

New City Agenda  
“Unelected Power: The Quest for Legitimacy in  
Central Banking & the Regulatory State”

– Sir Paul Tucker  
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**Opening Remarks**

**Lord McFall**  
New City Agenda

**I. Welcome**

Good morning everyone. Welcome to this New City Agenda event. It is great to have an old friend here, Sir Paul Tucker. For many years Paul and I had a dialogue in Portcullis House. This is the first time that we are on the same side of the table. It is great to have you back. There was certainly never an occasion, certainly with the Treasury Committee and the Bank of England, when we did not learn something from Paul. His new book, *Unelected Power*, is very much aimed at the politicians and legislators, so it is appropriate to have him here this morning to give his lecture on it. Paul now spends some of his time in America, in Harvard, and other areas, and he is still very much in demand, so, rather than me give a great introduction to him – you know him very well – let us use the time as much as we can. Paul will give his presentation and then we can encourage as many questions as possible.

**Presentation**

**Sir Paul Tucker**  
Chair, Systematic Risk Council

**I. Background**

John, thank you very much indeed, and to Lord Sharkey, and all of you for giving up your time this morning. I am flattered by that. As you say, it is a book aimed ultimately at legislators in this country, the States, France, Germany and Brussels.

It is quite an experience sitting on this side of the table rather than on the other side. The greatest privilege for me in serving as an unelected official was testifying to the House of Commons and, occasionally, House of Lords Committees. It came as a surprise to me, doing the work for this book, that that view would not be shared by my tribe of central bankers and regulators around the world.

If you ask the President of the Bundesbank – actually, any living former President of the Bundesbank – whether they do, or should, testify on monetary policy to the Bundestag, the answer is, ‘We testify on other things, other people’s affairs, but we do not testify on monetary policy, and nor should we, because it would undermine our independence.’ That is completely contrary to my view, the view of Mervyn King when he was Governor, and, I am absolutely certain, the view of the late Eddie George, who, of course, became a Member of this House before he passed away.

We saw testifying to Parliament as not only necessary in the sense of creating awareness of what we were doing – trying to speak to the public through the public’s representatives – but we also thought that it was completely necessary in terms of underpinning our independence. That is why it is a pleasure to be here, personally and professionally.

## **II. The Purpose of the Book**

Why did this I write this book? Had I not been in the business of needing to get the book sold, the sub-title would not have been *The Quest for Legitimacy in Central Banking and the Regulatory State*, it would have said something like *How Technocracy Should Retreat to preserve our System of Government and its Own Contribution to Welfare*.

Before I left office I had reached the view that the technocracy --- people like me --- were at risk of overstretching and needed to retreat. That view is held by some in the United States and a few in continental Europe, but by very few people amongst the establishment in this country. In a sense, that is why I wrote the book, but the book was also prompted by the greater powers that the Bank of England acquired in 2012 after the earlier crisis.

The Bank of England was completely redesigned, and I regard it as no longer a secret that the core of its new structure and responsibilities really came out of conversations that Matt Hancock, now a Cabinet Minister, and I had been having since the early 2000s, when he was my private secretary at the Bank of England (before he left the Bank to go and work for George Osborne as his chief of staff). We used to go down to the pub or bars and play what, looking back, amounted to Fantasy Bank of England. ‘What would the Bank look like if we could design it?’

When the legislation was actually being prepared to give the Bank more powers, it turned out, however, that some people wanted to give the Bank more powers than we at the Bank thought was sensible. For example, there were influential people close to the then Government who wanted the Bank of England to be the market regulator, which in the end stayed with the Financial Conduct Authority. We – including I – lent against that. A few years later, after I had left, I received a telephone call. I am not going to say who it was from, but it was not from the Governor. They said, ‘Why were you so keen that the Bank should not be the market regulator?’ and I said, ‘Because you would be too powerful.’ It behoves those who are unelected to be careful about the powers that they have.

## **III. Systems of Government**

### **1. Representative Democracy**

In one sense, the book is a contribution to theories of constitutionalism, because the principles of the structure of government in the Western world – stemming from Montesquieu, Madison and John Locke among others – make no place for the administrative state, regulators and central banks at all. This is problematic because the wonder of our system of government – representative

democracy – is that it separates, more cleanly than any other system of government, how we feel about the government of the day and how we feel about the system of government. Anyone who participates in government, whether local, regional or national, federal in the United States and Europe, unelected or elected, knows that eventually things will go horribly wrong in ways that damage the welfare of the people, sometimes for generations. The beauty of our system of government is that you can be completely fed up with the government of the day and vote it out without losing your loyalty or allegiance to the system of government. Well, that is just no longer completely true. The more of our government that is in the hands of unelected people the less it is true that the inevitable failures and mistakes of government can be remedied by a general election. So it matters how unelected power, beyond the judges, fits with our constitutionalist values.

## **2. What Happens In Other Countries?**

Let me say something briefly about other countries before turning to what I think is the solution. Our constitution, of course, is pretty flexible and so the country turned from being dead against delegating to central banks and independent regulators to it becoming a raving fashion from the 1990s onwards.

Germany is almost alone amongst advanced-economy democratic economies in making explicit provision in its constitution for the administrative state and it is absolutely unambiguous that the administrative state shall be under the day-to-day control of Ministers. In consequence, they have a problem that I am not going to discuss at all today, which is that this is not true in fact. It is true in law but, in my experience, not in fact. Germany faces a problem quite different from the problem that the United States, the UK or France faces.

The United States I will not dwell on other than to say this whole area is constantly fought out in the courts and there are people, both on what in the book I call the ‘constitutionalist right’ of politics and the ‘participatory left’, who are deeply averse to just how much power has been given to regulators of various kinds, and indeed to the Fed.

