III. A Lower Dividend for High Asset Federal Reserve Member Banks

A. Introduction

On December 14, 2015, President Obama signed into law the Fixing America's Transportation (FAST) Act, a $305 billion bill, just before federal funding expired for roads and transit systems.[1] Congress has historically funded such transportation projects through the gas tax, a federal excise tax on fuel.[2] However, the tax rates on gasoline and diesel have not changed since 1993, and the current gas tax does not generate enough revenue annually to fully fund transportation projects.[3] In its reluctance to increase the tax rate, Congress instead opted for alternative ways to raise the needed funds.[4] For example, Congress modified the dividend the Federal Reserve System (the Fed) pays to member banks that have assets of over approximately $10 billion.[5] The Fed previously paid a 6 percent dividend on the capital stock member banks are required to purchase.[6] The law changes the

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[1] Keith Laing, *Obama Signs $305B Highway Bill,* THE HILL (Dec. 4, 2015, 5:05 PM), http://thehill.com/policy/finance/262171-obama-signs-305b-highway-bill [http://perma.cc/FW33-SXU2].

[2] Tracey M. Roberts, *Picking Winners and Losers: A Structural Examination of Tax Subsidies the Energy Industry*, 41 COLUM. J. ENVTL. L. 63, 90 (2016).

[3] *Id.* at 90 n.184 ("This has led to shortfalls in the Highway Trust Fund, hampering the federal government's ability to fund highway repairs, environmental restoration, and public transit alternatives.").

[4] Laing, *supra* note 1 ("The gas tax has been the traditional source for transportation funding since its inception in the 1930s, but lawmakers have resisted increasing the amount that drivers pay.").

[5] *Federal Reserve Finalizes Lower Dividend for Member Banks*, REUTERS (Nov. 23, 2016, 11:06 AM), http://www.reuters.com/article/us-usa-fed-dividends/federal-reserve-finalizes-lower-dividend-for-member-banks-idUSKBN13I1VB [https://perma.cc/8EDR-Q9JY] ("[T]he Fed must pay institutions with $10 billion or more in assets either the traditional rate of 6 percent or the prevailing 10-year Treasury auction rate, whichever is less."); Press Release, Board of Governors of the Federal Reserve System, Federal Reserve Board Issues Final Rule Regarding Dividend Payments on Reserve Bank Capital Stock (Nov. 23, 2016), https://www.federalreserve.gov/newsevents/pressreleases/bcreg20161123a.htm [https://perma.cc/Y2QT-Z927]; *Fed Adjusts Reserve Bank Dividend Threshold*, CQ ROLL CALL (Feb. 24, 2017), 2017 WL 727112 (adjusting total assets cap to $10.122 billion to reflect inflation).

[6] *Id.*

payment to banks to the lesser of either the previous 6 percent rate, or the current yield on the ten-year Treasury note (T-note).[7] The T-note rate stood at 2.16 percent as of September 1, 2017. Therefore, at present, the law reduces the dividend close to two-thirds for affected member banks.[8] Even this figure is more generous to the banks than the original proposal, which would have lowered the dividend more drastically to 1.5 percent.[9] The Fed paid approximately $22.2 billion in dividends, cumulatively, to member banks between 1914 and 2015, including $1.7 billion paid in 2015 alone.[10]

In response, Washington Federal, National Association (Washington Federal), an affected large member bank, and the American Bankers Association (ABA) filed a class action complaint in the Court of Federal Claims (CFC) against the U.S. government on February 9, 2017, seeking reimbursement for the reduction.[11] The plaintiffs alleged that the action amounted to a breach of contract, as well as an unlawful taking under the Fifth Amendment.[12] The government countered that no such contract exists between the parties, and that there is no property right under which to allege a taking.[13]

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[7] *Id.* (outlining the finalized rule pertaining to the FAST Act's dividend modification).

[8] *Daily Treasury Yield Curve Rates*, U.S. DEP'T OF THE TREASURY, https://www.treasury.gov/resource-center/data-chart-center/interest-rates/Pages/TextView.aspx?data=yieldYear&year=2017 [http://perma.cc/YZE6-WLT8]; Kathleen Miller, Jeff Plungis & Richard Rubin, *Senate Highway Deal Relies on Reduced Fed Payments to Banks*, BLOOMBERG (July 21, 2015), www.bloomberg.com/news/articles/2015-07-21/highway-agreement-provides-three-years-of-funds-mcconnell-says (describing early proposal to cut dividend).

[9] Miller, Plungis & Rubin, *supra* note 8 (reviewing an early draft proposal of the FAST Act).

[10] 102 BD. GOVERNORS FED. RES. SYS. ANN. REP. 306 (2015).

[11] Press Release, American Bankers Association, ABA Files Suit Over Federal Reserve Dividend Cut (Feb. 9, 2017), https://www.aba.com/Press/Pages/020917FedDividendComplaint.aspx#_ga=2.47183591.1176976535.1505969209-1422627035.150499825 [https://perma.cc/FAK5-YVYD] ("[A] rate that was codified in the Federal Reserve Act of 1913 and is memorialized in contracts between the Federal Reserve Banks and their member bank stockholders.").

