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CENTRAL BANK-GOVERNMENT RELATIONS IN MAJOR OECD COUNTRIES

A STUDY

PREPARED FOR THE USE OF THE

JOINT ECONOMIC COMMITTEE CONGRESS OF THE UNITED STATES

AUGUST 1, 1991

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AUGUST 1, 1991.

To the Members of the Joint Economic Committee:

We are pleased to transmit to you this study entitled "Central Bank-Government Relations in Major OECD Countries". The study provides information on how other major industrial countries resolve the problem of central bank accountability within a system of democratic government.

In today's economic climate, much of the responsibility for the conduct of economic policy has devolved to the Federal Reserve, where monetary policy and interest rates are determined, and concerns have been expressed about the public accountability of the Federal Reserve. This study explores how other industrial democracies manage the conduct of monetary policy to accommodate the two objectives of public accountability and central bank independence.

The study examines both the legal and day-to-day relationships between the central banks and the governments of Canada, France, Germany, Italy, Japan, Switzerland and the United Kingdom. It provides a wealth of detail on how those responsible for the conduct of monetary policy are selected, the channels of communication that exist between the governments and the central banks, the ways in which the governments exercise oversight of central bank practices and procedures, and the ways in which central banks announce their policy decisions.

The study was prepared for the Joint Economic Committee by Professor John Goodman of the Harvard Business School. Professor Goodman specializes in the field of comparative business-government relations and has recently completed a book on *Monetary Sovereignty: The Politics of Central Banking in Western Europe.*

This study does not necessarily reflect the views of the members of the Joint Economic Committee. It is a factual analysis of central bank-government relations in major OECD countries and contains no policy recommendations. It does demonstrate, however, that there are a variety of ways of reconciling the needs of democratic accountability with those of central bank independence. Current practices of the Federal Reserve do not provide the only avenue for balancing these objectives. We hope this study will provide members of the Committee, the Congress and the public useful information that they may use in their evaluation of the relationship between the Federal Reserve System and the government in the United States.

With best regards,

Sincerely,

PAUL S. SARBANES,
Chairman,
LEE H. HAMILTON,
Vice Chairman.

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CENTRAL BANK-GOVERNMENT RELATIONS IN MAJOR OECD COUNTRIES

CENTRAL BANK-GOVERNMENT RELATIONS IN MAJOR OECD COUNTRIES

By John B. Goodman*

INTRODUCTION

Central banks play an important role in the process of economic policymaking. Their functions typically include: issuing national currencies, serving as bankers' banks, acting as financial agents to their governments, managing foreign exchange reserves and transactions, and conducting monetary and credit policies. For this reason, practically every country now has a central bank. Yet the relationships between central banks and their governments vary significantly across countries.

The appropriate relationship between a central bank and the government in democratic systems is often discussed in two ways: One view maintains that the central bank should be an agent of the Treasury in order to ensure its accountability to elected political authorities. The alternative view stresses that the central bank should be independent in order to guarantee the insulation of monetary policy from domestic political pressures. In practice, however, neither view does full justice to reality, since in no country is the need for a close working relationship between the government and the central bank seriously questioned.

This study surveys central bank-government relations in seven major countries: Canada, France, Germany, Italy, Japan, Switzerland, and the United Kingdom. It focuses, in particular, on six features of legislation and practice that characterize the relationship in each of these countries:

- **Institutional Structure and the Decisionmaking Process**
  In most countries, the Governor of the central bank is responsible for both managing and representing the central bank vis-a-vis the government and foreign institutions. Often, the Governor is assisted by one or more Deputy Governors. Many central banks also have either an

* Professor, Harvard Business School.

Executive Committee or a Board of Directors. Yet the decision-making process differs considerably across countries with respect to the degree of government participation in the deliberations of the central bank and the right of government to issue directives to the central bank in case of conflict. Differences also exist in the degree to which governments and central banks must engage in formal policy coordination.

- **Appointments**
  Legislation generally covers two critical issues for central bank-government relations: first, the role of the government in the appointment of Bank officials; and second, the tenure of their appointment. Although the specific process varies, the government in most of the countries surveyed in this report appoints the Governor and Deputy Governor(s). Differences exist, however, regarding the appointments of other members of the central bank Board of Directors or Council. Significant differences also exist in the tenure of appointment. In some countries, the Governor is appointed for a fixed term (which often exceeds the term of governments). In other countries, the Governor is appointed for an indefinite term and hence serves at the will of the government.
- **Announcement of Policy Decisions**
  Legislation generally requires most central banks, or their Governors, to issue an annual report, but does not specify how or when central banks must announce policy decisions. The process of monetary targeting has led most central banks to announce their targets annually, but the procedures for policy announcements vary.
- **Central Bank Financing of Government Borrowing**
  The government's access to borrowing from the central bank is governed both by central banking legislation and by regulations established outside that legislation. Most of this legislation concentrates on the regulation of direct—and often short-term—borrowing from the central bank, rather than indirect financing through, for example, open market operations. Across countries, there are considerable differences in the limits on government borrowing.
- **Budgetary Procedures**
  As a rule, the central banks surveyed in this report (with the exception of Japan) determine their current expenditures independently. This independence is generally implicit in central banking legislation. In some countries, government representation in the central bank's board has created an indirect channel for government involvement in budgetary procedures.

- **Audits of Central Bank Accounts and Practices**
  Most central banks have their own internal auditors. In some countries, however, the audit is carried out by the governments' auditors. Differences also exist in the extent to which the government may review and control other aspects of a central bank's internal practices.

In addition to these six features of central banking legislation, it should be noted that the relationship between central banks and their governments may be influenced by external commitments. Four of the countries surveyed in this report—France, Germany, Italy, and the United Kingdom—participate in the exchange rate mechanism of the European Monetary System (EMS). The obligation to defend a fixed exchange rate in the EMS at times creates a significant constraint for these central banks and their governments. At the domestic level, it should also be noted that traditions and personalities (of both the Governor and the political leaders) may lead the actual relationship between the government and the central bank to differ from the one specified in national legislation.

CENTRAL BANK-GOVERNMENT RELATIONS IN CANADA

The Bank of Canada was created in 1934 by an act of Parliament in order to "regulate credit and currency in the best interests of the economic life of the nation, to control and protect the external value of the national monetary unit and to mitigate by its influence fluctuations in the general level of production, trade, prices, and employment, so far as may be possible within the scope of monetary action, and generally to promote the economic and financial welfare of Canada."

INSTITUTIONAL STRUCTURE AND THE DECISIONMAKING PROCESS

The Bank of Canada Act vests responsibility for the affairs of the Bank in its Board of Directors. The Board of Directors consists of the Governor, the Senior Deputy Governor, and twelve directors selected from diverse occupations (other than direct clearers and investment dealers) and, in practice though not in law, various regions of Canada. The Board of Directors normally meets about eight times a year. An Executive Committee of the Board, composed of the Governor, the Senior Deputy Governor, and between two and four directors (selected by the Board) meets once a week. The Deputy Minister of Finance is a nonvoting member of both the Board of Directors and the Executive Committee. The Board is charged with ensuring the competence of the Bank's management, approving capital and current expenditures, and overseeing administrative policies.

Monetary policy, by contrast, is formulated by the Governor and officers of the Bank. A Management Committee, which includes the Governor, Senior Deputy Governor, Deputy Governors, Advisers and Secretary of the Bank meets daily in order to discuss both the formulation and implementation of monetary policy.

