

# Central Bank Oversight: Assessing the Fed's Accountability to Congress

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*Note: This presentation solely reflects the views of the authors and should not be interpreted as reflecting the views of any other person or institution.*

# The Context

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## Monetary Economics

- Longstanding consensus that monetary policymaking should be **insulated from political interference**.
- Recognition that central bank independence is only sustainable in a context of **transparency and public accountability**.

## Constitutional Law

- The U.S. Constitution specifically tasks Congress with the power to **regulate the value of money**.
- Congress can **delegate** this power but **cannot abdicate responsibility** for overseeing how it is carried out; i.e., the central bank cannot be a “fourth branch.”

# Milton Friedman's Perspective

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“The argument implicit in the defense of an independent central bank is...to let the central bank have authority largely coordinate with that of the legislature, the executive, and the judiciary....But is it really tolerable in a democracy to have so much power concentrated in a body free from any kind of direct, effective political control? ...How else can we establish a monetary system that is stable [and] free from irresponsible governmental tinkering? ...The enactment of rules would enable the public to exercise control over monetary policy...while at the same time preventing monetary policy from being subject to the day-to-day whim of political authorities.”

*“Should There Be An Independent Monetary Authority?” (1962)*

# Fed Chair Bernanke's Perspective

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*Q: What advice would you offer to the incoming Fed Chair, Janet Yellen, about dealing with Congress?*

**A: Well, I think the first thing to agree to is that Congress is our boss.** The Federal Reserve is an independent agency within the government. It's important that we maintain our policy independence in order to be able to make decisions without short-term political interference. At the same time, it's up to the Congress to set our structure, to set our mandate, and that's entirely legitimate, and we need to go and explain ourselves. We need to explain why certain approaches are not so good or might be better."

*FOMC Press Conference, December 2013*

# The Structure of Our Assessment

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- **Part I: Delegation of Article I Powers to the Fed**
  - **Regulating the Value of Money**
  - **Borrowing Funds from the Public**
- **Part II: Sources of Congressional Oversight**
  - **Information Constraints**
  - **Opacity of the Fed's Balance Sheet**
  - **Exemptions from Routine Forms of Oversight**
- **Part III: Approaches for Enhancing Oversight**
  - **Reports to Congress**
  - **Access to Internal Fed Information**
  - **Strengthening Congressional Watchdogs**

# Synopsis of Our Assessment

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- In recent years, the magnified scope and complexity of monetary policy has outpaced Congress' ability to oversee the Fed's exercise of these duties.
- Existing mechanisms of congressional oversight have become ineffectual and anachronistic.
- To restore effective oversight of the Fed's monetary policymaking, legislators may wish to consider adapting approaches used for overseeing other independent agencies.

# Constraints on Congressional Access to Information

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- **Opacity of Monetary Policy Reports to Congress**
  - No explanation of deviations from the Taylor Rule or other simple policy benchmarks
  - No scenario analysis or risk assessments
  - No cost-benefit analysis of FOMC programs
- **Secrecy of Internal Fed Information**  
*(not even disclosed to leaders of the Fed's oversight committees)*
- **Uniformity of FOMC Decisions**
  - magnification of Fed Chair's role
  - disappearance of dissenting votes

# The FOMC's Governance in Theory

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- In 1887 Congress established a set of principles for the governance of independent agencies:  
*“An uneven number of commissioners...appointed to staggered terms of a fixed period extending beyond the term of the President...can only be removed by the President for inefficiency, neglect of duty, or malfeasance in office...no more than a bare majority can come from the same political party.”*
- The FOMC was designed to ensure **individual accountability & insulation from political interference**:
  - Federal Reserve Board members with 14-year terms, only removable by the President “for cause”.
  - Fed Bank presidents appointed by boards of directors with approval by the Federal Reserve Board, and only removable by the Fed Board “for cause”.



