

GAO Highlights

Highlights of [GAO-17-243](#), a report to the Chairman, Committee on Financial Services, House of Representatives

Why GAO Did This Study

Member banks of the Federal Reserve must purchase stock in their regional Reserve Bank, but historically received a 6 percent dividend annually on paid-in stock. A provision of the 2015 FAST Act modified the dividend rate formula for 85 larger member banks—and currently reduces the amount these banks receive. The FAST Act also capped the surplus capital the Reserve Banks could hold and directed that any excess be transferred to Treasury's general fund. Congress offset payments into the Highway Trust Fund by, among other things, instituting the Reserve Bank surplus account cap.

GAO was asked to report on the effects of these changes and the policy implications of modifying the stock ownership requirement. Among its objectives, this report (1) examines the effects of capping the Reserve Banks' aggregate surplus account and reducing the Reserve Bank stock dividend rate, and (2) evaluates the potential policy implications of modifying the stock ownership requirement for member banks under three scenarios.

GAO reviewed legislative history and relevant literature about the Federal Reserve, prior GAO reports, and interviewed academics and current and former officials of the Board of Governors, Reserve Bank, other banking regulators, and industry associations. In addition, GAO conducted structured interviews with 17 commercial banks, selected based on bank size and regulator.

GAO makes no recommendations in this report. GAO requested comments from the banking regulators and Treasury, but none were provided.

View [GAO-17-243](#). For more information, contact Lawrence L. Evans, Jr., at (202) 512-8678 or evansl@gao.gov

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FEDERAL RESERVE SYSTEM

Potential Implications of Modifying the Capital Surplus Account and Stock Ownership Requirement

What GAO Found

According to Federal Reserve System (Federal Reserve) officials, capping the surplus account had little effect on Federal Reserve operations, and GAO found that modifying the stock dividend rate formula had no immediate effect on membership. Reserve Banks fund operations, pay dividends to member banks, and maintain a surplus account before remitting excess funds to the Department of the Treasury (Treasury). Whether the transfers to Treasury's General Fund in the Fixing America's Surface Transportation Act (FAST Act) when the act also funds specific projects should be viewed any differently than the recurring transfers of Reserve Bank earnings to Treasury is debatable. Some stakeholders raised concerns about setting a precedent—future transfers could affect the Federal Reserve's independence and, consequently, autonomy in monetary policymaking. Dividend payments to 85 banks decreased by nearly two-thirds (first half of 2016 over first half of 2015), but GAO found no shifts in Reserve Bank membership as of December 2016. Some member banks affected by the rate change told GAO they had a few concerns with it and some said they might try to recoup the lost revenue, but none indicated they would drop membership.

Assuming that the policy goals—*independence, balance of power, and geographical diversity*—reflected in the original private-public Federal Reserve structure remain important, the implications of modifying the stock ownership requirement and therefore the Federal Reserve structure could be considerable. The scenarios discussed in this report are illustrative and do not represent all the ways in which the Federal Reserve structure might be altered. Also, the discussion of effects is limited because exact replacement structures are unknown. Retiring the stock could result in changes to the existing corporate structure of the 12 Reserve Banks. These changes could

- diminish Reserve Bank autonomy in relation to the Board of Governors of the Federal Reserve System (Board of Governors) by removing or changing Reserve Banks' boards of directors, which could limit the diversity of economic viewpoints in monetary policy discussions and centralize monetary policy decision making in the hands of the Board of Governors,
- eliminate the private corporate characteristics of Reserve Banks and convert them to government entities (such as field offices of the Board of Governors), which could lead to less private sector involvement and reduced financial independence of the Federal Reserve, and
- remove the authority the Reserve Banks currently have to conduct activities critical to the Federal Reserve, such as executing monetary policy through open market operations and those related to the Reserve Banks' role as fiscal agents for the federal government.

Making stock ownership voluntary could increase fluctuations in outstanding shares, affecting Federal Reserve governance and complicating the Reserve Banks' processes for managing their balance sheets. While modifying the stock ownership requirement could give member banks greater control of the capital tied to the stock, member and nonmember banks with which GAO spoke indicated that they likely would not change their membership in response to any modifications discussed in this report.