Written by **Bob Adelmann** on June 6, 2011

The Federal Reserve Kids Page

In 2006 the Federal Reserve decided it was time to begin to reach out and influence middle schoolers with the party line about the Fed, and launched the Federal Reserve Kids Page. Consisting of 10 harmless-appearing questions, either in English or Spanish, the Fed's answers gloss over, and sometimes deliberately misstate, the correct answers.

Question 1: What is the Federal Reserve System?

Fed's answer: "The Fed is a bank for other banks and a bank for the federal government. It was created to provide the nation with a safer, more flexible, and more stable monetary and financial system. "

Better answer: The Fed is a cartel (a formal organization of service providers that agrees to fix prices and limit competition. The aim of such collusion is to increase individual members' profits by reducing or eliminating competition — see a broader definition here) which was formed to protect its member banks from suffering the consequences of bank runs (which occur when a bank's customers try to withdraw their money all at once because they're afraid the bank is, or might become, insolvent and unable to pay off their customers – see a broader definition here).

Thus, the Fed is known as the "lender of last resort" which means that if one of the cartel's banks gets in trouble, it can go to the Fed for money to tide the bank over until the run on the bank ends.

The Fed has no money of its own, but it can print money that looks like real money, which people will accept because other people will take it in trade for goods and services. This is often called fiat currency (money that has value only because the government says it does — for a broader discussion on fiat currency or money, go here).

The Fed's answer that the Fed was "created to provide the nation with a *safer*…monetary and financial system" must be challenged with the question, Safer than what? What was used as money before it became fiat or paper money? How does a person define safe for himself? At present, a piece of paper currency may be easily exchanged for goods and services at the store. It is easily recognized, and easily divisible into smaller or larger denominations. It is convenient to carry around, and since it represents purchasing power, it gives some people a sense of comfort and security in the event of an emergency. But will that piece of paper money always be able to buy the same amount of goods and services in the future? Is it safe to store paper money away to be spent later, perhaps much later?

The Fed also says it was created to provide the nation with a more *flexible* monetary system. What does flexible mean? Does it mean that paper is easier to carry than coins or checks or credit cards? Does it mean that money can be moved around from one bank to another quickly in the event of an emergency?

Does it mean that the Fed can take some of your money and give it to someone else without your permission?

The Fed says it was created to provide the nation with a more *stable* system. What does stable mean? Does it mean that people everywhere will always accept your paper money when you want to buy things? Does it mean that prices will never change? Does it mean that we will never have to worry about runs on the banks because experts at the Fed are watching things, so we don't have to? Does it mean that we can make plans for the future without having to worry about using our money then?

Question 2: Who created the Federal Reserve, and when was it created?

Fed's answer: "Congress created the Federal Reserve System on December 23rd, 1913, with the signing of the Federal Reserve Act by President Woodrow Wilson. "

Better answer: The creation of the Fed in 1913 was the culmination of efforts by bankers to create a central bank since the end of the Civil War in 1865. Resistance to central banking was very strong and as a result much of the negotiating had to take place secretly or else the public would find out and stop it. The most secret meeting took place in November, 1910 on Jekyll Island, off the coast of Georgia, where seven men (bankers affiliated with the biggest banks in the country) met to draw up plans for the Fed.

Here are some questions to ask about the creation of the Fed. Why was it done in secret? Why would the public have stopped the Fed if it had known about it beforehand? What didn't the public like about banks and bankers after the Civil War? What was wrong with the money system that needed to be fixed? Did the Fed fix what was wrong with the money system?

Question 3: What is the Board of Governors?

Fed's answer: "The Board of Governors oversees the Federal Reserve System. It is made up of seven members who are appointed by the President and confirmed by the Senate. "

Better answer: The Fed's answer is accurate, but it doesn't go very far. Who are the people who sit on the Board? Where did they come from? Are they bankers themselves? Who nominated them? Do they have special expertise and skills that qualify them? Are they political pay-offs to friends inside the banking system?

Question 4: Who are the members of the Board of Governors?

Fed's answer: Click here to find out.

Question 5: Where is the Federal Reserve Board of Governors located?

