A Review of
Proposed Organizational Changes
in the Policy-Making Structure
of the Federal Reserve System

By
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I. Introduction

The last major changes in the structure of the Federal Reserve System were introduced in the Banking Act of 1935. Suggestions for change have continued to come forth since that time. The issues raised by these proposals have been roundly discussed by legislators, government officials, bankers, and students of central banking. These discussions and debates, sometimes intense, have never culminated in the legislative enactment of any major structural change. The reasons for this are open to speculation. It seems doubtful that the failure to legislate demonstrates the perfection of the System. More likely, it reflects the absence since the mid-1930's of any crisis of public confidence in either the banking system or the central bank that would have generated a widespread call for amendment.

The present paper is a review of major proposals for changing the organizational structure of the Federal Reserve System and of the arguments put forward in both support and opposition. It covers the period 1949 through 1970 and should serve as a compilation to which easy reference can be made in searching for old or tracing the history of new proposals.

Virtually all of the proposed modifications in organizational structure have been advanced as means of (1) streamlining the decision-making procedure in the System; (2) altering the weight given to business, regional, and political viewpoints in the decision process; and (3) assuring better coordination between monetary and fiscal policy in striving to reach the
nation's economic goals. They have involved the four principal units in the legal makeup of the System: namely, the Board of Governors, the Federal Open Market Committee, the Federal Advisory Council, and the regional Federal Reserve Banks. The material that follows is organized under these headings. An appendix contains a listing of proposed structural changes, by source and by date.

II. Board of Governors

Various changes have been suggested with respect to the appointment process, size, designation of chairman, qualifications for membership, and length of term of the Board of Governors. In addition, there has been considerable discussion about the Board's proper place in the overall governmental structure.

Method of Appointment

There seems to be fairly widespread agreement that the present procedure of Presidential appointment and Senate approval of Board members is good and should not be changed. However, there are some who feel that central bank operations most directly affect bankers, businessmen, and the federal government and that these groups should be assured of representation on the Board.

Therefore, some have suggested that once again it be required that two members of the Board be experienced in banking. Another suggested procedure would permit the President and Senate to select three members of the Board, the Chairman, the Vice Chairman, and an additional member, all chosen to represent the general public. The other four members would be selected by the presidents of the banks that are members of the System. Two of the Governors would represent the banking community; the other two would represent nonbanking commerce and industry. Two selection methods would be used. One Governor in each class would be elected by commercial bank presidents on a
basis of one vote each. Election of the other Governor in each class would be based on one vote for each bank plus one additional vote for each ten million dollars of capital and surplus.²

Others believe that the Federal Reserve Banks should be represented on the Board.³ They suggest a Board of fifteen members. The President would appoint the Chairman and two Vice Chairmen. Each of the other Governors would be chosen by a Federal Reserve Bank.⁴

Qualifications

The present geographical and occupational qualifications for Board membership have been a point of considerable discussion. While some feel it is important to ensure that a certain number of different regions are represented,⁵ most seem to believe that the President should be able to appoint the best-qualified person he can find without the restriction of geographical location.⁶ While this qualification probably does ensure that different regional viewpoints will be heard, many claim information on regional conditions is all that is really necessary for policy considerations, not regional representation. Similar arguments are also given for and against retaining the present occupational guidelines. Some argue they are necessary to ensure that various viewpoints are recognized and heard. Others emphasize that policy decisions should be made with respect to the general interest of the nation, not with special consideration for specific groups.⁷ They claim that Governors chosen for their former occupations may feel that they should try to represent that group, and they do not feel that national monetary policy decisions should be a compromise between various interest groups.⁸ Also, representation of some interests -- real or imagined -- will lead other groups to want representation, and there certainly are not enough places to go around.
While the discussion goes on about eliminating some qualifications, others argue that additional qualifications are needed. Some, believing the duties of the Board are of a technical nature, would like to require that an appointee be well versed in banking and finance by education, training, or experience.\footnote{9}

Others have cautioned against having too many former bankers on the Board.\footnote{10} They believe that bankers, due to their past experience, tend to prefer high interest rates and that this might interfere with their consideration of what is good for the national economy. Still others would like an assurance against either political party clearly gaining control.\footnote{11} They suggest a rule be implemented prohibiting more than four of the Board members from belonging to the same political party.

