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THE SAFETY OF THE TEMPLE: Why Do Budget Cutters Spare the Federal Reserve?

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At present, most areas of government spending are facing significant cuts over the next few years. One major exception is the Federal Reserve System, where spending has been growing at a rate that significantly outpaces inflation. Over the next five years, spending by the Federal Reserve System is likely to continue to grow, despite additional cutbacks in other areas of domestic spending.

Unlimited Authority to Spend Money

Unlike other agencies of the government, the Federal Reserve System does not need to request appropriations from Congress; instead, it finances most of its operations through its power to print money. This mechanism gives it essentially unlimited authority to spend money as its governors and directors see fit, without congressional authorization and largely without congressional oversight.

In the current fiscal year, the Federal Reserve System's spending exceeded \$2 billion. Over the last three years, its spending has grown by approximately 20%, outstripping inflation by more than 10%. If, as Federal Reserve Board Chairman Alan Greenspan argues, current price measures significantly overstate the true rate of inflation, then Federal Reserve spending has grown even more rapidly relative to the true inflation rate.

With this funding, the Federal Reserve System fulfills a range of functions beyond serving the needs and protecting the integrity of the nation's banking system. It is the nation's top employer of economists, many of whom are primarily engaged in research that is of no obvious public interest. Over \$200 million a year (more than 10% of the Federal Reserve System's budget) is earmarked for "monetary and economic policy." Congress should ask whether this money could be better spent elsewhere.

The Greenspan Years: A Burgeoning Budget for the Board

Because the Federal Reserve System (comprising the Board of Governors and the 12 regional banks) relies on its government-granted monopoly on printing money to finance most of its operations, it would be reasonable to treat the whole system as a government agency. However, for budgetary purposes only

the operations of the Board of Governors count as government expenses. These also have grown far more rapidly than the general inflation rate.

During the Greenspan years, from 1988 until now:

- The budget of the Board of Governors has grown from \$89.9 million to \$177.4 million, an increase of more than 97%. A modest cut of 10% in the board's annual budget would be enough to finance the Council of Economic Advisors (currently slated for elimination) for five years.
- Employment at the Board of Governors has grown from 1,484 to 1,655, an increase of 11.5%. This growth occurred when employment for the federal government as a whole shrank by 4.6%.

There are no current plans to rein in this growth, even as the president and Congress move forward with their plans for further cuts in most areas of nonmilitary spending. For example, the proposal from the House-Senate conference committee would reduce spending on natural resources by the year 2000 by 27% from current levels, after adjusting for inflation. Spending on community development would fall by 58%, and spending on energy by 59%. The comparable numbers from the president's latest budget plan are 21%, 34%, and 51%.

Does Accountability Compromise Independence?

Congress should act to make the Federal Reserve Board both as accountable and as subject to austerity as other government agencies. It has been argued that making the Federal Reserve subject to congressional appropriation would eliminate its independence from politics. However, the Supreme Court relies on congressional appropriations, and this requirement has not compromised its independence in any obvious way.

Conclusion

The Federal Reserve System indeed fulfills many vital functions. It acts as a clearinghouse for the nation's banking system by processing checks and transferring funds. It monitors bank practices to ensure that regulations on ethics, soundness, and discrimination in lending are respected. However, in the present environment of fiscal austerity, all government agencies, even those making life and death regulatory decisions, such as the Food and Drug Administration, are being forced to accept cutbacks. There is no reason the Federal Reserve System should not also be expected to do more with less.

References

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