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Federal Reserve Works to Cultivate Stronger Ties to GOP

Bank's Lone Republican Governor Tries to Blunt Proposal He Says Risks Curbing Fed Independence

By Kate Davidson

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As the Federal Reserve prepares to begin raising interest rates later this year, it is readying for what may be another big challenge in 2015: the shift to a Republican-controlled Congress.

The Fed's only Republican governor, Jerome Powell, has begun making the central bank's case to the GOP, in public and private, against proposals Fed officials say could limit its independence. And the bank has hired and promoted Republicans within its Congressional Liaison Office since the November midterm elections, when the GOP won enough seats to take control of the Senate from the Democrats and expand its House majority.

It is unclear whether these efforts will overcome the perception among many Republicans that the liaison office, which lobbies for the bank's interests on Capitol Hill, has in recent years been too closely aligned with Democrats, and hasn't done enough to cultivate relationships within the GOP, according to current and former Hill staffers and financial-industry lobbyists.

"I think there's a recognition at the Fed that they need to at least make a gesture" to Republicans, said Mark Calabria, a former aide to Senate Banking Committee Chairman Richard Shelby (R., Ala.) and the director of financial-regulations studies at the Cato Institute. "Whether it changes policy or not I think is an open question."

In a speech Monday, Mr. Powell laid out his objections to GOP-backed proposals that he said would threaten Fed independence, including legislation to expand congressional oversight of the bank's interest-rate decisions. Advocates of the proposal say it would bring more transparency to policy decisions.

The so-called Audit-the-Fed bill, introduced by Sen. Rand Paul (R., Ky.), "risks inserting the Congress directly into monetary policy decision making, reversing decades of deliberate effort by the Congress to insulate the Fed from political pressure in carrying out its day-to-day duties," Mr. Powell said.

Mr. Powell, a former private-equity executive who served in the administration of George H.W. Bush, also met privately on Jan. 22 with Senate Republican chiefs of staff and staff directors.

The Fed last month hired Mike Lee, a former senior Republican economist on the Senate Banking Committee under Sen. Mike Crapo (R., Idaho), to join the Congressional Liaison Office, as well as Mark Libell, the former legislative director for retired Sen. John D. Rockefeller IV (D., W.Va.), who joined the office in December. And it promoted Jennifer Gallagher, a former aide to Sen. Judd Gregg (R., N.H.) on the Banking Committee, to the No. 2 position in the office.

The new hires are only filling existing positions. But the changes signal the Fed may be trying to shift its focus to Republicans after years of tilting toward Democrats while they controlled the Senate, said one Republican Senate aide .

The closer relationships in recent years with Democrats may have a straightforward explanation. Democrats controlled the Senate from 2007 through last year. They controlled the House, too, in 2010 when the Dodd-Frank financial overhaul law was passed, the last time the Fed faced a major challenge to its powers from Congress.

Now, GOP-backed proposals to change Fed operations that languished in the last Congress have better prospects of passage. One is the Audit-the-Fed bill. Another, a House bill, would require the bank to use a mathematical rule to guide rate decisions, which it would then have to explain to Congress. Mr. Powell said Monday there also is talk among lawmakers about proposing further curbs on the Fed's emergency lending powers.

He called all three ideas "misguided."

The Fed's first line of defense against such efforts is the Congressional Liaison Office, which coordinates communication between the bank and Congress. At its core, however, it is tasked with defending the Fed's interests on Capitol Hill. It is a delicate balance: the Fed is accountable to Congress, which sets its mandate, but it operates independently of the other branches of government.

Current and former Hill staffers noted the office is run by a Democrat, former Clinton administration official Linda Robertson, and that many of its lobbyists have worked for Democrats.

The Fed will need to maintain ties with Democrats even while reaching out to Republicans. Congress last month passed a bill with bipartisan support mandating the Fed have at least one governor with community banking experience. Fed officials had opposed the move. And several Senate Democrats say the Fed is opaque and too close to banks it regulates—charges that Fed officials dispute.