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The Federal Reserve's Mandates

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Article

The Federal Reserve's Mandates

David T. Zaring[†] and Jeffery Y. Zhang[††]

Solutions to systemic problems such as climate change and racial inequities have eluded policymakers for decades. In searching for creative solutions, some policymakers have recently thought about expanding the Federal Reserve's core set of macroeconomic mandates to tackle these issues. But there are real questions about whether that can *be done from a legal perspective and whether that* should *be done from a policy perspective.*

In this Article, we propose a framework to answer these two questions of "can we" and "should we"—a framework grounded in administrative law and macroeconomics. In Part I, we consider the legal challenges that the Federal Reserve would face if it tried to adopt new mandates by itself, without congressional blessing. These challenges include the major questions doctrine and procedural hurdles in administrative law. In Part II, we tackle the normative question by leveraging macroeconomic theory to understand whether new mandates can be successfully balanced against existing ones. Even if adopting a new mandate is legal, it might not be good policy—regardless of whether the Federal Reserve enacts the mandate itself or Congress does so.

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We then apply our framework to newly proposed policy objectives for the Federal Reserve, including the proposed purchase of green bonds, the implementation of climate stress tests, and the closing of racial wealth gaps. To be clear, nothing in our framework implies that Congress should ignore longstanding social problems. Rather, our framework suggests that Congress should not have a regulatory agency—with its limited set of tools—expand beyond its original mandates and core competencies to solve those problems. Instead, Congress should empower the agencies most closely aligned with those objectives, thereby avoiding real administrative law constraints and minimizing difficult policymaking dilemmas where the agency faces competing responsibilities. Indeed, if an agency tries to juggle too many balls at the same time, it may drop them all.

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INTRODUCTION

Congress tasked our nation's central bank, the Federal Reserve, with setting monetary policy by keeping inflation under control and maximizing employment.[1] Eight times per year, the Federal Reserve's Open Market Committee meets to deliberate monetary policy.[2] In the past fifteen years, however, the Federal Reserve has also had to rescue the financial system and economy during multiple emergencies: the 2008 global financial crisis, the onset of the pandemic in 2020, and the banking panic in 2023.[3] Each time, the Federal Reserve used its powers to implement new ways to deliver a broad-based rescue of the economy.

Understandably, because of the Federal Reserve's numerous successes, lawmakers and others have suggested that our central bank adopt new mandates to deal with problems outside of its core mission of maintaining economic stability. Democratic senators have asked the Federal Reserve to address systemic problems, such as climate change and closing the racial employment and wage gaps,[4] while Republican senators have asked the Federal Reserve to require banks to finance oil companies and firearms manufacturers.[5] Legal scholars also have weighed in on

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1. 12 U.S.C. § 225a.

2. *What Is the FOMC and When Does It Meet?*, BD. OF GOVERNORS OF THE FED. RSRV. SYS., https://www.federalreserve.gov/faqs/about_12844.htm [https://perma.cc/SG2V-B2JG] (last updated Jan. 30, 2019) ("The FOMC schedules eight meetings per year . . . .").

3. *See, e.g.*, Mark E. Van Der Weide & Jeffery Y. Zhang, *Tale of the Tape: Lessons from the 2008 and 2020 Financial Crises*, 26 STAN. J.L. BUS. & FIN. 413 (2021) (identifying key lessons from the 2008 financial crisis and COVID-19 pandemic); *Review of the Federal Reserve's Supervision and Regulation of Silicon Valley Bank*, BD. OF GOVERNORS OF THE FED. RSRV. SYS. (2023) (discussing factors that contributed to Silicon Valley Bank's failure in March of 2023).

4. *See* Heather Long, *Democrats Introduce Bill to Give the Federal Reserve a New Mission: Ending Racial Inequality*, WASH. POST (Aug. 5, 2020), https://www.washingtonpost.com/business/2020/08/05/fed-racial-inequality-democrats [https://perma.cc/4FB9-AV3N] ("Congressional Democrats introduced new legislation on Wednesday that would make reducing racial inequality in the U.S. economy an official part of the Federal Reserve's mission."); Ed. Bd., Opinion, *The Greening of the Federal Reserve*, WALL ST. J. (Jan. 11, 2022), https://www.wsj.com/articles/the-greening-of-the-federal-reserve-jerome-powell-climate-11641941000 [https://perma.cc/466R-PBF6] ("[T]he left is pressing the Fed to adopt climate bank stress tests.").

5. *See* Valerie Volcovici, *Republicans Urge Trump to Bar Banks from Shunning Fossil Fuel Loans*, REUTERS (May 8, 2020), https://www.reuters.com/article/us-health-coronavirus-energy/republicans-urge-trump-to-bar-banks

actions the Federal Reserve could take regarding climate, consumer financial services, and other pressing issues.[6]

Can the Federal Reserve legally expand beyond its core economic stability mandates by itself, given its existing statutory authorities? *Should* the Federal Reserve or Congress push for such an expansion as a matter of policy? In this Article, we explore these two questions through a framework grounded in law and economics, specifically in administrative law and macroeconomics.[7] In Part I, we ask whether the Federal Reserve's adoption of new mandates could pass administrative law scrutiny. In Part II, we pivot to a normative analysis and analyze whether new mandates could present unfavorable macroeconomic tradeoffs given the agency's existing set of priorities and toolkit. Part II is important because even if a newly proposed mandate passes

-from-shunning-fossil-fuel-loans-idUSKBN22K2PU [https://perma.cc/ECM5-A5GW] (noting that Republicans accused Federal Reserve fiduciaries, e.g., BlackRock, of "halting loans and investments with companies that produce oil and other fossil fuels"); *see also* Rachel Frazin, *GOP Bill Would Codify Trump Rule on Financing for Fossil Fuels, Guns*, HILL (Feb. 25, 2021), https://thehill.com/policy/energy-environment/540474-republican-seeks-to-codify-trump-proposal-to-force-banks-to-finance [https://perma.cc/KFY5-G66J] (noting that Republicans were trying to force banks to serve the fossil fuel and firearms industries by passing a bill which would disqualify banks that discriminate against these industries from "borrow[ing] money from the Federal Reserve through its discount window lending program").

6. And, of course, whether they should do so. For a discussion of how the Federal Reserve impacts areas such as climate change, see, for example, Peter Conti-Brown & David Wishnick, *Technocratic Pragmatism, Bureaucratic Expertise, and the Federal Reserve*, 130 YALE L.J. 636 (2021); Christina Skinner, *Central Bank Activism*, 71 DUKE L.J. 247 (2021) [hereinafter *Central Bank Activism*]; Christina Skinner, *Central Banks and Climate Change*, 74 VAND. L. REV. 1301 (2021) [hereinafter *Central Banks and Climate Change*]; Jeremy Kress, *Banking's Climate Conundrum*, 59 AM. BUS. L.J. 679 (2022).

7. One of the leading voices in the field has come from Yair Listokin, along with his co-authors. For a sampling of Listokin's administrative law and macroeconomics work, see, for example, Peter Conti-Brown, Yair Listokin & Nicholas Parrillo, *Towards an Administrative Law of Central Banking*, 38 YALE J. ON REGUL. 1, 38–64 (2021); Yair Listokin & Daniel Murphy, *Macroeconomics and the Law*, 15 ANN. REV. L. & SOC. SCI. 377 (2019); Yair Listokin, *Law and Macroeconomics: The Law and Economics of Recessions*, 34 YALE J. ON REGUL. 791 (2017).

legal scrutiny—for example, through explicit congressional endorsement—its adoption might not be good policy, whether it is expressed as regulation or legislation.[8]

In Part I, we identify a variety of legal problems associated with the Federal Reserve's adoption of new mandates under its existing statutory authorities. We begin by observing that the Federal Reserve is rarely litigated against, and judges have shown "super-deference" to financial regulatory agencies when they *are* litigated against. Nevertheless, the adoption of new initiatives to protect the environment, address inequality, or take on other worthy but *novel* responsibilities would increase litigation risk, and the Federal Reserve would be subject to at least four different kinds of administrative law challenges. Two are based in the Federal Reserve's statutory authority and raised by the nondelegation doctrine and the major questions doctrine, both of which have some roots in separation of powers concerns.[9] The third pitfall depends upon how the Federal Reserve might act to develop its new responsibilities. If the central bank acts through guidance or informal supervisory communication, it could run afoul of the requirement that it act through either rulemaking or adjudication when making law. Finally, the Federal Reserve's new policy would be subject to arbitrary-and-capricious review.

In Part II, we analyze macroeconomic trade-offs. Just because adopting a new mandate is legal does not necessarily imply that it is good policy. Indeed, we argue that adopting new goals outside of the Federal Reserve's core mission would make it more difficult for the Federal Reserve to meet its existing charges (i.e., keeping inflation in check and maximizing employment). The underlying idea is that if the central bank increases

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8. We present the legal and economic analysis in sequential order for ease of explanation. Agencies do not have to sequence their decision-making such that legal matters are always considered first. That may be true for some legal issues. But others, like whether a given action is arbitrary and capricious, are sufficiently tied to the merits such that it may make sense to do a preliminary policy analysis first.

9. *See* Aditya Bamzai & Aaron L. Nielson, *Article II and the Federal Reserve*, 109 CORNELL L. REV. (forthcoming 2024) (examining the separation of powers concerns with the central bank).

interest rates to fight inflation, it might also decrease employment in the short run.[10] Higher interest rates make it more expensive for individuals and businesses to obtain credit, thereby slowing economic activity and hiring. We see this trade-off in play today: as the Federal Reserve hikes interest rates to combat heightened inflation, it risks slowing economic growth.[11] We analyze the trade-offs created by the imposition of new mandates both as a matter of economic logic and through a formal model.

In Part III, we apply our administrative-law-and-macroeconomics framework to actual proposals that aim to expand the central bank's existing set of mandates. We explore four case studies in particular: climate change, distributional impacts, the expansion of consumer financial services, and financial stability. While these case studies are specific to the Federal Reserve, we note that our framework is broadly applicable to other government agencies as well.[12]

Our generalizable insight is that there is a significant cost for an agency to adopt mandates untethered to its central mission because it lacks the tools and expertise to properly address them. Imagine, for instance, Congress asking the EPA to maximize employment while carrying out its original mandates related to environmental protection. It would have to balance the

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10. *See How Does the Federal Reserve Affect Inflation and Employment*, BD. OF GOVERNORS OF THE FED. RSRV. SYS., https://www.federalreserve.gov/faqs/money_12856.htm [https://perma.cc/DV2A-8V7B] (last updated Aug. 27, 2020) (explaining how interest rates affect inflation and unemployment rates); *see also* Koshy Mathai, *Monetary Policy: Stabilizing Prices and Output*, INT'L MONETARY FUND, https://www.imf.org/external/pubs/ft/fandd/basics/monpol.htm [https://perma.cc/K4D4-5AQG] (discussing the relationship between interest rates, inflation, and unemployment rates).

11. *See* Steve Liesman, *Most Investors, Economists See Fed Rate Hikes Causing a Recession Within One Year, CNBC Survey Shows*, CNBC (Jul. 26, 2022), https://www.cnbc.com/2022/07/26/most-investors-economists-see-fed-rate-hikes-causing-a-recession-within-one-year-cnbc-survey-shows.html [https://perma.cc/JD2L-U36Q] ("The Federal Reserve's efforts to cool inflation by hiking rates is most likely to lead to a recession . . . .").

12. As one FTC commissioner put it in the context of reassessing that agency's consumer protection goal, "it is mathematically impossible to maximize more than one value, so the pursuit of one goal will require tradeoffs that adversely impact other competing interests." Fed. Trade Comm'n, Dissenting Statement of Commissioner Christine S. Wilson Regarding the "Policy Statement Regarding the Scope of Unfair Methods of Competition Under Section 5 of the Federal Trade Commission Act," Commission File No. P221202, 2022 WL 16919446, at *6 (Nov. 10, 2022).

resources it devoted to protecting the environment against those it could devote to employment maximization—perhaps even by relaxing environmental rules for businesses to hire more workers. Moreover, the EPA would have to obtain new tools, information, and expertise as the new mandate would be so distant from its existing ones.

In this, we have some august support: the Nobel prize-winning economist Jan Tinbergen developed a principle that governments should use multiple policy instruments if they want to impact multiple policy targets.[13] Rather than using one central bank to pursue policies related to banking and other subjects, Tinbergen argued that policies should be directly targeted, rather than collaterally addressed, by a policymaker with other subjects on her plate.[14]

To be clear, Congress need not have a rule of "one agency, one mandate." Indeed, the Federal Reserve is charged with balancing inflation and employment as well as regulating banks and being on standby as the lender of last resort. We are not arguing for Congress to allocate these functions to separate agencies. We do argue, however, that these existing mandates are strongly correlated with each other. Maintaining the banking sector's stability is critical to both maximizing employment and price stability.[15] As we have unhappily seen, financial contagion generates economic crises that can hurt employment, damage price stability, or both.[16] Thus, adding more mandates that are only tangentially related, or unrelated, to the core economic-stability mandates exacerbates the trade-offs.

Finally, our analysis does not suggest that new mandates are unimportant or should not be considered by any agency. Nor does it preclude the private sector from pursuing its own profit-

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13. *See* JAN TINBERGEN, ON THE THEORY OF ECONOMIC POLICY 39–40 (1952).

14. *See id.*

15. *See* CHARLES P. KINDLEBERGER & ROBERT ALIBER, MANIAS, PANICS, AND CRASHES: A HISTORY OF FINANCIAL CRISES 191–212 (6th ed. 2011).

16. The classic account of this tendency may be *Manias, Panics, and Crashes: A History of Financial Crises*. *Id.* (analyzing the cyclical nature and common features of financial crises).

maximizing mandates.[17] Our analysis recommends that Congress empower the agencies most closely aligned to and directly involved with those objectives it seeks to achieve.

I. ADMINISTRATIVE LAW CONSTRAINTS

Congress has identified the Federal Reserve's core priorities: it must balance inflation and employment,[18] and it has been given some authority over financial stability because of the risk that a financial institution's collapse might lead to a larger economic crisis.[19] The first part of our framework is focused on administrative law constraints, as the central bank faces litigation risk if it tries to make policy in new areas tenuously related to its core responsibilities.

Indeed, the embrace of new mandates would be subject to a handful of different kinds of legal challenges, most of which would immerse the central bank in political fights that might threaten its independence. Two are statutory and are posed by the major questions and nondelegation doctrines, both of which require agency policymaking efforts to have been subject to clear delegations from Congress. Another obstacle might arise if the central bank acts through guidance, or informal supervisory communication. The Federal Reserve could be accused of failing to act through either rulemaking or adjudication when making law. And, of course, the Federal Reserve's new policy would also be subject to arbitrary-and-capricious review. Lastly, we note

17. *See* Sarah E. Light & Christina P. Skinner, *Banks and Climate Governance*, 121 COLUM. L. REV. 1895, 1898 (2021) ("[R]ather than government regulators dictating compliance with environmental standards to address climate risks and promote sustainable economic activities, banks themselves are acting as change agents with respect to their lending portfolios . . . .").

18. As Christina Skinner has observed, "it could very well be costly to democratic values were the Fed to sidestep the legislative process with measures to deter the banks that it oversees from lending to brown businesses or households." *Central Banks and Climate Change*, *supra* note 6, at 1354.

19. We also note that the Federal Reserve has limited consumer protection responsibilities. It must establish that banks do not discriminate in lending, that they do not refuse to lend in places where its depositors reside, and that they do not violate the consumer protection obligations that prevent banks from defrauding their depositors. *See The Fed Explained: What the Central Bank Does*, *infra* note 132, at 70 (discussing how the Federal Reserve supervises large financial institutions by setting compliance standards, such as "risk-based capital and leverage requirements"). For an in-depth discussion of the Federal Reserve's consumer protection duties, see *id.* at 113–29.

that some constitutional rights could be implicated, depending on how the Federal Reserve sets policy.

In defending this litigation, the Federal Reserve, like any administrative agency, could raise issues of timing and standing that can pose real hurdles to litigants dissatisfied with new government policies.[20] In Part III, we turn to some recent proposals to incentivize or persuade the Federal Reserve to adopt new mandates, which led us to examine whether the Federal Reserve could use procedural defenses to prevent courts from passing judgment on its potential new policymaking initiatives.

A. Litigating Against the Federal Reserve

Before we move to the administrative law doctrine, we explore a threshold question: will the Federal Reserve actually be sued? One might worry less about these sorts of administrative law constraints when one considers the Federal Reserve's very sparse litigation docket. The sparse docket, as a matter of formal law, is surprising. The central bank is as subject to the Administrative Procedure Act (APA) as any other agency.[21] Courts have frequently said that the ordinary standard of review for APA cases applies to financial regulators and that there is no reason to apply anything other than ordinary principles of administrative law to regulatory efforts by banking supervisors.[22]

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20. For an overview of some of these defenses, see Zachary D. Clopton, *Justiciability, Federalism, and the Administrative State*, 103 CORNELL L. REV. 1431, 1440–41 (2018) ("[S]tanding is about parties, ripeness and mootness are about timing. Ripeness asks if a dispute is sufficiently developed to invoke the power of the federal courts. . . . [M]ootness, meanwhile, asks whether a case is 'too late' for judicial determination.").

21. *See, e.g.*, Kaplan v. U.S. Off. of Thrift Supervision, 104 F.3d 417, 421 (D.C. Cir. 1997) (holding, contrary to the position advanced by the Office of Thrift Supervision (OTC), which has now been merged with the Office of the Comptroller of Currency (OCC), that for the conduct to constitute an unsafe or unsound practice the agency must show that there is some "undue risk to the institution" that is "reasonably foreseeable").

22. For example, because the assessment of safety and soundness—the core of banking supervision—is set forth in a statute that awards power to multiple agencies, the courts have often said that it would be inappropriate to defer to the interpretation of any one of the agencies charged with ensuring that any particular bank is in fact operating safely and soundly. *See, e.g.*, DeNaples v. OCC, 706 F.3d 481, 488 (D.C. Cir. 2013) ("[The court has] repeatedly pointed to the agencies' joint administrative authority under [the FDI Act] to justify refusing to defer to their interpretations."); Grant Thornton, LLP v. OCC, 514 F.3d

But if there is a stream of "banking regulation is regulation" decisions by appellate courts, there is also a doctrinal unwillingness to second-guess the decisions of financial regulators for almost any reason. Jurists as distinguished as Augustus Hand have said that monetary policymaking was all but committed to the government's discretion.[23] APA aside, many courts have extended a form of super-deference to the Federal Reserve. The Second Circuit has, for example, concluded that banking rescues should be reviewed not under an ordinary arbitrary standard, but a "grossly arbitrary" one.[24] Michael Barr, Howell Jackson, and Margaret Tahyar have characterized the review of chartering decisions—the question of whether a bank should be permitted to open—as one where courts often offer "extraordinary deference."[25] In addition, Federal Reserve decisions on whether bank mergers should be permitted have rarely ever been reversed by the courts, especially in recent decades.[26]

Perhaps because of the difficult doctrinal lift that banks must undergo to win against the Federal Reserve—or perhaps because they are worried about retaliation from regulators—

1328, 1331 (D.C. Cir. 2008) ("We review the OCC's interpretation of FIRREA and related statutory provisions *de novo* because multiple agencies besides the Comptroller administer the act, including the Board of Governors of the Federal Reserve [System], the Federal Deposit Insurance Corporation, and the Office of Thrift Supervision in the Treasury Department.").