[12] *Id.*

[13] Chris Bruce, *U.S. Urges Dismissal of Bank Suit on Fed Dividends,* BLOOMBERG BNA (Apr. 11, 2017), https://www.bna.com/us-urges-dismissal-n57982086520 [https://perma.cc/F2HL-J5E6] ("The alleged contract, the

This article will discuss the origins of the 6 percent dividend payment to Fed member banks, the lawsuit, concerns pertaining to the legislation modifying the dividend, and the change's likely effects. First, Section B reviews the intended purposes of the dividend in the early history of the Fed. Second, Section C examines the lawsuit and the arguments presented by the government as well as by Washington Federal and the ABA. Third, Section D highlights criticisms regarding the dividend change voiced throughout the legislative process. Finally, Section E discusses the likelihood that the change will have no significant impact on Fed membership.

B. History of the Dividend

The Panic of 1907 illuminated the urgency in addressing the periodic bank runs that wreaked havoc on the decentralized banking system and dried up access to currency.[14] Senator Nelson Aldrich of Rhode Island chaired the National Monetary Commission, which was charged with the mission to determine the causes of the Panic and suggest possible remedies.[15] The review eventually led to the Federal Reserve Act of 1913, which established the Fed.[16] The legislation created the Fed to serve several roles, including as a lender of last resort, as well as to provide an elastic currency, maintain oversight for the nation's historically fragmented banking sector, and operate an efficient national check-clearing system.[17] Overall, the Fed was designed to strengthen the country's financial stability.[18] Just as state-

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government said, 'reflects nothing more than the parties' statutory and regulatory obligations.'").

[14] MICHAEL S. BARR ET AL., FINANCIAL REGULATION: LAW AND POLICY 42–44 (2016) ("After the Panic of 1907, many supported reforms that could reduce the banking system's susceptibility to panics as a result of seasonal demands.").

[15] Jerry W. Markham, *Banking Regulation: Its History and Future*, 4 N.C. BANKING INST. 221, 230–31 (2000) (describing the causes of the creation of the Monetary Commission).

[16] 12 U.S.C. § 221 (2012) (describing the organization of the Fed).

[17] Michael Wade Strong, *Rethinking the Federal Reserve System: A Monetarist Plan for a More Constitutional System of Central Banking*, 31 IND. L. REV. 371, 376 (2001) (describing the responsibilities of the new Fed).

[18] John L. Walker, *Emergency Tools to Contain a Financial Crisis*, 35 REV. BANKING & FIN. L. 672, 707–08 ("The Federal Reserve System was created in response to financial panics as a tool to preserve financial stability.

chartered banks could apply to become national banks, membership in the Fed was optional for state banks.[19] Membership was mandatory for nationally chartered banks.[20]

The policy of paying out a 6 percent dividend to member banks was an incentive for state banks taking a potentially significant risk in joining the Fed.[21] In order to become a member and receive the dividend payment, banks are required to purchase Federal Reserve Bank stock.[22] Specifically, banks must spend 6 percent of their capital to purchase capital stock of the district Federal Reserve Bank.[23] The bank contributes half of this amount to the Reserve Bank and the other half must be available on call.[24] Accordingly, the stock is illiquid, and, unlike corporate stock, cannot be sold, traded, or used as collateral.[25] In exchange for this "dead capital," the Federal Reserve Act included the payment of a 6 percent dividend to the member banks on the capital stock.[26] Membership also increased regulation on the banks' activities, including restrictions on how the banks could pay dividends, which previously only applied to national banks.[27] In the Fed's earliest

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Moreover, the recent financial crisis highlighted the significance of the financial stability goal in central banks' mandate.").

[19] Strong, *supra* note 17, at 377 (citing Brooks State Bank v. Fed. Reserve Bank of S.F., 281 F. 222, 225 (D. Or. 1922) ("Any nonmember bank . . . could avail itself of the Reserve's check clearing system, so long as it maintained an appropriate balance with the twelve Federal Reserve Banks.")).

[20] *Id.* (discussing the requirements for Fed membership).

[21] U.S. GOV'T ACCOUNTABILITY OFF., GAO-17-243, FEDERAL RESERVE SYSTEM: POTENTIAL IMPLICATIONS OF MODIFYING THE CAPITAL SURPLUS ACCOUNT AND STOCK OWNERSHIP REQUIREMENT 16 (2007) [hereinafter GAO Report], http://gao.gov/assets/690/683000.pdf [https://perma.cc/5QZ2-DF2K] (discussing that part of the initial mission of the Fed was to attract members despite higher regulations).

[22] *Id.* at 17 (outlining the stock purchase requirement for Fed membership). The membership requirements remain for all member banks, leading to the disparity between those now experiencing a lower divided due to their size, and all other member banks, which are unaffected by the legislation.