Some also suggest that age limitations be placed on Board members. One qualification might be that no one be appointed to the Board if they would become seventy before their term expired.\footnote{12} Others suggest that if reappointment is permitted, no Governor be eligible for reappointment after reaching the age of sixty-five.\footnote{13}

Size of Board

There have been many suggestions for change in the size of the Board.\footnote{14} Most have been for reducing the size. Those arguing against a size reduction claim there is greater safety and wisdom in a larger Board, and that because of the responsibilities of the Governors and their frequent need to be out of town it would be difficult for a smaller Board to conduct business. An argument in favor of a reduction in the size of the Board is that a large group is justified only if additional members add significantly to the decision process and that this is not true with respect to the present Board.\footnote{15}
They claim a smaller Board could act more quickly and with greater efficiency. Many further believe that a size reduction would add more prestige to the Board positions, making it easier to attract outstanding men. Establishment of a smaller Board might also be a step toward providing better government economic policy coordination since it might then be easier for all the Governors to be kept informed on the opinions of the Treasury and the Council of Economic Advisors.

There has also been some support for replacing the Board with a single executive. Some claim this structure would be desirable since one person would be able to act quickly and would clearly be held responsible for his actions. Requirements that the executive consult regularly with the Reserve Bank presidents would ensure that he would always be informed on significant regional matters.

**Term of Appointment**

Another area of debate which arises with discussions concerning changes in the size of the Board is the length of term. Almost all proposals have suggested a reduction in the term. While many of the shorter terms have been suggested to correspond with a decrease in the size of the Board, there are also arguments for change in the term structure. It is argued that during a fourteen-year term members may lose enthusiasm and effectiveness and let up on their responsibilities. Under present laws it is very difficult to remove a member from the Board. On the other hand, too short a term might make it possible for the appointment of Governors to become subject to political pressures or to become a political issue. There is also the danger that the decisions of Governors, especially of those returning to the fields of banking or business after serving just one short term, might be influenced by considerations of their own economic future.
Most suggestions are for terms of from five to ten years. This period, it is felt, is long enough to insulate the Governors from undue Presidential pressure. Yet it is short enough to ensure that some members will have views fairly similar to those of the President. However, at least one individual has suggested making all terms coterminous with that of the President.

In addition to suggestions of shorter terms, some would like to reexamine the present provision that a Governor may not be reappointed. The major argument for prohibiting reappointment is that Governors will make decisions without reflecting on how their opportunities for reappointment may be affected. However, with the shorter terms and no reappointment permitted, a well-qualified man would be available for only a limited period of time. An additional problem with shorter terms and no reappointment is that some well-qualified men might be reluctant to give up lucrative positions knowing they would be able to serve for just a brief period while on the Board.

Chairmanship

The term of the Chairman has been an item of some discussion. There is strong support for having the term of the Chairman, and possibly that of the Vice Chairman, coterminous with that of the President. Such a change would ensure that the President's views would be well represented on the Board while still not permitting him to control it. Indeed, even the Chairman of the Board would be free to disagree with the views of the President without risking immediate loss of his job. Others would go even further. They believe that the Chairman should always be representing the President's views and therefore should serve at the pleasure of the President.
Other Formal Policy Coordination Measures

Some suggested changes in the Board of Governors have resulted from a search for better ways to coordinate fiscal and monetary policies. It has been suggested that the Secretary of the Treasury be named to membership on the Board or that an Assistant Secretary of the Treasury be an ex-officio member. While the need for better coordination and communication is recognized, opponents of these suggestions argue that such changes might make the Treasury subordinate to the Federal Reserve System or vice versa and would at least place the Secretary of the Treasury in a position of having a conflict of interests. They claim that either of these suggestions would really be an awkward and unnecessary way of establishing a permanent liaison between the Treasury and the Fed. As a practical matter, it is further argued that the Secretary of the Treasury is too busy to attend the Board meetings.