23. *See* Raichle v. Fed. Rsrv. Bank of N.Y., 34 F.2d 910, 915 (2d Cir. 1929) ("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. Indeed, the correction of discount rates by judicial decree seems almost grotesque, when we remember that conditions in the money market often change from hour to hour, and the disease would ordinarily be over long before a judicial diagnosis could be made.").

24. *See* Huntington Towers, Ltd. v. Franklin Nat'l Bank, 559 F.2d 863, 868 (2d Cir. 1977) (holding that, while rescuing a bank, "[a]bsent clear evidence of grossly arbitrary or capricious action . . . it is not for the courts to say whether or not the actions taken were justified in the public interest, particularly where it vitally concerned the operation and stability of the nation's banking system").

25. MICHAEL S. BARR, HOWELL E. JACKSON & MARGARET E. TAHYAR, FINANCIAL REGULATION: LAW AND POLICY 169 (2d ed. 2018).

26. *See* Jeremy C. Kress, *Modernizing Bank Merger Review*, 37 YALE J. ON REGUL. 435, 458 (2020) ("Today, the agencies' merger decisions are effectively immune from judicial review because they no longer issue formal denials, and the public generally lacks standing to challenge merger approvals."). The Federal Reserve now generally approves mergers and counsels applicants with mediocre merger proposals to withdraw them.

banks rarely sue the Federal Reserve.[27] Between 2010 and 2020, the Federal Reserve reported being sued in approximately eight cases per year.[28] A total of eighty-three cases in one decade constitutes a very small number compared to other federal agencies. During the same decade, the EPA appeared in 369 cases in the nation's busiest administrative law court, the D.C. Circuit, *alone*.[29] The possibility that the Federal Reserve could adopt a controversial new mandate and still not get sued is real, which is worth noting as we proceed through the theoretical administrative law constraints.

On the other hand, extra-mandate policymaking is more likely to be the subject of litigation, because there are more potential plaintiffs and because some of those plaintiffs are well-advised, meaning that they are likely to develop their records cognizant of the procedural protections that the Federal Reserve has relied on in the past.[30] Some bankers may be willing to object to new regulatory missions despite the risks of retaliation by their supervisors. In 2015, a small bank stood in for a conservative constitutional challenge to various aspects of the Dodd-Frank Wall Street Reform Act;[31] other small banks could raise similar challenges to some of the novel mandates that have been proposed for the Federal Reserve.

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27. The claims were drawn from the Federal Reserve's annual reports over these years, and because the Federal Reserve does not get sued often, each case could be considered and analyzed. The Federal Reserve introduced its 2019 report as follows: "During 2019, the Board of Governors was a party in 7 lawsuits or appeals filed that year and was a party in 6 other cases pending from previous years, for a total of 13 cases. The Board intervened in or initiated one additional case relating to privileged documents or testimony. In 2018, the Board had been a party in a total of 19 cases. As of December 31, 2019, eight cases were pending." *106th Annual Report*, BD. OF GOVERNORS OF THE FED. RSRV. SYS. 349 (2019) https://www.federalreserve.gov/publications/files/2019-annual-report.pdf [https://perma.cc/CJX4-EFDV].

28. *See Annual Report*, BD. OF GOVERNORS OF THE FED. RSRV. SYS., https://www.federalreserve.gov/publications/annual-report.htm [https://perma.cc/NSC9-S6VG] (last updated July 14, 2023) (choose "HTML" or "PDF" of any given year; then choose "Litigation" to see pending and unresolved cases as of the publication of the report).

29. WESTLAW PRECISION, https://1.next.westlaw.com (search "Environmental Protection Agency" and narrow by jurisdiction to D.C. Circuit and date range from Jan. 1, 2010 to Dec. 31, 2019).

30. *See* David T. Zaring, *The Corporatist Foundations of Financial Regulation*, 108 IOWA L. REV. 1303, 1355 n.254 (2023).

31. *See* State Nat'l Bank of Big Spring v. Lew, 795 F.3d 48, 52 (D.C. Cir. 2015).

Other plaintiffs could come from outside banking—a risk the Federal Reserve has rarely had to face in the past.[32] Energy companies could posit that a climate rule affecting their access to credit is beyond the Federal Reserve's capabilities.[33] Payments processors could claim that the Federal Reserve's new forays into the payments system will hurt their businesses.[34] And a tweak of monetary policy designed to benefit some groups in particular, even the most worthy groups, could draw claims from those who would not benefit from the policy.[35]

States could also sue. The Supreme Court has held that it should be easier for states to establish that they have the standing to pursue a case that would affect their citizens. In *Massachusetts v. Environmental Protection Agency*, the Court found that the state of Massachusetts had standing to challenge the EPA's failure to regulate carbon dioxide and other greenhouse gases.[36] The Court held that states are entitled to "special solicitude" when it comes to standing issues, and found the state's case for injury—through injured citizens and harmed natural resources due to EPA inaction on greenhouse emissions—strong enough to entitle it to litigate its case.[37] Many states have now created professionalized solicitors general who excel at circumventing the procedural hurdles to a merits suit against administrative action.[38] These offices did not exist twenty years ago; now

32. *See, e.g.*, Zaring, *supra* note 30, at 1325 n.101 (noting that few non-bank plaintiffs sued the Federal Reserve during 2019); *see also 106th Annual Report*, *supra* note 27.

33. *See* Volcovici, *supra* note 5 (noting that some Republican lawmakers stated that "[c]onsidering BlackRock's central role as a Federal Reserve fiduciary for the distribution of CARES Act credit facilities, its hostility towards the American energy sector is unacceptable and should be closely scrutinized . . . .").

34. Zaring, *supra* note 30, at 1361.

35. There is a line of cases granting standing to economic competitors. *See, e.g.*, Clarke v. Sec. Indus. Ass'n, 479 U.S. 388, 403 (1987).

36. Massachusetts v. EPA, 549 U.S. 497, 517 (2007).

37. *Id.* at 520. Recently, to be sure, states have had less luck trading upon this special solicitude. *See, e.g.*, United States v. Texas, 143 S. Ct. 1964, 1970 (2023) (holding that, in a case where states sought to change the enforcement practices of the executive branch, "[t]he threshold question is whether the States have standing under Article III to maintain this suit. The answer is no"); *id.* at 1977 (Gorsuch, J., concurring) ("Nor has 'special solicitude' played a meaningful role in this Court's decisions in the years since.").

38. *See* Allison Orr Larsen & Neal Devins, *The Amicus Machine*, 102 VA. L. REV. 1901, 1917 (2016) ("Many states (currently the number has reached thirty-

they are staffed with excellent lawyers.[39] They have indicated that they are ready to sue government agencies that take on novel mandates. Indeed, West Virginia has successfully sued the EPA over its Clean Power Plan and has already threatened to sue the SEC over its proposed rule requiring public companies to disclose their climate-related emissions.[40]

The Federal Reserve is unlikely to be able to keep challenges to regulations adopted pursuant to new mandates out of court. With that in mind, we proceed to review the administrative law challenges that could arise.

B. Major Questions

The increasingly important and controversial major questions doctrine has been posited by some to be an extension of the nondelegation doctrine, which we briefly address in the next subsection.[41] In our view, the doctrine is something of an *anti-novelty* canon of legislative construction—and it is a real concern for the Federal Reserve when it comes to the question of whether it can adopt new mandates apart from its core objectives.

The major questions doctrine is best understood as a doctrine that originated as a necessary corollary to *Chevron* deference,[42] especially when that deference is afforded on the basis of

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eight) have built state solicitor general offices, modeled after the U.S. Solicitor General and typically staffed by former Supreme Court law clerks."); *see also* Jeffrey L. Fisher, *A Clinic's Place in the Supreme Court Bar*, 65 STAN. L. REV. 137, 140 (2013) ("Many states have followed [the federal government's] suit in recent years, establishing or enhancing existing solicitors general's offices."); William C. Kinder, *Putting Justice Kagan's "Hobbyhorse" Through Its Paces: An Examination of the Criminal Defense Advocacy Gap at the U.S. Supreme Court*, 103 GEO. L.J. 227, 247 (2014) (discussing the rise of the state solicitor general).

39. For a discussion of their history by James Ho, who served as the Solicitor General of Texas, see Symposium, *The Rise of Appellate Litigators and State Solicitors General*, 29 REV. LITIG. 545, 635–45 (2010).

40. *See* Letter from Patrick Morrisey, West Virgina Att'y Gen., to Hon. Allison Herren Lee, Acting Chair, SEC (Mar. 25, 2021), https://www.sec.gov/comments/climate-disclosure/cll12-8563794-230748.pdf [https://perma.cc/ZT87-H9BX].

41. *See also* Daniel T. Deacon & Leah M. Litman, *The New Major Questions Doctrine*, 109 VA. L. REV. 1009, 1012 (2023) (asserting that the "new" major questions doctrine requires explicit congressional authorization).

42. Chevron U.S.A., Inc. v. Nat. Res. Def. Council, Inc., 467 U.S. 837 (1984).

the text of the statute.[43] *Chevron* deference provides that when a court reviews an agency's construction of the statute the agency administers, a court must first determine whether Congress "has directly spoken to the precise question at issue."[44] If it has, the court must "give effect to the unambiguously expressed intent of Congress."[45] But if the statute is silent or ambiguous regarding the specific point, the court decides whether the agency interpretation is "based on a permissible construction of the statute."[46]

The major questions doctrine is a constraint on judicial deference to reasonable agency interpretations of ambiguous congressional grants of authority. It precludes agencies like the Federal Reserve from interpreting ambiguous grants of authority from Congress in ways that would allow them to take on expansive new responsibilities of economic or political magnitude—a new program to address climate change might be an example.[47]

However, the courts are more dubious of *Chevron* deference than they were in the past, and the Supreme Court has rooted the doctrine in "both separation of powers principles and a practical understanding of legislative intent."[48] Whatever its origins, the major questions doctrine is a real constraint on the adoption of new responsibilities by old agencies; the Court has used it to

43. *See, e.g.*, David T. Zaring, *The Government's Economic Response to the Covid Crisis*, 40 REV. BANKING & FIN. L. 315, 330 (2020). The corollary was necessary because it is easy to conclude that congressional directions contain some ambiguity. But "Congress, we have held, does not alter the fundamental details of a regulatory scheme in vague terms or ancillary provisions—it does not, one might say, hide elephants in mouseholes." Whitman v. Am. Trucking Ass'n, 531 U.S. 457, 468 (2001). We think that the original version of the major questions doctrine could deal with some of the extreme reliance on *Chevron* that many presidents succumb to. The Trump administration, for example, considered indexing capital gains for inflation without congressional consent—a trillion-dollar tax cut that would have been enacted not by Congress, but by the Treasury Department by a rule, or even less. *See* Daniel Hemel & David Kamin, *The False Promise of Presidential Indexation*, 36 YALE J. ON REGUL. 693, 695 (2019).

44. *Chevron*, 467 U.S. at 842.

45. *Id.* at 843.

46. *Id.*

47. *See* Jonas J. Monast, *Major Questions About the Major Questions Doctrine*, 68 ADMIN. L. REV. 445, 449, 488 (2016) (describing potential impacts of an expansive major questions doctrine specifically in the context of climate action).

48. West Virginia v. EPA, 142 S. Ct. 2587, 2609 (2022).

comprehensively limit regulatory policymaking.[49] It has been used in recent years to reverse a rental eviction moratorium issued by the Centers for Disease Control and Prevention,[50] a wide-ranging anti-climate change initiative issued by the EPA,[51] and a Department of Education effort to cancel $400 billion in student debt.[52]

In 2022, the Court indicated that it intended to take the major questions doctrine seriously with a last-day-of-term effort to gather the few cases applying the doctrine into a coherent whole. In *West Virginia v. EPA,* a case concerning the EPA's power to encourage power utilities to shift away from coal, and toward gas, wind, and solar, the Court explained that "in certain extraordinary cases . . . something more than a merely plausible textual basis for the agency action is necessary" to permit a new agency action to go forward.[53] To do so, the "agency instead must point to 'clear congressional authorization' for the power it claims."[54]

The major questions doctrine thus led the Court to presume that Congress wanted the EPA to use the Clean Air Act to do little more than to regulate emissions on a particularized basis—smokestack by smokestack, or plant by plant, rather than on an industry-wide basis, as its program to incentivize utilities to transition to cleaner forms of energy would have done. As the Court somewhat sarcastically put it,

> Under the Agency's prior view . . . , its role was limited to ensuring the efficient pollution performance of each individual regulated source. . . . Under its newly "discover[ed]" authority, however, EPA can demand much greater reductions in emissions based on a very different kind of policy judgment: that it would be "best" if coal made up a much smaller share of national electricity generation.[55]

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49. *See, e.g.*, *id.* at 2616 (invoking the major questions doctrine to invalidate the EPA's Clean Power Plan).

50. Ala. Ass'n of Realtors v. Dep't of Health & Hum. Servs., 141 S. Ct. 2485, 2490 (2021) (concluding that a federally imposed eviction moratorium should be authorized by Congress).

51. West Virginia v. EPA, 142 S. Ct. at 2595 (concluding that a decision to cap carbon emissions should be reserved for Congress).

52. Biden v. Nebraska, 143 S. Ct. 2355, 2375 (2023) (concluding that debt cancellation is a power Congress would have reserved for itself).

53. West Virginia v. EPA, 142 S. Ct. at 2609.

54. *Id.*

55. *Id.* at 2612 (citation omitted).

As we have observed, the Court indicated that the doctrine was rooted both in statutory interpretation principles and in considerations relating to the separation of powers.[56] And while it is by no means clear what the test for determining whether a regulatory endeavor is, in fact, an "extraordinary case" wanting application of the major question, the Court looked to "history and the breadth of the authority that the agency has asserted, and the economic and political significance" of the regulatory initiative.[57] Here, the Federal Reserve would be wading into dangerous legal territory if it attempted to add a new mandate (without congressional blessing) that is unrelated to its core monetary policy mission.

On this reading, once the major questions doctrine is triggered, the agency must point to a clear statement from Congress that it intended to delegate the power that the agency proposes to exercise to the agency. In *West Virginia*, the Court concluded that Congress had not.[58] The EPA's efforts to push power generation away from coal was rooted in a portion of the Clean Air Act that claimed to "empower[] [the EPA] to substantially restructure the American energy market," even though that portion used "vague language" and "was designed to function as a gap filler and had rarely been used in the preceding decades."[59]

The major questions doctrine, thus only recently named and acknowledged by the Supreme Court, has, unlike the nondelegation doctrine that we discuss below, a short origin story. The Court's first toe dip into the doctrine occurred in *MCI Telecommunications Corp. v. AT&T*, although there, the judicial analysis was linked closely to the *Chevron* doctrine obligating courts to defer to the reasonable interpretations by agencies of their governing statutes.[60] The Court had to interpret the Federal Communications Commission's power to "modify" tariffs, which it had interpreted to include the FCC's excusal of every long distance carrier from filing a tariff at all, except for AT&T, then the local telephone monopoly.[61] The Court reasoned that it was un-

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56. *Id.* at 2595.
57. *Id.* at 2608.
58. *Id.* at 2610.
59. *Id.*
60. MCI Telecomms. Corp. v. Am. Tel. & Tel. Co., 512 U.S. 218, 234 (1994).
61. *See id.* at 221–22.

likely that Congress would "effectuate an enormous and transformative expansion of the agency's regulatory authority"[62] with imprecise language in an old statute—in that case, the Federal Communications Act of 1934.[63]

The first full-blown entrance of the major questions doctrine appeared in *FDA v. Brown & Williamson Tobacco Corp*.[64] That case invalidated the FDA's effort to regulate tobacco products as "drug delivery devices" and the nicotine in tobacco as a "drug."[65] The literal language of the statute, which gave the agency the authority to regulate drugs and drug delivery devices, would seem to suggest that the FDA's assertion of jurisdiction over tobacco was entitled to deference because the statute was ambiguous as to what counted as drugs and drug delivery devices. This would, in turn, suggest that deference to the FDA's expert opinion would be appropriate. But the Court explained that Congress could not have intended to leave such a question to an agency alone. *Chevron* deference was not appropriate in such "extraordinary cases" where the jurisdictional question was one of "economic and political magnitude," and also where Congress had, over decades, developed a very different regulatory approach.[66]

In *King v. Burwell*, one of the challenges to the Affordable Care Act, the Court in 2015 took a slightly different approach to major questions by pulling the doctrine away from its *Chevron*-deference roots.[67] There, the Court ultimately reached the same conclusion as the Department of Health and Human Services in interpreting the Affordable Care Act—that language authorizing federal subsidies to state-created marketplaces for health insurance purchasers did not preclude the subsidies to a federal marketplace for health insurance purchases—not because the agency interpretation was reasonable but because the statute

62. Kevin O. Leske, *Major Questions About the "Major Questions" Doctrine*, 5 MICH. J. ENV'T & ADMIN. L. 479, 480 (2016).

63. *MCI Telecomms. Corp.*, 512 U.S. at 220.

64. FDA v. Brown & Williamson Tobacco Corp., 529 U.S. 120 (2000).

65. *Id.* at 131.

66. *Id.* at 123, 133.

67. King v. Burwell, 576 U.S. 473 (2015); *see also* Gonzales v. Oregon, 546 U.S. 243, 267 (2006) (testing whether the Attorney General could ban drugs used in state-legal assisted suicides, the Court stated that "[t]he idea that Congress gave the Attorney General such broad and unusual authority through an implicit delegation in the [Controlled Substances Act's] registration provision is not sustainable").

would not work as Congress intended without the assumption.[68] The Court explained that it had to interpret the statute in the way the government urged "to avoid the type of calamitous result that Congress plainly meant to avoid."[69] By taking away agency deference, the Court eliminated the opportunity for a future agency to reverse the decision.[70]

The major questions doctrine made a substantial impact only recently, however. In *Utility Air Regulatory Group v. EPA*,[71] the Court used the *Chevron* test to conclude that an agency could unreasonably interpret a statute if that interpretation would impact "a significant portion of the American economy."[72] As the Court put it, "if the statutory language is plain, we must enforce it according to its terms," a standard premise in statutory interpretation.[73] The rub came with the extent of the regulatory impact involved in the rule the Court was reviewing, which came from an initial version of the Clean Power Plan promulgated by the EPA. "In extraordinary cases," the Court concluded, "there may be reason to hesitate before concluding that Congress intended such an implicit delegation."[74]

The *West Virginia* case is the most elaborate invocation of the major questions doctrine that the current Supreme Court has taken up, but before it, the Court invoked major questions doctrine-like issues to scuttle two Biden-administration initiatives: (1) an eviction moratorium issued by the Centers for Disease Control and Prevention (CDC) to prevent landlords from forcing tenants to move during the COVID epidemic[75] and (2) an

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68. *See* Marla D. Tortorice, *Nondelegation and the Major Questions Doctrine: Displacing Interpretive Power*, 67 BUFF. L. REV. 1075, 1104 (2019) (analyzing the application of *Chevron* to the Affordable Care Act in *Burwell*).

69. *King*, 576 U.S. at 498.

70. *See id.*

71. Util. Air Regul. Grp. v. EPA, 573 U.S. 302 (2014).

72. *Id.* at 324.

73. *King*, 576 U.S. at 486.

74. West Virginia v. EPA, 142 S. Ct. 2587, 2608 (2022) (quoting FDA v. Brown & Williamson Tobacco Corp., 529 U.S. 120, 123 (2000)). For a discussion of these cases, and a critique, see Mila Sohoni, *The Major Questions Quartet*, 136 HARV. L. REV. 262, 266 (2022) ("In none of the three cases in which the government lost did the Court adequately ground its momentous and new clear statement rule with a meaningful constitutional justification.").

