

**The pursuit of financial stability post the Global Financial Crisis: Is Twin Peaks the
cure for South Africa?**

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TABLE OF CONTENTS

ABSTRACT	6
CHAPTER ONE: BACKGROUND TO THE STUDY	7
1. Introduction	7
1.1. Institutional Structure.....	8
1.2. The Institutional Approach.....	10
1.3. The Functional approach.....	11
1.4. The Integrated or Unified approach (mega regulator)	12
1.5. The Twin Peaks approach.....	13
1.6. Lessons from the 2008 Global Financial Crisis	15
1.7. Research statement and objectives	15
1.8. Methodology and structure.....	16
CHAPTER TWO: TWIN PEAKS IN SOUTH AFRICA.....	16
2. Introduction	17
2.1. South Africa's move towards Twin Peaks.....	17
2.2. Enactment of the Financial Sector Regulation Act (FSR Act).....	19
2.3. Role of the SARB.....	21
2.4. Special Features of the FSR Act	25
2.4.1. Establishment of the Prudential Authority.....	25
2.4.2. Establishment of the Financial Sector Conduct Authority	26
2.4.3. Co-operation and collaboration between regulators	28
2.4.4. Establishment of various structures to assist in achieving the objectives of the FSR Act: Financial Stability Oversight Committee (FSOC).....	29
2.5. Financial Sector Contingency Forum.....	29
2.6. Financial System Council of Regulators	30
2.7. Financial Sector Inter Ministerial Council.....	31
2.8. Ombud Council.....	31
2.9. Financial Services Tribunal.....	32
CHAPTER THREE: TWIN PEAKS IN THE NETHERLANDS	33
3. Introduction	33
3.1. The move to a Twin Peaks model in the Netherlands	34
3.2. The Netherlands' Twin Peaks model during the GFC	36
3.3. The Netherlands' Twin Peaks model post the GFC.....	38
3.4. Role of the Dutch Central Bank (DBN)	40
CHAPTER 4: CONCLUSION AND RECOMMENDATIONS	43
4. Introduction	43

4.1. Key differences and similarities between the Netherlands' and South African Twin Peaks model of financial regulation	45
4.1.1. Enabling legislation.....	45
4.1.2. Differences between the two Twin Peaks models	46
4.1.3. Similarities between the two Twin Peaks.....	47
4.2. Lessons learnt from the experience with Twin Peaks in the Netherlands.....	48
4.3. Final remarks	49
4.4. Recommendations.....	50
BIBLIOGRAPHY	51

The pursuit of financial stability post the Global Financial Crisis: Is Twin Peaks the cure for South Africa?

ABSTRACT

The South African Reserve Bank (SARB) derives its mandate from the South Africa Reserve Bank Act, 90 of 1989. This mandate is confirmed in section 224(1) of the Constitution of the Republic of South Africa, 1996 which provides that the objective of the SARB is to “protect the value of the currency in the interest of balanced and sustainable economic growth in the Republic”.

The SARB as the central bank of South Africa has various powers and functions in terms of section 10 of the South African Reserve Bank Act and its mandate for maintaining financial stability has historically been implied as a consequence of such powers. Financial stability has however not until very recently been captured in legislation as one of the explicit responsibilities of the SARB. However, recognising that achieving financial stability is the ultimate pursuit for economic growth, South Africa started a formal review of its financial regulatory system in 2007, and this review process which is detailed in the Treasury policy documents “A safer financial sector to serve South Africa better (2011) and “Implementing a Twin Peaks model of financial regulation in South Africa (2013)) eventually culminated in the enactment of Twin Peaks model of regulation in 2017.

In terms of the Twin Peaks model the prudential regulation of financial institutions and the regulation of market conduct are separated in order to put equal focus on both functions. Notably, the Financial Sector Regulation Act, 9 of 2017 (FSR Act) as a framework act for the South African Twin Peaks model also strengthened the mandate of the SARB by entrusting it with the responsibility of ensuring financial stability and generally the macro prudential oversight over financial institutions.

CHAPTER ONE: BACKGROUND TO THE STUDY

1. Introduction

In recent years, and especially since the Global Financial Crisis (GFC), many countries have been reviewing their institutional structures and approach to financial regulation on the basis that they may have become ineffective and inappropriate.¹

As pointed out by the Group of Thirty financial regulation is aimed at achieving certain policy goals namely:²

- safety and soundness of financial institutions;
- mitigation of systemic risk;
- fairness and efficiency of markets; and
- protection of customers and investors.

Several developments in the financial markets such as technology, various offerings in financial products, and growth in the globalisation of the financial services sector have however highlighted shortcomings of existing financial regulatory models.³ In the midst of the 2008 Global Financial Crisis (GFC), regulators, supervisors, policymakers and the public seriously questioned whether financial supervision of institutions was effective and whether changes needed to be made to existing models of financial regulation.⁴

According to the Group of Thirty Report, it was not a new phenomenon for countries to reconsider their financial supervisory models because financial market turmoil often results in regulatory reforms.⁵ Llewellyn argues that a financial system that is efficient has a significant bearing on a country's economic development and

¹ David T Llewellyn, "Institutional structure of financial regulation and supervision: the basic issues" (2006) a paper presented at the World Bank seminar titled "Aligning supervisory structures with country needs" 2. (hereinafter, Llewellyn 2006).

² Group of Thirty, "Structure of financial supervision: Approaches and challenges in a global market place" (2008) 21, available at www.group30.org/images/uploads/publications, accessed on 8 March 2019. (hereinafter, Group of Thirty).

³ Group of Thirty 18.

⁴ Group of Thirty 18.

⁵ Group of Thirty 18.

promotes consumer confidence in the integrity of the financial system.⁶ Consequently, when a regulatory regime is well structured, the financial system will very likely be efficient and stable.⁷ One of the recommendations by Group of Thirty in response to the GFC was for “countries to re-evaluate their regulatory structures with a view to eliminating unnecessary overlaps and gaps in coverage and complexity, removing the potential for regulatory arbitrage and improving regulatory coordination.”⁸

As argued by Llewellyn the institutional structure of financial regulation is pivotally important in ensuring that a country’s financial system is stable. What seems to be a key issue is whether supervision and regulation of different types of businesses should be integrated, or whether responsibility for financial regulation and supervision should be vested in a single agency.⁹

1.1. Institutional Structure

According to Llewellyn, institutional structure refers to how agencies that are responsible for financial regulation and supervision are structured, including the role of the central bank. Institutional structure is of importance as it establishes the framework within which a regulatory regime can be optimised,¹⁰ and may have a significant overall impact on the effectiveness of regulation and supervision.¹¹

There are four approaches to financial regulation and supervision that are applied in financial systems; namely¹²

- The Institutional approach;
- The Functional approach;
- The Integrated or unified approach; and

⁶ Llewellyn, 2006 5.

