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CENTRAL BANK ACTIVISM

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ABSTRACT

Today, the Federal Reserve is at a critical juncture in its evolution. Unlike any prior period in U.S. history, the Fed now faces increasing demands to expand its policy objectives to tackle a wide range of social and political problems—including climate change, inequality, and foreign and small business aid.

This Article develops a framework for recognizing and identifying the problems with "central bank activism." It refers to central bank activism as situations in which immediate public policy problems push the Fed to aggrandize its power beyond the text and purpose of its legal mandates, which Congress has established. To illustrate, this Article provides in-depth exploration of both contemporary and historic episodes of central bank activism, thus clarifying the indicia of central bank activism and drawing out the lessons that past episodes should teach us going forward.

This Article urges that, while activism may be expedient in the near term, there are long-term social costs. Activism undermines the legitimacy of central bank authority, erodes central bank political independence, and ultimately renders a weaker central bank. In the

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end, this Article issues an urgent call to resist the allure of activism. And it places front and center the need for vibrant public discourse on the role of a central bank in American political and economic life today.

TABLE OF CONTENTS

INTRODUCTION

On January 20, 2021, Joe Biden was sworn in as 46th President of the United States. A few hours into his first day in office, President Biden promised to "[c]ontrol the pandemic," "[p]rovide economic relief," "[t]ackle climate change," and "[a]dvance racial equity."[1] To be

1. Joe Biden (@POTUS), TWITTER (Jan. 21, 2021, 6:03 PM), https://twitter.com/POTUS/status/1352029117974278145 [https://perma.cc/H4GV-ZKNT].

sure, that is a veritable list of problems that require serious policy solutions. But among the various federal government institutions equipped to play a part, this Article questions whether the U.S. central bank—the Federal Reserve ("Fed")—should have an outsized role.

Indeed, the Fed has been pulled to the center of a wide range of social, political, and economic debates more forcefully than any other federal government agency or institution.[2] It has, for example, been called upon to help small business and local government, mitigate climate change, and redress wealth and income inequality, particularly along racial and ethnic lines.[3] The Fed is not alone. Central banks

2. A number of legal academics have advocated an expanded role of the Fed of late. *See, e.g.*, Jonathan Macey, *Fair Credit Markets: Using Household Balance Sheets To Promote Consumer Welfare*, 100 TEX. L. REV. (forthcoming 2022) (manuscript at 46, 52–54), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3781164 [https://perma.cc/6EBS-UGBW] (arguing for new Fed facilities that would be made available to individuals facing emergency liquidity needs); Saule T. Omarova, *The People's Ledger: How To Democratize Money and Finance the Economy*, 74 VAND. L. REV. (forthcoming 2021) (manuscript at 4–5), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3715735 [https://perma.cc/CA44-NK36] (arguing for an expanded use of the Fed's balance sheet to deliver more direct financial services to citizens); John Crawford, Lev Menand & Morgan Ricks, *FedAccounts: Digital Dollars*, 89 GEO. WASH. L. REV. 113, 115–19 (2021) (arguing for expanded access to bank accounts at the Fed). So, too, have policymakers. *See, e.g.*, Federal Reserve Racial and Economic Equity Act, H.R. 2543, 117th Cong. (2021) ("The Board of Governors of the Federal Reserve System and the Federal Open Market Committee shall exercise all duties and functions in a manner that fosters the elimination of disparities across racial and ethnic groups with respect to employment, income, wealth, and access to affordable credit . . . ."); Federal Reserve Racial and Economic Equity Act, S. 1327, 117th Cong. (2021) (same); Uplifting Our Local Communities Act, H.R. 7498, 116th Cong. (2020) (proposing to enable the Fed to finance state and local governments during "unusual and exigent circumstances," such as the COVID-19 pandemic); BIDEN-SANDERS UNITY TASK FORCE, BIDEN-SANDERS UNITY TASK FORCE RECOMMENDATIONS: COMBATTING THE CLIMATE CRISIS AND PURSUING ENVIRONMENTAL JUSTICE 64, 74 (2020), https://joebiden.com/wp-content/uploads/2020/08/UNITY-TASK-FORCE-RECOMMENDATIONS.pdf [https://perma.cc/5KVL-T26R] (calling on the Fed to "significantly elevate racial equity as part of its mandate by targeting not just the overall unemployment rate but disparate unemployment rate based on race" and provide "affordable bank account[s]" for all Americans and "create a real-time payment system, so families and individuals do not have to wait days for their checks to settle").

3. *See* BIDEN-SANDERS UNITY TASK FORCE, *supra* note 2, at 18; H.R. 7498; Rebecca Christie, Opinion, *Central Banks Don't Have To Pick Winners and Losers To Fight Climate Change*, MARKETWATCH (Mar. 11, 2021, 11:30 AM), https://www.marketwatch.com/story/central-banks-dont-have-to-pick-winners-and-losers-to-fight-climate-change-11614701257 [https://perma.cc/UYZ9-WH2T]; Victoria Guida, *An Activist Central Bank? Dems Push the Fed To Fight Racial Inequality*, POLITICO (Aug. 29, 2020, 7:00 AM), https://politi.co/3lxbdqC [https://perma.cc/6ZS6-SS4W]; Rachel Siegel, *To Narrow Racial and Economic Disparities, Atlanta Fed Chief Raphael Bostic Is Rethinking What the Fed's Mandate Means*, WASH. POST (Aug. 21, 2020, 6:00 AM), https://www.washingtonpost.com/business/2020/08/21/bostic-fed-race-economy [https://perma.cc/ 76VA-XHDQ].

around the world are now perceived to have "quite a bit" to do with "social justice and environmental decay."[4]

But this vision of central banking expands their role immensely. Central banks are constituted to be monetary authorities, and in many countries, bank regulators and supervisors, too.[5] Addressing a broader panoply of social ills largely falls outside their wheelhouse, for lack of the legal authority to do so and the policy tools to get such jobs done. Still, regardless of these limitations, as renowned financial historian Harold James recently remarked, the tremendous social, economic, and political shocks of the past ten years have put intense pressure on central banks to "multi-task."[6]

In some quarters, central bankers seem keen to engage in this mission creep. Christine Lagarde, president of the European Central

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4. Balazs Koranyi, Francesco Canepa & Frank Siebelt, *From Climate Change to Equality, Lagarde Turns ECB More Political*, REUTERS (Oct. 26, 2020, 2:10 AM), https://reut.rs/34qGi99 [https://perma.cc/FS93-DTFX]; Pedro Nicolaci da Costa, *Inequality, Climate Change and the Role of Central Banks*, FORBES (Dec. 4, 2019, 7:41 AM), https://www.forbes.com/sites/pedrodacosta/2019/12/04/inequality-climate-change-and-the-role-of-central-banks [https://perma.cc/DF64-HFPJ]. The press recently began commenting on the increasing pressure to conscript central banks into ancillary social issues, with varying opinions on the matter. *Compare* Editorial, *The Perils of Asking Central Banks To Do Too Much*, ECONOMIST (Mar. 13, 2021), https://www.economist.com/finance-and-economics/2021/03/13/the-perils-of-asking-central-banks-to-do-too-much [https://perma.cc/7GUR-KZAZ] ("[T]empting as it is to allow authority to flow to those who use it well, adding to central-bank mandates poses both economic and political risks."), *with* Martin Wolf, Opinion, *Monetary Financing Demands Careful and Sober Management*, FIN. TIMES (Apr. 9, 2020), https://www.ft.com/content/dc233540-798e-11ea-9840-1b8019d9a987 [https://perma.cc/VG6Y-58B7] (urging that "exceptional circumstances" make the "job of the central bank to support the overriding need for the state to protect people's lives and livelihood . . . [i]ts independence, while normally desirable, is a means to an end, not an end in itself"). Further, as one former deputy governor of the Bank of England has recently remarked, "Fifteen years ago, the world of central banking seemed sober, calm and apolitical. Since then the financial crisis, euro meltdown and now Covid-19, together with persistently weak underlying growth, have reinjected politics into central banking, creating dilemmas and tensions." Paul Tucker, *Do We Need a New Constitution for Central Banking?*, ECON. OBSERVATORY (Dec. 22, 2020), https://www.economicsobservatory.com/do-we-need-new-constitution-central-banking [https://perma.cc/2PTC-MD4W].

5. *See, e.g.*, Christina Parajon Skinner, *Central Banks and Climate Change*, 75 VAND. L. REV. 1301, 1325 (2021) (describing the various powers of the Fed).

6. *See* HAROLD JAMES, MAKING A MODERN CENTRAL BANK 457 (2020) (remarking, at the launch of this book, that tremendous social, economic, and political shock has put pressure on the central bank to "multi-task"); *see also* Laura Alix, *Pressure Mounts on U.S. Bank Regulators To Stress Test for Climate Change*, AM. BANKER (Sept. 20, 2020, 9:00 PM), https://www.americanbanker.com/news/pressure-mounts-on-u-s-bank-regulators-to-stress-test-for-climate-change [https://perma.cc/8AR3-23GA] (discussing recommendations by the Commodity Futures Trading Commission that banks and other federal regulators should use stress tests to anticipate the impact of climate change on the financial industry).

Bank ("ECB"), has committed to doing "whatever we can" to fight climate change;[7] just as her predecessor, Mario Draghi, promised to do "whatever it takes" to save the eurozone from the financial crisis—conjuring images of Machiavelli and the Medici, not a rules-bound institution.[8] Patrick Honohan, former governor of the Bank of Ireland, has likewise urged that "central banks have been behind the curve of society's response to these issues [like climate change and inequality] and could make a worthwhile contribution in a number of respects."[9] Even former U.K. Chancellor of the Exchequer, George Osborne, has extolled the virtues of an "activist central bank[]" as a means of ensuring "our best days lie ahead."[10] Putting their words to action, these various central banks have begun to engage in a range of actions and experiments, earning themselves new pithy epithets—"central bankers of the future"[11] and central bankers of a "brave new world."[12]

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7. Editorial, *Lagarde Does Whatever She Can*, WALL ST. J. (Dec. 9, 2020, 10:21 AM), https://www.wsj.com/articles/lagarde-does-whatever-she-can-11607527307?mod=opinion_lead_pos4 [https://perma.cc/3X66-YDQB].

8. Mario Draghi, President, Eur. Cent. Bank, Speech at the Global Investment Conference (July 26, 2012), https://www.ecb.europa.eu/press/key/date/2012/html/sp120726.en.html [https://perma.cc/5HGH-YD8A].

9. Patrick Honohan, *Should Monetary Policy Take Inequality and Climate Change into Account?* 2 (Peterson Inst. for Int'l Econ., Working Paper No. 19-18, 2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3478285 [https://perma.cc/296M-LK4Q].

10. George Osborne, Opinion, *How To Keep Proving the Economic Pessimists Wrong*, WALL ST. J. (Dec. 14, 2014, 6:42 PM), https://www.wsj.com/articles/george-osborne-how-to-keep-proving-the-economic-pessimists-wrong-1418600536 [https://perma.cc/3ZKV-KYHN].

11. Agustín Carstens, Gen. Manager, Bank of Int'l Settlements, Central Bankers of the Future, Speech at the Deutsche Bundesbank's Internal Discussion Series (Dec. 14, 2020), https://www.bis.org/speeches/sp201214.pdf [https://perma.cc/M8EE-NBM9].

12. Balazs Koranyi & Francesco Canepa, *Central Bankers Seek New Role in Brave New World*, REUTERS (Nov. 10, 2020, 12:25 PM), https://reut.rs/35ei3LH [https://perma.cc/6LC4-EJMP]; *see* Carola Conces Binder & Christina Parajon Skinner, Laboratories of Central Banking 33–44 (Aug. 9, 2021) (unpublished manuscript) (on file with author) (empirically demonstrating that Fed research departments have increasingly focused on topics like climate and inequality, along lines of race and gender); *see also The ECB's Monetary Policy Strategy Statement*, EUR. CENT. BANK, https://www.ecb.europa.eu/home/search/review/html/ecb.strategyreview_monpol_strategy_statement.en.html [https://perma.cc/545B-TD38] ("In addition to the comprehensive incorporation of climate factors in its monetary policy assessments, the Governing Council will adapt the design of its monetary policy operational framework in relation to disclosures, risk assessment, corporate sector asset purchases and the collateral framework."); Press Release, Bank of England, Bank of England Publishes the Key Elements of the 2021 Biennial Exploratory Scenario: Financial Risks from Climate Change (June 8, 2021), https://www.bankofengland.co.uk/news/2021/june/key-elements-of-the-2021-biennial-exploratory-scenario-financial-risks-from-climate-change [https://perma.cc/TS4A-GWTX] (announcing how the Bank will conduct a scenario analysis and stress test "to explore the financial risks posed by climate change for the

The Fed also faces considerable pressure to expand.[13] Indeed, some already see the Fed gradually succumbing to the pressure of unprecedented times, using "incremental adaptions of the policy instruments that are available" to accomplish new and larger aims.[14] The Fed has long been committed to a rhetoric of apolitical technocracy, but there is a growing chorus of media, commentators, and scholars suggesting it would be "morally and ethically wrong for central banks to . . . remain on the sidelines" of key social issues.[15] But such value judgments are for Congress, who has the constitutional authority to specify the policy objectives that the Fed has authority to pursue.[16]

Principally, the Federal Reserve Act mandates that the Fed maintain price stability and maximum employment[17] and gives the Fed responsibility to act as "lender of last resort" to financial institutions in distress.[18] Other legislation requires the Fed to mind the "safety" and

largest UK banks and insurers"); *Climate Change*, BANK OF ENG., https://www.bankofengland.co.uk/climate-change [https://perma.cc/N9FF-ECT6] (last updated Sept. 23, 2021) (discussing the Bank's scenario analysis and stress testing as a part of its toolkit to address climate change financial risk); *NGFS Publications*, NGFS, https://www.ngfs.net/en/liste-chronologique/ngfs-publications [https://perma.cc/DJ2H-JWDE] (listing NGFS publications, dating back to 2018, pushing forward a broader climate-related research agenda).

13. *See infra* Part I.A. For a broad empirical treatment of central banks and political pressure, see generally Carola Conces Binder, Political Pressure on Central Banks (Dec. 15, 2018) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3244148 [https://perma.cc/HL5M-CWMB] (analyzing whether central banks are likely to succumb to political pressure).

14. Mohamed A. El-Erian, *Evolution, Impact, and Limitations of Unusual Central Bank Policy Activism*, 103 FED. RSRV. BANK ST. LOUIS REV. 243, 258 (2012); *see* Peter Conti-Brown & David A. Wishnick, *Technocratic Pragmatism, Bureaucratic Expertise, and the Federal Reserve*, 130 YALE L.J. 636, 636, 639–41 (2021) (urging that the Fed can address things like climate change, the COVID-19 pandemic, and cyber risk under the umbrella of "technocratic pragmatism" which allows "the Fed to develop the expertise necessary to address emergent problems as long as it remains constrained by norms designed to preserve its long-run legitimacy").

15. El-Erian, *supra* note 14; *see supra* notes 2–4 and accompanying text.

16. *See infra* Part III.

17. *See* 12 U.S.C. § 225a.

18. *Id.* (price stability); *id.* § 343 (emergency lending to nonbank financial institutions); *id.* § 347b(a) (discount window). As will be later discussed, the original 13(2) power was not intended as a LOLR power, in the contemporary sense of the term. *See infra* notes 20 and 39 and accompanying text. Throughout the 1920s the Reserve Banks accepted eligible paper on demand, using the discount rate to adjust demand. *See infra* notes 260–84 and accompanying text. The philosophy behind the policy was grounded in the so-called real bills doctrine. *See generally* Stanley Fischer, Vice Chairman, Bd. of Governors of the Fed. Rsrv. Sys., The Lender of Last Resort Function in the United States, Address at a Committee on Capital Markets Regulations Conference (Feb. 10, 2016) (transcript available at https://www.federalreserve.gov/

"soundness" of financial institutions[19] and to look after the stability of the financial system overall.[20] Neither the text nor purpose of this legislation authorizes the Fed to redress problems associated with small business, climate, or inequality—regardless of how important these problems are today.[21] They may well be issues for other branches of the government, but strictly speaking, they are not problems for the Fed.

Yet central banks are often pressured to engage in "activism" when their policy goals and tools—set out ex ante by the legislature—fall short of some present economic problem. In principle, problems that fall outside the predetermined perimeter of central bank policy ought to be addressed by the elected legislature or executive, either through direct action or explicit allocation of responsibility to the

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newsevents/speech/files/fischer20160210a.pdf [https://perma.cc/TQ8H-YSRZ]) (highlighting how "the Fed executed its lender-of-last-resort responsibility" from the Great Depression to the Great Recession).

19. 12 U.S.C. § 1842(c)(4).

20. While this is not an express mandate of the Federal Reserve, it seems implied by the Dodd-Frank Act 2010. *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, §§ 113(a), 161–176, 124 Stat. 1376, 1398, 1420–1442 (2010) (codified at 12 U.S.C. §§ 5323, 5361–5374) (identifying the Board of Governors as the agency to supervise institutions that "could pose a threat to the financial stability of the United States" and providing the Board with various new legal authorities to carry out the § 113 supervisory responsibility); BD. OF GOVERNORS OF THE FED. RSRV. SYS., FINANCIAL STABILITY REPORT 1 (2021), https://www.federalreserve.gov/publications/files/financial-stability-report-20210506.pdf [https://perma.cc/7YQB-8E5H] ("Promoting financial stability is a key element in meeting the Federal Reserve's dual mandate for monetary policy regarding full employment and stable prices."); Jerome Powell, Chair, Bd. of Governors of the Fed. Rsrv. Sys., Press Conference 3 (July 28, 2021) (transcript available at https://www.federalreserve.gov/mediacenter/files/FOMCpresconf20210728.pdf [https://perma.cc/N9QT-C47W]) (recognizing the Fed has "responsibilities to promote the stability of the financial system").

21. The so-called "real bills" doctrine, which significantly influenced the original Federal Reserve Act, contended that monetary policy would become self-regulating if money supply was tied to real economic activity, such that "as a matter of law . . . certain types of business credit could *always* be converted into bank reserves." Perry Mehrling, *Economists and the Fed: Beginnings*, 16 J. ECON. PERSPS. 207, 210–13 (2002). Accordingly, section 14(d) of the original Federal Reserve Act required that the Fed make policy "with a view of accommodating commerce and business" and, in section 13(2), lend exclusively against "notes, drafts, and bills of exchange issued or drawn for agricultural, industrial, or commercial purposes." Federal Reserve Act, Pub. L. No. 63-43, §§ 13(2), 14(d), 38 Stat. 251, 263, 265 (1913) (codified as amended at 12 U.S.C. §§ 343, 357). However, the Fed abandoned the doctrine after its policy prescriptions led to disastrous results during the Great Depression—therefore, it does not justify the Fed redressing problems associated with small businesses today. For general history and discussion of the real bills doctrine, see THOMAS M. HUMPHREY & RICHARD H. TIMBERLAKE, GOLD, THE REAL BILLS DOCTRINE, AND THE FED: SOURCES OF MONETARY DISORDER, 1922–38 (2019); Jeffrey M. Lacker, *From Real Bills to Too Big To Fail: H. Parker Willis and the Fed's First Century*, 39 CATO J. 15, 17–18 (1999).

central bank. But should they fail to do so, likely because of insurmountable political frictions, central bankers may feel exogenously pressured (by the public or other branches of the government) or endogenously compelled (from factions within the institution) to step in and flex some muscle.

The core claim of this Article is that when the Fed bends or stretches its legal mandates to address social or economic problems of the day (if and as they might emerge), it engages in "activism" that will present problems for society on a number of dimensions. Each problem will build upon the last; they are as follows:

First, and most plainly, central bank activism can be ultra vires. Like all administrative agencies, the Board of Governors of the Federal Reserve System (the "Fed Board") makes policy and regulation based on authority delegated to it by the U.S. Congress. And, like all agencies, it is required to act within the ambit of the legislative authority it has been delegated; to go beyond what Congress has permitted and asked it to do would be an unconstitutional assumption of legislative authority.[22] Congress first conceived the Fed as an institution with a limited purpose in society; in 1913, the year of its founding, the Fed was tasked with maintaining an elastic currency and supervising its member banks.[23] While the Fed's legal purpose grew throughout the twenty and twenty-first centuries, that growth was always statutorily prescribed, not politically imposed or self-aggrandized.[24] The Fed—although a unique institution in many respects—is similar to other regulatory agencies insofar as its officials

22. *See* Bowen v. Georgetown Univ. Hosp., 488 U.S. 204, 208 (1988) ("It is axiomatic that an administrative agency's power to promulgate legislative regulations is limited to the authority delegated by Congress."). The structure of the Constitution allocates power among three distinct branches, with legislative power allocated to the legislative branch. *See generally* M.J.C. VILE, CONSTITUTIONALISM AND THE SEPARATION OF POWERS (2d ed. 1998) (discussing the three branches of government and the powers given to each).

23. Federal Reserve Act, Pub. L. No. 63-43, 38 Stat. 251, 251 (1913).

24. *See generally* SARAH BINDER & MARK SPINDEL, THE MYTH OF INDEPENDENCE: HOW CONGRESS GOVERNS THE FEDERAL RESERVE 19 tbl.1.1 (2017) (tabling "Key Episodes of Congressional Reform of the Fed, 1913-2015").

are unelected.[25] In a democratic society, the Fed must be constrained by Congress. Central bankers are not, after all, 'philosopher kings.'[26]

Second, central bank activism alters the balance of power between the Fed, the executive branch, and Congress. This can happen in a number of ways. Most generally, whenever the Fed enlarges the scope of its own authority, it assumes power from Congress to define the Fed's role while simultaneously undermining Congress's ability to hold the Fed accountable. Insofar as the Fed engages in credit allocation or monetary finance, for example, it acts in place of power that is more properly exercised by the fiscal authority of the Treasury. And, to the extent the Fed reacts to popular (and presidential) pressure for new or increased action, it enlarges the power of the presidency to influence the policy of the Fed—something Fed chairs have fought against since 1913.[27]

Third, activism invites political interference which may undermine the Fed's autonomy and perhaps its independence.[28] Independence from political pressure is generally recognized as critical to the Fed's ability to effectively transmit policy. In order to be effective at anchoring inflation expectations, for example, central banks have to be able to credibly commit to pursuing low inflation. But because politicians, seeking short-term gains in popularity, tend to want a 'hot economy,' politicians can inevitably be counted upon to try to pressure the Fed into keeping interest rates low, even if that means increased inflation down the road. A norm against political interference in this regard allows the Fed to commit to price stability without skepticism about its ability to remain stalwart. The Fed needs a widespread norm of independence because it is the steward of price stability in our

25. For a thorough treatment on the legitimacy of central bank power, see generally PAUL TUCKER, UNELECTED POWER: THE QUEST FOR LEGITIMACY IN CENTRAL BANKING AND THE REGULATORY STATE (2018).

26. *See* Grant Wilson, Opinion, *The Limits of Central Bank Activism May Finally Be in Sight*, FIN. REV. (Nov. 29, 2020, 3:32 PM), https://www.afr.com/markets/debt-markets/the-limits-of-central-bank-activism-may-finally-be-sight-20201129-p56iwb [https://perma.cc/TQU6-N3EA]. The notion of a philosopher king, an all-knowing, benevolent ruler, "handing down wisdom" to citizens and officials, was theorized by Plato. PLATO, THE REPUBLIC OF PLATO 175–256.

27. *See* Michael Salib & Christina Parajon Skinner, *Executive Override of Central Banks: A Comparison of the Legal Frameworks in the United States and the United Kingdom*, 108 GEO. L.J. 905, 905, 957–68 (2020).

28. For a general treatment of Fed independence, see PETER CONTI-BROWN, THE POWER AND INDEPENDENCE OF THE FEDERAL RESERVE 2–3, 179–80 (2016). *But see* BINDER & SPINDEL, *supra* note 24, at 4–5, 10–11, 16–18 (pointing out that, despite its now revered status in the popular mind, independence is far from absolute).

economy. But forward-leaning interpretations of its mandate, that suggest it to be politicized, will erode that norm. Damage to Fed independence can lead society down a very slippery slope. If beholden to political beliefs, the Fed will soon find itself in the business of restricting or redirecting dollars in the economy depending on which group or industries are in or out of political favor. Such practice is anathema to a market economy in a democratic society.

For all of these reasons, there is much at stake in seeing activism plainly—and actively debating it. Public understanding of and discourse around central bank activism makes a subterranean "transformation of the state"—which some central bank watchers are predicting—more difficult to accomplish.[29] It also may, in turn, place the onus on Congress to act through legislation and modify the duties of the Fed, should society demand it.

This Article begins that debate by creating a novel framework for viewing and understanding central bank activism. It offers a descriptive account of central bank activism, conceptualizing activism in terms of both current and historic episodes of activism. This Article also offers a normative account of activism, exploring the dangers of this behavior to the U.S. economy and its democracy. Finally, it makes suggestions for how to constrain activism while, at the same time, allowing for a central bank that is modern, adaptive, and agile.

To that end, this Article proceeds in three parts. The first Part examines various examples of central bank activism. How do we recognize central bank activism and set it apart from lawful policy maneuvering and application? Part I first offers a working definition of activism; it then explains the bases for that definition by considering the three arenas in which the Fed is or has been called on to engage in activism—in managing the global financial and economic crises of 2008 and 2020; in mitigating climate change; and in redressing wealth and income inequality. Without a doubt, these are all extremely important problems for society to solve—but to what extent are they problems that the Fed can undertake without damage to the rule of law and the efficacy of the central bank?

Part II gives more descriptive context by studying past episodes in history when the Fed has engaged in activism. This Part considers three examples in U.S. history where central bank activism occurred and draws out lessons learned. The first example involves the First and

29. *See* Wilson, *supra* note 26 (predicting an unnoticed transformation of the role of government).

Second Banks of the United States, America's earliest efforts at a central bank. Activist efforts in institutional design—fashioning a bank that would mix public and private functions in ways that facilitated credit allocation—doomed the Banks to popular resentment and ultimately Andrew Jackson's veto. The second example involves various activist endeavors of the Fed during the 1920s, largely under the leadership of the New York Federal Reserve Bank. That Reserve Bank's president, Benjamin Strong, pursued a policy objective of price stability long before Congress had given the Federal Reserve System a mandate to do so; Strong also set discount rate policy to help a foreign ally. The third example is from the 1970s, when the Fed's focus on price stability became blurred. Instead, it attended to more politically palatable objectives, like prodding up employment. This resulted in an uncontrolled period of "Great Inflation," which inflicted significant macroeconomic pain. On the whole, Part II shows that activism is not a new phenomenon and is never without costs.

