**[Is the Federal Reserve System a Governmental or a Privately controlled organization?](http://www.monetary.org/is-the-federal-reserve-system-a-governmental-or-a-privately-controlled-organization/2008/02%22%20%5Co%20%22Permanent%20Link%20to%20Is%20the%20Federal%20Reserve%20System%20a%20Governmental%20or%20a%20Privately%20controlled%20organization)**

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Students of our monetary system quickly encounter this important question, normally phrased as whether the Federal Reserve System is part of the U.S. Government or is a private organization. The importance people are placing on the answer is indicated by the over 36,000 web sites the question raises on internet search engines.

We’ll examine evidence in the Federal Reserve legislation; in how the Fed operates; from Congressional testimony; from statements from the Federal Reserve’s publications; in statements by former Chairmen of the House Banking Committee; and in official rulings by US courts, to show why we conclude that although there are some elements of ambiguity, the Federal Reserve system is essentially dominated and controlled by private financiers, not our government; and to the extent that there is ownership of it, it is entirely private. Therefore despite the ambiguity – and confusion – the Fed is more accurately seen as a private, not a governmental institution, though with substantial governmental ties.

The ambiguity arises from a combination of misleading appearances; the fact that our President appoints (with consent of the Senate) the Chairman of the Fed to four year terms, and the 5 member Board in Washington to 14 year terms; the fact that the Fed is supposed to promote governmental fiscal policy; and the fact that the system was originally set up in law by Congress in 1913 and can be altered, nationalized or even dismantled by Congress.

Most Americans understand that the Fed controls our money system, but they believe its part of our government, as would be expected of any organization holding that much power over the destiny of our country. Americans also erroneously believe the banking business consists of accepting deposits from clients and then re-loaning them to borrowers at a higher rate of interest. Though the number is definitely growing, most Americans have no idea that money (or more accurately interest bearing bank credits – purchasing media which serves as money) is created by the banking system when loans are made, through the fractional reserve provisions. This is understood by few novices, and often economists and even bankers fail to comprehend that they function as part of a money creation system, when they issue credits, and deposit them into their client’s accounts when loans are extended.

Therefore most Americans would be surprised to learn that almost all of what we use for money is not issued by our government, but by private banks. They have been “allowed” to form erroneous assumptions about our money and banking system that are far from reality and that serves to shield from closer scrutiny, whether the Fed is truly operating in the public interest or advancing more private agendas, either on purpose or by default.

Organization And Ownership:

The Federal Reserve consists of 12 regional Federal Reserve banks, with boards of Directors, under an umbrella direction of the 7 member Federal Reserve Board in Washington, with the power to determine major aspects of banking activity, such as setting interest rates, and the reserve and other operational requirements. There are no shares of the Washington Fed Board organization; the only “ownership” of the Fed is in shares of each of the 12 regional banks which are entirely owned by the private member banks within their respective districts, according to a formula based on their size (they must subscribe to the shares with 3% of their capital plus surplus).  The ownership is highly restricted in that such ownership is mandatory; the shares can’t be sold; and they pay a guaranteed 6% annual dividend..

Thus the stories that the Federal Reserve is “owned” by foreign bankers (the Rothschild’s and other prominent banker names usually come up) are not accurate and these types of rumors have mainly served to discredit wholesome criticism of the banking system. While it is true that our first central bank, the First Bank of the United States, upon dissolution in 1811 was found to be three quarters owned by British and Dutch interests, that bank was structured simply as a private share company on the Bank of England model.\* The control of the Federal Reserve System is more difficult to untangle and is not just a matter of counting shareholder votes. While foreign bankers might indirectly own shares of the regional Federal Reserve Banks through ownership of American banking companies, such ownership would be reported to the SEC if any entity held more than 5% of the American corporation. This however does not exclude strong, potentially undue foreign influence, for example through the Bank for International Settlements (BIS).

A “Non-Profit” Organization?