I need to be careful about what I mean by ‘independent agency’ and this will give me an opportunity to say something concrete about the UK. By an independent agency, I mean an agency that is insulated from day-to-day politics – not all politics – of both elected branches of government, both the legislature (or Parliament) and from the executive. The three markers of such an independent agency are that the policymakers have control over their instruments – Ministers cannot order them what to do; they have job security, not necessarily tenure – ie, life tenure like members of the US Supreme Court --- but job security, as the Prime Minister or President cannot get out of bed and sack them because they no longer like them; and they have budgetary autonomy, or at least they do not have to go back to Parliament or Congress to get their budget each year.

On those definitions, all sorts of agencies in the United States that are described as “independent”, such as the Securities and Exchange Commission, are not in fact independent because they have to go back to Congress each year for their money. I am not suggesting that that is a bad thing, but it most certainly makes the SEC sensitive to the shifting currents of Congressional thinking. I mention the SEC because it turns out that the UK’s equivalent body, the Financial Conduct Authority, is independent in the way I have defined. It is more independent than the SEC. In fact, you may not know this but the FCA is more independent, formally, than the Bank of England. That is because, whereas the Bank of England has to go to Treasury and Parliament and agree its budget every five years, which is a pretty crunchy moment, the FCA does not have to do so and nor,

previously, did the FSA have to. For what it is worth, this is a mistake given the principles I shall outline.

### **3. Possible Solutions**

Let me jump to what I think the solutions are. The solutions matter for two reasons. If we, the people, or you, our representatives, delegate power to insulated agencies where something like my criteria are not met, there is a legitimacy or democratic deficit, which is a slow motion ticking time bomb for the reasons I have said. If, on the other hand, you do not delegate to insulated agencies when you could, you are almost certainly sacrificing welfare benefits that people could enjoy through improving the performance of the agency. I think America incurs that quite a lot and Germany may do so a bit.

### **4. Criteria for Delegation**

I am going to run through some criteria from whether to delegate, how to delegate, and under what circumstances it is okay to combine different missions in an independent agency. That will bridge to a couple of points about the central banks.

The first criterion for whether to delegate – and this is going to sound quite innocuous, but I do not think it is – is that people out there, or political parties, should have a broad consensus around the purpose of the delegation. For example, in the United States, such a consensus does not exist in environmental policy. So, there are lots of people in the United States who are currently very angry about the environmental policies of the EPA – the Environmental Protection Agency – and its new leader, Mr Pruitt. But, actually, there are lots of people who are absolutely delighted, and not all of those people are in industry or business.

For whatever reason, there is simply not the consensus that could justify insulating environmental policy away from politicians. And in fact it is not: the EPA is led at the whim of the President. Now, in comparison, if you think about my former professional world, compared to when I was growing up in the 60s and 70s, there is not a constituency out there for high and variable inflation. There was once upon a time. People thought that you would get more growth, higher output, permanently by having a bit more inflation. Even less is there a constituency out there for financial instability: let us have more financial crises; either more frequently or let us make them deeper when we have them. There may be a few hedge fund guys that want that, but nobody in the population seriously wants that.

I name three massive areas of public policy, one of which actually does not lend itself to insulation of politics because there is deep disagreement about the goals. The others, potentially, do, because there is broad-based agreement on the goal.

The second criterion does a huge amount of work in my work, which is on the benefits of credible commitment. Why do we want to delegate to insulated officials at all? It is because, under certain circumstances, unelected officials are going to be better at sticking to a mandate and an objective. This is not because politicians are wicked or anything like that. It is because they run for election and therefore, if they can improve the people's short-term welfare by departing from the formal objective, they will. In fact, subject to staying inside the law, it would be crazy not to, given the need to get re-elected, but that may not be so great in the long run.

Notice, by the way, that I am not resting this on expertise; there is lots of expertise around and it is always flawed. The case for delegation cannot be based on expertise. Credible commitment, I think, really is a good driver for delegating, but the problem is that it runs absolutely through government, so politicians could delegate everything on that basis. Someone famously argued for that in the late 90s, in the States, but of course we would not want to delegate anything that touches big choices on distributional issues, or on values. That is why quantitative easing, credit easing and credit measures from the ECB and the Bank of England have been controversial. They do have distributional effects. To what extent has that reflected distributional choices? Perhaps we could discuss that.

On the ‘how’, I am going to mention two or three precepts. The first is that it is vital that an independent agency is set a clear objective that can be monitored. What this is absolutely against, in terms of an independent agency, is having three or four objectives in statute that are ranked equally and are vague. That is the position of the FCA. To be clear, the FCA, on my account, should not be independent. It is a mistake, and this is not just a theory.

What you see with the FCA now, the FSA in the past and actually with their peers all the way around the world – you do not want to be too incurious about the rest of the world – what typically happens is that a securities regulator, or market regulator, will embark on a particular policy and nobody will say anything. Then something will go wrong and the regulator will be told that they weighed their objectives incorrectly: they should have been putting more weight on investor protection relative to promoting market efficiency; more weight on promoting the City relative to investor protection; or whatever. That is fine, it seems to me, as long as you have an agent that is not completely independent, such as one that has to come back every year for its money and so is obliged to be sensitive to the shifting currents of parliamentary opinion about where they should direct their effort.

The second criterion is that decisions should be taken on the basis of one-person-one-vote and after deliberation. This is not just for what economists would regard as the welfare benefits of delivering better results. It does deliver better results, in my experience, but it is also so as to disperse power. And also because disagreement between minority voters and majority voters reveals what is really at stake in a decision, which helps to inform parliamentary oversight and public debate.

## **IV. Where Power Resides**

### **1. Why Unanimity is Dangerous**

When we were testifying to you, John, at the TSC, I imagine it was somewhat easier for your colleagues and yourself, and afterwards for Andrew Tyrie and co, where there had been a minority vote, because then you could press, ‘How big a difference is this? Where does this difference go?’

