The Treasury

Reserve Bank Act Review Phase 2 Submission Information Release

October 2019

This document has been proactively released by the Treasury on the Treasury website at

https://treasury.govt.nz/publications/information-release/reserve-bank-act-review-phase-2-proactive-release

Information Withheld

Some parts of this information release would not be appropriate to release and, if requested, would be withheld under the Official Information Act 1982 (the Act).

Where this is the case, the relevant sections of the Act that would apply have been identified.

Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Key to sections of the Act under which information has been withheld:

[1] 9(2)(a) - to protect the privacy of natural persons, including deceased people

Where information has been withheld, a numbered reference to the applicable section of the Act has been made, as listed above. For example, a [1] appearing where information has been withheld in a release document refers to section 9(2)(a).

Copyright and Licensing

Submission to consultation on Phase 2 of the Reserve Bank of New Zealand Act Review

David J Archer
24 September 2019

Submission provided in a personal capacity (and not as a representative of the Bank for International Settlements).

My background is as a central banker, and student of central banking. My current role, which I have occupied for 15 years, is researching the governance arrangements and institutional design features of central banks.

In what follows, I comment on two aspects addressed by Consultation Document 2A, namely the specification of objectives (Chapter 2) and aspects of Reserve Bank governance (Chapter 3); and two aspects addressed by Consultation Document 2B, namely the question of funding (Chapter 7) and governance of balance sheet resources (Chapter 4).

2A What other objectives should the Reserve Bank have?

An in-principle decision has been taken to include a high-level financial policy objective in the Act, along the lines of "Protect and enhance the stability of New Zealand's financial system". The consultation document asks whether this should be complemented by lower-tier objectives, and if so, what?

This submission argues strongly that additional, supplementary objectives are critically necessary.

Financial policy impacts many aspects of economic life of high political and social interest. Delegated powers for financial policy must, for the sake of proper accountability and hence legitimacy, be directed towards (and thus constrained by the need to take into account) all of the facets of high political and social concern. Without explicit Parliamentary directions that public officials must systematically address all aspects against which Parliament will later hold those officials to account, the delegation of state powers is dangerously incomplete.

Objectives for financial policy are inevitably multi-dimensional. Nor are the various dimensions merely variants of the same thing. From time to time they can be in significant tension. Former Chancellor George Osborne's 2011 comment that "Britain does not want the financial stability of a graveyard" illustrates the point. Financial systems appear to have become more crisis prone in recent decades, following substantial financial deregulation in the latter part of the C20th. That deregulation was purposeful, to allow financial systems better to facilitate economic activity and innovation. (Prior to deregulation, for many, financial systems indeed had some characteristics of the graveyard. For a privileged few – those with reputations, connections, collateral – financial systems were still active.) There is no guarantee that renewed regulation will be smarter than earlier forms. Especially when it seems likely that productivity growth has slowed, the potential chilling side effects of regulation are an important dimension to keep front and centre stage.

In this context, the consultation document is greatly mistaken in arguing that “financial stability” is a “clearer” concept than “soundness and efficiency”. The latter at least suggests the possible presence of the tradeoff that Osborne was highlighting; the former contains no hints of potential tensions.

More generally, any number of academics and practioners have acknowledged a substantial difference between the clarity of “price stability” and “financial stability” as objectives. To provide clarity, an objective should be specifiable along three dimensions: how *much*, of *what*, and at what *price*. For price stability it is possible to say what range of outcomes (how *much*) of what index of prices over what time horizon (*what*) is sought, and at what expense in terms of foregoing achievement of other objectives, eg stability of employment (the *price*). In sharp contrast, there are currently no accepted metrics of financial stability. The Reserve Bank is exploring expected shortfall types of metrics for calibrating capital buffers for microprudential purposes, but such measures are in their infancy in that context. They have not even reached the point of conception when it comes to the macroprudential dimension – the dynamics of interactions between components of the financial system and non-financial economic agents. Without a metric, it is not possible to specify how much of the intended outcome – whatever that is – is “right”, or “enough”. Which makes it particularly important to identify and limit the *price* that public officials are able to impose on society through the exercise of regulatory delegations.

What is the maximum price that Parliament thinks reasonable to pay to obtain this (as yet unspecifiable) outcome? Self-evidently, given the current state of knowledge, this question is impossible for Parliament to answer at the present time. The two options of first, abandoning the search for policy actions that can efficiently[1] reduce the risk of financial crisis, and second, reserving all such actions for elected officials, are flawed. The first because financial crises can be highly disruptive, and because progress is being made on efficient interventions that create systemic resilience[2]. Credible and effective resolution mechanisms may soon allow critical financial intermediation to be sustained while weak nodes fail. The second because elected officials are more likely than specially-appointed ones to underinvest in the design of efficient instruments. Investment in instrument design is a long horizon endeavor, and political budgetary processes have short horizons (dominated by annual appropriation contests for limited resources, and by electoral cycles). And successful incumbents have a vested interest in preserving the status quo – they usually gain, relative to potential rivals, from their

---

[1] In the sense, especially, of a low price in terms of side effects that impede the financial system’s ability to finance and support innovation.

[2] In the sense that the network that makes up the internet is resilient, not in the sense that a Maginot Line was resilient. The former can sustain the failure of nodes without detracting from system performance. The success of the latter is highly dependent on anticipating accurately what shocks will be forthcoming.

knowledge of and adaptation to existing policy instruments. Incumbents' ability to lobby elected officials to allow under-investment may be clearer in other jurisdictions than in New Zealand, but is unlikely to be an empty force.

All of which means that it is critical to identify the policy facets that Parliament will be concerned about when public officials use delegated regulatory powers, even if it is not possibly to assign weights to them ex ante. And to require that these facets be evaluated systematically, ahead of regulatory interventions. To make officials accountable against significant policy facets that are identified only ex post is not only unfair, but it is likely to encourage policy inaction when action is most needed.

Part 1 of Section 2 of the Consultation document lists many of the policy facets that Parliament will probably want to have been properly evaluated in ex ante regulatory cost-benefit analyses. Some are expressed positively, as outcomes to pursue; some negatively, as things to avoid. Both perspectives are welcome. Positively expressed elements may amplify the meaning of "financial stability" so that the *what* of the objective is better understood, helping make progress on the question of *how much*. Negatively expressed elements – things to avoid – are costs (*prices*) of regulatory intervention. Brief comments on the Consultation document's discussion are offered below:

A1. The concept of "resilience" used in the document mixes network concepts with those more applicable to concrete bunkers. Loading up a few nodes with extensive financial buffers, and constraining their risk taking freedom, arguably falls into the concrete bunker category. The network concept of resilience should be strongly preferred.

A2. Focusing on individual regulated entities perpetuates a fallacy of composition. A major lesson of the financial crisis was that the system can be at risk despite each component being sound.

A3. "Excessive variability" involves both problems discussed above. How much is excessive, and when is variability problematic? Prices and quantities *should* vary in response to changing circumstances, to help direct resources to their most efficient use, and most efficient time for use. Sometimes variation involves low levels of discrimination between the prices attached to different uses of resources, such as during manias and panics, and collective euphoria. But episodic low levels of price discrimination may also be a feature of Schumpeterian progress, or when technological progress occurs unevenly.

A4. Collective psychology is a powerful force in systems that depend on beliefs in order to determine prices, as with price setting for many financial instruments. And in the presence of leverage, which is a key design feature of fractional reserve systems (eg banking). Thus highly relevant, but as much symptom as cause.

A5. Continuity of critical functions is a key aspect that should be prominent in any definition of stability (in the sense of network resilience).

A6. Contagion creates externalities, and may warrant regulatory intervention because private actions will under-provision against wider risks. Contagion risk must be addressed in any regulatory design, but with a strong imperative to search for incentive-compatible regulatory forms (to reduce the price arising from moral hazard).

A7. Market discipline is substantially undervalued as a tool of financial regulation. Incentive incompatible regulation – the dominant form – has substantially neutered market discipline, allowing the creation of Too X To Fail (where X is big, interconnected, complex, politically sensitive, etc) entities. It would be wise to make incentive compatibility and market discipline leading components of the objective specification.

B1–5. are mostly secondary aspects of efficiency. The primary efficiency question concerns the ability of the financial system continuously to enable and facilitate the smart, innovative use of the nation's resources. The financial system's own efficiency is secondary to the dynamic efficiency of the wider economy that it serves.