⁷ Llewellyn, 2006 5.

⁸ Group of Thirty 18.

⁹ Llewellyn, 2006 4.

¹⁰ Llewellyn, 2006 42.

¹¹ Llewellyn, 2006 12.

¹² Group of Thirty 12.

- The Twin Peaks approach.

These approaches will be discussed in more detail below.

It should however be pointed out that there is no universal ideal model of financial regulation that countries agree upon as there are advantages and disadvantages to each model. Llewellyn also remarks that there is no single correct answer as to what is the optimal structure or model for organizing financial regulation and supervision, since this depends on specific needs and preferences of each country.¹³

Nevertheless, various countries appear to be in agreement on key points namely,¹⁴

- a) the need to substantially simplify and consolidate overly complex structures;
- b) the emphasis on clarifying and stressing guiding principles of regulation rather than a rules-based approach to regulation;
- c) the importance for much greater levels of international cooperation and coordination on such matters as accounting standards, listing standards, licenses to operate as regulated firms, supervisory oversight mechanisms and, most important, prudential capital and liquidity standards;
- d) the importance of regulatory arrangements having the flexibility to adapt to new types of institutions, instruments, and markets; and
- e) the need to ensure the political and market independence of national regulatory authorities. Finally, there is a growing appreciation of the importance of ensuring that central bank responsibility for promoting financial stability is supported by adequate authority and capacity.

Notably the debate about institutional structure is not about which of these activities are to be conducted, but about which agencies are to be responsible for which functions.¹⁵

¹³Llewellyn, 2006 7.

¹⁴ Group of Thirty 35.

¹⁵ Group of Thirty 24.

1.2. The Institutional Approach

The Institutional approach is a legal entity driven approach whereby the legal status of an entity determines which regulator will oversee its activity in terms of safety and soundness and from a business conduct perspective.¹⁶ The legal status of an entity also determines the kind of business activities the entity can conduct, although the Group of Thirty points out that regulators tend to expand the scope of an entities' business activities under their jurisdiction such that over time one finds that entities with different legal statuses have been permitted to engage in similar activities, but subject to different requirements by different regulators leading to a problem of regulatory arbitrage.¹⁷

According to Llewellyn, there is a fine distinction between the institutional and functional approaches because institution and function are synonymous, although he quickly points out that this may be less true when there are financial conglomerates and firms diversify and tread into each other's territory.¹⁸ Since regulators expand the scope of business activity permissible in a regulated entity, the institutional approach has the drawback that there is a likelihood of overlap with another supervisor's regulatory space and functions.¹⁹ Consequently, there may be inconsistencies in the application of rules and regulations by different regulators.²⁰ The Group of Thirty is particularly of the view that this approach is based on a business model that may no longer exist given financial conglomeration and diversification.²¹

Countries such as China, Mexico and Hong Kong have adopted the Institutional approach. Whilst many jurisdictions moved towards models such as Twin Peaks and Integrated approach, China moved to an institutional approach whereby separate agencies supervise the banking, securities and insurance sectors.²² The challenge with this approach is however that there tends to be duplication where

¹⁶ Group of Thirty 24.

¹⁷Group of Thirty 24.

¹⁸ Llewellyn, 2006 3.

¹⁹ Group of Thirty 34.

²⁰ Group of Thirty 34.

²¹ Group of Thirty 34.

²² Group of Thirty 25.

products and services offered by banks, securities and insurance companies are similar in nature and yet the regulation and supervision lies in different agencies. Accordingly it appears to be an outdated regulatory model.²³

1.3. The Functional Approach

The functional approach to financial regulation is about how an entity conducts its various businesses and how it behaves towards its customers.²⁴ With this approach, supervisory oversight is determined by the business transacted by the entity regardless of its legal status and therefore each business may be regulated according to its function. This means that one entity may have multiple regulators and this may attract compliance costs for entities.²⁵

One of the key benefits of the functional approach is that regulatory arbitrage is avoided since one single regulator is consistent in the application of rules pertaining to an activity irrespective of the entity in which it is conducted.²⁶ For this approach to function optimally, there needs to be sharing of information and co-ordination between regulators, otherwise a regulator may have insufficient information on all the activities of any particular entity to appropriately monitor systemic risk.²⁷ The challenge with the functional approach however is that with various activities, there may be confusion about the jurisdictional remit of each regulator.²⁸

Some of the countries that have adopted a functional approach are Italy and France. In Italy, financial regulation is traditionally organised along functional lines and each industry namely; banking, insurance, investment services and asset management has its own supervisor, legal framework and rules. However, financial oversight incorporates some elements of the Twin Peaks approach.²⁹ In recent

²³ Group of Thirty 34.

²⁴ Llewellyn 2006, 17.

²⁵ Group of Thirty 13.

²⁶ Group of Thirty 5.

²⁷ Group of Thirty 35.

²⁸ Group of Thirty 35.

²⁹ Pietro Vozzella, Giampaolo Gabbi, Massimo Matthias "Financial Regulation in Italy" (2014) *Journal of Economic Literature*: Working Paper Series No. 60, 6 available at www.fessud.eu accessed on 15 March 2019.

years there have however been some debates regarding the need for structural reforms in Italy with proposals aimed at reducing the number of supervisory authorities in order to design a more efficient regulatory model.³⁰

1.4. The Integrated or Unified Approach (mega regulator)

In the Integrated approach all prudential and conduct of business regulation in respect of all the sectors of financial services are vested in a single institution.³¹ This approach works efficiently in smaller markets and is particularly advantageous in a small market as there is less confusion or conflict on jurisdictional turfs that is often a problem in the Institutional or Functional models.³² It works optimally with regards to financial conglomerates because an integrated agency is able to have a holistic picture of the regulated entities' business and risks, thereby enabling the agency to intensify its supervision.³³ Arguments in favour of a single regulator are that efficiencies will be achieved due to shared resources, less inconsistencies, duplication and overlaps, and it is easy to deploy staff within a unified agency.³⁴

However, this approach is not without challenges. The Group of Thirty points out that a single agency poses the risk of a single point of failure because if the agency fails to spot the risk, there is no other agency that can fill the gap and thereby perform checks and balances.³⁵

The proponents of this model or approach are however of the view that a unified agency has greater authority and credibility within the financial system and further that there is clear accountability since the agency has the authority to regulate and supervise a full spectrum of institutions in the financial sector.³⁶ Taylor and Fleming contend that one of the disadvantages of a single agency is that it may be subject

³⁰ Group of Thirty 27.

