

INDEPENDENCE FROM CREDIT POLICY ACT OF 2017

JANUARY 2, 2019.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. HENSARLING, from the Committee on Financial Services,
submitted the following

R E P O R T

together with

MINORITY VIEWS

[To accompany H.R. 4278]

The Committee on Financial Services, to whom was referred the bill (H.R. 4278) to ensure that the operations of the Board of Governors of the Federal Reserve System remain independent from the credit policy of the United States, and for other purposes, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

The amendment is as follows:

Strike all after the enacting clause and insert the following:

SECTION 1. SHORT TITLE.

This Act may be cited as the “Independence from Credit Policy Act of 2017”.

SEC. 2. INDEPENDENCE FROM CREDIT POLICY.

(a) RETURNING TO A MONETARY POLICY BALANCE SHEET.—

(1) IN GENERAL.—Not later than 1 year after the date of the enactment of this Act—

(A) the Board of Governors of the Federal Reserve System shall transfer to the Department of the Treasury all covered assets that are neither gold stock, Treasury currency, nor direct obligations of the United States, foreign central banks, or the International Monetary Fund; and

(B) the Secretary of the Treasury shall transfer to the Federal reserve banks direct obligations of the United States of equivalent market value to such covered assets.

(2) COVERED ASSETS DEFINED.—In this subsection, the term “covered assets” means all assets—

(A) purchased through open-market operations by the Federal reserve banks; or

(B) acquired through transactions under the following sections of the Federal Reserve Act (12 U.S.C. 221 et seq.):

(i) Section 10A before the date of the enactment of this Act.

- (ii) Section 10B.
- (iii) Section 13.
- (iv) Section 13A.
- (v) Section 24.

(b) OPEN MARKET ASSET PURCHASES.—Section 14(b) (12 U.S.C. 355) of the Federal Reserve Act (relating to “Purchase and sale of obligations of United States, States, counties, etc.”) is amended to read as follows:

“(b) To buy and sell in the open market, at home or abroad, under the direction and regulations of the Federal Open Market Committee, gold stock, Treasury currency, or direct obligations of the United States, foreign central banks, or the International Monetary Fund. Nothing in this subsection shall be construed to limit advances under section 10B, or discount loans under sections 13, 13A, or 24.”.

(c) MAINTAINING A MONETARY POLICY BALANCE SHEET.—

(1) ASSETS ACQUIRED UNDER EMERGENCY LENDING.—Section 13(3) of the Federal Reserve Act (12 U.S.C. 343(3)) is amended by inserting after subparagraph

(E) the following new subparagraph:

“(F) Not later than 1 year after a Federal reserve bank acquires any assets under this paragraph that are neither gold nor direct obligations of the United States, foreign central banks, or the International Monetary Fund—

“(i) the Board shall transfer such assets of the Federal reserve bank to the Department of the Treasury; and

“(ii) the Secretary of the Treasury shall transfer to the Federal reserve banks direct obligations of the United States of equivalent market value to the assets described in clause (i).”.

(2) REPEAL OF AUTHORITY TO PROVIDE EMERGENCY ADVANCES TO GROUPS OF MEMBER BANKS.—Section 10A of the Federal Reserve Act (12 U.S.C. 347a) is repealed.

(3) ASSETS ACQUIRED THROUGH ADVANCES TO MEMBER BANKS.—The second undesignated paragraph of subsection (a) of section 10B of the Federal Reserve Act (12 U.S.C. 347b(a)) is amended—

(A) by inserting “not” before “secured by mortgage loans”; and

(B) by striking “lowest discount rate” and inserting “highest discount rate”.

PURPOSE AND SUMMARY

On November 7, 2017, Representative French Hill introduced H.R. 4278, the “Independence from Credit Policy Act of 2017”, which amends the Federal Reserve Act to provide for the Federal Reserve and the Department of the Treasury (“Treasury”) to engage in asset swaps, whereby the Treasury receives assets from the Federal Reserve that are neither gold nor Treasury securities, nor direct obligations of foreign central banks, or the International Monetary Fund, and in return the Federal Reserve receives Treasury securities of equivalent market value.

BACKGROUND AND NEED FOR LEGISLATION

The goal of H.R. 4278 is to increase monetary policy independence and decrease credit market distortions by maintaining the Federal Reserve’s role as a fiscal agent for our government without exploiting this agency to engage in off-budget credit policy.

An efficient monetary policy helps goods and services, which include labor, readily find their most promising opportunities. To be sure, realizing this ideal is hard, even under favorable conditions. It becomes harder still when central banks step beyond their fundamental economic role and into the political realm of favoring some credit prices over others (as the Federal Reserve has done, for example, by purchasing almost \$2 trillion of Mortgage Backed Securities (MBS) during and after the Financial Crisis).¹

¹ As of October 26, 2017, the Federal reserve banks own almost \$1.8 trillion of Federal agency debt securities and Mortgage-backed securities. Source: <https://www.federalreserve.gov/releases/h41/current/h41.htm>.

When fiscal policies grow at unsustainable rates, governments increasingly become prone to breaching the independence of their monetary authorities. Unfortunately, instead of fortifying themselves against such political risks, central banks have also stepped beyond their narrow remit without government prodding. In either case, the consequences are debilitating—asset price signals lose their ability to clearly communicate information about where goods and services can find their most promising economic opportunities, and are instead exploited to divert goods and services toward their most politically convenient uses.

The United States economic recovery has now entered its ninth year. Despite this persistence, economic opportunities continue to fall far short of potential. The important question is why this recovery failed households and businesses that continue to fall short of their pre-recession promise.

A frequent answer comes from highly regarded but otherwise diverse economists. They highlight the role of monetary policies that have morphed into credit policies. For example, testifying before the House Financial Services Subcommittee on Monetary Policy and Trade, MIT Professor Simon Johnson called attention to this debilitating consequence of a politicized monetary policy:²

I would emphasize, though, and I think we're all agreeing on this that fiscal policy infrastructure is the responsibility of the fiscal authority, which is that Congress in the United States, acting through the executive branch—it is not the responsibility, and should not become the responsibility of the Federal Reserve.

