CAN THE FEDERAL RESERVE ADOPT AN INFLATION TARGETING REGIME UNDER THE CURRENT STATUTORY ARRANGEMENTS?

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I. INTRODUCTION

The power to create money, together with the power to levy taxes and assemble an army, has always helped define the sovereignty of a country. Central banks have been empowered to create money. Thus one of the major objectives of central banks has been recognized as removing the possibility of monetary laxity and stabilizing prices. Through rehabilitation after World War II, global prosperity in the 1960s, and the subsequent recession in the 1970s, the view also emerged that central banks should pay attention to full employment and sustainable economic growth. In the case of the United States, this was specified in the Federal Reserve Reform Act of 1977 which laid out the objectives of the Federal Reserve as achieving price stability and maximum employment, and also in the

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1 Email: hkcho@bok.or.kr
Senior Economist, The Bank of Korea, Seoul, Korea; Juris Doctor 2007, Juris Scientiae Doctor 2009, Washington University School of Law, St. Louis, Missouri, U.S.A.; Master of Business Administration, Seoul National University, Seoul, Korea; Bachelor of Business Administration, Korea University, Seoul, Korea. The views expressed in this paper do not represent official positions of the central banks including the Federal Reserve and the Bank of Korea. The author takes full responsibility for errors.


3 Sec.2A of the Act provides: “… so as to promote effectively the goals of maximum employment, stable prices, …” See 12 U.S.C. § 225a (1977).
Full Employment and Balanced Growth Act of 1978⁴ which laid out the objectives that the federal government should pursue. Meanwhile, “central banks have traditionally been involved in a myriad of activities, such as formulating appropriate financial regulations, implementing effective bank supervision, and operating or overseeing efficient payment systems, all of which help to attenuate the risks of financial instability.”⁵ It has been imperative that financial stability has also emerged as a major concern of monetary policy. In the case of the Federal Reserve, it has a statutory basis implicitly referring to financial stability as its concern.⁶

In navigating toward these policy objectives, central banks have tried to find systems on which they can depend to secure their safe navigations. Those systems are generally called monetary policy frameworks.⁷ It seems that a single system that all central

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⁴ It is often called Humphrey-Hawkins Act of 1978 after its original sponsors. See 15 U.S.C. § 3101 (1978) that provides:
“(c) The Congress further finds that an effective policy to promote full employment and … balanced growth … and reasonable price stability … be based on the development of explicit economic goals and policies involving the President, the Congress, and the Board of Governors of the Federal Reserve System ….”


⁶ The preamble of the Federal Reserve Act provides that the Federal Reserve was created “to provide for the establishment of Federal reserve banks, to furnish an elastic currency, to afford means of rediscounting commercial paper, to establish a more effective supervision of banking in the United States, and for other purposes.” This language implicitly embodied financial stability as an objective of the Federal Reserve. The references to an “elastic currency” and the “rediscounting of commercial paper” fundamentally reflected concerns about financial market liquidity, and the reference to “more effective supervision of banking” captured the desire to develop a means to avoid or mitigate banking crises. In conducting monetary policy, the Federal Reserve normally prefers to focus on its broad macro policy objectives - low inflation and sustainable output growth - and to consider financial instability implicitly through its effect on these fundamental variables. See Roger W. Ferguson, Jr., Ibid. at 6,7,13.

⁷ Frederic S. Mishkin explained on the definition of monetary policy framework as follows:
banks both support and adopt as a monetary policy framework has not been developed. Mishkin examined four basic types of monetary policy frameworks: monetary targeting, exchange rate targeting, inflation targeting, and monetary policy with an implicit but not an explicit nominal anchor.  

Monetary targeting is a policy framework in which monetary aggregates or indicators, e.g., M1 (a narrow-level concept of money), M2 (an intermediate-level concept of money), or M3 (a broad-level concept of money), are used as an intermediate target to achieve a final objective such as price stability. Monetary targeting was widely adopted in the 1970s under the impetus of monetarism. “Monetary targeting may have more usefulness in certain emerging and transition economies than in advanced industrial economies.” In the less developed economies where other channels of finance such as “interest rate channel” are relatively undeveloped, monetary targeting may be relatively

“A central feature of monetary policy strategies in all countries is the use of a nominal anchor (a nominal variable that monetary policymakers use to tie down the price level such as the inflation rate, an exchange rate, or the money supply) as an intermediate target to achieve an ultimate goal such as price stability.” Frederic S. Mishkin, The Economics of Money, Banking, and Financial Markets, 6th ed. Addison Wesley Longman (2001), at 506.


9 See Monetary Policy Department of the Bank of Korea, Transmission Mechanism and Financial Liberalization (May 2001), Undisclosed Lecture Material (prepared by the author) for the Staff of the People’s Bank of China (PBOC: China’s central bank) during a workshop held in Suzhou, China. Under the paradigm of monetarism, the EC method based on Fisher’s exchange equation (MV=PY) was employed. So the important thing in conducting monetary policy was to calculate the monetary target level (M) and hit the target by the use of monetary policy instruments.


11 It is generally recognized that monetary policy effects can be transmitted to the real economy through interest rate channel. The effectiveness of the interest rate channel works upon the responsiveness of short-and long-term market interest rates as well as financial institutions’ lending
useful. Interest rate liberalization, absent in the less developed economies, is a prerequisite for the interest rate channel to work; when the financial institutions can decide the lending and deposit rates on their own under interest rate liberalization, the effect of monetary policy can be smoothly spread to the real sector across the entire spectrum of interest rates; therefore, where interest rate channel does not work well, monetary targeting can be a useful policy framework. However, if the relationship between the monetary aggregate and the final objective proves weak, it implies that the monetary aggregate will no longer provide an adequate signal about the true stance of monetary policy.