C1–4. are all relevant considerations, but the list should also include respecting the property rights of investors in the provision of financial services. Arbitrary and unpredictable seizures of property are a concern when, for example, special resolution regimes intervene before failure is clear. The rules of the game need to be clear ex ante, and respected ex post. (Unfortunately, during a transition from TBTF regulatory systems to incentive compatible ones, the rules of the game will need to be changed.)

I have no comments to offer on D1–3 or E1–2.

Concerning F1 and F2, both are dangerously exposed to reinterpretation in favour of active government policies that aim to redirect resources towards politically favoured enterprises.[3] The valuable aspects of F would better and more safely be covered by ensuring that any B. statements about economic efficiency properly direct attention to finance's enabling and facilitating role with respect to economic activity and innovation.

2C Where in the legislative hierarchy should any additional objectives sit? And

2D How should the Reserve Bank's objectives be specified? Do you see a role for a 'financial policy remit'?

These two questions intersect, in that a policy remit is just one of many devices that can occupy a similar in the legislative hierarchy (between primary legislation and non-binding policy strategy statements). Some form of secondary law or non-statutory device that directs and constrains the actions of public officials seems

[3] No implication of political corruption is intended. Often, certain activities "sound good" as building blocks of a better economy, notwithstanding low barriers to the entry of private capital, the absence of which should ring alarm bells with respect to the likely return on risky investments.

necessary, in this policy domain. Inherently multi-faceted objectives – one of the defining characteristics of this policy domain – cannot reasonably be left for public officials to infer at the time, to evaluate and weigh up which facets to emphasise, and which not, when they are in tension. It is for Parliament to identify what *must* be factored into the policy equation. To allow officials to place near zero weights on some elements, effectively undermining the will of Parliament, would be wrong. (So mere "considerations" that the Bank "may" include in its evaluation of policy options, to the extent that it sees fit, are not sufficient, in my view.) It would also be unwise for Parliament to attempt to predefine how tradeoffs should be made across the full range of circumstances that will be encountered. Humankind does not possess sufficient knowledge to allow prespecifying the weights on the various matters of high political concern listed above. Especially given typically lengthy time lags before law can be revised. Moreover, the values placed on each aspect may evolve.

For all these reasons, secondary law – or other high-powered non-statutory device – should be used to bridge the gap, in an arrangement and using processes explicitly required by primary law. Many options are possible. To anchor the thinking, I direct attention to the approach taken in the UK Banking Act 2009. There the UK Parliament stated, in a five point list expressly without priority order, a range of considerations that must enter any decision to use the powers and authorities provided by the Act, and defined the process by which the *assessment method*[4] to be used by officials when evaluating these statutory considerations. An assessment method sets out the basis for making tradeoffs between statutorily required considerations. It can be updated as knowledge and circumstances evolve, with a degree of flexibility impossible with primary legislation.

The process of designing and modifying an assessment method can be made subject to a wide range of checks and balances. For example, design and modification might be for mandatory negotiation between relevant implementation and policy agencies and an administrative law authority whose task would be to ensure respect for primary law. Negotiating power might be distributed evenly by way of a triple veto requirement, thereby limiting the effect of any existing dominant power structure. Circuit breaker mechanisms can be built in for use when negotiated agreements are not possible – with mandatory disclosure of the basis for negotiating positions, such that weak arguments or improper considerations are exposed.

A formal policy remit that conforms to a statutory authority and limitations is a legitimate device. Relative to the type of mechanism just described, however, it has the weakness that elected officials are more likely – for reasons earlier stated – to underinvest in longer horizon policy design. The elected official facing the greatest conflict of incentives is the Minister of Finance. A negotiated policy strategy, with veto powers given to different negotiating groups made up of appointed officials who structurally represent different legitimate interests, would

---

[4] This is not a term used in the Banking Act, but it captures the essence of what the Act requires by way of a "Code of Practice".

be less conflicted. That the Treasury would be one of the negotiating parties, and that the Treasury would be acutely aware of the political sensitivity of possible strategies, provides an appropriate connection to politics within the checks and balances structure. To further reinforce political legitimacy, the circuit breaker mechanism could be designed to increase the role of elected officials in the resolution of disputes.

Additional comment relevant to Questions 2A, 2C and 2D.

The multidimensionality of financial stability objectives, and the attendant need for a flexible approach to defining tradeoffs, were concerns of the 2011 Ingves Report.[5] The following extract from Box 1 of that Report is highly relevant to the current New Zealand enquiry, and has much that would recommend it to the Consultation:

> "In the context of financial stability policy in general (rather than bank resolution in particular), a multidimensional list of objectives might include:
>
> - resilience, such that shocks to essential services do not become self-reinforcing;
> - protection for naïve creditors;
> - anticipation by informed investors of a risk of loss;
> - protection of the fiscal position;
> - property rights protection, conditional on avoidance of moral hazard;
> - dynamic and productive efficiency;
> - respect for the rights of citizens of other jurisdictions.
>
> As with the [2009 UK] Banking Act model, an interpretative strategy statement [setting out the *assessment method*, in the terminology used in the present submission] would be called for, in order to elaborate the meaning of each component and to enunciate their relative weights – given the state of knowledge as to how welfare is affected, given what is technically feasible, and given societal preferences."

3E, 3F, concerning the structure and functioning of the proposed Governance board

Many problems are created by the in-principle decision to combine in one board the roles of (1) financial policy decision-maker, (2) overseer of central bank operations and of the executive responsible for those operations, (3) strategy setter for the provision of financial services, and (4) balance sheet/financial risk supremo. These roles each call for different skills, engagement contracts, and lines

---

[5] Report of a Central Bank Governance Group Study Group chaired by Stefan Ingves, Governor of the Sveriges Riksbank, "Central bank governance and financial stability", May 2011, Bank for International Settlements.

of authority and responsibility, creating a puzzle that will be almost impossible to solve. The most obvious solution would involve separating out financial policy decision-making, embedding that in a separate body with clear statutory responsibilities, and staffing that body accordingly. Even that would not be enough to deal with all the potential tensions that may arise. And it would call for the in-principle decision to be amended. Should that not be feasible, important additional constraints on the role and powers of the Governance board need to be considered.

Two things create particular problems, both flowing from the point that the oversight role calls for a significant proportion of part time outsiders on the board.

Firstly, policy roles require greater time commitment and rarer skillsets than those needed for oversight. Financial policy is an especially complex area of public policy – much more so than monetary policy – that is not yet well understood even by those who specialise in the subject. The complexities are illustrated by the multi-dimensionality of a fully-specified objective, and the recognition that weighing up the trade-offs that result is an evolving and difficult task. Devoting enough high level resource to financial policy analysis and decision-making limits the room for those who could make a useful, independent contribution to monitoring. Conversely, making enough room for high quality monitoring – which, given the information imbalance between insiders and outsiders, means a clear majority of outsiders who are not also policy-makers – reduces the potential for effective groups making policy. The Governor becomes more dominant in policy-making as the number of high-level policy executives with statutory backing falls.

Secondly, most important non-monitoring roles of a Governance board have the potential to cut across, and conflict with, policy-making. Three can be highlighted.

- The first involves control over *access to the operating budget*. This issue is recognized in the Consultation document, and need not be expanded on.
- The second involves control over *access to financial resources*. Both financial crisis management and monetary policy may need to use the balance sheet and risk taking capacity (explicit *and* implicit) of the institution. When they do, the situation may be critical, and fraught with uncertainty. Putting control over a key financial resource in the hands of people whose day jobs create instincts that may be completely at odds with what is needed for policy[6] constitutes a major design flaw. (These issues are addressed in more detail the last section of this submission.)
- The third area of potential conflict concerns decision-making on *central bank facilities*. Again, major policy connections can be identified, even though they usually don't make their presence known. The liquidity insurance role of

---

[6] Massive amounts of balance sheet risk were taken on by central banks using quantitative easing. Likewise, in the context of systemic liquidity crises, the only effective policy response available may involve the central bank taking on huge financial risk. A central bank's duty is to the future well-being of citizens, not some narrow conception of shareholder value. It is the narrow conception that private business executives are trained to respond to.

central banks can be configured in many different ways, via different types of facilities made available to the financial system, with important implications for the dynamics of liquidity gluts and strains and the associated interest rates. Who in the financial system can access what type of facilities, with what accompanying obligations, has significant connections with the design of regulatory boundaries. Which entities can utilize central bank accounts for payments and settlements, and on what terms, may have big implications for crisis dynamics, as well as the competitive process that determines access to rent extraction possibilities.

