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Observations on the Constitutional Position of the Federal Reserve Board

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OBSERVATIONS ON THE CONSTITUTIONAL POSITION OF THE FEDERAL RESERVE BOARD*

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During the Spring of 1964 the Subcommittee on Domestic Finance of the Banking and Currency Committee of the House of Representatives held a series of important hearings on the position of the Federal Reserve System in American Government and in the American economy The Subcommitttee, under the chairmanship of Representative Wright Patman of Texas, had five bills before it for consideration: H.R. 3783; H.R. 9631, H.R. 9685; H.R. 9686; H.R. 9687 In main thrust, these bills would, if enacted, substantially change the position of the Board of Governors of the Federal Reserve System by placing it under direct control of the President and would otherwise alter the System as it has existed since its establishment in 1913.

This brief paper discusses certain legal-policy questions involved in those bills. At the outset I should like to underscore two factors: first, that this is a public law analysis—a legal analysis, in other words—and the economic effects of the monetary structure are not a part of this discussion, although it is clear that a legal analysis cannot escape being concerned with certain policy questions; second, that in such a brief statement all details cannot be covered. Necessarily, then, I shall confine myself to several broad propositions. Some of what I will say may be obvious to some, but nonetheless I think it bears restatement.

1. *Although Congress has undoubted constitutional power over monetary matters, that power is in fact fragmented over several agencies of government.*

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*The substance of this article consists of testimony presented on April 14, 1964 before the Subcommittee on Domestic Finance of the Committee on Banking and Currency of the House of Representatives. The article has been left in the same form as it was presented the only additions are the introductory and concluding paragraphs.

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Under article I, section 8 of the Constitution, Congress could, of course, establish a system whereby it would itself regulate the value of money and such allied matters as were considered necessary and proper to carry out that goal. Or Congress, alternatively, could do nothing; there is nothing in the Constitution which affirmatively requires Government to take such action; it could be left entirely to private volition. I take it that neither of those alternatives is considered desirable.

What has been done seems to be a series of delegations of power from Congress—to the Treasury and to the Federal Reserve Board, and also to the Comptroller of Currency and the Federal Deposit Insurance Corporation—whereby either executive departments or agencies or "independent" organizations exercise some influence and power over monetary matters. It thus seems valid to conclude that the Congress, for whatever reasons, believes that such power should be fragmented and exercised by a congeries of organizations, not excluding the Congress itself.

This is in accord with our history, but the question now is whether such splintering of power is desirable. My conclusion, which I will expand a little later, is that whatever merit power fragmentation may have as between branches of government, it has little or none so far as one branch is concerned.

2. *Congressional delegations of power in monetary matters are valid under the Constitution.*

The law on delegation of power is a latterday gloss on the Constitution enunciated, as far as limitations are concerned, by the Supreme Court during the thirties. There have been only two cases in history which have invalidated attempted delegations to governmental agencies, both of which grew out of early legislation in the administration of President Franklin D. Roosevelt: The *Schechter*[1] and *Panama Oil*[2] cases, both of which did not involve delegation to a regularly constituted administrative agency which followed an established procedure designed to afford customary

1. Schechter Corp v. United States, 295 U.S. 495 (1935).
2. Panama Refining Co. v. Ryan, 293 U.S. 388 (1935).

safeguards to affected parties. There was a third case, the *Carter Coal*[3] decision, which did involve the agricultural legislation at that time and which to some extent concerned a delegation of what was considered to be a private organization. The Supreme Court in the *Carter Coal* case held this agricultural legislation invalid.

The black-letter rule of law, in brief, seems to be this: power committed by the Constitution to the Congress may be delegated, provided that the delegation is not of unlimited discretionary power As the Supreme Court said in 1928:[4]

> If Congress shall lay down by legislative act an intelligible principle to which the person or body authorized [to act] is directed to conform, such legislative action is not a forbidden delegation of legislative power

Using that principle, the Supreme Court struck down the two statutes in the cases mentioned above. Neither statute contained an "intelligible principle" to canalize the administrative action.

But that is not the end of the matter As subsequent court decisions have shown, and as practice has developed, Congress has delegated power to the executive branch and to the so-called independent regulatory commissions under the most liberal standards, with the net result that it is fair to say that the present-day viability of the *Schechter* and *Panama Oil* cases is extremely dubious. Thus to cite but two examples, Congress enacted legislation for the renegotiation of contracts during World War II and the recovery of "excessive profits," but failed to define "excessive"; nevertheless, the delegation was upheld by the Supreme Court[5]; and in the Communications Act of 1934[6], the Federal Communications Commission was invested with power to operate as the "public convenience, interest, or necessity requires." This, too, was upheld by the Supreme Court.[7]

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3. Carter v. Carter Coal Co., 298 U.S. 238 (1936).
4. Hampton & Co. v. United States, 276 U.S. 394, 409 (1928).
5. Lichter v. United States, 334 U.S. 742 (1948).
6. 48 Stat. 1064 (1934).
7. For a complete discussion of the cases on delegation, see 1 DAVIS, ADMINISTRATIVE LAW TREATISE ch. 2 (1958) see also Miller, *The Public Interest Undefined*, 10 J. Pub. L. 184 (1961).

