

# THE FED'S BIG BANK WELFARE PROGRAM: OVERSIGHT OF THE FED'S IORB REGIME

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## HEARING

BEFORE THE

COMMITTEE ON  
HOMELAND SECURITY AND  
GOVERNMENTAL AFFAIRS  
UNITED STATES SENATE  
ONE HUNDRED NINETEENTH CONGRESS

FIRST SESSION

DECEMBER 11, 2025

Available via the World Wide Web: <http://www.govinfo.gov>

Printed for the use of the  
Committee on Homeland Security and Governmental Affairs



U.S. GOVERNMENT PUBLISHING OFFICE

63–069 PDF

WASHINGTON : 2026

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## **THE FED'S BIG BANK WELFARE PROGRAM: OVERSIGHT OF THE FED'S IORB REGIME**

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**THURSDAY, DECEMBER 11, 2025**

U.S. SENATE,  
COMMITTEE ON HOMELAND SECURITY  
AND GOVERNMENTAL AFFAIRS,  
*Washington, DC.*

The Committee met, pursuant to notice, at 10:01 a.m., in room SD-342, Dirksen Senate Office Building, Hon. Rand Paul, presiding.

Present: Senators Paul [presiding], Johnson, Lankford, Scott, Hawley, Moody, Peters, Hassan, Blumenthal, and Fetterman.

### **OPENING STATEMENT OF SENATOR PAUL**

Chairman PAUL. The Federal Reserve Board (FRB) is one of the most powerful, secretive, and unaccountable institutions in U.S. history. Its insulation from oversight combined with massive coffers and strong statutory authorities makes it a uniquely troubling institution.

To give you an idea of just how powerful the Fed is, in 2018, Forbes ranked Jerome Powell, the Chairman of the Federal Reserve Board as the 11th most powerful person in the world, ahead of the prime ministers of England and France. But earnest oversight there, I think is long overdue.

Current law prohibits the Government Accountability Office (GAO) from auditing the Fed's vast monetary policy functions. The Fed's Inspector General (IG) serves at the pleasure of the Fed Board of Governors, the very institution it's supposed to hold accountable. This summer, I began investigating the Fed, and after months of stonewalling, the Fed finally produced information on one of the most significant tools of monetary policy, interest rates on reserve balances (IORB).

The interest on the reserve balances system began after the 2008 financial crisis, when the Fed aggressively purchased assets to flood the market with liquidity. This marked the beginning of a transition from the scarce resource reserves regime to an abundant reserves regime. The Fed vastly underestimated how the transition would play out.

Initial estimates put the cost of the transition at about 35 billion. As of May, 2022, these estimates increased to 2.3 trillion. Under this new regime of abundant reserves, banks would receive interest payments known as interest on reserve balances on deposits held at the accounts in the Fed. When interest rates are low and the Fed's balance sheet is small, this is a manageable regime.

Unfortunately, since 2008 both the size of the balance sheet and interest rates have increased the cost of this regime to unsustainable levels. Take the size of the Fed's balance sheet, before 2008, it was approximately five percent of gross domestic product (GDP). After the great financial crisis, it rose steadily reaching approximately 18 percent of GDP. During the Coronavirus Disease 2019 (COVID-19) pandemic, it soared to a record 35 percent of GDP in 2022.

It's since fallen to approximately 21 percent today, but remains well above historic levels. When interest rates were near zero from 2010 to 2016, the Fed to pay little in the form of interest on reserve balances. But when inflation concerns required the Fed to raise interest rates from 2016 to 2019 and again from 2022 to 2023, the interest on reserve balance rate was a primary tool to do so, requiring the Fed to increase the amounts it was paying the banks to get them to hold money at the Fed.

This led to distortions in the Federal funds markets, including periods where short term treasury yields were actually below the interest on reserve balance rates. When this happens, the Fed loses money and taxpayers underwrite the losses.

It's somewhat of a crazy notion to even imagine an organization that actually has the ability to print and create currency losing money. But the Fed has been losing money for the last couple of years. The Fed is supposed to send its profits to the Treasury. The interest on reserve balance system, though, however, has led to two years of operating losses where instead of the money going back to the treasury, the money's going to large banks in New York and large banks overseas.

The Fed is taking the Federal funds rate and most of this ends up in the largest banks in the world, both foreign and domestic. It's a double whammy for the taxpayers. Banks use your money that's sitting in a checking account to earn up to 5.4 percent interest from the Fed, the payment of which is underwritten by your tax dollars. Then you pay on average of 0.0 percent interest on your checking accounts, and they pocket the difference.

It's great for banks. Interest on reserve balance enables the Fed without any form of oversight or elections to unilaterally transfer wealth from the American taxpayer to the biggest banks on Wall Street. Interest on reserve balances have totaled hundreds of billions of dollars. Most people even don't know they exist.

Since 2013, the Fed has paid \$607 billion to both foreign and domestic banking institutions. In 2024 loan, the payments amounted to \$186 billion. This is essentially 10 percent of our deficit, so our deficit could have been reduced it by 10 percent of that money. We are going back to the treasury instead of going to private banks.

The secrecy surrounding the amounts of these payments have allowed unelected officials at the Fed to influence the American economy in ways that rival the power of elected Members of Congress. For the first time ever, the report I released this week revealed the true nature of these payments.

The data obtained from the Fed shows that the largest banks in the country made a windfall. Big names like JP Morgan Chase, Bank of America (BoA) City, Wells Fargo, and U.S. Bank raked in

tens of billions of dollars from holding their money at the Fed and essentially not loaning it to the public.

From 2013 to 2024, interest on reserve balance payments to the top five banks amounted to 136 billion, which equals 12 percent of their profits. Over 10 percent of the profit of the banks is basically being paid at no risk to these banks. They are not going out and loaning money. They are not having to judge risks of loaning it. They just park it at the Fed and are able to gather 10 percent of profit with no risk.

Money was not just flowing to Wall Street though, foreign banks also cashed in. 11 of the top 20 recipients of interest on reserve balances from 2013 to the present were foreign banks. It's kind of hard to fathom that we are using this quasi-governmental bank, the Federal Reserve to facilitate payments to foreign banks.

These funds are not exclusive to allied nations. Chinese banks alone received about 10 billion in interest on reserve balance payments. Oversight of the Fed's interest on reserve balance payments is the first step in finally auditing the Fed. But there's still much more work to be done.

My bill and the Fed's big bank bailout, would end the forcible transfer of wealth from average Americans to Wall Street institutions under the guise of interest on reserve balance payments. While my Federal Reserve Transparency Act, Audit the Fed, would also allow meaningful oversight of all functions of the Fed, which is long overdue.

If the Fed handed over this data, what is it hiding? What is the information they are still refusing to release? It was like pulling teeth to get the information we finally got from them. But I think it's high time that we do audit the Fed. Senator Peters.

#### **OPENING STATEMENT OF SENATOR PETERS<sup>1</sup>**

Senator PETERS. Thank you, Chair Paul, and thank you for each of our witnesses for being here before the Committee today. The Federal Reserve plays a critical role in implementing sound monetary policy to strengthen markets as well as the overall economy. The focus of today's hearing is on the Fed's authority to pay interest on reserve balances, which Congress created under the Financial Services Regulatory Relief Act of 2006 and directed the Fed to implement in response to the 2008 financial crisis.

Commercial banks hold cash balances at the Fed known as reserves, that play an important role in keeping financial markets functioning. The Fed pays interest on those reserves, allowing the Fed to set target interest rates that affect rates on everything, from mortgages, to car loans.

The Fed also receives interest payments from banks on the securities backing of those reserves, which the Fed then sends to the Treasury in the form of remittances. According to publicly available data in the past 16 years that the Fed has held this authority, it has actually remitted over \$900 billion to the United States Treasury even after making interest payments.

Although the last two years saw negative remittances, primarily due to the necessary responses in support of the economy during

<sup>1</sup> The prepared statement of Senator Peters appears in the Appendix on page 35.

the COVID-19 pandemic, the Fed has recently stated that it expects its negative remittances to turn positive again very soon. Repealing this authority would not save any money for the taxpayers and without this authority, the Fed would lose control of its ability to set a floor interest rate for lending.

Economists predict this would result in collapsing interest rates and much higher inflation, something we have quite enough of already. To restore rates, the Fed would need to shrink the level of reserves at an unprecedented speed and volume. Introducing volatility, comprising market resilience, and leaving banks prone to shocks.

Stability is absolutely critical. American financial markets remain the envy of the world in most ballparks due to the stability, the efficiency and liquidity provided by the Fed. If banks did not receive these payments on their reserves, they would simply buy other government securities that the government pays interest on like treasury securities, and as a result, be more prone to economic volatility.

Ultimately, this all comes back to affordability and making our economy work for small businesses and families. Economists argue that repealing this authority would disproportionately harm small and community banks and make borrowing harder for both businesses as well as consumers. Unfortunately, like so many things under President Trump, the Fed has been needlessly politicized. We are currently facing a dangerous ongoing threat to the Fed's independence. After repeatedly pressuring the Fed to lower interest rates, President Trump has tried to fire Governor Lisa Cook and has called Chair Jerome Powell to be replaced.

These actions are politically motivated and Congress should stand up for the Fed's independence and ensure that monetary policy remains insulated from political pressure. Finally, Mr. Chair, while the oversight of the Federal Reserve is certainly important, this Committee I think has not held oversight hearings on numerous topics that are actually in our jurisdiction, including the Federal Emergency Management Agency (FEMA's) failure to responding to disastrous floods in Texas, this spring, persistent cyberattacks by our adversaries against Federal information technology (IT) and critical infrastructure networks.

Or the administration's efforts on border security and drug trafficking. In fact, our colleagues in the House and the House Homeland Security Committee are actually sitting down right now as we speak with Secretary Noem across the Capitol to talk about threats posed to the homeland.

A serious topic that certainly demands the attention of this Committee, not just the house Committee. Mr. Chair, so I hope we will also prioritize hearings with administrative officials in the near future so we can fulfill that responsibility. Again, to our witnesses, thank you for being here.

Chairman PAUL. It is the practice of the Homeland Security and Governmental Affairs Committee (HSGAC) to swear in witnesses. Will each of you please stand and raise your right hand? Do you swear that the testimony you will give before this Committee will be the truth, the whole truth, and nothing but the truth, so help you, God?



[Witnesses answer in the affirmative.]

Thank you. You may be seated. Our first witness will be Norbert J. Michel, Vice President and Director of Cato's Institute Center for Monetary and Financial Alternatives.

Dr. Michel leads a team of nearly one dozen scholars that develop original policy solutions to expand freedom through improving financial markets and monetary policy. In addition to producing policy publication, his team regularly engages with policymakers on Capitol Hill. Dr. Michel, you are recognized.

**TESTIMONY OF NORBERT J. MICHEL, PH.D.,<sup>1</sup> VICE PRESIDENT  
AND DIRECTOR, CENTER FOR MONETARY AND FINANCIAL  
ALTERNATIVES, CATO INSTITUTE**

Dr. MICHEL. Good morning, Chair Paul, Ranking Member Peters, Members of the Committee, thank you for the opportunity to testify today. I am Norbert Michel, Vice President, Director of the Senate for Monetary and Financial Alternatives of the Cato Institute. The views that I expressed in this testimony are my own and should not be construed as representing any official position of the Cato Institute.

In my testimony today, I argue that it is time to wind down the Federal Reserve's balance sheet and once that wind down is complete, and the Fed's ability to pay interest on reserves. Importantly, these policy goals can be accomplished without harming the American economy. As part of its response to the 2008 financial crisis, the Federal Reserve purchased large quantities of long-term treasuries and mortgage-backed securities.

The Fed Securities holdings balloon from less than 1 trillion to four and a half trillion and on the eve of the COVID-19 pandemic remained elevated at approximately 4 trillion. Then a new round of purchases pushed this figure up to almost 9 trillion. As the first round of these purchases occurred, the public generally feared the Fed was stoking a massive inflation problem, and they were correct to be concerned.

Under a traditional monetary policy framework, Fed purchases are equivalent to expansionary monetary policy. However, during this period the Fed also changed its operating framework to one that could no longer be considered traditional. The main feature was that the Fed started paying interest on banks reserves. This new feature received much less attention than the Fed's asset purchases themselves, partly because interest rates were historically low at that time.

As many people recognize though, if and when rates eventually rose, the Fed would have to start paying large amounts of money on reserves, a move that would imperil its profitability and therefore its remittance to treasury. It would also put it in a politically difficult position.

After the post COVID-19 rise in inflation, that time finally came, the Fed's interest payments increased dramatically and the rate of increase in interest expenses closely mirror the rate of increase in the IOR rate, the rate that the Fed pays out on reserves. This latter fact was not true in the late 2010's when the Fed raised the

<sup>1</sup> The prepared statement of Dr. Michel appears in the Appendix on page 37.

IOR but kept interest payments in check because it only paid interest on excess reserves as opposed to all reserves.

A policy had changed during the pandemic. These large interest expenses resulted in the Fed's only recorded losses since 2008, and the only losses on record since the data has been available. Between 2023 and 2024, the Fed has lost nearly \$200 billion and it will likely take years of future profits to offset those losses from these past two years alone. Profits that would not usually go to treasury.

One obvious problem with this trend is that interest rates may not come down to their pre-pandemic levels, thereby failing to reduce the Fed's interest burden and allowing its financials to turn back to profit. However, regardless of the future path of interest rates, there are several other problems with the IOR framework that dictate it should be ended.

For instance, this IOR framework provides government dollars to large financial institutions at risk-free interest rates, essentially giving banks a massive government handout. The average American has no access to this risk-free investment. Next, the IOR framework leaves banks with less of an incentive to borrow from each other or lend funds to the public resulting lowered activity in private markets.

Then potentially large financial losses will also undermine the Fed's ability to support the banking sector and the U.S. government's ability to issue new debt. The losses create a potential complication for monetary policy because the Fed must increase the IOR in order to combat inflation even though every increase in the IOR increases the Fed's potential losses.

Then last and perhaps the most dangerous issue is that the IOR framework effectively divorces the Fed's monetary policy stance from the size of its balance sheet. In other words, the Fed's asset purchases which increase bank reserves are no longer automatically associated with expansionary monetary policy and inflation.

This feature increases the likelihood that the Fed will be used as a pawn of the Treasury, enabling the government to run even larger deficits and open new opportunities for political groups to pressure the Fed for direct funding, something that we have already seen start to happen. Congress should require the Fed to shrink its balance sheet in no more than 15 years, which is approximately the same amount of time it took to enlarge the balance sheet from 2008.

Faster would certainly be better. The goal should be to reduce the Fed's holdings to no more than the pre 2008 share of the commercial banking sector, which was approximately 10 percent. At that time, the Fed's authority to pay interest on reserves should be repealed. Thank you for your consideration. I am happy to answer any questions you may have.

Chairman PAUL. Our next witness is Ryan Young. Ryan is a senior economist at the Competitive Enterprise Institute. He specializes in trade, regulatory reform, antitrust policy, monetary policy, and other issues. He edited the essay collection, Adam Smith's Guide to Life, Loveliness and The Modern Economy, and his writing has appeared in USA Today, the Wall Street Journal, Politico, and dozens of other publications. Mr. Young.

**TESTIMONY OF RYAN YOUNG,<sup>1</sup> SENIOR ECONOMIST,  
COMPETITIVE ENTERPRISE INSTITUTE**

Mr. YOUNG. Chair Paul, Ranking Member Peters, distinguished Members of the Committee, thank you for holding this hearing and inviting me to testify today. My name is Ryan Young. My work focuses on monetary policy, trade policy, and regulatory policy at the Competitive Enterprise Institute, a nonpartisan public policy organization that concentrates on regulatory issues from a free market perspective.

I am pleased to speak to you today about a bipartisan goal, ending interest on reserve bank deposits. This is the practice of the Federal Reserve paying interest on account balances that other banks hold at the Fed. IORB was enacted in 2008 in response to the financial crisis. It has since proven to have few benefits and many drawbacks and it's time to end it.

The two IORB problems I wish to highlight today are cronyism and inflation. First, cronyism, the Committee's report points out that, in 2024, the Fed paid about \$180 billion in IORB to banks. While this number is likely to drop in 2025 and 2026 due to lower interest rates, it's still a bad look for the Fed.

IORB is free money for banks that don't need the help. Similar to Wall Street bailouts from past years, free IORB money encourages banks to take on risks they would otherwise avoid, and the taxpayer expense if they go bad. As we have found out the hard way several times over the years, extended excessive risk taking rarely ends well. If a recession or a financial crisis hits, IORB could be both a contributor to the problem and a prelude to more taxpayer bailouts.

The money spent on IORB repayments has other potential uses. It could have gone to the Treasury instead. \$180 billion is equivalent to about one tenth of last year's budget deficit. Savings from ending IORB could also have more than covered the Fed's 2024 operating losses of \$114 billion.

The second IORB problem I wish to discuss is inflation. IORB raises inflation risk in two ways. First, by potentially influencing the Fed's Federal fund rate decisions. Second, by influencing its open market operations policies. A high Federal funds rate already has unintended consequences such as higher interest rates on government bonds.

This makes government debt more expensive to repay, and is one reason why the political branches often pressure the Fed to lower rates. IORB creates an additional unintended consequence. The higher the Federal funds rate, the higher the Fed's Board of Governors (BoG) has to set the IORB rate. Otherwise, banks will take their money out of the Fed and try to earn a better return elsewhere. The higher the IORB rate, the more likely is the Fed to incur an operating loss.

In fact, IORB payments alone exceeded the Fed's 2023 and 2024 operating losses. The Federal Open Market Committee (FOMC) has a tough job as it is. IORB makes its job even more difficult. IORB, especially at the large scale it has reached in recent years, can po-

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<sup>1</sup>The prepared statement of Mr. Young appears in the Appendix on page 46.

tentially influence the FOMC to set interest rates lower than it would otherwise prefer, in order to save money on IORB payments.

IORB can also tempt the Fed to grow the money supply (M2) through open market operations, which can also cause higher inflation. If you or I were to buy government bonds, we would have to use our own money and take that money away from other potential uses. Unlike us, the Fed does not have to navigate that tradeoff. If it wants, it can buy government bonds with dollars that newly creates out of thin air.

This is how the Fed can directly grow the money supply. This was also the main driver of COVID-era inflation. From 2020 to 2022, the Fed added nearly \$5 trillion to its balance sheet. This roughly quadrupled its usual rate of money supply growth, and the inflation rate roughly quadrupled to match. The Fed could do something similar to fund IORB payments.

This would help it duck criticism from using IORB money to subsidize foreign and domestic banks. Rather than address its problems, the Fed could simply create more dollars in an attempt to have its cake and eat it too. This money supply growth has a tradeoff and that tradeoff is higher inflation. Fortunately, \$180 billion will do far less damage than \$5 trillion did.

But there is no need to make the FOMC's job even harder than it already is. Trial and error are essential to the public policy process. After a 17-year trial, we now know that IORB was an error. You now have the opportunity to fix it. Thank you for this opportunity. I look forward to your questions.

Chairman PAUL. Thank you. Our next witness is Brian Wesbury. He's the Chief Economist at First Trust Advisors L.P. Brian has been a member of the Academic Advisory Council of the Federal Reserve Bank of Chicago, as well as a fellow of the George W. Bush Presidential Center in Dallas. Previously, Brian served as chief economist of the Joint Economic Committee and has been ranked by the Wall Street Journal as the Nation's No. 1 economic forecaster. Mr. Wesbury.

**TESTIMONY OF BRIAN S. WESBURY,<sup>1</sup> CHIEF ECONOMIST,  
FIRST TRUST ADVISORS L.P.**

Mr. WESBURY. Thank you, Chair Paul, and Ranking Member Peters. Thank you for inviting me. Members of the Committee, I would like to submit my testimony into the record. I am going to summarize it. As I kind of go through this just in my mind because listening to all of this, your Committee and your staff has done fantastic work.

I know pulling information out of the Fed is very difficult and so I really appreciate what you have done here. You have highlighted this interest on excess reserves. I would like to say that this is pulling on this thread is like unwinding the whole sweater, the fabric of this new monetary policy.

It was started in 2008 during the great financial crisis and I believe it's supported by a myth. People believe that quantitative easing (QE) saved us during the great financial crisis and I do not believe that. I think it was a changing mark to market accounting

<sup>1</sup> The prepared statement of Mr. Wesbury appears in the Appendix on page 49.

rules that did. Nonetheless, it's lasted and so I want to think about what it really is.

The Federal Reserve, at the same time, governments during COVID and during 2008 boosted their purchases of government bonds. The government is issuing a lot of debt. The Federal Reserve is buying it. If banks were forced to buy it, they would have a different risk profile as Ryan just highlighted, then the Fed does not care about losses. As a result, the government can issue more debt at a lower rate than it would be able to if it had to sell it into the private marketplace.

What this did, in my opinion, is it allowed the government to grow bigger than it would have been able to if the Fed would not have followed this abundant reserve policy. The second thing is, it did not help stabilize the financial system. If you go back to the great financial crisis, the subprime loan losses were somewhere around \$400 or \$500 billion.

The system today, as it stands, has losses of over one and a half trillion dollars. In other words, we have tripled the amount of losses in the banking system and at the Fed today versus what existed at the beginning of the great financial crisis. The other thing that's happened is that we have tripled the money supply since 2008. The annual money supply was \$7 trillion in 2008.