Another suggested way to increase coordination is to make the Chairman of the Board a member of the President's Cabinet. Those favoring this proposal claim that in addition to allowing greater communication, it would enable the President to exert influence while still permitting the Board to take action in opposition to the views of the President. However, others argue this appointment would differ from the other Cabinet appointments and that the Chairman would not then be able to speak generally for the Board.

III. Federal Open Market Committee

Another part of the Federal Reserve structure which has been an object of much interest is the Federal Open Market Committee (FOMC). Suggestions for changing this committee range from enlarging it to abolishing it and turning its responsibilities over to the Board of Governors. One of the suggestions for enlarging it provides that it include as ex-officio voting members the Secretary of the Treasury and the Chairman of the Council of Economic Advisors in order to provide for better policy coordination.
Those in favor of abolishing it believe that its duties should be turned over to the Board of Governors. 34 They believe that decisions concerning monetary policy should be centralized in one group and that open market policy can be made just as well by the Board (implying that bank presidents are not necessary participants in monetary policy deliberations). Various reasons are also given for why the presidents in fact should not take part in such policy-making. Some believe they largely reflect just the viewpoints of bankers and businessmen. 35 Others argue that bank presidents place too much emphasis on regional considerations and that although knowledge of the conditions in the various regions is necessary and desirable, voting should not be continually influenced by special consideration of one region. 36 Defenders of such membership on the FOMC believe that the presidents have generally acted as a moderating influence and that their membership on the committee helps maintain a close relationship between the banks and the Board of Governors. 37 In addition, if the presidents did not have the responsibility of committee membership, they would really be nothing more than branch managers. This would make it difficult to attract top-quality men to the bank presidencies, and as a result the prestige and the efficiency of the entire System might fall. 38

Others have argued that even if the FOMC is retained, its size should be reduced. They claim the present committee is too large to permit decisions to be made on the basis of rigorous analysis and hard empirical work. They claim that presently much of the committee's time must be spent attempting to reach a consensus and the presence of much indecision within the committee means it is often slow in taking appropriate action. 39

Another aspect of the FOMC which has received some study is the special role played in it by the Federal Reserve Bank of New York. Since open market operations are meant to be national in impact, some argue there is no reason why the New York Fed should have special voting privileges. 40
role of the manager of the Open Market Account and his influence on the FOMC have also been questioned. 41

IV. Federal Advisory Council

The structure of the Federal Advisory Council has also been a matter for debate. Some argue in favor of abolishing it, asserting that it does not play any significant role. 42 The major argument for retaining it is that it does guarantee the Board will consult with someone from time to time. However, some would prefer to see an advisory board which represents a larger group than just commercial bankers. 43 Two specific plans that have been suggested probably do ensure that a somewhat wider range of viewpoints would be represented. One would enable the Reserve Banks to play a major role in appointing the Council. Each Reserve Bank would submit the names of two nominees and from all of the names submitted, the Board would appoint twelve men to the Council. They would serve three-year terms and could not be immediately reappointed. 44 The other plan provides for the Council to be considerably enlarged to not more than forty members, including the Comptroller of the Currency and the Chairman of the Board of Directors of the Federal Deposit Insurance Corporation. It is suggested that the terms remain at their present length of one year. 45

V. Federal Reserve Banks

Number of Districts

While no one strongly insists that twelve is necessarily the best number of Federal Reserve Districts, there has been little recent interest over the number of districts. However, in 1958 when Alaska and Hawaii gained statehood, some individuals suggested that this would perhaps be an appropriate time to make some changes in district boundaries. A bill was introduced in Congress which would have provided for one additional district and the boundaries shown below. 46
A plan for reducing the number of districts has also been suggested.\[47\]
It is claimed that reducing the number would result in districts with more in common than the present districts. Arguments for increasing the number of districts are based mainly on the belief that the present Twelfth District is too large and should be subdivided.