- Consideration of central bank facilities are usually focuses on the central bank's dealings with a small number of designated financial institutional counterparties. That limitation is itself a choice, and one coming into increasing question. Digital forms of central bank currency (CBDC) – currently, the one central bank facility available to the wider public – are becoming viable. And options are being sought for injecting money directly into the hands of high propensity-to-consume individuals (not necessarily including the option of "helicopter money") in situations where the conventional monetary policy transmission mechanism is weak. These potential innovations could have far reaching consequences for monetary policy, financial stability and the structure of the financial system, yet responsibility for deciding whether to adopt them, and if so in what form, would in the first instance fall to the Governance board.
- In short, central bank "facilities" are just as much to do with policy as with business operations.

As noted, the Consultation document recognizes the existence of the first potential tension (operating budgets), and to some extent also the second (balance sheet and risk). But its answer – that some agreement will need to be reached among interested parties – is totally inadequate. Governance design should proceed on the basis that the relevant parties have interests that are, or could be, misaligned with the public's long term ones. Leaving important matters to be sorted out later, if and when people have time and awareness of the implications, is a recipe for nothing to be done until too late.

Instead, all such potential conflicts between responsible parties should be identified, to the extent possible, and made subject to a mandatory conflict resolution process. One such process could be to allow the Monetary Policy Committee to over-ride decisions of the Governance board that prevent implementation of the MPC's policy. But that fits poorly with the idea that the Governance board oversees the implementation of policy.[7] Moreover, it would be difficult to define when a conflict between the bodies has become serious enough to make using the conflict resolution mechanism legitimate. Another process

[7] The Reserve Bank of Australia has such a mechanism built into its legislation. Where there is a conflict between the policies of the Payments System Board and those of the main Bank Board, the Bank Board's views take precedence. As the Bank Board is not overseen by the Payments System Board, there is no accountability relationship to cut across.

would be to allow appeals to a higher decision authority that can act fast. In this case, the higher decision authority is likely to be a political one (to which appeals would not be made lightly, given the value likely placed on independence by the arguing parties). As appeals would likely involve quite high stakes, and concern issues not well addressed in primary law, political involvement would add to the legitimacy of dispute resolution.

Quite probably, a single conflict resolution process could cover most identified sources of tension, and be made available – perhaps on the petition of a minimum proportion of the affected actors – in situations that have not been identified. As (almost) always, mandatory disclosure – potentially with a lag in strictly limited circumstances – of the use of a conflict resolution procedure, and the reasoning provided by all parties for their positions and final decisions, would help keep the parties honest and ultimately aligned with what the law requires.

Some additional comments, not directly sought by the questions for consultation:

1. For effective accountability – of Governance board members and of executives through Governance board oversight – it is vital that a Parliamentary committee[8] examines that board. The board should thus have obligation to account meaningfully in writing to Parliament, with (hopefully) Parliamentary procedure adjusting to regularize face-to-face examinations of the board. Notwithstanding any preference for collegial decision-making, Parliament should not be constrained to examine only the chair. Such examinations should also seek to uncover the nature of the board's evaluation of executive performance.

2. On the question of grounds for dismissal of board members and executives, the Consultation document notes a range of considerations and options. It is rare in central banking for key officials to be dismissable over their performance on policy, or things relating to policy (which can even include budgetary matters, given concern about finances being used as a back door to influence policy). It clearly weakens accountability when officials have blanket protection from dismissal for poor performance on the most important matters for which they are appointed. Moreover, such blanket protection appears to be unnecessary for achieving a suitable degree of operational independence. New Zealand is joined by Chile, Serbia and Thailand in allowing dismissal for policy mistakes, and no one has asserted that the respective central banks unusually beholden to the political authority holding dismissal power. The key to allowing dismissal while preventing misuse of the threat is to lay out the purpose of policy clearly – easier for monetary than financial policy, to be sure – and require that dismissal for policy reasons must first establish a chain of behavior that is (a) clearly inconsistent with stated policy purposes and (b) clearly responsible for harm being done. In this way, an

[8] In Finland, the whole of Parliament receives a report from the Bank of Finland's Parliamentary Supervisory Council, annually, in open session.

attempt to dismiss because a Minister wanted policy to pursue a different purpose, or because a Minister wanted a different method or strategy used in pursuit of the stated purpose, would not be feasible. In this context, restricting dismissal to "for just cause" does not clarify what is covered. In the United States, independent agency heads are usually protected by a requirement that dismissal must be "for cause", but courts must determine how far "cause" may reach, and so far they have determined that "cause" does not include policy. Greater clarity and better accountability are possible.

3. The involvement of Parliament itself in appointments, usually through a committee but sometimes involving the whole of Parliament, has wider precedent than noted in the Consultation document. Parliaments appoint the governors of the central banks of Bulgaria, Croatia, Latvia, Lithuania, Poland, North Macedonia, Romania, Russia, Serbia, and Slovenia, in processes that often involves voting by the legislature as a whole. Parliaments also formally ratify governors' appointments in Argentina, Brazil, Chile, China, Indonesia, Japan, Mexico, Peru, Slovakia and the United States. Consultation with Parliament is mandatory in the European Union (with respect to appointment of the ECB president), Korea, Hungary, Portugal, and Spain. In Romania, different Parliamentary actors nominate candidates and determine the appointment. In Croatia, three different Parliamentary actors are involved, nominating, being consulted, and making the appointment. Although Parliamentary and public sector traditions differ, the question of the feasibility of Parliamentary involvement seems settled.

   An attachment deals with appointments in more detail.

7. How should the Reserve Bank be funded and resourced?

Two types of financial resource are covered by question: the flow of money available to fund operating expenses, and the stock of financial resource needed to provide a financial transactional capacity in a wide range of circumstances. They are not independent – a stock of financial resource can also generate a flow of income, or be progressively run down to fund spending – but for the sake of exposition, they will be treated in turn.

Funding of expenditure

Operational independence is commonly held to require three components:

1. access to necessary powers/instruments that can used free of interference – other than the need to play by the rules (including the rule requiring that powers be deployed only in pursuit of stated objectives);
2. personal independence, meaning an absence of fear of dismissal or reprisals for using power/instruments as the law directs; and
3. financial independence, meaning having the resources needed to do the job effectively, with no strings attached – other than the need to account for use of the money made available, in terms of the stated objectives.

This linking of operational and financial independence typically leads to central bank being granted the authority to use seigniorage to fund expenditures, and pass some portion of the residual over to the state (according to the rules of a distribution scheme). In a few cases (less than ¼ of central banks – see Fig. 38 of Issues in the Governance of Central Banks (2009), p130), the expenditure budget is subject to external approval or veto; in another ¼ of cases the expenditure budget must be disclosed in advance; but in nearly half of central banks, there is no *external* control over the amount of expenditure drawn from the seigniorage revenue stream. However, where there is a supervisory board (around ⅔ of central bank), it usually (¾ of cases) must approve, or can veto, the expenditure budget. How effectively supervisory boards constrain central bank use of seigniorage is an open question. In the end, central banks can usually pay better salaries and have more money for research than public sector counterpart agencies that are funded out of annual appropriations of tax revenue (in contest with other agencies and in the face of a desire to keep taxes and debt under control).

The option of putting expenditure budgets under closer external influence or control – even short of making them subject to annual appropriation – runs into concerns about financial independence and hence operational independence. Yet, as the Consultation document rightly notes, the Bank earns and spends Crown revenue, so spending responsibly and delivering value for money is a vital public concern. The five year funding agreement approach was an attempt to balance these competing considerations. The construct was, and remains, an eminently sensible compromise. In my 15 years of examining institutional arrangements of central banks, across the range of central banks that belong to the Bank for International Settlements, I have not seen a better arrangement.