Part III answers the key normative question: Why worry (much) about central banking activism? For many, questions of activism fall in the gray. After all, if a central bank lacks the positive legal authority to engage in "green quantitative easing," but can use its policy tools to push the world towards a better climate equilibrium—would that be 'so bad'? Are there trade-offs worth accepting? While intoxicating to consider, it is a dangerous slippery slope that governments have slid down too fast before. Long-term costs usually outweigh the gains. For one, opening the door to ultra vires action—where ends may justify the means—can damage the Fed's legitimacy and independence. That damage translates to a less effective Fed—one that misallocates resources and can neither stymie economic crises nor buoy the economy. Moreover, overreliance on the Fed might provide just a temporary fix while obscuring the responsibilities of other institutions that should be taking action.

Still, nuance is important. It is practical to evaluate activism along a spectrum insofar as the Fed must have some leeway to modernize and react to emergent crises, while hewing closely to the rule of law. The legitimacy of activism may well vary, in this way, depending upon: (1) how explicit the legal authority is to address a particular problem; (2) how much expertise the Fed has with respect to that problem; and

(3) how strong the mechanisms for accountability are.[30] Accordingly, the final Part of this Article sketches out a framework that the Fed (or Congress) might use to ensure that newly pursued policy initiatives constitute in-bounds adaptations or agility maneuvers—not power-aggrandizing activism—and that the public understands as much.

Ultimately, this Article aims to generate public discourse surrounding the legitimate role of the Fed in our society.[31] Inasmuch as contemporary social and political pressures stand to fundamentally reshape the Fed, they have also thrown up critical questions core to a society founded on the rule of law and those that pertain to the scope, and power, of the administrative state. By stimulating that debate, this Article may also muster more attention to the need for Congress to reconsider the necessary and proper authority of the Federal Reserve in the United States today.

I. WHAT IS CENTRAL BANK 'ACTIVISM'?

How do we recognize central bank activism, and under what conditions does it occur? Answering that question is the focus of this Part. As the following case studies will show, central bank activism can arise in response to economic problems that require solutions that sit beyond or outside the Fed's legal mandates. Often, because these problems feel acute, political and popular pressure will build on the central bank to expand its policy tools beyond what the letter or spirit of the law admits and allows.[32]

To illustrate the concept, this Part considers three examples of contemporary activism. The first example involves the Fed's expansion

30. In this regard, this Article reinforces the work of those scholars like Professors Peter Conti-Brown and David Wishnick that seek to develop paradigms to help the Fed "navigate the tension" between popular demands to aggrandize power, on the one hand, and the need to avoid forays into "resolutely 'political problems,'" on the other. *See* Conti-Brown & Wishnick, *supra* note 14, at 639.

31. As Paul Tucker has surmised, it is now time for "[w]idespread vigilance and awareness of subtle but cumulative attempts to repoliticise central banking to service sectional interests—what is cheered today might bring tears tomorrow." Tucker, *supra* note 4.

32. Although this Article confines its study to central banks, activism among administrative agencies is not unique to the Fed. In recent months, commentators have also remarked on activism at the Federal Trade Commission ("FTC"). Editorial, *A Case of Blindside Regulation*, WALL ST. J. (Jan. 11, 2021, 6:31 PM), https://www.wsj.com/articles/a-case-of-blindside-regulation-11610407907?mod=opinion_lead_pos3 [https://perma.cc/9AZH-K4JD] ("Congress has empowered the FTC to prevent, prohibit and punish 'unfair or deceptive' business practices. The Federal Trade Commission Act doesn't define these terms, so the FTC is supposed to know them when it sees them. The agency increasingly sees them wherever it looks.").

of its "lender of last resort" ("LOLR") authority in the past ten years. The second two examples are presently hypothetical, but potentially imminent—they consider the pressure and potential for the Fed to engage in climate or redistributional policy.

Collectively, these three cases shed light on activism's main hallmarks: the rise of some tension between legal text and purpose or historic usage, on the one hand, and an economic policy problem on the other, which creates pressure on the central bank to take or evolve a legal power outside the legislative process. In addition, activism threatens to upset some structural dynamics, either by: (1) reallocating power between the Fed, Congress, and the Executive Branch (i.e., the Treasury); (2) creating an opening for new or increased political pressure going forward; or (3) making value judgments that are otherwise reserved for elected officials in the political branches. Ultimately, the various cases of present and past activism fall along different points on a spectrum of legitimacy, which will be considered in Part III.

A. Lender of Last Resort

The first example of central bank activism involves one of the Fed's core historic roles—its responsibility to act as a LOLR to financial institutions and the financial system during periods of crisis or emergency.[33] The basic notion of a central bank as LOLR is that, in situations of market turmoil, the central bank should step in and lend "freely," but only to solvent institutions and at a penalty rate.[34] This is famously known as Bagehot's dictum, named for Walter Bagehot, the so-called father of central banking.[35]

There are several provisions of the Federal Reserve Act that empower the Fed to act as a LOLR. One, authorized by section 10B of the Federal Reserve Act, is known as the "discount window" and was

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33. *See* Thomas M. Humphrey, *Lender of Last Resort: The Concept in History*, FED. RSRV. BANK RICHMOND ECON. REV., Mar.–Apr. 1989, at 8, 8.

34. *See* WALTER BAGEHOT, LOMBARD STREET: A DESCRIPTION OF THE MONEY MARKET 23, 25, 97 (1873).

35. *See* Ben S. Bernanke, *Fed Emergency Lending*, BROOKINGS (Dec. 3, 2015), https://www.brookings.edu/blog/ben-bernanke/2015/12/03/fed-emergency-lending [https://perma.cc/P9QH-MT9P] (discussing how Bagehot's dictum influences the Fed). Notably, there are many references to Bagehot in the 1913 Federal Reserve Act congressional records. *See, e.g.*, 51 CONG. REC. 667 (1913) (statement of Sen. Burton).

added to the Federal Reserve Act in February 1932.[36] Section 10B provides that "[a]ny Federal Reserve bank . . . may make advances to any member bank on its time or demand notes having maturities of not more than four months and which are secured to the satisfaction of such Federal Reserve bank."[37] Pursuant to that authority, Federal Reserve Banks can make loans to depository institutions that are part of the Federal Reserve System.[38]

Congress designed section 10B with financial and economic emergencies in mind.[39] For context, Congress added 10B to the Federal Reserve Act in the midst of the tremendous economic hardship of the Great Depression (in the Glass-Steagall Act), mainly in order to give banks the confidence they needed to continue lending despite the uncertain times.[40] Indeed, reflecting on that era, former Fed General

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36. Act of Feb. 27, 1932, Pub. L. No. 72-44, § 10(a), 47 Stat. 56, 56 (codified as amended at 12 U.S.C. § 347b(a)); *Discount Window Lending*, BD. OF GOVERNORS OF THE FED. RSRV. SYS., https://www.federalreserve.gov/regreform/discount-window.htm [https://perma.cc/76DD-W7X2] (last updated June 30, 2021) ("[T]he 'discount window'[] plays an important role in supporting the liquidity and stability of the banking system and the effective implementation of monetary policy."). This provision was added by emergency legislation in 1932, and the Glass-Steagall Act (also known as the Banking Act of 1933) made it a permanent fixture, with some amendments, to the Federal Reserve Act. *See* Anna J. Schwartz, *The Misuse of the Fed's Discount Window*, 74 FED. RSRV. BANK ST. LOUIS REV. 59, 60 (1992).

37. 12 U.S.C. § 347b(a).

38. There is other federal law that gives state nonmember banks and thrifts access to the Fed's discount window. *See* PETER CONTI-BROWN & DAVID SKEEL, USING THE FEDERAL RESERVE'S DISCOUNT WINDOW FOR DEBTOR-IN-POSSESSION FINANCING DURING THE COVID-19 BANKRUPTCY CRISIS 8 (2020), https://www.brookings.edu/wp-content/uploads/2020/07/Conti-Brown-Skeel.pdf [https://perma.cc/AT8S-4T8T] ("After the passage of the Monetary Control Act of 1980, any depository institution can access the Fed's discount window.").

39. These eligible institutions can borrow from the discount window at any time, but in practice banks tend to limit their discount window borrowing to emergency situations only to avoid a stigma associated with resorting to the Fed for help. *See The Discount Window*, FED. RSRV. BANK OF N.Y. (July 2015), https://www.newyorkfed.org/aboutthefed/fedpoint/fed18.html [https://perma.cc/SU52-2SF4]; HUBERTO M. ENNIS & DAVID A. PRICE, NO. EB20-04, UNDERSTANDING DISCOUNT WINDOW STIGMA 1 (2020), https://www.richmondfed.org/-/media/RichmondFedOrg/publications/research/economic_brief/2020/pdf/eb_20-04.pdf [https://perma.cc/CLW4-VDGP].

40. *See* HOWARD H. HACKLEY, LENDING FUNCTIONS OF THE FEDERAL RESERVE BANKS: A HISTORY 100–01 (1973) ("The Glass-Steagall Act was essentially an emergency measure . . . . [d]esigned to correct the abuses that had led to the unhappy days [of the Great Depression]."). As further proof that 10B was designed with emergencies in mind, the original bill imposed various conditions on accessing the discount window, including a penalty rate of interest, exigencies required, and a demonstration that the bank could not access credit elsewhere. *Id.* at 105–08.

Counsel Howard Hackley once remarked that the creation of the discount window was "largely psychological":

> it gives assurance to these frightened and timid bankers throughout the country that if they will only respond to the requirements of commerce, if they will only help in relieving themselves and the country from this depression and in doing so exhaust their eligible assets, then and only then may they make use of their ineligible assets.[41]

Congress displayed similar motivation when it expanded the Fed's LOLR powers to other kinds of institutions by adding section 13(3) in July 1932.[42] The addition of 13(3) made it possible for the Reserve Banks to lend to "individual[s], partnership[s], [and] corporation[s]," not just member banks.[43] But such loans had to be "strictly limited"[44] to "unusual and exigent" circumstances.[45] To cabin 13(3), Congress narrowed the kind of paper acceptable for discount more than it had under 10B.[46] Additionally, the statute gave permission for further conditioning by giving the Fed Board power to issue rules concerning the parameters by which Reserve banks would be allowed to make 13(3) loans.[47] Taking Congress up on that invitation, a July 26, 1932 circular set out even stricter terms than the text of the statute had: it required that the Reserve Banks demand a statement from each applicant seeking 13(3) assistance explaining the purposes for which the loan proceeds would be used and the efforts the borrower had made to obtain credit elsewhere first, from other financial

41. *Id.* at 101.

42. Act of July 21, 1932, ch. 520, § 210, 47 Stat. 709, 715 (codified as amended at 12 U.S.C. § 343). As will be discussed, two years later, the Industrial Advances Act added section 13(b) to the Federal Reserve Act, which, during the 1930s and 40s, became a much more active lending program. *See* Industrial Advances Act, Pub. L. No. 73-417, 48 Stat. 1105, 1105 (1934); *infra* notes 130–34 and accompanying text.

43. § 210, 47 Stat. at 715.

44. HACKLEY, *supra* note 40, at 128.

45. § 210, 47 Stat. at 715. There were other limiting conditions imposed at the time: five members of the Board had to vote in favor of the loan and could limit the duration of the assistance. HACKLEY, *supra* note 40, at 128.

46. *See* HACKLEY, *supra* note 40, at 128.

47. *See* 12 U.S.C. § 343(3)(A) ("All such discounts for any participant in any program or facility with broad-based eligibility shall be subject to such limitations, restrictions, and regulations as the Board of Governors of the Federal Reserve System may prescribe.").

institutions.[48] Again, this all shows that the purpose of 13(3) was foremost for emergency, "to provide needed credit to business concerns and individuals," and for sparing use.[49]

Section 13 has been amended several times since its original passage. Two separate legislative changes in the 1930s relaxed eligibility requirements in section 13 to facilitate emergency lending by the Reserve Banks. In 1933, Congress added section 13(13) to the Federal Reserve Act, which allowed the Reserve Banks to make ninety-day advances to individuals, partnerships, or corporations.[50] This provision did not contain language of exigency per se, but political and legislative context suggests that it was intended to supplement section 13(3); at the time, 13(3) authority for Reserve Bank discounting was limited to so-called real bills.[51] Section 13(13), in contrast, would allow for short-term advances (loans) secured by a broader set of collateral, U.S. treasury securities.[52] The Banking Act of 1935 would later relax the requirements for discounting in section 13(3) itself by removing a requirement that the borrower provides both an

48. HACKLEY, *supra* note 40, at 129–30. This would include description of all of the borrower's banking relationships maintained over the past year. *Id.*

49. *Id.* at 129. But not many nonbanks would have the necessary commercial paper to discount. *Id.* Notably, firms with a bank charter who are not subject to reserve requirements are not eligible for ordinary lending, even if they are member banks. *Cf. Discount Window Programs Participation and Pledging Guide*, FED. RSRV. BANK OF S.F., https://www.frbsf.org/banking/discount-window/banking/files/Discount-Window-Programs-Participation-Pledging-Guide.pdf [https://perma.cc/W9KT-5LKJ] ("By law, depository institutions that maintain reservable transaction accounts or nonpersonal time deposits (as defined in Regulation D) generally may establish a borrowing relationship at the Discount Window.").

50. Emergency Banking Act of Mar. 9, 1933, Pub. L. No. 73-1, sec. 403, 48 Stat. 1, 7. Although 13(13) does not contain language restricting it to emergencies, its ninety-day proviso suggests it envisions short-term liquidity problems apropos of emergency; the emergency-styled legislation is also telling context.

51. *See* Parinitha Sastry, *The Political Origins of Section 13(3) of the Federal Reserve Act*, FRBNY ECON. POL'Y REV., Sept. 2018, at 1, 21–26. The real bills doctrine had been hard-wired into the original Federal Reserve Act in, for example, section 13(2). The provision excludes "notes, drafts, or bills covering merely investments or issued or drawn for the purpose of carrying or trading in stocks, bonds, or other investment securities, except bonds and notes of the government of the United States" from being eligible for discounts by reserve banks. 12 U.S.C. § 343. The authority for the present-day discount window, section 10B, would not be added until 1932. *See supra* note 36.

52. Sec. 402, 48 Stat. 7; *see* Sastry, *supra* note 51, at 25.

"endorsement" *and* collateral that was satisfactory to the Reserve Bank (from then on it would be one or the other).[53]

In 1991, Congress loosened the collateral requirements of 13(3) more significantly—no longer would a 13(3) borrower need to supply collateral that was as good or better than what would otherwise be eligible for discount under section 13(2) (i.e., supply a real bill).[54] Collateral could henceforth be "secured to the satisfaction of the Federal reserve bank."[55] Section 13(3) was amended yet again in 2010, as part of the Dodd-Frank Act.[56] That time, Congress made it more difficult for the Reserve Banks to lend selectively under 13(3)—it gave Treasury a veto over such facilities and required that all 13(3) assistance be delivered through facilities "with broad-based eligibility."[57]

As this historical tour around section 13 should make plain, Congress generally intended and expressed section 13 to be robust in times of crisis, but not without restraint. Between 1932 and the present day, Congress understood section 13 as a vehicle for assistance specific to "individuals, corporations, or partnerships" in the business community; confined to emergency situations or of a time-limited nature; and for the purpose of easing liquidity conditions in the

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53. Act of Aug. 23, 1935, ch. 614, § 322, 49 Stat. 684, 714 (codified as amended at 12 U.S.C. § 343). This amendment was significant:

> The process of endorsement aims to provide the Bank with a measure of protection against loss. When a party unqualifiedly endorses commercial paper, it assumes secondary liability on that paper. Following endorsement, the Bank can bring a claim against the endorser in the event that the issuer of the paper does not pay.

Alexander Mehra, *Legal Authority in Unusual and Exigent Circumstances: The Federal Reserve and the Financial Crisis*, U. PA. J. BUS. L. 221, 228–29 (2010) (emphasis omitted) (footnotes omitted).

54. Act of Dec. 19, 1991, Pub. L. No. 102-242, tit. IV, § 473, 105 Stat. 2286, 2386. While other constraints remained in place, no longer would collateral need to be "of the kinds and maturities made eligible for discount for member banks." *Id.*

55. *Id.*; *see also* Colleen M. Baker, *The Federal Reserve As Collateral's Last Resort*, 96 NOTRE DAME L. REV. 1381, 1397–98 (2021) (discussing collateral requirements in connection with LOLR).

56. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 1101(a), 124 Stat. 1376, 2113 (2010) (codified at 15 U.S.C. § 343).

57. 12 U.S.C. § 343. That is, 13(3) requires any lending facilities to be structured to render eligibility to a class of institutions rather than as a loan to any one individual, partnership, or corporation. *See* Press Release, Bd. of Governors of the Fed. Rsrv. Sys., Federal Reserve Board Approves Final Rule Specifying Its Procedures for Emergency Lending Under Section 13(3) of the Federal Reserve Act (Nov. 30, 2015), https://www.federalreserve.gov/newsevents/pressreleases/bcreg20151130a.htm [https://perma.cc/C5PF-72T3].

financial system.[58] Since 2008, active interpretations of section 13(3) have expanded its scope beyond those key parameters.[59]

1. *Asset Purchases*. As part of its crisis-fighting role, the Fed has expanded its use of 13(3) to support asset markets—a seeming departure from the more traditional use of 13(3), which is aimed at providing liquidity to individuals or institutions.[60]

The original Federal Reserve Act empowered the Fed to buy assets in the open market under section 14 of that Act.[61] In normal times, the Fed uses this authority to engage in so-called open market operations ("OMOs") to effectuate monetary policy. OMOs affect the supply of reserves, which in turn impacts the federal funds rates and then other prevailing market rates.[62] The global financial crisis of 2008

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58. An open question is municipalities, which are corporations, not sovereigns. *See, e.g.*, N.Y. GEN. MUN. LAW § 119-N (2021). Likely, the Fed has not lent to municipalities because of the credit risk analysis (and politicization) that would attend such lending. Lev Menand, *The Federal Reserve and the 2020 Economic and Financial Crisis*, 24 STAN. J.L. BUS. & FIN. 295, 319–320 (2021); *see also* Beth LeBlanc, *Fed Chief Rejects Tlaib's Push To Lend to Distressed Cities Like Detroit*, DETROIT NEWS (Feb. 12, 2020, 2:13 PM), https://www.detroitnews.com/story/news/politics/2020/02/12/tlaib-pushes-federal-reserve-lend-distressed-cities/4737801002 [https://perma.cc/28M2-4AKJ] (reporting that, in response to Representative Tlaib's urging the Fed to lend more freely to distressed cities, states, and territories like Detroit and Puerto Rico, Chair Powell replied, "What I believe is that that's not a job for the Fed . . . . The Fed has a particular role and particular authorities, and lending to state and local governments and supporting them when they're in bankruptcy, that's not part of our mandate").

59. To preview, descriptively, what follows does fit the concept of activism; normatively, however, I accept LOLR activism as both desirable and inevitable, as will be discussed below. *See infra* Part III.

60. The observation that the Fed seems ready to rescue markets became known colloquially as the "Greenspan Put." *See* Sandeep Dahiya, Bardia Kamrad, Valerio Poti & Akhtar Siddique, The Greenspan Put 2 (Jan. 9, 2019) (unpublished manuscript), https://ssrn.com/abstract=2993326 [https://perma.cc/47AF-FLKH].

61. Federal Reserve Act, Pub. L. No. 63-43, § 14, 38 Stat. 251, 264 (1913) (codified as amended at 12 U.S.C. § 353) (empowering Reserve Banks to conduct open market operations). The reader should note that the Federal Open Market Committee ("FOMC") has a separate legal existence from the Board of Governors. Banking Act of 1933, Pub. L. No. 77-66, § 8, 48 Stat. 162, 168 (codified as amended at 12 U.S.C. § 263) (creating and authorizing the FOMC). For more detailed explanation of how the FOMC conducts monetary policy, see BD. OF GOVERNORS OF THE FED. RSRV. SYS., FUNCTION: CONDUCTING MONETARY POLICY 32–38 (2017), https://www.federalreserve.gov/aboutthefed/files/pf_3.pdf [https://perma.cc/FS75-SX9Y].

62. *See* Laura Hopper, *What Are Open Market Operations? Monetary Policy Tools, Explained*, FED. RSRV. BANK OF ST. LOUIS (Aug. 21, 2019), https://www.stlouisfed.org/open-vault/2019/august/open-market-operations-monetary-policy-tools-explained [https://perma.cc/N7XX-K22S]; *Effective Federal Funds Rate*, FED. RSRV. BANK OF ST. LOUIS, https://fred.stlouisfed.org/series/FEDFUNDS [https://perma.cc/2GU9-AJHL] (last updated June 1, 2021). Post-2008, the Fed adjusts the interest rate that banks earn on their reserves ("IOR")—an

exposed the limits of the Fed's traditional interest rate policy tools to stymie financial crisis,[63] driving the Fed to think about asset purchases on a large scale as a new kind of emergency crisis-fighting measure.[64] To that end, the Fed (like other central banks) resorted to "unconventional" monetary policy tools[65] such as quantitative easing ("QE").[66] The purpose of QE is to ease market conditions in the moment, and then to generally lower medium- and long-term interest

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administered rate—to "nudge" the market-determined federal funds rate (because, today, the Fed has opted to remain in an "ample" reserve environment thus rendering slightly moot its prior efforts to affect the amount of reserves as a means of influencing the money supply). For an explanation of these frameworks, see generally Jane Ihrig & Scott Wolla, *How Does the Fed Influence Interest Rates Using Its New Tools*, FED. RSRV. BANK OF ST. LOUIS (Aug. 5, 2020), https://www.stlouisfed.org/open-vault/2020/august/how-does-fed-influence-interest-rates-using-new-tools [https://perma.cc/H9ZX-R2CL]. The reader may also be interested to know that the Fed switched from borrowed reserves targets (M1 targeting) to federal funds rate targeting sometime in the 1980s. *See* Daniel L. Thornton, *When Did the FOMC Begin Targeting the Federal Funds Rate? What the Verbatim Transcripts Tell Us* 1–3 (Fed. Rsrv. Bank of St. Louis, Working Paper No. 2004-015, 2005), https://s3.amazonaws.com/real.stlouisfed.org/wp/2004/2004-015.pdf [https://perma.cc/AF7T-SETE].

63. During this period, the Fed dropped interest rates to close to zero in December 2008 (for the first time in decades) but without sufficient effect. BD. OF GOVERNORS OF THE FED. RSRV. SYS., MINUTES OF THE FEDERAL OPEN MARKET COMMITTEE OF DECEMBER 15–16, 2008, at 9 (2008) [hereinafter DECEMBER 15–16, 2008, FOMC MEETING], https://www.federalreserve.gov/monetarypolicy/files/fomcminutes20081216.pdf [https://perma.cc/9SKL-XX5C]; Glenn D. Rudebusch, *A Review of the Fed's Unconventional Monetary Policy*, FED. RSRV. BANK OF S.F. (Dec. 3, 2018), https://www.frbsf.org/economic-research/files/el2018-27.pdf [https://perma.cc/73 GK-5HM7].

64. Christopher J. Waller & Lowell R. Ricketts, *The Rise and (Eventual) Fall in the Fed's Balance Sheet*, REG'L ECONOMIST (Jan. 1, 2014), https://www.stlouisfed.org/publications/regional-economist/january-2014/the-rise-and-eventual-fall-in-the-feds-balance-sheet [https://perma.cc/2V8V-JUST]. Section 14 of the Federal Reserve Act was intended to give Reserve Banks authority to purchase government and agency-sponsored debt in the open market so as to affect the amount of money in circulation, that is, as part of ordinary monetary policy operations. *See* 12 U.S.C. § 353. The global financial crisis was the first time the Fed committed so much of its balance sheet to emergency asset purchases. Waller & Ricketts, *supra* (stating that successive rounds of QE "expanded the Fed balance sheet by close to $3 trillion from December 2007 to November 2013[, a] . . . figure [that] is nearly four times the prerecession average").

65. Rudebusch, *supra* note 63; *see also* Honohan, *supra* note 9 ("To contain the consequences of the crisis, central banks began to rely on a much wider range of tools than had been in recent use.").

66. Together with forward guidance, the Fed adopted QE as an "unconventional" monetary policy to supplement its interest rate moves (which were now, by default, the Fed's "conventional" monetary policy). *See* DECEMBER 15–16, 2008, FOMC MEETING, *supra* note 63. For a summary of how QE, in certain forms, could evolve into activism, see generally *Oral Evidence: Quantitative Easing Before the HL Select Comm. on Econ. Affs.*, 2019–21 (2021) (statement of Christina Parajon Skinner, Assistant Professor of Legal Studies & Business Ethics, The Wharton School of the University of Pennsylvania), https://committees.parliament.uk/oralevidence/2015/pdf [https://perma.cc/LX2B-KEG6].

rates.[67] The Fed also relied on QE in 2020, in response to the COVID-19 pandemic and ensuing market panic.[68] While QE has been billed as "unconventional," nothing in the text of section 14 prohibits the Fed from undertaking this manner of policy.[69]

More recent extensions of 13(3) into certain asset markets may be a grayer area.[70] In March 2020, the Fed relied on that LOLR authority to purchase corporate bonds and corporate bond exchange traded funds ("ETFs").[71] It did not characterize its authority for these bond purchases under section 14 (as QE is done), but rather, as liquidity assistance, under section 13(3).[72]

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67. The Fed expands its balance sheet by buying assets in the open market—in contrast to usual OMOs, however, which target the federal funds rate, and thus the short-term interest rate, *see Open Market Operations*, FED. RSRV. BANK OF N.Y., https://www.newyorkfed.org/aboutthefed/fedpoint/fed32.html [https://perma.cc/5E2T-QG3G], the QE aims to impact the medium-term interest rate, *see* Arvind Krishnamurthy & Annette Vissing-Jorgensen, *The Effects of Quantitative Easing on Interest Rates: Channels and Implications for Policy*, BROOKINGS PAPERS ON ECON. ACTIVITY, Fall 2011, at 215, 215–16 https://www.brookings.edu/wp-content/uploads/2016/07/2011b_bpea_krishnamurthy.pdf [https://perma.cc/H7KD-GPHK].

68. According to a March 2020 press release,

> [t]o support the smooth functioning of markets for Treasury securities and agency mortgage-backed securities that are central to the flow of credit to households and businesses, over coming months the Committee will increase its holdings of Treasury securities by at least $500 billion and its holdings of agency mortgage-backed securities by at least $200 billion.

Press Release, Bd. of Governors of the Fed. Rsrv., Federal Reserve Issues FOMC Statement (Mar. 15, 2020), https://www.federalreserve.gov/newsevents/pressreleases/monetary20200315a.htm [https://perma.cc/KLR4-XUDT]. At a March 15, 2020 press conference, Chair Powell announced that the Fed would commence asset purchases, to complement its other liquidity interventions, in an effort to "support liquidity and return to normal function." He noted that "the asset purchase programs . . . are designed to restore those key markets [Treasury and MBS] to normal function." Jerome Powell, Chairman, Bd. of Governors of the Fed. Rsrv., Press Conference Call (Mar. 15, 2020), https://www.federalreserve.gov/mediacenter/files/FOMCpresconf20200315.pdf [https://perma.cc/E36W-PDJ7].

