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Ref: Comments on Reserve Bank Amendment (Enhanced Independence) Bill 2008

Dear Sir/Madam,

Please find my comments on Reserve Bank Amendment (Enhanced Independence) Bill 2008.  
I have no problem if Senate discloses the following information if it feels necessary.

Sincerely,

Amirul Ahsan  
PhD (Candidate) in Central bank independence and governance  
Dept. Of Accounting and Finance

## **Comments on Reserve Bank Amendment (Enhanced Independence) Bill 2008**

### **Termination of Governor:**

Replacing Treasurer with Governor-General would not make any qualitative difference to central bank independence and governance (CBIG) as the Governor-General is presumed to act as per instruction of the Treasurer (though it appear better in the RBA Act if the Governor-General in charge).

The best option for CBIG is to have no provision<sup>1</sup> of dismissal of Governor. The second best option is to require the parliament<sup>2</sup> to approve it. (Ahsan, Skully and Wickramanayake 2008b). It would not make any difference that who (Governor-General or Treasurer) recommends to the parliament for removal as neither of them makes the final decision. Moreover, if it has been proposed by the Governor-General then it is definitely requested by the Treasurer in the first place. However, I have full support for the proposed amendment regarding Governor's termination as most academics share the view of keeping the termination power with the parliament (Cukierman 1992).

### **Approval by the each House of the Parliament:**

The proposed amendment says –

*“25(6) If a resolution is not passed by each House of the Parliament in accordance with subsection (4) in the same session of the Parliament, the suspension of the office holder identified in the statement terminates on the day after the last day that such a resolution could have been passed.”*

On one hand this will protect the Governor's office as the suspension will automatically terminate failing to pass it in the each House. On the other hand, it may create some unavoidable situation of conflict with Governor's office. The real day of auto termination (suspension) depends on the length of the parliamentary session. In such situation, if the session continues for long then it may create a hostile situation between Governor's office and the Government. It puts the Governor under psychological pressure and fear of elimination will continue until the parliament ends its session. The longer the period, the more the economy would suffer, as central bank may lose its focus on price stability. Moreover, Government's public image and CBIG both would suffer.

If having each Houses of the Parliament passing the resolution in the same session appears to have practical difficulty then this requirement (each House of Parliament) should be removed and approval by the upper House should be considered as enough. CBIG can be ensured not

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<sup>1</sup> Practised in South Korea and Taiwan.

<sup>2</sup> Practised in Indonesia and Japan.

by making termination process difficult or easier, rather by believing in whether the Governor should be terminated by the Government at all.

**Additional comment (not included in the Bill):**

I would like to make an additional comment related to RBA's independence. In my PhD<sup>3</sup> I had developed an index model<sup>4</sup> of CBIG (Ahsan, Skully and Wickramanayake 2006) and examined 36 Asia Pacific countries. I have ranked them and established relationship between CBIG and macroeconomic variables (such as inflation and economic growth).

The ranking based on average CBIG (1991-2005) (in column 2) of Table 3 Australia is in the first position; based on only year 2005's data (in column 3) Australia is in the second position; based on only year 1991's data (in column 4) in forth position; and based CBIG growth (in column 5) in the thirteenth position.

I had number of recommendations for RBA's operation during (1991-2005) but since recent update of RBA's independence status by the current government most of those recommendations have already been covered (Ahsan, Skully and Wickramanayake 2008a) and Australia's ranking has improved (not shown in the table).

In one of the areas RBA still need improvements i.e. "The final word in resolution of conflict". An independent central bank should retain the power to make such decision (see variable number 16 in table 1 and 2). In the current RBA's Act this power is retained by the Governor-General. In the history of last 49 years (1959 – 2008) the government had never exercised this power and RBA's Governor made the final decision, that itself is evidence about no uselessness of having such provision (few countries who abolished this provision include Philippines, China, Japan, Indonesia in table 1; and most of the central Asian countries in table 2). Moreover, it (retaining power by Governor General) reduces RBA's independence in official documents and internationally in the eyes of the academics and scholars. Revising this portion of act would increase RBA's CBIG and would be able to regain its top position.

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<sup>3</sup> Completing PhD by June 2008; Topic: Central bank independence and governance in Asia Pacific.

<sup>4</sup> The model has total 26 variables (see column 1 of Table 2 and 3). These 26 variables together form the CBIG overall index. The subset of these variables also forms six sub-indices (i.e. legal, political, price stability objectives, foreign exchange rate policy; monetary policy and deficit financing; and transparency and accountability).