Exchange rate targeting involves fixing the value of a nation’s currency to that of a large, low-inflation country such as the United States (called the anchor country). Under this system of exchange rate fixing, monetary policy serves to sustain the pre-determined target level of the exchange rate. This monetary policy regime can be appropriate in open economies in particular need of stabilization, in that monetary policy is subordinate to external factors under this regime by mitigating exchange rate fluctuations caused by external shocks. However, “an exchange rate target means that shocks to the anchor country are directly transmitted to the targeting country because changes in interest rates in the anchor country lead to a corresponding change in interest rates in the targeting

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12 See Andrew Crockett, Ibid.

13 See Monetary Policy Department of the Bank of Korea, Ibid.

country.”16 “Many countries moved to a free floating system amid skepticism about the sustainability of a fixed regime.”17

The rapid financial innovation and liberalization prominent in the 1980s blurred the distinctions between the monetary aggregates and destabilized the relationship between monetary aggregates and the real sector such as price or growth, and greatly reduced the effectiveness of monetary targeting. With this decline in the effectiveness of monetary aggregates, the introduction of inflation targeting as an alternative to monetary targeting came to be considered in the early 1990s. Central banks started to grope for an alternative and turned their attention to inflation targeting as a new policy framework, under which the central banks specify inflation targets and the focus of their monetary policy is placed on achieving the targets. This policy framework targets inflation itself without interposing any intermediate target such as monetary aggregates. “Since there is virtually no nominal anchor that can be relied upon other than the final objective which is inflation, the central bank should have a keen interest in how its specific actions are transmitted and perceived to the economy.”18 The central bank sets up the target interest rate (policy rate) in its operation of monetary policy instruments such as open market operations. Inflation targeting is a monetary policy framework aimed at guiding or modifying market expectations about inflation. Because the set target-inflation represents a contract between

15 See Id. at 508.
16 Id. at 509.
17 Monetary Policy Department of the Bank of Korea, Ibid.
18 Id.
the central bank and the economic agents (people) in society, it plays a role of reference in formulating inflation expectations or evaluating monetary policy. People watch the central bank’s actions to maintain or adjust their expectations while the contractual relationship lasts. The central bank tries to make people perceive its actions as it intended. Inflation targeting is a process whereby the central bank spells out its price stability goal explicitly and publicly, leading people to make decisions on their various economic behaviors using the target goal as a reference. So its highly distinctive feature is the importance of credibility. Under inflation targeting, it is important to acquire public support and confidence through effective communication and feedback. To acquire and deepen confidence in the contractual relationship, each party should know exactly what the other is doing and what the other’s true intentions are.\textsuperscript{19}

Mishkin’s fourth type of monetary policy framework, i.e., monetary policy with an implicit but not an explicit nominal anchor is called the Just-Do-It approach.\textsuperscript{20} It is seen in the case of the United States where monetary policy is being conducted without any of the above three types of monetary policy frameworks. The Just-Do-It approach Mishkin looked at employs the interest rate as an operating target so that the interest channel is also

\textsuperscript{19} Andrew Crockett pointed out four requirements for the success of an inflation targeting regime: (a) a track record of relatively low and stable inflation, which provides the credibility that enables the announcement of a target to stabilize expectations rather than act as a focus for speculative attack, (b) well-developed financial markets, which allow the authorities to influence the balance of supply and demand in the economy through indirect instruments that bring about incremental changes in monetary conditions, (c) an independent central bank that is believed by market participants to have the operational autonomy to pursue the inflation target, and (d) a supportive macroeconomic and structural environment, in which the budget remains under control and key domestic prices (especially wages) are responsive to changes in supply and demand conditions. See Andrew Crockett, \textit{Ibid.} at 224-25.

\textsuperscript{20} See Frederic S. Mishkin, \textit{The Economics of Money, Banking, and Financial Markets}, at 530-33.
important, like in inflation targeting. The Just-Do-It approach also has some of the key elements of inflation targeting. It is considered to have the advantages of this approach while some of the disadvantages may also be argued.\textsuperscript{21}

Since the early 1990s, many central banks have adopted inflation targeting as their monetary policy framework. An inflation targeting system is an institutional arrangement in which the central bank sets up an inflation target and conducts its monetary policy to achieve that target, and it thus involves “an institutional commitment to price stability as the primary, long-run goal of monetary policy and a commitment to achieve the inflation goal.”\textsuperscript{22} Even though inflation targeting has been fashionable in many countries, there have been debates as to whether to adopt the regime. It is basically because inflation targeting is related with the institutional status of central banking in the countries concerned. An inflation targeting system is often viewed as a contract between the central bank and society, which binds central banks to price stability.\textsuperscript{23} Thus adopting the regime requires social consensus about institutional framework of central banking.

The Federal Reserve has not yet adopted an inflation targeting system. But there have been debates inside and outside the Federal Reserve as to whether to adopt the regime. Even though there have been many debates from economic points of view, it is hard to find

\textsuperscript{21} See \textit{Id.}.

\textsuperscript{22} \textit{Id.} at 521.

\textsuperscript{23} This is usually compared to the story of Odysseus (Ulysses in Latin) that he tied himself to the mast so as not to be allured by the songs of the Sirens. See a relevant article, Juscelino F. Colares, \textit{Formal Legal Theory and The Surrender of Political Control over Monetary Policy: What can Ulysses’ Journey to Ithaca Teach Argentina about Appropriate Legal Form?}, Cornell International Law Journal (2003).
those from legal and institutional points of view. Monetary policy framework involves both institutional and economic approaches. In light of the institutional nature of monetary policy framework, the present paper purports to cast a legal eye on this issue. The current statutory arrangements of the Federal Reserve provides so called dual mandate, i.e., price stability and maximum employment. Can the Federal Reserve adopt an inflation targeting regime under the current statutory arrangements? The present paper tries to answer this question, albeit under bounded feasibility.

II. INSTITUTIONAL FEATURES OF THE FEDERAL RESERVE’S MONETARY POLICY FRAMEWORK

The legal mandate of the Federal Reserve is the pursuit of price stability and maximum employment, which is called dual mandate. This dual mandate mechanism arouses sharp debates on the institutional framework of the U.S. monetary policy and central bank accountability. The existence of a clear mandate in the central bank’s conduct of monetary policy “can enhance central bank accountability inasmuch as it may form an important precondition for the evaluation of its performance.”

