

# The Structure and Functions of the Federal Reserve System– SMART Lesson

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## Lesson by

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## Lesson Description

In this lesson, students will learn about the structure and functions of the Federal Reserve System. They will locate the 12 Federal Reserve District Banks on a map of the United States that is hyperlinked to slides highlighting the states found within each Reserve District.

## Concepts

Board of Governors  
Federal Open Market Committee  
Federal Reserve Advisory Councils  
Federal Reserve District Banks  
Monetary policy  
Payment services  
Regulation  
Supervision

## Objectives

Students will be able to:

- Describe the structure of the Federal Reserve System
- Locate the Federal Reserve System’s District Banks
- Identify the functions of the Federal Reserve System

## Materials

- SMART Notebook File—“The Structure and Functions of the Federal Reserve System”
- Handout 1—one copy per student
- Handout 2—one copy per student
- Handout 1—Answer Key, one teacher copy
- Handout 2—Answer Key, one teacher copy

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## Preparation

Before the lesson, make one copy of Handouts 1 and 2 for each student. Save a master copy of the SMART file.

**Procedure** – Instructions for the SMART Board have been put in italics. Content background is in regular type.

1. *Display slide 1—Start the SMART presentation.*

Introduce the students to the objectives for this lesson.

2. *Display slide 2— Click on each green box to link to a corresponding website where students can learn more about the Fed’s structure. Use the discussion questions on Handout 1 as a guide to explore websites.*

## Advisory Councils

The Board of Governors works with three Advisory Councils, which carry out varied responsibilities in advising the board on banking and consumer issues. The three councils are the Federal Advisory Council, the Community Depository Institutions Advisory Council (CDIAC), and the Depository Institution Model Validation Council.

- The Federal Advisory Council is made up of 12 representatives of the banking industry, who advise the Board on all matters over which the Board has jurisdiction.
- The Community Depository Institutions Advisory Council (CDIAC) was established in 2010 to advise the Board on economic and lending conditions and other issues pertinent to community depository institutions.
- The Depository Institution Model Validation Council gives the Board input on the effectiveness of its stress test models. The goal of this council is to improve these assessments so that the integrity and independence of the program is strengthened and maintained.

## Directors

Each of the 12 Federal Reserve Banks has its own board of directors, as specified under the Federal Reserve Act. The majority of these directors are elected by the commercial banks in each district that are members of the Federal Reserve System, with the remainder appointed by the Federal Reserve Board. Each Federal Reserve Bank has a nine-member board of directors, who serve staggered three-year terms. Directors are designated as being either Class A, B, or C.

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Class A directors represent the member banks that own stock in their District Reserve Bank, and Class B and C directors represent the public and may not be affiliated with any bank; Class C directors are also prohibited from owning bank stock. One Class C director at each District Bank is designated by the Board of Governors to serve as chair, with another Class C director as deputy chair.

Each of the 24 branches of the Federal Reserve Banks also has either a five- or seven-member board of directors, most of whom are appointed by the parent Federal Reserve Bank; the others are appointed by the Board of Governors. These directors serve staggered three-year terms, with one member annually appointed by the Federal Reserve Board as chair.

The boards of directors of the Reserve Banks and branches provide the Federal Reserve System with information on economic conditions from across the country, which is used by the Federal Open Market Committee and the Board of Governors to guide monetary policy.

The Board of Governors of the Federal Reserve System consists of seven members who are appointed by the president and confirmed by the Senate for 14-year terms. Members who fill an unexpired term may be reappointed for another term. The president selects both the Board's chair and vice chair, who serve four-year terms. The Board of Governors meets regularly, usually about twice a month.