75. Ala. Ass'n of Realtors v. Dep't of Health & Hum. Servs., 141 S. Ct. 2485 (2021).

Occupational Safety and Health Administration (OSHA) emergency rule that required large employers to prove that their employees were vaccinated or to make them undergo regular testing.[76]

As for the eviction moratorium issued by the CDC, the Court reversed the agency action in a way that again invoked the major questions doctrine.[77] The Court noted that the moratorium was important—it applied to "at least 80 percent of the country."[78] Moreover, the fact that Congress had provided almost $50 billion in emergency rental assistance demonstrated the moratorium's economic impact.[79] The moratorium also interfered with landlord-tenant relationships, a domain reserved for state law.[80] The Court concluded that its precedents required Congress to enact "exceedingly clear" language if it wanted to significantly change the balance between federal and state power and the power of the government over private property.[81]

In sum, it is our view that the major questions doctrine is akin to an anti-novelty canon of legislative construction. It is a real concern for the Federal Reserve as to whether it can adopt new mandates apart from its core macroeconomic objectives.[82] The major questions doctrine is particularly relevant for federal agencies that rely on old statutes to make new policy—and the Federal Reserve derives much of its authority from the Federal Reserve Act, which was first passed in 1913. It was given its new

76. Nat'l Fed'n of Indep. Bus. v. Dep't of Lab., Occupational Safety & Health Admin., 142 S. Ct. 661 (2022). The per curium opinion in the OSHA Vaccine Mandate case had not mentioned the major questions doctrine nor came up with a new test—but Justice Gorsuch's concurring opinion did. *Id.* at 667 (Gorsuch, J., concurring). He argued that "when it comes to that obligation, this Court has established at least one firm rule: 'We expect Congress to speak clearly' if it wishes to assign to an executive agency decisions 'of vast economic and political significance.'" *Id.* (quoting *Ala. Ass'n of Realtors*, 141 S. Ct. at 2489). He argued that OSHA's mandate "fails that doctrine's test" as the issue in hand was indeed a major question of significant importance, yet "Congress has chosen not to afford OSHA—or any federal agency—the authority to issue a vaccine mandate." *Id.* at 667–68.

77. *Ala. Ass'n of Realtors*, 141 S. Ct. at 2485.

78. *Id.* at 2489.

79. *Id.*

80. *Id.*

81. *Id.*

82. *But see* Graham S. Steele, *Major Questions' Quiet Crisis*, 31 GEO. MASON L. REV. (forthcoming 2023) (arguing that the major questions doctrine should not apply to financial regulation).

mandates in the Humphrey Hawkins Act, passed almost half a century ago. And the Federal Reserve has never issued environmental regulations, sought to create relationships with individual consumers, or based its macroeconomic policy on the fortunes of a subset of Americans in the past.

C. NONDELEGATION

The nondelegation doctrine prohibits Congress from delegating its legislative powers to other entities, including the President, administrative agencies, and, perhaps most disfavorably, private organizations. The doctrine is one of the classic constraints on the administrative state, often taught in the first week of an administrative law class in law school, but it is rarely deployed successfully. Invoking it against the Federal Reserve would be novel and would affect every regulator faced with a new problem and armed with an old statute granting authority to oversee a particular industry. The statute that created the Federal Reserve was passed in 1913, despite having been regularly amended, so the application of the doctrine to the agency's authority would certainly disturb settled expectations.[83] It would also be a novel application of nondelegation, which has in the past been used to police novel delegations by Congress, not longstanding ones.[84]

The nondelegation doctrine has a long history. As courts wrestled with the prospect of Congress delegating its lawmaking authority, they approached the rise of the administrative state with a combination of hostility and resignation. In *J.W. Hampton v. United States*, the Court ruled that Congress must give its delegates an "intelligible principle" on which to base their legislation-like regulatory actions and that, if it did so, it could appropriately transfer some of its legislative responsibilities.[85] The doctrine has not been used to strike down legislation since 1935,

83. *See, e.g.*, Federal Reserve Act of 1913, Pub. L. No. 63-43, 38 Stat. 251.

84. *See, e.g.*, *id.*

85. J.W. Hampton v. United States, 276 U.S. 394, 409 (1928) ("If Congress shall lay down by legislative act an intelligible principle to which the person or body authorized to fix such rates is directed to conform, such legislative action is not a forbidden delegation of legislative power.").

so although it is an "axiom in constitutional law,"[86] it is a doctrine that has, as Cass Sunstein has put it, had "one good year, and 211 bad ones (and counting)."[87]

Yet, since 2019, with Justice Neil Gorsuch filing a dissenting opinion expressing his interest in revitalizing the nondelegation doctrine in *Gundy v. United States*, it has become less clear whether the doctrine would remain moribund.[88] Three justices joined his opinion, and a fourth and fifth indicated their receptiveness to the reinvigoration possibility.[89] In 2022, Justice Neil Gorsuch filed a concurring opinion that reiterated his position on the nondelegation doctrine when the Court blocked the Biden Administration's vaccination mandate.[90] This time, he was no longer in the minority camp. And in this opinion, he tied the nondelegation doctrine and major questions doctrine together, stating that the two "serve[] [a] similar function" as they "[b]oth serve to prevent 'government by bureaucracy supplanting government by the people.'"[91]

Of course, nondelegation is an easier concept to grasp than to fully revive. Justice Kagan wrote in her plurality opinion in *Gundy* that if the Court really began to strike down congressional delegations on the basis of whether Congress had directly spoken to the issue on which an agency proposed to regulate, the

86. Field v. Clark, 143 U.S. 649, 697 (1892) (Lamar, J., concurring) ("That no part of this legislative power can be delegated by Congress to any other department of the government, executive or judicial, is an axiom in constitutional law . . . .").

87. Cass R. Sunstein, *Nondelegation Canons*, 67 U. CHI. L. REV. 315, 322 (2000).

88. Gundy v. United States, 139 S. Ct. 2116, 2130 (2019) ("[I]t is small wonder that we have almost never felt qualified to second-guess Congress regarding the permissible degree of policy judgment that can be left to those executing or applying the law." (quoting Mistretta v. United States, 488 U.S. 361, 416 (1989) (Scalia, J., dissenting))).

89. *Id.* at 2131 (Alito, J., concurring) ("If a majority of this Court were willing to reconsider the approach we have taken for the past 84 years, I would support that effort."). Justice Kavanagh later wrote that "Justice Gorsuch's thoughtful *Gundy* opinion raised important points that may warrant further consideration in future cases." Paul v. United States, 140 S. Ct. 342, 342 (2019) (mem.).

90. Nat'l Fed'n of Indep. Bus. v. Dep't of Lab., Occupational Safety & Health Admin., 142 S. Ct. 661, 667 (2022) (Gorsuch, J., concurring).

91. *Id.* at 669 (alteration in original) (quoting Antonin Scalia, *A Note on the Benzene Case*, 4 REGUL.: AEI J. ON GOV'T & SOC'Y 25, 27 (1980)).

consequences would be dramatic—in fact, "most of Government is unconstitutional."[92]

The problem for the Federal Reserve would be whether its new mandates would be consistent with its dual mandate and other congressional responsibilities explicitly given to it. If they were, "the law would afford [the Federal Reserve] discretion—and certainly impose no 'specific restrictions' that 'meaningfully constrai[n]' the agency."[93] But if they were not, then the Federal Reserve would have to identify an intelligible principle that Congress gave the Federal Reserve to justify its adoption of a new mandate.

D. PROCEDURAL HURDLES

In recent years, many representatives of regulated industries, including banks, have loudly complained that agencies rely too much on so-called guidance to evade judicial review.[94] Generally, the idea is that a rule designed to have "the force of law" must go through notice-and-comment rulemaking. The Federal Reserve does not ignore notice-and-comment rulemaking. In the decade between 2012 and 2022, it issued 320 final rules.[95] But during that decade, it also issued 146 supervisory guidance letters, which did not go through notice and comment.[96] And, in the past five years, the Federal Reserve has issued seventeen "reports, manuals, and other guidance that inform public understanding of how it supervises and regulates financial institutions

92. *Gundy*, 139 S. Ct. at 2130.

93. *Nat'l Fed'n of Indep. Bus.*, 142 S. Ct. at 669 (quoting Touby v. United States, 500 U.S. 160, 166–67 (1991)).

94. Accordingly, the courts have developed some doctrines designed to create "safeguards against agencies evading both judicial review and notice and comment by acting via nonlegislative rules." Cal. Cmtys. Against Toxics v. EPA, 934 F.3d 627, 636 (D.C. Cir. 2019).

95. *See* FED. REGISTER, https://www.federalregister.gov [https://perma.cc/7AYS-UJJP] (click "Advanced Document Search" under "Search" hyperlink and narrow dates from "01/01/2012 to 12/31/2022" under "Publication Date," "Rule" under "Type," and "Federal Reserve System" under "Agency").

96. *See Guidance & Supervision*, BD. OF GOVERNORS OF THE FED. RSRV. SYS., https://www.federalreserve.gov/supervisionreg.htm [https://perma.cc/A4FX-G62Y] (follow "Supervision and Regulation" hyperlink and click on "View by year" hyperlink to view supervisory letters issued by year).

to ensure they operate safely and soundly."[97] Moreover, much of the Federal Reserve's routine intercourse with banks takes the form of letters that outline matters requiring attention (MRAs) and matters requiring immediate attention (MRIAs). These have—although we cannot be sure, because the letters are not made public—led to "a vast consulting-industrial complex [that] has sprung up around the new high-volume, low-value MRA model."[98]

The informal notice-and-comment rulemaking provisions of Section 553 of the APA apply to most cases where an agency acts legislatively and prospectively.[99] They require that a proposed rule be published in the Federal Register and opened for comment from the public; the agency must consider public comments before amending the rule and promulgating a final version.[100] The APA's legislative history suggests that "matters of great import, or those where the public submission of facts will be either useful to the agency or a protection to the public, should naturally be accorded more elaborate public procedures"—a position that would suggest that notice-and-comment rulemaking is superior to regulation through guidance when the matter is an important one.[101] In this, the Federal Reserve appears to agree with us. It recently codified an interagency rule on the role of supervisory guidance through notice-and-comment rulemaking, in an effort to set the rules of the road for guidance.[102]

Courts have generally looked to see whether purportedly interpretive rules actually have legal effect if (1) the agency would have the power to enforce in the absence of the rule, (2) the agency publishes the rule, (3) the agency invoked its legislative authority when promulgating the rule, or (4) the rule amends a

97. *See Guidance & Supervision*, BD. OF GOVERNORS OF THE FED. RSRV. SYS., https://www.federalreserve.gov/publications/guidance-and-supervision.htm [https://perma.cc/ANF8-VUCK] (last updated Oct. 13, 2022).

98. *See* Greg Baer & Jeremy Newell, *The MRA Is the Core of Supervision, but Common Standards and Practices Are MIA*, BANK POL'Y INST. (Feb. 8, 2018), https://bpi.com/the-mra-is-the-core-of-supervision-but-common-standards-and-practices-are-mia [https://perma.cc/SS4R-9YAU].

99. Administrative Procedure Act, 5 U.S.C. § 553.

100. *Id.*

101. S. REP. NO. 79-248, at 201 (1946).

102. *See* Role of Supervisory Guidance, 86 Fed. Reg. 18173 (Apr. 8, 2021), https://www.federalregister.gov/documents/2021/04/08/2021-07146/role-of-supervisory-guidance [https://perma.cc/KWQ4-KGTR] (codified at 12 C.F.R. pt. 262).

prior legislative rule.[103] If a guidance document "alters the legal regime," then it should have gone through notice-and-comment rulemaking.[104] Moreover, where guidance constitutes an action "by which rights and obligations have been determined, or from which legal consequences will flow," it also must go through notice and comment.[105] Failure to go through notice-and-comment rulemaking when promulgating a legislative rule requires that the rule be vacated, unless the agency had good cause not to go through notice and comment (such as if it was an emergency), or if the failure to comply with the procedures was harmless.[106] The Fifth Circuit found that agency guidance on which immigration cases to prioritize amounted to an effort to create a federal policy on immigration without going through the requisite notice-and-comment rulemaking.[107]

The issue for the Federal Reserve here is that if a court found it was adopting a new mandate without going through these procedures—for example, implementing a climate change commitment through its supervisory process, or via a document outlining how it understood the dual mandate to encompass new priorities with regard to equity—the Federal Reserve could run into trouble under the APA.[108]

E. CONSTITUTIONAL LAW

Although we have focused on administrative law in this Part, we close by observing that the Federal Reserve's actions also could be challenged on constitutional law grounds. Indeed, depending on how the Federal Reserve pursued new mandate objectives, it could run afoul of the First Amendment—the fate of many regulations these days.[109] For instance, if the Federal

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103. *See, e.g.*, Am. Mining Cong. v. EPA, 824 F.2d 1177, 1179 (D.C. Cir. 1987).

104. Bennett v. Spear, 520 U.S. 154, 169 (1997).

105. *Id.* at 177–78.

106. *See* JARED P. COLE, CONG. RSCH. SERV., R44356, THE GOOD CAUSE EXCEPTION TO NOTICE AND COMMENT RULEMAKING: JUDICIAL REVIEW OF AGENCY ACTION 17 (2016) (discussing the good cause exception to notice-and-comment rulemaking process).

107. Texas v. United States, 809 F.3d 134, 169 (5th Cir. 2015).

108. *See* Christina P. Skinner, *Presidential Pendulums in Finance*, 2020 COLUM. BUS. L. REV. 532 (2020).

109. *See* Jack M. Balkin, *Republicanism and the Constitution of Opportunity*, 94 U. TEX. L. REV. 1427, 1446 (2016) ("By the early twenty-first century,

Reserve obligated banks to make disclosures about climate, inclusion, or equity in ways that suggested that the disclosing bank was not committed to these values—and if it required the bank to make those disclosures public, as opposed to confidential disclosures to the Federal Reserve's supervisors—the agency could be seen as requiring a bank to "confess blood on its hands," a form of compelled speech that industry has used to defeat financial regulations in other contexts.[110] For example, the D.C. Circuit has held that requiring manufacturers to reveal whether their inputs were "DRC conflict free," that is, not sourced from an African region undergoing civil strife, violated the First Amendment's protection against compelled speech.[111] Forcing banks to disclose whether they lent to companies that were not "DRC conflict free" would be the sort of regulatory requirement that may not survive judicial review, and one could imagine, depending on the way the regulator required the disclosure, that forcing a bank to reveal what kind of politically unpopular lending it was engaged in on a number of fronts would be at risk for a similar kind of judicial revision.[112]

The particular protections afforded speech in recent years mark a change in judicial policy. Disclosure regulation, which amounts, after all, to compelled speech, did not typically raise First Amendment concerns.[113] Many of the disclosure requirements banks face are disclosures to regulators, rather than to the general public. The First Amendment has not yet reached

the First Amendment has become the most powerful antiregulatory tool in the information age, especially in a world in which information and information goods are central to markets."); *see also* Amanda Shanor, *The New* Lochner, 2016 WIS. L. REV. 133, 171 (2016) ("The very feature that makes modern forms of regulation 'lighter-touch' is what brings it in greater potential conflict with the First Amendment.").

110. *See* Nat'l Ass'n of Mfrs. v. SEC, 748 F.3d 359, 371 (D.C. Cir. 2014) ("By compelling an issuer to confess blood on its hands, the statute interferes with that exercise of the freedom of speech under the First Amendment.").

111. *See id.* at 373.

112. *See id.*

113. *See* Michael R. Siebecker, *Corporate Speech, Securities Regulation, and an Institutional Approach to the First Amendment*, 48 WM. & MARY L. REV. 613, 619–20 (2006); *see also* Frederick Schauer, *The Boundaries of the First Amendment: A Preliminary Exploration of Constitutional Salience*, 117 HARV. L. REV. 1765, 1778 (2004) ("A prime example of speech residing almost imperceptibly outside the First Amendment's boundaries is the speech that is the primary target of federal securities regulation.").

those disclosures. But public disclosures are different. If the Federal Reserve tried to encourage banks to adopt particular policies by obligating them to disclose their approaches to climate or equity, the Federal Reserve could create the grounds for a First Amendment challenge.

To be sure, the government can regulate commercial speech, like advertising. Commercial speech restrictions are subject to intermediate scrutiny under the First Amendment, meaning that they must promote a reasonable government objective and be narrowly tailored to meet that objective.[114] As the Court outlined the test in the utility advertising case *Central Hudson v. Public Service Commission of New York*,

> [a]t the outset, we must determine whether the expression is protected by the First Amendment. For commercial speech to come within that provision, it at least must concern lawful activity and not be misleading. Next, we ask whether the asserted governmental interest is substantial. If both inquiries yield positive answers, we must determine whether the regulation directly advances the governmental interest asserted, and whether it is not more extensive than is necessary to serve that interest.[115]

The *Central Hudson* test does not apply to all sorts of speech. The state must be allowed to require its citizens to file accurate tax forms and to require businesses to disclose the impact of their activities. Government requirements that firms disclose "purely factual and uncontroversial information," like proscriptions to disclosure financial statements under Generally Accepted Accounting Principles, are reviewed only for a rational basis.[116]

The problem arises when the government forces businesses to disclose information that makes the businesses look bad. Consider when the SEC required publicly traded firms to assess whether they used "conflict minerals" in their manufactured products. "By compelling an issuer to confess blood on its hands, the statute interferes with that exercise of the freedom of speech under the First Amendment."[117] This sort of libertarian approach to commercial speech has plenty of critics, but it has

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114. *See* Bd. of Trs. of State Univ. of N.Y. v. Fox, 492 U.S. 469, 478 (1989).

115. Cent. Hudson Gas & Elec. Corp. v. Pub. Serv. Comm'n of N.Y., 447 U.S. 557, 566 (1980).

116. *See* Zauderer v. Off. of Disciplinary Couns. of the Sup. Ct. of Ohio, 471 U.S. 626, 651 (1985).

117. Nat'l Ass'n of Mfrs. v. SEC, 748 F.3d 359, 371 (D.C. Cir. 2014).

proven to be popular with both the Supreme Court and D.C. Circuit.[118]

Rules or guidance obligating banks to report on matters they do not want to report about—possible risks for climate, inclusion, and inequality disclosures—could be susceptible to this sort of First Amendment challenge. Some of the new proposed mandates for the Federal Reserve fall under the rubric of addressing the very real problems of racial and gender equity that the country faces. The legal constraint here lies in the Equal Protection Clause of the Constitution, which provides that the government shall not "deny to any person within its jurisdiction the equal protection of the laws."[119] The Supreme Court has applied this requirement to the federal government pursuant to the Due Process Clause of the Fifth Amendment.[120] Under that clause, courts apply strict scrutiny, which is almost always "fatal in fact," to laws that include "suspect classifications," including classifications on the basis of race or ethnicity.[121] Efforts to get the Federal Reserve to prioritize the economic outcomes of specific racial or ethnic groups would be at risk under this paradigm.[122]

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118. *See* Cass R. Sunstein & Adrian Vermeule, *Libertarian Administrative Law*, 82 U. CHI. L. REV. 393, 426 (2015) ("[Commercial speech cases] raise grave questions about compulsory disclosure, which is an increasingly popular (and minimally intrusive) regulatory tool."); *see also* Amanda Shanor, *supra* note 109, at 171 ("[T]he modern state regulates in ways that appear, or are more prone to appear, speech-regulating than earlier forms of administration.").

119. U.S. CONST. amend. XIV, § 1.

120. *See* Bolling v. Sharpe, 347 U.S. 497, 499 (1954) (holding that discrimination which violates equal protection "may be so unjustifiable as to be violative of due process").