³¹ Llewellyn 2006 15.

³² Group of Thirty 14.

³³ Llewellyn 2006 18.

³⁴ Llewellyn 2006 19.

³⁵ Group of Thirty 36.

³⁶ Llewellyn 2006 25.

to a hazard of “Christmas tree” effect, with several functions loaded onto one regulator and thus overburdening it with activities.³⁷

The United Kingdom (UK), Germany and Canada are some of the countries that have followed this approach. In 1997 there was a major reform in the financial services regulation in the UK which culminated in the establishment of a unified regulator, the Financial Services Authority (FSA).³⁸ The FSA was responsible for the prudential regulation and supervision of banks, securities and insurance, and the conduct of business activities. However, this model did not appear to be the optimal regulatory model for the UK because after the 2008 GFC, the UK dissolved the FSA and moved towards a Twin Peaks model of regulation which saw the creation of the UK Prudential Authority and the UK Financial Conduct Authority.³⁹

1.5. The Twin Peaks approach

The Twin Peaks approach that was conceptualised by Michael Taylor is an approach in terms of which regulation is structured around two agencies whereby one is responsible for the safety and soundness of all financial institutions and the other for regulating their conduct of business.⁴⁰ The objective of this approach pertains to three key goals namely; prudential supervision, market stability and business conduct. This approach ensures that each regulator focuses entirely on its particular mandate.⁴¹

According to the Group of Thirty, if the two functions or mandates that are split between the twin peaks are located within a single agency, a conflict of necessity arises between safety and soundness of financial institutions and issues relating to consumer protection. In such instance the likelihood of safety and soundness taking

³⁷ Michael Taylor and Alex Fleming Alex “ Integrated Financial Supervision: Lessons from Northern European Experience” Policy Research Working Paper No 2223 September 1999 World Bank Washington , available at <https://elibrary.worldbank.org/documents> 12 (accessed on 4 May 2019).

³⁸ Group of Thirty 28.

³⁹ Andrew Schmulow: “The four methods to financial system regulation : an international comparative survey” (2015) 26 *Journal of Banking and Finance Law and Practice* 164.(hereinafter Schmulow).

⁴⁰ Michael Taylor: “The road from Twin Peaks-and the way back”, (2009) *Connecticut Insurance Law Journal* 1(hereinafter The road from Twin Peaks).

⁴¹ Group of Thirty 38.

precedence is high since it is associated with financial stability.⁴² Therefore Twin Peaks provides a solution to such possible conflict. Notably one of the main issues in the Twin Peaks context is however whether or not the central bank should be responsible for prudential regulation and supervision.⁴³

Countries such as Australia and the Netherlands have adopted different Twin Peaks models. For example; in Australia, where the Twin Peaks model was pioneered in 1998, the prudential peak called the Australian Prudential Authority (APRA) is located outside the central bank, whilst in the Netherlands, that adopted a Twin Peaks model shortly before the GFC, it is located within the central bank.⁴⁴

As pointed out by Llewelyn there are various advantages to the Twin Peaks approach namely;⁴⁵

- Each agency has clear objectives, mandates and accountability;
- Each agency exists in its own right without fear that one will dominate the other;
- Power is spread between the two agencies without being concentrated in one agency as is the case with a unified model or approach; and
- Reputation and contamination risks are minimised.

Some disadvantages or weaknesses in the Twin Peaks approach have also been identified. The Bank of England has opposed Twin Peaks on the basis that proposals to adopt it were an attempt to divest it of its regulatory responsibilities.⁴⁶ There is also scepticism from the Group of Thirty that despite the separation of the two objectives between the two regulators, tension between them might still remain particularly when prudential supervision and systemic stability are perceived to override consumer protection issues in institutional failures.⁴⁷

⁴² Group of Thirty 14.

⁴³ Llewellyn 2006 27

⁴⁴ Llewellyn 2006 27.

⁴⁵ Llewellyn 2006 27

⁴⁶ Llewellyn 2006 23.

⁴⁷ Group of Thirty 38.

1.6. Lessons from the 2008 Global Financial Crisis

The Global Financial Crisis (GFC) that had its epicentre in the toxic sub-prime mortgage market in the US erupted in full force in 2008 and revealed some very important lessons for financial regulation, one of which was the importance of a good regulatory model and an effective and efficient institutional framework. It also revealed the need for a holistic macro-prudential approach to financial regulation; the need for prudential and business conduct regulation to operate in tandem; the failure of “light touch” regulation at global level; the need for global cooperation to prevent macroeconomic imbalances and the need for swift regulatory action.⁴⁸ Post the GFC financial regulation thus took a very focused trajectory, concentrating extensively on the maintenance of financial stability. In the new regulatory landscape, it has become a quest to find the optimal regulatory model that would promote and maintain financial stability.⁴⁹

1.7. Research statement and objectives

South Africa has recently, after a long reform odyssey, transitioned to a Twin Peaks model of financial regulation, as set out in more detail in Chapter Two. Prior to the introduction of Twin Peaks in South Africa, National Treasury found that strengthening the regulation of financial sector was necessary inter alia because of the existence of market failures in the provision of financial services.⁵⁰ It was therefore necessary for government to introduce policy objectives that sought to achieve soundness and stability of the financial system, financial inclusion, access to financial services and fair and equitable treatment of customers.⁵¹

It is consequently crucial to ascertain whether the transition to a Twin Peaks model of financial regulation will likely achieve these objectives particularly, the promotion and maintenance of financial stability.

⁴⁸ National Treasury Policy Document: “a safer financial sector to serve South Africa better” (2011) 24 available at www.treasury.gov.za accessed on 15 February 2019 (hereinafter “a safer financial sector to serve South Africa better”).

⁴⁹ Corlia Van Heerden and Getruida Van Niekerk: “Twin Peaks, the role of the South African central bank in promoting and maintaining financial stability” (2017) 80 *THRHR*, 638.

⁵⁰ A safer financial sector to serve South Africa better 24.