There have been other delegations of a similar nature under generous standards. This has led Professor Kenneth Culp Davis to make the statement: "Congress sees the problem, throws the ball to the administrative agencies, says in effect, 'Here is the problem, deal with it as you see fit' "[8]

The point is not that such delegations are either improper or even avoidable. I take it that they are—or seem to be—inescapable in our modern, industrialized economy Rather, the point is that Congress can, and apparently has, turned over complete control of monetary matters to nonlegislative organs. Congress, accordingly, appears to have lost whatever control it may once have had, and theoretically still retains. Thus, under the statute providing for the creation of a Federal Open Market Committee, the "intelligible principle" supposedly required for delegation to administrative agencies seems to have almost vanished. The statute reads:[9]

> (c) The time, character, and volume of all purchases and sales of paper described in sections 353-359 of this title as eligible for open-market operations shall be governed with a view to accommodating commerce and business and with regard to their bearing upon the general credit situation of the country

No doubt a higher degree of specificity delineating the powers of the delegate of congressional power would be difficult to come by in this instance, and still permit flexibility of operation. But this delegation does cede complete power to the Open Market Committee. Even so, my prediction would be that it would be upheld if ever challenged in court; and, parenthetically, I am not sure that it could be challenged in court, as it would be difficult to find a person with the requisite interest to have standing.[10]

As I see it, then, whatever the Constitution may give by way of formal authority over monetary matters to Congress,

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8. Paraphrased from DAVIS, *supra* note 7, at 82.
9. 12 U.S.C. § 263.

the effective control of such matters is a matter of administrative discretion. There are no checks in a legal sense on this power; such checks as do operate would seem to be political in nature.

When I use the word "political," I don't mean this in any invidious sense. I mean it to describe the operation of the American political system. Congress, in short, has abdicated—in this, as well as many other matters of great public importance. Furthermore, delegation to the Open Market Committee, which is partially a "private" organization, in that its membership is partly made up of bankers who are not government employees, is not out of the mainstream of modern constitutional law The agriculture program may be cited, as well as certain "delegations" under military contracts, for support of such a statement.[11] The flow of power toward the Executive, which is considered to be a fact of modern American government, has found a willing ally in Congress. It is not extravagant to say that Congress is slowly bleeding to death—largely from self-inflicted wounds.

3. *In order for the objectives of the Employment Act of* 1946 *to be carried out, it is desirable and necessary that economic policies be unified.*

Under the Employment Act,[12] it became a continuing policy and responsibility of the Federal Government to coordinate and utilize all its plans, functions, and resources for the purpose of creating and maintaining conditions under which there will be afforded useful employment opportunities and to promote maximum employment, production, and purchasing power

10. DAVIS, *supra* note 7, collects the cases on standing to challenge administrative action.

11. See *e.g.*, Miller, *Administration by Contract· A New Concern for the Administrative Lawyer* 36 N.Y.U.L. Rev. 957 (1961), and Lowi, *How the Farmers Get What They Want,* The Reporter, May 21, 1961, p. 34.

12. 60 Stat. 23 (1946). See ROSTOW, PLANNING FOR FREEDOM THE PUBLIC LAW OF AMERICAN CAPITALISM (1959) for a discussion of the operative impact of this statute.

This Act, which is of such basic importance that it takes on the character of a constitutional amendment, is the basic charter under which government affirmatively seeks to improve the American economy, and also the economic well-being of the American people.

I should think that if the objectives of the Employment Act are to be attained, as I believe they should, it is of the highest importance that the policies of all organs of government be consistent with each other; that, in other words, there be a high degree of congruity in economic policy It is my understanding that at present such congruity, if it is reached, is attained through a policy of consultation and coordination; but that, however, there is no legal requirement for the Federal Reserve Board to coordinate its policies with the Treasury Department, or with anyone else.

This violates at least two principles:

(a) In the first place, it makes congruity of policy a matter of accident of personality and of whether or not given governmental officials get along well enough together to cooperate rather than fight. I believe it to be a principle of good government that policy-makers dealing with the same matters be *required* to mesh their policies. Put another way, there may be validity in the constitutional separation of powers, and checks and balances, as between branches of government—but no merit whatever in a similar separation within a functional area of governmental concern and within a given branch of government.

