

WSJ Print Edition

Trump's nominee could spark scrutiny of a bank that has sweeping powers and a record of blunders.



POLITICAL ECONOMICS

Congress's Chance to Build a Better Federal Reserve

President Trump's nomination of Stephen Miran to the Federal Reserve Board of Governors has triggered another freak-out about politicization of the central bank. Once the Senate takes up the matter, attention inevitably will shift to Mr. Miran's writings on Federal Reserve reform, which are provocative. This column hasn't always been complimentary to Mr. Miran, but in this regard he has a point or two.

Mr. Miran and economist Daniel Katz in March 2024 published a paper at the Manhattan Institute proposing radical overhauls of the Fed. In recent years the central bank has delivered terrible policy outcomes, which include setting the stage for the 2008 financial panic and tolerating for too long the worst inflation in 40 years. The premise of the Miran-Katz paper was that different governance arrangements at the Fed might lead to smarter decisions.

When I describe the proposals as "radical," it's an understatement. Messrs. Miran and Katz suggested the president should be able to fire board members at will, and that the Fed's budget should be appropriated by Congress rather than set by the institution itself from its own resources.

They also proposed a transformation of the 12 regional reserve banks that make up the Federal Reserve System. The gist would be to allow state governors in the various regions to appoint the boards of the reserve banks, bodies that currently are selected by local business grandees. All 12 regional bank presidents (appointed by all those boards) would then vote at every meeting of the policy-setting Federal Open Market Committee, rather than only a few on a rotating basis as is done today.

The goal would be to improve democratic accountability at the regional level, while also injecting more intellectual diversity into FOMC decision making by weakening the power of the Washington-based board of governors—both of which are worthy goals.

None of this is likely to happen anytime soon. To the extent Congress has cared about Fed governance at all in recent years, the inclination has been to centralize control rather than disperse it as the Miran-Katz plan would. Their idea to introduce more executive oversight of the board in Washington assumed the Supreme Court would force the issue eventually anyway. The justices subsequently have indicated that whatever they think about presidential appointment powers for other agencies, they're reluctant to disturb the Fed's unique arrangements.

Which is just as well, since the palaver over these structural proposals misses the more profound point Messrs. Miran and Katz raised: Most of the Fed's political and policy problems arise because the central bank does way too much. "Scrutiny of Fed rhetoric and actions makes it clear that the Fed has moved beyond its traditional narrow, technocratic role and instead has pursued a much more expansive monetary and regulatory agenda that is more consistent with an explicitly political institution," the economists wrote.

They cite a long list of examples: After 2008, the expansion of the Fed's balance sheet made the central bank a significant participant in markets for longer-term Treasury debt and mortgage-backed securities. The Fed's suppression of longer-term interest rates encouraged Congress to ramp up spending, egged on by a few choice

Note

comments from Fed officials. When Mr. Trump whines that higher interest rates now cost the government globs of money in debt-service costs, the dirty secret is that he has half a point in his complaint that Chairman Jerome Powell helped created this mess.

Meanwhile, the Fed at times has strayed into the commercial-paper market and has subsidized smallbusiness lending, all under its expansive authority for emergency action. This forces the Fed into decisions about credit allocation that necessarily become political when any government entity makes them. *Note*

The Fed's regulatory power also creates temptations for political mischief. The Fed can inject climate mandates, for instance, into its regulatory criteria for banks. The Fed and other regulators already have been called out for applying nebulous cautions about "reputational risk" in ways that encouraged banks to ditch politically unpopular customers. And all while regulators miss looming disasters such as the implosion of Silicon Valley Bank.

The most important reform recommendations Messrs. Miran and Katz offered didn't concern who would make decisions at the Fed, but rather which decisions such people would be allowed to make. The economists proposed hiving off the Fed's regulatory role and also subjecting its crisis-response actions to direct scrutiny by elected officials.

Agree or disagree, this is a plausible answer to the most serious challenge to the Federal Reserve's prized institutional independence: No democratic political system can tolerate an unaccountable institution that exercises such awesome economic power and also makes so many mistakes. Witness mounting bipartisan frustration with the Fed in Congress. Mr. Miran's nomination presents an opportunity for senators to reflect on how Congress could build a better central bank.

By Joseph C. Sternberg *Note*

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