121. Gerald Gunther famously described strict scrutiny as "'strict' in theory and fatal in fact." Gerald Gunther, *Foreword: In Search of Evolving Doctrine on a Changing Court: A Model for a Newer Equal Protection*, 86 HARV. L. REV. 1, 8–9 (1972). For what it is worth, the Supreme Court noted in an earlier affirmative action case that "we wish to dispel the notion that strict scrutiny is 'strict in theory, but fatal in fact.'" Adarand Constructors, Inc. v. Pena, 515 U.S. 200, 237 (1995). A somewhat aged empirical study concluded that "[r]ather than 'fatal in fact,' strict scrutiny is survivable in fact." Adam Winkler, *Fatal in Theory and Strict in Fact: An Empirical Analysis of Strict Scrutiny in the Federal Courts*, 59 VAND. L. REV. 793, 796 (2006).

122. *See infra* Part III.B.

II. MACROECONOMIC TRADE-OFFS

In the second part of our framework, we pivot from the "can we" question to the "should we" question. We specifically ask whether the new mandate could exacerbate macroeconomic trade-offs, thereby detracting from the Federal Reserve's central mission.[123] In other words, even if it is legally permissible for the Federal Reserve to adopt a new mandate under existing statutory authorities, it still might not be the right policy decision, given the central bank's priorities and limited set of tools, information, and expertise. Congress is subject to the same normative policy consideration when it is deciding whether to require an agency to assume an expanded role.

We proceed by first explaining the theory of constrained optimization and then applying it to the Federal Reserve's conduct of monetary policy. Central banks, like individuals and firms, optimize their decisions subject to constraints. The Federal Reserve, in particular, is subject to a dual mandate when setting monetary policy.[124] It has to keep inflation in check while seeking to obtain maximum employment.[125] We therefore illustrate the Federal Reserve's constrained decision-making process using a stylized model in which the central bank has one main policy tool—its ability to adjust the interest rate—and observe that its one policy tool has opposite effects on its two monetary policy objectives: inflation and employment. The insight is that if the central bank increases interest rates to fight inflation, it might also decrease employment in the short run.[126] Higher interest rates would reduce economic activity and decrease hiring by making borrowing more expensive.

The Federal Reserve executes its core mission of maintaining economic stability by reconciling its two mandates: increasing employment and decreasing inflation. Setting the interest

123. In this Part, we use "mandates," "targets," and "objectives" interchangeably. They certainly have different legal definitions but are equivalent for purposes of our economic analysis.

124. *See* 12 U.S.C. § 225a ("[T]he Federal Reserve System . . . [works] to promote effectively the goals of maximum employment, stable prices, and moderate long-term interest rates.").

125. *See id.*

126. *See What Is the FOMC and When Does It Meet?*, *supra* note 2 (discussing Federal Reserve's sometimes competing goals of maximum employment and stable prices); *see also* Mathai, *supra* note 10 (discussing the relationship between interest rates and the net worth of individuals and businesses).

rate is the only tool it has to do both jobs, prompting the concern that it cannot optimize both at once. Adding a hypothetical new third mandate risks the subversion of all three mandates. An alternative approach is for Congress to empower the agencies most closely aligned with those objectives it seeks to achieve.

A. THE THEORY OF CONSTRAINED OPTIMIZATION

Pick up any basic microeconomics textbook,[127] and you will see a simple mathematical problem like this one: Jay is trying to decide the quantities to purchase of two different goods—call them ice cream (q_1) with price p_1 and coffee (q_2) with price p_2—and he is subject to a budget constraint of $20. This is a constrained optimization problem because Jay is trying to optimize—or, more specifically, to maximize—his utility subject to a budget constraint. Thus, one can write Jay's constrained optimization problem as maximizing his utility function $u(q_1, q_2)$ subject to spending $20:

$$\max u(q_1, q_2)$$

$$\textit{subject to}$$

$$p_1 q_1 + p_2 q_2 = \$20$$

Jay effectively makes only one choice: he can decide an amount of either q_1 or q_2—the amount of either ice cream or coffee—because his $20 budget constraint will then dictate how much of the second item he can purchase.[128] At the end of the day, the more of one item Jay decides to purchase, the less of the second item he can have. This is the inherent trade-off in constrained optimization.

Jay's dilemma involving ice cream and coffee may seem awfully trivial, but this example provides important insights for the rest of our discussion in this Part and throughout the Article. Because central banks are also trying to solve a constrained optimization problem in the context of monetary policy, they similarly face trade-offs in trying to achieve their desired objectives.

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127. *See, e.g.*, HAL R. VARIAN, INTERMEDIATE MICROECONOMICS: A MODERN APPROACH (Jack Repcheck ed., 8th ed. 2010).

128. Sorry, affogatos are not allowed in this illustration. Jay must consume ice cream and coffee separately. We are purists here.

B. THE FEDERAL RESERVE'S "DUAL MANDATE"

The Federal Reserve's current monetary policy mandate comes from the Federal Reserve Reform Act of 1977,[129] which modified the original Federal Reserve Act of 1913. Specifically, Congress tasked the Federal Reserve with "promot[ing] effectively the goals of maximum employment, stable prices, and moderate long-term interest rates" in its conduct of monetary policy.[130] As explained by former Federal Reserve Governor Frederic Mishkin, since long-term interest rates can remain low only in a stable macroeconomic environment, these goals are often referred to as the "dual mandate."[131] That is, the Federal Reserve seeks to promote the two *coequal* objectives of maximum employment and price stability.[132] Most of the time, the Federal Reserve's goals for employment and inflation are complementary. There are, however, situations where its goals are pulling in opposite directions, which we discuss in the next section.

The dual mandate, particularly the full employment half of the dual mandate, has its roots in the Great Depression, when

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129. Federal Reserve Reform Act of 1977, Pub. L. No. 95-188, 91 Stat. 1387. Interestingly, the Federal Reserve was not founded to conduct monetary policy, which is what many think of today when they think of the Federal Reserve. The Federal Reserve was established to preserve financial stability. *See* Ben S. Bernanke, Chairman, Bd. of Governors of the Fed. Rsrv. Sys., Address at the National Bureau of Economic Research Conference: A Century of U.S. Central Banking: Goals, Frameworks, Accountability (July 10, 2013), (transcript available at https://www.federalreserve.gov/newsevents/speech/bernanke20130710a.htm [https://perma.cc/F826-B23L]).

130. 12 U.S.C. § 225a.

131. Frederic S. Mishkin, Governor, Bd. of Governors of the Fed. Rsrv. Sys., Address at Bridgewater College: Monetary Policy and the Dual Mandate (Apr. 10, 2007), (transcript available at https://www.federalreserve.gov/newsevents/speech/mishkin20070410a.htm [https://perma.cc/E2RN-39W8]).

132. *See id.*; *see also* Aaron Steelman, *The Federal Reserve's "Dual Mandate": The Evolution of an Idea*, THE FED. RSRV. BANK OF RICHMOND: ECON. BRIEF 1 (Dec. 2011), https://www.richmondfed.org/-/media/RichmondFedOrg/publications/research/economic_brief/2011/pdf/eb_11-12.pdf [https://perma.cc/YV7M-ZEU7] ("Since 1977, the Federal Reserve has operated under a mandate from Congress to 'promote effectively the goals of maximum employment, stable prices, and moderate long term interest rates'—what is now commonly referred to as the Fed's 'dual mandate.'"); *The Fed Explained: What the Central Bank Does*, FED. RSRV. SYS. 22 (2021), https://www.federalreserve.gov/aboutthefed/files/the-fed-explained.pdf [https://perma.cc/MDE3-3PFX] ("Because long-term interest rates remain moderate in a stable economy with low expected inflation, this set of goals is often referred to as the dual mandate, comprising the coequal objectives of maximum employment and price stability.").

unemployment was systemic and human suffering was widespread.[133] After World War II came to an end, lawmakers were concerned that millions of American soldiers returning home would face Depression-era conditions.[134] In response, Congress passed the Employment Act of 1946, which directed the federal government to pursue "conditions under which there will be afforded useful employment for those able, willing, and seeking work, and to promote maximum employment, production, and purchasing power."[135] Notably, this Act did not target the Federal Reserve in isolation.

With concerns about unemployment again on the rise, in 1976, Senator Hubert Humphrey and Congressman Augustus Hawkins sponsored legislation promoting full employment.[136] Their efforts resulted in the 1977 amendment to the Federal Reserve Act, mandating the Federal Reserve's monetary policy promote "the goals of maximum employment, stable prices, and moderate long-term interest rates"[137]—the dual mandate as we know it today.[138] Subsequently, in 1978, Congress passed the Humphrey-Hawkins Full Employment and Balanced Growth Act, "requiring that the Federal Reserve regularly report to Congress on how monetary policy was supporting the twin goals."[139]

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133. *See* Lael Brainard, Governor, Bd. of Governors of the Fed. Rsrv. Sys., Address at the Harvard University EC10 Conference: How Should We Think About Full Employment in the Federal Reserve's Dual Mandate? (Feb. 24, 2021), (transcript available at https://www.federalreserve.gov/newsevents/speech/brainard20210224a.htm [https://perma.cc/L78Z-MM5S]) ("The belief that the federal government has a responsibility for full employment has its roots in the Great Depression.").

134. *Id.*; Bernanke, *supra* note 129 ("With respect to goals, the high unemployment of the Depression—and the fear that high unemployment would return after World War II—elevated the maintenance of full employment as a goal of macroeconomic policy.").

135. *See* Brainard, *supra* note 133 (quoting Employment Act of 1946, Pub. L. No. 79-304, 60 Stat. 23, as amended by the Full Employment and Balanced Growth Act of 1978, Pub. L. No. 95-523, § 102, 92 Stat. 1887, 1890 (codified at 15 U.S.C. § 1021)).

136. *Id.*

137. *Id.* (quoting 12 U.S.C. § 225a).

138. *See* 12 U.S.C. § 225a.

139. *See* Brainard, *supra* note 133; Full Employment and Balanced Growth Act of 1978, Pub. L. No. 95-253, 92 Stat. 1887 (requiring the Federal Reserve's Board of Governors to submit independent written reports to Congress biannually).

The vast majority of central banks around the world do not conduct monetary policy subject to a dual mandate. Instead, they typically operate under a single mandate, focused squarely on keeping inflation in check.[140] As noted by former Federal Reserve Vice Chair Lael Brainard:

> A few other central banks have an explicit employment mandate that has coequal weight as their price-stability mandate, such as the Reserve Bank of Australia and the Reserve Bank of New Zealand or most central banks, however, price stability is the single objective of monetary policy (Bank of Canada, Riksbank, and Bank of Japan) or its priority objective (for example, European Central Bank and Bank of England).[141]

C. THE FEDERAL RESERVE'S CONSTRAINED OPTIMIZATION PROBLEM

We now proceed to formalize the Federal Reserve's dual mandate by building upon the introductory constrained optimization problem presented above. In 1958, A.W. Phillips examined U.K. unemployment and wages from 1861–1957, and saw an inverse relationship between the level of unemployment and the rate of change in wages (i.e., wage inflation).[142] The thinking behind the Phillips curve was that lower unemployment is associated with higher inflation, while higher unemployment is associated with lower inflation.[143] As Michael Ng, David Wessel, and Louise Sheiner have explained, "when there are lots of unfilled jobs and few unemployed workers, employers will have to

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140. *See* Urban Bäckström, Governor, Sveriges Riksbank, Address at the Handelsbanken's Seminar: Maintaining Price Stability (Jan. 28, 1997) (transcript available at https://archive.riksbank.se/pagefolders/2874/970128e.pdf [https://perma.cc/VA8C-6QQM]) ("For most central banks today the primary monetary policy objective is price stability."); *see also* Simon Dikau & Ulrich Volz, *Central Bank Mandates, Sustainability Objectives and the Promotion of Green Finance*, 184 ECOLOGICAL ECON. 1, 3–9 tbl.1 (2021) (illustrating that the vast majority of central banks have "price stability" as their primary objective).

141. Brainard, *supra* note 133.

142. A.W. Phillips, *The Relation Between Unemployment and the Rate of Change of Money Wage Rates in the United Kingdom, 1861–1957*, 25 ECONOMICA 283, 299 (1958) ("[T]he rate of change of money wage rates can be explained by the level of unemployment and the rate of change of unemployment . . . .").

143. Michael Ng et al., *The Hutchins Center Explains: The Phillips Curve*, BROOKINGS INST. (Aug. 21, 2018), https://www.brookings.edu/blog/up-front/2018/08/21/the-hutchins-center-explains-the-phillips-curve [https://perma.cc/2KGD-QUJG] ("Inflation is higher when unemployment is low and lower when unemployment is high.").

offer higher wages, boosting inflation, and vice versa."[144] Notably, in subsequent years, it was Paul Samuelson and Robert Solow—winners of the Nobel Prize in economics—who coined the term "Phillips curve" and then showed an inverse relationship between unemployment and price stability using U.S. data.[145] Since then, central banks around the world have incorporated this trade-off into their decision-making process.[146] As Federal Reserve Chair Jerome H. Powell noted in a 2020 speech:

> In earlier decades when the Phillips curve was steeper, inflation tended to rise noticeably in response to a strengthening labor market. It was sometimes appropriate for the Fed to tighten monetary policy as employment rose toward its estimated maximum level in order to stave off an unwelcome rise in inflation.[147]

Coming out of the COVID-19 pandemic, the U.S. economy experienced strong economic and employment growth as well as substantial inflationary pressures. The unemployment rate fell from 14.7% in April 2020 to 3.6% in April 2022,[148] while twelve-month changes in the Consumer Price Index jumped from 0.4% to 8.2% over the same period.[149] As the Federal Reserve raised interest rates to combat heightened inflation, many argued that the Federal Reserve's actions would harm short-term employment conditions and economic growth. Former Treasury Secretary Larry Summers stated that a recession would be the most likely outcome, because, "monetary policy is going to have to

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144. *Id.*

145. Paul A. Samuelson & Robert M. Solow, *Analytical Aspects of Anti-Inflation Policy*, 50 AM. ECON. REV. PAPERS & PROC. 177, 192 fig.2 (1960).

146. *See, e.g.*, Donald L. Kohn, Vice Chairman, Bd. of Governors of the Fed. Rsrv. Sys., Address at the Federal Reserve Bank of Boston's 53rd Annual Economic Conference: Lessons for Central Bankers from a Phillips Curve Framework (June 11, 2008), (transcript available at https://www.federalreserve.gov/newsevents/speech/Kohn20080611a.htm [https://perma.cc/7MVY-9YQU]) ("A model in the Phillips curve tradition remains at the core of how most academic researchers and policymakers—including this one—think about fluctuations in inflation . . . .").

147. *See* Jerome H. Powell, Chair, Bd. of Governors of the Fed. Rsrv. Sys., Address at the Federal Reserve Bank of Kansas City's Economic Policy Symposium: New Economic Challenges and the Fed's Monetary Policy Review (Aug. 27, 2020) (transcript available at https://www.federalreserve.gov/newsevents/speech/powell20200827a.htm [https://perma.cc/L3LV-G4BC]).

148. *Unemployment Rate,* FED. RSRV. ECON. DATA, https://fred.stlouisfed.org/series/UNRATE [https://perma.cc/48B6-7G7M] (last updated Aug. 4, 2023).

149. *Consumer Price Index for All Urban Consumers: All Items in U.S. City Average*, FED. RSRV. ECON. DATA, https://fred.stlouisfed.org/series/CPIAUCSL [https://perma.cc/MRB3-CP2X] (last updated Aug. 10, 2023).

keep going until we see disinflation, and we're not going to see disinflation back towards the target range until we see unemployment rise, meaningfully."[150] Former Federal Reserve Vice Chair for Supervision, Randal Quarles, shared a similar view on recession prospects.[151] And Senator Elizabeth Warren voiced her concern that overly aggressive interest rate hikes by the Federal Reserve could prove disastrous.[152]

Thus, herein lies a well-known trade-off for central banks in conducting monetary policy. In an ideal world, central banks would live in a paradise of persistent low unemployment and low inflation. But reality is harsh. By lowering interest rates to stimulate aggregate demand and lower unemployment ("good"), central banks are potentially allowing for high inflation ("bad"). As taught in intermediate macroeconomics courses,[153] the central bank's stylized constrained optimization problem can be written as minimizing the following quadratic loss function:

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150. Michael Sasso, *Transcript: Larry Summers Says Recession More Likely Than Soft Landing*, BLOOMBERG (Apr. 14, 2022), https://www.bloomberg.com/news/articles/2022-04-14/transcript-summers-says-recession-more-likely-than-soft-landing [https://perma.cc/QE73-7BTD]; Interview by Michael Sasso with Larry Summers, Former Treasury Secretary in Bloomberg Podcast (Apr. 14, 2022).

151. *See* Rich Miller, *Former Fed Vice Chair Quarles Says U.S. Is Likely to Suffer Recession*, BLOOMBERG (May 3, 2022), https://www.bloomberg.com/news/articles/2022-05-03/ex-fed-vice-chair-quarles-says-u-s-likely-to-suffer-recession#xj4y7vzkg [https://perma.cc/HY33-CS5J] ("The effect [of intense inflation] is likely to be a recession.").

152. *See* Colby Smith, *Jay Powell Warns U.S. Recession Is "Certainly a Possibility*,*"* FIN. TIMES (June 22, 2022), https://www.ft.com/content/3e3dedc4-5ece-4a35-84c7-e3e670c29c72 [https://perma.cc/C2TX-2CHD] (quoting Senator Warren as saying, "[y]ou know what's worse than high inflation and low unemployment? It's high inflation and a recession with millions of people out of work . . . . I hope you will reconsider that before you drive this economy off a cliff").

153. *See, e.g.*, Wendy Carlin & David Soskice, *Teaching Intermediate Macroeconomics Using the 3-Equation Model*, *in* MACROECONOMIC THEORY AND MACROECONOMIC PEDAGOGY 13 (Giuseppe Fontana & Mark Setterfield eds., 2009) (citing Richard Clarida, Jordi Gali & Mark Gertler, *The Science of Monetary Policy: A New Keynesian Perspective*, 37 J. ECON. LITERATURE 1661 (1999)); MICHAEL WOODFORD, INTEREST AND PRICES: FOUNDATIONS OF A THEORY OF MONETARY POLICY (2003)); Stefania Paredes Fuentes, *The 3-Equation Model*, UNIV. OF WARWICK (2016), https://warwick.ac.uk/study/summer-with-warwick/warwick-summer-school/courses/banking/the_3_eq_model_-_web.pdf [https://perma.cc/EX83-2B89].

$$\min L = (y_1 - y_e)^2 + \beta(\pi_1 - \pi^T)^2$$

$$subject\ to$$

$$y_1 = A - ar$$

$$\pi_1 = \pi_0 + \alpha(y_1 - y_e)$$

In the loss function, the central bank seeks to minimize the output gap $(y_1 - y_e)$, as well as the deviation of inflation from its target $(\pi_1 - \pi^T)$.[154] The output gap is defined as the next period's output less equilibrium output, and inflation deviation is measured as this period's inflation less the target level. The term β reflects the central bank's relative aversion toward inflation.

The choice of interest rate r will only affect output next period y_1, because it takes time for interest rate changes to feed through to future expenditure decisions by individuals and businesses. And, in the Phillips curve, this period's inflation π_1 is influenced by the current output gap $(y_1 - y_e)$ and by last period's inflation π_0. This optimization problem is not trivial because the central bank only chooses the interest rate r, its one monetary policy tool.[155] As discussed, increases in r lead to a decrease in this period's output y_1 (because $y_1 = A - ar$) and a decrease in this period's inflation π_1 (because of the stylized Phillips curve $\pi_1 = \pi_0 + \alpha(y_1 - y_e)$).