⁵¹ National Treasury Policy Document: “Implementing a twin peaks model of financial regulation in South Africa” (2013), available at www.treasury.gov.za accessed on 15 February 2019, 31 (hereinafter “Implementing a twin peaks model of financial regulation”).

This research dissertation accordingly seeks to interrogate the following research questions:

- a) How does the Twin Peaks model of financial regulation compare with other models of financial regulation?
- b) What is the main institutional structure of the Twin Peaks model that was introduced by the FSR Act?
- c) How does the South African Twin Peaks model compare with the Twin Peaks model in the Netherlands, specifically in relation to its ability to promote and maintain financial stability given the institutional framework created by the model?

1.8. Methodology and structure

This research is desktop-based and critically examines various articles, journals, policy papers and legislation.

The dissertation comprises of four chapters and is structured as follows:

Chapter One is the roadmap to study, and provides background to the study by juxtaposing the various models of financial regulation and sets out the research statement and research objectives, the research methodology and the lay-out of the Chapters. Chapter Two provides an overview of South Africa's move to Twin Peaks, and the institutional framework of the South African Twin Peaks model as introduced by the FSR Act. Chapter Three comprises of a comparison between South Africa's Twin Peaks model of regulation and that of the Netherlands, focusing on the role of the Central Bank in the Netherlands and how Twin Peaks was implemented in the Netherlands. Chapter Four is the final chapter and comprises of the study's conclusion and recommendations.

CHAPTER TWO: TWIN PEAKS IN SOUTH AFRICA

2. Introduction

2.1. South Africa's move towards Twin Peaks

In the past South Africa's financial regulatory structure underwent several changes. In 1985 the Final Report of the de Kock Commission⁵² proposed reforms in the regulatory system which resulted in South Africa implementing a functional financial regulatory approach. A few years later, in 1993 the Melamet Commission⁵³ recommended a single regulator but this proposal was not implemented and the regulatory system remained functional and partially integrated, i.e. sectoral.⁵⁴

In recent years, South Africa has however undertaken major regulatory reforms that accompanied its transition to a Twin Peaks model of financial regulation. Although South Africa had initiated a formal review of the financial regulatory system in 2007 even before the 2008 GFC, the proposals on bank supervision reforms by the Basel Committee on Banking Supervision brought impetus to these reforms.⁵⁵

South Africa's regulatory reforms were inter alia in response to a negative report issued by the International Monetary Fund (IMF) in its 2008 Financial Sector Assessment Programme which identified amongst other things that although South Africa's regulatory system was modern and generally effective; there was a need to strengthen the supervision of conglomerates, more attention to be paid to risks that spread across more than one sector, and to further promote cooperation, consistency, and effectiveness among regulators.⁵⁶

In a policy document titled "A safer financial sector to serve South Africa better" which was released in 2011 (often referred to as the "Red Book"), the South African National Treasury outlined the government's vision to reform the model of

⁵² Commission of Enquiry into the Monetary System and Monetary Policy in South Africa, (1985).

⁵³ Melamet Commission Report of the committee of inquiry into the feasibility of a holistic approach for financial supervision of financial institutions, financial services and deposit-taking institutions (1993).

⁵⁴ Andrew Schmulow: "Financial regulatory governance in South Africa – the move towards Twin Peaks" 25 (2017) *African Journal of International and Comparative Law*, 401.

⁵⁵ "A safer financial sector to serve South Africa better", (2011) 2.

⁵⁶ Financial Sector Assessment Programme Report (IMF): "South Africa Financial System Stability Assessment, Including Report on the Observance of Standards and Codes on the following topic: Securities Regulation" 08/349 October 2008 available at www.imf.org/en/Publications accessed on 15 February 2019 (hereinafter the FSAP Report)

regulation of the financial sector and proposed a shift towards a Twin Peaks model of financial regulation, which proposal was adopted by Cabinet in 2011. The Red Book set the following objectives for such reform:⁵⁷

- Ensuring financial stability ;
- Customer protection and regulation of market conduct;
- Expanding access through financial inclusion; and
- Combating financial crime.

In 2012, the Minister of Finance in his Budget Speech committed to implementing the Twin Peaks model of regulation and remarked: “As announced last year we intend to shift towards a twin peaks system for financial regulation where we separate prudential from the market conduct supervision of the financial market sector”.⁵⁸

The Red Book was further enhanced in 2013 when National Treasury developed a follow up policy paper titled “Implementing a Twin Peaks model of financial regulation in South Africa” (also referred to as the “Roadmap”), which clearly set the scene on how the South African Twin Peaks model would look like. In terms of the Roadmap, the main focus of the South African Twin Peaks model is to:⁵⁹

- Separate prudential regulation and supervision from market conduct;
- Mandate the Prudential Regulator to be responsible for maintaining and enhancing the safety and soundness of regulated financial institutions; prudential regulation and supervision of banks; co-operative banks and insurers; adopt a risk based approach to supervision;
- Mandate the Market Conduct Regulator to be responsible for the promotion and fair treatment of financial services customers, protect and enhance the integrity and efficiency of South African financial markets, promote financial awareness

⁵⁷ A safer financial sector to serve South Africa better, (2011) 4.

⁵⁸ Implementing a twin peaks model of financial regulation 6.

⁵⁹ Implementing a twin peaks model of financial regulation 45.

and literacy amongst South Africans and contribute to policy objectives of financial stability, financial inclusion and combatting crime;

- Strengthen the financial stability mandate of the South African Reserve Bank (SARB);
- Provide for crisis management and resolution in terms of which the South African Reserve Bank is to be appointed as the resolution authority given its financial stability mandate; designing a resolution framework to apply to various systemically important financial institutions, financial market infrastructures and financial groups; and the resolution authority to be given wide powers including bail-in⁶⁰; and
- Provide for enforcement in terms of which the regulators are given wide powers including imposing of administrative penalties, suspension and withdrawal of licenses.

2.2. Enactment of the Financial Sector Regulation Act (FSR Act)

The Financial Sector Regulation Bill was first introduced in Parliament in October 2015.⁶¹ This was followed by a number of consultations with relevant stakeholders and various drafts of the Bill. This process resulted in the Bill eventually being approved by the National Assembly in 2017, and it was signed into law and gazetted in 2017, as the Financial Sector Regulation Act, 2017 (Act No.9 of 2017 hereinafter FSR Act).⁶² The main actors in the South African Twin peaks model are the South African Reserve Bank (SARB) as central bank and the two newly established twin regulators, namely the Prudential Authority (PA) tasked with systemwide prudential regulation and supervision and the Financial Sector Conduct Authority (FSCA) tasked with systemwide market conduct regulation and supervision.

