



House of Commons
Treasury Committee

**Appointment of Professor David
Miles to the Monetary Policy
Committee of the Bank of
England: Responses from the
Financial Services Authority,
Professor David Miles, and the
Bank of England to the Tenth
Report from the Committee**

Sixth Special Report of Session 2008–09

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The Treasury Committee

The Treasury Committee is appointed by the House of Commons to examine the expenditure, administration, and policy of HM Treasury, HM Revenue & Customs and associated public bodies.

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Committee staff

The current staff of the Committee are Dr John Benger (Clerk), Sian Woodward (Second Clerk and Clerk of the Sub-Committee), Adam Wales, Jon Young, Jay Sheth and Aliya Saied (Committee Specialists), Phil Jones (Senior Committee Assistant), Caroline McElwee (Committee Assistant), Gabrielle Henderson (Committee Support Assistant) and Laura Humble (Media Officer).

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Sixth Special Report

The Treasury Committee published its Tenth Report of Session 2008–09, Appointment of Professor David Miles to the Monetary Policy Committee of the Bank of England, on 6 July 2009, as House of Commons Paper No. 765. Responses from the Financial Services Authority, Professor David Miles, and the Bank of England, to this Report were received on 7 and 8 July 2009 and are published as appendices to this Special Report.

Appendix 1: Response from the Financial Services Authority

Letter from Lord Turner to John McFall, Chairman of the Committee

In the Treasury Committee's Press Notice of 2 July on the appointment of David Miles as an external member of the Monetary Policy Committee (MPC) of the Bank of England, the Committee recommended that the Bank of England and the FSA should 'consider the potential conflicts and benefits which might arise from cross-membership beyond Deputy Governor level and report back to the Treasury Committee'. This note responds to that request. It sets out the formal position relating to cross directorships and conflicts of interest, and then considers whether there is a potential for conflicts and also for benefits in this particular case. My strong conclusion is that there are no potential conflicts and some potential spin off benefits.

THE FORMAL POSITION

The Committee notes in its press release that there is an existing formal statutory link between the FSA and the Bank of England at Deputy Governor level, in relation to the two institutions' work on financial stability. In November 1997, the Treasury, the Bank of England and the FSA entered into a Memorandum of Understanding which created a framework for co-operation between the parties on Financial Stability. As part of that document, provision was made for the Deputy Governor (Financial Stability) to be a member of the FSA Board and for the Chairman of the FSA to sit on the Court of the Bank of England. The arrangement has been in operation since that time.

The situation in relation to the appointment of Professor David Miles to the MPC is quite separate from the FSA/Bank of England arrangement for cross-directorships. Professor Miles was appointed by the Treasury as a non-executive director of the FSA on 1 April 2004. He is currently in his second three year term as a Board member. That term ends on 31 March 2010, when he will step down from the Board. Neither his appointment as an external member of the MPC nor as a non-executive director of the FSA is linked to or associated with the arrangements between the Bank of England and the FSA dealt with in the Memorandum of Understanding referred to above.

When approached about the MPC position, Professor Miles discussed with me the implications and any potential conflict, and I conferred with the FSA's Company Secretary, Iain Brown. Our conclusion was that the two positions were entirely compatible and indeed raised far less potential for conflict than arises in respect to members of the Board who are executives of financial services firms. For all directors any conflicts of interest are covered by a Code of Conduct which they sign on being appointed. When considering whether a particular matter for discussion or decision at the FSA Board could create a conflict for that individual, the Board, on the advice of the Company Secretary, considers whether, taking into account any other relevant position held by a non-executive director, the director can properly take part in the relevant discussion or decision. If the Board concluded that such a conflict existed, the director concerned would play no part in that discussion or decision. Professor Miles' position as a non-executive director has been managed in such a way while he has, until now, been an employee of Morgan Stanley and will continue to be managed in this way for the remainder of his term as director.

