RETHINKING THE FEDERAL RESERVE SYSTEM: A MONETARIST PLAN FOR A MORE CONSTITUTIONAL SYSTEM OF CENTRAL BANKING

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INTRODUCTION

This Article examines the evolution of American monetary policy and bank regulation and proposes a monetarist plan for reformulating the constitutional relationship between Congress, the President, and the Federal Reserve System. Under the proposed plan, Congress would replace the Federal Reserve System as the regulator of monetary policy, and the President would assume responsibility for bank regulation. This Article concludes that while the Federal Reserve System has functioned successfully as an independent central bank, the implementation of a monetarist plan, which divides the responsibility of monetary policy and bank regulation between the Congress and the President, would more truly realize the separation of powers principles embodied in the Constitution.

Before discussing the specifics of the monetarist plan, this Article presents some necessary background. Part I of the Article provides a brief history of central banking in the United States and traces the development of the Federal Reserve System. Part II examines the tools that the modern Federal Reserve uses to implement monetary policy and bank regulation. Part III discusses the consistencies between the Monetarists' theory of minimal intervention and the Framers' conception of limited government. It also examines three reasons why it would be politically practical for Congress to be responsible for monetary policy. Part IV discusses the benefits of assigning the President control over bank regulation, including the several checks and balances within the federal executive branch that enable the President to control the banking industry. The conclusion summarizes the major themes of this Article.

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I. A BRIEF HISTORY OF CENTRAL BANKING IN THE UNITED STATES AND THE DEVELOPMENT OF THE MODERN FEDERAL RESERVE

A. The First and Second Banks of the United States

Maybe the Framers of the Constitution never envisioned an American political system in which monetary policy and bank regulation would substantially influence the daily movements of complex financial instruments such as commodity futures, stock options, and index funds. To be sure, the Framers did not seriously ponder political issues regarding bank regulation and monetary policy until nearly a decade after the passage of the Articles of Confederation and almost three years after the ratification of the 1788 Constitution.[1] Nonetheless, when the Framers chartered the First Bank of the United States in 1791, it became apparent that monetary policy and bank regulation would assume an all-important role in the American political system.

Prior to chartering the First Bank of the United States, the Framers saw no need to examine bank regulation and monetary policy in any significant detail. This stance was understandable. During that time, America was merely a fledgling democracy with a small agrarian economy and minimal banking needs.[2] By the late 1700s, however, the nation's financial landscape began to change. Most notably, the number of state-chartered banks began to proliferate well beyond the Framers' expectations.[3] To address this growth, the Framers found it necessary to design a central federal bank that could regulate and stabilize the development of state-chartered banks. However, no provision in the 1788 Constitution specifically authorized the creation of a central bank. As a result, a debate arose among the Framers regarding whether the Constitution permitted the Framers to establish the bank.

As the debate developed, two opposing sides arose. On one side, Secretary of the State Thomas Jefferson, a staunch agrarian, argued against creating the bank, fearing that it would unduly empower industrial proponents to promote a commercial agenda.[4] Jefferson also believed that it would be unconstitutional to

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1. *See* COMM'N ON THE BICENTENNIAL OF THE U.S. CONSTITUTION, THE CONSTITUTION OF THE UNITED STATES 40 (15th ed. 1991). The Articles of Confederation were ratified during the Revolutionary War in 1781 and governed the Colonies until June 21, 1788, when New Hampshire became the ninth state to ratify the U.S. Constitution. *See id.* The traditional view is that the Framers drafted the Constitution to correct defects in the Articles of Confederation related to economic concerns such as trade and commerce. The creation of the First Bank of United States in 1791 was an outgrowth of the economic concerns which inspired the Framers to draft the 1788 Constitution. *See* Maureen B. Callahan, *Cultural Relativism and the Interpretation of Constitutional Texts*, 30 WILLAMETTE L. REV. 609, 619 n.56, 622 (1994).

2. For an excellent historical overview of the banking industry in America, see JONATHAN R. MACEY & GEOFFREY P. MILLER, BANKING LAW AND REGULATION 2-36 (1992).

3. *See id.* at 5.

4. *See* DAVID S. KIDWELL ET AL., FINANCIAL INSTITUTIONS, MARKETS, AND MONEY 59 (5th ed. 1993).

establish the bank because no express provisions in the 1788 Constitution authorized its creation.[5] In Jefferson's mind, the only arguable constitutional authority for creating the bank was the necessary and proper clause contained in Article I, Section 8 of the Constitution.[6] Jefferson feared, however, that relying on the necessary and proper clause to justify creating the bank would initiate a slippery slope toward unlimited congressional power.[7] James Madison shared this concern, maintaining that creating the bank would result in unwarranted federal intrusion.[8]

On the other side of the debate, Alexander Hamilton, who drafted the bill for the bank, insisted that the Constitution's silence regarding the bank did not necessarily mean that creating the bank would be unconstitutional. Rather, in Hamilton's view, because the Constitution granted Congress the express power to tax, borrow, and regulate interstate commerce, the federal government had the authority to establish the bank. In contrast to Jefferson, Hamilton interpreted the necessary and proper clause as authorizing Congress to create any law that was "needful, requisite, incidental, useful, or conducive to" the ends of government.[9] Because a central bank would assist the federal government in conducting its financial affairs, Hamilton saw no problem establishing the bank.[10] In the end, Hamilton's view prevailed, and, on February 17, 1791, Congress approved a twenty-year charter for the First Bank of the United States—America's first central bank.[11]

Despite its controversial beginnings, the First Bank of the United States was a successful endeavor. Primarily, the Bank performed what would today be considered rudimentary tasks, such as financing the national government and offering loans to the general public.[12] During the colonial period, however, the concentration of these functions in one central bank was unprecedented. More significantly, the nationalization of the banking industry presented a grave threat

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5. *See* Stephen J. Friedman & Connie M. Friesen, *A New Paradigm for Financial Regulation: Getting from Here to There*, 43 MD. L. REV. 413, 416-17 (1984).

6. Congress shall have the power, "[t]o make all Laws which shall be necessary and proper for carrying into Execution the foregoing Powers, and all other Powers vested by this Constitution in the Government of the United States, or in any Department or Officer thereof." U.S. CONST. art. I, § 8, cl. 18.

7. *See* EDWARD L. SYMONS & JAMES J. WHITE, BANKING LAW: TEACHING MATERIALS 14 (2d ed. 1984).

8. *See id.*

9. Edward Flaherty, *A Brief History of Banking in the United States*, *in* THE AMERICAN REVOLUTION: AN HTML PROJECT (Department of Humanities Computing, 1997), *available at* http://members.home.net/flaherty15/history.pdf (last visited Mar. 16, 2001).

10. *See id.*

11. *See* ACTS TO CHARTER THE BANK OF THE UNITED STATES FEBRUARY 25; MARCH 2, 1791, § 3 (approved Mar. 2, 1791), *reprinted in* 1 DOCUMENTARY HISTORY OF BANKING AND CURRENCY IN THE UNITED STATES 307 (Herman E. Krooss ed., 1969).