**Table 1 CBIG (Asia Pacific)**

<b>EAST ASIA</b>	<b>New Zealand</b>		<b>Malaysia</b>		<b>Philippines</b>		<b>Japan</b>		<b>China</b>		<b>South Korea</b>		<b>Taiwan</b>	
CBIG Index Variables	2005	1991	2005	1991	2005	1992	2005	1991	2005	1995	2005	1991	2005	1991
1. Term of office of Governor/CEO	5YR	5YR	5YR	5YR	6YR	6YR	5YR	5YR	NM	NM	4YR	4YR	5YR	5YR
2. Legal power to appoint Governor/CEO	G	G	G	G	G	G	G+P	G	G+P	G+P	G	G	G	G
3. Legal power to dismiss Governor/CEO	G	G	G	G	G	G	P	G	G	G	NP	NP	NP	NP
4. Reappointment of Governor/CEO	YES	YES	YES	YES	YES	YES	YES	YES	NM	NM	YES	YES	YES	YES
5. Regulatory and supervisory power of CB	CB	CB	CB	CB	CB	CB	SRA	SRA	SRA	CB	SRA	CB	CB	CB
6. Turnover of Governor/CEO	1+	1+	1+	1+	1+	1+	1+	1+	1+	1+	1+	1+	1+	1+
7. Members of the management board of CB	NGP	NGP	NGP	NGP	NGP	NGP	NGP	NGP	CM	CM	NGP	NGP	NGP	NGP
8. Governor/CEO holds office in the government	NO	NO	NO	NO	NO	NO	NO	YES+P	NO	NO	NO	NO	NO	NO
9. The major objectives of the central bank	PSTB	PSTB	PSTB+	PSTB+	PSTB+	PSTB+	PSTB+	PSTB+	PSTB+	PSTB+	PSTB	PSTB	PSTB+	PSTB+
10. Inflation targeting	CB	CB	CB	CB	CB	CB	NO	NO	CB	CB	CB	NO	CB	CB
11. Interest rate setting	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB
12. Foreign exchange market intervention	CB	CB	CB	CB	CB	CB	G	G	CB	CB	G+CB	G+CB	CB	CB
13. Foreign exchange market regulations	G	G	G	G	G	G	G	G	G	G	G	G	G	G
14. Foreign exchange borrowing	CB	CB	CB	CB	CB	CB	G	G	G	G	G+CB	G+CB	G	G
15. Responsibility of monetary policy formulation	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB
16. The final word in resolution of conflict	G+CB	G+CB	G+CB	G+CB	CB	CB	CB	G	CB	CB	G	G	CB	CB
17. Provision for lending	NO	NO	YES15-	YES15-	YES15+	YES15+	NO	NL	NO	NO	NL	NL	NO	NO
18. Terms of lending	-	-	SBC	SBC	SBC	SBC	-	G	-	-	CB	CB	-	-
19. Maturity of loans	-	-	1	1	0.5	0.5	-	NM	-	-	NM	NM	-	-
20. Interest rates on loan	-	-	NM	NM	NM	NM	-	NM	-	-	NM	NM	-	-
21. Written objectives	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES
22. Clear priorities in objectives	YES	YES	NO	NO	YES	YES	YES-	NO	YES	YES	YES	YES	YES-	YES-
23. Policy Explanations provided for public	REG	REG	IRG	IRG	REG	REG	REG	REG	NO	NO	REG	REG	REG	REG
24. Publication of minutes of Board meeting	NO	NO	NO	NO	YES	NO	YES	NO	NO	NO	YES	YES	NO	NO
25. Accountability of the Governor/ CEO	P	P	CBB	CBB	G	G	P	G	P	P	P	P	P	P
26. Audit of central bank	EXA	EXA	AG	AG	AG	AG	IA	IA	EXA	EXA	EXA	EXA	IA	IA

**Notes**

-(Minus) = Below, Less than, to, Not Applicable	CM = Cabinet Minister	MR- = Below market rate	SRA = Separate Regulatory Authority
+ (Plus) = Higher, Addition	EXA = External Auditor	NO = Negative	SBC = Specified by bank charter
0.5 = Within 6 months	G= Government	NL = No Limit	SBC- = Some part not covered by CB charter
1+ = More than one year	GE = Government Employees	NM = Not Mentioned	YR = Year
1 = One year	G-CB = CB only advise does not take part	NP = No Provision	YES = Affirmative
AG = Auditor General	INA = International Auditor	P = Parliament	YES- = Yes but not clearly presented
CB = Central Bank	INX= Internal or External Auditor	PSTB = Price stability only major objective	YES+P = Yes can, but with permission
CB- = CB has no say	IA = Internal Audit	PSTB+ = Price stability plus more objectives	YES15- = Up to 15% of government revenue
CBB= Central bank board	IRG = Irregular communication	PSTB- =Price stability not included	YES15+ = Above 15% of government revenue
	MR = Market rate	REG = Regular communication	

