

**THE FEDERAL RESERVE SYSTEM AND THE CONSTITUTION**  
**Remarks by Robert P. Forrestal, President**  
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**to the Staff of the Atlanta Fed**  
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Good Afternoon! It's a pleasure any time I have the opportunity to talk to our entire staff together, and it's particularly meaningful to meet with you today on the 200th anniversary of the signing of the United States Constitution. I'd like to talk with you a bit about the Federal Reserve System as an outgrowth of the process set in motion by the signing of the Constitution. This process is captured in the phrase which opens the Preamble and gives the first reason for establishing the Constitution. Those words are, "We, the people of the United States, in order to form a more perfect union. . . ." They show that the intention of the Constitution was to provide a vehicle for moving from the imperfect form of government provided by the Articles of Confederation, where states were often in conflict with one another and with the weak central government, to a more thoroughly integrated mode of cooperative action. This was projected to be a "more perfect union," but, significantly, not the perfect and final phase of development. Indeed, the great virtue of the Constitution is that although it was signed 200 years ago, it provides the tools for our system of government to modify its approach to problem-solving as new conditions emerge or popular beliefs are transformed over time. Thus the desire to form a more perfect union is present in every law passed by the Congress, every executive action taken by the President, and every decision of the Supreme Court.

The Federal Reserve System is the most recent in our country's efforts to form a more perfect union through the workings of a central bank which would serve the economic and financial needs of the entire nation. It is the third such institution we have had, preceded by the First and Second Banks of the United States. The First Bank of the United States came into existence in 1791 under the guidance of Alexander Hamilton,

first Secretary of the Treasury. From the very beginning, there were attacks from opponents like Thomas Jefferson, who considered the establishment of a central bank beyond the Constitutional powers reserved for Congress, and despite the excellent record of the Bank, its charter was not renewed in 1811. The economic disruptions that followed, particularly in the wake of the War of 1812, offered vivid proof of the value of such an institution, however, and the Second Bank was chartered in 1816. Again powerful voices were raised against the constitutionality of the central bank, this time in the formidable person of Andrew Jackson, and the Second Bank's charter lapsed in 1836.

It is true that the Constitution nowhere gives explicit authority to form a central bank. However, as Hamilton long ago pointed out to Jefferson, the last clause of Article I, Section 8 authorizes Congress to do whatever is necessary and proper to carry out its enumerated powers. That clause reads, "The Congress shall have power to make all laws which shall be necessary and proper for carrying into execution the foregoing powers," and those foregoing powers under Section 8 include the power "to coin money, and regulate the value thereof," and, more importantly from a historical perspective, the power to collect taxes, to borrow money, to regulate interstate commerce, to provide for the common defense, and to declare war. Thus Hamilton reasoned that it would be quite proper for Congress to create a central bank to carry out its enumerated powers. Then in 1819, in one of the most famous early Supreme Court cases, McCulloch versus Maryland, Chief Justice John Marshall upheld the right of Congress to create a national bank as one of its "implied powers." This decision not only set a precedent for later cases involving the validity of the central bank through our own day, but it also became the pivotal case in clarifying the interpretation of the Tenth Amendment to the Constitution.

The first ten amendments are, of course, the Bill of Rights, and the tenth of these

reads, "The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people." This is a most interesting addition to the Bill of Rights, since its intention was not to add anything to the Constitution itself, unlike, say, the First Amendment which guarantees freedom of the press or the seventh, which ensures the right to trial by jury. Instead, the Tenth Amendment confirms the understanding of the founding fathers that the powers of the central government were to be limited. The decision in **McCulloch v. Maryland** clarified the Tenth Amendment by establishing that Congress was not restricted by the Tenth Amendment from actions like the formation of a national bank because, in Justice Marshall's opinion, Congress might employ whatever powers are "convenient and useful" in carrying out powers delegated by the people to the national government. Marshall's decision therefore set forth a broader view of the federal government's authority.