# The Fed's Governance in Practice

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- **The Fed Chair**

- Four-Year Term (renewable)
- Active Executive Officer
- Oversees all Fed Board staff
- Sets agenda for FOMC meetings

- **Other Fed Board Members**

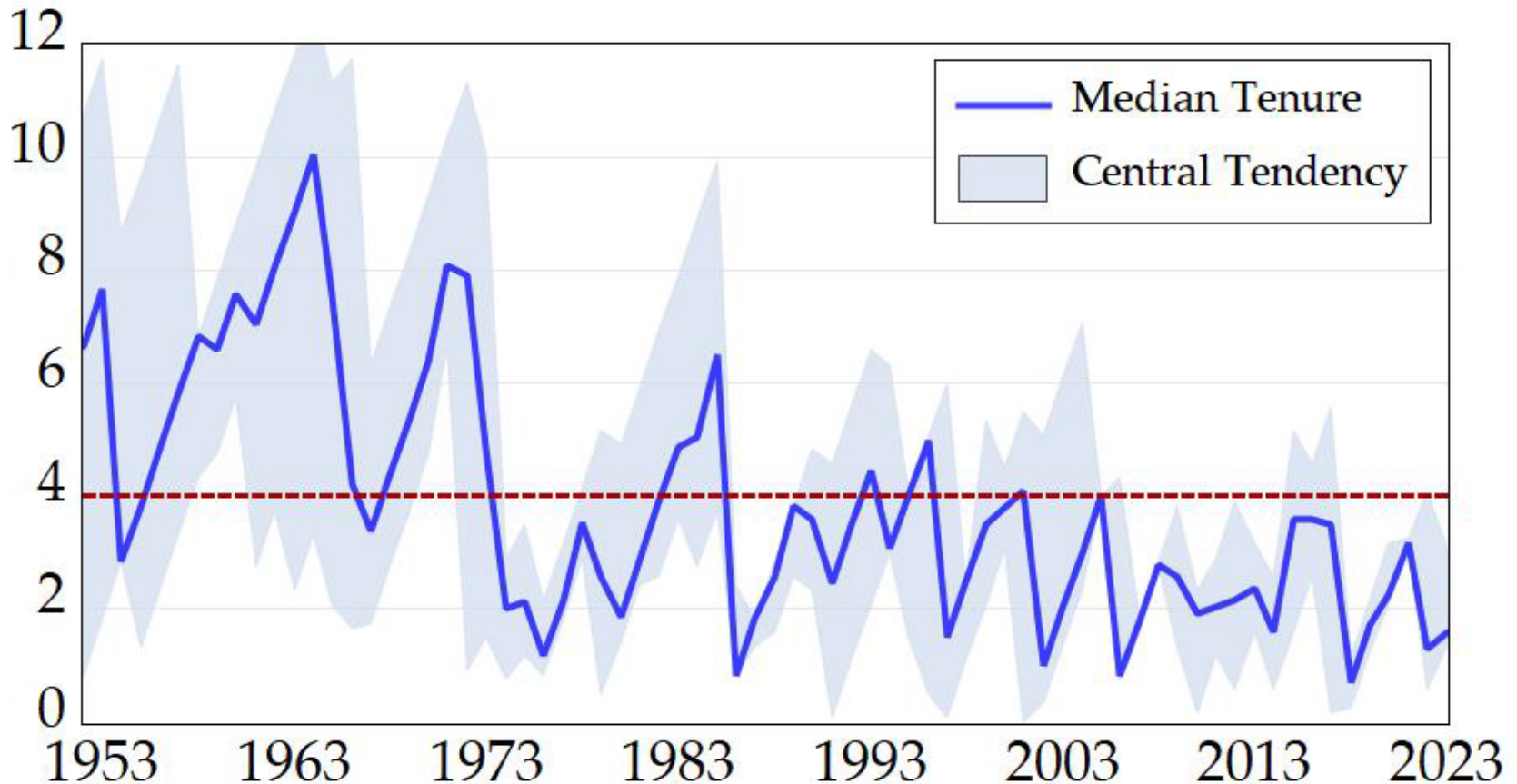
- Rarely stay for more than 3-4 years
- No dissents from FOMC decisions since 2006

- **Fed Bank Presidents**

- Now viewed as **“subordinates”** of Fed Board
- No dissents in 2021, no dissents since spring 2022