Today, it's 22 trillion. Let me put that in stark terms. If you have a \$100 bill in your wallet, 67 of those dollars were created in just the last 18 years. 33 of those dollars were created in the previous 200 years. That's how much money we printed and that's why we ended up with the inflation that we have. This is what's created the unaffordability problem because people with assets, one, if you already own a home, your home grows in value. If you own equities, your equities went up.

If you do not own a home or equities, you just face higher inflation. I believe this policy has created more inequality in America than any government policies we have ever followed in our history. As a result, I think it's undermined our political dynamic. It has created haves and have nots. It has created a divide between older generations that have built up assets and younger generations that haven't.

As a result, I believe this policy has been a complete failure in our system. It's created inflation, it's created more risk, it's also created this appearance of paying private banks and foreign banks money. It has taken the risk away from the government of issuing debt into the private sector. I think it needs to be unwound and unwound completely and never allowed to come back again. Thank you very much for the time.

Senator PETERS. Our next witness, Dr. Kohn, formerly served as a member and then Vice Chair of the Federal Reserve Board of Governors from 2002 to 2010. Previously, he held several staff positions, including Secretary of the Federal Open Market Committee and Director of the Division of Monetary Affairs.

Dr. Kohn also advised Federal Reserve Chairman Ben Bernanke throughout the 2008 and 2009 financial crisis and former Chairman Alan Greenspan. He received a bachelor's degree in economics from the College of Rooster and more significantly a Ph.D. in economics from the University of Michigan. No one would question the

academic rigor of your studies at that fine institution. Dr. Kohn, welcome to the Committee. Thank you for your expertise. You may proceed with your opening remarks.

**TESTIMONY OF DONALD KOHN, PH.D.,<sup>1</sup> ROBERT V. ROOSA  
CHAIR IN INTERNATIONAL ECONOMICS AND SENIOR FEL-  
LOW, ECONOMIC STUDIES, BROOKINGS INSTITUTION**

Dr. KOHN. Thank you, Senator Peters. Thank you, Chair Paul for inviting me. In my view, the payment of interest on reserve balances serves critical public policy purposes and should be retained. IORB is required to enable the Federal Reserve to take actions to meet its legislative monetary policy mandates for maximum employment and stable prices.

When the economy and employment are weak, the Federal Reserve normally reduces its target for short term rates to stimulate spending. Twice in the past 20 years, the Fed has lowered its target to zero but recovery from recession still has been slow or uncertain. In these circumstances, to reduce longer term interest rates further to encourage spending and job creation, avoid persistent deflation, the Fed purchases longer term government securities.

Those purchases create a large volume of reserves and when it comes time to raise interest rates, inflation fighting depends on raising the IORB, which puts a floor under market interest rates. IORB also supports the Federal Reserve's ability to foster financial stability. It enables the Federal Reserve to make purchases to stabilize Treasury agency and MBS markets when they are disrupted, threatening the flow of credit to public and private borrowers.

The market seized up in late 2008 and again in the spring of 2020. Because of IORB, the Federal Reserve was able to step in, make purchases of securities to restore market functioning, assure credit flowing to businesses and households. They were able to do that without losing control of monetary policy.

IORB means the Fed can supply reserves to enhance the resilience of the banking system to unexpected adverse liquidity shocks, such as deposit runs; deposits at the Fed are the safest, most liquid assets banks can hold. IORB means that banks see reserves as a viable source of liquidity to manage risks without harming the bottom line.

With IORB, the Fed can meet their demands for this asset without sacrificing its ability to control short-term rates for monetary policy purposes. Being able to use interest bearing deposits at the Fed to manage liquidity is especially important for smaller banks.

Larger banks have access to a much wider variety of instruments to meet unexpected outflows. IORB does not result in a windfall to the banks. Banks have to fund their holdings of reserves with deposits or borrowing just as they do with other assets they hold. Banks pay interest and face other costs associated with those sources of funding.

The rate paid on reserves is very close to the rate on a range of other short-term instruments which banks and others can borrow and invest. Moreover, any individual bank can increase its holdings

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<sup>1</sup> The prepared statement of Dr. Kohn appears in the Appendix on page 55.

and reserves by raising its deposit rate to attract new funds and leaving the funds in its reserve account.

If the rate paid on reserves offered banks an excessive profit, increased competition in our market system among banks for deposits would push up bank funding costs offsetting that profit. IORB will not result in a net cost to the treasury over the long run. While a larger Fed balance sheet means the Fed is supplying more reserves to banks on which it pays interest, it also means that the Fed is holding more government securities purchase with those reserves and it earns interest on those.

Fed interest income and expense can differ significantly in some periods. This is a temporary condition. Over time the effects of a larger Fed balance sheet on interest payments to banks and interest receipts on security should be roughly offsetting. IORB and ample reserves do not crowd out consumer or business lending. Deposits are the counterpart of those reserves.

When a bank receives the deposit, it compares the risk adjusted returns on various uses of the deposit. Before IORB, a bank might compare making a loan to lending to another bank in the Federal funds market. Today, the bank compares making a loan to holding onto the deposit at the Fed. IORB is almost identical to the funds rate. So it has not altered this calculus about making loans. While not allowing the Fed to pay interest on reserve balances would have little effect on treasury income over time or bank profits, that would handicap the Fed's ability to promote economic and financial stability.

It should be left in place. If Congress wishes to raise additional taxes from banks, it should do so directly, not by forcing them to make interest free loans to the government. Thank you, Mr. Chair.

Chairman PAUL. Thank you for your testimony. I would like to enter into the record the report<sup>1</sup> produced by the Committee majority as part of this investigation. Without objection, these records will be entered into the hearing record. We will now proceed to questions where each Member will have five minutes. We will start with Senator Johnson.

#### OPENING STATEMENT OF SENATOR JOHNSON

Senator JOHNSON. Have you all read the Creature from Jekyll Island? Have you all read it? The basic premise of that is the Federal Reserves, a cartel of the big banks, right? It shouldn't be there. And to a certain extent, I find this debate very confusing. I think part of it is we shouldn't have a Federal Reserve. We should run monetary policy a different way.

I am not sure how you do that. I don't think anybody really understands monetary policy. We try things and they do not work. But hear me out. Tell me where I'm wrong. If the Fed runs a \$200 billion loss because it's paying interest on these reserves, it's basically hiding a \$200 billion loss that otherwise would be shown on our books.

Instead of a \$1.9 trillion deficit, we have \$2.1 trillion deficits. Is that basically true? We are allowing this supposedly independent agency—I don't think it's particularly independent, but it's running

<sup>1</sup> The report submitted by Senator Paul appears in the Appendix on page 61.

a \$200 billion deficit while fiscally we are running \$1.9 trillion deficit. It's a shell game. Where are we doing it now? I understand the impact potentially on inflation is it allows us to run higher deficits.

Because we are kind of hiding that interest expense. Personally, I do not think that would restrain Congress. I think we would just run a \$2.1 trillion deficit. So where am I missing this? Because I also hear the arguments from other Fed presidents that, again, if they are not paying interest on the reserves, they will just buy treasury bill anyway.

Again, that's where the government is on the hook for another \$200 billion as Mr. Kohn talked about. Industries are pretty equivalent. So, I guess, where am I wrong? Briefly, please.

Dr. MICHEL. Sure, I would not say that you are wrong. I think you could absolutely look at it and you can make an argument that you should look at a unified Federal budget and there would be no problem there at all. It is either in one place or the other right now, but it's all in the same place.

Senator JOHNSON. OK. Again, you could all get your microphones a little bit closer because it's kind of hard to hear you. Mr. Wesbury.

Mr. WESBURY. The United Kingdom takes the loss—the Bank of England has the same loss because they pay interest. They are paying more in interest to their banks than they are earning from the bonds that the Bank of England owns. They take that loss and put it into their deficit. In fact, they have had a big political fight about how they are able to increase spending because the central banks are losing money.

Senator JOHNSON. This problem masking the true deficit, \$200 billion. I would argue that's the problem. I don't think it's a master problem. Mr. Wesbury you mentioned that we have increased the money supply.

Here's the fact. A dollar you held in 1998 is worth 51 cents. A dollar you held in 2014 is worth 74 cents. A dollar you held in 2019 is worth 80 cents. But the money supply increased a lot more than that. What's the difference? Why is it a direct relationship?

Mr. WESBURY. Because the Federal Reserve, as they have added money to the banking system through this process of quantitative easing has instituted heavier capital requirements and liquidity rules on banks. In other words, they have flooded the system with money but then they have forced the banks to hold on to that money.

As a result, it didn't turn into inflation as much as you might have thought. Back after the 2008 quantitative easing, everybody thought inflation was going to pick up and it didn't. However, it did during COVID and the difference was——

Senator JOHNSON. That's just my point.

Mr. WESBURY. Yes.

Senator JOHNSON. Everybody thought inflation didn't——

Mr. WESBURY. Yes.

Senator JOHNSON. Again, that's what's so confusing. This is why I focus on fiscal policy. I mean, to me, the problem is we are running these enormous deficits. We are going to finance it one way or the other. Either finance it through the Fed or we finance it



through the treasury and selling bonds. We are screwed either way.

We need to get our fiscal house in order. We can argue about this. Again, I don't know if we should pay them or not. I don't think it really makes that much difference. I understand the argument, it hides it that in theor, would increase inflation. Although we thought it would and it did not. Again, my point would be—I am running out of time, is we need to focus on fiscal problems, our massive fiscal deficits and how we finance it. It's kind of a horse of piece.

Mr. WESBURY. Dr. Kohn, I think wanted to respond.

Dr. KOHN. I just wanted to point out to the Senator that there's never been a really tight relationship between money supply and inflation. There's been a long-term relationship but it's not that tight. As you and Brian talk, there was a lot of discussion in the 20 teens about how this blow up in the balance sheet and in the money supply was going to cause inflation. Inflation was very low the whole time. People were surprised at how low it was.

Senator JOHNSON. Which again, underscores my point. I really don't think we understand monetary that nobody does. It's a guessing game.

Chairman PAUL. I would also say that while there's not an exact mathematical correlation, increasing the money supply is what causes inflation. I don't think that's disputed. Mr. Wesbury.

Mr. WESBURY. Yes. I did not expect inflation after 2008 because the M2 was contained with regulatory rules. I did expect inflation during COVID because we relaxed those regulatory rules and M2 exploded. It was one of the easiest forecasts I have ever made in my career. Chair Paul is exactly right. M2, it's money printing that causes inflation.

That's what worries me about quantitative easing is we have flooded the system and if we let it out then it becomes inflation. Then the second quick point, it's not about interest rates because Chair Bernanke held interest rates at zero for seven years, and we did not get inflation. Chair Powell only held them at zero for two years, and we had nine percent inflation.

It's not about rates, it's about the money supply. That's why taking away the ability to pay interest on reserves will not cause inflation. That's not what causes inflation. It's the money supply that does.

Chairman PAUL. Senator Peters.

Senator PETERS. Dr. Kohn, focused answer, just try to answer something related to exactly what we are dealing with right now. You emphasized in your testimony the importance of interest on reserve balances as a tool and monetary policy. For the Committee and all of you talked about this and you have been trying to distill it down for us.

Why is this authority necessary to retain in order to maintain a strong economy? What are the risks if we repeal it? How would you summarize that quickly for us?

Dr. KOHN. I think there are a couple of things there, Senator Peters. One, if the economy is very weak and the Fed reduces its interest rates to zero, as Brian was just talking about, and the economy remains weak or they are concerned that the economy will

remain weak—this is the 20 teens—you need to do something else to stimulate spending.

You need to lower mortgage rates to get people to buy houses, to get lower interest rates, to get people to buy cars, et cetera. That's what QE does. That's what buying the securities does. So buying those securities helps stabilize the economy and promote employment. Once the Fed does that, it really needs the interest on reserves then to tighten policy to fight inflation as it did in 2022.

It was a bit late to that game. I agree and I have made that criticism publicly but it did fight. It did it with IORB. Without IORB, it would not have been able to stabilize the system when COVID hit, which is a big difference there. A lot of COVID distortions and it would not have been able to fight inflation. It's brought inflation from six down to three with IORB. So very important for stabilizing the economy and fighting inflation.

Senator PETERS. You made the argument why it's important. I would like to turn the idea that we have heard that banks are receiving a windfall as a result of this. How would you respond to those would argue that?

Dr. KOHN. Banks have to get those reserves somehow. The Fed goes out and it buys securities from someone holding treasury securities. That person then takes the deposit and puts it in the bank. That person isn't going to deposit it at 0.5 interest rate, right? It's going to want a rate that's somewhat comparable to the securities that's sold to the Fed.

The bank then has the deposit at the Federal Reserve. The bank has attracted a deposit that pays almost what it's being paid at the Federal Reserve. You can't compare the money that the Fed pays to the banks to net interest margin. You have to talk about what the banks have paid to get that money. My view is they are paying something comparable to IORB in order to get that money. The net profit to the banks is quite small.

Senator PETERS. In fact, those remittances are back to the Treasury, which I mentioned in my opening comments. I also mentioned that the Fed is asserting that it's going to return to positive remittances back to the treasury in the near future. Would you agree with that and explain to us what that means for the taxpayers?

Dr. KOHN. I think the Fed's recent weekly balance sheet suggests that it is already earning profits. The amount of accumulated losses that it's showing has started to go down very slowly. As interest rates go down and they went down further yesterday with the FOMC's decision, the Fed's profits will pick up. The Fed is already on a path to recoup the losses that it made and start putting money back to the Treasury.

Senator PETERS. A final point—my time is running out. To the average person, if you are a small business or a family and you are hearing this debate about interest on these reserve balances, how does it impact them? Why is it a good thing that this law is in place and are there concerns that you have?

Dr. KOHN. I think it's a good thing because it helps. This goes back to the first question, Senator Peters. It goes back to what it enables the Fed to do. It enables the Fed to protect economic stability and financial stability. Without that, the recession in 2008

would have been much worse. The recession after COVID hit and the disruption in financial markets, the financial markets were not working.

When you are not working, you can't get credit to households and businesses, small businesses, or large households, et cetera. The Fed had to step in and buy those securities in order to restore functioning. IORB enabled it to do that knowing that when it was time to fight inflation, they still had the tool to fight inflation. Without IORB, inflation might be higher, the economy might be weaker, the stagflation could be worse.

Senator PETERS. Thank you. Thank you, Mr. Chair.

Chairman PAUL. Senator Lankford.

#### **OPENING STATEMENT OF SENATOR LANKFORD**

Senator LANKFORD. Thank you. Thanks for the conversation on this. This is important because we are dealing with the financial future of the country. The two big issues here, Congress has got to be able to work on getting our debt down, first, our deficit down, our debt down.

All these things are patchwork with the Federal Reserve trying to be able to figure out how to be able to manage economy with the amount of debt that we are currently carrying as a Nation. Second thing on this though, is this is an entirely new system that's out there. We are talking the last 15 years, the rules have changed and everything, the amount of quantitative easing, what's actually having the interest on reserve balances.

This is an experiment we really don't know where this goes 50 years from now, 35 years from now, and some of the acceleration. It's entirely reasonable for us to be able to have this dialog, to be able to talk it through and to be able to deal with. Let me try to deal with a couple of things on this. One, is the interest on reserve balances given to foreign banks.

Obviously, that is in direct competition with our domestic banks obviously, but it's also what would have been American tax dollars going back into the Treasury actually going to a foreign bank to be able to stabilize their reserve balance as well. What effect does that have on our American economy for that much money? Does anyone know the amount of interest on reserve balances Federal Reserve has paid to foreign banks?

Dr. KOHN. I think this was in the study that that Dr. Paul released and it is substantial.

Senator LANKFORD. Substantial.

Dr. KOHN. Because the foreign banks do hold lots of deposits at the Federal Reserve. It serves a purpose for United States and foreign citizens. The foreign banks help to facilitate transactions between countries. They help U.S. exporters, for example.

Senator LANKFORD. But if we go back 15 years ago, it was bank to bank that were actually dealing with this rather than the Federal Reserve being able to hold it over.

Dr. KOHN. Right.

Senator LANKFORD. My bigger question on this is, if we were to, let's say, slowly taper this away, there's been some arguments to say six months is too fast. Dr. Paul is always in a hurry to solve every problem. They have said, do you know what? His bill's just

too fast to be able to implement on this. We need more time than that. When I asked the question of banks and to say, how much time you need, it's always as much time as we can get.

But then my second question to them is, what would you do instead? Every one of them I have talked to said the same thing, "We would buy treasuries." I was like, "Why is that a bad thing for our economy, for banks to be able to buy into treasuries?" We are selling treasuries already at record numbers out there. We need consistent buyers on this. Why is this a bad thing for us to switch from interest on reserve balances to actually banks actually buying treasuries?

Dr. MICHEL. It's not a bad thing. If they want to buy treasuries, they can buy treasuries, then that's fine. If I want to buy treasuries, I can buy treasuries, but I cannot take the proceeds from my sale of treasuries and park them at the Fed and earn exactly what I was earning when I had the treasuries. That's why it's a rainfall.

Senator LANKFORD. Right. Do you anyone make a comment on that?

Dr. KOHN. You are talking about whether the Fed should be buying the treasuries or the banks.

Senator LANKFORD. Yes, the banks.

Dr. KOHN. Right. So, the same number of treasuries need to be sold to fund the deficit that you and Senator Johnson were talking about. So that, and the question is whether it's the Fed or the banks. Certainly before 2008 the banks found ways of making these transactions, it was perhaps a bit more cumbersome than it is today, with the interest on reserves.

So yes, they will find a way of doing the same things, but you will handicap the Federal Reserve. Remember, Congress actually authorized this in 2006. I testified in 2004 in favor of paying interest on reserve. So I'm a little consistent over time. And my point then was not paying interest on reserve balances was a tax on the banks. The banks naturally were trying to avoid the tax as we all do.

They avoided the tax by keeping deposits lower by discouraging certain kinds of deposits where they have to hold reserves and by passing on that cost to borrowers and lenders. I think the Congress recognized the inefficiencies of not paying interest on reserves and authorized the Fed to do it with no expectation that a 2008 would come about.

Senator LANKFORD. Right. Yes, the challenge is just for basic safety and soundness of a bank, there is a good reason to be able to keep significant reserves in a bank. But to be able to say that just because we require you to be safe and sound, that's a tax on the bank, that's a part I guess I don't agree with.

Dr. KOHN. When we were not paying, so we said to the banks, you have to keep deposits at the Federal Reserve paying zero. You have to make an interest free loan to the government. That's a tax.

Senator LANKFORD. Mr. Wesbury you were about to say something as well.

Mr. WESBURY. Yes. From the beginning of the Fed all the way through 2008, we did not have banking problems because banks had too fewer reserves. That's not why we had banking problems. The great financial crisis did not come about because banks had too

few reserves. That's not what was the problem. The second point I would make is that quantitative easing didn't save the economy either.

We passed quantitative easing in September 2008, and the market fell another 40 percent after that in the next nine months. It wasn't until March 2009 that everything turned around. The one thing that changed then was we altered this mark to market accounting rule. That was the real problem with the banking system.

What the Fed did is they took advantage of that crisis and grew their balance sheet massively from 850 billion to today over almost \$7 trillion. The second point I would make is, yes, the bank should own the treasury bonds. Instead, what's happened is that the Fed buys them and. On the Fed's books, there are \$800 billion of losses from the treasury bonds it bought during 2008 and then again during COVID.

What they really did is they took the risk out of the free market and put it on the Fed's balance sheet. Because the Fed does not care about losses, they do not mark them to market, they can print money to take care of the losses. What this has done is distorted the economy and allowed us to spend more as a nation than we would if we had to pay the real price of that borrowing.

Senator LANKFORD. Thank you.

Chairman PAUL. Senator Scott.

#### OPENING STATEMENT OF SENATOR SCOTT

Senator SCOTT. Mr. Chair, thanks for doing this. Thanks for holding this hearing. I think Jay Powell is a disaster. If you just look while—it started a little bit before him, but the balance sheet went from what you said, Mr. Wesbury, 800 what billion dollars to now it's got to 9 trillion?

Mr. WESBURY. Yes.

Senator SCOTT. Now it's starting to increase it again.

Mr. WESBURY. Yes.

Senator SCOTT. They are going to announce it, 40 billion dollars more a month. I mean, we do not have a financial crisis today. I have been trying to get an independent inspector general because nobody will even investigate the fact that they have had insider trading issues, stuff like that there. It makes no sense to me.

Mr. Wesbury, let me ask you my first question. What's the balance sheet and what's the liabilities? What's the spread right now?

Mr. WESBURY. At the Federal Reserve?

Senator SCOTT. Right.

Mr. WESBURY. The balance sheet is now 7.6 times larger than it was back in 2007. It's six and a half trillion dollars. We have gone from 850 billion to six and a half trillion. The Federal Reserve owns the bonds on the other side, but they have an \$800 billion loss on those bonds—

Senator SCOTT. Marked to market? If you were a bank?

Mr. WESBURY. Yes, they would be 850 billion in the hole.

Senator SCOTT. Right. The capital count's only like \$45 billion, \$43 billion at the Federal Reserve anyway?

Mr. WESBURY. They have lost 40 times their capital. I have tried to get an answer to a question is how does the Fed keep the lights

on? Because they have lost 850 billion on their portfolio and they are losing \$180 billion this year.