12. *See* C. James Judson & Susan G. Duffy, *State and Local Taxation of Financial Institutions: An Opportunity for Reform*, 39 VAND. L. REV. 1057, 1060 (1986).

to state-chartered banks which, in relative terms, lacked the legal and financial resources to compete with a federal institution. This threat arose primarily because state-chartered banks focused exclusively on local affairs, whereas the First Bank of the United States, with its superior resources, operated across state lines.[13] The First Bank of the United States also enjoyed a limited degree of branching capability.[14] Eventually, the economic impact of the Bank even astounded its creators, who never expected it to have a significant impact on national affairs. Yet to state-chartered banks, who feared its influence, the First Bank of the United States was a behemoth that had to be slain. Soon, the state banks' concerns gained the ear of Congress, which responded by rekindling the original constitutional debate regarding the Bank's creation.[15] Ultimately, Congress acquiesced to the state-chartered banks and voted against rechartering the Bank.[16] As a result, the First Bank of the United States disappeared from existence when its twenty-year charter expired in 1811.[17]

The demise of the First Bank of the United States did not squelch the movement towards central banking. To the contrary, the Bank's success made it clear to both its proponents and critics that a central bank could not only stabilize the banking industry, but could also enhance the government's ability to serve the public. This fact became even more apparent just one year later when, due to the Bank's absence, America struggled to finance the War of 1812.[18] After the war ended, America's financial health further deteriorated as the nation grappled with price inflation resulting from the war.[19] Faced with a financial and political crisis, the American people urged its leaders to create a new institution—one that could fill the void left by the First Bank of the United States. Answering the call, Congress drafted legislation for a second central bank, and on April 10, 1816, the Second Bank of the United States came into existence.[20]

Like its predecessor, the Second Bank of the United States was chartered for a finite period of twenty years.[21] During its early years, however, the Bank was

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13. *See* Stacey Stritzel, *The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994: Progress Toward a New Era in Financial Services Regulation*, 46 SYRACUSE L. REV. 161, 165 (1995).

14. *See id.*

15. *See* Flaherty, *supra* note 9.

16. *See* MACEY & MILLER, *supra* note 2, at 6-8. A secondary argument that Congress advanced against the First Bank of the United States focused on the Bank's encroachment into the area of state sovereignty preserved by the Tenth Amendment. *See id.* Although Congress did not recharter the Bank, it is worthwhile to note that the vote on rechartering the Bank was lost by only one vote in both the House and Senate. *See id.*; BRAY HAMMOND, BANKS AND POLITICS IN AMERICA FROM THE REVOLUTION TO THE CIVIL WAR 222 (1957).

17. *See* MACEY & MILLER, *supra* note 2, at 6.

18. *See* Judson & Duffy, *supra* note 12, at 1060.

19. *See* Flaherty, *supra* note 9.

20. *See id.*

21. *See id.*

grossly mismanaged and did little to cure the nation's woes.[22] Trumpeting this impotence, a group of the Bank's staunchest opponents mounted two new legal challenges against the Bank.[23] In 1819, the Supreme Court repelled the first of these challenges when, in *McCulloch v. Maryland*, the Court voted 9-0 to uphold the constitutionality of the Bank.[24] Writing for the Court in *McCulloch*, Chief Justice Marshall found that both the necessary and proper clause and Congress' power to declare war and raise revenue provided constitutional bases for establishing the Bank.[25] Five years later, in 1824, the Supreme Court repelled a second constitutional challenge against the Bank when, in *Osborn v. Bank of the United States*, the Court once again concluded that the Bank was "an instrument which is 'necessary and proper' for carrying on the fiscal operations of government."[26] The *Osborn* court reaffirmed *McCulloch* in reaching this conclusion.[27]

McCulloch and *Osborn* breathed new life into the Second Bank of the United States, providing the time it desperately needed to solve its managerial problems. This new life, however, was not enough to save the Bank. Merely four years after the *Osborn* decision, the death-knell rung when Andrew Jackson, one of the Bank's fiercest critics, became President of the United States. Once inaugurated, Jackson wasted no time in ensuring the Bank's demise. In 1832, Jackson's efforts to destroy the Bank took full effect when he vetoed a bill to recharter the Bank.[28] Though anticipated, Jackson's action came much earlier than expected, as the twenty-year charter for the Bank was not due to expire until 1836.[29] In the wake of Jackson's veto, Congress presented no other bills to recharter the Bank. Consequently, the Second Bank of the United States ceased operations in 1836.[30] For the next seventy-seven years, America conducted its financial affairs without the benefit of a central bank. Then, on December 23, 1913, that trend changed forever when President Woodrow Wilson signed the Federal Reserve Act into law—the scion of the Second Bank of the United States.[31]

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22. *See* JOHN KENNETH GALBRAITH, MONEY: WHENCE IT CAME, WHERE IT WENT 76-78 (2d ed. 1995).

23. *See* Osborn v. Bank of the United States, 22 U.S. 738 (1824); McCulloch v. Maryland, 17 U.S. 316 (1819).

24. *See McCulloch*, 17 U.S. at 436.

25. *See id.* at 324.

26. *Osborn*, 22 U.S. at 861.

27. *See id.*

28. *See* Flaherty, *supra* note 9.

29. *See id.*

30. *See id.*

31. *See* BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, THE STRUCTURE OF THE FEDERAL RESERVE SYSTEM: THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM (1994), *at* http://www.Federalreserve.gov/pubs/frseries/frseri.htm [hereinafter THE STRUCTURE OF THE FEDERAL RESERVE SYSTEM] (last visited Mar. 16, 2001).

B. The Modern Federal Reserve

Like the legislation that created the Second Bank of the United States, the Federal Reserve Act of 1913 was intended to restore stability to the American banking industry, which had been in a state of disarray since the Banking Panic of 1907.[32] The Federal Reserve Act, however, was more ambitious than either of the charters for the First or Second Bank of the United States.[33] Indeed, its drafters intended this effect by assigning four expansive responsibilities to the new central bank. First, the Bank was "to serve as the lender of last resort during times of [financial] crisis,"[34] similar to the role that the First Bank of the United States potentially would have served during the War of 1812. Second, the Bank was to provide a flexible national currency that would be responsive to changes in supply and demand—a trait that neither of its predecessors possessed.[35] Third, the Bank was assigned the supervisory responsibility over the banking industry, which historically had been disjunctive and fragmented throughout the states.[36] Finally, the Bank was intended to improve the nation's check-clearing system, which likewise had been a poster-child for unpredictability and delay.[37]

To achieve these lofty goals, the Federal Reserve Act established a system of twelve Federal Reserve Banks located in major cities throughout the nation.[38] The Act also established a seven member Federal Reserve Board,[39] headquartered in Washington D.C. In addition to supervising the twelve Federal Reserve Banks, the Board maintained general control over the Federal Reserve System.[40]

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32. *See* THIBAUT DE SAINT PHALLE, THE FEDERAL RESERVE: AN INTENTIONAL MYSTERY 48-49, 54 (1985). The Banking Panic of 1907 was the worst of four national banking crises occurring since 1873. *See* Federal Reserve Bank of Minneapolis, *Born of a Panic: Forming the Federal Reserve System*, THE REGION, Aug. 1988, *at* http://woodrow.mpls.frb.fed.us/pubs/region/reg888a.html (last visited Mar. 16, 2001) [hereinafter *Born of a Panic*]. The Panic arose primarily because the existing banks chose to operate independently, rather than as a collective unit, when cash ran short. *See id.* Had the banks lent funds to one another, instead of hoarding cash, the Panic may not have occurred.