The Federal Reserve System puts itself forward as a non-profit organization that turns over its operating profits to the U.S. Treasury, after all expenses, including the 6% dividend to member banks. However this misses the point on several scores. First, the banking profits coming through the privileged money creation process mainly occurs at the member bank level of operation, and those profits are not turned over to the Treasury. That is, the net earnings from the member banks seigniorage privilege are not turned over to our government but kept by the private member banks. For England this amount has been estimated at 41 Billion Pounds per year. For the US we think it’s between $100-200 billion per year; but we need to know the amount more precisely from the Fed itself.

This money creation which is put into the system when the banks extend loans, eventually becomes a source of funding when our government’s bonds are sold to the public. Here is how Wright Patman, former House Banking and Currency Committee Chairman for 16 years criticized that process:

“I have never yet had anyone who could, through the use of logic and reason, justify the Federal Government borrowing the use of its own money….I believe the time will come when people will demand that this be changed. I believe the time will come in this country when they will actually blame you and me and everyone else connected with the Congress for sitting idly by and permitting such an idiotic system to continue.”

We think the time has come.

Secondly, how extravagant are the FED’s operating expenses? Reputedly quite high, but in order to determine that for sure a proper audit would be necessary. Just where did the extensive real assets of the Fed come from if all the earnings are turned over to the Treasury? (Fed capital as of June 28, 2006 was $29.462 billion) Perhaps some part of it comes from member bank subscriptions to the regional Fed shares. Another question for the audit to address. (If memory serves correctly, the Fed used to turn over 90% not all, of its earnings over to the Treasury; but now its 100%.

Control:

Private ownership does not guarantee private control – they can be two different things. Although ownership of the fed is admittedly private in a restricted way, it is control which is the more important factor in regarding the Fed as private, not governmental. Remember the question is whether the control rests more in private or governmental hands, not whether it rests directly in shareholders hands.

It will be clear from the following points that the Fed is definitely not part of the US Government:

\* The Fed is not organized within the Executive, Legislative or Judicial branches of our government.

\* Who pays the Fed’s bills and determines its budget? Not any part of our government. The Fed gets its funding from its own specially privileged operations. The Fed Board determines Fed budgets.

\* Who monitors and oversees Fed activities? Again the Fed itself. While some important elements of proper auditing have taken place, there has not yet been a comprehensive independent audit, by the Government Accountability Office as proposed in a recent letter from Ralph Nader to new Fed Chairman Ben Bernanke, calling for greater monetary transparency.

\* Federal Reserve Employees are not part of the US Civil Service System and are not covered by government employees’ health insurance or pension programs. Who does the hiring and firing? Except for the highly publicized Chairman and 7 member Washington Board, this is in private, unelected hands.

\* Federal Reserve Banks are not listed as government organizations by the telephone companies, a small but telling fact.
Here is how the Fed describes the Control situation, in the FAQ’s on its website:

“As the nation’s central bank, the Federal Reserve derives its authority from the U.S. Congress. It is considered an independent central bank because its decisions do not have to be ratified by the President or anyone else in the executive or legislative branch of government, it does not receive funding appropriated by Congress, and the terms of the members of the Board of Governors span multiple presidential and congressional terms. However, the Federal Reserve is subject to oversight by Congress, which periodically reviews its activities and can alter its responsibilities by statute. Also, the Federal Reserve must work within the framework of the overall objectives of economic and financial policy established by the government. Therefore, the Federal Reserve can be more accurately described as “independent within the government.”

We’d suggest the phrase “independent within the government” is much too ambiguous and has the effect of conveying great power while avoiding responsibility.

The Fed’s FAQ’s continue regarding control:

“The Federal Reserve’s ultimate accountability is to Congress, which at any time can amend the [Federal Reserve Act](http://www.federalreserve.gov/GeneralInfo/fract/default.htm). Legislation requires that the Fed [report annually](http://www.federalreserve.gov/boarddocs/rptcongress/) on its activities to the Speaker of the House of Representatives, and [twice annually](http://www.federalreserve.gov/boarddocs/hh/) on its plans for monetary policy to the banking committees of Congress. Fed officials also testify before Congress when requested.

