

Accountability Mechanisms of Major Central Banks and Possible Avenues to Improve the ECB's Accountability

Compilation of papers



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This document was requested by the European Parliament's committee on Economic and Monetary Affairs.

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CONTENTS

Accountability Mechanisms of the Bank of England and of the European Central Bank

Author: Rosa M. LASTRA 5

Independence with Weak Accountability: The Swiss Case

Author: Charles WYPLOSZ 43

How Can the European Parliament Better Oversee the European Central Bank?

Authors: Grégory CLAEYS and Marta DOMÍNGUEZ-JIMÉNEZ 64

Accountability at the Fed and the ECB

Author: Karl WHELAN 90



Accountability Mechanisms of the Bank of England and of the European Central Bank

Rosa M. LASTRA



Abstract

This paper analyses the accountability mechanisms of the European Central Bank and of the Bank of England and focuses on parliamentary accountability for the monetary policy functions. The paper suggests ways to improve the Monetary Dialogue between the ECB and the Committee on Economic and Monetary Affairs (European Parliament).

This document was provided by Policy Department A at the request of the Committee on Economic and Monetary Affairs (ECON).

CONTENTS

LIST OF ABBREVIATIONS	8
EXECUTIVE SUMMARY	9
1. INTRODUCTION	10
2. ACCOUNTABILITY, LEGITIMACY AND TRANSPARENCY	11
2.1. Accountability	11
2.2. Legitimacy	14
2.3. Transparency	15
3. THE BANK OF ENGLAND	17
3.1. The Bank of England Act 1998	17
3.2. The Financial Services Act 2012 and post-crisis reforms	18
3.2.1. Transparency	19
3.2.2. Governance of the Bank	19
3.2.3. The Policy Committees	20
3.3. The Bank of England and Financial Services Act 2016	20
3.4. The role of the National Audit Office and the MoU with the Bank of England	21
3.5. The design of parliamentary accountability – the Treasury Committee of the House of Commons	22
3.6. Relationship with the HMT and ‘override powers’	24
4. THE EUROPEAN CENTRAL BANK	27
4.1. Accountability of the European Central Bank	27
4.2. The relationship between the European Central Bank and the European Parliament	28
4.3. Locus of parliamentary accountability	30
4.4. Ways of improving the Monetary Dialogue	31
4.5. Transparency	33
5. CONCLUDING OBSERVATIONS	35
ANNEX	37
REFERENCES	39

LIST OF ABBREVIATIONS

CJEU	Court of Justice of the European Union
EAC	Economic Affairs Committee
EAOS	Euro Area Oversight Subcommittee
ECON	European Parliament's Committee on Economic and Monetary Affairs
ECB	European Central Bank
EP	European Parliament
ESCB	European System of Central Banks
FCA	Financial Conduct Authority
FED	Federal Reserve
FOMC	Federal Open Market Committee
FPC	Financial Policy Committee
GFC	Global Financial Crisis
HC	House of Commons
HMT	Her Majesty's Treasury
IEO	Independent Evaluation Office
MEP	Member of European Parliament
MOU	Memorandum of Understanding
MPC	Monetary Policy Committee
NAO	National Audit Office
NCB	National Central Bank
PAC	Public Accounts Committee
PRA	Prudential Regulation Authority
PRC	Prudential Regulation Committee
QE	Quantitative Easing
SSM	Single Supervisory System
TFEU	Treaty on the Functioning of the European Union
TSC	Treasury Select Committee

EXECUTIVE SUMMARY

- In a democratic system governed by the rule of law, **central bank independence must always be accompanied by adequate mechanisms of accountability.**
- **While too broad independence may lead to an unacceptable 'state within the state', too much accountability threatens the effectiveness of independence.** The design of 'accountable' independence varies across jurisdictions.
- **Institutional accountability ought to be 'diversified' (*trias politica*),** encompassing parliamentary oversight, judicial review, audit control, and a degree of 'executive' responsibility. The emphasis of this paper is on accountability to Parliament.
- **Performance control is conditional upon the objectives and targets imposed upon the central bank, while the principle of transparency is a market-based form of accountability.**
- **Public support (*de facto* accountability) contributes to societal legitimacy.**
- **The UK experience – presented in this paper – is significant** in that it has expanded and reformed the accountability arrangements (parliamentary oversight and others) of the Bank of England in response to the expansion of the Bank's powers in recent years.
- **The role of the ECB has also grown significantly in response to the global financial crisis and to COVID-19.** The pandemic also evidences the need for better coordination in economic policy making.
- **This paper focuses on accountability for the monetary policy functions,** though both the ECB and the Bank of England have a wide range of other functions (including prudential supervision post GFC).
- **The adequate locus of institutional accountability for the ECB in the conduct of monetary policy resides at the European level** (judicial review by the European Court of Justice and accountability to the European Parliament/Committee on Economic and Monetary Affairs - ECON).
- **This paper recommends that European Parliament/parliamentary accountability be strengthened** and that the 'Monetary dialogue' be renamed as 'Monetary hearings' reflecting the need for enhanced oversight.
- **In terms of the content of such 'hearings', compliance with the ECB mandate (primary and secondary objectives) will remain of paramount importance** and must be continuously explained and justified. Hearings are particularly important when the central bank navigates through a crisis.
- The paper seconds the **establishment of a euro area subcommittee within ECON** to scrutinise monetary policy.
- **Effective audit control provides a basis and input for subsequent parliamentary oversight and improves transparency.**
- **ECB monetary policy measures must be subject to a proportionality test when subject to judicial review** by the Court of Justice of the European Union (Weiss).
- **The distributional and other effects of monetary policy are important issues from the perspective of democratic legitimacy** and must be considered by the EP/ECON.

1. INTRODUCTION

In a democratic system governed by the rule of law (like the EU is) central bank independence must always be accompanied by adequate mechanisms of accountability.

This paper is written at the request of European Parliament's Committee on Economic and Monetary Affairs (ECON) in preparation for the September 2020 'Monetary Dialogue' and aims to cast some light on possible ways to improve the accountability framework of the European Central Bank (ECB) in the conduct of monetary policy – in particular the relationship between the ECB and the European Parliament in the 'Monetary Dialogue' – taking into account the institutional balance enshrined in the Treaty, standing practices and recent developments. The paper also presents the accountability mechanisms of the Bank of England, as a comparative case study.

The impact of the ECB has grown significantly in response to the global financial crisis (GFC) and to COVID-19. The GFC changed the traditional understanding of the instruments of monetary policy, adapting the conventional tools, namely, open market operations, discount policies and reserve requirements, and adding a range of unconventional instruments. This has brought monetary policy into uncharted territory. The distributional and other effects of monetary policy are important issues from the perspective of democratic legitimacy and the evolving framework of enhanced accountability.

This report is divided into three parts.* Part 1 provides definitions of accountability, legitimacy and transparency and articulates the concept of 'diversified accountability'. Though the report focuses on parliamentary accountability, it also considers other mechanisms of accountability, notably judicial review, audit control and the relationship with the executive. In the same way that there are different degrees and indicators of central bank independence, there are also variations in the design and level of central bank accountability.

Part 2 of this report surveys the accountability arrangements and mechanisms of the Bank of England. Part 3 examines the accountability of the European Central Bank. The key issue is to strike the right balance between independence and accountability.¹

* Thanks to Marco Bodellini for research assistance and to Fabian Amtenbrink, Christina Skinner, Paul Tucker and Jens van 't Klooster for helpful suggestions.

¹ Though the ECB and the Bank of England have a wide range of other functions (in particular supervisory responsibilities), this report focuses on accountability for the monetary policy functions. Accountability varies across functions.

I have dealt with the concept of central bank accountability extensively in my publications, commencing with an article on "The independence of the ESCB" (a seminal contribution) published by the Harvard International Law Journal in the spring of 1992 and then in: *Central Banking and Banking Regulation* (LSE, 1996, ch. 1), *Legal Foundations of International Monetary Stability* (OUP, 2006, ch. 2 and ch. 7) and *International Financial and Monetary Law* (2015, ch. 2 and ch. 7). I also co-authored a book chapter with Heba Shams ('Public Accountability in the Financial Sector', in Eilis Ferrán and Charles Goodhart (eds.), *Regulating Financial Services and Markets in the XXIst Century*, Hart Publishing, Oxford, 2001, pp. 165-188; a book chapter with Geoffrey Miller ('Central Bank Independence in Ordinary and Extraordinary Times' in Jan Kleineman (ed), *Central Bank Independence. The Economic Foundations, the Constitutional Implications and Democratic Accountability* (The Hague: Kluwer Law International, 2001, pp. 31-50); a paper with Fabian Amtenbrink ('Securing Democratic Accountability of Financial Regulatory Agencies – A Theoretical framework' in *Mitigating Risk in the Context of Safety and Security. How Relevant is a Rational Approach?*, edited by R.V. de Mulder (Rotterdam: Erasmus School of Law & Research School for Safety and Security (OMV) 2008, pp 115-132); an article with Luis Garicano ('Towards a new Architecture for Financial Stability: Seven Principles', *Journal of International Economic Law*, Vol. 13, No. 3, September 2010, pp. 597-621) and a recent paper with Charles Goodhart, ("Populism and Central Bank Independence", *Open Economies Review* (2017)).

2. ACCOUNTABILITY, LEGITIMACY AND TRANSPARENCY

2.1. Accountability

Accountability can be defined as an obligation owed by one person (the accountable) to another (the accountee) according to which the former must give account of, explain and justify his actions or decisions against criteria of some kind, and take responsibility for any fault or damage.² Four elements are at the core of this definition³: (1) the accountable, (2) the accountee, (3) the content of the obligation and (4) the criteria of assessment.

- 1) A holder of power (the 'accountable'). Accountability presupposes that a person is in a position to make decisions that are likely to have an impact on others and to implement those decisions. Accountability is often categorised with reference to 'the accountable'. We speak of individual accountability, ministerial accountability, **central bank accountability**, corporate accountability and market accountability.
- 2) An authority to whom accountability is owed (the 'accountee'). Who guards the guardians? Accountability as an obligation must be owed to another party. The latter becomes by virtue of this obligation in a position of authority *vis-à-vis* the accountable.⁴ There are various types of accountability according to the authority that exacts it. In the context of central banking, we speak of **parliamentary accountability** (or accountability to parliament), of executive accountability (to the government for delivering the targets, like the letters to the Chancellor the Governor by the Bank of England, further discussed below) of judicial accountability (or accountability to the judiciary), of audit control, exercised by an audit office (like the National Audit Office in the UK) or court of auditors; and of accountability to the public to refer to the general public as the accountee.
- 3) The content of the obligation. A distinction is often made between 'explanatory accountability' where the obligation is to answer questions, to give account of action, and 'amendatory accountability' where there is an obligation to make amends and grant redress.⁵ With regard to monetary policy central bank accountability is typically explanatory.⁶

² This usage is borrowed from Oliver (1994). According to Bank for International Settlements (2009), accountability encompasses three main characteristics: (i) scrutiny by others; (ii) regular accounting for one's actions; and (iii) the risk of negative repercussions, if performance is considered unsatisfactory. Bovens (2007) defines accountability as "a relationship between an actor and a forum, in which the actor has an obligation to explain and to justify his or her conduct, the forum can pose questions and pass judgment and the actor may face consequences".

³ Based on Lastra and Shams (2001).

⁴ In its *Codes of Good Practice on Transparency* (Section IV), the IMF (2000) argues that "Officials of the central bank should be available to appear before a designated public authority to report on the conduct of monetary policy, explain the policy objective(s) of their institution, describe their performance in achieving their objective(s), and as appropriate, exchange views on the state of the economy and the financial system." This approach is in line with the aims set out by the UK [House of Commons] Treasury Committee (1997) which examined how it might best hold the Monetary Policy Committee to account and concluded that: "... by bringing information into the public domain we can help clarify the thinking and actions of those responsible for the formulation and delivery of monetary policy and the rigorous scrutiny of the basis for policy decisions will enhance the credibility and effectiveness of the monetary framework as a whole." I was asked to contribute to this report and submitted written evidence to the UK House of Commons at the request of the Treasury Committee regarding its inquiry into the accountability of the Bank of England. The written evidence, "The Parliamentary Accountability of the Bank of England", was ordered by the House of Commons to be printed, 23 October 1997, House of Commons, Session 1997-98, HC 282. In June 2011, I was invited to give oral evidence to the Treasury Committee of the House of Commons, as part of the Committee's inquiry into the accountability of the Bank of England. The report HC 874 (21st report of Session 2010-12) was [published](#) in November 2011.

⁵ Through judicial review and legislative mechanisms, central bank decisions are often protected by judicial deference and/or immunity. Many central banks have immunity from liability in damages in carrying out their functions provided that they are acting in good faith (see Section 244 of the Banking Act 2009 for the Bank of England).

⁶ Arguably, a significant conceptual reform to a monetary policy framework (such as that recently announced by the US Federal Reserve) could warrant some degree of amendatory accountability insofar as such shift signifies a departure from baseline monetary policy strategies or goals. Chairman Powell [presented](#) in August 2020 a revised Statement on Longer-Run Goals and Monetary Policy Strategy at See: Federal Reserve [press release](#): "On price stability, the FOMC adjusted its strategy for achieving its longer-run inflation goal of 2 percent by noting that it 'seeks to achieve inflation that averages 2 percent over time.' To this end, the revised statement states that 'following periods

- 4) Criteria of assessment. Any form of accountability presupposes that there are objectives or standards according to which an action or decision might be assessed. In other words, accountability implies an obligation to comply with certain standards in the exercise of power or to achieve specific goals. The more complex the activity, the more difficult it is to establish clear standards of conduct and specific outcomes. In which case accountability becomes ever more difficult. The more specific the goals and standards the more effective the accountability. This might induce the 'accountees' to resort to economic or other measurable criteria of performance (hence the term 'performance accountability'). A further twist to understand the notion of accountability is the distinction between *ex ante* and *ex post* accountability. Accountability can either be exercised before/during the process of taking the decision/action, or after the decision/action has been taken. It is with reference to this fact, the fact of concluding a decision or action, that we define accountability as either *a priori* (*ex ante*) or *a posteriori* (*ex post*).

An example of ***ex ante*** accountability is where the 'accountee' becomes involved in the process of choosing the holders of power, or where the consent of 'the accountee' is required for the decision of 'the accountable' to be final. For instance, the appointment procedures of central bank officials, when such procedures require parliamentary approval, (as in the US), and the parliamentary debate of inflation targets (if such a parliamentary debate is required) can be regarded as ways of exercising accountability *ex ante*.⁷ The reporting requirements and the appearances of the central bank chairman or governor in front of parliamentary committees (such as ECON) are ways of exercising accountability through control or ***ex post***.⁸

Lawyers and economists tend to give emphasis to different issues when they try to articulate the accountability of independent central banks. Lawyers emphasise the political and institutional dimension, i.e., the placing of the institution (the independent central bank) within the existing system of checks and balances, in relation to the three branches of the State - legislative, executive and judiciary (the question of who guards the guardians). Lawyers emphasise 'input accountability'.⁹

Accountability should be 'diversified' to include parliamentary accountability (the key source of accountability in a representative democracy), judicial review of the central bank's acts and decisions, audit control, and a degree of co-operation with the executive to ensure consistent overall policy making. "Parliamentary accountability should be exercised through a variety of procedures and

when inflation has been running persistently below 2 percent, appropriate monetary policy will likely aim to achieve inflation moderately above 2 percent for some time."

⁷ At least where appointments are concerned, political actors can use this kind of vetting-accountability to ascertain conceptual or methodological alignment with the appointee—and thus, implicitly, some manner of *de facto* control in the future.

According to Article 11 ESCB Statute, the ECB Executive Board members are appointed at European level; the European Council is also the depository of a democratic mandate, from the Member State governments and the European Parliament – as well as the ECB Governing Council – gives an opinion on the appointments.

⁸ Based on Lastra and Shams (2001). Hüpkes et al. (2005) provide a table (Table 2) mapping possible accountability arrangements for financial sector supervisors (comprising central banks endowed with supervisory responsibilities and other authorities), according to content and form, and whether it is *ex ante* (explanatory) or *ex post* (amendatory). In terms of accountability to the legislative branch they include: Regular report (annual) to assembly or committee; Ad hoc questioning and oral presentations, Ad hoc presentations of proposals for new laws; Presentation of budgetary outcome and Audit report (a mix of *ex ante* and *ex post* mechanisms). In terms of accountability to the executive branch, they include: Regular report to minister of finance or government; ad hoc formal presentations, information on sectorial developments and Proposals for new government regulations/ decrees (a mix of *ex ante* and *ex post* mechanisms). In terms of accountability to the judicial branch (by definition *ex post*) they include judicial review and supervisory liability for faulty supervision. In terms of accountability to the market or supervised industry they include consultations on new regulations and Regulatory impact analysis and cost-benefit assessments (a mix of *ex ante* and *ex post* mechanisms). In terms of accountability to customers and the public at large they include: Mission statement; Information on regulatory and supervisory practices on the website, annual reports, press conferences and public statements of representatives of the RSAs and Consumer education and Ombudsman schemes and consumer grievance board (a mix of *ex ante* and *ex post* mechanisms).

⁹ For a discussion of 'input' and 'output' accountability see Lastra and Garicano (2010), above note.

mechanisms, including annual reports and appearances in front of parliament of public officials on a regular basis, and also in the case of an emergency situation.

Judicial review of the agency's actions and decisions (conducted by an independent and depoliticised judiciary) is essential to prevent and control the arbitrary and unreasonable exercise of discretionary powers. This is a fundamental element of the rule of law. The discretion of public officials should never be unfettered but subject to legal control.”¹⁰

Audit control provides financial accountability. The necessary cooperation with the executive remains a most contentious issue in the design of accountability arrangements. The balance between independence and accountability varies across jurisdictions, depending upon the particular economic and political circumstances, legal traditions, institutional frameworks and constitutional requirements.

Accountability requires mechanisms that ensure that those involved in the decision making process explain the actual decisions and the process leading to them.

Economists, while accepting the ‘institutional’ articulation of accountability according to the *trias politica* (separation of powers) and, in particular, parliamentary accountability, tend to give emphasis to performance accountability and disclosure (both can be regarded as ‘output’ accountability). Disclosure or transparency can be viewed as a ‘market-based’ form of accountability. For instance, with regard to the transparency required in the monetary policy decisions taken by an independent central bank, the minutes of the Federal Open Market Committee (in the US) or of the Monetary Policy Committee of the Bank of England must be published. The ECB publishes the monetary policy accounts four weeks after a monetary policy decision is announced.

“Performance control (the question of how accountability is to be achieved) is (...) conditional upon the objectives and targets imposed upon the agency (for example, upon the central bank). Performance control is facilitated first by the existence of one rather than multiple goals or by their unambiguous ranking and, secondly, by the existence of a clearly stated and narrowly defined goal.”¹¹

The support of public opinion is another form of *de facto* accountability which finds echo in the media, in an independent press (the ‘court of public opinion’),¹² though some segments of the media are either politicised or subject to ideological constraints (or ‘fake news’). The support of public opinion - as further discussed below from the perspective of societal legitimacy - is important.

In a representative parliamentary democracy voters can trigger legislative amendments (one statute may be removed by another) or question the integration process (as Brexit has indeed done).

“Independence and accountability can be seen as opposite ends of a continuum. While too much independence may lead to the creation of a democratically unacceptable ‘state within the state’, too much accountability threatens the effectiveness of independence, and in some instances (particularly

¹⁰ Lastra and Shams (2001). That the ECB is subject to judicial control by the Court of Justice of the European Union (CJEU) is uncontested. The ECB's decisions and the acts preparatory to them can only be challenged in front of the CJEU according to Article 263 TFEU and Article 35 of the Statute of the ESCB, which gives exclusive jurisdiction to the CJEU to review the legality of the ECB's acts and decisions. However, in the USA, monetary policy decisions are thought not to be justiciable (though supervisory and other decisions are). The authority for the non-justiciability of monetary policy decisions dates back to *Raichle v Federal Reserve Bank of New York*, 34 F.2d 910 (2d Cir. 1929):

“It would be an unthinkable burden upon any banking system if its open market sales and discount rates were to be subject to judicial review. Indeed, the correction of discount rates by judicial decree seems almost grotesque, when we remember that conditions in the money market often change from hour to hour, and the disease would ordinarily be over long before a judicial diagnosis could be made.”

Judicial decisions in the UK have shown deference towards the discretion of the Bank of England.

¹¹ Lastra and Shams (2001).

¹² Paul Tucker (2018) talks about “360-degree democracy as watchfulness” in Chapters 9 and 10.

in the case of the exercise of a government override) may actually nullify independence.”¹³ There is also the issue of efficiency and coordination in economic policy making as COVID-19 clearly evidences.

The debate about independence and accountability resembles, the philosophical debate about freedom and responsibility: independence without accountability would be like freedom without responsibility.

2.2. Legitimacy

The question of legitimacy pre-exists and is a prerequisite of accountability. The creation of an independent central bank must therefore be the fruit of a democratic act (an act of the legislator like in the case of the Bank of England, a constitutional decision, or a treaty provision like in the case of the ECB). This first source of legitimisation is fundamental in a democratic society. However, while this legal basis legitimises the establishment of the independent agency, it cannot by itself legitimise on a continuous basis the exercise of the powers delegated to such agency. It is then in the continuing life of that entity that accountability becomes necessary to ensure legitimacy: accountability is thus the process of bringing back (by giving account, explaining, justifying, or taking measures of amendment or redress) an independent entity to the procedures and processes of a democratic society.¹⁴

However, accountability also encompasses other ‘technical’ elements that are not related to the ‘political’ legitimacy of the institution, such as performance control. Accountability per se does not politicise a central bank. Conversely, while accountability is needed to ensure ongoing democratic legitimacy, legitimacy has two aspects: a formal, normative one which refers to legality of the political system and a societal or empirical one, which is determined by the acceptance of or loyalty to the system.¹⁵

The legitimacy of independent institutions may be understood by reference to the ‘Robinson Crusoe’ paradigm. Just as an individual—recognising his own imperfection in the face of possible temptations—imposes constraints upon himself, “in order to channel his own expedient behaviour towards rationally selected norms”,¹⁶ a government, recognising its own weakness in the face of temptations, limits itself by allowing or creating autonomous or independent bodies. This willingness to submit itself to restrictions provides a degree of democratic legitimacy.

“Central banks are not majoritarian, democratic institutions.¹⁷ Central banks are, instead, technocratic bureaucracies, staffed by career employees and, typically, a few leaders who have been appointed by the political authorities.”¹⁸ “Central banks do not only administer a technical regulatory scheme affecting discrete industries or interests. In their core monetary policy role they regulate price levels,

¹³ Lastra and Shams (2001).

¹⁴ de Boer and van ‘t Klooster (2020) (cited with permission by the authors), advocate a revision of the key treaty provisions to improve the legitimacy of the ECB (activating Article 40 of the ESCB Statute) and argue that “procedural arguments always had a role in providing central bank independence with legitimacy”. They contemplate the role of judicial review, whether the courts do “too little” or “too much” and further argue that the CJEU and the German Constitutional Court adopt different approaches in their judicial review post Weiss. While the CJEU defers to the ECB “as long as it pursues the objective of price stability”, the German Constitutional Court (GCC) insists on stricter scrutiny and demands “that the central bank weighs the economic policy effects of its monetary policies” and approaches the issue “through the lens of proportionality”. The GCC “requires the ECB to explain and justify how it has taken into account the potential negative effects of its monetary policies”. They note, however, that “judicial review does not solve the problem of democratic legitimacy”.

¹⁵ See Verhoeven (2002). Charles Goodhart and myself (Lastra and Goodhart, 2017) wrote: “Legitimacy in turn is rooted in the concept of sovereignty.(...) Of course, societal legitimacy can be fickle since public acceptance is also influenced by politics, the media, current events, changes in circumstances, sentiment, and other factors. In any case, when societal legitimacy weakens or is no longer present, the law is bound to change.”

¹⁶ See Buchanan (1975).

¹⁷ See Lastra and Miller (2001), above note. See also Majone (1994).

¹⁸ For discussion in the American context, see e.g. Lawson (1994); Miller (1986); Strauss (1984); ‘Symposium, Administering the Administrative State’ (1990) 57 University of Chicago Law Review 331; ‘A Symposium on Administrative Law: The Uneasy Constitutional Status of Administrative Agencies’ (1987) 36 American University Law Review 277.

which is one of the most fundamental powers of government, and one of the most important practical concerns of the public at large.”¹⁹

“The case for central bank independence can be reconciled, in general, with the theory of democratic self-determination. An analogy to the independent judiciary may be useful in this respect.”²⁰ Like central banks, the judiciary administers the nation’s laws going to the core of a nation’s political identity. And like central bankers, judges, in general, are not popularly elected in liberal democracies.”²¹ The theory of judicial legitimacy is better developed than the theory of central bank legitimacy, so it is enlightening to turn to this analogy for instruction.

2.3. Transparency

“Prior to the 1980’s, transparency was hardly discussed in academic and policy literature.” “This inevitably begs the question of *why* the recent concern with transparency. Transparency is an essential feature of governance in a market economy.” “[The] link between transparency and the market is further illustrated by the increased emphasis on transparency in the 1990’s following the collapse of the Soviet Union and the global trend towards a market economy.”²² Dhonte and Kapur have pointed out that “a market system pre-ordains the rule of law by ensuring three basic conditions: free entry to markets, *access to information*, and the objective sanctity of contracts.”²³

“Any recent discussion of accountability often includes a reference to transparency and vice versa. This poses the question of the relationship between the two concepts.” “Accountability is an obligation to give account of, explain and justify one’s actions, while transparency is the degree to which information on such actions is available. The provision of information is clearly an element of accountability.”²⁴ However, the provision of information is hardly ever a neutral account of what happened or of what is happening; hence, the need for an explanation or justification of the agency’s actions or decisions (i.e., accountability). Thus, accountability must involve defending the action, policy or decision for which the accountable is being held to account.

The provision of information in the context of accountability, whether in an *ex ante* investigation or an *ex post* requirement of disclosure, facilitates transparency. On the other hand, a transparent economic and political environment enhances the effectiveness of accountability. The two concepts are therefore mutually enforcing, and they both share the provision of information as a common requirement.

Notwithstanding the benefits of transparency in the area of monetary policy, with regard to supervision²⁵ (and resolution) the disclosure of some sensitive decisions can end up generating a panic. Accordingly, certain supervisory decisions require a degree of confidentiality given the psychological connotations of bank panic and contagion;²⁶ another reason for confidentiality is the need to facilitate

¹⁹ Above note Lastra and Miller (2001).

²⁰ Goodhart and Meade (2004) have also written a paper on this.

²¹ Lastra (2010).

²² Lastra and Shams (2001).

²³ Dhonte and Kapur (1997).

²⁴ Lastra and Shams (2001). According to the Scott Report [Inquiry into exports of defense related equipment and dual use of goods to Iraq and related prosecution HC 115 I (1995-96) cited in H. Fenwick & G. Philipson, *Sourcebook on Public Law* (London 1997), ¶ D4.58]: “The importance (...) of the provision of full and adequate information is, in my opinion, self evident, whether in answering parliamentary questions or in debate or to a select committee. Withholding information on the matter under review, it is not a full account, and the obligation to account for what has happened or for what is being done has prima facie not been discharged. *Without the provision of full information, it is not possible for parliament, or for that matter the public, to hold the executive fully to account.*” (emphasis added)

²⁵ It should be noted that there have also been some moves to transparency in supervision, such as stress testing.

²⁶ The need for covert assistance in the case of lender of last resort operations is of particular importance to contain a crisis, since the belief in a panic is self-fulfilling and the fact that an institution is known to require official assistance may trigger the very run the authorities are keen to prevent, and thus “stigmatise” the provision of such assistance.

candid information sharing between the supervisor and the supervisee and also to facilitate sharing between supervisors.²⁷ In any case, the main focus of this paper concerns monetary policy accountability and not supervisory accountability. It is in the realm of transparency where significant developments have taken place over the last two decades. Some 'new paradigms' of accountability - such as consultations with consumers, industry groups, or the public in general, or proportionality assessments - contribute to transparency, though they must be channelled through adequate institutional mechanisms. I will return to this adequate channelling when discussing the accountability of the ECB.

²⁷ See also the recent [CJEU case of Baumeister](#).

