Testimony of

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Good Morning Chairman Shelby, Ranking Member Sarbanes, and Members of the Committee. I am J. Edward Norris, III, Chairman, President, and CEO of Plantation Federal Bank. I appreciate the opportunity to speak to you today about the Federal Home Loan Bank (FHLBank) System, something that is very important to my bank and to my community.

Plantation Federal is a “community-grown" financial institution in Pawleys Island, South Carolina, with over $300 million in assets. As with many community banks, we realize that we are in partnership with our customers, and our success depends on helping them become successful. While Plantation Federal offers a full line of financial services, our primary line of business is originating mortgages for families.

Plantation Federal Bank is a member of FHLBank Atlanta. I have been very active in FHLBank matters, primarily because of the importance of FHLBank Atlanta to my bank and my community. I served as a Director of FHLBank Atlanta for eight years, from January 1996 until the end of my term in December of 2003. During the last two years of my directorship, I served as the board’s vice-chair and then as chairman. I also served on the Board of the Council of FHLBanks from 2000 to 2003. I am a member of America’s Community Bankers and currently chair its GSE Policy Committee. Today, however, I am here representing Plantation Federal Bank.

At the outset, I would like to commend Chairman Shelby and Ranking Member Sarbanes for your commitment and hard work in ensuring that the GSEs do have a true world- class regulator with the necessary regulatory tools to ensure that the GSEs fulfill their missions in a safe and sound fashion. I also commend you for holding this hearing today focusing on the FHLBank System, the value of which is often minimized or unrecognized.

Over seventy years ago, when the FHLBank System was created to stabilize and increase the availability of funds to support homeownership, Congress created an exceptional System that has been able, with modest legislative changes, to adjust to the changing business climates of its member/owners and to continue to fulfill its mission.

The regionally-based cooperative structure of the System enables each individual FHLBank to address specific and often different geographic needs of its member institutions and the very different communities that we serve. The System's joint and several liability enables the twelve (12) FHLBanks to access the capital markets on a combined basis, permitting them to deliver wholesale funding to their members at capital market rates.

I characterized the System as exceptional, and I would like to briefly explain why before I get into the substance of my testimony. The twelve FHLBanks are each different in varying ways, but they also share great commonality. Each FHLBank's membership is made up of commercial banks, thrifts, credit unions and some insurance companies. Each has members of varying sizes, from the smallest community banks to the largest money-center banks. It is this dynamic that makes the System work so well. The FHLBanks, as a result, are able to go to the capital markets for large- scale funding, which allow even the smallest community bank to access capital at rates well below anything else available. Affordable Housing Program funding, which is based on a percentage of each district bank's income, is improved with the larger membership base, and this, in turn, allows smaller institutions a greater opportunity for funding and affordable housing projects.

As a community banker, I know first-hand how FHLBank Atlanta helps Plantation Federal Bank deliver financial services to the communities that we serve in an environment of ever-growing competition. Plantation Federal uses almost all of FHLBank Atlanta's products and as I go through my testimony I will expand on this aspect.

FHLBank Modernization

The Gramm-Leach-Bliley Act of 1999 brought about the most significant changes to the FHLBank System since the passage of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA"). Thanks in large part to the work of Senators Hagel, Johnson, and Bayh, the Gramm-Leach-Bliley Act established universal voluntary membership for the FHLBank System; provided for a permanent capital structure; expanded the types of collateral that community institutions can pledge to secure advances, and increased the independent corporate governance of each FHLBank.

Although that legislation was enacted over five years ago, some of the changes are today still being adjusted to and implemented by the FHLBanks and their member banks. Nearly all the FHLBanks have converted to their new capital structures, and all are expected to complete their conversions by the end of 2006. The Act's expanded provisions of eligible collateral that community financial institutions can pledge as security for FHLBank advances are being implemented, depending on the demand and appropriate development of sound underwriting standards by each FHLBank.

I believe that it was clear with the passage of Gramm-Leach-Bliley that Congress affirmed and broadened the mission of the FHLBanks to promote affordable housing, community development and the delivery of financial services through their members, the owners of the System.

