On my first day on the job as president of the Federal Reserve Bank of Kansas City, Oct. 1, 1991, I was a participant at the Federal Reserve’s Federal Open Market Committee (FOMC) meeting, and that following January, I was a voting member. As prescribed by a rotating schedule of votes, I have voted every three years since then. In 2010, in an environment of unprecedented challenges, I will again be a voting member.

The Federal Reserve has three mission areas, each focused on financial stability—financial services, banking supervision and regulation, and monetary policy. Though the Federal Reserve’s broad role in monetary policy is well-known to the public, the regional Reserve Banks’ role in monetary policy is less well-known or understood.

In some way this lack of understanding is not surprising as it contrasts with the Reserve Banks’ local business activities. For example, the connection between our regional Bank providing local financial services to commercial banks—including the processing of currency, providing transactions accounts and supporting interbank payments—seems natural. Similarly the value of the regional structure in our regulation and supervision of nearly a thousand banks and bank holding companies located within the Tenth Federal Reserve District is pretty basic.

But where the regional structure plays its most important role is in the formation of a national monetary policy that is based on local input. In various forums, including public speeches and in past editions of TEN magazine, I have discussed at length the important reasons behind the Federal Reserve’s innovative regional structure that links the central bank’s national policy deliberations directly to the local communities we serve. This connection is crucial in preventing the Federal Reserve from becoming an “inside the beltway,” Washington-based entity. In fact, the key reason for its design by Congress nearly a century ago was the recognition that an institution viewed as under the control of Washington or Wall Street was not a central bank the public would trust to best serve the interests of the entire nation—as evidenced by two previous failed attempts to run a central bank from the then-power center of Philadelphia. The structure of the Federal Reserve System is truly a product of the populist movement. Although the world has changed much in the last 100 years, many argue this broad representation from across our nation is even more important today than it was at the time of the Federal Reserve’s founding.

History

The FOMC is responsible for the Federal Reserve’s open market operations, which is the most often used of the Federal Reserve’s monetary policy tools. The FOMC’s decisions about its target for the federal funds rate, which is the interest rate that depository institutions lend their balances at the Federal Reserve to other depository institutions overnight, are closely followed because of the impact they have on the broader economy. Moves in the federal funds rate eventually influence borrowing costs.
for everything from credit cards to mortgages, which means they can either stimulate or slow the economy.

The structure of the FOMC was created by the Banking Act of 1935, largely through the work of then-Sen. Carter Glass. Although many individuals were involved in 1913’s passage of the Federal Reserve Act—including Oklahoma Sen. Robert Owen—perhaps no individual is as readily identified with the nation’s central bank as Glass. As a congressman, Glass was not only the House sponsor of the legislation that created the Federal Reserve, but also a key figure in its design. Later, in the mid-1930s as the nation was emerging from the Great Depression, Glass played the key role in making sure that the Federal Reserve’s regional structure—its key strength—was utilized on what some consider its most important committee. In that battle, he faced some strong opposition from an unlikely source—one that was within the Federal Reserve.

Then-Federal Reserve Chairman Mariner Eccles wanted to consolidate control of the decentralized bank under his direct authority in Washington. Eccles saw the financial crisis as an opportunity. In his landmark history of the Federal Reserve, historian and economist Allan Meltzer writes that “Eccles wanted a central bank with authority concentrated in Washington, specifically in his hands.”

Glass, meanwhile, argued that centralized control was an affront to the System, designed and approved by Congress and signed by President Woodrow Wilson. Glass, it seems clear, recognized the extreme risks of such a consolidation. World history has shown time and again that monetary policy, when it is linked too closely to the political process, becomes an extremely seductive tool for elected office holders. The lure of creating an artificial economic boom for a short-term boost in the polls is powerful and often overwhelms concerns about long-term economic consequences.

The battle between Glass and Eccles came to something of a head when Eccles testified before Glass’ Senate Committee. Glass and Michigan Sen. James Couzens both asked Eccles repeatedly how the centralization he favored would have helped the nation when the stock market collapsed and the Great Depression began to take shape. Eccles was unable to come up with a response to the question and later wrote a letter admitting that the powers would not have made a difference in 1929.