Equations and Greek letters aside, the takeaway is straightforward: a central bank faces trade-offs when its policy lever has different effects on its targets. To see this logic play out in a simple example, let's take a step back and assume that the central bank only cared about minimizing the output gap and did not care about inflation at all. That is, suppose $\beta = 0$ in the original

154. Minimizing a loss function is similar to maximizing utility. With maximizing a utility function, one typically thinks of maximizing happiness. In minimizing a loss function, one is typically engaged in minimizing regret. These are two sides of the same coin.

155. Within the realm of monetary policy, it's fair to assume for a stylized example that the central bank has one policy lever to pull—adjusting the interest rate. Outside of monetary policy, the central bank has many more policy levers. For example, the Federal Reserve can use its rulemaking authority to increase minimum capital requirements for banks, create a new payments system, establish emergency lending facilities, etc.

loss function. Then the central bank's loss function would be revised to read:

$$\min L = (y_1 - y_e)^2$$

In this case, the central bank could theoretically set y_1 exactly equal to y_e in order to perfectly minimize $L = 0$. Similarly, if the central bank only cared about inflation and did not care about the output gap, its loss function could be rewritten as:

$$\min L = (\pi_1 - \pi^T)^2$$

The central bank could achieve $L = 0$ by setting $\pi_1 = \pi^T$ in the Phillips curve equation. Importantly, the central bank can achieve $L = 0$ only when it has one mandate in its loss function. (And, even with one mandate, it is very hard to hit this target perfectly in reality as opposed to in theory.) As soon as the number of mandates increases, and assuming the central bank's policy tool r still causes trade-offs, then we have $L > 0$.

D. ADDITIONAL STRAIN FROM ADDITIONAL MANDATES

Former Federal Reserve Chair Paul Volcker cautioned that multiple mandates—meaning even two mandates—risked overburdening the central bank, leading it to do a worse job on all fronts:

> I know that it is fashionable to talk about a "dual mandate"—that policy should be directed toward the two objectives of price stability and full employment. . . . Asked to do too much . . . [the Federal Reserve] will inevitably fall short. If in the process of trying it loses sight of its basic responsibility for price stability, a matter which is within its range of influence, then those other goals will be beyond reach.[156]

Other Federal Reserve officials have also made this point. Raphael Bostic—the president of the Federal Reserve Bank of Atlanta and proponent of research into how the central bank's policies affect different American communities—has observed

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156. *What Is Central About Central Banking? A Study of International Models: Hearing Before the Subcomm. on Monetary Pol'y & Trade of the H. Comm. on Fin. Servs.*, 113th Cong. 62 (2013) (statement of Athanasios Orphanides), https://mitsloan.mit.edu/shared/ods/documents?DocumentID=2358 [https://perma.cc/64LJ-9DYJ] (citing Paul Volcker, *Central Banking at a Crossroad*, ECON. CLUB OF N.Y. (May 29, 2013)), https://www.econclubny.org/documents/10184/109144/2013VolckerTranscript.pdf [https://perma.cc/2VWC-YTWF]).

that "there are a lot of traditionalists who would say, when you ask institutions to do more than one thing, they don't do either of them well."[157] As shown with the stylized loss functions, increasing the number of mandates in the objective function makes the central bank's optimization problem more complicated and the central bank less effective, all else equal.[158]

Of course, these loss functions are highly simplified models. Reality is more complicated. Consider a few examples. First, suppose the central bank was given a climate change mandate by the legislative body and was required to purchase "green bonds"—that is, the debt of corporations seeking to create or facilitate improvements in environmentally friendly technologies—in order to mitigate the harms of climate change.[159] This additional mandate could exacerbate existing trade-offs in the central bank's monetary policy decision-making process. As mentioned earlier, the Federal Reserve has decided to raise interest rates in order to slow down inflation. If the Federal Reserve had to subsidize green companies presently, the Federal Reserve would ironically be working against its monetary policy goals by increasing green-sector employment and, hence, contributing to inflationary pressures. In general, making trade-offs more numerous and more complicated would make the Federal Reserve's constrained optimization problem harder to solve.

Second, consider the Environmental Protection Agency (EPA), which ensures that our air and water are clean.[160] The EPA has policy tools at its disposal to achieve that goal, and its

157. *Jobs vs Prices: The Fed's Dueling Mandates*, NPR (Jan. 12, 2023), https://www.npr.org/transcripts/1148895861 [https://perma.cc/2TUC-TU4L].

158. *See* MARC LABONTE, CONG. RSCH. SERV., R41656, CHANGING THE FEDERAL RESERVE'S MANDATE: AN ECONOMIC ANALYSIS 8 (2013), https://crsreports.congress.gov/product/pdf/R/R41656/10 [https://perma.cc/X8KH-FFQU] ("One criticism of the dual mandate is that the Fed has multiple goals, but only one instrument (open market operations) to pursue those goals. When goals conflict, the mandate offers no guidance as to which goal takes precedence.").

159. *See* Domenico del Re & Sarah Strang, *Green Bonds: How Do They Work and Are They Right for Your Project?*, PWC, https://www.pwc.co.uk/services/sustainability-climate-change/insights/green-bonds.html [https://perma.cc/BTJ5-XMCJ] (explaining what green bonds are, how they are issued, and why to invest in them).

160. *See Our Mission and What We Do*, EPA, https://www.epa.gov/aboutepa/our-mission-and-what-we-do [https://perma.cc/2B8B-JBRC] (last updated May 23, 2023) ("EPA works to ensure that . . . Americans have clean air, land and water . . . .").

tools—to the best of our knowledge—work in the same direction.[161] But now suppose Congress tasked the EPA with an additional mandate that is outside of its core mission: "promote maximum employment." Suddenly, the EPA would be faced with awkward trade-offs. When going through the rulemaking process, how would the EPA balance the ramifications of limiting emissions from coal plants with the employment generated by those not-so-environmentally-friendly plants? The EPA could surely do it, but the resulting balance would likely be suboptimal relative to the status quo.

An administrative agency can do a better job when it focuses on its core objectives because it has limited tools and competencies. This is how the administrative state was designed. Congress did not create a single agency to achieve every public objective. Instead, agencies are focused. One agency carries out objectives related to education, another to protect the environment, another to further international diplomacy, and so on and so forth.[162] Therefore, the analysis of economic trade-offs yields an alternative path for Congress: do not task an agency to expand its priorities in ways that are not related to, or only loosely related to, its original mandates. Instead, empower the agencies most closely aligned with those objectives. If Congress wants to make greater headway in the fight against climate change, strengthen the EPA, not the Federal Reserve. The EPA's existing mandates are more strongly correlated with climate change mitigation and the agency has greater expertise to consider trade-offs regarding climate policy.

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We want to be as clear as possible on the caveats and limits associated with analyzing macroeconomic trade-offs. First, the trade-offs described in this Part do *not* imply that new mandates

161. *See, e.g.*, *FY 2022–2026 EPA Strategic Plan*, EPA 7 (Mar. 2022), https://www.epa.gov/system/files/documents/2022-03/fy-2022-2026-epa-strategic-plan.pdf [https://perma.cc/6VPZ-BGMY] ("EPA is charting a course in this Strategic Plan where tackling climate change and advancing environmental justice and civil rights are integral to all the Agency does in carrying out the mission.").

162. Some may ask why Congress cannot solve this problem by simply giving a single agency more tools to accommodate an expanded set of mandates. First, practically speaking, agencies have limited competencies. Just like a company, an agency that becomes larger and larger will become less nimble, less efficient. Second, from a legal perspective, the more that Congress tries to create a mega-agency that can do it all, the greater the probability that nondelegation or major questions will be triggered.

should be dismissed. We are *not* saying that the federal government should not take proactive steps to combat climate change. This macroeconomic theory merely tells us that we should not have the *same* agency, with its limited toolkit, expand beyond its core competencies. The Federal Reserve should not be trying to juggle short-run macroeconomic stability with long-run climate change policies. The resulting trade-offs would be suboptimal.

Second, the theory also does *not* imply that Congress should not impose new mandates on the Federal Reserve, the EPA, the SEC, or another agency. Indeed, these agencies all currently have multiple mandates. The EPA protects people and the environment from significant health risks, sponsors and conducts research, and develops and enforces environmental regulations. The Federal Reserve conducts monetary policy subject to the dual mandate described above and regulates and supervises banks. The SEC protects investors; maintains fair, orderly, and efficient markets; and facilitates capital formation. Agencies strive for many goals at the same time. However, the theory does caution against adding new mandates that are *outside* of an agency's central mission. The Federal Reserve's current mandates are all centered on macroeconomic stability in one form or another, and it has an appropriate toolkit and expertise for the task. Trade-offs would worsen if the Federal Reserve's set of mandates expended beyond macroeconomic stability.

Finally, we close out this Part with a discussion about the limits of this theory. Some trade-offs exist in theory but fail to fully emerge in practice. Others are well-understood. In our monetary policy example, the Phillips curve trade-off between employment and inflation is well-known and has been studied and debated for decades. Indeed, over the years, many economists and policymakers have proposed limiting the Federal Reserve's monetary policy to a single mandate: focus on inflation.[163]

Yet, for the better part of the two or three decades prior to the COVID-19 pandemic, many economists argued whether the

163. *See* LABONTE, *supra* note 158 ("Some economists have argued that this mandate should be replaced with a single mandate of price stability. Often the proposal for a single mandate is paired with a more specific proposal that the Fed should adopt an inflation target. Under an inflation target, the goal of monetary policy would be to achieve an explicit, numerical target or range for some measure of price inflation.") (summary of Congressional Research Service reports).

trade-off existed.[164] The former president of the Federal Reserve Bank of Boston, Eric S. Rosengren, gave a speech in which he observed that the Federal Reserve, with its dual mandate for monetary policy, actually performed better than many central banks with a single price-stability mandate.[165] Moreover, one could argue that even if the trade-off existed at one point in time, it's not a natural law that must always hold true. The Phillips curve is not a law of physics.

Therefore, while we believe the intuition provided by the theory of constrained optimization is straightforward and helpful, we also believe that lawmakers and policymakers should be careful to examine new mandates on the merits, on a case-by-case basis. Some mandates may be wholly consistent with existing ones—that is, no new trade-offs given existing tools—while others may be unrelated to or opposite from the existing framework. Moreover, we can even imagine a situation where lawmakers give an agency responsibility for a set of new mandates while emphasizing that the new mandates should not take priority

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164. *See, e.g.*, Peter Hooper et al., *Prospects for Inflation in a High Pressure Economy: Is the Phillips Curve Dead or Is It Just Hibernating?*, 74 RSCH. ECON. 26, 26 (2020) ("[O]bservers are increasingly inclined to declare the demise of the Phillips curve, that is, the flattening of its slope to zero."); Brian Reinbold & Yi Wen, *Is the Phillips Curve Still Alive?*, 102 FED. RSRV. OF BANK ST. LOUIS REV. 121, 137 (2020) (noting that their work "casts doubt on the so-called tradeoff between unemployment and inflation"); David Ratner & Jae Sim, *Who Killed the Phillips Curve? A Murder Mystery* 32 (Fed. Rsrv. Bd., Wash. D.C., Working Paper No. 028, 2022) ("[T]he origin of the break down of the Phillips curve relationship may be found in the collapse of worker bargaining power since 1980s."); Kate Bahn & Austin Clemens, *The Death of the Phillips Curve Is the Time to Lift up New Economic Indicators*, WASH. CTR. EQUITABLE GROWTH (Sept. 4, 2019), https://equitablegrowth.org/the-death-of-the-phillips-curve-is-the-time-to-lift-up-new-economic-indicators [https://perma.cc/QTY5-TKRJ] (suggesting alternative economic tools to correct for the Phillips Curve's insufficiencies).

165. *See* Eric S. Rosengren, President, Fed. Rsrv. Bank Bos., Address at the Federal Reserve Bank of Boston's 57th Annual Economic Conference: Should Full Employment Be a Mandate for Central Banks? (Apr. 12, 2013) (transcript available at https://www.bostonfed.org/news-and-events/speeches/should-full-employment-be-a-mandate-for-central-banks.aspx [https://perma.cc/9SG4-TG97]) ("[T]he U.S. has a tighter inflation range and a broader unemployment range than many other countries with a single inflation mandate is striking, as is the very high unemployment rate in Europe. The results suggest that criticism that a dual mandate country might suffer from more frequent and enduring spells of high inflation is overdone—and if anything, the evidence might raise the question of whether, with a dual mandate, there should have been more aggressive monetary accommodation during periods of elevated unemployment, particularly in the past five years.").

over the original mandates given to the agency, essentially dictating prioritization.

III. CASE STUDIES

What are policy objectives that some politicians and commentators hope the Federal Reserve might take up in the coming years? In this Part, we discuss four case studies related to climate change, financial stability, distributional impacts, consumer financial services, and financial stability. In each case study, we examine the potential addition of a mandate through the legal obstacles provided in Part I and the economic framework provided in Part II. While these case studies are specific to the Federal Reserve, we note that our analysis is broadly applicable to other government agencies as well. The questions of "can we" and "should we" are generalizable.

A. CLIMATE CHANGE

1. Buying Green Bonds

One of the most widely wished-for expansions of the Federal Reserve's mandates is to address climate change. The Federal Reserve's most important tool—the ability to raise or lower interest rates—is of little use when it comes to fighting climate change. But some argue that when the Federal Reserve purchases assets, it should consider favoring purchases of "green bonds" issued by companies which provide products or services that address climate change.[166] Doing so would effectively subsidize these companies and indirectly help tackle climate change. The goal is a sympathetic one, and it seems intuitive. However, based on the constrained-optimization framework, adding this objective could adversely affect the Federal Reserve's conduct of monetary policy.

Imagine a scenario in which the Federal Reserve were trying to cool inflation by raising interest rates and shrinking its balance sheet. If the Federal Reserve were also required to buy green bonds, the central bank would partially counteract its

166. *See* Megan Greene, Opinion, *How the Fed Could Give a Green Light to Environmentally Sustainable Investments*, MARKETWATCH (Apr. 14, 2021), https://www.marketwatch.com/story/how-the-fed-could-give-a-green-light-to-environmentally-sustainable-investments-11618340575 [https://perma.cc/NXQ5-GKLU] (urging the Federal Reserve to purchase green bonds).

fight against inflation. That is because buying green bonds would stimulate economic activity (e.g., in the renewable energy sector), which would put upward pressure on prices. Stimulating economic activity is usually a "good" thing, but not when the central bank is trying to pull back aggregate demand to combat inflation. In fact, when the central bank fails in its core macroeconomic objectives—when prices are rising dramatically, or the economy is in a recession—there is less policy or political appetite to tackle climate change.

Based on the legal framework presented in Part I, there are a number of reasons to think that if the Federal Reserve tried to put a thumb on the scale in favor of environmental protection, courts would thwart that attempt. The central bank would certainly be sued over a green bond purchase program. Competitors to the renewable energy sector would be injured by the policy, as they would not be eligible for financing that the government was offering to issuers of green bonds, and so would have standing to sue. If the Supreme Court decided that EPA did not have the authority under the Clean Air Act to systematically encourage power companies to switch from coal to gas, wind, and solar power, then there is little likelihood that the Court would look on the Federal Reserve's climate efforts with much solicitude.[167]

The Federal Reserve has never attempted to address the important issue of climate change in the past, so a new regulation attempting to do so would break new regulatory ground. In fact, the Federal Reserve has tried as hard as possible to conduct bond purchases as neutrally as possible, without favoring or disfavoring any sector of the economy.[168] For example, during the COVID

167. *See* Lawrence Hurley & Valerie Volcovici, *U.S. Supreme Court Limits Federal Power to Curb Carbon Emissions*, REUTERS (June 30, 2022), https://www.reuters.com/legal/government/us-supreme-court-limits-federal-power-curb-carbon-emissions-2022-06-30 [https://perma.cc/3RGL-VZ4G] ("The ruling is likely to have implications beyond the EPA as it raises new legal questions about any big decisions made by federal agencies.").

168. *See FAQs: Treasury Purchases*, FED. RSRV. BANK OF N.Y. (Feb. 11, 2022), https://www.newyorkfed.org/markets/treasury-reinvestments-purchases-faq.html [https://perma.cc/F9P9-WGSB] ("In general, the Desk seeks to operate in a manner that is relatively neutral to the securities available for purchase and in a way that limits the potential for operations to affect normal market functioning . . . .").

response in 2020, the Federal Reserve generally structured purchases of bonds through a bond exchange-traded fund,[169] which meant that it would not have to hold the bonds of any identifiable issuer on its books. Could it only purchase the bonds of some corporations that are aligned with the presidential administration's policies? Under § 13(3) of the Federal Reserve Act, Congress does not allow the Federal Reserve to pick individual companies to support.[170] Most importantly, Congress directed the Federal Reserve to offer emergency lending in certain circumstances, but has never suggested that the central bank condition that lending on compliance with its other policy priorities.[171] Unless the Federal Reserve receives new statutory authorization from Congress to proceed in this direction, the Federal Reserve's novel attempt would face significant headwinds from the major questions doctrine.

Here, an international comparison is instructive.[172] The European Central Bank (ECB) decided to "gradually decarbonise its corporate bond holdings, on a path aligned with the goals of the Paris Agreement."[173] To achieve this goal, the ECB is trying to tilt its portfolio of corporate bonds away from companies with

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169. *See* April Joyner, *Fed's Bond Purchase Program Closing Price Gaps in ETF Market*, REUTERS (Apr. 16, 2020), https://www.reuters.com/article/us-health-coronavirus-etfs/feds-bond-purchase-program-closing-price-gaps-in-etf-market-idUSKBN21Y394 [https://perma.cc/D2PV-VZZT] (explaining the Federal Rerserve's bond purchase program and its positive effects on the exchange-traded funds market during the Pandemic).

170. 12 U.S.C. § 343 (excluding from discount eligibility any program "that is structured to remove assets from the balance sheet of a single and specific company, or that is established for the purpose of assisting a single and specific company avoid bankruptcy").

171. *See id.* Congress directed that any emergency lending "shall be designed to ensure that any emergency lending program or facility is for the purpose of providing liquidity to the financial system, and not to aid a failing financial company, and that the security for emergency loans is sufficient to protect taxpayers from losses and that any such program is terminated in a timely and orderly fashion," which would seem to limit the lending to matters of financial instability. *Id.*

172. *See Central Bank Activism*, *supra* note 6, at 290–91 ("[U]nlike 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 environmental goals of the government.").

173. *ECB Takes Further Steps to Incorporate Climate Change into Its Monetary Policy Operations*, EUR. CENT. BANK (July 4, 2022), https://www.ecb.europa.eu/press/pr/date/2022/html/ecb.pr220704~4f48a72462.en.html [https://perma.cc/8DGU-EFFT].