Bradeis Professor Steven Cecchetti shared the same concern as a minority witness for a joint hearing with the Financial Institutions and Monetary Policy and Trade Subcommittee:³

Many people, including me, are uncomfortable with the fact that the Federal Reserve owns so many mortgages.

In addition, the New York Times' Paul Krugman highlighted how the Fed's unconventional balance sheet blurs the lines between monetary and fiscal policies.⁴ And also responding to such concerns, Federal Reserve Board Chair Janet Yellen committed the FOMC during her semi-annual testimony before Congress to reestablish a brighter line between monetary and credit policy:⁵

Well, the FOMC, in its principles for normalization of monetary policy, has clearly indicated that it intends to return, over time, to a primarily treasury-only portfolio, and that's in order not to influence the allocation of credit in the economy.

²See the MPT Subcommittee hearing entitled "Unconventional monetary policy," December 7, 2016. Archived webcast available at <https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=401201>.

³See the MPT-FI Joint hearing entitled "Examining the Relationship Between Prudential Regulation and Monetary Policy at the Federal Reserve," September 12, 2017. Archived webcast available at <https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=402279>.

⁴Paul Krugman, "Fiscal aspects of quantitative easing," *New York Times*, March 20, 2009.

⁵Full-Committee hearing entitled "Monetary Policy and the State of the Economy," July 12, 2017. Archived webcast available at <https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=402098>.

Finally, recent research from the Federal Reserve Board provides empirical support for this bi-partisan concern.⁶ According to the report's authors, both the first and third round of unconventional monetary policies (that is, QE1 and QE3) caused commercial banks to both lower their lending standards and take on more risk. Moreover, these perverse effects grew stronger as banks became more heavily invested in MBS.

Coupled with common concerns from otherwise diverse economic viewpoints, this research highlights how the Independence from Credit Policy Act can provide for a more stable financial system and a more productive allocation of credit. H.R. 4278 provides for an orderly return of the Federal Reserve's balance sheet to, as Chair Yellen described, "a primarily treasury-only portfolio." In addition, it maintains the Federal Reserve's ability to act as our government's fiscal agent during financial emergencies—that is, the Federal Reserve can continue its role as an originator of emergency loans, but must swap out unconventional assets acquired through such lending facilities in return for Treasury securities of equal value.

HEARINGS

The Subcommittee on Monetary Policy and Trade held a hearing titled "Examining Federal Reserve Reform Proposals" to examine matters relating to H.R. 4278 on November 7, 2017.

COMMITTEE CONSIDERATION

The Committee on Financial Services met in open session on November 14 and 15, 2017, and ordered H.R. 4278 to be reported favorably to the House without amendment by a recorded vote of 33 yeas to 26 nays (Record vote no. FC-99), a quorum being present.

COMMITTEE VOTES

Clause 3(b) of rule XIII of the Rules of the House of Representatives requires the Committee to list the record votes on the motion to report legislation and amendments thereto. The sole recorded vote was on a motion by Chairman Hensarling to report the bill favorably to the House without amendment. The motion was agreed to by a recorded vote of 33 yeas to 26 nays (Record vote no. FC-99), a quorum being present.

⁶Robert Kurtzman, Stephen Luck, and Tom Zimmermann, "Did QE lead banks to relax their lending standards? Evidence from the Federal Reserve's LSAPs," Finance and Economics Discussion Series 2017-093, Board of Governors of the Federal Reserve System, <https://doi.org/10.17016/FEDS.2017.093>.

Record vote no. FC-99

Representative	Yea	Nay	Present	Representative	Yea	Nay	Present
Mr. Hensarling	X			Ms. Maxine Waters (CA)		X	
Mr. McHenry				Mrs. Carolyn B. Maloney (NY)		X	
Mr. King	X			Ms. Velázquez		X	
Mr. Royce (CA)	X			Mr. Sherman		X	
Mr. Lucas	X			Mr. Meeks		X	
Mr. Pearce	X			Mr. Capuano		X	
Mr. Posey	X			Mr. Clay		X	
Mr. Luetkemeyer	X			Mr. Lynch		X	
Mr. Huizenga	X			Mr. David Scott (GA)		X	
Mr. Duffy	X			Mr. Al Green (TX)		X	
Mr. Stivers	X			Mr. Cleaver		X	
Mr. Hultgren	X			Ms. Moore		X	
Mr. Ross	X			Mr. Ellison		X	
Mr. Pittenger	X			Mr. Perlmutter		X	
Mrs. Wagner	X			Mr. Himes		X	
Mr. Barr	X			Mr. Foster		X	
Mr. Rothfus	X			Mr. Kildee		X	
Mr. Messer	X			Mr. Delaney		X	
Mr. Tipton	X			Ms. Sinema		X	
Mr. Williams	X			Mrs. Beatty		X	
Mr. Poliquin	X			Mr. Heck		X	
Mrs. Love	X			Mr. Vargas		X	
Mr. Hill	X			Mr. Gottheimer		X	
Mr. Emmer	X			Mr. Gonzalez (TX)		X	
Mr. Zeldin	X			Mr. Crist		X	
Mr. Trott	X			Mr. Kihuen		X	
Mr. Loudermilk	X						
Mr. Mooney (WV)	X						
Mr. MacArthur	X						
Mr. Davidson	X						
Mr. Budd	X						
Mr. Kustoff (TN)	X						
Ms. Tenney	X						
Mr. Hollingsworth	X						

COMMITTEE OVERSIGHT FINDINGS

Pursuant to clause 3(c)(1) of rule XIII of the Rules of the House of Representatives, the findings and recommendations of the Committee based on oversight activities under clause 2(b)(1) of rule X of the Rules of the House of Representatives, are incorporated in the descriptive portions of this report.

PERFORMANCE GOALS AND OBJECTIVES

Pursuant to clause 3(c)(4) of rule XIII of the Rules of the House of Representatives, the Committee states that H.R. 4278 will increase monetary policy independence and decrease economic distortions by providing for the maintenance of a Federal Reserve system that can serve as our government's fiscal agent but not fiscal principal.

NEW BUDGET AUTHORITY, ENTITLEMENT AUTHORITY, AND TAX EXPENDITURES

The Committee has not received an estimate of new budget authority contained in the cost estimate prepared by the Director of the Congressional Budget Office pursuant to Sec. 402 of the Congressional Budget Act of 1974. In compliance with clause 3(c)(2) of rule XIII of the Rules of the House, the Committee opines that H.R. 4278 will not establish any new budget or entitlement authority or create any tax expenditures.