3. THE BANK OF ENGLAND

Over the last two decades, the Bank of England has undergone a number of reforms and structural changes impacting upon its objectives, functions, and internal organization.²⁸ The Bank's powers have been significantly expanded in particular in the aftermath of the GFC. With expanded powers comes enhanced accountability.²⁹

Today, the Bank of England is the micro and macro prudential supervisor, the financial markets infrastructure regulator and the resolution authority in addition to its traditional monetary policy and other central banking responsibilities (such as note issue, bankers' bank and lender of last resort). The current mandate of the Bank, encompassing both price stability and financial stability, is reflected in its organisational structure, with the Monetary Policy Committee (MPC) established in 1998 and the Financial Policy Committee established in 2013.³⁰

It is important to bear in mind that all reforms were adopted on the premise that "a transparent, accountable and well-governed central bank is essential not only for effective policy, but also for democratic legitimacy".³¹

3.1. The Bank of England Act 1998

The Bank of England was given operational independence in the conduct of a price stability oriented monetary policy with the passage of the Bank of England Act 1998.³² The Bank's independence is 'instrumental' and could be repealed through ordinary legislation. There is no specific 'declaration of independence' protecting the Bank of England from political interference.³³

Accountability is exercised via a number of formal and informal mechanisms, including parliamentary scrutiny, with the Governor and other Bank officials being called to testify in the front of the Treasury Committee (TSC), and reporting requirements, such as the obligation to publish the minutes of the meetings of the Monetary Policy Committee and the publication of the Bank's Inflation Reports on a quarterly basis (which inform also the questions posed to the Governor by the TSC).

As Salib and Skinner explain, monetary policy in the UK is conducted as follows:

- 1) Parliament sets the Bank the goal of maintaining price stability;

²⁸ The Bank was in private hands for the first 252 years of its existence and then nationalised with its capital stock transferred to HM Treasury in 1946; see [Bank of England Act 1946](#), 9 & 10 Geo. 6 c. 27, § 1(1) (UK). The shares are held by the Treasury Solicitor on behalf of HM Treasury. See "[Who Owns the Bank of England?](#)".

²⁹ See generally Tucker (2018), *passim*. Tucker explains how the regulatory state need not be a fourth branch of government free to steer by its own lights, and how central bankers can emulate the best of judicial self-restraint and become models of dispersed power.

Briault, Haldane and King (1996) created an accountability index based on four criteria: a) Whether the central bank is subject to external monitoring by Parliament; b) Whether the minutes of the meetings in which monetary policy is decided are published; c) Whether the central bank publishes an inflation or monetary policy report in addition to the standard central banks bulletins and d) Whether there is a clause that allows the government to override a decision by the central bank.

³⁰ See UK Government (2016), stating that "*The Financial Services Act 2012 dismantled the failed tripartite system, putting the Bank of England at the centre of a new framework of financial regulation*".

³¹ See Bank of England (2014).

³² In the 1990s a broad consensus emerged in relation to the economic benefits arising from granting central banks instrument independence over monetary policy. See Lastra (1992) and Lastra (1996), chapter 1. A distinction was made between goal independence, referring to the central bank being free to set its monetary policy goals, and instrument independence, referring to the central bank being free to choose the means by which it achieves its goals. See Debelle and Fischer (1994). See also Balls et al. (2016).

³³ Although this is made unlikely by non-legal reasons, since - as Salib and Skinner (2019) point out - independence gives the central bank credibility and market confidence in the pursuit of its objectives. They emphasise that there is "*no oath that its political masters must swear requiring them to respect central bank independence*" and recall (id, 913) the words of Chancellor Lawson saying that "*there would be a powerful market sanction against that: the mere announcement of the intention to do so would in itself be so damaging to market confidence that any Government would be extremely reluctant to attempt it*".

- 2) Parliament empowers HM Treasury to define this on an annual basis;
- 3) The Bank has operational independence in setting policy to achieve price stability (and is accountable to HM Treasury and Parliament for doing so);
- 4) Yet this operational independence is not immutable and can be overridden by HM Treasury in extreme economic circumstances; but
- 5) Should HM Treasury wish to do so, it can only do so transparently and with the approval of Parliament.

Parliament empowers HM Treasury to elaborate on the Bank's statutory objectives. In practice, this takes the form of letters from the Chancellor to the statutory committees, which are issued and published on a regular basis. As one would expect, the scope of the letter varies depending on the committee. "The Chancellor's remit to the MPC, which must be issued at least once every twelve months, defines price stability (an inflation target) and specifies the economic policy of the government. Since 1997, the remits have required an exchange of 'open letters' between the Governor and the Chancellor if inflation moves away from the target by more than 1% in either direction".³⁴

The fact that the MPC has external members to avoid groupthink also facilitates accountability.

In 2011, the TSC published a report (following an extensive inquiry) into the accountability of the Bank of England.³⁵ The TSC recommended inter alia a clarification of the lines of accountability between the Chancellor, Her Majesty's Treasury (HMT) and the Bank of England at times of financial difficulty, and generally that the Bank should be more open about its work and must be held to account more clearly than in the past. The response to the Report by the Court of the Bank was published on 23 January 2012, together with a short Report by the Committee.³⁶ The Court suggested that it was indeed in the public interest that the new legislation would provide a long term framework for the accountability of the Bank of England, which would increase, not diminish the authority of the Bank of England.

3.2. The Financial Services Act 2012 and post-crisis reforms

The Financial Services Act 2012 – a legislative response to the GFC of 2007-2009 – gave the Bank of England responsibility for overseeing the UK financial system as a whole. The Act established the Financial Policy Committee (FPC) and the Prudential Regulation Authority (PRA). The PRA was set up (at the outset) as a subsidiary of the Bank.

With expanded responsibilities "comes the need for effective transparency, genuine accountability and robust governance arrangements".³⁷

In 2014, the Bank of England proposed a series of changes aimed at reinforcing its transparency, accountability and governance, some in response to the Warsh Report.³⁸ With a view to strengthening the ability of the Parliament and the public to hold the Bank accountable for its actions, the 2014 changes were as follows:

³⁴ See Salib and Skinner (2019).

³⁵ The [report](#) was published on 8 November 2011.

³⁶ UK [House of Commons] Treasury Committee (2012).

³⁷ See Bank of England (2014). See also the [Governor's introduction](#) of the Warsh report and the Bank's response to it at.

³⁸ See review by Kevin Warsh (2014). Warsh (a former Governor of the Federal Reserve System) identified four distinct objectives of monetary policy transparency (1. sound policy, 2. effective communication, 3. public accountability and 4. accurate historical record-keeping), and made recommendations with respect to each of them.

- 1) Improvements to Monetary Policy Committee transparency (MPC) by publishing in part a transcript of the MPC meetings (though the minutes with votes were published since 1997) and publication of the minutes of Court meetings;
- 2) The simplification of the governance and structure of the Bank's Court of Directors (which turned back into a unitary body; and
- 3) The alignment of the status of the FPC and the PRA Board with that of the MPC.³⁹

3.2.1. Transparency

With regard to MPC transparency, the Bank decided to publish, with an appropriated delay (*i.e.* 8 years), the transcripts of that part of its meeting at which policy is decided and the Inflation Report⁴⁰ (though, as I have already mentioned, the minutes with votes were published since 1997).

Concerning the interaction between the MPC and FPC, both committees considered it appropriate to enhance such interaction by scheduling four joint meetings per year.⁴¹ It is important to emphasise that though the minutes of the MPC and the minutes of the FPC routinely are published, the PRC meetings are never published, for the reasons discussed above as regards the need for confidentiality to avoid bank runs and panics.

MPC minority votes help focus public debate and oversight by the TSC. The FPC never has any minority votes. Some argue that this is not a commendable practice, while others hold that consensus decision making is important on financial stability issues, that the institution should speak with one voice and that financial stability decisions do not lend themselves to yes/no votes.

Since April 2013, the Bank has published the minutes of its Court meetings six weeks after the meeting to which they relate, or, if there is no further meeting within that period, then two weeks after the date of the next Court meeting. Yet, pursuant to the 1998 Act, the Court may decide to omit information from its published record in the public interest as well as information which is legally sensitive or commercially confidential.⁴² With a view to enabling the Parliament, through its Treasury Committee, to hold the Bank to account, the latter – after sustained pressure from TSC – decided to publish also the minutes of the historical court meetings. The 2007-2008 court minutes were in fact published at the time of the transparency report in 2014.

3.2.2. Governance of the Bank

The Bank proposed to simplify its governance structure on the grounds that direction and oversight were divided between two statutory boards, *i.e.* the Court and the Oversight Committee, whose functions overlapped. The Bank believed that a single unitary board could be more effective both in managing the Bank and in delivering a more convincing framework for accountability.⁴³

The Independent Evaluation Office (IEO) was established in 2014 to assess the Bank of England's performance and, as a result, to "increase public trust in the Bank and to improve its openness, learning culture and public accountability. The IEO is an independent unit that sits within the Bank. It operates at arm's length from other areas so as not to compromise the independence of the Bank's policy

³⁹ Id., 1, also stating that these changes were expected 'to enhance the Bank's ability to fulfil its mission to promote the good of the people of the United Kingdom by maintaining monetary and financial stability'.

⁴⁰ See Bank of England (2014), 2.

⁴¹ Id., 3.

⁴² Id., 4, also underlining that 'these passages are omitted from the published minutes, but are still transferred to the Bank's Archive, for eventual release in line with the Bank's archive policy for Court minutes'.

⁴³ Id., 4-5.

making. The Court of Directors has a statutory obligation to keep the Bank's performance under review, and the IEO supports this through its in-depth evaluations. When necessary, the IEO also supports reviews carried out by independent third parties. The IEO reports directly to the Chair of Court, who sets the IEO's remit and work programme, typically in consultation with other Court Directors."⁴⁴

3.2.3. The Policy Committees

The MPC was already a Committee of the Bank operating under objectives set in legislation (according to the 1998 Act) so as "to maintain price stability and, subject to that, to support the economic policy of Her Majesty's Government, including its objectives for growth and employment."⁴⁵ Such a structure was considered particularly effective and therefore it was suggested that the FPC and Prudential Regulation Committee (PRC) should also adopt the same structure.

HMT effectively issues three remit letters, one to each of the three policy committees.⁴⁶ They are slightly different with the PRC one much less frequent (once a Parliament) but essentially allowing HMT to set out its economic policy and issue the Bank of England should have regard to.

3.3. The Bank of England and Financial Services Act 2016

The changes proposed by the Bank of England which needed a legislative reform to effect have been implemented through the Bank of England and Financial Services Act 2016. For the purposes of accountability and independence, the most relevant elements of the 2016 Act are the following:

- 1) Improvement of the accountability and governance of the Bank by making its Court of Directors a smaller, more focused unitary board;
- 2) Moving the MPC to a schedule of a minimum of 8 meetings a year;
- 3) Finalisation of the Governor's 'One Bank' reforms by bringing the PRA within the Bank, ending its status as a subsidiary, and establishing a new PRC;
- 4) Changes to the FPC, by making it a statutory committee of the Bank, in line with the MPC and the new PRC;
- 5) Appointment of a new Deputy Governor for Banking and Markets in legislation, adding the position to the Court of Directors and the FPC. This can be criticised however, on the basis that no other than the Governor covers the whole Bank, since four Deputy Governors can be considered like 'Department Heads' (or like the four executive directors that existed for decades and decades);
- 6) Bringing the Bank within the purview of National Audit Office (NAO) value for money studies, improving transparency and accountability for its use of resources; and
- 7) Further coordination arrangements between the Treasury and the Bank in protecting taxpayers and the wider economy from bank failures.

⁴⁴ It is worth noting that one of the IEO reports relates to monetary policy forecasting available at <https://www.bankofengland.co.uk/independent-evaluation-office>.

The IEO of the Bank of England is similar in nature to the [IMF IEO](#) which was established by the IMF Executive Board in July 2001 to provide objective and independent evaluation on issues related to the IMF.

⁴⁵ Bank of England (2014), Id., 5.

⁴⁶ As noted above, Salib and Skinner (2019), op cit. 922: "Parliament empowers HM Treasury to elaborate on the Bank's statutory objectives. In practice, this takes the form of letters from the Chancellor to the statutory committees, which are issued and published on a regular basis. As one would expect, the scope of the letter varies depending on the committee". "The Chancellor's remit to the MPC, which must be issued at least once every twelve months, defines price stability (an inflation target) and specifies the economic policy of the government. Since 1997, the remits have required an exchange of "open letters" between the Governor and the Chancellor if inflation moves away from the target by more than 1% in either direction".

The Bank of England and Financial Services Act 2016⁴⁷ is the last major milestone in this far reaching series of reforms. This 2016 Act strengthened the governance and accountability of the Bank, by ending the subsidiary status of the PRA and allowing the NAO to undertake value for money reviews of the Bank for the first time. With these reforms Bank of England aspired to continue to be an international example of best practice. The Bank of England's website summarises some of this arrangements.⁴⁸

3.4. The role of the National Audit Office and the MoU with the Bank of England

Audit control provides a basis and input for subsequent parliamentary scrutiny, as long as it is strong, accurate and independent.

Following the Bank's 'transparency and accountability' report of 2014⁴⁹, the 2016 Act⁵⁰ made the Bank subject to the NAO. NAO 'value for money' reviewed for the first time (albeit with important exceptions around policy decisions) the BoE relationship with the NAO⁵¹, which was articulated in a carefully negotiated Memorandum of Understanding (MOU) between the Bank of England and the NAO⁵² with the aim to enable the latter to conduct "examinations into the economy, efficiency and effectiveness with which the Bank has used its resources in discharging its functions".

"The Comptroller and Auditor General, as head of the NAO, helps Parliament to hold to account those responsible for the use of public resources. In order to perform this function effectively, the Comptroller has wide-ranging powers within a statutory framework that enshrines his independence and ability to exercise discretion in the choice and conduct

⁴⁷ UK Government (2016).

It also included other measures to ensure that senior managers across the financial services industry can be held to account for failings that occur on their watch, through the extension of the Senior Managers and Certification regime to all authorised persons. Though this last measure is not relevant for central bank accountability, it should be noted that the Bank of England has said publicly that it applies the principles of the senior managers regime to its own officials and published an associated "responsibilities map".

⁴⁸ See <https://www.bankofengland.co.uk/knowledgebank/how-is-the-bank-of-england-independent-of-the-government> and <https://www.bankofengland.co.uk/about/governance-and-funding>: The Bank of England is a public body that must answer to the people of the UK through Parliament. The Bank answers to Parliament's [House of Commons Treasury Committee](#) publicly holds the Bank to account. It regularly asks the Governor and other senior representatives to explain how and why they arrive at their decisions and asks questions about our approach to [monetary policy](#), [financial stability](#) and [prudential regulation](#). It also questions new members of the three policy committees before they start their role. Find transcripts, reports and videos of these events on the [UK Parliament website](#).

⁴⁹ Bank of England (2014).

⁵⁰ UK Government (2016).

⁵¹ The provisions concerning the Comptroller and the Bank were inserted into the 1998 Act by the Bank of England and Financial Services Act 2016. The relevant statutory provision for NAO accountability is section 6 of the Bank of England Act 1998 which reads as follows:

"7D Examination by Comptroller and Auditor General

(1) The Comptroller and Auditor General ("the Comptroller") may carry out examinations into— (a) the economy, efficiency and effectiveness with which the Bank has used its resources in discharging its functions; (b) the economy, efficiency and effectiveness with which a Bank company has used its resources in discharging its functions. (2) An examination under this section may be limited to such functions (however described) of the Bank or the Bank company as the Comptroller considers appropriate. (3) An examination under this section is not to be concerned with the merits of the Bank's policy objectives. (4) An examination under this section is not to be concerned with the merits of— (a) policy decisions taken by the Financial Policy Committee, the Monetary Policy Committee or the Prudential Regulation Committee; (b) policy decisions taken by a committee or other body within the Bank for the time being having responsibilities for the supervision of payment systems, settlement systems [central securities depositories] or clearing houses, so far as the decisions relate to that supervision. (5) Subject to subsection (6), an examination under this section is not to be concerned with the merits of policy decisions taken by a committee or other body within the Bank for the time being having responsibilities for the exercise of any of the Bank's resolution functions, so far as the decisions relate to those functions. (6) Where the Bank has exercised relevant resolution functions in relation to a financial institution, subsection (5) does not prevent an examination under this section being concerned with the merits of policy decisions within that subsection which are relevant to the Bank's exercise of its resolution functions in relation to that institution (whether or not those policy decisions are also relevant to other financial institutions). (7) "Relevant resolution functions" are (...) (8) Before carrying out an examination under this section, the Comptroller must consult the court of directors of the Bank. (9) The Comptroller may report to the House of Commons the results of any examination carried out by the Comptroller under this section. (10) For the purposes of this section (...) (11) Section 6 of the National Audit Act 1983 (Comptroller may carry out economy, efficiency and effectiveness examinations) does not apply to the Bank or a Bank company."

⁵² See Memorandum of Understanding between the National Audit Office and the Bank of England.

of his work'.⁵³ 'While the Comptroller will not examine the merits of policy objectives or the merits of policy decisions of the relevant committees (including advice on which decisions on individual cases are based), the Comptroller may examine the efficiency and effectiveness with which the Bank uses its resources to discharge its functions including whether the capability maintained by the Bank to support those policy processes is appropriate'.⁵⁴

The NAO has done a report into the Bank's central services⁵⁵ to which the Bank responded⁵⁶ raising criticisms of the Bank that were picked up in the press.⁵⁷ Also because of the NAO angle – in terms of parliamentary scrutiny it was the Public Accounts Committee (PAC) that took responsibility – it was probably the first time Bank officials went before the PAC (the Treasury Committee is the usual avenue of parliamentary accountability).

Both the NAO and the IEO provide input for subsequent parliamentary scrutiny.⁵⁸

3.5. The design of parliamentary accountability – the Treasury Committee of the House of Commons

The expansion of the powers of the Bank of England leads inevitably to a rethink of the accountability arrangements.⁵⁹ Parliament is regarded as the best institution to play the role of guarding the guardians of monetary and financial stability in a representative democracy.⁶⁰ In practice, a number of issues arise for parliamentary scrutiny to function effectively. To begin since monetary and banking issues are highly specialised matters, such scrutiny should be exercised by a specialised parliamentary committee.⁶¹

The Treasury Committee (often referred to as the Treasury Select Committee or TSC) is appointed by the House of Commons (HC) to examine HM Treasury, HM Revenue and Customs, the Bank of England and the Financial Conduct Authority (FCA),⁶² while the House of Lords Economic Affairs Committee (EAC) also exercises its own power to hold hearings with HMT and the Bank.

⁵³ Id., 2.

⁵⁴ Id., 3.

⁵⁵ National Audit Office: "[Managing the Bank of England's Central Services](#)".

⁵⁶ Bank of England: "[Bank of England press statement on NAO Report](#)".

⁵⁷ Financial Times (19 December 2018): "[Spending watchdog criticises Bank of England's 800 empty desks](#)"; BBC (19 December 2018): "[Bank of England rebuked over £5m in unchecked spending](#)".

⁵⁸ As stated above, since 2014 the Bank of England has its own Independent Evaluation Office (IEO). In July 2019, for example, the Court commissioned the IEO to carry out an in-depth evaluation of the Bank's Asset Purchase Programme.

⁵⁹ "With power comes responsibility". As they say, *Quis custodiet ipsos custodes?*, Lastra (2011), 20, "Lord Acton's dictum resonates in the background of the corridors of power, as a key reminder of the importance of accountability".

⁶⁰ See Lastra, *Accountability of the Bank of England*. First Report. House of Commons – Treasury Committee, Session 1997-1998, London, 27 October 1997, 28, clearly saying that "in a democracy, an independent central bank needs to be accountable to the elected representatives of the will of the people, i.e. to Parliament".

⁶¹ Andrew Tyrie, former chairman of the TSC, argued in his 2015 book that "Select Committees are now much more effective scrutineers and investigators than they were even five years ago" (Tyrie, 2015: 33). This surely had to do – when he wrote these lines – with his own strong chairmanship and knowledge of the subject matter.

⁶² Tucker, above note, at p. 368, recalls how the UK government historically was accountable "on the Floor of the House" and how the emergence of powerful House of Commons select committees in the early 1980s has been an 'important constitutional evolution'. And since 2010, the chairs of those committees are elected by the House of Commons rather than party managers. Tucker reflects upon this development and concludes that "it would be no exaggeration to say that the growth of the UK's regulatory state and of the standing of parliamentary committees has been symbiotic".

The Treasury Committee chooses its own subjects of inquiry. Depending on the subject, external deadlines, and the amount of oral evidence the Committee decides to take, an inquiry may last for several months and give rise to a report to the House; other inquiries may simply consist of a single day's oral evidence which the Committee may publish without making a report. When the Committee has chosen an inquiry it normally issues a press notice outlining the main themes of inquiry and inviting interested parties to submit written evidence. It may also identify possible witnesses and issue specific invitations to them to submit written evidence. The House has given

The Treasury Committee of the House of Commons is a multi-partisan committee made up of 11 members. The members of the Treasury (Select) Committee are elected representatives of the House of Commons appointed by the House of Commons, which also elects the chair of the Committee. Differently from the ECB and the Federal Reserve System, the Bank of England Governor participates to the hearings together with other members of the MPC. While the Treasury Committee has sole statutory authority to scrutinise the BoE, also the Economic Affairs Committee of the House of Lords holds hearings with the Bank of England. It holds regular hearings with MPC members on the Bank of England's Quarterly Inflation Report and with FPC members of the Bank on the Financial Stability Report⁶³. The role of the TSC in the appointment process of the Governor and other senior officials has become more 'muscular' in recent years. For example, the debate around the appointment of Charlotte Hogg as deputy governor (conflicts of interest) is an example of this vetting process since the publication of the TSC report (under the strong chairmanship of Andrew Tyrie) led to her resignation.⁶⁴

The Economic Affairs Committee of the House of Lords is usually made up of thirteen members, appointed by the House for each Session of Parliament. It holds less hearings than TSC. The EAC's main function is to examine matters within its remit with which Parliament ought to be concerned, and to report to the House of Lords with recommendations for government action. Each inquiry leads to a report, published together with the evidence on which it is based, setting out the committee's findings and making recommendations to the Government and others.⁶⁵

Members of the EAC and TSC need to have a good understanding of monetary and financial matters as, otherwise, the control would simply be ineffective. And in order to properly perform this they need time, information and resources.⁶⁶

the Committee the power to send for "persons, papers and records". It therefore has powers to insist upon the attendance of witnesses and the production of papers and other material. These formal powers are rarely used.

⁶³ The TSC established separate hearings for the members of the newly created Financial Policy Committee to discuss the Financial Stability Report. See Fraccaroli et al. (2020).

According to Cheryl Schonhardt-Bailey (2015): "With respect to the partisan composition of select committees, the membership reflects the proportional partisan balance in the House of Commons, so that a government majority will translate into a majority of members on each of the select committees. The committee chairmanships are, moreover, allocated among the main parties (Conservative, Labour, Liberal Democrat—and, since 2015, SNP), in proportion to the partisan balance in the House. From 2010, they have been elected from the whole membership of the House of Commons. In contrast, committee members are elected by their own party cohorts. An important feature of British select committees is that, in contrast to many legislative committees elsewhere in the world, they do not explicitly consider legislation. Instead, the normal committee stage of the legislative process is left to temporary and non-specialist "public bill committees" (Russell and Benton 2011: 11). Thus select committees do not scrutinize government legislation but rather oversee government departments. In order to effect this oversight, frontbench ministers and opposition spokespersons are usually not members of select committees. Reforms enacted in 2010 have further solidified this independence of select committees (Russell and Benton 2011; Gordon and Street 2012; Kelso 2012) (...). "[D]eliberation must entail a critical review of the decisions of the witnesses giving testimony across all relevant issues".

⁶⁴ Financial Times (14 March 2017): "[New BoE deputy governor Charlotte Hogg resigns after damning report](#)".

⁶⁵ Cheryl Schonhardt-Bailey, above note, points out that "the EAC is a relatively new committee, growing from ad hoc status in 1998 (to monitor the new MPC, as the Blair-Brown Labour Government made the Bank independent) to permanency in 2001". She also notes that "Committees in the House of Lords operate quite differently from those in the House of Commons. Most importantly, Lords committees do not scrutinize government departments in the way that Commons committees do. Instead, Lords committees are more thematically constructed, focusing on four main areas—economics, Europe, science and the UK constitution. And, because individuals typically become peers based on years of experience and excellence in their fields, committees in the upper house typically exploit this expertise in the composition of committee memberships. (For instance, a key member of the Economic Affairs Committee in the 2010-15 Parliament was Nigel Lawson, Baron Lawson of Blaby, who served in the Thatcher Cabinet, ultimately as Chancellor of the Exchequer). Whereas since 2010, members in Commons committees are elected with party groups and chairs are elected in a secret ballot by the whole chamber, members of committees in the Lords are appointed by more traditional means—namely, via the whips. Broadly speaking, investigative committees in the Lords have a reputation for investigating issues that are both "more strategic" and "more technical"—thereby reflecting the expertise of their members (Russell 2013: 210). In a recent comparison of Commons and Lords committees, Russell has described the latter as "less adversarial" in hearings with experts (Russell 2013: 211)". Russell (2013) also notes that while the Treasury Committee is officially responsible to hold the BoE accountable for its policy, the Economic Affairs Committee focuses more on issues related to administration, clarification and simplification.

⁶⁶ Cheryl Schonhardt-Bailey (2015), above note: "While Russell describes the division of responsibility between the TSC and the EAC as 'not necessarily clear,' she maintains that the official role of the former is to cover policy while the latter focuses on 'technical issues of administration, clarification and simplification' (Russell 2013: 216-17). So, while the TSC clearly retains the formal responsibility for economic policy oversight, it is less clear where, exactly, the EAC contributes to the broader rubric of holding the Government to account for economic policy. If, however,

An efficient mechanism that, in my opinion, could enable MPs to successfully perform this task, would be the creation by the Treasury Committee of a sub-committee with the specific role of monitoring the Bank of England.⁶⁷ Of course this mechanism of control could only work properly if the members of such a sub-committee have “the technical expertise required to deal with monetary matters” and are multi-partisan, on the very assumption that “accountability requires knowledge”.⁶⁸ MPs who are members of the Committee (or sub-committee), are meant to act as a “filter for the house in holding the Bank of England accountable to Parliament”.⁶⁹

In his excellent book, Paul Tucker⁷⁰ compares the MPC in the UK, the Federal Open Market Committee (FOMC) in the US and the Governing Council in the ECB (Chapter 11), linking this comparison to the adequacy of parliamentary oversight committees (Chapter 15). Drawing on his own personal experience, he points out that the strength of the MPC in the UK lies on the exploration of arguments “with fellow experts before voting” (p. 264) and that, on “that basis”, both FOMC and ECB Governing Council “are too large” (p. 265). Committees with one person-one vote help identify the issues where parliamentary oversight committees should ask questions and thus facilitate public debate. While the parliamentary hearings in the US Congressional committees⁷¹ in the case of the Federal Reserve System and ECON in the case of the ECB “are centered on the chair” (Chairman of the Federal Reserve and President of the ECB), in the UK “typically four or five members of the Bank of England policy committee attend a hearing” (p.374). Tucker further points out: “This is not ‘testimony’ in the sense of an occasion for the chair to read out a long essay, which would often be unwelcome as Treasury Committee members (...) want to use the time to ask the Bank about material (e.g., an Inflation Report) that is already in the public domain. To be clear, it is not always comfortable for the central bankers on parade: the ‘hunting the pack’ metaphor can be apposite. But the hearings are invariable occasions when the UK central bankers find an opportunity, if they wish, to raise their own questions and ideas about the regime” (p.374).⁷²

3.6. Relationship with the HMT and ‘override powers’

The relationship between and independent central bank and the executive is always a difficult balancing act in the design of accountable independence. The importance of independence arises from the need to insulate from partisan political influence the pursuit of monetary policy and financial stability.

With regard to monetary policy, the Bank of England is meant to put in place measures with a view to reaching the inflation target set by the Chancellor, which “provides a clear quantifiable indicator”.⁷³ By

Russell's depiction is correct, an investigation of the content of the hearings for each committee should observe more of a focus on policy in the TSC and a more administrative focus in the EAC.” See also Lastra (2011), 20.

⁶⁷ See Lastra, *Accountability of the Bank of England*. First Report. House of Commons – Treasury Committee, Session 1997-1998, London, 27 October 1997, 28-29, when I was asked to submit written evidence to the House of Commons Treasury Committee with regard to its inquiry into the parliamentary accountability of the Bank of England back in 1997, I advocated that the Treasury Committee could appoint a sub-committee with the specific task of monitoring the Bank of England. The sub-committee should be chaired by an opposition MP.

⁶⁸ See Lastra (2011) also suggesting that this sub-committee should have either three or five members.

⁶⁹ See Lastra, *Accountability of the Bank of England*. First Report. House of Commons – Treasury Committee, Session 1997-1998, London, 27 October 1997, 28, emphasising that the members of the Committee should explain in clear terms to the House whether the Bank has managed to achieve its goals or not.

⁷⁰ Tucker, above note. The point about the size of ECON is in page 299, as part of a discussion of how incentives are structured.

⁷¹ In the US, Monetary Policy Reports (previously referred to as Humphrey-Hawkins reports) require the Federal Reserve to formally report on its activities to Congress. The Chairman of the Board of Governor is called on to offer oral testimony about the report to the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on Financial Services of the House of Representatives.