One of the most important changes in that Act was the shift of governance from the regulator to the individual boards of the FHLBanks. That change permitted the FHLBanks to better manage their business plans and meet their members' specific needs. Nine years ago when I joined the board of FHLBank Atlanta, the Atlanta Bank had just over $30 billion in assets. Today, the Atlanta Bank has assets of over $130 billion and almost $160 billion in off-balance sheet derivatives. The directors of the FHLBanks are facing greater and greater responsibility.

With the Finance Board's mandate that all FHLBanks register with the SEC, that shift in governance takes on even greater meaning. As a former director and chairman of the board, I can tell you that the FHLBank Atlanta board is a true managing board of directors. It is more important now than ever before that FHLBank Atlanta, and each of the other eleven FHLBanks, have the ability to ensure that it has the necessary experience and expertise on its board of directors to fulfill its corporate governance responsibilities. The FHLBank Atlanta board has eighteen (18) directors; at the beginning of 2005, Atlanta had three vacancies and only three of its directors have served for three years or longer. A proper balance of experience, knowledge and fresh ideas is necessary to most effectively run these important businesses. The newer individuals who are currently serving on that board are fine directors who will need to rapidly learn the operations and complexities of the FHLBank. I caution that the management of the FHLBanks is having to spend excessive man-hours because of this constant need to educate new board members on the intricacies of the operations of the Banks.

Attracting and retaining qualified directors is a growing challenge today; that challenge will not lessen as the banks become SEC and Sarbanes-Oxley compliant. It was an honor for me to serve on FHLBank Atlanta's board, but in today's environment with the statutory cap on compensation and possible restrictions on a FHLBank's ability to indemnify its employees or directors, fewer qualified individuals may be willing to serve.

The FHLBank as a Funding Source

The FHLBanks were originally created in 1932 to help expand home-ownership by providing liquidity to their member financial institutions for the extension of longer-term mortgage credit. It does not take long for a banker today, if he or she spends any time in their community, to realize that providing homeownership opportunities entails far more than simply making mortgage loans. As a community banker, I know that in addition to available home loans, home ownership opportunities also require affordable, traditional financial services like savings and checking accounts, good jobs and competitive business opportunities, and quality community-based schools and health systems. Community banks are often in the best position in their own communities to help provide all of these opportunities. The FHLBanks help community banks make it possible to improve their local municipalities.

FHLBank advances, or loans to their members, provide financial institutions with various funding options to meet the housing and community development credit needs of their communities. The FHLBank Atlanta, whose district covers the southeast from Maryland down to Florida including Alabama, has approximately $97 billion in outstanding advances to its members. For many FHLBank members that are small or medium-sized community banks, direct borrowing in the capital markets is not a viable option. By providing a source of wholesale funding to help members manage liquidity, loan demand, and interest rate risk, the FHLBanks enable financial institutions, such as mine, to remain independent and continue to serve the needs of our local communities. To me, FHLBank Atlanta is the most important partner that my bank has in allowing me to be a viable, independent bank. And believe me, it is a partnership! Plantation Federal fully utilizes the advance programs offered by the Bank and has $60.5 million of advances outstanding, which comprises 21.5% percent of our liabilities. Without access to FHLBank advances, Plantation Federal could not effectively compete in our market area, nor could we offer the mortgage products that enabled us to originate more than $380 million in mortgage loans over the past three years.

In effect, the FHLBank is my Wall Street, but with a big difference. As a cooperative, the FHLBank System does not have to meet public stock holder demands for expansion and return on equity. It can work with its members to ensure that they understand the products that are available to them; it can tailor its programs and products to its members' demand. Because the FHLB System is a cooperative, its members own it. Plantation Federal's largest single asset on its balance sheet is its stock in FHLBank Atlanta….we own over $ 3.3 million in the stock of our FHLBank. As an owner of the Bank, I am indeed concerned with its safe and sound operation. I cannot afford to lose my bank's access to the FHLBank.

Allow me to emphasize the value of FHLBank advances, both from the daily availability of liquidity and the actual provision of short- and long-term funding at capital market rates. In the case of Plantation Federal, and I believe research would show in the case of FHLBank System members generally, we are able to hold a higher share of our assets in housing and community development loans compared to non-members simply because of this access to liquidity.