“To ensure financial accountability, the financial statements of the Federal Reserve Banks and the Board of Governors are audited annually by an independent outside auditor. In addition, the General Accounting Office, as well as the Board’s Office of Inspector General, can audit Federal Reserve activities.”

We agree with Mr. Nader that it is time for the General Accountability Office to carry out this full audit of the Federal Reserve System. We take at face value the Fed’s statement that the only way for our government to exert necessary societal controls on the Fed is through legislation altering the Federal Reserve Act.
The Federal Reserve Act

Reading the Act with the question of control in mind, what one finds are primarily an enumeration and description of vast powers over our monetary system being ceded to the non – governmental Federal Reserve. Primary among these are the powers necessary to administer a fractional reserve banking system in which the creation of money – what we use for purchasing media – is in private hands.

One is struck by the general absence of governmental controls over Fed activity, and lack of requirements toward our elected representatives.

One is struck by the lack of accountability of the Fed to our governmental officials or bodies.

One is struck by the lack of any specified penalties should the system be found to not be promoting governmental public policy at all.

One is struck by the lack of formal oversight procedures to determine whether that is happening or not.

The Act requires the Chairman to appear before Congress and Congressional committees four times a year, and requires the Board to submit two written reports to Congress annually. To understand that this is not sufficient oversight, one need only read Congressman Bernie Sanders questioning of Chairman Greenspan, from the Congressman’s website. When tough questions were put to the Chairman, as Congressman Sanders did, forms of stalling non-answers came back until the announcement, “Your time is up Mr. Congressman.”

While the act specifies that the Comptroller of the Currency has the power to directly examine any member bank in the system, he is not empowered to examine Federal Reserve Regional banks – that is in the hands of the Washington Board. 14 year appointments – a one time event for them – places them outside the influence of our elected officials, in other words outside the democratic process.

Probably this “independence” was sold as a good thing! From the time of Adam Smith, there has been a growing attack against government, as being incapable of managing the monetary system. Despite the evidence that government has a far better record controlling money than private bankers have\*; despite the fact that government is the only organizational form with ability to stand between the people and the “Enrons” of the world. It is time to rethink this “independence” question and examine the actual evidence, rather than to continue relying on free market ideology – really a form of elitist propaganda. It would be smarter to examine mankind’s actual experience with government controlled money systems – especially in America.  For what reason did the Federal Reserve Act envision that it would be saints serving on the Fed Board?
Some Conclusions from Court Cases

Several legal proceedings further illuminate the private aspects of the Fed. This case refers to several of those cases.

1) JOHN L. LEWIS, Plaintiff/Appellant, vs. UNITED STATES OF AMERICA, Defendant/Appellee.

(No. 80-5905, UNITED STATES COURT OF APPEALS, NINTH CIRCUIT

680 F.2d 1239; 1982 U.S. App. LEXIS 20002; March 2, 1982, Submitted; April 19, 1982, Decided)

[Lewis had been injured by a car owned by the San Francisco Fed and sued the US Government for damages. Note that this ruling particularly applies to the regional Federal Reserve Banks, not necessarily the Federal Reserve Board. Thus even more ambiguity!]

Excerpts from the ruling:

The district court dismissed, holding that the Federal Reserve Bank is not a federal agency within the meaning of the Federal Reserve Act and that the court therefore lacked subject matter jurisdiction….

“Federal agency” is defined as: the executive departments, the military departments, independent establishments of the United States, and corporations acting primarily as instrumentalities of the United States, but does not include any contractors with the United States.

There are no sharp criteria for determining whether an entity is a federal agency within the meaning of the Act (28 U.S.C. § 2671), but the critical factor is the existence of federal government control over the “detailed physical performance” and “day to day operation” of that entity…. Other factors courts have considered include whether the entity is an independent corporation…, whether the government is involved in the entity’s finances…. and whether the mission of the entity furthers the policy of the United States… Examining the organization and function of the Federal Reserve Banks, and applying the relevant factors, we conclude that the Reserve Banks are not federal instrumentalities for purposes of the FTCA, but are independent, privately owned and locally controlled corporations.