⁷² Tucker cites (p. 374) Schonhardt-Bailey's comparative study on “Monetary Policy Oversight” (fn 41).

⁷³ Id., 21.

contrast, in the area of financial stability the absence of universally accepted specific targets complicates performance accountability.

The relationship between the HMT and the Bank of England is based on cooperation and coordination between the two. “Accordingly, there is a broad suite of formal and informal mechanisms to manage when different views on issues of policy or a course of action to be taken emerge”.⁷⁴

The Bank of England operates in accordance with a statutory framework set by Parliament. Such a framework is designed to ensure that the Bank is free from day-to-day political influence and direction. Still, coordination becomes particularly important in areas placed at the border between fiscal policy, monetary and financial stability.

In this regard, a review on the monetary policy framework conducted by HMT in 2013 “highlighted that the development of new unconventional instruments (such as Quantitative Easing) should include consideration with Government of appropriate governance and accountability arrangements to ensure that the respective objectives of the government and central bank are clear and transparent”.⁷⁵ The need for such fiscal and central bank coordination in relation to such instruments is important because the instruments risk blurring the line between monetary and fiscal responsibilities, as such policies can (1) involve credit risk (which ultimately has implications for the taxpayer as governments back the public sector balance sheet) and (2) influence credit allocation (which raises the question about the appropriate role of central banks in such decisions).⁷⁶

Furthermore, a wide range of supporting coordination mechanisms are in place between HM Treasury and the Bank, both specifically in relation to the three statutory committees and also more generally.⁷⁷

However, in specified circumstances, HM Treasury has a set of backstop legal powers to override—specifically to ‘direct’—the Bank of England. As explained by Salib and Skinner, the powers of direction that HM Treasury has over the Bank of England include a general power of direction “in the public interest”, introduced as part of the post-war legislation that took the Bank into public ownership in 1946;⁷⁸ a reserve power over monetary policy “in extreme economic circumstances”, retained by the Treasury at the time the Bank was granted operational responsibility for monetary policy in 1998 (and subject to stringent triggers as well as procedural and transparency requirements)⁷⁹ and a specific

⁷⁴ See Salib and Skinner (2019), p. 920.

⁷⁵ HM Treasury (2013), [Review of the Monetary Policy Framework](#), Cm. 8588, at 4–5 (UK).

⁷⁶ See Salib and Skinner (2019), p. 922, who argue that ‘a practical example of such coordination is the public exchange of letters between the Bank and HM Treasury when the Bank commenced gilt purchases via its Asset Purchase Facility in 2009. See [letter](#) from Alistair Darling, Chancellor of the Exchequer, HM Treasury, to Mervyn King, Governor, Bank of Eng. (29 January 2009); [letter](#) from Alistair Darling, Chancellor of the Exchequer, HM Treasury, to Mervyn King, Governor, Bank of England (3 March 2009). The letters set out the monetary policy purposes and operation of the facility, and the delegation of the instrument of asset purchases financed by the issuance of central bank reserve to the MPC. HM Treasury also undertook that “the Government will not alter its issuance strategy as a result of the asset transactions undertaken by the Bank of England for monetary policy purposes.”

⁷⁷ Id., 923–924, making the example of an HM Treasury official being permitted to attend and speak at MPC and FPC meetings, yet without voting rights. Additionally, there are formal memoranda of understanding explaining the financial relationships between the two Institutions and their responsibilities regarding resolution planning and financial crisis management.

⁷⁸ Section 4 of the Bank of England Act of 1946, through which the Bank was nationalised, provided for the Treasury’s legal power to direct the Bank. It stated simply that “the Treasury may from time to time give such directions to the Bank as, after consultation with the Governor of the Bank, they think necessary in the public interest”. Notwithstanding its broad formulation there was “an implicit understanding within HMT that it would show considerable restraint in ever resorting to the power and that directions could only be properly made on matters of major policy in respect of which no Governor could fail to acknowledge the right of the Government to decide”. In 1998 the power of direction was amended to include the following limiting caveat “except in relation to monetary policy”. Partly through these six words, the Bank of England was given operational independence over monetary policy. By contrast, in place of the general power of direction, HM Treasury was granted a tightly constrained “reserve power” in the field of monetary policy. Since 2017 HM Treasury has been “precluded from using the 1946 power of direction in relation to the Bank’s functions as the Prudential Regulation Authority”. Id., 924–925.

⁷⁹ Id., 930. The extension of the general HMT’s power of direction “in the public interest” became problematic at the end of the 1990s, since the Labour Government was committed to give the Bank full independence in the area of monetary policy. This goal was achieved through removing monetary policy from HM Treasury’s general power of direction. The Bank of England Act 1998 indeed introduced in

power of direction introduced in Section 61 of the Financial Services Act 2012 (and separate from the general power under the 1946 Act) as a crisis-management tool where public money is at risk, introduced as part of post-crisis legislative reforms.⁸⁰

its place a highly constrained “reserve power”, about which the then Chancellor Gordon Brown explained that he expected the override power “to be exercised rarely, if at all”. This is unsurprising since the reserve power effectively nullifies independence. The reserve power provides that “HM Treasury, after consultation with the Bank, may direct the Bank with respect to monetary policy only if HM Treasury is satisfied that the direction is required in the public interest and by extreme economic circumstances”. “The direction can be immediately effective, but it is time-limited. It ceases to be law within twenty-eight days unless both Houses of Parliament hold a debate and each approve it by resolution, and even then, the direction can only last for a maximum period of three months. While the direction is in effect, the statutory objectives regarding monetary policy do not have effect. The direction can also be used to make consequential modifications to the legislation to relieve the MPC from having to comply with its usual procedural requirements, which may be a hindrance in a time of crisis”. What constitutes an “extreme economic circumstance” has intentionally been left undefined, but the use of the word “extreme” suggests the existence of war or a very severe economic emergency or crisis, of the “once in a lifetime” variety and therefore it sets a much higher bar than “in the public interest”. Id., 930-931.

See also <https://publications.parliament.uk/pa/cm201012/cmselect/cmtreasy/874/87409.htm>.

⁸⁰ Id., 913-914. These powers and their extension have led commentators to argue that “the Bank of England’s independence from HM Treasury is a complicated affair, and one which has evolved over time in a piecemeal fashion”.

4. THE EUROPEAN CENTRAL BANK

4.1. Accountability of the European Central Bank

The European Central Bank is a relatively “young” central bank. Its independence is enshrined in the Treaty on the Functioning of the European Union (TFEU) in Article 130, which gives it a very strong legal protection, stronger indeed than that afforded to other central banks around the world with statutory independence (whereby one statute may be removed by another). The ECB is *sui generis* in that it is the central bank of the euro area, a jurisdictional area without legal personality. (The legal personality resides in the European Union, Article 47 Treaty on European Union [TEU], not in the euro area).

Since 1992, I have advocated the need for accountable independence of the European System of Central Banks (ESCB).⁸¹ An independent central bank is a particular kind of institution that is independent in some respects, but highly constrained in others: constrained by the goal (established in the law: the Treaty in the case of the ECB, a statute in the case of the Federal Reserve System and Bank of England) and by the demands of democratic legitimacy and accountability.⁸²

In order to assess how the accountability of the ECB in the conduct of monetary policy can be improved, we must assess the current accountability channels.

The accountability of the ECB is ‘diversified’ in line with the traditional articulation of accountability discussed in the introduction (*trias politica*).

First and foremost, the ECB is accountable to the European Parliament according to Article 284 (3) TFEU and Article 15 of the ESCB Statute.

Secondly, the ECB is subject to judicial review by the Court of Justice of the European Union (CJEU), which is the only Court that can judge the legality of the acts and decisions of the ECB according to Article 263 TFEU and Article 35 of the Statute of the ESCB.

Thirdly, the ECB is subject to audit control. There are different layers of audit control. First of all, an external auditor firm has the “full power to examine all books and accounts of the ECB and NCBs” (Article 21.1 of the Statute of the ESCB).⁸³ Secondly, the European Court of Auditors examines the operational efficiency aspects (Article 27.2 of the Statute of the ESCB).⁸⁴ In addition, there is internal audit by a high-level Audit Committee – established by the Governing Council pursuant to Article 9b of the Rules of Procedure of the ECB. The latter enhances the corporate governance of the ECB and the Single Supervisory Mechanism (SSM), covering both central banking and banking supervisory functions, and the Eurosystem.⁸⁵

⁸¹ Lastra (1992).

⁸² See Lastra and Miller (2001).

⁸³ The ECB external auditor is Baker Tilly, see [recommendation](#) on its appointment.

The report of the external auditors is published together with the annual accounts, see page 62 of the 2019 [annual report](#).

⁸⁴ The [European Court of Auditors](#) is one of the 7 EU institutions. It was set up in 1975 as guardian of EU finances.

The European Court of Auditors submit the previous year’s audit reports to the Parliament and the Council every year. The Parliament decides whether to approve the Commission’s budget after reviewing the Court of Auditors’ report. If the Court of Auditors considers the execution satisfactory, it sends a report to the Council and the Parliament mentioning that the European taxpayers’ funds have been properly used. Finally, the Court of Auditors also discusses proposals on EU financial legislation and EU anti-corruption actions. If auditors detect any corruption or irregularity, they notify the European Anti-Fraud Office (OLAF).

When it comes to supervisory data, the ECB and ECA signed an [MOU on Banking supervision in the EU](#).

⁸⁵ Amongst its responsibilities, the [Audit Committee](#) shall receive, at the same time as they are transmitted to the Governing Council, (i) the annual audit opinion on the ECB’s financial statements; (ii) the management letter of the ECB’s external auditor, together with the Executive Board’s response; (iii) the preliminary observation report of the European Court of Auditors (ECA), together with the Executive Board’s response; and (iv) an advance copy of the ECA public report before its publication. See [Audit Charter](#).

Finally, there are also mechanisms of accountability *vis-à-vis* the Council and the Commission, in line with Article 284(3) TFEU and Article 15 ESCB Statute (see Annex).

The cooperation with ‘the executive’ is *sui generis* given the fact that only responsibility for monetary policy (but not fiscal policy) has been transferred from the national to the supranational arena and that, therefore, the ECB has no European fiscal counterpart in the sense that there is [at least not yet] a Euro Treasury or Euro Minister of Finance. The fiscal counterparts remain national; fiscal policy remains decentralised at the level of the Member States, albeit subject to EU rules. The ECB is also accountable to the public and ways to enhance ECB transparency are further discussed below.

The overall accountability of the ECB as the central bank of the euro area needs to be examined in the context of the developments of the GFC and its aftermath, as the ECB has gained additional powers (in the area of supervision) and the impact of its main basic task has changed (effects of unconventional instruments of monetary policy).

4.2. The relationship between the European Central Bank and the European Parliament

On monetary policy, the European Parliament holds the ECB accountable⁸⁶ through the following activities:

1) Monetary Dialogue

The Monetary Dialogue is by far the most important measure of parliamentary accountability in the EU/euro area, a mechanism for the ECB to explain and justify its discretionary decisions in front of the Members of the European Parliament (providing also a source of formal legitimacy). The ECB President⁸⁷ participates in quarterly hearings of the ECON Committee of the European Parliament.⁸⁸ During these quarterly hearings, the President of the ECB delivers a statement on the ECB’s monetary activities and decisions and answers questions from Members of the European Parliament (MEPs) attending the hearing based on reports prepared by an expert panel.⁸⁹

All political groups are represented in ECON.⁹⁰ Other Executive Board members also participate in hearings of this ECON committee to explain the ECB’s reasoning and decisions on specific topics.

The primary law basis for the Monetary Dialogue is Article 284(3) TFEU. The Protocol on the Statute of the ESCB and of the ECB reasserts accountability to the European Parliament in Article 15(3). Formally, the Monetary Dialogue was set up by the European Parliament’s Resolution on “democratic accountability in the third phase of EMU of 4 May 1998” which called for the organisation of a dialogue between the European Parliament and the future ECB on monetary and

⁸⁶ See Fraccharoli et al. (2020). See also Fraccharoli et al. (2018).

⁸⁷ The ECB has had 4 Presidents so far: Wim Duisenberg (1998-2003), Jean-Claude Trichet (2003-2011) and Mario Draghi (2011-2019) and Christine Lagarde (2019 -).

⁸⁸ Through the prism of a principal-agent relationship, the principal is the holder of sovereignty, namely the Euro-area citizens through their elected representatives (European Parliament), and the agent is the ECB. ECB (2002; 45-46): “An integral part of this (...) relationship between principal and agent are provisions on accountability, *i.e.* mechanisms by which the principal holds the agent responsible for its performance. To that end, a system of appropriately designed incentives must be in place”.

⁸⁹ The Monetary Expert Panel has produced papers on related topics to accountability on three previous occasions: in November 2005, in [September 2009](#) and in [March 2014](#). In March 2009, the European Parliament commissioned a study on “Accountability and Transparency in Central Banking”, written by Paul de Grauwe and Daniel Gros.

⁹⁰ Pursuant to [Rule 209](#) of the Rules of Procedure of the European Parliament.

economic affairs, the framework for which dialogue should be confirmed through a mutual agreement.⁹¹

2) Annual Report

"The ECB submits an annual report on its tasks, the activities of the ESCB and the Eurosystem's monetary policy to the European Parliament, the Council of the EU, the European Commission and the European Council. The report is presented annually to the European Parliament by the ECB President in a dedicated session of the ECON Committee and by the ECB President on the occasion of a plenary debate. The annual accounts of the ECB are part of the annual report."⁹²

The primary law basis for the presentation of annual reports is Article 284(3) TFEU.⁹³

3) Parliamentary written questions

All Members of the European Parliament (not just ECON members) can address written questions to the ECB, with the aim of clarifying the central bank's motives and reasoning underlying a certain policy decision. The answers to these questions are signed by the ECB President and published on the ECB's and the European Parliament's websites.

There is no legal basis in the Treaty for these written questions. The applicable norm is Rule 140 of the Rules of Procedure of the European Parliament.⁹⁴

The European Parliament is also involved, in a consultative role, in the appointment procedures for the members of the ECB's Executive Board (and it has a veto right in the case of the Chair and Vice Chair of the Supervisory Board).⁹⁵ In contrast to the ECB's supervisory function, beyond the Treaty provisions, there is no interinstitutional arrangement that formalises the ECB's accountability *vis-à-vis* the Parliament in the area of monetary policy.⁹⁶

In the course of 2020, the ECB Governing Council has adopted an unprecedented package of monetary policy measures⁹⁷ to address the fallout of the COVID-19 crisis. This, together with the legal ramifications of the 5 May 2020 decision of the German Constitutional Court and other possible legal challenges in the future call for the reaffirmation and enhancement of the appropriate levels and mechanisms of scrutiny of monetary policy in the euro area, in line with the legal framework established by the Treaty.⁹⁸

With the growing complexity and expansion of central bank responsibilities in the monetary sphere, effective parliamentary scrutiny becomes ever both more important and more challenging, in particular given the distributional and other effects of monetary policy operations.⁹⁹

⁹¹ See European Parliament (1998), "[Resolution on democratic accountability in the third phase of EMU](#)". See also Rule 135 of the Rules of Procedure of the European Parliament in Annex.

⁹² ECB website, "[Accountability](#)".

⁹³ See also Article 15 of the ESCB Statute and Rule 135 of the Rules of Procedure of the European Parliament (Statements by the ECB) in Annex.

⁹⁴ See Rule 140 of the Rules of Procedure of the European Parliament (Questions for written answer to the European Central Bank) in Annex.
⁹⁵ See Rakic (2019).

⁹⁶ The ECB accountability in the discharge of banking supervision since the advent of banking union is subject to a specific regime set down in the SSM Regulation. How the supervisory accountability requirements are to be fulfilled in practice is clarified in an interinstitutional agreement between the European Parliament and the ECB and a MOU between the Council of the EU and the ECB. This paper deals with the "monetary dialogue", not with the "banking dialogue" (where the SSM, SRM and the pursuit of financial stability are subject to account). See inter alia Amtenbrink (2019).

⁹⁷ See Rakic (2020).

⁹⁸ Through the prism of a principal-agent relationship, the principal is the holder of sovereignty, namely the euro area citizens through their elected representatives (European Parliament), and the agent is the ECB. See ECB (2002; 45-46).

⁹⁹ The notion that very low interest rates and QE have fuelled a surge in asset prices, which mostly benefits the wealthy, has become quite prevalent. See e.g., Cohen-Setton (2014). "[The distributional effect of quantitative easing](#)". Bruegel blog post 29 October 2014. Paul Tucker

European Parliament/ECON accountability ought to be strengthened to match the expanded range of instruments the ECB uses in the conduct of monetary policy.

4.3. Locus of parliamentary accountability

The adequate locus of accountability for the ECB regarding the conduct of its monetary policy responsibilities resides at the European level, not at the national level. Thus, accountability should be discharged in a way that is congruent with the principle of conferral. Monetary policy is an exclusive competence of the ECB.¹⁰⁰ This is in line with EU law, with the transfer of sovereign monetary powers to the supranational arena and the legitimacy of the Union mechanisms.

The following argument made by the ECB in 2002 remains valid in my opinion:

“[T]he ECB has taken the view that a system of individual accountability of the members of the Governing Council and the Executive Board would be inconsistent with the institutional structure and policy substance. For instance, a system whereby all the members of the Governing Council were held individually accountable by the European Parliament would be inconsistent in the case of the National Central Bank (NCB) Governors, since no EU body plays a role in their appointment. At the same time, neither would it be coherent for NCB Governors to give account of their actions as members of the Governing Council to their national parliaments, as national parliaments would lack the legitimacy to judge how NCB Governors perform their “European” duties – duties which explicitly preclude them from acting as defenders of national interests. From this it follows that the decision-making bodies of the ECB are held collectively accountable for all decisions which they take and it is for the President of the ECB and the other members of the Executive Board to justify and explain the decisions taken collectively to the European Parliament.”¹⁰¹

Recent developments following the May 2020 decision of the German Constitutional Court, and subsequent delivery of a set of confidential documents by the ECB via the Bundesbank to the Bundestag, which then issued a positive opinion on proportionality, raise some concerns from the perspective of the appropriate locus of accountability, since a national legislature (the German Bundestag) was given non-public documents related to the PSPP before the European Parliament.¹⁰²

The response from President Lagarde to a question from Sven Simon, MEP regarding the PSPP judgement,¹⁰³ emphasises the central role that the dialogue with the European Parliament plays in the design of the accountability of the ECB. The speech by Yves Mersch, “In the spirit of European

wrote in his comments that, given that the interest rate is probably close to the facto zero lower bound, he would have combined very easy monetary policy with a macro prudential increase in margin requirements, in order to dampen exuberance in shadow banking markets. Paul Tucker also noted in his comments that over-reliance on monetary support (as opposed to fiscal support) creates risks for financial stability.

¹⁰⁰ Article 282 and Article 127 TFEU. Article 3.4 of the Treaty on European Union and Article 5 as regards the principle of conferral leave no doubt about the exclusive nature of monetary policy.

¹⁰¹ ECB (2002).

¹⁰² It is also a matter of concern that there are some talks that the Bundestag is planning to organise its own “Monetary Dialogues”, Bundestag (2020), [press release](#), 11 September 2020.

¹⁰³ [Letter](#) by President Lagarde to Sven Simon of 29 June 2020 (regarding the PSPP).

*“Regarding your question on the judgement of the German Federal Constitutional Court, the ECB has taken note of the judgement. (...) In line with the **principle of sincere cooperation**, the Governing Council has decided to accommodate this request and to authorise the Deutsche Bundesbank to disclose these documents to the German Federal Government, provided that the non-public elements are treated confidentially. On the same condition, the German Federal Government may share the documents if need be with the German Parliament. As I have said before, **the dialogue between the ECB and the European Parliament is an essential element of the ECB’s accountability**. I thus look forward to continuing discussing with the European Parliament the substance of our monetary policy actions, as also covered in the aforementioned documents and the many types of document that we publish on a regular basis”.* (Emphasis added)

cooperation” of 2 July 2020¹⁰⁴ notes that “In this spirit, the ECB – which is exclusively subject to the jurisdiction of the Court of Justice of the European Union and accountable to the European Parliament – supports the Deutsche Bundesbank in its cooperation with the German Federal Government and the Bundestag.” But there was and there is no obligation.

Draghi’s practice of visiting national parliaments to explain the ECB’s monetary policy decisions, engaging in an ‘exchange of views’ with elected representatives,¹⁰⁵ should not be seen as an obligation (not even a soft obligation) to be accountable to national parliaments.¹⁰⁶ It should simply be seen, in the spirit of cooperation mentioned above, as educating European citizens about the role of the ECB.

It should also be noted that while proportionality is also a mechanism that facilitates transparency and accountability, it needs to be channelled through the established adequate institutional channels. And that these reside at the EU level. This is also in line with the principle of democracy, a founding value of the EU according to Article 2 TEU.¹⁰⁷

The Court of Justice of the EU in its *Weiss* ruling held that the proportionality principle should apply to determine the legal limits on the use of monetary policy action and that proportionality requires that the instruments chosen are ‘necessary’ to achieve the price stability objective. The ECB may thus be called to justify in front of the Court that the measures adopted to fight the pandemic are *necessary* to ensure the effective functioning of its monetary policy and to meet the price stability objective.¹⁰⁸

The topic of ECB accountability, at the core of the September 2020 Monetary Dialogue, is again very topical and important for the future of the ECB and for the future of the EU.

4.4. Ways of improving the Monetary Dialogue

The Monetary Dialogue is an essential mechanism of accountability in the life of the ECB.¹⁰⁹ A number of studies have looked at the history of the Monetary Dialogue, its efficacy and evolution.¹¹⁰

It is interesting to observe that the name ‘Monetary Dialogue’ does not convey the spirit of scrutiny, of giving account, explain and justify that is at the core of accountability. I would recommend that the ‘monetary dialogue’ be renamed as ‘monetary hearings’, as proposed earlier by Guillermo de la

¹⁰⁴ Mersch (2020). “In the spirit of European cooperation”. Introductory remarks by Yves Mersch, Member of the Executive Board of the ECB and Vice-Chair of the Supervisory Board of the ECB, at the Salzburg Global webinar, 2 July 2020.

There was a similar debate about this when, during the sovereign debt crisis, President Draghi made seven visits to national parliaments between 2012 and 2017. See Tesche (2018).

¹⁰⁵ Bovens and Curtin (2016).

¹⁰⁶ This is different from Articles 20 and 21 of the SSM Regulation in the exercise of prudential supervision.

¹⁰⁷ Article 2 of the Treaty on European Union firmly establishes the values upon which the Union is founded: respect for human dignity, freedom, democracy, equality, the rule of law and respect for human rights, including the rights of persons belonging to minorities. These values are common to the Member States in a society in which pluralism, non-discrimination, tolerance, justice, solidarity and equality between women and men prevail.

¹⁰⁸ Lastra and Alexander (2020), id.

¹⁰⁹ Fraccaroli et al. (2018): “A study published in 2004 found that the frequency of the ECB’s appearances before the European Parliament exceeds the average of appearances by other central banks before their respective parliaments. In addition, ECB Executive Board members have participated on numerous occasions in hearings of the ECON committee to explain the ECB’s reasoning and decisions on specific topics”.

¹¹⁰ Collignon and Diessner (2016) note that “Political accountability is a multi-level process. While the European Parliament holds the ECB to account, electors do likewise with MEPs.” They report on the performance of the members of ECON during the seventh parliament and presents answers to a questionnaire submitted to all members of the committee inquiring how they assessed the dialogue themselves. “The seventh parliamentary ECON committee had 99 members, of whom 50 were full members and 49 were substitutes (with some participants having been replaced over time, thus marking a total of 110 MEPs). Of all those, 43 never asked a question during the five-year term of the parliament. With respect to those who have intervened, the average number of questions per session asked by all MEPs was 22.5. (...) The ECON committee was made up of 67 per cent euro area and 32 per cent non-euro area MEPs. Members from the euro area asked 79 per cent of all questions addressed to the ECB president. They found “that while the monetary dialogue may have had little or even negative impact on financial markets, it plays a significant role in informing and involving members of parliament and their constituencies”.

Dehesa.¹¹¹ “In contrast to the Congressional hearings of the chairman of the Fed, which are feverishly expected, widely reported and intensely scrutinised, the European media have long learnt that there will be no news and, understandably they devote little space, if any, to reporting on the Monetary Dialogue.”¹¹² By renaming the Monetary Dialogue as hearings, they would be treated less as a ‘lecture’ or statement by the ECB President to MEPs and more as an opportunity to explain and justify the actions and decisions taken.¹¹³

The Monetary Dialogue is particularly important when the ECB navigates through a crisis such as the GFC and more recently COVID-19. Crises give rise to extraordinary measures, leading to increased attention toward central banking policies¹¹⁴, making the scrutiny of monetary policy ever more necessary and ever more complex.¹¹⁵

The effectiveness of parliamentary hearings depends in part on the topics which are discussed.¹¹⁶ Though the tone of the debate¹¹⁷ need not be adversarial, it should befit the nature of the hearing, reflecting oversight, adequate deliberation and a duty by the ECB to explain and justify in front of MEPs how the ECB evaluates the effectiveness of its monetary policy operations (in particular when resorting to non-conventional instruments) and how it balances its primary and the secondary objectives in accordance with the Treaty requirements.¹¹⁸

Michelle Chang and Dermot Hodson¹¹⁹ contrast the European Parliament’s Monetary Dialogue which has run since 1998, with the Economic Dialogue, a forum launched in 2011 to hold EU institutions and Member States involved in EU economic governance to account. They argue that the Monetary Dialogue has helped to promote greater transparency over euro area monetary policy, although it would benefit from focusing on a narrower range of policy issues and closer cooperation between MEPs and that though the Economic Dialogue is a welcome addition to the EU’s economic governance architecture, its effectiveness has been limited due to a lack of resources and institutional constraints.

Chang and Hodson call for both the Monetary and Economic Dialogues to be delegated to a new ECON Euro Area Oversight Subcommittee (EAOS). I second the establishment of a euro area specialised

¹¹¹ This was also proposed by de la Dehesa (2009): “The ECON Committee should try to reach an agreement with the ECB President in order to transform the present Monetary Dialogue into a Monetary Hearing.”

¹¹² Id.

¹¹³ See also European Parliament (2014). “[Monetary Dialogue 2009-2014: Looking Backward, Looking Forward](#)”. Study for the Committee on Economic and Monetary Affairs, p. 32: “The practice, however, is less satisfactory. The President of the ECB appears before the ECON Committee with carefully scripted preliminary remarks, designed to shape the discussion. During the following Q&A part, he fields questions from any member of the Committee. The questions cover a bewildering range of issues and speakers can only ask one follow-up question. The result is an unstructured and often superficial exchange of views.”

¹¹⁴ Fraccharoli et al. (2020), 4.

¹¹⁵ Coeuré (2018).

¹¹⁶ European Parliament (2014). “[Monetary Dialogue 2009-2014: Looking Backward, Looking Forward](#)”. Study for the Committee on Economic and Monetary Affairs: “Earlier assessments of the Monetary Dialogue have often been critical. Academics have observed lack of forcefulness and insufficient qualification of MEPs; a tendency to talk cross-purpose; the absence of common grounds or concerns between ECB and EP, reinforced by the large size of the ECON; questions have covered less often monetary and more frequently fiscal policy; and on most issues the ECB holds the discursive monopoly. Nevertheless, in their study of previous parliaments, Eijfinger and Mujagic (2004) observed that in 71 % of the cases the ECB had implemented changes requested by ECON.”

¹¹⁷ Fraccharoli et al. (2020): “The tone of the deliberations may be driven by negative economic conditions, regardless of the central bank’s ability to cope with them and some politicians may assume a more aggressive tone for electoral reasons, regardless of the central bank’s performance in fulfilling the objective”.

¹¹⁸ In 2005, Anne Siebert noted in a [briefing note](#) for ECON at that “one issue that the European Parliament has been greatly interested in is the ECB’s attitude towards its secondary goal”. For a recent report, see Lastra and Alexander (2020).

¹¹⁹ Chang and Hodson (2019). They summarise “the monetary dialogue in action”: “It takes place four times a year, commencing with an introductory statement by the ECB president and followed by questions from the ECON MEP members.” A monetary expert panel (economists and a few lawyers) supports the work of ECON by providing briefing papers and studies on a range of issues related to monetary policy and suggesting questions that MEPs can ask during the Monetary Dialogue. “Since 2006, for each hearing two topics are identified for which the experts write papers.(...). **The dialogue is conducted between the ECB and individual MEPs.** Although MEPs speak on behalf of their constituents and, perhaps, their political group, they do not speak for the EP. The EP’s own-initiative report in response to the ECB’s annual report is more representative of the institution in this regard since it is voted on in plenary prior to the annual debate with the ECB president.”

subcommittee to scrutinise monetary policy. Size is an important consideration.¹²⁰ As stated above, I proposed in 1997 - in the context of an inquiry into the accountability of the Bank of England - that the House of Commons Treasury Committee should create a sub-committee with the specific role of monitoring the Bank of England and suggested that it be chaired by a member of the opposition (not of the ruling party).