[23] 12 U.S.C. § 287 (2012).

[24] *Id.* (reviewing Fed member bank stock purchase requirements).

[25] *Fed Adjusts Reserve Bank Dividend Threshold*, *supra* note 5 ("The dividend was established in 1913 to encourage banks to join the national banking system and had been largely unchanged since that time.").

[26] *Id.* (describing how given that the stock was illiquid, the bank would in exchange receive a guaranteed dividend amount).

[27] Robert F. Weber, The Comprehensive Capital Analysis and Review and the new Contingency of Bank Dividends, 46 SETON HALL L. REV. 43, 58–63

days, the dividend constituted a risk premium for banks due to the uncertainty of the stock's success among the various Fed branches.[28] Additional uncertainty surrounded the survival of the Reserve Banks themselves.[29] Smaller Reserve Banks in rural areas, which typically did not have enough capital for the dividend to serve as an incentive, were especially worried.[30]

Applying to become a member bank also effectively required the bank to cede its potentially lucrative check clearing business.[31] As explained above, the Fed was intended to serve as an efficient check-clearing system, and more centralization in this service resulted in lower check-clearing income for the scattered state banks.[32] In sum, between stock purchase requirements, increased regulatory burden, and lost services, Fed membership posed a high opportunity cost, which the 6 percent dividend rate was intended to offset.[33]

C. American Bankers Ass'n v. United States

On February 9, 2017, the ABA and Washington Federal filed a lawsuit against the United States government in the CFC seeking

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(2015) (stating the rules "prohibit[ed] them from effectuating distributions of corporate property, including dividends, out of their 'capital,' . . . [so] a bank could only pay dividends out of its retained earnings—that is, current earnings or past earnings kept within the firm . . . .").

[28] GAO Report, *supra* note 21, at 18 (describing the incentive of the 6 percent dividend).

[29] *Id.*

[30] *Id.* (describing how banks in urban areas were inherently better equipped to take advantage of and benefit from the dividend).

[31] David Dayen, *This Is the Fed's Most Brazen and Least Known Handout to Private Banks*, NEW REPUBLIC (Mar. 9, 2014), https://newrepublic.com/article/116913/federal-reserve-dividends-most-outrageous-handout-banks [https://perma.cc/HEZ3-JDG2] (quoting Allan Meltzer, former professor of political economy at Carnegie Mellon University and historian of the Federal Reserve, "They had to give up a major source of revenue, the charge they made for check clearing. Back then, if you received a check for $10, you might get back $9.50.").

[32] *Fostering Payment and Settlement System Safety and Efficiency* 120, https://www.federalreserve.gov/aboutthefed/files/pf_6.pdf [https://perma.cc/ZQ8Z-2WLF].

[33] *See* GAO Report, *supra* note 21, at 18 ("The rationales for paying a 6 percent dividend rate included compensating banks for opportunity costs for providing capital and reserves to the Reserve Banks and attracting state-chartered banks to Federal Reserve membership.").

reimbursement for affected member banks for the difference in the annual dividend payment reduction.[34] The plaintiffs sought certification as a class under CFC Rule 23(a).[35] In the revised complaint filed in April 2017, Washington Federal described itself as one of seventy-two banks with more than $10 billion in assets which the legislation targets.[36]

1. The ABA and Washington Federal's Complaint

The ABA and Washington Federal alleged that the government effectively committed "highway robbery," arguing that the failure to pay dividends to affected banks at the previous standard of 6 percent resulted in a breach of contract.[37] In the alternative, the plaintiffs claimed that the failure to pay the dividends at the 6 percent rate amounts to a Fifth Amendment taking.[38] With respect to the breach of contract argument, the plaintiffs cited Washington Federal's compliance with member bank requirements, including "paying the requisite amounts to purchase Federal Reserve Bank stock, agreeing to keep the requisite amounts on call, and submitting themselves to enhanced regulatory oversight" as obligations under the contract.[39] Consequently, they alleged that the government had a "contractual obligation" to pay the dividends.[40]

The plaintiffs offered two breach of contract theories.[41] First, the plaintiffs claimed an express written contract existed between the

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[34] Press Release, American Bankers Association, *supra* note 11 (describing the grounds for the suit).

[35] Chris Bruce, *Federal Judge Skeptical of U.S. Arguments in Bank Dividends Case*, BLOOMBERG BNA (July 31, 2017), http://bit.ly/2Cmusje ("The suit was brought as a class action, though so far Washington Federal is the only bank in the case.").

[36] Am. Class Action Compl. at 1, Am. Bankers Ass'n v. United States, No. 1:17-cv-00194 (Fed. Cl. Apr. 14, 2017) [hereinafter Class Action Compl.].

[37] *Id.*

[38] *Id.*

[39] *Id.* at 20 (suggesting that while the arrangement for dividends was legislated, the exchange for consideration of purchasing stock amounted to a contractual arrangement).