If you have wall-to-wall unanimity for years and years and years, it is much harder for the public to see where the debate is. Now, on the criterion of one-person-one-vote almost none of our Ofcom, Ofgem, Ofeverything passes that test because although they have Boards these are more like public company boards. The power really resides with the chief executive or the director general or whatever they are called. When I first said this to a few people, they were a bit affronted, particularly members of the Boards, and would say, ‘No, no, I am really involved in policy.’ I would say, ‘Do you have a confirmation hearing in the Commons?’ ‘No.’ ‘Are your votes published?’ ‘No.’ ‘Do you testify when you disagree with the director general? Do you go into the agency every day?’ ‘No.’ Then I asked a few people and Ministers I still know. I asked one of

them, ‘Who is the policymaker on X?’ They said, ‘So and so’ – I am not going to name anyone. I said, ‘So what about the Chair?’ ‘The Chair is quite useful for overseeing management of the organisation but on policy, no.’ ‘So you are saying only X is responsible for policy then?’ ‘Yes.’ To be insulated from Government, and to put all that insulated power in one person’s hands, is just a mistake if our political values matter.

Actually, the UK is an outlier in this respect. This is not what France or, typically, the United States have done. We seem to have done it because of the fashion for the New Public Management during the 90s. Doctrine was to model all these regulatory agencies on public companies, with a Board and then a chief executive, and so on. We made a mess out of this. That is not how you should design a government agency that can issue, with independence, rules and regulations that are legally binding. It is quite a big deal to issue legally binding regulations; it is to be a law maker, backed by the coercive power of the state. Why put the de facto power in one person’s hands?

## **2. Constrained by Under-Resourcing**

The third precept I will mention is being sufficiently transparent to be properly accountable to Parliament via its Select Committees. There was a Chairman of the House of Commons Agriculture Committee quite a few years ago – well over a decade ago – who said something along the lines of, ‘We just do not have the resources to do all of this properly.’ I cannot evaluate whether or not that is true, but, if it were true, actually, that should be a constraint on the number of truly independent agencies that we are prepared to have.

My sense is, as a citizen, that the quality of the TSC’s oversight of the Bank of England, particularly of monetary policy – not so much, in fact, of its other functions, partly because there are never any minority votes – is better than the oversight of some of the other Committees of some of the other independent agencies. Of course, to some extent, this not only impairs the oversight, it also impairs the de facto independence, because it leaves more room for Ministers to influence policy discreetly behind the scenes.

## **V. Competition Policy**

### **1. Transformation in the US**

Let me say something about anti-trust policy and prudential supervision, and then talk a little bit about central banking and multiple-mission agencies.

In some respects, the most problematic example in my book is not central banking, it is anti-trust policy, competition policy, which is going to become – I will say only one thing about Brexit: after Brexit, this country will realise just how incredibly important the competition authority is. It tends to loom in other countries’ lives much more than it looms here. That is partly because the big competition decisions are being taken in DG Comp, which is clearly part of the Commission.

The most striking thing about anti-trust policy is the transformation it went through in the United States, and then everywhere else, in the 1970s without the change going anywhere near Congress or anybody who had been elected to any office. The two founding competition statutes of the States are the Sherman Act of the Progressive era and the Clayton Act of the New Deal era. The objectives that they set for competition policy are very vague.

## **2. Educating the Judges**

With some sweeping approximation, for the first few decades of competition policy in the States, the dominant doctrines were associated with what was called the Harvard School, which can crudely be approximated as: if a merger or tie-up accounts for more than X percent of a market, then it is per se illegal, and the legal burden of proof is on the parties to demonstrate that it is not.

A bunch of Chicago economists pointed out, from the 60s and 70s onwards, that this was nonsense if you thought in terms of consumer welfare, and instead judgement ought to be based on whether a merger or tie-up would push prices down for consumers and/or push volumes up. This makes room for taking the long run into account as well. The economics won the day. The striking thing about it was that this was an absolutely massive change, and seems over time to have led to a much more concentrated business community in the States, which also has now concentrated political power.

For me, the interesting thing is not whether that was a good or bad idea in terms of public policy, it was that this went nowhere near the Congress or the President. This was decided by the Court, and the way that the policy change came about was that the Chicago guys – and they were all guys, I think – decided that the way to change policy was to educate the judges, so the Economics department effectively merged with the Chicago Law School to teach a generation of judges how to think about this. As a long-term strategy, it prevailed. It is absolutely the guiding policy of our competition policy, and of European competition policy. There is something wrong about that in terms of who is meant to frame high policy. And, of course, it kind of betrayed the origins of competition policy associated with Woodrow Wilson in the States and with the ordo-liberals in Germany, both pre-war and particularly post-war, who thought policy should be about constraining the political power of business, not just about economic welfare. So that is one example.

## **VI. The Need for Greater Transparency**

### **1. Independence of Prudential Supervisors**

Another example, and I am slightly ashamed about this – my shame being reduced only by my having spotted the problem and recanted before the end of my term of office – is the area of prudential supervision, supervising banks and ensuring they are safe and sound. It has been doctrine for 40 years at least that the supervisors should be independent of Government. This is enshrined in international agreements like the Basel Core Principles of Banking Supervision and the equivalent for securities regulators. More important, it is promulgated around the world by the IMF and imposed sometimes as part of their conditionality. So that is the first plank: we, the supervisors, must be independent, so they say.

### **2. Sensitive Issues**

The second plank is that this field or work is all terribly sensitive. The supervisors have maintained something like: we cannot publish anything we do and we cannot tell you anything about the financial health of the banks and the dealers, or about what we are doing with the banks and the dealers, because were we to do so it could bring about the very problem that we are charged with averting. If you think about this for five seconds, in the way that I put it, it is an absolute disgrace. It amounts to my tribe, as it was, saying to your tribe, ‘Trust us. Pass legislation that makes us independent. We cannot possibly tell you what is going on until, of course, it all ends in failure, there is a complete mess and you demand to know what was going on.’

There are two solutions to this. They are not mutually exclusive. One is for Select Committees to hear evidence on these sensitive things (and I accept that some of them are sensitive) in the way that they hear evidence in camera on security and intelligence affairs. That can be done and happens a little bit in Europe as there is, I believe, a committee of the European Parliament that holds hearings on banking in camera.