CONGRESSIONAL BUDGET OFFICE ESTIMATES

The cost estimate prepared by the Director of the Congressional Budget Office pursuant to Sec. 402 of the Congressional Budget Act of 1974 was not submitted timely to the Committee.

FEDERAL MANDATES STATEMENT

This information is provided in accordance with section 423 of the Unfunded Mandates Reform Act of 1995. The Committee has determined that the bill does not contain Federal mandates on the private sector. The Committee has determined that the bill does not impose a Federal intergovernmental mandate on State, local, or tribal governments.

ADVISORY COMMITTEE STATEMENT

No advisory committees within the meaning of section 5(b) of the Federal Advisory Committee Act were created by this legislation.

APPLICABILITY TO LEGISLATIVE BRANCH

The Committee finds that the legislation does not relate to the terms and conditions of employment or access to public services or accommodations within the meaning of the section 102(b)(3) of the Congressional Accountability Act.

EARMARK IDENTIFICATION

With respect to clause 9 of rule XXI of the Rules of the House of Representatives, the Committee has carefully reviewed the provisions of the bill and states that the provisions of the bill do not

contain any congressional earmarks, limited tax benefits, or limited tariff benefits within the meaning of the rule.

DUPLICATION OF FEDERAL PROGRAMS

In compliance with clause 3(c)(5) of rule XIII of the Rules of the House of Representatives, the Committee states that no provision of the bill establishes or reauthorizes: (1) a program of the Federal Government known to be duplicative of another Federal program; (2) a program included in any report from the Government Accountability Office to Congress pursuant to section 21 of Public Law 111–139; or (3) a program related to a program identified in the most recent Catalog of Federal Domestic Assistance, published pursuant to the Federal Program Information Act (Pub. L. No. 95–220, as amended by Pub. L. No. 98–169).

DISCLOSURE OF DIRECTED RULEMAKING

Pursuant to section 3(i) of H. Res. 5, (115th Congress), the following statement is made concerning directed rulemakings: The Committee estimates that the bill requires no directed rulemakings within the meaning of such section.

SECTION-BY-SECTION ANALYSIS OF THE LEGISLATION

Section 1. Short title

This section cites H.R. 4278 as the Independence from Credit Policy Act of 2017.

Section 2. Independence from credit policy

This section provides for the Federal Reserve and the Treasury to engage in asset swaps, whereby the Treasury receives assets from the Federal Reserve that are neither gold nor Treasury securities, nor direct obligations of foreign central banks, or the International Monetary Fund, and in return the Federal Reserve receives Treasury securities of equivalent market value.

CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3(e) of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, and existing law in which no change is proposed is shown in roman):

FEDERAL RESERVE ACT

* * * * *

【SEC. 10A. Upon receiving the consent of not less than five members of the Board of Governors of the Federal Reserve System, any Federal Reserve bank may make advances, in such amount as the board of directors of such Federal Reserve bank may determine, to groups of five or more member banks within its district, a majority of them independently owned and controlled, upon their time or demand promissory notes, provided the bank or banks which receive the proceeds of such advances as herein provided have no adequate

amounts of eligible and acceptable assets available to enable such bank or banks to obtain sufficient credit accommodations from the Federal Reserve bank through rediscounts or advances other than as provided in section 10(b). The liability of the individual banks in each group must be limited to such proportion of the total amount advanced to such group as the deposit liability of the respective banks bears to the aggregate deposit liability of all banks in such group, but such advances may be made to a lesser number of such member banks if the aggregate amount of their deposit liability constitutes at least 10 per centum of the entire deposit liability of the member banks within such district. Such banks shall be authorized to distribute the proceeds of such loans to such of their number and in such amount as they may agree upon, but before so doing they shall require such recipient banks to deposit with a suitable trustee, representing the entire group, their individual notes made in favor of the group protected by such collateral security as may be agreed upon. Any Federal Reserve bank making such advance shall charge interest or discount thereon at a rate not less than 1 per centum above its discount rate in effect at the time of making such advance. No such note upon which advances are made by a Federal Reserve bank under this section shall be eligible under section 16 of this Act as collateral security for Federal Reserve notes.

[No obligations of any foreign government, individual, partnership, association, or corporation organized under the laws thereof shall be eligible as collateral security for advances under this section.]

[Member banks are authorized to obligate themselves in accordance with the provisions of this section.]

SEC. 10B. (a) IN GENERAL.—Any Federal Reserve bank, under rules and regulations prescribed by the Board of Governors of the Federal Reserve System, may make advances to any member bank on its time or demand notes having maturities of not more than four months and which are secured to the satisfaction of such Federal Reserve bank.

Notwithstanding the foregoing, any Federal Reserve bank, under rules and regulations prescribed by the Board of Governors of the Federal Reserve System, may make advances to any member bank on its time notes having such maturities as the Board may prescribe and which are *not* secured by mortgage loans covering a one-to-four family residence. Such advances shall bear interest at a rate equal to the [lowest discount rate] *highest discount rate* in effect at such Federal Reserve bank on the date of such note.

(b) LIMITATIONS ON ADVANCES.—

(1) LIMITATION ON EXTENDED PERIODS.—Except as provided in paragraph (2), no advances to any undercapitalized depository institution by any Federal Reserve bank under this section may be outstanding for more than 60 days in any 120-day period.

(2) VIABILITY EXCEPTION.—

(A) IN GENERAL.—If—

(i) the head of the appropriate Federal banking agency certifies in advance in writing to the Federal

Reserve bank that any depository institution is viable;
or

(ii) the Board conducts an examination of any depository institution and the Chairman of the Board certifies in writing to the Federal Reserve bank that the institution is viable,

the limitation contained in paragraph (1) shall not apply during the 60-day period beginning on the date such certification is received.

(B) EXTENSIONS OF PERIOD.—The 60-day period may be extended for additional 60-day periods upon receipt by the Federal Reserve bank of additional written certifications under subparagraph (A) with respect to each such additional period.