Chairman PAUL. How do they finance this year, which they are financing on other profits as well.

Senator SCOTT. Yes. And he's losing about \$200 billion a year, right? OK. He's funding that by just issuing treasuries, right?

Dr. KOHN. By issuing reserves, basically by writing the paycheck.

Senator SCOTT. I mean, he just gets to keep—

Dr. KOHN. The Fed is not a profit-making institution.

Senator SCOTT. Wait. Before Powell, had sent money every year, right? They sent money every year to the treasury?

Dr. KOHN. The Congress has given the Fed certain responsibilities for stabilizing the economy and stabilizing prices and protecting the financial market. These purchases and those losses were incurred in the process of meeting the goals that you, the Senate, and the House set for the Federal Reserve. You did not set a goal of profit for the Federal Reserve.

Senator SCOTT. Yes, and I think that's legitimate. But they failed in doing that. As Mr. Wesbury said, they bought these treasuries to try control all the interest rate through the—not just short term, but 10 year, and 20, and 30 year, OK? And cause misallocation of capital. I mean, complete misallocation of capital is what he's done, and no accountability.

Here's what I am getting. Why do they have reserves in the first place? Let's go through that. They have reserves because in a normal business, you have to have reserves. I have owned manufacturing companies, OK? If I went to the bank and said, I want you to lend me a hundred percent of the money, they would have laughed at me. Then the bank said, "OK, we will lend you money, but we are not going to pay you to hold the reserves you have to hold." Right? Isn't that the same thing? How's it any different? Any of you? I mean, I never get this, why we are paying them to hold what a normal business has to hold and their leverage to the hilt.

Dr. KOHN. For decades, banks held about 10 percent reserves. Now by doing quantitative easing, we bumped that up to over 30 percent and then we pay them to hold them.

Senator SCOTT. They use our guarantee to get deposits. They use the Federal Government's guarantee to get deposits and then we pay them to get the reserves to justify us giving them a Federal guarantee. But I used to borrow money from banks. They didn't say, "Well you got to hold capital, 20, 30 or 40 percent capital, and I am going to pay you for that. That's what is crazy about this.

Then the fact that they keep losing this money and they act like it's going to change. I do not get how it keeps saying, "It's going to get better. Well, how?

Dr. KOHN. As interest rates come down, the amount of money they are paying the banks will come down and the money they are earning on their portfolio comes down much more slowly because it's a longer-term portfolio.

Senator SCOTT. If that's true, then why would they have to yesterday announce agreement to start buying another \$40 billion of treasuries?

Dr. KOHN. Because the funding markets were being disrupted because reserves had dropped low enough that the banks were not

arbitraging back and forth in these funding markets. They are increasing those disposal—

Senator SCOTT. It is because they could not get the bank. The banks were not happy with the interest rate they were getting. So now they have to buy up the treasuries to deal with that.

Dr. KOHN. We have to remember that the Federal Reserve is the one who creates the reserves. The banking system does not control the amount of deposits at the Fed, the Fed controls the amount of deposits at the Fed. The banking system can pass those deposits around.

Senator SCOTT. Let's make it real simple. We are paying banks to hold treasuries or we are paying them interest, one or the other, right?

Dr. KOHN. Right.

Senator SCOTT. Right. I just don't get why we are paying on capital and how that helps. Like in my State, if you go around my State, the rich are doing fine, right? I live in Naples, Florida, they are doing fine. I talk to them, they are doing great. Do you know who is getting creamed because of the Federal Reserve? The poor. Mortgage rates are up. As they keep playing with short term entry rates, what's happened to the 10 year and 30 year? It's gone up.

Dr. KOHN. Yes.

Senator SCOTT. Now they have to try to play that and that's been building the balance sheet again. This makes no sense. Since Powell's started down there, I mean, you said inflation was transitory. It wasn't. What they have done is cost massive inflation in this country. Stop doing it. I don't get this stuff. Why we just allow them to pay interest to banks, keep buying more treasuries.

It just doesn't make sense. They are out of control. Do you guys disagree? Am I looking at it differently than you look at a normal business?

Dr. MICHEL. Yes. It's not a normal business. It's part of the government, which is why Senator Johnson is right. You should look at it on a unified basis. The issue here is that we should take away the market distorting piece of this and let it be priced in accurately.

Senator SCOTT. But the market work?

Dr. MICHEL. Yes.

Senator SCOTT. I wanted to borrow money at zero. When I was in business, I got stuck with the darn banks what they wanted to charge. Why don't we let the Federal Reserve do that? Let the market work. I am sorry.

Chairman PAUL. No, that's good. We are going to continue for a walk. I would like the discussion. Dr. Kohn, you said that really one of the primary goals of the Federal Reserve is not to make money. That's correct. You would have inflation and unemployment, but there are infinite amount of ways they could address those goals.

You might also argue that a central bank that loses money might not be of course, for bragging about or that it might not be part of your goals to have a central bank that loses money, that it might not be comforting or accentuate or help with the idea of stability within the economy. I am going to throw out a question that I

think I just want to hear the response, and it may be a little bit off the wall.

What if we had a banking system that was just based on fraud and lack of fraud? If I give you money and you decide to loan it, you have to pay me interest and we have a contract. I am not going to come get my money for five years and you are going to loan it and that's all you would loan. We did not have any other rules.

The interesting thing is this, about 25 percent of money that's loaned out is checking account money. But you don't have a contract with me. The reason why the whole system is always a house of cards and could go under is if everybody wants to get their checking account money, it's not enough money.

Basically, we have a fraudulent system. Fractional reserve is a fraudulent system. But what if you did nothing else? I am not asking you to advocate for the policy. I just want to know. About 25 percent of the deposits are checking, you could still loan some of that if you tell me I can only remove 90 percent of my checking that you will pay me a little bit of interest.

But right now, you take my checking account money and basically don't pay me anything and the banks get to make money on it. What if we just had a system of banking based on fraud? We will start with Dr. Michel.

Dr. MICHEL. If I understand where you are going—

Chairman PAUL. You go and loan out money that you have permission to loan out and you got to make an agreement with me if you are going to loan my money out and give it to somebody else. I am going to forego it, you got to pay me some money and you are going to take a portion of it. But I did not make that. When I put my money in my checking account, I want it all there, but it's not all there because you are loaning it out. It is a fraud, the banks are committing a fraud every day by loaning out my checking account money.

Dr. MICHEL. I mean, that is disclosed. I wouldn't call that fraud, but if—

Chairman PAUL. What if you weren't allowed to loan out stuff you did not have permission to? Let's assume that would be good—

Dr. MICHEL. If you weren't allowed to loan out stuff that you did not have permission to loan out, I would be OK with that.

Chairman PAUL. I guess it's too far outside the box. Mr. Wesbury.

Mr. WESBURY. I am going to take this in a little different way. We have the Federal Deposit Insurance Corporation (FDIC) insurance right now, so everybody's covered to \$250,000. I have always argued that we should get rid of that. Like that encourages banks to not—actually, Silicon Valley Bank went under, we covered every penny of all their deposits.

What we should have is a system of gradation. I am a bank, you give me your money, you want no risk, I take it and I buy treasury bills. Then you only earn two percent. You will take some risk. I buy half treasury bills and I make some loans with the others. Now you earn three percent or you want all risk, and I make all loans and you make four percent and you get to choose.



Then on the way out the door, you could buy insurance from Goldman Sachs. They have a desk at the door. You just deposited your money. You can get private insurance. What you are really getting to is where the depositor has control over how the money is used. That's a system that's a free market system of dealing with insurance.

Right now, we have government insurance on banking deposits, and that can lead to really risky bank behavior.

Dr. MICHEL. I think that's called mutual funds, isn't it?

Mr. WESBURY. It is. Yes.

Dr. MICHEL. Those things are available. I wouldn't say it's based on fraud, Dr. Paul. I would say there is liquidity transformation in the system, and there always has been in which the banks lend out at a longer term than they get their funds in and demand deposits or savings deposits or short-term deposits. And that creates risk.

Our country was subject before 1913, before the Fed was founded to periodic recessions, very severe recessions. When there were runs on the banks, the Fed was created to have a lending facility so the banks could meet those runs and wouldn't tighten the credit system and create very severe recessions. There is a risk in the system. We need to make sure the banks are resilient and can take the risk and understand the risk and the deposits that the Fed are—

Chairman PAUL. The reason there is a fraud that exists is that if a hundred percent of people want their checking account money in every bank in America tomorrow, it's not there, right. We still are liable for bank ones. The government just pays sort through the FTIC and we still do have bank runs on occasion. We have had some of these crises going back to the issue of the money supply tripling.

It's always fascinating me, I know it's not arithmetic. It isn't exactly, you don't triple it and have a third, prices go up as triple. Some of that, you could argue that the IORB is, if you are going to have massive inflation, is a useful tool. But the opposite argument of that is if you have this useful tool, you are going to have a lot of inflation.

It's a way to make inflation not so bad when you are going to pump tons of money into the system. But the counter argument would be maybe you shouldn't be pumping tons of money into the system. It's the same way with the Federal Reserve. We have many people out there, you may not know them, but think we shouldn't have a Federal Reserve.

But I always tell them, yes, if we had a balanced budget every year, we probably could. Artificial Intelligence (AI) could run the system, have one or two percent inflation a year, and tell everybody what's going to be, it would be very predictable. We would not have any ups and downs, swings of this. It just is what it is. You would have great predictability, but you would have to balance your budget each year, so you did not have to have these wild swings.

That was the whole thing of the pandemic, was this massive amount of borrowing and then all the flooding of money in there, everybody got free checks. It was a terrible thing we did. None of it was necessary, including the whole science behind making every-

body crazy over COVID. Sure, it was bad, but it wasn't anything like the response to it. The response was insane.

But going back to the inflation issue, I have just one other question, just sort of for the panel is, I have always wondered whether some of the reason we do not have as much inflation as the money supply created, or at least some of this, is that we export inflation in the sense that we import more than we export. So, we are always sending dollars overseas, over goods.

It's an enormous amount of money. I know it equilibrates within the system, but we have entire countries that are on the dollar standard now. As we inflate, there are whole countries in Africa are, the only thing you see change in hands is dollars, South America the same way. So is some facet of the lessening of inflation that all those dollars aren't chasing American goods. We export them and there chasing worldwide goods. We do not have quite the impact of inflation that we would have with the tripling of the money supply. Why don't we just go down? I will start with Dr. Michel.

Dr. MICHEL. From the studies that I am familiar with, I would say, no, that's not the primary reason.

Chairman PAUL. Ryan.

Mr. YOUNG. I would say dollars come back to the United States that come abroad generally in the form of foreign investment. If our countries choose to dollarize their economies, whether it's by importing dollars from here—

Chairman PAUL. I guess the question could be some of that investment goes into the stock market. The stock market may have inflation, but the consumer price index isn't. I mean, that's what I'm asking. Could you be shifting some of it away from consumer price index and you see inflation in the stock market, but Mr. Wesbury?

Mr. WESBURY. Yes, there's a number of ways that the amount of money does not always equal the amount of inflation and it's productivity. We never know where the money can go into—there are countries that are dollarized, they completely use dollars. And so that money is out of the system and that means money growth doesn't matter as much. But a question or a point you just made before, I want to highlight something. Between 2020 and 2022, COVID, the Federal Government issued \$7 trillion worth of debt. The Federal Reserve bought 45 percent of that debt.

This is monetizing the debt. The Fed always says they don't coordinate with the Treasury. I would argue there's probably not a phone call that says, we are going to issue this, you are going to buy that. But isn't it interesting that quantitative easing happens at the same time we pass these huge spending bills? Then the Fed ends up buying over half of that debt.

The Fed does not have the same risk. They have a different risk tolerance than the banking system would. They will pay or accept a lower interest rate than the market would have in order to do this. Not only did we do crazy things during COVID that we shouldn't, we overreacted, but we overspent. Then the Fed financed it. That's one of the huge problems of this abundant reserve policy, is that the Fed is monetizing our debt.

Chairman PAUL. That's a corollary of what Friedman would say about spending, that nobody spends somebody else's money as

wisely. It's the same with borrowing, individual bankers and people who will lose their livelihood are going to be wiser, not because they are smarter people than the Fed, but because they stand to lose more. They have a personal responsibility to it. Senator Johnson.

Dr. KOHN. I think the fact that the Federal spending and the money supplied and the QE were correlated were a separate response of the Congress and the Federal Reserve to what they perceived to be a very serious problem caused by COVID. There wasn't a cause and effect.

I don't think the Trump Biden deficits of 2020, 2021, would have been affected if interest rates had been a few basis points higher, the Congress would not have passed those bills. They are both responding to the same thing. I think you talked, Senator Dr. Paul, about sort of the money supply allowing inflation. There's some truth there because rather than the money supply causing inflation, the Fed supplies the amount of money people demand.

You set an interest rate and you supply the money people demand at that interest rate. That's the way monetary policy has worked. They demand more in inflation. If you want to stop the inflation, set the interest rate higher, they will spend less, they will demand less money in those circumstances.

I do think the stability of our financial markets is really important for the inward investment to see the dollar as a reserve currency, to see U.S. securities markets as the safest, most liquid markets in the world as a very important piece of keeping the——

Chairman PAUL. I think what causes inflation is an important question. Mr. Wesbury.

Mr. WESBURY. Yes. OK. The way you described monetary policy, that the Fed supplies the money that people demand. I would argue that is absolutely true prior to 2008, because what abundant reserve policy does is it separates the money supply and interest rates. For example, yesterday we saw it that we are going to change—we are going to buy \$40 billion worth of bonds, but we are going to lower the interest rate at the same time.

You did not have to do both or the Fed, you are not the Fed anymore, but you represent the Fed. But what we did is we completely separated and when we changed from a scarce reserve system to an abundant reserve system, we took supply and demand out of interest rate markets. The Fed or banks used to trade Federal funds every single day. Banks had a Federal funds trading desk. The minute we started abundant reserves, all those desks are gone.

There's no more jobs as Federal funds traders because banks are overwhelmed with Federal funds. They do not borrow them anymore. So you really do not have any way of knowing what the demand for money is anymore. It's not related to interest rates at all.

Dr. KOHN. I would say yes, IORB and abundant reserves, separated reserves and interest rates. Absolutely. The Fed's balance sheet and interest rates are now different—operate on different things. That's a feature, not a bug in my view. A bug in your view, I get that. But I think the amount of money that people outside the Federal Reserve—not talking about banks.

But people, you and me, Senator Johnson, Dr. Paul demand in our bank accounts, it's not really affected by IORB. Well, it's af-

fectured by the level of interest rates, right? I think it's still M2, which is the stuff that people hold is still demand determined based on the interest rate. The reserve's part is not totally.

Senator JOHNSON. Let me try and clarify this by doing what I do, problem solving. Let's define the problem we are talking about here. I mean, you go back millennia. The Federal Reserve is really the culmination of millennia of people trading. You used to do barter, that was very efficient.

So you started creating money, all kinds of different things were using trinkets and pebbles and all of a sudden precious metals, coins, that type of thing. In order to grow an economy, you need to expand the money supply. If you want to kill your economy, decrease the supply of money, but it's how you manage it. Even though I agree with the gibbons of the author of the Creature from Jekyll Island, that the Federal Reserve is literally a cartel of these banks, and we have these central banks.

The main task from my standpoint that I believe is they are trying to manage that money supply. Try and grow it to accommodate a growing economy so we have prosperity. The problem is do we do it smartly? I want a quick go to market to market. I am back there in Oshkosh, Wisconsin going, my factory's humming along. Why do we have this great recession? What caused this? It was stupid regulation.

You can say these mortgage backed securities was a stupid financing tool, but they weren't worth zero, right. But our stupid regulation forced banks to write that down to zero and we bankrupted banks. But I think in the end, those mortgage backed securities were probably worth 80 cents on the dollar. Is that about right?

Mr. WESBURY. Absolutely.

Senator JOHNSON. I mean, how stupid is a self-inflicted wound? What I am hearing out of this hearing, and I told you this, I walked by, said this confuses me. Again, this is complex, but I don't think it is. I love Senator Scott. I think he's basically getting all concerned about us paying interest to foreign banks.

I mean, foreign banks who buy our treasuries and the lawsuit just show up on the Federal Government's balance sheet versus the Federal Reserve. I don't think the Federal Reserve is all that particularly independent, OK? It's been given a task to try and manage our money supply. I think the main issue here is the moral hazard.

By separating supply and demand.

Mr. WESBURY. Yes.

Senator JOHNSON. And by not having those daily markets. Again, the beauty of a free market competitive system are literally billions of transactions, billions of consumers doing all this stuff and just magically works out the pricing. The minute you have government starting to do this, you just screw things up.

I would really have to try and understand and nobody does. Nobody understands how the Federal Reserve uses this buying and selling out to, I just don't get it. But I do get the moral hazard of doing this. I have no problem. The banks are going to park their money somewhere.

They are going to get an industry. Either they are going to buy the treasuries directly. Foreign banks, same way. Again, the problem is our massive debt suspended. It has to be financed somehow. We give the Federal Reserve the ability to do that. Again, I think it's probably on the margins, because we keep industry artificially low, we feel a little bit less constrained. If we were paying \$2 trillion in interest expense, it might.

I am saying it might cause us to spend less money. I am not necessarily sure, I have been trying to get my colleagues to spend less money, we all have. Here are three fiscal hawks. It's an impossible task. But in my base, it's really the moral hazard. Again, Mr. Kohn, you are obviously on different side of these.

Do you acknowledge that is a problem with the Federal Reserve doing all this, we do not have all that market, we have that disconnect where we are making it easier for Congress to spend money. And that's a moral hazard.

Dr. KOHN. I think it's very small. That is the amount of securities that the Fed holds, first of all has gone down by, what, about a trillion dollars along with reserves. The reserves were over four at one point and now they are around three. So that's gone down over the last year. I haven't seen any move toward fiscal responsibility.

Senator JOHNSON. That's what I was talking about the size of the balance sheet, who were \$38 trillion in debt. Would we have a bigger balance sheet on this side? Again, I just think it's a shell game. I just think it's a county convention in terms of how we are doing this. The main problem is, again, what the Federal Government spends, what we do not take in and the difference between that. I just think that is the problem that we are simply not cracking.

Dr. KOHN. It's a huge problem, the trajectory of the Federal debt, relative GDP is a big problem.

Senator JOHNSON. I am well aware.

Dr. KOHN. It's a time bomb waiting to go off, but I don't think the Fed has caused it.

Senator JOHNSON. Let me end on this. The only thing that keeps all this thing going is confidence, right? It means it's a wonderful life. It's just back then when you didn't have reserves and all of a sudden I can't get my money and you get to run the bank and nobody had confidence in the system.

Dr. KOHN. Yes.

Senator JOHNSON. Confidence is absolutely critical. That's what happened in 2008. We broke the bank and that money market fund and confidence just evaporated. I would say the one tool that the Federal Reserve provides is just that backstop confidence. It's like we will prick the fucking money to make sure the defense system doesn't collapse.

Dr. KOHN. Right.

Senator JOHNSON. To have one central bank do that, I think that does provide confidence. That's what FDIC insurance is for. Again, we see this loan crisis, they increase that too much, create a moral hazard. But there's got to be a sweet spot that we should have some deposit insurance to provide that confidence, but not a dollar more or else you create that moral hazard. It's confidence versus moral hazard.

Dr. KOHN. I think that's why the Fed was created in 1913, because there were these periodic losses of confidence. The thought was, if you have a discount window, a lending facility, and banks can come and take their loans and borrow against them and pay out the deposit.

Senator JOHNSON. So you have to read *Creature from Jekyll* and then we have to have a conversation. I am not kidding. You ought to read that. It's a fascinating book. OK. Then, Mr. Wesbury, you had a comment on that.

Mr. WESBURY. I just wanted to say that in 2008, we had a problem, subprime loans. It was a \$400, \$500 billion problem. It was not enough. Even Chairman Greenspan has said or Chairman Bernanke said this, it wasn't enough alone to take down the U.S. economy. Today, with this new system, this experimental system, as Senator Lankford said, the banks plus the Fed have over a trillion and a half dollars of losses on their books.

It's because all these bonds were sold during COVID, during 2008, at extremely low interest rates. Now, interest rates are higher—

Senator JOHNSON. But again, we had \$38 trillion of losses on our books. You add another trillion and a half trillion over 39 and a half trillion.

Mr. WESBURY. Yes.

Senator JOHNSON. By the way, on the path of about 62 trillion in 10 years.

Mr. WESBURY. What I would argue is we have a bigger financial problem today than we did back in 2008. It's with all of this supposed monetary policy that's made us safer. I would argue that we are less safe today as a financial system than we were when we started this back in 2008. Thank you.

Senator JOHNSON. Again, I want to thank the Chair for having this hearing. I want to thank all of you guys. I mean, really, this has been a good discussion. This is absolutely within this committee's jurisdiction. So I really appreciate this.

Chairman PAUL. Senator Scott.

Senator SCOTT. Let's go to what Senator Johnson said, paying money into foreign banks. Let's say we stopped doing it. What would happen? Let's say we stopped, we said we are only going to do it to U.S. banks and banks domiciled in the United States, headquarters in the United States. What would happen?

Dr. KOHN. Stop paying interest to the foreign banks. Is that what you said?

