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Floor Situation | Summary | Background | Cost | Staff Contact

H.R. 3189, Fed Oversight Reform and Modernization (FORM) Act of 2015

FLOOR SITUATION

On Wednesday, November 18, 2015, the House will begin consideration of H.R. 3189, the Fed Oversight Reform and Modernization (FORM) Act of 2015, under a structured rule. H.R. 3189 was introduced on July 23, 2015, by Rep. Bill Huizenga (R-MI) and was referred to the Committee on Financial Services, and in addition, to the Committee on Oversight and Government Reform. The Financial Services Committee ordered the bill reported by a vote of 33 to 25 on July 29, 2015. The Rules Committee print combines the text of H.R. 3189 and H.R. 2912, the Centennial Monetary Commission Act of 2015, as ordered reported by the Committee on Financial Services.

SUMMARY

H.R. 3189 makes a variety of changes to the Federal Reserve (Fed) system in an effort to increase transparency regarding Fed monetary policy decision making, systemically important financial institutions (SIFI) stress testing, and emergency lending, among other reforms. Major provisions of the bill include:

Monetary Policy Rule – The bill requires the Fed to generate a monetary policy rule to provide added transparency about the factors leading to future rate recommendations. A monetary policy rule is an equation that empirically shows why the Fed recommends a particular monetary policy course and allows the public to predict how the Fed will change course in the future depending on changes in the economy. The bill also requires the Fed to use cost-benefit analysis when promulgating all regulations.[1]Note: The section legislates how the Fed *communicates* monetary policy to make it more transparent, but this section *does not legislate* any particular monetary policy course and therefore does not threaten the Fed's independence in setting monetary policy.

Fed Audit—The bill requires the Government Accountability Office (GAO) to conduct an audit within 12 months of the date of enactment and to report to Congress within 90 days of completion of the

[1] See House Report 114-332 Part 1 at 20.

audit. The audit must include a detailed description of the findings of the audit with GAO's recommendations for legislative and administrative action.[2] Additionally, if the Fed's submission does not meet the bill's requirements for a valid monetary policy rule, the bill allows the House Financial Services Committee or the Senate Banking Committee to instruct the GAO to conduct a one-time audit of the Fed's conduct of monetary policy along certain parameters specified by the requesting committee.[3]

Federal Open Market Committee (FOMC) "Blackout Period"—The bill specifies that the blackout period associated with meetings of the FOMC --a Federal Reserve policy that prohibits Fed Governors and officials from speaking in public on any matter during the week prior to an FOMC meeting and immediately following an FOMC meeting--begins immediately after midnight on the day that is one week before the meeting and ends at midnight on the day after the meeting takes place.[4]

Reforms to the Federal Open Market Committee (FOMC)—The bill reforms the FOMC voting membership to increase the number of District Bank Presidents on the FOMC. Currently, the FOMC consists of twelve members--the seven members of the Board of Governors of the Federal Reserve System; the president of the Federal Reserve Bank of New York; and four of the remaining eleven Reserve Bank presidents, who serve one-year terms on a rotating basis.[5] Under the bill, voting members consist of the seven members of the Fed's Board of Governors and six of the twelve Fed District Bank Presidents on a rotating basis. Thus, each District Bank president would be a voting member of the FOMC every other year. The bill also amends the Federal Reserve Act to specify that the FOMC, not the Fed Board of Governors, shall be responsible for setting the rate of interest paid on excess reserves held by or on behalf of depository institutions at Reserve Banks.

Stress Tests—The bill requires the Fed to issue regulations to govern how it conducts stress tests for systemically important financial institutions (SIFIs) and increases transparency surrounding this process. Under the Dodd-Frank Act, these SIFIs, which are comprised of certain large bank holding companies, state member banks, savings and loan holding companies, and designated nonbank financial companies, are required to undergo regular stress testing conducted by the Fed in an attempt to ensure sufficient capital during cyclical economic cycles.[6]

Emergency Lending Powers—The bill amends the Federal Reserve Act to allow the Fed to invoke its emergency lending powers only upon a finding that "unusual and exigent circumstances exist that pose a threat to the financial stability of the United States." This creates a more stringent standard for the Fed to use its emergency lending authorities. It also requires that nine of the 12 District Fed Bank Presidents must also vote to approve such an action in addition to the current requirement that five of seven Fed Board Governors approve such an action.[7]

Establishment of the Centennial Monetary Commission—The bill establishes the Centennial Monetary Commission to study monetary policy and requires the Commission to recommend to Congress changes to the Fed.[8]

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[2] Id. at 23.
[3] Id. at 15.
[4] Id. at 18.
[5] See Federal Reserve website, Federal Open Market Committee
[6] See House Report 114-332 Part 1 at 19.
[7] See House Report 114-332 Part 1 at 22.
[8] See House Report 114-331 at 2.