Where there might be some general advantages to making district boundaries coincide with state lines, the general feeling seems to be that the potential advantages do not warrant the cost of changing district boundaries.

There have been a variety of viewpoints expressed about the Boards of Directors of the Federal Reserve Banks. Many feel the Boards serve no useful purpose and should be abolished. Others feel the method of selecting Directors should be changed to include a wider range of interests than just bankers and businessmen. However, others caution that any change in the selection procedure of Directors could cause considerable misunderstanding as member banks might feel that they were losing most of the voice which they now have in the Federal Reserve Banks.

In addition to the discussion of whether or not bank presidents should serve on the Federal Open Market Committee, there has been some discussion on how they should be selected, especially if the presidents continue to serve on the FOMC. One suggestion would have appointments made by the President, subject to Senate confirmation. Another plan would have the Federal Reserve Bank presidents appointed by Congress.
APPENDIX

Proposals for Structural Change
by Year and by Source

1949: **Background:** The Senate instructed the Joint Economic Committee to carry out four studies, one of which was an examination of the effectiveness and coordination of monetary, credit, and fiscal policies in dealing with general economic policy. Paul H. Douglas chaired the subcommittee which executed this study and gathered opinions of a large number of individuals through surveys and hearings.

**Recommendations:**
(i) The size of the Board of Governors should be reduced to not more than five.
(ii) There should be established a National Monetary and Credit Council to help coordinate monetary policy.

1951: **Background:** In 1951, after the Treasury-Federal Reserve "accord," the Joint Economic Committee established a subcommittee to conduct a general inquiry into monetary policy and debt management. This subcommittee was chaired by Wright Patman and solicited opinions by means of an extensive questionnaire and formal hearings.

**Recommendations:**
(i) The Federal Open Market Committee should continue in the role of a useful link between directors and managements of the individual reserve banks, on the one hand, and the Board of Governors on the other.
(ii) The Board of Governors should consider including representatives of labor among those whom it regards as eligible for appointment as Class C directors.
(iii) The term of office of the Board of Governors should be reduced from fourteen to six years, and members of the Board should be made eligible for reappointment.
(iv) The number of members of the Board should be reduced from seven to not more than five, and the number of Federal Reserve Bank presidents on the Federal Open Market Committee should be reduced to maintain, as far as possible, the present proportion between members of the Board of Governors and Federal Reserve Bank presidents in the composition of the Committee.
(v) The Chairman of the Board of Governors should be appointed by the President and his term be made coterminous with that of the President.
(vi) Present geographical and other qualifications for membership on the Board of Governors should be eliminated.
1958: Alaska and Hawaii were admitted as new states and Senator Magnuson of Washington introduced a bill (S4298) to increase the number of Federal Reserve Districts to thirteen.

1961: Background: In 1958 the Board of Trustees of the Committee for Economic Development established a Commission on Money and Credit to initiate studies into the United States monetary and financial system. After extensive research, the Commission's report was published in 1961 and the Joint Economic Committee held hearings reviewing the report.

Recommendations:

(i) The Federal Reserve Board Chairman and Vice Chairman should be designated by the President from among the Board's membership, to serve for four-year terms coterminous with the President's.

(ii) The Federal Reserve Board should consist of five members, with overlapping ten-year terms, one expiring each odd-numbered year; members should be eligible for reappointment.

(iii) Occupational and geographical qualifications for Board members should be eliminated. Instead, the statute should stipulate that members shall be positively qualified by experience or education, competence, independence, and objectivity commensurate with the increased responsibilities recommended for them in the achievement of low levels of unemployment, an adequate rate of economic growth, and reasonable stability of price levels in the economy. Salaries of top officials throughout the government should be sharply increased, and in view of the gravity of their responsibilities, Federal Reserve Board members should be compensated at the highest salary level available for appointive offices in the government.