69. Notably, Section 14 authorizes various kinds of open market operations (with Treasury securities, cable transfers, etc.) as well as discount rate setting *with no regard to end goal*—so "scope of section 14" has nothing to do with monetary policy vs. LOLR, conventional vs. unconventional policies. *See* Federal Reserve Act, Pub. L. No. 63-43, § 14, 38 Stat. 251, 264 (1913) (codified as amended at 12 U.S.C. §§ 353–354, 357).

70. *See* Menand, *supra* note 58, at 300. As some have pointed out, aspects of asset-purchases such as liquidity assistance had some precedent in "the global financial crisis." *See* J. Nellie Liang, *Corporate Bond Market Dysfunction During COVID-19 and Lessons from the Fed's Response* 11 (Hutchins Ctr., Working Paper No. 69, 2020), https://www.brookings.edu/wp-content/uploads/2020/10/WP69-Liang_1.pdf [https://perma.cc/9HH2-5APA].

71. *Secondary Market Corporate Credit Facility*, BD. OF GOVERNORS OF THE FED. RSRV. SYS., https://www.federalreserve.gov/monetarypolicy/smccf.htm [https://perma.cc/RV9J-77J5].

72. *Id.*; *FAQs: Primary Market Corporate Credit Facility and Secondary Market Corporate Credit Facility*, FED. RSRV. BANK OF N.Y., https://www.newyorkfed.org/markets/primary-and-

A section 13(3) justification for asset purchases—for fighting crisis—probably better matches the policy purpose of the Fed's 2020 action than a section 14 justification would have. Nevertheless, that interpretation of section 13(3) may well have expanded its breadth beyond the traditional discounting of "notes, drafts, and bills of exchange" to eligible participants who are "unable to secure adequate credit accommodations from other banking institutions."[73] After all, the text of 13(3) does not expressly authorize the Fed to buy private corporate bonds (or bond ETFs) as these 2020 programs did.[74] The corporate bond facilities depended, it would seem, on an interpretation of 13(3) that presumes equivalence between buying a corporate bond and discounting a note (or some other eligible collateral). And to be fair, such interpretation does square with 13(3)'s original purpose, namely, to provide liquidity assistance to members of the business community. Consequently, while these new actions stretched the text and purpose of 13(3), they did not go out of bounds.

Still, these novel bond facilities may be a ghost of activism yet to come. If bond purchase programs in the future were ever to become too large or too prolonged (that is, if assets are not removed from the central bank balance sheet promptly, with maturities run-off or sold back into the open market), the Fed could slip into a debt monetization

secondary-market-faq/corporate-credit-facility-faq [https://perma.cc/ZL5E-HS8L]. In contrast, the QE undertaken after 2008 involved, for the most part, the purchase of Treasuries and agency mortgaged-backed securities. Krishnamurthy & Vissing-Jorgensen, *supra* note 67, at 215, 217.

73. 12 U.S.C. § 343. To be clear, this Article does not suggest that lending to nonbanks under § 13(3) was a form of activism. Those actions were squarely within the realm of the Fed's authority under that provision.

74. In similar fashion, other 13(3) facilities were stood up to support money markets, commercial paper, and other asset-backed securities. Menand, *supra* note 58, at 310–11, 315–16, 325. Accordingly, somewhat afield from 13(3)'s language aimed at businesses and individuals, 13(3) was deployed in 2020 (as it had also been in 2008) as LOLR for asset classes (corporate bonds was a new, 2020, addition). *See id.* at 326 & n.119. For a fuller discussion of the Fed's authority in 2020 lending facilities, grouping and categorizing the Fed's 2020 lending facilities as authorized or unauthorized, see *id.* at 303–24.

role.[75] (This point holds true for QE programs under section 14 as well.[76])

Debt monetization refers to situations in which newly 'printed' money pays for new government spending.[77] Not surprisingly, central banks are not supposed to do this for reasons relating to inflation and the central bank's independence.[78] To go down such a path would be a return to a bygone era when the Treasury dominated the Fed to precisely such an end. As Fed historian Allan Meltzer wrote, during World War I, "the Treasury's financial demands controlled monetary policy."[79]

A brief reflection on that period is instructive. In 1917, Secretary of the Treasury Carter Glass notified the Federal Reserve that the government wanted to float wartime bonds "at a rate well below the

75. After all, there is no meaningful difference between large-scale "liquidity" purchases continuing into perpetuity (how can there even be a permanent liquidity crisis?) and direct debt monetization. This applies to the purchase of both corporate and Treasury securities. *See* GEORGE SELGIN, THE MENACE OF FISCAL QE 1 n.1 (2020) (using the term "'fiscal QE' to refer to . . . any large-scale central bank asset purchases undertaken not for strictly macroeconomic purposes but for the sake of either propping up particular firms or markets or funding particular government programs"). As Ben Bernanke has described the practice, "[m]onetizing the debt means using money creation as a permanent source of financing for government spending." Ben Bernanke, Chairman, Bd. of Governors of the Fed. Rsrv. Bd., Five Questions About the Federal Reserve and Monetary Policy, Address at the Economic Club of Indiana, Indianapolis (Oct. 1, 2012), https://www.federalreserve.gov/newsevents/speech/bernanke20121001a.htm [https://perma.cc/7D7K-JM95]. For a straightforward explanation of debt monetization, see Ben Holland, *How Long-Feared 'Monetary Finance' Becomes Mainstream: QuickTake*, BLOOMBERG (May 5, 2020, 11:54 AM), https://www.bloomberg.com/news/articles/2020-05-05/how-long-feared-monetary-finance-becomes-mainstream-quicktake [https://perma.cc/9JKJ-YL26].

76. *See generally* ECON. AFFS. COMM., QE: A DANGEROUS ADDICTION? 2021–22, HL 42 (UK) (discussing the risk of debt financing associated with very long—or too prolonged—QE programs).

77. Holland, *supra* note 75.

78. *See* Jose A. Lopez & Kris James Mitchener, *Uncertainty and Hyperinflation: European Inflation Dynamics After World War I*, at 1 (Fed. Rsrv. Bank of S.F., Working Paper No. 2018-06, 2018), https://www.frbsf.org/economic-research/files/wp2018-06.pdf [https://perma.cc/69GQ-KVFX]. Countries that historically used debt monetization—1920s Germany, Austria, Poland, and Hungary, for example—saw severe inflation as a result of those war-financing induced policies. *See id.* at 1–2. The United States also flirted with debt monetization after World War II when it agreed to keep interest rates artificially low to help facilitate the market for U.S. Treasuries. *See* Salib & Skinner, *supra* note 27, at 960–63 (discussing the impact on postwar debt monetization and Fed independence from the Treasury).

79. 1 ALLAN H. MELTZER, A HISTORY OF THE FEDERAL RESERVE: 1913–1951, at 16 (2003).

market."[80] The Fed accommodated the government's wishes by maintaining such favorable financing conditions for bond purchasers.[81] Eventually, the Treasury's financing needs obstructed the Fed's objectives. When the president of the New York Fed, Benjamin Strong, sought to raise interest rates in 1919 to fend off inflation, Treasury Secretary Glass threatened to ask the sitting U.S. president to remove Strong from office.[82]

The Fed was again pressed into a similar position in the run-up to World War II. The Fed agreed to maintain an interest rate peg that would help the government's bond sales, which hamstrung its ability to set monetary policy against inflation.[83] The Fed attributes the subsequent postwar bout of inflation to this money financing arrangement, noting that surging price levels were only reined in after the rate peg was phased out in 1951.[84]

For now, the Fed appears resistant to slipping into monetary finance—the perception as much as the practice.[85] The 13(3) corporate bond facilities have been in runoff mode since December 2020, and the Fed seems committed to soon scaling back (even ceasing) its QE.[86] But

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80. Allan Sproul, *The "Accord"—A Landmark in the First Fifty Years of the Federal Reserve System*, 58 ECON. POL'Y REV. 227, 277 (1964).

81. MELTZER, *supra* note 79, at 102. As Clay J. Anderson notes,

> The Chairman of the Board of Governors stated [that] . . . "Everything else was thrown into the background. The Board necessarily was obliged to follow the policies of the Treasury Department and the Government." . . . The preferential rates were kept in line with the coupon rates on Treasury obligations, usually below the coupon rate on current issues.

CLAY J. ANDERSON, A HALF-CENTURY OF FEDERAL RESERVE POLICYMAKING, 1914–1964, at 11 (1965), https://fraser.stlouisfed.org/files/docs/meltzer/andhal65.pdf [https://perma.cc/L5FJ-XJAV].

82. MELTZER, *supra* note 79, at 102.

83. Memorandum from Radha Chaurushiya & Ken Kuttner to Messrs. Kos & Reinhart on Targeting the Yield Curve: The Experience of the Federal Reserve, 1942–51 (June 18, 2003) [hereinafter Targeting the Yield Curve], https://www.federalreserve.gov/monetarypolicy/files/FOMC20030618memo01.pdf [https://perma.cc/D97E-BBSW].

84. *Id.* at 11.

85. It is not clear that the first three rounds of QE post-2008 were ever intended to be monetary finance; indeed, the Fed committed to balance sheet normalization and took significant steps to do this in 2017. Press Release, Bd. of Governors of the Fed. Rsrv. Sys., FOMC Issues Addendum to the Policy Normalization Principles and Plans (June 14, 2017), https://www.federalreserve.gov/newsevents/pressreleases/monetary20170614c.htm [https://perma.cc/LA3M-EQE4].

86. *See* Jerome H. Powell, Chair, Bd. of Governors of the Fed. Rsrv. Sys., Monetary Policy in the Time of COVID, Address at the Macroeconomic Policy in an Uneven Economy Economic Policy Symposium (Aug. 27, 2021),

so long as popular appetite for monetary finance exists, the Fed remains vulnerable to pressure to restart that long-ago discarded practice.[87] Indeed, such pressure can mount from different quarters: from those who favor Modern Monetary Theory or from markets that become dependent on asset-related interventions.[88]

Asset purchase programs could also, one day, evolve into more activist versions if designed to allocate credit to certain groups (and not others).[89] Credit allocation is generally considered a fiscal, not a monetary, function.

In crafting the Federal Reserve Act in 1913, Congress plainly intended the Treasury to predominate where fiscal or credit matters were concerned. Indeed, out of explicit concern that a newly created Fed would take too much fiscal-type power, the Congress of 1913 added section 10(6) to that Federal Reserve Act. It provides:

> Nothing in this Act contained shall be construed as taking away any powers heretofore vested by law in the Secretary of the Treasury which relate to the supervision, management, and control of the Treasury Department and bureaus under such department, and wherever any power vested by this Act in the Federal Reserve Board or the Federal reserve agent appears *to conflict* with the powers of the

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https://www.federalreserve.gov/newsevents/speech/powell20210827a.htm [https://perma.cc/9LXC-7QWA]; *cf.* Press Release, Bd. of Governors of the Fed. Rsrv. Sys., Federal Reserve Issues FOMC Statement (Jul. 28, 2021), https://www.federalreserve.gov/newsevents/pressreleases/monetary20210728a.htm [https://perma.cc/ H28G-GA5S] (implying that tapering will come in due course).

87. As one observer remarked in May 2020, "the Federal Reserve is buying Treasury debt on a scale that dwarfs 2008 and recalls the monetary-financing arrangements during World War II." Holland, *supra* note 75; *see* Daniel L. Thornton, *Monetizing the Debt*, FED. RSRV. BANK OF ST. LOUIS, at 30, 40–41 (Dec. 1994). Those who espouse Modern Monetary Theory would, for example, favor Fed financing of the deficit. *See* Dylan Matthews, *Modern Monetary Theory, Explained*, VOX (Apr. 16, 2019, 1:00 PM), https://www.vox.com/future-perfect/2019/4/16/18251646/modern-monetary-theory-new-moment-explained [https://perma.cc/QCY8-LDCU].

88. *See* Marvin Goodfriend & Jeffrey M. Lacker, *Limited Commitment and Central Bank Lending*, FED. RSRV. BANK RICHMOND ECON. Q., Fall 1999, at 1, 1–2; *see also* ECON. AFFS. COMM, *supra* note 76, at 23, 47–52 (making this point in regard to QE).

89. As one member of the FOMC remarked in 2008 in regard to QE, "I continue to believe that the FOMC is the appropriate body for making monetary policy decisions and that replacing monetary policy with credit policies that are unconstrained by this Committee is to violate both good governance and the spirit of the operating understanding of the FOMC." DECEMBER 15–16, 2008, FOMC MEETING, *supra* note 63, at 192.

> Secretary of the Treasury, such powers shall be exercised subject to the *supervision and control* of the Secretary.[90]

Here, Congress created a statutory bulwark against Fed incursion into fiscal powers. Fast-forwarding to modern day, Congress also expressed a wish to have the Fed remain out of credit policy when it amended the language of section 13(3) to limit how the Fed could go about "providing liquidity to the financial system."[91] By requiring that all 13(3) assistance have "broad-based eligibility,"[92] Congress explicitly denied the Fed's ability to conduct credit policy using its section 13(3) authority.[93]

In addition to what Congress has said and done, the Fed itself has established informal norms against a credit role. One of the most recent statements to this effect is a 2009 joint press release by the Fed and Treasury titled "The Role of the Federal Reserve in Preserving Financial and Monetary Stability," which included a passage specifically directing the Fed "to avoid credit risk and credit allocation"[94]:

> The Federal Reserve's lender-of-last-resort responsibilities involve lending against collateral, secured to the satisfaction of the responsible Federal Reserve Bank. Actions taken by the Federal Reserve should also aim to improve financial or credit conditions broadly, not to allocate credit to narrowly-defined sectors or classes of borrowers. Government decisions to influence the allocation of credit are the province of the fiscal authorities.[95]

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90. Federal Reserve Act, Pub. L. No. 63-43, § 10, 38 Stat. 251, 261 (1913) (codified as amended at 12 U.S.C. § 246) (emphasis added).

91. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 1101, 124 Stat. 1376, 2113 (2010) (codified at 12 U.S.C. § 343).

92. *Id.*

93. *See* Menand, *supra* note 58, at 300, 326–27. Today, Bagehot's dictum is touted as a rule that differentiates liquidity policy from credit policy—with good security, the Fed will not be exposed to credit risk, and thus cannot be said to be engaging in any kind of credit policy. Admittedly, however, Congress itself muddied these waters by blessing the Fed-Treasury joint ventures in the 2020 liquidity facilities in the CARES Act. I will return to this below. *See infra* notes 138–43 and accompanying text.

94. Press Release, Bd. of Governors of the Fed. Rsrv. Sys. & Dep't of the Treasury, The Role of the Federal Reserve in Preserving Financial and Monetary Stability (Mar. 23, 2009) (emphasis omitted), https://www.federalreserve.gov/newsevents/pressreleases/monetary20090323b.htm [https://perma.cc/GRU8-CSWN].

95. *Id.*

This statement is consistent with the Fed's postwar view that engaging in credit policy would directly conflict with its core mandate. As will be discussed in further depth below, in connection with the Fed's Main Street Lending Facilities, the Fed Board has recognized that financing industry is (or should be seen) to be outside the Fed's core mandate since at least the 1950s.[96] The dispositive question where activism is concerned is thus whether allocation is an "incidental" feature of a Fed program (as appeared to be the case in 2020) or a program's primary aim.[97] Credit allocation, via asset purchases, appears unsupported by the text or purpose of the Federal Reserve Act and likely to skew the ordinary balance of power between the Treasury and the Fed.[98]

Accordingly, while the 2020 asset purchases *qua* liquidity facilities may have flirted with activism, they did not engage in it overtly. Nevertheless, this expansion may have created precedent for increasingly creative (or political) uses of the Fed's balance sheet that more boldly approach the line between the monetary and fiscal

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96. *See infra* notes 134–36 and accompanying text.

97. As economist George Selgin explains, "Although every sort of central bank monetary undertaking has fiscal consequences of some kind, economists typically distinguish between those that have only incidental fiscal consequences and those specifically aimed at supporting particular enterprises, markets, and investments. Only the last undertakings are generally understood to encroach upon 'fiscal' policy." SELGIN, *supra* note 75, at 7. For a thorough treatment of the distinction between credit policy and monetary policy, see generally FED. RSRV. BANK OF BOS., CREDIT ALLOCATION TECHNIQUES AND MONETARY POLICY (1973). In addition, a point of nuance here is required. The above text means to urge that credit policy, driven by the Fed, is inconsistent with the purpose of the Federal Reserve Act—particularly when read against contemporary notions of central bank independence. Section 13(2), and the Reserve Banks' ability to fashion discount window policy, does, strictly speaking, afford those banks some legal room to maneuver credit policy. For a seminal work arguing for a clear distinction between monetary policy and credit policy, see generally Marvin Goodfriend & Robert G. King, *Financial Deregulation, Monetary Policy, and Central Banking*, FED. RSRV. BANK RICHMOND ECON. REV., May/June 1998, at 3.

98. Charles I. Plosser, Fiscal Policy and Monetary Policy: Restoring the Boundaries, Speech at the U.S. Monetary Policy Forum 6 (Feb. 24, 2012) (transcript available at https://fraser.stlouisfed.org/title/statements-speeches-charles-i-plosser-6101/fiscal-policy-monetary-policy-restoring-boundaries-us-monetary-policy-forum-initiative-global-markets-university-chicago-booth-school-business-new-york-586709 [https://perma.cc/WN55-QQ86]) (noting that "[w]hen the Fed engages in targeted credit programs that seek to alter the allocation of credit across markets . . . it is engaging in fiscal policy and has breached the traditional boundaries established between the fiscal authorities and the central bank"). That being said, these 2020 facilities were done in partnership with Treasury, where Treasury provided a sizable amount of equity and took a first loss position in each of these facilities. Menand, *supra* note 58, at 300, 330–32. This point will be returned to in Part III, where this Article offers some normative views on when, if ever, activism is acceptable.

domains.[99] Examples of what crossing over the line might look like, with the Fed's balance sheet and beyond, are considered in Part I.B and I.C. in regard to climate change and inequality.

2. *Foreign Exchange Swaps*. The Fed has some authority in the Federal Reserve Act to lend dollars abroad. Section 14 of the Federal Reserve Act authorizes "cable transfers"—which encompass transactions in foreign exchange[100]—which the Fed has used to justify

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99. It bears noting that in 2020 and 2021, two other leading central banks came under scrutiny as activist for their role in regard to asset purchases and quantitative easing. In Europe, that program is known as the Public Sector Purchase Program ("PSPP"). In May 2020, a German Constitutional Court ruled that the ECB exceeded its monetary policy authority and entered into the arena of economic policy, which the EU treaties reserve for national governments. *See* Adam Tooze, *The Death of the Central Bank Myth*, FOREIGN POL'Y (May 13, 2020, 2:57 PM), https://foreignpolicy.com/2020/05/13/european-central-bank-myth-monetary-policy-german-court-ruling [https://perma.cc/UPA6-8KWU]. The opinion, in German, can be found here, BVerfG, 2 BvR 859/15, May 5, 2020, https://www.bundesverfassungsgericht.de/SharedDocs/Downloads/DE/2020/05/rs20200505_2bvr085915.pdf?__blob=publicationFile&v=4 [https://perma.cc/LPN2-G9QT]. In addition, the Royal Bank of New Zealand ("RBNZ") was also heavily criticized for engaging in QE on the ground that it "herald[ed] a shift into activism, where the institutional distinction between monetary and fiscal policy is degraded." Grant Wilson, Opinion, *RBNZ Puts Its Credibility on the Line*, FIN. REV. (May 31, 2020, 6:26 PM), https://www.afr.com/markets/currencies/rbnz-puts-its-credibility-on-the-line-20200531-p54y3a [https://perma.cc/EH72-2X9E]; *see also* Wilson, *supra* note 26 (describing the negative effect of QE on central banks' credibility).

100. DAVID H. SMALL & JAMES A. CLOUSE, THE SCOPE OF MONETARY POLICY ACTIONS AUTHORIZED UNDER THE FEDERAL RESERVE ACT 26 & n. 55 (2004), https://www.federalreserve.gov/pubs/feds/2004/200440/200440pap.pdf [https://perma.cc/2TV4-VX4M] ("At the time the Federal Reserve Act was passed in 1913, cable transfers were the method by which foreign exchange could be purchased or sold: The purchase of foreign exchange was referred to as the purchase of a cable transfer."); *Credit and Liquidity Programs and the Balance Sheet: Central Bank Liquidity Swaps*, BD. OF GOVERNORS OF THE FED. RSRV. SYS., https://www.federalreserve.gov/monetarypolicy/bst_liquidityswaps.htm [https://perma.cc/6SF4-3K2V]. As Edwin M. Truman explained:

> Federal Reserve power to engage in "cable transfers" was the legal basis in the Federal Reserve Act under which the Federal Reserve had operated in the foreign exchange market in the past. There was a big examination of all this history in the early 1960s with memos and opinions by the Attorney General. In the end, it was concluded that the Federal Reserve did indeed have this authority, which it began to use again to a limited degree in the early 1960s.

FEDERAL RESERVE BOARD ORAL HISTORY PROJECT: INTERVIEW WITH EDWIN M. TRUMAN 106 (2009) [hereinafter INTERVIEW WITH EDWIN M. TRUMAN], https://www.federalreserve.gov/aboutthefed/files/edwin-m-truman-interview-20091130.pdf [https://perma.cc/PR6F-HEDS]. The other possible source of authority is 14(e). *See* Alexander R. Perry, Note, *The Federal Reserve's Questionable Legal Basis for Foreign Central Bank Liquidity Swaps*, 120 COLUM. L. REV. 729, 751–53 (2020).

so-called "swap lines" with foreign countries.[101] Swap lines work by "swapping" dollars for the foreign currency—informally, the dollars are a loan on an article of faith, not meaningfully secured.[102] Swaps are justified as support for the dollar market in a foreign country and thereby protective of the global U.S. dollar markets and, in turn, U.S. consumers and businesses.[103] In particular, the Fed has explained the swaps lines as designed to "help improve liquidity conditions in U.S. dollar funding markets and to prevent the spread of strains to other markets and financial centers."[104] But they sometimes also serve as lifelines to foreign allies.[105] As such, though couched under section 14, these interventions can have a distinctively global LOLR flavor.

Again, some history of the origin of swaps lines provides instructive context for their recent evolution. The Fed's "network of swap lines" with central banks around the world has roots in the Bretton Woods era, when the Fed, at the direction of the Treasury, offered swaps to its foreign counterparts as an alternative to redeeming their excess cash for dwindling U.S. gold stock.[106] Following the

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101. *See* Peter Conti-Brown & David Zaring, *The Foreign Affairs of the Federal Reserve*, 44 J. CORP. L. 665, 692 (2018).

102. *See* Baker, *supra* note 55, at 1389–90. Technically, however, they are not loans, they are foreign exchange swaps or foreign exchange purchases and sales. The Fed's transfer of USD to its foreign central bank counterparty is fully secured by taking possession of an equal amount of the counterparty's home currency. *Id.*

103. As the Fed describes them, they "are designed to improve liquidity conditions in dollar funding markets in the United States and abroad by providing foreign central banks with the capacity to deliver U.S. dollar funding to institutions in their jurisdictions during times of market stress." *Credit and Liquidity Programs and the Balance Sheet: Frequently Asked Questions: U.S. Dollar and Foreign Currency Liquidity Swaps*, BD. OF GOVERNORS OF THE FED. RSRV. SYS. [hereinafter *Credit and Liquidity Programs: FAQs*], https://www.federalreserve.gov/monetarypolicy/bst_swapfaqs.htm [https://perma.cc/ES7P-J3QP].

104. Press Release, Bd. of Governors of the Fed. Rsrv. Sys., FOMC Statement: Federal Reserve, European Central Bank, Bank of Canada, Bank of England, and Swiss National Bank Announce Reestablishment of Temporary U.S. Dollar Liquidity Swap Facilities (May 9, 2010), https://www.federalreserve.gov/newsevents/pressreleases/monetary20100509a.htm [https://perma.cc/9AK6-P8DF].

105. *See* David Zaring, The Government's Economic Response to the COVID Crisis 39 (July 28, 2020) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3662049 [https://perma.cc/5NKT-KSTP]; *see also* Perry, *supra* note 100, at 746 (describing the selective nature of central bank swap lines).

106. Michael D. Bordo, Owen F. Humpage & Anna J. Schwartz, The Evolution of the Federal Reserve Swap Lines Since 1962, at 3–5 (Nat'l Bureau of Econ. Rsch., Working Paper No. 20755, 2014). As Michael Bordo explains,

> The [Bretton Woods] system was a compromise between the fixed exchange rates of the gold standard, seen as conducive to rebuilding the network of global trade and finance, and the greater flexibility to which countries had resorted in the 1930s to

collapse of the Bretton Woods system, however, the Fed began using swap lines on a more ad hoc basis, whenever it was necessary to counter "disorderly market conditions."[107] Notable examples include the U.K. sterling crisis of 1964–67[108] and the Mexican peso crisis of 1994–95.[109]

Historically, the Fed opened swap lines on an emergency-type basis—only when necessary to counter "disorderly market conditions."[110] But in 2007, the Fed began to ramp up its foreign exchange affairs. That year, after the mounting financial crisis put pressures on dollar funding markets around the world, the Fed created two swap lines, with the ECB and the Swiss National Bank..[111] Twelve more—with Japan, the United Kingdom, Canada, Australia, Sweden, Norway, Denmark, New Zealand, Brazil, Mexico, South Korea, and Singapore—followed in late 2008, for a total of fourteen swap lines, with their aggregate value peaking at $583 billion in December of that year.[112]

> restore and maintain domestic economic and financial stability . . . . The compromise created an adjustable peg system based on the US dollar convertible into gold at $35 per ounce along with capital controls.

Michael Bordo, The Operation and Demise of the Bretton Woods System: 1958 to 1971, VoxEU (Apr. 23, 2017), https://voxeu.org/article/operation-and-demise-bretton-woods-system [https://perma.cc/WG3A-A8R2].

107. *Foreign Exchange Operations*, FED. RSRV. BANK OF N.Y., https://www.newyorkfed.org/markets/international-market-operations/foreign-exchange-operations [https://perma.cc/29JM-TSNV]; Bd. of Governors of the Fed. Rsrv. Sys., *Treasury and Federal Reserve Foreign Exchange Operations*, 52 FED. RSRV. BULL. 316–18 (1966) [hereinafter *Foreign Exchange Operations*].

108. Michael D. Bordo, Ronald MacDonald & Michael J. Oliver, *Sterling in Crisis, 1964–1967*, 13 EUR. REV. ECON. HIST. 437, 440–44 (2009).

109. Edwin M. Truman, *The Federal Reserve Engages the World (1970–2000): An Insider's Narrative of the Transition to Managed Floating and Financial Turbulence* 32 (Peterson Inst. for Int'l Econ., Working Paper No. WP-14-5, 2014).