The issue of technical expertise can be a double-edged sword,¹²¹ as politicians and MEPs (as well as judges) need not be trained in monetary affairs. But holding to account an independent central bank requires such technical expertise¹²² (as well as adequate resources). Populist movements have criticised the institutional tenets of central banks (technocracies) including the ECB. It has been observed that the change of public perception towards central banks might put their independence at risk.¹²³ Thus, the discussion about legitimacy and accountability is ever more relevant.

The European Parliament (ECON) should also have a formal enhanced role (not simply consultative) in the appointment procedure of the ECB President and other members of the Executive Board of the ECB. As stated in part 2 of this report, though the UK does not have a formal vetting/confirmation power (as opposed to the US), a negative 'opinion' by the TSC carries a heavy weight (the appointment of Charlotte Hogg as deputy governor of the Bank of England discussed above being a case in point). The role of the TSC in the appointment process of the Governor and other senior officials has indeed become more 'muscular' in recent years. Though the EP opinion carries 'heavy weight', as explained by Rakic, in the case of Yves Mersch, the Council appointed him nevertheless and the EP subsequently approved its appointment as Vice-Chair thus 'clearing' him.¹²⁴

Amtenbrink and Van Duin (2009) have argued that the EP has achieved a level of oversight for euro area monetary policy beyond that envisaged in the Treaty, even if doubts remain about whether the ECB is being held sufficiently to account. The fact that the minutes of the Monetary Dialogue and the expert reports are published in ECON's website – contributes in part to the success of the Monetary Dialogue.¹²⁵

4.5. Transparency

Though the Monetary Dialogue has contributed to provide both ex-post scrutiny by the EP and "an opportunity for the ECB to enhance its transparency" (Chang and Hodson) and, despite commendable

¹²⁰ European Parliament (2014). "[Monetary Dialogue 2009-2014: Looking Backward, Looking Forward](#)". Study for the Committee on Economic and Monetary Affairs, p. 33: ***'Given its size, the ECON Committee is a small parliament in itself. As befits a parliament, its members represent the whole spectrum of nationalities and political parties. All of them are allowed to attend and take part in the Monetary Dialogue. This means that it is not a dialogue at all: the President of the ECB addresses a large crowd. The very idea that the ECB is brought to account is absent from the start. The obvious solution would be that the President of the ECB only meets a subcommittee, with the other ECON members allowed to attend – possibly in reserved seats separate from those for the public at large – but not to intervene. Such an arrangement should be an internal matter for the Parliament to settle and should not require any new treaty.'***

¹²¹ A key rationale for independence (technical expertise) can also be a hindrance in terms of democratic accountability as politicians can find monetary policy too technical. This notwithstanding, those conducting the hearings should have an understanding of monetary affairs. See Clayes et al. (2014), *passim*.

¹²² Lastra and Goodhart (2017).

¹²³ Id. Reliance on "experts" (as the Brexit referendum evidenced) has become controversial.

¹²⁴ Rakic (2019). The Executive Board appointment procedure is set out in the Treaty on the Functioning of the European Union (TFEU), Article 283(2). The European Council has the power to appoint the board, after consulting the European Parliament and the ECB's Governing Council. The Parliament adopted its own rules to define internal procedures leading up to the adoption of a formal opinion (Rule 130, Rules of Procedure of the European Parliament). The Parliament has used this opinion-giving power to convey its positions on the candidates and the process itself. Greater democratic legitimacy in ECB appointment procedures has been advocated by Positive Money and Transparency International, recommending a formal EP confirmation role in the Executive Board appointments.

¹²⁵ Amtenbrink and Van Duin (2009).

efforts to become more transparent, the ECB been criticised for being an “unaccountable and opaque” institution.¹²⁶

As stated in Part 1 transparency has to do with the provision of information¹²⁷ and facilitates accountability. In an era in which communication and forward guidance have become an important tool of monetary policy, the central bank guides the markets.

Currently the ECB publishes:¹²⁸

- The [Economic Bulletin](#) (formerly Monthly Bulletin) which presents the economic and monetary information that form the basis for the Governing Council’s policy decisions. It is published eight times a year, two weeks after each monetary policy meeting.
- The Eurosystem’s consolidated [weekly financial statement](#) which provide information on monetary policy operations, foreign exchange operations and investment activities.
- The [press conferences](#) and the many press statements which the ECB holds after each Governing Council monetary policy meeting setting key interest rates for the euro area, i.e. every six weeks.
- The [monetary policy accounts](#) of the Governing Council’s discussions (which are published four weeks after each monetary policy meeting). These monetary policy accounts, which were introduced in 2015 during Draghi’s presidency, have been regularly published since then. The intention of these accounts is not to provide a verbatim transcript but rather a summary of the Governing Council members’ monetary policy discussions. When a monetary policy decision is taken, the President of the ECB makes an introductory statement to the press conference¹²⁹ and four weeks after the ECB publishes an account of the Governing Council’s monetary policy discussions to make the rationale behind the decisions more transparent.¹³⁰ The account typically begins with an overview of the financial market and economic and monetary developments. The ECB Governing Council’s discussions are then summarised, and economic and monetary analyses are presented along with the monetary policy viewpoints expressed. These monetary policy accounts do not report how individual members of the Governing Council voted or put names to comments made by individuals. Article 10.4 of the ESCB Statute prescribes that only the outcome can be published but not the minutes: “The proceedings of the meetings shall be confidential. The Governing Council may decide to make the outcome of its deliberation public.” Furthermore, the voting records are not published in order to protect the personal independence of the members of the Governing Council, who could otherwise be subject to undue political pressure from the country/countries where they come from. It is for these reasons (the requirement of Article 10.4 ESCB Statute, the protection of personal independence and a civil law tradition of not publishing dissenting opinions to reinforce collegiality) that the ECB does not publish the minutes, nor the voting records nor the dissenting opinions.

Effective audit control, as stated earlier in the case of the Bank of England, provides a basis and input for subsequent parliamentary scrutiny and can enhance transparency.

¹²⁶ Tesche (2019). See also Buiter (1999); Transparency International (2017). [“Two Sides of the Same Coin? Independence and Accountability of the European Central Bank”](#).

¹²⁷ According to its own [website](#): “Transparency means that the central bank provides the general public and the markets with all relevant information on its strategy, assessments and policy decisions as well as its procedures in an open, clear and timely manner. (...) Transparency helps the public to understand the ECB’s monetary policy. Better public understanding makes the policy more credible and effective.”

¹²⁸ See ECB website, [“Accountability”](#).

¹²⁹ See e.g., [introduction to the press conference](#) by President Lagarde on 16 July 2020.

¹³⁰ For the decision of 16 July 2020, see [‘monetary account’](#) of 20 August 2020.

5. CONCLUDING OBSERVATIONS

With independence comes accountability, hence the term 'accountable independence'.

Fabian Amtenbrink argued in his book¹³¹ that the existing democratic deficit of the European Central Bank is an expression of the democratic deficit of the EU at large, rather than a particular deficiency of the institution. In contrast, Chiara Zilioli¹³² has stated that the ECB is accountable if we use a new 'economic paradigm of accountability' rather than the traditional 'formalistic' notion of accountability based on the theory of the division of powers. Zilioli argues that the ECB is highly transparent and that it has developed both an inter-institutional dialogue and a dialogue with financial markets, thus facilitating the disclosure of information with regard to its activities and *modus operandi*.

When the ECB was created, it was influenced by the Bundesbank model of stability and independence. The Bundesbank Law contained few provisions regarding the accountability of the central bank, relying instead on the support of public opinion, consensus rather than dissent and the statutory objective to legitimise its existence in a democratic society. This contributes to explain, in my opinion, why accountability may have only played a 'subsidiary role' in the negotiations that led to the establishment of the ECB.

The independence of the ECB is anchored in the Treaty, granting it a greater level of protection than statutory central bank independence. The treaty is the result of a political compromise amongst sovereign states that have voluntarily transferred monetary powers – important attributes of sovereignty – from the national to the supranational arena. In contrast, in the UK (as well as in the US) it is possible to change the statutory framework of the Bank of England (or of the Fed).

The complexity that the ECB faces in the discharge of its monetary policy responsibilities arises from the fact that:

- The fiscal counterparty is not European, but national Ministries of Finance;
- There are different national interests;
- There are different national parliaments with different and conflicting interests; and
- The national governors are appointed at home, need to operate in the interest of the whole euro area, and can be put under pressure at home.

This jurisdictional complexity that the ECB confronts is not faced by the Bank of England in the UK nor by the Fed in the US and justifies the strong protection afforded to it by Article 130 TFEU.

Given the extension of monetary policy instruments post GFC and post Covid-19, the need for adequate accountability is of paramount importance for the future of the ECB and of European integration in the light of the distributional and other effects of monetary policy operations.

Due to the transfer of monetary powers (exclusive competence, principle of conferral) the locus of accountability is European, not national.

Accountability cannot be guaranteed by the fact that the initial stage of its creation is legitimate democratically. Accountability is judged through the life of the institution. "It is in its continuing operations and policies that the institution must be subject to appropriate mechanisms of accountability."

¹³¹ See Amtenbrink (1999).

¹³² See Zilioli (2003).

And if the ECB gives ‘proper account’, explains and justifies the actions or decisions taken (or omitted) in the exercise of its responsibilities, is subject to judicial review and to audit control”¹³³, and responds to the European Parliament through a meaningful Monetary Dialogue (renamed as Monetary Hearings) along the lines proposed in this report, then it can be judged to be sufficiently accountable. The jury is out!

¹³³ Lastra and Louis (2013).

ANNEX

Article 284 TFEU

1. The President of the Council and a Member of the Commission may participate, without having the right to vote, in meetings of the Governing Council of the European Central Bank. The President of the Council may submit a motion for deliberation to the Governing Council of the European Central Bank.
2. The President of the European Central Bank shall be invited to participate in Council meetings when the Council is discussing matters relating to the objectives and tasks of the ESCB.
3. The European Central Bank shall address an annual report on the activities of the ESCB and on the monetary policy of both the previous and current year to the European Parliament, the Council and the Commission, and also to the European Council. The President of the European Central Bank shall present this report to the Council and to the European Parliament, which may hold a general debate on that basis. The President of the European Central Bank and the other members of the Executive Board may, at the request of the European Parliament or on their own initiative, be heard by the competent committees of the European Parliament.

Article 15 of the ESCB Statute

- 15.1. The ECB shall draw up and publish reports on the activities of the ESCB at least quarterly.
- 15.2. A consolidated financial statement of the ESCB shall be published each week.
- 15.3. In accordance with Article 284 (3) of this Treaty, the ECB shall address an annual report on the activities of the ESCB and on the monetary policy of both the previous and the current year to the European Parliament, the Council and the Commission, and also to the European Council.
- 15.4. The reports and statements referred to in this Article shall be made available to interested parties free of charge.

Rule 134 of the Rules of Procedure of the European Parliament (Statements by the Court of Auditors)

1. In the context of the discharge procedure or of Parliament's activities in the sphere of budgetary control, the President of the Court of Auditors may be invited to make a statement to Parliament in order to present the comments contained in the Annual Report, special reports or opinions of the Court, or in order to explain the Court's work programme.
2. Parliament may decide to hold a separate debate, with the participation of the Commission and the Council, on any questions raised in such statements in particular when irregularities in financial management have been reported.

Rule 135 of the Rules of Procedure of the European Parliament (Statements by the European Central Bank)

1. The President of the European Central Bank shall be invited to present to Parliament the Bank's Annual Report on the activities of the European System of Central Banks and on the monetary policy of both the previous and the current year.
2. This presentation shall be followed by a general debate.
3. The President of the European Central Bank shall be invited to attend meetings of the committee responsible at least four times a year in order to make a statement and to answer questions.

4. If they or Parliament so request, the President, Vice-President and other Members of the Executive Board of the European Central Bank shall be invited to attend additional meetings.
5. A verbatim report of the proceedings under paragraphs 3 and 4 shall be drawn up.

Rule 140 of the Rules of Procedure of the European Parliament (Questions for written answer to the European Central Bank)

1. Any Member may put a maximum of six questions for written answer per month to the European Central Bank in accordance with criteria laid down in an annex to these Rules of Procedure (1). The content of questions shall be the sole responsibility of their authors.
2. Such questions shall be submitted in writing to the Chair of the committee responsible. On receiving such questions, the Chair of the committee responsible shall notify them to the European Central Bank. Issues concerning the admissibility of a question shall be decided by the Chair of the committee responsible. The questioner shall be notified of any such decision.
3. Such questions, as well as the answers to them, shall be published on Parliament's website.
4. If a question for written answer has not received a reply within six weeks, it may, at the request of its author, be included on the agenda for the next meeting of the committee responsible with the President of the European Central Bank.

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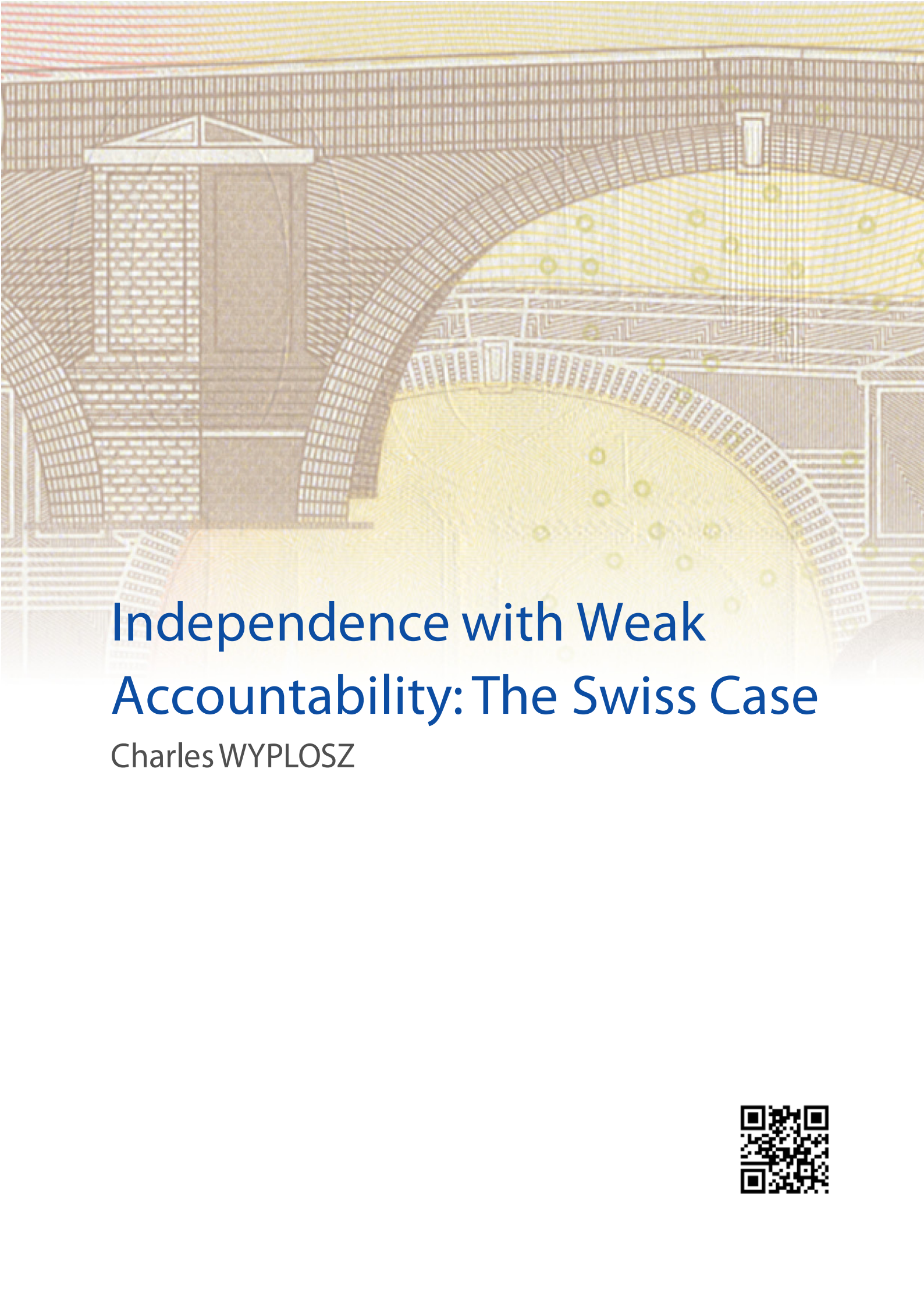
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Independence with Weak Accountability: The Swiss Case

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Abstract

The Swiss National Bank is highly independent but weakly accountable. Weak accountability is rooted in the formal legislation on central banking but also in the reputation of the Bank, which is unanimously considered as highly successful. The ECB too is highly independent and weakly accountable but it faces diverse public opinions whose views differ across countries. Buttressing ECB accountability is important, therefore, and the European Parliament should consider strengthening the Monetary Dialogue.

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CONTENTS

LIST OF ABBREVIATIONS	46
EXECUTIVE SUMMARY	47
1. INTRODUCTION	48
2. THE SWISS NATIONAL BANK	49
2.1. Legal status	49
2.2. Independence and accountability in practice	49
2.3. Inflation and accountability	51
2.4. Financial stability and accountability	53
2.5. Profits distribution	54
2.6. Evaluation	54
3. ACCOUNTIBILITY OF THE ECB	56
3.1. Comparison with the SNB	56
3.1.1. Formal differences	56
3.1.2. Public opinions	56
3.1.3. Performance	56
3.2. The challenges of accountability in the euro area	58
3.2.1. Many countries	58
3.2.2. Unclear performance	58
3.3. Relations with governments	59
3.4. The role of the European Parliament	59
3.4.1. The current situation	59
3.4.2. How could the EP exercise accountability?	59
3.4.3. Accountability and the broad public	60
4. SUMMARY AND CONCLUSIONS	62
REFERENCES	63

LIST OF ABBREVIATIONS

CPI	Consumer Price Index
ECB	European Central Bank
EP	European Parliament
ESCB	European System of Central Banks
FINMA	Financial Markets Supervision Authority
MEP	Member of the European Parliament
PEPP	Pandemic Emergency Purchase Programme
SNB	Swiss National Bank

EXECUTIVE SUMMARY

- **The SNB is formally independent and subject to weak accountability requirements.** In addition, on the basis of a strong track record, the consensus is that the SNB is delivering on its mandate. These two elements explain that there is hardly any debate about monetary policy in Switzerland. Experts may quibble with some decisions, but criticism is generally absent from debates within political and media circles and the broader public.
- **The accountability requirements from the ECB are rather weak too.** The ECB is accountable to the European Parliament whose powers are limited and the process, the Monetary Dialogue, is not particularly demanding. Yet, the need for effective accountability is much stronger in the euro area.
- **One reason is that public opinion is divided.** The decisions by the ECB can be simultaneously lauded and criticised, including by policymakers, financial market participants and even academics because of pre-existing prejudices.
- **Another reason is that the hearings of the President and of other members of the Executive Board before the Economic and Monetary Affairs Committee do not allow for precise and in-depth questioning.** In addition, MEPs frequently reflect in their interventions the views of their public opinions. Opposite views make it nearly impossible to focus on important but highly technical issues.
- **A more dynamic Monetary Dialogue would attract more attention from the media, which would translate into heightened public visibility.** It could well emphasise disagreements, which some may see as potentially dangerous.
- **Prejudices will not vanish soon but the European Parliament has a particular responsibility.** The Monetary Dialogue can be much improved by allowing an in-depth discussion of ECB actions.

1. INTRODUCTION

Consensus is rare in macroeconomics, so it is all the more remarkable that the institutional setup of central banks is widely agreed upon. With very few exceptions¹, it is generally accepted that strong theoretical and empirical evidence implies that central banks must be independent and that independence requires accountability.² However, while independence is simple to define and establish, accountability is more challenging, because it involves specific arrangements that must take national characteristics into account.

Serving independent states, each with its own specificities, the European System of Central Banks (ESCB) resembles a federal arrangement, as does the European Court of Justice. In both cases, decisions are taken without the involvement of Member States and they apply to the whole membership without further ado.³

For this reason, looking at central banks in federal countries is interesting. In many ways, the Swiss National Bank (SNB) is a special case. The Swiss Confederation is a highly decentralised system where cantons retain a large degree of independence in most domains, mainly excluding defence, foreign affairs (including international treaties) and, to some extent, justice or education. Taxation is split, with local tax income exceeding that of federal taxes, and public spending that benefits from an automatic transfer of resources, which are regularly renegotiated among cantons. The federal government is limited in size to seven ministers, who rotate annually to hold the Presidency of the Confederation. In addition, referenda and initiatives (proposals to valid laws or amend the Constitution) are organised regularly (usually four times a year) to contest parliamentary decisions, approve (and often disapprove) changes in the Constitution and international agreements, or propose changes to the Constitution. These referenda take place at the local, cantonal and federal level; in the latter case, approval requires a double majority of votes and cantons.⁴ As a result, the powers of (local, cantons and federal) governments and parliaments are weak.

When thinking about the ECB, it may be of interest to examine how the Swiss central bank operates in such a highly decentralised federation. However, there are important differences between the ECB and the SNB, including the continuing existence of national central banks in the euro area and the details of the accountability regimes. More important, perhaps, is the particular status of the SNB, which enjoys nearly total support in the country, which stands in contrast with national divergences among euro area Member States.

¹ The Modern Monetary Theory can be seen as fringe departure from the consensus.

² The literature is vast. A few key references are Alesina and Summers (1993), Grilli et al. (1991), Fischer (1995), Berger et al. (2001).

³ The recent decision of the German Federal Constitutional Court is a new development that might challenge this statement. This issue lies far beyond the topic of the present report.

⁴ Optional referenda, which are triggered by collecting signatures to oppose laws passed by Parliament, only require a majority of people.

2. THE SWISS NATIONAL BANK

2.1. Legal status

The SNB is a joint stock corporation with a modified status enshrined into a specific law. Its shares are held by the broad public, by the cantons and cantonal banks (owned by the cantons). There is an annual General Assembly of the shareholders but the Assembly's powers are limited. The bank is run by a three-member Governing Board. Oversight and control are entrusted to the eleven-member Bank Council appointed for four-year terms, with a maximum of 12 years. Six of the Council members are appointed by the federal government, the remaining five by the General Assembly of the shareholders. The three members of the Governing Board, and their deputies, are nominated by the Bank Council and appointed by the federal government for six years and can be reappointed indefinitely. The Federal government – officially called the Federal Council – chooses among them a President and a Vice-President. The members of the Governing Board and of the Bank Council cannot be removed from office unless they commit grave offense.

The Swiss Constitution establishes that the SNB is independent and tasked with price stability, oversight powers on banks and financial institutions to establish financial stability, and the production of financial statistics. Independence is described in no uncertain terms while the Constitution articles remain rather vague on the objectives.

Formally, the SNB must inform ahead of time the Federal government of its intentions and present an annual report to the Parliament. The report is also published. Finally, the SNB is also requested to inform the broad public.

The rights of the shareholders are strictly limited by the Central Bank Law. The General Assembly of shareholders can vote on proposals to change some items in the law. A proposal has to come from at least 20 shareholders. If approved by the General Assembly, the proposal goes to the Parliament. Proposals by shareholders may concern only the parts of the Law that deal with the SNB as a company (for instance there have been votes on the selection of auditors). The mission of the SNB is off limits.

2.2. Independence and accountability in practice

The current legislation was put in place in 2003. It mainly refined the policy objectives. Before that, the SNB had already enjoyed strong independence and was tasked with price stability. After the revision, the SNB specified that price stability is achieved when CPI inflation rate is less than 2%. A few years later, in order to quiet down fears of deflation, the SNB formally stated that this means an inflation rate between 0% and 2%.

As previously indicated, the SNB is required to brief the political authorities at the national level (the Federal government and the finance commission of the two chambers of parliament) of its intentions. At the same time, the Constitution stipulates that “the members of the Bank's bodies shall not be permitted to seek or accept instructions either from the Federal Council or from the Federal Assembly or any other body”. In practice, this means that the SNB exchanges information with the federal government (the Federal Council) and that its reports to the parliament (the Federal Assembly) are for information only. Its statutory authority, the Bank Council, is not allowed to discuss monetary policy issues.

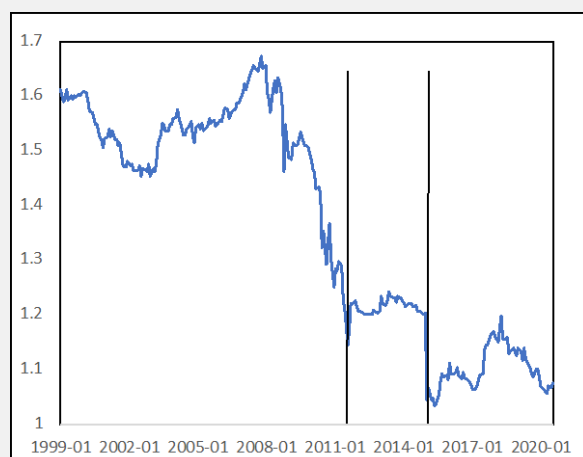
As noted above, the shareholders can only make proposals regarding business practice and this right is barely ever used. In recent years, a group of militant investors offered proposals but most of them could not be voted upon, and the one that could was massively rejected.

Similarly, The SNB's accountability to the People is for information only. The Governing Board members make a large number of speeches to various constituencies to explain their actions. It also holds quarterly press conferences after its policy-making meetings but these are very polite encounters with very few pointed questions. The press typically reports faithfully what the Governing Board has said. Criticism is virtually non-existent. The only exception occurred in January 2015 as recounted in Box 1.

Box 1: January 2015: the end of the floor

In the wake of the global financial crisis, Switzerland came to be seen as a safe haven. Surprisingly perhaps, this was the case even though its two global banks, Credit Suisse and UBS, faced large losses and UBS was promptly bailed out by the SNB (with a Treasury guarantee). In September 2011, the SNB announced that it would intervene without limit to ensure that the franc would not appreciate below 1.20 francs for one euro. The exchange rate promptly stabilised slightly above the floor. When the Greek debt crisis intensified in late 2014, massive inflows resumed, forcing the SNB to intervene. Its balance sheet hugely expanded. With no end in sight, the SNB announced in January 2015 that it was abandoning the floor. Figure 1 shows that the franc immediately appreciated.

Figure 1: The exchange rate (CHF/EUR)



Source: Swiss National Bank.

The decision had not been announced, and could not be announced for fear of intense speculative pressure. The surprise was resented by the public, especially by exporting firms that faced a stiff worsening of competition and by financial institutions and investors that suffered large book losses on their foreign investments. Public discussions about the SNB, often with a negative tone, represented a rare event. The Bank's communication was seen as less than convincing since it centered on the risk of large losses on its foreign assets along with reassurances that the export sector would be able to adjust. Eventually, following large foregone exchange market interventions by the SNB, the exchange rate depreciated to the range 1.05-1 and the export sector weathered the shock.

It remains that the system of direct democracy gives the possibility to call initiatives by collecting a sufficient number of signatures over a given period of time. Since 2000, four initiatives have concerned the SNB, all of which have been rejected. The three first ones focused on the assets of the SNB. The two first (in 2002 and 2006) aimed at directing SNB's gold and profits toward financing health insurance

and the third one (in 2014) intended to have the SNB retain a given proportion of gold. None of them were related to monetary policy. It suggests that most Swiss people see the SNB as a highly profitable operation, a national treasure of sorts. Indeed, its assets already in 2005 large at the time of the initiatives, further grew enormously in the wake of the global financial crisis as the Bank was struggling to prevent large capital inflows from leading to what it saw as an unbearable over-appreciation of the franc.

Table 1: Assets of the Swiss National Bank (% of GDP)

	2005	2019
Gold	6.1	5.5
Foreign currency investments	11.5	110.0
Repo transactions	6.4	1.0
Other	2.7	2.8
Total	26.7	119.3

Source: Swiss National Bank.