Although the Bank of Canada is granted a degree of autonomy in these matters, ultimate responsibility for monetary policy is vested in the government. The Bank of Canada Act (as amended in 1967) stipulates that "the Minister [i.e., Finance Minister] and the Governor shall consult regularly on monetary policy and on its relation to general economic policy. . . If, notwithstanding the consultations . . . there should emerge a difference of opinion between the Minister and the Bank concerning the monetary policy to be followed, the Minister may, after consultation with the Governor in Council [the Cabinet], give to the Governor a written directive concerning monetary policy, in specified terms, and the Bank shall comply with this directive." The directive must be specific, presented to Parliament, and published in the Canada Gazette. In practice, however, the Finance Minister has never issued such a directive.[1]

The 1967 amendment to the Bank of Canada Act provided a mechanism for dealing with disagreements between the Bank and the government and thereby enhanced cooperation between the two. Consultation between the government and central bank is assured at the highest level through weekly meetings between the Governor and the Finance Minister. Occasionally, the Finance Minister and the Governor also meet with the Prime Minister to provide information about the state of the economy.

Such cooperation has, however, left room for differences between the Bank of Canada and the Finance Ministry. At times, for example, the economic projections for inflation in the Federal Government's budget have appeared to be inconsistent with the Bank's announced policy.

APPOINTMENTS

The Governor and Senior Deputy Governor are appointed by the Bank's twelve directors, with the approval of the Governor in Council [Cabinet] for renewable terms of seven years. The directors, in turn, are appointed by the [Finance] Minister with the approval of the Governor in Council, for renewable terms of three years. For all intents and purposes, the Governor and Senior Deputy Governor are therefore selected by the government.

The Bank of Canada Act stipulates that the Governor and Senior Deputy Governor must fulfill their terms in "good behavior," but it contains no further provisions regarding the dismissal of the Governor, Senior Deputy Governor, or directors. Apart from a single episode in 1961, the government has never attempted to dismiss any of these officers.[2]

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[1] Since the 1967 amendment, every governor has, upon appointment, announced that he would resign if such a directive were issued, thereby raising the cost of issuing such a directive.

[2] In 1961, the government objected to the tight monetary policy pursued by the governor of the day. On the basis of a technical disagreement over the management of Bank's pension fund, the government requested his resignation. The Governor at first

(continued...)

ANNOUNCEMENT OF POLICY DECISIONS

The Governor of the Bank of Canada is required to submit an annual report to the Finance Minister. Since 1987, the Bank has also published a synopsis of the Governor's regular report to the Board of Directors. These synopses are published with a delay of approximately six weeks.

At times, the Bank's policy objectives have been announced in the form of targets, while at other times there have not been precise targets. From 1975 to 1981, the Bank used M1 as a formal target; announcements of these targets were made by the Bank roughly on an annual basis. However, shifts in the demand for money due to financial innovation led the Bank to abandon M1 as a target in 1981. In the following decade, the Bank's objectives were expressed in terms of policy goals, rather than precise targets. From 1981, for example, the Bank's stated objectives were to sustain economic recovery while maintaining continued progress toward price stability. After the economic recovery was well underway, achievement of price stability became the principal objective. Such objectives were announced and explained in the speeches and presentations of the Governor, as well as in the publications of the Bank. In 1991, the Governor and the Minister of Finance jointly announced the setting of targets for the reduction of inflation in Canada. As the Bank does not directly target interest rates or monetary growth, no announcement is made of what level of interest rates or monetary growth is consistent with these inflation targets. The Bank will, however, comment from time to time on the consistency of the emerging paths for monetary and credit aggregates with the targeted path for inflation.

The Governor is frequently asked to appear before committees of both the houses of Parliament to explain the policies pursued by the Bank of Canada, as well as to provide testimony on other issues affecting the conduct of monetary or credit policy. The actual number of the Governor's appearances before Parliament has varied over time:

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[2](...continued)
refused, prompting the government to request a vote of Parliament declaring the governor's position vacant. A majority of the Senate however voted against the government. Thus vindicated, the governor then resigned on his own accord. It was this episode that prompted the 1967 amendments to the Bank of Canada Act.

Appearances of the Governor before Parliament

Years	Number of Appearances
1975-1978	3
1979-1982	10
1983-1986	7
1987-1990	6

Central Bank Financing of Government Borrowing

The Bank of Canada may buy and sell securities of the federal government or the provincial governments. The amount of direct credit that the Bank can extend to the federal government is limited to one-third of the federal government's estimated revenue each year. The amount of direct credit that the Bank can extend to any provincial government, by contrast, is limited to one-quarter of that government's estimated revenue. In practice, the Bank has never lent directly to either the federal or the provincial governments; the Bank, furthermore, has never purchased provincial government securities.

Budgetary Procedures

The Bank of Canada has budgetary autonomy; this autonomy is implicit in the Bank of Canada Act, which only requires the Bank to submit regular statements of its assets and liabilities to the Finance Minister. Its budget is reviewed by the Bank's Budget Committee of the Board of Directors and then approved by the Board itself. The Governor's annual report must be provided to the Finance Minister within two months after the end of each fiscal year, who then is required to submit to Parliament the Governor's report including the Bank's financial accounts. (There is no requirement for the publication of a detailed breakdown of the Bank's expenditures, but such a breakdown is nonetheless provided in its Annual Report.) All the net revenues of the Bank flow back to the government.

Audit of Central Bank Accounts and Practices

On the recommendation of the Finance Minister, the Cabinet each year appoints two auditors (certified to be appointed as auditors of a chartered bank) to audit the affairs of the Bank. The Minister can require the auditors to report at any time on the adequacy of the central bank's procedures adopted by the Bank for the protection of its creditors or shareholders; the Minister can also, at his or her discretion, enlarge or extend the scope of the audit "as the public interest may seem to require." (The Bank's activities as fiscal agent for the federal government are audited by the Auditor General.)

MONETARY DECISIONMAKING IN CANADA

BANK OF CANADA

Ministry of Finance

Ministry of Finance

In case of policy disagreement, Minister of Finance may issue a written directive to the Bank

Board of Directors[1]

Governor
Senior Deputy Governor
12 Outside Directors
Deputy Minister of Finance (non-voting)

Ensures competence of Bank's management;
Approves expenditures;
Oversees administrative policies.

Bank Management Committee[2]

Governor
Senior Deputy Governor
Deputy Governors
Advisers
Secretary of the Bank

Governor sets and implements monetary policy.

1 Meets 8 times per year; Executive Committee of Board meets weekly
2 Meets daily

CENTRAL BANK-GOVERNMENT RELATIONS IN FRANCE

The Bank of France was established by Napoleon in 1800 as a privately owned company engaged in the banking business. The Bank of France came under government control in 1936, when the government acquired the authority to nominate the Bank's governing bodies. The Bank was nationalized in 1945, and its current statutes were adopted in 1973. Those statutes changed the details, but not the substance of the Bank's subordinate position relative to the government. According to Article 4, "The Bank of France is entitled to give advice on all questions relating to the currency. It contributes to the formulation and participates in the implementation of the monetary policy decided by the government * * *."

INSTITUTIONAL STRUCTURE AND THE DECISIONMAKING PROCESS

Within the Bank of France, power is vested in the Governor and the General Council. The Governor, assisted by two Deputy Governors, is responsible for executing the laws, statutes, and deliberations of the General Council, over which he presides. He also exercises all powers not expressly reserved to the General Council. The Governor alone can sign conventions and treaties in the name of the Bank; he appoints and dismisses the Bank's staff (with the exception of the branch managers who are appointed by the Minister of Economics and Finance based on the proposal by the Governor.) And, he may exercise any additional powers, regarding, for example, the procedures for the fixing of rates or for market interventions, which are delegated to him by the General Council.

In addition to the Governor and the two Deputy Governors, the General Council consists of ten councilors. Nine, chosen for their abilities in the economic, monetary or financial areas, are appointed by a decree of the cabinet (on the basis of a proposal of the Minister of Economics and Finance). The tenth is elected by the personnel of the Bank. All ten councilors are appointed for terms of six years; one-third of the government appointees come up for renewal every two years.