Another indication of the importance of the FHLBank System to the liquidity and funding of community banks can be found in a recent study[1] by America's Community Bankers which indicated that advances comprised 21 percent of the liabilities for member banks that are active in the System. Also, in a recent Survey of Community Bank Executives[2] conducted by Grant-Thornton, fifty-six percent (56%) of respondents reported that they used FHLBank advances as a source of funding in 2004, and sixty-three percent (63%) expect to use them in 2005. These numbers confirm the importance of the FHLBank System to a broad base of community banks and reaffirm the evolution of the FHLBank System over the past 15 years.

The advance programs are, and should continue to be, the core business for the FHLBanks. However, when the advance programs of the FHLBanks are combined with the relatively new mortgage-purchase programs, the original mission of the System is compounded. The mortgage-purchase programs provide

[1] *Washington e-Perspective*, America's Community Bankers, March 9, 2005
[2] *Twelfth Annual Survey of Community Bank Executives*, Grant Thornton, March 2005

me with another funding alternative from my FHLBank that helps me extend residential mortgage credit to my community.

Federal Home Loan Bank Mortgage Purchase Programs

The Federal Housing Finance Board (Finance Board) approved the first mortgage- purchase program, known as the acquired member asset program (AMA), as a pilot program in 1997. At that time, the chairman of the Federal Housing Finance Board described the program in a Senate hearing[3] as "a new way for the FHLBank System to serve its fundamental mission of increasing the credit that goes to creditworthy people to purchase homes and to creditworthy projects that revitalize communities." He went on to say these programs provided "innovation in the ways that the FHLBanks and their members are partnering -- using the unique cooperative structure of the System -- to meet housing finance needs." The mortgage purchase programs provide FHLBank members, particularly smaller community banks, with an alternative to holding loans in portfolio by providing them with an alternative to the traditional secondary market.

The two programs that operate under the AMA program are the Mortgage Purchase Finance ® Program (MPF) and the Mortgage Purchase Program (MPP). FHLBank Atlanta offers both programs to its members. Under the programs, the member financial institution and the FHLBank share risk. Each program may be designed a little differently, but there is a risk-sharing component in each. By adding additional competition and efficiency in the secondary mortgage market and giving lenders additional choices, these programs help drive down the costs of mortgage finance, while enhancing homeownership opportunities.

[3] Testimony of Bruce Morrison, Chairman of the Federal Housing Finance Board before the Senate Banking, Housing and Urban Affairs Committee, Subcommittee on Financial Services and Technology, September 24, 1997

The mortgage purchase programs have proven to be very popular among the members of the System, with over 1000 participating financial institutions, the majority of which have assets of less than $550 million. Plantation Federal participates in both programs, as well as delivering loans to both Fannie Mae and Freddie Mac. We have sold over $40 million in loans into the MPF program and nearly $500,000 into the MPP program, with commitments for about $12 million more into the MPP program. Like advances these programs help us compete in our market and help us generate the necessary capital to continue to extend important mortgage credit in our communities.

FHLBank Atlanta has developed its mortgage purchase programs carefully and deliberately ensuring that a sound infrastructure was in place before building a large portfolio of purchased loans. FHLBank Atlanta has nearly $2.4 billion of these assets on their balance sheets. The interest rate risk of these loans is managed according to conservative internal and regulatory risk limits. As the volume of mortgage loan assets grows, substantial time, effort and resources must be expended to further enhance and build their risk management capabilities.

The programs have provided a second profitable line of business for the FHLBanks, in addition to the traditional core business of advances. Profits generated by the mortgage programs, just like profits generated by the advances and other FHLBank business, are paid out in four ways. A portion may be required to maintain retained earnings; twenty percent goes to the payment of the RefCorp obligation; $100 million or ten percent, which ever is greater, goes toward the affordable housing program; and the remainder is paid out in the form of dividends to the member/owners of the FHLBank System.

There has been much talk about the future of the programs. It is important to remember that these programs are relatively young. With any new businesses, adjustments over time must be expected for maximum success and achievement. As a banker, I know the value of the mortgage purchase programs to my bank and thus to my community; as a former FHLBank board member, I know that these programs can be an important part of the FHLBank's business mix. However, I also recognize that as the programs grow in popularity and the assets build on the balance sheet of the FHLBanks that there must be an effective way to manage that risk. At Plantation Federal, if our balance sheet grows too heavy in one area, we can "lay off" that risk by selling the assets. We can also sell the whole loans or securitize the assets and then sell the securities. As constructed, the FHLBanks do not have that ability with the mortgage purchase programs. I believe it is not prudent to book illiquid assets on a bank's balance sheet; therefore, the FHLBanks should also have the ability to manage their mortgage loan capacity.