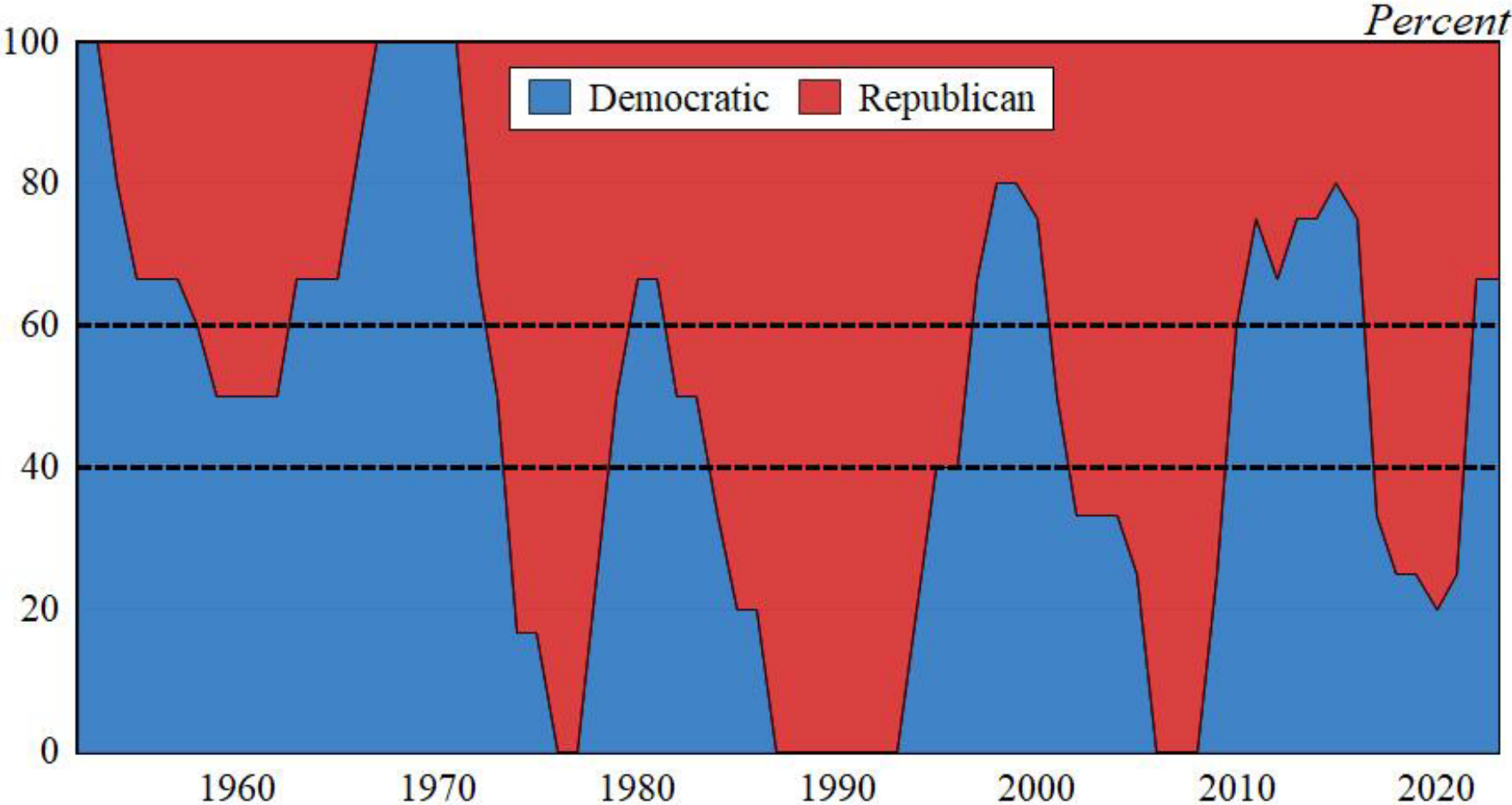
# Tenure of Fed Board Members *(excluding Fed Chair)*