⁶⁰ "bail-in" is defined as any process outside of liquidation that has the effect of allocating losses to liability holders or shareholders, for the purpose of increasing the capital ratio of the institution. National Treasury Policy Document " Strengthening South Africa's Resolution Framework for Financial Institutions" available at www.treasury.gov.za accessed on 6 May 2019.

⁶¹ National Treasury Media Statement: Tabling of Financial Sector Regulation Bill to give effect to Twin Peaks reform available at www.treasury.gov.za/twinpeaks accessed on 25 February 2019.

⁶² Government Gazette No. 41060 dated 22 August 2017, available at www.treasury.gov.za accessed on 25 February 2019.

Chapter 2 of FSR Act gives the SARB a specific mandate to protect and enhance financial stability. The codification of this mandate is a major development in terms of strengthening the mandate of the SARB because traditionally, although the SARB had a *de facto* financial stability mandate, such mandate was never captured in legislation.⁶³ The Constitution and the South African Reserve Bank Act indicate the SARB's primary mandate as the protection of the value of the currency in the interest of balanced sustainable economic growth in the Republic⁶⁴, and the function of maintaining financial stability was implied in other functions of the SARB.⁶⁵

The SARB's functions in respect of the promotion and maintenance of financial stability as captured in the FSR Act entail the prevention, mitigation and management of risks to financial stability, particularly systemic risks. For such purposes the SARB is required and empowered to monitor systemic risks⁶⁶ and to designate an event as a "systemic event"⁶⁷ which in turn serves to trigger certain emergency powers to preserve financial stability.⁶⁸

The SARB is further required to publish a bi-annual stability review⁶⁹ and, in line with international trends, to designate certain institutions as Systemically Important Financial Institutions (SIFI)⁷⁰ so that the Prudential Authority may regulate these

⁶³ Martha Gertruida Van Niekerk "The role of the central bank in promoting and maintaining financial stability in South Africa – A comparative Analysis (LLD Thesis, University of Pretoria 2018) 152. (hereinafter Van Niekerk).

⁶⁴ Section 224 of the Constitution of the Republic of South Africa 1996, and section 3(1) of the South African Reserve Bank Act, 1989.

⁶⁵ Section 10 of the South African Reserve Bank, 1989.

⁶⁶ Systemic risk is the risk of disruptions to the provision of key financial services that is caused by impairment to all or parts of the financial system which can cause serious consequences to the economy as explained by Hendrik Nel "Introduction to macro prudential policy and instruments of the SARB" SAIFM Regulatory Summit, 2017.

⁶⁷ The FSR Act defines systemic event as "an event or circumstance, including one that occurs or arises outside the Republic, that may reasonably be expected to have a substantial adverse effect on the financial system, or on economic activity in the Republic, including an event or circumstance that leads to a loss of confidence that operators of, or participants in, payment systems, settlement systems or financial markets or financial institutions are able to continue to provide financial products or financial services or services provided by a market infrastructure".

⁶⁸ In terms of section 11 of the FSR Act, if a systemic event has occurred or is imminent, the SARB must restore or maintain financial stability.

⁶⁹ Section 13(1) of the FSR Act.

⁷⁰ SIFIs are institutions of such size, market importance and interconnectedness that their distress or failure would cause significant dislocation in the financial system and adverse economic consequences, - Van Niekerk, 31.

institutions more intrusively for purposes of financial stability.⁷¹ The Financial Stability Oversight Committee (FSOC), comprising of the Governor and the CEOs of the various regulators, is established to support the SARB in its execution of the financial stability mandate, and also to facilitate co-operation and collaboration between the SARB and other regulators.⁷²

2.3. Role of the SARB

In older countries such as Europe, central banks evolved from being commercial banks to being responsible for issuing notes and acting as government bank⁷³. The role of the central bank varies in many countries; however traditionally many central banks have been responsible for monetary policy, systemic stability, and maintenance of the value of the currency, prudential regulation and supervision of banks.⁷⁴ In some countries central banks are responsible for banks only, whereas in other countries they are responsible for banks, insurance companies and securities trading.⁷⁵

Financial stability is therefore an activity that central banks have traditionally been involved with and which is receiving more prominence in many jurisdictions post GFC.⁷⁶ According to the Group of Thirty, over and above performing the function of implementing monetary policy, central banks of developed economies also perform the roles of prudential supervision, ensuring financial stability and acting as lender of last resort (LOLR).⁷⁷ De Jager argues that since central banks are usually authorities that are able to influence the costs and availability of credit in their

⁷¹ Section 29-31 of the FSR Act.

⁷² Section 33 of the FSR Act.

⁷³ Johan De Jager "The South African Reserve Bank: An Evaluation of the Origin, Evolution and Status of a Central Bank" (2006) 18 *South African Mercantile Law Journal* 159-174, 162 (hereinafter De Jager).

⁷⁴ Llewellyn 2006 28.

⁷⁵ Llewellyn 2006 28.

⁷⁶ Nout Wellink "Central Banks as guardians of financial stability- De Nederlandsche Bank" (2002) – Speech delivered by Nout Wellink, President of the De Nederlandsche Bank at a seminar titled "Current issues in central banking" available on www.dnb.nl/en/news/news/new-and-archive/speeches accessed on 18 April 2019 (hereinafter central banks as guardians of financial stability).

⁷⁷ Group of Thirty 39.

economies, they are therefore capable of determining monetary policy in their respective jurisdictions.⁷⁸

There are several reasons that are advanced in favour of having the central bank performing the function of banking supervision. Those that advocate for the central bank retaining banking supervision argue that there are synergies to be derived since the central bank is also performing the role of lender of last resort.⁷⁹ Taylor further advances this argument to say that the information acquired in the capacity of bank supervisor is critical for the bank performing the function of lender of last resort, and therefore it is sensible for the roles of lender of last resort and banking supervision to be located in the same institution.⁸⁰

According to the Group of Thirty central banks have a supervisory competitive edge due to their expertise and knowledge of market conditions; therefore they will be compromised if the role of banking supervision were allocated to another supervisor or agency. If central banks perform the function of banking supervision, this gives them a bird's eye view into the activities of financial institutions' which is necessary in performing other functions such as setting interest rates, liquidity providers in a crisis and lender of last resort.⁸¹ Proponents of this approach further argue that since the central bank is responsible for systemic stability, if it also does not perform the function of banking supervision there will be duplication of effort and challenges in information gathering between the central bank and another supervisory agency.⁸²

There are however also arguments against having the central bank as banking supervisor namely:⁸³

⁷⁸ De Jager, 164. However he argues that monetary policy cannot be seen in isolation from other economic measures such as fiscal policy.