The other, more important, part is for prudential supervisors to be much more transparent about the state of the banks. If they do not do that, they basically should lose the independence that they insist is so important. I believe that democracy and our system of government is more important than the insulation of bank supervisors, but I also happen to believe that they can solve that problem. Something they now do, called stress testing, which the Americans stumbled into during the crisis, allows them to be much more transparent about firms than ever in the past.

## **VII. Central Banking**

### **1. Monetary Policy**

Let me come, finally, to the core of my old world. I am going to say a few words about central banking. The central bank independence debate has dominated Britain's discussion of delegation for the past 30-odd years or more.

The first sentence of my book recounts Terry Burns, when he was permanent secretary at the Treasury, coming to see Robin Leigh-Pemberton, when he was governor of the Bank of England, and I was sitting there as the governor's private secretary. This must have been the very early 1990s and so during the debate about giving the Bank of England independence for monetary policy. Some of you will remember the Rolls report. That debate was under way. Nigel Lawson suggested independence to Margaret Thatcher. It was a few years before Norman Lamont suggested it to John Major. That was all in the swirl. Terry comes across and says to Robin, 'Of course, if ever you were to gain monetary independence, you would very likely have to lose banking supervision, because otherwise you would be over mighty citizens.' It is a word still used in the core mandarin discussions about the Bank of England, from time to time.

Terry's prediction was absolutely right. When the Bank of England did get monetary independence from the Labour Party in 1997, banking supervision was duly taken away. And then the crisis happened and it was given back. The question is: was it a good idea to give it back? Certainly, the instinct of, 'You will be very powerful if you do both' is dead right. So the instinct of, 'Would it not be good to separate these two missions?' is not an outrageous instinct.

### **2. Lender of Last Resort**

What it does, and what it did, however, is to deny an unalienable fact, which is that, if you are the monetary authority then when banking gets into difficulty with its liquidity, you, the central bank, as the lender of last resort, will be at the scene of a disaster and, as you make your way through the scene of the disaster, it will turn out that you want to know a lot about the banks that want you to lend to them, and some of which you do not want to lend to. It also gives you a stake in how well the banks are being supervised and in how sound they have been required to be. This is exactly what your TSC report on the Run on the Rock was about.

I will say, as an aside, that the key governance failure of the Bank of England, highlighted during that period, has not been fixed. For all of the talk of improvements, from Treasury and in

Parliament, in BoE governance – and I do not doubt there have been some – there is one, I think only one, element of the Bank’s governance that was important to the mess of 2007 and it has not been addressed. This is never discussed in this country. I mention it now simply because it highlights that oversight of independent agencies is perhaps not what it is cracked up to be.

Anyway, my view is that if, by virtue of being lender of last resort, a central bank is inalienably involved in overseeing the resilience of the banking system, then given our political values its role, responsibilities and powers should be formalised, so that it possible to hold it to account.

### **3. The German View**

Years ago, I was sitting next to Helmut Schlesinger, past president of the Bundesbank and by far the dominant president of the Bundesbank over recent decades, who probably still goes there frequently and in some sense is still very much a guiding spirit. It would be very difficult for a President to go against the will of Schlesinger without carrying Bundesbank staff. We have had no central bank governor in this country like him, other than perhaps Montagu Norman.

Anyway, I said to Dr. Schlesinger, ‘Why is it that you are against the Bundesbank being a supervisor?’ and he said, ‘Oh, because it always goes wrong. We do not want to be accountable for that because it would undermine our monetary independence.’ I said, ‘But lots of your staff work on banking supervision, because they have to, because you are the lender of last resort.’ What I did not say, which I believe to be true, is that, actually, most Bundesbank staff work on banking supervision, not on monetary policy. Schlesinger said, ‘Well, even so, we do not have formal responsibility, so are protected from accountability.’ Can you imagine that being true here or in the United States? It is impossible. If you actually do something, then you are accountable for it. You work back from that. Parliament should take the responsibility and structure it in the appropriate way. There has now been an attempt to do that for banking supervision in this country. But I do not think there has been a particular attempt to do that for lender of last resort.

## **VIII. Conclusion**

Let me stop there, other than to say that the reason this matters to me is that I happen to have spent most of my working life in an institution that gained more and more power in a healthy democracy, and it did so during a period when more and more power was also given to unelected regulators of various kinds. As a country we did not seem to stop to debate whether this was a good thing, or how best to do it, very much at all. If you want proof of that, I would mention that there have been lots of constitutional changes in this country over the last 25 years or so, and if you go and buy books by the leading constitutional scholars of this country, the chapter headings will be about devolution, the EU, reform of the House of Lords, human rights, creating a supreme court and moving it out of the House of Lords. The Bank of England, in one book, gets a sentence or so, and nothing is said about the regulatory state. It does not feature at all.

Let me finish with this. In the United States, the marginal lawmaker is an unelected judge or an unelected regulator. Do we want to be like that?

Thank you very much.

## **Response to Presentation**

**Lord McFall**  
**New City Agenda**

### **I. Parliamentary scrutiny**

From my point of view it is welcome that Paul is prompting the debate about the process and resources available for parliamentary scrutiny and accountability. In my present position in the House of Lords, I am leading a review of Committees, the first for 20 years, and have been approached by a couple of peers who actually have chaired these independent agencies. They tell me, ‘When we were chairing these agencies we were not subject to that scrutiny at all.’ You have to have a committee that is looking at regulation and regulators, so there is an issue of accountability there. It is a big deficiency. Certainly, in my time in Parliament, I have seen the leakage of responsibility, the franchising of responsibility from politicians outward. But then when we come to ask the real questions about how to fix things, we cannot, because it is one removed from us, as a result of that. Certainly that comment that you made there, Paul, was very, very relevant to the work that actually we are doing in the House of Lords at the moment on that.

Paul mentioned, in his book, about the Treasury Committee. One MP, who was a Member, said ‘All we can do is ask simple questions and listen to your erudite explanations.’ You will agree with that, at the end of this morning, Paul. The MP said “What good is that sort of accountability to elected politicians?” And then the MP asked for examples of when the Bank had changed policy because of what the politicians had said, and the Governor responded that no such examples could be given because to do so would compromise the Bank of England’s independence, so we are back to square one.