Senator SCOTT. Yes. Stop paying any interest.

Dr. KOHN. They would get rid of the reserves, right? They would sell off the reserves. That would put downward pressure on interest rates. The Fed would have to absorb that in order to keep interest rates from falling—or the U.S. banks would have to end up with the reserves.

They would have to be induced to take those reserves. So it would end up—

Senator SCOTT. Why wouldn't they—

Dr. KOHN. It would tend to pressure interest rates lower at a time when inflation is already at three percent. I think that would be a problem.

Senator SCOTT. If the U.S. banks are going to get paid interest on it, why wouldn't they just pick up the slack?

Dr. KOHN. They already have the reserves they want to hold. The Fed could make them, they could have to pick up the slack, the Fed determines it. They could pick up the slack and then they would have the reserves. But I am not sure what you would accomplish that way.

Senator SCOTT. It accomplishes the fact that I think the Chinese government wants to destroy my way of life and my family's way of life. I don't want to give them a dime. I don't want Chinese banks to have a dime. If the Chinese government's despicable, they are going to take everything they get. They are going to build a military to destroy my way of life and my kids' way of life.

Dr. KOHN. I think that's a potential argument. You don't want Chinese banks operating in the United States. Then somebody, not the Federal Reserve, but somebody needs to pull that plug.

Senator SCOTT. If the IORB was eliminated, would the banks also lend more money to small businesses? My first business was a donut shop. I went to the bank, they lent me \$7,500. You can't get a loan like that from a bank today. I don't know any bank that's going to make a loan like that today.

If we stop paying interest on reserves, would they maybe start helping small businesses, which they don't do anymore? Any of you?

Mr. WESBURY. What they would have to do is take whatever assets they have, the reserves, they would have to trade them for some other asset. They could buy treasury bonds with those reserves. They could make loans with those reserves, right. Now they are constrained by rule. One of the interesting things is that Chairman Powell yesterday said, we are going to start buying \$40 billion more of treasury bills every month. The reason is because there are now pressures in the repo market, we can see interest rates starting to act funky and volatile.

Senator SCOTT. They have lost control of interest rates.

Mr. WESBURY. Right.

Senator SCOTT. Well, if they're acting funky, that means they don't get to dictate exactly the price.

Mr. WESBURY. That's exactly right.

Senator SCOTT. That's why they should be honest. They want to control everything.

Mr. WESBURY. Yes, that's exactly right. But what's interesting is the reason we are at that point is because they have set regulations so tough on these banks that they are forcing them to hold this amount of reserves. Then they brought the reserves down right to that level.

And they go, "Oh, no. Now we have to increase them." They could easily reduce the liquidity rules. If they did that, more loans would go to small businesses.

Senator SCOTT. Because you can make a profit off it.

Mr. WESBURY. Yes. Exactly.

Senator SCOTT. What they are doing is impacting small business ability to get a loan?

Mr. WESBURY. Absolutely. They are forcing banks to hold reserves instead of make loans or buy treasury bonds.

Senator SCOTT. My State who's getting hurt are the poorest families that don't have the relationships to go get a loan. Like I had no relationships to go get the \$7,500 when I got out of the Navy to buy a donut shop.

If the bank hadn't lent me money, I don't know how it would have gotten started. I had no relative, I knew that had a thousand bucks.

Mr. WESBURY. Yes.

Senator SCOTT. What they are doing is they are making it harder for small businesses to get started. It hurts the poorest families in this country.

Mr. WESBURY. Exactly.

Dr. KOHN. That's a product of the regulation, not of the interest by Federal Reserve. All the other regulators trying to keep these banks safe. Now, you could argue that they went too far after 2008. That's what the administration is arguing and they are pulling the regulations back.

We will see whether that happens. But it's not the reserve balances. What would happen when the Fed sold the securities that created the reserve balances in your world in which the balances went down, they would extinguish deposits. They sell me a security, they get my check, they clear it against my bank, right. The bank doesn't have—just because the reserves go down doesn't mean it has more money to make loans. It just has fewer deposits. The reserves and the deposits will go down together.

Senator SCOTT. But they have an incentive to make a loan because there would be more money.

Dr. KOHN. But they also have more trouble managing the liquidity. This is a problem for smaller banks.

Senator SCOTT. I mean, the way I look at it is, what we have done is we have created all these rules and regulations so the banks can't even do what they are expected to do. Lend me money so I can start my little business. They are not doing that today. Your consumer credit is a interest rate of 20 percent plus from the credit card.

That's the only place you can get it. I think Dr. Kohn, you said that, they did not have an impact on interest rates. If the Federal Reserve had not been buying 40 plus percent of the treasuries during the Biden term, right? You think interest rates would have stayed the same?

Dr. KOHN. No, I think the treasury rates would have been a bit higher and mortgage rates would have been a bit higher, and rates on auto loans would have been a bit higher, and there would be less spending on houses, autos, and the recession would have been deeper.

Senator SCOTT. OK. All we did is we decided when we do that, so now what's happening, like in my State, is the interest rates are not coming down. Long-term rates are not coming down, then the value of homes are coming down. So, what they did is they caused a significant asset bubble,

Dr. KOHN. But that's not under the control. You said the Fed wants to control everything. What they want to control are the rates at the very short end of the market, the repo rates—



Senator SCOTT. That's not what they bought. They bought long term, but now they are getting rid of them, right?

Dr. KOHN. Yes.

Senator SCOTT. They bought long term.

Dr. KOHN. Yes. In order to keep those rates down, they stopped doing it. They were until December 1st, reducing the amount of securities.

Senator SCOTT. They caused this ridiculous bubble. Now what's happening in my State, people are getting their butts kicked. They bought a house, right? They bought a house and now the prices of the house is coming down because interest rates are not coming down.

It hurts the poor. Again, it's always the poorest families that get hurt. The rich have plenty of cash. They can't do it. The people are leveraged to the hilt. They are getting their butts kicked. It's so frustrated. They cause these bubbles. Then the poorest people are the one that get hurt.

Chairman PAUL. Thank you. One of the points that Dr. Kohn made is that the Fed tries to accommodate the public's demand for money. I guess I would argue that particularly in the subprime loan crisis, that it was made worse by the Fed creating interest rates below the market rate. In a real economy where the interest rates, because they are set by a vote.

We do not set the price of bread by a vote. This isn't a real good, real market pricing system. A bunch of old guys at the Fed vote on what the price of money should be. But in a real economy that has freely floating interest rates, if you have a housing boom and everybody wants to borrow money, you have increased demand for the money, the response would be the interest rates would rise.

But you had a period of time from like 2000 to 2007 where you got interest rates are like two, which is essentially zero. If you got inflation of two or three, and you got interest rates of two, your real interest rates is like zero. That's not a real interest rate. I don't think the market would do that.

As you have this housing boom, interest rates would have risen. The cycle of the economy is incredibly dependent on interest rates to tamponade the effect of the boom. As you get a boom, as interest rates go up, only the better projects, the ones more likely to succeed will happen. If I am borrowing something with no capital and stuff, like I am falling away as interest rates go up.

But if you don't allow that, you are part of what creates the boom, the Federal Reserve was responsible in some way for the boom by keeping interest rates below the market rate. I am not going to start with you, but I will come back to you. Let's start with Dr. Michel. What do you think of what I said?

Dr. MICHEL. It definitely has an effect on rates. It's probably not positive in the sense that it's not a good outcome. But I also think it's very important that we don't divorce what the Fed's doing in that regard from what the rest of the Federal Government is doing. The Fed didn't decide to create tarp. So, there's a lot of money floating around and any of the money that they did provide for liquidity could have been provided through Congress. A lot of it was done in both places. I think it's hard to separate out—

Chairman PAUL. The low interest rates leading up to it also have a reason. I think, one, they may say they want to help the economy, but they are really trying to keep the financing of a \$38 trillion debt manageable. That's a big reason for why we will——

Dr. MICHEL. Also combined. Yes.

Chairman PAUL. Yes.

Dr. MICHEL. Yes.

Chairman PAUL. Ryan?

Mr. YOUNG. Yes, it's a question of tradeoffs. If you lower interest rates, yes, you lower the price of government debt and that can be very important for the Federal Government's fiscal health. But the tradeoff of that is higher inflation for the rest of us. So you can choose one policy or the other, but you can't choose both because there will always be a tradeoff.

Chairman PAUL. Mr. Wesbury.

Mr. WESBURY. Yes. Bubbles as well. I mean, Ryan, you are absolutely right. The interesting thing today is pre-2008, we had a scarce reserve system and banks traded reserves, every single day there was a marketplace. Once we have made abundant reserves, nobody trades Federal funds. There is no market rate anymore. Dr. Paul, you are absolutely right. They sit around a table and they go, what do you think? Three and a quarter? Three and a half——

Chairman PAUL. But I guess my response to that is between 2000 and 2007, we were still doing, as you say, having this daily marketplace. I would still argue that from 2000 and 2007, that the interest rates were at the direction of the Fed below the market.

Mr. WESBURY. I agree. Because they were adding reserves that they shouldn't have added. It can happen under either system. It can totally happen. But today there is no market input at all. That's what I would argue. That the Fed cannot see the demand for money, when the rate would want to go up under the old system, that was a demand for money. Today there is no sign of demand for money like that.

Chairman PAUL. I think we have pretty good focusing of this debate. Is this debate going on outside this room?

Mr. WESBURY. I wish it was going on more. One of the things I will say is that you and your staff study, which is fantastic. For the first time that I know of forced Chairman Powell to address the ample abundant reserve issues in a speech because the Federal Reserve has kind of ignored, acted as if it doesn't really exist and the press doesn't ask questions. Thank you for pushing this.

Chairman PAUL. I think the point that we have gotten to is a better and more important point about whether the treasury loses money, the profit loss of the Fed. We are talking about whether or not the interest rates are being set by a daily marketplace versus a long-term thing, which seems to be more of a decision by fiat, a decision by a bunch of, let's just call them grumpy old man around the table.

Mr. WESBURY. I call it brace fixing.

Dr. KOHN. I don't think there's any difference between the way rates basically were set before 2008, and I was part of this back into the 1970s when I joined the Federal Reserve. Every day we had a call with the Federal Reserve Bank in New York and the

board staff decided how much money they needed to put in or take out in order to fix the interest rate, right?

The mechanism was a little different under scarce reserves. But the control of the Federal funds rate of the short-term interest rates, the repo rates, were just as strict before 2008 as after 2008.

Chairman PAUL. I would argue that one of the things that brought down the Soviet Union is that nobody knew the correct price of bread because the marketplace doesn't work because nobody does. I set it here and then I have bread rotting on the shelves. I set it too low, all the bread's gone.

The only thing that can figure out, and this is the miracle of capitalism, is that supply and demand, and as Senator Johnson, millions and billions of people trading instantaneously leads to justice, this incredible knowledge that no one possesses, right? It was this whole idea that Hayak talked about. The conceit of a bunch of 10 really smart men. I am not begrudging the people of the Fed not being smart.

They probably are very smart, but they are not as smart as a million people in the marketplace. What we should try to do is have as little impact from the Fed on what interest rates are and figure out a way if there is a transition to a more market oriented where most of the interest rate is determined by the market because I think between 2000 and 2007 under the old system, they were manipulating it.

I think it caused the subprime crisis. I agree mark to market probably exponentially made the subprime crisis work, but it got started with the subprime crisis, which I think is directly related to interest rates being lower than what the market would have dictate—

Dr. KOHN. I mean, the market controls every interest rate beyond the overnight interest rate. If the market thought what the Fed was doing was right now, lowering rates was inflationary, you would see it in the bond market and you don't see it.

Chairman PAUL. Then they also control the money supply. Don't you think the money supply has something to do with interest rates also?

Dr. KOHN. I think it's the amount of money, the M2 money supply, the amount of money people want to hold at the current interest rate. Yes.

Mr. WESBURY. I would argue the Fed influences interest rates out the yield curve too. That's what the whole idea of forward guidance is. I do not mean to take us off this path, but they have tried to influence long-term rates with forward guidance and by buying different parts of the yield curve—

Dr. KOHN. In these zero interest rate situations—

Mr. WESBURY. Under the old system, they certainly could hold interest rates lower than they should. And they did. They, in fact, they helped cause the housing bubble. The interesting thing is, in that system at least there was some market input, Federal funds trading desk giving a signal.

Under this current system, there is no market input. As a result, I think it's even moving back a step to that scarce reserve system would be a step forward. Then we can talk about moving forward.

Chairman PAUL. Dr. Kohn, are you familiar with the Austrian understanding of the business cycle and explanation of the business cycle? Do you accept the idea?

Dr. KOHN. A little bit.

Chairman PAUL. The ideas were basically that inflation and the effects of expanding credit hit different segments of the economy at different times. They lead to misinformation. They lead to a theory that you believe you are better off than you actually are. And so capital goods makes a decision. Consumers make a decision. There's a time lag between these two.

By the time it catches up and the consumers say, "Oh gosh, we have three times as much money." It's worth a third less the capital goods people are still making stuff. Then that differential and that separation is what causes it. That it isn't like on TV, it's presented as "Well, gosh darn it, we just don't know what causes inflation and we don't know what causes it. It's just a mystery what causes the business cycle." I think it was actually explained pretty well by the Austrians.

Dr. KOHN. Yes. I think I agree that expectations are very important for how people spend and they form their expectations by looking around them. I also agree that people tend to get very optimistic in the up parts of the cycle and very pessimistic in the down parts. That's consistent with the story they are telling.

Chairman PAUL. The key fact is that counteracts either irrational exuberance or any of that is the interest rate. If the interest rate doesn't rise, it's the one price that is universally throughout the economy. It's the one thing that will slow an economy down that is going too rapid. By too rapid, I don't know that it just there is a point at which the economy is growing so rapidly that you feel you are in a bubble.

It's not my job to figure that out or to tell the economy to stop. But as interest rates rise, less things will be financed. There will be less loans.

Dr. KOHN. There was very little inflation in 2006 and 2007. I was voting on interest rates in 2006 and 2007, and we did raise rates for a while up to around five percent, I think. So not two percent, but more like five percent. So the real rates were positive.

There was an argument, and I have had this discussion with John Taylor for example, that the Fed should have raised rates a little more because the inflation threat was higher. I think the problem was regulation. There was too much deregulation, there was too much reliance on the private sector to make decisions and without constraint, and without recognizing the knock-on effects, the externalities economists call them of the decisions they were making.

And risk built up in this euphoria to your point about cycles. Then when it collapsed, it really collapsed. You are right. It was a loss of confidence that really caused the financial crisis in 2008. The losses were there.

Chairman PAUL. Thank you.

Senator JOHNSON. I just have one question. It does relate with markets setting interest rates. My stance, is there's two problems. I just wanted to ask whether they ever consider the other problem. Obviously interest rates too high, it constricts economic growth.

Too low, it could maybe lead to exuberance. Is there ever a consideration of the misallocation of capital within that?

In terms of where capital actually flows, first of all, just in terms of far riskier assets, which can misallocate capital, is that ever part of the equation? Or is it simply just, is the economy going to heat up? It's going to slow down?

Dr. KOHN. That's part of the discussion, but the Fed really has one instrument. Let's forget the QE period. Under 95 percent of the time, the Fed is trying to balance the economy using the short-term interest rate and giving them another target telling them that maybe a problem.

Senator JOHNSON. Yes, I am not asking them to manage. I mean, is that a consideration? Have anybody looked back for the last 25 years and go, man, we really misallocated capital. We had too many things flow into this sector of economy because we kept interest rates artificially wrong. It was just free money. Or am I just off base here?

Mr. WESBURY. It happened in the housing bubble in 2005, 2006, 2007, and I would argue we have misallocated capital toward government with these zero percent interest rates in nine out of the last 15 years. When you have zero percent interest rates, it's pretty easy to finance government and make it seem cheaper.

Senator JOHNSON. It's been more than nine out of the last 15 years.

Mr. WESBURY. Yes. But I mean zero. They had zero.

Senator JOHNSON. I am getting this misallocation to the government.

Mr. WESBURY. By the way, it's one of the arguments that I would use about getting rid of interest on reserve balances. The Fed did hold interest rates basically at zero for nine years. That was OK by them. Now when we want to get rid of interest on reserve balances, they go, "Well, you can't force us to hold them at zero. We can only hold them at zero when we want to."

And so, I would argue that's not a really good argument to make.

Senator JOHNSON. By the way, you are right, the primary misallocation was to government.

Mr. WESBURY. Yes. It was also the houses and other things. But the Austrian business cycle is a fabulous thing. That misallocation of resources happens when you hold interest rates too low.

Chairman PAUL. I think this has been my favorite hearing of the whole year. Even though the minority says it wasn't under our jurisdiction, the one prerogative of the chairman is I get to decide what is under my jurisdiction. We were not creating law today, but I think we had a very helpful discussion.

We had viewpoints, I think, across the spectrum. I think it was very good. I hope we will pursue this. To each of the participants, Republican and Democrat, I am happy to hear from you anytime. If you have advice, something you have written and you want to send it to us, I don't claim to know everything about it.

I mean this much and like the subject and want to know more. But I would claim a lot of other people are in the same boat, not necessarily that there is some committee that knows more than the rest of us.

But thank you all for coming. The record for this hearing will remain open until 5 p.m. on Friday, December 12, 2025, for the submission of statements and questions for the record. The hearing is now adjourned. Thank you.

[Whereupon, at 11:47 a.m., the hearing was adjourned.]

## A P P E N D I X

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**‘Ranking Member Peters Opening Statement as Prepared for Delivery  
Full Committee Hearing: The Fed’s Big Bank Welfare Program: Oversight of the Fed’s  
IORB Regime  
December 11, 2025**

Thank you, Chairman Paul, and thank you to the witnesses for appearing before the Committee today.

The Federal Reserve plays a critical role in implementing sound monetary policy to strengthen markets and the overall economy.

The focus of today’s hearing is on the Fed’s authority to pay interest on reserve balances, which Congress created under the Financial Services Regulatory Relief Act of 2006 and directed the Fed to implement in response to the 2008 financial crisis.

Commercial banks hold cash balances at the Fed, known as reserves, that play an important role in keeping financial markets functioning.

The Fed pays interest on those reserves, allowing the Fed to set target interest rates that affect rates on everything from mortgages to car loans.

The Fed also receives interest payments from banks on the securities backing those reserves, which the Fed sends to the Treasury in the form of remittances.

According to publicly available data, in the past 16 years that the Fed has held this authority, it has remitted over \$900 billion to the Treasury, even after making these interest payments.

While the last two years saw negative remittances, primarily due to necessary responses to support the economy during the COVID-19 pandemic, the Fed has recently stated that it expects its negative remittances to turn positive again soon.

Repealing this authority would not save any money for taxpayers.

Without this authority, the Fed would lose control of its ability to set a “floor” interest rate for lending. Economists predict this would result in collapsing interest rates and much higher inflation.

To restore rates, the Fed would need to shrink the level of reserves at an unprecedented speed and volume, introducing volatility, compromising market resilience, and leaving the banking system prone to shocks.

Stability is critical. American financial markets remain the envy of the world, in no small part due to the stability, efficiency, and liquidity provided by the Fed.

If banks did not receive these payments on their reserves, they would simply buy other government securities that the government pays interest on, like Treasury securities, and as a result, be more prone to economic volatility.

Ultimately, this all comes back to affordability and making our economy work for small businesses and families. Economists argue that repealing this authority would disproportionately harm small and community banks and make borrowing harder for business and consumers.

Unfortunately, like so many things under President Trump, the Fed has been needlessly politicized. We are currently facing a dangerous, ongoing threat to Fed independence. After repeatedly pressuring the Fed to lower interest rates, President Trump has tried to fire Fed Governor Lisa Cook and has called for Chair Jerome Powell to be replaced. These actions are politically motivated, and Congress must stand up for the Fed's independence and ensure monetary policy remains insulated from political pressure.

Finally, while oversight of the Federal Reserve is important, this Committee has neglected to hold oversight hearings on numerous topics that are actually in our jurisdiction, including FEMA's failures in responding to disastrous floods in Texas this spring, persistent cyber attacks by our adversaries against our federal IT and critical infrastructure networks, or the Administration's efforts on border security and drug trafficking. In fact, our colleagues on the House Homeland Security Committee are sitting down for a hearing right now across the Capitol for a hearing to evaluate the threats posed to our homeland, a serious topic that demands this committee's attention.

I hope Mr. Chairman, that you will prioritize hearings with Administration officials on all these issues so that we can fulfill our responsibility to conduct oversight of the Executive Branch.





Testimony  
Before the U.S. Senate Homeland Security & Governmental Affairs Committee  
Hearing on "Interest on Reserves Payments "

Norbert J. Michel  
VP and Director  
Center for Monetary and Financial Alternatives, Cato Institute

December 11, 2025

**Introduction**

Chairman Paul, Ranking Member Peters, and Members of the Committee, thank you for the opportunity to testify at today's hearing. My name is Norbert Michel, and I am Vice President and Director for the Center for Monetary and Financial Alternatives at the Cato Institute. The views I express in this testimony are my own and should not be construed as representing any official position of the Cato Institute.

