

Review of the Reserve Bank Act

Release Document – Monetary Policy Committee Appointment Process

July 2018

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Treasury Report: Monetary Policy Committee Appointment Process

Date:	23 May 2018	Report No:	T2018/1265
		File Number:	MC-1-7-6

Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Grant Robertson)	<p>Agree to the recommendations in this report.</p> <p>Refer this report to the Associate Ministers of Finance (Hon Parker, Hon Jones, Hon Shaw) for their information.</p>	Tuesday 29 May 2018

Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
Felicity Barker	Principal Advisor - Macroeconomic and Fiscal Policy Team	[2] (wk) [1] (mob)	✓
Renee Philip	Manager - Macroeconomic and Fiscal Policy Team	[2] (wk) [1] (mob)	

Actions for the Minister's Office Staff (if required)

Subject to the Minister of Finance's decisions, **arrange a meeting** with the Chair of the Reserve Bank Board to discuss the process for appointing MPC members and **refer** this report to the Associate Ministers of Finance (Hon Parker, Hon Jones and Hon Shaw) for their information.

Return the signed report to Treasury.

Note any feedback on the quality of the report

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Enclosure: No

Treasury Report: Monetary Policy Committee Appointment Process

Purpose of Report

1. This report advises you on the detailed process for appointing members to the Monetary Policy Committee (MPC). This advice follows on from your earlier decision that the provisions in the Reserve Bank Act relating to the process for appointment of MPC members be non-prescriptive (T2018/998 refers).

Background

2. On 19 March 2018, Cabinet agreed to amend the Reserve Bank of New Zealand Act 1989 (the Act) to establish an MPC at the Reserve Bank (the Bank) [CAB-18-MIN-0086 refers]. All of the members will be appointed to the MPC by the Minister of Finance (the Minister) on the recommendation of the Reserve Bank Board (the Board). This appointment process is modelled on the process that currently applies to the Reserve Bank Governor (the Governor), as discussed below.
3. At that time you also indicated to Cabinet that it is your intention that the MPC will initially have seven members: the Governor; the Deputy Governor; two members from the Bank's staff; and three members external to the Bank.
4. Finance Ministers (Hon Robertson, Hon Parker, Hon Jones, and Hon Shaw) have been delegated authority to make second-order policy decisions to progress the drafting of the amendment Bill.
5. On 12 April 2018, officials recommended, and Finance Ministers agreed, that no further details relating to the appointment process be provided for in the legislation (T2018/998 refers). This ensures that the appointment process will be flexible, and is consistent with the approach to appointments to Crown entity boards (refer to Annex One). In this same report, the Treasury also undertook to report back to you on the detailed process for appointments before draft legislation is agreed by Cabinet.

The Existing Appointment Process for the Governor

6. Since 1989 the Governor has been appointed through a process known as the “double veto”, where the Minister appoints a candidate recommended by the Board. This process was intended to reduce the risk of political interference in monetary policy. This has allowed the Board to determine how the appointment process works in practice.
7. While the process followed depends on the Board Chair, the typical approach has been for the Board to nominate a single candidate to the Minister when making a recommendation. This has often left the Minister with a binary choice to either accept or reject a nomination.
8. This is an unusual approach in the context of the wider state sector. Appointments to most public posts in New Zealand are made by the responsible Minister. Where checks are deemed necessary in an appointment process, for example in the appointment of judges, they are normally provided by vesting the appointment power in the Governor-General, on the recommendation of the responsible Minister. As set out

in Annex Two, a wide variety of appointment models is used across central banks internationally.

Recommended Approach to MPC Appointments

9. As noted in our 12 April advice, the Act is, and will remain, flexible enough to enable the Board to engage with the Minister during the appointment process, as is the case, for example, with appointments to Crown entity boards. Moreover, the proposed change to the Act, which will have the Minister appoint the Board Chair and Deputy, will support such a process.
10. In our initial advice on the MPC, we recommended a “Minister focussed” appointment process in legislation (T2018/321 refers). This would see the Minister appointing all members of the MPC on the recommendation of the Board. The Treasury recommended ministerial appointments to ensure that MPC members have democratic legitimacy, and to align with international practice for central banks. Consistent with this initial advice, we also propose changing the conventions to increase ministerial engagement in the appointment process.
11. To be clear, appointment processes should continue to ensure merit-based selection, and the Board should make its recommendations based on who it judges to be the best candidate. However, there are likely to be a number of candidates that have the requisite skills to make them suitable for the roles.
12. As noted above, the committee will include both internal and external members, alongside the Governor and the Deputy Governor. We consider that slightly different processes are appropriate, depending on the type of member being appointed.