The inclusion of more than one mandate in a central bank’s objectives without establishing a hierarchy between the mandates leaves the central bank with a large degree of discretion. “Neither the Federal

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25 See *Id.*
Reserve Act nor any other law provides for any hierarchy”\textsuperscript{26} between the mandates. “However, multiple objectives can conflict with each other and in order to strike an even balance between them judgments have to be made by the institution charged with the implementation of such objectives.”\textsuperscript{27}

The Federal Reserve’s Just-Do-It approach, which features monetary policy with an implicit but not an explicit nominal anchor,\textsuperscript{28} is seen where monetary policy is being conducted without any particular type of policy framework. Under the circumstances that the Congress gave the Federal Reserve its current objectives of monetary policy as a dual mandate, it is in a sense inevitable for the Fed to have been employing somewhat obscure monetary policy framework called Just-Do-It approach. Inflation targeting as a monetary policy framework, is well acceptable where the primary statutory objective is price stability. For example, the primary mission of the Bank of England (BOE) is the pursuit of price stability. Section 11 of Bank of England Act provides:

“In relation to monetary policy, the objectives of the Bank of England shall be – (a) to maintain price stability, and (b) subject to that, to support the economic policy of Her Majesty's Government, including its objectives for growth and employment.”

Under this statute, the BOE adopted an inflation targeting system. But in the Federal Reserve’s case under its legal mandate, it cannot bind itself only to the price stability because it should also take into account another objective of maximum employment which

\textsuperscript{26} Fabian Amtenbrink, \textit{Ibid.} at 189.

\textsuperscript{27} \textit{Id.}

\textsuperscript{28} See Frederic S. Mishkin, \textit{The Economics of Money, Banking, and Financial Markets}, at 530-33. Also see Frederic S. Mishkin, \textit{International Experiences with Different Monetary Policy Regimes}, \textit{Ibid.}
can contradict price stability at least in a short term for which the Fed should be accountable.

Inside and outside the Federal Reserve, there have been hot debates with respect to the Fed’s monetary policy framework. The focus of the arguments hovers over whether the Federal Reserve may have to choose inflation targeting. Inside the Federal Reserve, current Chairman Ben S. Bernanke supported inflation targeting preferably without changing the statutory objectives of the current dual mandate: he expressed that “although it would be important to vet these ideas [inflation targeting without changing the statutory objectives] thoroughly with the relevant Congressional committees before proceeding, I am hopeful that a change of the type I am proposing would be acceptable to Congress as being within the spirit of existing legislation.” Former Governor Laurence H. Meyer was also a strong supporter of an inflation targeting system without changing the current statute. Former Vice Chairman Donald L. Kohn mentioned that “if we moved toward setting a[n] [inflation] goal for ourselves, perhaps even if we just defined price stability, we would need to consult carefully with both houses of the Congress.” So far, even though economists’ view has been relatively much presented with respect to the policy regime change of the Federal Reserve, legislators’ view has not been clearly shown. To touch this issue in view of legitimacy, legal approach together with economic approach should be essential. After


the Federal Reserve Reform Act of 1977, the environment for the U.S. monetary policy has undergone many changes reflecting economic and institutional factors. Should a new approach in the U.S. monetary policy framework be pursued? The answer depends on the judgment on the basis of legal and economic considerations with respect to the adoption of an inflation targeting regime.

III. LEGAL PERSPECTIVES IN THE ISSUES OF THE FEDERAL RESERVE’S MONETARY POLICY FRAMEWORK

A. LEGAL STATUS OF THE FEDERAL RESERVE

1. THE CONCEPT OF ADMINISTRATIVE AGENCIES

   Under administrative law, administrative agencies are defined as units of government other than the legislature and the courts.³² “Throughout the modern era of administrative regulation, the government’s response to a public demand for action has often been to establish a new agency, or to grant new powers to an existing bureaucracy.”³³ Agencies were created in an attempt to control the anticompetitive conduct of monopolies and powerful corporations.³⁴ Agencies were also established to mobilize manpower and

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production, and to administer price controls and rationing.\footnote{See \textit{Id.}.}

“The primary reason why administrative agencies have been called upon to deal
with diverse social problems is the great flexibility of the regulatory process.”\footnote{Ernest Gellhorn, Ronald M. Levin, \textit{Ibid.} at 2.} “In
comparison to courts or legislatures or elected executive officials, administrative agencies
have several institutional strengths that equip them to deal with complex problems.”\footnote{\textit{Id.}.}

“Perhaps the most important of these strengths is specialized staffing: an agency is
authorized to hire people with whatever mix of talents, skills and experience it needs to get
the job done.”\footnote{\textit{Id.}.} “Moreover, because the agency has responsibility for a limited area of
public policy, it can develop the expertise that comes from continued exposure to a public
area.”\footnote{\textit{Id.}.}

“Agencies typically have legal power to affect the rights or duties of individuals or
entities outside the government.”\footnote{Michael Asimow, Arthur Earl Bonfield, Ronald M. Levin, \textit{Ibid.} at 1.} “Agencies administer or execute law under powers
delegated to them by statutes.”\footnote{\textit{Id.}.} “Administrative agencies may be headed by a single
official or by several officials, and may be called a department, commission, board or
another name.”\footnote{\textit{Id.}.} “Agencies are specialists.”\footnote{\textit{Id.}.} “Some specialize in a particular problem
wherever it occurs, like labor-management relations or consumer protection, while others specialize in problems arising in particular industries, like transportation or securities.”

2. CREATION OF INDEPENDENT [ADMINISTRATIVE] AGENCIES

“Most agencies are part of the executive branch of government but others are independent of the executive.”

“The Humphrey’s Executor decision” fostered the development of the so-called ‘independent agencies.’

“The issue came to a head when President Roosevelt sought to remove a chairman of the Federal Trade Commission (FTC) who was unsympathetic to some of the New Deal programs that the FTC was responsible for administering.”

