

# Opening the Temple

An Essay by President and CEO  
John C. Williams



FEDERAL RESERVE BANK OF SAN FRANCISCO  
2011 ANNUAL REPORT

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*By President and CEO John C. Williams*

**T**wenty-five years ago, a popular book about the Federal Reserve carried the provocative title *Secrets of the Temple*. The Federal Reserve described in that book was secretive, tight-lipped, and remote. Its deliberations were shielded from scrutiny. It chafed at Congressional attempts to cast sunlight on its operations. And its policy decisions were not even announced, let alone explained.

A fundamental shift has taken place in the years since then. Today's Fed has become much more open and transparent. Our websites contain detailed information about our policies and programs, our governance structure, and our code of ethics. We've also made far-reaching changes in how we communicate our monetary policy decisions. For example, after every policy meeting, we release a statement explaining what we've done and why we've done it. We publish detailed minutes just three weeks after we meet. And, last year, Chairman Bernanke began holding regular press conferences.

The Fed's move out of the shadows has been at times slow and hasn't always been voluntary. It's fair to say that, in many ways, a clamor from Congress, the media, and the public initially forced the doors open. Nor has it always been comfortable, for example, to see our internal deliberations and disagreements laid bare.

But the fact is that this greater openness is genuine, it's positive, and it's irreversible. Inside the Fed, a consensus has developed on the necessity and value of greater disclosure, accountability, and candor, a view that has taken hold strongly under the leadership of Chairman Bernanke. Transparency "not only helps make central banks more accountable, it also increases the effectiveness of policy," the Chairman said in 2010. When the public better understands what the Fed is trying to do, uncertainty about its policies is reduced, and households and businesses are able to make spending and investment decisions with greater confidence.

More fundamentally, in a democratic society, an institution that performs functions as vital as the Federal Reserve must operate in the public eye as much as possible. What we do at the Fed is not always easy for the public to understand. Clear communication and greater openness are essential to promote understanding, counter misinformation, and earn public trust and support.

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This is all the more true because of the Fed's special status. Congress chartered the Federal Reserve Board of Governors in Washington, D.C., and the 12 Reserve Banks, including the San Francisco Fed, to carry out important public policy functions. Notable among those functions is setting the nation's monetary policy. Congress granted us a large measure of independence in setting monetary policy so we wouldn't be subject to the whims of short-term political pressures, and our decisions would be based solely on what is good for the country. This independence gives us a rare and privileged status among agencies charged with a public purpose. However, with this privilege comes a great responsibility: to operate for the public good, to be accountable to the public, to hold ourselves to the highest ethical standards, and to be open to criticism.

I would be among the first to argue that the steps the Fed already has taken toward transparency are far-reaching. In many ways, they amount to a cultural regime change. But I believe we must strive to find ways to further earn the trust and understanding of the American people. For example, we can do a better job of explaining what our mission is, how we're structured, and why we do what we do. That also means making clear what the Fed does not control, such as tax and spending decisions. We can also do better at showing how the Federal Reserve affects the everyday lives of people across the country. And, we can make increasing use of new technologies, such as social media, to encourage real dialog between the Fed and people from all walks of life.

It's worthwhile examining where we've made progress and where we still have room for improvement if we are to be exemplary in the area of transparency. So let me review our accomplishments and our remaining challenges in three areas: monetary policy, financial stability, and governance.

## Monetary policy

Monetary policy is a core area of responsibility for the Fed. Our actions to set interest rates and influence credit conditions are critical factors affecting the levels of inflation, employment, and overall economic activity. The past two decades have seen a steady progression in the quality and quantity of information the Fed makes public about its monetary policy decisions.

It was just 18 years ago, in 1994, that our monetary policy body, the Federal Open Market Committee (FOMC), first began releasing statements following its meetings describing its policy decision. Before then, financial markets were expected to figure out what we decided by watching the movements of the federal funds rate, the key short-term interest rate we control. The statement issued on February 4, 1994, said, "the Federal Open Market Committee decided to increase slightly the degree of pressure on reserve positions. The action is expected to be associated with a small increase in short-term money market interest rates. The decision was taken to move toward a less accommodative stance in monetary policy in order to sustain and enhance the economic expansion."

This first step toward greater transparency was hesitant. The statement actually justified its own existence, saying that a decision was made “to announce this action immediately so as to avoid any misunderstanding of the Committee’s purposes, given the fact that this is the first firming of reserve market conditions by the Committee since early 1989.” Moreover, those early statements wouldn’t win any prizes for clarity. Indeed, the FOMC statements did not explicitly spell out the Fed’s target for the federal funds rate until July 1995. Yet, despite the initial awkwardness, these statements were an important move in the right direction.