[40] *Id.* ("The Government has a contractual obligation to pay a six percent dividend to Washington Federal and all other member bank stockholders.").

[41] *See id.* at 9–10 (claiming the existence of an express written contract, and in the alternative, a contract implied in fact).

parties.[42] Washington Federal's application in 2013 for stock in the San Francisco Federal Reserve Bank, they alleged, constituted an "offer to subscribe to stock . . . that would pay an annual dividend" according to the terms of Federal Reserve Act.[43] The argument maintained that the San Francisco Reserve Bank's subsequent approval of the application "constituted acceptance of Washington Federal's offer," and that nowhere in the alleged contract was any indication that the terms pertaining the 6 percent dividend were subject to modification.[44] Second, the plaintiffs claimed in the alternative the existence of a contract implied in fact.[45] According to this theory, Washington Federal's subscription to and payment for Reserve Bank stock, as well as the San Francisco Reserve Bank's issuance of the stock and payment of the dividend, demonstrated the existence of a contract.[46] Further, the government's actions, as illustrated in the Federal Reserve Act's invitation for banks to "subscribe" to stock, show it intended to contract with Washington Federal.[47] Therefore, in consideration for Washington Federal chartering as a national bank subject to the mandatory stock purchase and corresponding regulation, the government issued the stock, and agreed to pay the 6 percent dividend.[48]

As for the Fifth Amendment argument, the plaintiffs alleged the government conducted an illegal taking without compensation.[49] In changing the dividend, they argued, the government "deprived Washington Federal and other member bank stockholders of the value of their investments."[50] Alternatively, the plaintiffs alleged that the

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[42] *Id.*
[43] *Id.* at 9 (explaining that the possibility to subscribe creates a contractual offer).
[44] *Id.* at 10 (detailing the acceptance needed to create a contract with the U.S. government).
[45] *Id.*
[46] *Id.* at 10–11 ("The implied in fact contract is evidenced by the Federal Reserve Act, Washington Federal's subscription to San Francisco Reserve Bank stock, Washington Federal's payment of $24,048,444.75 to the San Francisco Reserve Bank, the San Francisco Reserve Bank's issuance of 479,610 shares of stock, and the San Francisco Reserve Bank's payment of a six percent dividend for two years.").
[47] *Id.* at 11.
[48] *Id.*
[49] *Id.* at 1 (alleging that the government's refusal to pay the 6 percent dividend constitutes an unlawful taking).
[50] *Id.* at 22.

"reduction in the interest paid on capital that Washington Federal . . . invested in Federal Reserve Bank stock . . . constitutes a taking . . . without just compensation in the form of a market return on the invested capital."[51]

2. U.S. Government's Response

In response, the U.S. government submitted a motion to dismiss and a motion for partial summary judgment.[52] The government maintained that no such contract exists, neither expressly nor implied, and even if such a contract existed, the only promise was to pay the statutory dividend rate, which the government continues to fulfill.[53]

The government offered its strongest argument in refuting the plaintiff's claim that the Federal Reserve Act demonstrated an intent to form a contract. The government highlighted the 1985 Supreme Court decision in *National Railroad Passenger Corp. v. Atchison*,[54] which upheld the "well-established presumption" that "a law is not intended to create private contractual or vested rights but merely declares a policy to be pursued until the legislature shall ordain otherwise."[55] This case suggests strong deference by courts to Congress, as it allows Congress to create and modify laws without having to consider whether the very act of legislating amounts to breaching a contract.[56] During oral arguments on July 27, 2017, Washington Federal alleged that a word such as "subscription" is understood to refer to a

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[51] *Id.*

[52] Def.'s. Mot. to Dismiss Pl.'s. Am. Compl. and Mot. for Partial Summ. J. at 1, Am. Bankers Ass'n v. United States, No. 1:17-CV-00194 (Fed. Cl. May 15, 2017) [hereinafter Mot. to Dismiss] (claiming that "the undisputed facts establish that there was no contract between either Washington Federal or the ABA, and the United States.").

[53] *Id.* at 19 (explaining that the government continues to execute the terms of the statute, despite the terms having been modified by the FAST Act).

[54] 470 U.S. 451, 465–66 (1985) (quoting Dodge v. Bd. of Educ., 302 U.S. 74, 79 (1937) (finding that Congress retained the ability to amend the Rail Passenger Service Act of 1970)).

[55] Mot. to Dismiss, *supra* note 52, at 19 ("[T]here is no indication in the Act or the Board's regulations that the United States intended to bind itself by contract to Federal Reserve member banks for the payment of Reserve Bank stock dividends.").