Paul has elaborated on the issue of principles for delegation. You can tell that your book was partly written in America, Paul, because you mentioned the Hamiltonian drive for efficiency, the Madisonian fragmentation of power and the Jeffersonian voice of the people. Now, let us translate that into the UK. Given that you have said that the principles for delegation have to be exposed to national debate, how do we go about that so that we change the situation?

## **Further Recollections**

**Sir Paul Tucker**  
**Chair, Systemic Risk Council**

### **I. Hearings in the House**

Thank you very much, John. It is great that you mentioned George Mudie asking Mervyn and me that question. What we said was, ‘Well, we go back and decide what we think is right, precisely because Parliament has made us independent. What these hearings are for is essentially for you to

decide whether we should carry on being independent.’ Mervyn and I talked about this. We did not feel we should defend the Bank of England’s independence that much; whereas the Fed certainly defends their independence an awful lot. We felt it was a gift that Parliament gave and it was our duty to act in an independent way and provide Parliament with the information that we felt was necessary for you to evaluate whether to sustain it.

So, where do you need the debate about the design and oversight of independent agencies? Fundamentally, you need it centred on this building, in the two Houses, and that means in the Select Committees and, at times, on the floor of the House.

## II. Why France Was Right

Let me give you an example of where it did not happen. A year or so ago there was a report – in fact by an ex-Bank of England person, David Clementi – on the new BBC: what to do with the governance of the BBC. Part of that boiled down to a debate about whether the BBC should self-regulate and, if not, should there be a new independent regulator or should it be regulated by Ofcom. The debate gravitated to Ofcom being the line of least resistance. I am deliberately putting it that way. There was no public debate about whether or not Ofcom was fit for purpose to do this. I do not mean individuals being fit for purpose, I mean the structure of Ofcom, where power is concentrated.

That concern featured in a similar debate in France. France concluded that you certainly should not put the regulation of media content together with the regulation of the economics of the media and telecom, because it would simply make the agency concerned too powerful for comfort in a democracy. So I put this to some people concerned in the BBC debate. First of all they said that it had been debated. I was once a bank clerk, so I asked them to send me all the submissions that had been made on the matter, and it turned out that the point about Ofcom power and design was not debated. Nor was it in David’s report.

I said to people who know about Ofcom, ‘What do you do to split decision taking on these two areas?’ They said, ‘We have a Content sub-committee of the Board.’ I said, ‘Does that have a formal authority [from Parliament] and does it take decisions?’ The answer was, ‘No.’ I thought, ‘Why is it that France can have this debate better than us?’ I do not mean that we should have followed France in what they did because, actually, I think that the statutory structure of Ofcom could have been amended along the lines taken with the Bank of England, where Parliament created three statutory bodies, one for each distinct mission, that are independent of each other.

When banks fail in this country [or monetary policy goes very badly wrong], it should not be the B-of-E executive that is called first to Parliament to explain themselves. It should be the independent (external) members of the PRA, FPC or MPC; otherwise you cannot justify giving that much power to the institution. That is a neat solution to the problem of concentrated institutional power. The same could have been adopted with Ofcom, but, so far as I can tell, it was not debated whatsoever.

The debate about these things --- design, objective and powers --- has to be here, and it is going to be most crunchy when something big is changing. In a sense that means the Select Committees – not only the Treasury Select Committee, which does a great job – but the other Committees with vast responsibilities somehow having the incentives and resources to do oversight well. It is easier for the TSC overseeing monetary policy and the Bank of England, because interest rate decisions are so salient. They affect savings rates and mortgage rates. It is harder to make the oversight of a utility regulator interesting except during rough times.

## **Questions and Answers**

### **Lord McFall**

Are there any questions? If people could identify themselves. Paul has given a speech already, so questions, please.

### **Archie Hamilton, House of Lords**

I have two questions, really. The first is the question of the growing constituency for deficit financing, which seems to be getting rather bi-partisan, which worries me tremendously. Do you have concerns about that?

The second, which is linked, is quantitative easing. You talked about wall-to-wall unanimity. I do not think we have explored very well the effect of quantitative easing on asset prices, which actually leads to a very large gap in wealth terms and people who happen to own houses and shares are infinitely richer than those who do not.

The other question is banks. They still seem to be very large to me. If there was a major financial crisis, they are all too big to fail and the state would be forced to walk in and bail them out. On the other hand, breaking up banks does not seem to be going very well, and Williams and Glynn seems to be a complete disaster. How are we going to get competition for the banks?

### **Alan Brener, University College of London, Queen Mary's**

One of the issues in the book and also from the Chair is that the various Select Committees are largely under-resourced, with one key exception in terms of the Public Accounts Committee, which is the chosen instrument of the National Audit Office. Do you think that the other Select Committees would benefit from having, let us call it, an inspectorate with similar powers, but obviously different remits, as the National Audit Office?

### **Kishwer Falkner, Chair, House of Lords EU Sub-Committee on Financial Affairs**

Sir Paul, you said a couple of things which seemed to value confidence in the American system of accountability versus continental Europe or British systems. You talked about confirmation hearings, but if I understand the American system correctly, if someone does not get through their confirmation hearing they cannot be appointed, whereas here in the UK, we just had a recent example – I do not want to name the Committee – where someone did not get through but the Government nevertheless went ahead and appointed them. Is there a problem with the way that our statutes and rules on confirmation hearings operate, or do you want them strengthened?

The other interesting point is that you did not say anything broadly about levels of accountability that exist in the European supervisory/regulatory institutions. There has been quite a lot of criticism of the level of lack of accountability within most of the European institutions. I wonder whether you care to answer that? Thank you.