Each Federal Reserve Bank is a separate corporation owned by commercial banks in its region. The stockholding commercial banks elect two thirds of each Bank’s nine member board of directors. The remaining three directors are appointed by the Federal Reserve Board. The Federal Reserve Board regulates the Reserve Banks, but direct supervision and control of each Bank is exercised by its board of directors. 12 U.S.C. § 301. The directors enact by-laws regulating the manner of conducting general Bank business, 12 U.S.C. § 341, and appoint officers to implement and supervise daily Bank activities. These activities include collecting and clearing checks, making advances to private and commercial entities, holding reserves for member banks, discounting the notes of member banks, and buying and selling securities on the open market. See 12 U.S.C. §§ 341 [\*\*5] 361….

It is evident from the legislative history of the Federal Reserve Act that Congress did not intend to give the federal government direction over the daily operation of the Reserve Banks: It is proposed that the Government shall retain sufficient power over the reserve banks to enable it to exercise a direct authority when necessary to do so…. In other words, the reserve-bank plan retains to the Government power over the exercise of the broader banking functions, while it leaves to individuals and privately owned institutions the actual direction of routine…[Note: neither the Act, nor this court explained how that is done] the Federal Reserve Banks, though heavily regulated, are locally controlled by their member banks. Unlike typical federal agencies, each bank is empowered to hire and fire employees at will. Bank employees do not participate in the Civil Service Retirement System. They are covered by worker’s compensation insurance, purchased by the Bank, rather than the Federal Employees Compensation Act. Employees traveling on Bank business are not subject to federal travel regulations and do not receive government [\*\*7] employee discounts on lodging and services.

The Banks are listed neither as “wholly owned” government corporations under 31 U.S.C. § 846 nor as “mixed ownership” corporations under 31 U.S.C. § 856, … a factor considered in Pearl v. United States, 230 F.2d 243 (10th Cir. 1956), which held that the Civil Air Patrol is not a federal agency under the Act. … Additionally, Reserve Banks, as privately owned entities, receive no appropriated funds from Congress. …The Reserve Banks have properly been held to be federal instrumentalities for some purposes….The Reserve Banks are deemed to [\*\*10] be federal instrumentalities for purposes of immunity from state taxation…. The Reserve Banks, which further the nation’s fiscal policy, clearly perform an important governmental function….Performance of an important governmental function, however, [\*\*11] is but a single factor and not determinative in tort claims actions…. Brink’s Inc. v. Board of Governors of the Federal Reserve System, 466 F. Supp. 116 (D.D.C.1979), held that a Federal Reserve Bank is a federal [\*\*12] instrumentality for purposes of the Service Contract Act, 41 U.S.C. § 351. … For these reasons we hold that the Reserve Banks are not federal agencies for purposes of the Federal Tort Claims Act and we affirm the judgment of the district court. [end of excerpts]

Is the Fed Operating in the Public Interest and Promoting Governmental Policy?

Short answer: No.

Some Details:

Macroeconomic policy goals are generally agreed to include: full employment, stable prices, satisfactory balance of payments; and sustainable economic growth.
A) The Full Employment Laws

Last April at a Levi Institute April conference (Bard College), Fed Governor Donald L. Kohn gave his luncheon talk, and nobody had a question for him (economists seem afraid of Fed officials) so I stood up and asked “Whatever happened to the Fed’s full employment directive?” (Well that got a rise out of Jamie Galbraith, who was sitting at the next table!) Gov. Kohn’s answer (paraphrasing) was “Yes we consider that, but we also consider price stability.”

Price stability is the economists mantra for tight money policies, that put a special strain on the barely employed. The important employment question especially indicates how the Fed does not implement Governmental policy. Two laws were passed by Congress on this and both are being effectively ignored by the Fed:

The 1946 Employment Act directed policy makers to pursue policies promoting full employment. This apparently was not enough. The Humphrey-Hawkins Act had to be passed in 1978 requiring monetary policymakers to pursue full employment and non-inflationary economic growth.