33. *See id.*

34. *Id.*

35. *See id.*

36. *See id.*

37. *See id.* The preamble to the Federal Reserve Act memorializes these aims, stating that the Act was intended "to provide for the establishment of Federal reserve banks, to furnish an elastic currency, to afford a means of rediscounting commercial paper, to establish a more effective supervision of banking in the United States, and for other purposes." Federal Reserve Act, 38 Stat. 351 (1913) (codified as amended in scattered sections of 12 U.S.C.).

38. Currently, the twelve regional Federal Reserve Banks are located in Atlanta, Boston, Chicago, Cleveland, Dallas, Kansas City, Minneapolis, New York, Philadelphia, Richmond, St. Louis, and San Francisco. *See* DE SAINT PHALLE, *supra* note 32, at 4.

39. *See Born of a Panic, supra* note 32. This governing body is now known as the "Board of Governors" of the Federal Reserve System. *See id.*

40. *See* THE STRUCTURE OF THE FEDERAL RESERVE SYSTEM, *supra* note 31.

All nationally chartered banks were required to become members of the Federal Reserve System.[41] State-chartered banks, by contrast, were accorded the option to join.[42] Additionally, "nonmember banks" were not governed by the Federal Reserve Act.[43] Any nonmember bank, however, could avail itself the Federal Reserve's check clearing system, so long as it maintained an appropriate balance with the twelve Federal Reserve Banks.[44]

Unlike most government entities, the Federal Reserve System was not established under the direct control of any branch of the federal government.[45] Nor was the system funded by government appropriations.[46] Instead, each Federal Reserve Bank, or District Bank, was established as a banking corporation and acquired funds from interest earned on government securities and income provided by the banking industry.[47] Each District Bank, like any private corporation, also maintained the power to appoint its own board of directors, officers, and employees.[48] The board of directors, comprised of two local bankers, headed each District Bank.[49] However, by the late 1920s, nine members made up of the board—three of whom were selected from the member banks, another three of whom were selected from the banking industry, and a final three of whom were appointed by the Federal Reserve Board.[50] The board of directors for each District Bank maintained the power to elect one representative to the Federal Advisory Board,[51] which periodically met in Washington D.C.[52]

Analogous to a corporation and its stockholders, the twelve District Banks provided financial services to their member banks.[53] Such services now include holding monetary reserves for the member banks, discounting certain financial notes, drafts, and bills of exchange, and offering monetary advances on certain promissory notes.[54] No agency relationship exists, however, between the Federal

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41. *See id.*

42. *See Born of a Panic*, *supra* note 32.

43. *See* Brookings State Bank v. Fed. Reserve Bank of S.F., 281 F. 222, 225 (D. Or. 1922).

44. *See id.*

45. *See* THE STRUCTURE OF THE FEDERAL RESERVE SYSTEM, *supra* note 31.

46. *See id.*

47. *See id.*

48. *See* DE SAINT PHALLE, *supra* note 32, at 4-5.

49. *See id.*

50. *See* Raichle v. Fed. Reserve Bank of N.Y., 34 F.2d 910, 912 (2d Cir. 1929).

51. Under the Federal Reserve Act, the Federal Advisory Board is empowered to confer directly with the Federal Reserve Board on issues regarding the general condition of business. It is also empowered to call for information and make recommendations regarding discount rates and the general affairs of the Federal Reserve System. *See* Federal Reserve Act of 1913 c. 6. § 12A, 12 U.S.C. § 263(a) (2000).

52. *See id.* § 12, 12 U.S.C. § 261 (1999).

53. *See* THE STRUCTURE OF THE FEDERAL RESERVE SYSTEM, *supra* note 31. Under the Federal Reserve Act, each member bank is a stockholder of the twelve Federal Reserve Banks.

54. *See Raichle*, 34 F.2d at 913.

Reserve Banks and the member banks.[55] Rather, both groups are separate and distinct corporate entities, and neither group has the authority to act on behalf of the other.[56] The District Banks derive their authority solely from the Federal Reserve Act.[57] The Banks have no powers greater than those granted by the Act and certain incidental powers necessary to carry on the business of banking.[58]

In its current form, the Federal Reserve System, through its seven member Board of Governors, functions as the sole implementor of the monetary policy.[59] At its inception, however, the Board of Governors devoted little or no attention to establishing monetary policy.[60] Indeed, during their early years, neither the Board of Governors nor the Federal Reserve District Banks even considered asserting control over the money supply. Instead, both the Board and the Federal Reserve Banks concentrated on performing the basic functions specified in the Federal Reserve Act.[61] Ignorance, to a great extent, spawned this indifference. And, because no express provisions in the Federal Reserve Act authorized the Board of Governors or the District Banks to assert control over monetary policy, the issue never produced any serious debate. In the early 1920s, however, the Board of Governors shed its ambivalence as a result of the incredible foresight of Benjamin Strong—the extraordinary Governor of the New York Federal Reserve Bank.[62]

Governor Strong was the first influential banker to realize that the Federal Reserve System possessed the means to establish monetary policy.[63] To the chagrin of many prominent bankers, Strong understood that by adjusting reserve requirements and buying or selling government securities, the Federal Reserve could actively control the money supply.[64] Initially, Strong implemented his policies exclusively through the New York Federal Reserve Bank.[65] In 1922, however, Strong expanded his operations. That year, both he and other powerful leaders, such as Treasury Secretary Andrew Mellon, joined forces to create a special government commission on monetary policy.[66] Ultimately, Strong's New York activities garnered the attention of the Board of Governors in Washington, D.C., which had accorded little notice to his work. But once aware of Strong's initiative, the Board replaced the special government commission with its own regulatory committee. The new committee, known as the Open Market Investment Committee of the Federal Reserve System, took over most of Strong's

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55. *See* Fed. Reserve Bank of Richmond v. Lakin, 81 F.2d 1003, 1005 (4th Cir. 1936).
56. *See id.*
57. *See* Armano v. Fed. Reserve Bank of Boston, 468 F. Supp. 674, 675-76 (D. Mass 1979).
58. *See id.* at 676.
59. *See* DE SAINT PHALLE, *supra* note 32, at 3.
60. *See id.* at 57.
61. *See id.*
62. *See* MACEY & MILLER, *supra* note 2, at 16.
63. *See* DE SAINT PHALLE, *supra* note 32, at 61.
64. *See id.*
65. *See id.*
66. *See id.* at 62.

operations and formally placed them under the direct supervision of the Board in Washington, D.C.[67] Later, due to Strong's efforts, the Open Market Investment Committee became the evolutionary predecessor to the current Federal Open Market Committee[68]—the most important policy-making body in the Federal Reserve System.