## **Sir Paul Tucker**

I am going to go backwards, if I may. On confirmation systems, I rather like our system, although it is not perfect. With Britain's informal system, if you do badly enough, you may well not survive. You gave an example of where someone did survive. I can think of one where someone did not and I can also think of one where they did but, actually, they were slightly damaged, which perhaps created an incentive. I do not think in our parliamentary system I would adopt the US formal confirmation system, but having said that I am concerned that there are lots of positions where there is no confirmation hearing. There is not a confirmation hearing for everyone who goes onto the board of an independent regulator. In what I said earlier, I was simply using that as informal evidence that those office holders do not really have that much power, whereas there is a confirmation hearing for the DG (or the chief executive) because that is where the power lies. My argument was that, at those independent agencies, too much power is in one set of hands.

On Europe, or rather on the EU, there are two things to be said. First of all, a striking difference, which this country will bump into after Brexit, is that a lot of rules and regulations in the regulatory sphere go by the Council and the Parliament. Either can veto so-called level 2 rules, and there is a full debate for level 1 rules. That was not the position in the UK before and perhaps will not be in the future, and it is not the position in the United States either.

That is something that might not get debated as part of the Brexit debate. I am in no position to say whether it should be or not, but it will be something that people will bump into afterwards. There is a complicating factor, and I do not mean a technical one, whereby, because all level 2 rules and so on have to be issued by the Commission, the Commission can have an invisible influence over these independent regulators whereas the Council and the Parliament have to exercise their veto in public. For the aficionados in the room, what this means is that getting to a cleaner, more transparent system in the EU would entail diluting further the Meroni Doctrine, and eventually shifting away from the Commission having to be issuer of rules, but keeping in place the veto of the Council and Parliament, but that will be for them.

To Alan's question, well, I certainly do not think that you need staff support on the scale of the United States, because there are costs to that: if committees have a vast staff, you release Members of the House (perhaps not so much the Senate) to spend much of their time on fund-raising. The percentage of time spent by Members of the House on fund-raising is quite extraordinary, way above 50% I believe. I am not in a position to judge what resources are needed by each committee here in Britain, but you have to be careful for it not to be too big.

In this county one of the great things, when you are testifying, is that the only members of Parliament who read out the question they are asking you are the members who are new. Of course they do; all of us have been new in a job. What is great after that – and it is not always very comfortable – is you do not know what is going to happen if you are testifying, and that is a great strength of our system. That does not come down just to the staff. That comes down to the incentives of the Members of the Committee to take oversight seriously because that can enhance their standing, prestige and leverage in the House.

On the first set of questions, I am going to start with quantitative easing. Quantitative easing was a good thing to do. I do not regret it at all. I think it helped here, on the continent and in the States. It helped to avoid a vortex of a great depression, which is no small thing. I think we were slow [to explain some of the side effects], and it is hard for me to say this but probably in the States, and elsewhere, central banks continued not to make things clear enough. Although QE might work in aggregate, it has costs in terms of fuelling speculation in the financial markets, by holding down the

yield curve, and in that the group of society that probably does least well out of it are middle class savers living off a certain amount of investment income. Of course, they are also politically potent, as they have a very high propensity to vote.

The lesson for central banks is that even when you think something is net good, and what you should do, you should be very open about what you think the costs are. The reasons for that are essentially political with a small 'p'. When the world was depending on QE in the early months of 2009, it seems to me that there was no alternative. The only bodies that could act quickly enough were the central banks. As the years passed, as you got into 2012, 2013 and beyond –

I am really not making a point about the UK here, but think of the United States and Germany, two countries that definitely had fiscal capacity --- this was a world in which it suited politicians to sit on their hands, and not to try and build the constituency for fiscal measures. That is because they knew that if they did sit on their hands, the central banks would have no choice but to reinvent themselves as the US cavalry and continue to do more and more and more. This is pretty deeply problematic and has left the Fed and the ECB deeply unpopular with some parts of the political community – although not with all parts of the community.

On banks, every time anyone in the House – the House of Commons or House of Lords – asks whether the requirements on banks have been softened, they ask a vital but difficult question for any outsider. Softening the requirements is a slippery slope, but it is so techy that it is hard to be sure when it is happening. I chair something called the Systemic Risk Council, which is a transatlantic group. Even for us – Paul Volcker, John-Claude Trichet, Sheila Blair, Adair Turner, and others – it is very hard, John, from outside to see what is really going on and where the authorities might be softening. We [the public] should know more because on both sides of Atlantic there were terrible costs from the last crisis: costs that are still flowing through into politics and culture but now, somehow, are being forgotten in Congress, in parts of the regulatory system in the States, and in parts of continental Europe. I do not know about here in the UK.

On deficit financing – speaking as a former central banker – I do not have anything to say. But I am not a central banker, so speaking as a citizen, I want to underline that this is a long-running issue. The easiest solution for democracies is to buy their way out of trouble by borrowing money. That can be a sensible thing to do sometimes, but it cannot go on for ever. Ultimately, with an ageing society, this is going to be at the centre of the great problems that you face here in parliament. That is why we have Parliament, so you do not have to rely on unelected people like me on the really big issues.

### **Lord McFall**

Good. On the Systemic Risk Council, a number of years ago, I was at a lecture at Harvard and I suggested that we should be looking at a transatlantic body, because we are not going to sort it out here on our own. I said, 'Look, I am here. I am the brawn, so let us get the brains in with the brawn.' We have Paul in his chair and he does a great job. The only hope for the way forward is to have that bridge between ourselves and the States in terms of international regulation. Only the other day, Paul, we sent an email about the latest exchange around the SEC, so it is very, very important. If we are left on our own here, we will never get anywhere. That is the real message.

### **Mike Baliman, London Fintech Podcast**

Thank you, Sir Paul, for a very eloquent exposition of the *quis custodiet*. I have a question which kind of follows on from that if you have been thinking about what they should be doing and how they are reporting it. The question is: how, having seen how the regulators are doing it? Having been in the City long enough, I have seen it go from highbrows through principles to *annuncia*. We have, for example, one and a half million words in MiFID. That is the question.

### **Lisa King**

My name is Lisa King. I have a few questions for you. In your pamphlet, you mention the rule of law. It is very interesting. The rule of law implies that everyone is subject to the law, or are we now living in a dictatorship where the bankers are in fact above the law? Is the Government not under the influence of the large banks? Iceland did, in fact, jail their leading bankers for the financial crisis. We have done nothing here.