[56] *See* Nat'l R.R., 470 U.S. at 466 ("[T]he principal function of a legislature is not to make contracts, but to make laws that establish the policy . . . .").

contract.[57] The government countered, alleging that the wording of the act, along with several words taken from it, do not amount to the creation of such a contract.[58] Similarly, the government argued that far from establishing any intent to create a contract, the law established a mandate that national banks purchase Reserve Bank capital stock, just as the law mandated that Reserve Banks pay dividends according to the statutory rate.[59] Underscoring this claim, the government noted that Reserve Banks are "expressly authorize[d]" to enter into some agreements, such as those for "enforcement or regulatory" purposes, whereas there is no language concerning a contract for the 6 percent dividend payment.[60]

The government's second-strongest argument refuting the existence of a contract alleged that at best, the presence of an offer and acceptance was ambiguous.[61] This is crucial because it places a greater burden of showing offer and acceptance on Washington Federal.[62] The government argued that the only terms of Washington Federal's "offer" were "dictated by statute," namely, the number of shares it was required to purchase and the price per share.[63] The government

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[57] Bruce, *supra* note 35 ("'The language of the application is that of contract,' Obermeier [counsel for the ABA and Washington Federal] said. He also said the dividend payments can't be a 'fee,' saying the Federal Reserve Act uses the word 'stock.'").

[58] *Id.* ("Attorney Eric P. Bruskin of the Justice Department's civil division said there was no contract for those payments, which he said were made in accordance with the Federal Reserve Act.").

[59] Mot. to Dismiss, *supra* note 52, at 20 ("[T]he applicable provisions of the Act contain mandatory statutory provisions, which courts have held do not indicate intent to contract.").

[60] *Id.* at 21–22 (citing 12 C.F.R. § 265.11(a)(15)(i) (2017) and stating, "Consequently, there is nothing in the Act or its implementing regulations to indicate the Government's intent to bind itself by contract regarding bank membership or stock dividends").

[61] *Id.* at 28–29 ("The purported offer and acceptance between the FRB and Washington Federal lack nearly every material term required to form a binding contract.").

[62] *Id.* at 28 (citing Petrini v. United States, 19 Cl. Ct. 41, 45 (1989) (finding that along with the required elements including "a mutual intent to contract" and "authority to contract on the part of the government agent, to "establish the existence of a contract with the Government," a party "must . . . demonstrate[] . . . lack of ambiguity in offer and acceptance")).

[63] *Id.* at 29 ("The purported offer and acceptance between the FRB and Washington Federal lack nearly every material term required to form a binding contract.").

suggested that the plaintiffs attempted to "avoid these defects in its offer" by relying on the Federal Reserve Act to provide the terms of the contract.[64] The government illustrated this claim's weakness by explaining that such a contract using extrinsic material "must explicitly, or at least precisely, identify the written material being incorporated and must clearly communicate that the purpose of the reference is to incorporate the referenced material into the contract."[65] Further, the Court is "reluctant to find that statutory or regulatory provisions are incorporated into a contract with the government unless the contract explicitly provides for their incorporation."[66] The government argued that no such provisions existed in any materials the plaintiffs submitted that would suggest the Federal Reserve Act provided proof of a contract.[67]

The government also claimed that there was no consideration for the alleged promise to pay a 6 percent dividend.[68] The government explained that, while Washington Federal may have alleged it entered into a contract, the bank's decision was in fact a voluntary action that bound it to the requirements of the Federal Reserve Act.[69] In response to the claim of an implied contract, the government reiterated its arguments against the existence of an express contract.[70] Further, the government warned that "[c]onstruing actions . . . pursuant to statute

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[64] *Id.* (suggesting that the plaintiffs lack sufficient offer and acceptance to illustrate the existence of a contract).

[65] *Id.* (citing Earman v. United States, 114 Fed. Cl. 81, 103–04 (2013) (explaining that a contract cannot "merely . . . acknowledge that the referenced material is relevant to the contract, e.g., as background law or negotiating history background law or negotiating history")).

[66] *Id.* at 30 (citing St. Christopher Assocs., L.P., v. United States, 511 F.3d 1376, 1384 (Fed. Cir. 2008) (finding that the Department of Housing and Urban Development was not required to consider an increase in rent in its regulatory agreement with the owner of apartment project)).

[67] *Id.* ("Here, Washington Federal's FR 2030a application contains no explicit or precise reference to any provision of the Act, or to the Board's regulations.").

[68] *Id.* at 31 ("Plaintiffs cannot establish consideration for the purported contract between Washington Federal and the FRB.").

[69] *Id.* at 33 ("[T]he actions alleged . . . do not constitute contractual consideration . . . but rather arose from . . . pre-existing duties as a national bank.").

[70] *See id.* at 45–46 (explaining that because express contracts and implied in fact contracts share the same elements, the Court should find in favor of the government "for the same reasons").

or regulation as manifest assent to the terms of an implied-in-fact contract . . . would transform every legislative program into a contractual program."[71]

Finally, in response to Washington Federal's Fifth Amendment argument, the government maintained that a bank could not "possess a reasonable investment-backed expectation that their stock would receive a six-percent dividend in perpetuity."[72] Not only is the stock not actually an "investment,"[73] but the highly regulated nature of Fed membership diminishes any reasonable expectation that the dividend rate would remain constant in perpetuity.[74]

3. CFC's Order Granting the Government's Motion to Dismiss

On October 30, 2017, the CFC granted the government's motion to dismiss the complaint.[75] The Court first held that the ABA did not have standing, finding that the ABA "did not allege that" it "suffered any monetary injury, nor did it allege that any member bank assigned to [it] the right to recover damages on their behalf."[76] As for

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[71] *Id.* (claiming that the government had no "intent to bind itself to Federal Reserve member bank").