As the Open Market Investment Committee gained importance, the Federal Reserve System entered its adolescent stage. However, it was not until the 1930s that the Federal Reserve System matured completely and assumed its modern form. At that time, Marriner C. Eccles, another extraordinary banker, took the mantle from Strong and spearheaded a new initiative for restructuring the Bank. Foremost, during a 1934 appearance before the Senate Finance Committee, Eccles recommended that the Federal Reserve System be reformed through the codification of the many informal policies for controlling the money supply.[69] Under this proposal, decisions regarding monetary policy would emanate directly from the Board of Governors in Washington, D.C., rather than from the twelve District Banks.[70] To achieve this end, Eccles assigned the Board of Governors the authority to oversee the internal operations of the District Banks. The Board could also override the Banks' policy decisions whenever they conflicted with those of the Board.[71]

Eccles' changes had the practical effect of reducing the status of the twelve District Banks, making each bank subservient to decisions of the Board.[72] Control over the Federal Open Market Committee was also assigned to the Board.[73] Finally, Eccles isolated the Board from political influence by removing the Secretary of the Treasury and Comptroller of the Currency from the Board, both of whom represented the President of the United States.[74] With this change, the Board became insulated from public accountability,[75] as no member of the Board was under the direct control of an elected official. In essence, the Board could formulate any policies it wished, and the President would not be politically accountable.[76] On August 23, 1935, Eccles' plan was formally codified in Title II of the Glass-Steagall Act.[77] At that point, the modern Federal Reserve System

67. *See id.*

68. In its present form, the Federal Open Market Committee consists of the President of the New York Federal Reserve Bank, the seven members of the Board of Governors in Washington, D.C., and four of the presidents of the eleven other district banks. *See* 12 U.S.C. § 261 (2000).

69. *See* DE SAINT PHALLE, *supra* note 32, at 74.

70. *See* WILLIAM GREIDER, SECRETS OF THE TEMPLE: HOW THE FEDERAL RESERVE RUNS THE COUNTRY 312 (1987).

71. *See id.*

72. *See id.* at 312-13.

73. *See id*. at 313. Seven of the twelve votes were from the governors. The remaining votes rotated among the Reserve Bank Presidents. *See id.*

74. *See id.*

75. *See id.*

76. *See id.*

77. *See* Banking Act of 1935, c. 614, § 1, 49 Stat. 685 (codified as amended in scattered

came into existence. In all basic respects, it has remained unchanged since that time.

II. The Policy-Making Tools of the Modern Federal Reserve

As previously discussed, the Federal Reserve Act of 1913 contained no provisions which authorized either the Federal Reserve Board or the twelve Federal Reserve Banks to establish monetary policy.[78] To the contrary, the Act created the Federal Reserve System for the general purpose of reducing the risk of failures in the banking industry. However, as the System matured, both the Federal Reserve Board and the twelve Federal Reserve Banks acquired control over monetary policy through human innovation.[79] Be that as it may, nothing in the original Federal Reserve Act provided the Federal Reserve System with the formidable array of policy-making tools it now possesses to regulate banks and the money supply.

The modern Federal Reserve has many tools at its disposal to assist it in regulating banks and the money supply. For the purposes of policy-making, however, it has only four significant tools:[80] (1) open market operations, (2) the discount rate, (3) reserve requirements, and (4) authority over member banks and bank holding companies.[81]

A. Open Market Operations

Open market operations are the most important policy-making tool of the modern Federal Reserve System.[82] As the name suggests, these operations involve the buying and selling of government securities, such as Treasury bonds and bills,[83] on the "open market." This open market consists of numerous parties, including individuals, banks, and corporations.[84]

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sections of 12 U.S.C.).

78. In this Article, the term "monetary policy" refers to the Federal Reserve's decisions regarding the amount of money it desires to circulate in the economy. *See* Shahriar Tavakol, Comment, *Digital Value Units, Electronic Commerce and International Trade: An Obituary for State Sovereignty over National Markets*, 17 J. MARSHALL J. COMPUTER & INFO. L. 1197, 1206-07 n.94 (1999) (citing N. GREGORY MANKIW, MACROECONOMICS 144 (2d ed. 1994)).

79. *See* MILTON FRIEDMAN, A PROGRAM FOR MONETARY STABILITY 25 (1960). Friedman argues that Federal Reserve's "haphazard assortment of tools reflects mainly historical accident." *Id.* He further asserts that since control over monetary policy did not develop from a prior commitment to history, any proposed reforms for streamlining the Federal Reserve may be implemented without concern about disrupting the operations of the existing system. *See id.*

80. *See id.*

81. See *infra* Part II.D for definitions of member banks and bank holding companies.

82. *See* Fed. Open Mkt. Comm. of the Fed. Reserve Sys. v. Merrill, 443 U.S. 340, 343 (1979).

83. *See* MAXWELL NEWTON, THE FED: INSIDE THE FEDERAL RESERVE, THE SECRET POWER CENTER THAT CONTROLS THE AMERICAN ECONOMY 64 (1983).

84. *See generally* BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, THE FEDERAL

When the Federal Reserve buys government securities on the open market, it purchases them with a Federal Reserve check.[85] When the Federal Reserve issues this check, payment for the securities is ordinarily credited in the reserve account of the seller's bank.[86] Receipt of this payment augments the amount of reserves in the seller's bank with no offsetting decline in reserves elsewhere, thereby increasing the supply of money that is available for lending.[87] When the Federal Reserve sells government securities on the open market, the opposite occurs. In that situation, the securities' purchaser pays the Federal Reserve with a check on his or her bank.[88] When the check clears, the sale price of the securities is debited in the reserve account of the purchaser's bank.[89] Debiting this payment reduces the amount of reserves in the purchaser's bank with no offsetting decline in reserves elsewhere, thereby decreasing the supply of money that is available for lending.[90]

By statute, the Federal Open Market Committee (FOMC) has exclusive authority to conduct open market operations.[91] Because it is the sole governing body with this power, the FOMC possesses complete policy-making control over the money supply. Ordinarily, the amount of reserves available for lending dictates the FOMC's approach toward setting the money supply. For example, if the circumstances indicate that the amount of reserves will require constant adjustment, then the FOMC will directly purchase and sell securities on the open market.[92] In turn, if the amount of reserves requires only a temporary adjustment, then the FOMC may enter into repurchase agreements (when temporary additions are needed) or engage in matched sale-purchase transactions (when temporary reductions are required).[93] In most cases, the amounts of reserves will require only a temporary adjustment.[94] Consequently, when the FOMC implements monetary policy, it typically does so by entering repurchase agreements and engaging match-sale purchase transactions rather than dealing in direct purchases and sales of securities on the open market.[95]

Through open market operations, the Federal Reserve attempts to sustain economic growth and stabilize the money supply.[96] In theory, if the Federal

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RESERVE SYSTEM: PURPOSES & FUNCTIONS 35-41 (8th ed. 1994) [hereinafter THE FEDERAL RESERVE SYSTEM: PURPOSES & FUNCTIONS].

85. *See* NEWTON, *supra* note 83, at 65.

86. *See id.*

87. *See id.*

88. *See id.*

89. *See* Fed. Open Mkt. Comm. of the Fed. Reserve Sys. v. Merrill, 443 U.S. 340, 343 (1979).