“The Federal Trade Commission Act provided that FTC commissioners were to serve for a fixed term of years and that they could be removed during their term only for ‘inefficiency, neglect of duty, or malfeasance in office.”

“The President did not claim that the recalcitrant chairman was guilty of any of these offenses; he simply wanted to change the policy direction of the agency.”

43 Id.
44 Id.
45 Id.
48 Ernest Gellhorn, Ronald M. Levin, Ibid. at 55.
49 Id.
50 Id.
chairman brought suit to challenge the legality of his removal, the Supreme Court held that
the statutory removal-for-cause provision was a constitutionally proper limit on the
President’s removal power.”\footnote{Id.}

“The Federal Reserve Board, the Nuclear Regulatory Commission, the Securities
and Exchange Commission, and the Federal Communications Commission are familiar
eamples of agencies that are considered independent and thus not subject to direct
presidential control.”\footnote{Id.} “On the other hand, executive [branch] agencies whose top officers
serve at the pleasure of the President include Cabinet departments headed by a Secretary.”\footnote{Id.}
Independent agencies are usually (but not all) constituted as multi-member boards or

“Theoretically, at least, Congress creates an independent agency in the hope of
lessening political influences over its decisions; the idea is that, free of direct executive
control, the agency can perform its administrative functions impartially and regulate purely
in the public interest.”\footnote{Michael Asimow, Arthur Earl Bonfield, Ronald M. Levin, \textit{Ibid.} at 476.} “The most fundamental characteristic of an independent agency is
that its head or heads may not be removed by the [head of government], except for ‘good
cause.’”\footnote{Id.}
B. CONSTITUTIONAL ISSUES WITH RESPECT TO MONETARY POLICY FRAMEWORK

1. EXTENT OF DELEGATION AND INTELLIGIBLE PRINCIPLE

The Constitution of the United States conferred the power to create money on the U.S. Congress.\textsuperscript{57} The Congress again delegated the power on American central bank, based on the enactment\textsuperscript{58} creating the Federal Reserve. The Congress also gave the Federal Reserve its current objectives of monetary policy as a dual mandate under the Federal Reserve Reform Act of 1977.\textsuperscript{59}

With respect to the extent of delegation by the Congress to the agencies such as the Federal Reserve, the Supreme Court established the theory of intelligible principle in its landmark case of\textit{Whitman v. American Trucking Ass’ns, Inc.}, 531 U.S. 457 (2001).\textsuperscript{60} Under the theory, when Congress confers decision-making authority upon agencies, it must lay down by legislative act an intelligible principle to which the person or body authorized to act is directed to conform.\textsuperscript{61} Would it be seen that Congress has laid down an intelligible principle so that the Federal Reserve could adopt inflation targeting under the current dual

\textsuperscript{57} “The Congress shall have power … To coin Money, regulate the Value thereof, and of foreign Coin, and fix the Standard of Weights and Measures.” \textit{U.S. Const. art. I, § 8, cl. 5.}

\textsuperscript{58} Federal Reserve Act of 1913 (amended in the sections of 12 U.S.C.)

\textsuperscript{59} See supra note 3, 4.


\textsuperscript{61} See Id.
mandate regime? The answer will not be easy. It will be so particularly in that an agency cannot adopt, in its discretion, a limiting construction of the statute.62

2. INSTRUMENTALIST VIEW VERSUS FORMALIST VIEW VIS-À-VIS AGENCY EXPERTISE

Under the statutory structure that Section 2A of the Federal Reserve Act parallels price stability with maximum employment, if the Federal Reserve sets priority on price stability, it might be a limiting construction of the statue. It would be so, particularly in light of a textual interpretation of the statue under formalist view. The plain meaning of “… so as to promote effectively the goals of maximum employment, stable prices, ….” in Section 2A does not grant any priority on stable prices. This is manifest, e.g., when looking at the European Central Bank (ECB) legislation63 which provides: “[t]he primary objective of the ESCB shall be to maintain price stability.” The ECB legislation further specifies that “[w]ithout prejudice to the objective of price stability, the ESCB shall support the general economic policies.” The BOE legislation64 has the similar structure to that of the ECB’s.

Thus, under the Federal Reserve’s current statutory regime, the judgment of whether intelligible principle exists shall be important. However, it seems that the legislature did not provide any explicit clue for the existence of intelligible principle within its legislation.

62 Id.
63 Article 105(1), the Treaty establishing the European Community
64 See supra II.
Section 2A looks simple and straightforward. Only implicit existence of intelligible principle might be inferred, if any. Agency expertise and specialization could account for that. The Federal Reserve, as American central bank, has an expertise and specialization in the conduct of monetary policy. The theory of intelligible principle might be applied in a form of accepting its implicit existence: legislature might have laid down intelligible principle implicitly so that the Federal Reserve could set a priority on stable prices in the actual conduct of monetary policy. The Federal Reserve’s expertise and specialization in monetary policy could make it possible for the Fed to achieve maximum employment and stable prices in the longer time horizon, particularly in that inflation targeting is set and managed over a medium and long term period rather than a short term horizon.

In practice, many central banks pursue flexible inflation targeting that takes into account both price stability and growth/employment, rather than stick to rigid inflation targeting focusing only on price stability. Medium-term targeting system, which most inflation targeting countries are actually adopting, can make the flexible inflation targeting pretty workable. Under this flexible inflation targeting, central bank’s priority on price stability will not hurt the concern of maximum employment in the medium-term. Because time horizon for monetary policy should at least be medium-term, the expertise and specialization of the Federal Reserve could achieve the dual mandate, unless legislature’s intent is such that the dual mandate must be achieved in a short-term. In this regard, it might be presumed that legislature implicitly granted the Federal Reserve an intelligible principle that allows the Fed to adopt an inflation targeting system unless it is too rigid.
In view of formalists’ interpretation, however, this presumption of implicit legislative intent of intelligible principle might be rebutted by the conspicuous textual construction of the Federal Reserve Act. The formalists might above all argue that the spirit of separation of power between legislature and the executive branch will not allow such a flexible interpretation. Nonetheless, the instrumentalists might argue that agency expertise should allow such a flexible interpretation without which the Federal Reserve’s monetary policy cannot exert its full underlying authority with respect to its ultimate goal of achieving the sustainable economic growth. Under an inflation targeting system, the central bank specifies an inflation target and the focus of its monetary policy should be placed on achieving the target. In light of the instrumentalists’ view, an inflation targeting system could be a means of monetary policy to achieve sustainable economic growth, so the central bank can adopt the system, if it thinks it necessary, so that it could achieve its ultimate goal of monetary policy.