110. *Foreign Exchange Operations*, *supra* note 107. However, as Broaddus and Goodfriend point out, that term has never been defined operationally. J. Alfred Broaddus, Jr. & Marvin Goodfriend, *Foreign Exchange Operations and the Federal Reserve*, FED. RSRV. BANK RICHMOND ECON. Q., Winter 1996, at 1, 9. *See generally* INTERVIEW WITH EDWIN M. TRUMAN, *supra* note 100, at 106, 139, 313 (describing the Fed's limited early use of foreign exchange interventions).

111. *Credit and Liquidity Programs: FAQs*, *supra* note 103; *U.S. Dollar Liquidity Swaps, Supplementary FAQs*, BD. OF GOVERNORS OF THE FED. RSRV. SYS. (Dec. 21, 2010), https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20100510.pdf [https://perma.cc/46YP-WFAU]; Michael J. Fleming & Nicholas J. Klagge, *The Federal Reserve's Foreign Exchange Swap Lines*, FED. RSRV. BANK N.Y. CURRENT ISSUES ECON. & FIN., Apr. 2010, at 1, 3–4.

112. *Id.* at 3–5; Alister Bull, *Top Central Banks Renew Currency Swaps as Precaution*, REUTERS (Dec. 13, 2012, 8:56 AM), http://reut.rs/XgCJFV [https://perma.cc/X49Q-SWCH]; Iñaki Aldasoro, Torsten Ehlers, Patrick McGuire & Goetz von Peter, *Global Banks' Dollar*

Fourteen of the swap lines created during the 2008 financial crisis were retired by early 2010; but five of them—with the Bank of Canada, Bank of England, Bank of Japan, ECB, and Swiss National Bank—were resurrected later that spring, once the Eurozone Crisis created new pressures in dollar funding markets abroad.[113] And after several renewals, the Fed announced in 2013 that these swap lines would be made into a permanent and standing arrangement, billing them as a "prudent liquidity backstop" to "ease strains in financial markets and mitigate their effects on economic conditions."[114]

In 2020, amidst the market fallout of the COVID-19 pandemic, the Fed reopened swap lines with nine of its central bank counterparties from the financial crisis, effectively cementing its global LOLR role.[115] It made $60 billion available to each of the central banks in Australia, Brazil, Korea, Mexico, Singapore, and Sweden; $30 billion was available to Denmark, Norway, and New Zealand.[116] The Fed thus embraced a relatively larger LOLR role during the 2008 global financial crisis and the COVID-19 pandemic than it had practiced before.[117] The expanse of this contemporary support for foreign dollar markets prompted one Fed watcher to prickle: "Why is the Fed sending billions of dollars all over the world?"[118]

Whether swaps are activist central banking policy again depends on the purpose for which they are used. Operations aimed to support the dollar markets are distinct from foreign aid. There is tremendous U.S. interest in the sturdiness of the dollar as the reserve currency of the world. On the other hand, a global LOLR role is not consistent with the text and purpose of section 13(3), which contemplates assistance to

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Funding Needs and Central Bank Swap Lines, BIS BULL. (BIS, Basel, Switzerland), July 16, 2020, at 1, 6.

113. *Id.*

114. Press Release, Bd. of Governors of the Fed. Rsrv. Sys., Federal Reserve and Other Central Banks Convert Temporary Bilateral Liquidity Swap Arrangements to Standing Arrangements (Oct. 31, 2013), https://www.federalreserve.gov/newsevents/pressreleases/monetary20131031a.htm [https://perma.cc/49CQ-NDY3].

115. *Central Bank Swap Arrangements*, FED. RSRV. BANK OF N.Y., https://www.newyorkfed.org/markets/international-market-operations/central-bank-swap-arrangements [https://perma.cc/4XL9-3AKD].

116. *Id.*

117. *See* Conti-Brown & Zaring, *supra* note 101, at 691–92; Zaring, *supra* note 105.

118. Greg Rosalsky, *Why Is the Fed Sending Billions of Dollars All Over the World*, NPR: PLANET MONEY (Apr. 21, 2020, 6:30 AM), https://www.npr.org/sections/money/2020/04/21/839374663/why-is-the-fed-sending-billions-of-dollars-all-over-the-world [https://perma.cc/5SXT-YCZ6].

domestic institutions, not a foreign economy.[119] Swaps used as foreign aid raise structural concerns by inserting the Fed into foreign affairs—a domain reserved for Congress and the president.[120] As Professor David Zaring notes, adopting a global LOLR role "places the Fed in the position of making foreign policy determinations about which foreign central banks to favor and which to disfavor."[121] Those kinds of value and political judgments are more properly for the legislature (or the president).

Optics also matter. The perception that the Fed uses swaps to dispense foreign aid could invite pressure on the Fed to go further. If the Fed appears, at least to some, to select dollar winners and losers around the world, that activity will raise questions in the minds of those concerned about the disparate impact of globalization and the duties attendant to world economic power. Some already suggest that the Fed should be lending more generously to developing market economies, presumably as a means of promoting redistribution from wealthy to poorer nations.[122] Today, the Fed can defend its decisions regarding which central banks to lend to based on the creditworthiness of the borrowing nation and ensuing implications for the U.S. public fisc. But such explanations may carry less weight if and as the Fed lends dollars abroad much more widely, inviting calls upon the Fed to start acting more like a backup IMF.[123] For those that would favor activism, the Fed might seem to assume responsibility for providing all of the dollars that the global economy needs when it needs them.[124]

3. *Small Businesses*. The final example of LOLR expansion involves Congress's decision to involve the Fed in small business ("Main Street") lending in 2020. The economic impact of the COVID-19 pandemic strained not only financial institutions but also businesses and households. But, on their face, the Fed's liquidity assistance tools

119. *See* 12 U.S.C. § 343.

120. *See* Conti-Brown & Zaring, *supra* note 101, at 666.

121. Zaring, *supra* note 105, at 38.

122. *See, e.g.*, Daniel Bradlow & Stephen Park, *A Global Leviathan Emerges: The Federal Reserve, Covid-19, and International Law*, 114 AM. J. INT'L L. 657, 662–65 (2020).

123. *Id.*

124. *See* Barry Eichengreen, George C. Pardee & Helen N. Pardee Professor of Econ. & Pol. Sci. at the Univ. of Cal., Berkeley, Butlin Lecture: It May Be Our Currency, but It's Your Problem 1–2 (Feb. 18, 2011) (transcript available at https://www.ineteconomics.org/uploads/papers/BWpaper_EICHENGREEN_040811.pdf [https://perma.cc/444J-AM2P]).

did not stretch that far—again, 10B is limited to banks[125] and 13(3) to the provision of liquidity to the "financial system" only.[126] Small and medium-sized businesses are not financial firms. To get around these obvious limitations in the Fed's LOLR powers, Congress authorized the Fed in the Coronavirus Aid, Relief, and Economic Security ("CARES") Act to offer assistance to small and medium sized businesses through a (one-time-only?) expanded reading of 13(3).[127] Accordingly, and under 13(3), the Fed created its Main Street Lending Program, which operated through five separate lending facilities.[128] Perhaps not surprisingly, these facilities exposed the Fed to political pressure to assist one sector of the real economy or another.[129]

There is certainly some historical dissonance in the Main Street Lending Program. The Fed, for a time, did have the power to lend to industry under section 13(b) of the Federal Reserve Act.[130] But most historical accounts of 13(b) recognize it as a mistaken attempt to position the Reserve Banks as pseudocommercial lenders during a decades-long confusion about their role within the Federal Reserve System.[131] As David Fettig of the St. Louis Fed explains, this confusion was mostly resolved by 1957.[132] At that point, the then-Fed chair William McChesney Martin had "exorcised most of the demons of Section 13(b)" by informing the Senate Banking and Currency Committee that the Board has eschewed "small business financing" out of

125. 12 U.S.C. § 347b(a).

126. *Id.* § 343.

127. CARES Act, Pub. L. No. 116-136, § 4003(c)(3)(D)(ii), 134 Stat. 470, 474 (2020) (authorizing the Fed to use section 13(3) to establish a "Main Street Lending Program").

128. *Main Street Lending Program*, BD. OF GOVERNORS OF THE FED. RSRV. SYS., https://www.federalreserve.gov/monetarypolicy/mainstreetlending.htm [https://perma.cc/5G7F-NB6L].

129 *See e.g.*, Rachel Siegel, *Congress Needs To Weigh in on Expanding Main Street Loan Program to More Businesses, Boston Fed Chief Says*, WASH. POST (Sept. 8, 2020), https://www.washingtonpost.com/business/2020/09/08/main-street-fed-loans [https://perma.cc/AKN3-PBFD]; Jeanna Smialek, *Oversight Member Blasts the Fed's Efforts To Rescue Main Street*, N.Y. TIMES (Aug. 7, 2020), https://www.nytimes.com/2020/08/07/business/economy/federal-reserve-main-street-lending.html [https://perma.cc/U4GJ-RKD6].

130. *See* HACKLEY, *supra* note 40, at 133.

131. *See, e.g.*, David Fettig, *Lender of More than Last Resort*, FED. RSRV. BANK OF MINNEAPOLIS, (Dec. 1, 2002), https://www.minneapolisfed.org/article/2002/lender-of-more-than-last-resort [https://perma.cc/4BR5-CA8C] (describing Section 13(b) as a "discomfiting" chapter in the history of Federal Reserve policy).

132. *Id.*

> concern . . . from the belief that it is good government as well as good central banking for the Federal Reserve to devote itself primarily to objectives set for it by the Congress, namely, guiding monetary policy and credit policy so as to exert its influence toward maintaining the value of the dollar and fostering orderly economic growth.[133]

Congress removed 13(b) from the Federal Reserve Act the following year.[134] In the pointed words of the late economist Anna J. Schwartz, 13(b) has gone down in history as "a sorry reflection on both Congress's and the Fed's understanding of the System's essential monetary control function."[135]

It seemed unthinkable that industrial lending would come back onto the Fed's lending menu. Indeed, on March 15, 2020, Fed Chair Jerome Powell disavowed a modern role for the Fed in supporting the businesses of the real economy. In a press conference, Powell remarked,

> [W]e don't have the tools to reach individuals and particularly small businesses and other businesses and people who may be out of work . . . . We don't have those tools. . . . [T]his is a multifaceted problem, and it requires answers from different parts of the government and society. . . . I think fiscal policy is a way to direct relief, really, to particular populations and groups. . . . We do think fiscal response[s] [are] critical.[136]

Either oblivious or unconcerned with the history of 13(b), a few days later, Congress put the Fed back into this quasi-fiscal role of allocating credit to non-financial small businesses.[137]

While the congressional authorization in CARES mutes activism concerns, it does not obviate them—it simply demonstrates that legislatures can themselves create the conditions for the Fed to engage

133. *Id.*

134. *Id.*; *see also* HACKLEY, *supra* note 40, at 144–45 (describing how business interest in 13(b) loans "tapered off" as early as 1936, just two years after the authority was created, and did not recover until 13(b) was repealed in 1958). In any case, by that point, the program had become moribund. To browse the archive of William McChesney Martin, see *William McChesney Martin, Jr., Papers*, FRASER, https://fraser.stlouisfed.org/archival-collection/william-mcchesney-martin-jr-papers-1341 [https://perma.cc/VHT6-6HFD].

135. Anna J. Schwartz, Senior Rerseach Fellow, Nat'l Bureau of Econ. Rsch., The Misuse of the Fed's Discount Window, Address at St. Louis University (Apr. 9, 1992), *in* 74 FED. RSRV. BANK ST. LOUIS REV. 58, 61 (1992).

136. Powell, *supra* note 68.

137. *See* CARES Act, Pub. L. No. 116-136, § 4003(c)(3)(D)(ii), 134 Stat. 470, 474 (2020).

in activism.[138] Congress did not, after all, make it clear—even with the CARES Act—that small business lending was an appropriate task for the Fed to do.[139] For one, Congress did not resolve the "unusual and exigent" proviso in section 13(3).[140] So questions of interpretation remain. For instance, does "unusual and exigent" circumstances equal recession-like conditions?[141] Furthermore, section 13(3) requires, in its text, that a borrower demonstrate it cannot obtain adequate financing elsewhere.[142] But the Main Street lending facilities (as revised) appeared to allow a lower standard.[143] Did Congress bless this sub silentio?

Outside of the Main Street facilities, the Fed also supported the real economy indirectly by lending to banks that would provide small business loans—the Fed incentivized the banks to make those loans by agreeing to take the small business loans (which were government-

138. *See* Menand, *supra* note 58, at 351–52 (noting that in sub silentio overriding the Federal Reserve Act, Congress leaves many questions unanswered).

139. The main concerns the Board of Governors harbored about 13(b) throughout the 1950s were that: (1) lending directly to small businesses forced the Fed to work with long-term interest rates and equity-like assets, both of which were far removed from the short-term rates and Treasury bills the Fed has expertise in working with, *see Credit Needs of Small Business: Hearings Before the Subcomm. on Small Bus. of the S. Comm. on Banking and Currency*, 85th Cong. 512 (1957) (statement of William McChesney Martin, Jr., Chairman, Board of Governors of the Federal Reserve System), and (2) lending extensively to the real economy could undermine monetary discipline, creating inflationary pressures, *see* Fettig, *supra* note 131. Congress appeared to concur with these concerns when it repealed 13(b) in 1958 —but when it retasked the Fed with lending to the real economy through the CARES Act, it made no effort to explain why these "demons of 13(b)" were no longer of concern. *Id.* In fact, there was no acknowledgment of this legislative history at all.

140. 12 U.S.C. § 343.

141. *See* Thomas L. Hogan, *Small Business Lending Is Not the Fed's Job*, AM. INST. FOR ECON. RSCH. (Apr. 24, 2020), https://www.aier.org/article/small-business-lending-is-not-the-feds-job [https://perma.cc/Q6T6-83F2] (arguing that construing "unusual and exigent" to mean recession-like conditions would be too broad).

142. 12 U.S.C. § 343.

143. For eligibility requirements, see 13 C.F.R. § 120.111 (2021). The original term sheets for the Main Street Lending Program required eligible borrowers to attest that they "require[d] financing" due to the COVID-19 pandemic, but that requirement was dispensed with in subsequent term sheets. *Compare* Press Release, Bd. of Governors of the Fed. Rsrv. Sys., Term Sheet: Main Street New Loan Facility (Apr. 9, 2020), https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200409a7.pdf [https://perma.cc/4UVA-9QA7] (containing a requirement that applicants attest they need financing due to the COVID-19 pandemic), *with* Press Release, Bd. of Governors of the Fed. Rsrv. Sys., Term Sheet: Main Street New Loan Facility (Apr. 30, 2020), https://www.federalreserve.gov/newsevents/pressreleases/files/monetary20200430a1.pdf [https://perma.cc/H87F-36RT] (containing no such requirement).

guaranteed) as collateral.[144] Though collateral requirements are a grayer area, some may wonder whether stretching collateral eligibility requirements in this way—that is, accepting good collateral but with a clear fiscal policy purpose in view—could be considered activist as well.[145]

On the whole, Congress may have prodded the Fed into activism by vaguely asking the central bank to develop and administer the Main Street Lending Program. Congress instructed the Fed to act beyond its mandate but did not in fact amend or suspend the law in the Federal Reserve Act.[146] As a result, Congress muddied the LOLR waters, thereby setting the stage for future bouts of activism.

B. Inequality

In 1977, Congress added section 2A to the Federal Reserve Act, which confers a so-called dual mandate on the Fed.[147] In particular, 2A requires the Fed to fashion monetary policies that pursue price stability (i.e., guard against inflation[148]) and maximum employment.[149] Starting

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144. Haoyang Liu & Desi Volker, *The Paycheck Protection Program Liquidity Facility (PPPLF)*, LIBERTY ST. ECON. (May 20, 2020), https://libertystreeteconomics.newyorkfed.org/2020/05/the-paycheck-protection-program-liquidity-facility-ppplf.html [https://perma.cc/5T9H-EB74]. The Paycheck Protection Program Liquidity Facility ("PPPLF") was viewed as an important step in supporting the Paycheck Protection Program, administered by the Small Business Administration, given that smaller banks were more likely to reach a broader swath of underserved communities. *Id.* PPPLF involves ensuring that smaller originators can get funding on attractive terms and that there will be a favorable regulatory treatment for the PPP loans. *Id.* It works by allowing financial institutions to borrow money while pledging PPP loans as collateral and giving zero risk weight to any PPP loans pledged to the PPLF. *Id.*

145. *See infra* Part II.B (discussing collateral policy in the 1920s). The Reserve banks have considerable discretion here. *Infra* Part II.B.

146. Menand, *supra* note 58, at 351–53 (arguing that CARES sub silentio overruled section 13(3) of the Federal Reserve Act, but it remains unclear to what permanent effect).

147. 12 U.S.C. § 225a.

148. "Inflation is a general, sustained upward movement of prices for goods and services in an economy. (Think overall prices–not the price of a single good.)." Kristie Engemann, *The Fed's Inflation Target: Why 2 Percent?*, FED. RSRV. BANK OF ST. LOUIS (Jan. 16, 2019), https://www.stlouisfed.org/open-vault/2019/january/fed-inflation-target-2-percent [https://perma.cc/J8HJ-JPU6].

149. 12 U.S.C. § 225a. The Fed is notably distinct among other of the world's leading central banks, most of which have a price stability mandate but not one that regards employment. Simon Dikau & Ulrich Volz, *Central Bank Mandates, Sustainability Objectives and the Promotion of Green Finance*, 184 ECOLOGICAL ECON., Apr. 2021, at 1, 10–14 (reviewing the "mandated objectives" of various central banks). Note that "price stability" or "inflation targeting" is most common, with only a handful of banks also being required to support the economic policy of the government and/or focus on growth or employment. *See id.*

in the mid-1990s, the Fed unofficially pursued a target of 2 percent inflation per year;[150] and that 2 percent target was formalized in 2012.[151] Since the 1990s, the world's leading central banks have built consensus around that 2 percent inflation target.[152]

In 2020, however, the Fed overhauled its monetary policy framework for the first time in more than a decade. In an August 2020 press announcement, Chair Powell announced that the FOMC would no longer target a 2 percent inflation rate, but rather, an *average* inflation rate of 2 percent.[153] The difference may seem subtle, but it is tremendously substantive. It means that the Fed will no longer take steps to cool down economic activity when inflation reaches 2 percent. Instead, the Fed has committed to taking a wait-and-see approach—it will only decide to "liftoff" when the FOMC has also satisfied its employment goals.[154] In essence, this policy of average inflation targeting ("AIT") commits the Fed to keeping "interest rates low for as long as it takes to employ as many people as possible."[155]

As explained by the Fed and on its face, this methodological shift was in the first instance a reaction to real developments in the United

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150. James Bullard, President, Fed. Rsrv. Bank of St. Louis, CFA Society Chicago – Distinguished Speakers Series: What is the Best Strategy for Extending the U.S. Economy's Expansion (Sept. 12, 2018) (presentation slides available at https://www.stlouisfed.org/~/media/Files/PDFs/Bullard/remarks/2018/Bullard_CFA_Chicago_12_Sept_2018.pdf?la=en [https://perma.cc/U6P8-6QTP]).

151. Press Release, Bd. of Governors of the Fed. Rsrv. Sys., Federal Reserve Issues FOMC Statement of Longer-Run Goals and Policy Strategy (Jan. 25, 2012), https://www.federalreserve.gov/newsevents/pressreleases/monetary20120125c.htm [https://perma.cc/ZJ9Q-L4B4] ("The Committee judges that inflation at the rate of 2 percent, as measured by the annual change in the price index for personal consumption expenditures, is most consistent over the longer run with the Federal Reserve's statutory mandate.").

152. *See* John Ammer & Richard Freeman, *Inflation Targeting in the 1990s: The Experiences of New Zealand, Canada, and the United Kingdom*, 47 J. ECON. & BUS. 165, 165–66 (1995).

153. Jerome H. Powell, Chair, Bd. of Governors of the Fed. Rsrv. Sys., New Economic Challenges and the Fed's Monetary Policy Review, Speech at Federal Reserve Bank of Kansas City Economic Policy Symposium (Aug. 27, 2020), https://www.federalreserve.gov/newsevents/speech/powell20200827a.htm [https://perma.cc/5PY4-7MCH].

154. *Id.*; *see also* Richard H. Clarida, Vice Chair, Bd. of Governors of the Fed. Rsrv. Sys., The Federal Reserve's New Framework: Context and Consequences, Speech at the Brookings Institution (Nov. 16, 2020), https://www.federalreserve.gov/newsevents/speech/clarida20201116a.htm [https://perma.cc/YZ6Y-Y9EU] (noting that "at the time of liftoff, in addition to inflation reaching 2 percent (on an annual basis), labor market conditions must have also reached levels consistent with the Committee's assessments of maximum employment").

155. Guida, *supra* note 3.

States and global economies over the past few decades.[156] In view of these economic shifts, the adoption of AIT is best seen as an effort to realign policy in light of these real-world developments. A secondary benefit is that AIT also allows the Fed to avoid socially undesirable distributional impacts associated with tightening prematurely, as it might under a firm 2 percent regime.

However, as with other examples discussed above, this move has left room for activism at points later down the road. AIT is sufficiently open-ended to allow for an offensive targeting of inequality via greater emphasis on the employment arm of the Fed's dual mandate. But Congress did not give the Fed a mandate to use monetary policy to mitigate inequality in section 2A (or elsewhere).

The first time Congress contemplated a federal role in employment was in the Employment Act of 1946.[157] In that piece of legislation, the government committed to the principles of Keynesian economics, which was ascendent in the 1930s and 1940s.[158] Accordingly, in the context of the period, the Employment Act's references to the term "full employment" imported the Keynesian logic that the point of frictional unemployment is also the point of optimal economic growth.[159]

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156. *See* BD. OF GOVERNORS OF THE FED. RSRV. SYS., MONETARY POLICY REPORT TO CONGRESS 40 (2021), https://www.federalreserve.gov/monetarypolicy/files/20210219_mprfullreport.pdf [https://perma.cc/N4YG-K767]; Richard H. Clarida, Vice Chair, Bd. of Governors of the Fed. Rsrv. Sys., U.S. Economic Outlook and Monetary Policy, Speech at the International Economics Council on Foreign Relations (Jan. 8, 2021), https://www.federalreserve.gov/newsevents/speech/clarida20210108a.htm [https://perma.cc/S8D5-D2FG]. The Fed extensively publishes internal documents and models that show optimal monetary policy today—because of highly uncertain estimates of neutral interest rates and sinking inflation expectations (relatively to pre-GFC levels)—is more accommodative than rational agent models would imply. *See, e.g.*, Andrea Ajello, Isabel Cairó, Vasco Cúrdia, Thomas A. Lubik & Albert Queralto, *Monetary Policy Tradeoffs and the Federal Reserve's Dual Mandate* 1–4 (Bd. of Governors of the Fed. Rsrv., Working Paper No. 2020-066, 2020), https://www.federalreserve.gov/econres/feds/files/2020066pap.pdf [https://perma.cc/L6LL-NU2D]. This "make-up" strategy is deemed optimal without taking political considerations into account. *See id.* at 6.

157. Employment Act of 1946, ch. 33, § 2, 60 Stat. 23, 23 (codified as amended at 15 U.S.C. § 1021).

158. *See* RUTH ELLEN WASEM, TACKLING UNEMPLOYMENT: THE LEGISLATIVE DYNAMICS OF THE EMPLOYMENT ACT OF 1946, at 1–45 (2013).

159. *See id.*; *see also* PERRY MEHRLING, THE NEW LOMBARD STREET: HOW THE FED BECAME THE DEALER OF LAST RESORT 52–53 (2011) (discussing the Employment Act). *See generally* J. Bradford De Long, *Keynesianism, Pennsylvania Avenue Style: Some Economic Consequences of the Employment Act of 1946*, 10 J. ECON. PERSP. 41 (1996) (discussing this period generally).

The term "maximum employment" thus considered full employment and economic growth as two sides of the same coin.[160] Eventually, the employment goals of the Employment Act found their way into section 2A of the Federal Reserve Act (by way of the Humphrey Hawkins Act).[161] That employment was a proxy for growth seemed a relatively well-accepted meaning—indeed, so much so that "until recently the [FOMC] had been cautious not to state its policy objectives in terms of either full employment or the unemployment rate, preferring instead to state its dual mandate in terms of price stability and *economic growth*."[162] It thus seems possible to conclude that, since at least 1946, Congress has equated "employment" with "economic growth"—not necessarily equality.[163]

But at least some of the current Fed Governors appear to favor such interpretive slippage. As Fed Governor Lael Brainard explained the 2020 revamp, "[t]he deep and disparate damage caused by the pandemic, coming just over a decade after the financial crisis, underscores the vital importance of full employment, particularly for low- and moderate-income workers and those facing systemic challenges in the labor market."[164] Fed Chair Powell has also made some statements to similar effect:

> With regard to the employment side of our mandate, our revised statement emphasizes that maximum employment is a broad-based and inclusive goal. This change reflects our appreciation for the

160. *See* § 2, 60 Stat. at 23.

161. *See* Full Employment and Balanced Growth Act of 1978, Pub. L. 95-523, 92 Stat. 1887 (1978) (codified at 15 U.S.C. §§ 3101–3152).

162. Daniel L. Thornton, *The Dual Mandate: Has the Fed Changed Its Objective*, 94 FED. RSRV. BANK ST. LOUIS REV. 117, 117 (2012) [hereinafter Thornton, *The Dual Mandate*]; Daniel L. Thornton, *What Does the Change in the FOMC's Statement of Objectives Mean?*, ECON. SYNOPSES (Fed. Rsrv. Bank of St. Louis, St. Louis, M.O.), Jan. 3, 2011, at 1, 2 (noting that between 1978 and 2010, there was virtually no mention of the Fed's "employment" target in any FOMC minutes).

163. *See* Aaron Steelman, *The Federal Reserve's "Dual Mandate": The Evolution of an Idea*, ECON. BRIEF (Fed. Rsrv. Bank of Richmond, Richmond, V.A.), Dec. 2011, at 1, 5 (discussing the dual mandate and its origins).

164. Lael Brainard, Governor, Bd. of Governors of the Fed. Rsrv. Sys., Inaugural Mike McCracken Lecture on Full Employment: Full Employment in the New Monetary Policy Framework (Jan. 13, 2021), https://www.federalreserve.gov/newsevents/speech/brainard20210113a.htm [https://perma.cc/LE45-S558].

> benefits of a strong labor market, particularly for many in low- and moderate-income communities.[165]

Arguably, the Fed would require additional instruction from Congress to equate its employment mandate with a mandate for equality in the way that these remarks could be taken to suggest.