The Consultation document notes some concerns about the effectiveness of the funding agreement, not so much in constraining waste or inefficiencies in allocation, but rather in providing sufficient money to cover expanded responsibilities. Yet the discussion of the possible constraints on expanding the funding base does not identify a structural problem. Five yearly renegotiations provide scope to expand the amount of seigniorage made available; the ability to draw on reserves means that there is no obligation to wait until the next renegotiation; and in any case a concern about excessive use of reserves, with no guarantee of success at the point of renegotiation, can be handled by a request for a mid-term renegotiation. Bank officials may have been unconvinced that expanded responsibilities were warranted. They may have under-estimated the scale of resources required. They may have been hesitant to run down reserves, out of fear of being left stranded at the next scheduled renegotiation point. They may have been hesitant to ask for a mid-term renegotiation, out of fear of being seen incapable to make ends meet through efficiencies, or out of fear of strings being attached to policy (loss of independence). Ministers may have signaled a reluctance to engage, or to treat bids for additional resources more favourably than bids made by other public agencies. Treasury officials may have signaled their sense that the Bank is richly funded, and ought to be able to fund more work on financial stability policies with the existing resource base.

All these possibilities concern how the funding agreement mechanism is used in practice, rather than its inherent design. Most if not all of these behavioural constraints would apply equally to other funding mechanisms. Structural reforms to the funding mechanism do not seem to be the answer. In particular, there is nothing in the disclosed history that points to value in greater Ministerial control over the budget. Ministers face many competing demands on the limited financial resources available to them, and they are highly unlikely to be a promoter of budgetary expansionism – the single concrete problem with current arrangements that the Consultation document points to – in areas where the additional spend is mostly invisible to voters. In addition, considering the use of fees and charges (for services, and where indirect benefits accrue to a few), Ministers are more exposed to lobbying than are unelected public officials debating how to achieve best value for taxpayer money.[9]

Having said that, financial accountability appears to have been comparatively lightweight. The Board of Directors does not appear to have put the Bank under as close scrutiny as it could have, and the scrutiny that has taken place is mostly invisible to the public (the Board's section of the Annual Report is insufficient in length and depth to give a clear sense of their assessment of strengths and weaknesses of financial processes, and the use made of those processes). The absence of close scrutiny will likely become a bigger structural problem should the current oversight Board be replaced by a Governance Board, given a notably higher proportion of the board that is conflicted by having executive responsibilities for spending functions. In this context, some of the ideas canvassed in the Consultation document – eg adding a legislative requirement for disclosure in forms that enable meaningful scrutiny of benefits relative to costs; allowing the Controller and Auditor-General to conduct performance audits; establishing Ministerial expectations for reporting – are worth considering.

Balance sheet resources

Chapter 4 addresses issues relating to the balance sheet, capital and dividend arrangements. The aim is to identify governance arrangements that allow a proper balancing of competing considerations. The main competing considerations are: on the one hand, Bank's (and MPC's) ability to implement policies delegated to them, in unusual and emergency circumstances; and, on the other hand, constraints on the Bank's (and MPC's) ability to create debts for the taxpayer and on the Treasury's freedom to determine the Crown's debt strategy. These are the right issues. Unfortunately the chapter does not fully get to grips with them.

A central bank's balance sheet is a key instrument for the implementation of a range of policies. In normal times (sufficiently away from the Effective Lower Bound (ELB) for interest rates that QE is not a relevant prospect), the balance sheet instrument is latent, but still powerful. The central bank's willingness to

9 Fees and charges are, in general, appropriate devices. Not so much for their fund raising benefits, but rather for reducing inadvertent transfers from taxpayers to entities that benefit disproportionately from the services provided and policies conducted by a public agency.

trade essentially unlimited amounts at posted interest rates determines the rates that market participants are willing to bid and offer because the central bank has the balance sheet to make good on its stated willingness. That it does not need to trade in any volume in order to influence market prices reflects the power of the balance sheet.

However, as the chapter rightly notes, there is a range of circumstances where latent power does not suffice, and changes in the balance sheet's size and composition are necessary to achieve policy objectives. Such changes in size and composition are characterized by changes in the financial riskiness of the balance sheet. Consider the following examples:

1. QE at or near the ELB can be characterized as a carry trade (Goodfriend, 2014, "Monetary policy as a carry trade", lays out the reasoning). QE involves balance sheet expansion, potentially in very large magnitude – doubling through quadrupling of advanced economy balance sheets have been seen during the last decade – with purchases of assets (the entry into the carry trade) focused on long duration instruments close to the peak of their price cycle (ie at very low yields). The proximate policy objective is to drive those prices even higher (ie force down long government debt yields) while, simultaneously, allowing private financial institutions to rid themselves of duration risk (by transferring that risk to the central bank).
   A carry trade motivated by financial returns would have the investor exit the trade while the market price of the asset remained above the purchase price, having in the meantime earned extra returns from the higher yield on the purchased asset than on the cash given up. A policy carry trade, in sharp contrast, is motivated by a desire to stimulate nominal economic activity such that market interest rates return to normal – well away from the ELB. Reaching the policy objective involves interest rates rising, at both the short and long ends of the curve, above the point at which the central bank started to enter the QE carry trade. That is, at prices of the asset purchased below those at which they were purchased. Attempting to exit the carry trade as early as a financially-motivated investor would may indeed impede reaching the policy objectives. The Federal Reserve has, for example, found it necessary to sequence balance sheet normalization after interest rate normalization in order to prevent market disruption.
   In this light, the effect of QE on the central bank's financial risk may be quite dramatic. It deliberately acquires duration risk while effectively promising, for good policy reasons, not to hedge or downscale that risk until prices have returned to being favourable. All potentially in very large quantities.
2. A central bank's role as "the lender of last resort" is not as unidimensional as that label implies.
   To act as a lender of last resort (LOLR) with respect to an event affecting *a single* financial institution raises significant questions relating to credit risk – how assured is the central bank that the counterparty is solvent, and will remain so for the foreseeable future? Such questions themselves raise

significant policy questions – who should make decisions to put Crown finances at risk of a credit loss, when the benefits would accrue disproportionately to a single commercial entity. (As a subsidiary matter, such circumstances do not *require* the involvement of the central bank, as an expansion of central bank money is not needed. Indeed, any injection of central bank money arising from a central bank loan or, say, a Treasury decision to draw on its account at the central bank in order to make a loan to the financial institution facing funding difficulties, would be sterilized in the normal course of open market operations. The issue is solely one of the distribution of the amount of central bank money that the central bank judges is consistent with the interest rates that it is targeting.)

In sharp conceptual contrast, to act as LOLR in the context of a financial *system wide* liquidity crisis both necessarily involves the central bank and is inextricably connected to the pursuit of monetary policy objectives. Necessarily involves the central bank, because the sharp rise in demand for central bank money that characterizes a systemic liquidity crisis requires an expansion in central bank money, something that the central bank alone can determine. Inextricably connected to monetary policy, because without accommodating the increased demand for central bank money, financial conditions would tighten inconsistently with what the central bank believes is needed to meet hit policy targets. LOLR and monetary policy are Siamese twins in the context of a systemic liquidity crisis.

One reason for highlighting the distinction between idiosyncratic and systemic LOLR is that in the former context, the costs of the Crown refusing to take on credit risk might be sufficiently contained to make that refusal to lend feasible. A judgement call on the probabilistic tradeoffs would be needed, and it is an open question as to who is best placed to make that call. But, in the latter context, the potential costs – including multiple institutional failures, on top of putting monetary policy targets at risk – are such as to remove the option of not acting, and acting fast. And credit risk is unavoidable in the face of a systemic liquidity crisis. Without the Bank's intervention large sections of the financial system would be at risk of failure. Even with the intervention, fragile parts could fail, and foreknowledge of which parts is beyond anyone's capacity. As solving the liquidity crisis would typically involve not making credit risk distinctions between counterparties – with multiple institutions facing a liquidity crunch, any attempt to fine tune collateral rules on an individual counterparty basis could easily go wrong, and the imperative is to alleviate panic – the Bank would be obliged to offer normal-times terms to all counterparties. That is, lending would occur at pre-crisis rates, with pre-crisis haircuts on eligible collateral, and with haircuts on expanded collateral types reflecting calm conditions. In short, the Bank would be obliged to operate essentially blind to credit risk.

The upshot is that, given a systemic liquidity crisis, the Bank's ability to reach its monetary objectives, let alone its financial stability objectives, would be rendered null should the Bank be prevented from taking on the concomitant credit risk.