I strongly believe that this is where the paths of the regulator and the FHLBanks must supportively meet. Just as the regulator must insure the safe and sound operations of these programs, so must the regulator enable the ongoing operation and functionality of the programs. I would urge you to support such action by the regulator.

FHLBank Affordable Housing Programs

Another vital role that the FHLBanks play is in affordable housing and community development. FIRREA created the Affordable Housing Program (AHP) and directed the Banks to develop community investment programs. These programs are designed to provide funding through members in support of community and economic development activities.

Through an ongoing commitment to affordable housing and community development, and in partnership with its member financial institutions, FHLBank Atlanta is improving the future for individuals and families in its district and beyond. As part of its public mission, FHLBank Atlanta provides grants, loans, and low-cost financing with its affordable housing and community economic development programs. Each year the Bank provides at least ten percent (10%) of its net income[4] to fund the AHP programs and additional funds for community economic development.

The AHP program competitive awards are granted twice a year to member financial institutions and their community based partners. Since 1990, FHLBank Atlanta has awarded more than $240 million in grants for construction and rehabilitation of nearly 49,500 affordable housing units. During that same period, all twelve FHLBanks combined to provide more than $2 billion in grants for affordable housing for a total of about 430,000 affordable housing units.

FHLBank Atlanta added the First-time Homebuyers Program to the AHP program in 1997 and provides up to $5000 per household for down-payment and closing cost assistance to low- and moderate income homebuyers. More than 4300 families have purchased their homes with the help of this program.

FHLBank Atlanta has been enormously helpful in our efforts at Plantation Federal to address the affordable housing and community development needs of our communities. Through our FHLBank partnership, we can get assistance directly through the programs or through technical assistance. Plantation Federal has been able to offer low-cost housing assistance in our community because of the FHLB Atlanta's AHP programs and we are taking part this month in a Housing Fair to educate our community on the availability of low-to-moderate income housing grants and subsidies. Two examples of AHP projects FHLBank Atlanta has partnered with FHLBank members on in South Carolina follow. Hickory Hollow in Sumter, South Carolina is a newly constructed multi-family rental development consisting of 64 apartments that received a $500,000 grant through FHLBank Atlanta's AHP. In this project targeting very low- and low-income families, residents will benefit from an extensive social services program. The complex is 100% leased and the grand opening is scheduled for tomorrow. Saluda Crossing in Saluda, South Carolina which provided a $250,000 grant to help

[4] FIRREA requires the FHLBank System provide $100 million or ten percent (whichever is greater) of its net income annually toward the Affordable Housing Program

construct twenty-five single-family detached homes that will be rented to very low-income families. This project is very unique because low-income housing tax credits were used to build the homes. At the end of the tax credit compliance period (fifteen years), the families will have the opportunity to own the homes with the tax credits as equity.

Earlier I talked about the importance of the regionally-based cooperative structure of the FHLBank System, one of those benefits is evidenced in the community development programs of the FHLBanks. While all the FHLBanks offer community development programs, each individual FHLBank has the flexibility to develop the programs that best suit their regional housing and community development finance needs.

FHLBank Atlanta offers a number of programs. The Community Investment Program (CIP) provides attractively priced funds, in the form of discounted advances, to member financial institutions, which are used to fund single-family mortgage-loans or commercial loans for multi-family housing for low- and moderate-income families. The Economic Development and Growth Enhancement Program (EDGE) provides below market-rate loans for community economic development projects that directly benefit low-income neighborhoods or families. These projects include services and facilities that every hometown needs, like health, child-care, recreational, commercial, industrial or commercial development projects and neighborhood redevelopment. Since this program began, more than 78 neighborhoods have benefited by receiving subsidy grants of more than $22 million. The Economic Development Program (EDP) offers longer-term funding that supports community economic development at interest rates from 5 – 22 basis points lower than regular advance rates. These funds are often used to fund multiple smaller loans or to match-fund larger loans.

FHLBank Atlanta also operates a predevelopment fund, a new markets fund, and offers technical assistance and training to community partners on a wide range of topics including grant applications, financial analysis and infrastructure development. FHLB Atlanta also partners with Historically Black Colleges and Universities in the Southeast.