Short of equating employment with equality, the Fed could also reshuffle its priorities, elevating the employment arm of the 2A mandate over the price stability arm. While perhaps not legally prohibited, policy that prioritizes employment over price stability would seem contrary to the overarching purpose of section 2A. To see why, consider the origins of the Fed's price stability mandate in the 1970s and the intellectual paradigms of the day.[166]

During that decade, the theoretical connection between price stability and the aggregate welfare was borne out empirically.[167] The U.S. economy suffered greatly from a period of "stagflation" at that time—that is, years of intractable inflation and very high unemployment.[168] Until that point, economists and policymakers believed that an economy could always dig its way out of an unemployment rut by accepting more inflation. This Keynesian view of the economy theorized that programs of government spending would be likely to reduce the relative value of the dollar but, on the plus side, such programs would also increase labor demand and thus employment.[169] But in practice, it did not work. Eventually, Paul Volcker arrived as Chairman of the Fed in 1979 with a winning strategy

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165. Powell, *supra* note 68. Politico reporter Victoria Guida has put it in less veiled terms: "It's an acknowledgment that rate hikes in previous business cycles, intended to head off inflation, have caused some people to miss out on the benefits of economic growth. Disproportionately, those people have been minorities." Guida, *supra* note 3.

166. The Fed's monetary policy authority hinges on an economic understanding that stable prices maximize utility and in turn social welfare. Prices that vary in sporadic and unpredictable ways would give rise to deadweight losses. Michael Woodford, *Inflation Stabilization and Welfare* 3 (Nat'l Bureau of Econ. Rsch., Working Paper No. 8071, 2001). "A deadweight loss is a cost to society as a whole that is generated by an economically inefficient allocation of resources within the market. Deadweight loss can also be referred to as 'excess burden.'" Prateek Agarwal, *Deadweight Loss*, INTELLIGENT ECONOMIST (Mar. 18, 2020), https://www.intelligenteconomist.com/deadweight-loss [https://perma.cc/ZM5F-QKTC].

167. This Article returns to lessons from the 1970s *infra* Part II.C.

168. *See* BRIAN W. CASHELL & MARC LABONTE, CONG. RSCH. SERV., RL34428, UNDERSTANDING STAGFLATION AND THE RISK OF ITS RECURRENCE 1–5 (2008).

169. For a short primer on Keynes, see Sarwat Jahan, Ahmed Saber Mahmud & Chris Papageorgiou, *What Is Keynesian Economics*, FIN. & DEV., Sept. 2014, at 53, 54, https://www.imf.org/external/pubs/ft/fandd/2014/09/pdf/basics.pdf [https://perma.cc/4BGN-KF2C].

for beating stagflation—getting inflation in check without worrying about employment.[170]

The Volcker Fed adopted a price-stability-first policy.[171] This was not because unemployment was not concerning, but rather, as economists had come to realize, employment could not be increased without price stability. As Volcker explained before becoming Chair,

> I don't think that we have the choice in current circumstances—the old tradeoff analysis—of buying full employment with a little more inflation. We found out that doesn't work, and we are in an economic situation in which we can't achieve either of those objectives immediately. We have to work toward both of them; we have to deal with inflation.[172]

In a similar vein, Volcker reported to Congress that:

> I do not want to suggest or claim other factors are not relevant in the inflationary process, but I do believe that moderation in monetary growth is a necessary condition for the restoration of reasonable price stability, and that progress in that direction, far from conflicting with growth and employment goals, will over time prove a prerequisite to continued and orderly growth. Put another way, I think the experience of recent years strongly suggests that a resurgence of inflationary pressures would be damaging to our employment goals and to the purpose of sustaining the expansion.[173]

Ultimately, the Volcker Fed was correct on the merits. With considerable tightening of interest rates, the "Great Inflation" of that era eventually came under the Fed's control.[174] To avoid future economic "disarray," the Fed continued to be disciplined about inflation targeting[175] (until August 2020).

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170. *See* Thornton, *The Dual Mandate*, *supra* note 162, at 128.

171. *See id.*

172. Steelman, *supra* note 163, at 3.

173. *Federal Reserve Reform Act of 1977: Hearing on H.R. 8094 Before the H. Comm. on Banking, Fin. & Urban Affs.*, 95th Cong. 90 (1977) (statement of Paul Volcker, Chair, Federal Reserve).

174. William Poole, *President's Message: Volcker's Handling of the Great Inflation Taught Us Much*, FED. RSRV. BANK OF ST. LOUIS (Jan. 1, 2005), https://www.stlouisfed.org/publications/regional-economist/january-2005/volckers-handling-of-the-great-inflation-taught-us-much [https://perma.cc/QU38-T5YB].

175. *See* Marvin Goodfriend, *How the World Achieved Consensus on Monetary Policy* 24–25 (Nat'l Bureau of Econ. Rsch., Working Paper No. 13580, 2007), https://www.nber.org/system/files/working_papers/w13580/w13580.pdf [https://perma.cc/EUU8-S5S9]; Adam Shapiro

Against this background and history, one can see why elevating the employment side of the mandate—in this case, to strive for more equality—would divorce the economic logic behind the Fed's monetary authority from the legal power in section 2A, with potentially problematic macroeconomic effect.

Now, to be sure, the global economy has changed significantly since the Volcker days. Among these changes, neutral interest rates have declined and the Phillips curve—which assumes a tradeoff between inflation and employment—seems flatter.[176] But those economic shifts do not necessarily mean monetary policy can or should let the rope slip on inflation. An expansive monetary policy—driven forward by efforts to reduce inequality by pressing too hard on employment—could usher in a period of inflation reminiscent of the 1970s or the postwar periods. This prediction will become more likely if and as the government's budget deficit grows.[177]

As with other forms of activism, there would be larger structural costs were the Fed to use its new framework to proactively pursue equality. For one, by interpreting section 2A in this way, the Fed would be making a value judgment—society should accept higher inflation (less stable prices) in favor of more employment.[178] But, as will be

& Daniel J. Wilson, *The Evolution of the FOMC's Explicit Inflation Target*, FRBSF ECON. LETTER (Fed. Rsrv. Bank of S.F., San Francisco, C.A.), Apr. 15, 2019, at 1, 1–3, https://www.frbsf.org/economic-research/files/el2019-12.pdf [https://perma.cc/YS53-EE4U].

176. *See* Kristie Engemann, *What Is the Phillips Curve (and Why Has It Flattened)?*, OPEN VAULT BLOG (Jan. 15, 2020), https://www.stlouisfed.org/open-vault/2020/january/what-is-phillips-curve-why-flattened [https://perma.cc/R5X6-MX9G].

177. *See* Kate Davidson, *U.S. Ran Record $1.9 Trillion Budget Deficit in First Seven Months of Fiscal Year*, WALL ST. J. (May 12, 2021, 2:17 PM), https://www.wsj.com/articles/u-s-ran-record-1-9-trillion-budget-deficit-in-first-seven-months-of-fiscal-year-11620842400 [https://perma.cc/47PC-BK5W]; Anita Kumar, *Biden Begins Selling His $4T Spending Plans*, POLITICO (Apr. 29, 2021, 7:34 PM), https://politi.co/2SgguZN [https://perma.cc/9G84-CY5V]; CONG. BUDGET OFF., THE 2021 LONG-TERM BUDGET OUTLOOK 5 (2021) (estimating that at this rate, debt-to-GDP ratio will exceed 200 percent by 2051). Modern monetary theorists ("MMT") essentially believe that government spending is benign and should be used toward progressive ends. *See* Alex J. Pollock, *Inflation Comes for the Profligate*, LAW & LIBERTY (Mar. 2, 2021), https://lawliberty.org/inflation-comes-for-the-profligate [https://perma.cc/3KC4-DZYR]. As one writer noted, "[s]ounding the alarm about inflation is out of vogue." Michael D. Bordo & Mickey D. Levy, *The Short March Back to Inflation*, WALL ST. J. (Feb. 3, 2021, 2:17 PM), https://www.wsj.com/articles/the-short-march-back-to-inflation-11612378471 [https://perma.cc/NM6U-VBWR].

178. This statement is premised on a non-vertical long-run Phillips curve. It remains to be seen whether the Phillips curve is permanently or temporarily flattened. *See* Olivier Blanchard, *Should We Reject the Natural Rate Hypothesis?* 2, 15 (Peterson Inst. for Int'l Econ., Working Paper No. 17-14, 2017), https://www.piie.com/system/files/documents/wp17-14.pdf

discussed in full below, that should be Congress's decision. Moreover, to the extent the Fed were to shoehorn inequality into "employment," it may appear a reaction to political, popular, and international pressure.

Yet when the Fed appears malleable to pressure, it opens the door to future trade-offs for political gain. A Fed that is tied to a 2 percent mast maintains a valuable political economy buffer—self-constrained as such, the Fed had principled grounds for resisting presidential pressure to, for example, run a 'hot' economy at the expense of price stability.[179] By unmooring itself from the 2 percent anchor, the Fed may invite such pressure going forward and weaken its defenses against politics.

C. Climate Change

The final case study of contemporary activism looks into 2021 and beyond in regard to climate change.[180] In recent years, central banks worldwide have begun to consider how their array of monetary policy, regulatory, and supervisory tools might be expanded to mitigate climate change.

In broad strokes, the movement endorses a variety of policy measures geared toward making the economy greener. In regard to monetary policy, for example, some central banks now consider whether a green version of quantitative easing could be adopted, whereby central banks commit to buying "green bonds"—not for purposes of mitigating economic crisis—but instead for the purpose of facilitating more green business.[181] Other policy suggestions involve

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[https://perma.cc/5BTR-E25F] (explaining the natural rate hypothesis and suggesting that the long-run Phillips curve could be sloped).

179. *See* Salib & Skinner, *supra* note 27, at 960–68 (discussing those presidents that did inappropriately lean on Fed Chairs to inflate the economy in order to gain political popularity associated with a strong economy); *see also* Allan H. Meltzer, *Origins of the Great Inflation*, 87 FED. RSRV. BANK ST. LOUIS REV. 145, 145–75 ("Politicians elected for four- or five-year terms put much more weight on employment—jobs, jobs, jobs—than on a future inflation.").

180. For a comprehensive account of the Fed's legal power to address climate change, see generally Skinner, *supra* note 5.

181. *See, e.g.*, Press Release, Bank for Int'l Settlements, BIS Launches Second Green Bond Fund for Central Banks (Jan. 25, 2021), https://www.bis.org/press/p210125.htm [https://perma.cc/4F6S-VJFY]; Emanuele Campiglio, Yannis Dafermos, Pierre Monnin, Josh Ryan-Collins, Guido Schotten & Misa Tanaka, *Climate Change Challenges for Central Banks and Financial Regulators*, 8 NATURE CLIMATE CHANGE 462, 465 (2018); Benoît Cœuré, Member of the Exec. Bd. of the Eur. Cent. Bank, The Role of Central Banks: Monetary Policy and Climate

using regulation and supervision to deter banks from lending to "brown" business while incentivizing them to lend to green ones.[182] Prominent ideas for this kind of regulation include increasing risk-based capital requirements in regards to certain kinds of nongreen loans, thereby disincentivizing their origination.[183] Informally, supervisory priorities and pronouncements could accomplish similar effects.[184]

Numerous central banks are moving in such direction.[185] For the most part, central bankers have framed the climate conversation in stark, but not necessarily legal, terms. As Jen Weidmann, Chair of the Board of Directors for the Bank for International Settlements, remarked in January 2021, "climate change presents a challenge for all humanity. . . . Therefore, every institution is right to ask itself what contribution it can make to mitigating climate change within the remit

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Change, Speech at the Conference on Scaling Up Green Finance 1, 6 (Nov. 8, 2018) (transcript available at https://www.bis.org/review/r181109f.pdf [https://perma.cc/2ULV-S2MW]).

182. *See* Skinner, *supra* note 5, at 1301, 1340–41, 1344–47 (describing these ideas in depth); *see also* GRAHAM STEELE, THE GREAT DEMOCRACY INITIATIVE, A REGULATORY GREEN LIGHT: HOW DODD-FRANK CAN ADDRESS WALL STREET'S ROLE IN THE CLIMATE CRISIS 14–20 (2020); Conny Olovsson, *Is Climate Change Relevant for Central Banks*, ECON. COMMENTS. (Sveriges Riksbank, Stockholm, Sweden), Nov. 14, 2018, at 1, 5–6.

183. Skinner, *supra* note 5, at 1301. When regulators increase capital requirements for a certain kind of loan, it tends to disincentivize such lending relative to other kinds of assets. DOUGLAS J. ELLIOTT, THE BROOKINGS INST., QUANTIFYING THE EFFECTS ON LENDING OF INCREASED CAPITAL REQUIREMENTS 1 (2009), https://www.brookings.edu/wp-content/uploads/2016/06/0924_capital_elliott.pdf [https://perma.cc/6V7F-2KPJ]. It is well understood that increases in capital requirements have an inverse relationship to lending because higher capital requirements "make it harder for businesses and individuals to obtain loans, raise the cost of loans, lower the interest rates offered to depositors and other suppliers of funds, and reduce the market value of the common stock of existing banks." *Id.* This empirical observation motivated the now-famous Modigliani-Miller theorem. Franco Modigliani & Merton H. Miller, *The Cost of Capital, Corporation Finance and the Theory of Investment*, 48 AM. ECON. REV. 261, 288 (1958) (positing that corporations should be indifferent between funding themselves with debt versus equity under certain conditions); *see also* Harry DeAngelo & Rene M. Stulz, *Liquid-Claim Production, Risk Management, and Bank Capital Structure: Why High Leverage Is Optimal for Banks* 5 (Fisher Coll. of Bus., Working Paper No. 2013-03-08, 2014), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2254998 [https://perma.cc/R4EP-SUCZ] (discussing the reasons why it is more efficient for a bank to finance its credit investments (i.e., loans) with debt than equity).

184. *See, e.g.*, Skinner, *supra* note 5, at 1337–41; STEELE, *supra* note 182, at 16–17.

185. *See, e.g.*, NETWORK FOR GREENING THE FIN. SYS., A CALL FOR ACTION: CLIMATE CHANGE AS A SOURCE OF FINANCIAL RISK 13–17 (2019), https://www.ngfs.net/sites/default/files/medias/documents/ngfs_first_comprehensive_report_-_17042019_0.pdf [https://perma.cc/HV89-U2JR]; *Climate Change*, BANK OF ENG., https://www.bankofengland.co.uk/climate-change [https://perma.cc/T6FP-D9N9]; *Climate Change and the ECB*, EUR. CENT. BANK, https://www.ecb.europa.eu/ecb/orga/climate/html/index.en.html [https://perma.cc/VY5K-L6P9].

of its mandate."[186] Awash in pressure to do something about the climate, the Fed has also taken early steps. First, in a November 2020 financial stability report, it indicated that climate change could be a financial stability risk, thus opening the door to a certain set of policy tools in a fight against climate change.[187] Then, in December 2020, the Fed joined the Network for Greening the Financial System ("NGFS")—a group of central bankers and bank supervisors that are committed to using central banking tools to mitigate climate change—a group the Fed had abstained from for several years.[188]

For the Fed, most climate initiatives sit well outside its mandate and would therefore require activist central banking.[189] Consider monetary policy first. Green QE is most assuredly outside the Fed's section 2A power.[190] A program of non-crisis-era asset purchases, like green QE would be, necessarily would fall to section 14 of the Federal Reserve Act, which provides authority for open-market operations in normal times.[191] But section 14 does not expressly allow for purchasing private corporate bonds of any kind, including those that are green.[192] While corporate bond purchases might skate through section 13(3) on a crisis basis, it is another matter altogether to use section 14 as a hook for making finance greener.[193] Notably, unlike the ECB and the Bank of England, the Fed does not have a secondary mandate in its constitutive statute that directs the central bank to have regard to the

186. Jens Weidmann, President of the Deutsche Bundesbank and Chair of the Bd. of Dirs. of the Bank for Int'l Settlements, What Role Should Central Banks Play in Combating Climate Change, Remarks at the ILF Online-Conference 1 (Jan. 25, 2021) (transcript available at https://www.bis.org/review/r210128a.pdf [https://perma.cc/AM99-Q69X]).

187. BD. OF GOVERNORS OF THE FED. RSRV. SYS., FINANCIAL STABILITY REPORT: NOVEMBER 2020, at 58–59 (2020), https://www.federalreserve.gov/publications/files/financial-stability-report-20201109.pdf [https://perma.cc/5XYE-KN2R] (implicating that climate change may pose financial stability risks).

188. Press Release, Bd. of Governors of the Fed. Rsrv. Sys., Federal Reserve Board Announces It Has Formally Joined the Network for Greening the Financial System, or NGFS, as a Member (Dec. 15, 2020), https://www.federalreserve.gov/newsevents/pressreleases/bcreg20201215a.htm [https://perma.cc/9WK6-VDV5].

189. *See* Skinner, *supra* note 5, at 1353–54.

190. 12 U.S.C. § 225a.

191. *Id.* § 353.

192. That provision provides a list of the debt securities that the Fed "shall have power" to buy. *Id.* § 354. It includes gold, Treasury bonds, bonds guaranteed by a government agency (i.e., MBS from the GSEs), municipal bonds, and bonds issued by the now-defunct Home Owners' Loan Corporation. *Id.*

193. The justification being that the bond purchases are necessary to ease credit conditions after a financial crisis. *See* Skinner, *supra* note 5, at 1330–31.

environmental goals of the government.[194] The Fed lacks such political cover.

Regulatory efforts to deter "brown" lending would also smack of activism.[195] Risk weights must be tied to concrete, verifiable, objective evidence that a particular asset class is truly riskier than another.[196] By that measure, safe assets (like cash and Treasury securities) carry a zero risk-weight, while a junk bond (lower than BBB) would receive a risk weight of 75 to 100 percent.[197] But much is still uncertain about the physical and transition risks associated with climate change, such that accurately specifying what incrementally higher risk-weight would be appropriate for "brown assets" (relative to others) seems beyond the Fed's present expertise.[198] Moreover, and perhaps more importantly, the legislative purpose of capital requirements is to safeguard the solvency of a bank.[199] But today, banks' exposure to carbon-intensive industries is a small—and steadily decreasing—aspect of their balance sheets.[200] As an accounting matter, it appears unlikely that any of the large banks could fail as a result of their carbon-rich loans gone sour—

194. *See* Consolidated Version of the Treaty on the Functioning of the European Union, art. 127, Oct. 26, 2012, 2012 O.J. (C326) 102; Bank of England Act 1998, c.11 §§ 2A, 9E (UK).

195. The Fed has legal authority under various pieces of banking legislation—most recently, the Dodd-Frank Act of 2010—to establish set capital requirements for the bank holding companies that it oversees. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 171, 124 Stat. 1376, 1435–39 (2010); *see* Joseph G. Haubrich, *A Brief History of Bank Capital Requirements in the United States*, ECON. COMMENT. (Fed. Rsrv. Bank of Cleveland, Cleveland, O.H.), Feb. 28, 2020, at 1, 4–5. Still, this may reflect more practice than law.

196. *See* IRB Approach: Overview and Asset Class Definitions Chapter of Calculation of RWA for Credit Risk, BIS, https://www.bis.org/basel_framework/chapter/CRE/31.htm [https://perma.cc/3RQD-BM4H] (summarizing how risk weight formulas work with data points like probability of default, loss-given-default, and exposure at default).

197. *U.S. Basel III Final Rule: Standardized Risk Weights Tool*, DAVIS POLK (2016), http://usbaseliii.com/tool/index.html [https://perma.cc/NUF5-DXJ3] (showing a 0 percent risk weight when a viewer clicks on "[e]xposures to, and portions of exposures that are directly and unconditionally guaranteed by, the U.S. government, its agencies and the Federal Reserve"); *Basel III: Post Crisis Reforms*, DELOITTE, https://www2.deloitte.com/content/dam/Deloitte/my/Documents/risk/my-ra-basel-iv-placemat.pdf [https://perma.cc/R3N5-5G45] (demonstrating a risk weight of 75 percent for bonds ranked BBB+ to BBB-, and risk weights of 100 percent or more for bonds ranked BB+ and below).

198. For a collection of Fed papers on climate and uncertainty, see Douglas Clement, *Uncertainty, Asset Prices, and Policy: Brief Reviews of Seven Conference Papers*, FED. RSRV. BANK OF MINNEAPOLIS (Jan. 9, 2019), https://www.minneapolisfed.org/article/2019/uncertainty-asset-prices-and-policy [https://perma.cc/T7H8-V5EL].

199. *See* Bank Holding Company Act 1956, 12 U.S.C. § 1844(c)(2)(A) (grounding capital requirements in goals of bank safety and soundness).

200. Skinner, *supra* note 5, at 1318–19.

an examination of bank financials shows that even if 100 percent of big U.S. banks' wholesale loan exposure to automatable and oil and gas companies failed, these institutions' tier 1 equity capital would be three to four times more than necessary to absorb those cumulative losses.[201]

Without sufficient grounding in financial risk, the use of regulation to deter banks from lending to certain kinds of business would be an activist move for the Fed to make. And it would appear political.[202] Without clear evidence that climate change will impact financial assets in ways that banks are unable to withstand, new climate-related regulation would force the Fed to make subjective value judgments about which industries and companies should win or lose in the new green versus brown equation. Again, such value judgments are for the political branches, and especially for Congress.

Finally, what of supervision? Fed supervision has always been flexible, discretion bound, and woolly.[203] General language surrounding a bank's "safety and soundness" provides the basis for most microprudential supervision of bank balance sheets, governance, and operations.[204] Meanwhile, general references to "financial stability" and "systemic risk" in Titles I and II of the Dodd-Frank Act (combined with the Fed's historic role as LOLR) are thought to provide an implied mandate to the Fed to mind the financial stability of the system as a whole (and thus to engage in macroprudential forms

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201. For a collection of this data, see *id.* at 18. As I acknowledge in this related work, "[o]f course, in all things, there is a possibility of Knightian uncertainty: the unknown unknown; or, as Mervyn King and John Kay refer to it, 'radical uncertainty.'" *Id.* at 21 n.92 (quoting JOHN KAY & MERVYN KING, RADICAL UNCERTAINTY (2020)).

202. Notably, when the Office of the Comptroller of the Currency ("OCC") passed a final rule prohibiting banks from categorically declining credit to certain industries, without a risk-based assessment, in January 2021, there was significant public outcry concerning the interference of the OCC in banks' decision-making process. *See* OCC Fair Access to Financial Services, 12 C.F.R. Part 55 (2020); *see, e.g.*, Jesse Hamilton, *Banks Blast Rule That Would Force Lending to Oil, Gun Firms*, BLOOMBERG (Jan. 5, 2021, 11:43 AM) https://www.bloomberg.com/news/articles/2021-01-05/banks-blast-u-s-rule-that-would-force-lending-to-oil-gun-firms [https://perma.cc/J9MH-XPEW].

203. *See Guidance, Supervisory Expectations, and the Rule of Law: How Do the Banking Agencies Regulate and Supervise Institutions? Hearing on Examining How Banking Agencies Supervise and Regulate Financial Institutions, How Regulated Institutions Interact with Their Regulators, and the Congressional Review Act and the Scope of Its Applicability to Agency Statements of Policy Before the S. Comm. on Banking, Hous., and Urb. Affs.*, 116th Cong. 4 (2019) [hereinafter *Tahyar Testimony*] (statement of Margaret E. Tahyar). The word "supervision" does, however, appear in the preamble to the Fed. Federal Reserve Act, Pub. L. No. 63-43, 38 Stat. 251, 251 (1913).

204. *See* 12 U.S.C. § 1844(c)(2)(A).

of banking system supervision).[205] It is an open secret among Fed experts and lawyers that these statutes, so broadly worded, give the Fed considerable latitude to exercise its judgment as to whether any given bank activity or investment will implicate its 'safety and soundness' or 'financial stability' overall.

Thus, the risk of supervisory activism toward climate change exists. While supervision may properly monitor credit risk and the banks' efforts to adapt to emerging climate risks,[206] it also has potential to mask efforts to deter politically unpopular kinds of loans through the use of informal supervisory scolding or "Dear CEO" letters that can punish or intimidate.[207] Going forward, to avoid a charge of activism, the Fed will have some burden of showing that its supervision of climate-related risks is narrowly tailored to the risk at hand—and not an exercise in partisan or politically driven sorting.

* * *

By this point, this Article has sketched the landscape of central bank activism in its various forms. These three case studies of contemporary and potential Fed activism have suggested some indicia of the phenomenon. In its hallmark trait, activism features a disconnect between the statutory power (in text and purpose) and a novel application of the power. In addition to that disconnect, activism upsets some structural dynamic, either by:

(1) a reallocating power between the Fed, Congress, and the executive branch (i.e., the Treasury);

(2) creating openings for political pressure going forward; or

(3) assuming value-judgment-making that is otherwise reserved for elected officials in the political branches.

The next Part builds on this descriptive analysis by situating contemporary central bank activism in historical context.

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205. *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, §§ 111, 203, 124 Stat. 1376, 1392, 1450 (2010) (codified at 12 U.S.C. §§ 5301, 5321, 5383).

206. *See* Letter from Jerome H. Powell, Chair, Bd. of Governors of the Fed. Reserve Sys., to Brian Schatz (Apr. 18, 2019), https://www.schatz.senate.gov/imo/media/doc/Chair%20Powell%20to%20Sen.%20Schatz%204.18.19.pdf [https://perma.cc/MJT5-XQAV] (conceding that the Fed supervises all manner of credit risk, including climate risk).

207. *See Tahyar Testimony*, *supra* note 204, at 13 (noting the power of suasion supervisors have over banks).

II. CENTRAL BANK ACTIVISM IN U.S. HISTORY

As central bank activism looms, lessons once learned from past episodes of political and monetary activism are now dulled or wholly forgotten. Revisited, these stories caution against the revival of activist policies or structures today. This Part considers several significant cases of central bank activism that transpired between America's Founding and 2010, dusting off their lessons. Accordingly, whereas the cases in Part I allowed us to induce some indicia of central bank activism—what might it look like today?—the historical cases in Part II provide some further color on the economic and political consequences of, and conditions conducive to, activist institutional behavior.

A. First and Second Banks of the United States

Alexander Hamilton was the first to experiment with central banking in the United States.[208] The United States had significant economic problems immediately after winning the Revolutionary War. The first leaders of the nation were faced with a slew of financial problems such as "re-establishing commerce and industry, repaying war debt, restoring the value of the currency, and lowering inflation."[209]

Inspired by the Bank of England, Hamilton made a proposal to Congress for a national bank.[210] Like other public or proto central banks of the era, the national bank Hamilton envisioned would be an institution to support public finance—it would "issue paper money," provide a place to store money, "act as the government's fiscal agent," and "offer banking facilities for commercial parties."[211] But it would also have private elements.[212] Congress chartered the Bank of North America in 1781 (justified as a war exigency)[213]—and Hamilton

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208. FED. RSRV. BANK PHILA., THE FIRST BANK OF THE UNITED STATES: A CHAPTER IN THE HISTORY OF CENTRAL BANKING 1 (2021), https://www.philadelphiafed.org/-/media/frbp/assets/institutional/education/publications/the-first-bank-of-the-united-states.pdf [https://perma.cc/53NX-UF3N].

209. *Id.* at 1.

210. *Id.* at 2.