And what has been the result? Games are played with the unemployment statistics. Unemployment is grossly underestimated by ignoring those whose unemployment benefits have run out; by not counting those who have given up looking, or who have accepted jobs requiring only a small part of their qualifications at low wages, or who have accepted part time work in desperation. The Fed has done little or nothing to gain and publicize an accurate estimate of unemployment in America.

A case could probably be made that the Fed Board is flaunting the Humphrey-Hawkins Law.

There have been unsuccessful attempts through former Senator Mack of Florida and Congressman Saxton of New Jersey to promote legislation which would render the employment question moot, by making “price stability” the Fed’s priority. That the “full employment” language is considered an annoyance is indicative of the Fed’s political bias against middle class Americans.

Several additional societal/governmental problems with direct connection to monetary policy follow below. Taken individually, they might leave room for question, or even be characterized as “anecdotal,” Greenspan’s favorite description for inconvenient facts; but when seen in their entirety they demonstrate to reasonable minds that the Fed has not been operating in the public interest, except incidentally. The Fed has been promoting, or at least supporting plutocracy – the rule by wealth. (The connection between the Fed’s monetary policy, and governments funding abilities should be fairly clear, but just in case, we are writing a longer explanation that does connect those dots.)

When a long string of events and factors evinces a particular design or motivation behind them, we should draw the proper inference, just as the American Declaration of Independence did. In the Fed’s case we infer that a form of class warfare has been an inextricable part of its make up from its beginning. It’s not really hidden now. Billionaire speculator Warren Buffet recently remarked “If there is a class war, my class has won.”  Buffet was being facetious. He would not characterize the destruction of the most vulnerable among us and their children, as “winning.” He would probably join with me in calling it cannibalism, and predicting that indigestion is sure to follow.

This warfare is not all the Fed’s fault, a large part of the warfare is inherent in the present day make up, definitions and assumptions of economics itself. But the single most decisive factor in that wealth concentrating “victory” has been the privately controlled monetary system.
B) The appalling condition of America’s crucial infrastructure

The American Society of Civil Engineers gives our infrastructure an overall “D” rating, and predicts it will fall to D- soon. They tell us it will cost $1.6 trillion to bring it up to safe levels. The education sector already receives a failing F grade! This represents an unanswerable indictment of the present monetary system as either unwilling or unable to handle these crucial pillars of our society.
C) The growing concentration of wealth

Under 1% of the population is claiming ownership to almost 50% of the wealth. This spells disaster for our democracy unless quickly corrected. Private control of the money system is the most powerful engine continuing this destructive concentration process. It has become the primary tool of class warfare. I’ve only heard from one Fed official, the President of one of the regional Federal Reserve banks, who seemed to care; but in a private conversation. Yet hearing that from her was the one human signal I’ve encountered from the Fed in all the years I’ve watched it.
D) The previous Chairman, media darling Alan Greenspan Promoted Warfare and Bad Tax Cuts

Greenspan promoted the dual disasters of de-funding government through tax cuts to the super-rich, and paving the road to war in Iraq. Who can defend these “errors?” In effect they became “Fed policy” for our country.

E) Health care and education

Some figures say 45 million of us are without health insurance. Other estimates place it much higher. Then there are all those who think they are insured, but will find out otherwise when a health problem does strike. Regarding education, just the physical plant is graded F (failing) by our engineers. Is that American public policy? Or is it a financial system gone amuk?
F) The Real Estate Bubble

This is a double negative for the Fed. Counter to their professed price stability goal, they created massive inflation in housing costs, since about 70% of all Fed money creation goes into real estate loans. Then they look at soaring house prices and say “Aren’t we wise – the collateral we loaned on is worth much more than we allowed” – instead of saying “look at what our loans are doing to the real estate market – putting it further out of reach for too many.” (And now we see where this has led, in the banking debacle misnamed the “sub prime” mortgage crisis).

G) Stock market bubbles

Past pandering of Greenspan’s Fed to the financial sectors led to stock market bubbles, still being unwound. Exclamations of “irrational exuberance” was just talk, when he had the power to act on margin requirements, for example, but did nothing.