[72] *Id.* at 53. The government added, "Nor has Washington Federal suffered a sufficiently adverse economic impact to its Reserve Bank stock to establish a taking." *Id*.

[73] *Id.* at 54 (citing Lee Constr. Co., Inc. v. Fed. Reserve Bank of Richmond, 558 F. Supp. 165, n.17 (D. Md. 1982) (explaining that because Fed member banks are required to purchase stock, "stock of Federal Reserve Banks, unlike stock in a private corporation, is not acquired for investment purposes.")).

[74] *Id.* at 54–55 (citing Fed. Housing Auth. v. The Darlington, Inc., 358 U.S. 84, 91 (1958) ("Those who do business in the regulated field cannot object if the legislative scheme is buttressed by subsequent amendments to achieve the legislative end.")).

[75] Mem. Op. & Final Order Granting the Gov't's Mot. to Dismiss at 1, Am. Bankers Ass'n v. United States, No. 1:17-cv-00194 at 13 (Fed. Cl. Oct. 30, 2017) [hereinafter CFC Final Order] ("The court has determined, however, that as a matter of law, Washington Federal . . . had neither a contractual, statutory, nor property right to a six percent dividend rate that would entitle it to relief.").

[76] *Id.* at 9; *see* United Food & Commercial Workers Union Local 751 v. Brown Grp., Inc., 517 U.S. 544, 554 (1996) (citing Hunt v. Wash. State Apple Advert. Comm'n, 432 U.S. 333 (1996) ("An association has standing to bring suit on behalf of its members when . . . neither the claim asserted nor the relief

Washington Federal's argument claiming a contractual right to a 6 percent dividend, the Court noted that the Federal Reserve Act "expressly" reserves for the Congress "[t]he right to amend, alter, or repeal this act."[77] Finding this fact "dispositive," the Court cited *Bowen v. Public Agencies Opposed to Social Security Entrapment*, in which the Supreme Court found that the U.S. government had reserved for itself the ability to amend sections of the Social Security Act, as well as "Agreements entered into 'in conformity with'" such sections.[78] Similarly, the government in this case had the authority to modify the dividend rate, and the legislation did not establish an unalterable right to collect a dividend at any rate.[79] Further, the Court held "where Congress expressly reserves the right to amend, alter, or repeal legislation, such statutory text 'is hardly the language of contract.'"[80]

The Court also rejected Washington Federal's Fifth Amendment taking argument, finding that no property interest existed under which to allege a taking.[81] First, while Washington Federal may have expected the 6 percent dividend, "[s]uch an 'expectation' does not rise to the level of 'property' protected by the taking[] clause" against the government.[82] This is true even if the expectation could otherwise have supported the existence of a contract in the private

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requested requires the participation in the lawsuit of each of the individual members.")).

[77] CFC Final Order, *supra* note 75, at 10 (citing 12 U.S.C. §226 (2012)).

[78] *Id.* (citing Bowen v. Pub. Agencies Opposed to Soc. Sec. Entrapment, 477 U.S. 41, 48–49, 54 (1986) ("The language of [the statute's] reservation expressly notified . . . that Congress retained the power to amend the law under which the Agreement was executed and by amending that law to alter the Agreement itself.")).

[79] *Id.* ("In short, the Federal Reserve Act conferred no right to Washington Federal or any other holder of Federal Reserve Bank stock to receive a dividend at any rate certain that Congress could not amend, change, or even eliminate.").

[80] *Id.* at 11 (quoting Nat'l R.R. Passenger Corp. v. Atchison, Topeka and Santa Fe Ry. Co., 470 U.S. 451, 467 (1985)).

[81] *Id.* at 13 (rejecting the existence of Washington Federal's alleged "cognizable private property interest" in the 6 percent return).

[82] *Id.* at 12 (quoting Zucker v. United States, 758 F.2d 637, 640 (Fed. Cir. 1985)).

sector.[83] Second, the Court explained that in addition to the fact that the government reserved the ability to amend the law, the illiquid nature of the Federal Reserve Bank stock from which the banks receive dividends illustrates the lack of a property right.[84] Washington Federal's ownership of the stock lacks the "crucial indicia" of a property right, such as "the ability to assign, sell, or transfer" the right.[85] The Court therefore determined that a property right to the value of the dividend did not in fact exist for which Washington Federal could claim a Fifth Amendment taking.[86]

D. Impact of the Decreased Dividend Rate

Apart from the lawsuit, additional considerations surrounding the legislation include frustration over the legislative process, the role of the Fed as a result of the legislation, and the law's impact on Fed membership.[87]

First, when Congress finalized the FAST Act, some raised concerns about the impact of altering such a relatively obscure element of the Federal Reserve Act.[88] Prior to passage, Sherrod Brown, the lead Democrat on the Senate Banking committee, voiced frustration about the lack of panel review of an earlier version of the modified dividend.[89] He expressed disapproval at the process, as well as the

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[83] *Id.* (differentiating between Washington Federal's longstanding expectations and the existence of an enforceable contract with the government).