"a poorer climate performance" to those with a better record—ones with "lower greenhouse gas emissions, more ambitious carbon reduction targets and better climate-related disclosures."[174] It also has invested in green bonds, or "debt securities whose proceeds are used to finance investment projects with an environmental benefit," under various purchase programs for the past few years.[175]

The ECB can rely on different legal authorities than the Federal Reserve. Article 127(1) of the Treaty on the Functioning of the European Union (TFEU), the treaty that created the ECB, provides that the ECB has a secondary monetary policy objective of "support[ing] the general economic policies in the Union with a view to contributing to the achievement of the objectives of the Union as laid down in Article 3 of the Treaty on European Union [(TFEU)]."[176] Article 3 of the TEU provides that "a high level of protection and improvement of the quality of the environment" is one of the Union's objectives.[177] Article 11 of the TFEU states that "[e]nvironmental protection requirements must be integrated into the definition and implementation of the Union's policies and activities, in particular with a view to promoting sustainable development."[178] Therefore, from another perspective, the ECB must also consider environmental protection requirements when making monetary policy. However, the TFEU provides that the ECB can only pursue its secondary objective if such a policy is "without prejudice to the [primary] objective of price stability."[179]

The Federal Reserve has no such clear legal mandate, which is a real administrative law problem not shared by its European counterpart. But we also wonder about the trade-offs faced by the ECB with regard to its green bond purchasing program. Its

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174. *Id.*

175. Roberto A. De Santis et al., *Purchases of Green Bonds Under the Eurosystem's Asset Purchase Programme*, 7 EUR. CENT. BANK ECON. BULL. (2018), https://www.ecb.europa.eu/pub/economic-bulletin/focus/2018/html/ecb.ebbox201807_01.en.html [https://perma.cc/D4D4-ZSXD].

176. Consolidated Version of the Treaty on the Functioning of the European Union art. 127, Oct. 26, 2012, 2012 O.J. (C 326) 47 [hereinafter TFEU].

177. Consolidated Version of the Treaty on European Union art. 3, Oct. 26, 2012, 2012 O.J. (C 326) 13.

178. TFEU, *supra* note 176, art. 11.

179. *Id.* at art. 127.

first and only mandate has been price stability. It has no maximum-employment mandate. But green bonds finance, and thus stimulate, the work of the issuers of those bonds. Stimulative programs exacerbate, rather than quell, the risks of inflation. A green bonds obligation at the ECB creates new trade-offs: the central bank has to decide whether to maximize environmental protection or inflation reduction, and the green bonds mandate makes it difficult to do both at the same time.

2. Climate Stress Tests

The Federal Reserve was given the power to conduct stress testing under Dodd-Frank.[180] Since then, the Federal Reserve has required large financial institutions to conduct stress tests on the basis of a regularly changed hypothetical scenarios.[181] The idea is that the "stress test assesses whether banks are sufficiently capitalized to absorb losses during stressful conditions while meeting obligations to creditors and counterparties and continuing to be able to lend to households and businesses."[182] Mehrsa Baradaran has called this sort of regulation "regulation by hypothetical," as the stress tests require banks to establish that their balance sheets could survive a fictional disaster, a sterner test than merely establishing that the capital they maintain is sufficient to handle a downturn in the prices of assets they currently own.[183]

Some policymakers have suggested that the Federal Reserve ought to emphasize climate scenarios in their stress tests. Graham S. Steele, the Assistant Secretary of the Treasury for Financial Institutions under the Biden administration, wrote in

180. For an overview of how the Federal Reserve has exercised its stress testing authority, see Matthew C. Turk, *Stress Testing the Banking Agencies*, 105 IOWA L. REV. 1701, 1713–15 (2020).

181. *See e.g.*, *Dodd-Frank Act Stress Test 2021: Supervisory Stress Test Results*, BD. OF GOVERNORS OF THE FED. RSRV. SYS. 3–9 (June 2021), https://www.federalreserve.gov/publications/files/2021-dfast-results-20210624.pdf [https://perma.cc/TF4C-3DT2] (providing an overview of stress testing conducted in 2021).

182. *Stress Tests*, BD. OF GOVERNORS OF THE FED. RSRV. SYS., https://www.federalreserve.gov/supervisionreg/stress-tests-capital-planning.htm [https://perma.cc/8RXU-MAJ7] (last updated June 22, 2022).

183. *See* Mehrsa Baradaran, *Regulation by Hypothetical*, 67 VAND. L. REV. 1247, 1283–85 (2014) (describing stress tests as a prominent instance of regulation by hypothetical).

2020 that "regulators could incorporate a series of scenarios involving climate shocks and transition pathways into agency-run supervisory stress tests."[184] Academics also have recognized the need for climate stress testing.[185] Senate Democrats have proposed legislation that would require the Federal Reserve to develop climate stress tests.[186]

Climate stress testing is more closely related to the Federal Reserve's mandates than is the green bond purchasing program. Section 165 of Dodd-Frank provides that the Federal Reserve "shall conduct annual analyses" of bank holding companies "of whether such companies have the capital, on a total consolidated basis, necessary to absorb losses as a result of adverse economic conditions," a procedure that Congress described as a "stress test."[187] The Federal Reserve has sufficient discretion as to how it will structure the test, but "shall provide for at least 2 different sets of conditions under which the evaluation required by this subsection shall be conducted, including baseline and severely adverse" and must "publish a summary of the results of the tests required."[188]

It is certainly possible to imagine banks running into trouble for climate change reasons. For instance, a bank might be overexposed to mortgages, or a company's value could be impaired by rising sea levels and a transition away from fossil fuels. It makes

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184. Graham S. Steele, *Confronting the "Climate Lehman Moment": The Case for Macroprudential Climate Regulation*, 30 CORNELL J.L. & PUB. POL'Y 109, 147 (2020).

185. *See, e.g.*, Stefano Battiston et al., *A Climate Stress-Test of the Financial System*, 7 NATURE CLIMATE CHANGE 283, 285 (2017) (concluding that as much as forty-eight percent of relative equity holdings face indirect exposure to climate change risks because they rely on financial institutions directly exposed to climate risk as a result of their lending).

186. *See* Press Release, Sen. Dianne Feinstein, Feinstein to Secretary Yellen: Use Financial System to Mitigate Climate Change Risk (Jan. 8, 2021), https://www.feinstein.senate.gov/public/index.cfm/press-releases?ID=F494CF21-B927-404B-876A-CF80D3231985 [https://perma.cc/8DKZ-J2S8].

187. 12 U.S.C. § 5365(i)(1)(B).

188. *Id.* Only large banks must participate in stress testing. *See id.* § 5365(a)(1) (exempting banks and non-bank financial institutions with under $250 billion in assets from Federal Reserve stress tests). Dodd-Frank initially set this exemption at $50 billion under management for banks and $10 billion under management for non-bank financial institutions. *See* Dodd-Frank Act, Pub. L. No. 111-203, § 165(a), (i), 124 Stat. 1376, 1423, 1430 (2010). For criticism of this exemption, see Jeremy C. Kress & Matthew C. Turk, *Too Many to Fail: Against Community Bank Deregulation*, 115 NW. U. L. REV. 647, 651 (2020).

sense for regulators to occasionally make sure that banks are prepared by running them through hypothetical situations involving sea level rise, exposure to so-called "stranded assets," or energy investments that are unlikely to pay off because the world has turned to other kinds of energy.

The Federal Reserve has accordingly gone so far as to dip a cautious toe into the water of climate stress testing. In 2022, it announced that six of the nation's largest banks would participate in a pilot climate scenario analysis.[189] But it hastened to explain that the exercise would differ from bank stress tests and that the purpose of the exercise would be research: the Federal Reserve would publish insights gained from the pilot, and "there [would] be no capital or supervisory implications from the pilot."[190] The pilot, whatever its bindingness, would look like a climate stress test: the banks would be asked to run scenarios, which would include climate, economic, and financial variables, on their various portfolios and business strategies.[191] But the authority to pursue broader based stress testing would be more likely to result in a legal challenge.[192]

The rub lies in the purpose of climate stress testing. If the Federal Reserve can credibly assure its critics that it is running a climate stress test for the purpose of assessing the bank's safety and soundness, then there is little reason to worry about legal pushback. If, on the other hand, the Federal Reserve repeatedly ran climate-oriented stress tests designed to discourage banks from lending to energy companies on the view that those companies were damaging the planet, then the Federal Reserve

189. Press Release, Bd. of Governors of the Fed. Rsrv. Sys., Federal Reserve Board Announces That Six of the Nation's Largest Banks Will Participate in a Pilot Climate Scenario Analysis Exercise Designed to Enhance the Ability of Supervisors and Firms to Measure and Manage Climate-Related Financial Risks, (Sept. 29, 2022), https://www.federalreserve.gov/newsevents/pressreleases/other20220929a.htm [https://perma.cc/K4P6-AFEA].

190. *Id.*

191. *See id.*

192. *See, e.g.*, Matthew Bisanz et al., *Climate Scenario Analysis Exercise Announced by US Federal Reserve*, MAYER BROWN (Oct. 3, 2022), https://www.mayerbrown.com/en/perspectives-events/publications/2022/10/climate-scenario-analysis-exercise-announced-by-us-federal-reserve [https://perma.cc/A5Z7-9BU8] ("[I]f the Federal Reserve were to expand the exercise to a broader set of banking organizations, we expect it would need to clearly articulate a legal basis for doing so and address both public comments and congressional oversight concerns.").

would be in the role of a climate regulator, using the stress test tool to do what it could not do through a green bonds program. The Federal Reserve would, to put it simply, not be imposing climate stress tests to improve the safety and soundness of banks, but rather to enlist the banks in climate control priorities.

And, of course, this would force the Federal Reserve to make trade-offs. It could pursue its unemployment minimization mandate by encouraging banks to lend into all sectors of the economy, including the energy production sectors. Or it could use the stress tests to encourage banks to minimize lending to oil and gas extraction industries, potentially increasing unemployment in those parts of the economy. The trade-offs would affect the energy mix adopted by the United States and its unemployment rate, and it is hard to know how the Federal Reserve should balance these policy implications.

The kind of climate stress test would also be relevant. Consider the climate stress test conducted by the Bank of England in 2021, a stress test like the Federal Reserve's, replete with caution.[193] The test posed three different scenarios for British financial institutions to apply, assuming collective responses to climate change.[194] Only some firms were required to participate: seven banks, five life insurers, six general insurers, and ten selected Lloyd's of London syndicates.[195] The result was not used by Bank of England to set capital requirements or to compel participants to take certain actions, but to further "system-wide policy issues" and future collaboration between participants and supervisory agencies.[196]

Moreover, the Bank of England had a firmer government mandate to conduct climate change stress tests than does the Federal Reserve. The Bank of England Act 1998 specifies that the Bank of England is required to "support[] the economic policy of Her Majesty's Government, including its objectives for growth

193. *Key Elements of the 2021 Biennial Exploratory Scenario: Financial Risks from Climate Change*, BANK OF ENG. (June 8, 2021), https://www.bankofengland.co.uk/stress-testing/2021/key-elements-2021-biennial-exploratory-scenario-financial-risks-climate-change [https://perma.cc/Y42Y-7ZMD] (exploring the vulnerability of current business models to future climate policy pathways and how businesses intend to adapt those models in response to climate change).

194. *Id.*

195. *Id.*

196. *Id.*

and employment."[197] And the Treasury has the obligation to state government's economic policy objectives via Her Majesty's Treasury monetary policy remit at least once every twelve months.[198] In the 2021 remit letter, the Treasury updated the remit "to reflect the government's economic strategy for achieving strong, sustainable and balanced growth that is also environmentally sustainable and consistent with the transition to a net zero economy."[199]

The Federal Reserve, however, is not required to support the President's economic policy and, as an independent agency, is not required to (and some would argue, is not permitted to) take direction from either the President or the Treasury Secretary.[200] It has the discretion to conduct climate stress testing, but must be able to show that the stress testing is relevant to economic safety and soundness.

B. DISTRIBUTIONAL IMPACT

Neither economic losses nor gains are shared equally. Research shows that "young and less educated workers have always been affected more in recessions, while women and Hispanics were more severely affected during the [COVID-19

197. Bank of England Act 1998, c. 11, § 9C.

198. HM Treasury, *HMT Monetary Policy Remit*, GOV.UK, https://www.gov.uk/government/collections/monetary-policy-remit [https://perma.cc/T7GH-H9G7] (last updated Nov. 17, 2022).

199. Letter from Rishi Sunak, Chancellor of the Exchequer, Her Majesty's Treasury, to Andrew Bailey, Governor, Bank of Eng. (Mar. 3, 2021), https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/965782/2021_MPC_remit_FNAL_1_March_.pdf [https://perma.cc/Z746-B4ES].

200. The famous Fed-Treasury Accord of 1951 established the Federal Reserve's independence in matters of monetary policy. The accord provides, in full, that "[t]he Treasury and the Federal Reserve System have reached full accord with respect to debt management and monetary policies to be pursued in furthering their common purpose to assure the successful financing of the Government's requirements and, at the same time, to minimize monetization of the public debt." The accord does not clearly, by its language, provide the Federal Reserve with its independence guarantee, but it has been thought to be origin of this monetary independence. *See, e.g.*, PETER CONTI-BROWN, THE POWER AND INDEPENDENCE OF THE FEDERAL RESERVE 35 (2016) (quoting and analyzing the accord).

recession]."[201] Consider the aftermath of the 2008 financial crisis. The net worth of the average household fell by 40%, or about $50,000. But Black Americans saw their median net worth fall by 53%, while white household net worth dropped by 17%.[202]

The asymmetry holds during economic upswings as well. In the United States, the average Black and Hispanic or Latino household earns about half as much as their average white counterpart.[203] The racial wealth gap has persisted for generations.[204] According to researchers at the Federal Reserve:

> In the 2019 [Survey of Consumer Finances], White families have the highest level of both median and mean family wealth: $188,200 and $983,400, respectively. Black and Hispanic families have considerably less wealth than White families. Black families' median and mean wealth is less than 15 percent that of White families, at $24,100 and $142,500, respectively. Hispanic families' median and mean wealth is $36,100 and $165,500, respectively.[205]

What can be done about this intergenerational problem? The Federal Reserve is one of the most powerful, if not the most powerful, economic institution in the United States. It might be able to play a role in alleviating these economic disparities. In

201. Ippei Shibata, *The Distributional Impact of Recessions: The Global Financial Crisis and the COVID-19 Pandemic Recession*, 115 J. ECON. & BUS. 1, 1 (2021).

202. Christopher Famighetti & Darrick Hamilton, *The Great Recession, Education, Race, and Homeownership*, ECON. POL'Y INST. (May 15, 2019), https://www.epi.org/blog/the-great-recession-education-race-and-homeownership [https://perma.cc/TQ83-C8ER].

203. Aditya Aladangady & Akila Forde, *Wealth Inequality and the Racial Wealth Gap*, BD. OF GOVERNORS OF THE FED. RSRV. SYS.: FEDS NOTES (Oct. 22, 2021), https://www.federalreserve.gov/econres/notes/feds-notes/wealth-inequality-and-the-racial-wealth-gap-20211022.html [https://perma.cc/LY6D-KSDG].

204. Fabian T. Pfeffer & Alexandra Killewald, *Intergenerational Wealth Mobility and Racial Inequality*, 5 SOCIUS: SOCIO. RSCH. DYNAMIC WORLD 1 (2019).

205. Neil Bhutta et al., *Disparities in Wealth by Race and Ethnicity in the 2019 Survey of Consumer Finances*, BD. OF GOVERNORS OF THE FED. RSRV. SYS.: FEDS NOTES (Sept. 28, 2020), https://www.federalreserve.gov/econres/notes/feds-notes/disparities-in-wealth-by-race-and-ethnicity-in-the-2019-survey-of-consumer-finances-20200928.html [https://perma.cc/737R-PYJK]; *see also* Liz Mineo, *Racial Wealth Gap May Be a Key to Other Inequities*, HARV. GAZETTE (June 3, 2021), https://news.harvard.edu/gazette/story/2021/06/racial-wealth-gap-may-be-a-key-to-other-inequities [https://perma.cc/Y68K-7BYA] ("The typical white American family has roughly 10 times as much wealth as the typical African American family and the typical Latino family. In other words, while the median white household has about $100,000-$200,000 net worth, Blacks and Latinos have $10,000-$20,000 net worth.").

2021, the House passed H.R. 2543, the Federal Reserve Racial and Economic Equity Act. That bill provides that:

> 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, including actions in carrying out—
>
> (1) monetary policy;
>
> (2) regulation and supervision of banks, thrifts, bank holding companies, savings and loan holding companies, and nonbank financial companies and systemically important financial market utilities designated by the Financial Stability Oversight Council;
>
> (3) operation of payment systems;
>
> (4) implementation of the Community Reinvestment Act of 1977;
>
> (5) enforcement of fair lending laws; and
>
> (6) community development functions.[206]

In short, this legislation would add an additional mandate to the Federal Reserve's operations in various arenas. When setting monetary policy, for example, the Federal Reserve would have to consider price stability, maximum employment, *and* whether its action would reduce racial economic disparities.

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Should the Federal Reserve have an additional mandate related to distributional impacts, whether by race or income or some other category? Since its founding, the Federal Reserve has not had a mandate to consider distributional impacts. The Employment Act of 1946 directed the entire federal government to pursue "conditions under which there will be afforded useful employment opportunities for those able, willing, and seeking work, and to promote maximum employment, production, and purchasing power."[207] But that was an objective in the aggregate. The Federal Reserve Reform Act of 1977 added the dual mandate, but did not cite subgroups.[208] In short, the Federal Reserve has always acted with respect to the aggregate economic conditions.

If Congress passes legislation requiring the Federal Reserve to emphasize the "elimination of disparities across racial and

206. Federal Reserve Racial and Economic Equity Act, H.R. 2543, 117th Cong. § 101 (2021).

207. Employment Act of 1946, Pub. L. No. 79-304, § 2, 60 Stat. 23 (prior to 1978 amendment).

208. Federal Reserve Reform Act of 1977, Pub. L. No. 95-188, 91 Stat. 1387.

ethnic groups with respect to employment, income, wealth, and access to affordable credit,"[209] the central bank could tailor its monetary policy to emphasize these directives. Congress would give the Federal Reserve an "intelligible principle" under the currently applicable nondelegation doctrine to address disparities in wealth—it is certainly as intelligible as regulation communications in the "public interest."[210] Moreover, the major questions doctrine requires an explicit grant of authority to an agency from the legislature, and the Federal Reserve Racial and Economic and Equity Act clearly provides this sort of specific legislation.

However, if Congress did not pass such a statute, the Federal Reserve's adoption of a mandate to focus not on aggregate employment and inflation, but rather on the effect of monetary policy on employment and inflation on ethnic groups that prospered least under a colorblind regulatory policy, would risk reversal in the courts. Nothing in the legislation that currently governs the Federal Reserve encourages it to focus on a particular community in the United States, rather than on the country as a whole. It would be novel for the Federal Reserve to presume otherwise, and such novelty is now policed by the major questions doctrine.

Finally, the Equal Protection Clause might raise an independent issue. Under that clause, courts apply strict scrutiny, which is almost always "fatal in fact," to laws that include "suspect classifications," including classifications on the basis of race or ethnicity.[211] The Federal Reserve Racial and Economic Equity

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209. Federal Reserve Racial and Economic Equity Act, H.R. 117-228, 117th Congr. § 101 (2022).

210. *See* Nat'l Broadcasting Co. v. United States, 319 U.S. 190, 216 (1943) (holding that a congressional delegation to the Federal Communications Communication to regulate radio communications "in the public interest," in context, was a sufficiently intelligible principle under the nondelegation doctrine). For one of the first invocations of the intelligible principle test, see J.W. Hampton Jr. & Co. v. United States, 276 U.S. 394, 409 (1928) ("If Congress shall lay down by legislative act an intelligible principle to which the person or body authorized . . . is directed to conform, such legislative action is not a forbidden delegation of legislative power."). For one of the most recent, see Gundy v. United States, 139 S. Ct. 2116, 2123 (2019) (plurality opinion) ("The constitutional question is whether Congress has supplied an intelligible principle to guide the delegee's use of discretion.").

211. *See* Winkler, *supra* note 121, at 870.