Today, the FOMC statements provide much greater clarity about why we make our policy decisions. The FOMC issues a statement immediately following every scheduled meeting. These offer a concise description of and reasons for our policy decisions, an assessment of current economic conditions and the outlook for the economy, and guidance on the possible future course of policy. In addition, the statements include the policy votes of all Committee members, with explanations of the reasons for any dissenting votes.

The Fed has greatly improved and expanded its public communication of its policy actions in other ways too. The detailed minutes we release three weeks after each scheduled meeting provide a richer description of the Committee’s views on economic conditions and the considerations underlying policy decisions than can be included in post-meeting statements. Moreover, the Fed releases transcripts of its meetings with a five-year lag. In addition, Federal Reserve Board governors and Reserve Bank presidents regularly speak before business, community, government, and academic groups. At these events, Fed speakers often take questions from the audience and hold briefings for reporters. And Board governors and staff routinely testify to Congress about Fed policies.

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In 2011, Chairman Bernanke started holding regular press conferences following policy meetings. This has proved an excellent opportunity for the Chairman to explain Federal Reserve policies and answer questions from the media. Four times a year, Federal Reserve governors and presidents now publish their three-year projections for gross domestic product, unemployment, and inflation. And, at the San Francisco Federal Reserve Bank, we publish our own economic outlook 11 times a year on our website under the name *FedViews*, a practice we started back in 1996.

In January 2012, we took two of the boldest steps toward greater transparency and openness yet, significantly broadening and deepening our openness about monetary policy. First, we released a document called “Statement of Longer-Run Goals and Policy Strategy.” This is the first time the FOMC has offered a detailed and specific explanation of how Fed policymakers interpret the mandate Congress assigned the Fed: to promote maximum employment and stable prices. Among other things, the document states

that Fed policymakers view an inflation rate of 2 percent as most consistent with our mandate. Other central banks, including those of New Zealand, Canada, Australia, and the United Kingdom, as well as the European Central Bank, had already issued similar statements, so we were behind in this important area. The statement also notes the estimates of FOMC participants that, in the long run, the normal rate of unemployment falls between 5.2 and 6 percent. The statement clarifies that the FOMC “follows a balanced approach in promoting (its goals), taking into account the magnitude of the deviations and the potentially different time horizons over which employment and inflation are projected to return to levels judged consistent with its mandate.”

Second, FOMC participants now regularly report their views about the probable course of short-term interest rates over the next few years. In essence, that’s a way for policymakers to explain what they think monetary policy should be in the years ahead. Releasing the views of FOMC participants this way should help the public understand better our policy plans and the factors that cause us to change them. This greater clarity about our thinking, in turn, improves the effectiveness of our policies in achieving our mandated goals, and enhances the accountability and transparency of our actions.

These initiatives represent almost a total turnaround from the days when the public had to guess what the Fed was doing. I am proud to say that we’ve gone from being behind the curve relative to other central banks to becoming one of the leaders in transparency, accountability, and openness about monetary policy.

## Financial stability

Since the financial crisis of 2007–2009, no area of our work has sparked more controversy than our role as guardian of financial stability. Just a few short years ago, the financial system was in crisis. After the housing bubble burst and the private financial markets teetered on the edge of a complete breakdown, the Fed, along with the Treasury Department and other U.S. agencies, intervened on a massive scale to provide emergency funding to hundreds of financial institutions. Those programs were essential in staving off a catastrophic collapse of the financial system. They helped avert economic catastrophe and unemployment comparable to the Great Depression, when a quarter of the workforce was idled. But such large-scale aid to financial institutions at a time when millions of ordinary Americans were losing their jobs or their homes made many people confused and angry.

When the stakes are as big as they were then, accountability and disclosure are more critical than ever. Events occur at a dizzying pace. The Fed’s actions can be confusing and unclear, and can easily be misinterpreted. The American people are entitled to a

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complete explanation of how the Fed uses its emergency authority and its other powers. And only by the fullest possible disclosure can we gain a measure of public understanding and support for such actions.

I would give the Fed very high marks for its financial rescue efforts. But I would give us lower marks for explaining and building support for them. For example, one myth that gained a lot of currency was that our crisis lending programs were kept secret. In fact, we publicly disclosed all our loan programs and released the amounts lent in weekly financial statements available on our website. We also posted detailed descriptions of the programs on our websites, and Chairman Bernanke testified to Congress about them on numerous occasions. The only things we didn't disclose at the time were the identities of individual borrowers and the amounts lent to them.

