

# Parliament, senior experts rally to defend public power over RBA

In the Senate Economics Committee's first 22 February hearing on the RBA Reforms Bill 2023, the Reserve Bank Review panel and Treasury representatives doubled down on their demand for changes to "future proof" RBA "independence" but failed to present any compelling arguments. After nearly four hours of scrutiny, defenders of the Review's recommendations, enshrined in the government's Reserve Bank Reforms Bill 2023, were deep into quicksand. Here's how the battle lines were drawn regarding the recommended removal of Section 11 (s.11) of the *Reserve Bank Act*:

**For:** Treasury and the RBA Review panel.

**Against:** Former RBA governors; former treasurers; all public submitters to the inquiry.

**Abstaining:** RBA Governor Michele Bullock, who stuck to the line she struck with Greens Senator Nick McKim during a Senate Estimates session a week earlier: "I am agnostic."

Even before the hearing had concluded, word was going around that Treasurer Jim Chalmers would be forced to cave on the inquiry's prescriptions, ditching the removal of s.11 at the very least. Such a stink had been kicked up over s.11 that it was on the minds of all the Senators involved in the hearing and heavily dominated the day's proceedings, with one superseding question: where did this recommendation come from?

## Where did it come from?

Throughout the entire hearing Deputy Chair of the committee, Liberal Senator Andrew Bragg returned to that key question: "Why is this on the agenda at all?" The matter had not been raised by any politician during the push for a review of the RBA, was not flagged in the Terms of Reference of the Review, nor in the Review panel's Issues Paper, and no submissions from the public during the consultation process had raised it.

Former Reserve Bank Governor Ian Macfarlane laughed at the question and said, "I don't know!" He said he didn't think there was any "deep thinking" behind the recommendation. He also revealed that when he was Governor of the RBA, the s.11 power "was definitely on people's minds, and that's why you can't dismiss it simply on the grounds that it hasn't been used".

Former Treasurer Peter Costello made it clear that s.11 certainly doesn't compromise the independence of the bank. He noted that the removal of s.11 comes up repeatedly, as it did when he was treasurer, and called the RBA Review panel "an inquiry in search of a recommendation. We go down to the bottom drawer—here's one—let's get rid of Section 11!"



Deputy Committee Chair Andrew Bragg tweeted his verdict. Photo: Screenshot

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Representatives of the RBA Review panel were at first vague about the recommendation's origins, with Australian Public Service Commissioner Gordon de Brouwer saying only that "it came up in discussions". When the questioning continued, ANU Professor Renée Fry-McKibbin answered, "We commissioned papers on this topic, and that was one of the recommendations"; throughout her answer she was looking around nervously and then down at the table. Drawn out, she referred to the sole (invited) "expert" submission which had recommended removal of the government power to override the RBA—written by 20-year US Federal Reserve veteran Andrew Levin, currently an IMF visiting scholar—which proposal the review panel had accepted.

## Preventing 'populist' moves

The review panelists confirmed the need to strengthen RBA independence to embed the future financial control that will include unpopular moves such as deposit bail-in and deep austerity measures.

McKibbin said RBA independence is crucial because "they have to make difficult decisions, they need to be, I guess protected from the short-run political process of populist politics ... the RBA having to make hard decisions is hard sometimes and they need to be protected, as well."

Reflecting recent demands that the government rein in the RBA, De Brouwer added that “There is usually a lot of pressure on the central bank, and conversations around the treasurer using the override power doesn’t help public debate, or accountability, it just increases, sometimes, the political friction.”

The existence of s.11, he said, shifts the focus away from the necessary, hard decisions, making it an issue for every rate decision. “[M]ost decisions of central banks on interest rates are right”, he claimed, “but almost all of them are very hard, and you’ve got a highly contested political environment, and that just makes it harder, actually, for the central bank, and”, he added as an afterthought, “for executive government. ... Putting it always directly into confrontation between executive government and the central bank is not healthy.”

Responding to Senator McKim, De Brouwer continued: “What happens if you have a populist executive, who wants to then, [on] every interest rate decision, override that interest rate decision because it’s not politically convenient? By keeping Section 11 you bring that exercise of populist power into the executive rather than the parliament.” McKim shot back: “Well my response to that would be that they are accountable to the people, in a way that the board of the RBA is not.”

## **Preserving power of elected government**

Senior past officials stressed the need to protect government control over banking. The removal of s.11 “would be a big mistake”, said Macfarlane. After decades of reflection, he said, it is *valuable*—to resolve a “once or twice a century” irreconcilable difference between bank and government.

As important as central bank independence is, said McFarlane, “it’s not God-given. It was delegated to the central banks, *by elected governments*, because they concluded it would lead to better decision-making. But conflicts can arise, usually small ones, but how we would we resolve the situation if there was a really big one, a rare event?” The reason it has never been used, is that it “imposes a very politically demanding process that governments would only be willing to use in the most extreme and rare circumstances.” In a really big conflict it would be very useful, he said, such as in the early 1930s when the head of the central bank refused to facilitate government plans to combat the Depression.

“In short I think s.11 protects central bank independence in that it prevents short-term government meddling and decisions, but it preserves the authority of the elected government in those rare and unforeseen major events.”

And, he told McKim, “At the end of the day the elected government has to have priority. If the issue was big enough I think we have to accept the elected government is more important than the central bank. In some rare or wartime event, government has to have power in a democracy.”