(C) AUTHORITY TO ISSUE A CERTIFICATE OF VIABILITY MAY NOT BE DELEGATED.—The authority of the head of any agency to issue a written certification of viability under this paragraph may not be delegated to any other person.

(D) EXTENDED ADVANCES SUBJECT TO PARAGRAPH (3).—Notwithstanding paragraph (1), an undercapitalized depository institution which does not have a certificate of viability in effect under this paragraph may have advances outstanding for more than 60 days in any 120-day period if the Board elects to treat—

(i) such institution as critically undercapitalized under paragraph (3); and

(ii) any such advance as an advance described in subparagraph (A)(i) of paragraph (3).

(3) ADVANCES TO CRITICALLY UNDERCAPITALIZED DEPOSITORY INSTITUTIONS.—

(A) LIABILITY FOR INCREASED LOSS.—Notwithstanding any other provision of this section, if—

(i) in the case of any critically undercapitalized depository institution—

(I) any advance under this section to such institution is outstanding without payment having been demanded as of the end of the 5-day period beginning on the date the institution becomes a critically undercapitalized depository institution;
or

(II) any new advance is made to such institution under this section after the end of such period;
and

(ii) after the end of that 5-day period, the Deposit Insurance Fund of the Federal Deposit Insurance Corporation incurs a loss exceeding the loss that the Corporation would have incurred if it had liquidated that institution as of the end of that period,

the Board shall, subject to the limitations in subparagraph (B), be liable to the Federal Deposit Insurance Corporation for the excess loss, without regard to the terms of the advance or any collateral pledged to secure the advance.

(B) LIMITATION ON EXCESS LOSS.—The liability of the Board under subparagraph (A) shall not exceed the lesser of the following:

(i) The amount of the loss the Board or any Federal Reserve bank would have incurred on the increases in the amount of advances made after the 5-day period referred to in subparagraph (A) if those increased advances had been unsecured.

(ii) The interest received on the increases in the amount of advances made after the 5-day period referred to in subparagraph (A).

(C) FEDERAL RESERVE TO PAY OBLIGATION.—The Board shall pay the Federal Deposit Insurance Corporation the amount of any liability of the Board under subparagraph (A).

(D) REPORT.—The Board shall report to the Congress on any excess loss liability it incurs under subparagraph (A), as limited by subparagraph (B)(i), and the reasons therefore, not later than 6 months after incurring the liability.

(4) NO OBLIGATION TO MAKE ADVANCES.—A Federal Reserve bank shall have no obligation to make, increase, renew, or extend any advance or discount under this Act to any depository institution.

(5) DEFINITIONS.—

(A) APPROPRIATE FEDERAL BANKING AGENCY.—The term “appropriate Federal banking agency” has the same meaning as in section 3 of the Federal Deposit Insurance Act.

(B) CRITICALLY UNDERCAPITALIZED.—The term “critically undercapitalized” has the same meaning as in section 38 of the Federal Deposit Insurance Act.

(C) DEPOSITORY INSTITUTION.—The term “depository institution” has the same meaning as in section 3 of the Federal Deposit Insurance Act.

(D) UNDERCAPITALIZED DEPOSITORY INSTITUTION.—The term “undercapitalized depository institution” means any depository institution which—

(i) is undercapitalized, as defined in section 38 of the Federal Deposit Insurance Act; or

(ii) has a composite CAMEL rating of 5 under the Uniform Financial Institutions Rating System (or an equivalent rating by any such agency under a comparable rating system) as of the most recent examination of such institution.

(E) VIABLE.—A depository institution is “viable” if the Board or the appropriate Federal banking agency determines, giving due regard to the economic conditions and circumstances in the market in which the institution operates, that the institution—

(i) is not critically undercapitalized;

(ii) is not expected to become critically undercapitalized; and

(iii) is not expected to be placed in conservatorship or receivership.

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POWERS OF FEDERAL RESERVE BANKS.

SEC. 13. Any Federal reserve bank may receive from any of its member banks or other depository institutions, and from the United States, deposits of current funds in lawful money, national-bank notes, Federal reserve notes, or checks, and drafts, payable upon presentation or other items, and also, for collection, maturing notes and bills; or, solely for purposes of exchange or of collection, may receive from other Federal reserve banks deposits of current funds in lawful money, national-bank notes, or checks upon other Federal reserve banks, and checks and drafts, payable upon presentation within its district or other items, and maturing notes and bills payable within its district; or, solely for the purposes of exchange or of collection, may receive from any nonmember bank or trust company or other depository institution deposits of current funds in lawful money, national-bank notes, Federal reserve notes, checks and drafts payable upon presentation or other items, or maturing notes and bills: *Provided*, Such nonmember bank or trust company or other depository institution maintains with the Federal reserve bank of its district a balance in such amount as the Board determines taking into account items in transit, services provided by the Federal Reserve bank, and other factors as the Board may deem appropriate: *Provided further*, That nothing in this or any other section of this Act shall be construed as prohibiting a member or nonmember bank or other depository institution from making reasonable charges, to be determined and regulated by the Board of Governors of the Federal Reserve System, but in no case to exceed 10 cents per \$100 or fraction thereof, based on the total of checks and drafts presented at any one time, for collection or payment of checks and drafts and remission therefor by exchange or otherwise; but no such charges shall be made against the Federal reserve banks.

Upon the indorsement of any of its member banks, which shall be deemed a waiver of demand, notice and protest by such bank as to its own indorsement exclusively, any Federal reserve bank may discount notes, drafts, and bills of exchange arising out of actual commercial transactions; that is, notes, drafts, and bills of exchange issued or drawn for agricultural, industrial, or commercial purposes, or the proceeds of which have been used, or are to be used, for such purposes, the Board of Governors of the Federal Reserve System to have the right to determine or define the character of the paper thus eligible for discount, within the meaning of this Act. Nothing in this Act contained shall be construed to prohibit such notes, drafts, and bills of exchange, secured by staple agricultural products, or other goods, wares, or merchandise from being eligible for such discount, and the notes, drafts, and bills of exchange of factors issued as such making advances exclusively to producers of staple agricultural products in their raw state shall be eligible for such discount; but such definition shall not include notes, drafts, or bills covering merely investments or issued or drawn for the purpose of carrying or trading in stocks, bonds, or other investment securities, except bonds and notes of the Government of the United States. Notes, drafts, and bills admitted to discount under the terms of this paragraph must have a maturity at the time of discount of not more than 90 days, exclusive of grace.