Act does not identify any particular race or ethnicity to be favored by the central bank, and instead focuses on eliminating disparities between races or ethnicities. That language probably insulates it from a facial equal protection challenge—a challenge to the statute before the Federal Reserve implemented it.[212] But that does not mean that the Federal Reserve's implementation of the new mandate could not be subject to "as applied" challenges. The Supreme Court has subjected the discriminatory implementation of facially neutral laws to strict scrutiny in the past,[213] and implementing monetary policy or bank supervision to ensure the elimination of disparities between ethnic groups might require the central bank to favor a particular ethnic group.

Economically, having this additional mandate would likely present trade-offs for the Federal Reserve. Within the realm of monetary policy, for example, it's unclear whether keeping interest rates low (i.e., expansionary monetary policy) would help or hurt. Research by Christina D. Romer—former Chair of the Council of Economic Advisers—and David H. Romer show that expansionary monetary policy in the United States is associated with improved conditions for the poor in the short run.[214] Thus, a central bank might be incentivized to provide easier monetary conditions in the short run to achieve a distributional mandate. However, Romer and Romer's analysis of a large sample of countries shows that low inflation and stable growth are associated with improved well-being of the poor in the long run.[215] Both the short-run and long-run impacts are quantitatively large, statistically significant, and robust. But because "the cyclical effects of monetary policy are inherently temporary," the authors concluded that "that monetary policy that aims at low inflation and stable aggregate demand is the most likely to result in genuinely improved conditions for the poor."[216] In other words, this is a case

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212. *See, e.g.*, Cong. Rsch. Serv., *Facially Neutral Laws Implicating Suspect Classifications*, CONST. ANNOTATED, https://constitution.congress.gov/browse/essay/amdt14-S1-8-5/ALDE_00013838 [https://perma.cc/S3NU-C9CN]).

213. *See id.*

214. Christina D. Romer & David H. Romer, *Monetary Policy and the Well-Being of the Poor*, 1998 FED. RSRV. BANK OF KAN. CITY 159, 198 (1998) (one of several articles in an annual research symposium hosted by the Federal Reserve Bank of Kansas City).

215. *Id.* at 159.

216. *Id.* at 160–61.

where the Federal Reserve's most important policy tool—the ability to raise or lower interest rates—may be sufficient to make the best contribution it can to this distributional goal.

In that sense, the Federal Reserve could provide the greatest assistance on the distributional front by simply being a good steward of the economy. Its distributional-impact mandate is already baked in because keeping inflation in check is important for equity in the long run. An elevated inflation rate typically increases poverty because the poorest members of society do not have access to the sorts of financial instruments that would help protect them against inflation.[217] Said differently, when the price of groceries and gas go up, many minority households will suffer disproportionately.

C. CONSUMER FINANCIAL SERVICES

More than 5.9 million American households—or over five percent of households—lack access to a bank account.[218] As such, they lack access to an entire payment system that allows them to send and receive money. Policymakers now realize that the existing system burdens Americans, especially those who are already struggling financially.

Indeed, those who do not have access to a bank account or who are reluctant to pay overdraft fees often turn to payday lenders, who charge very high interest rates. Research from the Federal Reserve Bank of St. Louis shows that twelve million Americans use payday loans annually, and the interest charged on

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217. *See* Mishkin, *supra* note 131; *see also* Philip N. Jefferson, Governor, Fed. Rsrv. Bd., Speech at the 2022 Institute Research Conference: Opportunity and Inclusive Economic Growth (Nov. 17, 2022) (transcript available at https://www.federalreserve.gov/newsevents/speech/jefferson20221117a.htm [https://perma.cc/D9HD-PTGT]) ("Monetary policy cannot address the specific reasons that low-income households suffer the most from high inflation. But these reasons help to illustrate the importance of low inflation: Low inflation is key to achieving a long and sustained expansion—an economy that works for all. Pursuing our dual mandate is the best way for the Federal Reserve to promote widely shared prosperity.").

218. *2021 FDIC National Survey of Unbanked and Underbanked Households*, FED. DEPOSIT INS. CORP., https://www.fdic.gov/analysis/household-survey [https://perma.cc/7G32-333F] (last updated July 24, 2023).

those loans can be astronomical.[219] Thus, while technological advances have made retail payments more convenient for many Americans, those benefits have not helped the millions of households who frequently turn to payday lenders or incur overdraft fees partly because of payments delays.

The Federal Reserve plays a sizeable role in the consumer financial services space. Retail payments can be made with cash or through other means. In the United States, cash consists of coin, which is issued by the U.S. Department of the Treasury and Federal Reserve notes, which are issued by the Federal Reserve.[220] Non-cash retail payments are conducted by check, credit cards, debit cards, prepaid cards, or ACH. Of note, ACH is an electronic payments network that tells financial institutions whether to debit or credit an account.[221] It was developed by the Federal Reserve in the 1970s as an alternative to clearing paper checks.[222] Examples of ACH transactions include employers depositing money into their employees' bank accounts, businesses paying suppliers for products, individuals moving money from one bank account to another, and monthly mortgage payments.[223]

Can the Federal Reserve go further in solving the problems associated with the existing financial services infrastructure?

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219. Jeanette N. Bennett, *Fast Cash and Payday Loans*, FED. RSRV. OF BANK ST. LOUIS 4 (Apr. 10, 2019), https://research.stlouisfed.org/publications/page1-econ/2019/04/10/fast-cash-and-payday-loans [https://perma.cc/D5TW-EZWA].

220. COMM. ON PAYMENT & SETTLEMENT SYS. OF THE GRP. OF TEN COUNTRIES, *Payments Systems in the United States*, *in* PAYMENT AND SETTLEMENT SYSTEMS IN SELECTED COUNTRIES 427, 439 (2003), https://www.bis.org/cpmi/publ/d53.pdf [https://perma.cc/D9ND-TAJE] (discussing different forms of payment used by non-financial entities).

221. According to the Comptroller's Handbook, "an ACH transaction is a batch-processed electronic funds transfer between an originating bank and a receiving bank. An ACH transaction may be either a deposit (credit) or withdrawal (debit)." *Comptroller's Handbook: Payment Systems*, OCC 8 (Oct. 2021), https://www.occ.gov/publications-and-resources/publications/comptrollers-handbook/files/payment-sys-funds-transfer-activities/pub-ch-payment-systems.pdf [https://perma.cc/N9SR-45HD].

222. Bd. of Governors of the Fed. Rsrv. Sys., *Money and Payments: The U.S. Dollar in the Age of Digital Transformation*, FED. RSRV. 1 (Jan. 2022), https://www.federalreserve.gov/publications/files/money-and-payments-20220120.pdf [https://perma.cc/9LRJ-JCKX].

223. *The ABCs of ACH*, NACHA, https://www.nacha.org/content/what-is-ach [https://perma.cc/ZFD5-59GR].

Should the Federal Reserve expand into consumer financial services? Should Congress require the Federal Reserve do so? Legal scholars such as John Crawford, Robert Hockett, Lev Menand, Saule Omarova, and Morgan Ricks have explored a rethinking of the government's role in providing key financial services to households and businesses.[224] Through that lens, proposals such as the "People's Ledger" or "FedAccounts" have emerged to substantially modify or replace the role of financial intermediaries. Senator Sherrod Brown has introduced legislation to "[a]llow everyone to set up a digital dollar wallet, called a 'FedAccount,' a free bank account that can be used to receive money, make payments, and take out cash."[225]

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In general, the Federal Reserve has a rich history of providing payment services. The following Table 1 is adapted from Section 6 of the Federal Reserve's publication, *The Fed Explained: What the Central Bank Does*.[226] Congress has repeatedly given the central bank a mission in the payments sphere since its founding in 1913.[227] Of note, the Federal Reserve's operations with respect to the clearing of cash, check, and electronic transactions do not present economic trade-offs that compromise

224. *See* Robert C. Hockett & Saule T. Omarova, *The Finance Franchise*, 102 CORNELL L. REV. 1143, 1147 (2017) (analogizing the existing financial system to a franchisor-franchisee setup, with the government as the franchisor and the financial intermediaries as the franchisees); Saule T. Omarova, *The People's Ledger: How to Democratize Money and Finance the Economy*, 74 VAND. L. REV. 1231, 1232 (2021) (exploring the implications of replacing the financial intermediary franchisees with a reconfigured, more powerful Federal Reserve); John Crawford et al., *FedAccounts: Digital Dollars*, 89 GEO. WASH. L. REV. 113, 116–19 (2021) (proposing the creation of an account at the Federal Reserve for everyone, thereby bypassing or significantly reducing the need for private bank accounts); Mehrsa Baradaran, *It's Time for Postal Banking*, 127 HARV. L. REV. F. 165, 165–66 (2014) (advocating for a system in which the U.S. Postal Service provides banking services). *See generally* CHRISTINE DESAN, MAKING MONEY: COIN, CURRENCY, AND THE COMING OF CAPITALISM (2015) (arguing that money—the currency underlying our entire financial system—is political by design as opposed to a creation of the free market, and is thus subject to change by the sovereign).

225. Press Release, U.S. Senate Comm. on Banking, Hous., & Urb. Affs., Brown Introduces New Legislation to Help Hardworking Americans in the Coronavirus Relief Package (Mar. 24, 2020), https://www.banking.senate.gov/newsroom/minority/brown-introduces-new-legislation-to-help-hardworking-americans-in-the-coronavirus-relief-package [https://perma.cc/KLS7-44LN].

226. *See The Fed Explained: What the Central Bank Does*, *supra* note 132.

227. *Id.* at 21–22.

other parts of the central bank's mission. Providing a more efficient financial services infrastructure to individuals and businesses will not cause higher inflation, will not cause higher unemployment, and will not harm financial stability. If anything, having faster payment systems would help the cause of effectively conducting monetary policy.

Table 1: Major Events in the History of the Federal Reserve's Role in the U.S. Payment System

1907	Many banks and clearinghouses refuse to clear checks drawn on certain other banks, leading to the failure of otherwise solvent banks.
1913	Congress creates the Federal Reserve System, giving it the authority to establish a nationwide check-clearing system to eliminate system inefficiencies and inequities.
1918	The Federal Reserve Banks establish Fedwire, the world's first wire transfer system.
1974	The Federal Reserve Banks begin operating their automated clearinghouse service.
1980	The Monetary Control Act reaffirms the Federal Reserve's role in providing payment services.
2003	The Check Clearing for the 21st Century Act required the Federal Reserve to preside over the transformation of the check-collection system from a paper-based to a virtually all-electronic system.
2010	The Dodd-Frank Wall Street Reform and Consumer Protection Act expands the Federal Reserve's supervision of systemically important financial market utilities and payment, clearing, and settlement activities.

There are, however, legal limits to the role that the Federal Reserve, by itself, can play in providing financial services to everyday Americans. According to the Federal Reserve, its existing statutory authorities do "not authorize direct Federal Reserve accounts for individuals, and such accounts would represent a significant expansion of the Federal Reserve's role in the financial system and the economy."[228]

228. *Money and Payments: The U.S. Dollar in the Age of Digital Transformation*, *see supra* note 222, at 13.

The critical distinction here turns on the relevance of the agency's past practice in determining whether a new regulatory initiative is a "major question." The Supreme Court reversed OSHA's vaccine mandate because the "lack of historical precedent" was a "telling indication" that OSHA's rule "extends beyond the agency's legitimate reach."[229] The Federal Reserve's work in facilitating payments between banks has a rich tradition. But the Federal Reserve has no such relationship with individual consumers, who have never been able to take advantage of the payment systems organized or overseen by the central bank.

For example, the Check Clearing for the 21st Century Act facilitated electronic check clearing, an issue important to consumers, but did so by giving banks and other organizations the ability to create electronic images of checks.[230] The Federal Reserve helped to birth the process known as "check truncation" by regulating and overseeing financial institutions, not by establishing a relationship with individual checking accounts.[231] Its other payment systems work in the same way. Fedwire Funds Service is used by "depository institutions and certain other financial institutions that hold an account with a Federal Reserve Bank," amounting to approximately 7,300 participants, all of whom are financial institutions or government agencies.[232] The Federal Reserve's effort to develop a new instant payment service, FedNow, is an innovation that is consistent with the sort of clearing and settlement capabilities that the Federal Reserve has provided in the past. Indeed, FedNow will only operate between financial institutions, rather than be a service that individuals could use.[233]

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229. Nat'l Fed'n of Indep. Bus. v. Dep't of Lab., Occupational Safety & Health Admin., 142 S. Ct. 661, 666 (2022) (quoting Free Enter. Fund v. Pub, Co. Acct. Oversight Bd., 561 U.S. 477, 505 (2010)).

230. Check Clearing for the 21st Century Act, Pub. L. No. 108-100, 117 Stat. 1177 (2003).

231. *Id.*

232. *Fedwire Funds Services*, BD. OF GOVERNORS OF THE FED. RSRV. SYS., https://www.federalreserve.gov/paymentsystems/fedfunds_about.htm [https://perma.cc/XA9V-CSNE] (last updated May 7, 2021).

233. *See FedNow Service*, BD. OF GOVERNORS OF THE FED. RSRV. SYS., https://www.federalreserve.gov/paymentsystems/fednow-additional-questions-and-answers.htm [https://perma.cc/3RS9-GLTV] (last updated July 20, 2023) ("The FedNow Service will be available to depository institutions in the United

We accordingly believe that the Federal Reserve's long legal tradition of facilitating payments between banks—one that dates to the central bank's founding—gives the Federal Reserve a strong legal claim to be able to continue to innovate and payments system facilitation between banks. But Congress has never told the Federal Reserve to develop payment systems that put the Federal Reserve in a relationship with individuals, and the Federal Reserve has never developed its own such relationship. Because this sort of tradition matters when it comes to assessing whether the Federal Reserve could by regulation create that sort of relationship, we believe that explicit congressional approval would be required.

Finally, we note that an expansion into consumer financial services beyond payments could result in undesirable macroeconomic trade-offs that harm the Federal Reserve's existing core mandates. Suppose millions of consumers deposit money directly at the central bank. That would, first and foremost, mean hundreds of billions (or trillions) of dollars are exiting the commercial banking sector—a sector that is providing loans to households and businesses. These loans would disappear unless the central bank started to act as a loan officer for American households and businesses. This change is probably not advisable because it could bring about tremendous economic turbulence.

D. FINANCIAL STABILITY

Financial crises are devastating. Consider these U.S. statistics from the 2007–08 financial crisis: real gross domestic product contracted by approximately $605 billion, or 3.8%, from the fourth quarter of 2007 through the second quarter of 2009.[234] The unemployment rate rose from 5% in December 2007 to 10%

States and will enable individuals and businesses to send instant payments through their depository institution accounts.").

234. *Real Gross Domestic Product*, FED. RSRV. ECON. DATA: ST. LOUIS, https://fred.stlouisfed.org/series/GDPC1 [https://perma.cc/H75Z-RQDF] (last updated July 27, 2023).

in October 2009.[235] Over 8.3 million workers lost their jobs during that same period.[236] An entire generation of college graduates suffered a permanent setback.[237] And the U.S. economy experienced another blow during the onset of the COVID-19 pandemic in 2020.[238] In both instances, the Federal Reserve had to step in to stabilize financial markets and, in turn, the entire economy.[239]

Counting the recent banking turmoil in March 2023, the Federal Reserve has now rescued financial markets, including banks and nonbanks, three times in the span of fifteen years. Should Congress give the Federal Reserve an *explicit* mandate to preserve financial stability? To be clear, we are not referring to a mandate to promulgate macroprudential financial regulations for banks; Congress very clearly asked the Federal Reserve

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235. *Unemployment Rate*, FED. RSRV. ECON. DATA: ST. LOUIS, https://fred.stlouisfed.org/series/UNRATE [https://perma.cc/VQE3-LWZW] (last updated Aug. 4, 2023).

236. *All Employees, Total Nonfarm*, FED. RSRV. ECON. DATA: ST. LOUIS, https://fred.stlouisfed.org/series/PAYEMS [https://perma.cc/2NB5-HDVV]. (last updated Aug. 4, 2023).

237. *See* Jesse Rothstein, *The Lost Generation? Labor Market Outcomes for Post Great Recession Entrants* (Nat'l Bureau of Econ. Rsch., Working Paper No. 27516, 2020) (examining how "the Great Recession" impacted "labor market outcomes of recent college graduates"); Hanan Morsy, *Scarred Generation*, 49 INT'L MONETARY FUND FIN. & DEV. 15, 15 (2012) ("In advanced economies, the crisis sparked a huge increase in unemployment among younger workers that will take a long time to abate."); Lisa B. Kahn, *The Long-Term Labor Market Consequences of Graduating from College in a Bad Economy*, 17 LAB. ECON. 303, 303 (2010) ("The effects of both national and state economic conditions at time of college graduation on labor market outcomes for the first two decades of a career.").

238. *See* Van Der Weide & Zhang, *supra* note 3, at 416–17; Heather Long & Andrew Van Dam, *U.S. Unemployment Rate Soars to 14.7 Percent, the Worst Since the Depression Era*, WASH. POST (May 8, 2020), https://www.washingtonpost.com/business/2020/05/08/april-2020-jobs-report [https://perma.cc/R39J-MLSW] ("The U.S. unemployment rate jumped to 14.7 percent in April, the highest level since the Great Depression . . . ."); Liz Frazier, *The Coronavirus Crash Of 2020, and the Investing Lesson It Taught Us*, FORBES (Feb. 11, 2021), https://www.forbes.com/sites/lizfrazierpeck/2021/02/11/the-coronavirus-crash-of-2020-and-the-investing-lesson-it-taught-us/?sh=324c1e7746cf [https://perma.cc/DHH5-TVKM] ("Investors watched as their retirement savings lost 30% in two weeks, and speculation about how bad it could get created even more fear among investors.").

239. *See The Fed Explained: What the Central Bank Does*, *supra* note 132, at 29 (noting tools used by the Federal Reserve, such as the balance sheet, to provide guidance in the wake of serious economic crisis).

to do that via the Dodd-Frank Act.[240] Rather, we are referring to an explicit mandate to stabilize financial markets—banks *and* nonbanks—in times of heightened economic uncertainty.

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We begin with the legal analysis. The origins of the Federal Reserve as the lender of last resort with a discount window for banks, plus language in the Dodd-Frank Act, suggests that the central bank already possesses a mandate to engage in broad rescues of financial markets.[241] In the Dodd-Frank Act, the Federal Reserve was given an important role on the so-called Financial Stability Oversight Council (FSOC).[242] That collection of agencies, chaired by the Treasury Department, included the Federal Reserve as one of its ten voting members.[243] The FSOC has been charged with identifying "risks to financial stability," promoting "discipline" by avoiding bailouts, and responding to "emerging threats to the stability of the United States financial

240. For an argument of the value of such a mandate, see Renee Haltom & Jeffrey M. Lacker, *Should the Fed Have a Financial Stability Mandate? Lessons from the Fed's First 100 Years*, 101 FED. RSRV. BANK RICHMOND ECON. Q. 49, 49 (2015) ("[The Dodd-Frank Act] enhanced the Fed's surveillance powers and imposed new constraints on risk-taking in the financial sector, all aimed at reducing the probability of . . . financial market turmoil . . . .").