I think it is important to reemphasize again the point that the funds that are directed to affordable housing through AHP are not insignificant. Even though it is mandated by statute, the FHLBanks invest at least ten percent (10%) of their net income to these low-income housing programs. However, the other economic development programs that I reference that FHLBank Atlanta offers...and similar ones offered by the other FHLBanks...are subsidized funds provided voluntarily by the boards of the twelve district FHLBanks. I think this is an important story of the exceptional nature of the public-private partnership that has resulted because of the cooperative structure of the FHLBank System.

Future Challenges Facing the System

Perhaps the greatest challenge facing the FHLBank System today is the challenge facing this committee and the Congress today. Ensuring that the FHLBank System engages in a safe and sound operation without increasing systemic risks is imperative; however, the FHLBanks must have the flexibility to provide advance funding and other program services its member/owners who need and want to deliver credit and financial services to their communities.

The FHLBanks are as relevant today as they were when Congress created them in 1932. They can best support and build upon their successful record with a strong, independent regulator, an engaged corporate governance structure, and an effective risk management program. Under the current regulatory regime, the FHLBanks' regulator, the Federal Housing Finance Board, is an independent agency that is not limited by funding constraints in fulfilling its regulatory responsibilities. Its funding is provided by direct assessments to the FHLBanks. Maintenance of this basic approach is essential in any new regulatory structure to assure continued safety and soundness, as well as the ability to oversee their mission.

Looking to the future, the FHLBanks have at least two primary challenges facing them: (1) meeting their corporate governance responsibilities and (2) having the flexibility to address their members' changing mission-related funding and liquidity needs.

As I suggested earlier in my testimony, since the passage of the Gramm-Leach-Bliley Act and even more so since the passage of the Sarbanes-Oxley Act, a Board of Directors' corporate governance responsibilities are far greater today then they were even a year ago. With greater responsibility comes greater liability and the need for more expertise and experience. I believe it is important to have a combination of industry and outside directors on the boards of the FHLBanks. The outside, or public interest directors, bring independence, different experiences and often expertise that is vital to the good management of the FHLBanks.

I mentioned the FHLBank Atlanta board's vacancies and relatively modest experience level. I would urge two things: First, if possible, these vacancies should be quickly filled with individuals that have the necessary knowledge and experience to effectively govern on that board. Secondly, whether through the regulatory process or through legislation, a new method should be developed that will give the FHLBanks and their boards of directors a greater role in the process of choosing qualified candidates for outside directorships. The method should insure that the right expertise is brought to the boards and that unnecessary breaks in director service do not occur. I also believe the ability to attract and retain qualified FHLBank board members would be greatly enhanced by adopting legislative changes to remove the statutory caps on director compensation and to extend director terms from three years to four years.

The FHLBanks must retain the ability to be flexible in addressing their members changing mission-related funding and liquidity needs. All of the programs that have been developed by the FHLBanks, from the business funding programs like advances and the mortgage purchase programs to the affordable housing and community development programs, have been created or changed to meet member demands. That is the nature and beauty of a cooperative and that is what has made the FHLBank System work for community bankers and the communities their banks serve.

In developing a new regulatory structure, the real challenge is not only in creating strong regulation to ensure safety and soundness, but in doing it in a manner that does not diminish the creativity and vitality of the FHLBanks. Any new regulator of the System must have the authority to maintain the FHLBanks' access to the capital markets under the current well-defined mission to support the mortgage finance, affordable housing, and community development activities of member banks. The regulator must also be flexible and equipped to address the differences in the businesses and operations among the FHLBanks.

Conclusion

Over the years, the FHLBank System has repeatedly demonstrated its ability as a cooperative to evolve, to meet the changing needs of its membership, and to provide valuable services to its members and their local communities. I cannot stress strongly enough the importance of maintaining the cooperative nature of the FHLBank System under a new structure of regulation and supervision. It is essential in preserving the economic benefits that member institutions provide to communities and families.

As a taxpayer, I want the FHLBank System to operate safely and soundly; as an owner and stockholder in the FHLBank, I want my investment to be safe; and as a member-user of the System, I want to continue to have access to the products and services of the FHLBank to help me deliver the competitive financial services my community needs.

Mr. Chairman, thank you for the opportunity to address the Committee on this important matter. I will be happy to answer questions at the appropriate time.