211. *Id.*

212. *Id.*

213. H. Wayne Morgan, *The Origins and Establishment of the First Bank of the United States*, 30 BUS. HIST. REV. 472, 476 (1956). Hamilton billed the bank as a war measure, writing to the new Superintendent of Finance, Robert Morris, that

declared it to be "the best expedient" for the national cause.[214] This bank, however, ran into legal problems involving the legitimacy of its charter and was reduced to a local Pennsylvania bank by 1790.[215]

Once appointed Secretary of the Treasury in 1789, Hamilton realized his dream for a full-fledged national bank—which, in his view, was a "necessary auxiliary . . . [and] indispensable engine in the administration of finances."[216] Hamilton's plan clearly envisioned the Bank of the United States to be a public finance institution, along the lines of contemporaneous central banks. Historian Paul Kahan refers to a letter written by then-Secretary of the Treasury Alexander J. Dallas in 1815. The letter, though referring to the Second Bank of the United States, "capture[d] the essence of Hamilton's vision" for these public finance institutions.[217] In particular, the Bank of the United States

> ought not to be regarded as a commercial bank. It will not operate upon the funds of the stockholders alone, but much more upon the funds of the nation. Its conduct, good or bad, will not affect corporate

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> [a]ll we have to fear is that want of money may disband the army, or . . . create in the people a general disgust and alarm . . . But if a judicious administration of our finances, assisted by a bank takes place . . . no convulsion is to be apprehended . . . . Tis by introducing order into our finances . . . not by gaining battles, that we are finally to gain our object[, independence].

Letter from Alexander Hamilton to Robert Morris (Apr. 30, 1781), *in* THE PAPERS OF ALEXANDER HAMILTON 1757–1804 (Harold C. Syrett ed., 1961). Notably, appeals to the exigencies of war were also made by Congress in connection with the National Bank Acts of 1863 and 1864 which would establish a national banking system for the express purpose of maintaining a stable currency and bolstering civic confidence in that currency. *See* John Wilson Million, *The Debate on the National Bank Act of 1863*, 2 J. POL. ECON. 251, 256–58, 279–80 (1894). But by that time, the First (and Second) Banks of the United States ceased to exist (they had not been rechartered after their terms expired), *id.* at 262, and the U.S. Federal Reserve System had not yet been created. So, in this intervening period, Congress turned to private banks to play this role. *See id.* at 270. As scholars of the era have remarked, viewing the national banking system as created to aid the nation in combatting this emergency puts the National Banking Act in its "proper historical bearing." *Id.* at 258; *see also Founding of the OCC & the National Banking System*, OFF. OF THE COMPTROLLER OF THE CURRENCY, https://www.occ.treas.gov/about/who-we-are/history/founding-occ-national-bank-system/index-founding-occ-national-banking-system.html [https://perma.cc/FXD2-ZSZ3].

214. DAVID COWEN & RICHARD SYLLA, ALEXANDER HAMILTON ON FINANCE, CREDIT, AND DEBT 53 (2018).

215. *See* JOHN JAY KNOX, A HISTORY OF BANKING IN THE UNITED STATES 31–32 (1900).

216. COWEN & SYLLA, *supra* note 214, at 116; *see* Joseph H. Sommer, *The Birth of the American Business Corporation: Of Banks, Corporate Governance, and Social Responsibility*, 49 BUFF. L. REV. 1011, 1076–88 (2001) (discussing how the national bank facilitated the creation of the American corporation).

217. PAUL KAHAN, THE BANK WAR 7 (2016).

> credit alone, but must much more the credit and resources of the government. In fine, it is not an institution created for the purposes of commerce and profit alone, but much more for the purposes of national policy, as an auxiliary in the exercise of some of the highest powers in government.[218]

In his *Report On A National Bank*, Hamilton explained the role he envisioned for the Bank. For one, the Bank would control the money supply—in his view, the federal government—"of a nature so liable to abuse"—should not have the power to issue money.[219] Rather, a national bank would have the prudence that was necessary for adequate restraint.[220] The Bank would also play some fiscal roles and support the government. It would act as the government's fiscal agent, storing and transporting specie free of charge, facilitating payments on and subscriptions for national debt, and even handling payroll for government employees.[221] In addition, the Bank would issue loans to the government, therein creating public debt,[222] and help finance taxes.[223]

But the Bank would have a private ownership and governance structure. The bank would have $10 million of capital; 20 percent of subscriptions would be held by government and the other 80 percent by private shareholders.[224] In terms of governance, Hamilton also preferred private over public control: he believed that private directors would have better incentives flowing "[f]rom the influence of . . . a desire of enhancing [the bank's] profits."[225] And he distrusted governmental motives, asking "what Government ever uniformly consulted its true interest, in opposition to the temptations of momentary exigencies? What nation was ever blessed with a constant

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218. *Id.*

219. ALEXANDER HAMILTON, TREASURY DEP'T, REPORT ON A NATIONAL BANK 321 (1791).

220. *Id.* at 313.

221. COWEN & SYLLA, *supra* note 214, at 120.

222. The bank would give "[g]reater facility to the Government in obtaining pecuniary aids, especially in sudden emergencies" by perpetually standing ready with a pool of capital that could be mobilized. *Id.* at 126.

223. *Id.* ("Those who are in a situation to have access to the Bank can have the assistance of loans to answer with punctuality the public calls upon them . . . [and all taxpayers benefit from] the increasing of the quantity of circulating medium and the quickening of circulation.").

224. FED. RSRV. BANK PHILA., *supra* note 208, at 2.

225. HAMILTON, *supra* note 219, at 326.

succession of upright and wise Administrators?"[226] Here, Hamilton appears to have identified the time-inconsistent nature of public policy, stemming from political and electoral cycles. He understood that the fruits of the Bank's labor, like monetary stability, were public goods that had to be produced by a government institution but governed by actors with the right incentives.[227]

Importantly, the Bank would also be designed to serve these private interests. In particular, it would be tasked with assisting "trade and industry" with "[t]he augmentation of the active or productive capital of a country," by enabling "more effective utilization of capital by which scattered and otherwise idle amounts are concentrated and made to serve the uses of business."[228]

The First Bank opened on December 12, 1791 and had a twenty-year charter.[229] But Congress voted not to renew its charter in 1811, and the First Bank closed.[230]

Alas, America sorely missed a public finance institution during the War of 1812. As Professor Larry White explains, "[b]y 1815, the United States found itself heavily in debt, much like it had been at the end of the Revolutionary War thirty years earlier."[231] And so a Second Bank of the United States was chartered in 1816, again for twenty years.[232] The Second Bank performed similar functions as the First Bank (and even engaged in rudimentary monetary policy) and maintained the

226. *Id.* at 331. Hamilton did, however, reserve certain powers for the Treasury secretary, such as the power to inspect the bank's books. JOHN THOM HOLDSWORTH, THE FIRST BANK OF THE UNITED STATES 20 (1910). Interestingly, this role for the Treasury secretary in the central banks' affairs held over in the original Federal Reserve Act of 1913 and was not removed until 1935. *Compare* Federal Reserve Act, Pub. L. No. 63-43, § 10, 38 Stat. 251, 260 (1913) (designating the secretary of the Treasury as an ex officio member of the Board), *with* Banking Act of 1935, Pub. L. No. 74-305, sec. 203(b), 49 Stat. 684, 704 (1935) (designating the composition of the Board as "seven members, to be appointed by the President").

227. *See* KAHAN, *supra* note 217, at 9 (noting that, what had always made the Bank attractive, in Hamilton's view, "was that it sidestepped what he saw as the downside of representative government, namely, that politicians would be unwilling to make necessary but politically difficult decisions in times of crisis or that they would be tempted to manipulate the money supply for short-term political gain").

228. HAMILTON, *supra* note 219, at 306; HOLDSWORTH, *supra* note 226, at 14.

229. *See* HOLDSWORTH, *supra* note 226, at 20, 29.

230. *Id.* at 97.

231. *See* Andrew T. Hill, *The Second Bank of the United States*, FED. RSRV. HIST. (Dec. 5, 2015), https://www.federalreservehistory.org/essays/second-bank-of-the-us [https://perma.cc/M9YQ-3SXJ].

232. For a history of the Second Bank, see generally JAY COST, THE PRICE OF GREATNESS (2018); FED. RSRV. BANK PHILA., *supra* note 208; KAHAN, *supra* note 217, at 20.

same mostly private ownership structure.[233] However, the Second Bank was considerably larger and more powerful[234]: it had $35 million in capital and eighteen branches nationally, compared to the eight possessed by the First Bank.[235] But like the First Bank, the Second Bank's charter was not renewed upon its expiration and, indeed, became the subject of considerable political acrimony.

Specifically, the election of Andrew Jackson to the presidency was fateful for the Second Bank.[236] In the so-called "Bank War," Andrew Jackson crossed political swords with the then-president of the Second Bank, Nicholas Biddle. For Jackson, defeating the Bank became part of his populist, antibank, anti-elitist dogma—and he went to great lengths to bring the Second Bank to its knees, particularly during his second term in office.[237] Jackson regularly spoke out against the Bank and, in a final blow in 1833, removed all federal deposits from the Bank and transferred them to state banks.[238] Later, Jackson would order the Secretary of War to demand that the Bank stop paying pensions to the Revolutionary War veterans.[239]

Biddle fought back by inducing a recession (by contracting the money supply) and refusing to comply with the pension cessation order.[240] But he was no match for Jackson's antibank fervor. To gain a

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233. FED. RSRV. BANK PHILA., *supra* note 208, at 6.

234. Paul Kahan argues that, by 1829,

> the bank originated one out of every five bank loans in the nation and emitted approximately one-fifth of the country's bank notes. More impressive, the bank held one third of the nation's specie reserves, making it the most important financial institution in the United States. . . . "[I]ts operations touched virtually every aspect of the nation's economic life."

KAHAN, *supra* note 217, at 55 (footnote omitted) (quoting Arthur Fraas, *The Second Bank of the United States: An Instrument for an Interregional Monetary Union*, 34 J. ECON. HIST. 447, 447 (1974)).

235. *Id.* at 20.

236. Kahan references a contemporary observer, remarking in 1836, "If any man but Andrew Jackson had been at the head of the government, the Bank of the United States would still have been in existence." *Id.* at 27–28.

237. *See* Andrew Jackson, Veto Message (July 10, 1832) (transcript available at https://millercenter.org/the-presidency/presidential-speeches/july-10-1832-bank-veto [https://perma.cc/C9LU-33RF]). In his judgment, though a national bank may be necessary in principle, the particular powers Congress endowed in the Second Bank—monopoly; freedom to decide where to branch based on profit motive, without consulting government; and exemption from various taxes state banks were subject to—were neither necessary nor proper. *Id.*

238. COST, *supra* note 232, at 157.

239. *See* KAHAN, *supra* note 217, at 65.

240. *See* RALPH C. H. CATTERALL, THE SECOND BANK OF THE UNITED STATES 314–21 (1903) (describing how Biddle, in response to Jackson withdrawing government deposits from the

sense of just how committed Jackson was to destroying the Bank, historians refer to one particularly illuminating conversation between Jackson and Martin Van Buren in the summer of 1832: "The bank," Jackson began, "is trying to kill me, *but I will kill it*."[241] Jackson wanted to turn the question of the Bank's existence into a popular referendum on the people versus what he saw as a technocratic elite.[242]

For students of contemporary central bank activism, the story of the First and Second Banks offers two cautionary tales. The first is about the perils of private credit allocation undertaken by a public finance institution. Both Banks competed with state-chartered banks and effectively controlled credit conditions in ways that could benefit their private stockholders. The Second Bank made loans to private individuals, and, because it received all of the government's deposits, had a significant competitive advantage over state banks to make more loans.[243] Writing today, historian Jay Cost analogizes the First and Second Bank to government-sponsored enterprises ("GSEs"), Fannie Mae and Freddie Mac; like the GSEs, the two Banks benefited (perhaps even more so) from the government's explicit backing.[244]

The very notion that the Bank could exercise public functions while serving and being governed by private interests nettled republican ideals and worried James Madison greatly. Among other things, Madison warned that "[t]he power of granting charters . . . is a great and important power."[245] Madison further noted in this regard that "Public Affairs in Europe" had shown that such a public-private corporation had the potential to become a "powerful machine . . . competent to effect objects on principles, in a great measure independent of the people."[246]

Bank and its branches, launched a "reduction in discounts [loans] . . . to the amount of $13,300,000–a preposterously large sum"). As Andrew Hill notes,

> [t]his contraction of credit . . . might create a backlash against Jackson and force the president to relent and redeposit government funds in the Bank, perhaps even renewing the charter. But Biddle's move backfired: in the end, it helped support Jackson's claim that the bank had been created to serve the interests of the wealthy, not to meet the nation's financial needs.

Hill, *supra* note 231.

241. KAHAN, *supra* note 217, at 95.

242. *See id.* at 102–03.

243. FED. RSRV. BANK PHILA., *supra* note 208, at 6.

244. COST, *supra* note 232, at 161.

245. *Id.* at 65.

246. *Id.*

In the end, Madison's fears of corruption and profligacy manifested most pointedly in the Second Bank. The Second Bank opened amidst the economic boom that followed the War of 1812—but "promptly discredited itself by speculation, stockjobbing, and, at some branches, outright fraud."[247] And it did a terrible job managing the panic of 1819. Worried about regional drains of capital, the then-president of the Bank, William Jones, ended the practice whereby notes of one branch could be redeemed at any other; the consequence was that Western and Southern branches had to reduce their credit, straining those regions.[248] At the same time, Jones required state banks to resume redeeming notes for specie, which forced those banks to call in existing loans and reduce new lending.[249] When Biddle took over as president of the Second Bank in 1822, he wrote to President James Monroe: "The Bank is of vital importance to the finances of the govt. and an object of great interest to the community. That it has been perverted to selfish purposes cannot be doubted—that it may—& must—be renovated is equally certain."[250]

But even under Biddle, the institution's power to further private interests was too great to resist. As historians at the Reserve Bank of Philadelphia remarked, "Biddle also wasn't above allowing the bank to make loans to his friends while denying loans to those who were deemed not so friendly."[251] In 1826, for example, Biddle used the Bank's economic power to crush a financial empire that had been built by Jacob Barker when Biddle became worried that Barker's institutions had grown too large.[252] Ultimately, it seems that the power to dispense credit selectively, for private or political interests, became a rallying cry for the Bank's opponents: most formidably, President Andrew Jackson.[253]

The second lesson to be drawn from the First and Second Banks regards the dangers that presidential populism poses for a technocratic central bank. Though many ideological battles were waged during the

247. Daniel Feller, *King Andrew and the Bank*, 29 HUMANITIES, Jan./Feb. 2008, https://www.neh.gov/humanities/2008/januaryfebruary/feature/king-andrew-and-the-bank [https://perma.cc/87X5-U2KN].

248. KAHAN, *supra* note 217, at 25.

249. *Id*.

250. *Id.* at 47.

251. FED. RSRV. BANK PHILA., *supra* note 208, at 14.

252. KAHAN, *supra* note 217, at 55.

253. *See* COST, *supra* note 232, at 156–57.

Bank War, perhaps the most fundamental clash came over the Bank's inclination (and ability) to respond to popular forces. Hamilton never intended either of the Banks to be overly responsive to the changing tides of popular or presidential opinion—to the contrary, he designed the Banks as "a hedge against the unpredictability of democracy."[254] Biddle, who firmly grasped the role of the Bank in American public life—at least as far as its public policymaking was concerned—was a steadfast believer in technocracy.[255] But Jackson, and those most loyal to him, preferred a national bank that would appear popularly accountable while dispensing political patronage to executive devotees.[256] The fact that the Bank had the power to cater to private interests may well have created a toehold for Jackson to socialize the idea that the Bank could, and should, be meeting popular demands of the day. Madison had recognized that danger early on.[257] This basic lesson in republican theory and central banking—that credit allocation and populism erode technocratic neutrality of a central bank—may well resonate today and at intervals in the future.

B. The 1920s: Discretionary Monetary Policy

It was not long after the Federal Reserve System (the "System") was created that various organs of the System would engage in monetary policy activism. The original Federal Reserve Act of 1913 had empowered the Fed as first and foremost a bank supervisor and currency manager.[258] At the outset of the 1920s, the macroeconomic effects of the money supply were still not well understood, and the expansion and contraction of money were thought to be automatically managed by international flows of gold and the expansion and contraction of credit throughout the country pursuant to the so-called real bills doctrine.[259] Monetary policy, as it were, was a passive feature of the System.

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254. KAHAN, *supra* note 217, at 9.

255. *See* COST, *supra* note 232, at 154–55.

256. *See* KAHAN, *supra* note 217, at viii, 61–62.

257. *See* COST, *supra* note 232, at 64–68.

258. *See, e.g.*, Lev Menand, *Why Supervise Banks? The Foundations of the American Monetary Settlement*, 74 VAND. L. REV. 101, 150–52 (2021).

259. *See* Robert W. Dimand, *Competing Visions for the U.S. Monetary System, 1907-1913: The Quest for an Elastic Currency and the Rejection of Fisher's Compensated Dollar Rule for Price Stability*, 2003 PAPERS POL. ECON. 101, 102; MELTZER, *supra* note 79, at 137–90. Robert Hetzel explains,

But throughout the 1920s, the Federal Reserve Bank of New York, under the leadership of its president, Benjamin Strong, actively evolved the System's objectives and its policy tools. In particular, Strong believed that the System should steer monetary conditions toward price stability and aid European economic reconstruction.[260] Strong's activist policies, deployed to achieve those objectives, shaped the System throughout the 1920s in ways that would bring it closer to the modern conception of the Federal Reserve System than its framers had originally designed.[261] By 1924, Strong and other senior System officials had developed an intellectual and policy framework that would (or already had) inspired and justified proactive uses of monetary policy.[262]

Strong also created the institutional and governance structure to implement his novel policies. He innovated a "Governors' Committee"—a sort of proto FOMC—that was a consortium of Reserve Bank presidents that would be tasked with cohering policy around OMOs and giving the Board policy advice.[263] Fortuitously for Strong, the System had newly acquired access to the raw material with

> [t]he founders of the Federal Reserve System had assumed that the Fed would operate subject to the discipline of the international gold standard . . . . [T]he gold standard was the accepted means of keeping [the power to control the price level] from the government . . . . [Policymakers like FRBNY President Benjamin] Strong had more faith in the automatic operation of a gold standard to limit inflation and to preserve social stability . . . .

Robert L. Hetzel, *The Rules Versus Discretion Debate over Monetary Policy in the 1920s*, FED. RSRV. BANK RICHMOND ECON. REV., Nov./Dec. 1985, at 3, 3, 8. *See generally* HUMPHREY & TIMBERLAKE, *supra* note 21 (2019) (providing an account of the use of the real bills doctrine in the 1920s and 1930s).

260. LESTER V. CHANDLER, BENJAMIN STRONG, CENTRAL BANKER 198 (1958). In a Letter from Benjamin Strong to Oliver M. W. Sprague, Nov. 3, 1922, Strong recounts his realization that the System "could not escape either responsibility for monetary conditions or the necessity of exercising broad discretion." *Id.*

261. As Strong's only biographer recounts,

> [n]o other peacetime period in the history of the System has witnessed a faster development of both Federal Reserve thinking and policies than that starting around the end of 1921 and culminating in 1924. At the beginning of this period, Federal Reserve officials were confused and uncertain as to both ends and means. They were questioning old objectives and policy guides but had not yet developed new ones; they neither understood the instruments at their disposal nor were skilled in their use.

Id. at 188.

262. *See id.* at 189 ("Theirs had now become a philosophy of positive regulation, and they were consciously using their powers to promote high and stable levels of business activity and employment, stability of price levels, and European monetary reconstruction.").

263. *See id.* at 187, 216.

which it could conduct such offensive monetary policy. Thanks to the Treasury's wartime bond programs, there were more government debt assets in circulation than ever before, at levels now sufficient to enable the System's first efforts at OMOs.[264] The Governor's Committee experimented with OMOs to "prevent undesirable effects" on the economy, from things such as gold movements or currency outflows, and also "dynamically" to effectuate changes in the money market.[265]

Strong turned to proactive monetary policy to solve at least two major economic issues of the day—one domestic and one abroad. At home, gold inflows had created the potential to adversely impact price levels. Between 1920 and 1924, monetary gold stock in the United States rose to 70 percent, sparking fears of inflation and subsequent deflation.[266] To counter inflationary pressures, the New York Fed responded decisively to defend the gold reserve ratio.[267] Strong's formula was to "sterilize" gold inflows.[268] This is to say that the System would "offset" gold inflows by taking other money out of circulation (e.g., by selling government securities and / or reducing discount window lending).[269] The use of OMOs to pursue this rudimentary form

264. *Id.* at 205, 208 (discussing Strong's early discovery, experimentation, and learning curve with open market operations).

265. *Id.* at 234. The reader may be interested to know that Strong's committee was disbanded by the Fed Board in 1923 while he was in Colorado recuperating from tuberculosis. *Id.* at 221–23; *see* MELTZER, *supra* note 79, at 149–50 (detailing how a 1923 Board resolution abolished the Committee on Centralized Purchases and Sales, which Strong had founded outside of the Board's reach, and appointed the five members of that committee to the Open Market Investment Committee ("OMIC"), which was firmly "under the Board's control"). So it would not have played a role in monetary policy decisions after that time. Also of note is that the OMIC, which Strong continued to serve on, played a major role in monetary policy after 1923, *see* Hetzel, *supra* note 259, at 3 n.2, 4, 5, even when the Committee on Centralized Purchases and Sales no longer existed.

266. LIAQUAT AHAMED, LORDS OF FINANCE: THE BANKERS WHO BROKE THE WORLD 162–63 (2009).

267. *See* Priscilla Roberts, *Benjamin Strong, the Federal Reserve, and the Limits to Interwar American Nationalism: Part I: Intellectual Profile of a Central Banker*, FED. RSRV. BANK RICHMOND ECON. Q., Spring 2000, at 61, 90.

268. Leland Crabbe, *The International Gold Standard and U.S. Monetary Policy From World War I to The New Deal*, 75 FED. RSRV. BULL. 423, 428 (1989). At least one scholar, however, doubts whether Strong was acting to stabilize the price level. *See* David Glasner, *The Great, but Misguided, Benjamin Strong Goes Astray in 1928*, UNEASY MONEY (June 24, 2015), https://uneasymoney.com/2015/06/24/the-great-but-misguided-benjamin-strong-goes-astray-in-1928 [https://perma.cc/QH2W-84MZ].

269. David C. Wheelock, *Conducting Monetary Policy Without Government Debt: The Fed's Early Years*, FED. RSRV. BANK ST. LOUIS, May/June 2002, at 1, 6 n.24. Sterilization works as follows: when gold flows in, the System can sell assets in the open market, which will reduce the

of price stability expanded the then common understanding of section 14 of the Federal Reserve Act. As one former Fed official has remarked, "the provisions of the Federal Reserve Act permitting the Reserve Banks to acquire government securities were little more than an afterthought" to the Act's framers.[270]

Strong's correspondence suggests that his initiative to sterilize gold not only stretched legislative purpose, but it also pushed the boundaries of the Fed Board's own policy. In a June 28, 1923, letter to Professor Charles J. Bullock, Strong explained:

> If I were Czar of the Federal Reserve System I'd see that the total of our earning assets did not go much above or below their past year's average, after deducting an amount equaling from time to time our total new gold imports. This is the song I've been singing in Washington since April 1922 with but moderate success. Most of them don't see the point about gold![271]

Congress had, at various intervals, tried to legislate a price stability mandate for the Fed during much of the 1920s.[272] But the bills met considerable resistance from various Fed members, including and especially Benjamin Strong.[273] In Strong's words: "If you will let me alone I will try to do the best I can but if you make me do by law what I am trying to do without legislative control, I will be so afraid that I cannot fill the bill that I will not accept responsibility."[274] Discretion to engage in activism was preferable in Strong's opinion.[275]

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money supply thereby offsetting the increase in the money supply that the additional gold will have created. *See* Roberts, *supra* note 267, at 90.

270. Wheelock, *supra* note 269, at 6. Strictly speaking, the original intention behind section 14 was to allow the Fed to invest excess cash in government securities. *See* Sastry, *supra* note 51, at 6.

271. *See* CHANDLER, *supra* note 260, at 191.

272. *See, e.g.*, MELTZER, *supra* note 79, at 190–92; *Stabilization: Hearing on H.R. 11806 Before the H. Comm. on Banking & Currency*, 70th Cong. 1–2 (1928).

273. Testimony from the Fed board members contributed to the failure of a 1928 bill that would have formally added price stability as a goal. *See* MELTZER, *supra* note 79, at 187–92.

274. Thomas F. Cargill, *Irving Fisher Comments on Benjamin Strong and the Federal Reserve in the 1930s*, 100 J. POL. ECON. 1273, 1274 (1992) (quoting Letter from Irving Fisher to Clark Warburton (July 23, 1946)); *see also* Roberts, *supra* note 267, at 93 ("Although Strong doggedly resisted attempts to pass legislation demanding that the Federal Reserve System employ rate policy and open market operations to ensure price stability, preferring that Federal Reserve officials should be allowed to use their discretion in attaining this objective, it was a goal he broadly shared.").

275. In all fairness to Strong, an equally significant motivation could have been a desire to protect the Fed from political attacks, should it fail to achieve the perfect price stability that

European economic reconstruction was the second policy problem that Strong addressed with activist monetary policy. He, like other members of the New York financial elite at the time, believed in "internationalist" central banking policies and particularly those which would support a postwar international economic order with America and England at the helm.[276] He viewed it as an obligation of the System to aid the allies in their postwar rehabilitation.[277] However, discerning this role for the Fed required an activist interpretation of the Federal Reserve Act. To that end, Strong, along with Fed architect Paul Warburg, "waged a persistent battle as to whether Federal Reserve regulations should be framed and interpreted in such a way as to facilitate the Allies' ability to finance their war purchases in the American market."[278]

Perhaps most concretely, Strong used a monetary policy tool already at his disposal—the discount rate—to assist Britain to return to the Gold Standard.[279] Britain was facing a balance of payments problem that inhibited its ability to restore the prewar parity it so desired.[280] Strong wanted to assist Britain and the Bank of England by lowering the Reserve Banks' discount rate, which would make the "dollar and sterling respectively less and more attractive," thereby driving up the value of sterling.[281]

Yet the System was divided. From a domestic standpoint, many in the Fed wished to tighten rates in order to dampen what seemed to be an impending equity bubble fueled by rampant speculation in the stock market.[282] Ultimately, the New York Reserve Bank and eight others lowered rates by .5 percent, while the Chicago, San Francisco, Minneapolis, and Philadelphia banks split out of fear of fanning the flames of speculation.[283] Many in the System saw these rate reductions

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proposed mandates would require. This motivation would have centered on fundamental uncertainty—it was unclear whether the Fed could even achieve price stability, yet elements of Congress wanted to rush to hammer out an ironclad price stability mandate. Glasner, *supra* note 268 and accompanying text.

276. Roberts, *supra* note 267, at 63–64.

277. *See id.*

278. *Id.* at 72.