3. Foreign exchange market stabilization. In extreme circumstances, the amount of capital that market makers are willing to commit may not increase commensurate with the ongoing expansion of currency and counterparty risk. Market makers' foreign currency inventory would rise as liquidity thinned out, and the risks of that inventory would become difficult to hedge. As some market makers pulled back, the problems for the remaining ones compound. As would the problems confronted by their corporate clients confronted with legal obligations to settle foreign currency debts, or commit to long term contracts sensitive to the exchange rate.
   In such circumstances, the central bank may need to use its own foreign currency inventory, and a willing to take risk, and act as market maker of last resort. This is one of the original reasons for holding an FX reserve in the first place (Archer and Halliday, 1998, "The rational for holding foreign currency reserves").

The foregoing discussion is an extension of the Consultation document's brief coverage of the connections between central bank policy and the balance sheet, with a focus on crisis circumstances. The points to be registered are first, that central bank absorption of financial risk may be an inescapable feature of the execution of central bank policy in such circumstances, and second, that the amount of financial risk that needs to be taken on may be an order of magnitude greater than in normal times. The raises serious questions about the Chapter's underlying presumptions that crisis management policies should be constrained by the Bank's conventionally assessed risk capacity, and that current dividend (and recapitalization) policies need not be revisited.

Consider the proposal that MPC be advised by the Governance Committee on the Bank's risk taking capacity for QE. Views on that risk taking capacity can vary enormously, depending on whether one takes an economic view of a central bank's financial strength, or a current accounting view of capital. (The latter is implied by references in the Chapter to the Governance Committee having an "implicit obligation to safeguard the Reserve Bank's capital" and to the Minister having "ultimate responsibility for setting the dividend … [which] … affects the Reserve Bank's capital base and therefore its capacity to take financial risks.") As Archer and Moser-Boehm report (in "Central bank finances", 2013, Table 1), some calculations made in 2012 show that the Eurosystem, the Bank of England, and the Federal Reserve had, respectively, comprehensive net worth at price stability (CNW@ps, an economic measure of risk taking capacity) 12, 49, and 31 times larger than their accounting-based shareholder equity at the end of 2010. An MPC, likely dominated by economists and concerned about the long run effectiveness of monetary policy, would probably favour the economic view of risk taking capacity. A Governance Committee could potentially be dominated by people well versed in current accounting representations of the world – given the Committee's primary responsibilities for bank supervision and for the Bank's financial reporting – and could thus favour the current accounting view.

To further drive home the practical implications of these differences in conceptual approach, were the Reserve Bank to use a CNW@ps view of financial risk-taking capacity, given the presence of crisis conditions of the type discussed above, it could take actions in pursuit of its statutory objectives that result in significant financial losses. Such losses could lead to current accounting net worth being reported as deeply negative, while CNW@ps remained assuredly positive. From one perspective, the Bank would have acted properly, with no negative consequences for its future capacity to implement policy (since, for a central bank, negative accounting capital does not mean failure[10]). From the other perspective, the Bank may have overstepped the boundaries of its mandate, and raised questions about its ongoing ability to implement policy.

These "boundary issues" are of such a potential magnitude that they should not be left for sorting out when the need arises. Because major financial risks for the Crown may be involved, they cannot be left to central bank discretion. Because constraints on policy capacity might inadvertently prevent rapid deployment of urgently needed public policy interventions, these issues would not sensibly be left to the fiscal authorities to evaluate de novo, in the heat of crisis.

Prepositioning sufficient (accounting) financial capacity at the Reserve Bank, by way of an injection of capital, is not a robust option, as illustrated by recent events concerning the Reserve Bank of India, and ongoing disputes concerning the Sveriges Riksbank, where apparently large pots of unused (and seemingly) unneeded state money have resulted in capital raids (or threatened ones). Viable options include: risk sharing rules whereby dividends are conditioned on accounting capital targets that are in turn conditioned on an acceptance that accounting capital may be in negative territory for extended periods; pre-positioned financial risk transfer mechanisms whereby the Crown directly accepts the financial consequences of central bank emergency policy actions, subject to decision-making protocols that give the fiscal authorities greater involvement than normal, but that make refusals to financially back the central bank subject to mandatory immediate disclosure of the competing arguments of the contending parties[11]; and recapitalization mechanisms that are consistent with the foregoing. These options require statutory backing, at least in terms of the principles if not the full details. A statutory requirement for new dividend policies, financial risk

---

[10] As Archer and Moser-Boehm (2013) report, there are several modern cases of successful central banks achieving their policy objectives while maintaining deeply negative accounting capital.

[11] The Memorandum of Understanding on financial crisis management between the Treasury and the Bank of England, required by law, provides examples of aspects of such an arrangement, notably with respect to establishing decision responsibilities and an on-the-shelf indemnity arrangement. It does not, however, go as far as it could in requiring the basis for disagreements between the Bank and Treasury to be immediately disclosed to Parliament.

taking rules and risk transfer mechanisms to be put in place, in accordance with stated principles, is highly desirable.

Attachment: Appointments of central bank governors

Introduction

As Chief Policy Makers (and usually chairs of policy committees) and as Chief Executive Officers, central bank governors are crucial actors. Selecting suitable people is thus very important. Especially in central banks placed at arm's length from political direction and sanction, the selection process must aim to deal with several problems:

- Mandates are never fully specified. Governors may need to make important judgements that have significant welfare consequences, often while maintaining the distance from politics. Candidates must therefore have both an aptitude for addressing economic policy under uncertainty and a clear recognition of the proprieties involved in making decisions that carry the weight of the state and impact the lives of its citizens.
- In most cases, to preserve distance from politics, governors are protected from dismissal throughout their often lengthy terms. This usually means that mistakes in selection cannot be undone, for several years. The selection process thus needs to be especially careful.
- To maintain independence from politics, governors should not be beholden to the government of the day. Likewise in relation to any private interest group. At the same time, the legitimacy of their appointment may depend on the sanction of duly elected political representatives.
- In many jurisdictions, the number of suitable candidates is rather limited. This may mean needing to open the process to non-citizens (if the law allows), and foregoing otherwise sensible devices such as open application and selection that might put off good candidates.

Who selects?

The tables annexed provide details on the law's specification of the selection process for the governors of 59 BIS central banks. The tables sort the array of actors into 7 categories. Broadly speaking (and with exceptions) the ordering of these categories is intended to reflect the likely ability and motivation (at least in principle) of that type of actor to represent society's long term interests, rather than narrower electoral ones. The actors least likely (again, in principle) to be swayed by electoral advantage – and correspondingly, more able to reflect society's longer term interests (at least as they understand that; itself an open question) – are listed first.

1. A board of the central bank. Usually a supervisory board (comprised mostly of part-time, non-executive appointed members or part-time ex officio members), but in a couple of cases a senior policy or executive board.

   In principle, involving a central bank board helps bring a non-partisan, apolitical approach to the assessment of the technical, experiential and personal suitability of candidates, aided by inside knowledge of the requirements of the task.

   In practice, though, most supervisory boards have little or no involvement in central bank policy-making or its delivery of key functions, limiting the depth of inside knowledge. Moreover, the process for appointing supervisory board members is not usually designed around the task of being a selection panel for the bank's key official, notwithstanding this probably being the supervisory board's most important task. In some countries, appointments to supervisory boards are quite partisan, undermining the ability of such a board to play an apolitical role, although behaviour once appointed and exposed to a long-range task performed jointly with others of different political persuasion might not always conform to the appointer's intentions. More generally, inferring society's longer-term interests that are relevant to the tasks of governors is not easy, even given some – often vague – guidance from statutory statements of policy objectives. One danger is that non-specialists approach their engagement in a selection process from an idiosyncratic viewpoint of how the central bank best serves society, paying little attention to such statutory statements (where they exist).

2. An external commission. In some countries commissions are used for selecting senior public officials. In Singapore, the Public Service Commission has the selection of top public officials as one of its main tasks. In Iceland and Thailand, special commissions are assembled, under rules set out in law, when a new governor needs to be appointed. These commissions are staffed by people with long experience of public service roles, but without conflicts. In Croatia, a special-purpose committee of parliament is used in the evaluation of candidates for top public sector roles. In Israel, special committees, usually headed by retired judges, are often assembled to assist in scrutinising the suitability of candidates.