[84] *Id.* at 13 (citing 12 U.S.C. § 287 (2012) ("Shares of the capital stock of Federal reserve banks owned by member banks shall not be transferred or hypothecated.")).

[85] *Id.* (quoting Am. Pelagic Fishing Co., L.P. v. United States, 379 F.3d 1363, 1374 (Fed. Cir. 2004) (finding that the owner of a commercial fishing vessel did not have a property interest in its corresponding permits and authorizations, and therefore was not entitled to compensation for the purposes of a Fifth Amendment taking)).

[86] *Id.*

[87] George Cahlink, *Fed Divided Prompts Interest in Congress*, CQ ROLL CALL (Aug. 6, 2015), 2015 WL 4647104 ("[Federal Reserve Chairwoman] Yellen warned about 'unintended consequences' if the dividend were altered and said it could cause smaller banks to flee the Federal Reserve system.").

[88] *Id.* (explaining that Congress last held hearings on the dividend paid to member banks in 1960).

[89] Steven Harras, *Fed Issues Rules to Cut Dividends Paid to Banks*, CQ ROLL CALL (Feb. 22, 2016), 2016 WL 690502; *see All Actions H.R.22—114th*

method of funding, which he described as "taking money from the banks and the Fed."[90] Others were concerned about the precedent of using the Fed to generate revenue to pay for legislative priorities.[91] They preferred that Congress find a more "honest" source of income.[92] In fact, the dividend reduction was not the only funding the Fed provides to pay for the legislation.[93] While the bill re-appropriates dividends as a source of funding, it also draws from Fed's surplus fund.[94] The legislation would extract any Fed surplus over $10 billion.[95] Just before the bill's passage in 2015, the surplus "totaled $29.3 billion as of Nov. 25."[96]

Furthermore, some question what effect, if any, the lowered dividend rate will have on the member banks.[97] Initial worries about banks leaving the Fed mellowed upon passage of the act, which removed earlier proposals that would have transferred even more funds from more banks.[98] For example, when the plan called for the historical 6 percent dividend to be paid out only to banks with assets

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Congress (2015–2016), CONGRESS.GOV, www.congress.gov/bill/114th-congress/house-bill/22/all-actions?overview=closed&q=%7B%22roll-call-vote%22%3A%22all%22%7D [https://perma.cc/EF5R-Y4NT] (explaining that, despite his concerns, Senator Brown voted in favor of the bill through passage).

[90] *Id.*

[91] George Cahlink, *Congress Raids Fed's Surplus for Highway Funding*, ROLL CALL (Dec. 8, 2015), http://www.rollcall.com/news/congress_raids_feds_surplus_for_highway_funding-245048-1.html [https://perma.cc/FRD7-ASK7] (explaining Senator Martin Heinrich's concerns about the method of funding the bill).

[92] *Id.* (detailing that Sen. Heinrich "said he backed the highway bill's infrastructure investments but would prefer they were made with 'honest payments' rather than coming out of the Fed account").

[93] Cheyenne Hopkins, *Fed Money Tapped in Highway Bill as Banks Get Dividend Break*, BLOOMBERG (Dec. 1, 2015), https://www.bloomberglaw.com/product/blaw/document/NYPNVE6TTDS3?bc=W1siU2Vhcm (explaining that "[t]he dividend reduction wouldn't be as much as originally proposed").

[94] *Id.*

[95] *Id.*

[96] *Id*.

[97] Cahlink, *supra* note 87 (reviewing the revived discussion regarding the Fed dividend payments).

[98] *Id.* ("The Senate highway bill would cut the rate to 1.5 percent, but only for banks with assets of more than $1 billion in a bid to shield smaller, community banks.").

under $1 billion, Federal Reserve Chairwoman Janet Yellen voiced concerns about the change's "unintended consequences."[99] She has since softened her criticism following the change to allow all banks under $10 billion to continue to receive the full 6 percent dividend.[100] As a result of the change, the law only immediately affected eighty-five of 1,896 member banks, though this figure contrasts slightly with the seventy-seven banks the plaintiffs cite in their complaint in *American Bankers Ass'n v. United States*.[101] The historical average of the new gauge of paying dividends—the yield on the 10-year Treasury note—is lower than the original 6 percent return, averaging approximately 4.7 percent since 1990, and 2.7 percent in the past ten years.[102] While the T-note yield is less predictable than the historical 6 percent figure, the current rate, while generationally low, is still higher than the original 1.5 percent cap on dividends the Senate originally considered.[103] As a result, the scaled-down legislation President Obama finally signed into law likely mitigates many initial concerns about the lowered dividend.