In terms of instrumentalists’ rationale, the objectives of monetary policy may differ over time according to the situations of respective countries. But price stability is recognized as one of the most important objectives of monetary policy under the conviction that various pursuits of monetary policy, e.g., economic growth, maximum employment, and/or financial stability, can only be achieved on the firm basis of price stability. If inflation takes place, uncertainties over the future grow to dampen long-term financial contracts and economic activities as a whole; likewise, economic efficiency declines as a result of the distorted distribution of income and resources. Consequently, from the instrumentalist view, price stability should be recognized as an instrumentality for the
successful attainment of various ultimate policy goals. In this respect, even though the textual structure of the statute sets forth dual mandate, the Federal Reserve could conduct its monetary policy focusing on achieving the inflation target set, bearing in mind the objectives of both maximum employment and stable prices.

Meanwhile, the Federal Reserve might prescribe a standard with regard to its monetary policy framework, for example, as illustrated in the ECB. On October 13, 1998, the Governing Council\(^6\) of the ECB announced a press release titled, “A stability-oriented monetary policy strategy for the ESCB,” which enumerated its monetary policy framework.\(^6\) The press release, even though not a statute,\(^6\) has worked as an official presentation of the ECB’s monetary policy framework. What if the Federal Reserve prescribes such a standard even if it might be an internal guideline? In term of the theory of intelligible principle in *Whitman v. American Trucking Ass’ns, Inc.*, the court says that “the prescription of a standard that Congress had omitted, [if any,] would itself be an exercise of the forbidden legislative authority.”\(^6\) If it is deemed that the Congress omitted

\(^6\) Decision-making body of the ECB, equivalent to the Board of Governors or the Federal Open Market Committee (FOMC) of the Federal Reserve

\(^6\) At the press release, the Governing Council announced: “Price stability shall be defined as a year-on-year increase in the Harmonized Index of Consumer Prices (HICP) for the euro area of below 2%. Price stability is to be maintained over the medium term ... Money will be assigned a prominent role. This role will be signaled by the announcement of a quantitative reference value for the growth of a broad monetary aggregate [Harmonized M3].”


\(^6\) Some countries have statutory monetary policy framework. For example, Article 6(1) of the Bank of Korea Act provides that the Bank of Korea shall set a price stability target in consultation with the Government.

\(^6\) *Whitman v. American Trucking Ass’ns, Inc.*, 531 U.S. at 473.
the standard particularly under formalist view, the Fed’s prescription of any guideline about inflation targeting would be an exercise of the forbidden legislative authority.

However, instrumentalists might argue that agency specialization and expertise provide the discretion in such a way that the agency can adopt its own guidelines to the extent that they do not hurt the legislative intent. If the Congress acknowledged the Federal Reserve’s specialization and expertise as the central bank in the field of monetary policy, it would have intended to give the Fed a broad authority over the conduct of monetary policy. Because monetary policy is a specialized area, there should be an aspect that legislature cannot but grant the central bank a broad or flexible authority reasonably needed to conduct its monetary policy. From an instrumentalist view, the Federal Reserve might also argue that an inflation targeting system in the long run will not contradict the legislative intent embedded in the dual mandate.

As such, the clue should be the existence of intelligible principle laid down, even if implicitly, by the Congress with respect to the dual mandate. If any intelligible principle could not be found in all instances, the Fed might seek proceedings to get the intelligible principle first through the conversation with the Congress.

C. RULEMAKING ISSUES WITH RESPECT TO MONETARY POLICY FRAMEWORK

1. AGENCY’S AUTHORITY ON RULEMAKING
Whether given intelligible principle or not, the Federal Reserve, as a federal agency, could have general rulemaking authority with respect to the conduct of its monetary policy, absent any clear legislative intent to withhold the authority. The subsequent issue would be whether the Federal Reserve can adopt an inflation targeting system by the appropriate agency rulemaking procedure within the current legislation.

So far, the Federal Reserve’s monetary policy framework has been Mishkin’s fourth type of monetary policy framework, i.e., monetary policy with an implicit but not an explicit nominal anchor. This has been called the Just-Do-It approach, where monetary policy is being conducted without any particular types of monetary policy frameworks such as monetary targeting, exchange rate targeting, and/or inflation targeting. This means that the Federal Reserve does not have any generally applicable rule in conducting its monetary policy. Instead, it is certainly seen that the Federal Reserve has chosen to make individualized or personalized determinations in its policymaking depending on discretionary judgment pursuant to specific circumstances. This is so because the Federal Reserve’s Just-Do-It approach is “strongly dependent on the preferences, skills, and trustworthiness of the individuals in charge of the Federal Reserve.”

Despite the potential time-inconsistency problem of such discretionary monetary policy having no explicit rule, the Federal Reserve’s policy has so far demonstrated success.

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69 See supra I.


71 *Id.* at 532.