Years of Tenure



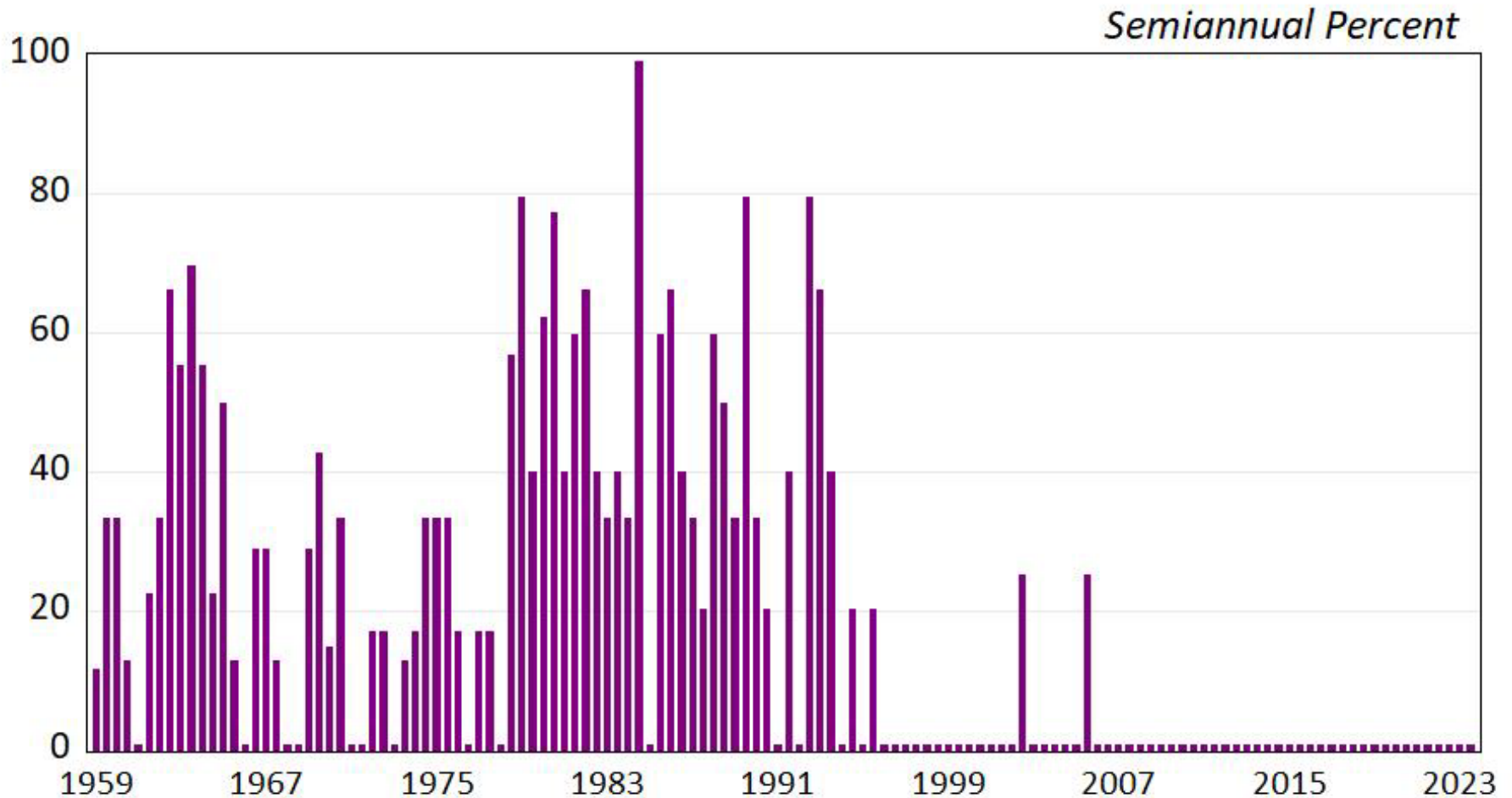
*Source: Federal Reserve Board, authors' calculations*