⁷⁹ Taylor, "The road from Twin Peaks 84.

⁸⁰ Taylor, "The road from Twin Peaks 84.

⁸¹ Group of Thirty "Structure of Financial Supervision" 39.

⁸² Llewellyn 2006 30.

⁸³ C.A.E Goodhart and D. Schoemaker "The Institutional Separation between Supervision and Monetary Policy in The Central Bank and the Financial System" (1995) 341.

- There may be conflict of interest between the central banks' monetary policy objectives and maintaining the safety and soundness of banks;
- There might be concentration of power in the hands of the central bank;
- There might be a perception of creation of moral hazard⁸⁴ if the public is enjoying the protection of deposit insurance, as it is with the banks; and
- The authority of the bank in its other activities might be compromised if there are regulatory failures.

Goodhart and Schoemaker have also expressed their concern about the reputation and credibility of the central bank being damaged in case there are banking supervision failures.⁸⁵ Although there is inconsistency amongst various jurisdictions on the role of the central bank, there is a universal approach in allocating the role of maintaining systemic stability to the central bank even if it is not involved in the prudential regulation and supervision of the banks.⁸⁶

It seems therefore that it is inevitable that banking supervision will never be completely independent of the central bank since the central bank is monopoly provider of the reserves, lender of last resort, and is also responsible for macro prudential policy and payment and settlement system. The connectedness of all these roles places the central bank at the centre of the financial system and requires it to have close relationships with all regulators.

According to Svensson, macro prudential policy is about crisis prevention and is a subset of financial stability policy that includes macro and micro prudential policy and resolution.⁸⁷ He argues that the goal for macro-prudential regulation is financial stability but he admits that the exact definition of financial stability is not clear.

⁸⁴ Moral hazard refers to the tendency for excessive risk taking by those protected by deposit insurance as defined by the Financial Stability Forum on guidance for developing effective deposit insurance systems (2001) available at <http://www.fsb.org/wp-content/uploads/> (accessed on 4 April 2019).

⁸⁵ Llewellyn 2006 28.

⁸⁶ Llewellyn 2006 32.

⁸⁷ Lars E.O Svensson, "Monetary policy and macroprudential policy: different and separate"? (2018) *Canadian Journal of Economics* 5 (hereinafter Monetary Policy and Macro prudential Policy).

However, he goes on to define financial stability as “a financial system that can fulfil its three main functions (transforming saving into financing, allowing risk management, and transmitting payments) with sufficient resilience to disturbances that threaten these functions”.⁸⁸ In his analysis whether macro prudential and monetary policy are distinct policies, he poses the question whether financial stability is a suitable goal for central banks. He distinguishes between crisis prevention and crisis management and arrives at the conclusion that central banks should have financial stability as an objective in crisis management and indicates that in crisis prevention this will depend on whether central bank has control of macro prudential instruments.⁸⁹ It is submitted that this analysis is misguided because central banks should have financial stability as an objective that is embedded within all its functions at all times. Consequently, these functions are complementary and if they function optimally, then financial stability should be a normal function of central banks and not only be approached by way of crisis prevention and crisis management.

Regardless of the structure of regulation and supervision, it is of critical importance for central banks to have access to information of large and systemically important financial institutions. Equally, irrespective of the structure adopted if information sharing and decision making structures are not functional between the central bank and other regulators, this can have a negative impact on the required collaboration during financial crisis.⁹⁰

Before South Africa moved to the Twin Peaks model of regulation in 2017, it had worked out a compromise whereby the Registrar of Banks was located within the South African Reserve Bank (SARB), but was autonomous and operated on the basis of an arm’s length relationship with the SARB.⁹¹ However, with the move to Twin Peaks, banking supervision (prudential supervision) is now the responsibility of the Prudential Authority (PA) as discussed in more detail below. Since is it critical

⁸⁸ Svensson, “Monetary Policy and Macro prudential policy 4.

⁸⁹ Svensson, “Monetary Policy and Macro prudential policy 6.

⁹⁰ Group of Thirty 15.

⁹¹ Llewellyn 2006 31.

for the SARB to have access to information pertaining to financial institutions, the relationship between the PA and the SARB is of utmost importance.

In addition to its new mandate of promoting and maintaining financial stability, the SARB is continuing to perform its functions as per the SARB Act.⁹² Notably the SARB, PA, FSCA and other regulators are in the process of implementing Twin Peaks and, as discussed in more detail below, it is important that there is proper co-ordination and collaboration for this model of regulation and supervision to work efficiently.

2.4. Special Features of the FSR Act

2.4.1. Establishment of the Prudential Authority

Section 32 of the FSR Act establishes the first peak, the Prudential Regulator (PA) as a separate juristic person located within and under the administration of the SARB. The PA is empowered to regulate and supervise financial institutions that provide financial products and securities services.

The objective of the PA is to (i) promote and enhance the safety and soundness of financial institutions that soundness of market infrastructures, (ii) protect financial customers against the risk that those financial institutions may fail to meet their obligations; and (ii) assist in maintaining financial stability.⁹³

There are several functions that the PA is mandated to perform in order to carry out its mandate and achieve its objectives, which include the following:⁹⁴

- Regulating and supervising financial institutions that provide financial products and services and market infrastructures in accordance with financial sector laws;
- co-operating and assisting the SARB, FSOC, FSCA, the National Credit Regulator (NCR) and the Financial Intelligence Centre (FIC) as required by the FSR Act;
- co-operating with the Council for Medical Schemes in handling matters of common interest;

⁹² Section 10 of the SARB Act.

⁹³ Section 33 of the FSR Act.

⁹⁴ Section 34 of the FSR Act.

- Supporting sustainable competition and co-operate and collaborate with the Competition Commission; and
- supporting financial inclusion.

