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POLICY SPOTLIGHT

Closing the Fed's Oversight Gap

For more than a century the Federal Reserve has had only minimal oversight. Here are options for strengthening the Fed's accountability.

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The Federal Reserve's governance framework has significant gaps in accountability that are impairing its credibility and democratic legitimacy. The Fed's programs and operations are not subject to comprehensive external reviews, because its inspector general is a Fed employee (not a presidential appointee), and current law limits the scope of reviews by the Government Accountability Office (which reviews the performance and cost effectiveness of every other federal agency). Specifically, there have been no external reviews of the Fed's balance sheet programs, which are now costing taxpayers more than \$1 trillion; no external reviews of Fed salaries, which are roughly twice those of any other federal agency; and no external reviews of the design and cost of the Fed's \$3.1 billion upgrade of its headquarters. Consequently, statutory measures are urgently needed to ensure effective oversight and prudent stewardship without undermining the Fed's independence in determining the appropriate stance of monetary policy.¹

1. Establish a presidentially appointed inspector general (IG).

At every other federal agency whose operating budget exceeds \$5 billion, the IG is a federal official appointed by the president and confirmed by the Senate and directly accountable to Congress. In contrast, the Fed's IG is merely an employee appointed by the Fed chair who works "under the authority, direction, and control" of the Fed chair on all policy-related matters. Establishing a presidentially appointed IG at the Fed should not be characterized as undermining the Fed's independence in setting monetary policy, because external watchdogs are in place at other major central banks. For example, the Bank of England has an Independent Evaluation Office that reports directly to an external oversight committee.

¹ Scan the QR code below for a comprehensive list of Mercatus research products by this author, including studies of the issues and policy measures described in this policy spotlight.



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2. Initiate comprehensive reviews by the Government Accountability Office (GAO).

GAO is an independent, nonpartisan agency that reviews the programs and operations of all other federal agencies, including regulatory commissions such as the SEC and CFTC, whereas the Fed has been exempted from comprehensive GAO reviews. Authorizing GAO to evaluate the efficacy and efficiency of all Fed programs and operations would align its public accountability with that of other major central banks. For example, the Bank of England's performance is reviewed by the UK National Audit Office, and the European Central Bank's performance is reviewed by the European Court of Auditors (the counterpart of GAO).

3. Reassess the use of upgraded Federal Reserve headquarters.

Congress could explore whether any of the Fed's upgraded HQ buildings should be transferred to other agencies, especially since the Fed has recently announced that its staff will be shrinking significantly over coming years relative to what was envisioned when the upgrade was initiated. For example, the building at 1951 Constitution Avenue was transferred from GSA to the Fed in 2018 for \$43 million and is now undergoing a \$1.5 billion upgrade; that building could potentially serve as the new headquarters for the State Department, whose main offices are located just a block away.

4. Convene a blue-ribbon commission to review the Fed's structure and governance.

Congress designed the Fed's monetary policy committee to be composed of individually accountable experts with a Fed chair who would serve as "first among equals," similar to the role of the chief justice at the US Supreme Court. Since 2015, however, the Federal Reserve Board has been directly involved in selecting the heads of each of the 12 Federal Reserve Banks, and those officials are now viewed as "subordinates" of the Fed Board. Moreover, the Fed Board's staff report solely to the Fed chair, who is designated as its CEO, whereas the rest of the Board members have nonexecutive roles. A blue-ribbon commission could revisit the Fed's institutional structure and provide specific recommendations to Congress.

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