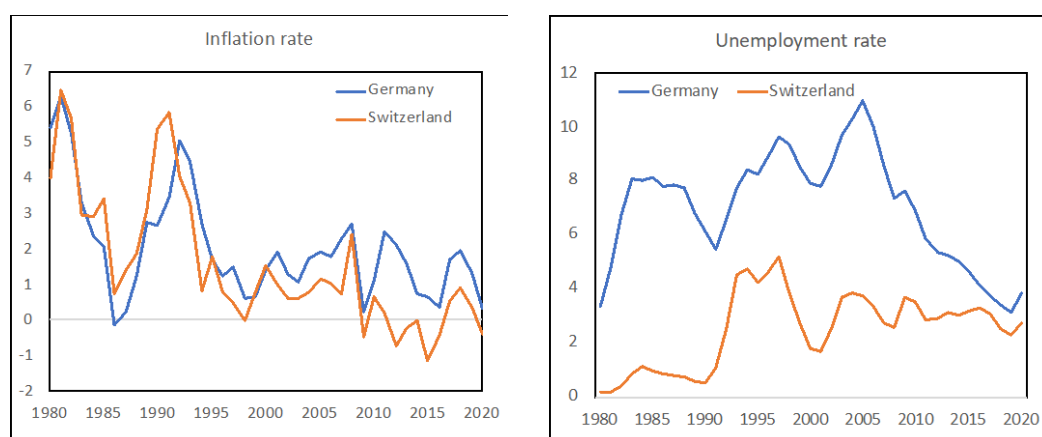
The fourth referendum, held in 2018, directly aimed at monetary policy. The proposal was indeed radical. The proponents denounced the classic two-tier banking system whereby commercial banks create the bulk of fiduciary money. They criticised the resulting profits for commercial banks and the fragility of the architecture, which is open to bank runs and may force the authorities to undertake huge bailouts. The proposal, called “full money” was to restrict any money creation to the SNB. Although it could be seen as a tribute to its trustworthiness, the Bank was alarmed, in part because it would all but destroy large segments of the Swiss financial system, but also because it could make monetary policy much more challenging. The SNB engaged in an unprecedentedly vigorous campaign. In the end, the proposal was strongly defeated (by more than 75% of votes). Yet, it showed that the SNB’s independence and integrity was more vulnerable than hitherto believed. Popular initiatives can change the constitution and the SNB needs to avoid to be seen as missing on its mandate, which concerns price stability and financial stability.

2.3. Inflation and accountability

Figure 2 compares inflation and unemployment in Switzerland and Germany, where the Deutsche Bundesbank, which had built a reputation for keeping inflation in check at all times since its creation in 1957 and until the creation of the euro in 1999. The joint evolution of inflation and unemployment is known to shape monetary policy as captured by the Taylor rule. Keeping both rates low is therefore a gauge of the quality of monetary policy.⁵ On both counts, the performance of Switzerland has been better than that of Germany.

⁵ This is not entirely correct. The Taylor rule is driven by the deviations of inflation from its target and of unemployment from its equilibrium rate. The targets in Switzerland and Germany are similar but the equilibrium unemployment rate is lower in Switzerland than in Germany. The generally higher rate of unemployment is due to a host of factors – including the flexibility of labour markets – that are out of the purview of central banks.

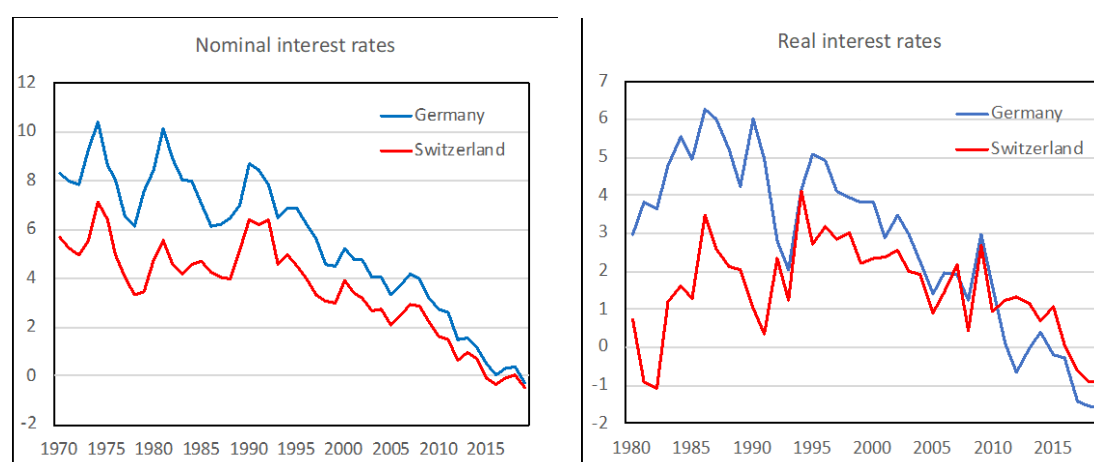
Figure 2: Switzerland and Germany



Source: *World Economic Outlook*, IMF.

Indeed, the SNB is keen to observe that its credibility is superior to that of any other central bank in the world. As a supporting “proof”, it regularly mentions that interest rates in Switzerland are lower than elsewhere, including Germany, because the Swiss franc benefits from a credibility premium. The left-hand chart in Figure 3 confirms that it is the case but this is not exactly a proof because the difference partly reflects lower inflation in Switzerland. The right-hand chart, which displays the real interest rates, indicates that the real German rate has been lower since the 2010s. But this corresponds to the period when inflation has been negative in Switzerland while monetary policies in both countries were pushing the nominal interest rates down to their effective lower bounds. Careful studies by Kugler and Weder di Mauro (2005) and Baltensperger and Kugler (2016) formally confirm that the Swiss franc interest rates are indeed unique in displaying a premium. They relate this result to the safe haven nature of Switzerland, which they trace back to the aftermath of World War I. The safe haven effect is due to the neutral position of the country, its strong legal system and confidence in the stewardship of the SNB.

Figure 3: Long term bond rates in Switzerland and Germany



Source: *Economic Outlook*, OECD.

Accountability, however, requires more than this. In a democracy, an independent institution under the aegis of non-elected officials – a.k.a. bureaucrats – must be subjected to precise objectives. As

noted, the SNB is committed to keep the inflation rate between 0% and 2%. Figure 2 shows that, in the 13 years 2008-2019 since the global financial crisis, inflation has been negative seven times. The stated target range has been missed more than half of the time. In the first part – entitled *Accountability Report* – of its *Annual Report* for 2016, the second consecutive year of negative inflation, the SNB reminds the readers that:

“The SNB equates price stability with a rise in the Swiss consumer price index (CPI) of less than 2% per annum. Deflation is also regarded as a breach of the objective of price stability.” (p.19).

Thus, the objective has been breached more often than it has been met during this twelve-year period. How has the accountability mechanism dealt with such repeated breaches? The only reference concerning the missed objective in the 2016 *Accountability Report* is as follows:

“In 2016, the Swiss consumer price index (CPI) fell by 0.4% on average, declining less strongly than the year before (– 1.1%). This was primarily due to the stabilisation of the nominal Swiss franc exchange rate and the pick-up in oil prices. It also became evident that the price-dampening effects of the Swiss franc appreciation had faded.” (p. 12)

This short statement apparently was sufficient to dispel any notion that something was amiss. There has been no public discussion of what could be seen as a failure, neither this year nor in other years. A number of issues could have been raised:

- The policy interest rate was set in 2016 at -0.75%, as in the previous year. It showed that the SNB was determined to carry out a nonstandard policy to achieve its own definition of price stability, but then why was it not delivering? Was Switzerland getting caught in a “Japanese trap”? That the policy rate is still at the same level in 2020, suggests that this is a valid topic.
- The explanation explicitly refers to the 2015 exchange rate appreciation described in Box 1. Was the outcome a consequence of a policy mistake?
- Could the SNB have taken other measures to meet its mandate of price stability?

Somehow, the institutions – the federal government, the federal parliament, the people – to which the SNB is accountable were satisfied by the above statement.⁶

2.4. Financial stability and accountability

The SNB's mandate includes financial stability, although supervision is the responsibility of another institution (FINMA). The financial sector is an important component of the Swiss economy. Two banks operate at the global level with balance sheets which far exceed the country's GDP. In the aftermath of the 2008 crisis, one of these banks (UBS) had to be rescued. In agreement with the federal government and FINMA, the SNB promptly created a “bad bank”, the StabFund. It was set up as a special-purpose vehicle, which took over close to USD 40 billion of toxic assets from UBS at (low) market price, technically a loan to UBS. The SNB was protected from the associated risk through a complex arrangement with UBS and by a capital injection from the federal government. The arrangement stipulated that a first tranche of any loss would be borne by UBS.

⁶ There is currently a growing discussion on the investments of the SNB in equity of private firms (20% of assets in foreign currencies held by the SNB), especially regarding environment and human right impact. There will be a vote on a proposal to ban investment in the weapon industry.

Over time, Stabfund proceeded to gradually sell its portfolio, which reduced UBS's debt to the SNB. After five years, UBS bought back the remaining assets and thus extinguished its debt to the SNB, which ended up making a sizeable profit from the operation (more than USD 5 billion).

At the inception phase, the federal government was directly involved but the operation was entirely controlled by the SNB, which designed and then managed the Stabfund. As the large central banks (from the US, the euro area, the UK, Japan) forcefully intervened in September and October 2008, the financial markets promptly stabilised, which made it unlikely that the SNB would suffer losses. Given the complexity of the operation, the public and parliament were told that the SNB had prevented a collapse of UBS, which would have had incalculable consequences for the Swiss economy, and that it well protected taxpayers. Grumbles, limited to small parts of the population, were focused on the political aspects of saving a bank.

2.5. Profits distribution

Probably the most visible – and potentially controversial – role of the SNB is its wealth and the distribution of its profits. As noted above, the SNB is a special-statute joint-stock company and its shares are held by the cantons and the cantonal banks, which own just under half, and the rest by private individuals. The special status affects the distribution of profits. Not all profits are distributed. The SNB equity includes its capital, reserves for future payments (the tool to smooth payments to cantons and the Confederation, see below) and a “provision for currency reserves” which is the bulk of the equity. This last provision grows each year (currently by 8%). The remaining profits are distributed to shareholders, to cantons and to the Federal government, which is not a shareholder, according to a rule agreed with the government, which is renegotiated every five years.

In a nutshell, shareholders receive a very small amount, which is capped by law at CHF 2.5 millions (6% of shares nominal value). The bulk of distributed profits are shared between the cantons, which receive 2/3 of the total⁷, and the federal government, which receives the remaining third. Since profits are very volatile, the rule is designed to smooth payments through a reserve fund. The amounts are significant for the cantons. In 2017, in average they received amounts representing 0.22% of GDP, or 1.7% of their expenses. The amount was multiplied by 4 in 2019 and 2020, a consequence of large SNB profits.

Even though the distribution of profits is codified, the SNB enjoys quite a lot of freedom in deciding what share of its profits is to be distributed. Each year, unless it suffers losses, it sheds aside money for its monetary operations, for its foreign exchange interventions and for the distributions reserve. In 2019, a record year, the amounts distributed amounted to 11% of profits worth 5% of GDP. As a result, at end 2019, the total equity of the SNB represents 24% of GDP (the size of the balance sheet is 123% of GDP, the result of large foreign exchange interventions since 2008, the Swiss version of QE).

2.6. Evaluation

The SNB is special in being very independent with weak formal accountability, in practice negligible accountability. This is in line with the constitution and the law on the central bank which specifies that the SNB should not seek or receive instructions from the federal government and parliament, to which it is accountable. As a result, the SNB and the federal government exchange information on their respective intentions but the government does not try to influence the SNB and stays clear from airing any criticism. The parliament receives the Bank's annual report but does not discuss monetary policy in any meaningful way. The SNB is also tasked with reporting to the public at large, which it does through numerous meetings and conferences. The general perception is that the Bank is delivering on its

⁷ The repartition among cantons is based on a formula that combines population size, total income and a few other criteria.

mandate better than any other central bank. Importantly, this perception does not vary among cantons. While public opinions diverge between the linguistic groups on various issues, monetary policy is not subject to any noticeable cleavage.

All in all, the SNB enjoys great respect to the point that its independence, which goes back to the aftermath of World War II, is never questioned, nor is its performance, which is indeed impressive. Backed by an efficient economic system, which balances economic effectiveness through the market mechanism, and a highly developed welfare system, which corrects and complements the markets, the SNB has achieved a high degree of price stability while unemployment has remained low. Its safe haven status delivers a strong currency: since 1973, its effective exchange rate has appreciated by 260% nominally, and by 40% in real terms. It has been able to cope with this real appreciation; its current account has been above 10% of GDP over the last 25 years. The result is that there is no perceived need to make the SNB really accountable (beyond the possible use of its asset holdings to exercise on environment and human right issues).

3. ACCOUNTABILITY OF THE ECB

3.1. Comparison with the SNB

3.1.1. Formal differences

The accountability requirements are formally more demanding for the ECB than for the SNB. The quarterly sessions of the Monetary Dialogue provide for direct, public contact between the ECB President and the European Parliament. Along with other Board members' testimonies and written questions and answers, the ECB is subject to substantial oversight.

In addition, the large Governing Council of the ESCB naturally implies that consensus is more difficult to achieve than among the three members of the SNB's policymaking body. Since disagreements often leak out, the public – media, academics, financial market participants – are aware of issues that are delicate to grapple with, while disagreements at the SNB are never known outside the Governing Board.

3.1.2. Public opinions

As noted above, monetary policy is not a topic that elicits divergences of opinion among the various groups, mostly linguistic, that make up the Swiss electorate. The situation in the euro area is radically different. It always has been the case that national public opinions held different views of monetary policy. From its inception, the ECB has recognised this challenge. Its response has been to formally ignore that different countries may, at times, require different policy actions. By insisting that it only looks at the area as a whole, the ECB officially manages the "average member country". Since this "average country" does not exist, it is not surprising that ECB decisions may not please occasionally most countries. In practice, in some instances, the ECB has paid particular attention to a country. A good example is the Pandemic Emergency Purchase Programme (PEPP) that allows asset purchases not in proportion to the usual key.

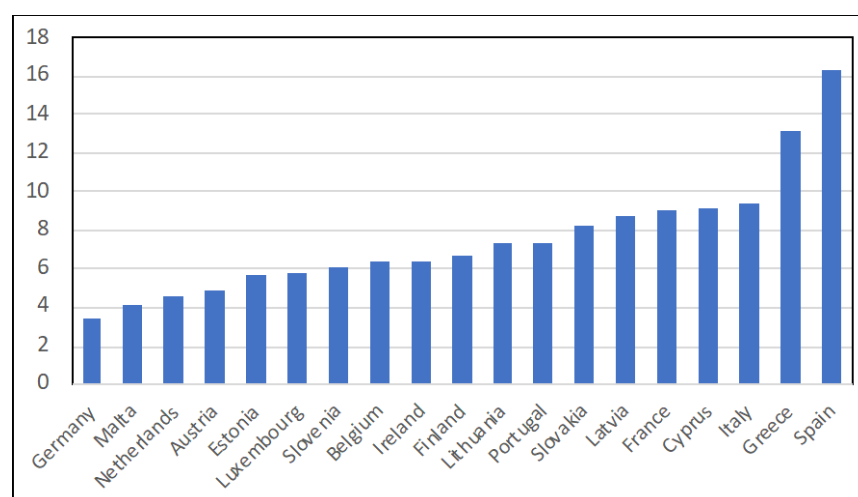
One lesson from the SNB experience is that when they are satisfied, public opinions do not ask for accountability. Since the ECB cannot always please simultaneously all national public opinions, the democratic demand for accountability is high. What makes the situation even more complicated is that the European Parliament is occasionally torn along national lines by divergences in public opinions.

3.1.3. Performance

The other lesson from the SNB experience is that the ultimate accountability test for a central bank is to deliver a faultless performance, or at least to convince the broad public that such is the case. The previous section warns that this is mission impossible for the ECB because there will almost always be a member country that feels poorly treated by the common monetary policy. Evaluating ECB policies since the creation of the euro is far beyond the limits of this report. This section only looks at national outcomes in terms of unemployment and inflation, the drivers of the Taylor rule as examined in Section 2.3.

The unemployment rate differs quite substantially across the euro area member countries. Most of these differences are due to structural differences, especially concerning the functioning of the labour markets. This is captured by the equilibrium rate of unemployment, which is intended to measure what would the unemployment rate be if the economy would be "in macroeconomic equilibrium", i.e. neither in a boom nor in a slump. Figure 4 presents estimates of equilibrium unemployment rates by the European Commission (the NAWRU concept). The differences are huge.

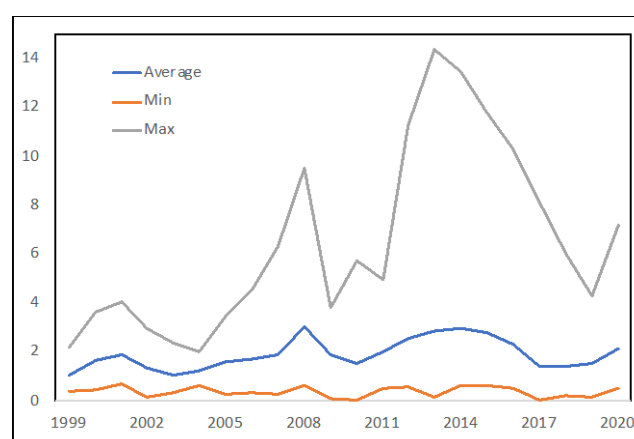
Figure 4: Equilibrium unemployment rates in the euro area - 2019



Source: AMECO Database, European Commission.

Monetary policy is powerless as far as labour market structures are concerned. Therefore, the ECB is not expected to deal with the level of the equilibrium unemployment rate, only with cyclical deviations of the unemployment rate from its equilibrium value. This is why Figure 5 looks at the deviations of inflation from the (unofficial) target of 1.75% and at deviations of the unemployment rate from its equilibrium value at national levels. It uses a version of the “misery index”, here the sum of these deviations.⁸ For each year since 1999, the figure displays the average value of the index among member countries along with minimum and maximum values.⁹ If monetary policy could stabilise equally well inflation and unemployment in each and every member country, there would be no difference in the average, minimum and maximum values of the misery index. Clearly, this is not the case. Each year some countries face much less satisfactory macroeconomic conditions than others.

Figure 5: The misery index



Source: AMECO Database, European Commission.

⁸ More precisely, the index is the square root of the sum of both deviations squared: $\sqrt{(\pi - 1.75)^2 + (u - u^*)^2}$, where π is the annual inflation rate, u is the unemployment rate and u^* its equilibrium level.

⁹ The sample expands as new countries adopt the euro.

It must be emphasised that the cyclical evolution of inflation and unemployment are not driven only by monetary policy. National policies, including fiscal policy and structural policies, also have powerful influences on cyclical variations. The ECB cannot be held responsible for the divergences observed in Figure 5. The danger is that it is easy to scapegoat the ECB. This observation carries important implications for accountability.

3.2. The challenges of accountability in the euro area

While the ECB is formally accountable only to the European Parliament, the experience of other countries, as exemplified by the Swiss case, indicates that any central bank must establish its reputation with its population. This is the issue discussed in this section, while the next one considers the relationship with the European Parliament.

3.2.1. Many countries

While the three members of the SNB's Governing Council devote a significant amount of time and effort to address the broad public, the situation is much more complicated in the euro area. In effect, each country is a different constituency and has its own central bank. In principle, national central bank governors and other officials can act as spokesperson for the ESCB, and many do. But there occasionally exists disagreements within the Governing Council and national central bank governors often air their viewpoints, presumably to reassure their constituents that they are in tune with national public opinion, and possibly also as a way to reinforce their positions within the Council. This is notably the cases when the ECB faces difficult decisions, which are naturally controversial. The resulting "cacophony" alerts the public and observers that there are disagreements, which may overlap with differing national interests and conventional wisdoms. The members of the ECB's Governing Council could travel to all member countries, and many travel a lot, but language barriers are bound to reduce the effectiveness of communication.

The official position is that there is no cacophony, which is sporadically proven wrong. There is no magic bullet here.¹⁰ It is worth remembering that the same situation arose in the early years of the Federal Reserve of the US, where the regional governors were appointed locally. This has changed following the Banking Act of the 1935, 22 years after the creation of the Federal Reserve, which strengthened the hand of the Board – the equivalent of the ECB Executive Board – and led to a considerable reduction of local influence of the regional banks.

3.2.2. Unclear performance

Section 3.1 argues that any evaluation of the performance of the ECB is bound to depend on which country is looked at. As noted, this means that the overall performance is difficult to ascertain.

To make matter worse, differences of opinions within the Governing Council inevitably weigh on decisions. In difficult times, this affects the overall performance of the Bank. Two cases can be mentioned. In the wake of the global financial crisis, the ECB has been slow to cut its interest rates and engage into quantitative easing, which has worsened the subsequent crisis (Orphanides, 2018; Wyplosz, 2016). Then, during the European debt crisis, the ECB has let two years pass before acting as lender of last resort (De Grauwe, 2012; Wyplosz, 2015), allowing the crisis to spread and deepen.

The result is that criticism of the ECB is unavoidable. It is unfortunate that the ECB be made a scapegoat of poor national policies.

¹⁰ Burda (2013) makes the original proposal, based on the US experience, to establish regions that do not overlap with national borders.

3.3. Relations with governments

A key condition for central bank independence is that the political authorities not be allowed to interfere, or even be seen to try. This applies first and foremost to the governments. Yet, a central bank does not operate in a vacuum, it needs to cooperate with its government. In the short to medium run, inflation is influenced by government policies and most issues of financial stability require government involvement. The situation of the ECB requires even more cooperation because it faces many governments and because public opinion support is essential to preserve independence while, as noted, there are as many public opinions in the euro area as there are countries.

The ECB has ostentatiously chosen to not engage in systemic exchanges with its governments but, in fact, the contacts are numerous and continuous. These exchanges could be usefully made more formal and systematic. It would be better than the current practice which includes ritual statements about fiscal policies at ECB press conferences. By the way, while the ECB cringes when public officials make critical statements about monetary policy, rightly so, it does not hesitate to complain about fiscal policies.

3.4. The role of the European Parliament

In the end, the only formal accountability obligation of the ECB is to the European Parliament, and this is how it should be. Fraccaroli et al. (2018) describes the procedure and show that the practice has evolved in the wake of the debt crisis. However, since the start, the “Monetary Dialogue” has been shaped in a way such that accountability is de facto limited. An indication is that the formal quarterly auditions of the President of the ECB attracts limited press coverage – and therefore limited awareness by the broad public – and rarely affects the fickle and information-hungry financial markets (Fraccaroli et al., 2018). Wyplosz (2015) has identified a number of shortcomings, most of which remain intact.

3.4.1. The current situation

- Accountability is about evaluating past actions. The President of the ECB, instead, is more interested in sharing his/her thoughts about future actions. Because of the sensitivity of such statements, the President’s presentation is carefully scripted presentation and he/she sticks to it during the Q&A session that follows.
- Monetary policy is highly technical, if only because it operates through financial markets. Technical discussions do not appeal to non-economists while economists relish in technicalities. While some Members of the European Parliament (MEPs) are highly competent, for lack of time they are not able to cross-examine the ECB’s testimonies.
- Indeed, the format of these testimonies precludes in-depth examination of ECB actions. Within the few minutes and at most one follow-up question that they are allotted, MEPs can only scratch the surface of the issues that they raise.
- Written questions, which have increased in numbers, do not add much.
- The papers written by the experts are usually of a high quality and could help the exchanges during the Monetary Dialogue, but the limits mentioned above (time available, follow-up) make it impossible.

3.4.2. How could the EP exercise accountability?

To be effective, accountability needs to delve into past decisions in detail. It does not have to be systematically critical but it has to be so when warranted. Monetary policy decisions occasionally are difficult, with several possible options. The options are based on assumptions – forecasts, channels of

transmission, risks – that need to be examined with an open mind. The purpose is to evaluate all options that were available, the reasons why one of them was chosen and to compare outcomes with anticipations. Here are a few suggestions:

- These inevitably technical issues must be tackled at great depth. It requires a fluid debate, with a limited number of participants who can intervene in the discussion and jointly pursue various lines of thoughts. This is incompatible with the current format that packs a large number of interventions, each of which is time-constrained and with just one follow-up question, thus barely scratching the surface.
- Those who will intervene could prepare the discussion with the experts ahead of time.
- Going further, the MEPs could be allowed to interrupt the President who may move away from pointed questions.
- Finally, it is difficult to understand why the sessions have a time limit. Given the importance of accountability, the hearings should be allowed to last as long as needed.

This approach has three important advantages.

- It prevents the superficial nature of current exchanges on issues that require a high degree of precision.
- It will affect future decisions once the ECB officials know how carefully scrutinised they eventually will be.
- Focusing on past actions greatly reduces the prudence and confidentiality that ECB officials naturally require when discussing future actions.

Such an approach would be a major change to current practice. It would challenge agreements with the ECB and it would require rethinking the way the Economic and Monetary Affairs Committee has been operating since 1999. Given the utmost responsibility of the Parliament in a crucial collective policy domain, continuation of past practice amounts to accepting weak accountability. What is acceptable, maybe, in the case of the SNB, is not in the case of the ECB.

3.4.3. Accountability and the broad public

The Swiss case shows that accountability is not really exercised when the broad public is fully satisfied by the actions of the central bank. This may be a unique case, not necessarily desirable because the technical nature of monetary policy may deter the public from trying to understand the actions of the central bank, with the result that occasional mistakes go largely undetected. Nor is it generalisable to the case of the euro area where, as noted, there are as many public opinions as there are countries.

Nevertheless, an important implication is that accountability and public opinion are intimately linked. The accountability body's deliberations are more effective when the broad public is cautious and public opinions can be shaped, partly at least, by the views of the accountability body.

This link is largely lost in the euro area by the multiplicity of public opinions. The European Parliament cannot hope to build its effectiveness on diverging public opinions. In fact, during the Monetary Dialogue sessions, MEPs often visibly convey the views of their public opinions, which prevents the emergence of a common assessment. Similarly, diverging public opinions will not be swayed by the current format of the Monetary Dialogue.

Dealing with public opinions remains an important weakness for accountability, and it affects the conduct of monetary policy. The ECB seems to recognise the importance of this observation since its

new President has clearly stated that she intends to speak a bit less to the financial markets, in technical terms, and a bit more to the broad public.¹¹ The Parliament too should make efforts to publicise its work. It is suggested here that a deeper Monetary Dialogue stands to attract the attention of the media, which can then translate the technical discussion into their own communication with the broad public

¹¹ She has announced her intention in her first meeting with the Economic and Monetary Affairs Committee on 4 September 2019.

4. SUMMARY AND CONCLUSIONS

The SNB is formally independent and subject to weak accountability requirements. In addition, on the basis of a strong track record, the consensus is that the SNB is delivering on its mandate. These two elements explain that there is hardly any debate about monetary policy in Switzerland. Experts may quibble with some decisions, but criticism is generally absent from debates within political and media circles and the broader public.

The accountability requirements from the ECB are rather weak too. The ECB is accountable to the European Parliament but its powers are limited and the process, the Monetary Dialogue, is not particularly demanding. Yet, the need for effective accountability is much stronger in the euro area.

One reason is that public opinion is divided. The decisions by the ECB can be simultaneously lauded and criticised, including by policymakers, financial market participants and even academics because of pre-existing prejudices.

Another reason is that the hearings of the President and of other members of the Executive Board before the Economic and Monetary Affairs Committee do not allow for precise and in-depth questioning. In addition, MEPs frequently reflect in their interventions the views of their public opinions. Opposite views make it nearly impossible to focus on important but highly technical issues.

A more dynamic Monetary Dialogue, as suggested in the previous section, would attract more attention from the media, which would translate into heightened public visibility. It could well emphasise disagreements, which some may see as potentially dangerous.

Prejudices will not vanish soon but the European Parliament has a particular responsibility. The Monetary Dialogue can be much improved by allowing an in-depth discussion of ECB actions.

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How Can the European Parliament Better Oversee the European Central Bank?

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Abstract

This paper assesses how the European Parliament (EP) holds the European Central Bank (ECB) accountable. The same exercise is done for the Bank of Japan, in order to identify possible lessons for the ECB and the EP. Possible improvements to the ECB accountability framework include procedural changes to the Monetary Dialogue to increase its effectiveness, the release of detailed minutes and votes from ECB governing council meetings, and the establishment of a ranking by the EU legislators of the ECB's secondary objectives.