(3)(A) In unusual and exigent circumstances, the Board of Governors of the Federal Reserve System, by the affirmative vote of not less than five members, may authorize any Federal reserve bank, during such periods as the said board may determine, at rates established in accordance with the provisions of section 14, subdivision (d), of this Act, to discount for any participant in any program or facility with broad-based eligibility, notes, drafts, and bills of exchange when such notes, drafts, and bills of exchange are indorsed or otherwise secured to the satisfaction of the Federal Reserve bank: *Provided*, That before discounting any such note, draft, or bill of exchange, the Federal reserve bank shall obtain evidence that such participant in any program or facility with broad-based eligibility is unable to secure adequate credit accommodations from other banking institutions. All such discounts for any participant in any program or facility with broad-based eligibility shall be subject to such limitations, restrictions, and regulations as the Board of Governors of the Federal Reserve System may prescribe.

(B)(i) As soon as is practicable after the date of enactment of this subparagraph, the Board shall establish, by regulation, in consultation with the Secretary of the Treasury, the policies and procedures governing emergency lending under this paragraph. Such policies and procedures shall be designed to ensure that any emergency lending program or facility is for the purpose of providing liquidity to the financial system, and not to aid a failing financial company, and that the security for emergency loans is sufficient to protect taxpayers from losses and that any such program is terminated in a timely and orderly fashion. The policies and procedures established by the Board shall require that a Federal reserve bank assign, consistent with sound risk management practices and to ensure protection for the taxpayer, a lendable value to all collateral for a loan executed by a Federal reserve bank under this paragraph in determining whether the loan is secured satisfactorily for purposes of this paragraph.

(ii) The Board shall establish procedures to prohibit borrowing from programs and facilities by borrowers that are insolvent. Such procedures may include a certification from the chief executive officer (or other authorized officer) of the borrower, at the time the borrower initially borrows under the program or facility (with a duty by the borrower to update the certification if the information in the certification materially changes), that the borrower is not insolvent. A borrower shall be considered insolvent for purposes of this subparagraph, if the borrower is in bankruptcy, resolution under title II of the Dodd-Frank Wall Street Reform and Consumer Protection Act, or any other Federal or State insolvency proceeding.

(iii) A program or facility that is structured to remove assets from the balance sheet of a single and specific company, or that is established for the purpose of assisting a single and specific company avoid bankruptcy, resolution under title II of the Dodd-Frank Wall Street Reform and Consumer Protection Act, or any other Federal or State insolvency proceeding, shall not be considered a program or facility with broad-based eligibility.

- (iv) The Board may not establish any program or facility under this paragraph without the prior approval of the Secretary of the Treasury.
- (C) The Board shall provide to the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on Financial Services of the House of Representatives—
 - (i) not later than 7 days after the Board authorizes any loan or other financial assistance under this paragraph, a report that includes—
 - (I) the justification for the exercise of authority to provide such assistance;
 - (II) the identity of the recipients of such assistance;
 - (III) the date and amount of the assistance, and form in which the assistance was provided; and
 - (IV) the material terms of the assistance, including—
 - (aa) duration;
 - (bb) collateral pledged and the value thereof;
 - (cc) all interest, fees, and other revenue or items of value to be received in exchange for the assistance;
 - (dd) any requirements imposed on the recipient with respect to employee compensation, distribution of dividends, or any other corporate decision in exchange for the assistance; and
 - (ee) the expected costs to the taxpayers of such assistance; and
 - (ii) once every 30 days, with respect to any outstanding loan or other financial assistance under this paragraph, written updates on—
 - (I) the value of collateral;
 - (II) the amount of interest, fees, and other revenue or items of value received in exchange for the assistance; and
 - (III) the expected or final cost to the taxpayers of such assistance.
- (D) The information required to be submitted to Congress under subparagraph (C) related to—
 - (i) the identity of the participants in an emergency lending program or facility commenced under this paragraph;
 - (ii) the amounts borrowed by each participant in any such program or facility;
 - (iii) identifying details concerning the assets or collateral held by, under, or in connection with such a program or facility,
 shall be kept confidential, upon the written request of the Chairman of the Board, in which case such information shall be made available only to the Chairpersons or Ranking Members of the Committees described in subparagraph (C).
- (E) If an entity to which a Federal reserve bank has provided a loan under this paragraph becomes a covered financial company, as defined in section 201 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, at any time while such loan is outstanding, and the Federal reserve bank incurs a re-

alized net loss on the loan, then the Federal reserve bank shall have a claim equal to the amount of the net realized loss against the covered entity, with the same priority as an obligation to the Secretary of the Treasury under section 210(b) of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

(F) Not later than 1 year after a Federal reserve bank acquires any assets under this paragraph that are neither gold nor direct obligations of the United States, foreign central banks, or the International Monetary Fund—

(i) the Board shall transfer such assets of the Federal reserve bank to the Department of the Treasury; and

(ii) the Secretary of the Treasury shall transfer to the Federal reserve banks direct obligations of the United States of equivalent market value to the assets described in clause (i).

Upon the indorsement of any of its member banks, which shall be deemed a waiver of demand, notice, and protest by such bank as to its own indorsement exclusively, and subject to regulations and limitations to be prescribed by the Board of Governors of the Federal Reserve System, any Federal reserve bank may discount or purchase bills of exchange payable at sight or on demand which grow out of the domestic shipment or the exportation of nonperishable, readily marketable agricultural and other staples and are secured by bills of lading or other shipping documents conveying or securing title to such staples: *Provided*, That all such bills of exchange shall be forwarded promptly for collection, and demand for payment shall be made with reasonable promptness after the arrival of such staples at their destination: *Provided further*, That no such bill shall in any event be held by or for the account of a Federal reserve bank for a period in excess of ninety days. In discounting such bills Federal reserve banks may compute the interest to be deducted on the basis of the estimated life of each bill and adjust the discount after payment of such bills to conform to the actual life thereof.