In 2008, as part of its response to the 2008 financial crisis, the Federal Reserve purchased large quantities of long-term Treasuries and mortgage-backed securities. These purchases, and the corresponding dramatic increase in the Fed's balance sheet, were highly controversial, with many people fearing the Fed's actions would rapidly lead to higher inflation. However, the Fed managed to keep inflation in check after those purchases created enormous quantities of excess reserves by implementing a new operating framework, one where it began paying interest on banks' excess reserves.

This operating framework, which received much less attention than the Fed's asset purchases themselves, effectively divorces the Fed's monetary policy stance from the size of its balance sheet. In other words, unlike under its previous operating framework, the Fed's asset purchases, which increase bank reserves, could no longer automatically be associated with expansionary monetary policy (or its natural effect, inflation).

**Traditional Monetary Policy Framework**

A central bank exercises monetary control by regulating the economy's overall liquidity (the availability of cash or cash-like assets) to indirectly influence the economy's general course of spending, prices, and employment. Prior to the 2008 financial crisis, the Fed exercised

monetary control mainly through open market operations, that is, the buying and selling of short-term Treasury securities on the open market.<sup>1</sup>

The Fed conducted these operations with the specific intent of increasing or decreasing the quantity of reserves—a highly liquid asset—in the banking system, thereby increasing or decreasing the amount of money that banks could lend. This system worked because banks need reserves to make new loans, and only the Fed can increase (or decrease) the total amount of reserves in the banking system.

Under this traditional framework, when the Fed wanted banks to create less money, it took reserves out of the banking system by selling the Fed’s own securities. These sales reduced the aggregate amount of money that banks could create because it caused banks to use reserves for buying securities from the Fed rather than for funding additional private loans. Conversely, when the Fed purchased securities on the open market it increased reserves in the system, thus enabling banks to create more money with new loans. When an individual bank did not have enough reserves to make more loans (create more deposits or currency), it would simply borrow those reserves from another bank. Thus, while the Federal Reserve decided the total amount of reserves in the banking system, private banks ultimately determined how those reserves were allocated throughout the system.

Traditionally, banks commonly lent and borrowed reserves to satisfy their legal (and precautionary) requirements. This activity took place in the federal funds market, so named because banks hold reserve balances at the Federal Reserve. Traditionally, the interest rate in this lending market, the federal funds rate (FFR), was a market-determined rate. In other words, private banks’ lending negotiations—not the Federal Reserve—determined the FFR. While the Federal Reserve did not set the FFR itself, it did set a *target* for the FFR based on ensuring that overall liquidity was consistent with its broader macroeconomic goals. The Fed then conducted its open-market operations to ensure that the FFR stayed near the desired target.

#### ***Influencing Rates vs. Setting Rates.***

The Fed did not set the FFR, but the Fed’s open market operations typically had a great deal of influence on the FFR—especially over short intervals—because the Fed is the monopoly supplier of bank reserves. While the Fed determines the total quantity of reserves in the banking system, market forces (banks’ decisions based on their individual reserve needs) determined the distribution of reserves *within* the system in the traditional framework. This process allowed the Fed to rely on banks’ demand for reserves as a decent indicator of the demand for money (or, more generally, liquidity). The aggregate demand for reserves, in conjunction with the total supply, ultimately determined the FFR.

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<sup>1</sup> Norbert Michel, “The Crisis Is Over: It Is Time to End Experimental Monetary Policy,” Heritage Foundation [Backgrounder No. 3265](#), November 9, 2017.

By adjusting the supply of reserves in the system “just enough” to meet the demand for reserves at its chosen target, the Fed was (in theory) able to offset changes in demand without disrupting market forces. In such a system, the target FFR is merely a means to an end—it is a policy instrument but it is not a policy objective.

This policy framework depends on the Fed keeping a minimal footprint in the market for reserves, causing some economists to refer to the traditional framework as a *reserve-scarcity* regime. All else constant, a scarcity of reserve balances (relative to demand for reserves) results in a larger volume of reserve lending between banks. In such an operating environment, the FFR conveys information based largely on conditions in private credit markets, as perceived by the private lenders and borrowers putting their capital at risk.

On the other hand, the Fed’s open market operations would have very little influence on the federal funds market if reserves were more attractive (on a regular basis) than other uses of funds. In such an environment, with plentiful reserves that have little opportunity cost, banks would find it unnecessary to borrow reserves and the FFR would no longer be the result of the same market process. In fact, the enormous buildup in reserves during the 2008 crisis ultimately caused interbank lending markets to break down and contributed to the Fed abandoning its traditional operating procedures. As a result of switching to the new operating procedures, daily trading volume in the fed funds market fell from its pre-2008 level of \$150–\$175 billion to just \$60–\$80 billion in the mid-2010s.<sup>2</sup>

#### Post-2008 Monetary Policy Framework

As the 2008 crisis unfolded and the Fed engaged in more emergency lending, the Fed found it difficult to meet its overall macroeconomic goals and maintain what control it had over the FFR. While trying to keep inflation under control required tighter monetary conditions, providing emergency liquidity to the financial system required looser monetary conditions. To resolve these policy conflicts and allow further emergency liquidity provisioning, the Fed changed its operating framework by moving to a system that depends on making interest payments on reserves.

Economists have long recognized that requiring banks to hold non-interest-bearing reserves acts as a tax on bank deposits and, therefore, on bank depositors.<sup>3</sup> However, the Fed

<sup>2</sup> Gara Afonso et al., “[Who’s Borrowing and Lending in the Fed Funds Market Today?](#),” *Liberty Street Economics* (blog), Federal Reserve Bank of New York, October 10, 2023.

<sup>3</sup> Norbert Michel and Jai Kedia, “[Reforming the Federal Reserve, Part 5: Ending the Interest on Reserves Program](#),” July 11, 2025. The same economic arguments do not apply to banks’ decisions to hold excess reserves, and prior to 2008 it was long-standing bank management practice to minimize excess reserves. Timothy Koch, *Bank Management*, 3rd ed., (Orlando, FL: The Dryden Press, 1995), p. 462. The idea of paying interest on required reserves was considered, though ultimately rejected, when Congress created the Federal Reserve in 1913. Also see *Monetary Policy v. Fiscal Policy: Risks to Price Stability and the Economy*, George Selgin, [testimony](#) before the Monetary Policy and Trade Subcommittee, Committee on Financial Services, U.S. House of Representatives, July 20, 2017.

asked Congress for this authority for reasons that went well beyond merely offsetting the cost of reserve requirements. In his memoir, former Fed Chair Ben Bernanke explained the request as follows:

We had initially asked to pay interest on reserves for technical reasons. But in 2008, we needed the authority to solve an increasingly serious problem: the risk that our emergency lending, which had the side effect of increasing bank reserves, would lead short-term interest rates to fall below our federal funds target and thereby cause us to lose control of monetary policy. When banks have lots of reserves, they have less need to borrow from each other, which pushes down the interest rate on that borrowing—the federal funds rate.

Until this point we had been selling Treasury securities we owned to offset the effect of our lending on reserves (the process called sterilization). But as our lending increased, that stopgap response would at some point no longer be possible because we would run out of Treasuries to sell. At that point, without legislative action, we would be forced to either limit the size of our interventions... or lose the ability to control the federal funds rate, the main instrument of monetary policy.

So, by setting the interest rate we paid on reserves high enough, we could *prevent the federal funds rate from falling too low*, no matter how much lending we did.<sup>4</sup> (Emphasis added.)

As this passage demonstrates, Fed officials believed that paying interest on reserves would help the Fed hit its interest rate target, and that the rate they paid on reserves would serve as a *floor* for the FFR. Their intent had been to create a *corridor* system, whereby the interest rate on reserves would be set below the target FFR. However, the Fed did not successfully create a corridor system due to its conflicting goals.

The Fed wanted to pay interest on excess reserves so that banks would hold their excess reserves at the Fed rather than lend them in the federal funds market. The only possible way to accomplish this task, of course, was to offer banks a *higher* rate of interest on excess reserves than they could earn by lending those reserves in the federal funds market. Thus, the rate it paid on these reserves could not serve as a floor for the FFR *and* sterilize the Fed's asset purchase/emergency lending operations.

The Fed's flooding of the banking system with reserves in the aftermath of the 2008 crisis necessitated reliance on the interest on reserve (IOR) program because the Fed lacked an alternative way to dissuade banks from using those reserves to create new loans and deposits. In this new "abundant reserve" framework, changing the *quantity* of these reserves no longer affects the FFR, so normal open market operations—the buying and selling of Treasury

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<sup>4</sup> Ben Bernanke, *The Courage to Act: A Memoir of a Crisis and Its Aftermath* (New York: W.W. Norton & Company, 2015), pp. 325-326.

securities—became an ineffective tool for implementing monetary policy. However, the IOR should still be effective at changing the interbank lending rate because banks generally will not lend to other banks at rates lower than the risk-free rate at which they can collect interest from the Fed. Consequently, changing the IOR rate to affect the cost of holding reserves is now the Fed’s main instrument for changing the FFR and thereby conducting monetary policy.

#### Complications of the New Framework

The Fed’s IOR program has been a controversial inclusion to US monetary policy. While the program received little attention from critics prior to the COVID-19 crisis, that inattention is largely due to interest rates being at historic lows.<sup>5</sup> That is, because the US remained in a period of historically low interest rates, the Fed’s interest payments through the IOR program were relatively small. However, because interest rates rose in response to the post-pandemic surge in inflation, the Fed has disbursed billions in risk-free government payments to large banks. These losses, of course, have brought unfavorable political attention to the program.<sup>6</sup>

As Figure 1 shows, the Fed’s interest payments (adjusted for inflation to 2024 dollars) have increased dramatically.<sup>7</sup> Moreover, the rate of increase in interest expenses closely mirrors the rate of increase in the rate the Fed pays out on the reserves (the “IOR” rate). This latter fact was not true in the late 2010s when the Fed raised the IOR but kept interest payments in check because it only paid interest on excess reserves as opposed to on *all* reserves, a policy it changed during the pandemic.

As Figure 2 shows, these large interest expenses resulted in the Fed’s only recorded losses since 2008 and the only losses on record since the data became available. The Fed has mostly hand-waved these losses away and used financial gimmickry to label them “deferred assets” that they have promised to balance with future profits.<sup>8</sup>

<sup>5</sup> Norbert J. Michel, “[Risks from Fed’s Interest on Reserves Threaten More Than Monetary Policy](#),” *Forbes*, April 6, 2015.

<sup>6</sup> Jai Kedia, “[Fed’s IOR Gamble Results in Second Straight Year of Operating Losses](#),” *Cato at Liberty*, March 31, 2025. For more on the asset side of the Fed’s balance sheet, see Norbert Michel and Jai Kedia, “[Reforming the Federal Reserve, Part 4: Restoring Sensible Asset Purchases](#),” *Cato Institute*, June 25, 2025.

<sup>7</sup> This figure, as well as much of this section of the testimony, relies heavily on Jai Kedia, “[Fed’s IOR Gamble Results in Second Straight Year of Operating Losses](#),” *Cato at Liberty*, March 31, 2025.

<sup>8</sup> Federal Reserve Board of Governors, “[Federal Reserve Board announces preliminary financial information for the Federal Reserve Banks’ income and expenses in 2023](#),” Press Release, January 12, 2024.

Figure 1

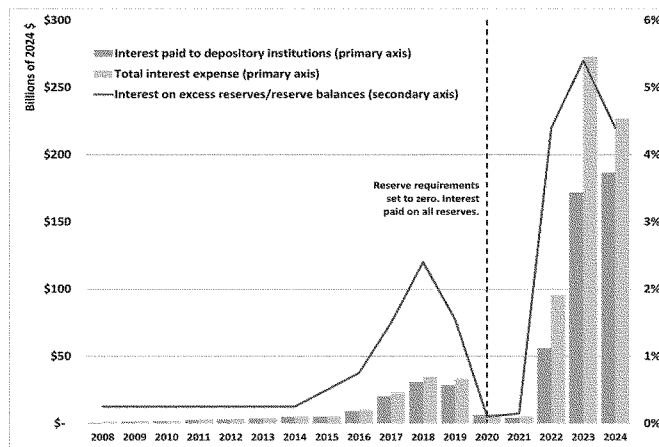
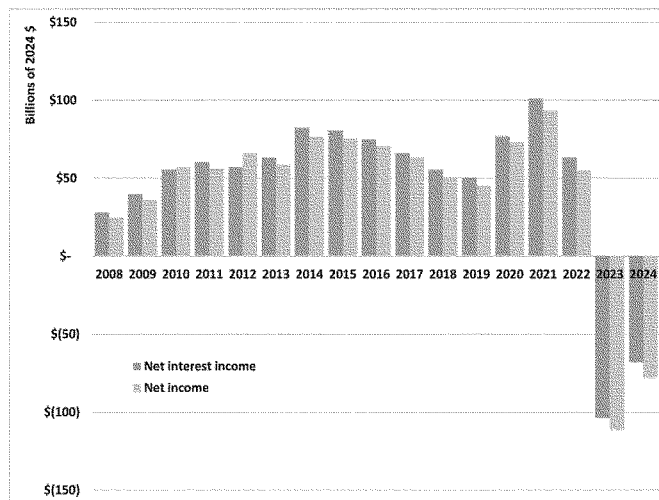


Figure 2



One obvious problem with these current events is that there is no guarantee interest rates will come down to their pre-pandemic levels, reducing the Fed's interest burden and allowing its financials to turn back to profit rather than loss. Even if the Fed manages to turn a profit, taxpayers are unlikely to reap those benefits. It will likely take years of future profits to offset the nearly \$200 billion the Fed has already lost in the past two years alone—profits that would usually go to the Treasury to help relieve some of our massive fiscal deficit.

Regardless of the future path of interest rates, the IOR program provides billions of government dollars to large financial institutions as risk-free interest, essentially giving banks a massive government handout. The average American, though, earns close to nothing on their own savings accounts at these same institutions.

Moreover, the IOR program leaves banks with little incentive to borrow from each other or lend funds to the public, resulting in significantly lowered activity in the federal funds market.<sup>9</sup> One consequence of this inactivity has been a dampening of the effects of the FFR on other borrowing costs.<sup>10</sup> At the same time, inflation went far beyond the Fed's 2 percent target, ultimately requiring the Fed to severely tighten its monetary policy stance. By late 2023, the Fed had increased the FFR by raising the IOR rate to 5.40 percent. The consequence of this post-pandemic policymaking was a dramatic increase in both the principal and interest rate of the Fed's liabilities.

Fed officials are largely unconcerned about losses from interest payments or the deferred assets they create to offset these losses. According to a press release: "A deferred asset has no implications for the Federal Reserve's conduct of monetary policy or its ability to meet its financial obligations."<sup>11</sup>

It is technically true that the Fed can continue to exhibit losses, as it does not require operational profitability like a private financial firm does, but this view is unwarranted. Indeed, if the Fed were a private bank, any one year of such losses may have been enough to shutter its business. Still, while the Fed is not a private bank and it can sustain these losses for a longer period, it is not true that there are no causes for concern due to these losses and the IOR framework. The following list provides four major reasons for concern over the IOR framework and the resulting Fed losses.

- **The economic costs of these losses are high.** Assuming that marking off future profits to account for current losses has no economic effects is economically unsound. Balancing books via accounting rules ignores opportunity costs. That is, accounting rules do not

<sup>9</sup> Norbert Michel and Jai Kedia, "[Reforming the Federal Reserve, Part 5: Ending the Interest on Reserves Program](#)," July 11, 2025.

<sup>10</sup> Jai Kedia, "[Borrowing Rates Much Less Correlated with Fed's Policy Rate](#)," *Cato at Liberty* (blog), Cato Institute, October 24, 2024.

<sup>11</sup> "[Federal Reserve Board Announces Preliminary Financial Information for the Federal Reserve Banks' Income and Expenses in 2023](#)," news release, Federal Reserve, January 12, 2024.



quantify the gains that could have been achieved from using funds for alternative purposes, such as paying down federal debt. In fact, for decades profits from the Fed's operations have been remitted to the Treasury and gone toward paying off the federal government's massive fiscal deficit. Now, the Treasury will have to issue even more debt, which will lead to an even greater fiscal imbalance. In other words, these higher interest payments will place a higher burden on future taxpayers even though the Fed's accounting costs appear to be zero.

- **The IOR framework creates a conflict of interest with the Fed's mandate to stabilize prices.** The Fed's primary mechanism for achieving stable prices is to influence the FFR by altering the IOR. Specifically, to combat inflation, the Fed tightens its monetary policy stance by raising the IOR. However, as shown in Figures 1 and 2, increases in the IOR result in large interest expenses and consequently losses for the Fed. Despite what they may claim publicly, Fed officials cannot continue to exhibit losses on their financial statements indefinitely. Realistically, at some point, large financial losses would undermine the Fed's ability to support the banking sector and the US government's ability to issue new debt, just as it would in politically unstable countries. Moreover, losses create a potential complication for monetary policy because the Fed must increase the IOR to combat inflation even though every increase in the IOR rate increases the Fed's potential losses.<sup>12</sup> This inherent conflict only makes the Fed's fight against inflation more difficult.
- **The IOR system facilitates government support for the private financial sector.** At its core, the IOR policy is a government subsidy to large financial institutions. Banks now have their own risk-free savings accounts, giving them returns that are hundreds of basis points higher than what regular consumers receive on their own deposits at the very same institutions (the current rate is 3.9 percent).<sup>13</sup> Moreover, the billions that banks receive in interest payments have reduced their incentive to lend in the private market, reducing the cash available to regular Americans to borrow while flooding the banking system with trillions in reserves.
- **More accessible money spigot.** The IOR framework divorces the Fed's monetary policy stance from the size of the Fed's balance sheet. It is designed to allow the Fed to purchase as many assets as it would like, all while paying firms to hold on to the excess cash that these purchases create. This framework can all too easily allow the Fed to be a

<sup>12</sup> Jai Kedia, "[Pandemic Policymaking Warrants Narrower Fed Mandate](#)," *Cato at Liberty* (blog), Cato Institute, December 6, 2023.

<sup>13</sup> Board of Governors of the Federal Reserve System (US), Interest Rate on Reserve Balances (IORB Rate) [IORB], retrieved from FRED, Federal Reserve Bank of St. Louis; <https://fred.stlouisfed.org/series/IORB>, December 6, 2025.



pawn of the Treasury, enabling the government to run larger deficits. It also opens new opportunities for political groups to pressure the Fed for direct funding.

### **Winding Up the IOR Program**

In the wake of the 2008 crisis, the Federal Reserve made trillions of dollars in emergency loans and expanded its balance sheet by purchasing large quantities of long-term Treasuries and MBS. These operations gave rise to an experimental policy framework that replaces traditional market activity with bureaucratically administered interest rates. To normalize monetary policy and restore the market forces that the Fed has displaced, the Fed must shrink its balance sheet *and* end the IOR program.

Prior to the 2008 financial crisis, the Fed's balance sheet held less than \$1 trillion in securities, and its total assets rarely exceeded 10 percent of the commercial banking sector's total assets. After the financial crisis, this share has regularly exceeded 20 percent, with asset purchases during the pandemic increasing the share to 40 percent (and inflating the balance sheet to nearly \$9 trillion at its peak in 2022). Since 2022, the share has fallen to 28 percent, and the Fed now holds approximately \$6.5 trillion in assets.

Many point to the dangers of rapidly shrinking the Fed's balance sheet and ending the IOR program, and they are right to be concerned.<sup>14</sup> An immediate end to the IOR program would result in banks rapidly lending those reserves to the public. Such a sudden and large outflow of cash from banks into the wider economy could cause high inflation. But a careful approach that winds down the size of banks' balance sheets over time would allow the repeal of IOR while also ensuring consumers don't suffer another bout of severe inflation.

Congress should require the Fed to implement a plan that shrinks the balance sheet in no more than 15 years, approximately the same amount of time it took to enlarge the balance sheet since the aftermath of the 2008 financial crisis. The goal should be to reduce the Fed's holdings to no more than the pre-2008 share of the commercial banking sector. Congress should also limit the size of the Fed's balance sheet by, for example, capping the Fed's total assets at no more than 10 percent of the commercial banking sector's total assets, the approximate share held by the Fed prior to the 2008 financial crisis.

Naturally, these changes would come with an implicit promise to end quantitative easing as a monetary policy tool. At that time, the Fed's authority to pay interest on reserves should be repealed. In this scenario, bank reserves would once again be scarce, and the system would revert to an interest rate corridor with the FFR divorced from the value of the IOR. Consequently, eliminating IOR would be minimally economically disruptive.

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<sup>14</sup> Bank Policy Institute staff, "[Prohibiting Interest on Reserves Harms the Economy and Disrupts Credit Markets](#)," October 9, 2025.

**United States Senate**  
**Committee on Homeland Security and Government Affairs**  
**SD-342 Dirksen Senate Office Building**  
**December 11, 2025**  
**Hearing on “The Fed’s Big Bank Welfare Program: Oversight of the Fed’s IORB Regime”**  
**Written Statement of Ryan Young**  
**Senior Economist**  
**Competitive Enterprise Institute**

Chair Paul, Ranking Member Peters, and distinguished members of the committee, thank you for holding this hearing and inviting me to testify today.

My name is Ryan Young. My work focuses on monetary policy, trade policy, and regulatory policy at the Competitive Enterprise Institute, a non-partisan public policy organization that concentrates on regulatory issues from a free-market perspective.