The General Council, which meets every two weeks, is officially charged with overseeing policy regarding the administration of the Bank, fixing the terms and conditions for the issuing of paper money, setting the discount rates, and approving agreements concerning the central

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bank's financial assistance to the State. In practice, the General Council exercises little independent authority vis-a-vis either the Governor or the Treasury. Regulations governing the recruitment, promotion, and conduct of Bank staff are formally adopted by the General Council, although these must be submitted by the Governor to the Minister of Economics and Finance for approval.

The law provides the government with a means to review, and if it so desires, postpone decisions of the General Council. A *censeur* (auditor) appointed by the Minister of Economics and Finance (along with an alternate) attends all meetings of the General Council. The *censeur*, usually a senior member of the Treasury (and generally the Director), is charged with supervising the Bank's management on behalf of the State. The *censeur* may oppose a decision of the General Council, in which case the Governor must have the matter reconsidered at a later time.

Overall, the legal framework makes clear that the general lines of monetary policy are drawn up in the Treasury Division, in consultation with the Bank of France. In practice, this process involves frequent contact at all levels between the Bank and the Treasury. Such cooperation is designed to ensure, for example, that the Bank's monetary targets remain consistent with the government's flow of funds projections. With these general guidelines set, the Bank takes the initiative for policy implementation.

To assist in these efforts, the Banking Law of 1984 created a consultative body, the National Credit Council.[1] The National Credit Council, which meets at least twice a year, is composed of the Minister of Economics and Finance (who serves as chairman); the Governor of the Bank of France (who serves as vice-chairman); members of Parliament; and representatives of the French administration, regional and local governments, trade unions, and various economic and financial interests.

The Banking Law of 1984 also created:

- the Bank Regulation Committee, which fixes general rules applicable to credit institutions (regarding, for example, the instruments and rules of credit policy);

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[1] The National Credit Council was originally established in 1941 and, at that time, was intended to serve as a deliberative body. However, it did not perform this function in practice. The Banking Law of 1984 thus brought the National Credit Council's legal framework in line with reality.

- the Credit Institutions Committee, which takes decisions regarding individual institutions (regarding, for example, the granting of bank licenses); and
- the Banking Commission, which is in charge of banking supervision.

The responsibilities of the Bank Regulation Committee can have important implications for the conduct of monetary policy, for example, in setting the global framework for reserve requirements. In this context, it is important to note that the Minister of Economics and Finance serves as chairman; the Governor serves as vice chairman. If the Minister cannot attend a meeting, however, it is the Governor, not the Minister's alternate who presides.

Appointments

The Governor and the two Deputy Governors are appointed by an executive order of the President of the Republic. The duration of their term in office is indefinite, and they may be dismissed by the President at any time. In the past decade, the government has implicitly limited the Governor's mandate to five years.

Announcement of Policy Decisions

The annual monetary targets are formally announced by the Governor to the National Credit Council. (The National Credit Council used to announce the annual credit ceilings, which were previously used to implement policy.) Mid-year changes in policy objectives are generally announced in the same way. The National Credit Council is required to make an annual report to the Minister of Economics and Finance (which is, in practice, written by the staff of the Bank of France). Although it does not publish its minutes, the National Credit Council generally does make a brief announcement at the end of its meetings.

Changes in the discount rate are announced after they are formally approved by the General Council. In the past two decades, the discount rate has become a minor tool of monetary policy. The Bank currently makes use of regular auctions (appele d'offres) repurchase agreements and other market instruments to effect a change in the level of interest rates. As a result, a change in the Bank's view regarding the appropriate level of interest rates is more likely to become known indirectly through its intervention in the market, rather than through a formal announcement.

The Governor of the Bank of France is also required to make an annual report to the President of the Republic.

Central Bank Financing of Government Borrowing

Limitations on central bank financing of the government are not specified in law. The Law of 3 January 1973 states only that central bank advances or loans to the state are set by agreement between the Minister of Economics and Finance and the Governor, with the authorization of the General Council and the approval of Parliament. The current agreement governing the Bank's financial relations with the government was signed in September 1973 and has not been modified since then. The agreement set a ceiling of 20,500 million francs (interest-free) on central bank loans to the government. (Since this amount was specified in nominal terms, its real value and relation to GNP have declined with time.) In order to neutralize the effect of the periodic revaluations of the foreign exchange reserves held by the Foreign Exchange Stabilization Fund, the agreement also stipulated that the maximum amount of the Bank's assistance to the government may be increased by any loss, or reduced by any profit, made by the Fund. Currently, central bank loans to the government are interest free.

Budgetary Procedures

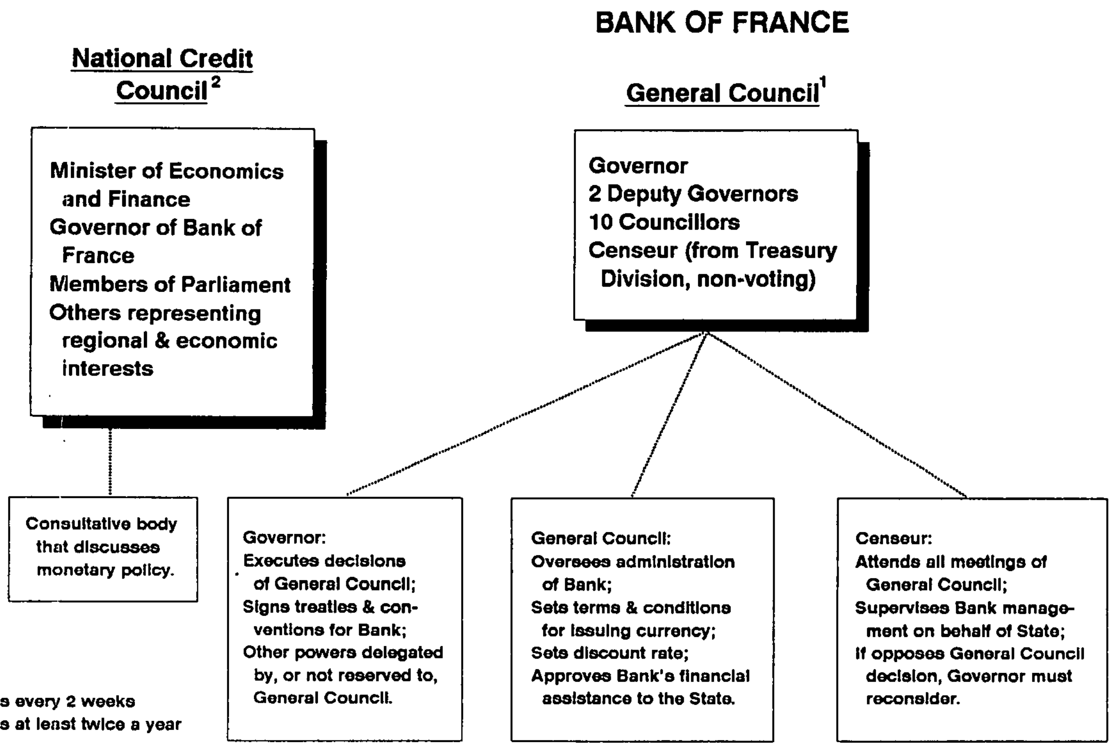
The Law of 3 January 1973 places responsibility for the budget with the General Council. The General Council draws up the Bank's estimated expenditures, makes up the annual accounts, and proposes the distribution of profits and the amount of the dividend to be paid to the State. The participation of the *censeur* (appointed by the Minister of Economics and Finance) in the meetings of the General Council enables the government to follow the budgetary process closely.