(b) In the second place, the Federal Reserve Board, in all of its operations, seems to be an independent organization, not responsible or accountable to any official, including the President, within the Executive branch, and the oversight of which by the Congress may be more apparent than real. To the extent that the Board operates autonomously, it would seem to run contrary to another principle in our constitutional order—that of the accountability of power

In brief, then, once the Federal Government undertook the affirmative responsibility of maintenance of minimal conditions of economic prosperity within the country, the question of fragmentation of power became acute. In my judgment, it is no longer desirable, if indeed it ever was, for there to be several agencies working at cross purposes within any area of concern. Other techniques must be devised to insure against despotism, or the improper use of power Government must be accountable, in other words, but officials must be enabled to do necessary tasks.

I might add that of course this is not the only area in which a proliferating governmental structure finds agencies and policies working toward inconsistent goals. To mention but one example, even a cursory examination of the contracting policies of the Government will quickly indicate a number of inconsistencies and incongruities in policies and programs.[13]

Furthermore, it must be noted that even if the Federal Reserve Board is put by law within the Executive Branch, that does not mean that the President can or would exercise complete control. Modern studies of decision-making in that branch, such as Neustadt's *Presidential Power*, clearly indicate that the executive departments and agencies have power of great importance, and that the President, contrary to popular opinion, ordinarily cannot flatly order many actions he personally might deem desirable. He still, as Neustadt points out, must negotiate with the leaders of the "feudalities" within the Executive branch. Former President Truman put this in words recently in a quotation which Neustadt has in his book.[14] He says, "I sit here all day trying to persuade people to do the things they ought to have sense enough to do without my persuading them." And that is about all the presidential power amounts to, according to the former President.

4. *The Federal Reserve Board, under present constitu-*

13. Discussed in Miller & Pierson, *Observations on the Consistency of Federal Procurement Policies with Other Governmental Policies*, 29 Law & Contemp. Prob. 277 (1964).
14. NEUSTADT, PRESIDENTIAL POWER 9-10 (1960).

tional law, is not a part of the Executive branch of government.

The Board was described by the Attorney General shortly after its creation as "an independent board or Government establishment."[15] There is no authoritative court decision indicating the constitutional nature of the Board or of the Open Market Committee. What decisions as there are relate to the power of the President to remove a postmaster, an officer of the Federal Trade Commission, an official of the Tennessee Valley Authority, and of the War Claims Commission. We have four recent Supreme Court decisions dealing with the power of the President to remove officials within the Executive branch of government. These are decisions which are of relevance here.[16]

An attempt by the President to remove an appointed member of the Board of Governors prior to the end of the term for which he has been appointed would probably be invalidated by the Supreme Court, unless the Court was willing to overrule, or to distinguish, the *Humphrey* and *Wiener* decisions. Whether it would so rule is a matter of conjecture. Under the terms of section 10 of the Federal Reserve Act of 1913,[17] the President may remove Board members "for cause." The statutory command, however, is unclear as to what "cause" may mean. If the Court follows the *Humphrey* case then it would likely be that the Board members would not be called purely executive officers but rather would be considered to exercise executive power not vested by the Constitution in the President. If that be valid, then it may be appropriate to recall the words of the late Justice Jackson about administrative agencies:[18]

> They have become a veritable fourth branch of Government, which has deranged our three-branch legal

15. 30 OPS. ATT'Y GEN. 308 (1914).

16. The leading cases are Myers v. United States, 272 U.S. 52 (1926), upholding removal of a postmaster; Humphrey's Executor v. United States, 295 U.S. 602 (1935), awarding back pay to estate of invalidly removed Federal Trade Commissioner; Morgan v. Tennessee Valley Authority, 115 F.2d 990 (6th Cir. 1940), *cert. denied*, 312 U.S. 701 (1941) upholding removal of a director of TVA; Wiener v. United States, 357 U.S. 349 (1958), invalidating attempted removal of War Claims Commissioner.

17. 12 U.S.C. § 242.

18. F.T.C. v. Ruberoid Co., 343 U.S. 470, 487-488 (1952).

> theories much as the concept of a fourth dimension unsettles our three dimensional thinking. Courts have differed in assigning a place to these seemingly necessary bodies in our constitutional system. Administrative agencies have been called quasi-legislative, quasi-executive or quasi-judicial, as the occasion required, in order to validate their functions within the separation-of-powers scheme of the Constitution. The mere retreat to the qualifying "quasi" is implicit with confession that all recognized classifications have broken down, and "quasi" is a smooth cover which we draw over our confusion as we might use a counterpane to conceal a disordered bed.