Fed's answer: The Federal Reserve Board of Governors is located in Washington, DC.

Question 6: What are the twelve Federal Reserve Districts?

Fed's answer: Click on Question 6 here

Question 7: What are some of the main responsibilities of the Federal Reserve System?

Fed's answer: "Conduct…monetary policy to help maintain employment, keep prices stable, and keep interest rates relatively low. " "To make sure [the banks] are safe places for people to keep their money. " "Provide financial services [such as] clearing checks, processing electronic payments, and distributing coin and paper money to the nation's banks, credit unions, savings and loan associations, and savings banks. "

Better answer: How does the Fed do that? How does the Fed keep prices stable when the paper money supply can be expanded at any time, which makes each piece of paper worth less? How does it maintain employment? With unemployment higher now than it has been in years, does that mean the Fed is failing in its purposes? How does it know how low interest rates should be? Isn't that set by people making purchases and loans in the marketplace? What if the interest rates that the Fed sets are too low? Won't that trick people into making bad economic decisions, such as when to buy a house or invest in a business? What if interest rates are too high? Won't that slow down economic activity, and put people out of work? And why is the Fed involved in processing checks and making sure that banks have enough coin and currency? Isn't that something a private company could do just as well?

Question 8: What are interest rates and why are they important?

Fed's answer: "Interest rates are the prices people pay to borrow money or are paid to lend money. Interest rates, like other prices, are determined by the forces of supply and demand…the Federal Reserve System is able to affect the level of interest rates through its monetary policy. "

Better answer: Part of the Fed's answer is true: interest rates are the prices people pay to borrow and lend money, and they are "determined by the forces of supply and demand. " But then the Fed contradicts itself, doesn't it, when it says it's "able to affect the level of interest rates through its monetary policy"? Why would it want to affect interest rates if people are already setting interest rates through supply and demand? If the Fed lowers interest rates, won't that mislead people into thinking that money is cheap and then decide to borrow while rates are low? If lots of people borrow while rates are low, what happens if those rates go up? What if lots of people make bad decisions all at the same time? Won't that create an imbalance in the economy? What happens if lots of people can't pay back those cheap loans? What does the Fed do then? What do those people who borrowed the money do?

Question 9: What is inflation?

Fed's answer: "Inflation means that the general level of prices of goods and services is increasing. When inflation is rapid, the prices of goods and services can increase faster than consumers' income, and that means the amount of goods and services consumers are able to purchase goes down. In other words, the purchasing power of money has declined. With inflation, a dollar buys less and less over time. "

Better answer: Inflation as defined by the Fed is the increase in the prices of goods and services. But what made those prices go up in the first place? Some prices might go up due to a shortage, or a poor crop, or a disruption in the manufacturing process. But other prices might go down as companies figure out ways to make things cheaper, or because consumers no longer want to buy a particular item. For example, a desktop computer 10 years ago might have cost $3,000, but today might cost only $500. So prices go up and down, according to supply and demand. But if you see prices of everything go up at the same time, isn't that different? Doesn't that mean that something else is responsible? Think about it: if the Fed is in charge of the supply of money, and it decides to increase the supply of money, what does that do to each piece of money already in your pocket? Doesn't it mean that each piece is worth less and will consequently purchase less when you go to spend it?

The Fed's answer is backwards. They increase the supply of money (to keep interest rates low, let's say). That is inflation. When that new money comes into the market place, it means that each piece of money is worth less which is then reflected as higher prices. In other words, higher prices are the result of the inflation that the Fed already created by increasing the supply of money. Think of it this way: prices aren't going up. The value of each piece of paper money is going down. That's the result of inflation.

Question 10: What is the FOMC, and what does it do?

Fed's answer: "FOMC stands for the Federal Open Market Committee. The FOMC consists of twelve members…The purpose of the FOMC is to determine the nation's monetary policy…The actions taken…affect…the prices of goods and services. "

Better answer: There is no better answer! The FOMC decides to adjust interest rates according to their "policy", and increases the supply of money accordingly, which then "affect[s]…the prices of goods and services. " In other words, when there is inflation (prices rising in the marketplace) it's because the Fed wanted it that way.