Source: Ahsan, Skully, Wickramanayake (2008)

**Table 2 CBIG (Asia Pacific)**

CENTRAL ASIA	Azerbaijan		Kazakhstan		Kyrgyzstan		Tajikistan		Turkmenistan		Uzbekistan	
CBIG Index Variables	2005	1996	2005	1995	2005	1992	2005	1996	2005	1993	2005	1991
1. Term of office of Governor/CEO	5YR	5YR	6YR	6YR	7YR	5YR	NM	NM	7YR	7YR	5YR	5YR
2. Legal power to appoint Governor/CEO	G	G	G+P	G+P	G+P	G	G+P	G+P	G	G	G+P	G+P
3. Legal power to dismiss Governor/CEO	G	G	G	G	G+P	G	G+P	G+P	G	G	G+P	G+P
4. Reappointment of Governor/CEO	NM	NM	NM	NM	YES	YES	NM	NM	YES	YES	NM	NM
5. Regulatory and supervisory power of CB	CB	CB	SRA	CB	CB	CB	CB	CB	CB	CB	CB	CB
6. Turnover of Governor/CEO	1+	1+	1+	1+	1+	1+	1+	1+	1+	1+	1+	1+
7. Members of the management board of CB	NGP	NGP	NGP	NGP	NGP	NGP	NM	NM	NGP	NGP	NGP	NGP
8. Governor/CEO holds office in the government	NO	NO	NO	NO	NO	NO	NO	NO	YES	YES	NO	NO
9. The major objectives of the central bank	PSTB	PSTB+	PSTB+	PSTB+	PSTB	PSTB+	PSTB+	PSTB+	PSTB+	PSTB+	PSTB	PSTB
10. Inflation targeting	CB	CB	CB	NO	CB	CB	CB	CB	YES	YES	CB	CB
11. Interest rate setting	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB
12. Foreign exchange market intervention	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB	CB
13. Foreign exchange market regulations	G	G	CB	CB	G	G	CB	CB	CB	CB	CB	CB
14. Foreign exchange borrowing	G	G	CB	CB	G	G	CB	CB	CB	CB	G	G
15. Responsibility of monetary policy formulation	CB	G+CB	CB	CB	G+CB	G+CB	CB	CB	CB	CB	CB	CB
16. The final word in resolution of conflict	CB	CB	CB	CB	G	G	CB	CB	CB	CB	CB	CB
17. Provision for lending	YES15-	NL	NO	NO	YES15-	YES15-	YES15-	YES15-	YES15-	YES15-	NL	NL
18. Terms of lending	SBC	G	-	-	SBC	SBC	G	G	SBC	SBC	G+CB	G+CB
19. Maturity of loans	0.5	NM	-	-	0.5	0.5	NM	NM	0.5	0.5	G+CB	G+CB
20. Interest rates on loan	NM	NM	-	-	NM	NM	NM	NM	MR	MR	NM	NM
21. Written objectives	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES	YES
22. Clear priorities in objectives	YES	NO	YES	YES	YES	NO	NO	NO	YES-	YES-	YES	YES
23. Policy Explanations provided for public	REG	NO	NO	NO	IRG	NO	IRG	IRG	NO	NO	NO	NO
24. Publication of minutes of Board meeting	NO	NO	NO	NO	NO	NO	NO	NO	NO	NO	NO	NO
25. Accountability of the Governor/ CEO	G	G	G	G	P	G	P	P	G	G	P	P
26. Audit of central bank	INA	INA	EXA	EXA	INA	INA	INA	INA	EXA	EXA	EXA	EXA

**Notes:**

- (Minus) = Below, Less than, to, Not Applicable	CM = Cabinet Minister	MR- = Below market rate	SRA = Separate Regulatory Authority
+ (Plus) = Higher, Addition	EXA = External Auditor	NO = Negative	SBC = Specified by bank charter
0.5 = Within 6 months	G= Government	NL = No Limit	SBC- = Some part not covered by CB charter
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CB = Central Bank	INX= Internal or External Auditor	PSTB = Price stability only major objective	YES+P = Yes can, but with permission
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CBB= Central bank board	IRG = Irregular communication	PSTB- = Price stability not included	YES15+ = Above 15% of government revenue
	MR = Market rate	REG = Regular communication	

Source: Ahsan, Skully, Wickramanayake (2008)