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CONTENTS

LIST OF ABBREVIATIONS	67
EXECUTIVE SUMMARY	68
1. INTRODUCTION	70
2. HOW DOES THE EUROPEAN PARLIAMENT HOLD THE ECB TO ACCOUNT?	71
2.1. ECB Mandate	71
2.2. ECB Transparency	72
2.3. The ECB's relationship with the European Parliament	73
3. LESSONS FROM THE BANK OF JAPAN AND THE JAPANESE DIET	76
3.1. Mandate of the BoJ	76
3.2. BoJ Transparency	77
3.3. Relationship of the BoJ with the Diet and the government	78
4. RECOMMENDATIONS TO IMPROVE ECB ACCOUNTABILITY BEFORE THE EUROPEAN PARLIAMENT	82
4.1. Improving the monetary dialogue	82
4.2. Pushing for even more transparency in decision making	83
4.3. Ranking the ECB's secondary objectives	84
5. CONCLUSION	86
REFERENCES	87

LIST OF ABBREVIATIONS

ECB	European Central Bank
EP	European Parliament
MEP	Member of European Parliament
BoJ	Bank of Japan
ESCB	European System of Central Banks
ECON	European Parliament's Committee on Economic and Monetary Affairs
Fed	Federal Reserve System
BoE	Bank of England
GDP	Gross domestic product
MPM	Monetary Policy Meeting
MEPs	Members of the European Parliament
TEU	Treaty on the European Union
TFEU	Treaty on the functioning of the European Union
BVerfG	Federal Constitutional Court for the Federal Republic of Germany

EXECUTIVE SUMMARY

- **In the wake of the successive crises that have affected the euro area over the last twelve years, the role of the European Central Bank (ECB) in managing the euro-area economy has expanded considerably.** Its use of less-conventional monetary tools and various asset purchase programmes has increased its footprint in financial markets and in the real economy. Although we consider that this development has been warranted by the situation, it increases the need to ensure effective accountability to the European Parliament (EP), the only directly-elected EU institution.
- **This paper assesses the current ECB accountability framework, and compares it to that of the Bank of Japan (BoJ).** Even if the functioning and degrees of independence of the BoJ and ECB differ significantly, some useful lessons can nonetheless be drawn from the Japanese experience.
- **To be more accountable, the ECB's primary and secondary objectives should be clarified and transparency about decision-making should be increased.** Moreover, in contrast to parliaments of other jurisdictions, the European Parliament's competences are very limited: it can neither appoint nor sanction the ECB's Executive Board members, while fundamental changes in the functioning of the ECB would require a change to the EU Treaties, which must be approved unanimously by EU Member States.
- **The BoJ Act of 1997 intended to increase BoJ independence, but the BoJ remains much less independent than other major central banks, and in particular the ECB.** There is a high degree of government involvement in monetary policy decisions in Japan, as "close contact" and coordination are written into law and established in practice. For instance, while the main objectives of the BoJ are enshrined in Japanese law, the quantitative definition of price stability (which evolved over time) is determined by the BoJ, but the most recent change has been heavily influenced by the government. The Japanese Parliament is also much more powerful than the EP as it can modify the law governing the functioning of the BoJ and veto appointments to the BoJ Policy Board. BoJ decision-making processes are also more transparent than those of the ECB, as the BoJ publishes detailed minutes of monetary policy meetings with details of individual votes and reasons for dissent.
- **We make three main recommendations to improve the ECB accountability framework.** First, the EP can, and should, **improve the Monetary Dialogue**, to transform it into a real hearing aimed at evaluating the ECB's effectiveness in fulfilling its price stability mandate and in contributing to the achievement of EU objectives. The EP should also look into the proportionality of the tools used by the ECB to fulfil its mandate in order to ensure that the ECB does not overstep its treaty-based competences. The Monetary Dialogue would also benefit from a reduction in the number of MEPs participating, to give participants the chance to engage genuinely with the ECB President and to ask follow-up questions (as is the case in Japan). The ECON Chair should also ask at each meeting a fixed set of questions related to the ECB's performance.
- Second, **the EP should push the ECB (using in particular the ongoing strategy review) to publish more detailed minutes of Governing Council meetings**, which would include the votes of the members (as is the case for the BoJ), as this is legally at the discretion of the ECB. This would enable more effective scrutiny, create the right incentives at the individual level for Governing Council members, and, by allowing easier identification of the pros and cons of its policies, it would also alleviate concerns raised in some euro area countries about the proportionality of the ECB's actions.

- Finally, **amid calls for the ECB to 'green' its monetary policy, additional clarity on the role and ranking of secondary objectives is required.** However, ranking of goals is a political task, so it should preferably be decided by elected bodies and not by unelected technocrats. The EU's legislators should thus reveal their preferences. This clarification about the ECB's objectives would in turn facilitate parliamentary scrutiny.

1. INTRODUCTION

From a democratic perspective, an effective accountability framework is a pre-requisite for central bank independence, which many countries introduced in the 1980s and 1990s when they amended their monetary frameworks to insulate monetary policy from day-to-day politics in order to avoid high inflation episodes. As unelected officials, to whom responsibilities for managing the currency have been delegated by political bodies, central bank decision-makers need to be guided by clear mandates and to be accountable to citizens or the institutions representing them.

This is particularly true in Europe, given the considerable expansion of the role of the European Central Bank (ECB) in managing the euro area economy, and the development of its toolbox away from basic short-term interest rate changes, first with the global financial crisis, then the euro crisis and now the COVID-19 crisis. With the introduction of its various asset purchase programmes and of other so-called unconventional policies, the ECB's direct involvement in particular segments of the financial market and its role in credit allocation have increased dramatically. This increases the need for strong democratic oversight of these activities.

For central banks to be accountable, three main elements are generally considered crucial¹: first, that the objectives of the central banks are well-defined (legally established and clear) so they can be monitored easily by a responsible political body; second, that the central bank is highly transparent in its decision-making and in the implementation of monetary policy (so that there is no information asymmetry between the agent, the central bank, and its principal, the citizens); and third, that the political body to which it is accountable is able to question, and preferably to sanction in some way, the central bank if it does not fulfil its mandate.

We use this simple framework – focusing mainly on these three elements – to assess the accountability of the ECB. We also compare this framework with that of the Bank of Japan (BoJ). We make recommendations, which do not necessitate unrealistic treaty changes and could be implemented immediately, on how the European framework could be improved without compromising the independence and effectiveness of the ECB. In particular, we focus on how the European Parliament (EP) could better scrutinise the implementation of monetary policy in the euro area.

¹ See for instance Briault et al. (1997), De Haan, Amtenbrink and Effinger (1999), Eijffinger and Geraats (2002), De Haan and Amtenbrink (2003), Fry et al. (2000).

2. HOW DOES THE EUROPEAN PARLIAMENT HOLD THE ECB TO ACCOUNT?

ECB independence is clearly enshrined in the European Treaties, with Article 130 of the Treaty on the functioning of the European Union (TFEU) stipulating that ECB decision-making bodies (i.e. the ECB Governing Council and Executive Board) shall not “seek or take instructions from Union institutions, bodies, offices or agencies, from any government of a Member State”, while TFEU Article 282 adds that the ECB “shall be independent in the exercise of its powers and in the management of its finances”.

As a result, the ECB enjoys a very high level of independence: it is target-independent, as the ECB sets its own quantitative definition of price stability; it has full operational independence, as ECB decision-making bodies can take fully autonomous decisions in their areas of competence; and it is financially independent, as the ECB has sufficient own resources to conduct its activities (Chiacchio et al., 2018). In addition, given that its autonomy is legally ensured by Treaties that can only be changed by the unanimity of European Union Member States, the ECB is often considered as the most independent central bank in the world. This makes effective accountability before a democratically elected institution even more crucial. In this section we discuss how accountable the ECB is by taking a look at the three elements necessary to successfully make a central bank accountable: a clear mandate, a high level of transparency and a political body able to undertake effective oversight.

2.1. ECB Mandate

Well-defined and legally enshrined objectives are paramount if a central bank is to be held accountable because these objectives are yardsticks against which to assess a central bank's performance. As far as the ECB is concerned, its objectives derive from the EU Treaties. Article 127 of the TFEU stipulates that: “the primary objective of the European System of Central Banks (hereinafter referred to as ‘the ESCB’) shall be to maintain price stability. Without prejudice to the objective of price stability, the ESCB shall support the general economic policies in the Union with a view to contributing to the achievement of the objectives of the Union as laid down in Article 3 of the Treaty on European Union”. The EU objectives are very broad and include “peace”, “freedom, security and justice”, “balanced economic growth”, “a highly competitive social market economy”, “full employment and social progress”, and “improvement of the quality of the environment”, etc.

Two main issues arise concerning the objectives of the ECB. First, the European Treaties do not provide a specific numerical definition of price stability, which means that the ECB has the competence to set its own quantitative target in order to comply with its mandate. In 1998, the Governing Council adopted the quantitative definition: “price stability is defined as a year-on-year increase in the Harmonised Index of Consumer Prices (HICP) for the euro area of below 2%”. In 2003, this definition was clarified by the Governing Council, which announced that the ECB objective was to maintain inflation rates “below, but close to, 2% over the medium term”.

The fact that this quantitative objective was not set through a legislative process is not a problem per se, but it is crucial that there is a comprehensible quantifiable benchmark in order to assess the ECB's performance. In the case of the ECB, we believe that the current definition of price stability has led to some confusion among market participants and the broader public. In particular the expression “below but close” suggests that the ECB targets a smaller number than 2%. Even though former ECB chief economist Otmar Issing (2003) explained that the ECB should be comfortable with inflation expectations between “1.7 percent and 1.9 percent”, an indication that the ECB is targeting an inflation rate of about 1.8%, it is not obvious why there needs to be some room for interpretation of the inflation target. In our view, this lack of clarity adds unnecessary noise in the pursuit of price stability, negates

the coordination benefits of having a clear numerical target, and makes the assessment of the ECB's performance more difficult. In addition, the word 'below' can be interpreted to mean that the ECB has a downward bias in its definition. This forced former ECB president Mario Draghi to highlight on many occasions the ECB's commitment to symmetry in the inflation aim to avoid a downward drift in inflation expectations². That is why a clearer definition is desirable (Claeys et al., 2018).

Second, while the primacy of the price stability mandate is clearly established by the Treaty and should not be compromised in the pursuit of its secondary objectives, there is no ranking established between the latter objectives in case of a trade-off when the ECB intends to contribute to achieving these multiple objectives.

2.2. ECB Transparency

A high level of transparency is also essential to ensure the accountability of independent central banks, as it allows for close and effective monitoring by the competent authorities and by the general public. Explaining the central bank's decisions and their implementation, but also showing that it does not overstep its mandate, and that the tools used are proportional to the fulfilment of its mandate, is crucial. This can take various forms: to explain and justify their decisions, central banks around the world organise press conferences, they publish minutes of the discussions of their respective monetary policy committees, they prepare inflation reports, they participate in public hearings, give interviews to the media, and publish research papers.

Overall, the ECB is fairly transparent and uses many of these different avenues to explain its decisions. Beyond the regular press conference and the publication of the Economic Bulletin that follows each of its monetary policy meetings, members of the Governing Council also participate in public events, make speeches and give interviews to the press. In March 2020, they also started writing blog posts to provide insights on recent policy decisions and to discuss specific timely topics related to the euro area economy³.

However, the ECB, unlike other major central banks like the Fed, the Bank of England (BoE), and – as we will see in the next section – the Bank of Japan (BoJ), publishes neither the detailed minutes of its monetary policy meetings nor the votes of Governing Council members. The ECB started publishing so-called 'monetary policy accounts' in February 2015 after each meeting, but these accounts remain imprecise, and when disagreements (most often called "reservations") are mentioned, the points of view are kept impersonal. On this particular issue of the publication of the deliberations, the Treaties leave open the possibility of greater transparency, but the decision lies entirely with the ECB⁴. There is no legal obligation for the ECB to provide access to its deliberations, and so far the Governing Council has decided not to publish detailed minutes or the votes of its members.

Although full transparency on every issue is not a panacea for central banking (Demertzis and Hallett, 2007), we consider that this lack of transparency on the votes can be problematic. For instance, as shown by Claeys and Linta (2019), decisions on the eligibility criteria and haircuts applied to assets to be used as collateral in the refinancing operations of the ECB are very opaque, even though these decisions can have a major impact on which assets can be considered as safe assets by the market. Given the importance of these sometimes controversial decisions, the ECB should be more transparent

² See for instance: European Central Bank Press Conference on 25 July 2019, <https://www.ecb.europa.eu/press/pressconf/2019/html/ecb.is190725~547f29c369.en.html>.

³ See European Central Bank, The ECB Blog, available at <https://www.ecb.europa.eu/press/blog/html/index.en.html>.

⁴ Article 132 of the TFEU stipulates that "The European Central Bank may decide to publish its decisions, recommendations and opinions", while Article 10 of the Statute of the ESCB and ECB adds that: "The proceedings of the meetings shall be confidential. The Governing Council may decide to make the outcome of its deliberations public".

about how these decisions are taken, in particular when it concerns the sovereign bonds of euro area members.

The main reason for the secrecy is that the ECB considers that detailed discussions or votes could result in political pressure on members of the Governing Council, especially from their home countries, should the economic interests of a Member State be at odds with those of the euro area as a whole. This degree of privacy is seen by the ECB as a necessary safeguard of its independence.

2.3. The ECB's relationship with the European Parliament

As far as its monetary policy task is concerned⁵, the ECB is accountable to the European Parliament, as established in the TFEU, the Treaty of the European Union (TUE), and the Protocol on the Statute of the European System of Central Banks and of the ECB. These three legal documents, together with the European Parliament's Rules of Procedure govern the interactions between the two EU institutions.

The EU Treaties require the ECB to publish an annual report, to be presented at the European Parliament by the ECB president⁶. This publication and its presentation provide an occasion for the EP to adopt a resolution about the ECB⁷, allowing the EP to express its opinion on ECB monetary policy decisions, with the Committee on Economic and Monetary Affairs (ECON) as the responsible committee. It has become customary for the Vice-President of the ECB to present the ECB annual report to ECON on its publication (typically in April), providing time for the EP to draft the aforementioned resolution for the plenary session in which the ECB president presents the report.

In addition to this yearly requirement, the EU treaties allow for additional exchanges between the ECB and the EP, based on Article 284 of the TFEU: "The President of the European Central Bank and the other members of the Executive Board may, at the request of the European Parliament or on their own initiative, be heard by the competent committees of the European Parliament". Furthermore, given that Article 232 allows the EP to establish their own Rules of Procedure, the EP has used this opportunity to increase the intensity of its exchanges with the ECB through rule 135: "The President of the European Central Bank shall be invited to attend meetings of the committee responsible at least four times a year in order to make a statement and to answer questions [...] If they or Parliament so request, the President, Vice-President and other Members of the Executive Board of the European Central Bank shall be invited to attend additional meetings".

This rule establishes the legal basis for the meeting known as the Monetary Dialogue, the quarterly hearing of the ECB president by the European Parliament's ECON Committee. The ECB President typically makes an introductory statement followed by questions from Members of the European Parliament (MEPs). Before each meeting, the European Parliament also assembles a panel of external experts to prepare and present reports on relevant monetary policy topics, published on the EP's website⁸.

⁵ Concerning the ECB supervisory role (which is not discussed in this briefing note), the interactions between the ECB and the European Parliament are established in the EU regulation 1024/2013 (<https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32013R1024>) and formalised in detail in an Interinstitutional Agreement concluded in 2013: [https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32013Q1130\(01\)&from=EN](https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32013Q1130(01)&from=EN).

⁶ Article 284 of the TFEU states that: "The European Central Bank shall address an annual report on the activities of the ESCB and on the monetary policy of both the previous and current year to the European Parliament, the Council and the Commission, and also to the European Council. The President of the European Central Bank shall present this report to the Council and to the European Parliament, which may hold a general debate on that basis."

⁷ See for instance the EP report on the ECB annual report for 2018: https://www.europarl.europa.eu/doceo/document/A-9-2020-0016_EN.html.

⁸ Reports are available at: <https://www.europarl.europa.eu/committees/en/econ/econ-policies/monetary-dialogue>.

The Monetary Dialogue represents the primary channel for ECB accountability. However, whether these hearings provide effective oversight is debateable. MEPs' questions are often unfocused, and many questions are not related to monetary policy or financial issues, but focus on other topics, often of national or even personal interest. There is little specific scrutiny of the ECB's recent track record in fulfilling its mandate. Perhaps as a result, these hearings receive little media attention, and their market effect is negligible (Fraccaroli et al., 2018). This is in contrast to other speeches or interviews given by the President of the ECB.

Finally, the EP Rules of Procedure provide MEPs with another way to interact with the ECB by allowing them to submit written questions to the ECB⁹, a possibility that has been used quite extensively in recent years by MEPs (the number of letters sent per year peaked in 2015 at 152).

While all these tools allow MEPs to monitor the ECB's activities and to question the ECB President and other members of the Executive Board, the EP does not have the power to sanction the ECB, or to initiate legislation to change the ECB framework, should MEPs consider that the ECB is not fulfilling its mandate.

Indeed, to amend fundamental aspects of the ECB's mandate or its accountability framework would require the approval of all Member States. It is true that the European Parliament can participate in the amendment of certain sections of the ESCB/ECB statute¹⁰. However, there are two caveats: first, the articles that can be modified mainly relate to less fundamental issues, and, second these amendments must be done under the EU's ordinary legislative procedure, meaning that the EP does not have the right of initiative, which belongs to the European Commission, and that the Council needs to agree with the EP.

The appointment of decision-makers could provide another way for the EP to influence the policy adopted by the ECB in the future. But on that front, the role of the European Parliament is also very limited. The European Parliament only participates in the appointment of the members of the ECB's Executive Board in an advisory capacity, as it can only provide a non-binding opinion, similarly to the current ECB Governing Council members¹¹. In practice, the EP holds a hearing for prospective Executive Board candidates and has a vote. If this vote is negative, the EP can ask European Council for a new candidate, but the Council has no obligation to comply¹². The EP's influence over the choice of ECB Executive Board members relies exclusively on peer pressure. These appointments are a prerogative of the Council. This is not a problem per se, as the Council is also a legitimate institution representing European Member States and their citizens. However, it could be considered inconsistent to give the responsibility for oversight and the responsibility for appointments to different institutions. That said, even if the Council is able to choose Executive Board members, its influence over their decisions of is

⁹ Rule 140 states that: "Any Member may put a maximum of six questions for written answer per month to the European Central Bank [...] If a question for written answer has not received a reply within six weeks, it may, at the request of its author, be included on the agenda for the next meeting of the committee responsible with the President of the European Central Bank".

¹⁰ Article 129 of the TFEU: "Articles 5.1, 5.2, 5.3, 17, 18, 19.1, 22, 23, 24, 26, 32.2, 32.3, 32.4, 32.6, 33.1(a) and 36 of the Statute of the ESCB and of the ECB may be amended by the European Parliament and the Council, acting in accordance with the ordinary legislative procedure. They shall act either on a recommendation from the European Central Bank and after consulting the Commission or on a proposal from the Commission and after consulting the European Central Bank".

¹¹ Article 283 of the TFEU: "The President, the Vice-President and the other members of the Executive Board shall be appointed by the European Council, acting by a qualified majority, from among persons of recognised standing and professional experience in monetary or banking matters, on a recommendation from the Council, after it has consulted the European Parliament and the Governing Council of the European Central Bank".

¹² Rule 130 of the EP Rules of Procedure: "1. The candidate nominated as President, Vice-President or Member of the Executive Board of the European Central Bank shall be invited to make a statement before the committee responsible and to answer questions put by its members. 2. The committee responsible shall make a recommendation to Parliament as to whether the nomination should be approved [...] 4. If the opinion adopted by Parliament on a nomination is unfavourable, the President shall ask for the withdrawal of the nomination and for the submission to Parliament of a new nomination".

also limited by the fact that board members' 8-year terms are not renewable. Given that re-appointment is not possible, this means that once someone has been appointed, they have no strong incentive to please those with the power to appoint. This was again decided in order to provide a high degree of independence to the Executive Board members, but the price to pay for that independence is that there exists no mechanism to incentivise them to do their jobs properly and fulfil their mandates after they have been appointed.

Furthermore, the European Parliament does not have the ability to sanction central bankers for their actions, in particular for the failure to fulfil their mandate. The ESCB/ECB statute contemplates the possibility of the EU Court of Justice retiring a member of the ECB's Executive Board. However, this process cannot be initiated by the EP but only by the ECB itself, and it would require either a serious allegation of misconduct or a medical reason making it impossible for a board member to perform his or her duties¹³. Therefore, it is highly unlikely that this could be used as a credible threat to incentivise Executive Board members to fulfil their mandates more diligently.

Finally, it is also interesting to note that even though the ECB is accountable to the EP, the possibility for other institutions (for members of the European Commission or the president of the Council) to be present during the ECB's Governing Council meetings is not offered to MEPs¹⁴.

Overall, the power of the European Parliament to discipline the ECB is very limited. There is rather little the EP can do to incentivise the ECB to fulfil its mandate beyond monitoring its activities and asking questions to the ECB President in the Monetary Dialogue. That is why it is crucial that this occasion is well used to increase the European Parliament pressure on the ECB to do its job well. We will come back to this in our final section.

¹³ Article 11 of the Statute stipulates: *"If a member of the Executive Board no longer fulfils the conditions required for the performance of his duties or if he has been guilty of serious misconduct, the Court of Justice may, on application by the Governing Council or the Executive Board, compulsorily retire him"*.

¹⁴ Article 284 of the TFEU states that: *"1. The President of the Council and a Member of the Commission may participate, without having the right to vote, in meetings of the Governing Council of the European Central Bank. The President of the Council may submit a motion for deliberation to the Governing Council of the European Central Bank. 2. The President of the European Central Bank shall be invited to participate in Council meetings when the Council is discussing matters relating to the objectives and tasks of the ESCB"*.

3. LESSONS FROM THE BANK OF JAPAN AND THE JAPANESE DIET

In Claeys et al. (2014) we discussed the Fed's and the BoE's accountability frameworks and compared them with the ECB. In this paper, we complete our study of the accountability of major central banks around the world by discussing how the Bank of Japan (BoJ) is accountable to the Japanese National Diet – i.e. the bicameral legislature of Japan consisting of the House of Representatives and the House of Councillors. The BoJ is interesting because its functioning is very different to its counterparts in Europe and North America.

The Bank of Japan was created in 1882, following the Meiji restoration and shortly after the establishment of the yen as the new decimal national currency, but its current functioning was primarily determined by the 1997 Bank of Japan Act. The Act represented a move towards greater independence – to increase the credibility of the central bank both domestically and in the eyes of international capital markets (Dwyer, 2004) – and towards more transparency – to ensure the accountability of the central bank in the light of its greater autonomy¹⁵. The BoJ Act also set the BoJ's main objectives and the functioning of its decision-making body, a Policy Board of nine members, including the Governor and two Deputy Governors.

In this section, we assess how the BoJ is held to account, based on the three criteria highlighted before: 1) clarity of its mandate and objectives enshrined in law; 2) transparency of decision-making and implementation of monetary policy; and 3) degree of responsibility held by the political body holding the central bank accountable (in appointments, monitoring, possibility to change the law or to sanction the central bank, etc.).

3.1. Mandate of the BoJ

As explained before, enshrining specific and clear objectives into law is essential to ensure the accountability of the central bank, as it provides a benchmark that aids political bodies in monitoring and assessing the central bank's performance. This is done in Article 1 of the BoJ act: "(1) The purpose of the Bank of Japan, or the Central Bank of Japan, is to issue banknotes and to carry out currency and monetary control. (2) In addition to what is prescribed in the preceding paragraph, the Bank of Japan's purpose is to ensure smooth settlement of funds among banks and other financial institutions, thereby contributing to the maintenance of stability of the financial system", while Article 2 adds that: "Currency and monetary control by the Bank of Japan shall be aimed at achieving price stability, thereby contributing to the sound development of the national economy".

In theory, this means that the BoJ has a double mandate: it is responsible for ensuring both financial and price stability. However, there is neither a clear ranking between the two main objectives nor a numerical target for price stability in the BoJ Act. This means that in practice the BoJ should determine its own quantitative definition of price stability and would need to rank its objectives if a trade-off between the two were to arise.

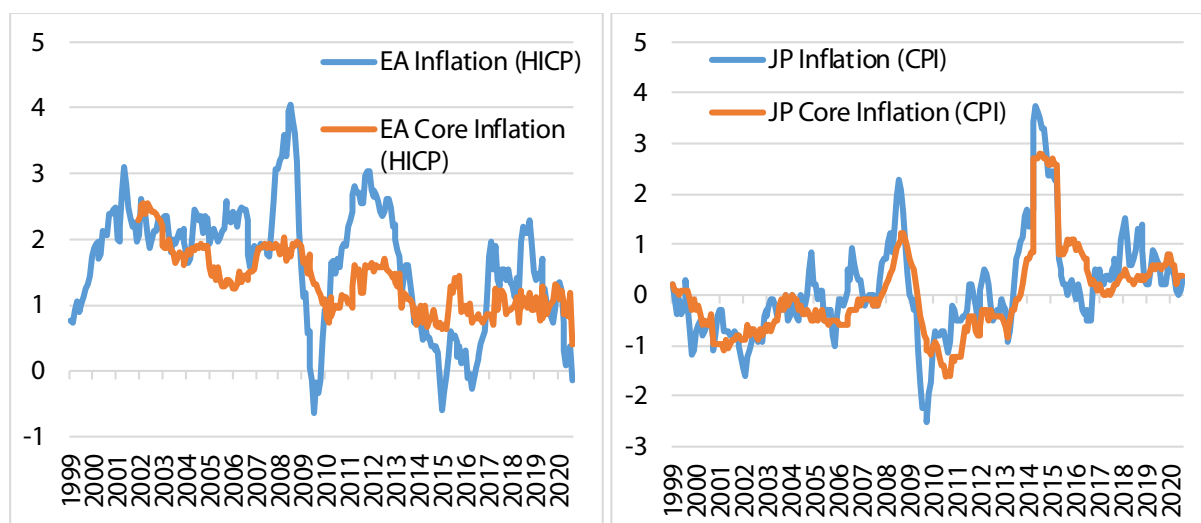
As far as price stability is concerned, the Bank of Japan has established its own quantifiable target which has evolved over the years. Between 2006 and 2012 the BoJ had an implicit target of 1 percent, which was the level considered by Policy Board members as consistent with price stability in the medium to long term. In February 2012, the BoJ announced an official inflation target "within a positive range of 2

¹⁵ Article 3(1) of the BoJ Act stipulates that: "The Bank of Japan's autonomy regarding currency and monetary control shall be respected", while Article 3(2) adds that: "The Bank of Japan shall endeavor to clarify to the citizen the content of its decisions, as well as its decision-making process, regarding currency and monetary control".

percent or lower" while setting the goal at "1 percent for the time being" (BoJ, 2012). However, less than a year later, in January 2013, it introduced a new price stability target "at 2 percent in terms of the year-on-year rate of change in the consumer price index" (BoJ, 2013b). We see this as a positive development not only because a clearer target should act (at least in theory) as a better focal point to anchor inflation expectations (Blinder et al., 2008) but also in terms of accountability. While the new target is not enshrined in law and has not been determined directly by an elected assembly, the 2 percent target finally provides a precise and understandable quantitative benchmark against which the Diet can judge the BoJ's performance.

The fact that the adoption of the new target coincided with the election of prime minister Shinzo Abe in December 2012 – who publicly called for such a change before the election – did not escape observers (e.g. Neely, 2013), who interpreted this as a sign of political influence over the BoJ's decision. Another strong indication that this change might have resulted from the political pressure from the new government is that this move was executed in parallel to the issuance of a joint statement between the BoJ and the government in which the BoJ pledged to "pursue monetary easing and aim to achieve this target at the earliest possible time" (BoJ, 2013a). This seems to indicate, at least on that occasion, some form of political involvement in setting the BoJ target. Pressuring the BoJ to adopt a higher and more precise target might have been justified, given the BoJ's underperformance leading to two decades of mild deflation from the BoJ Act of 1997 to Abe's election at the end of 2012 (Figure 1). However, the new target was hardly the result of a transparent review of the BoJ target by the Diet, but of indirect pressure from the new government, and was done in a rather opaque manner.

Figure 1: Headline and core inflation in the euro area (LHS) and in Japan (RHS), year on year change in %



Source: Bruegel based on Eurostat and Statistics of Japan. Notes: Euro area core inflation excludes energy, food, alcohol and tobacco; Japanese core inflation excludes fresh foods and energy.

3.2. BoJ Transparency

The need for transparency is enshrined in the Bank of Japan Act¹⁶. In practice, in Japan this entails that the BoJ Policy Board releases its monetary policy decisions, the detailed guidelines for its open market

¹⁶ See previous footnote.

operations and, more generally, its views on economic and financial developments. As for other central banks, this takes various forms.

First, to fulfil its legal obligations¹⁷, after each Monetary Policy Meeting (MPM), held eight times per year, the BoJ releases a 'Statement on Monetary Policy' containing the decisions taken by the Policy Board, and the BoJ governor usually holds a press conference later on the same day. This is followed by the publication of a 'Summary of Opinions' a few days later. In addition, the main report in which the BoJ explains its policies and describes the state of the Japanese economy in detail, the Outlook for Economic Activity and Prices, is published quarterly (immediately after every second MPM).

Second, the minutes of the monetary policy meetings are published around one month later. In contrast to the ECB, these minutes are very precise and include the votes cast by each member of Policy Board on each decision, as well as the reasons for dissent from those not who have voted against the majority. Exact transcripts of MPM discussions are also released after ten years.