Congress's authority in this area is once again at issue in a current Constitutional challenge to the Federal Reserve System. Senator John Melcher of Montana is contending in a suit before the United States Court of Appeals in Washington, D.C., that the Federal Open Market Committee--the FOMC--is unconstitutionally constituted because it determines the monetary policy of the entire nation, yet several of its members--the Reserve Bank Presidents--are not officers of the United States. As you probably know, the voting members of the FOMC are the Board of Governors, the president of the New York Fed, and 4 other district presidents who serve on a rotating basis. Melcher objects to this arrangement because only the Governors are appointed by the President and confirmed by the Senate. Reserve bank presidents are appointed by the District Boards of Directors, with the approval of the Board of Governors. Melcher would prefer to see monetary policy entirely as the business of United States officers, without the direct participation of what he views as essentially "private" district banks.

Melcher's argument rests on the question of whether Congress could properly establish an organization with both public and private elements, like the Fed, to serve the public interest. I am optimistic that the question will be decided in the affirmative on the basis of McCulloch v. Maryland and many other cases and precedents important to our form of government. It is worthwhile to go back beyond Justice Marshall, however, and review the intention of the Framers of the Constitution as seen in the debate over the First Bank of the United States. In that controversy Alexander Hamilton was most insistent that the central bank should feature private participation with government oversight. Hamilton considered it essential that the First Bank be (and I quote) "under the guidance of individual interest, not a public policy." Although an advocate of strong federal government, he feared that if government control over the amount of money in the economy were not tempered by the market experience of bankers and business leaders, the temptation to pump up the economy for purely political ends would be too much to withstand. In his words, "What government ever uniformly consulted its true interest in opposition to the temptations of money exigencies? What nation was ever blessed with a constant succession of upright and wise administrators?" In Hamilton's view, a system of checks and balances between public and private interests was critical to the effectiveness of a central bank. Agreement that this arrangement was in keeping with the Constitution is underscored by the fact that all but one of the Senate committee members who reported favorably on the creation of the First Bank of the United States had been members of the Constitutional Convention.

The commitment to the concept of a central bank independent of daily government control is preserved in our present Federal Reserve System. Ours is a central bank that is unique among the world's central banks for its degree of independence in formulating monetary policy. Nevertheless, when the FOMC was formed in 1933 and strengthened in

1935, those acts represented a tilt toward government control of monetary policy because the Board of Governors--whose members are appointed by the President and confirmed by the Senate--has seven members on the FOMC. This may be contrasted with the Reserve Bank presidents--the private element on the FOMC--who make up only five of the members of the FOMC. Unlike Senator Melcher, we believe it is important for the private element of the Federal Reserve System to continue to have a full voice in FOMC deliberations.

When I participate in FOMC meetings every six weeks, I bring the special economic concerns and problems of the six states in our district to the attention of other monetary policymakers. I gather information from around the District through talks with business and labor leaders, bankers, farmers, educators--people from all walks of life. I have the benefit of our network of 44 Directors, all of whom provide valuable input on their own areas and businesses, as well as the thoughts of our staff of economists who sort out and interpret the significant facts from a plethora of regional and national data. Even though I don't vote this year, my views and those of every district president are given equal attention in the process of deciding on the one course of action we will take on behalf of all Americans.

Just last week, at the dedication of our new building in Jacksonville, Chairman Greenspan commented on the valuable contribution of the directors, who enable us to know what is going on, what is happening, at the local level.

In conclusion, it is very interesting to me, and very surprising, that, on the 200th anniversary of our Constitution and in the 74th year of our Federal Reserve System, we are having Constitutional challenges to the structure of the Federal Reserve System. That shows that our Constitution lives, shaping our lives on a daily basis.

The challenges to the Constitution and the challenges before the Federal Reserve System never cease. And that why it's important that you and I are always working to preserve the integrity of the System, and the efficiency of the System. It's hard to attack a shining light.

The Constitution has served us well, and I am delighted to be here with you to celebrate its 200th birthday. The Declaration of Independence says that: "We hold these truths to be self-evident, that all men are created equal, that they are endowed by their Creator with certain unalienable Rights, and that among these are Life, Liberty, and the pursuit of Happiness, that to secure these rights governments are instituted among Men..." I don't know of any document that could have served these ends better than has our Constitution.