Audit of Central Bank Accounts and Procedures

In addition to the general supervision of the activities of the Bank of France by the government's *censeur*, the central bank is subject to the supervision by the Audit Commission (Cour des Comptes), which is responsible for the supervision of all public agencies and undertakings.

On behalf of the General Council, the Governor submits an annual report on the Bank's operations to the President of the Republic.

MONETARY DECISIONMAKING IN FRANCE



1 Meets every 2 weeks
2 Meets at least twice a year

CENTRAL BANK-GOVERNMENT RELATIONS IN GERMANY

The first German central bank, the Reichsbank, was established in 1876. After the Second World War, the Allied Occupation authorities replaced the Reichsbank with several Land Central Banks in the occupied western zones. In 1948, they created the Bank deutscher Länder, which was to serve as an interim central bank, pending the foundation of a new German state. The Basic Law of the Federal Republic passed in 1949 required the federal government to replace the central banking legislation imposed during the Occupation and establish a new central bank. Eight years later, on July 26, 1957, the Deutsche Bundesbank was established. The Deutsche Bundesbank, like its immediate predecessor, enjoys significant independence from the federal government. According to Article 3 of the Bundesbank Act, its principal responsibility is "to regulate the quantity of money in circulation and of credit supplied to the economy * * * with the aim of safeguarding the currency."

INSTITUTIONAL STRUCTURE AND THE DECISIONMAKING PROCESS

The governing board of the Deutsche Bundesbank is the Central Bank Council, which is composed of the President and Vice President of the Bundesbank, the other members of the Directorate and the eleven Land Central Bank Presidents. The Central Bank Council determines the money and credit policy of the Bank. It generally meets every two week and makes its decisions by a simple majority of the votes cast.

The Directorate is composed of the President and Vice President of the Bundesbank and up to eight other members. (There are currently five.) It is the executive organ of the Bundesbank and is responsible for administering the decisions of the Central Bank Council. In addition, the Directorate is responsible for all transactions with the federal government, transactions with banks that operate throughout the Federal Republic, foreign exchange transactions, and open market operations.

The Bundesbank operates a main office, known as a Land Central Bank, in every Land, including West Berlin. The Land Central Banks are responsible for both transactions with the public authorities in the Land and transactions with banks in their area. Each Land Central Bank is headed by a Managing Board, which consists of a President, a Vice President, and in the larger Länder, of a third member.[1]

The Bundesbank Act is very explicit about the relations between the Bundesbank and the federal government. Article 12 calls upon the Bank to support the general economic policy of the federal government, "but only insofar as this support does not undermine its assigned task of preserving monetary stability." It states, in addition, that the Bundesbank "shall be independent of instructions from the federal government." The Bundesbank Act commits both the federal government and the Bundesbank to cooperation and mutual consultation. Article 13 states that the Bundesbank shall "advise the federal government in monetary policy matters of major importance and provide it with information on request." The federal government should invite the Bundesbank President and Vice President to all cabinet meetings in which issues affecting monetary policy (such as the financing of the federal budget) are discussed. Similarly, government ministers or their representatives are entitled to attend all meetings of the Central Bank Council. They may propose motions to the Council, but they have no right to vote. They can, however, delay any Central Bank Council decision by two weeks. In practice, the government has never formally exercised its power to delay a Central Bank Council decision. On occasion, members of earlier governments have put motions to the Central Bank Council (only to be voted down).

APPOINTMENTS

Members of the Bundesbank Directorate, including the President and the Vice President are nominated by the federal government and appointed by the President of the Federal Republic for a period of eight years, or in exceptional circumstances for shorter periods of at least two

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[1] The Unification Act, which formally unified the Federal Republic of Germany and the German Democratic Republic (GDR) on October 3, 1990 requires the Federal Government to amend the Bundesbank Act by October 3, 1991. As a transitional measure, local management of the Bundesbank in the five new Länder is provided by a Provisional Administrative Office in East Berlin. This office is headed by a member of the Directorate, under the guidelines and instructions of the Directorate. The amendments to the Bundesbank Act are necessary to determine how the five new Länder will be ultimately represented. An extension of the existing structure would lead to the creation of five new Land Central Banks. Many feel, however, that this would make the Central Bank Council an unwieldy body. Thus, one proposal is to replace the existing structure with a smaller number of Land Central Bank districts.

years. Directorate members can and generally are reappointed until they reach the retirement age of 68.

The eleven Land Central Bank Presidents who serve on the Central Bank Council are nominated by the Bundesrat, the upper house of parliament which represents the Länder. In making a nomination, the Bundesrat is required to follow the recommendation of the political authority in the Land concerned. Like the members of the Directorate, Land Central Bank Presidents are appointed by the President of the Federal Republic for eight year (renewable) terms. (Vice Presidents of the Land Central Banks are nominated by the Central Bank Council and appointed by the Bundesbank President.)

Before any Directorate member or Land Central Bank President can be appointed by the President of the Federal Republic, the Central Bank Council must comment on the nomination. The Central Bank Council pays particular attention to the requirement of the Bundesbank Act, which stipulates that holders of both offices must have "special professional qualifications." The Central Bank Council's role is purely advisory, however. In practice, a negative comment from the Council has not prevented an appointment.

The Bundesbank Act thus provides for the appointment of up to ten members of the Directorate and the Land Central Bank Presidents (currently eleven). In this way, it ensures that the federal government is not able to nominate directly a majority of the Central Bank Council. The autonomy of the Members of the Council is also enhanced by the fact that they cannot be dismissed in accordance with their contract before the end of their terms except for reasons which lie in their person.

ANNOUNCEMENT OF POLICY DECISIONS

Article 33 of the Bundesbank Act states that the Bundesbank shall publish announcements intended for the general public—particularly the calling in of banknotes, the setting of interest rates, discount rates, and minimum reserve requirements—in the Federal Gazette.

Such decisions, including changes in the level of the discount and lombard rates, or in the annual target for monetary growth, are announced after the meeting of the Central Bank Council in which they are decided. Announcements are often made by the Bundesbank President in a press conference following the meeting. Announcements are also made in the form of written press releases. In addition, the Bank maintains an automatic telephone answering machine to provide information on its decisions. However, unlike the Open Market Committee of the Federal Reserve, the Central Bank Council never publishes the minutes of its meetings. The Bank's publications, including its monthly and annual reports, provide broader analyses of monetary policy conditions and explanations of the Bank's actions.

Central Bank Financing of Government Borrowing

Article 20 of the Bundesbank Act authorizes the Bundesbank to grant short-term cash advances to the federal government, to its Special Funds (the Federal Railways, Federal Post Office, Equalization of Burdens Fund, and the ERP Special Fund), and to Länder governments. The amount of such credit is, however, strictly limited. The credit ceiling for the federal government is DM 6 billion. The ceilings applied to the various Special Funds range from DM 50 million to DM 600 million. And the ceiling for Länder governments is DM 40 per inhabitant in the large Länder—DM 80 per inhabitant in the Land of Berlin and the Free and Hanseatic Cities of Bremen and Hamburg. It should be noted that these ceilings do not imply a right to borrow; rather, they represent an upward limit of what the Bank may choose to lend.

The Bundesbank Act prohibits the Bundesbank from purchasing bonds issued directly by these same public authorities. However, the Bundesbank may purchase bonds on the secondary market, but only for the purpose of regulating the money market, specifically for influencing the level of bank liquidity and interest rates.

Budgetary Procedures

The Bundesbank is not required, and does not, publish a budget. The Bank decides upon its own expenditures without government supervision, but is controlled by the Federal Court of Audit (Bundesrechnungshof).

Audit of Central Bank Accounts and Procedures

The Directorate is responsible for drawing up the annual accounts of the Bank. The accounts are then audited by one or more auditors appointed by the Central Bank Council in agreement with the Federal Court of Audit. After the Central Bank Council approves the accounts, they are published by the Directorate.