In addition to making sure the regional banks had a voice in open market operations, Glass also made sure that the individuals who provided that voice—the regional Reserve Bank presidents—were free of Washington influence. At Glass’ direction, the 1935 Act includes language that says the regional Federal Reserve Bank Boards of Directors, who come from local communities within each District, appoint presidents and other officers of their respective Federal Reserve Banks.

**Structure**

By design, there are 12 members who vote at each FOMC meeting; they include all seven members of the Federal Reserve’s Board of Governors as well as presidents from four of the 11 regional Federal Reserve Banks on a rotating basis. The New York Federal Reserve president was designated as a permanent voting member of the FOMC on the premise that it has a special role in the markets. This structure
carefully balances public and private interests by giving a majority of the 12 votes to the seven Federal Reserve governors, who are presidential appointees who have been confirmed by the Senate. In recent history, however, that has not been the case. Due to a lack of presidential appointments, there has not been an FOMC meeting involving seven governors for almost five years, and for much of the time since spring 2005, the Board of Governors, which also has broad oversight for the entire Federal Reserve System, has had two vacancies.

The intent of the lengthy terms of the governors (14 years for members and four years for the chairman and vice chairman) and the independent status of Reserve Bank boards and presidents provides the System with a needed degree of independence to resist pressure for short-run decisions based on Washington’s two-, four-, and six-year election cycles. The central bank must be free to make decisions that it judges to be in the long-run best interest of the national economy.

Media coverage of the regional Reserve Bank presidents often notes if they are a “voter” or “non-voter” on the FOMC. In terms of policy deliberations, the distinction between the two is perhaps less substantial than some might assume.

All Federal Reserve Bank presidents participate in all FOMC meetings. Both voters and non-voters provide the committee with information about business activity within their regions. During the first of two go-rounds that are the key elements of each FOMC meeting, the presidents each provide
the full committee with a brief but important report on local economic conditions. These reports are based on firsthand accounts that the regional Reserve Banks receive from business and banking contacts within their Districts. Through their comments, the presidents weave an insightful tapestry of the U.S. economy for the FOMC. It is a picture that is more current than even the most recently available data, which can be weeks or even months old. Because this is firsthand information, rather than being backward looking, it is focused on immediate conditions and future concerns. Often, these accounts are the first indications of changing economic conditions or emerging issues. It is perhaps impossible to overstate the valuable role this insight can have in our policy deliberations.

The regional Bank presidents, of course, offer much more to the monetary policy process than reports about their Districts. All members, regardless of voting status, analyze national trends and offer comments on the national and international outlook. They ask questions of other Reserve Bank presidents and the governors. And during a second go-round, each president discusses the possible policy action and has ample opportunity to offer his or her insights and opinions regarding policy to the full committee prior to the vote. All participants play a vital role in the process.

There are some who believe very strongly that the Federal Reserve must always present a united front in terms of policy action or risk weakening its stature. I strongly disagree with that position, and the structure supports my position.

If there was no room for dissention, then why would the FOMC vote on policy actions? If the goal was to keep differences in opinion a private matter, why would the outcome of those votes be made available to the public? The Federal Reserve’s founders, as well as those members of Congress involved in forming the FOMC during the crisis of the 1930s, recognized that an institution with room for dissent and a willingness to entertain contrasting opinions is stronger overall and more worthy of public trust. Although these disagreements or dissenting votes may be portrayed by Federal Reserve watchers as signs of weakness or a struggling central bank, to me they are a mark of strength and evidence that the system is functioning exactly as it was designed.

Voting

Having said all this, I do not want to downplay the significance of being a voting member. It is, in fact, among the key responsibilities of a regional Federal Reserve Bank president and it is certainly one of the most important components of our System.

For more information, read:
• “Presidents, Governors & the FOMC: Regional Bank Leaders Provide Long-term Stability”
• “Twelve Banks: The Strength of the Federal Reserve”
• “The Federal Open Market Committee”
• “The Balance of Power: The Political Fight for an Independent Central Bank”

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