I am pleased to speak to you today about a bipartisan goal: ending interest on reserve bank deposits (IORB). This is the practice of the Federal Reserve paying interest on account balances that other banks hold at the Fed.

IORB was enacted in 2008 in response to the financial crisis. It has since proven to have few benefits and many drawbacks. It is time to end it.

The two IORB problems I wish to highlight today are cronyism and inflation.

First, cronyism. The Committee’s report points out that, in 2024, the Fed paid about \$180 billion in IORB to banks. While this number is likely to drop in 2025 and 2026 due to lower interest rates, it is still a bad look for the Fed.

IORB is free money for banks that don’t need the help. Similar to Wall Street bailouts from past years, free IORB money encourages banks to take on risks they would otherwise avoid, and at taxpayer expense if they go bad. As we have found out the hard way several times over the years, extended excessive risk-taking rarely ends well. If a recession or financial crisis hits, IORB could be both a contributor to the problem, and a prelude to more taxpayer bailouts.

The money spent on IORB payments has other potential uses. It could have gone to the Treasury instead; \$180 billion is equivalent to about one-tenth of last year's budget deficit. Savings from ending IORB could also have more than covered the Fed's 2024 operating losses of \$114 billion.<sup>1</sup>

The second IORB problem I wish to discuss is inflation. IORB raises inflation risk in two ways: First by potentially influencing the Fed's federal funds rate decisions, and second by influencing its open market operations policies.

A high federal funds rate already has unintended consequences, such as higher interest rates on government bonds. This makes government debt more expensive to repay, and is one reason why the political branches often pressure the Fed to lower rates.

IORB creates an additional unintended consequence: The higher the federal funds rate, the higher the Fed's Board of Governors has to set the IORB rate. Otherwise, banks will take their money out of the Fed and try to earn a better return elsewhere.

But the higher the IORB rate, the more likely is the Fed to incur an operating loss. In fact, IORB payments alone exceeded the Fed's 2023 and 2024 operating losses.

The Federal Open Market Committee (FOMC) has a tough job as it is. IORB makes its job even more difficult. IORB, especially at the large scale it has reached in recent years, can potentially influence the FOMC to set interest rates lower than it would otherwise prefer, in order to save money on IORB payments.

IORB can also tempt the Fed to grow the money supply through open market operations, which can also cause higher inflation.

If you or I were to buy government bonds, we would have to use our own money, and take that money away from other potential uses. Unlike us, the Fed doesn't have to navigate that tradeoff. If it wants, it can buy government bonds with dollars it newly creates out of thin air. This is how the Fed can directly grow the money supply.

This was also the main driver of COVID-era inflation. From 2020-2022, the Fed added nearly \$5 trillion to its balance sheet.<sup>2</sup> This roughly quadrupled its usual rate of money supply growth, and the inflation rate roughly quadrupled to match.

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<sup>1</sup> Asher Rose, "Fed projected to turn profitable again after three years of losses," Peterson Institute for International Economics, June 18, 2025, <https://www.piie.com/research/piie-charts/2025/fed-projected-turn-profitable-again-after-three-years-losses>.

<sup>2</sup> St. Louis Federal Reserve data series, Total Assets (Less Eliminations from Consolidation): Wednesday Level, <https://fred.stlouisfed.org/series/WALCL>. Tim Congdon, *Money and Inflation at the Time of Covid*, (Northampton, MA: Edward Elgar, 2025).

The Fed could do something similar to fund IORB payments. This would help it duck criticism for using IORB money to subsidize foreign and domestic banks. Rather than address its problems, the Fed could simply create more dollars in an attempt to have its cake and eat it, too.

This money supply growth has a tradeoff. And that tradeoff is higher inflation. Fortunately, \$180 billion will do far less damage than \$5 trillion did. But there is no need to make the FOMC's job even harder than it already is.

Trial and error are essential to the public policy process. After a 17-year trial, we now know that IORB was an error. You now have the opportunity to fix it.

Thank you for this opportunity and I look forward to your questions.

# **Testimony**

**Of**

**Brian S. Wesbury**

**United States Senate**

**Committee On**

**Homeland Security and Government Affairs**

**December 11, 2025**

## **The Abundant Reserve Policy: The Experiment That Went Awry**

In 2008, the Federal Reserve (“the Fed”) began experimenting with a new monetary policy regime. With Quantitative Easing (QE) the Fed shifted from a “scarce reserve policy” to an “abundant reserve policy.” This new policy was a mistake on multiple levels. In no way should it continue. The Fed should return to its scarce reserve management of the banking system.

Today’s hearing is focused on the fact that the Fed has paid, and is paying, “private banks,” including foreign banks, hundreds of billions of dollars. As Chairman Paul and his staff have found, these numbers are a significant portion of bank earnings. This is a perversion of free market economics and it masks excessive government spending. Many Fed supporters demand Fed Independence, but the Fed itself has violated so many rules of being an independent entity it only has itself to blame for its current predicament.

Ending interest on bank reserves (IOBR) is an essential step in restoring a healthier monetary and fiscal framework. In fact, it would be like pulling the one loose thread that unravels the whole system. But to understand why, it is important to lay out how this shift in Fed policy came about. The move to paying interest on reserves represents a dramatic change. Moreover, it has not made the banking system safer, it has made it more fragile. It has raised costs for taxpayers, enabled a larger federal government than would otherwise be possible, obscured the true cost of that bigger government, encouraged mission creep at the Federal Reserve, and contributed to inequality that is reshaping the political fabric of our nation. In my opinion this experiment needs to end. A three-year reversal of these policies would allow it to happen without severe market disruption.

Below is a partial list of the results of this experiment.

- 1) QE expanded the Fed’s balance sheet more than 10-fold at its peak, from \$850 billion at the end of 2007 to \$8.929 trillion in April 2022 – larger than the top nine sovereign wealth funds in the world, combined. The Fed has peeled off some of those assets, but it still has a balance sheet of \$6.5 trillion, 7.6 times larger than in 2007. Along with this growth in its assets, employment at the Fed has grown from 17,100 in 2012 to 21,000 today. This has happened in spite of the fact that checks are now cleared electronically. The Fed has used its larger budget to engage in Mission Creep, or as Treasury Secretary Bessent has called it “Gain of Function Monetary Policy.” It does research on climate change, lead water pipes and all kinds of other issues like “inequality” and “racism.” This research has nothing to do with monetary policy, although the Fed claims it does.
- 2) In 2007, the Fed’s balance sheet was equal to just 5.8% of GDP. Today it is equal to 21.3% of GDP. The Fed owns 12.5% of all Treasury bonds outstanding and 11% of all mortgages. Between Q1 2020 and Q2 2022, the Fed bought almost one-half (45.4%) of all Treasury Securities issued. In other words, the Treasury only needed to find buyers for \$4.0 trillion of the debt it issued, not \$7.3 trillion. This allowed the Treasury to borrow at artificially low interest rates. While this may seem to be a positive, it isn’t.

- 3) Quantitative Easing is a way to shift the risk of federal government debt issuance from an independent bond market to the Fed. The Treasury issues debt to primary dealers, which are mainly large money center banks. When the Fed purchases these bonds with Quantitative Easing, it credits the banks with reserves (new money). The Fed takes those bonds onto its books, banks get reserves (cash). While the Fed claims to make its decisions independently of Treasury decisions, QE and large deficits after 2008 and again during COVID happened simultaneously. This was not a coincidence. Banks are fully aware of the Fed's schedule for purchasing those bonds. The Fed announces its QE intentions in advance so banks know exactly how long they may be exposed to the risk of holding bonds. As long as the Fed is doing QE, it is in effect financing government borrowing and spending.
- 4) This process increases the money supply (M2) by injecting new money into the banking system. This money is technically excess liquidity which could cause inflation. As a result, back in 2008 the Fed set up a regulatory system to contain these inflationary pressures. It raised capital requirements on banks, instituted new liquidity ratios and requirements and runs banks through Stress Tests. These rules are designed to force banks to hold more cash and make fewer loans than they could if they were to use all the new reserves created by the Fed when it bought Treasury bonds from the banks. The Fed also asked for, and received from Congress, the right to pay Interest on Reserve Balances (IORB). So, the Fed has a "carrot and stick" approach to stopping inflation. Interest payments encourage banks to hold reserves (the carrot), while regulations force them to hold them (the stick).
- 5) During COVID, however, the Treasury needed banks to be conduits for its COVID spending. Paycheck Protection Program (PPP) loans, and direct deposits of COVID Economic Impact Payments, all went through banks. In order to facilitate this the Fed eased liquidity rules to allow banks the ability to push that money out. This is why the second round of QE (during COVID) led to a huge surge in the money supply and inflation while the first round (after 2008) didn't. When COVID payments finally ended, the Fed reinstituted the liquidity rules.
- 6) The inflation these policies caused have undermined living standards and created more inequality in the United States. The Fed tripled the money supply between 2007 and 2022. People with assets (equities, homes, other property) won as the prices of those assets rose. People without assets face higher prices (inflation) with no positive wealth effect. This has set off a great divide in America, between the haves and the have nots and younger and older generations. This divide is not driven by productivity and entrepreneurship, it is driven by excessive liquidity, which is an artificial driver of inequality.
- 7) Many will use what is called a "counterfactual" to say all of this worked. They say "if the Fed had not done QE, the world would have collapsed, either in 2008, or during COVID." However, this is an unprovable claim. An economy is much too complex to argue that one policy changed all outcomes. Moreover, as the failure of Silicon Valley Bank shows, the distortions in interest rates that these new policies cause can lead to catastrophic results.

- 8) It is much more likely that because of QE, government expanded more than it should have. The Fed does not care about losses in its portfolio, it can print money to offset any losses. Banks do care. And if the Fed had not done QE, and the private markets, including banks, were the end purchasers of ALL new debt, interest rates would have been higher than they were. The market would have demanded it. If the Treasury had faced real market interest rates, it is highly likely spending decisions by politicians would have been adjusted and smaller. In other words, the government is bigger and more indebted today than it would have been if the Fed had not bought its debt. Simply put...the Fed has a different risk appetite than the private sector because the Fed does not face market forces. As a result, the real cost of government programs was hidden.
- 9) The Fed started this entire experiment in 2008 when a faltering subprime loan market was exposed. Total failing subprime loans were estimated to be between \$400 and \$500 billion. Large, but not large enough to take down the entire banking system. Mark-to-market accounting was the reason the crisis spread; it compounded losses and froze markets. Few discuss the facts, but QE was started in September 2008, TARP was passed in October 2008, and yet stocks continued to fall, with the S&P 500 down another 40% between QE/TARP and March 2009. Only then was the mark-to-market accounting rule (FASB 157) changed. That was when the stock market and economy both bottomed. It was not QE that saved the world, but the end of this highly damaging accounting rule.
- 10) Mr. Chairman, Fed Chair Jerome Powell recently said that these new abundant reserve policies promote "financial stability." However, because the Fed held interest rates artificially low during QE, both the Fed itself and banks have investments on their books at rates well below current market rates. With rates now up, combined un-realized losses at the Fed and in the banking system total roughly \$1.5 trillion. In other words, this new policy regime has created losses three times larger than the losses that precipitated the Great Financial Crisis. How can anyone call that financial stability? One reason this is not a crisis is that overly strict mark-to-market accounting rules for banks no longer exist while the Fed has no reason to worry about losses. The other is that markets expect the Fed to do further rounds of QE if something goes wrong, allowing the system to sweep problems under the rug and finance debt at artificially low rates.
- 11) In addition, the Fed is now paying more in IORB than it is earning on its portfolio of bonds. Contrary to those who dismiss this as a costless movement of money, it actually does cost taxpayers. The Bank of England includes similar losses in the deficit of the United Kingdom, while the Fed dumps the losses into an accounting entry called a "deferred asset" with a promise to make profits again in the future. Losses are hidden from taxpayers. Somehow, even with losses exceeding its capital, the Fed still pays its enormous staff, funds the building of a new headquarters, and keeps the lights on. It appears that it does this by printing more money, which undermines the value of the dollar because it is printing money to fund its own activities which do not add to GDP. Interestingly, the Fed has created an environment with the press where questions about this are never asked.



- 12) So far, we have avoided talking about other implications of this experimental monetary policy. Prior to 2008, banks traded federal funds, because reserves were scarce. If one bank had excess reserves, it could lend those reserves to a bank that had fewer reserves than required. Just about every bank had a "Federal Funds Trading Desk." The Fed influenced the federal funds rate by adding or subtracting reserves, but the rate was set in a marketplace. With the advent of QE, reserves became abundant. So abundant that banks no longer trade federal funds. No bank needs to borrow them. With no actual market for federal funds, where does this interest rate come from? The answer: the Fed just makes it up. The rate may be too low, or it may be too high. No one really knows.
- 13) In monetary policy terms, the Fed separated the money supply and interest rates. They no longer have anything to do with each other. The Fed claims this isn't true and points to pressures in the repo market as a sign that they have shrunk their balance sheet too much – taken too many reserves out of the system. They say we will know when reserves are no longer abundant by observing pressures in repo markets. But these are artificial pressures, created by whatever liquidity and capital rules exist. If the Fed raises liquidity or capital requirements on banks, they can make money tight. If they reduce them, they can encourage banks (and the money supply) to expand. In the scarce reserve model, there were simple rules and the trading of federal funds sent a signal. Today, the signal is distorted by rules and regulations. In essence, the US is moving toward a national bank where government policy is more important than market forces. This process is slowly, but surely, undermining capitalism in numerous ways. One of those ways in the world of banking is making it more and more difficult for small and mid-size banks to compete.
- 14) Chair Powell argues that if the Fed were not allowed to pay interest on reserves, it "would lose control over rates." This is absolutely true. The reason it is true is that there is no real market (borrowing and lending) for federal funds. The Fed completely controls the level of rates with no real market signals. Yet, the Fed did hold rates near "zero" for nine years – from 2008-2015, and again 2020-2022. So, what the Fed is really saying is that it will hold rates at zero when it wants to, but it doesn't want to be told they should be zero. If the Fed were to lose the ability to set rates where it wants – if the Congress does force the Fed to stop paying IORB – then the Fed would need to completely reverse quantitative easing and go back to a scarce reserve model. At that point it could influence rates again. The Fed would need to exchange its bonds for the reserves in the system. The Fed is right that this would cause dislocations if done too quickly. So, a transition period would be appropriate in order to make this process orderly.
- 15) Government programs, once started, create new behaviors and alter the make-up of markets. Throughout history, governments have resisted reversing course because it might be disruptive. Jerome Powell spoke of this in October... "If our ability to pay interest on reserves... were eliminated, the Fed would lose control over rates." He added "To restore rate control, large sales of securities... would be needed to shrink... the quantity of reserves in the system. [This] could strain Treasury market functioning and financial stability. Market participants would need to absorb the sales of Treasury securities and agency MBS, which would put upward pressure on the entire yield curve, raising borrowing costs for the Treasury and the private sector... [and] the banking system would be less resilient and more

vulnerable to liquidity shocks.” In other words, now that this system is in place, we can’t change it. This is a woefully inadequate argument. Just because unwinding something is difficult does not mean it should not be unwound. In addition, it is not clear at all that the banking system really is more resilient. Certainly, both the Fed and overall government are larger than they would have been without these changes in the policy regime at the Fed.

16) One thing not discussed so far is a massive growth in the Treasury General Account (TGA) – basically the Treasury’s checking account at the Fed. For decades this account was managed at a level of roughly \$5 billion. The Fed and the Treasury settled on this amount because of this accounts potential to impact monetary policy. When people pay their taxes, or buy Treasury bonds, for example, they write a check. In other words, money in the banking system is transferred to the Treasury. When the government spends that money it comes right back into the system and the money supply does not change. But if the Treasury deposits it in the TGA it is removed from the banking system and it reduces M2. This account started to grow in 2008, with the advent of the abundant reserve system. Today, the TGA has \$900 billion in it and taxpayers are paying interest on debt so that the Treasury can maintain this cash balance. Why the Treasury needs that much cash in a checking account is a mystery. Moreover, Jerome Powell says “unpredictable swings” in the TGA are one reason to maintain the abundant reserve regime. In other words, once started we can’t go back. Again, this is a highly inadequate defense. For decades there were no unpredictable swings in this account...so why are there unpredictable swings now? The Treasury can borrow at will and was able to operate normally prior to 2008. It could do so again.

17) So, to summarize. Having the Fed pay “private banks” and “foreign banks” hundreds of billions of dollars, which make up a significant share of their profits, violates the separation of government and markets in an unprecedented way. Mr. Chairman, your proposal to end these payments is appropriate. And moving in this direction would force the Fed to unwind its “crisis-era” management of monetary policy. This also is appropriate. The Fed has become too large. Already, we have seen that these new policies are not risk free. Unwinding these policies too quickly would be disruptive. So, in your bill Mr. Chairman, set a timeline of three years to wind down IORB, realizing fully that it will also force the Fed to pull back abundant reserves, and then make sure they can never come back again.

Testimony before the Senate Committee on Homeland Security and Governmental Affairs

On Interest on Bank Reserves held at the Federal Reserve

December 11, 2025

By: Donald Kohn

Robert V Roosa Chair in International Economics and Senior Fellow, Economic Studies,  
The Brookings Institution<sup>1</sup>

Thank you Chairman Paul and ranking member Peters for holding this hearing and inviting me to testify on this important topic.

The last time I testified on this subject was in 2004 when I testified as a member of the Board of Governors in favor of allowing the Federal Reserve to pay interest on the deposits that banks held at the Federal Reserve—their reserves.<sup>2</sup> I argued then, as I will argue today, that not paying interest on these deposits was, in effect, a tax on banks, forcing them to make interest free loans to the government. Naturally, banks tried to avoid that tax by reducing the amount of reserves they held by reducing customer deposits subject to reserve requirements. And to the extent they were still subject to this tax, they passed as much as possible along to their depositors and borrowers.

Congress ultimately agreed that the tax induced unnecessarily wasteful and harmful actions and it authorized the payment of interest on reserves in the Regulatory Relief Act of 2006; this legislation also included additional flexibility for the Board of Governors to reduce reserve requirements, which the Board had also requested. The authorization to pay interest was scheduled to take effect in 2011, but Congress sped up its implementation to 2008 to facilitate the Federal Reserve's actions to stabilize financial markets and the economy during and after the Global Financial Crisis of 2008-09.

In my view, the payment of interest on reserve balances (IORB) serves critical public policy purposes: It enables the Federal Reserve to meet its Congressional monetary policy mandates for stable prices and maximum employment in some circumstances, and it enhances financial stability. If Congress wishes to raise additional taxes from banks, it should do so directly, not by forcing them to make interest-free loans to the government.

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<sup>1</sup> In addition to my position at Brookings, I have a consulting relationship with T Rowe Price focused on monetary policy and I am on the board of Forbrite Bank—a \$7.7 billion institution (as of September 30) headquartered in Chevy Chase MD; on September 30, Forbrite held \$ 576 million of deposits at the Federal Reserve.

<sup>2</sup> <https://www.federalreserve.gov/boarddocs/testimony/2004/20040622/default.htm>

In the remainder of my testimony, I will explain the positive benefits of IORB and address some of the criticisms that have been leveled against it.<sup>3</sup>

**IORB is required to enable the Federal Reserve to take actions under some circumstances to meet its legislative monetary policy mandates for maximum employment and stable prices.**

When the economy and employment are weak, the Federal Reserve normally reduces its target for short-term interest rates to stimulate spending. Twice in the past 20 years, the Fed has lowered its target interest rate to zero, but recovery from recession still has been slow or uncertain. In these circumstances, to reduce longer-term interest rates further to encourage spending and job creation and avoid persistent deflation the Fed has purchased longer-term government securities (known as quantitative easing, QE). Those purchases create a large volume of reserves. When it comes time to tighten policy—to raise interest rates—to combat actual or potential inflation, small adjustments in reserves will not suffice; inflation fighting depends on raising IORB, which puts a floor under market rates. We saw this be effective in 2015-19 and again in 2022-24.

Without IORB the Fed could be constrained from taking actions required to meet Congressional mandates. If it refrained from QE in weak economies when rates were already zero because it lacked the tools to tighten policy when appropriate, more people would be unemployed for longer; if it undertook QE without the ability to move against rising prices after the economy recovered, it would not be able to preserve price stability--inflation would be high and persistent. IORB and QE have contributed to economic and price stability over the past 20 years. I'm not arguing that the Fed has used these tools perfectly; I myself have been critical of some aspects of monetary policy in the post-Covid period.<sup>4</sup> But the economy did better than it would have if the Fed wasn't able to take these actions, and they need to be available in the future.

**IORB supports the Federal Reserve's ability to foster financial stability.**

**It enables the Federal Reserve to make purchases to stabilize Treasury, agency, and MBS markets when they are disrupted, threatening the flow of credit to public and private borrowers.** Financial markets seized up in late 2008 and again in the spring of 2020 as lenders ran to the safest, most liquid instruments. That disfunction meant that

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<sup>3</sup> This testimony draws from a blog post I recently co-authored with William English.  
<https://www.brookings.edu/articles/what-would-happen-if-congress-repealed-the-feds-authority-to-pay-interest-on-reserves/>

<sup>4</sup> <https://www.brookings.edu/articles/the-inflation-surge-of-the-2020s-the-role-of-monetary-policy/>;  
<https://www.brookings.edu/articles/fed-should-be-sure-to-include-monetary-policy-tools-in-forthcoming-framework-review/>.

households, businesses and governments were unable to borrow to finance the normal flow of spending; if those effects had persisted, the result would have been to make already very serious recessions even deeper and longer. Because of IORB the Federal Reserve was able to step in to make purchases of Treasury, agency and agency-guaranteed mortgage-backed securities to restore normal functioning in those foundational markets. I was on the FOMC in 2008-09; many policymakers were concerned that the securities purchases undertaken to stabilize markets and support the recovery not impede our ability to tighten policy to head off inflation when the time came. IORB gave us the confidence we needed to take the actions required to limit the damage to the economy from the financial crisis.