(iv) The present statutory Federal Advisory Council should be replaced by an advisory council of twelve members appointed by the Board from nominees presented by the boards of directors of the Federal Reserve Banks. At least two nominations, not more than one of them from any single sector of the economy, should be presented by each Bank. The Board should make its selection, one from each district, in such a manner as to secure a council broadly representative of all aspects of the American economy. Council members should serve three-year terms, not immediately renewable. The council should meet with the Federal Reserve Board at least twice a year.

(v) An important internal source of advice should be further recognized and strengthened. The law should formally constitute the twelve Federal Reserve Bank presidents as a Conference of Federal Reserve Bank Presidents, to meet at least four times a year with the Board, and more frequently as the Board finds necessary.

(vi) The determination of open market policies should be vested in the Board. In establishing its open market policy the Board should be required to consult with the twelve Federal Reserve Bank presidents. The determination of the rediscount rate (the same for all Reserve Banks) should be vested
With the Board. In establishing this rate the Board should be required to consult with the twelve Federal Reserve Bank presidents. The determination of reserve requirements should continue to be vested in the Board. In establishing these requirements the Board should be required to consult with the twelve Federal Reserve Bank presidents.

1964: Background: Representative Wright Patman introduced a bill (H.R. 9631) in the House of Representatives which would provide for the following structural changes in the Federal Reserve System.

(i) A Federal Reserve Board of twelve members would be established to replace the Board of Governors. The Secretary of the Treasury would serve as Chairman; and the President, with the advice and consent of the Senate, would appoint the remaining eleven members.

(ii) Terms of appointment would be four years.

(iii) The duties of the Federal Open Market Committee would be turned over to the Board.

(iv) The present Federal Advisory Council would be abolished and a Federal Advisory Committee would be established. It would be comprised of the Comptroller of the Currency, the Chairman of the Board of Directors of the Federal Deposit Insurance Corporation, and not more than fifty other members appointed for one-year terms.

This bill served as a starting point for discussion and hearings by the Subcommittee on Domestic Finance of the House Committee on Banking and Currency on "The Federal Reserve System After Fifty Years." The subcommittee took no action on the bill, but its Democratic members did make some recommendations for further study.

Recommendations:

(i) Vest all power to conduct open market operations in the Federal Reserve Board.

(ii) Remove occupational requirements for Governors and instead require only that they be men of integrity devoted to the public interest.

(iii) Reduce the size of the Board of Governors to five, make the terms five years, and permit reappointment.

(iv) Make the Chairman's term coterminous with that of the President.

1964: Background: The Subcommittee on Domestic Finance of the House Committee on Banking and Currency commissioned economists Karl Brunner and Allan Meltzer to do a study analyzing Federal Reserve monetary policy.

Recommendations:

(i) The FOMC should be abolished.

(ii) Serious consideration should be given to replacing the Board of Governors with a single administrative official assuming that the principal responsibility of the officer becomes deciding on the appropriate growth rate of the monetary base after interpretation of events occurring in the economy.
1965: The Joint Economic Committee held an inquiry into the breakdown of economic policy coordination called for in the Employment Act of 1946. During these hearings there was considerable concern shown over the need for changes in the Federal Reserve System. No specific recommendations were issued. However, in its 1966 Joint Economic Report the committee stated that legislation, of an unspecified nature, was needed to assure no future breakdowns in coordination.

1967: A bill (H.R. 11) was introduced in the House of Representatives intended to make the following changes in the structure of the Federal Reserve System:

(i) The Board of Governors would be reduced to five members.
(ii) A Governor's term of office would be reduced to five years.
(iii) The Chairman's term would be coterminous with that of the President.