In light of an institutional framework of monetary policy, current statutory scheme in the Federal Reserve Act might act as an underlying condition for no-explicit-rule policy, even though such a construction is presumed to be “inconsistent with democratic principles in that the central bank is not highly accountable.”\(^{73}\) But absent any clear legislative intent, the current statutory scheme may not be a shield for the Just-Do-It approach. In *American Hospital Ass’n v. NLRB*,\(^ {74}\) the court says that “even if a statutory scheme requires individualized determinations, the decision-maker has the authority to rely on rulemaking to resolve certain issues of general applicability unless Congress clearly expresses an intent to withhold that authority.”\(^ {75}\) Even if the current statutory scheme in the Federal Reserve Act requires the Federal Reserve to adopt the Just-Do-It approach, the decision-makers in the Federal Reserve could have the authority to rely on rulemaking to resolve certain monetary policy issues of general applicability unless legislature clearly expresses any intent to withhold that authority. In the ECB’s case, the language of the Treaty establishing the European Community is quite broad, giving the ECB considerable lee-way in interpreting how to define its objectives for itself.\(^ {76}\) The ECB’s Press Release of 1998 represents a form of authority on rulemaking.\(^ {77}\)


\(^{77}\) See supra note 66.
2. INFLATION TARGETING AND RULEMAKING

Inflation targeting certainly triggers important monetary policy issues of general applicability, so the decision-makers in the Federal Reserve will be able to have an authority to rely on some rulemaking with regard to the issues of adoption and operation of inflation targeting if they intend to do so. American central bank is deemed to have such authority on the ground of its expertise and specialization in monetary policy. Legislature will not ban it, absent any current statutory expression with respect to those issues.

Agencies have quasi-legislative power, absent legislature’s clear intent to ban it. Agencies’ quasi-legislative power usually takes the form of rulemaking particularly because rulemaking procedure is consistent with democratic principles. “The rulemaking procedure performs important functions.”78 “It gives notice to an entire segment of society of those controls or regimentation that is forthcoming.”79 “Failure to make full use of rulemaking power is attributable at least in part ‘to administrative inertia and reluctance to take a clear stance.’”80 “[Rulemaking] does force important issues into full public display and in that sense makes for more responsible administrative action.”81 In this light, the Federal Reserve’s rulemaking authority needs to be paid attention to with regard to its monetary policy framework issues.

79 Id.
80 NLRB v. Wyman-Gordon Co., 394 U.S. at 779.
81 Id.
It makes sense that notwithstanding the rationale for the rulemaking, agencies’ quasi-legislative authority needs to be flexible rather than rigid, so that agencies should be able to tackle flexibly their specialized tasks. “In performing its important functions, an administrative agency must be equipped to act either by general rule or by individual [determination].”[82] “To insist upon one form of action to the exclusion of the other is to exalt form over necessity.”[83] “[T]he choice made between proceeding by general rule or by individual [determination] is one that lies primarily in the informed discretion of the administrative agency.”[84]

Current Just-Do-It approach has not been represented as a form of rulemaking. The underlying reason is deemed to be the ambiguous nature of the Just-Do-It approach. The Just-Do-It approach features an individualized determination of monetary policy. It is “strongly dependent on the preferences, skills, and trustworthiness of the individuals in charge of the Federal Reserve.”[85] Thus, the Just-Do-It approach is to some degree inappropriate for a representation of the form of rulemaking.

To the contrary, an inflation targeting regime is a particular type of monetary policy framework. If the Federal Reserve intends to adopt it, rulemaking procedures will be suitable for that. The essence of inflation targeting is a contract between the central bank and people in society. In a contractual relationship between the two parties, the target

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[83] Id.
inflation binds the central bank, and people form an inflation expectation based on the target inflation. In a principal (people) – agent (the central bank) paradigm, the agent’s (central bank’s) commitment to the target inflation becomes the key reference in the principal’s (people’s) evaluation of the agent’s performance. As such, the underlying and crucial elements of inflation targeting are mutual communication, credibility, and transparency. That explains why the rulemaking procedures are appropriate in case the Federal Reserve changes its policy regime into inflation targeting.

Procedural fairness and public participation will be required in case the Federal Reserve initiates rulemaking proceedings. Section 553(c) of the Federal Administrative Procedure Act provides:

“… the agency shall give interested persons an opportunity to participate in the rulemaking through submission of written data, views, or arguments with or without opportunity for oral presentation. After consideration of the relevant matter presented, the agency shall incorporated in the rules adopted a concise general statement of their basis and purpose. ….”

Pursuant to this rulemaking procedure, the agencies could usually have “discretion” in “fashion[ing] their own rules of procedure absent constitutional constraints or extremely compelling circumstances.” See Vermont Yankee Nuclear Power Corp. v. NRDC, 435 U.S. 519, 543, 546 (1978). An agency could follow the rulemaking procedures “on the basis of its conception of how the public and private interest involved could best be served.”

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87 *Vermont Yankee Nuclear Power Corp. v. NRDC*, 435 U.S. at 544.
In light of these references, it would be desirable that the Federal Reserve seek broad consensus and discussion with the public and related parties while having discretion in the rulemaking procedures in regard to the adoption of inflation targeting. The procedural fairness together with sufficient public participation would need to be pursued in the Federal Reserve’s rulemaking procedures regarding an inflation targeting regime if any; it should be born in mind that “the very legitimacy of general policymaking performed by unelected administrators depends in no small part upon the openness, accessibility, and amenability of these officials to the needs and ideas of the public from whom their ultimate authority derives, and upon whom their commands must fall.”

In the ECB’s case, the Press Release of 1998 as a rulemaking established not only the ECB’s own definition of price stability, but also the time horizon relevant for achieving that.

3. AGENCY’S INTERPRETATION OF THE STATUTE

In reviewing agency’s interpretation of the statute which the agency has concern with, “[i]f the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress.”

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89 See Charles Goodhart, Allen Meade, Ibid. at 30.

court is whether the agency’s answer is based on a permissible construction of the statute.”