**IORB means that the Fed can supply reserves to enhance the resilience of the banking system to unexpected adverse liquidity shocks such as deposit runs.**

Reserves—deposits at the Fed—are the safest, most liquid assets banks can hold. IORB means that the banks see reserves as a viable source of liquidity to manage their risks and make interbank payments without harming their bottom line. And the Fed can meet their demands for this asset without sacrificing its ability to control short-term interest rates for monetary policy purposes. The “ample reserves” operating regime the Fed is now utilizing gives it the same control over money market interest rates it had in the pre-2008 scarce reserves operating system, but at the same time provides a much higher level of reserves—high-quality liquidity—to the banking system. Being able to use interest-bearing deposits at the Fed to manage liquidity is especially important for small and medium sized banks; larger banks have access to a much wider variety of instruments to meet unexpected outflows or generally to adjust their liquidity positions.

**IORB does not result in a windfall for banks**

Banks have to fund their holdings of reserves with deposits or borrowing, just as they do with other assets that they hold. And banks pay interest and face other costs associated with those sources of funding. The key issue, then, is how the interest on reserves compares to the banks’ cost of funding. There are three reasons to believe that the difference between the two is small. First, the rate paid on reserves is very close to the rates on a range of other short-term instruments with which banks and others can borrow and invest. Second, the Fed’s payments of interest on reserves have increased immensely in recent years, reflecting both a higher level of reserves and higher interest rates, but that increase does not appear to have affected bank profitability. Specifically, between 2021 and 2024, payments of interest on reserves increased by more than \$150 billion, but bank profits changed little, remaining near \$300 billion, suggesting that higher bank funding costs offset the rise in interest income on reserves. Finally, any individual bank can

increase its holdings of reserves by raising its deposit rates to attract new funds and leaving the funds in its reserve account at the Fed. If the rate paid on reserves offered banks an excessive profit, increased competition among banks for deposits would push up bank funding costs, offsetting that profit.

**IORB will not result in a net cost to the Treasury over the long run**

While a larger Fed balance sheet means that the Fed is supplying more reserves to banks on which it pays interest, it also means that the Fed is holding more government securities purchased with those reserves, and it earns interest on those. Thus, the implication for Fed profits (which are turned over to the Treasury after paying the Fed's expenses)—and so, the budget deficit—depends on the *net* interest earned or paid by the Fed.

The interest rate paid on reserves is a short-term rate—reserves are held overnight—while the rate on the Fed's securities holdings is a mix of short, intermediate, and long-term rates, depending on the particular portfolio of securities the Fed is holding. Thus, Fed interest income and expense (including interest payments to banks) can differ significantly in some periods. Indeed, the Fed had large profits and made large remittances to the Treasury for a number of years following the financial crisis and again in the immediate aftermath of the pandemic, but it has had substantial losses recently, reflecting the rapid rise in short-term rates put in place to combat the post-COVID inflation. But this is a temporary condition. Over time, yields on long-term securities have somewhat exceeded, on average, those on short-term debt as investors arbitrage across instruments with different maturities to achieve roughly equal risk-adjusted returns. As a result, the effects of a larger Fed balance sheet on interest payments to banks and interest receipts on securities should be roughly offsetting, leaving Fed income and the federal budget deficit about unchanged.

**IORB and ample reserves do not crowd out consumer or business lending.**

Deposits are the counterpart of those reserves. When a bank receives a deposit, it is credited to its account at the Federal Reserve. The bank then compares the risk-adjusted returns on various uses of the deposit, taking account of capital charges and other costs associated with each investment opportunity. Before IORB a bank might compare making a loan to lending to another bank in the federal funds market, reducing its (noninterest earning) deposit at the Fed. The key question facing the bank was whether it would earn a higher risk-adjusted return after costs on a loan to businesses and households or a loan to another bank. Today the bank would compare making the loan to

holding onto the deposit at the Fed. So the key question is whether it would earn a higher return in a loan to businesses and households or on reserves held at the Fed. The IORB rate is almost identical to the federal funds rate, so IORB hasn't altered the calculus behind the loan decision-- the incentives to make loan haven't changed materially.

Observers have been concerned that the ample reserves regime could crowd out other risk-free investments like Treasury securities at banks constrained by the leverage ratio. The leverage ratio imposes the same capital charge against both risky and safe assets. It's intended to be a backstop for risk-based capital regulation, but the provision of ample reserves has pushed banks closer to leverage ratio limits. To be clear, the problem is not ample reserves or IORB, it's the leverage ratio. The regulatory authorities have recognized the problem and proposed reforms to the calculation of the leverage ratio to make it more of a backstop for risk-based capital requirements, as intended, not the binding constraint. They are also looking at aspects of the special capital requirements for too-big-to-fail banks--the GSIB requirements--that might also have the effect of discouraging purchase and market making in Treasuries and are moving to address this problem too. I have supported these efforts.<sup>5</sup> Once they take effect, ample reserves should not have a significant effect on bank support of a wide variety of security and loan markets.

**While not allowing the Fed to pay interest on reserve balances would have little effect on Treasury income over time or on bank profits, it would handicap the Fed's ability to promote economic and financial stability.**

If Congress repealed the Fed's authority to pay interest on reserves, the Fed would turn to other tools to implement monetary policy. In the short run, the Fed probably would make greater use of reverse repurchase agreements to provide a floor for short-term interest rates. In a reverse repurchase agreement, the Fed essentially borrows short-term in financial markets; counterparties will not lend to anyone else at a rate lower than the Fed is offering. Reverse repurchase agreements have effects—and costs—similar to those of the payment of interest on reserves. Thus, ending interest on reserves would leave Fed interest payments little changed in the short run, and so would have little effect on Fed profits and so on the federal budget.

If the Fed were unable to pay interest on reserves, it might reconsider its decision to implement monetary policy with a large balance sheet, and so move, over time, back to a smaller balance sheet and policy implementation using a scarce reserves framework.

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<sup>5</sup> <https://www.brookings.edu/articles/donald-kohns-thoughts-on-supplementary-leverage-ratio-reform/>

(Shifting back to a scarce reserves system quickly would not be feasible because the huge sales of Treasuries required would disrupt the Treasury market.) Such a shift would lead the Fed to decrease its holdings of securities, reducing interest income and largely offsetting, on average, the savings from not paying interest on reserve balances, as discussed above. The net effect on Fed income, and so on the federal budget, would depend on banks' residual demand for non-interest-bearing reserves. That demand would surely be small—vastly smaller than the level of reserves today. Moreover, the lack of interest on the reserves that banks chose to continue holding—or were required to hold because the Fed had to revive reserve requirements to induce a stable predictable demand for reserves—would still be an implicit tax on bank intermediation, falling on bank customers and inducing wasteful avoidance efforts. Such a change in policy implementation would also require the Fed to give up the benefits it saw to operating with an ample reserves framework, including potential improvements in financial stability from more liquid bank balance sheets.

Perhaps most importantly, under some critical circumstances the repeal of IORB would constrain the Fed's ability to meet its goals for maximum employment, stable prices, and a well-functioning financial system. In a future economic or financial crisis, it would be forced to choose between a longer period of higher unemployment because it foreswore asset purchases; or if it made those purchases it would risk saddling the US economy with higher inflation as it undertook the reduction in its balance sheet.

In sum, IORB has been a critical aspect of bank deregulation that reduces inefficient and distortive behavior by banks and benefits depositors and borrowers. It strengthens the safety and soundness of banks, and it enables the Federal Reserve use all its tools to stabilize the economy and financial system in an emergency without losing control of monetary policy. It should be left in place.



# THE FED'S CORPORATE WELFARE PROGRAM

AN ANALYSIS OF THE FEDERAL RESERVE'S  
INTEREST ON RESERVE BALANCES PAYMENTS



UNITED STATES SENATE COMMITTEE ON  
**HOMELAND SECURITY**  
& GOVERNMENTAL AFFAIRS  
CHAIRMAN RAND PAUL, M.D.

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## Executive Summary

On July 15<sup>th</sup>, 2025, Chairman Rand Paul of the U.S. Senate Committee on Homeland Security and Governmental Affairs (HSGAC) launched an investigation on the Federal Reserve's use of Interest on Reserve Balances (IORB). After months of correspondence, the Federal Reserve Board of Governors produced over 40,000 pages of documents detailing IORB payments for every two-week period from July 2013 through July 2025. This report outlines the following key findings from the contents of the data:

### 1. IORB payments equal 10 percent of the Federal Deficit:

- a. The magnitude of IORB payments equaled **10.3 percent (\$187 billion) of the FY24 Federal deficit** and **8.8 percent (\$149 billion) of the FY23 deficit**.

### 2. The Federal Reserve has used IORB payments to subsidize Wall Street's largest banks:

- a. IORB payments account for **12 percent** of all profits for the 5 largest American banks from 2013-2024.
- b. In 2024, IORB payments accounted for **16 percent** of U.S. banking sector's net interest income.
- c. **The top 20 banks account for over half (\$305 billion) of total payments** with the remaining 4,500 banks accounting for the remaining half (\$302 billion).

### 3. IORB payments are also subsidizing foreign banks:

- a. **11 of the top 20 recipients of IORB payments are foreign banks.**
- b. From July 2013 – July 2025, **\$235 billion has been paid to foreign banks** by the Fed through IORB payments (see figure 9).
- c. **\$10 billion of these payments were made to Chinese banks** such as Bank of China, China Construction Bank, Industrial and Commercial Bank of China, and Bank of Communications.

## A Note from Chairman Paul

The Federal Reserve (The Fed) is one of the most powerful yet secretive and unaccountable institutions in U.S. history. Its insulation from oversight, combined with its massive coffers and strong statutory authorities, makes it a uniquely troubling institution. In fact, in 2018, Forbes ranked Jerome Powell, the Chairman of the Federal Reserve Board of Governors, as the 11<sup>th</sup> most powerful person in the world, ahead of the heads of state of the U.K. and France.<sup>1</sup>

As Chairman of the Senate Homeland Security and Governmental Affairs Committee, I launched an investigation into the Fed in July of 2025. After months of stonewalling and obfuscating, the Fed finally produced information partially responsive to my oversight letters. This report analyzes never-before-seen data on one of the most important tools the Fed uses to influence monetary policy – Interest on Reserve Balances (IORB).

The Fed uses funds that would otherwise go to the taxpayer to make IORB payments to the largest banks in the world, both foreign and domestic. It's a double whammy. Banks use your money that's sitting in a checking account to earn as much as 5.4% interest,<sup>2</sup> underwritten by your tax dollars, then pay you an average of 0.07% interest, and pocket the difference. IORB enables the Fed, without any form of oversight or elections, to unilaterally transfer wealth from the American taxpayer to the wealthiest banks on Wall Street.

IORB payments have totaled hundreds of billions of dollars since 2013, and to date, most people don't even know they exist. Those that do have been denied meaningful data to understand how they have been used to influence the American economy, allowing unelected officials at the Fed to influence the American economy in a way that rivals elected Members of Congress.

This report marks the first step in finally Auditing the Fed, but there is still much more work left to do. My "End the Fed's Big Bank Bailout Act" would end the forcible transfer of wealth from average Americans to Wall Street institutions under the guise of IORB payments, while my "Federal Reserve Transparency Act" would allow meaningful oversight of all functions of the Fed, which is long overdue. If the Fed handed over this data, what is hiding in the information they still refuse to provide?

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<sup>1</sup> <https://www.forbes.com/powerful-people/list/#tab:overall>

<sup>2</sup> See Figure 2 on page 8.

## **Methodology**

In the document production by the Federal Reserve (Fed) Board of Governors, the Senate Committee on Homeland Security and Governmental Affairs (HSGAC) received over 40,000 pages of PDF documents. This data featured the Interest on Reserve Balances (IORB) payments paid out by the Fed in every 2-week period from July 2013 to July 2025 by financial institution. Financial Institutions were identified by ABA routing numbers.

HSGAC majority staff created a dataset aggregating the payments by ABA numbers and routing numbers and cross-referenced these numbers with available datasets to identify financial institutions and the country of the parent organization. While this report accounts for all payments on the documents produced to HSGAC, 1.5 percent of the payments in this dataset were to unidentified ABA numbers. As a disclosure, the information presented in the report that is attributable to specific financial institutions or by nations only reflects the payments with identified ABA numbers. Total sums reflect all payments including unidentified payments unless otherwise specified.

Additionally, the sum of payments reflected in this dataset reflect 95 percent of the payments listed in the Fed's consolidated financial statements from 2013-2024 under the line item "Interest payable to depository institutions and others." While the Fed's financial disclosures indicate that IORB payments are a component of this figure, IORB payments do not account for the full amounts listed in their financial statements.

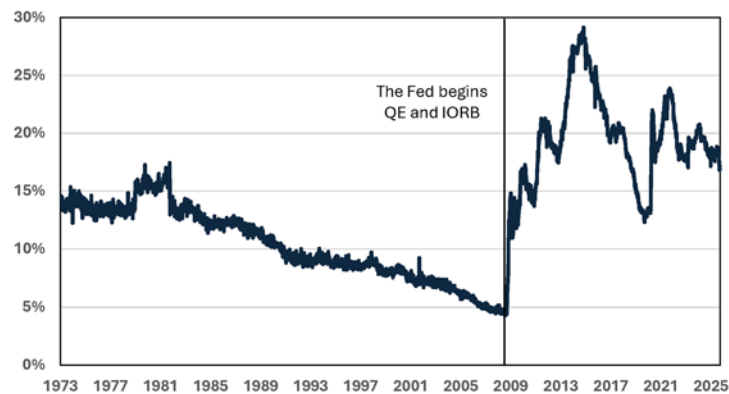
## The Cost of IORB Payments

### Rising Reserves

In the aftermath of the 2008 Financial Crisis, the Federal Reserve (the Fed) flooded the capital markets with reserves through Quantitative Easing (QE). While prior to the financial crisis, the Fed's traditional tools of monetary policy, such as reserve requirements, were effective in a scarce reserves environment, QE provided an abundance of capital that banks could either loan out or keep on hand as excess reserves, making these traditional tools of regulating the monetary supply ineffective.

While Congress originally granted the Fed the authority to pay Interest on Reserve Balances (IORB) in 2006 (to be implemented in 2011)<sup>3</sup> as a means of mitigating the "implicit tax" of requiring banks to keep a certain percentage of assets in reserves through reserve requirements, Congress accelerated its implementation to 2008<sup>4</sup> to assist the Fed in continuing to retain control over interest rates while simultaneously flooding the market with capital through QE. As a result of both QE and IORB, banks had significantly more capital yet a large incentive to keep this cash idle at the Fed (see Figure 1).

**Figure 1: Percent of Deposits Held in Cash Reserves**



Source: Federal Reserve Board H.8 Reports

### IORB Rates Rise

Prior to 2021, IORB rates peaked at 2.4 percent, however in the inflationary period after the COVID stimulus in 2021, the Fed began to raise rates in an attempt to rein in inflation. The Fed raised IORB rates to a high of 5.4 percent in July 2023 (see figure 2).

<sup>3</sup> Financial Services Regulatory Relief Act, Pub. L. 109-351, 120 Stat. 1966 (2006)

<sup>4</sup> Emergency Economic Stabilization Act, Pub. L. 110-343, 122 Stat. 3765 (2008)

The Fed's increased IORB rates incentivized eligible domestic and foreign banks to place reserves at the Fed instead of lending out these funds, buying treasury bills, or other financial activities effectively setting a floor on interest rates. IORB payments from the fed ballooned from **an average of \$17 billion prior to the pandemic to over \$100 billion in each of the last two fiscal years** (See figure 3).

Figure 2: IORB Rates Since 2016

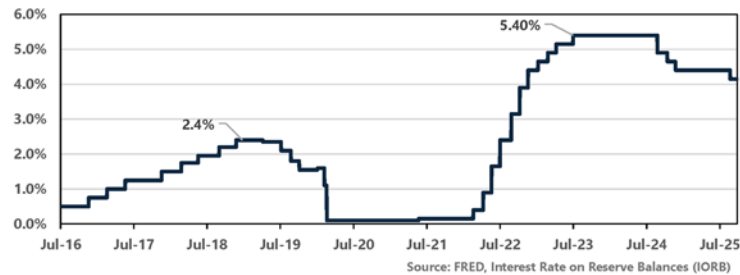
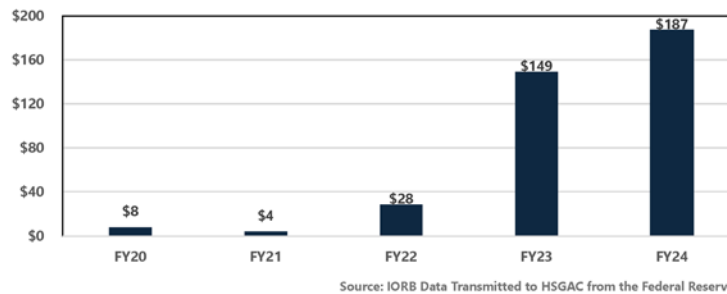


Figure 3: IORB Payments Over Time (\$billions)



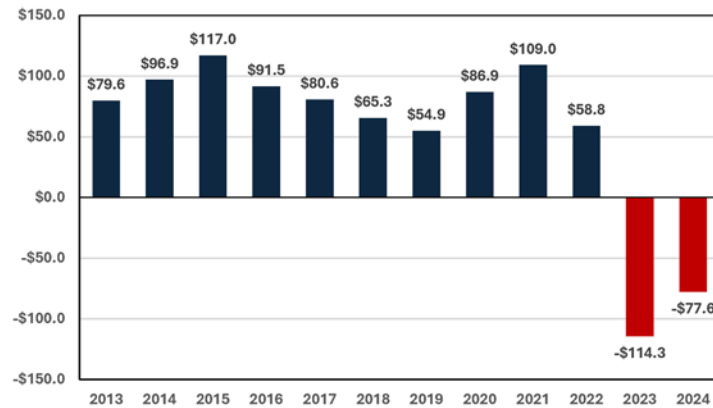
### IORB Leads to Taxpayer Losses

These payments ultimately come at a cost to the taxpayer. Under current law,<sup>5</sup> the Fed is required to send operating profits back to the Department of Treasury (Treasury) to pay down the federal deficit. Prior to 2022, the Fed routinely remitted profits to Treasury, **reducing the Federal deficit by an average of \$84 billion** from 2013 to 2022. Since 2022 the Fed has been operating at an unprecedented loss, **averaging \$96 billion in losses** in each of the last two years (see figure 4).

<sup>5</sup> 12 U.S.C. § 289



**Figure 4: Net Federal Reserve Remittances to Treasury (\$billions)**



Source: Audited Annual Financial Statements of the Federal Reserve System

#### IORB Payments and the Federal Deficit

IORB payments, which accounted for more than the entirety of operating losses posted by the Fed in 2023 and 2024, also equal a substantial portion of the Federal budget deficit. The figure below compares the magnitude of IORB payments with the size of the deficit. In 2023 IORB payments equaled **8.8 percent of the federal deficit**. In 2024, IORB payments equaled **10.3 percent of the federal deficit**. These payments would have otherwise gone back to the taxpayer.

Year	Deficit (On-budget, \$ billions)	IORB Payment (\$ billions, by FY)	Percent of Deficit
FY20	\$3,132	\$8	0.3%
FY21	\$2,776	\$4	0.1%
FY22	\$1,376	\$28	2.0%
<b>FY23</b>	<b>\$1,695</b>	<b>\$149</b>	<b>8.8%</b>
<b>FY24</b>	<b>\$1,817</b>	<b>\$187</b>	<b>10.3%</b>

Source: Congressional Budget Office; IORB Data Transmitted to HSGAC from the Federal Reserve

## IORB Payments as Corporate Welfare

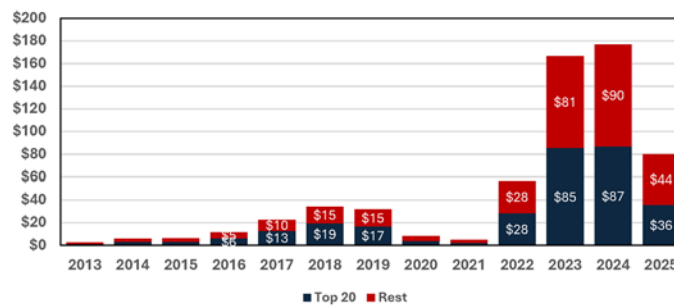
### Introduction

IORB payments, as currently structured, take the Fed's operating profits that could be used to pay down the deficit and pay these funds out to world's largest banks. Since 2013, the Fed has paid \$607 billion in identified payments to both foreign and domestic financial institutions to keep their reserves idle and interest rates artificially high. This costly means of conducting monetary policy has **prevented the Fed from remitting profits to Treasury to pay down the Federal deficit and instead directed these funds into Wall Street's profit margins.**

### Characteristics of IORB Payment Recipients:

Analysis of these payments shows that large banks are the primary beneficiary of this reallocation of taxpayer funds. The allocation of IORB payments is disproportionately skewed to large financial institutions. The top 20 bank recipients (see Figure 6) received approximately the same amount of IORB payments from 2020-2025 (**\$305 billion**) as the next 4,500 banks received (**\$302 billion**).