It is notable that the PA is clothed with wide powers as the Act provides that it may do anything reasonably necessary to achieve its objectives, and further it is mandated to perform its functions without fear, favour or prejudice.⁹⁵ The PA must also to the extent practicable, have regard to international regulatory and supervisory standards set by international standard setting bodies and is, aptly, required to have regard to circumstances prevailing in the Republic.⁹⁶

The PA performs the same functions that were performed previously by the Bank Supervision Department under the SARB - however it has new focus areas such as the regulation and supervision of financial conglomerates, financial market infrastructures and insurance companies and upon instruction of the SARB, it has to issue prudential standards to Systemically Important Financial Institutions (SIFIs).⁹⁷ The PA is headed by the Chief Executive Officer (CEO) who is a Deputy Governor of the SARB and is appointed by the Governor with the concurrence of the Minister of Finance. A Prudential Committee is established in order to generally manage and oversee the operations and administration of the PA.⁹⁸ The Prudential Committee is comprised of the Governor of the SARB (who is also the Chairperson), the CEO and other two Deputy Governors of the SARB. The SARB is mandated to provide staff and resources to the PA.⁹⁹

2.4.2. Establishment of the Financial Sector Conduct Authority

The second peak, the Financial Sector Conduct Authority (FSCA) is established in terms of section 56 of the FSR Act with the objective of protecting financial customers and ensuring fair treatment of customers by financial institutions. The

⁹⁵ Section 34(3) and 5 of the FSR Act.

⁹⁶ Section 34(4) of the FSR Act.

⁹⁷ Section 30 of the FSR Act.

⁹⁸ Section 41 of the FSR Act.

⁹⁹ Section 51 of the FSR Act.

FSCA is a separate juristic person and is a national public entity¹⁰⁰ located outside the SARB headed by a Commissioner. The FSCA's mandate is to regulate and supervise the conduct of financial institutions and amongst other functions to assist the SARB in maintaining financial stability and also co-operate and collaborate with other regulators.

The FSCA's objective is to (i) enhance and support the efficiency and integrity of financial markets and protect financial customers by promoting fair treatment of financial customers by financial institutions and (ii) provide financial customers and potential financial customers with financial education programs, and otherwise promoting financial literacy and the ability of financial customers and potential financial customers to make sound financial decisions; and (iii) assist in maintaining financial stability.¹⁰¹

In order to achieve its objectives, the FSCA is mandated to perform the following functions:¹⁰²

- to regulate and supervise the conduct of financial institutions in accordance with the financial sector laws;
- to co-operate with, and assist, the SARB, the FSOC, the PA, the NCR and the FIC as required in terms of the FSR Act;
- to promote, to the extent consistent with achieving its objectives, sustainable competition in the provision of financial products and financial services, including through co-operating and collaborating with the Competition Commission;
- to promote financial inclusion;
- to administer the collection of levies and the distribution of amounts received in respect of levies;
- to conduct and publish research relevant to its objective;
- and to formulate and implement strategies and programs for financial education for the general public.

¹⁰⁰ Section 56(1) and (2) of the FSR Act.

¹⁰¹ Section 57 of the FSR Act.

¹⁰² Section 58 of the FSR Act.

Similar to the PA, the FSCA has wide powers to do anything reasonably possible in order to achieve its objectives including co-operating and collaborating with other jurisdictions.¹⁰³ It must further perform its functions without fear, favour or prejudice.¹⁰⁴

Section 60 of the Act establishes an Executive Committee which is comprised of the Commissioner and Deputy Commissioners to govern the affairs and administration of the FSCA and to ensure its efficiency.

2.4.3. Co-operation and collaboration between regulators

According to Llewelyn, irrespective of the kind of model of regulation a country opts for, there are key issues that are universal amongst all models such as the need for co-operation, collaboration and information sharing between the regulators.¹⁰⁵ Given the fragmented history of the South African financial system,¹⁰⁶ National Treasury emphasised that it is particularly important for regulators to co-operate and collaborate in order for the Twin Peaks model to work.¹⁰⁷

The FSR Act provides for co-operation and collaboration between the various financial sector regulators (the PA and FSCA as the twin regulators as well as the FIC, NCR and the SARB). This is important because there is bound to be conflict, duplication and overlap of regulation and functions. Such cooperation and collaboration has to occur on two levels: firstly for the dedicated purpose of maintaining financial stability (as per section 26) and secondly, on a broader level for the general effective and efficient working of the Twin Peaks model (as per section 76).

Co-operation and collaboration is enabled through entering into various Memoranda of Understanding (MOU's) by the SARB with other regulators in relation to financial

¹⁰³ Section 58(4) of the FSR Act.

¹⁰⁴ Section 58(6) of the FSR Act.

¹⁰⁵ Llewellyn 2006 11.

¹⁰⁶ Implementing a Twin Peaks model of financial regulation in South Africa 28.

¹⁰⁷ Implementing a Twin Peaks model of financial regulation in South Africa 19.

stability,¹⁰⁸ and between regulators themselves when performing their functions in terms of financial sector laws.¹⁰⁹

2.4.4. Establishment of various structures to assist in achieving the objectives of the FSR Act: Financial Stability Oversight Committee (FSOC)

The FSOC, as referred to in paragraph 2.2 above, was established in terms of section 20 of the FSR Act and its primary objective is to support the SARB in pursuing its mandate of promoting and maintaining financial stability. It also facilitates co-operation and collaboration between the SARB and other financial sector regulators on matters pertaining to financial stability.¹¹⁰ The FSOC is chaired by the Governor of the SARB and consists of the CEO of the PA who is also one of the SARB's Deputy Governors, the Deputy Governor responsible for financial stability matters, the FSCA's Commissioner, the Chief Executive Officer of the NCR, the Director General of National Treasury, the Director of the FIC, and a maximum of three additional members appointed by the Governor.¹¹¹ The composition of this Committee is representative of major stakeholders and therefore its importance cannot be overemphasised. Some of its functions entail making recommendations to the Governor on the designation of SIFIs, advising the Minister of Finance and the SARB on steps to be taken to promote, protect and maintain or to manage or prevent risks to financial stability, and on matters related to crisis management and prevention.¹¹²

2.5. Financial Sector Contingency Forum

The Financial Sector Contingency Forum is established in terms of section 25 of the Act with the primary objective of assisting the FSOC with identifying any possible risk of systemic events occurring and co-ordinating plans and mechanisms for mitigating such risks.¹¹³ The Financial Sector Contingency Forum is comprised of at least eight members who are: the Deputy Governor designated by the Governor

¹⁰⁸ Section 27 of the FSR Act.

¹⁰⁹ Section 76 and 77 of the FSR Act.

¹¹⁰ Section 20 of the FSR Act.

¹¹¹ Section 22 of the FSR Act.