90. *See* NEWTON, *supra* note 83, at 65.

91. *See* 12 U.S.C. § 263(b) (2000).

92. *See* THE FEDERAL RESERVE SYSTEM: PURPOSES & FUNCTIONS, *supra* note 84, at 38-39.

93. *See id.*

94. *See id.*

95. *See id.*

96. *See id.*

Reserve were able to accurately predict the movements of the "money multiplier" (i.e., the ratio of the amount of money circulating in the economy to the amount of money on deposit at the Federal Reserve), then the FOMC could use open market operations to control the money supply exactly.[97] In reality, though, the money multiplier is extremely unpredictable.[98] As a result, open market operations cannot be utilized to set the supply of money at any predetermined level for any significant period of time.[99] Despite this shortcoming, the dollar-for-dollar impact of open market operations on bank reserves makes those activities the Federal Reserve's most powerful, flexible, and precise policy-making tool.[100]

B. The Discount Rate

The discount rate is the Federal Reserve's second most powerful policy-making tool. Simply defined, the discount rate is the interest rate that member banks are charged when they borrow funds from the Federal Reserve.[101] Originally, the discount rate was set independently by each Federal Reserve District Bank, depending on the banking and credit conditions in the subject district.[102] Over time, however, the nationalization of the banking industry diminished the practicality of setting the rate on a regional basis.[103] "As a result, the Federal Reserve maintains a uniform structure of discount rates across all Reserve Banks."[104]

All banks must maintain a set level of reserves with the Federal Reserve System.[105] When banks do not have enough funds to meet the prevailing required level of reserves, they must borrow money from the Federal Reserve at the discount rate.[106] Typically, banks will hold more reserves during periods of high discount rates because a high discount rate means that the cost of borrowing money is also high.[107] Holding more reserves means banks have less money available for lending.[108] Hence, by setting a high discount rate, the Federal Reserve can increase the amount of reserves held by banks, and thereby reduce

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97. *See* RUDIGER DORNBUSCH & STANLEY FISCHER, MACROECONOMICS 375-76 (Paul V. Short ed., 4th ed. 1987).

98. *See id.* at 375.

99. *See id.* at 375-76 (citing James M. Johannes & Robert H. Rasche, *Predicting the Money Multiplier*, 5 J. MONETARY ECON. 301 (1979)).

100. *See* THE FEDERAL RESERVE SYSTEM: PURPOSES & FUNCTIONS, *supra* note 84, at 36.

101. *See* DE SAINT PHALLE, *supra* note 32, at 91.

102. *See* THE FEDERAL RESERVE SYSTEM: PURPOSES & FUNCTIONS, *supra* note 84, at 44.

103. *See id.*

104. *Id.*

105. *See id.* at 46.

106. *See* NEWTON, *supra* note 83, at 65.

107. *See generally* DORNBUSCH & FISCHER, *supra* note 97, at 390.

108. *See id.*

the money supply.[109] Conversely, when the discount rate is low, banks will hold less reserves.[110] Maintaining less reserves increases the amount of money available for lending.[111] Thus, by setting a low discount rate, the Federal Reserve decreases the amount of reserves held by banks and increases the money supply.[112]

Historically, the discount rate has not been a reliable policy-making tool. This unreliability stems from the extreme sensitivity of the discount rate to changes in the velocity of money.[113] Due to this sensitivity, the Federal Reserve has been unable to consistently predict the proportional effect of an incremental increase in the discount rate on the money supply. The most likely reason for this unpredictability is that individual banks, not the Federal Reserve, decide the quantum by which they wish to increase (or decrease) the amount of reserves they hold when the Federal Reserve decides to raise (or lower) the discount rate. Perhaps if the Federal Reserve could directly control the reserve decisions of individual banks, the discount rate would be a more powerful policy-making tool.[114]

C. Reserve Requirements

Reserve requirements are the Federal Reserve's third most important policy-making tool. To satisfy reserve requirements, banks must keep a percentage of their deposits on reserve with the Federal Reserve System in specified assets.[115] Prior to 1980, only the member banks of the Federal Reserve were required to satisfy reserve requirements.[116] Today, however, all depository institutions, regardless of their membership status, are subject to the reserve requirements established by the Federal Reserve.[117]

When the Federal Reserve increases reserve requirements, banks must keep a larger sum of deposits on account and, therefore, have less money available for lending. Thus, an increase in reserve requirements results in a decrease in the money supply. In turn, when the Federal Reserve decreases reserve

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109. *See id.*

110. *See id.*

111. *See id.*

112. *See id.*

113. "The . . . *velocity of money* is the number of times the stock of money is turned over per year in financing the annual flow of income." *Id.* at 359. In mathematical terms, the velocity of money is the "ratio of nominal income to nominal money stock." *Id.* at 360.

114. The Federal Reserve adjusts the discount rate when the market reflects a change in the velocity of money. Since the Federal Reserve usually changes its policy in reaction to a change in the velocity of money, the discount rate is said to be a lagging indicator. Because lagging indicators record instead of predict changes in the economy, they are not effective policy-making tools. *See* DE SAINT PHALLE, *supra* note 32, at 92.

115. *See* THE FEDERAL RESERVE SYSTEM: PURPOSES & FUNCTIONS, *supra* note 84, at 53.

116. *See id.*

117. *See id.* at 53-54.

requirements, banks can keep a smaller sum of money available for lending. Hence, a decrease in reserve requirements results in an increase the money supply. By ordering only a small increase (or decrease) in reserve requirements, the Federal Reserve can remove (or inject) an enormous amount of funds into the money supply.[118]

Because the precise quantitative effect of a change in reserve requirements is nearly impossible to predict, the Federal Reserve rarely uses reserve requirements as a policy-making tool.[119] Furthermore, like the discount rate, reserve requirements have not functioned effectively as a policy-making tool. From the Federal Reserve's perspective, a good policy-making tool is one that produces fine, graduated changes in the money supply. Changes in the reserve requirements typically do not have this effect. Rather, such changes more often result in crude, haphazard changes in the money stock. Thus, ordinarily, the Federal Reserve will implement monetary policy by changing reserve requirements only as a measure of last resort.

D. Member Banks and Bank Holding Companies

The power to regulate member banks and bank holding companies represents the Federal Reserve's fourth most important policy-making tool. In simple terms, a member bank is any financial institution that maintains ownership of stock in the Federal Reserve.[120] A bank holding company is any firm that maintains authority over a bank or any other firm that controls a bank.[121]

As noted earlier, all national banks are required to become member banks of the Federal Reserve System.[122] State-chartered banks, however, are not required to join.[123] Through strict regulation, the Federal Reserve can dictate the day-to-day decisions of its member banks, including their policies and procedures. For this reason, the number of member banks in the Federal Reserve System has steadily declined over the last fifty years.[124] Despite this trend, the Federal Reserve continues to strictly regulate its member banks, which significantly impedes its ability to implement effective monetary policy.