## 12 Federal Reserve Banks

The Federal Reserve System is made up of 12 regional banks and 24 branches. Each bank and its corresponding branches are listed below. *Clicking on the box will take you to a System map.*

1st District: Boston

2nd District: New York

3rd District: Philadelphia

4th District: Cleveland (Cincinnati, Pittsburgh)

5th District: Richmond (Baltimore, Charlotte)

6th District: Atlanta (Birmingham, Jacksonville, Miami, Nashville, New Orleans)

7th District: Chicago (Detroit)

8th District: St. Louis (Little Rock, Louisville, Memphis)

9th District: Minneapolis (Helena)

10th District: Kansas City (Denver, Oklahoma City, Omaha)

11th District: Dallas (El Paso, Houston, San Antonio)

12th District: San Francisco (Los Angeles, Portland, Salt Lake City, Seattle)

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## Federal Open Market Committee

The Federal Open Market Committee (FOMC) is made up of 12 members--the seven member Board of Governors of the Federal Reserve System; the president of the Federal Reserve Bank of New York; and four of the remaining 11 Reserve Bank presidents. Each of these 11 Reserve Bank presidents serve one-year terms on a rotating basis, with the rotations coming from these four groups: Boston, Philadelphia, and Richmond; Cleveland and Chicago; Atlanta, St. Louis, and Dallas; and Minneapolis, Kansas City, and San Francisco. Nonvoting Reserve Bank presidents fully participate in the meetings by being involved in discussions and assessments of the national economy and various policy options. The FOMC meets about every six weeks, for a total of eight regularly scheduled meetings each year. Additional meetings and telephone conferences may be called as necessary. At these meetings, the FOMC determines the appropriate monetary policy actions, given a thorough review of current economic and financial conditions and the Federal Reserve's commitment to its dual mandate (price stability and maximum employment).

### *3. Display slide 3— Share the following information with your students.*

The Federal Reserve System is led by the Board of Governors, headquartered in Washington, D.C. The Board consists of seven members who are appointed by the president and confirmed by the Senate. The members serve staggered 14-year terms, but if they fill an unexpired term, they may be reappointed for another full 14-year term. The president also chooses two members to serve as chairman and vice chairman. These appointments are for four years and are approved by the Senate.

The primary responsibilities of the Board are to supervise and regulate banks that are members of the Federal Reserve System, bank holding companies, international banking operations that are in the United States, and the U.S. activities of foreign banks. All banks seeking a merger must apply to the Federal Reserve for approval, and all merger applications are reviewed by the Federal Reserve Board.

The Board shares responsibility for the policy on the discount rate, the interest rate at which financial institutions may take a loan from the Fed, with the 12 Reserve Banks, and is also responsible for setting the reserve requirement, the percentage of deposits that financial institutions must keep on reserve for their everyday financial transactions, either on their own premises or with their local Federal Reserve Bank or branch. The Board is responsible for the oversight of the 12 Federal Reserve Banks and their branches, including appointing certain

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members of the Bank and Branch Board of Directors, and approving the members who are chosen as chairman and deputy chairman.

#### 4. *Display Slide 4 -*

The Board of Governors works with three Advisory Councils who carry out varied responsibilities in advising the board on banking and consumer issues. The three councils are The Federal Advisory Council, The Community Depository Institutions Advisory Council (CDIAC) and The Depository Institution Model Validation Council.

*Students will match the description of the duties of each council with the appropriate council name. Students can check their answers by clicking on the “Check” button, or solve the puzzle by clicking on “solve”. The puzzle can be reset using the “reset” button.*

- The Federal Advisory Council is made up of twelve representatives of the banking industry, who advise the Board on all matters over which the Board has jurisdiction.
- The Community Depository Institutions Advisory Council (CDIAC) was established in 2010 to advise the Board on economic and lending conditions and other issues pertinent to community depository institutions.
- The Depository Institution Model Validation Council gives the Board input on the effectiveness of their stress test models. The goal of this council is to improve these assessments so that the integrity and independence of the program is strengthened and maintained.