**Figure 6: Share of IORB Payments to Top 20 Recipients vs. Other 4,500 Recipients (in \$billions)**



Source: IORB Data Transmitted to HSGAC from the Federal Reserve; HSGAC Analysis  
2025 data represents through July 2025

### IORB Payments as a Driver of Bank Profits

The five largest banks in the U.S. by consolidated assets: JP Morgan Chase, Bank of America, Citibank, Wells Fargo, and U.S. Bank received \$136 billion in IORB payments from 2013 to 2024, with 2024 payments alone amounting to \$43.9 billion. In 2024, taxpayer-financed IORB payments were a considerable driver for profitability for these banks accounting for **16.5 percent of net interest income for the U.S.'s 5 largest banks in 2024**. Looking at the entirety of the banking sector, **IORB payments accounted for 16.1 percent of all net interest income of U.S. banks in 2024.**

Figure 7: 2024 IORB Payments and Top Bank Net Income (\$ billions)			
Bank	Net Interest Income (2024)	IORB Payment (2024)	IORB Payment as Percent of NII
J.P. Morgan Chase	\$92.6	\$15.0	16.2%
Bank of America	\$56.1	\$14.0	25.0%
Citi	\$54.1	\$5.7	10.5%
Wells Fargo	\$47.7	\$6.9	14.5%
U.S. Bank	\$16.3	\$2.3	14.1%
<b>Total</b>	<b>\$266.8</b>	<b>\$43.9</b>	<b>16.5%</b>

Source: IORB Data Transmitted to HSGAC from the Federal Reserve; Bank 10-K Filings

To put the magnitude of these payments in perspective, JP Morgan Chase, one of the most prestigious banks on Wall Street, received \$15 billion in IORB payments in 2024. According to its 2024 annual report, its total investment banking fees charged to clients only totaled \$9.1 billion, showing that the Fed's interest payments were a larger driver of profits for JP Morgan Chase than its entire investment banking division. This trend held for 4 of the top 5 banks in 2024, with the table below comparing investment banking fee revenues to IORB payments.

Figure 8: Investment Banking Income vs. IORB Income (\$ billions)		
Bank	Investment Banking Fee Revenue (2024)	IORB Payment (2024)
J.P. Morgan Chase	\$9.1	\$15.0
Bank of America	\$6.2	\$14.0
Citi	\$3.9	\$5.7
Wells Fargo	\$2.7	\$6.9
U.S. Bank	N/a	\$2.3
<b>Total</b>	<b>\$21.9</b>	<b>\$43.9</b>

Source: IORB Data Transmitted to HSGAC from the Federal Reserve; Bank 10-K Filings

## IORB Payments as Foreign Aid

### Introduction

Regulation D (12 CFR Part 204)<sup>6</sup> lays out the definitions of financial institutions subject to reserve requirements, which also determines eligibility for a depository institution to participate in the Fed's IORB program. Notably, these requirements place no unique restrictions on foreign financial institutions with U.S. branches or subsidiaries so long as each of these U.S. branches or subsidiaries remain compliant with the laws and regulations required for other domestic depository institutions.

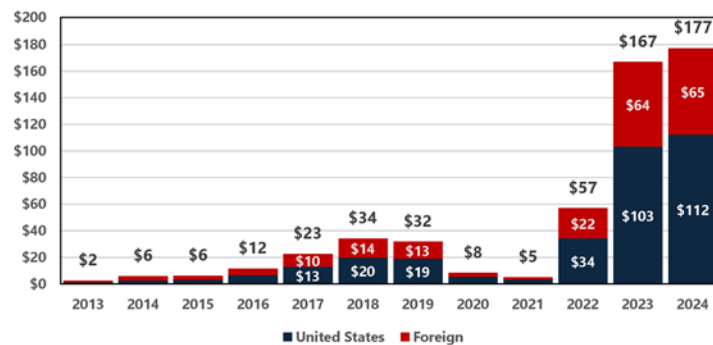
An analysis of the Fed's IORB documents shows that from January 2013 through July 2025, **39 percent (\$235 billion) of IORB payments were issued to foreign or majority foreign-owned banks.**

Whether intended or not, The Fed's IORB payments are a taxpayer-financed tool that unelected officials can use to engage in policies that affect foreign capital markets and the interaction between domestic and foreign capital markets. In other words, the Fed can set and administer foreign policy, and at times, foreign policy that may run contrary to the policy set by the president or by Congress without any accountability to elections or independent oversight.

### Share of Foreign and Domestic Payments

While the proportion of IORB payments to foreign banks has decreased slightly since 2013, the gross amount in payments sent to foreign banks continues to grow substantially each year as the Fed has increased IORB rates. In 2019, prior to the pandemic, \$13 billion in IORB payments were paid to foreign banks. Since 2022, however, the Fed has paid an **average of \$50 billion in IORB payments to foreign institutions** and this number continues to grow.

**Figure 9: Foreign and Domestic IORB Payments (\$billions)**



Source: IORB Data Transmitted to HSGAC from the Federal Reserve

<sup>6</sup> <https://www.federalreserve.gov/aboutthefed/section19.htm>

As IORB rates drastically increased in late 2021 and 2022, not only did domestic banks rush to park capital at the Fed, but foreign banks also seemed to inject dormant capital from their international banks into their U.S. subsidiary to take advantage of the more generous risk-free interest offered for excess reserves. The share of IORB payments jumped from 28.5 percent foreign banks (the lowest since 2013) to nearly 40 percent of payments (see Appendix Figure 1). Many of the world's largest banks have been the largest beneficiaries of IORB payments. **Of top 10 recipients of IORB payments from July 2013 to July 2025, 4 are foreign banks (bolded)**, and 11 of the top 20 are foreign banks (see Figure 10, and Appendix Figure 2):

Figure 10: Top 10 Recipients of IORB payments			
No.	Bank	Country	2013-2025 IORB Payments
1	JPMorgan Chase Bank, National Association	United States	\$60,355,717,554
2	Bank of America, National Association	United States	\$40,414,268,683
3	Citibank NA	United States	\$22,847,562,330
4	Wells Fargo Bank National Association	United States	\$22,032,069,144
5	Goldman Sachs Bank USA	United States	\$20,542,834,557
6	<b>Mizuho Bank Ltd</b>	<b>Japan</b>	<b>\$15,155,492,673</b>
7	<b>Barclays Bank PLC</b>	<b>United Kingdom</b>	<b>\$12,807,429,989</b>
8	<b>Deutsche Bank AG</b>	<b>Germany</b>	<b>\$12,122,207,420</b>
9	<b>Sumitomo Mitsui Banking Corporation</b>	<b>Japan</b>	<b>\$10,289,470,641</b>
10	Chicago Mercantile Exchange (CME)	United States	\$9,101,480,715

Source: IORB Data Transmitted to HSGAC from the Federal Reserve

### **IORB Payments as a Foreign Bank Subsidy**

In 2024, while 16.1 percent of the U.S.'s banking sector's net interest income comes at the expense of the taxpayer through IORB, **5 percent of all the participating foreign banks net interest income comes from the U.S. taxpayer**. Figure 11 shows the top 10 benefitting nations and the percentage of bank profits is subsidized by the U.S. taxpayer. "Bank profit subsidy" reflects the percent of participating depository institution's net interest income that is attributable to IORB payments from the Fed. Notably, the American taxpayer has financed over **50 percent of Bahrain's bank profits, 47 percent of Norway's bank profits, and 22 percent of Japan's bank profits** (see Appendix Figure 5 for the full table).

**Figure 11: Table of Foreign IORB Payments**

No	Country	2024	2024 Bank Profit Subsidy	Total Payments from 2013-2024
<b>United States</b>		<b>\$112,774,136,577</b>	<b>16.1%</b>	<b>\$325,831,264,205</b>
1	Japan	\$10,807,772,791	22.6%	\$34,656,768,985
2	France	\$8,811,369,374	17.7%	\$28,892,888,881
3	United Kingdom	\$8,322,011,557	11.3%	\$23,883,572,625
4	Germany	\$6,248,801,856	14.1%	\$21,598,319,696
5	Canada	\$6,235,406,330	7.9%	\$19,618,928,516
6	Switzerland	\$3,376,316,955	9.3%	\$9,971,515,199
7	China	\$2,954,756,710	0.7%	\$9,910,316,535
8	Norway	\$2,765,650,185	47.4%	\$6,256,987,794
9	Sweden	\$2,263,171,918	23.6%	\$6,868,478,184
10	United Arab Emirates	\$2,083,912,596	30.3%	\$6,947,270,925

Source: IORB Data Transmitted to HSGAC from the Federal Reserve

## Conclusion

These findings are the first step in removing the cloak of secrecy that the Fed has operated under since its inception. Now, cold, hard data is in the public domain, allowing the public to have an honest conversation about how the Fed operates.

At the Fed, however, Chairman Powell remains defiant. Before this data was released, Chairman Powell defended the practice, stating that "Some have questioned whether the interest we pay on reserves is costly to taxpayers. In fact, that is not the case... While our net interest income has temporarily been negative due to the rapid rise in policy rates to control inflation, this is highly unusual. Our net income will soon turn positive again, as it typically has been throughout our history."<sup>7</sup>

In short, the Fed maintains they deserve an indefinite line of taxpayer-financed credit, no matter how costly it may prove to be, without a single elected official's approval.

Specifically, Chairman Powell contends that, "since 2008, even after accounting for the recent period of negative net income, our total remittances to Treasury have totaled more than \$900 billion."<sup>8</sup> While factually accurate, it doesn't excuse the fact that, **without an IORB regime, total remittances to the Treasury would have totaled more than \$1.5 trillion.**

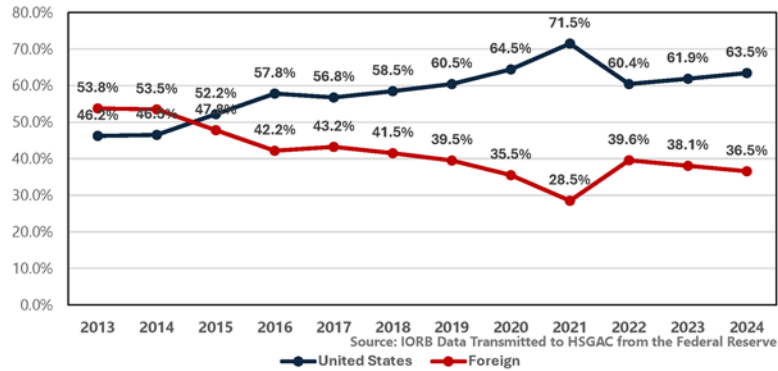
Matters that affect trillions of dollars in taxpayer funds merit discussion, debate, and accountability. Until this point, there has not been any form of truly independent oversight of the Fed's IORB payments. **Hundreds of billions of dollars for the taxpayer have been sent to foreign banks, hundreds of billions of dollars for the taxpayer have padded Wall Street's profit margin, all without a single election, public debate, or independent audit. This is the first step in what should be a continued effort to audit the Federal Reserve.**

<sup>7</sup> <https://www.federalreserve.gov/newsevents/speech/powell20251014a.htm>

<sup>8</sup> Ibid

## Appendix

**Appendix Figure 1: Share of Foreign and Domestic IORB Payments**



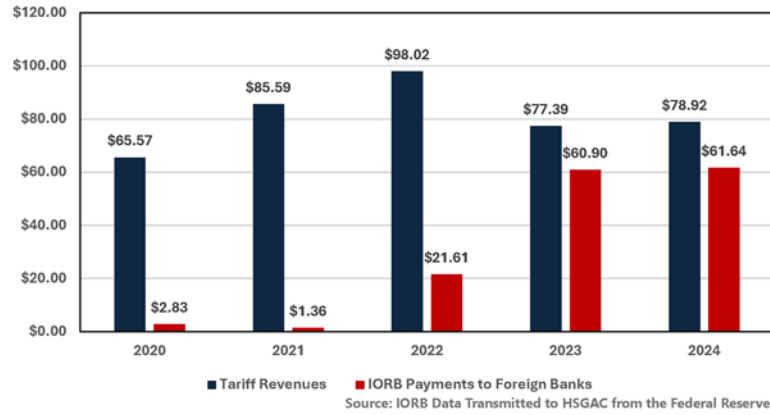
**Appendix Figure 2: Top 20 Recipients of IORB payments**

No.	Bank	Country	2013-2025 IORB Payments
1	JPMorgan Chase Bank, National Association	United States	\$60,355,717,554
2	Bank of America, National Association	United States	\$40,414,268,683
3	Citibank NA	United States	\$22,847,562,330
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8	Deutsche Bank AG	Germany	\$12,122,207,420
9	Sumitomo Mitsui Banking Corporation	Japan	\$10,289,470,641
10	CME CUST SEG ACCT- FUTURES	United States	\$9,101,480,715
11	Societe Generale S.A.	France	\$8,314,278,650
12	Royal Bank of Canada	Canada	\$8,088,537,686
13	Credit Agricole Corporate and Investment Bank	France	\$7,908,339,610
14	MUFG Bank Ltd.	Japan	\$7,700,205,664
15	First Abu Dhabi Bank USA NV	UAE	\$7,673,352,991
16	The Bank of New York Mellon	United States	\$7,607,203,850
17	DNB Bank ASA	Norway	\$7,418,484,002
18	American Express National Bank	United States	\$7,223,579,591
19	BNP Paribas SA	France	\$7,219,493,987
20	PNC Bank National Association	United States	\$6,993,418,852

Source: IORB Data Transmitted to HSGAC from the Federal Reserve



**Appendix Figure 3: Tariff Revenues and IORB Payments to Foreign Banks (\$billions)**



**Appendix Figure 4: IORB Payments to Foreign Banks and Tariffs (Apr - Jul 2025)**

No	Countries	Percent of Tariffs remitted back through IORB	IORB Payments	Tariffs Collected
1	Kuwait	13398%	\$51,221,066	\$382,290
2	Norway	626%	\$689,754,950	\$110,151,497
3	United Arab Emirates	275%	\$689,755,602	\$250,759,067
4	Australia	194%	\$509,643,704	\$262,263,800
5	United Kingdom	192%	\$2,619,960,032	\$1,364,681,708
6	Nigeria	189%	\$13,535,029	\$7,167,205
7	France	177%	\$2,400,042,924	\$1,354,248,815
8	Finland	159%	\$231,657,367	\$145,397,237
9	Sweden	126%	\$666,020,244	\$528,589,000
10	Switzerland	106%	\$779,379,981	\$735,663,192
11	Panama	94%	\$7,793,462	\$8,279,188
12	Austria	82%	\$422,502,995	\$513,629,053
13	Spain	76%	\$465,169,284	\$615,320,569
14	Canada	70%	\$2,029,438,948	\$2,913,483,904
15	Belgium	63%	\$198,820,833	\$315,233,697
16	Netherlands	62%	\$312,170,830	\$500,429,928
17	Singapore	50%	\$128,696,415	\$259,704,616
18	Japan	42%	\$2,767,364,630	\$6,592,619,712
19	Germany	39%	\$1,937,496,454	\$4,953,920,804



20	Bahrain	31%	\$18,961,281	\$61,272,933
21	Brazil	10%	\$115,923,387	\$1,170,403,568
22	Ireland	10%	\$32,386,697	\$335,009,812
23	India	10%	\$229,454,736	\$2,404,965,923
24	Taiwan	7%	\$136,182,757	\$1,838,462,373
25	Argentina	6%	\$7,129,282	\$115,783,507
26	Chile	6%	\$11,552,175	\$200,046,218
27	Italy	6%	\$126,776,713	\$2,200,710,638
28	Israel	5%	\$12,721,784	\$234,460,371
29	Uruguay	4%	\$4,110,157	\$104,098,934
30	China	3%	\$946,800,288	\$36,067,838,161
31	Malaysia	2%	\$17,654,779	\$922,183,569
32	South Korea	1%	\$56,626,692	\$4,700,078,887
33	Colombia	1%	\$2,754,216	\$239,725,515
34	Peru	1%	\$1,384,232	\$125,657,702
35	Ecuador	1%	\$1,096,464	\$118,497,265
36	Indonesia	1%	\$10,719,876	\$1,230,649,602
37	Turkey	1%	\$4,731,013	\$579,825,382
38	Thailand	0%	\$3,269,457	\$1,728,270,673
39	Pakistan	0%	\$312,066	\$274,609,269
<b>Total from All Countries</b>		<b>25%</b>	<b>\$18,660,972,799</b>	<b>\$76,084,475,584</b>

Source: IORB Data Transmitted to HSGAC from the Federal Reserve, Calculated Duties by Country USITC

Appendix Figure 5: Table of Foreign IORB Payments				
No	Country	2024	2024 Bank Profit Subsidy	Total Payments from 2013-2024
<b>United States</b>		<b>\$112,774,136,577</b>	<b>16.1%</b>	<b>\$325,831,264,205</b>
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9	Sweden	\$2,263,171,918	23.6%	\$6,868,478,184
10	United Arab Emirates	\$2,083,912,596	30.3%	\$6,947,270,925
11	Spain	\$1,758,628,305	2.2%	\$5,024,535,428
12	Australia	\$1,669,423,354	2.0%	\$5,971,467,399
13	Austria	\$1,475,772,923	17.6%	\$3,592,373,202
14	Netherlands	\$1,246,972,906	9.8%	\$4,737,211,235
15	Finland	\$1,046,708,876	12.8%	\$3,810,773,997
16	Brazil	\$565,339,213	1.0%	\$1,460,376,838
17	Belgium	\$483,351,365	6.9%	\$1,862,672,923

18	Taiwan	\$395,981,076	2.5%	\$1,487,359,116
19	India	\$381,271,129	0.9%	\$1,136,972,342
20	Italy	\$332,770,318	1.0%	\$1,078,851,005
21	Singapore	\$323,403,646	2.2%	\$976,035,428
22	Kuwait	\$157,004,718	4.6%	\$600,208,051
23	South Korea	\$154,055,340	0.3%	\$354,565,851
24	Israel	\$73,885,160	1.7%	\$436,810,520
25	Bahrain	\$73,131,680	50.7%	\$224,305,665
26	Ireland	\$70,339,047	0.8%	\$159,990,432
27	Malaysia	\$59,816,284	1.3%	\$228,926,907
28	Nigeria	\$54,014,695	5.4%	\$94,043,293
29	Chile	\$50,429,480	2.7%	\$222,445,097
30	Panama	\$40,658,197	0.0%	\$126,134,813
31	Indonesia	\$36,481,719	0.3%	\$88,437,412
32	Argentina	\$20,693,565	0.0%	\$59,216,983
33	Uruguay	\$20,085,164	1.6%	\$48,531,603
34	Thailand	\$17,610,262	0.5%	\$63,979,344
35	Turkey	\$14,283,240	0.5%	\$65,779,635
36	Colombia	\$10,345,315	0.8%	\$82,379,826
37	Ecuador	\$3,790,192	0.4%	\$14,243,811
38	Peru	\$3,295,758	0.1%	\$20,773,202
39	Pakistan	\$2,304,805	0.1%	\$11,495,288
40	Costa Rica	-	#N/A	\$4,587,601
41	Venezuela	-	#N/A	\$40,850
Unassociated ABA Numbers		\$1,950,230,709	#N/A	\$7,920,704,092
<b>Total Observed Payments</b>		<b>\$179,135,385,287</b>	<b>5.3%</b>	<b>\$536,402,540,734</b>

Source: IORB Data Transmitted to HSGAC from the Federal Reserve, Calculated Duties by Country USITC

# THE FED'S +\$1 TRILLION DRAIN ON TAXPAYERS

IN 2024 ALONE, THE FED PAID \$186 BILLION TO BANKS. THE FED WILL CONTINUE MAKING INTEREST PAYMENTS TO BANKS FOR THE NEXT DECADE, COSTING TAXPAYERS OVER A TRILLION DOLLARS.

COST TO TAXPAYERS: \$1.1 TRILLION OVER 10 YEARS

	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035
FEDERAL FUNDS RATE (PROJECTED)	3.58%	3.35%	3.36%	3.34%	3.31%	3.28%	3.25%	3.23%	3.22%	3.21%
FEDERAL RESERVE PAYMENTS TO BANKS (BN)	\$117	\$109	\$109	\$109	\$108	\$107	\$106	\$105	\$105	\$104

SOURCES: CBO, THE FOUNDATION FOR GOVERNMENT ACCOUNTABILITY (FOGA)



## BOTTOM LINE:

THE FED IS WASTING AMERICAN TAXPAYER DOLLARS TO PAY BANKS ON THEIR RESERVES. CONGRESS MUST ACT TO REPEAL THE FED'S AUTHORITY TO PAY BANKS, TO SAVE TAX DOLLARS, & RESTORE FISCAL RESPONSIBILITY.

**RICK SCOTT**  
FLORIDA'S U.S. SENATOR