   The degree to which such a commission can play an apolitical role focussed on longer term societal interests depends on, inter alia, whether the commission is assembled for the sole purpose of appointing a governor (in which case the commissioners may pay more attention to expected policy outcomes than to proven policy and management capability); and whether the process of selecting commissioners guards against partisanship.

3. Parliament, or the committee thereof that normally oversees economic policy agencies.

   A central bank's policy powers and tasks are delegated to it by the legislature; legislatures also allow central banks to use income generated from their legally-backed monopoly over fiat currency issuance. A high degree of involvement of parliament in the appointments of those who will wield state powers therefore adds democratic legitimacy – especially necessary where those powers include coercive regulation and alter the distribution of burdens and risks across and within generations.

   Compared with assigning the appointment power – or aspects thereof – to the government of the day, the involvement of the legislature as a whole may somewhat reduce the risk of a partisan approach to the selection of governors. This may be more so the case when the governor's term is long, increasing the likelihood that they will serve during the terms of governments of more than one political complexion. However, parliament and its committees are often numerically dominated by the governing party, sometimes to an extent that obviates the need for cross-party coalition building and maintenance.

4. The Head of State.

   In many countries, the Head of State (HoS) plays a key role in appointments. Depending on the jurisdiction, the HoS may be more or less an actively partisan political figure. In the Czech Republic and Singapore (for example) the HoS is a political figure, associated with a political faction. In Germany and Italy (for example) by tradition they operate above politics. In Belgium, Norway and the United Kingdom (for example), the HoS is a monarch, wielding a distinctly non-partisan but mostly ceremonial power. In these latter cases, the actual influence usually rests with the government of the day which advises the monarch who is in turn expected to act semi-automatically on that advice.

The following three types of actor on this list are clearly political ones, each being a component of the government of the day. Each are likely to be more strongly attuned to electoral advantage than any of the preceding four types of actors. In what follows, we use the collective noun "conflicted actors" to refer to these three types (which is not intended to convey that other actors do not also face conflicts of varying types, merely that partisan political drivers are especially strong for this group).

5. The government, or cabinet.

   Being (notionally, at least) considered by a group rather than an individual, a decision of the government, or specifically of the cabinet, may reflect a range of perspectives including some that go beyond electoral advantage.

6. The Prime Minister.

   With a wider scan, the Prime Minister may consider a wider range of factors in the decision than would the Minister of Finance. Still, the Prime Minister is also often the party boss, and most responsible for getting the party re-elected.

7. The Minister of Finance.

   Although not party boss, and although perhaps better placed than the Prime Minister to understand prerequisites for good economic policy-making, the Minister of Finance is the actor from whom decision authority was taken away in the process of delegating that authority to the central bank. They may therefore have the most powerful drive to reassert authority over central bank functions indirectly, through appointing like-minded or compliant governors.

Single or multiple actors in appointments?

The foregoing discussion of types of actors highlighted a range of factors that might distort or bias decision-making on appointments away from society's long term interests. For the conflicted actors, the potential biases are the same as those that led to the decision to delegate important state powers to the central bank. Yet the involvement of such conflicted actors in appointments may be needed for political legitimacy.[12]

One approach would be to give conflicted actors clear statutory objectives and boundaries for which they are genuinely accountable (and feel that way). Clear objectives and proper accountability might help constrain the risk of bad outcomes while maintaining political legitimacy. But one may be sceptical on both counts: objectives are often not clear; and accountability is often weak, partly because of difficulties in cross-checking the consistency of resulting appointments with criteria that optimistically stress apolitical, long-term interests.

A second approach would be for parliament as a whole to make appointments, constructing parliamentary processes to mute the influence of partisanship when processing these appointments, achieving alignment with society's long-term interest while maintaining political legitimacy. Parliaments indeed are often involved, but muting partisanship is far easier said than done.

A third alternative is to require conflicted actors to obtain the agreement of others who are more likely to be looking after society's long term interests. Multiple veto arrangements, which have this structure, are in fact the majority arrangement for appointments of governors.

Cases involving one dominant actor

As the Annex tables show, in 40% of the country cases a single actor is legally responsible for choosing and appointing governors. In about 1/3rd of those cases *consultation* with another

[12] Whether the active involvement of conflicted actors is in fact needed to assure legitimacy is likely to be a jurisdiction-specific matter. In some cases a proper delegation of appointment powers by the legislature to other actors may be regarded as fully legitimate. The more so that the other actors are clearly apolitical, as well as appropriately qualified to know what characteristics would make for a good governor. Appointments of judges by colleges of judges seems to be an acceptable practice in many countries.

actor is required, though as another 1/3rd involve appointments made by the HoS, consultation with other government actors can be presumed.

More specifically, in 17 laws appointments may legally involve just one actor. In 8 of those it is the HoS; in 5 others appointments are made by the current government or Minister of Finance; while 1 is made by parliament as a whole. In 3 cases (Bosnia-Herzegovina, Colombia, Sweden) the top board of the central bank is the single appointer. Although this suggests an unusual degree of distance from electoral sanction for such an important public policy appointment, the impression may be misleading: in the latter two cases, the boards have politicians as members.

Where the law requires that the single appointer *consults* another party – 7 cases – in 3 (Finland, South Africa, Switzerland) the other party is the Bank's board, and in 2 (Iceland and Singapore) an external commission. These consultation requirements offer a route for wider societal or management and policy capability considerations to be injected into the discussion, although without veto force. The strength of the consulted party's voice is perhaps increased in 5 of these 7 cases by virtue of the law giving that party the right and obligation to provide a *recommendation* or *recommendations*; in the other 2 cases the law merely requires consultation (without any apparent obligation to take the consultation into account).

Cases involving more than one veto actor

In the other 60% of cases surveyed, more than one actor has a determinative say in the decision. *Double veto* arrangements are the majority (32 cases), with 10 of those also requiring consultations with third parties. *Triple veto* arrangements are in place in 3 cases, given three actors a determinative role.

A determinative role can come in three ways. One party may have the right to nominate a candidate for appointment, with the appointer having a yes/no choice (but not the ability to appoint a different person). The right to say yes (and formally make the appointment) or say no confers a determinative say. And the third mechanism involves another party confirming the appointment before it can take effect. Confirmation powers also take the form of a yes/no choice, but they do not confer an appointment power.

Of the 32 double veto arrangements, fully 25 involve the HoS as one of the veto actors. Of that 25, the other party is the legislature (or responsible standing committee thereof) in about half of the cases, and a government actor (government, cabinet, prime minister, minister of finance) in the other half. In just one case the HoS appoints someone nominated by the central bank board. Where the dual veto pair involves the HoS and legislature, it is just about as common for the HoS to appoint subject to parliamentary conformation as it is for the HoS to nominate for parliamentary appointment.

Power balance among veto actors: dominations and standoffs

Possessing a determinative say is one thing; using it may be another. Where one of them wields greater power (through channels outside of the appointment process), the two (or three) appointing parties might not act independently. For example, in one (undisclosed) case of a central bank board having the right to nominate a new governor, the appointing Minister of Finance exerted pressure to ensure that an "acceptable" name would be offered. In Argentina, and more recently in the United States (for appointments of other officials) appointments have been made by the HoS but not confirmed by the legislature, creating a standoff. Standoffs have also been experienced in central bank appointments in Israel, where two committees – each with a determinative role – have fought over the scope of their respective responsibilities. Another type of standoff would be repeated rejections of nominated candidates, until an "acceptable" name appears.

Guarding against the former type of problem (pressure being applied by one of the veto players on the other(s)) may be possible where external commissions are one of the veto actors and the appointment of commissioners is made by people not involved in central bank appointments. It may be more difficult where a central bank board is one of the veto players, as central bank boards are usually appointed by the same (political) actors that appoint the governor. This is most relevant when the government making board appointments can expect a long term in office.

Guarding against the latter type of problem (standoffs) requires some kind of circuit breaker mechanism to be built into the law. An example is found in the Bank Indonesia law. Should the legislature not approve HoS's nominees twice in a row, an alternative procedure is invoked with the objective of having a legally-appointed governor in place. In Argentina, appointed but unconfirmed governors appear to be able to serve while awaiting confirmation (though the legal status of decisions they make while serving may be ambiguous and subject to court challenge).