5. *Display slide 5—Have students identify what the 12 cities listed have in common. Click the question mark to reveal a picture of the Board of Governors facility in Washington, D.C. These are the 12 Federal Reserve District Banks. Use the discussion questions on Handout 2 as a guide to answer questions about the Board of Governors. Click the white star in the top left hand corner to advance to slide 6. Students can click the white star marking Washington, D.C., on the U.S. map on slide 6 to return to slide 5 as a reference.*

6. *Display slide 6—Have students write the names of each of the 12 Federal Reserve District Banks in their respective boxes on slide 6. (Slide the boxes to check the answers.) Students can click the red dots to advance to slides revealing the states that are located in each District. Ask students to identify their District Bank based on the location of your school. Slides 7-18 are hyperlinked from slide 6 and represent each of the 12 Federal Reserve Districts.*

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7. Display slide 19 —Students will sort items connected with the Fed’s three main functions. Have students slide the activities into the appropriate categories. Students can check their work by clicking on the “check” button or see all of the correct answers by clicking on “solve.” The grid can be reset so that other students can play by clicking on “reset.”

## **Answer Key:**

### **Payment Services**

Processing checks  
U.S. Treasury’s Bank  
Distributing currency  
Automated Clearing House  
Banker’s Bank

### **Supervision and Regulation**

International banking institutions  
Promoting the safety and soundness of financial institutions  
State chartered banks  
Bank, financial, and thrift holding companies

### **Monetary Policy**

Reserve requirements  
Price stability  
Open Market operations  
Maximum employment  
Discount rate  
Economic growth  
Interest paid on reserves

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## Handout 1 —Discussion Questions

### **Board of Governors**

1. Who is the current Chairman of the Board of Governors?
2. What are the duties of the Chairman?

### **Directors**

1. How many classes of directors are there? Who appoints each class?
2. Who is represented by Class A directors? Class B directors? Class C directors? What restrictions do these directors have?
3. Do the 24 branches have boards? How are they appointed?
4. What role do the directors play in the Federal Reserve System? How do they connect with the Federal Open Market Committee? Where are their contributions recorded?

### **12 Federal Reserve Banks**

1. Which district are you located in? What are its branches? (Click on the appropriate website to find the answer.)
2. Where are most of the banks located? Why do you think they are located the way they are geographically?

### **Federal Open Market Committee**

1. Who are the members of the Federal Open Market Committee? Which bank always sits on the FOMC?
2. How many FOMC meetings are held each year? What happens at these meetings?
3. Which four banks, besides New York, are currently voting members?
4. Which rotation is your District Bank located in? When will it vote?

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## Handout 1— Discussion Questions (Answer Key)

### Board of Governors

1. Who is the current Chairman of the Board of Governors? (*The Current chair as of December 2012 is Ben Bernanke.*)
2. What are the duties of the Chairman? (*The Chairman manages the Board’s staff, presides over Board meetings, and serves as the public spokesperson for the Board.*)

### Directors

1. How many classes of directors are there? Who appoints each class? (*There are three classes of directors, A, B, and C. The member banks elect three Class A and three Class B directors, and the Board of Governors appoints three Class C directors.*)
2. Who is represented by Class A directors? (*Stock holding member banks of the Federal Reserve District*). Class B directors? Class C directors? (*Both Class B and Class C directors represent the public*). What restrictions do these directors have? (*Class B and C directors may not be officers, employees, or directors of any bank. Class C directors may not be stockholders in any bank.*)
3. Do the 24 branches have boards? How are they appointed? (*Yes. The majority of the branch boards of directors are chosen by the parent Federal Reserve Bank, with the rest chosen by the Board of Governors.*)
4. What role do the directors play in the Federal Reserve System? (*The directors provide the System with information on economic conditions from their district.*) How do they connect with the Federal Open Market Committee? (*The information given by the directors help to inform the FOMC in their policymaking decisions.*) Where are their contributions recorded? (*The Beige Book shares the information from the directors with the public.*)