Costello, responding to Senator Andrew Bragg, was similarly blunt: “The only reason you would get rid of s.11 is if you don’t trust the parliament. If you think the parliament might wrongly intervene. Now, it’s a funny thing, I think, for the parliament to say we don’t trust ourselves. ... But it’s such a difficult power to execute ... that it can only be done in extreme circumstances.” Which is why, Costello explained— and as history shows—“it’s not a problem”.

“It’s a question of sovereignty: Does parliament think it should still have powers in this area or not?”

## **Lived experience vs theory**

Nick McKim summed up the hearing thus far: the RBA didn’t ask for s.11 removal; the current RBA governor is agnostic and says the RBA has enough independence already; two former RBA governors not only oppose it but say removing it may compromise RBA independence; and two of our highest-profile former treasurers, Costello and Keating, publicly oppose it.

Other Senators repeated this list of opposition, including Liberal Senator Dean Smith, who asked the Review panel witnesses if they could identify some equally esteemed people that support the removal of s.11. The only example forthcoming, from McKibbin, was the aforementioned expert submitter. “Well, Andy Levin”, said McKibbin, “he’s a professor from the US, he wrote an in-depth paper for us. ... I guess there’s a lot of academic work ... [showing that] the more independent a central bank is the better inflation outcomes are.”

Smith responded: “I suppose for me as a layperson, what I’m seeing is a clear delineation between those with lived experience and those you’ve identified as academic. Can you identify someone with perhaps more practical or lived experience?” McKibbin returned lamely, “So Professor Levin was a member of the US Federal System for a long period of time ...” De Brouwer added that the US Federal Reserve and European Central Bank are “both major central banks that don’t have an override power and that’s specifically to ensure their independence *under difficult and stressful circumstances*.” (Empasis added.)

Discussing the proposal for a separate monetary policy committee, former RBA governor Bernie Fraser said he was worried about “the concentration of monetary policy, monetary theory that’s envisioned in respect of the committee to make the decision on interest rates is very much organised around monetary policy and monetary theory; in other words, we’re getting close to having a committee of

super nerds on monetary theory and monetary policy making decisions on interest rates. And while inflation is very much a monetary phenomenon, the cause of inflation and the consequence of inflation go way beyond monetary policy and monetary theory....” Judgements need to take into account, he said, all the other things that bear on inflation, such as supply problems and productivity.

Costello, who lamented the lack of scrutiny of the “cult of the central banker”, added to the picture: “You’ll always find economists who’ll say parliament should give up its power, *because they’re economists*, they believe they should have the power.” Senator Smith weighed in on the addition of expert external members to the proposed Monetary Policy Committee, suggesting that adding another six professional economists is not a good idea; the RBA is already full of them.

“The review was carried out by three economists”, Macfarlane had previously written in the *AFR*. “As others have observed, it is not surprising they recommend increasing the number of economists in monetary policy decisions. Not only will there be more economists, but more boards, more board papers, more levels of management, more staff and more public pronouncements.”

Officials from the Treasury warned that governments might try to use s.11 to lower rates every time they are raised, but that is not lived experience. Out of the two cases where use of the power was entertained, one (Paul Keating in the late 1980s) was part of a push to raise rates. And the Australian Citizens Party has maintained that the government should have stopped the RBA from lowering rates and creating the housing bubble, which would have saved homeowners from the grinding rate rises today.

### **Supreme irony: What’s the alternative?**

Senators put to the witnesses the question of how differences between the government and bank would be resolved without s.11. For instance, if the governor “goes rogue” with 20 per cent interest rates.

Macfarlane said that “whatever came in its place would be inferior” and would not enhance RBA independence; Fraser said that “In its absence ... [there] would be an *ad hoc* process whereas now it’s determined and clear.” That process could include “the Donald Trump solution”, he warned, of threatening to sack the Fed governor. Costello indicated that the parliament would have to legislate, “so you’d be back to square one, you’d be legislating all over again”.

The Review’s De Brouwer defended the posited 20 per cent interest rate scenario: “There may be occasions where ... in a very bizarre or strange world that may be a proper decision” made by a board taking full account of all the information. Senator Bragg asked him to clarify the resolution process, in the absence of s.11. Displaying the insanity of ditching the current legislation, De Brouwer affirmed that the government could put a bill through the parliament, effectively, as Senator Bragg drew out, replacing what is there today.

Stunningly, when asked the same question, current RBA Governor Michele Bullock said she didn’t know what would happen if the government and RBA reached an impasse over monetary policy. Her sidekick and RBA legal counsel reiterated that ultimately the government could legislate some provision to resolve the dispute. Oh, exactly like s.11, asked Senator McKim, which is already formally established and transparent? Bullock could not disagree.

Likewise, the Treasury witnesses had to concur, saying that in the absence of s.11, “in an extreme case the parliament has the power to step in as appropriate to address the issue.” “And legislate?” asked Bragg—“You’re effectively saying that if there’s a problem they have to re-legislate the same thing?” Treasury responded: “At the moment the power is with the government of the day; the pressure can be extreme with rising interest rates. With shifts to the Act of parliament, the bar will be lifted higher, and independence of the RBA increased.”

All witnesses, including those from the RBA, RBA Review and Treasury—who could only blather about “future-proofing” the central bank’s independence—affirmed the adequacy of the existing independence of the central bank, taking the only real argument for removal of s.11 firmly out of the equation.

*By Elisa Barwick, Australian Alert Service, 28 February 2024*

For more information on this topic, including the ACP submission to the Senate inquiry into the Treasury Laws Amendment (Reserve Bank Reforms) Bill 2023, [click here](#).