Such disclosures are always a dilemma for a lender of last resort in a time of panic. Naming the institutions using our emergency lending programs identifies borrowers that may be struggling to raise funds in the open market. That can intensify panic, and spur creditors and depositors to take their money out of those institutions as fast as they can. The fear of such a stigma makes it less likely that institutions will borrow from us, which could worsen the problems in the financial system. If everyone is afraid to come to the Fed because of this stigma, then our lending programs won't help. For this reason, the Fed in the past did not make public the names of our borrowers or the amounts they individually received.

This too has changed. The Dodd-Frank Act (DFA) passed by Congress in 2010 requires the Fed to release details of loans to banks and thrifts after a two-year waiting period. In addition, the DFA requires the Fed to publish detailed accounts of all its emergency lending programs put in place during the financial crisis. The Fed has done this. The law also requires the Fed to release detailed accounts of future emergency lending programs within a year of program closures. Furthermore, the DFA authorizes the Government Accountability Office (GAO), an independent arm of Congress, to perform audits of such programs. These measures represent a reasonable balance between accountability and transparency on the one hand and, on the other hand, the need to guard against panics and bank runs in the midst of a crisis.

In addition, the Fed has become more open regarding its assessments of the financial health of the largest banks in the country. Traditionally, all supervisory information about banks was kept secret. But, during the depth of the crisis, no one was sure which banks were strong and which could be on the verge of collapse. As a result, confidence in the entire banking system plummeted. In early 2009, the Fed, working with other regulatory agencies, published the results of the first stress tests of the largest banks. These tests gave the public a better understanding of the financial health of each of the largest banks, reducing uncertainty and fear. In March of this year, the Federal Reserve publicly released the results of its latest stress tests of the largest banks. Publication of the stress test results has proven to strengthen public confidence in the banking system.





## Governance

Accountability and openness cannot just be about the policy decisions we make. They must also be about how we operate as an organization. Given our special status as an independent agency with both public and private features, it's imperative that we work for the public good, and avoid both the substance and appearance of conflicts of interests. We have among the most stringent ethics rules of any public agency, as we should. Because of the sensitive nature of the work we do, we can't allow any questions to arise about our integrity. But in the past we were not as effective as we should have been at communicating these policies. This is another area of change. We have highlighted our ethics and conflict of interest policies on our websites. And we've made available the financial disclosure forms of the 12 Bank presidents, a practice the Board of Governors already followed.

High ethical standards must hold not only for employees of the Federal Reserve System, but also for the directors of the nation's 12 Federal Reserve Banks. The law that created the Fed specified that some of those directors must represent the banking industry. And, of course, supervision and regulation of that industry is one of our most important functions. We have strict rules that prohibit our directors from the banking industry from interfering with bank supervision. The Dodd-Frank Act required the GAO to review Reserve Bank governance, with special attention to the role of Reserve Bank directors. In general, the GAO found that the Reserve Banks work conscientiously to avoid director conflicts, especially in bank supervision. The GAO made four recommendations to strengthen protections against conflict and improve public disclosure. These included increasing the economic and demographic diversity of board members; spelling out clearly the responsibilities of directors in Bank bylaws; developing clear policies for allowing exceptions to our rules on board eligibility or conflict; and improving public disclosure of information on board committee and ethics policies.

The Reserve Banks are actively moving to carry out the GAO recommendations. At the San Francisco Fed, we finished putting into effect policies and practices in line with the recommendations in February 2012. Shortly after that, we went live with a new governance section of our website, which includes our bylaws and related documents. Finally, the Fed is audited. In fact, due to our special public-private organizational structure, we are audited several times over! We publish a detailed account of our balance sheet every week on Thursday. Our books are subject to a stringent reporting process and are regularly reviewed by an external auditor. And the GAO regularly examines our activities and programs.

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In sum, our moves over the past few decades to be a more open organization are essential and, in many respects, overdue. Every step we've taken toward greater openness and clearer communication has made our policies more effective and has served to enhance the Fed's accountability and transparency. This is imperative in a democratic society. We must not rest on our laurels. We have a great deal more to do. We must examine all areas of our operations to identify where we need to improve, and we need to move forward with resolution and conviction.

Greater openness is not always easy. Transparency also means recognizing that questions and constructive criticism help us do our job better. This may at times be uncomfortable, but it spurs us to consider our decisions with an open mind, an essential first step in making better decisions in the future. It's clear that there's much to gain and little to lose as the Fed becomes more open and accountable. It's good public policy, it's the right policy, and it's good monetary policy.