**Table 3 CBIG Ranking**

	(1)	(2)	(3)	(4)	(5)
Country	Data Availability	Average (1991-05)	Year (2005)	Year (1991-92)	Average Growth
Australia	1991-2005	0.8015 (1)	0.8269 (2)	0.7197 (4)	0.0103(13)
Kazakhstan	1995-2005	0.8003 (2)	0.8377 (1)	-	0.0116(12)
New Zealand	1991-2005	0.7942 (3)	0.7942 (4)	0.7942 (1)	0.0000(30)
Afghanistan	2003-2005	0.7496 (4)	0.7496 (6)	-	0.0000(30)
Taiwan	1991-2005	0.7442 (5)	0.7731 (5)	0.7397 (2)	0.0032(24)
Philippines	1992-2005	0.7354 (6)	0.7453 (7)	0.7314 (3)	0.0015(27)
Turkmenistan	1993-2005	0.7074 (7)	0.7244 (9)	-	0.0069(19)
Nepal	2002-2005	0.6972 (8)	0.6972 (11)	-	0.0000(30)
Korea Rep.	1991-2005	0.6852 (9)	0.7244 (9)	0.6356 (7)	0.0097(17)
Malaysia	1991-2005	0.6841 (10)	0.6878 (13)	0.6878 (5)	0.0005(29)
Tajikistan	1996-2005	0.6817 (11)	0.6873 (14)	-	0.0098(16)
Uzbekistan	1995-2005	0.6789 (12)	0.6789 (15)	-	0.0000(30)
Kyrgyzstan	1992-2005	0.6623 (13)	0.7370 (8)	0.5167 (10)	0.0304(8)
Sri Lanka	1991-2005	0.6510 (14)	0.6714 (16)	0.6436 (6)	0.0031(25)
India	1991-2005	0.6333 (15)	0.6378 (19)	0.6044 (8)	0.0042(23)
China	1995-2005	0.6173 (16)	0.6446 (18)	-	0.0055(21)
Fiji	1991-2005	0.5928 (17)	0.5928 (22)	0.5928 (9)	0.0000(30)
Mongolia	1991-2005	0.5865 (18)	0.6325 (21)	0.4500 (13)	0.0268(10)
Cambodia	1992-2005	0.5692 (19)	0.6369 (20)	0.4000 (19)	0.0456(3)
Azerbaijan	1996-2005	0.5637 (20)	0.6894 (12)	-	0.0328(7)
Japan	1991-2005	0.5483 (21)	0.6645 (17)	0.4156 (16)	0.0428(6)
Indonesia	1991-2005	0.5468 (22)	0.8256 (3)	0.3143 (21)	0.1133(1)
PNG	1991-2005	0.5091 (23)	0.7083 (10)	0.4072 (17)	0.0492(2)
Pakistan	1991-2005	0.4947 (24)	0.5169 (24)	0.4892 (12)	0.0056(20)
Vanuatu	1991-2005	0.4892 (25)	0.4929 (26)	0.4929 (11)	0.001(28)
Solomon Island	1991-2005	0.4469 (26)	0.4469 (28)	0.4469 (14)	0.0000(30)
Samoa	1991-2005	0.4381 (27)	0.4381 (29)	0.4381 (15)	0.0000(30)
Macao-SAR	1999-2005	0.4289 (28)	0.4289 (30)	-	0.0000(30)
Tonga	1991-2005	0.4164 (29)	0.4497 (27)	0.3942 (20)	0.0101(15)
Bhutan	1991-2005	0.4014 (30)	0.4100 (31)	0.4008 (18)	0.0016(26)
Thailand	1991-2005	0.4009 (31)	0.5261 (23)	0.3128 (22)	0.0435(5)
Hong Kong-SAR	1993-2005	0.3605 (32)	0.3733 (32)	-	0.0102(14)
Bangladesh	1991-2005	0.3589 (33)	0.4958 (25)	0.3125 (23)	0.0440(4)
Laos PDR	1994-2005	0.2687 (34)	0.2733 (33)	-	0.0232(11)
Maldives	1991-2005	0.2593 (35)	0.2667 (34)	0.2389 (24)	0.0083(18)
Vietnam	1991-2005	0.1476 (36)	0.1742 (35)	0.1186 (25)	0.0297(9)

Source: Ahsan, Skully and Wickramanayake (2008)

## References:

- Ahsan, Amirul, Skully, Michael and Wickramanayake, Jayasinghe. (2006). Determinants of Central Bank Independence and Governance: Problems and Policy Implications. *Journal of Administration and Governance*, 1(1), 47-67.
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