# Political Affiliation of Fed Board Members *(excluding Fed Chair)*



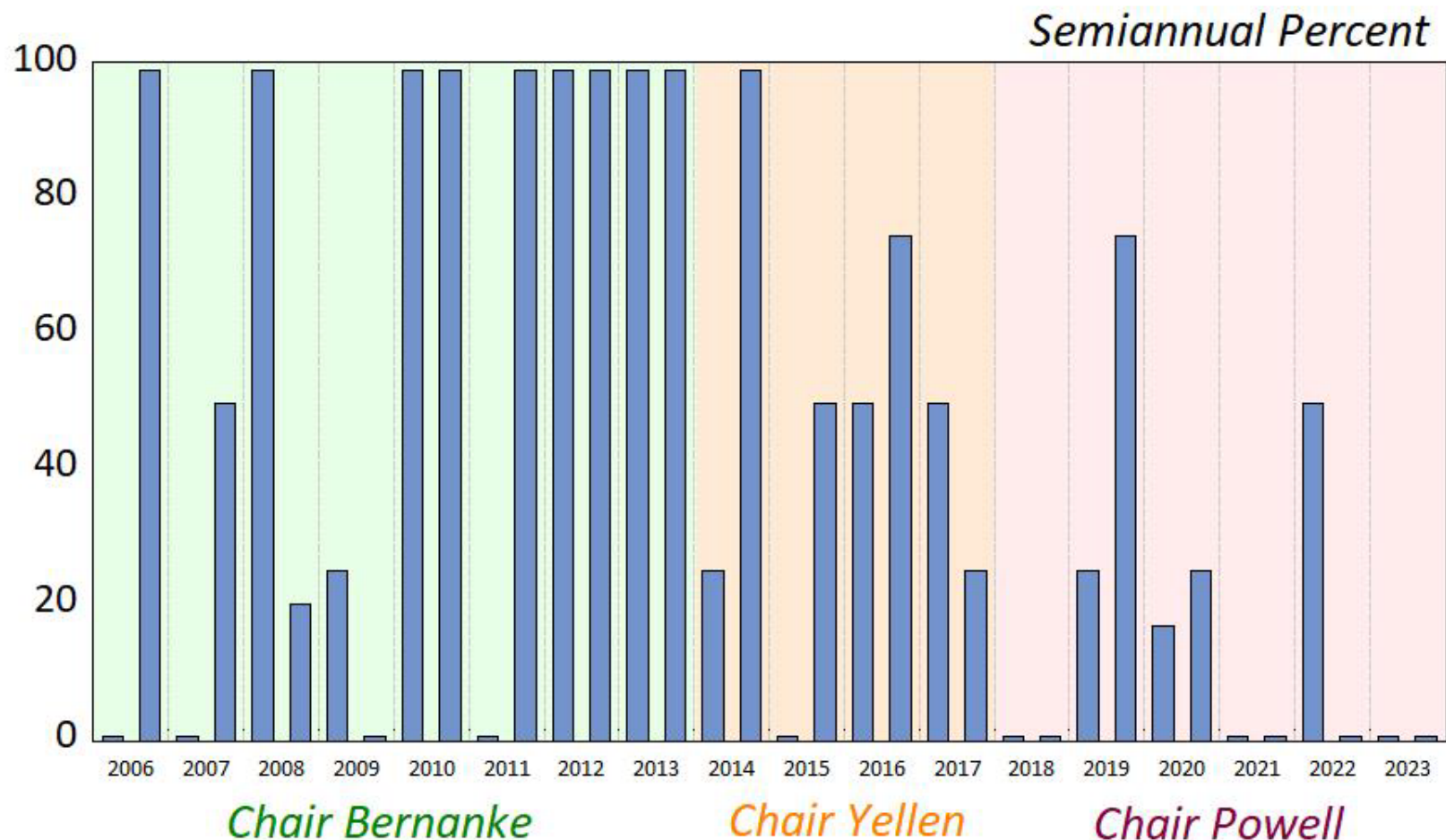
*Source: Authors' calculations.*

# FOMC Dissents of Fed Board Members



*Source: Federal