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MarketWatch

Republicans praise audit of Fed crisis response

Conflicts of interest remedies, further and faster audits on GOP wish list

By Ronald D. Orol, MarketWatch

WASHINGTON— Republican lawmakers led by Rep. Ron Paul of Texas on Tuesday praised a recent audit of the Federal Reserve's crisis-response emergency lending programs.

"We've made a lot of progress," said Paul, the chairman of the Domestic Monetary Policy subcommittee at a hearing on the new audit. "More people now are starting to realize that the Fed isn't independent of political independence because indirectly and some times more directly it is involved in political decisions or at least private decisions to serve some political interest."

At issue is a one-time Government Accountability Office audit of the Fed's emergency loan programs and other emergency loan programs during the financial crisis of 2008. The audit was required as part of the Dodd-Frank Act, signed into law in July, 2010. There is a follow-up report that the GAO says will be sent to Capitol Hill later this month.

WSJ's Nick Timiraos has details of a plan by which 4.5 million homeowners who faced foreclosure in 2009 and 2010 could face a review of their foreclosure procedures due to errors by banks.

In addition to praising the audit, Republicans said they wished the statute had permitted more regular audits of the Fed's policies and more expedited disclosures of which firms received assistance during the crisis.

"Would it be much of a problem if we were doing this [audit of the Fed] every year?" asked Paul.

GAO managing director Orice Brown, testifying before the committee, said the audit was an "enormous" undertaking. She noted that Dodd-Frank provides additional authority for the GAO to look at any future credit facilities the Fed may establish, one year after the termination of the lending facility. Rep. Blaine Luetkemeyer, Republican of Missouri, raised concern that the audit was completed even though some of the loans were outstanding.

“They haven’t all been paid back, but your audit authority is over with,” Luetkemeyer said.

Brown pointed out that institutions borrowing from most of the Fed’s lending programs have paid back the central bank. However, she pointed out that there are still outstanding loans associated with the lending facilities as part of the assistance provided to Bear Sterns and AIG.

Luetkemeyer also noted that the statute does not require the Fed to disclose the results of its open market operations -- purchases and sales of U.S. Treasury and federal agency securities -- until two years after they have taken place. The statute requires the release of information about Fed discount window lending and open market operations after July 21, 2010, with a two-year lag.

Chairman of the Federal Reserve Ben Bernanke

“How do you get hold of information that is pertinent and time sensitive?” asked Leutkemeyer. “A two year time frame seems almost beyond the ability to impose any controls or corrections.”

The GAO found that many employees and contractors of the New York Fed were allowed to keep investments in companies that received Fed assistance. It pointed to William Dudley, the current president of the New York Fed but at the time the head of its open-markets group, was granted a waiver to let him retain his shares in American International Group Inc. AIG -4.20% and General Electric GE -1.94% . It found that there were opportunities to limit conflicts of interest procedures and lacked guidance and documentation for some decisions.

Responding to Republican concerns about the conflicts, Brown said the GAO made a series of recommendations to the Fed seeking to strengthen their management of these conflicts. She noted that the GAO did not see a pattern of conflicts.

Also testifying at the hearing, Mark Calabria, Director of Financial Regulation Studies at the Cato Institute, pointed to provisions in the GAO audit about details describing how the central bank and New York Fed “exercised considerable discretion in designing” the lending programs and that they did so in an “ad hoc manner.”

Robert Auerbach, Professor of Public Affairs at the University of Texas told the subcommittee that ongoing audits would not infringe on the central bank’s independence.

“The Fed’s mythical flag of independence from politics, a favorite Fed mantra to avoid individual responsibility, is merely a shield intended to protect the institution from being forced to act in a more transparent fashion,” Auerbach said.

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