On the terms of the FCA being independent, the FCA, in fact, banks with Lloyds Banking Group. Now I know they have to bank with someone. They have a £150 million unsecured overdraft. With that in mind, can the FCA really be classed as truly independent?

When it comes to redress claims the FCA imposes on Lloyds Banking Group, Lloyds Banking Group seem to be able to override anything the FCA says or advises them to do, so I cannot see how the FCA is independent, or is ever going to be, because it is reliant on one of the largest banks within the UK.

### **Simon Gleeson, Clifford Chance**

Supervision without influence is useless. There is no point supervising any agency unless the supervisor can actually call on the agency to change its behaviour. The reason we created independent agencies in the first place was to protect those agencies from political influence. The reason the Bank of England was given independence was because of the politicisation of interest rate setting. What we are talking about here are constitutional arrangements. Constitutional arrangements are not here just to provide good government, but to protect against bad government, and it is foolish to assume that what has happened in America, Spain, Italy, whatever could not happen here. So my concern with what you are saying is that by making independent agencies more open to political scrutiny, are you increasing the risk of politicisation of those agencies' activities?

### **Sir Paul Tucker**

It is a good challenge, Simon. I am going to do them in reverse order this time as well. I think you have to determine what set of risks you want to run. There is a set of risks that arise when politicians decide not to have agencies testify very much, as with the Bundesbank example. That seems to me to be a brittle system, or at least it would be in this country, as when things go badly wrong, people are liable say, 'My God, no-one told us that they were responsible for all of that; that they were our governors. We have had enough of this.' There is that risk, and that is the risk I do not want to run.

Your risk can be navigated, I believe. It goes back to the exchange between George Mudie at the Treasury Committee and Mervyn and, to a lesser extent, myself. We were there to describe what we did, what we thought and how we understood the mandate, not so that we would go out and

change our minds – although I think those hearings can alert you to factors that you have not thought about before, and I think I said that in my answer – but so that Parliament can decide whether it wants to tweak or repeal the regime.

You know, the banking regulatory regime in this country before the crisis was useless, and I believe was known to be useless, yet nobody could quite bring themselves to say it in public. Actually, if only it had been discussed more publicly, something could have been done about it in time. I do not mean sufficient to avoid the crisis. Making the crisis just, say, 10% smaller would have been quite something in the scale of things. So it is a curious form of oversight that I am arguing for in one sense. It is oversight so that Parliament can decide whether to change the law, not whether to give some non-legal instruction. But Parliament determines the law, so that is a perfectly reasonable thing for it to do, would be my answer.

Moving on, you have raised something that was invisible in my presentation. I made a presentation in terms of independence (insulation) from government, but, of course, actually you want regulators to be insulated from the sectors and firms that they regulate as well. I hugely agree with that. The questions are not entirely separable. The solution amounts to pretty much the same thing, which is that if you give a very clear objective that can be monitored from outside, you can see where they have abandoned their objective and tacked to the industry or part of the industry, a political party or some other sectional interest in the country, whereas if the objectives are multiple and vague, you cannot tell. Where you cannot tell what the regulators are doing, I suppose it is better to be captured by politics than to be captured by the private sector. Some people would disagree with that. But if you want enhanced welfare then you can seek to achieve that via credible commitment, requiring insulation from both. Institutions with vague objectives cannot do this, so the proper (decent) space for truly independent agencies is narrower than the course taken in the UK.

And then Juvenal: the infinite regress of who guards the guardians. I think of democracy as breaking the infinite regress. I talk about this at some length in the book. I think democracy basically can deliver 360 degree monitoring when helped by the media and the public. When I talk about Select Committee oversight of the regulators and the Bank of England, or whatever, this is of course only one dimension. Who is overseeing or watching the Select Committees? The Select Committees only have incentives to do a good job if people are watching them. The media are part of the group who are watching them. Something that happens in this country, but does not happen so much in the United States, is if a Select Committee has a really bad day, the media will say so. Because of the nature of the Westminster village, of which the media are a part, that affects the incentives of Members of Select Committees to do a good job.

On principles versus rules, that is not debated very much in my book. For what it is worth – and I have written about this elsewhere – I believe the only way to do conduct regulation effectively is to legislate principles, and to order in the governing legislation that, when they pass rules, both the regulator and the courts should construe those rules in light of the statutory principles. This is associated with a man called John Braithwaite of ANU in Australia. This is different from David Walker-SIB-type – if I go techy for a second – principles, which were not statutory principles laid down by Parliament; and it is different from a world of pure regulatory agency-issued rules with no over-arching principles. At least the approach I favour would have the elected representatives taking responsibility for the big picture, via the statutory principles. Although not discussed in my book, that fits with its basic thrust. The big decisions should lie with the people we elect, and here in the UK with the second chamber, and not with people who are appointed, like my former self.

### **Lord Tunnicliffe, House of Lords**

Since 2010, I have been the number two Labour whip on Treasury matters in the House of Lords, and therefore, regrettably, I have seen every bit of legislation passed about the Bank of England. We tried, in doing that legislation, to understand the Bank of England and we failed. We discovered there was a thing called court and that it created the MPC, FPC, PRA, PRC or whatever it is called.

It was evident that, in those various committees, we created power probably greater than the Chancellor over macro-economic policy and outcomes. That may have been the intent of the Government, and it may have been a good thing. But then we looked at the internal controls, and it seemed to us that the only person who was a consistent member of all four committees was the Governor. In fact, to some extent, we created, accidentally, the sun king. He may be a benign king but he does seem to have all power.

Are you satisfied, or would you like to comment on the internal structure of the Bank of England and how these very powerful institutions can have more internal accountability to ensure that a single individual does not dominate and, at the end of the day, does not lead us into difficult waters?