The report of these auditors serves as the basis for an audit carried out by the Federal Court of Audit. The report, along with the comments of the Federal Court of Audit, must be communicated to the federal

Ministry of Finance. The Minister of Finance thus receives, but does not control or approve, the Bank's accounts.

The profits of the Bank, which are in excess of the authorized deductions for reserves, are transferred to the federal government.

MONETARY DECISIONMAKING IN GERMANY

DEUTSCHE BUNDESBANK

	Directorate	Central Bank Council[1]	Land Central Banks
Government ministers	President of the Bundesbank Vice-President Up to 8 Other Members	Members of Directorate Presidents of the Land Central Banks	Land Central Bank President Vice-President(s)
May attend Central Bank Council meetings on non-voting basis; May propose policies to Central Bank Council; May delay Council decisions 2 weeks.	Administers decisions of Central Bank Council; Conducts transactions with federal government; open market operations; and foreign exchange transactions.	Determines money and credit policy; Sets monetary targets.	Bundesbank office in each Land; Conducts transactions with public authority in Land.

1 Meets every 2 weeks

CENTRAL BANK-GOVERNMENT RELATIONS IN ITALY

The Bank of Italy was founded in 1893. The actions of the Bank and its relationship to the government are covered in a series of laws, statutes, and decrees. Most important are the Statute of the Bank of Italy (1936), the Banking Law (1936), and the law governing note-issuing banks (1910). The Bank of Italy has no statutory obligations. The Italian Constitution of 1947 makes no reference to monetary policy or the central bank, noting only that the Republic has a duty to protect savings.

INSTITUTIONAL STRUCTURE AND THE DECISIONMAKING PROCESS

The government formally has the power to set general economic guidelines and to approve monetary and credit policy. The Interministerial Committee for Economic Planning (Comitato Interministeriale per la Programmazione Economica or CIPE), which was created in 1967, bears the principal responsibility for setting economic policy guidelines. Its membership consists of the Prime Minister and fourteen other government ministers.

These guidelines must then be taken into account by the Interministerial Committee on Credit and Savings (Comitato Interministeriale per Credito e Risparmio or CICR), which is formally responsible for setting credit policy. The CICR is composed of the Treasury Minister (who serves as chair), as well as the Ministers of Public Works, Agriculture, Foreign Trade, Budget, Industry, Southern Affairs, EEC Affairs, and State Participations. The central bank serves as the CICR's technical agent. Despite its formal authority, however, the CICR does not play a significant role in monetary policymaking and generally has consented to decisions which have already been taken by the Treasury Minister and Governor of the Bank of Italy.

All responsibilities and authority in the Bank of Italy are concentrated in the hands of the Governor. However, in practice, important monetary decisions are thoroughly discussed in the Bank's Directorate, which consists of the Governor, the Director General and two Deputy Director Generals. The Directorate meets at least twice a month to review economic and monetary conditions with the senior staff of the Bank.

The government is formally involved in the Bank's choice of certain monetary policy instruments. Changes in reserve requirements beyond a preestablished limit must be officially approved by the CICR and enacted by a decree of the Treasury Minister. Similarly, any change in the discount rate must also be enacted by a decree of the Treasury

Minister, although the law provides that the initiative for such a change must come from the Governor. The amount, timing, and technical form of intervention on the money market and the foreign exchange market, by contrast, is at the discretion of the central bank.[1] The importance of different instruments in the conduct of monetary policy has evolved considerably over time. In the 1970s and early 1980s, the Bank of Italy made extensive use of direct credit controls to achieve its objectives. In recent years, the Bank has placed much greater reliance on indirect intervention in the secondary money market.

The Bank of Italy has set targets on a combination of broad credit and monetary aggregates since the mid-1970s. The setting of the targets occurs on an annual basis and is incorporated into the government's financial planning process. A three year budgetary projection is issued by the government in May. Subsequently, in early Autumn, the Minister of the Budget sets out macroeconomic forecasts for the coming year in a detailed document, Relazione Previsionale e Programmatica (RPP). This document must be approved by the CIPE and is then presented to Parliament. The Bank of Italy is actively involved in the preparation of these forecasts and is therefore able to develop consistent monetary targets which the Governor must present to the CIPE before it approves the RPP. The government's financial plans are then embodied in its annual budget law which is presented to the Parliament by the end of September and must be approved by the end of the year.

Due to the high quality of its technical staff and the personalities of its governors, the Bank of Italy has long enjoyed great prestige in Italian political and economic life. These qualities have also granted the central bank greater autonomy in both the formulation and implementation of monetary policy than might be assumed on the basis of Italian law. There have, for example, been no instances when a Governor's proposal for a change in the discount rate has been rejected.

As far as administrative matters are concerned, the Bank is not subject to direct government involvement. Under the Bank's statutes, the Governor is responsible to the General Assembly of Shareholders, and

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[1] The Italian Exchange Office (Ufficio Italiano dei Cambi or UIC) was created in 1945 to undertake the management of Italy's foreign exchange. Although legally a separate body from the Bank of Italy, the UIC is closely linked to the central bank. The Governor of the Bank of Italy is also chairman of the UIC and therefore chooses an intervention policy consistent with the Bank's monetary policy goals. The UIC generally operates through the Bank of Italy's operational structure; its balance sheet is consolidated into the Bank's.

the Board of Directors. Shares of the Bank of Italy are held by savings banks, the larger commercial banks, insurance companies, and social security institutions. (The government, however, owns a sizable share of the stock in some of these institutions.) The Board of Directors is composed of the Governor and thirteen directors who are elected by the shareholders of the Bank for renewable three year terms.[2] The Board meets quarterly, but it may meet more often at the determination of the Governor or at the request of at least three members. Every year, the Board of Directors appoints four of its members to serve, along with the Governor on an Executive Board, which meets once a month. The principal duties of the Board of Directors involve supervision of administrative matters in the Bank and appointment of the Bank's personnel. A government inspector or representative of the Treasury Minister may participate in meetings of the Assembly, the Board of Directors, and its Executive Committee. This official has the power to suspend the implementation of any policy which he or she believes is contrary to law, or to the statutes governing the Bank, for up to five days. The Treasury Minister then is authorized to annul the decision. For this reason, no decision of the Board becomes official until this five day period has elapsed. In practice, however, the Treasury Minister has never annulled the Board's decisions.

APPOINTMENTS

The Board of Directors both nominates and dismisses the members of the Directorate; however, the Governor's appointment must be approved by a decree of the President of the Republic on the proposal of the Prime Minister, in agreement with the Treasury Minister and after consultations with the Cabinet. The Bank's postwar history suggests that the government's ability to influence the selection of the members of the Directorate is limited. Most Governors of the Bank have served long terms in office; indeed, there have been only five Governors in the past forty years. And, the last two Governors have come from within the Bank of Italy itself.

[2] The directors are elected by shareholders to represent the thirteen major offices of the Bank. The offices of Florence and Leghorn combine to select one director. Elections are scheduled so that roughly one-third of the directors are elected every year.

ANNOUNCEMENT OF POLICY DECISIONS

The annual monetary and credit targets of the Bank of Italy are announced by the Governor in his parliamentary address during the debate over the Relazione Previsionale e Programmatica and in the October edition of the Bank of Italy's Economic Bulletin. The Bulletin also lays out the Bank's opinion regarding the official forecasts.

Decisions regarding changes in reserve requirements or the discount rate are announced by the government. In recent years, however, the discount rate has become a less important policy instrument, compared to intervention on the secondary market. Any change in the Bank's views regarding the desired levels of interest rates generally becomes apparent through its interventions on this market, rather than through a formal announcement of its policy intentions.