The aggregate of notes, drafts, and bills upon which any person, copartnership, association, or corporation is liable as maker, acceptor, indorser, drawer, or guarantor, rediscounted for any member bank, shall at no time exceed the amount for which such person, copartnership, association, or corporation may lawfully become liable to a national banking association under the terms of section 5200 of the Revised Statutes, as amended: *Provided, however*, That nothing in this paragraph shall be construed to change the character or class of paper now eligible for rediscount by Federal reserve banks.

Any Federal reserve bank may discount acceptances of the kinds hereinafter described, which have a maturity at the time of discount of not more than 90 days' sight, exclusive of days of grace, and which are indorsed by at least one member bank: *Provided*, That such acceptances if drawn for an agricultural purpose and secured at the time of acceptance by warehouse receipts or other such documents conveying or securing title covering readily marketable staples may be discounted with a maturity at the time of discount of not more than six months' sight exclusive of days of grace.

(7)(A) Any member bank and any Federal or State branch or agency of a foreign bank subject to reserve requirements under section 7 of the International Banking Act of 1978 (hereinafter in this paragraph referred to as "institutions"), may accept drafts or bills of exchange drawn upon it having not more than six months' sight to run, exclusive of days of grace—

(i) which grow out of transactions involving the importation or exportation of goods;

(ii) which grow out of transactions involving the domestic shipment of goods; or

(iii) which are secured at the time of acceptance by a warehouse receipt or other such document conveying or securing title covering readily marketable staples.

(B) Except as provided in subparagraph (C), no institution shall accept such bills, or be obligated for a participation share in such bills, in an amount equal at any time in the aggregate to more than 150 per centum of its paid up and unimpaired capital stock and surplus or, in the case of a United States branch or agency of a foreign bank, its dollar equivalent as determined by the Board under subparagraph (H).

(C) The Board, under such conditions as it may prescribe, may authorize, by regulation or order, any institution to accept such bills, or be obligated for a participation share in such bills, in an amount not exceeding at any time in the aggregate 200 per centum of its paid up and unimpaired capital stock and surplus or, in the case of a United States branch or agency of a foreign bank, its dollar equivalent as determined by the Board under subparagraph (H).

(D) Notwithstanding subparagraphs (B) and (C), with respect to any institution, the aggregate acceptances, including obligations for a participation share in such acceptances, growing out of domestic transactions shall not exceed 50 per centum of the aggregate of all acceptances, including obligations for a participation share in such acceptances, authorized for such institution under this paragraph.

(E) No institution shall accept bills, or be obligated for a participation share in such bills, whether in a foreign or domestic transaction, for any one person, partnership, corporation, association or other entity in an amount equal at any time in the aggregate to more than 10 per centum of its paid up and unimpaired capital stock and surplus, or, in the case of a United States branch or agency of a foreign bank, its dollar equivalent as determined by the Board under subparagraph (H), unless the institution is secured either by attached documents or by some other actual security growing out of the same transaction as the acceptance.

(F) With respect to an institution which issues an acceptance, the limitations contained in this paragraph shall not apply to that portion of an acceptance which is issued by such institution and which is covered by a participation agreement sold to another institution.

(G) In order to carry out the purposes of this paragraph, the Board may define any of the terms used in this paragraph, and, with respect to institutions which do not have capital or capital stock, the Board shall define an equivalent measure to which the limitations contained in this paragraph shall apply.

(H) Any limitation or restriction in this paragraph based on paid-up and unimpaired capital stock and surplus of an institution shall

be deemed to refer, with respect to a United States branch or agency of a foreign bank, to the dollar equivalent of the paid-up capital stock and surplus of the foreign bank, as determined by the Board, and if the foreign bank has more than one United States branch or agency, the business transacted by all such branches and agencies shall be aggregated in determining compliance with the limitation or restriction.

Any Federal reserve bank may make advances for periods not exceeding fifteen days to its member banks on their promissory notes secured by the deposit or pledge of bonds, notes, certificates of indebtedness or Treasury bills of the United States, or by the deposit or pledge of debentures or other such obligations of Federal intermediate credit banks which are eligible for purchase by Federal reserve banks under section 13 (a) of this Act, or by the deposit or pledge of bonds issued under the provisions of subsection (c) of section 4 of the Home Owners' Loan Act of 1933, as amended; and any Federal reserve bank may make advances for periods not exceeding ninety days to its member banks on their promissory notes secured by such notes, drafts, bills of exchange, or bankers' acceptances as are eligible for rediscount or for purchase by Federal reserve banks under the provisions of this Act, or secured by such obligations as are eligible for purchase under section 14(b) of this Act. All such advances shall be made at rates to be established by such Federal reserve banks, such rates to be subject to the review and determination of the Board of Governors of the Federal Reserve System. If any member bank to which any such advance has been made shall, during the life or continuance of such advance, and despite an official warning of the reserve bank of the district or of the Board of Governors of the Federal Reserve System to the contrary, increase its outstanding loans secured by collateral in the form of stocks, bonds, debentures, or other such obligations, or loans made to members of any organized stock exchange, investment house, or dealer in securities, upon any obligation, note, or bill, secured or unsecured, for the purpose of purchasing and/or carrying stocks, bonds, or other investment securities (except obligations of the United States) such advance shall be deemed immediately due and payable, and such member bank shall be ineligible as a borrower at the reserve bank of the district under the provisions of this paragraph for such period as the Board of Governors of the Federal Reserve System shall determine: *Provided*, That no temporary carrying or clearance loans made solely for the purpose of facilitating the purchase or delivery of securities offered for public subscription shall be included in the loans referred to in this paragraph.

The discount and rediscount and the purchase and sale by any Federal reserve bank of any bills receivable and of domestic and foreign bills of exchange, and of acceptances authorized by this Act, shall be subject to such restrictions, limitations, and regulations as may be imposed by the Board of Governors of the Federal Reserve System. (Omitted from U.S. Code)

That in addition to the powers not vested by law in national banking associations organized under the laws of the United States any such association located and doing business in any place the population of which does not exceed five thousand inhabitants, as shown by the last preceding decennial census, may, under such

rules and regulations as may be prescribed by the Comptroller of the Currency, act as the agent for any fire, life, or other insurance company authorized by the authorities of the State in which said bank is located to do business in said State, by soliciting and selling insurance and collecting premiums on policies issued by such company; and may receive for services so rendered such fees or commissions as may be agreed upon between the said association and the insurance company for which it may act as agent: *Provided, however*, That no such bank shall in any case assume or guarantee the payment of any premium on insurance policies issued through its agency by its principal: *And provided further*, That the bank shall not guarantee the truth of any statement made by an assured in filing his application for insurance.