Reserve Bank of St. Louis, authors' calculations*

# FOMC Dissents of Fed Bank Presidents



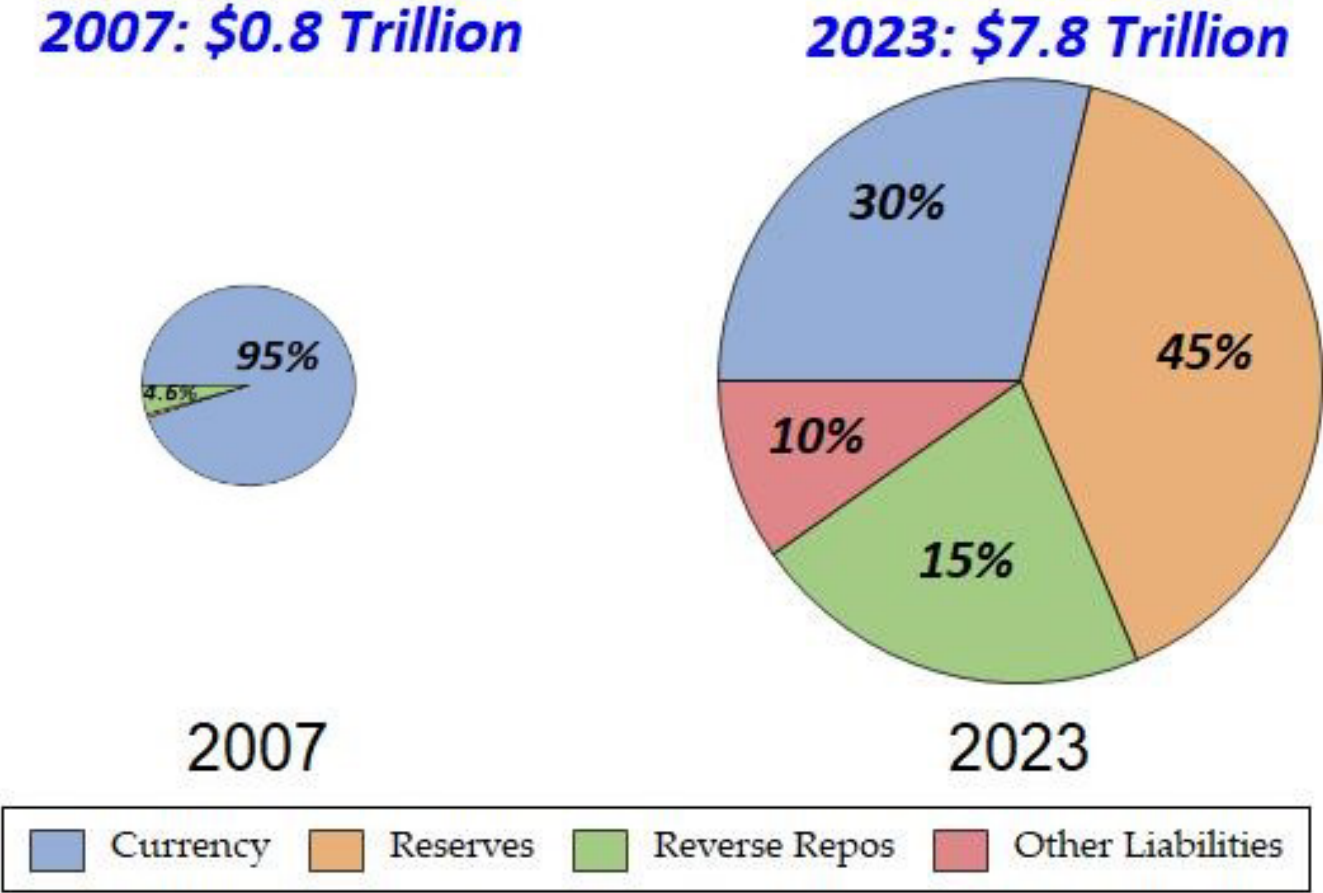
*Source: Federal Reserve Bank of St. Louis, authors' calculations*