### 12 Federal Reserve Banks

1. Which district are you located in? What are its branches? (Click on the appropriate website to find the answer). (*Answers will vary.*)



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2. Where are most of the banks located? Why do you think they are located the way they are geographically? *(Most District Banks are located on the East Coast; this reflects the major population centers of 1913, when the Federal Reserve System was established.)*

## **Federal Open Market Committee**

1. Who are the members of the Federal Open Market Committee? Which bank always sits on the FOMC? *(The FOMC has twelve members—the seven member Board of Governors, the president of the Federal Reserve Bank of New York, and four of the remaining eleven Federal Reserve bank presidents, who serve on a rotating basis of one year terms. The Federal Reserve Bank of New York always sits on the FOMC).*
2. How many FOMC meetings are held each year? What happens at these meetings? *(There are eight regularly scheduled meetings. At the meetings, economic and financial conditions and risks to the Federal Reserve’s long-term goals are discussed so that the appropriate monetary policy actions may be conducted.)*
3. Which four banks, besides New York, are currently voting members? *(Answers will vary.)*
4. Which rotation is your district bank located in? When will it vote? *(Answers will vary.)*

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## Handout 2 —Discussion Questions

### Members of the Federal Reserve Board of Governors

*Students should answer the questions below using information found on the Board of Governors' website About the Fed. <http://www.federalreserve.gov/aboutthefed/default.htm> For additional information, click the link “Current FAQ: Who are members of the Federal Reserve Board, and how are they selected”? [http://www.federalreserve.gov/faqs/about\\_12591.htm](http://www.federalreserve.gov/faqs/about_12591.htm)*

1. How many members are on the Federal Reserve's Board of Governors?
2. Who nominates the members of the Board of Governors?
3. What U.S. congressional body confirms the appointment of a Federal Reserve Governor?
4. How long is a full term for a Federal Reserve Governor?
5. In contrast, how long is the term of the Chairman and Vice Chairman of the Board of Governors?
6. May Federal Reserve Governors be removed from their position because of their policy views?
7. Why are Federal Reserve Governors' terms staggered?
8. Why do you believe the law requires that nominees to the Board of Governors reflect a “fair representation of the financial, agricultural, industrial, and commercial interests and geographical divisions of the country”?
9. Who is the current Chairman of the Board of Governors?
10. Who is the current Vice Chair of the Board of Governors?

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Handout 2 — Discussion Questions (Answers: **Certain answers will vary as the composition of the Board of Governors changes.**)

1. How many members are on the Federal Reserve’s Board of Governors? (*When all positions are filled, there are seven members.*)
2. Who nominates the members of the Board of Governors? (*The president of the United States nominates the members of the Board of Governors.*)
3. What U.S. congressional body confirms the appointment of a Federal Reserve Governor? (*The U.S. Senate confirms all presidential appointments.*)
4. How long is a full term for a Federal Reserve Governor? (*A full term, when served, is 14 years.*)
5. In contrast, how long is the term of the Chairman and Vice Chairman of the Board of Governors? (*The Chairman and Vice Chairman serve four-year terms and they can be reappointed to serve until their 14-year term as Governor expires.*)
6. May Federal Reserve Governors be removed from their position because of their policy views? (*No. This helps to insulate the Board from political pressures and promotes an independent policymaking process.*)
7. Why are Federal Reserve Governors’ terms staggered? (*Staggered terms also contribute to the Board’s independence.*)
8. Why do you believe the law requires that nominees to the Board of Governors reflect a “fair representation of the financial, agricultural, industrial, and commercial interests and

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geographical divisions of the country”? *(This helps to provide insights from these industries and geographical divisions during FOMC policy discussions.)*

9. Who is the current Chairman of the Board? *(Ben Bernanke is the current Chairman; however, this answer will vary in the future.)*

10. Who is the current Vice Chair of the Board of Governors? *(Janet Yellen is the current Vice Chair; however, this answer will vary in the future.)*