Any member bank may accept drafts or bills of exchange drawn upon it having not more than three months' sight to run, exclusive of days of grace, drawn under regulations to be prescribed by the Board of Governors of the Federal Reserve System by banks or bankers in foreign countries or dependencies or insular possessions of the United States for the purpose of furnishing dollar exchange as required by the usages of trade in the respective countries, dependencies, or insular possessions. Such drafts or bills may be acquired by Federal reserve banks in such amounts and subject to such regulations, restrictions, and limitations as may be prescribed by the Board of Governors of the Federal Reserve System: *Provided, however*, That no member bank shall accept such drafts or bills of exchange referred to this paragraph for any one bank to an amount exceeding in the aggregate ten per centum of the paid-up and unimpaired capital and surplus of the accepting bank unless the draft or bill of exchange is accompanied by documents conveying or securing title or by some other adequate security: *Provided further*, That no member bank shall accept such drafts or bills in an amount exceeding at any time the aggregate of one-half of its paid-up and unimpaired capital and surplus. (Omitted from U.S. Code)

Subject to such limitations, restrictions and regulations as the Board of Governors of the Federal Reserve System may prescribe, any Federal reserve bank may make advances to any individual, partnership or corporation on the promissory notes of such individual, partnership or corporation secured by direct obligations of the United States or by any obligation which is a direct obligation of, or fully guaranteed as to principal and interest by, any agency of the United States. Such advances shall be made for periods not exceeding 90 days and shall bear interest at rates fixed from time to time by the Federal reserve bank, subject to the review and determination of the Board of Governors of the Federal Reserve System.

Subject to such restrictions, limitations, and regulations as may be imposed by the Board of Governors of the Federal Reserve System, each Federal Reserve bank may receive deposits from, discount paper endorsed by, and make advances to any branch or agency of a foreign bank in the same manner and to the same extent that it may exercise such powers with respect to a member bank if such branch or agency is maintaining reserves with such Reserve bank pursuant to section 7 of the International Banking Act of 1978. In exercising any such powers with respect to any such

branch or agency, each Federal Reserve bank shall give due regard to account balances being maintained by such branch or agency with such Reserve bank and the proportion of the assets of such branch or agency being held as reserves under section 7 of the International Banking Act of 1978. For the purposes of this paragraph, the terms "branch," "agency," and "foreign bank" shall have the same meanings assigned to them in section 1 of the International Banking Act of 1978.

* * * * *

OPEN-MARKET OPERATIONS

SEC. 14. Any Federal reserve bank may, under rules and regulations prescribed by the Board of Governors of the Federal Reserve System, purchase and sell in the open market, at home or abroad, either from or to domestic or foreign banks, firms, corporations, or individuals, cable transfers and bankers' acceptances and bills of exchange of the kinds and maturities by this Act made eligible for rediscount, with or without the indorsement of a member bank.

Every Federal reserve bank shall have power:

(a) To deal in gold coin and bullion at home or abroad, to make loans thereon, exchange Federal reserve notes for gold, gold coin, or gold certificates, and to contract for loans of gold coin or bullion, giving therefor, when necessary, acceptable security, including the hypothecation of United States bonds or other securities which Federal reserve banks are authorized to hold;

[(b)(1) To buy and sell, at home or abroad, bonds and notes of the United States, bonds issued under the provisions of subsection (c) of section 4 of the Home Owners' Loan Act of 1933, as amended, and having maturities from date of purchase of not exceeding six months, and bills, notes, revenue bonds, and warrants with a maturity from date of purchase of not exceeding six months, issued in anticipation of the collection of taxes or in anticipation of the receipt of assured revenues by any State, county, district, political subdivision, or municipality in the continental United States, including irrigation, drainage and reclamation districts, and obligations of, or fully guaranteed as to principal and interest by, a foreign government or agency thereof, such purchases to be made in accordance with rules and regulations prescribed by the Board of Governors of the Federal Reserve System. Notwithstanding any other provision of this Act, any bonds, notes, or other obligations which are direct obligations of the United States or which are fully guaranteed by the United States as to principal and interest may be bought and sold without regard to maturities but only in the open market.

[(2) To buy and sell in the open market, under the direction and regulations of the Federal Open Market Committee, any obligation which is a direct obligation of, or fully guaranteed as to principal and interest by, any agency of the United States.]

(b) To buy and sell in the open market, at home or abroad, under the direction and regulations of the Federal Open Market Committee, gold stock, Treasury currency, or direct obligations of the United States, foreign central banks, or the International Monetary Fund. Nothing in this subsection shall be construed to limit ad-

vances under section 10B, or discount loans under sections 13, 13A, or 24.

(c) To purchase from member banks and to sell, with or without its indorsement, bills of exchange arising out of commercial transactions, as hereinbefore defined;

(d) To establish from time to time, subject to review and determination of the Board of Governors of the Federal Reserve System, rates of discount to be charged by the Federal reserve bank for each class of paper, which shall be fixed with a view of accommodating commerce and business; but each such bank shall establish such rates every fourteen days, or oftener if deemed necessary by the Board;

(e) To establish accounts with other Federal reserve banks for exchange purposes and, with the consent or upon the order and direction of the Board of Governors of the Federal Reserve System and under regulations to be prescribed by said board, to open and maintain accounts in foreign countries, appoint correspondents, and establish agencies in such countries wheresoever it may be deemed best for the purpose of purchasing, selling, and collecting bills of exchange, and to buy and sell, with or without its indorsement, through such correspondents or agencies, bills of exchange (or acceptances) arising out of actual commercial transactions which have not more than ninety days to run, exclusive of days of grace, and which bear the signature of two or more responsible parties, and, with the consent of the Board of Governors of the Federal Reserve System, to open and maintain banking accounts for such foreign correspondents or agencies, or for foreign banks or bankers, or for foreign states as defined in section 25 (b) of this Act. Whenever any such account has been opened or agency or correspondent has been appointed by a Federal reserve bank, with the consent of or under the order and direction of the Board of Governors of the Federal Reserve System, any other Federal reserve bank may, with the consent and approval of the Board of Governors of the Federal Reserve System, be permitted to carry on or conduct, through the Federal reserve bank opening such account or appointing such agency or correspondent, any transaction authorized by this section under rules and regulations to be prescribed by the board.