241. *See id.* at 51 ("Government-lending programs often appeared to stabilize markets because they confirmed hopes of intervention, and so have been hailed as successes. But this has come at the cost of moral hazard, greater risk-taking, and greater instability down the road." (footnote omitted)); Christina P. Skinner, *Regulating Nonbanks: A Plan for SIFI Lite*, 105 GEO. L.J. 1379, 1397 (2017) (discussing the value of financial stability mandates such as the Financial stability Oversight council created by the Dodd-Frank Act); *see also* Hilary J. Allen, *Putting the "Financial Stability" in Financial Stability Oversight Council*, 76 OHIO ST. L.J. 1087, 1092 (2015) ("Such a mandate would be designed to mitigate the political economy of the financial regulatory cycle by training regulatory attention on financial stability issues even in normal and boom times, when the public is largely oblivious to such issues."); Renee Haltom & John A. Weinberg, *Does the Fed Have a Financial Stability Mandate?*, FED. RSRV. BANK RICHMOND ECON. BRIEF 2 (2017) [hereinafter *Haltom & Weinberg (2017)*] ("Dodd-Frank almost made the Fed legally and singularly responsible for the nation's financial stability.").

242. Dodd-Frank Act, Pub. L. No. 111-203, § 111(a)–(b), 124 Stat. 1376, 1392 (2010) (establishing the Financial Stability Oversight Council and outlining membership for the Council which includes the Board of Governors of the Federal Reserve System).

243. *Id.*

system."[244] Among other powers, the FSOC has the power to designate nonbanks as systemically important, which subjects those institutions to Federal Reserve supervision.[245]

Congress has not, however, expressed its support for a general financial stability "firefighter role" for the Federal Reserve with clarity.[246] In the CARES Act, Congress *temporarily* invited the Federal Reserve to lend freely to nonbanks.[247] But still, the case for a financial stability mandate is not obvious. Section 13(3) of the Federal Reserve Act does use the term "emergency."[248] It provides that in "unusual and exigent circumstances," the Federal Reserve can, subject to a variety of procedural requirements, provide "emergency lending" to nonbanks.[249] The statute was barely used until the 2008 global financial crisis, when the Federal Reserve relied on it to provide

244. *Id.* § 112(a)(1)(c) (defining one of the purposed of the Council as "respond[ing] to emerging threats to the stability of the United States financial system."); *see also* Skinner, *supra* note 241, at 1389 ("[C]ongress for the first time created a financial regulatory institution that was both cross-sectoral in scope and 'functional' in approach."); Robert F. Weber, *The FSOC's Designation Program as a Case Study of the New Administrative Law of Financial Supervision*, 36 YALE J. ON REGUL. 359, 366 (2019) ("The FSOC was conceived of as a sort of regulatory sealant, filling in the perceived 'gaps' in the institutional apparatus of financial regulation that policymakers identified, in hindsight, as having catalyzed the financial crisis."); Daniel Schwarcz & David Zaring, *Regulation by Threat: Dodd-Frank and the Nonbank Problem*, 84 U. CHI. L. REV. 1813, 1815–17 (2017) (describing one purpose of the FSOC as using the threat of designation to induce responsible behavIor by financial firms).

245. Dodd-Frank Act § 113(a)(1) ("The Council . . . may determine that a U.S. nonbank financial company shall be supervised by the Board of Governors . . . .").

246. *Haltom & Weinberg (2017)*, *supra* note 241, at 2 (recognizing that in a "near-final" version of the Dodd-Frank Act included language that indicated that the Federal Reserve's Board of Governor's "shall identify, measure, monitor, and mitigate risks to the financial stability of the United States"); *cf.* Allen, *supra* note 241 (arguing that financial regulators, particularly the Financial Stability Oversight Council, need an explicit responsibility to help prevent a financial crisis before it occurs to fulfill their financial stability mandate).

247. CARES Act, Pub. L. No. 116-136, § 4003, 134 Stat. 281, 470–71 (2020) (codified as amended at 15 U.S.C. § 9042) ("The Secretary may enter into agreements to make loans or loan guarantees to 1 or more eligible businesses . . . .").

248. Federal Reserve Act, Pub. L. No. 63-43, § 13(3), 38 Stat. 251 (1913) (as amended through Pub. L. 117-263).

249. *Id.*

emergency lending to investment banks and an insurance company.[250] But Congress never indicated that the statute was meant to be used to ensure financial stability. In theory, the Federal Reserve could provide emergency lending to nonbanks for nonfinancial stability related reasons—for example, to shore up some private firms involved in providing critical infrastructure relevant to national security.

From an economics perspective, we first observe that crafting a permanent financial stability mandate would increase moral hazard for the entire financial ecosystem, because banks and nonbanks alike would know—not just believe but know with certainty—that the Federal Reserve would have to intervene during tough times, because Congress has explicitly tasked the Federal Reserve with doing so. During normal times, financial markets—and nonbanks in particular because they are not regulated as strictly as banks—would be less disciplined and engage in riskier transactions.

Moral hazard aside, we argue based on our theoretical framework that such an explicit mandate of maintaining financial stability could sometimes conflict with the execution of monetary policy and vice versa. We explore three examples below.

First, we observe that broad financial market rescues could hurt monetary policy goals, specifically with respect to inflation. As part of its efforts to mitigate the impact of the COVID-19 pandemic, the Federal Reserve expanded its balance sheet at a historic rate.[251] In March 2020, the Federal Reserve balance sheet was roughly $4.3 trillion; by early June, its balance sheet had ballooned to $7.2 trillion.[252] In three months, the balance sheet had expanded by nearly three trillion dollars. The expansion continued, though at a slower pace, through March 2022 when

250. U.S. GOV'T ACCOUNTABILITY OFF., GAO-11-616, FINANCIAL CRISIS: REVIEW OF FEDERAL RESERVE SYSTEM FINANCIAL ASSISTANCE TO AMERICAN INTERNATIONAL GROUP, INC. 22–25 (2011) (detailing the Federal Reserve's approval of emergency lending to American International Group and several failing investment banks).

251. *See The Fed Explained: What the Central Bank Does*, *supra* note 132, at 33–36 (reviewing the measures taken by the Federal Reserve that led to the three trillion dollar spike in the balance sheet).

252. *Id.* at 35.

the Federal Reserve's balance sheet reached $8.9 trillion.[253] During this time, the Federal Reserve purchased over $3 trillion in Treasuries[254] and over $1.3 trillion in mortgage-backed securities.[255] Unprecedented, to say the least.

This balance sheet expansion was a major contributing factor to regaining stability in the financial markets and in the economy broadly. Without government intervention, the economy would have fallen off a cliff. However, this stability-enhancing intervention may have also increased inflationary pressures. As 2021 unfolded, inflation readings began to climb and exceeded the Federal Reserve's stated two percent target.[256] Monetary policy was not the only contributing factor to inflation, to be sure. There was also historic fiscal policy expansion[257] and global supply chain disruptions.[258] But herein lies the trade-off: in pursuing financial stability following a once-in-a-lifetime pandemic, the Federal Reserve may have inadvertently increased inflation. Could the Federal Reserve have been less aggressive in its response during 2020? Yes, but then the subsequent economic recovery might have looked very different.

253. *Assets: Total Assets: Total Assets (Less Eliminations from Consolidation): Wednesday Level*, FED. RSRV. ECON. DATA: ST. LOUIS, https://fred.stlouisfed.org/series/WALCL [https://perma.cc/K7F5-NJJD] (last updated Aug. 17, 2023).

254. *Assets: Securities Held Outright: U.S. Treasury Securities: All: Wednesday Level*, FED. RSRV. ECON. DATA: ST. LOUIS, https://fred.stlouisfed.org/series/TREAST [https://perma.cc/EL5Y-KEX4] (last updated Aug. 17, 2023).

255. *Assets: Securities Held Outright: Mortgage-Backed Securities: Wednesday Level*, FED. RSRV. ECON. DATA: ST. LOUIS, https://fred.stlouisfed.org/series/WSHOMCB [https://perma.cc/G6N2-LSND] (last updated Aug. 17, 2023).

256. *See* Gwynn Guilford, *U.S. Inflation Remained High in August*, WALL ST. J. (Sept. 13, 2022), https://www.wsj.com/articles/us-inflation-august-2022-consumer-price-index-11663017630 [https://perma.cc/F5XX-LKFD] (noting record high inflation and rising consumer-price index since 2021).

257. *See* JEFFREY M. STUPAK, CONG. RSCH. SERV., R45723, FISCAL POLICY: ECONOMIC EFFECTS (2019) ("[E]xpansionary fiscal policy can result in rising interest rates, growing trade deficits, and accelerating inflation . . . .").

258. *See* Ana Maria Santacreu & Jesse LaBelle, *Supply Chain Disruptions and Inflation During COVID-19*, FED. RSRV. OF BANK ST. LOUIS: ECON. SYNOPSES 2 (May 12, 2022), https://files.stlouisfed.org/files/htdocs/publications/economic-synopses/2022/05/12/supply-chain-disruptions-and-inflation-during-covid-19.pdf [https://perma.cc/T2LC-Y8RH] ("Supply chain disruptions have contributed large increases in PPI inflation during the COVID-19 pandemic.").

Second, we note that expansionary monetary policy could cause financial instability by creating asset bubbles.[259] This occurs when the Federal Reserve leaves interest rates too low for too long.[260] For instance, in response to the recession caused by the dot-com bubble burst, the Federal Reserve lowered interest rates in 2001 and kept them low through 2004.[261] Many argue that this low interest environment boosted asset markets, particularly housing markets.[262] (Low interest rates make it cheaper to obtain a mortgage which, all else equal, makes it easier to purchase a house.) As is well-known now, the bursting of the housing market bubble precipitated the global financial crisis. Thus, we see the trade-off from the other side: as the Federal Reserve lowered interest rates in response to a recession and kept them low for years to maintain the economic recovery, its monetary policy facilitated the growth of an asset bubble that led to financial instability later on. Going back to our discussion of the COVID response, some also argue that the Federal Reserve's monetary policy response in 2020 led to a speculative asset bubble in equities and cryptocurrencies.[263] Indeed, once the Federal Reserve started tightening, equity markets and cryptocurrency prices fell dramatically.[264]

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259. *See* Feng Dong et al., *Asset Bubbles and Monetary Policy*, 37 REV. ECON. DYNAMICS S68, S69 (2020) ("An expansionary monetary policy by cutting the interest rate or raising the money supply can raise the initial size of the asset bubble . . . .").

260. *Id.*

261. *See* Ben S. Bernanke, Chairman, Bd. of Governors of the Fed. Rsrv. Sys., Address at the Annual Meeting of the American Economic Association: Monetary Policy and the Housing Bubble (Jan. 3, 2010) (transcript available at https://www.federalreserve.gov/newsevents/speech/bernanke20100103a.htm [https://perma.cc/5MD7-ELFR]) ("[T]he target federal funds rate was lowered quickly in response to the 2001 recession, from 6.5 percent in late 2000 . . . to 1 percent in June 2003. After reaching the then-record low of 1 percent, the target rate remained at that level for a year.").

262. *See* John B. Taylor, *Housing and Monetary Policy* (Nat'l Bureau of Econ. Rsch., Working Paper No. 13682, 2007) (arguing that the low interest rate before the Great Recession led to excessive investment in housing).

263. *See* Ron Surz, *Money Printing and Inflation: COVID, Cryptocurrencies and More*, NASDAQ (Nov. 16, 2021), https://www.nasdaq.com/articles/money-printing-and-inflation%3A-covid-cryptocurrencies-and-more [https://perma.cc/RK5Q-S963] (noting that concerns over inflation have pushed many to invest in cryptocurrencies).

264. *See* Sunil Jagtiani, *Bitcoin, Ether Drop as Fed Move Hits Crypto Assets*, L.A. TIMES (Sept. 21, 2022), https://www.latimes.com/business/story/2022-09

Third, we note the general difficulty with striking the right balance between financial stability, even stability on a more micro scale than rescuing the entire economy, and monetary policy. This technical example involves the Federal Reserve's purchases of Treasuries in 2020 and a regulation called the leverage ratio.[265]

In March 2020, aggregate demand for Treasury market liquidity (i.e., offers to sell Treasury securities for cash) from a wide range of investors exceeded the aggregate supply of Treasury market liquidity on offer (i.e., the market's ability to purchase those Treasury securities).[266] The Treasury market became illiquid. According to research produced by staff at the Federal Reserve Bank of New York, the bid-ask spread—defined as the difference between the lowest ask price and the highest bid price for a security—spiked to levels unseen since the 2008 global financial crisis; and order book depth—the average quantity of securities available for sale or purchase at the best bid and ask prices—declined to levels unseen since the 2008 crisis.[267] This was traumatic because the U.S. Treasury market is the most important sovereign debt market in the world. Treasury securities are used to finance the U.S. government, serve as a risk-free investment for investors that seek safety and liquidity,

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-21/bitcoin-ether-drop-fed [https://perma.cc/7TR4-LSSN] ("Cryptocurrencies came under pressure Wednesday after the Federal Reserve delivered another big interest rate hike and warned of economic pain from the aggressive policy tightening still to come.").

265. *See* Eric Milstein et al., *What Does the Federal Reserve Mean When It Talks About Tapering?*, BROOKINGS INST. (July 15, 2021), https://www.brookings.edu/articles/what-does-the-federal-reserve-mean-when-it-talks-about-tapering [https://perma.cc/6P4C-RA4Y] (noting the Federal Reserve's purchase of $80 billion in Treasury securities from June 2020 to October 2021).

266. *See* Michael S. Derby, *Fed Official Wonders Whether Treasury Market Can Handle Massive Issuance Alone*, WALL ST. J. (Oct. 14, 2020), https://www.wsj.com/articles/fed-official-wonders-whether-treasury-market-can-handle-massive-issuance-alone-11602713864 [https://perma.cc/2BVW-W8V8] (quoting Federal Reserve Vice Chair for Supervision, Randal Quarles, "[i]t may be that there is a simple macro fact that the Treasury market, being so much larger than it was even a few years ago, much larger than it was a decade ago, and now really much larger than it was even a few years ago, that the sheer volume there may have outpaced the ability of the private-market infrastructure to kind of support stress of any sort there").

267. Michael Fleming & Francisco Ruela, *Treasury Market Liquidity During the COVID-19 Crisis*, LIBERTY ST. ECON. (Apr. 17, 2020), https://libertystreeteconomics.newyorkfed.org/2020/04/treasury-market-liquidity-during-the-covid-19-crisis [https://perma.cc/Q9EP-FDHB].

act as a risk-free benchmark for pricing other financial instruments, and are the primary asset class through which the Federal Reserve implements monetary policy.[268]

During that time, the bindingness of an institution-level regulation called the supplementary leverage ratio (SLR) conflicted with the operation of monetary policy—namely, purchases of Treasuries by the Federal Reserve. The SLR is a simple regulation used by financial regulators to ensure that firms have enough capital to support their assets.[269] The leverage ratio requires a regulated organization to maintain a minimum level of regulatory capital relative to its total assets.[270] The denominator includes all assets equally—it does not put a higher weight on riskier assets or a lower weight on safer assets.[271] The risk-insensitivity of a leverage ratio has drawbacks and, on the margin, can disincentivize banking firms from holding or acquiring low-risk assets like Treasuries. In March 2020, banks faced massive draws on corporate credit facilities and a sudden inflow of deposits,[272] increasing the denominator of their leverage ratios—that is, increasing the size of their balance sheets. This growth moved large banks closer to breaching their SLR requirements, and it made accumulation of additional Treasury securities challenging.

Initial purchases of Treasuries by the Federal Reserve did not free up much space on bank balance sheets, because the Federal Reserve paid for Treasuries with reserves (i.e., deposits at Federal Reserve Banks), and those reserves were still subject to

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268. U.S. DEP'T TREASURY, BD. OF GOVERNORS OF THE FED. RSRV. SYS., FED. RSRV. BANK. N.Y., U.S. SEC. EXCH. COMM'N & U.S. COMMODITY FUTURES TRADE COMM'N, RECENT DISRUPTIONS AND POTENTIAL REFORMS IN THE U.S. TREASURY MARKET: A STAFF PROGRESS REPORT 1 (Nov. 8, 2021).

269. *See* Mark E. Van Der Weide & Jeffery Y. Zhang, BANK CAPITAL REQUIREMENTS AFTER THE FINANCIAL CRISIS, *in* OXFORD HANDBOOK OF BANKING 707, 721 (Allen N. Berger, Philip Molyneux & John O.S. Wilson eds., 3d ed. 2019) (noting the "comprehensive capital stress tests" regulators conduct for large banks to "ensure that the capital levels of the firms are consistent with their withstanding a severe macroeconomic stress").

270. *Id.*

271. *See* Alice Abboud et al., *COVID-19 as a Stress Test: Assessing the Bank Regulatory Framework*, BD. OF GOVERNORS OF THE FED. RSRV. SYS. FIN. & ECON. DISCUSSION SERIES 2021-024 (Mar. 2021) (explaining the denominator of the leverage ratio is daily average assets).

272. *Id.* at 4 ("During March, 2020, dislocations appeared in financial markets, as firms withdrew from market making activity . . . .").

the SLR.[273] This is an underappreciated point: the Federal Reserve cannot simply buy its way out of this problem. To preserve the functioning of the Treasury market, the Federal Reserve first had to free up space on the banks' balance sheets. As a result, the Federal Reserve took the unprecedented step of temporarily excluding Treasury securities and deposits at Federal Reserve Banks from the calculation of the SLR applicable to large banking firms.[274] This example highlights the difficulty with harmonizing financial stability (even at an institutional level with the leverage ratio) and implementing monetary policy.[275]

CONCLUSION

Lawmakers and commenters have called upon the Federal Reserve to take on several new tasks in recent years, and no wonder: the central bank is seen as an effective steward of macroeconomic growth, and it has been an extremely effective firefighter during economic emergencies in 2008 and 2020. In this Article, we propose a framework grounded in law and economics to examine whether the Federal Reserve should adopt an array of new priorities to deal with important social issues that are outside of its core mission and expertise.

The first part of our framework analyzes the legal challenges that might arise by focusing on the major questions doctrine, the nondelegation doctrine, and procedural hurdles in administrative law. In the second step, we utilize economic theory to argue that adopting unrelated mandates might make it more

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273. *See* Darrell Duffie, *Still the World's Safe Haven? Redesigning the U.S. Treasury Market After the COVID-19 Crisis*, BROOKINGS INST. (June 22, 2020), https://www.brookings.edu/research/still-the-worlds-safe-haven [https://perma.cc/UTM9-D776].

274. *See* Press Release, Bd. of Governors of the Fed. Rsrv. Sys., Federal Reserve Board Announces Temporary Change to its Supplementary Leverage Ratio Rule to Ease Strains in the Treasury Market Resulting from the Coronavirus and Increase Banking Organizations' Ability to Provide Credit to Households and Businesses (Apr. 1, 2020) (on file with the Univ. of Minn. L. Libr.).

275. One idea, proposed by the former president of the Federal Reserve Bank of New York, Bill Dudley, is to permanently exempt central bank reserves from the leverage ratio. *See id.* at 2. This would not amount to a watering down of regulatory benefits because central bank reserves are essentially cash and therefore risk-free. *See also* Bill Dudley, Opinion, *The Longer-Term Lessons of the Repo Turmoil*, BLOOMBERG (Oct. 23, 2019), https://www.bloomberg.com/opinion/articles/2019-10-23/the-longer-term-lessons-of-the-repo-market-turmoil#xj4y7vzkg [https://perma.cc/F2AK-WZNQ].

difficult for the Federal Reserve to meet its original charges related to keeping inflation in check and maximizing employment.

To be clear, our framework does *not* imply that Congress should ignore longstanding problems like climate change or the wealth gap. Rather, our framework suggests that Congress should not have any single regulatory agency—with its limited set of tools—expand beyond its original mandates and core competencies to solve those problems. To best achieve those objectives, Congress should instead empower the agencies most closely aligned with those objectives.