The text of Section 2A of the Federal Reserve Act is not unambiguous with respect to the issue of the Fed’s monetary policy framework. The Fed’s interpretation of the statute thus deserves deference, because the Fed is charged with the administration of the statute. The *Chevron* court says that “[i]f Congress has explicitly left a gap for the agency to fill, there is an express delegation of authority to the agency to elucidate a specific provision of the statute by regulation, [and] [s]uch legislative regulations are given controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute.” The court also says that “[s]ometimes the legislative delegation to an agency on a particular question is implicit rather than explicit, [and] [i]n such a case, a court may not substitute its own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency.” In regard to this *Chevron* test, the ABA Section of Administrative Law and Regulatory Practice tells: “[i]f the statutory meaning on the precise issue before the court is not clear, or if the statute is silent on that issue, the court is required to defer to the agency’s interpretation of the statute if that interpretation is

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92 *Id.* at 843-44.
93 *Id.* at 844.
‘reasonable’ or ‘permissible.’”94 Under *Chevron* test, “[s]tatutory ambiguity may reflect a deliberate delegation.”95

Under this approach, it is strongly presumed that the Federal Reserve Act (which is silent on the monetary policy framework issue) delegated the Fed an interpretation and subsequent rulemaking authority with respect to the monetary policy framework issue, unless the Fed’s interpretation and rulemaking are unreasonable. “Congress cannot, and does not, resolve all policy disputes when it enacts a statute … Congress leaves many policy issues open.”96 “When Congress drafts a statute that does not resolve a policy dispute that later arises under the statute, some institution must resolve that dispute.”97 The Federal Reserve could be the institution that must resolve such policy issue that the legislature left open; this could be an “institutional allocation of responsibility that is based on political accountability, a value central to the concept of democratic government.”98

D. LEGISLATIVE CONTROL ISSUES WITH RESPECT TO MONETARY POLICY FRAMEWORK

1. RESOLUTIONS BY THE LEGISLATURE

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97 *Id.*
The Congress can provide resolutions passed by one or two houses of the legislature, or by a legislative committee, without the enactment of a statute. Those resolutions can have control over the agencies’ action. Could the Federal Reserve utilize this function of legislative controls by way of resorting to the Congress’s resolution, given the Congress’s support of an inflation targeting system? Assume this is Scenario 1. Could the Federal Reserve conversely defend itself from the Congress’s resolution, if any, against the adoption of an inflation targeting system? (e.g., under the circumstances that the Congress prefers maximum employment rather than focusing on price stability) Assume this is Scenario 2. Either scenario could be a practical way that the Federal Reserve can get or clarify legislature’s intent regarding whether to adopt inflation targeting under the dual mandate regime. Article I of the U.S. Constitution provides:

“Every Order, Resolution, or Vote to which the Concurrence of the Senate and House of Representatives may be necessary (except on a question ofadjournment) shall be presented to the President of the United States; and before the Same shall take effect, shall be approved by him, or being disapproved by him, shall be repassed by two thirds of the Senate and House of Representatives, according to the Rules and Limitations prescribed in the Case of a Bill.”

With respect to the Congress’s adoption of resolutions, the Presentment Clause in the above provision represents that “lawmaking [is] a power to be shared by both Houses and the

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98 Id.


100 See Id.

101 U.S. Const. art. I, § 7, cl. 3.
President.”102 The resolutions, even though initiated by the legislature, shall be presented to the President, so the President is a nexus in addressing the legislative control issues.

2. SEPARATION OF POWER ISSUE IN AN ALTERNATIVE SCENARIO

If the legislature adopts a resolution for an inflation targeting system, which is Scenario 1, it will be clarifying the affirmative legislative intent under the dual mandate statute. If the legislature adopts, to the contrary, a resolution against the Federal Reserve’s planned (whether pronounced or not) inflation targeting, which is Scenario 2, the Presentment Clause in Article I will work. “The President’s participation in the legislative process [is] to protect the Executive Branch from Congress”103 The President’s participation in lawmaking process strikes a concern “on how to reconcile the practical need for [executive] agencies in the complex, modern world with basic principles of separation of powers and checks and balances.”104 The President’s participation in the legislative process has a rationale in that “[t]he President is a representative of the people just as the members of the Senate and of the House are, and it may be, at some times, on some subjects, that the President elected by all the people is rather more representative of them all than are the members of either body of the Legislature whose constituencies are local and not countrywide.”105

103 INS v. Chadha, 462 U.S. at 951.
As such, even in Scenario 2, the Federal Reserve will not lose the whole chance of adopting an inflation targeting regime, provided that the Federal Reserve could persuade the President who is the Chief Executive representing the whole executive branch including the central bank.

Meanwhile, “the Congressional Review Act\textsuperscript{106} requires that virtually all rules of general applicability, adopted by virtually all agencies (including independent agencies), be submitted to Congress and to the General Accounting Office (GAO) before they take effect.”\textsuperscript{107} Under the Act, “Congress can veto the rule by enacting a joint resolution of disapproval.”\textsuperscript{108} “A joint resolution is like a statute; it must be approved by both houses and signed by the President (or repassed by two-thirds of each house if the President vetoes it).”\textsuperscript{109} In case the Congress vetoes the Federal Reserve’s rule, if any, regarding an inflation targeting system, the situation will be similar to Scenario 2 due to the President’s participation in the procedure under the Congressional Review Act. This means the Federal Reserve still will not lose the whole chance of adopting an inflation targeting system.

3. CENTRAL BANK’S ROLE IN A “ZONE OF TWILIGHT”

\footnotetext{106}{5 U.S.C. § 801-08.}
\footnotetext{107}{Michael Asimow, Arthur Earl Bonfield, Ronald M. Levin, State and Federal Administrative Law, at 456.}
\footnotetext{108}{Id.}
\footnotetext{109}{Id.}
With respect to the tension between the Congress and the President, attention would need to be paid to the “zone of twilight”\textsuperscript{110} theory which makes it possible to “[take] a more flexible view of the President’s power.”\textsuperscript{111} In the “zone of twilight,” the President and the Congress “may have concurrent authority, or its distribution is uncertain.”\textsuperscript{112} “In this area, any actual test of power is likely to depend on the imperatives of events and contemporary imponderables rather than on abstract theories of law.”\textsuperscript{113} In considering the Federal Reserve’s crucial monetary policy issues such as monetary policy framework, the imperatives of events and contemporary imponderables could be the important criteria for the actual test of power between the Congress and the President.

