why they are being asked to vote on a dividend waiver, much less how a waiver would affect them.

While the common stock issued by a mid-tier stock holding company to its MHC parent is of the same class as the common stock sold to the public, it should be noted that it has substantially different characteristics and arguably should be considered a separate class of stock. Common stock held by an MHC is not transferable and is not traded on an exchange. Moreover, unlike the common stock held by minority stockholders, neither the Third Federal MHC nor the members invested risk capital in the Company's common stock. Members do not have the right to force a liquidation of the MHC or the insured institution, or to receive any distribution of the assets of the MHC other than in the event of a liquidation of the MHC. We do not believe there has ever been a voluntary liquidation of an MHC and distribution of its surplus to members. Members also do not have the right to receive any dividends paid by the Company to the MHC. Members also have no right to receive any distribution on the MHC's common stock interest in the Company in the event of a conversion of the MHC to a full stock form. Instead, members simply have the first right to purchase such stock at fair value like other members of the public. Members are primarily depositors who receive their required return in the form of interest on their deposit. Members are first and foremost depositors and customers who are interested in a strong financial organization. The dividend waiver enhances the ability of MHCs to attract stockholders willing to invest capital in the organization which maintains that strength and flexibility. If members truly had an issue with the dividend waiver, they would have voiced their concerns many years ago. Third Federal MHC holds an annual members' meeting and has never received any complaints from members about its dividend waivers.

The ability to pay dividends to our minority stockholders was a key factor in the Company's ability to raise approximately \$1 billion of new capital in our 2007 initial public offering, which contributed to the overall strength of the entire Third Federal organization. The prospectus clearly disclosed that the Company anticipated that Third Federal MHC intended to waive any dividends the Company paid. The Company believes that paying dividends to

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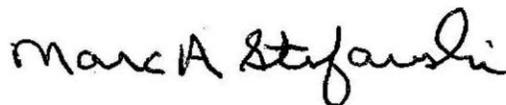
minority stockholders, with Third Federal MHC waiving dividends, will help build long term stockholder loyalty and value by providing minority stockholders with a reasonable dividend and overall return on their investment. This is particularly important for community banks with a local stockholder base and generally in the current weak economic environment where stockholders have suffered significant losses on financial institution stocks. These stockholders are seeking dividend paying stocks to improve their overall return on investment. Additionally, a stronger stock price may serve to increase Third Federal's presence in its retail markets because of its local stockholder base. We have continued the practice of Third Federal MHC waiving its rights to dividends for all dividends paid by the Company since our 2007 initial public offering. That practice is also a big part of attracting future capital to our organization. As a Grandfathered MHC, the ability to waive dividends was certainly recognized and preserved in the Dodd-Frank Act. We believe this intent and practice is being challenged, not because of any financial issues or safety and soundness concerns, but simply because of a change in regulators. The Interim Final Rule is inherently unfair to our stockholders and members who have trusted their investments with us.

Mutual community banks and thrifts have a long history of providing service to their communities and most have the goal to grow and prosper and continue as independent organizations. The MHC structure and the ability of these organizations to waive dividends have been key to fostering this responsible growth. Adopting a rule that has a negative effect on the ability of mutuals and MHCs to raise capital makes no sense and is counter-intuitive, particularly in the current economic environment.

We respectfully request that the Federal Reserve eliminate any member vote requirement for Grandfathered MHCs under the Interim Final Rule since there is nothing in Section 625 of the Dodd-Frank Act that gives the Federal Reserve the authority to require such an affirmative vote. Requiring a majority of those eligible to vote seems onerous and unnecessary. Rather, the statute requires that a board of directors analyze whether a dividend waiver would be consistent with its fiduciary duties to the mutual members. Such analysis also does not require board members who are also stockholders to waive their individual right to receive dividends.

Thank you for allowing me the opportunity to comment on the Interim Final Rule as it will have, if left unchanged, a significant adverse impact on the entire Third Federal organization. Please contact me at (216) 429-5400 or Paul Huml, our Chief Operating Officer at (216) 429-5325, if you have any questions or need any clarification of these issues.

Sincerely,



Marc A. Stefanski  
Chairman of the Board, President and Chief  
Executive Officer

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cc: Paul J. Huml, Chief Operating Officer  
Eric Luse, Esq. (202) 274-2002  
Ned Quint, Esq. (202) 274-2007