

## Holding central banks accountable

René Smits Thursday 25 September 2014, 13:39

Increasing powers require increased accountability. The crisis has seen unprecedented actions being undertaken by central banks. Traditionally mandated to maintain price stability independent of political influence, central banks have acted more and more as lenders of last resort for solvent banks that were unable to fund themselves with frightened market parties and as providers of liquidity to frozen markets. Central banks have been engaged in 'unconventional measures' to kick-start the economy. Quantitative Easing in the US and the UK. Funding for Lending schemes (Bank of England) and Targeted Long-Term Refinancing Operations (ECB) that seek to promote lending to the real economy by commercial banks. The ECB has undertaken other unconventional methods, as well: negative interest rate on deposits with the Eurosystem, programmes to buy bonds, including the announced Outright Monetary Transactions, currently subject to judicial scrutiny. Central banks are called to directly supervise commercial banks: the Bank of England is again prudential supervisor after having lost this role in 1997; the European Central Bank will assume direct supervision of the Eurozone's significant banks and oversee the supervision of its other banks by national authorities as of 4 November 2014. How do independent central bankers account for their tasks? The Managing Director of the IMF considers central banks notoriously impenetrable. In a recent interview with the Financial Times, Christine Lagarde laments: "Then there is the question of how we co-ordinate better with the key central bankers in the world," she sighs. "They meet by themselves. They play by their own rules, they are so clubby and secretive. But we have to find ways to co-ordinate."

Traditional accounting mechanisms for central banks boil down to 'giving reasons requirements': being transparent about the actions undertaken, explaining their rationale as good as possible. (Other accountability mechanisms include non-voting political representation in the central bank's decision-making body and independent administrative and judicial review of its decision. Disclosure: I have been appointed an alternate member in the administrative review board for the ECB's supervisory decisions.) Central banks are in the unenviable position that their ex post explanations need to satisfy widely different audiences: the technical expertise of the banking world and the 'central bank watchers', as well as the broader public and its representatives, the parliamentarians. Each public requires its own level of explanation. When central banks exercise different functions (most do), their distinct tasks may require different modes of explanation. For monetary policy, consistency, predictability and the 'anchoring of inflation expectations' are

key. The ECB introduces transparency in part as an instrument for the effectiveness of its monetary policy in turbulent times. In prudential supervision, the protection of business secrets, the avoidance of a run on a bank (remember Northern Rock), the privacy of bank managers and the need for more intrusive accountability than in other areas of central bank activity pose conflicting demands. Other tasks may require a different balancing of secrecy and transparency.

The ECB's announced transparency through the publishing of minutes of the meetings of the Governing Council will require even more astute balancing. The new practice will start soon after the ECB will have assumed new powers under 'banking union'. Elaborate arrangements for far-reaching accountability have been mandated by the EU legislator and agreed between the ECB and the European Parliament as well as with the Ecofin Council and the Eurogroup. Also, the new approach follows soon after the Governing Council will begin working with rotating voting powers. Welcome though this new transparency is in my view, it will be seriously tested on two fronts: (1) how the ECB will balance transparency and confidentiality applying the new approach in its various fields of competence and (2) how to handle transparency in sensitive areas of European policy in nationalistic times. The ECB is to follow an innovative interpretation of the applicable provision respecting its underlying rationale for confidentiality that the Treaty's authors had in mind when they wrote Article 10.4 of the ESCB Statute: *The proceedings of the meetings shall be confidential. The Governing Council may decide to make the outcome of its deliberations public.* The Treaty acknowledges the multinational context in which the young ECB operates; linguistic and cultural differences are to be put aside as members of the ECB's Governing Council meet – after all, they don't have national mandates: they are Working for Europe.

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