Whereas member banks have always been regulated by the Federal Reserve, bank holding companies have only been regulated by the Federal Reserve since 1956. That year, Congress passed the Bank Holding Company Act as a response to the rapidly growing use of bank holding companies as mechanisms for maneuvering around legal limitations on depository institutions.[125] Earlier, Congress attempted to stop the maneuvering by passing the Glass-Steagall Act,

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118. *See* DE SAINT PHALLE, *supra* note 32, at 92.
119. *See id.*
120. *See id.* at 6.
121. *See* MACEY & MILLER, *supra* note 2, at 296.
122. *See* THE STRUCTURE OF THE FEDERAL RESERVE SYSTEM, *supra* note 31.
123. *See id.*
124. *See* DE SAINT PHALLE, *supra* note 32, at 6.
125. *See id.* at 7-8.

which somewhat randomly assigned the responsibility of holding company regulation to the Federal Reserve. However, because the Glass-Steagall Act only accorded the Federal Reserve minimal authority to regulate holding companies, Congress passed the 1956 Act with the intent to expand and formalize the Federal Reserve's regulatory power. In short, the Federal Reserve acquired its regulatory power over bank holding companies because Congress viewed it as the organization most capable of assuming that responsibility.

III. A MONETARIST PLAN FOR CONGRESSIONAL CONTROL OF THE MONEY SUPPLY

A. Monetarist Theory and The Framers' Constitution

Although meticulous and astute, the Framers included no clauses or provisions in the 1788 Constitution that explicitly addressed the issue of monetary policy. Even today, despite the fact that the Federal Reserve has acquired exclusive control over the money supply, the Constitution neither expressly affirms nor denies that it should be the province of the federal government to control monetary policy. Yet, in theory, Congress is the most acceptable "constitutional candidate" for controlling the money supply because Article I of the Constitution specifically enumerates the power to coin and regulate the value of money to the federal legislative branch. Specifically, Article I states: "The Congress shall have Power . . . To coin Money, regulate the Value thereof, and of foreign Coin, and fix the Standards of Weights and Measures . . . ."[126]

From an economist's point of view, it makes perfect sense to interpret this as providing Congress with the constitutional authority to set monetary policy and control the money supply.[127] This is because, by definition, the power to regulate the value of money is the lynchpin of monetary policy. The most profound statement of this maxim resides in the economic theory of monetarism, which asserts that monetary policy is directly influenced by the value of money.[128]

Basic monetarist theory posits that changes in the value of money are proportional to changes in the money supply.[129] The theory also maintains that

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126. U.S. CONST. art. I, § 8, cl. 5.

127. Modern investment theory maintains that the money supply is a critical determinant of the level of interest rates in the economy. By definition, interest rates determine the value of money with the general rule being that the higher (or lower) the interest rate, the more (or less) valuable money becomes. For a complete discussion of the connection between interest rates and monetary policy, see ROBERT A. HAUGEN, MODERN INVESTMENT THEORY 310-31 (2d ed. 1990).

128. *See* DORNBUSCH & FISCHER, *supra* note 97, at 667-73. The authors assert that the basic tenants of monetarism focus on the money supply as being determinative of two things: the rate of change in value of money (inflation), and the growth rate of the national economy. *See id.*

129. Although there are many founders of monetarism, Milton Friedman and Irving Fischer have been, by far, the most influential contributors to this school of thought. Friedman, in

the best way to regulate the value of money is by maintaining a gradual, stable rate of growth in the money supply.[130] As earlier observed, this view of monetary policy comports nicely with the text the Constitution, which lists control over the value of money among the powers specifically enumerated to Congress. Could this consistency between monetarist theory and Article I be merely a coincidence? Maybe so. Can it be ignored? Undoubtedly not. Rather, in the absence of any antithetical, constitutional text, it can only be presumed that the Framers, although untrained in monetarist theory, probably intended to assign Congress the responsibility of managing monetary policy when they enumerated the power to regulate the value of money to the legislative branch.

The Framers' minimalist view towards national government strengthens this presumption. Article I is the only provision in the 1788 Constitution that makes express reference to the power to create money and regulate the money supply. Neither Article II, which deals with the President and the executive branch, nor Article III, which deals with the Supreme Court and the judiciary, contains any express reference to this power. This is not surprising. The Framers designed the Constitution with the intention of creating a strong, but limited, national government.[131] To effect this intention, the Constitution established a centralized government that maintained indefinite authority over individual citizens and vested supremacy in the legislative branch.[132] The Framers did not intend for the national government to micro-manage local economic affairs.

Monetarists share in this belief. In their view, the most effective means of establishing monetary policy is by having the central government play only a minimal role in managing the money supply. In short, both the Framers and Monetarists agree that less government is better government regarding the issue of monetary policy.

B. Congress and the Money Supply

The Framers' view and the Monetarists' notion that limited government constitutes the best means for monetary policy suggests that a central banking system in which the national government plays only a small regulatory role, as opposed to the current regime, would more truly realize the philosophical principles contained in the Constitution. Similarly, apportioning the responsibility of monetary policy to the three branches of government would more truly realize the constitutional principle of separation of powers. Hence, the monetarist plan discussed in this Article seeks to achieve both of these aims by proposing a regulatory scheme that reconciles monetary policy with the

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particular, has asserted that the steady growth of the money supply has a stabilizing influence on the national economy. *See* MILTON FRIEDMAN & WALTER W. HELLER, MONETARY VS. FISCAL POLICY (1969).

130. *See id.*

131. *See, e.g.,* William H. Rehnquist, *Point, Counterpoint: The Evolution of American Political Philosophy*, 34 VAND. L. REV. 249, 249-50 (1981).

132. *See id.* at 252.

Framers' constitutional design.

Currently, none of the three branches of the federal government maintains any direct responsibility for monetary policy. Rather, the Federal Reserve implements monetary policy as an independent central bank. However, from a monetarist point of view, the concept of an independent central bank, such as the modern Federal Reserve, may now be an anachronism in light of technological innovations in economic analysis. In 1913, at the time of the Federal Reserve's creation, most elected politicians had neither the technological capacity nor the intellectual training to perform the complex calculations that underlie monetary policy. Rather, only professional economists, highly trained in mathematics and finance, possessed the ability to perform this task. But even in 1913, even most professional economists, though highly trained in theory, were technologically limited in the types of monetary calculations they could perform.

Today, this paradigm has changed. Now, most elected politicians understand economics and finance much better than their counterparts of the early Twentieth Century. In addition, modern economists are now virtually unfettered, in light of the prevailing technology, in the types of mathematical calculations and financial models they can perform and create. Indeed, the use of computers to perform these tasks is now a common part of most undergraduate curricula. With these capabilities, almost anyone can create the basic financial models that the modern Federal Reserve uses to establish monetary policy.[133] Thus, the capacity to formulate sound monetary policy is no longer unique to the Federal Reserve. Instead, due to technological changes and the current political climate, the responsibility of setting monetary policy can be apportioned among the three branches of government. In light of this fact, it may be the appropriate time to rethink the Federal Reserve System in terms of the philosophical and political principles underlying the Constitution. The first step of this undertaking calls for assigning Congress control over the money supply.