1969: In the January Economic Report of President Johnson the following changes were recommended to Congress:

(i) The term of Chairman of the Federal Reserve Board should be appropriately geared to that of the President to provide further assurance of harmonious policy coordination.
(ii) The rigid requirement that no more than a single member of the Federal Reserve Board may be appointed from any one Federal Reserve District should be removed so that the President, with the advice and consent of the Senate, may choose the very best talent for the Board.
(iii) The Congress should review procedures for selecting the presidents of the twelve Reserve Banks to determine whether these positions should be subject to the same appointive process that applies to other posts with similarly important responsibilities for national policy.

1970: President Nixon appointed a Commission on Financial Structure and Regulation. The Commission began meeting in June. It expects to work through a series of special study groups to formulate recommendations for legislation on the structure and regulation of financial institutions in the United States.
FOOTNOTES


2 James Washington Bell and Walter Earl Spahr (eds.), A Proper Monetary and Banking System for the United States (New York: Ronald Press, 1960), p. 65. (An accompanying change would be the abolition of the FOMC and turning over its duties to the Board.)

3 This suggestion is also meant to combine the Board and the FOMC into one unit.


7 Commission on Money and Credit, p. 88.


Fergusson, p. 38.
The following sizes and term structures have been suggested as possible changes:

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<thead>
<tr>
<th>Board Size</th>
<th>Term Length (if specified)</th>
<th>Sources</th>
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<tr>
<td></td>
<td>no exact length specified but suggests shorter than 14 years</td>
<td>New York Clearing House Association, p. 138.</td>
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<tr>
<td>5</td>
<td>12 years</td>
<td>Joint Committee, Monetary, Credit, and Fiscal Policies..., 1949, p. 68.</td>
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<tr>
<td>5</td>
<td>1 year rotation</td>
<td>Joint Committee, Monetary, Credit, and Fiscal Policies..., 1949, p. 164.</td>
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<tr>
<td>5</td>
<td>10 years</td>
<td>Joint Committee, Monetary, Credit, and Fiscal Policies..., 1949, p. 68.</td>
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<tr>
<td>Board Size</td>
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<td>Joint Committee, Monetary, Credit, and Fiscal Policies..., 1949, p. 308.</td>
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<td>12 Secretary of the Treasury as Chairman</td>
<td>1-4 years</td>
<td>U.S., Congress, House, Federal Reserve System After Fifty Years: Hearings, 1964, p. 4.</td>
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<td>7</td>
<td>7 years</td>
<td>U.S., Congress, House, Compendium..., 1968, p. 80.</td>
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<td>3</td>
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<td>Fergusson, p. 37.</td>
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18 Goldenweiser, p. 301.
20 U.S., Congress, House, Compendium..., 1968, pp. 45, 64.


26 Commission on Money and Credit, p. 87.


Reagan, p. 75.


29 Fergusson, p. 37.


31 Goldenweiser, p. 301.


Commission on Money and Credit, p. 90.

Fergusson, p. 39.


20


37 Bell and Spahr, pp. 69-70.


39 Bach, Excerpts from Making Money and Fiscal Policy, p. 42.
Goldenweiser, p. 300.


42 Reagan, p. 67.


44 Commission on Money and Credit, p. 89.


46 "Shuffle in Bank Districts?" Business Week, October 18, 1958, p. 27.

47 Bell and Spahr, p. 56.


52 U.S., Congress, House, Compendium…, 1968, p. 82.

53 A committee established under the Employment Act of 1946 which has as one of its duties to make a continuing study of matters relating to the Economic Report and means of coordinating programs in order to further the policy of the Employment Act.


56. Commission on Money and Credit, pp. 87-90.


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Monetary Policy and the Management of the Public Debt: Their Role in Achieving Price Stability and High-Level Employment - Replies to Questions and Other Material for the Use of the Subcommittee on General Credit Control and Debt Management, Parts 1 and 2. 82nd Cong., 2nd Sess., 1952.


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