The Governor's address to the General Meeting of Shareholders, in which he analyzes monetary conditions and discusses necessary future policies, is considered one of the most important economic speeches in Italy. In addition, the Governor is often called to testify before parliamentary commissions.

CENTRAL BANK FINANCING OF GOVERNMENT BORROWING

From 1975 to 1981, the Bank was committed to purchasing all Treasury bills which were not purchased at auction, thereby providing the Treasury with virtually unlimited financing. Since the "divorce" between the Treasury and the Bank of Italy in 1981, the Bank has no longer been required to act as the residual buyer at Treasury auctions. The Bank still participates from time to time in primary auctions, primarily with the purpose of managing its own portfolio.

The Bank of Italy is required to provide a direct credit line to the Treasury, which enjoys an unconditional overdraft of this account up to 14 percent of all expenditures (both current and capital) planned in the annual budget law. Extraordinary loans above this amount can be required, but only by a vote of Parliament specifying the exact amount of the loan.[3]

[3] Such a case occurred in 1983, when the Treasury had exhausted its overdraft facility and the Bank of Italy refused to provide any additional financing through the purchase of government securities. Parliament then approved an extraordinary loan of eight trillion lire, which, as required, was repaid by the end of the year.

BUDGETARY PROCEDURES

The budget for the Bank of Italy is drawn up on an annual basis within the Bank. It is then examined by the inspector or Treasury representative, who also has the authority to inspect the projections and estimates on which the budget is based. The budget is then set and approved by the Board of Directors, and, subsequently, by the General Assembly. Since the inspector or Treasury representative sits on the Board and has the power to suspend any decision which is contrary to the laws or statutes governing the Bank, the government legally has the ability to influence the budgetary process under certain limited conditions. In practice, the government's inspector or Treasury representative has never taken such action.

AUDIT OF CENTRAL BANK ACCOUNTS AND PRACTICES

Audits of the Bank of Italy are performed both internally and externally. The General Meeting of Shareholders appoints five auditors and two alternates (Collegio sindicale), who, operating as a group, are charged with examining the Bank's administration. The auditors may report directly to the Governor.

The Treasury Minister is formally responsible for the supervision of the Bank. The Minister may, if need be, make use of a Permanent Committee, consisting of six members of parliament (elected by both houses) and five members chosen among government officials and judges. At the request of the Minister, the Permanent Committee expresses its opinion on a variety of subjects ranging from the issuing of bank notes to the modification of the statutes of the central bank.

For the supervision of the administration of the Bank and its various decisionmaking bodies, the Treasury Minister relies upon the same government inspector mentioned above, who examines among other things the annual financial statement of the Bank.

MONETARY DECISIONMAKING IN ITALY

		BANK OF ITALY — Bank Directorate	BANK OF ITALY — Board of Directors[1]
Interministerial Committee on Credit & Savings: Treasury Minister & 8 other ministers	Treasury Minister	Governor Director General 2 Deputy Director Generals	Governor 13 other Directors
Formally responsible for credit policy; Approves changes in reserve requirements beyond set limits.	Enacts changes in discount rates & reserve requirements; Attends meetings of shareholders & Board of Directors; May annul Bank decisions contrary to law or statute.	Governor sets and implements monetary policy; Proposes changes in discount rate; and Sets monetary targets, with assistance of the Directorate.	Supervises administration of Bank; Appoints officers of Bank.

1 Meets quarterly; Executive Committee of the Board meets monthly

CENTRAL BANK-GOVERNMENT RELATIONS IN JAPAN

According to the Bank of Japan Law of 1942, as amended in 1947 and 1949, the central bank "has for its object the regulation of the currency, the control and facilitation of credit and finance, and the maintenance and fostering of credit system, pursuant to the national policy, in order that the general economic activities of the nation might adequately be enhanced."

INSTITUTIONAL STRUCTURE AND THE DECISIONMAKING PROCESS

The Policy Board is the supreme decisionmaking body of the Bank of Japan. It consists of seven members: the Governor of the Bank of Japan; four voting members (one with experience and knowledge in the field of city banking, one in regional banking, one in industry or commerce, and one in agriculture); plus two nonvoting representatives of the Japanese government (one from the Ministry of Finance, the other the Economic Planning Agency). The Chairman of the Policy Board can be elected from any of these seven members, but the position has traditionally been assumed by the Governor.

The Governor is also head of the central bank's Executive Committee. The Executive Committee—which is often referred to as marutaku, or round table meeting—consists of the Governor, the Senior Deputy Governor, the Deputy Governor for International Relations, and at least three executive directors.

Policy proposals are normally drafted by departments of the Bank of Japan and then discussed at Executive Committee meetings (which are held every business day except Wednesday). Once the Executive Committee has concluded that a measure is necessary, the Governor presents the proposal to the Policy Board for its decision. (Other members of the Policy Board may also present proposals, but have generally not done so.) Meetings of the Policy Board are normally held twice a week, unless an issue requires more urgent attention.

The Policy Board is formally invested with decisionmaking authority in the area of monetary policy. It has, for example, the authority to set the discount rate and determine the Bank's operations in the money market. In practice, the Policy Board fixes the overall framework for such operations (i.e., categories of eligible bonds and bill, eligible financial institutions, and rate-fixing methods), and delegates daily market management (choice of instruments, rates, and timing) to the Bank's Credit and Market Management Department. However, reserve requirement changes must be endorsed by the Finance Minister and published in the Official Gazette before becoming effective. The Law concerning the Reserve Requirement System requires such procedures since reserve requirements are compulsory and backed by legal sanction.

According to the Bank of Japan Law, the Finance Minister may, "if deemed particularly necessary for the attainment of the object of the Bank of Japan," direct the central bank to change its bylaws or to undertake any necessary actions.[1] This power, however, has never been exercised. In practice, conflicts between the central bank and the government are ironed out informally. Communication and cooperation between the Ministry of Finance and the Bank of Japan are facilitated by the inclusion of the two government officials on the Policy Board. In addition to this more formal channel, frequent discussions occur between officials at all levels from the Bank of Japan and other government agencies.

APPOINTMENTS

The Governor and the Senior Deputy Governor are appointed by the Cabinet. The four voting members of the Policy Board are appointed by the Cabinet with the consent of the two houses of the Diet. The Governor and Senior Deputy Governor serve terms of five years, while the voting Policy Board members serve terms of four years. By contrast, the Deputy Governor for International Relations and the executive directors are appointed by the Finance Minister (based on the recommendation of the Governor) for terms of four years.

For the past two decades, the Governor's post has alternated between former senior officials from the Ministry of Finance and from the Bank of Japan. Although all Policy Board members and Bank officers are eligible for reappointment, recent governors have only served a single term in office.

The Bank of Japan Law stipulates that the four voting members of the Policy Board may not be dismissed against their will, unless they

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[1] In the postwar period, disagreements have arisen within Japan over the appropriate degree of central bank independence. The issue was raised in the late 1950s in the context of a study conducted by a Government research committee on Japan's financial system. Because the Committee members disagreed on this point, the Ministry of Finance took no action on a proposed revision in the Bank of Japan law.

have been sentenced to imprisonment or have been judged either physically or mentally incompetent. In such an instance, the dismissal is effected by the Cabinet. Senior officers of the Bank, on the other hand, may be dismissed by the Cabinet (in the case of the Governor and the Senior Deputy Governor) and by the Finance Minister (in the case of the other senior officers) for violating the law, for contravening the orders of the Finance Minister, or more generally "whenever it is deemed necessary for the attainment of the object of the Bank." This clause would appear to provide the government with a relatively easy means to remove Bank officers. In practice, however, it has never been invoked.