Finally, the BoJ Governor and the other members of the Policy Board also make regular speeches to explain the decisions of the BoJ and provide their views on the situation of the Japanese economy.

3.3. Relationship of the BoJ with the Diet and the government

Parliamentary hearings have become an essential tool in holding central banks accountable, and this is also the case in Japan. In that regard, to fulfil its legal accountability obligations to the Diet¹⁸, the BoJ submits twice a year a 'Report on Currency and Monetary Control' to the Parliament, in June and December. These publications are accompanied by hearings in each of the two chambers of the Diet to explain the main points of the reports, resulting in practice in a minimum of four annual hearings on monetary policy matters. The BoJ Governor also frequently attends other sessions of the Japanese parliament¹⁹. As far as we can see²⁰, the hearings lead to a courteous interaction between a limited number of Members of the Diet and the BoJ Governor. In these hearings, Japanese Parliamentarians typically intervene for around five minutes and can ask follow-up questions, in which lawmakers can respond or question the governor's response.

In addition, unlike the ECB, the Bank of Japan is more directly subject to the control of the Parliament, because the Bank of Japan Act was passed by both houses of Parliament in 1997. This means that the functioning of the BoJ could be amended with a new bill with a simple majority in both chambers, the House of Representatives and the House of Councillors. This provides the Diet with the power to alter many of the above-mentioned norms.

¹⁷ Article 20 of the Act: "(1) After each Board meeting for monetary control matters, the chairperson shall promptly prepare a document describing an outline of the discussion at the meeting in accordance with the decisions made by the Board, and make public the document following its approval at another Board meeting for monetary control matters. (2) The chairperson shall prepare a transcript of each Board meeting for monetary control matters in accordance with the decisions made by the Board, and make public the transcript after the expiration of a period of time which is determined by the Board as appropriate."

¹⁸ Article 54 of the Bank of Japan Act states: "(1) The Bank of Japan shall, approximately every six months, prepare a written report on the Policy Board [...] and conditions of business operations that the Bank has conducted based thereon and submit it to the Diet through the Minister of Finance. (2) The Bank of Japan shall endeavor to explain to the Diet the written report set forth in the preceding paragraph. (3) The Bank of Japan's Governor or the chairperson of the Policy Board, or a representative designated by them, shall attend the sessions of the House of Representatives, the House of Councillors, or their Committees when requested by them, in order to explain the state of the Bank's business operations and property."

¹⁹ For instance, Lepper and Sterne (2002) counted 34 appearances of Policy Board members in front the Diet in one year (from May 2000 to May 2001), placing Japan second (after Israel) in a list of 14 mayor central banks in terms of parliamentary appearances.

²⁰ To the best of our knowledge there are no transcripts available of these hearings (in English), but videos are available online. See for instance, recent hearings with the House of Councillors: <https://www.youtube.com/watch?v=xjCabZ2MIV4>, <https://www.youtube.com/watch?v=Sf24JLlbY6c>, <https://www.youtube.com/watch?v=w1uQFyTla6Q> and with the House of Representatives: <https://www.youtube.com/watch?v=zz5OL8V7560>.

The appointment (and possible reappointment) of Policy Board members is also a tool of parliamentary influence, given that these members will ultimately take monetary policy decisions²¹. In Japan, the Governor, two Deputy Governors and the six other Members of the Policy Board “shall be appointed by the Cabinet, subject to the consent of the House of Representatives and the House of Councillors”, as per Article 23 of the BoJ Act. This means that the Japanese Diet has the ability to explicitly veto appointments to the Policy Board²². In addition, all nine members, which are appointed for five years, can be reappointed, with no specific legal limit on the number of mandates. Reappointments are not that frequent: the current governor, Haruhiko Kuroda, is the first BoJ governor to serve more than one five-year mandate since Masamichi Yamagiwa who served for almost two full terms from 1956 to 1964. However, the option for the Diet to accept or reject a reappointment could provide a source of influence over future board members’ decisions.

In parallel to the BoJ’s relationship to the legislative branch, the Bank of Japan Act also established the need for permanent contact between the BoJ and the executive branch of the government, with Article 4 giving a greater role to the government than is customary in other independent central banks around the world: “The Bank of Japan shall, taking into account the fact that currency and monetary control is a component of overall economic policy, always maintain close contact with the government and exchange views sufficiently, so that its currency and monetary control and the basic stance of the government’s economic policy shall be mutually compatible”.

The degree of government involvement in monetary policy matters is reinforced by the fact that ministers and government officials can take part in monetary policy meetings²³. The BoJ Act even specifies that the government representatives present in the MPM can “submit proposals concerning monetary control matters, or request that the Board postpone a vote on proposals on monetary control matters”. Minutes from these meetings reveal the regular presence of between two and five government representatives (typically ministers and other high-ranking officials such as state ministers and vice-ministers). These government representatives actively participate in meetings, and minutes even contain a section titled “remarks by government representatives”, which covers the activities that “the government expect” the bank to engage in after the meeting²⁴. This leaves little doubt about the high degree of influence to government representatives in monetary policy matters.

There are even certain areas in which the government can directly instruct the BoJ to conduct specific operations. This is the case for actions to influence the exchange rate. The BoJ should not independently look to influence the exchange rate, but can be instructed to do so by the government, as stated within the BoJ’s own Functions and Operations of the Bank of Japan document²⁵: “When the yen becomes unstable in the foreign exchange market, the Japanese government (Finance Minister) may instruct the Bank of Japan, its agent, to conduct foreign exchange intervention by buying or selling yen against foreign currencies as needed”²⁶. This differentiates clearly the BoJ from other major central

²¹ Article 15 of the BoJ Act stipulates that “matters concerning currency and monetary control shall be decided by the (Policy) Board”. Article 18 further states that “matters shall be decided by a majority of votes cast by (Policy) Board members who are present”. The Policy Board also elects its own chairperson, who shall decide in case of a tie.

²² Indeed, while Article 23 further states appointment can occur without consent “if the Diet is out of session”, this appointment must be approved ex-post. Indeed, “if the Cabinet fails to obtain such ex post approval, it shall immediately dismiss the said Governor, Deputy Governor, or Member of the Policy Board”.

²³ Article 19 of the Act stipulates that: “The Minister of Finance or the Minister of State for Economic and Fiscal Policy [...] (in the case where the office is vacant, it shall be assumed by the Prime Minister) may, when necessary, attend and express opinions at Board meetings for monetary control matters, or may designate an official of the Ministry of Finance or the Cabinet Office, respectively, to attend and express opinions at such meetings”.

²⁴ See minutes from the last five MPM: BoJ (2020a, 2020 b, 2020 c, 2020d and 2020 e).

²⁵ Bank of Japan, *International Operations and Services*, available at <https://www.boj.or.jp/en/about/outline/data/foboj10.pdf>.

²⁶ The legal basis is Article 40 of the BoJ act, which states that the BoJ “shall buy and sell foreign exchange as an agent handling national government affairs”. It later goes on to specify that “when buying and selling foreign exchange on its own account” the BoJ will “conduct

banks as the exchange rate policy is very often, in practice, under the central bank's responsibility and generally subordinated to monetary policy goals.

The influence of the government even appears to have increased (or at least to have become more visible) in after the election of Shinzo Abe in 2012, who served as prime minister until August 2020. His campaign touched heavily on monetary policy matters, advocating for "unlimited easing" (Dickie, 2012), which led the yen to depreciate by 15% against the US dollar between Abe's nomination as head of the liberal party and his first months in office (even if other factors may have played a role). As mentioned previously, after the election, the BoJ and the government issued a joint statement, in which they pledged to "strengthen their policy coordination" (BoJ, 2013a). In practice, this was mainly done by increasing the role for the Council on Economic and Fiscal Policy, established in 2001 within the Cabinet, whose objective is to: "regularly review the progress in the conduct of macroeconomic policies including monetary policy, the current condition and future prospects of prices in the context of the price stability target under those policies".

Overall, the Bank of Japan operates very differently to other major central banks, being subject to a much greater degree of government involvement in its decision-making. Our analysis indicates that, in the case of Japan, the balance between independence and accountability is clearly tipped towards a high degree of political accountability both legally and in practice, with the government having a significant influence over the BoJ's decisions (in particular since 2013). This has even led some to argue that monetary policy in Japan can sometimes be the outcome of a bargaining process between the Ministry of Finance and the BoJ (Reszat, 2013). It is also worth highlighting that it is clearly the government that plays the greater role and not the Japanese Parliament – although, given that Japan is a parliamentary democracy, this still signifies a degree of indirect parliamentary power.

The ECB is at the opposite end of the spectrum between independence and accountability, and it is not clear that it would be desirable (especially in a multi-country union such as the euro area) to move very far in the direction of the BoJ. But there are still some lessons to be learned when looking at the Japanese framework, which we discuss in the next section.

Table 1: Comparison of the ECB and BoJ in term of accountability

	European Central Bank	Bank of Japan
Legal Basis	TEU, TFEU, Statute of the ESCB, international law (requires unanimity of member states to be altered)	1997 Bank of Japan Act
Accountability to	European Parliament	Japanese Diet (House of Representatives and House of Councillors). Permanent contact with the Government (see below).
Mandate	The ECB's primary mandate is 'price stability', enshrined in the treaties along with secondary objectives. No quantifiable objective is set in law, the ECB can set its own quantitative target for price stability: it is currently defined as a level of inflation, "below but close to" 2% in the medium term (since the 2003	The BoJ's objectives enshrined in the BoJ Act are 'price stability' and 'stability of the financial system'. There is no ranking of objectives, or quantifiable objective set by law. The BoJ can set its own quantitative target for price stability: it is currently defined as 2% inflation (since 2013).

the buying and selling for the purpose which the Minister of Finance specifies as constituting cooperation in the field of international finance, at the request, or upon the approval, of the Minister of Finance".

	clarification). Secondary objectives are very broad and not ranked.	
Meeting Minutes	The ECB does not publish the minutes of its Governing Council monetary policy meetings, however since February 2015 they publish monetary policy accounts following meetings. The EU treaties give the ECB the competence to decide upon this.	The BoJ releases Monetary Policy Meeting (MPM) minutes after each session. While these do not entail a full transcript (these are only available after 10 years) they do include votes cast by each member and reasons for dissent.
Appearances before Parliament	The ECB President appears before the ECON Committee four times a year. At Parliament's request, the President, Vice President and other members of the Executive Board shall be invited to attend additional meetings.	The Governor and other members of the Policy Board shall attend sessions in the House of Representatives and House of Councillors or their Committees when requested by them (no specific number of hearings, subject of coordination).
Reports and written communication	The President presents the Annual Report to the plenary, previously presented to the ECON Committee by the Vice-President. The ECB answers written questions from MEPs	The Bank of Japan submits a 'Report on Currency and Monetary Control' to the Diet in June and in December, followed by a hearing with the Governor in each of the two houses of the Diet.
Appointment of Board Members	The President, the Vice-President and other members of the Executive Board shall be appointed by the European Council, after consulting the European Parliament and Governing Council.	The Governor, two Deputy Governors and the other six members of the Policy Board shall be appointed by the Cabinet, subject to the consent of the two houses of the Japanese Diet.
Sanctions/Removal from office	The President and other Executive Board members cannot be dismissed by politically elected bodies. On application by the Governing Council or Executive Board, the EU Court of Justice may remove an Executive Board Member from office.	Members of the Board may not be dismissed over Policy differences (Article 25 BoJ Act), only certain types of misconduct as well as failure to receive Parliamentary approval following appointment.
Government involvement	The ECB has full operational independence. The relevant Commissioner and the President of the Council may attend Governing Council meetings.	The BoJ maintains close contact with the government to ensure coordination between economic and monetary policy. Government members actively participate in the MPM. The government may instruct the BoJ to conduct foreign exchange interventions under certain circumstances.

Source: Bruegel based on ECB and BoJ.

4. RECOMMENDATIONS TO IMPROVE ECB ACCOUNTABILITY BEFORE THE EUROPEAN PARLIAMENT

With the COVID-19 pandemic, the euro area faces the worst contraction of GDP ever recorded, forcing the ECB to play again an influential role and introduce a wide range of new measures in 2020. This makes an effective oversight of the ECB more important than ever.

To make the ECB more accountable to the European Parliament, we make a series of recommendations that can be immediately implemented by the Parliament and do not involve changes to the European Treaties. Our recommendations can be divided into three main categories. First, the quarterly hearing of the president of the ECB, the so-called Monetary Dialogue, should be improved. The EP can do this unilaterally as its format is based on its own Rules of Procedure and general practices. Second, the EP should continue to push for greater transparency in ECB decision-making. As discussed before, under the current Treaty, this is largely at the discretion of the ECB, but this also means that the EP has some scope to lobby for a greater degree of transparency. Third, the EP could help the ECB rank its secondary objectives, as the treaties clearly enshrine the primacy of achieving price stability, but specify little else about the ECB's so-called secondary objectives. As these objectives remain eminently political, they should be ranked by political bodies and not by the ECB. This role should be played by the EU's co-legislators. The EP should also try during the on-going review of the ECB's strategy to push the ECB to adopt a clearer and better definition of price stability.

4.1. Improving the monetary dialogue

Article 284 of the TFEU provides the general framework of ECB accountability to the EP, but the details about the Monetary Dialogue, its format and frequency, actually come from the European Parliament's Rules of Procedure²⁷. As a result, the debates will typically contain a section when time is pre-allocated to speakers in accordance with the political groups. The debate may then have a second section where the Chair can call upon Members freely.

In practice, recent Monetary Dialogues have followed a similar procedure: a two-hour meeting that includes a 15 minutes introductory statement by the ECB President, followed by a Q&A session with around 15 initial slots pre-allocated to MEPs from different political groups (with two minutes maximum for the questions and three minutes maximum for the answers by the ECB President) and finally a 'catch-the-eye' (unallocated) session, if time allows at the end of the meeting, in which other MEPs present can ask questions, typically with no more than one minute allowed. In addition, before the meeting takes place, a preparatory meeting with a panel of experts is set up to provide expertise to MEPs, with topical reports and presentations, which also allows for informal exchanges between the experts and the MEPs or their assistants.

There are several procedural changes that could lead to a more effective dialogue that would strengthen the oversight role of the European Parliament:

First, the Monetary Dialogue rarely focuses on assessing the ECB's performance, either in fulfilling its price stability mandate by meeting its self-assigned quantitative target, or in supporting the EU to fulfil its objectives. Instead, MEPs ask questions on a broad range of issues, sometimes of national focus and sometimes even on issues that are not of the ECB's responsibility, as noted by Jean-Claude Trichet

²⁷ They are laid out in Rule 135, which specifies that there should be a "general debate", and the procedure is specified in Rule 216 and especially in Rule 171. This states that: "The Conference of Presidents may propose to Parliament that speaking time be allocated for a particular debate. Parliament shall decide on this proposal without debate."

during the Q&A during the June 2011 Monetary Dialogue²⁸. In order to ensure the focus of the EP on the ECB's mandate, it could become customary for the Chair of the ECON Committee to ask an agreed set of questions that remain constant at every hearing. Examples include inquiring about the reasons for the divergence of inflation from the ECB's target, the measures taken to remedy this, the reasons for the most recent decisions of the Governing Council and any secondary objectives that have recently been taken into account. This would allow the EP to effectively assess how the ECB is fulfilling its mandate, and put the ECB President in a position to justify all major decisions in front of the European citizens' representatives. Also, given the doubts raised by the German Constitutional Court about the proportionality of the ECB's actions in its 5 May 2020 ruling on the Public Sector Purchase Programme (BVerfG, 2020), the EP could pay particular attention to the issue of the proportionality of the tools used by the ECB. In general, fixed questions on these issues (performance and proportionality) in every meeting would also facilitate comparison over time. From a symbolic perspective, the setting of the Monetary Dialogue could also be changed so that it looks more like a hearing than a conference given by the ECB President.

Second, the number of MEPs that participate in the dialogue should be reduced, so that participants can have a real dialogue with the ECB President with the opportunity to ask follow-up questions. In the case of the Bank of Japan, members of the Diet have a proper conversation with the governor, with follow-up questions that allow them to reply or ask for additional details about answers given by the BoJ governor. The US Congress' system of hearings with the Fed also works more effectively at least in part because it involves a much smaller number of committee members. One way for the EP to do this could be to give all the allotted time to seven ECON coordinators, especially as these must express the view of their parliamentary groups. As such they would be less prone to ask questions that are of little value, in particular questions that are not related to the ECB's responsibilities but are of personal interest to a particular MEP.

Third, the experts participating in the preparatory meeting and writing briefings to advise MEPs on pertinent topics regarding monetary policy and recent ECB performance could be better used. While we believe that it is useful – given the technical nature of monetary policy – to help MEPs to provide effective oversight, in practice attendance at preparatory meetings is generally very low and thus their value reduced. More attention could be given to the topics chosen by the MEPs themselves for each dialogue and the briefing papers prepared, so that these relevant topics are discussed during the hearing.

4.2. Pushing for even more transparency in decision making

While the ECB was an early innovator as one of the first major central banks to introduce a press conference with a Q&A session after each of its policy decisions, and has also made substantial progress over the years when it comes to transparency, it still lags other central banks in some particular aspects. This is the case when it comes to publishing the minutes of its monetary policy meetings and disclosing the votes of the members of the Governing Council.

In this aspect, it differs from other major central banks such as the Bank of Japan, as seen above, and also the Bank of England and the Fed. Even if, since 2015, the ECB has published accounts after each monetary policy meeting that go through the main areas of discussion, the monetary accounts remain

²⁸ Jean-Claude Trichet in the June 2011 Monetary Dialogue: "I would have expected a lot of questions on our monetary policy, on the level of inflation, on what inflation will be in two years' time, on whether our projections are right or wrong, and on whether we are right or wrong to have the present level of interest rates, taking into account other decisions taken elsewhere in the world. However, I see that you have such a confidence in my institution that these are not a problem or an issue at all! I have also had a lot of questions on issues for which we are not responsible." (p.15, <https://www.europarl.europa.eu/cmsdata/174379/20110711ATT23762EN.pdf>).

mostly focused on assessing the economic situation (rather than laying out the different points of view of the members of the Governing Council) and, crucially, views are not attributed to the speakers. Similarly, the votes cast by each member remain private.

This could be changed by the ECB unilaterally. It is legally at the discretion of the ECB to decide to publish more detailed minutes²⁹. Trends would indicate the ECB has been moving in the direction of greater transparency for some time, not only by publishing accounts of meetings but also more generally issuing more and more details to back up their decisions.

This is not only possible, but also clearly desirable in our view. Without transparency on votes, incentives at the individual level become weaker, especially in a large decision-making body such as the ECB Governing Council. While the argument has been made in the opposite direction, with the ECB arguing that national central bank governors would be subject to national pressure, we believe that greater transparency in the vote would on the contrary allow for greater scrutiny of decisions and incentivise the governors to vote not with a national mind-set but according to the interests of the entire euro area, as they are supposed to do according to the TFEU. As argued by Buiter, (2014): “Voting in the national rather than the European interest is a lot easier if one cannot be held to account for such mandate-violating actions because these votes are not in the public domain. Any formal political or judicial sanctions against such mandate violations become impossible if there are no formal votes or if the individual votes remain a secret.”

In addition, we believe that in the current circumstances publishing more detailed minutes of the discussions in the Governing Council would also be in the interest of the ECB. It would in particular help the ECB allay the concerns of the German Constitutional Court about the proportionality of its actions (BVerfG, 2020) by showing that there are frank and honest debates in the Governing Council in which pros and cons and alternative policies are discussed. Would that mean that the difficult negotiations between members of the Governing Council would move to another, more informal forum, before the actual meeting, to avoid exposing their disagreements to the world? This is not what we observe at the BoJ, the Fed or the BoE, where members of monetary committees have genuine discussions during their meetings, even if they know they are going to be quoted in the minutes. Knowing that they are going to be quoted in the minutes can give members an incentive to take their jobs seriously and to participate actively in the discussion.

Therefore, it is up to the European Parliament to use its political influence to push the ECB for greater transparency, so that it can best ensure the ECB remains accountable to its citizens. The EP should in particular use the occasion given by the on-going ECB strategy review to do that.

4.3. Ranking the ECB's secondary objectives

Finally, there is the question of the ECB's objectives. While its primary objective, price stability is clearly enshrined in the treaties, Article 127 of the TFEU adds that the ECB should also contribute to the achievement of the EU objectives (as long as it does not endanger price stability). The ECB is thus entitled to pursue these objectives as secondary aims, but has little guidance on their respective priority. This has become a particularly relevant aspect of the debate recently, due to widespread calls for the ECB to ‘green’ its monetary policy in order to participate to the fight against climate change.

²⁹ Article 132 of the TFEU states that the ECB may “decide to publish its decisions, recommendations and opinions”, while Article 10 of the ESCB statute allows the Governing Council to “decide to make the outcome of its deliberations public”.

In this context, it would therefore be useful to have additional clarity on the ranking of these secondary objectives. Such clarity would result in a more detailed mandate, and would help in the EP's assessment of the ECB's performance in meeting its objectives.

We believe this ranking should be decided at the political level and not by the ECB itself. There is no indication of what the ECB should do if these objectives require contradictory policies. These objectives remain at the core of the EU's purpose and cover highly political topics. Deciding between their relative importance is essentially a political endeavour and should be dealt with by political bodies. The ECB, which, under the EU treaties, has some discretion to determine how it views these objectives, should give back this task to the EU's legislators. The European Parliament as representative of European citizens and the Council of the EU as representative of EU Member States should take the primary roles in determining the ranking of secondary objectives. As far as the EP is concerned, its resolution on the ECB's annual report would be a clear medium for the Parliament to make this ranking.

Finally, as far as objectives are concerned, the EP should also use the occasion of the ECB strategy review to push the ECB to adopt a clearer and better definition of price stability, as Japan did in 2013 after tweaking its definition for a while. This would also facilitate its own job of assessing the ECB's performance.

5. CONCLUSION

Once again, the ECB is playing an important role in shouldering the burden of the current crisis, with programmes that will affect financial markets and the real economy. Even if we think that these actions are welcome and warranted by the current situation (Claeys, 2020), it becomes even more important for the ECB to be effectively and democratically held accountable. As the only directly-elected EU institution, the European Parliament has a central role to play. This report has assessed the ECB accountability framework based on three criteria: 1) clarity of mandate and objectives enshrined in law, 2) transparency in decision-making and 3) the degree of responsibility ultimately held by political bodies (power of appointment, instruction and sanction, etc.). The same analysis has also been applied to the practices of the Bank of Japan, in order to identify possible lessons for the ECB.

While the ECB already performs quite well in terms of accountability, there are evident improvements to the process that could be made, some of which can be inspired by BoJ practices. For example, the current version of the Monetary Dialogue does not focus enough on assessing the performance of the ECB in fulfilling its mandate. A hearing with a smaller number of participating MEPs (like in Japan), a set of fixed questions on the ECB's performance (and possibly on the proportionality of the instruments used) and better use of the material produced by the panel of experts could be substantially more effective. It is well within the EP's competences to alter the format of the Monetary Dialogue, as it depends exclusively on the EP's Rules of Procedure. Additionally, while some of our recommendations lie outside the EP's explicit competence, such as the release of Governing Council meeting detailed minutes and votes, the EP should still use its power to call for greater transparency in order to reinforce its own ability to scrutinise the ECB's decisions. Furthermore, it would also be beneficial to clarify several issues surrounding the ECB's mandate, including the ranking of secondary objectives. This is an inherently political decision, and the EP should establish a ranking of secondary objectives to help the ECB decide which secondary objective it should prioritise in case trade-offs arise.

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Accountability at the Fed and the ECB

Karl WHELAN



Abstract

This paper reviews the independence and accountability of the ECB and the Federal Reserve. While the ECB makes significant efforts to be accountable for its actions, there are several improvements that could be made to European institutions to improve its independence and accountability. These include reforming the process of appointing ECB Executive Board members, improving the transparency of ECB decision-making and reforming aspects of the Monetary Dialogue to make the questioning more effective.

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CONTENTS

LIST OF ABBREVIATIONS	93
EXECUTIVE SUMMARY	94
1. INTRODUCTION	95
2. INDEPENDENCE AND ACCOUNTABILITY FOR THE ECB	97
2.1. Appointments	97
2.2. Independence	98
2.3. Accountability	99
3. INDEPENDENCE AND ACCOUNTABILITY FOR THE FEDERAL RESERVE	101
3.1. Appointments	101
3.2. Independence	102
3.3. Accountability	103
4. RECOMMENDATIONS	104
4.1. European Council	104
4.2. ECB	104
4.3. European Parliament	106
5. CONCLUSIONS	108
REFERENCES	109

LIST OF ABBREVIATIONS

ECB	European Central Bank
ECJ	European Court of Justice
ELA	Emergency Liquidity Assistance
FOMC	Federal Open Market Committee
MEP	Member of European Parliament
TFEU	Treaty on the Functioning of the European Union

EXECUTIVE SUMMARY

- **This paper reviews the independence and accountability of the ECB and the Federal Reserve.**
- **While the ECB makes significant efforts to be accountable for its actions, there are several improvements that could be made** to European institutions to improve its independence and accountability.
- These include **reforming the process of appointing ECB Executive Board members, improving the transparency of ECB decision-making** and **reforming aspects of the Monetary Dialogue** to make the questioning more effective.
- **Accountability starts with the process of appointing central bankers.** The European Parliament has correctly called for a dialogue with the European Council about how members of the Executive Board are appointed.
- The paper recommends that the European Council should only appoint Executive Board members that have been **recommended by the European Parliament and should avoid appointing people who are currently serving in political roles.**
- **The ECB can improve its communication procedures and accountability surrounding emergency lending to banks** as past failures in this area have been damaging to its reputation.
- **The ECB should consider providing more information about Governing Council meetings,** including explicit vote tallies and meeting accounts that provide names of which Council members made which points.
- **In many ways, the Federal Reserve's institutions are inferior to those of the Eurosystem.** The Eurosystem is far more independent from political control than the Federal Reserve and the process of appointing the executive board of the ECB is less politically charged than the process of appointing members of the Board of Governors of the Fed.
- **However, the US Congressional hearings with the Federal Reserve chairman are more effective at holding the Fed accountable** for its actions than the Monetary Dialogue is with the ECB.
- **This partly reflects the current procedures of the Dialogue meeting,** which does not feature regular back-and-forth exchanges of views with the President.
- **The ECON committee should consider adapting the Dialogue to have fewer Members asking questions,** but with each member given more time.
- **The committee should also consider having specific themed sub-sessions** where all of the questions for a period of time cover the same topic.
- **The Committee should consider moving the Dialogue meetings to a smaller committee room,** allowing the MEPs to sit closer to the President, in a similar way that Senators and Congressmen sit relative to the Fed Chair at their hearings.

1. INTRODUCTION

The past 40 years have seen the emergence of a consensus among policy makers and mainstream academics that monetary policy is best implemented by central banks that are independent from political influence. Former Federal Reserve chairman, Ben Bernanke (2010), summarised the argument for this position as follows:

“To achieve both price stability and maximum sustainable employment, monetary policymakers must attempt to guide the economy over time toward a growth rate consistent with the expansion in its underlying productive capacity. Because monetary policy works with lags that can be substantial, achieving this objective requires that monetary policymakers take a longer-term perspective when making their decisions. Policymakers in an independent central bank, with a mandate to achieve the best possible economic outcomes in the longer term, are best able to take such a perspective.

In contrast, policymakers in a central bank subject to short-term political influence may face pressures to overstimulate the economy to achieve short-term output and employment gains that exceed the economy's underlying potential. Such gains may be popular at first, and thus helpful in an election campaign, but they are not sustainable and soon evaporate, leaving behind only inflationary pressures that worsen the economy's longer-term prospects. Thus, political interference in monetary policy can generate undesirable boom-bust cycles that ultimately lead to both a less stable economy and higher inflation.”

While these arguments are widely accepted in central banking circles, it could be argued that similar arguments could be made about fiscal policy. Fiscal policy can also work with lags and since budgetary policy making generally occurs in annual cycles, fiscal policy tends to be innately slower to implement than monetary policy. And as discussed in the enormous literature on “political business cycles”, there is evidence that governments manipulate tax and spending policies to improve their chances of re-election.

Of course, decisions by governments about what precisely to spend money on and who to tax have clear and direct distributional consequences and turning over these decisions to “technocrats” is not likely to be politically feasible. That said, while monetary policy is seen as a more sensible candidate for technocratic control, it is still the case that monetary policy decisions can have distributional effects. This has always been the case (for example interest rate cuts have a positive effect on borrowers and a negative effect on savers) but as central bank balance sheets have expanded and central banks have taken on new and extensive powers such as “macro-prudential” policies and greater responsibility for banking supervision, the implications of their actions for income distribution have become more obvious.