H) Attempts to Remove the Estate Tax on the Super Wealthy

Predictably, we heard nothing from Fed officials on why this would be one of the worst fiscal acts to take against America.

I) Worker Earnings Dropping since 1973

Since when is it U.S. public policy to pressurize workers incomes? In effect the Fed has placed the working sector into a form of deflation, while at the same time running a grand inflation in property values (until the inevitable collapse!).
J) Child mortality

Believe it or not, the U.S. ties for the worst ranking among all “developed” nations, by recent U.N. Figures.
K) And We Haven’t Looked at New Orleans Yet

Instead of our government being able to spend the $12 billion to repair levees and protect a key port city, we’re going to spend at least $400 billion to repair the damage. This too should be laid at the Fed’s doorstep, including the thousands of unnecessary deaths of our people. The Fed facilitated that well publicized maniac who wants to make our government small enough so that he can drown it in a bathtub.
L) Nuclear Weapons face off

We continue to be in an ever more dangerous face off with the Russians involving potentially thousands of nuclear detonations on our land. Just a few of these would end our civilization. When one examines the control of the monetary system, it’s not just about money. It is about the mis-direction of humanity. Money plays such a large role in that process that this nuclear stalemate too must be laid in part at the Feds door. Not entirely, because the Soviet Union had a hand in it too.
M) The Balance of Payments Fiasco

Shipping American jobs overseas has led to an imbalance of payments that has benefited financiers, but devastated working people. Where has the Fed ever issued a warning about this process?
N) And Now the Inflation

These misdirected monetary policies are finally taking a toll on inflation. The CRB Price Index has reached 409 decisively surpassing its former all time high of 338 reached in 1980, a year of surging metals prices, and a near 20% prime rate! But with much of the work force experiencing deflation in their earnings, it is a nightmare that they are now facing real inflation in their daily expenditures, for example for fuel and electricity.

O)  More to come!

P) etc

Q) etc

R) etc

Foreign Influence Through the Bank for International Settlements (BIS)

We’ll examine this important question in a continuation of the discussion in the future articles.

The Effect of Ambiguity

Ambiguity of control has resulted in the monetary power being misused. It has allowed great power to be wielded without responsibility. No amount of false PR will change that.

Conclusions and Solution:

The money power vested in Congress by the Constitution has been improperly delegated to private interests without sufficient public interest benefit, if any. Congress must resume the power vested in it. Had such delegation of power been shown to work in the public interest, one could consider maintaining or adjusting the present system. But look what it has done. This calls for a major shifting of how our money system operates and is controlled. Anything less, with minor benefits that merely alleviate the problems temporarily, will allow the destructive process to eventually resume.

The ambiguity must cease.

The American Monetary Institute has been working on comprehensive legislation called The American Monetary Act, to remedy this problem at its root, summarized in our brief statement, The Need for Monetary Reform and presented in full at our web site [http://www.monetary.org](http://www.monetary.org/)

This Act puts into legal terminology the reform proposal put forward in Chapter 24 of The Lost Science of Money book, by Stephen Zarlenga.
(available at <http://www.monetary.org/lostscienceofmoney.html>). Chapters 1 thru 23 give the historical background and case studies on which the reforms are based.

We realize that this Act has its best chance of passage under emergency conditions. The idea is to have it ready and to inform enough citizens and lawmakers around the country about it.

At the same time, it is necessary to begin action now and there is a “small step” called the Monetary Transparency Act, attached below. It starts the process of making the Fed more accountable to the Congress, by requiring the compilation of certain statistics which are otherwise difficult to get. These are numbers which almost automatically point the way toward better public policy decisions.

Please be assured of our desire to provide whatever assistance we can in helping create a monetary system for America that is in harmony with our best possibilities as a nation. That’s an explicit part of our 501c3 mission statement. Those of you who really want to help in this process should read The Lost Science of Money, and consider makng a donation to the American Monetary Institute. See [http://www.monetary.org](http://www.monetary.org/)

Sincerely,

Stephen Zarlenga
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