# Exemptions from Routine Oversight

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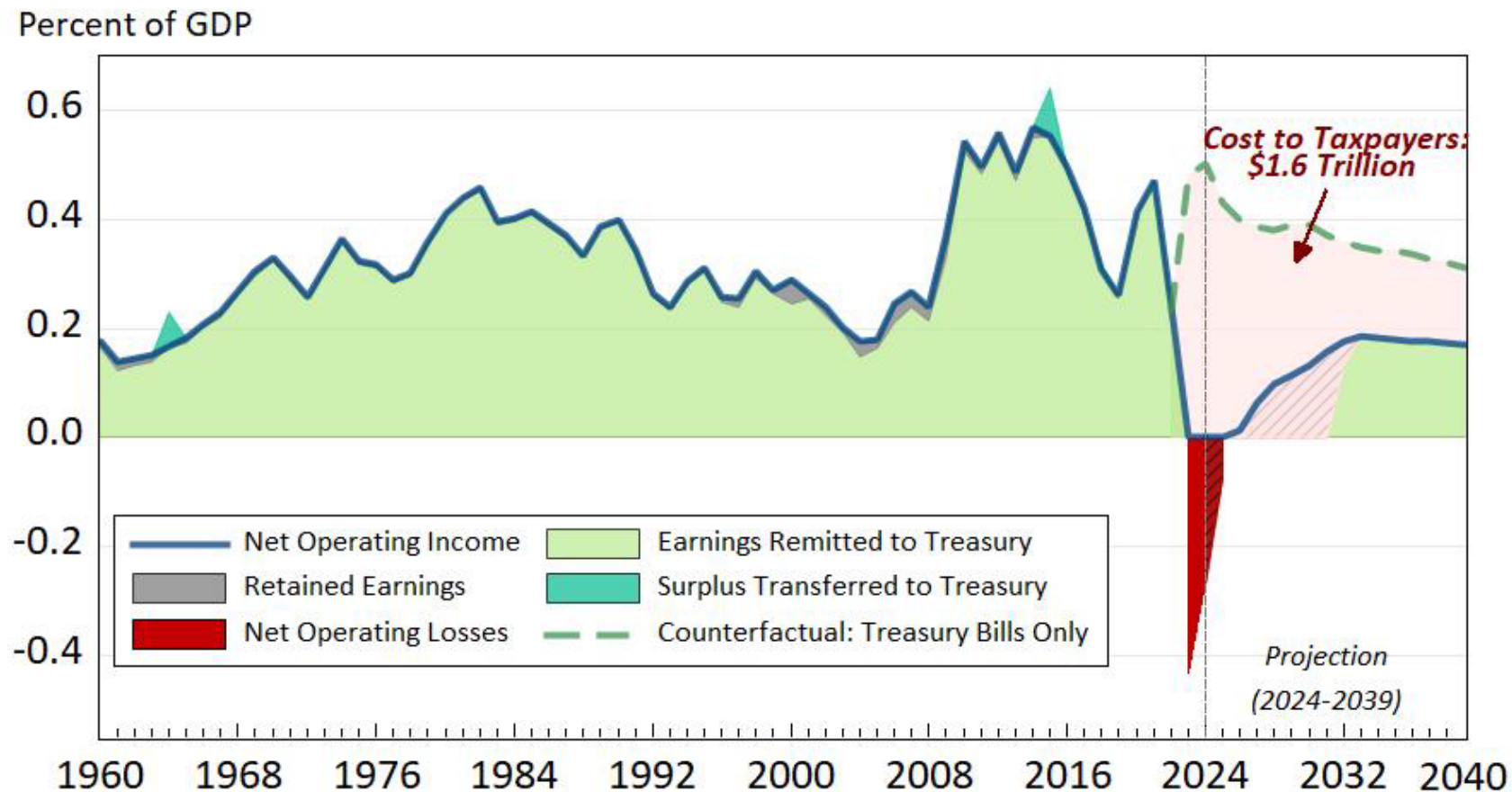
- The Fed is the only independent agency whose operating budget is not included in the annual **appropriations process** (unlike CFTC, FDIC, FHFA, OCC, and SEC).
- The Fed issues interest-bearing liabilities to the public that are not subject to the **federal debt ceiling**.
- The Fed sets its own **accounting rules**, whereas all other federal agencies follow standards set by FASAB.
- The Fed's monetary policymaking is exempt from **performance reviews by GAO**, which reviews all other independent agencies (such as CFTC, FDIC, OCC, SEC).
- The Fed's **inspector general** is a Fed employee, whereas every other major agency has a fully independent IG.