ANNOUNCEMENT OF POLICY DECISIONS

The Bank of Japan Law contains no specific provisions regarding procedures by which the central bank must announce its policy decisions. The Governor of the Bank of Japan holds a press conference every other week and after each quarterly branch manager's meeting, as well as in the course of his business trips within Japan and abroad. He can also be called upon to explain the conduct of monetary policy to the Diet. In recent years, the Governor has appeared before the Diet about ten times a year, although in 1986, the year after the Plaza Agreement was reached, he gave testimony on 32 separate occasions.

More generally, the Bank of Japan has, since 1985, published a Quarterly Economic Outlook, which analyzes monetary conditions, forecasts future trends, and explains the policy orientation of the Bank. The Policy Board also submits an annual report to the Diet, via the Minister of Finance, which covers the financial condition of financial institutions, the changes in the Bank's supervisory policy, and an explanation of the policies it has pursued.

CENTRAL BANK FINANCING OF GOVERNMENT BORROWING

Central bank financing of the government is discussed in both the Bank of Japan Law and the Finance Law. The former authorizes the central bank to make advances to the government without collateral and to participate in government bond issues. The latter prohibits the Bank from underwriting government bonds or extending long-term loans to the government. The Finance Law was passed most recently and thus supercedes the Bank of Japan Law. The conditions governing central bank financing of the government are laid out in Article 5 of the Finance Law. The Bank of Japan may underwrite short-term bills which are not purchased at the public offering. In practice, there has been virtually no market demand since the interest rate on those bills has been below the official discount rate. The Bank of Japan is also allowed to underwrite, up to an amount authorized by the Diet, government bonds issued for the sole purpose of refinancing those bonds at maturity which were purchased from the private sector.

BUDGETARY PROCEDURES

The Bank of Japan is the only central bank in the G–10 which does not have budgetary autonomy. Unlike other central banks, it must obtain prior approval of its budgeted expenditures from the government. The Bank of Japan Law charges the Policy Board with "deciding on the estimate of expenditures * * * of the Bank of Japan." Yet, the Bank of Japan must then "in accordance with prescriptions of the competent Minister, make an estimate of the expenditures of each business period, and submit the same to the competent Minister for his permission prior to the commencement of the business period."

AUDIT OF CENTRAL BANK ACCOUNTS AND PRACTICES

The Bank of Japan Law provides the government with extensive supervisory powers over the Bank's accounts and practices. Auditors, who are senior officers of the Bank, inspect the business of the Bank internally; the Finance Minister also appoints the Comptroller of the Bank of Japan (generally a senior Finance Ministry official) to oversee the business of the Bank. The Finance Minister can require the Bank of Japan "to make reports on the condition of its business and property, make inspection of the Bank's affairs, or issue orders to take such actions as are necessary in the exercise of his supervision."

MONETARY DECISIONMAKING IN JAPAN

BANK OF JAPAN

Ministry of Finance

Approves reserve requirement rates;
Approves central bank budget;
May issue directive to central bank.

Policy Board[1]

Governor
4 Voting Members
2 Nonvoting Members, representing Finance Ministry & Economic Planning Agency

Principal decisionmaking body:
Sets discount rate;
Sets open market operations;
Sets monetary targets.

Executive Committee[2]

Governor
Senior Deputy Governor
Deputy Governor for International Relations
3 or more Executive Directors

Considers policy proposals from central bank staff and submits them to Policy Board;
Implements Policy Board decisions.

1 Meets twice a week
2 Meets daily ex. Wednesday

CENTRAL BANK-GOVERNMENT RELATIONS IN SWITZERLAND

The Swiss National Bank was established in 1907 as a joint stock company.[1] Its shares are registered; that is, ownership in the Bank is controlled and, specifically, is limited to Swiss citizens and corporations. Article 39 of the Swiss Constitution states that the principal function of the Swiss National Bank is to "regulate the country's money circulation, to facilitate payment transactions, and to pursue a credit and monetary policy serving the interests of the country as a whole." The Bank, which is independent of the government, has interpreted its mandate to mean maintaining price stability.

INSTITUTIONAL STRUCTURE AND THE DECISIONMAKING PROCESS

The Governing Board is the principal body responsible for monetary policy within the Swiss National Bank. It consists of three full-time members—a Governor and two deputies. Actions of the Governing Board are supervised by the Bank's Shareholders, the Bank Council, and the Bank Committee. The federal government and the Shareholders together select the Bank Council. The Bank Council consists of forty members (including both its president and vice president), representing both the economic interests and the regions of Switzerland. The Bank Council meets quarterly and is charged with supervising the Bank's administrative practices. The Bank Committee serves as the executive committee of the Bank Council. It meets monthly and bears most of the Bank Council's supervisory responsibilities.

In addition, the Governing Board is required to consult the Bank Committee on changes in the discount or lombard rates. Historically, it was in this way that the Bank Committee was able to exert some influence over the conduct of monetary policy. However, these rates no

[1] The Swiss Constitution did not specify the precise legal form of the central bank. Instead, the government was authorized to establish the bank either as a state bank of issue (thus under direct government control) or a joint stock company. In a 1897 referendum, the government first proposed a state bank of issue, but this plan was rejected by voters who feared that such a bank would be unable to resist demands for state financing. Having lost this vote, the government then presented a plan for the creation of an independent stock company which was approved by voters.

longer play a key role in the formation of monetary policy. Discounting bills is no longer a significant source of variation in the monetary base; the lombard rate now serves primarily as a safety valve for banks with immediate liquidity needs. Since 1989, the lombard rate has floated so as to remain two points above the overnight lending rate.

Since 1975, the Swiss National Bank has framed its monetary policy objectives in terms of an annual monetary target. After consultations within the Bank, the Governing Board decides upon an appropriate target in November, which is then announced to the public in December. (In 1979, the Governing Board experimented with an exchange rate target instead.) In the late 1980s, the Swiss National Bank came to the conclusion that this specific target was both difficult to control and not closely linked to its ultimate policy objectives. As a result, its announcement of the target is currently accompanied by a statement that describes the forecasts underlying its target, as well as the conditions that might lead the Bank to alter its desired monetary course.

The overall course of monetary policy is reviewed by the Governing Board in the context of its quarterly report and may be reviewed even more frequently if problems arise. The Governing Board meets weekly to evaluate monetary conditions and decide upon the guidelines to be used for the implementation of policy.

The Swiss National Bank is not subject to instructions from the federal government. The law does require government approval if the Bank wishes to restrict either capital inflows from abroad or issues of domestic securities in the Swiss capital market. In the last ten years, however, neither instrument has been used due to strong support for freedom of international capital movements in both the government and the central bank.

Policy coordination between the Swiss National Bank and the federal government occurs frequently and at all levels. The Governing Board meets regularly with members of the federal cabinet responsible for economic policy. A meeting between the Governing Board and the cabinet as a whole is also held prior to the announcement of the annual monetary target. Senior officers of the Bank are also in regular contact with their counterparts in the federal Finance Ministry.

APPOINTMENTS

Members of the Governing Board are appointed by the Federal Council (the Cabinet) for renewable six year terms.

Members of the Bank Council are appointed for renewable four year terms by the Federal Council and the General Meeting of Shareholders in a specific order. The Federal Council first appoints the President and Vice President of the Bank Council. Second, the General Meeting of the Shareholders elects fifteen members of the Council. The Federal Council then selects the remaining twenty-five members, making sure that the overall membership reflects the country's various regions and economic interests. No more than five can be members of the federal parliament; and no more than five can be members of cantonal governments.

Members of the Bank Council then appoint the eight members of the Bank Committee for renewable four year terms. The members of the Bank Committee are selected with a view to representing various regions of the country.

All employees of the Swiss National Bank, including the members of the Governing Board, Bank Council, or Bank Committee, may be dismissed for cause. In practice, however, there appear to be no instances in which members of the Governing Board, Bank Council, or Bank Committee have actually been dismissed.