### **Frances Coppola**

My question concerns degrees of independence. We have, since the crisis, growing calls for economic intervention that require co-ordinated approaches between Treasury and the central bank. Some of them have been done, such as funding for lending, but some go much further than that. For example, there have been calls recently from the IPPR for there to be investment in infrastructure supported by banking buying bonds. My question concerns how close should the relationship between Government and the central bank be, and should there be, as there is in Europe, explicit legislation that limits the ability of the central bank to intervene in fiscal affairs?

### **Lord Wood**

A quick question on your criterion for distribution: you said you did not think there was a case for delegation away from elected politics when there is no distribution issue at stake, but surely the Bank of England engages in massive distribution of decisions all the time. QE has massive distribution consequences, so I do quite not understand how that criteria would apply in reality. I will go the other way a bit. The obvious question: is there not a case for delegating away from elected politics on some issues where there is a market failure of politics, like issues which are cross-generational – the retirement age, for example. Should that not be taken out of politics precisely because politics cannot get to a decision which enables business and individuals to plan properly?

### **Sir Paul Tucker**

The last is the best challenge that can be made against my ‘no distributional choices’ precept, by bringing in inter-generational issues. If you were going to do delegate such matters away from day-to-day politics then, going back to Simon’s point, you would have to do it in a constitutionalist way. This would be a truly first-order reform of our system of government, throughout the democratic world. This is not like making the Bank of England independent for monetary policy; it is a much

bigger deal indeed. So I just want to park that there. That is not complete disagreement, and obviously it matters for environmental policy, for example.

On QE, for what it is worth – and this is contestable – there is a distinction between making big choices on distribution issues and having distributional effects. I thought of QE, for what it is worth – I think in good faith, but I may be wrong; I do not know – as certainly having distributional effects, but not involving distributional choices. It was, ‘What shall we do? We are at the effective zero lower band for interest rates. We need to inject more money so as to bring longer yields down’ etc., etc., etc. The most vanilla way of doing that is by buying long-term government bonds.’ That was done in order to stimulate aggregate demand, but for no other reason. As I see it, that is not a distributional choice but it certainly has distributional effects.

It comes back to the answer I gave to Lord Hamilton earlier. I do not know about this country, but certainly in the States and continental Europe it would have been far better if fiscal policy had come in more powerfully a bit later, reducing the burden on monetary policy, and with the distributional effects being acknowledged and so maybe offset. What I think my own tribe could have done is to be more open about the distributional effects. We started to do so in 2012, when I was still there – I do not know how much of that there has been since. I think there should have been more and more of it throughout the advanced-economy democracies..

This goes to the question about co-ordination. I obviously think that co-ordination can occur without breaking independence, because that is what we did, as I was then, with the Funding for Lending Scheme. Where the limits to that are is the issue. First of all, I do not think that the central bank’s independence should be sustained if you are involved in things where you are no longer pursuing price stability and financial stability but you are actually really pursuing other welfare objectives. To keep the answer short, I would say that people should articulate where those boundaries are.

On Lord Tunnicliffe’s question, I am going to say two things. This is curiously under-debated in this country. The first – there is no secret about this but it is never observed --- is that the greatest oddity in the constitution of the Bank of England is that – and this is not a post-office thought – except where functions are conferred by Parliament on a particular body – the MPC, the FPC, the PRA – all the powers of the Bank of England through its 1694 constitution and other pieces of legislation are vested in the Court. The Court then has a document called – it is on the website – *Matters Reserved to Court*. Everything that is not reserved to Court, which is basically the oversight of the management plan, is delegated to the Governor. That includes the lender of last resort function. I have long thought that a mistake [as alluded to in an earlier answer]. The Treasury know that I wanted to reform that. It is not just our central bank, of course, that needs to fragment power, but it is done quite well in some other countries, so the BofE is an outlier amongst the big central banks on this.

The other thing I would say is that, in terms of internal organisation, I thought it was at its best when I saw a governor work very effectively with a single deputy-governor in the late 80s and early 90s, although that was before independence. The effect was that Robin Leigh-Pemberton had to carry first of all George Blunden and later Eddie George on anything massive concerning the organisation, and vice versa. That meant there were always at least two people who were responsible for the organisation as a whole.

The solution to the issues you are concerned about will not lie with Court. In my time, Court was terrific at making the Bank of England better at those things that the Bank of England has in common with a travel agency or a manufacturer: projects, human resources, IT, the building are

done much better thanks to Court. But I do not think it is the solution to the set of issues you are concerned about (who holds which of the Bank's formal powers). The solution to those set of issues lies with you, here in Parliament, thank God.

## **Closing Remarks**

### **Lord McFall**

Can I thank Paul very much for his speech. It was a fascinating morning and his book is really a warning for all of us. He says very clearly that central banks must work in clear democratic constraints and oversight.

If you take Simon's point: Simon, my experience of the Treasury Committee is, I do not want to be the final judge at a confirmation hearing, but there are there other ways of skinning a cat, you know. There are a number of people who came before the Treasury Committee who did not have a job later on as a result of it, so their legitimacy, and the Treasury's legitimacy, is important, but there have to be constraints on the politicians as well.

The reason I did not want that was I was not in receipt of all the information. I did not understand everything, so you do not take a decision when you do not have that. Politicians have to realise that Paul's point about the culmination of wide-ranging regulatory powers in the wake of the financial crisis is very important. He does make the point that it is seeing the re-emergence of unelected power – in your opinion – that is one of the defining features of modern government. It reminds me of Mervyn King's book – his autobiography – when he said that central bankers are like cyclists who are cycling uphill and the hill is getting steeper; they keep going but some decision has to be made at some point or they hit the wall, and we are going to hit the wall at some point.

What Paul has done has been to articulate that. This is a political issue, and a political problem, and it is aimed right at legislators. You have done a service to us in providing that challenge, Paul, for the legislators. But the legislators – again from my own experience – do not move unless there is civic pressure and civic engagement. That combination this morning of the legislators and the civic audience is really important. Paul, we will have you for part two, to see how you are getting on with it.

It was very, very insightful indeed. We are really grateful to you. Can I also thank everyone for their attendance this morning.

### **Sir Paul Tucker**

Thank you.