(f) To purchase and sell in the open market, either from or to domestic banks, firms, corporations, or individuals, acceptances of Federal Intermediate Credit Banks and of National Agricultural Credit Corporations, whenever the Board of Governors of the Federal Reserve System shall declare that the public interest so requires.

(g) The Board of Governors of the Federal Reserve System shall exercise special supervision over all relationships and transactions of any kind entered into by any Federal reserve bank with any foreign bank or banker, or with any group of foreign banks or bankers, and all such relationships and transactions shall be subject to such regulations, conditions, and limitations as the Board may prescribe. No officer or other representative of any Federal reserve bank shall conduct negotiations of any kind with the officers or representatives of any foreign bank or banker without first obtaining the permission of the Board of Governors of the Federal Reserve System. The Board of Governors of the Federal Reserve System shall have the right, in its discretion, to be represented in any

conference or negotiations by such representative or representatives as the Board may designate. A full report of all conferences or negotiations, and all understandings or agreements arrived at or transactions agreed upon, and all other material facts appertaining to such conferences or negotiations, shall be filed with the Board of Governors of the Federal Reserve System in writing by a duly authorized officer of each Federal reserve bank which shall have participated in such conferences or negotiations.

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MINORITY VIEWS

H.R. 4278, the so-called “Independence from Credit Policy Act,” purports to address Republicans’ concern that monetary policies are morphing into credit policies. However, the bill fundamentally misunderstands the role of the Federal Reserve and its conduct of monetary policy. At its core, the purpose of monetary policy is to manage the level of interest rates and thereby influence the availability and cost of credit in the economy. In doing so, the Federal Reserve affects spending, investment, production, employment and inflation within the U.S. economy. Put simply, monetary policy and credit policy are fundamentally linked, and as the Center for Popular Democracy points out in a letter submitted for the record “mak[ing] the Fed independent from credit policy—is neither possible nor desirable.”

However, H.R. 4278 does not just misunderstand the Federal Reserve’s role in setting monetary policy, it would fully eliminate the Federal Reserve’s ability to purchase certain assets, including GSE mortgage-backed securities (MBS) going forward—an important tool that was deployed effectively by the Federal Reserve in response to the 2008 financial crisis. Had this legislation been in effect prior to the 2008 crisis, the Federal Reserve would have been unable to make the significant MBS purchases that supported the flow of credit to the housing sector—a sector that was deeply impaired.

At a legislative hearing held by the Subcommittee on Monetary Policy and Trade to examine this proposal, Dr. Jared Bernstein wrote in his testimony that restricting the Federal Reserve’s asset purchases in the manner called for in this bill “would have been a serious mistake that would likely have prolonged the downturn.”¹ Dr. Bernstein’s testimony also cited research supporting the positive effects of the Federal Reserve’s MBS purchases. For example, he noted that research conducted by economists Diana Hancock and Wayne Passmore found that the Federal Reserve’s MBS purchases lowered mortgage rates by roughly 1 to 1.5 percentage points.

¹Dr. Jared Bernstein, Testimony before the U.S. House of Representatives, Subcommittee on Monetary Policy and Trade hearing titled *Examining Federal Reserve Reform Proposals*, (November 7, 2017) available at <https://financialservices.house.gov/uploadedfiles/hhrg-115-ba19-wstate-jbernstein-20171107.pdf>.

Other experts have also highlighted the important benefits of the Federal Reserve’s MBS purchases. For example, in April 2017, Dr. William Spriggs noted that the Federal Reserve’s MBS purchases “helped to stabilize housing prices” and also “help[ed] stabilize the household balance sheet.”² Similarly, Dr. Alan S. Blinder and Dr. Mark Zandi have noted that the Federal Reserve’s MBS purchases “helped end the housing crash.”³ Taking away the Federal Reserve’s authority to purchase MBS—which has put money back in the pockets of creditworthy borrowers and helped shore up the home values of those who were devastated by the subprime crisis—would be foolish and shortsighted.

We also note that unlike many other major central banks, the Federal Reserve is relatively limited in terms of the assets it can purchase in its conduct of monetary policy. Whereas the central banks of England, Japan, Canada and Europe have few restrictions on the kinds of assets they can purchase, our central bank is generally limited to purchasing Treasury and GSE securities. In discussing this proposal, Dr. Bernstein noted that, in a sense, Americans were “‘lucky’ that the cause of the recession was the bursting of the housing bubble, as a channel existed by which the Fed could prevent the excessive tightening of credit in that sector.” Rather than constrain its ability to respond to financial crises, Congress should consider the ways in which the Federal Reserve can be more effective in correcting the damages that households may suffer as a result of any future downturn.

Finally, the swap of MBS with Treasury assets called for in the bill creates a number of additional problems. Specifically, the bill fails to account for the fact that the issuance of Treasury debt that would be needed for such a swap to occur would also require Congress to raise the debt ceiling. Without the inclusion of a provision to lift the debt ceiling, such legislation could not go into effect. Under the unlikely scenario where the debt ceiling is lifted to allow the bill to go into effect, the bill nonetheless fails to contemplate what Treasury would do with the MBS. The sale of the assets would likely cause needless volatility in financial markets, and increase mortgage rates, taking money out of the pockets of middle class families and slowing the economy’s recovery.

²Dr. William E. Spriggs, Testimony before the U.S. House of Representatives, Subcommittee on Monetary Policy and Trade hearing titled *Examining the Federal Reserve’s Mandate and Governance Structure*, (April 4, 2017), available at <https://financialservices.house.gov/uploadedfiles/hhrg-115-ba19-wstate-wspriggs-20170404.pdf>.

³Dr. Alan S. Blinder and Dr. Mark Zandi, “The Financial Crisis: Lessons for the Next One,” (October 15, 2015), available at <https://www.cbpp.org/research/economy/the-financial-crisis-lessons-for-the-next-one>.

For these reasons, we oppose this bill.

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