# The Evolution of the Fed's Liabilities



Source: Federal Reserve Board (H.4.1), authors' calculations

# Evolution of the Fed's Remittances

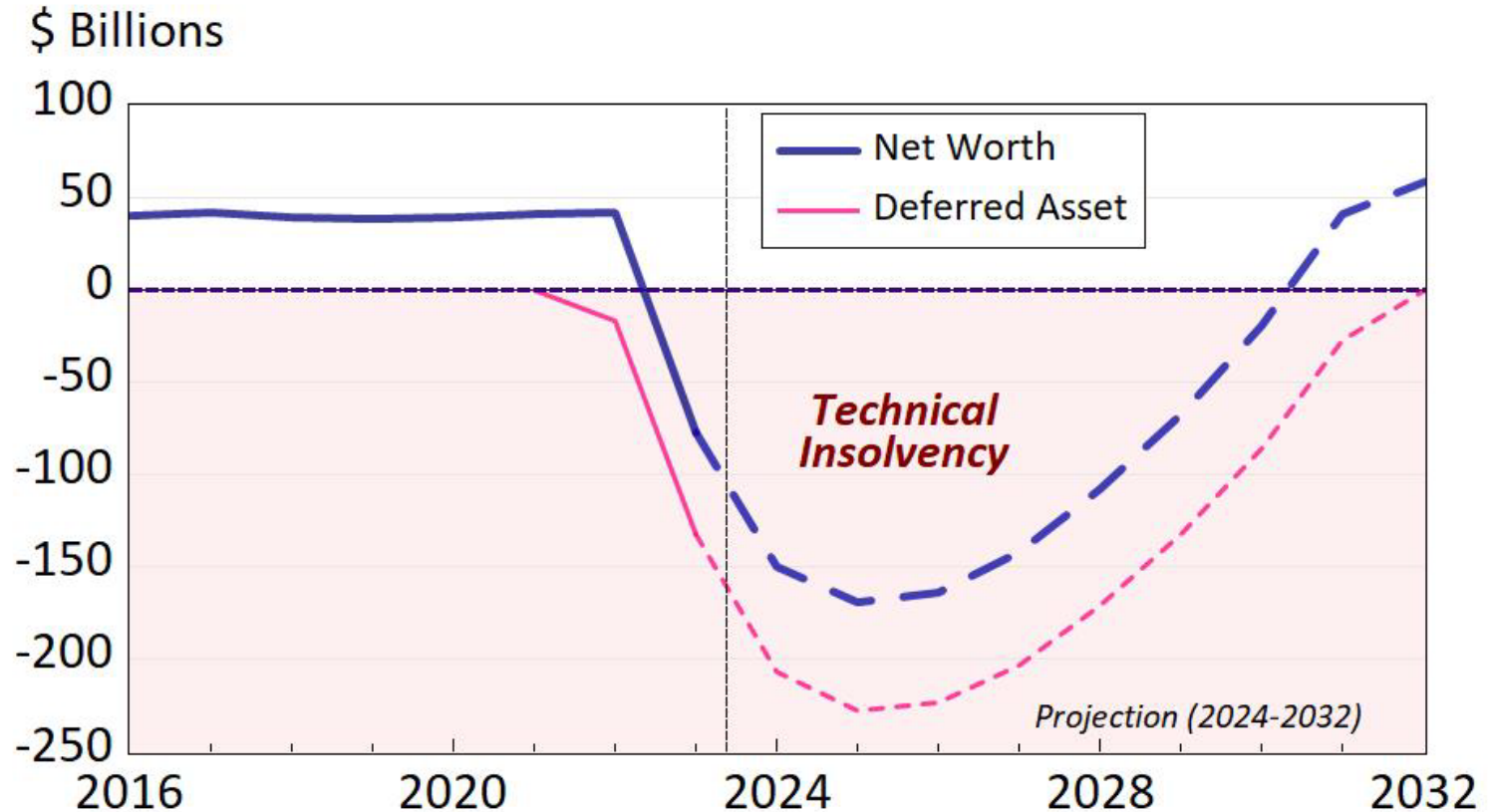


*Source: Federal Reserve Board, BEA, authors' calculations.*

*Note: This projection is an update of Levin, Lu & Nelson (2022) using data and market expectations at the end of 2023:Q3.*



# Evolution of the Fed's "Magic Asset"



*Source: Federal Reserve Board, authors' calculations.*

*Note: This projection is an update of Levin, Lu & Nelson (2022) using data and market expectations at the end of 2023:Q3.*

# Limitations of the Fed's Current Audits

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- **Limited Scope**

- Aimed at identifying material misstatements & fraud
- No consideration of efficacy or efficiency

- **Imperfect Credibility from Recurring Scandals**

***FIFA Scandal:** "There were sufficient red flags of improper and highly suspicious payments...and other highly questionable activities, coupled with a history of similar issues...that should have caused the auditors...to recommend further investigation."*

***Carillion Scandal:** "I would not hire you to do an audit of the contents of my fridge, because when I read it, I would not know what was actually in my fridge or not."*

***Silicon Valley Bank & Signature Bank:** the auditor issued unqualified audits just weeks before the failure of each institution*

# GAO: “The Taxpayer’s Best Friend”

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- **Independent and Non-Partisan**
  - Comptroller General selected via bipartisan process
  - Appointed to a single non-renewable 15-year term
- **Comprehensive Reviews of All Federal Agencies**  
*(including SEC, CFTC, FHFA, FDIC, NASA, etc.)*
  - Financial Audits
  - Efficacy and Efficiency
- **Extraordinary Track Record**
  - Documented savings to U.S. taxpayers of **nearly \$1 trillion** over the past decade (2011-2022)

## GAO report warns Artemis 3 landing may be delayed to 2027

Jeff Foust December 1, 2023



Illustration of a SpaceX Starship lunar lander on the moon. Credit: SpaceX

# Restoring Congressional Oversight

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- **Specific Reporting Requirements**
  - Analysis of simple policy benchmarks
  - Alternative Scenarios (*“stress tests for monetary policy”*)
- **Congressional Access to Fed Information**
  - Sensitive FOMC information can be handled just like sensitive national security information
- **Congressional Watchdogs**
  - GAO authorized to conduct comprehensive reviews of Fed’s monetary policy framework & operations
  - Fully independent IG with authority to investigate all aspects of the Fed’s internal appointments, policymaking, and operations.