279. *Id.* at 78. For Britain, the ability to return to prewar parity was a matter of economic and national pride and prestige. *See id.* at 91.

280. Crabbe, *supra* note 268, at 423–40.

281. Roberts, *supra* note 267, at 78–79; *see id.* at 430–31.

282. MELTZER, *supra* note 79, at 226–27.

283. *See id.* at 227–50. For an account of these events, see Roberts, *supra* note 267, at 78–81.

as activist insofar as the decision broke with settled understanding of when the Fed should seek to ease credit conditions. Specifically, it

> irritated members of the Federal Reserve Board, who believed that the committee of governors had overstepped its authority. Several members of the Board also opposed open market purchases, especially in 1927, on economic grounds. Most members of the Board, and officials of some Reserve Banks, believed that Federal Reserve credit should be extended only at the initiative of member commercial banks through the rediscounting of commercial and agricultural loans. Otherwise, those officials argued, the Fed risked contributing to speculative activities that could prove harmful to the economy.[284]

There may well have been legitimate reasons to ease credit conditions that were separate from foreign affairs. After all, the United States had been recovering from a mild recession in 1926.[285] Yet it does seem that Strong was principally influenced by financial unease abroad and, in particular, the Bank of England's crisis.[286] Strong believed it a crucial duty of the Fed to ensure that Britain could recommit to the gold standard and restore prewar parity to the pound.[287] In 1931, Russell Leffingwell wrote to Thomas W. Lamont, that "Monty" had "called upon Ben to defend [her gold] by making it cheaper in America. This Ben did for Monty consistently and persistently, and

284. Wheelock, *supra* note 269, at 6–7.

285. MELTZER, *supra* note 79, at 215–17. In a 1926 report to the Board of Governors, Strong argued that "[s]hould we go into a business recession while the member banks were continuing to borrow . . . we should consider taking steps to relieve some of the pressure which this borrowing induces by purchasing government securities and thus enabling member banks to reduce their indebtedness." MELTZER, *supra* note 79, at 212–13; *see also* MILTON FRIEDMAN & ANNA JACOBSON SCHWARTZ, A MONETARY HISTORY OF THE UNITED STATES, 1857-1960, at 269 (1963) (agreeing with others "who concluded that foreign considerations were seldom important in determining the policies followed but were cited as additional justification for policies adopted primarily on domestic grounds whenever foreign and domestic considerations happened to coincide").

286. *See, e.g.*, Letter from Benjamin Strong to G. L. Harrison (May 15, 1926), https://fraser.stlouisfed.org/archival-collection/papers-benjamin-strong-jr-1160/foreign-countries-473581 [https://perma.cc/9GYD-KACB]; Letter from Benjamin Strong to G. L. Harrison (July 29, 1926), https://fraser.stlouisfed.org/archival-collection/papers-benjamin-strong-jr-1160/foreign-countries-473617 [https://perma.cc/MRC4-7EDR].

287. Roberts, *supra* note 267, at 64, 67, 78–79.

successfully until the return of France to the gold standard in 1927 . . . ."[288]

Still, it became a widely held belief that Strong's decision to lower rates in 1927 damaged the U.S. economy in the years that followed. In 1931, Adolph Miller, a then-member of the Fed Board, would testify that he believed the 1927 open market operations were the

> greatest and boldest operation ever undertaken by the Federal Reserve System, and, in my judgment, resulted in one of the most costly errors committed by it or any banking system in the last 75 years . . . . That was a time of business recession. Business could not use and was not asking for increased money at that time.[289]

Others joined in Miller's assessment, with the view that Strong's 1927 open market operations, and the rate reduction they occasioned, did in fact contribute to the speculative bubble that would become the great Stock Market Crash of 1929.[290]

In summary, the story of the Fed's 1920 activism mainly features Benjamin Strong, whose visions of price stability and internationalism led him to push wider interpretations of sections 14 and 13(2). In regard to Strong's discount window policies, the discretion in those provisions' language makes it difficult to know fully the reasons behind the 1924 and 1927 rate reductions. That opacity has been unhelpful to his legacy. Some judge Strong's policies as those that were ultimately guided by a sense of "economic nationalis[m]"; yet many others lay the Great Depression at his feet.[291] The 1920s' story may, as such, provide a lesson for both Congress and Fed leaders in the urgency of coupling robust mechanisms for transparency and accountability alongside broad grants of discretion. This period may also be seen as a warning concerning Reserve Banks' discretion over discount window policy, and collateral especially.

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288. *Id.* at 87–88 ("Monty" is Montagu Norman, Governor of the Bank of England; "Ben" is Benjamin Strong; Russell Leffingwell and Thomas W. Lamont were American bankers).

289. Wheelock, *supra* note 269, at 10.

290. *Id.*

291. *Compare* Roberts, *supra* note 267, at 81–86, 97 (claiming that "Benjamin Strong who, in his support of the fateful decision in 1928 to raise interest rates and force a monetary contraction to bring down stock prices, was an economic nationalist"), *with id.* at 77–78 (noting that President Hoover repeatedly blamed the Great Depression on Strong's policies of discount rate reduction).

C. The 1970s: Stop-Go Inflation

Fast-forwarding fifty years, the Fed's attention to presidential and popular pressure in the early 1970s may also, in that sense, be seen as a period of activism. The period between 1965 and 1982 is now referred to as "The Great Inflation, during which period inflation rose above 10 percent in 1974 and 1980."[292] The decade warrants careful study as the only "peacetime outburst of inflation" that had occurred at the time.[293] What role did activism play in contributing to the "disarray" in monetary policy that could not—or would not—curb inflation?[294]

There were various pressures in the political economy of the day that took the Fed's attention away from fighting inflation. For one, on a theoretical level, anti-inflationary sentiment had gone out of fashion among those in a position to influence policy. As Professor John Taylor points out, Milton Friedman seemed to be alone among professional economists urging inflation as a "disease" that needed to be reduced.[295] Meanwhile, others in the field of professional economics snickered at the thought. At the 1974 White House Economics Conference on inflation, economists dismissed the idea of constraining economic activity in the interest of reining in inflation: famed-economist Paul Samuelson quipped that the United States did not need a "Winston Churchill" style "'blood, sweat, and tears' program to reduce inflation."[296]

Instead, it had become much more popular to focus on employment. In retrospect, however, the desire to "squeeze" more than was structurally possible on that front (i.e., driving unemployment to below 3 percent) may have been a significant contributing factor to

292. Goodfriend, *supra* note 175, at 1; *see* Michael Bryan, *The Great Inflation: 1965–1982*, FED. RSRV. HIST. (Nov. 22, 2013), https://www.federalreservehistory.org/essays/great-inflation [https://perma.cc/8EWK-7M9K].

293. J. Bradford DeLong, *America's Peacetime Inflation: The 1970s*, *in* REDUCING INFLATION: MOTIVATION AND STRATEGY 247, 247 (Christina D. Romer & David H. Romer eds., 1996).

294. Goodfriend, *supra* note 175, at 1; *see also* ATHANASIOS ORPHANIDES, BD. OF GOVERNORS OF THE FED. RSRV. SYS., MONETARY POLICY RULES AND THE GREAT INFLATION 1 (2002), https://www.federalreserve.gov/pubs/feds/2002/200208/200208pap.pdf [https://perma.cc/BV99-GZGR] (noting that with the exception of the Great Depression of the 1930s, the Great Inflation of the 1970s is generally viewed as the most dramatic failure of macroeconomic policy in the United States since the founding of the Federal Reserve).

295. DeLong, *supra* note 293, at 279.

296. *Id.*

inflation.[297] As Professor Brad DeLong writes, it took most of the 1970s "to persuade economists, and policymakers, that 'frictional' and 'structural' unemployment were far more than 1–2 percent of the labor force. . . . [And] that the political costs of even high single-digit inflation were very high."[298] The popularity of an economic thought, rather than measures of pure technocracy, may have influenced Fed policy.

Setting economic fashions to one side, overt political pressure also played a role. Under the leadership of Fed Chair Arthur Burns, the Fed appeared to respond, with monetary policy, to popular opinion and the wishes of President Richard Nixon.[299] With regard to the latter, the Fed's policy seemed to fluctuate in response to the public's "shifting" concern between inflation and unemployment. In particular, the Fed adopted a so-called "go-stop" monetary policy,[300] toggling between policies aimed at employment and those at inflation. The Fed would press "go" on monetary loosening, until popular concerns about inflation mounted; it would then pump the brakes to "stop" inflation from rising with "aggressive interest rate policy."[301] But, because the public would not support interest rate increases once employment begins to rise, the Fed found itself in a political trap of facilitating creeping inflation.[302]

Naturally, this kind of waffling monetary policy skewed expectations about inflation, which in turn, drove inflation up further. Problematically,

> [w]age and price setters learned to take advantage of tight labor and product markets in the "go" phase of the policy cycle to make increasingly inflationary demands, which neutralized the monetary stimulus. As a result, central banks became ever more expansionary in the pursuit of low unemployment. . . . By pursuing low unemployment and fighting inflation only when it became the

297. *Id.* at 273.

298. *Id.* at 251 (emphasis omitted).

299. *Id.* at 263.

300. Goodfriend, *supra* note 175, at 48. Apparently, however, Nixon did not believe he could control inflation. *See* Robert L. Hetzel, *Arthur Burns and Inflation*, FED. RSRV. BANK RICHMOND ECON. Q., Winter 1998, at 21, 22.

301. Goodfriend, *supra* note 175, at 48.

302. *Id.* at 48–49.

> predominant public concern, central banks then increased the volatility of both inflation and output.[303]

Precisely as this Fed Board researcher concludes, "had policymakers concentrated their efforts on safeguarding price stability alone, better outcomes for both employment and price stability would have been likely."[304]

Moreover, the Fed's then-Chair, Arthur Burns, directly accommodated President Nixon. Tapes between Nixon and Burns feature Nixon pressuring Burns into running an expansionary monetary policy to boost his reelection prospects.[305] Burns often agreed to the President's requests. As one example of these interactions, in a December 10, 1971, tape, Nixon and Burns are recorded conversing as follows:

> Burns: "I wanted you to know that we lowered the discount rate . . . got it down to 4.5 percent."
>
> Nixon: "Good, good, good . . . . You can lead 'em. You can lead 'em. You always have, now. Just kick 'em in the rump a little."
>
> Burns: "Time is getting short. We want to get this economy going."[306]

In another, Nixon chuckles at Fed independence. To Burns, he says,

> I know there's the myth of the autonomous Fed . . . [short laugh] and when you go up for confirmation some Senator may ask you about your friendship with the President. Appearances are going to be important, so you can call Ehrlichman to get messages to me, and he'll call you.[307]

Burns' leadership certainly seems to teach a lesson in the wisdom of staying an apolitical course—popular or presidential pressure may be

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303. *Id.* at 49.

304. ORPHANIDES, *supra* note 294, at 8. *See generally* GEORGE P. SHULTZ & JOHN B. TAYLOR, CHOOSE ECONOMIC FREEDOM: ENDURING POLICY LESSONS FROM THE 1970S AND 1980S (2020) (discussing the economic policy failures of that era). Interestingly, though, Burns very much wanted Nixon to let monetary policy alone and try doing something on the economic policy front to tackle stagflation. *See* Letter from Arthur Burns to Richard Nixon (June 22, 1971), *in* SHULTZ & TAYLOR, *supra*, at app. B ("I doubt if we will bring inflation under control, or even get a satisfactory expansion going, without a major shift in economic policy.").

305. *See* Burton A. Abrams, *How Richard Nixon Pressured Arthur Burns: Evidence from the Nixon Tapes*, 20 J. ECON. PERSPS. 177, 178 (2006).

306. *Id.* at 181.

307. DeLong, *supra* note 293, at 259.

a palliative for Fed leaders in the short term, but it is a dangerous monetary cocktail for the long term.[308] It also highlights once again how the Fed's broad grants of discretion may make it difficult to detect policy decisions that are more political than technocratic.[309] Now, to be fair, the Fed did not gain a formal mandate to maintain price stability until 1977—so it did not shirk a legal obligation when it let stable prices slide.[310] Nevertheless, Fed policies that are shaped in view of economic groupthink, popular opinion, or presidential priorities do check the box for activism—at least as far as its structural indicia go.

* * *

Activism, as Parts I and II have shown, is not a monolithic concept—the cases do not all fit one tidy archetype. Sometimes activism happens in "wartime" (crisis mode) while in other cases activism has or could transpire during a "peacetime" transformation of the Fed. Still, these cases all hang together by their trademark characteristics and structural impacts: by pushing text, purpose, or conventional usage of a power—in response to popular, political, or international pressure—activism enlarges the Fed's role relative to the job that Congress gave it. Still, normative judgments of these cases may well vary. As the final Part discusses, activism can be evaluated along a spectrum—with crisis-era action on the one end and social policymaking on the other.

III. Assessing Central Bank Activism

By now this Article has set out a range of examples where the Fed (or actors within the institution) have or might one day engage in "activism." These studies have indicated a Fed policy as "activist" when it breaks from statutory text, purpose, or historical usage of a power; and disrupts structural divisions between the Fed and more democratically responsive actors. The lessons learned were broad. Part

308. The dynamic of conflicting interests between elected politicians and monetary policy is a timeless one. As Holland describes, "Driven by election timetables or other short-term goals, [politicians will] splash too much of what feels like free cash around the economy. History is full of examples, from Germany's Weimar Republic a century ago to Latin America today, of the disastrous effects of losing monetary discipline." Holland, *supra* note 75.

309. Indeed, "[t]he period is often cited as a prime example of the dangers associated with discretion." Orphanides, *supra* note 294, at 1.

310. DeLong, *supra* note 293, at 271. DeLong suggests that Fed Chair Arthur Burns did not believe he had the authority to quickly bring inflation down. *Id.* at 250–51.

II demonstrated that the practical dangers of Fed activism range from monetary policy failures to popular antipathy, reminding us that politics and central banking do not go well together.

This Part addresses the sticky normative questions that follow: What are the reasons why central bank activism should generally be constrained? Could central bank activism ever be justifiable? And, of key importance, what guardrails should be sought for navigating between modernizing adaptation or wartime agility on the one hand, and activism that overreaches on the other?

A. Legitimacy Concerns

This Article has thus far mainly wrestled with the question of what the law empowers the Fed to do. Yet to understand fully the problems with the practice of activism, one must consider the ancillary question of legitimacy, which speaks to the Fed's authority to push on the edges of the law or go beyond them.

As scholars have elsewhere discussed at length, legitimacy matters a great deal for central banking power. Former Deputy Governor of the Bank of England, Sir Paul Tucker, studies the question of central bank legitimacy at length in his book, *Unelected Power*.[311] So, too, have Professors Charles Goodhart and Rosa Lastra in exploring the nexus between populism and legitimacy.[312] In all of these scholars' views, legitimacy is a first-order question for any adjunct of the state that exercises power on a delegated and independent—and thus attenuated—basis, as most central banks do.[313] Legitimacy forms the basis for societal "acceptance" of any given power.[314] As Tucker explains, acceptance means that people will "go along with the decisions and with the right of the central bank to make them . . . [and] not systemically get in the way of the implementation of agency policy . . . or otherwise seek to undermine" the institution.[315] Acceptance thus

311. *See generally* TUCKER, *supra* note 25.

312. Charles Goodhart & Rosa Lastra, *Populism and Central Bank Independence*, 29 OPEN ECON. REV. 49, 50, 53–58 (2018).

313. *Id.* at 54.

314. As Tucker explains, legitimacy thus allows the coercive power of the state to fade into the background, and it also makes it possible to explain how the central bank may affect its purpose without extracting some moral duty to obey from people. *See* TUCKER, *supra* note 25, at 148.

315. *Id.* at 155.

becomes necessary for a central bank to sustain its grip on power and a linchpin for the efficacy of its policy.

But in some cases, Fed activism could be at odds with its continued legitimacy.[316] To see why, it is useful to lean again on Paul Tucker's analysis. In explaining the conditions necessary for the legitimate exercise of power, Tucker refers to the work of British social scientist David Beetham.[317] The Tucker-Beetham view sets up three conditions necessary to "justify" as legitimate any given exercise of power[318]: that it be "established and exercised" (1) "by legally valid means"; (2) "under laws, norms, and conventions that conform to a society's deep values and normative beliefs about governance"; (3) pursuant to some "collective acceptance" of the practice.[319]

The first condition is straightforward enough to consider where activism is concerned. Whether the Fed is acting within the bounds of what the law says and what it intended is a question of what Lastra and Goodhart refer to as "formal legitimacy."[320] Activism, in its strongest forms, cannot comport with this condition. Even in its milder versions, activism seems generally at odds with the notion that any use of power has been established through "legally valid means."[321] Activism, after all, comes about from subtle (or, sometimes overt) aggrandizements of power that result from the Fed's specific efforts to expand a flexible, broadly worded mandate. While Congress allows administrative agencies to interpret their own mandates to some extent, there is always a line that, once crossed, violates the limits to how far any agency can go in this regard.[322]

For example, efforts to retool monetary policy to offensively reduce climate change would, if that came to pass, fall on the other side

316. For a discussion of the legitimacy of the Fed, in light of growing pressure to engage in activism, see generally Carola C. Binder & Christina P. Skinner, The Legitimacy of the Federal Reserve (July 2021) (unpublished manuscript) (on file with author).

317. *See* TUCKER, *supra* note 25, at 159–60.

318. *Id.* at 147 (quoting moral philosopher Bernard Williams for the principle that "[t]he Basic Legitimation Demand implies . . . the state . . . hav[ing] to offer a justification of its power to each subject").

319. *Id.* at 159–60. This conception thus combines legal legitimacy with notions of democratic legitimacy.

320. Goodhart & Lastra, *supra* note 312, at 54.

321. *See* TUCKER, *supra* note 25, at 159.

322. *See* Chevron U.S.A. Inc. v. Nat. Res. Def. Council, Inc., 467 U.S. 837, 843 (1984) ("If Congress has explicitly left a gap for the agency to fill, there is an express delegation of authority to the agency to elucidate a specific provision of the statute by regulation.").

of that line. Again, it is difficult to establish that Congress had climate mitigation in mind with section 2A; accordingly, in the absence of congressional instruction to "have regard" to climate policy of the government (as the ECB and Bank of England have),[323] a Fed initiative to take on climate change in that way would seem inconsistent with this first condition of legitimacy.[324]

As regards the second condition, activism may also come in conflict with the well-established principle of democratic governance that only elected leaders decide which goals the government pursues and establish laws that seek those ends.[325] But when a central bank engages in activism it substitutes its unelected power—to borrow Tucker's term—for the power of the legislature to decide what law and its design should be. Several of the case studies above demonstrate how the Fed's broadly worded legal authorities render it susceptible to popular or political pressure to sidestep an inert or indecisive Congress.[326]

The Fed does not itself share legislative power with Congress where its own mandate amendments are concerned. Congress should not put the Fed in the uncomfortable position of acting like a supralegislature, as it forces the central bank to substitute unelected

323. *See* note 194 and accompanying text; *see, e.g.*, Rosa M. Lastra & Kern Alexander, *The ECB Mandate: Perspectives on Sustainability and Solidarity*, 2020 MONETARY DIALOGUE PAPERS 1, 11–13, https://www.europarl.europa.eu/RegData/etudes/IDAN/2020/648813/IPOL_IDA(2020)648813_EN.pdf [https://perma.cc/F23N-LRKC].

324. As Goodhart and Lastra point out, this can also be problematic for accountability reasons. If the Fed decides for itself what goals to pursue, how can one know whether they "are on the right track"? Instead, society must default to deference to their expert technocracy. Goodhart & Lastra, *supra* note 312, at 55–56.

325. The notion that "people . . . being able to shape and challenge (or contest) public policy" reflects a republican ideal of government, with roots in "Rome, the late-medieval Italian city-states, English seventeenth-century debates, and America's founding fathers . . . . Power is to be dispersed, office held temporarily, and officeholders accountable." TUCKER, *supra* note 25, at 165. Translating these republican notions to central banking terms, as Ben Bernanke has remarked, there is "[a] broad consensus . . . around the world that the goals of monetary policy should be established by the political authorities, but that the conduct of monetary policy in pursuit of those goals should be free from political control." Ben S. Bernanke, Central Bank Independence, Transparency, and Accountability, Speech at the Institute for Monetary and Economic Studies International Conference (May 25, 2010), https://www.federalreserve.gov/newsevents/speech/bernanke20100525a.htm [https://perma.cc/NLY9-Z3YN]. This second prong of legitimacy also implies some requirement of political independence for the Fed, which will be discussed in further depth below.

326. *See supra* notes 148–179 and accompanying text (discussing the Fed's new monetary policy framework).

judgment for that of Congress and to make political decisions about where scarce governmental resources should be allocated.

And quite often, activist policies will require significant value judgments, further clashing with condition two. Where green policies are concerned, for instance, the Fed would need to make decisions about which companies classify as "brown" or "green" for purposes of adjusting risk-based capital requirements, chastising banks for holding certain assets, or for engaging in green QE. Meanwhile, the new policy framework invites the FOMC to make a number of such decisions—answering, for example, how far past 2 percent inflation will the economy be permitted to go, and how will the FOMC satisfy itself that employment conditions are sufficiently strong (and for which segments of the population) before it allows liftoff to occur? Will this be a moving target?[327] It bears repeating that politicization of the discount window has been difficult to sustain in periods before.[328] Of course, the active exercise of discretion is not a litmus test for activism. But discarding a monetary policy rule in favor of a capacious standard certainly opens the door to eventual activist applications.

The third condition of "collective acceptance" is more difficult to pin down against central bank activism. One can point to the popular desire to tackle climate change and inequality, and to foster collegial relations with our allies, as goals so important as to justify Fed intervention even absent clear law. While tempting at first blush, it puts the cart before the horse. That initial question of what society deems important should not be up to the Fed's perception of social mores of the time. This circles back to conditions one and two. Yet the notion that there is a 'collective' will driving the Fed forward seems to be the implicit rationale for much of the central bank's (potential) activism today. In summary, as measured against these three criteria, certain versions of central bank activism would not often appear to meet the conditions necessary for legitimacy.

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327. *See* Tyler Powell & David Wessel, *What Do Changes in the Fed's Longer-Run Goals and Monetary Strategy Statement Mean*?, BROOKINGS (Sept. 2, 2020), https://www.brookings.edu/blog/up-front/2020/09/02/what-do-changes-in-the-feds-longer-run-goals-and-monetary-strategy-statement-mean [https://perma.cc/7X2Z-RAFQ] (noting that the new framework "does not specify over what period of time the Fed will seek to have inflation average 2 percent or how much over 2 percent it intends to push inflation as part of this 'make-up' strategy").

328. *See* Charles W. Calomiris, *Is the Discount Window Necessary? A Penn Central Perspective*, 76 FED. RSRV. BANK ST. LOUIS REV. 31, 31 (1994).

Of course, a central bank can muddle through periods of low legitimacy. Take the activist monetary policy of the 1970s as one example—those policies were soon seen as clearly ineffective, but the institution carried on.[329] But when activism mixes with the wrong political economy, it can pose a more existential threat. This was the lesson of the Second Bank of the United States[330]—and indeed, the Fed is not immune to such popular hostility today.[331]

In turn, the popular antipathy that can result from low legitimacy can create problems for transparency. If central banks become unduly worried about public censure, their leaders may develop incentives to obfuscate their actions to conceal the weak basis of their power. Indeed, the decisions of former New York Fed President Benjamin Strong typify this point. Recall that Strong resisted clear lines from Congress, or open deliberation, in the interest of his ability to retain the autonomy to be activist.[332] Such opacity is, of course, inversely related to accountability. Activism can thus create a spiral of diminishing legitimacy, reduced transparency, weakened accountability, and ultimately, the erosion of authority.

Finally, and shifting gears, aside from the relationship between activism and legitimacy, activism can also affect a central bank's

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329. *See supra* notes 299–304 and accompanying text.

330. Referring to the founding of the National Bank system in 1864, one scholar reflected on the First and Second Banks and the danger of politicization, noting that

> [a]s compared with the Second Bank of the United States, the system now to be inaugurated looked very formidable. If the Second Bank was discontinued for fear of its becoming a dangerous political weapon, how much more ought one to hesitate before the inauguration of a similar system on a much larger scale.

Million, *supra* note 213, at 251, 274.

331. In 2013, knee-deep in QE, the Fed's popularity was quite low. *See* Jeffrey M. Jones & Lydia Saad, *Americans Sour on IRS, Rate CDC and FBI Most Positively*, GALLUP (May 23, 2013), https://news.gallup.com/poll/162764/americans-views-irs-sharply-negative-2009.aspx [https://perma.cc/GHZ9-YUTS] (noting that the Fed has a less positive image than before, with only 33 percent voting for excellent or good performance). Additionally, there have been repeated calls—on the left and right of the political spectrum—for greater transparency at the Fed. *See, e.g.*, Federal Reserve Transparency Act, S. 148, 116th Cong. (2019) (commonly known as "Audit the Fed"). Other government officials, like former FDIC chair Sheila Bair, have also called for a reckoning of the Fed, on the ground that it has amassed too much power and exercises that power beyond its capabilities. *See* Sheila Bair, Opinion, *Overreliance on the Fed Is Compromising the Future for Millennials*, CNBC (Apr. 14, 2020, 6:01 AM), https://www.cnbc.com/2020/04/13/op-ed-overreliance-on-the-fed-is-compromising-millennials-future.html [https://perma.cc/4NUM-VGWY] (opining that "our elected officials have ceded too much responsibility for the economy to the Federal Reserve. But the Fed is not well equipped for this role. It is essentially a big bank, primarily configured to lend to other big banks").

332. *See supra* note 274 and accompanying text.

independence—both operational and political. Today, most central banks enjoy a significant degree of political independence—that is, a sustained commitment from the political branches (especially the executive branch) to abstain from pressuring the central bank to fashion policies for the purpose of supporting the government's popularity or prerogatives more broadly.[333] However, when the Fed engages in activism, it breaches the conventional barriers between branches. As discussed above, by too actively interpreting a mandate—so as to enlarge it in substance and scope—the Fed adopts a legislative role. Benjamin Strong did this in the 1920s by innovating a price stability role, fifty years before Congress would give the Fed that job.[334] Also at times with activism, the Fed can cross into the executive branch's arena by playing an outsized fiscal role.[335]

Playing fast and loose with the separation of powers stands to make the Fed vulnerable to political or partisan pressure in the future. Heading too far—and too often—down fiscal roads could return the Fed to its pre-1951 role that was highly subservient to Treasury. As will be recalled, prior to 1951, the Treasury was successful, again and again, at pressuring the Fed to manipulate interest rates to serve the government's need for generous war financing—even well after both World Wars had ended.[336] Falling back into such rhythm could happen easily where the Fed plays a consistent fiscal role.[337] The Federal

333. *See, e.g.*, Salib & Skinner, *supra* note 27, at 908–09 (noting that the Bank of England is independent from political influence); Rosa Maria Lastra, *The Independence of the European System of Central Banks*, 33 HARV. INT'L L.J. 475, 475–76 (1992) (discussing the independence of the European System of Central Banks). It bears emphasizing again that the Fed has a relatively much stronger political independence than several European counterparts, like the ECB and the Bank of England; as those foreign central banks are explicitly mandated to have regard to government policy. *See supra* note 194 and accompanying text.