Other considerations

The surprising absence of commissions

External commissions (whether special purpose, or of the standing variety set up to make top public sector appointments) do not in practice have determinative roles. There are three cases (Iceland, Singapore, Thailand) where commissions must be consulted, making a recommendation (rather than nomination; see next section) in each case.

This relative absence of commissions as a determinative participant in governors' appointments seems odd. A commission structure in principle allows decisions to be made by people of standing who are independent of politics and of the central bank, but who have the capability to draw on experts for advice should the commissioners themselves not possess the necessary specific knowledge of job requirements (and be aware of that fact).[13] A standing commission that also makes other senior public service appointments would develop expertise in assessing candidates for public sector roles that have significant policy components. In addition a standing commission is likely to be comprised of commissioners appointed at different times, by different governments, providing a higher chance of political neutrality.

Recommendation vs. Nomination

We have drawn a distinction between recommendations and nominations. We use the former term for lists of names presented to the appointing actor, and for cases where the appointer is not required to choose only from the name(s) provided. Nominations, in contrast, are cases where a single name is provided, for an up/down decision. In this terminology, recommendations do not confer veto status, whereas nominations do.

There are, however, boundary cases. For example, in Thailand, a commission (or "selective committee" in the semi-official English translation of the law) is required to provide "no less than two" names to the minister of finance, for the minister to carry to cabinet for decision on who to present to the King for appointment. It appears that the minister is obliged to carry those names to cabinet, perhaps narrowing the list but not expanding it. This provides a semi-veto role for the commission, allowing it to filter out unsuitable candidates, while

---

[13] In Thailand's case, the law specifies that commissioners be drawn those who have previously occupied one of several senior public sector roles: the Secretary of the Ministry of Finance, the Secretary of the Ministry of Commerce, the Secretary of the Ministry of Industry, the Director of the Bureau of Budget, the Secretary of the Council of State, the Secretary of the Office of the National Economic and Social Development, the Director of the Fiscal Policy Office, the Governor of the Bank of Thailand or the Secretary of the Securities and Exchange Commission. They may not be political officials or have other conflicts at the time of the appointment or during their term as commissioner.

leaving more choice for elected representatives than would be the case with a pure nomination by the commission.[14]

More generally, the influence of both single-name nominations and short lists of names provided as recommendations will likely depend on their visibility. In the absence of visibility, an appointer could repeatedly reject nominations until a politically acceptable candidate turns up, or appoint someone who had not been recommended, with no risk to their reputation. Visibility at the sharp end of an appointment process might put off some potential candidates. On the other hand, the role for which they are applying is one fully in the public eye; mandatory visibility may act as a useful screening device.

Parliamentary involvement

Concerns are sometimes raised about the ability of parliaments to play useful roles in candidate selection, and/or the opportunity cost of that use of the legislature's time. Such concerns are more prevalent where parliamentary committees are weak or ineffective scrutineers of public administration, or are overly staffed with junior politicians seeking favour from party bosses or activists. But there are good counter-examples. In the United States, Senate committees have long played a useful role in checks and balances around Presidential appointments. In the United Kingdom, the Treasury committee is starting to be an effective screening device for candidates for high central bank office, though it does not as yet have a statutory veto role.[15]

Such concerns may also reflect a lack of imagination about parliamentary process. Consider the case of Bulgaria, where parliament proposes, evaluates and appoints the governor. The process is very elaborate, probably exceeding what would be thought reasonable in other places, but it illustrates what is possible, with imagination. Here is a full description of the process, from knowledgeable Bulgarian sources:

> According to the provisions of the Bulgarian legislation the Governor of the Bulgarian National Bank is elected by the National Assembly (Article 84, point 8 of the Constitution of the Republic of Bulgaria; Article 12, para. 1 of the Law on the Bulgarian National Bank). The election of a new Governor is made not earlier than three months and not later than two months before the end of the term of office of the current Governor. The selection and appointment process is further specified by the provisions of the Rules of Organization and Procedure of the National Assembly – the rules in accordance with which the National Assembly organises and performs its work. Article 89, paragraph 1 of these rules stipulates that following a public procedure, the National Assembly elects bodies, in whole or in part, in accordance with the legislation in force. Article 89, paragraph 7 regulates the adoption of rules of procedure by the National Assembly governing the terms, conditions and procedures for nomination of candidates, the submission and public announcement of documents and the hearing of candidates in the relevant Standing Committee, as well as the procedure for their election by the National Assembly. The draft rules shall be prepared and submitted to the National Assembly by the relevant Standing Committee in charge of each election.
>
> In accordance with the provisions of the Rules of Organization and Procedure of the National Assembly, in June 2015 the National Assembly adopted a *Decision for adoption of rules of procedure governing the terms and conditions for nomination of candidates for Governor of the Bulgarian National Bank, for submission and public announcement of documents and the hearings of the candidates in the Parliamentary Budget and Finance Committee, as well as the procedures*

14 Note that the commission (selective committee) in Thailand is assembled for the purpose of selecting a governor (or board member) and disbands afterwards. As the membership criteria for the commission would make it suitable for a wide range of senior public sector appointments, it would seem possible – and beneficial – for another jurisdiction following the model to modify it by designing a standing commission covering several appointments.

15 The Treasury Committee induced Charlotte Hogg to withdraw her candidacy for a Deputy Governor position at the Bank of England, following revelations that she had ignored the requirements of the staff code of conduct that she had authored. And it revealed the lack of engagement of the Bank's Court in decisions on where the Bank deployed its policy analytic resources, despite the Court notionally being responsible for overseeing use of resources.

for election by the National Assembly. These rules of procedure specify in detail the participants involved in the process (process drivers and decision-makers), as well as the process steps for nomination of candidates for Governor, for selection among them and for appointment.

Pursuant to the procedure a nomination of candidates for Governor of the Bulgarian National Bank may be submitted by the parliamentary groups and by the unaffiliated members of the National Assembly. The written proposal for applicants is submitted to the Parliamentary Budget and Finance Committee via the Chairperson of the National Assembly within seven days from the adoption of the rules of procedure for the election of the Governor by the National Assembly. The nominations for Governor of the BNB shall be accompanied by a detailed written reasoning of the professional qualities and reputation of the applicant.

The following documents should be enclosed: the written consent of the applicant; the applicant's detailed CV, documents, certifying the professional qualification of the candidate in the area of economics, finance and banking (a copy of the diploma of higher education, certificates, recommendations and etc.), a conviction status certificate and a declaration related to the requirements for incompatibility that are set out in Article 11, paragraph 4, items 2–5 of the Law on the Bulgarian National Bank.

The selection proposals, along with the enclosed documents, shall be published on the website of the National Assembly not later than seven days before the hearing, in accordance with the Law on Personal Data Protection.

Non-profit legal entities and professional organizations may, not later than three days before the hearing, submit to the Budget and Finance Committee statements about the applicant, including questions to be asked to him/her. The media may send to the Budget and Finance Committee questions to be asked to the applicant. Anonymous statements and submissions shall be disregarded. The statements and questions are published on the website of the National Assembly in accordance with the Law on Personal Data Protection and the Law on Protection of Classified Information.

Before the hearing, the Budget and Finance Committee checks the documents submitted and examines whether the relevant applicant meets the requirements for taking the position. The hearing is public and it shall be broadcast live on the website of the National Assembly.

During the hearing the applicant is presented by the author of the proposal within two minutes. The presentation shall specify the existence of specific expertise, motivation, public reputation and public support for the relevant applicant. The applicants present their concept about performing the activity of the central bank within 20 minutes. All statements and questions submitted are presented within two minutes per statement/question. The applicant has ten minutes for answer. The members of the parliament have two minutes each for their questions and the applicant - ten minutes for answer. The committee may request further information both from the applicant, and from the respective competent authority.

Full stenographic minutes from the hearing of each applicant are published on the specialized page of the website of the National assembly. The committee draws up a report from the hearing of each applicant which shall contain a conclusion of the committee as regards the compliance with the minimum legal requirements for filling the post on the part of each applicant, as well as regarding the availability of data that calls into question the applicants' morality, competence, qualification, experience and professional assets. The report is submitted to the National Assembly along with a draft decision for election of each of the applicants.