Additionally, the change is unlikely to have a significant impact on Fed membership, as there is little incentive to leave the Fed. As noted above, the change directly affects fewer than 100 banks, though they possess the highest assets of any member banks in the country.[104] The GAO report found that there is some concern among banks with assets under $10 billion about the precedent of modifying

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[99] *Id.* (discussing Yellen's earlier concerns that the lower threshold would have caused member banks to leave the Fed).

[100] *Id.* (stating the number of affected banks, which is significantly limited compared to the original proposal Congress considered).

[101] GAO Report, *supra* note 21, at n.14 (calculating the number of banks affected by dividend modification); *see* Class Action Compl., *supra* note 36, at 1.

[102] Peter Schroeder, *Banks Score Win as House Kills Fed Dividend Offset in Highway Bill*, THE HILL (Nov. 5, 2016), thehill.com/policy/finance/259252-banks-score-win-as-house-kills-fed-dividend-offset-in-highway-bill [https://perma.cc/M6Q9-42V5] (comparing earlier plans that likely would have lowered dividends to figures lower than the current T-note yield); *Daily Treasury Yield Curve Rates*, *supra* note 8 (compiling daily T-note rates).

[103] *Id.* ("To entice banks to participate, the Fed pays out a 6 percent dividend payment, which the Senate bill proposed slashing to 1.5 percent, calling it 'overly generous.'").

[104] GAO Report, *supra* note 21, at n.14 (explaining the scope of banks affected by the legislation).

the dividend rate.[105] However, none of the fourteen member banks the GAO interviewed intended to drop membership due to the modified dividend.[106] The sample included six banks with assets above $10 billion, which face the impact of the new law.[107] In the six months following passage of the FAST Act, there was a 2 percent drop in Fed membership, totaling forty-six banks, though this is attributed to "normal contrition and consolidation in the industry," and follows a larger recent downward trend in membership.[108] In May 2016, the Federal Deposit Insurance Corporation officials reported no impact from the changed dividend rate on state-chartered member and non-member banks, and the Office of the Comptroller of the Currency (OCC) maintained it was "too early to determine the impact of the dividend rate modification on national banks."[109] Rather, the GAO found banks are more likely to consider alternative methods to gain back the lost revenue.[110] This data suggests that while the change in the dividend rate will result in lower income, at least in the short term, affected banks will be able to weather the immediate shock.

Further, dropping membership would likely only harm the individual bank.[111] The GAO report cites OCC officials who stated that "costs associated with changing membership can be significant and can be a decision-making factor."[112] In addition, while state regulations, which guide nonmember banks, are generally less stringent than Federal Reserve requirements, legislation such as the Monetary Control Act of 1980 have strengthened requirements even among nonmember banks.[113] Therefore, the incentive to drop

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[105] *Id.* at 28 (finding that despite concerns, leaving the Federal Reserve was not a likely route for member banks).
[106] *Id.* (characterizing the results of the GAO's interviews).
[107] *Id.* (stressing that even banks immediately affected by the legislation do not intend to drop Fed membership).
[108] *Id.* (reflecting no significant drop-off of bank membership outside of trends that began in 2010).
[109] *Id.* (reviewing the findings and predictions of financial regulators pertaining to the Fed dividend modification).
[110] *Id.* at 26 ("[S]ome [interviewed banks] mentioned employee layoffs and increased fees on consumers as potential options to recoup the lost revenue.").
[111] *See id.* at 28 ("For example, industry association officials said that such costs could include those associated with changing the institution's name.").
[112] *Id.* (explaining banks' considerations in dropping membership outside of the modified dividend alone).
[113] Kenneth J. Robinson, *Depository Institutions Deregulation and Monetary Control Act of 1980*, FED. RES. HIST. (Nov. 22, 2013),

membership is further diminished. As a result, it is of little surprise that, despite the immediate decrease in income, the lasting impact of dividend modification on the member banks and the Fed as a whole is likely insignificant.

E. Conclusion

The dispute behind the ABA and Washington Federal's lawsuit against the government spotlights the challenge of modifying a long-standing incentive to joining the Federal Reserve. It also highlights the modern legislative challenges of identifying sources of revenue without resorting to increasing taxes, even those taxes established to fund the very types of projects in consideration. In light of the government's success in establishing that the Federal Reserve Act of 1913 created no contract or property rights, it is unclear at this time how the lower dividend rate will adversely affect Fed membership, or affect member banks themselves in the long run.

Harrison Kessler[114]

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federalreservehistory.org/essays/monetary_control_act_of_1980 [https://perma.cc/2A3Q-C2ZW] (discussing the impact of the Monetary Control Act of 1980 on nonmember banks).

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