

AMERICAN BANKER

Washington shrugs off report of Chinese informants at the Fed

By Kyle Campbell

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A congressional report about Federal Reserve employees providing confidential information to the Chinese government has been met with little fanfare in Washington.

Sen. Rob Portman, R-Ohio, the ranking member on the Senate Homeland Security Committee, published the findings from his staff's two-year investigation ahead of the Fed's Federal Open Market Committee meeting last week. The release came amid soaring tensions between the U.S. and China leading up to House Speaker Nancy Pelosi's visit to Taiwan this week.

The report was laced with details about the Chinese government's nearly decadelong effort to influence policy and acquire sensitive information about the U.S. financial system — such as detaining a Fed staff member in Shanghai and coercing him into disclosing nonpublic research. It led to a burst of media coverage in the hours after its release, but little follow-up.

Despite the explosive nature of the report and involvement of China, a prime target for hawks on both sides of the aisle, Portman released the report alone and has had little support in spreading the message of his findings.

The response from Fed watchers has also been muted.

"I didn't think there was enough there to get excited about," said Norbert Michel, director of the Cato Institute's Center for Monetary and Financial Alternatives.

The report centered on Fed employees with ties to China's Thousand Talents Program, which confers money and preferred visa status to individuals who contribute to the country's academic advancements. The FBI has accused the program of engaging in "economic espionage" by directing recruits to bring privileged information back to China. Billions of dollars of trade secrets have been stolen by program affiliates, according to the FBI, much of it related to innovations in science and technology.

Portman's report is the first indication that similar efforts are being made to access key information about the U.S. financial system. Citing the Fed's own internal counterintelligence findings from 2015 and 2017, the report notes that 13 staffers were identified as having ties to Chinese recruitment programs or working with academic or governmental institutions in the country.

"I am concerned by the threat to the Fed and hope our investigation, which is based on the Fed's own documents and corresponds with assessments and recommendations made by the FBI, wakes the Fed up to the broad threat from China to our monetary policy," Portman said at the time of the report's release.

Fed Chair Jerome Powell does not share Portman's concern about Chinese infiltration of the central bank. In fact, in a response letter, Powell rejected the report's assertions that it needed to beef up its practices for securing sensitive information and screening staffers.

Powell said the central bank has "robust policies, protections and controls in place," and strong ties to federal law enforcement. In the case of the detained staffer, the individual reported the incident and the Fed informed the FBI, as the report noted. None of the individuals highlighted in the report were in violation of the Fed's rules about foreign engagements.

Powell accused the report of including out-of-context facts and speculating, noting that the Fed encourages staffers to work with international organizations and attend conferences with officials from other central banks. He added that most data the Fed analyzes is made available to the public and that which is not is tracked carefully.

"We would be concerned about any supportable allegation of wrongdoing, whatever the source," Powell wrote. "In contrast, we are deeply troubled by what we believe to be the report's unfair, unsubstantiated, and unverified insinuations about particular individual staff members."

The FBI has made numerous recommendations to the Fed about how it might keep out foreign interests and stop information theft, according to the report. So far, the Fed has only adopted one set of suggestions: in June 2021 it banned officials from receiving payments from certain countries, including China.

Kathryn Judge, a law professor at Columbia University who specializes in financial systems and regulations, said she was not surprised by the revelation that China would seek to infiltrate the Fed. She said the episode should not be viewed as an isolated incident, but rather an endemic issue that threatens all significant U.S. institutions.

"It's just a reminder that we ought not be naive when it comes to China," Judge said. "The particular type of globalization we've seen over the last few decades has been undermined and it's going to be further undermined in ways where we have to be more honest about the significance of who our friends are and who our enemies might be."

Aaron Klein, a senior fellow in economic studies at the Brookings Institution and a former Treasury official, agrees that the threat presented by China is not unique to the Fed. But, because of the Fed system's unique structure as part government agency, part private entity, he said, monitoring for such risks externally could be difficult.

Klein added it is natural for the Fed to see its standards as sufficiently robust and it is unlikely to change policies on its own.

"All institutions are incentivized to see the current situation as adequate until something shows them otherwise," he said. "I would hope that Congress would use these issues to engage in thoughtful reform, including strengthening the reach of the inspector general, and refrain from using it to take political pot shots at a central bank while it tries to handle an episode of high inflation and an economic recession."