ACTUAL POTENTIAL FOR CONFLICT IN THIS CASE

The actual potential for conflict in the case of Professor Miles is however extremely low. Indeed I find it almost impossible to envisage a situation where a serious conflict could arise. Where a member the Board is an employee of a financial services company it is possible, and does occasionally occur, that conflict can arise because FSA policies could have consequences for the economic prospects of that firm: the procedures for managing conflicts referred to above then come into play. No such conflict could arise as a result of Professor Miles's role on the MPC. Nor can I imagine any circumstances in which Professor Miles's decision-making on the MPC would be influenced by conflicting interests arising from his membership of the FSA Board. There is no conflict of private interest versus public interest created by such a cross-membership: and there is no conflict between the MPC's responsibility to ensure sound monetary policy in pursuit of the inflation target and the FSA's responsibility to foster financial stability, the soundness of firms, and consumer protection.

Conversely it is essential that the FSA's Board includes, among a range of relevant skills, a strong capability in economic theory and understanding of economic trends: for this reason, as Professor Miles leaves the board next March, we will be seeking to ensure that someone from a similar background is appointed. It is also essential that the FSA monitors overall macroeconomic trends carefully and identifies their potential implications for emerging financial stability risks: indeed the failure to identify the importance of macro trends (e.g. rapid increases in economy wide credit in the period before the crisis) has been rightly identified as one of the key deficiencies of our past regulatory approach. This implies the need for close working relationships between the FSA and the Bank. These can be achieved in a number of ways and it is very unlikely that cross-membership between the MPC (a policy committee) and the FSA Board (a governance body) would ever be seen as a required element in effective arrangements. But there is certainly no downside to such cross-membership and there could be spin off benefits.

7 July 2009

Appendix 2: Response from Professor David Miles

Letter from Professor David Miles to John McFall, Chairman of the Committee

The Treasury Committee raised the issue of the balance between potential conflicts of interest and benefits in a member of the Monetary Policy Committee (MPC) also being a Non-Executive Director of the Financial Services Authority (FSA). I considered that issue before accepting the position on the MPC, having some months of my term as a Non-Executive Director on the board of the FSA still to run. I concluded that there were no conflicts from serving out my remaining months as a non-executive Director at the FSA. This was a view with which the Governor of the Bank of England and the Chairman of the FSA agreed, and it is a view they still take. Given that my appointment to the MPC was made by The Treasury, I have also spoken to the permanent secretary there. He confirmed that they also saw no conflicts.

I remain clear that there are very unlikely to be conflicts in my role on the MPC and as a Non-Executive at the FSA. In addition I believe that close co-operation and collaboration between the Bank and the FSA is essential.

I do not therefore believe that the Committee has grounds for concern that a conflict exists. The expression of concern by the Committee has, however, produced some press commentary which could lead people to believe that conflicts were possible and thus lead to questioning of my independence. I have only a few months of my term as a non-executive at the FSA to run. To remove completely any doubts that some might have over my facing any possible conflicts, I believe it is now better that I should not serve out those months. I informed the Chairman of the FSA of this today. I plan to step down from the Board after the July meeting.

8 July 2009

Appendix 3: Response from the Bank of England

Letter from the Governor of the Bank of England to John McFall, Chairman of the Committee

At its hearing last week, the Treasury Committee asked for a response to concerns raised by some members that the presence of Professor David Miles on both the Monetary Policy Committee and the FSA Board might constitute a conflict of interest.

You will recall that, in testimony to your Committee—most recently on 29 April this year—I myself have raised concerns about the potential conflicts caused by the cross membership of the two boards at executive level, which involves the Chairman of FSA sitting on the Court of the Bank and the Deputy Governor of the Bank sitting on the FSA Board. The Committee as a whole has taken a different view however—for instance in its report on Banking Reform last September. If conflicts are not thought to arise at an executive level, they surely do not arise at a non-executive level. Professor Miles is neither a member of the executive of the Bank of England nor of the executive of the FSA. His presence on both boards is as an independent external member. As such he was appointed to provide outside expertise and advice to the regulatory decisions of FSA and the monetary policy decisions of the Bank. I believe he is very well qualified to do both.

In the end, however, this must be a personal decision for Professor Miles. I understand that he has written to you to say that, in view of the concerns expressed by some members of the Treasury Committee, and to put to rest any perceptions - however misguided - about his personal position, he has decided to bring forward the date on which he stands down from the FSA Board from next spring to now. I respect his reasons for making this decision, and want to offer him my wholehearted support in the period ahead.

I hope this answers the Committee's concerns. Please feel free to call me if you would like to discuss this matter further.

8 July 2009