The Governor and the external members

13. For the appointment of the Governor and the external members, we recommend ministerial involvement during the recruitment and nomination process.
14. For example, the process could see the Board Chair consult the Minister on the position specification before beginning the search process, and then again once a short-list has been finalised. Furthermore, where the Board finds that there is more than one suitable candidate for a role, the Board could explicitly recognise this when making its recommendation.
15. Such a process would bring MPC appointments in line with other state sector appointments where the relevant Minister is the key decision-maker. While the process could increase political influence on appointments, we consider that having the Board nominate candidates ensures a sufficient check on the Minister. Moreover, increasing ministerial involvement in the appointment process should serve to increase the accountability of both the Minister and the appointed candidate. This in turn should increase the MPC’s legitimacy in the eyes of the public.
16. As highlighted in Annex Two, central banks follow a variety of processes for appointing MPC members, but it is more often the case that appointments are made by elected politicians without a nomination process set out in legislation.

The Deputy Governor

17. For the appointment of the Deputy Governor, we recommend a similar process to the Governor and external members. However, the process should be amended to recognise that the Deputy Governor will report to the Governor and will be a key part of the Bank’s executive.

18. Cabinet has already agreed that the Board should be required to consult the Governor regarding the appointment of the Deputy Governor [CAB-18-MIN-0086 refers]. The Board could, for example, choose to do this by including the Governor on the interview panel. Moreover, where the Governor's views differ to those of the Board, we consider it prudent for the Board to relay those differences of view directly to the Minister when making its nomination.

The internal members

19. We recommend a process with less ministerial involvement for the other internal members than applies to the Governor and the Deputy Governor. This is because the appointments will necessarily be made from within the Bank's existing staff, which makes it important to ensure the appointee holds a suitable role within the Bank's organisational structure.
20. For these internal members, we recommend that ministerial engagement before a nomination is limited to consultation about the position description and the general timing of the appointment process. We also consider it appropriate for the Board to recommend a single preferred candidate to the Minister, unless the Board and Governor have different views on the preferred candidate, or the Board and the Governor consider there are multiple suitable candidates but no preferred candidate. As noted with the process for the Deputy Governor, since the Board is required to consult the Governor before making recommendations to the Minister, the Board may wish to involve the Governor on any interview panel for the internal MPC members.

Implementing the Recommended Appointment Process

21. Given the Board Chair will be instrumental in ensuring the appointment process meets your expectations, we suggest that you meet with the Board Chair to discuss the appointment process and agree an approach to the first round of appointments.
22. We do not consider it necessary or desirable to formally codify the exact process, as we expect that it will need to evolve over time. However, after meeting with the Chair, we recommend that you set out your high-level expectations for the appointment process by sending a letter of expectations to the Board. The previous letter of expectations was sent in November 2015. We consider that an updated letter is appropriate given the change in Government, the forthcoming changes to the Act, and the consequential changes to the Board's role.

Timing for Initial Appointments to the MPC

23. For the MPC to become operational by April 2019 at the latest, you will need to appoint three external members and two internal members (the Governor and Deputy Governor will be *ex-officio* members). We expect that the Board will need to begin its recruitment search for the external members, which will include public advertising, in September or October this year. This will enable interviews with a shortlist of candidates to take place in November, and appointments to be finalised in the new-year shortly after the amendment Bill is passed.
24. We expect the appointment process for the internal candidates will be shorter given that the candidates will be Bank staff. However, if you coordinate the announcement of the internal and external members of the committee, we recommend you also discuss the timing of the appointment process for internal members with the Board Chair.

Fiscal Implications

25. Cabinet has noted that introducing an MPC will have fiscal implications, which we currently estimate at between \$200,000 and \$400,000 per year. The exact fiscal implications are still unknown however, given that the remuneration for external members will be set by you through the Cabinet appointments process.
26. Officials will report to you on the recommended level of remuneration prior to the commencement of the Board recruitment process. At this stage we also intend to advise you on whether any changes to the Reserve Bank's funding agreement are necessary to meet the costs of the MPC. At this stage the Reserve Bank consider that an amendment to the funding agreement (which expires in 2020) will not be necessary, however this will depend on the total final costs.
27. If an increase in the funding agreement is required, there would be no charge against Budget allowances as the costs would be funded from the Bank's income (reducing the Bank's dividend) rather than through direct Crown funding. However, the cost of the committee will impact on the Crown's operating balance before gains and losses and net core Crown debt.

Consultation

28. This report has been developed in consultation with the Reserve Bank. The Reserve Bank Board have been consulted on this report and are comfortable with the recommendations.

Recommended Action

We recommend that you:

- a **note** that Finance Ministers have agreed that the provisions in the amended Reserve Bank of New Zealand Act 1989 relating to the process for appointing Monetary Policy Committee (MPC) members be non-prescriptive (T2018/998 refers).
- b **agree** to meet with the Board Chair to discuss your expectations for the MPC appointment process.

Agree/disagree.