1. The Basic Plan.—The monetarist plan proposed in this Article would require the repeal of the statutory provisions underlying the modern Federal Reserve. At first blush, such a proposal may seem radical. But when placed in a historical context, such a proposal is no more extreme than the unprecedented legislation that created the Federal Reserve. Under the monetarist plan, Congress would enact new legislation that provides the federal government only minimal control over the money supply. This legislation would also require Congress, through its subcommittees, to conduct open market operations and set monetary targets on an annual or semiannual basis. Consistent with the monetarist theory, no other intervention would occur between those times. Thus, true to the philosophical and separation of powers principles underlying the Constitution, power over the "value of money" would reside in the federal legislative branch.

2. Three Benefits of the Plan.—

a. Political accountability.—From a philosophical, economic, and political perspective, there are three reasons why assigning Congress control over

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133. *See* DE SAINT PHALLE, *supra* note 32, at 82-83. Historically, Congress has only taken affirmative action in monetary affairs during emergency situations. *Id.* at 83.

monetary policy would function better than the modern Federal Reserve. First and foremost, such control would reincorporate the principle of political accountability into the creation of monetary policy. In its simplest form, the political accountability principle asserts that elected politicians are more responsible to their constituents than appointed officials because the latter are shielded from political pressure, whereas the former are not.[134] Under the monetarist plan, assigning Congress control over monetary policy would make its members more accountable to the public because Congress is a body of elected officials, whereas the modern Federal Reserve is not.[135]

Congress virtually eliminated political accountability from monetary policy when it created the Federal Reserve. Indeed, as exemplified by the Banking Panic of 1907, the fiscal climate at the time of the Federal Reserve's creation promoted banks' self-interests over collective endeavors.[136] For this reason, the American people harbored a great distrust for financiers and politicians with respect to national concerns such as monetary policy. Consequently, it was thought that only an independent agency—one that is shielded from political pressure—could be trusted to put national concerns first. With this in mind, Congress designed the Federal Reserve to function independently from any branch of the federal government.

Today, the fiscal climate in America is much different than it was at the time of the Federal Reserve's creation. While there is still self-interest, modern innovations such as the Internet have facilitated more collective activity. Technology has also made blatant corruption harder to conceal because information becomes public knowledge as soon it is disclosed. In turn, elected politicians are more aware (and concerned) about public sentiment, making it nearly impossible for unilateral corruption to occur. In this new climate, Congress can be trusted to enact sound monetary policy. Accordingly, by making Congress directly accountable to the electorate for its monetary decisions, the proposed monetarist plan has the benefit of incorporating political accountability into monetary policy.

b. Predictability.—Predictability is the second benefit of assigning Congress control over monetary policy. At it stands, the Federal Reserve releases monetary data on a weekly basis. Depending upon whether the statistics are good or bad, financial markets adjust to incorporate the new information. For example, if weekly statistics lead economic analysts to believe that the Federal Reserve will increase the money supply, then financial markets will adjust

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134. The philosophical principle of political accountability originates with Montesquieu and Rousseau. In general terms, the principle asserts that governmental decisions should not be too far removed from the people and that governmental authority, which is not answerable to the people directly, undermines the basic premises of democracy. *See* BARON DE MONTESQUIEU, THE SPIRIT OF THE LAWS 316-30 (Thomas Nugent trans., Hafner Publ'g Co. 1949) (1751).

135. As it exists today, the Federal Reserve is an independent agency whose members are appointed by the President and confirmed by the Senate. Once appointed and confirmed, the members of the Federal Reserve are not directly accountable to any branch of government.

136. *See generally Born of a Panic*, *supra* note 32.

upward. This is because an increase in the money supply leads to a decrease in interest rates, which in turn represents good news to financial markets.[137] The converse is also true. Thus, as the system exists today, economic analysts cannot predict ex-ante the effect that monetary policy will have on financial markets until the Federal Reserve releases its weekly statistics.

The proposed plan will improve the ability of economic analysts to predict movements in financial markets. By limiting the adjustments in the money supply to only annual or semiannual adjustments, the monetarist plan eliminates the present market adjustments that accompany the weekly release of statistics. Analysts will have ex-ante knowledge of the level on a weekly basis. Under monetarist theory, analysts' inaction will have a stabilizing effect on the money supply—the precise goal of effective monetary policy.[138] Thus, by allowing only annual or semiannual monetary adjustments, the monetarist plan improves the predictability of movements in financial markets.

c. Timing.—Timing is the third benefit of assigning congressional control over the money supply. Under the prevailing system, a considerable period ordinarily elapses after the Federal Reserve conducts an open market purchase (or sale) before such a transaction has the desired effect on the market. In fact, using empirical analysis, Monetarists have shown that the initial effect of an open market transaction is rather small.[139] However, over time, the effect continues to grow and proliferate.[140] Hence, the timing of open market purchases is a critical aspect of establishing effective monetary policy.

Historically, the Federal Reserve has done a poor job in timing its monetary policy.[141] Indeed, most Monetarists assert that poor timing on the part of the Federal Reserve is the overriding reason that its monetary policies have been ineffective in resolving major crises in the American economy.[142] Consequently, the historical record of the Federal Reserve has led Monetarists to believe that many of the crises in American banking could have been quelled had the Federal Reserve better timed adjustments to its policy.

The proposed plan would eliminate those timing errors. This is because if Congress were to establish monetary policy on an annual or semiannual basis, there would be no intermittent disruptions such as those that occur when the Federal Reserve proactively alters the money supply. In short, once the annual or semiannual growth rate is set, it is final, and Congress can make no further adjustments in policy.

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137. *See* DORNBUSCH & FISCHER, *supra* note 97, at 390-98.

138. For a complete explanation of the efficient market hypothesis, see R. A. BREALEY, AN INTRODUCTION TO RISK AND RETURN FROM COMMON STOCKS 3-61 (2d ed. 1984). According to Brealey, the hypothesis states that "[a] market in which prices reflect [all] available information is known as an efficient market." *Id.* at 25.

139. *See* DORNBUSCH & FISCHER, *supra* note 97, at 445.

140. *See id.* at 445-46.

141. *See* FRIEDMAN & HELLER, *supra* note 129, at 25.

142. *See id.* at 22.

IV. A MONETARIST PLAN FOR PRESIDENTIAL CONTROL OF BANK REGULATION

Article II of the Constitution, unlike Article I, does not specifically enumerate any powers to the President and the executive branch. Rather, the Constitution's clearest statement of executive authority resides in Article II, Section 1, which provides: "[t]he executive Power shall be vested in a President of the United States of America."[143]

Traditionally, the courts have interpreted this provision as giving the President the power to "carry out" and enforce the legislation enacted by Congress.[144] As a practical matter, though, it would be impossible to follow a literal reading of Article II, Section 1 because the President alone cannot personally enforce every enactment of Congress. Instead, the President relies upon executive departments and agencies to assist him in enforcing the law. For the purposes of this Article, the most important powers that the President maintains over those departments and agencies are the powers of appointment and removal. Both powers are discussed in the section below.