Where the “Congress has neither authorized nor prohibited,”\textsuperscript{114} “[the] legality [might be] rooted in the President’s constitutional duty to ‘take Care that the Laws be faithfully executed.’”\textsuperscript{115}\textsuperscript{116} In a “zone of twilight,” the President’s Take Care Clause in the position of the Chief Executive representing the whole executive branch including the Federal Reserve could play a role. Where the Congress did not directly address American central bank’s monetary policy framework, and also where there is no clear delegation of


\textsuperscript{112} \textit{Id.} at 497.

\textsuperscript{113} \textit{Id.}

\textsuperscript{114} \textit{Id.} at 501.

\textsuperscript{115} \textit{U.S. Const.} art. II, § 3.

authorities on the monetary policy framework, the expertise and political accountability of the executive branch including agencies, represented by the President, may have got to come forward.

“While agencies are not directly accountable to the people, the Chief Executive is [directly accountable to the people], and it is entirely appropriate for this political branch of the Government to make such policy choices – resolving the competing interests which Congress itself either inadvertently did not resolve, or intentionally left to be resolved by the agency charged with the administration of the statute in light of everyday realities.”\(^{117}\)

Even though agencies are not directly accountable to the people, core agency heads are usually appointed by the Chief Executive together with legislature’s participation, which makes sure that unelected agency heads also have accountability to the people. Chairman and members of the Board of Governors of the Federal Reserve are appointed by the President “with the advice and consent of the Senate.”\(^{118} \text{ 119}\)

As such, the expertise, experience with good track record, and accountability of the Federal Reserve as American central bank and a core executive agency are presumed to be enough to make sure that the “zone of twilight” issue be addressed properly in terms of reforming the Federal Reserve’s monetary policy framework.

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\(^{118}\) Article II of the Constitution provides:

“the President shall nominate, and by and with the advice and consent of the Senate, shall appoint ambassadors, other public ministers and consuls, judges of the Supreme Court, and all other officers of the United States, whose appointments are not herein otherwise provided for, and which shall be established by law: but the Congress may by law vest the appointment of such inferior officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments.” U.S. Const. art. II, § 2, cl. 2.
IV. IMPLICATIONS

Central banking has some aspects of a political process. Central bank’s legal mandate and social imperatives are often in conflict. In addition, monetary policy is frequently termed a creative art rather than a routine or mechanical skill. This being the case, several dimensions should be taken into account when interpreting a particular central bank’s legal mandate. Thus, in addressing the issue of the Federal Reserve’s monetary policy framework from a legal perspective, it needs to be born in mind that, even though a clear-cut legal conclusion or solution may not be promptly visible, this is no reason to relax efforts to reach toward the building of a future oriented social consensus.

Currently the Federal Reserve has a somewhat vague monetary policy framework called the Just-Do-It approach, even though it may not be in full accord with the intention of the legislature. News reports have for some time been hinting that the Federal Reserve may be cautiously considering shifting toward a more specific type of monetary policy framework such as an inflation targeting system. Even though a particular monetary policy framework may appear on the surface as a tactical issue, this does not rule out scope for legislative interpretation and discussion of the legal points at issue. From the discussion so far, it is apparent that complex legal issues may be involved with respect to the Federal Reserve’s adoption of an inflation targeting system. In the absence of any preceding studies on this question of which I am aware, this paper sets out to examine some legal perspectives that may be assumed, albeit under bounded feasibility.

Both Federal Reserve policy-makers and Congressional legislators, as well as many members of the general public, will have concerns on this question as to whether the Federal Reserve can adopt an inflation targeting regime under the current statutory arrangements. A practical issue faced by concerned economic decision-makers is to figure out whether the Federal Reserve is pursuing a price rule or some other policy concerns.\footnote{120}{See Victor A. Canto, Arthur B. Laffer, \textit{Monetary Policy, Taxation, and International Investment Strategy} (1990), "Part One. Monetary Policy."}

“[A] commitment to use monetary policy solely for the purpose of stabilizing prices provides the basis for a successful and sustainable monetary system that will insure price stability for years to come.”\footnote{121}{Victor A. Canto, Arthur B. Laffer, \textit{Ibid}.}

If the purchasing power of a currency was literally assured indefinitely under a policy framework focusing on price stability, nearly everyone would hold the currency rather than gold or other inflation hedges.\footnote{122}{See Victor A. Canto, Arthur B. Laffer, \textit{Ibid}.}

In the real world of the economy, “[f]inancial economists are interested in anticipating movements in financial variables [such as interest rates].”\footnote{123}{Victor A. Canto, Arthur B. Laffer, \textit{Ibid}.}

Where possible, “[a]n [investment] portfolio strategy can be designed to take advantage of the anticipated changes.”\footnote{124}{Id.}

“Crucial to the strategy is the development of a framework which will anticipate changes in key monetary indicators and market expectations, and determine their potential impact on interest rates and inflation.”\footnote{125}{Id.} Market participants, for their part, would wish to see such an institutional
framework in order to anticipate what the underlying policy direction of the central bank might be and what central bank decision-makers must take into prior account. Those seeking to navigate the markets need to be aware of the ocean currents as well as foams and waves for a safe and prosperous voyage in their economic decision-making; if day-to-day or monthly decisions on monetary policy are like foams and waves on the surface of the sea, the underlying and sustainable directions of monetary policy, which are crucially influenced by the institutional framework, are like the currents in the ocean depths.

“[E]conomic performance is determined largely by the kind and quality of institutions that supports markets.”\textsuperscript{126} Markets are crucially underpinned by a monetary system,\textsuperscript{127} and central bank’s monetary policy stands in the axis of monetary system. To provide the central bank with a robust institutional framework is a mandate of society. A robust institutional framework could be a necessary condition for a robust monetary policy, even though it may not be a sufficient condition. It should not be forgotten that, despite the brilliance of the Federal Reserve, central bankers are only human and, as such, are at times subject to the songs of the Sirens, in the story of Ulysses, seeking to lure them onto the rocks of monetary laxity. It is anticipated that further studies and discussions are necessary to help build up a more robust and resilient institutional framework for the American central bank. Well thought-out institutional arrangement regarding the monetary policy framework and the relevant policy instrumentalities hold out the promise of heightened effectiveness in the conduct of monetary policy.


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