- c **agree** to discuss with the Board Chair being engaged in appointments on the following basis:

Position	Your involvement
Governor and external members	<ul style="list-style-type: none"> The Board Chair consults you on the position specification and timeline before the recruitment process commences; The Board Chair consults you once the shortlist is developed; Where multiple suitable candidates exist, the Board explicitly recognises this when making a recommendation.
Deputy Governor	<ul style="list-style-type: none"> Your involvement would be the same as the process for the Governor and external members, but the Board would consult the Governor before engaging with you.
Internal members	<ul style="list-style-type: none"> Before a candidate is nominated, your involvement would be limited to consultation on the position description and the timeline.

Agree/disagree.

- d **agree** to send a letter of expectations to the Board, after your meeting with the Board Chair, that records your expectations for the appointment process

Agree/disagree.

- e **note** that introducing an MPC with external members will increase the Bank's operating expenses, and that officials will advise you on the fiscal implications at the same time as we advise you on the level of remuneration for the MPC members

- f **refer** this report to the Associate Ministers of Finance (Hon Parker, Hon Jones and Hon Shaw) for their information.

Refer/not referred.

Renee Philip
Manager, Macroeconomic and Fiscal Policy

Hon Grant Robertson
Minister of Finance

Annex One: The Crown Entity Appointment Process

The Crown entity appointment process provides an example of how the appointment process often works in the wider state sector. While we have not recommended this exact process for MPC appointments, we consider it is a useful comparator.

Members of statutory entities appointed under the Crown Entities Act are appointed by the responsible Minister (or the Governor-General on the recommendation of the responsible Minister in the case of an independent Crown entity).

The Crown Entities Act does not establish a formal nomination process as will apply for the MPC. However, the State Services Commission provides guidance on appointments, and supporting departments will typically follow a consistent process when nominating candidates to their Minister.

For Crown entity appointments made by the Minister of Finance, the Treasury will undertake the search process on the Minister's behalf. The typical process followed by the Treasury is as follows:

- The Treasury will report to the Minister seeking agreement to begin the recruitment process. This report will include a position specification, which the Minister may wish to comment on.
- Candidates in the Treasury's appointment database will be notified of the vacancy and nominations sought. At this stage the Minister may also encourage their caucus colleagues to nominate candidates for consideration, and recommendations may also be sought from other departments.
- The Treasury will recommend a short-list to the Minister. At this stage the Minister will be informed of all the candidates that applied for a position, as well as any candidates that the Treasury has independently identified as potential candidates.
- The Treasury will conduct interviews before making a recommendation to the Minister on the favoured candidate or candidates.
- Once the Minister has decided on a preferred candidate, the Treasury will prepare the necessary appointment paper for Cabinet's Appointment and Honours Committee, along with any other documents required for the appointment.

Annex Two: Appointment Processes for International Central Banks

Country	Nomination	Appointment	Other
Australia	Not specified in legislation	By the Treasurer	RBA Board includes the Secretary to the Treasury as an <i>ex officio</i> member
Canada	Not specified in legislation	By the Board, with the approval of Governor-General	The equivalent of the Treasury Secretary is an <i>ex-officio</i> member of the Board
European Central Bank	Executive Board recommended by the European Council after consultation with the European Parliament and the ECB's Governing Council	Executive Board appointed by the European Council	Monetary policy decisions are taken by the Governing Council of the ECB, which includes the Executive Board and the governors of each national central bank whose currency is the euro.
Iceland	Not specified in legislation	By the Minister of Finance	A three-member committee is required by law to evaluate the qualifications of the Governor and Deputy Governor before appointment.
Israel	Government recommends Governor Governor recommends Deputy Governor Candidate search committee recommends externals	President appoints Governor Government appoints Deputy Government appoints externals Governor appoints internals	The candidate search committee is established under the Bank of Israel Act and includes three members. The Chair must be qualified to be a judge, with the other two members appointed by the Government. The Appointment Review Committee must be consulted.
Japan	Not specified in legislation	By the Cabinet	Appointments are subject to the consent of the House of Representatives and the House of Councillors
Norway	Not specified in legislation	By the King in Council of State (Cabinet)	A review has recommended that one internal member be appointed by the Board on the recommendation of the Governor.
Sweden	Not specified in legislation	By the Governing Council of the Riksbank (Board)	The Riksbank's Governing Council is appointed by the Riksdag (Parliament)
United Kingdom	Not specified in legislation	Queen appoints Governor and Deputy Governors Chancellor appoints external members Governor appoints one internal member	Governor and Deputy Governor appointments will be made by the Queen on the recommendation of the Chancellor of the Exchequer. The Governor must consult the Chancellor before appointing an internal member. By convention, Bank of England staff are involved in the recruitment process.
United States	Not specified in legislation	The President appoints all members of the US Federal Reserve Board	Appointments by the President are subject to Senate confirmation. Regional representatives are chosen through a different mechanism.