Other Miscellaneous Fed Reforms—The bill also makes a variety of other changes to the Fed, including: increasing the number of times the Fed Chair must testify before Congress from semi-annually to quarterly, increasing reporting requirements relating to proposed and anticipated rulemakings, increasing transparency regarding senior-level official's compensation, increasing transparency regarding rule-making that relates to international regulatory negotiations, and requiring the Fed to analyze and report on the economic impacts of the Export-Import Bank.

BACKGROUND

The Federal Reserve Act of 1913 created the Federal Reserve as the nation's central bank (commonly referred to as the "Fed") to serve as an independent agency of the Federal government to govern U.S. monetary policy.[9] The Congress established maximum employment and stable prices as the key macroeconomic objectives for the Federal Reserve in its conduct of monetary policy.[10]

"The Federal Reserve does not receive funding through the congressional budgetary process. The Fed's income comes primarily from the interest on government securities that it has acquired through open market operations. […] After paying its expenses, the Federal Reserve turns the rest of its earnings over to the U.S. Treasury."[11]

The Fed is composed of 12 regional Federal Reserve banks overseen by a Board of Governors. Governors are appointed by the President and confirmed by the Senate and serve staggered 14-year terms. U.S. monetary policy decisions are made by the Federal Open Market Committee (FOMC), which is comprised of seven governors, the president of the New York Fed, and four other regional bank presidents.[12]

The Fed's responsibilities fall into four main categories: monetary policy, the lender of last resort, prudential supervision of SIFIs and other financial firms, and provision and oversight of payment systems.[13]

"The Fed's primary monetary policy instrument is the federal funds rate (the overnight bank lending rate). The Fed influences interest rates to affect interest-sensitive spending on capital investment, consumer durables, and housing. Interest rates also indirectly influence the value of the dollar and therefore spending on exports and imports. The Fed reduces rates to stimulate economic activity and raises rates to slow activity. Monetary policy is considered a blunt instrument that cannot be targeted to affect specific regions, certain industries, or the income distribution.[14]

"The Fed traditionally acts as lender of last resort by making short-term, collateralized loans to banks at its discount window. The Fed generally sets the discount rate charged for these loans above market rates. In the recent financial crisis, it created a series of temporary emergency facilities to provide broader assistance to the financial system. In normal market conditions, the Fed's lending operations are minimal. In a liquidity crunch, it is also able to flood the market with liquidity through open market operations."[15]

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[9] See CRS Report, "Introduction to Financial Services: The Federal Reserve," June 9, 2015.
[10] See Federal Reserve Website, What does it mean that the Federal Reserve is "independent within the government"?
[11] Id.
[12] See CRS Report, "Introduction to Financial Services: The Federal Reserve," June 9, 2015.
[13] Id.
[14] Id.
[15] Id.

Rules-Based Monetary Policy—The Fed has broad discretion to set policy as it sees fit to meet its mandate. Some have called for monetary policy to instead be benchmarked against a Taylor rule (a mathematical formula to determine certain interest rates) to promote transparency and reduce discretion. Critics believe that the interaction between policy and the economy is too complex to be reduced to a concise formula, and discretion is necessary to respond to unforeseen circumstances.[16]

According to the bill sponsor, "With the Federal Reserve having more power and responsibility than ever before, it is imperative the Fed changes its opaque structure and becomes more transparent and accountable to the American people. The Fed's recent high degree of discretion and its lack of transparency in how it conducts monetary policy demonstrate that not only are reforms needed, but more importantly that reforms are necessary. We need to modernize the Federal Reserve and bring it into the 21st Century."[17]

COST

The Congressional Budget Office (CBO) estimates enacting H.R. 3189, as ordered reported by the Financial Services Committee (without the text of H.R. 2912) would reduce revenues by $109 million over the 2016-2025 period. CBO also estimates that the bill would result in an insignificant increase in direct spending. Because the bill affects revenues and direct spending, pay-as you-go procedures apply. Further, CBO estimates that the bill would increase discretionary spending by $7 million over the 2016-2020 period, assuming appropriation of the necessary amounts.

AMENDMENTS

1. Rep. Denny Heck (D-WA)—The amendment suspends the requirement for rules-based decision making when unemployment or inflation significantly diverges from targets.

2. Rep. Denny Heck (D-WA)— The amendment requires FOMC to use fully revised data rather than the initial readings that are first available.

3. Rep. Alan Grayson (D-FL)—The amendment provides for an annual audit of the Federal Reserve.

4. Rep. Steve King (R-IA)—The amendment requires study of the effects of the GDP output section of the "dual mandate" on the US economy, Fed Actions, and federal debt.

5. Rep. Alan Grayson (D-FL)—The amendment establishes three new Federal Reserve districts: one for Northern California (located in San Francisco); one for Southern California (located in Los Angeles); and one for Florida (located in Orlando).

6. Rep. Steve King (R-IA)—The amendment requires the FOMC to make public the full transcriptions of their meetings.

[16] Id.
[17] See Rep. Bill Huizenga Press Release, "Huizenga Fed Reform Legislation Passes Committee," July 30, 2015.

STAFF CONTACT

For questions or further information please contact John Huston with the House Republican Policy Committee by email or at 6-5539.