334. *See supra* notes 267–270 and accompanying text. Looking ahead, should the Fed pursue green policies, it would again usurp lawmaking power.

335. Allocating credit, along the lines of a permanent QE, is the prime example. Notably, there is also practical significance to political pressure to allocate credit selectively, as the government has done at various periods in history in regard to, for example, the Penn Central Corporation (1970) and New York City (1975)—it makes monetary policy less effective. *See* Wheelock, *supra* note 269, at 12.

336. *See supra* notes 75–80 and accompanying text.

337. As preeminent twenty-first century economist Anna Schwartz writes, alongside Walker Todd, this breed of activism also misallocates scarce government resources:

> For the Fed to lend directly to the Treasury, to government agencies, or even to private entities that the Treasury otherwise would have to fund through the regular congressional appropriations process, is a slippery slope. The costs of doing so are politicization of the money supply process. As a general principle, the Fed's charter wisely prohibits such lending. Discount window accommodations to insolvent

Reserve Act, after all, cautions the Fed that the Treasury "*shall* . . . supervis[e] and control" the Board of Governors if and as their powers overlap.[338] Congress, for its part, may have already indicated some irreverence for Fed independence by reducing the Fed to a national piggybank with the 2020 CARES Act. And activism caters to the image of a Fed that is subservient to the Treasury or a lackey of Congress, thus increasing the chances that these practices become new custom.[339]

Just as legitimacy links to accountability, so too does independence. Where the Fed steps fluidly—but unpredictably—into fiscal and legislative roles, neither Congress nor the public can be sure which master the Fed is serving, when, and why. Such questions beg another: What interests are the Fed taking into account when fashioning new policy?[340]

Ultimately, these rule of law problems create practical challenges for the central bank. In a world in which political pressure might be inevitable, central banks' mandates are their commitment devices. It is long-established that the Fed needs to be able to credibly anchor the public's expectations about what it will—or will not—do, to assure the public that it will make technocratic expert judgments about the economy, or the financial system, absent political considerations. The public's ability to trust the Fed's commitment is crucial to its legitimacy, as articulated above, but also to its ability to effectively transmit its policies.[341]

> institutions, whether banks or non-banks, misallocate resources. Political decisions in those cases are substituted for market decisions. Institutions that have failed the market test of viability should not be supported by the Fed's monetary issues, and the Fed's discount window lending expands banking reserves just as much as open-market operations do.

Anna J. Schwartz & Walker F. Todd, *Why a Dual Mandate Is Wrong for Monetary Policy*, 11 INT'L FIN. 167, 171 (2008).

338. Federal Reserve Act § 10(6), 12 U.S.C. § 246 (emphasis added).

339. *See* Jeff Cox, *The Fed's Main Street Problem: Worries Rise that Money Won't Go Where It's Most Needed*, CNBC (Apr. 15, 2020, 9:24 PM), https://www.cnbc.com/2020/04/15/feds-main-street-problem-worries-that-money-wont-go-where-its-needed.html [https://perma.cc/DW8A-ZWCV] (paraphrasing George Selgin's position that CARES is an instance in which "Congress [is] using the Fed balance sheet as a 'slush fund' to juice the economy without the political consequences").

340. Along the lines of these concerns, Marvin Goodfriend has proposed a "credit accord" similar to the agreement struck between the Treasury and Fed over monetary policy in 1951. Marvin Goodfriend, *Why We Need an "Accord" For Federal Reserve Credit Policy: A Note*, 26 J. MONEY CREDIT & BANKING 572, 572 (1994).

341. The Fed requires commitment devices due to the so-called time-inconsistency problem—the awareness that central banks can always promise something in the short run (i.e.,

This is to say that the public must be able to trust that the Fed will keep its word and not be swayed by politics or the desire to multitask. Only if the Fed behaves reliably, and with such credibility, can it expect to elicit an economic reaction from its pronouncements about interest rates or the banking system's overall resilience.[342] As such, it is only by sticking to the boundaries of its mandates, and its informally established rules and norms for exercising power,[343] that the Fed can maintain the credibility required for effective policy execution.

B. Activism Falling on a Spectrum

By this point, this Article has described a range of historical, current, and potential forms of activism. It has also considered the various threats to principles of classical republicanism that activism might pose. Minding these cases and their implications, this Article now develops a spectrum of legitimacy along which various forms of activism might fall in view of: (1) how explicit is the Fed's legal authority to address a particular problem; (2) how much expertise the Fed has with respect to that problem; (3) how robust are the mechanisms for holding the Fed accountable for explaining to the public and the legislature points one through three.

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to pursue low inflation, to stress test banks) to achieve a desired reaction; but could then renege in the longer-term after the intended impact of their statement has been realized. *See* Richard Dennis, *Time-Inconsistent Monetary Policies: Recent Research*, FRBSF ECON. LETTER (Fed. Rsrv. Bank of S.F., San Francisco, C.A.), Apr. 11, 2003, at 1, 1, https://www.frbsf.org/economic-research/files/el2003-10.pdf [https://perma.cc/TMJ8-LM2N] (explaining that "[t]ime-inconsistency describes situations where, with the passing of time, policies that were determined to be optimal yesterday are no longer perceived to be optimal today and are not implemented").

342. By issuing forward guidance about interest rates and releasing public information about stress tests, the Fed uses its word and assurances to the public as a means of influencing the economy. *Cf.* Ben S. Bernanke, Distinguished Fellow, Brookings Inst., American Economic Association Presidential Address: The New Tools of Monetary Policy 20 (Jan. 4, 2020) (transcript available at https://www.brookings.edu/wp-content/uploads/2019/12/Bernanke_ASSA_lecture.pdf [https://perma.cc/4RDQ-2E9N]) ("The limits to forward guidance depend on what the public understands, and what it believes. . . . [Thus,] [e]nsuring the credibility of forward guidance is also essential.").

343. The "Taylor rule" may be a good example of this. Ben S. Bernanke, *The Taylor Rule: A Benchmark for Monetary Policy?*, BROOKINGS (Apr. 28, 2015), https://www.brookings.edu/blog/ben-bernanke/2015/04/28/the-taylor-rule-a-benchmark-for-monetary-policy [https://perma.cc/T2UT-3BW4] (explaining that the "Taylor rule is a . . . rule of thumb . . . intended to describe the interest rate decisions of the Federal Reserve's Federal Open Market Committee . . . However, [some have] argued that [the] rule should prescribe as well . . . that it (or a similar rule) should be a benchmark for monetary policy").

Activism is at the far end of the spectrum—high legitimacy—when the Fed evolves policy tools to address a financial crisis. The Fed has clear, multiple, and longstanding authorities to stymie financial crisis in its LOLR capacity and with the use of its monetary policy tools.[344] The Fed has over a century of expertise in this regard and a wide range of nuanced tools that can readily be evolved.[345] There is also a significant amount of built-in accountability where these facilities are concerned. They are statutorily time limited ("unusual and exigent circumstances"), and Congress keeps a watchful eye through regular hearings while the facilities are in use.[346] As such, the Fed's use of a new tool (like market-based LOLR facilities) to combat an extreme or novel crisis (like in 2008 and 2020) may be nominally activist but nonetheless acceptable provided the use of those tools is transparent and time-limited to emergency situations.[347]

On the other hand, use of the Fed's balance sheet to 'fight' crises is less clearly tolerable from a legitimacy perspective when it occurs in

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344. *See supra* Part I.A.

345. *See supra* Part I.A.

346. *See* 12 U.S.C. § 343. The CARES Act created a Congressional Oversight Commission to act as a watchdog for the Fed and Treasury's use of appropriations. *About*, CARES ACT CONG. OVERSIGHT COMM'N, https://coc.senate.gov/about [https://perma.cc/SF49-D5QA]. For the COC hearings and reports, see *Hearings*, CARES ACT CONG. OVERSIGHT COMM'N, https://coc.senate.gov/hearings [https://perma.cc/Z4WG-MVRE] and *Reports*, CARES ACT CONG. OVERSIGHT COMM'N, https://coc.senate.gov/reports [https://perma.cc/R6W9-KLTT]. Additionally, the Fed Chair appears in front of the House Financial Services Committee and Senate Banking Committee on a quarterly basis to report the current state of response. 15 U.S.C. § 9060(c). For the testimony of the Federal Reserve officials before Congress, see *Testimony of Federal Reserve Officials*, BD. OF GOVERNORS OF THE FED. RSRV. SYS., https://www.federalreserve.gov/newsevents/testimony.htm [https://perma.cc/N95D-6YDJ]. The Fed, furthermore, publishes monthly reports on state of emergency lending facilities as required under 13(3). 15 U.S.C. § 9060(b); *see Reports to Congress Pursuant to Section 13(3) of the Federal Reserve Act in Response to COVID-19*, BD. OF GOVERNORS OF THE FED. RSRV. SYS., https://www.federalreserve.gov/publications/reports-to-congress-in-response-to-COVID-19.htm [https://perma.cc/MJ9V-4CR4].

347. *See* Salib & Skinner, *supra* note 27, at 908 (accepting, even, an executive power of override in times of crisis or emergency). Governor Waller has also remarked that

> in times of crisis, coordination allows policies to be implemented quickly and forcefully to set the stage for a strong path of recovery. But for this arrangement to work, the political independence of the Federal Reserve is essential—it is the best way for the Federal Reserve to meet its congressional mandate and allow policymakers to meet the longer-term needs of the American people.

Christopher J. Waller, Governor, Bd. of Governors of the Fed. Rsrv. Sys., Treasury-Federal Reserve Cooperation and the Importance of Central Bank Independence, Speech at the Peterson Institute for International Economics (Mar. 29, 2021), https://www.federalreserve.gov/newsevents/speech/waller20210329a.htm [https://perma.cc/9HHS-CDHC].

ways not clearly contemplated by the Federal Reserve Act, or in ways that seem more properly the role of fiscal authorities (like lending to small business). It may be more difficult for the public (and Congress) to scrutinize the Fed's decisions when its lending steps outside the financial system.

Policy frameworks also sometimes evolve. Activism examples fall on two different ends of the spectrum. On the high-legitimacy side are moves to modernize monetary policy taken in reaction to observed changes in the domestic or global economies. This would cover some of Benjamin Strong's efforts at price stability in the 1920s.[348] Some may well even look with hindsight upon Strong's pursuit of a price stability objective as operationalizing that objective in a regime in which central banking had severed the mechanical linkage between gold and the price level. This view would also capture the ostensible reasons for the August 2020 monetary policy framework revamp.

But on the low-legitimacy side of the spectrum is the use of monetary policy tools to achieve political or social policy objectives. This would be the case where the Fed uses its balance sheet to try to make the financial system greener or uses the employment arm of its mandate to effectuate greater income or gender equality. Championing certain causes or acting as the first institutional mover in structural transformation of the economy is more activism than agility or adaptation.

Of course, the cases in this Article are not exhaustive. Other problems and pressures will confront the Fed. But the traits are generalizable: activism arises from popular or political pressure to do more than Congress has instructed and often involves credit allocation (that is not sector neutral) or use of discretion to pursue new objectives that are not set out in the Fed's statutes. The overarching lesson to remember is that populism does not mix well with Fed technocracy.[349]

Regardless of where activism falls along this spectrum, guardrails are important. Whether activism is ultimately judged as inevitable adaptation, agility, or ultra vires action (or something in between) may

348. *See supra* Part II.B.

349. For a general discussion of central bank populism, see POPULISM, ECONOMIC POLICIES AND CENTRAL BANKING (Ernest Gnan & Donato Masciandaro eds., 2002).

come down to how well the Fed communicates its new endeavors to the public and to Congress.[350]

C. Installing Guardrails

This Section briefly considers how the Fed might distinguish adaptation of or flexibility in its existing tools—to address new financial risks or macroeconomic emergency—from activism that poses problems for its legitimacy. It suggests a framework the Fed might use to communicate to the public, and accordingly, a framework that Congress (and the public) might use to hold the Fed accountable. Specifically, the framework would invite the Fed to elaborate on four questions.

> *1. What does the law say regarding the Fed's ability to target a new objective with supervisory, regulatory, or monetary policy tools?*
>
> *2. How will a new policy be operationalized, as a matter of law and policy fact?*
>
> *3. How will the new framework or regime interface with existing Fed law and policy regimes?*
>
> *4. What guardrails are already or will be put in place to prevent legally inappropriate mission creep?*

What follows is a brief explanation of how each prong might be developed into a broader set of tools for the Fed to use in justifying a new policy action as adaptation versus activism.

1. *How does the law support the novel form of monetary policy, regulation, or supervision?* The first question to ask is whether the possible policy target is a problem for the Fed. Inevitably, there will be a range of important social and economic issues that may implicate the real or financial economies, but they may not all be the lawful targets of Fed power. Arguably, establishing a legal basis for policy action is a necessary ingredient for the Fed to legitimately exercise its power.

Within this prong, there are two questions to be answered. The first is what mandate does the Fed have to engage in a new kind of policy activity? How, precisely, and with what concrete and verifiable

350. The Fed's ability to communicate the significance of its policy moves along a spectrum of adaption should be able to satisfy the requirements of *Chevron* deference. *See* Chevron U.S.A. Inc. v. Nat. Res. Def. Council, Inc., 467 U.S. 837, 844 (1984) (noting that the court will defer to an agency's reasonable interpretations of its statute).

facts, does the Fed see this new manner of policy intervention as required to fulfill its legal mandates? What kinds of data and evidence could or should the Fed marshal to make an intervention case? If the new intervention bears on monetary policy, what presently manifest link is there to price stability or full employment—how will the intervention impact the Fed's ability to keep prices stable?

The second question within this prong is of a microlegal nature—one that regards the Fed's reliance on legal terms of art. Statutes such as the Dodd-Frank Act—and the academic literature subsequently interpreting that law and the events around it—spawned a new set of terminology that now occasions policy responses. In particular, terms like "contagion" and "financial stability" risk and "systemic risk" are byproducts of the 2008 global financial crisis and the crisis legislation.[351] However, while these terms have not been more specifically defined in statute or regulation, they now operate as triggers for regulatory or supervisory scrutiny and the development of new policy regimes.[352] Should these terms be more clearly understood—and cabined to certain facts—if they are to be the basis for expanded Fed interventions?

2. *How will the new policy be implemented?* The second question is a mixed examination of fact and law. Here, the Fed would need to answer how a newly proposed or considered policy regime accomplishes the goals it has set out.

a. Transmission channels. The big picture issue for Fed policymakers is the nature of the transmission channel from policy to the mitigation of any given risk.

b. Design choices. It would also be beneficial for the private sector and public to know, and have some input into, the design choices involved in the development of a new policy apparatus. There are standard options to be sure. But to the extent other options are considered or

351. The phrase "systemic risk" appears thirty-nine times in the Dodd-Frank Act. *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010). Important scholars, theorizing the mechanism of systemic risk, soon coined the phrase "contagion." Gary Gorton & Andrew Metrick, *Getting Up to Speed on the Financial Crisis: A One-Weekend-Reader's Guide*, 50 J. ECON. LIT. 128, 129, 141–44, 150 (2012) (summarizing contributions to "contagion" literature motivated by the financial crisis).

352. *See, e.g.*, 12 U.S.C. § 5323 (providing authority for heightened prudential and supervisory requirements for financial institutions that pose a threat to the stability of the financial system, e.g., a systemic risk).

suggested, the Fed may also do well to make those details known and invite conversation about feasibility, costs, and benefits.

c. Informal norms. In addition to spelling out the basic mechanism of the new approach, the Fed would also need to make plain—to the extent it can anticipate—any soft law or conventions that might influence the application of the regime.

d. Communication strategy. A question for the Fed to understand internally is how this strategy will be communicated to the public and, in turn, how the public will come to understand that the Fed has been transparent in its decision-making process. This kind of framework would assist the Fed in communicating to the public, specifically, by explaining how it comports with current academic and policy conversations about central bank transparency.[353] Explaining the basis for new policy action would become an effort in transparency that shores up the accountability of the Fed's decisions.

3. *How does the new policy regime interoperate with other central banking frameworks?* Third, it is important for the public—and the banks—to understand the expected impact on other areas of central bank activity. As the Fed expands its role in our economy, in addition to its range of policy tools, this question of interoperability becomes increasingly important. Some scholars, for example, have begun to study the interaction between monetary and prudential policy—noting the tradeoffs between 'lean against the wind' policies and inflation and between capital and liquidity requirements and inflation targeting.[354]

353. For post-financial crisis burst of interest in communicating financial stability objectives, see generally David M. Arseneau, *Central Bank Communication with a Financial Stability Objective* 2 (Fin. & Econ. Discussion Series, Working Paper No. 2020-087, 2020), https://www.federalreserve.gov/econres/feds/files/2020087pap.pdf [https://perma.cc/WP7R-2JZM]; Benjamin Born, Michael Ehrmann & Marcel Fratzscher, *Communicating About Macroprudential Supervision — A New Challenge for Central Banks*, 15 INT'L FIN. 79 (2012). For historical literature on monetary policy and communication, see generally Matthew B. Canzoneri, *Monetary Policy Games and the Role of Private Information*, 75 AM. ECON. REV. 1056 (1985); Alex Cukierman & Allan H. Meltzer, *A Theory of Ambiguity, Credibility, and Inflation Under Discretion and Asymmetric Information*, 54 ECONOMETRICA 1099 (1986); Petra M. Geraats, *Central Bank Transparency*, 112 ECON. J. 532 (2002).

354. *See generally* Matthieu Bussière, Jin Cao, Jakob de Haan, Robert Hills, Simon Lloyd, Baptiste Meunier, Justine Pedrono, Dennis Reinhardt, Sonalika Sinha, Rhiannon Sowerbutts & Konstantin Styrin, *The Interaction Between Macroprudential Policy and Monetary Policy: Overview* (Bank of Eng., Working Paper No. 886, 2020), https://www.bankofengland.co.uk/-

Will a new kind of policy program be a complement, a substitute, or a distraction to other related central bank mandates and interventions?

Externally, there are similar questions to be answered. Will the new policy regime implicate the fiscal authority of the Treasury? One can see above how certain kinds of policy actions that seek aims similar to, for instance, credit policy, give rise to Fed-Treasury tensions or uncertainty. As well, it would be critical to understand the extent to which the policy is likely to deter lending to certain kinds of borrowers, thereby impacting bank credit intermediation, and, one step removed, any "pass through" effects of the new regime that could affect other parts of the financial system (i.e., nonbanks) and their ability and appetite to serve as financial intermediaries.[355]

4. *What are the checks against overreach and mission creep?* To be sure, the Fed—like all central banks—will be called upon at certain intervals to modernize its approach and understanding of new financial risks.[356] But critical to the public's acceptance of a modernizing central bank is that bank's ability to demonstrate the checks in place. Many of the guardrails that could be offered up likely exist already, but clearly explaining them to the public and to banks will make them more robust—and, if need be, the process will expose any shortfall in protections against inappropriate aggrandizement of power.[357]

D. What role for Congress?

In the end, perhaps we cannot place too much blame with the Fed for being activist. Today, the Fed faces constant pressure from

/media/boe/files/working-paper/2020/the-interaction-between-macroprudential-policy-and-monetary-policy-overview.pdf [https://perma.cc/64EG-MJZ6] (studying the interaction between monetary and macroprudential policy).

355. *See* Nina Boyarchenko, Thomas M. Eisenbach, Pooja Gupta, Or Shachar & Peter Van Tassel, *How Has Post-Crisis Banking Regulation Affected Hedge Funds and Prime Brokers*, LIBERTY ST. ECON. (Oct. 19, 2020), https://libertystreeteconomics.newyorkfed.org/2020/10/how-has-post-crisis-banking-regulation-affected-hedge-funds-and-prime-brokers.html [https://perma.cc/T6SD-78GS] (using studies to "suggest a pass-through of regulation from the directly affected sector to other parts of the financial system").

356. *See, e.g.*, JAMES, *supra* note 6, at 1–2; Conti-Brown & Wishnick, *supra* note 14, at 645.

357. Traditionally, there has been little—if any—judicial review of the Fed's actions, and most assuredly not its monetary policy actions. *See* David Zaring, *Law and Custom on the Federal Open Market Committee*, 78 LAW & CONTEMP. PROBS. 157, 174–75 (2015) (explaining that Judge Augustus Hand, in *Raichle v. Federal Reserve Bank*, established a "lack of a standard for reviewability" for the Fed's actions by opining, "It would be an unthinkable burden upon any banking system if its open market sales and discount rates were to be subject to judicial review").

politicians, people, and the press. As in the case with all agencies, actors within the institution have rational incentives to increase—or at least retain—their power and remain relevant.[358] Thus, against a backdrop of broadly worded mandates to pursue "price stability," "financial stability," and "safety and soundness," is it any wonder that the architects and leaders of America's central banks can succumb to activism?

Inasmuch as Congress seeks to hold the Fed accountable, it may also be partially at fault. This final Section briefly proposes ways that Congress could act to reduce opportunity for activism or stipulate conditions under which activism might be acceptable—but render it containable. These ideas, curating suggestions made by other scholars that study power in the administrative state, cannot be fully developed here. Rather, they are offered to give a sense of where responsibility for activism fully lies and, of course, to plant the seeds for future research on the role of the Fed in contemporary U.S. society.

First, and most fundamentally, Congress would do well to 'clean up' the Federal Reserve Act.[359] Since the founding of the Fed in 1913, Congress has revised this constitutive document a handful of times—yet each of these revisions was ad hoc and reacting to a particular political economy and (naturally) interest groups.[360] As this Article has identified, activism seems to blossom at fifty-year intervals. As such, a

358. There is substantial literature on public choice theory, which essentially lays out incentives for those in positions of regulatory power to retain or enlarge power by finding ever-new things to regulate. *See generally* JERRY L. MASHAW, GREED, CHAOS, & GOVERNANCE: USING PUBLIC CHOICE TO IMPROVE PUBLIC LAW (1999) (arguing to apply public choice theory to improve public law); WILLIAM C. MITCHELL & RANDY T. SIMMONS, BEYOND POLITICS (1994) (discussing public choice theories and offering case studies).

359. On this score, the judiciary also has a part to play in scrutinizing the breadth of delegations. *See* Goodhart & Lastra, *supra* note 320, at 62–65 (calling for greater judicial review of central bank decisions); *see also* Gundy v. United States, 139 S. Ct. 2116, 2133 (2019) (Gorsuch, J., dissenting) ("The framers understood, too, that it would frustrate 'the system of government ordained by the Constitution' if Congress could merely announce vague aspirations and then assign others the responsibility of adopting legislation to realize its goals."). As one former Fed official noted in 1993,

> the Fed does not now have, and it never has had, a clear congressional mandate to stabilize the price level. Consequently, the Fed's success in stabilizing the price level in at least some periods of its history has been and continues to be a function largely of 1) prevailing general economic conditions, 2) the strength of the Federal Reserve's leaders, and 3) old fashioned luck.

J. Alfred Broaddus, President, Fed. Rsrv. Bank of Richmond, Central Banking: Then and Now, Speech to the Woodrow Wilson Forum (Apr. 2, 1993), https://www.richmondfed.org/press_room/speeches/j_alfred_broaddus/1993/broaddus_speech_19930402 [https://perma.cc/R3GA-59DA].

360. *See, e.g.*, *supra* notes 42–47 and accompanying text.

review of these statutes every thirty years might be a rough and ready guide to follow.[361]

Second, Congress may also wish to acknowledge statutorily that sometimes activism will be inevitable. In particular, times of national crisis are most conducive to such behavior. This is understandable. Central banks' original purpose was to stymie economic crisis; their tools are designed to fight such wars. In these moments, where national exigencies arise, we must assume that the Fed's political independence will cede to the government's requirements at hand—be that supporting the Treasury's emergency economic policy or rescuing American small business.[362]

Congress can legislate for these realities, blunting the impact of these periods of activism on the Fed's legitimacy and its independence. There are two legislative measures in particular that could operationalize this notion. For one, the Fed could possibly benefit from a formalized power of executive "override," where, as in the United Kingdom, the Treasury gains a formal power to direct the monetary policy operations of the Fed (or generally) during periods of crisis.[363] Provided these overrides were "transparent, subject to legislative scrutiny, constrained by clear criteria, and in practice rare,"[364] they could obviate the appearance of and concerns with activism. A second idea, proposed by David Zaring, is to legislatively convert what are today ad hoc facilities (like, the "Term Asset Lending Facility" or "TALF") into permanent Fed facilities, triggered upon certain kinds

361. Going even further than periodic review, Paul Tucker would have legislatures fundamentally re-evaluate the purpose and role of central banks: "Advanced economies need a money-credit constitution – one that makes clear what central banks are for, and recognises our broader constitutionalist values." Tucker, *supra* note 4. Paul Tucker would not, however, favor this manner of ex-post control if it were exercised at too regular an interval. As he explains, doing so would undermine the "purpose of [independent agency] regimes being for the legislature to tie society to its desire mast." TUCKER, *supra* note 25, at 125. It should be noted that Roberta Romano has elsewhere suggested sunset provisions in crisis legislation for political economy reasons. *See* Roberta Romano, *The Sarbanes-Oxley Act and the Making of Quack Corporate Governance*, 114 YALE L.J. 1521, 1595 (2005) (suggesting that Congress should "when legislating in crisis situations . . . include statutory safeguards" like a sunset provision).

362. *See* Waller, *supra* note 347 ("The virus . . . led the Federal Reserve to establish emergency lending programs to serve as lending backstops and support the flow of credit to households, businesses, nonprofits, and state and local governments.").

363. *See* Salib & Skinner, *supra* note 27, at 977–78 (noting, based on the U.K. approach, that legal overrides might "make a central bank less legally independent" but promote overall institutional independence).

364. TUCKER, *supra* note 25, at 125.

of predefined events and perhaps a presidential proclamation.[365] Notably, each gives the executive branch more power over the Fed in times of crisis, but does so within a clearly established legal framework that the public and legislature can scrutinize and debate.

IV. CONCLUSION

As this Article has shown, central bank activism is an age-old problem with some hallmark characteristics. Activism is enabled by broadly worded legal mandates. And activism is reactive—arising in moments of broad political and popular pressure on the Fed to solve new categories of problems with its existing tools. Consequentially, activism impacts our democratic structure, blurring lines of authority between the Fed, Congress, and the Executive Branch. By thus upsetting traditional separation—and balance—of power between and among these branches, activism may be expedient, but it carries long-term social costs. This Article ultimately points to Congress as the original source of Fed activism, and the most viable solution. Only when Congress speaks clearly and deliberately, can society properly debate its ideal role for the Fed in the United States today and over time.

365. *See* Zaring, *supra* note 117, at 6.