Announcement of Policy Decisions

The future direction of Swiss monetary policy is made known primarily through the annual announcement of the Bank's monetary target for the coming year. Intrayear changes will be announced by the Governing Board in speeches, interviews, or its biannual press conference. The Swiss National Bank also explains its own evaluation of monetary conditions and trends in its monthly, quarterly, and annual reports.

Central Bank Financing of Government Borrowing

The National Bank Law does not mention central bank lending to either the Swiss federal or cantonal governments. It is thus theoretically possible for the Bank to provide unlimited credit to the government, either by purchasing government securities or by granting lombard credit based on collateral in the form of government securities. In practice, government borrowing from the central bank has had a relatively small effect on monetary base creation, due to a common belief on the part of both the Bank and the government that monetary policy should be insulated from debt management.

Budgetary Procedures

The Bank Council approves the annual limits on the Bank's current expenditures; it also approves all capital expenditures. The Governing Board of the Swiss National Bank is required to submit the Bank's annual accounts to the Federal Council for approval before they are published and before they are received by the General Meeting of Shareholders.

Audit of Central Bank Accounts and Practices

Audits are first conducted by the Bank's own auditors and then by an external Committee of Auditors. The Committee of Auditors, which consists of three members and alternates, is elected annually by the General Meeting of Shareholders. It is responsible for auditing the annual accounts and balance sheet of the Swiss National Bank. The Committee of Auditors is required to submit a written report to the General Meeting and to inform the Federal Council of its findings. In addition to these annual audits, the Committee of Auditors is entitled to examine at any time all aspects of the Bank's business.

MONETARY DECISIONMAKING IN SWITZERLAND

SWISS NATIONAL BANK

Governing Board

Governor
2 Deputy Governors

Sets and implements monetary policy;
Sets monetary targets.

Bank Committee[1]

8 Members of the Bank Council

Executive Committee of Bank Council;
Carries out most supervisory functions;
Consults with Governing Board on lombard and discount rates.

Bank Council[2]

President
Vice President
38 other Members, representing economic & regional interests

Supervises administrative practices of the Bank.

1 Meets monthly
2 Meets quarterly

CENTRAL BANK-GOVERNMENT RELATIONS IN THE UNITED KINGDOM

The Bank of England Act of 1946 consists primarily of the provisions necessary to bring about the nationalization of the central bank. It provides for the transfer of ownership of the Bank's stock, authorizes the government to appoint the Bank's senior officials, and empowers the Treasury to issue directives to the Bank, but makes no direct reference to monetary policy or the Bank's role in it.

INSTITUTIONAL STRUCTURE AND THE DECISIONMAKING PROCESS

The Bank of England is formally governed by its Court of Directors which consists of the Governor, Deputy Governor, and sixteen directors, no more than four of whom can be employed full time by the Bank. The twelve (nonexecutive) directors are drawn from commercial banking, industry, and academia; since 1946, one has usually been a trade-unionist. The Court meets weekly, but has not been active in important policy decisions, in part because of a concern of outside nonexecutives obtaining inside information on future policy changes. Its principal role therefore has been to serve as a sounding board for the Governor. In practice, therefore, the Bank is managed by the Governor, with the assistance of the Deputy Governor and the four executive directors.

The Bank's subordination to the government is firmly grounded in the Bank of England Act, which stipulates that the Chancellor may issue directions to the Bank of England after consultation with the Governor. The power was not designed to permit day-to-day interference by the Treasury in the ordinary work of the Bank, but rather to ensure that, in the event of disagreement, the government would have the last word. In fact, although disagreements have arisen between the Treasury and the Bank, the process of policy coordination has ensured that no Chancellor has ever issued a directive to the Bank.

There is considerable contact at all levels between the Bank of England and the Treasury. The Chancellor and Governor, for example, meet at least once a week. The precise details of the arrangements for meeting at more junior levels change overtime, but at least for some years there has been a formal process of coordination that coincides with the collation of monthly data. Each month, the Monetary Committee within the Bank of England meets under the direction of one of the executive directors to form preliminary judgments on monetary conditions and trends. These judgments form the basis of discussions held in a smaller meeting with the Governor and senior officers. The process culminates in a report, which reviews both domestic and international monetary conditions and sets out the Bank's views on the appropriate interest rate policy for the forthcoming weeks. A similar report is also prepared within the Treasury. The two reports are then discussed at a meeting of senior Bank and Treasury officials, held at the Treasury and chaired by the permanent secretary to the Treasury. The senior Bank official in attendance is the director for home finance. Subsequent to these meetings, the Governor of the Bank of England regularly lays out the Bank's views in writing to the Chancellor of the Exchequer, who is then responsible for making ultimate policy decisions.

APPOINTMENTS

The Governor, Deputy Governor and directors of the Bank of England are all appointed by the Crown, which in practice means the Prime Minister acting on the advice of the Chancellor of Exchequer after consultation with the Governor (or where the appointment of the Governor is concerned, usually with senior Bank's officials, present and past). All are appointed for renewable terms: five years in the case of the Governor and Deputy Governor, four years for the directors. (Four of the sixteen directors retire in rotation each February.) However, the Bank of England Act does not provide the government with the power to dismiss senior Bank officials. Since the officers are formally appointed by the Crown, they can only be dismissed by the Crown. Presumably a government could request the Crown to dismiss the Governor, but such an eventuality has never occurred.

ANNOUNCEMENT OF POLICY DECISIONS

The Bank of England is accountable to the Chancellor of the Exchequer, who in turn is responsible for monetary policy before Parliament. The Chancellor thus may both announce and answer questions on monetary policy.

Since 1980, the government has set out its views on monetary policy in a Medium-Term Financial Strategy (MTFS) at the time of its annual spring budget. The MTFS has undergone considerable evolution in the past decade. Originally, it specified a target for the annual growth of a broad monetary aggregate for the forthcoming four year period.

However, the authorities soon concluded that the aggregate was not linked closely enough to their ultimate objective (nominal income) and, equally important, that they could not exercise sufficient control over the supply of money. For this reason, the MTFS currently specifies a wide range of economic and financial indicators that will be used to evaluate monetary conditions and to guide monetary policy.

Amendments to policy may also be announced at any time by the Chancellor, but typically in a major occasion like the Mansion House speech or the Autumn Statement setting out the government's expenditure plans is used.

For its part, the Bank of England also evaluates current monetary policy conditions and requirements in both its Quarterly Bulletin and Annual Report. The Annual Report is laid before Parliament, but has never been subject to debate. The Governor and other officers are regularly examined on the policies and administration of the Bank of England by Select Committees of the Parliament.

CENTRAL BANK FINANCING OF GOVERNMENT BORROWING

The Bank of England may make direct short-term loans to the Treasury to cover its current budget spending requirements. It does not participate significantly in the direct financing of the Treasury, but there exists no specific limits on Bank purchases of government paper in the market.

BUDGETARY PROCEDURES

The Bank of England Act implicitly grants the central bank budgetary independence. Until the 1970s, the Bank was not even required to publish accounts. The recommendations of a Select Parliamentary Committee led the Bank to publish its accounts with its Annual Report (beginning in 1971).

AUDIT OF CENTRAL BANK ACCOUNTS AND PRACTICES

The accounts of the Bank of England are audited annually by a leading firm of chartered accountants.

MONETARY DECISIONMAKING IN THE UNITED KINGDOM

BANK OF ENGLAND

Court of Directors[1]

Chancellor of the Exchequer

Makes ultimate monetary policy decisions;
May issue policy directive to the Bank of England.

Governor
Deputy Governor
4 Executive Directors
12 Outside Directors

Court of Directors:
Formal governing body, but in practice, acts as advisor to the Governor.

Governor:
Manages Bank;
Implements monetary policy.

1 Meets weekly

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