Given these developments, it is appropriate that more questions need to be asked about how central bank independence should work. Some influential thinkers in the world of central banking, such as Sir Paul Tucker (2018), former Deputy Governor of the Bank of England, have been flagging the dangers associated with central banks having too much independence.¹ Of particular importance is the question of accountability for independent central banks. What should be the mechanisms through which a central bank explains its actions? What should happen if an independent central bank persistently fails to meet the goals set for it by legislation? What happens if an independent central bank acts outside its legal mandate or fails to always operate in the wider public interest?

¹ This short video interview with Tucker gives a good sense of his arguments: <https://www.youtube.com/watch?v=XVN5pk4cbXM>.

There are unlikely to be simple answers to these questions and the right answers likely vary depending on the institutional setting. For example, the correct forms of accountability may depend on the extent of the powers central banks are given beyond monetary policy. The political context also matters: Accountability is inherently more complex for transnational bodies such as the European Central Bank than it is for traditional national central banks. For the European Central Bank, political accountability lies largely in the hands of the European Parliament – most notably through the regular Monetary Dialogue with the ECB President – but the interaction between a trans-national independent agency and a trans-national parliament is riddled with political and operational complexities.

Related to central bank accountability is the question of transparency. The more transparent a central bank is, the less need there to use political accountability mechanisms to get central banks to explain their actions to the public. At the same time, independent central banker may feel there is a point where too much transparency threatens their ability to do their jobs as effectively as they would like, in particular making it hard to make decisions that would be politically unpopular in the short run.

This paper explores some issues related to the independence and accountability of the Eurosystem and provides some comparisons with the Federal Reserve System. Section 2 provides a brief outline on the independence of the Eurosystem and current procedures relating to accountability of its monetary policy. Section 3 discusses how the Federal Reserve's independence and political accountability works in practice. Section 4 then provides some recommendations for European Council, for the ECB and for the Economic and Monetary Affairs Committee (ECON) in relation to the operation of the Monetary Dialogue.

2. INDEPENDENCE AND ACCOUNTABILITY FOR THE ECB

To understand the need for accountability at central banks, it is important to understand the full relationship between these institutions and politicians. In the next two sections, I describe how the European Central Bank and Federal Reserve interact with the political sphere in three different ways: How the central bankers are appointed, the level of independence that central bankers have in setting monetary policy and the level of accountability for their actions. I will restrict the discussion to monetary policy and leave aside the various complex issues relating to either central bank's role in banking supervision or regulation.

2.1. Appointments

For those who believe central banks should be “technocratic” institutions, perhaps the ideal appointment procedure would be to have a board of monetary policy experts appoint members of the ECB Governing Council based on which candidate has the best skill set.² In practice, the appointment process for Governing Council members is innately political. Most of the members of the ECB's Governing Council are governors of national central banks and these are generally appointed directly by national governments without parliamentary approval. There is nothing in the European Treaty requiring national central bank governors to have expertise in monetary policy or to prevent governments appointing those with strong political links to governing political parties.

The other members of the ECB Governing Council are the ECB Executive Board members. The appointment of these board members and the selection of one of them to be ECB President is made by the European Council in a process that has, from the beginning of the euro, been innately political.³ Appointments to the ECB Executive Board are an example of the type of “plum jobs” that are subject to a complex haggling process prior to appointment. While the exact process underlying these appointments is never fully clear, it seems they are often bundled in with other appointments and various informal queuing systems are used. For example, it is agreed that one country can have the current ECB Executive Board member but another country gets a senior position at the European Investment Bank and everyone agrees that a third country deserves to get the next plum job that comes up. It is unclear what role qualifications for the job play in these discussions, though Article 11.2 of the legal protocol underpinning the ECB states the appointments must be “*persons of recognised standing and professional experience in monetary or banking matters.*”

The protocol on the ECB does have one mechanism for encouraging transparency in the appointment of Governing Council members because it requires the European Council to only make these appointments after it has consulted the European Parliament. The need to consult with the European Parliament has likely had an influence on the type of candidates selected by the European Council but the consultation process is non-binding and the Council can ignore the Parliament's recommendation. This happened in December 2012 when Yves Mersch was appointed to the Executive Board despite failing to get approval from the European Parliament, due to concerns about the implication of Mr.

² This does, of course, raise the question of the appointment procedure for the board of monetary experts who then appoint the central bankers.

³ The appointment of the first ECB president proved to be highly contentious, ending with the Dutch nominee, Wim Duisenberg, agreeing to serve only half of his eight-year term to make way for the proposed French nominee, Jean-Claude Trichet. While officially Duisenberg was free to decide to serve a full term, it was clear that he was honouring a political agreement and this agreement could be said to have undermined the independence of the ECB presidency from that start of the euro.

Mersch's appointment for the gender balance of the board. While the European Parliament's objections delayed the appointment for six months, ultimately it did not affect the outcome.⁴

More recently, there was clear unhappiness among many MEPs at the process in 2018 to appoint Luis de Guindos as Vice-President of the ECB. The ECON committee held informal hearings with Mr. de Guindos and the other candidate for the job, Philip Lane, and communicated that it found Mr. Lane's performance "*more convincing*."⁵ However, following a recommendation of the Eurogroup of finance ministers that Mr. de Guindos should be appointed, the European Parliament approved his appointment. However, in a formal statement the parliament noted that it⁶

"expresses concerns regarding gender balance, the selection procedure, the timing of the appointment and political independence, and requests that the Council engage in a dialogue with Parliament as regards how to improve the process for upcoming appointments."

I am unaware of whether this dialogue has occurred.

2.2. Independence

By international standards, the ECB is a highly independent central bank. This independence is enshrined in law via Article 130 of the Treaty on the Functioning of the European Union (TFEU) which states

"When exercising the powers and carrying out the tasks and duties conferred upon them by the Treaties and the Statute of the ESCB and of the ECB, neither the European Central Bank, nor a national central bank, nor any member of their decision-making bodies shall seek or take instructions from Union institutions, bodies, offices or agencies, from any government of a Member State or from any other body. The Union institutions, bodies, offices or agencies and the governments of the Member States undertake to respect this principle and not to seek to influence the members of the decision-making bodies of the European Central Bank or of the national central banks in the performance of their tasks."

This influence of this article is not restricted to the ECB. It also affects how decision-making bodies at national central banks operate. To give an example I know, the Central Bank of Ireland is run by a politically appointed board known as the Central Bank Commission. However, this Commission does not discuss the Governor's role in setting monetary policy at the ECB Governing Council.

In relation to "not seeking to influence members" of the Governing Council, there have not (to my knowledge) ever been any legal cases brought against politicians or other groups for trying to influence the ECB and I suspect such cases would be difficult to prosecute, but at least thus far in its history, the principle is generally well respected by European politicians. One would worry, however, if members of the euro area began electing populist, nationalistic leaders, whether this pattern would be sustained.

The Treaty-based nature of the Eurosystem's goals and operational procedures also strengthens the ECB's independence because the rules for changing the Treaty are so arduous – and unanimous

⁴ See Rakic (2019) for more detail on the history of the European Parliament's consultative role in the appointment of Executive Board members.

⁵ European Parliament (2018). "Informal exchanges of views with candidates for ECB Vice-President". Press Release 15 February 2018. <https://www.europarl.europa.eu/news/en/press-room/20180215IPR97911/informal-exchanges-of-views-with-candidates-for-ecb-vice-president>.

⁶ European Parliament report on the Council recommendation for appointment of the Vice-President of the European Central Bank. 6 March 2018. https://www.europarl.europa.eu/doceo/document/A-8-2018-0056_EN.html.

agreement on changing the monetary policy elements is so unlikely to be achieved – meaning it is highly unlikely the ECB's legal framework will be changed in the foreseeable future. The fixed nature of its legal framework may prove to be a disadvantage for policy making in the future: As economic thinking and research progress, experts may agree on new goals or functions for the ECB that would improve social welfare but an ECB bound to honour the existing Treaties would be limited in how much it could change. However, from the point of view of independence, the unlikelihood of treaty change is a positive, since it means that Eurosystem central bankers can carry out their tasks without being concerned that politicians could pass new legislation to change the terms and conditions under which the central bank operates.

Another element strengthening the independence of the Eurosystem is the relatively long terms of Governing Council members. Article 11.2 of the ECB protocol ensures that members of the Executive Board, including the President and Vice-President are appointed to non-renewable terms of eight years. The terms of national central bank governors must also be at least five years in length.

These long terms provide some protection for members of the Governing Council from political influence. Executive Board members know their term will not be renewed so they do not feel pressure to make politically popular decisions to get reappointed by the European Council. Most national central bank governors are appointed relatively late in their careers and plan to serve only one term anyway.

That said, it is likely that political reputation is important for at least some members of the Governing Council, particularly those who have either come from a political career or those who are perhaps planning such a career after their term on the Governing Council. One way to reduce the influence of political concerns would be for the European Council to decide to not nominate people to go directly from elected or governmental positions to the ECB Executive Board.

2.3. Accountability

There is very little in the European Treaties in relation to making the ECB accountable for its actions. The ECB's legal protocol commits it reporting a weekly financial statement, a report on its activities that must be at least quarterly and to provide an annual report on its activities and monetary policy to the European Parliament. Article 284 of TFEU also allows a member of the European Commission and the President of the Council of the EU to attend Governing Council meetings, thus allowing the politically-appointed executive leadership of the EU to be informed as to how and why the ECB takes its decisions. To my knowledge, the Council President does not attend the Governing Council meetings but a member of the European Commission usually does.

Thankfully, the ECB operates with a much higher level of transparency than this legally-required minimum level. Here, I will outline the various ways in which the ECB's can be held accountable. For now, I will describe the various modalities and hold off on making normative judgements or recommendations about any of them until Section 4.

- 1. Press conferences:** The ECB has, in some dimensions, been a leader in the areas of transparency and accountability. The lengthy press conference after each monetary policy meeting of the Governing Council is a crucial element of the ECB's communications of its policies and the reasons for its decisions.
- 2. Meeting accounts:** Since 2015, the ECB has provided a series of "accounts" of its Governing Council which appear a month after the meetings.
- 3. Annual report:** In addition to publishing its annual report, the ECB leadership attends meetings of the European Parliament to discuss its contents and answer questions. The current tradition is that

the ECB Vice-President appears before the ECON committee and subsequently the ECB President appears before the full plenary session.

- 4. Monetary dialogue:** While press conferences play an important role in establishing transparency and accountability for the ECB's decisions, these press conferences are ultimately controlled by the ECB itself. The ECB decides which journalists to admit, who to call on to ask questions and the ECB President can evade or dismiss questions from journalists should they chose. This is why the quarterly Monetary Dialogue between the ECB and the European Parliament's ECON Committee is so important. It is based on a rule of procedure of the European Parliament rather than the EU Treaties but the ECB has agreed to fully cooperate with the process and it provides a unique opportunity for elected politicians to relate concerns about the ECB's actions directly to its President. The status of MEPs as public representatives means there is a greater moral incentive for ECB officials to respond to their concerns than to questions from journalists.
- 5. Written questions:** The rules of procedure of the European Parliament allow MEPs to submit written questions to the ECB with the understanding that if the ECB has not responded to the question prior to the next Monetary Dialogue meeting, then the question may be asked at that meeting. My sense is that these written questions have often been useful in obtaining information from the ECB, particularly in relation to more technical matters that are less easily understood when debated in public meetings.
- 6. European Court of Justice:** While the Eurosystem may be independent and free to pursue its monetary policies without political interference, this does not mean the central bankers are free from constraints. The European Treaties set down a strict legal mandate and place a number of clear restrictions on the Eurosystem's potential actions. Ultimately, the ECB is accountable to European Court of Justice (ECJ) and the various cases presented before them in recent years has meant that the ECJ has been active in setting out opinions on the limits to the ECB's activities. It is important to stress that this form of accountability only applies to the ECJ. Despite the recent opinion offered by German Constitutional Court, the ECB is not accountable to national courts or parliaments.

Taken together, these various mechanisms provide a substantial amount of accountability for the ECB. Still, there is room for some improvements. I will list some recommendations for improvements in Section 4.

3. INDEPENDENCE AND ACCOUNTABILITY FOR THE FEDERAL RESERVE

This section discusses how the Federal Reserve operates under the same three headings just discussed for the Eurosystem.

3.1. Appointments

Like the Eurosystem, the Federal Reserve has a “hub and spoke” system with a central board (the Board of Governors in Washington DC) combining with a decentralised set of geographically-based institutions (the Federal Reserve Banks) to implement monetary policy and the Fed’s other tasks. However, unlike the Eurosystem, the hub of the system plays a dominant role. Monetary policy is set by the Federal Open Market Committee (FOMC) which has twelve members: The seven members of the Board of Governors, the President of the New York Fed and four other regional Fed presidents who rotate on and off the committee.

Members of the Board of Governors are appointed by the President, subject to Congressional approval. The appointments process has often generated political controversy. For example, when President Obama nominated Nobel-prize-winning economist Peter Diamond to fill a position on the Board, the nomination failed to get congressional approval because Senate Republicans argued that Mr. Diamond did not have sufficient competence to serve on the board. The difficulty with getting Congressional approval for these positions has increasingly led to Board positions being unfilled for large amounts of time. For example, the current Board of Governors only has five members and filling the remaining two positions has been held up by controversy over President Trump’s nomination of Judy Shelton, who has advocated in the past for a return to the gold standard.

The position of Chairperson of the Board of Governors (who is also by tradition chair of the FOMC) is a critical one. While technically only one vote on the FOMC, the Chair is the public face of the Fed and controls the substantial resources of specialist expertise employed by the Board of Governors. Transcripts of FOMC meetings generally show the Chair as leading the discussion and instigating policy recommendations and, traditionally, the other Governors tend to vote with the Chairperson of the Board. The position of Chairperson of the board comes with a four-year term, meaning each President gets to pick who they want to be Chair. Should a Fed Chair not be reappointed, they can continue to serve on the Board of Governors but in practice, Fed chairs that were not reappointed have chosen to resign from the Board.

Over most of the past 50 years, the re-appointment of Federal Reserve chairs has been relatively uncontroversial with bipartisan agreements that successful chairs should be re-appointed. Presidents have regularly reappointed Fed chairs that were appointed by predecessors from the different parties. However, this is no legal requirement for this approach and President Trump broke with historical convention by deciding not to reappoint Janet Yellen as chair in 2018, despite widespread agreement that she was highly qualified and had performed well in the role. Several respected news outlets reported that a key reason why President Trump chose not to reappoint Yellen was because he thought she was too short.⁷

The appointments procedure for the Reserve Bank Presidents that serve on the Board is a complex one. The current procedure is that Presidents are appointed by subcommittees of boards of the Reserve Banks equally made up of two types of directors: Directors directly appointed by the Board of

⁷ See, for example, the following story from the Washington Post. <https://www.washingtonpost.com/business/2018/12/03/trump-thought-yellen-was-too-short-be-fed-chair-thats-not-how-any-this-works/>.

Governors (who are themselves appointed by the President) and directors appointed by banks in the district. In this sense, Presidents can either directly or indirectly control the appointment of every member of the FOMC.

3.2. Independence

Unlike the Eurosystem, the Federal Reserve has no formal legal declaration of independence and it is one of the less independent central banks in modern advanced economies.

The Federal Reserve Act is the key piece of legislation underpinning the Fed and it makes no explicit reference to the type of independence that the ECB has. Indeed, the history of the Fed shows many examples of monetary policy being set to suit the wishes of the governing administration. Only in the era since the appointment of Paul Volcker as Fed chair in 1979 did a broad cross-party consensus emerge that it was best for the President to not interfere in monetary policy making. It appears, however, that President Trump does not agree with this consensus. During his term in office, he has regularly made public comments expressing his desire for the Fed to lower interest rates and his decisions to not reappoint Yellen and to nominate an unsuitable candidate such as Shelton indicate a politicisation of the appointments process that has not been seen over the past forty years.

The relatively short terms for Fed chairs and the fact that presidentially-appointed Board of Governors make up a majority of the FOMC combine to mean that US Presidents (in particular Presidents that serve two terms) have the ability to reshape the composition of the FOMC to their liking, potentially having consequences for the implementation of monetary policy.

The Federal Reserve Act was designed to limit the ability of politicians to influence the Board of Governors by giving board members non-renewable 14-year terms, with new 14-year terms starting every two years. The motivation for this system was that board members with a 14-year term would not feel under pressure to please the ruling party in order to get re-appointed and with new terms only starting every two years, there would only be two new appointments during each four-year Presidential term. In practice, however, board members regularly resign before the end of their term. Conti-Brown (2015) documents that the average length of time for board members to serve is under seven years, meaning there tends to be an average of one Presidential appointment per year. This means that even one-term Presidents can end up appointing a majority of the members of the board.

Another area where the Fed is considerably more vulnerable to political interference than the Eurosystem is the possibility of new legislation that changes its mandate or operational procedures. Bills to change how the Federal Reserve operates have regularly appeared in Congress over the years. For example, Senator Rand Paul has promoted an “Audit the Fed” campaign, which is not really about auditing the Fed (the Fed’s accounts are externally audited every year and its spending is overseen by the Government Accountability Office) but rather about increasing political influence over monetary policy.⁸

Thankfully for the Fed, the gridlocked nature of Washington politics has prevented any of these legislative attempts from passing. It is relatively rare for one of the parties to control the House, Senate and Presidency and, even when they do, the filibuster tradition in the Senate prevents many bills from passing. However, just as the Fed’s appointments process under President Trump has become more politicised, a scenario in which the filibuster is dropped and one of the parties changes the Fed’s mandate or independence seems more realistic now than it did in the recent past. There is a real

⁸ See Bermanke (2016).

possibility that the threat of legislative changes could be used by future administrations to influence Fed officials to take decisions they may not be comfortable with.

3.3. Accountability

Federal Reserve governors and officials regularly appear before Congress to testify and answer questions on the Fed's work in relation to monetary policy, financial regulation and supervision, payments systems and financial stability. In relation to monetary policy, the key appearances are set out in Section 2 of the Federal Reserve Act. The Fed is required to submit a report to Congress twice a year on monetary policy and economic developments and the Chair is required appear before the Congress after the release of the reports. Specifically, the Chair appears on successive days before the Senate Committee on Banking, Housing, and Urban Affairs and the House Committee on Banking and Financial Services.

In many ways, these Congressional appearances are similar to the Monetary Dialogue. The quality of the questioning from politicians is widely variable and it is common to see politicians ask about issues that are largely irrelevant to the Federal Reserve's mandate, to attempt to get the Fed Chair to support positions of their political party or to use the appearance to promote businesses in their home districts. However, overall, I believe these meetings do a pretty good job in keeping the Federal Reserve accountable.

In particular, while the committees are large (particularly the House committee which has about 60 members) and questioners are usually given only five minutes, there is a strong culture of investigation and exploration among the committee members. Many of the politicians are well-briefed and come prepared to explore specific issues in depth. The Chair is regularly exposed to relatively forensic examination on specific issues, with politicians asking a series of inter-linked questions related to a particular issue.

As documented here, the Eurosystem should not in any way envy the Federal Reserve's position in terms of its political independence. However, I believe the Congressional hearings do a relatively good job in making the Fed accountable for its monetary policy and in explaining its actions to the public. As I discuss below, it is my opinion that the European Parliament could learn several useful things from these hearings and should consider adapting its procedures to resemble them more closely.

4. RECOMMENDATIONS

I conclude with some recommendations that could improve the independence and accountability of the ECB.

4.1. European Council

The starting point for accountability of a central bank should be the process by which central bankers get appointed. The current process for appointing ECB Executive Board members is not transparent and does not necessarily produce the best qualified candidates. While the European Treaties do not explicitly require the European Parliament to approve all appointments, decisions to appoint candidates that are not approved by the European Parliament seems to run counter to the spirit of the law. However, it seems likely the legal requirement to consult with the European Parliament was inserted to avoid candidates being appointed that did not have parliamentary approval.

While it is not easily possible to change the Treaty to make this requirement explicit, the European Council should take up the Parliament's request for a dialogue about the appointments process. Ideally, the result of this dialogue would be a new process in which the Parliament holds exploratory hearings with potential candidates and the Council agrees to appoint the candidate favoured by the Parliament.

Considering the need to keep the ECB Governing Council independent from political control, the Council should also avoid nominating candidates for the Executive Board who are coming directly from a political or ministerial role.

4.2. ECB

While the ECB is to be commended for its commitment to accountability via the availability of the President at press conferences and appearances at the European Parliament, there are still a number of aspects of ECB communications that could be improved.

Emergency Liquidity Assistance: One area where there have been serious problems with transparency and accountability has been emergency lending to banks in distress. As I have written about on several occasions (Whelan, 2014, 2015, 2016) there have been several controversies associated with how Emergency Liquidity Assistance (ELA) programmes have been operated. There have been examples of lending to severely insolvent banks, a lack of clarity surrounding the terms under which the Eurosystem caps or withdraws ELA and a series of decisions made where the granting or curbing of ELA appeared to be directly related to political developments in various countries. In my opinion, the uncertainty surrounding the ECB's performance of its role as lender of last resort to the banking system has tended to worsen banking crises and the politicisation of this role has damaged the reputation of the ECB as an institution in a number of Member States.

A small amount of progress has been made in recent years in clarifying the procedures surrounding ELA. The ECB first published a short document describing these procedures in 2013 and updated it in 2017.⁹ These documents are clear in that ELA should not be provided to insolvent banks and with the Single Resolution Board in place, there is no reason why the ECB should provide liquidity in this situation. So hopefully, some of the more serious errors in this area—such as the large amounts of Eurosystem credit provided to Laiki Bank and Anglo Irish Bank—will not be repeated.

That said, the guidelines for providing ELA to banks remain *ad hoc* and rely on a complex set of arrangements in which ELA is granted by the national country central banks but ELA programmes then

⁹ The current ELA agreement is available at <https://www.ecb.europa.eu/mopo/ela/html/index.en.html>.

need to be continually renewed by the ECB Governing Council with a two-thirds majority required to stop a programme. Given the importance of a well-functioning lender of last resort function to any banking system, I recommend the ECB adopt a new policy structure in this area. Since ECB is now the supervisor for all of euro area banks and the importance of “legacy issues” has begun to recede, there is also a stronger moral argument than in the past that decisions about emergency liquidity should be taken at a central level and profits or losses from these operations should be shared.

Voting: In its early years, the ECB acted as though all important decisions were taken with unanimous approval by the Governing Council. It is clear that this has not been the case in recent years but the ECB has not given clear explanations of the extent of disagreement. For example, a number of members of the ECB Governing Council disagreed with the package of monetary policy measures introduced in September 2019. In the subsequent press conference, President Draghi was evasive about the extent of disagreement on the package, preferring to emphasise that all members were in favour of introducing a package of some sort.

The motivation for not holding explicit votes and revealing the outcomes is likely to reduce controversy over difficult decisions and to prevent media coverage that emphasises which countries’ representatives support or oppose particular policies. The problem, however, is that Governing Council members have tended to quickly leak their opposition to policy decisions to the press. See, for example, the Bloomberg story on 12 September 2019 (the day of the press conference) titled “*Draghi Faced Unprecedented ECB Revolt as Core Europe Resisted QE*.”¹⁰ The article suggested that countries accounting for a majority of euro area GDP opposed the resumption of the Asset Purchase Programme. While this is not the criteria used to make monetary policy decisions, the package of measures could be interpreted by some as possibly “undemocratic” because representatives of countries with smaller populations appear to have outvoted some that had larger populations.

The ECB should consider whether an open and transparent approach to explaining how its decisions were made may be preferable to its deliberations being reported by the press via leaks.

Meeting Accounts: The meeting accounts that have been published since 2015 have provided insights into how the Governing Council meetings operate and the considerations taken into account when making monetary policy decisions. However, there are a number of odd aspects to these accounts.

The only two Governing Council members named in the accounts are the Executive Board members responsible for financial markets (currently Isabel Schnabel) and economics (currently Philip Lane). The accounts describe how the board member responsible for markets discusses recent events in financial markets while the “chief economist” discussing economic developments and the outlook for price stability and then makes proposals for decisions on monetary policy. I am sure these are a fair description of how the meetings begin but one can assume that the ECB President has played a key role in preparing the policy proposals and in explaining them to the other members of the Governing Council. The absence of names for other individuals also requires guessing to figure out what really happened. For example, for the September 2019 meetings we are told “*A number of members assessed the case for renewed net asset purchases as not sufficiently strong*” but we are not told how many or who these members are.¹¹ Perhaps in relation to the latter, it is felt that if particular members of the Governing Council are recorded as objecting to a package of measures, then these members will not be able to defend the policy decisions effectively. The counterpoint to that is that if these same

¹⁰ Randow, Jana (2019). Draghi Faced Unprecedented ECB Revolt as Core Europe Resisted QE. Available at <https://www.bloomberg.com/news/articles/2019-09-12/draghi-faced-unprecedented-ecb-revolt-as-core-europe-resisted-qe>.

¹¹ ECB (2019). Account of the monetary policy meeting of the Governing Council of the European Central Bank held in Frankfurt am Main on Wednesday and Thursday, 11-12 September 2019. Available at <https://www.ecb.europa.eu/press/accounts/2019/html/ecb.mg191010~d8086505d0.en.html>.

members leak their objections to the press, then perhaps it would be better for the ECB to provide a more complete account of the meeting.

4.3. European Parliament

I believe the current format of the Monetary Dialogue meetings is not well suited to the necessary detailed exploration of the various complex monetary policy issues that have emerged in recent years. The format could be improved by making some changes to procedures, including learning some lessons from the Federal Reserve's Congressional hearings.

The format for the Monetary Dialogue hearings is as follows. After an opening statement from the ECB president, the meetings proceed with a large number of questions (usually over fifteen) from MEPs. MEPs are given up to two minutes to ask questions and then there is a response from the ECB President with the total time taken up being five minutes. There is no tradition of follow-up questions, so that, relative to US Congressional hearings, the meetings are more "stilted" with less focus and far less interaction. The ECB Presidents tend to "run down the clock" by taking right up to the allocated five minutes of time. There is very little MEPs can do if they view the ECB President as having provided an inadequate answer.

Perhaps unsurprisingly, given the large number of questions, the quality of questioning during the Dialogue varies widely in content and usefulness. While many of the questions asked are well-informed and address key issues relating to the ECB's policies, questions that focus on narrow national interests (and thus add little to our understanding of the ECB's role or policies) are also common. Overall, my biggest concern is that the Dialogue sessions generally do not allow for a sustained focus on a smaller number of important (and potentially complex) issues.

I would recommend that the ECON committee consider adapting the format of the Monetary Dialogue meetings be changed in a number of ways.

First, the committee should consider changing the "culture" of the Dialogue to be closer to US Congressional hearings. Rather than asking each questioner to bundle questions together for two minutes, it would be better for MEPs to often ask short questions and then follow up on them based on the answers given. I believe this more inquisitive style of questioning would shed more light than the current hearings. I am aware, of course, of some important complexities that make the ECON Committee meetings different from US Congressional hearings. In particular, if MEPs want to ask a question in a language that it is not either English or the President's mother tongue, then the questions need to be translated, which makes a back-and-forth discussion almost impossible. That said, most of the questions asked can be directly understood by the President.

Second, it may be preferable to facilitate more intense questioning by having a smaller number of MEPs ask questions in any given session. I understand this may be difficult to achieve given the large size of the committee, which has 60 members, but this could be offset by making more use of written questions to coincide with the dialogue.

Third, I would also note that the room the Dialogue takes place in is very large and the questioners are often very far away from the ECB President. This may partly explain the lack of interaction during these meetings. A setting that allowed those MEPs designated to ask questions to sit closer and be more engaged with the President would be preferable. Committee staff should examine the seating arrangements at US Congressional hearings to get a sense of how these meetings can work well. Media and staff assistants who currently attend the Dialogue meetings could observe the sessions via a live webcast. The current period, in which the Dialogue will be taking place online for a while, perhaps offers an opportunity to change the format to be more interactive.

Fourth, the dialogue could benefit from themed sub-sessions. For example, the ECB President could be informed that a first group of MEPs will be asking questions on a particular topic and that the sub-session on this topic will run for 45 minutes. Questions from MEPs could be co-ordinated to avoid repetition.

5. CONCLUSIONS

In many ways, the institutions underlying the Eurosystem's monetary policy are superior to those of the Federal Reserve. The Eurosystem is far more independent from political control than the Federal Reserve and the process of appointing the Executive Board of the ECB is somewhat less political than the process of appointing members of the Board of Governors of the Fed.

Nevertheless, there are a number of ways to improve the accountability of the Eurosystem. These include requiring European Parliament approval as a condition for appointment to the Executive Board. The ECB could also improve communications in various ways, including providing more information about its meetings.

In addition, the Federal Reserve's processes for accountability are, in my opinion, more effective than the European Parliament's current procedures. I recommend that the ECON committee consider changing the culture and format of the Monetary Dialogue meetings to allow a more inquisitorial approach, featuring longer time limits for questions and the encouragement of back-and-forth exchanges with the President.

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