In my judgment, however, it may well be, or certainly could be argued, that the President could constitutionally remove a member of the Board of Governors of the Federal Reserve System, provided he avoided the bald statements which the President used in the *Humphrey* and *Wiener* cases. In the *Wiener* case President Eisenhower said that he regarded it in the national interest "to complete the administration of the War Claims Act of 1948 with personnel of my own selection."[19]

An arguable constitutional case could possibly be made, so far as the law is concerned, for the President to remove a member of the Board of Governors. I do not make any statement about whether this is wise or politically feasible. That is quite another question. I do not think that we have any solid precedent, on the other hand, which necessarily rules out the power of the President in this area.

In sum, then, the Board of Governors of the Federal Reserve System reflects what the President's Committee on Administrative Management said in 1937:[20]

> [The independent agencies] are in reality miniature independent governments set up to deal with the railroad problem, the banking problem, or the radio problem. They constitute a "headless" fourth branch of Government, a haphazard deposit of irresponsible agencies and uncoordinated powers. They do violence to the basic theory of the American Constitution that

19. 357 U.S. at 351 (1958).
20. Quoted in JAFFE, ADMINISTRATIVE LAW CASES AND COMMENTS 96 (1954).

> there should be three major branches of government and only three. The Congress has found no effective way to deal with them, they cannot be controlled by the President, and they are answerable to the courts only in respect to the legality of their actions.

We have come a long way since 1937, when that statement was made, far enough to realize that a rigid tripartite division of governmental power is not necessarily sacred. The doctrine of the separation of powers does not so severely compartmentalize governmental powers as some students of the Constitution have thought. But that statement does, nonetheless, seem to characterize the situation.

5. *The crisis in American institutions.*

In conclusion, in my judgment the United States is undergoing a crisis in the sense that its institutions are being tested, as never before in our history, to determine their adequacy in meeting the pressing needs of the day The challenges to the American system are many and obvious. Pre-eminent is that of the Soviet Union, as a center of power and as a contestant for the loyalties of hundreds of millions of the peoples of the world.

Equally challenging—but in a different way—is the "revolution of rising expectations" of the underprivileged nations of the world. Within the United States itself there are a number of problems which are not being met in any adequate manner Thus, to take only one example, our educational system seems unable to produce enough high quality people for all the professions. The point I want to emphasize is that just because something has existed for some time does not mean that it retains whatever validity it may once have had. Justice Holmes once said that it is odious to have no other reason than history to support a given idea.

There is a need for a re-examination of all government policies, including monetary policies, in the light of the responsibilities undertaken by the Federal Government in the last thirty years. If the economists can show, as I take it they can, that the activities of the Federal Reserve Board and the Open Market Committee have substantial importance

for the American economy,[21] then in my judgment these activities should be brought within the Executive branch proper Without reflecting in the slightest degree on the integrity of Board officials, I do not believe that they should operate independently of the Chief Executive.

It is, of course, true that other segments of the economy are left to similar devices, all at the instance of Congress. I refer here to the several so-called independent regulatory commissions. The same case that can be made for bringing the Federal Reserve Board of Governors and the Open Market Committee within the framework of the Executive branch can also be made for other independent agencies. Power under a constitutional order means accountable, that is, responsible, power

Furthermore, the factual situation in 1964 is markedly different from that existing in 1913 when the Federal Reserve System was established. Fundamentally, this can be reduced to the concept that governmental responsibility has been assumed for the well-being of the economy, a goal for which all organs of government are concerned and which calls for the close meshing of public policies. The "headless fourth branch of government" should be brought within the Executive branch; it should be made responsive to the public interest, broadly conceived; it should, in other words, be given a "head."

I realize that there is a considerable amount of discussion going on about the concept of the public interest, who determines it, how it is determined, and how it is furthered by officials of government, including Congressional officials. The concept of the public interest is, as Justice Frankfurter once said, a tapestry of many threads. As the legislation delegating power to the administrative agencies has developed it, it is really an empty vessel into which the agencies can pour anything they wish. A devotion to the "public interest," which I take it all of us have, in government and out, and including members of the Open Market Committee

21. See *Hearings Before the Subcommittee on Domestic Finance of the House Banking and Currency Committee* ("The Federal Reserve System After Fifty Years"), vol. 1, 88th Cong., 2d Sess. (1964).

as well as any other members of the banking community, does not answer any questions in and of itself. It seems to me we have to go much further in asking difficult questions of what is the content to be given the public interest in a given factual situation, such as the monetary system of this country [22]

It may be said in conclusion that the question of monetary and fiscal policy, as an intergral part of the over-all economic policy of the American government, will be in the forefront of attention for many years. In this process, the decision made in 1913 to establish the Federal Reserve System in its present form will be thoroughly re-examined. Changes may well be in the offing, perhaps not in the next year or two, but possibly within the next decade. What those changes might be cannot be forecast at the present time. It is likely, however, that if changes do occur, they will be in the direction of greater control by the President over the operations of the Board of Governors of the Federal Reserve System.

22. See Miller, *supra* note 7, for a discussion of "the public interest."