The session of the National Assembly for election of a Governor is broadcast live on the website of the National Assembly. The relevant applicant is present during the session if the National Assembly decides so. The Budget and Finance Committee presents its report summarizing the results of the hearing. Each applicant is presented within two minutes by the author of the proposal. Debates on the nominations shall be held in accordance with the Rules of Organization and Procedure of the National Assembly. The vote shall be open and it shall be performed by the electronic voting system. If there are several applicants, a separate vote for each of the applicants shall be performed in accordance with the alphabetical order of their first name. An applicant shall be deemed elected if he/she has been supported by more than one half of the members of the National Assembly present. If several applicants receive more than one half of the votes of the members of the National Assembly present, the applicant who receives the most votes „in favour" shall be deemed approved. If nobody of the applicants receives the necessary votes, a second round of voting shall be held between the two candidates having obtained most votes „in favour".

If after the second round, nobody receives the necessary votes, the National Assembly takes a decision for opening of a new procedure for selection and appointment of a Governor.

According to the legal provisions the Governor is appointed by the National Assembly and the National Assembly passes a decision for the appointment (Article 84, point 8 and Article 86, para. 1 of the Constitution of the Republic of Bulgaria with reference to Article 12, para. 1 of the Law on the Bulgarian National Bank). At entering into office, the Governor swears an oath to the National Assembly to abide the law, to contribute to the performance of the functions entrusted to the Bank, as well as to keep professional, bank, commercial and another secrecy protected by law even after their duties have ceased (Art. 13 of the LBNB).

With reference to the question for the degree of embedding, please note that a separate procedure for the selection and appointment of a Governor should be approved with a decision of the National Assembly every time when a new Governor has to be elected.

It may be worth reinforcing the point made in the last paragraph of this description, namely that the National Assembly's detailed procedures for appointing the governor are effectively revisited and potentially modified each time, perhaps resulting in a degree of instability (or flexibility, to be more positive).

ANNEX 1: Appointment by a single actor

Country	Institution	Governor title	Recommended by (multiple name or other cases not involving veto):	Nominated by (single name offered, dual veto cases)	Consultation required with:	Appointed by:	Appointment approved by:
Bosnia Herzegovina	Central Bank of Bosnia and Herzegovina	Governor				Board	
Colombia	Central Bank of Colombia	Governor				Board	
Sweden	Sveriges Riksbank	Governor				Board	
Bulgaria	Bulgarian National Bank	Governor				Legislature	
Algeria	Bank of Algeria	Governor				Head of State	
Belgium	National Bank of Belgium	Governor				Head of State	
Czech Republic	Czech National Bank	Governor				Head of State	
Denmark	National Bank of Denmark	Chairman of the Board of Governors				Head of State	
Malaysia	Central Bank of Malaysia	Governor				Head of State	
Norway	Central Bank of Norway	Governor				Head of State	
Philippines	Central Bank of the Philippines	Governor				Head of State	
France	Bank of France	Governor				Cabinet/Govt	
India	Reserve Bank of India	Governor				Cabinet/Govt	
Turkey	Central Bank of the Republic of Turkey	Governor				Cabinet/Govt	
Australia	Reserve Bank of Australia	Governor				Minister	
Hong Kong	Hong Kong Monetary Authority	Chief Executive				Minister	

United Kingdom	Bank of England	Governor				Head of State	None Non-binding post-appointment suitability hearings are held by Parliament's Treasury Committee. Hearings may impact the appointment but the Committee has no statutory veto or approval authority.

ANNEX 2: Appointment by single actor, but requirement to consult additional actor(s)

Country	Institution	Governor title	Recommended by (multiple name or other cases not involving veto):	Nominated by (single name offered, dual veto cases)	Consultation required with:	Appointed by:	Appointment approved by:
South Africa	South African Reserve Bank	Governor			Board Minister	Head of State	
Finland	Bank of Finland	Governor	Board			Head of State	
Switzerland	Swiss National Bank	Chairman of the Governing Board	Board			Cabinet/Govt	
Singapore	Monetary Authority of Singapore	Managing Director	Commission			Head of State	
Latvia	Bank of Latvia	Governor	Legislature			Legislature	
Iceland	Central Bank of Iceland	Governor	Commission			Minister	
Austria	Austrian National Bank	Governor			Cabinet/Govt	Head of State	

ANNEX 3: Dual veto cases

Country	Institution	Governor title	Recommended by (multiple name or other cases not involving veto):	Nominated by (single name offered, dual veto cases)	Consultation required with:	Appointed by:	Appointment approved by:
Estonia	Bank of Estonia	Governor		Board		Head of State	
Canada	Bank of Canada	Governor				Board	Cabinet/Govt
New Zealand	Reserve Bank of New Zealand	Governor		Board		Minister	
Brazil	Central Bank of Brazil	Governor				Head of State	Legislature
Chile	Central Bank of Chile	Governor				Head of State	Legislature (for initial appointment as Board Member)
Indonesia	Bank Indonesia	Governor				Head of State	Legislature
Lithuania	Bank of Lithuania	Chair of the Board		Head of State		Legislature	
Mexico	Bank of Mexico	Governor				Head of State	Legislature
Poland	National Bank of Poland	President of the NBP		Head of State		Legislature	
North Macedonia	National Bank of the Republic of N. Macedonia	Governor		Head of State		Legislature	
Peru	Central Reserve Bank of Peru	President				Head of State	Legislature
Russia	Central Bank of the Russian Federation	Chairman of the Bank of Russia		Head of State		Legislature	
Serbia	National Bank of Serbia	Governor		Head of State		Legislature	
Slovenia	Bank of Slovenia	Governor		Head of State		Legislature	
Romania	National Bank of Romania	Governor		Legislature		Legislature	
Argentina	Central Bank of Argentina	Governor				Cabinet/Govt	Legislature
Japan	Bank of Japan	Governor				Cabinet/Govt	Legislature
Ireland	Central Bank of Ireland	Governor		Cabinet/Govt		Head of State	

Israel	Bank of Israel	Governor		Cabinet/Govt		Head of State		
Luxembourg	Central Bank of Luxembourg	Director-General		Cabinet/Govt		Head of State		
United Arab Emirates	Central Bank of the United Arab Emirates	Governor				Head of State	Cabinet/Govt	
United States	Federal Reserve System	Chairman of the Board of Governors of the Federal Reserve System			Legislature	Head of State	Legislature	

ANNEX 4: Dual veto cases, with requirement to consult additional actor(s)

Country	Institution	Governor title	Recommended by (multiple name or other cases not involving veto):	Nominated by (single name offered, dual veto cases)	Consultation required with:	Appointed by:	Appointment approved by:
Croatia	Croatian National Bank	Governor		Legislature	Legislature	Legislature	
Greece	Bank of Greece	Governor	Board	Cabinet/Govt		Head of State	
Thailand	Bank of Thailand	Governor	Commission	Cabinet/Govt		Head of State	
Germany	Deutsche Bundesbank	President of the Deutsche Bundesbank		Cabinet/Govt	Executive Board	Head of State	
Italy	Bank of Italy	Governor		Cabinet/Prime Minister	Board	Head of State	
European Union	European Central Bank	President of the ECB		Minister (as in Council of Ministers)	Board Legislature	Other (By common accord of the governments of the Member States at the level of the Heads of State or Government.)	
Korea	Bank of Korea	Governor		Cabinet/Govt	Legislature	Head of State	
Hungary	Magyar Nemzeti Bank	Governor		Prime Minister	(Parliament's Standing Committee for Economic Affairs has a non-statutory role)	Head of State	
Spain	Bank of Spain	Governor		Prime Minister	Legislature	Head of State	
Portugal	Bank of Portugal	Governor		Minister	Legislature	Cabinet/Govt	

ANNEX 5: Triple veto cases

Country	Institution	Governor title	Recommended by (multiple name or other cases not involving veto):	Nominated by (single name offered, dual veto cases)	Consultation required with:	Appointed by:	Appointment approved by:
China	Peoples Bank of China	Governor		Prime Minister		Head of State	Legislature
Slovakia	National Bank of Slovakia	Governor		Cabinet/Govt		Head of State	Legislature
Saudi Arabia	Saudi Arabian Monetary Authority	Governor		Minister		Head of State	Cabinet/Govt