A. Appointment and Removal Powers

The President has two checks on the authority of executive departments and agencies: (1) the power of appointment, and (2) the power of removal. As it exists today, members of the Federal Reserve Board are appointed by the President and, as such, they are subject to his power of appointment.[145] However, since the Federal Reserve is an independent agency of the federal government, meaning that it is neither purely executive or legislative, the Supreme Court has held that the President does not possess the absolute power to remove the members of the Board.[146] But historically, the President has maintained unlimited authority to remove the leaders of purely executive agencies.[147]

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143. U.S. CONST. art. II, § 1.

144. The Supreme Court's decision in *Youngstown Sheet & Tube Co. v. Sawyer*, 343 U.S. 579 (1952), is the case most often cited for the proposition that the President, as the sovereign of executive power, can only "carry out" laws, not make them. In that case, the Court concluded that President Truman's executive order to seize and operate steel mills was unconstitutional because it clearly undermined the lawmaking authority of Congress. *See id.* at 558-59.

145. The Constitution provides that the President has the power, subject to the advice and consent of the Senate, to appoint all officers of the United States whose appointments are not otherwise provided for by the Constitution. *See* U.S. CONST. art. II, § 2, cl. 2.

146. The Supreme Court's decision in *Humphrey's Executor v. United States,* 295 U.S. 602 (1935), is the case most often cited for the proposition that the President does not have the unlimited power to remove the head officials of independent agencies.

147. Recently, though, the scope of the President's power to remove purely executive officers has become a very controversial legal question. The Supreme Court's decision in *Morrison v. Olson*, 487 U.S. 654 (1988), is the leading case on the issue. In *Morrison*, the Supreme Court held that Congress may limit the President's power to remove executive officers, unless the removal limitations "are of such a nature that they impede the President's ability to perform his constitutional duty." *Id.* at 691.

B. The President and Bank Regulation

As earlier noted, the Federal Reserve possesses the exclusive authority to regulate the activities of its member banks and bank holding companies. It also maintains the independent power to influence the purely executive agencies that regulate banks. However, from a constitutional point of view, direct Presidential control over regulation of banks and bank holding companies is more consistent with the broad, extensive mandate of Article II of the Constitution than it is with the independence currently maintained by the Federal Reserve. Accordingly, the monetarist plan proposed in this Article posits that the President, through a new, purely executive agency known as the Department of Monetary Affairs (DMA), is a better constitutional candidate for regulating banks and other aspects of monetary policy than is the modern Federal Reserve.

Under the monetarist plan, the DMA would possess three structural characteristics: First, the President, with the advice and consent of the Senate (Article II, Section 8), would have the unlimited power both to appoint and remove the Chairman of the DMA. Second, the Chairman of the DMA would serve a four year term that would run concurrently with the President's term of office. The Chairman would also supervise all agencies responsible for bank regulation. Third, the DMA, like the modern Federal Reserve, would have the power to adjust interest rates and reserve requirements.

The purely executive DMA would fit nicely within the Framers' constitutional architecture of a Congress, which has the power to enact legislation, and a President, who has the authority to enforce legislation.[148] Because the functions of the DMA would be purely executive in nature, and thus under the exclusive authority of the President, Congress could not use the power of removal to influence the decisions of the DMA.[149]

In addition, the monetarist plan would enable the President and the Chairman of the DMA to coordinate their policies regarding bank regulation.[150] With the existing system, policy coordination cannot be achieved because the President

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148. *See* THE FEDERALIST NO. 51 (James Madison) (Clinton Rossiter ed., 1961). On the issue of maintaining separate legislative and executive branches of government, Madison states:

> In order to lay a due foundation for that separate and distinct exercise of the different powers of government, which to a certain extent is admitted on all hands to be essential to the preservation of liberty, it is evident that each department should have a will of its own; and consequently should be so constituted that the members of each should have as little agency as possible in the appointment of the members of others.

Id. at 321.

149. The Supreme Court's decision in *Buckley v. Valeo*, 424 U.S. 1 (1976), is the case most often cited for the proposition that Congress has no constitutional right to appoint officers of the United States where the responsibilities fulfilled by those officers are executive in nature.

150. For a detailed discussion about coordination among executive agencies, see STEPHEN G. BREYER & RICHARD B. STEWART, ADMINISTRATIVE LAW AND REGULATORY POLICY 105-08 (3d ed. 1992).

and the Federal Reserve Chairman serve non-concurrent terms of office.[151] Coordination is also hindered because the Federal Reserve is only one of many agencies that regulates the banking industry.[152] In contrast, the monetarist plan establishes concurrent terms of office for the President and the Chairman of the DMA. It also assigns control of all agencies to the executive branch. Hence, the coordination problems germane to the current system will be greatly reduced under the monetarist plan.

Consistent with the Framers' design, the monetarist plan also provides a constitutional check against Congress' monetary enactments by empowering the President to adjust reserve requirements and the discount rate. Like the veto power,[153] Presidential control over discount rates and reserve requirements would enable the President to monitor Congressional enactments because discount rates and reserve requirements, as noted earlier, have the same effect on the money supply as open market operations. With this power, the President could make emergency adjustments to Congress' annual legislation in the event of a financial crisis. The President does not have this power vis-a-vis the modern Federal Reserve. Accordingly, the monetarist plan represents an improvement upon the existing system because it establishes an executive mechanism to check monetary policy.

CONCLUSION

The evolution of monetary policy and bank regulation, like the Constitution, is a product of historical forces—the progeny of many governmental institutions that were given form and substance because of political responses to financial crises. Indeed, just as the anticipated role of Bank of the United States exceeded the opaque vision of its creators, the modern Federal Reserve has transcended the limitations of its original design. Historical accidents, such as the brilliant innovations of Benjamin Strong and Marriner Eccles, contributed greatly to the Federal Reserve's development. Yet, nothing in the Constitution or the Federal Reserve Act gave the Federal Reserve the extensive control over monetary and bank regulation that it exercises today.

The monetarist plan proposed in this Article seeks to reallocate the powers of the Federal Reserve in a manner that is more consistent with the Framers' conception of national government. Although the Framers were without the benefit of monetarist theory, their view of limited national government is strikingly similar to the Monetarists' view of minimal intervention. In particular,

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151. Under the current system, the members of the Federal Reserve Board serve terms of fourteen years. *See Born of a Panic*, *supra* note 32.

152. There are seven agencies in the United States that have some control over bank regulation: The Federal Reserve, Comptroller of the Currency, Federal Deposit Insurance Corporation, The Federal Home Loan Bank System, The Federal Savings and Loan Insurance Corporation, The National Credit Union Administration, and The National Credit Union Share Insurance Fund. *See* DE SAINT PHALLE, *supra* note 32, at 15.

153. *See* U.S. CONST. art. I, § 7, cl. 2.

both the Framers and Monetarists agree that the best way to secure stable economic growth is by keeping government regulation to a bare minimum.

In addition, while the Framers never anticipated the need for centralized control of monetary policy and bank regulation, it is the responsibility of lawmakers to preserve the Framers' intention that constitutional power reside securely within three branches of government. The monetarist plan proposed in this Article restructures monetary policy and bank regulation to fit the Framers' architecture by relying upon the philosophical and political principles calling for separate governmental branches. In so doing, it embraces the advent of the new financial and technological innovations that have accompanied the change in times.