¹¹² Section 21 of the FSR Act.

¹¹³ Section 25 of the FSR Act.

(Chairperson of the forum), representatives of each financial sector regulator, representatives of other organs of state as determined by the Chairperson, and such representatives of financial industry bodies as the Chairperson may determine.¹¹⁴

2.6. Financial System Council of Regulators

This Council is established with the primary objective of facilitating co-operation and collaboration and consistency of action between institutions represented on the Council and the regulators, thereby creating a platform to discuss matters of common interest. It is constituted of the Director-General of National Treasury; the Director-General of the Department of Trade and Industry; the Director-General of the Department of Health; Chief Executive Officer of the PA; the FSCA Commissioner; Chief Executive Officer of the NCR; the Registrar of Medical Schemes; the Director of the FIC; the Commissioner of the National Consumer Commission; the Commissioner of the Competition Commission; the Deputy Governor responsible for financial stability matters; and the head of any organ of state or other organisation that the Minister may determine.¹¹⁵ The Council meets twice a year and meetings are chaired by the Director General of National Treasury.¹¹⁶

The Council must establish working groups and sub-committees that deal with financial stability and resolution, enforcement and financial crime, policy and legislation, standard setting, financial inclusion, financial sector outcomes, transformation in the financial sector and any other matter as determined by the Director General after consultation with the Financial Sector Council of Regulators.¹¹⁷ The size and composition of the Council signifies the importance of co-operation and collaboration between financial sector regulators and organs of state in working together towards the achievement of the objectives of Twin Peaks.

¹¹⁴ Section 79 of the FSR Act.

¹¹⁵ Section 79 of the FSR Act.

¹¹⁶ Section 80 of the FSR Act.

¹¹⁷ Section 81 of the FSR Act.

2.7. Financial Sector Inter Ministerial Council

The Act takes cognisance of the fact that some policy decisions might have to be made at higher levels than those structures already provided for. To this end, it establishes the Inter Ministerial Council for the Financial Sector (IMC) whose objective is to facilitate co-operation and collaboration between cabinet members responsible for administering relevant financial sector laws so that matters of common interest can be discussed in this forum. The IMC is comprised of the Minister of Finance; Cabinet members responsible for consumer protection and consumer credit matters; the Cabinet member responsible for health; and the Cabinet member responsible for economic development.¹¹⁸ The IMC meets as and when determined by Minister of Finance who chairs the meetings, or nominates a chair in his stead.

2.8. Ombud Council

In keeping with some of the objectives of the FSCA, the Ombud Council was established with the aim of ensuring that financial customers have access to affordable, effective and fair alternative dispute resolution processes which they are able to use in referring their complaints about financial institutions in respect of financial products or services or services provided by market infrastructures.¹¹⁹ The Council must recognise industry ombuds schemes. Some of the functions that the Council is responsible for are promoting co-operation between and coordination of activities between ombuds, it must strive to protect the independence and impartiality of ombuds, resolve, in accordance with the Act, overlaps of the jurisdictional coverage of different ombud schemes and support financial inclusion. The Council has wide powers and is mandated to do everything reasonably necessary to achieve its objectives,¹²⁰ including performing its functions without fear, favour or prejudice.¹²¹

¹¹⁸ Section 83 of the FSR Act.

¹¹⁹ Section 175 of the FSR Act.

¹²⁰ Section 177 of the FSR Act.

¹²¹ Section 177(3) of the FSR Act.

2.9. Financial Services Tribunal

The Financial Services Tribunal is established in terms of section 219 to reconsider decisions of various institutions including decisions by financial services regulator provider or Ombuds Council, financial service provider decision by a market infrastructure, statutory ombud and its powers include consideration of omissions by the said institutions to take decisions within prescribed period in terms of the applicable financial sector law.¹²² The Tribunal is constituted by at least two persons who are retired judges, or who are persons with suitable expertise and experience in law; and at least two other persons with experience or expert knowledge of financial products, financial services, financial instruments, market infrastructures or the financial system.¹²³ The Minister must appoint one of the Tribunal members as the Chairperson, and may appoint another Tribunal member as Deputy Chairperson. The Chairperson determines the rules of the Tribunal.

¹²² Section 177(4) of the FSR Act.

¹²³ Section 218 of the FSR Act.

CHAPTER THREE: TWIN PEAKS IN THE NETHERLANDS

3. Introduction

The Dutch central bank, De Nederlandsche Bank (DNB), was founded in 1814 and has evolved through the years from being a private lender to becoming part of the European System of Central Banks and subsequently being both the systemic and prudential supervisor of the entire Dutch financial sector.¹²⁴ As the DNB was evolving, its role was defined in the Banks Act of 1948 which gave it a joint responsibility with the Ministry of Finance for price stability.¹²⁵ The Banks Act of 1948 gave DNB an explicit mandate for monetary policy and the stability of the financial system. However, this reference to financial system stability only extended to the stability of the currency and there was no explicit mandate for DNB to be responsible for financial stability which was in actual fact a role it executed *de facto* by virtue of its position as central bank.¹²⁶

In 1952 the Wet toezicht kredietwezen (Supervision of the Credit System Act) was promulgated and it established a statutory basis for banking supervision in the Netherlands. Financial supervision in the Netherlands in the pre-Twin Peaks era was sector-based with DNB supervising banks, collective investment entities and exchange offices,¹²⁷ whilst the Securities Board (STE) supervised all participants in the securities trade, and the Pension and Insurance Supervisor (PVK) was the prudential supervisor of insurers and pension funds.¹²⁸ DNB had traditional central bank roles such as responsibility for monetary policy, bank supervision, supervision of payment and settlement system acting as lender of last resort, although, as indicated, it had no explicit mandate for financial stability but merely fulfilled a *de facto* mandate this regard.¹²⁹ In order to cooperate on cross sector regulatory and supervisory issues, DNB, STE and PVK established a Council of Supervisors (Raad van Financiële Toezichthouders or RFT) in 1999.¹³⁰ The RFT was created with the

¹²⁴ History of De Nederlandsche Bank available at www.dnb.nl/en/about-dnb/organistaion/history accessed on 5 April 2019 (hereinafter History of DNB).

¹²⁵ Group of Thirty 199.

¹²⁶ Van Niekerk, 244.

¹²⁷ History of DNB.

¹²⁸ Group of Thirty, 198.

¹²⁹ Everdingen H, Grundman-van der Krol, Saschse Aspecten van toezicht: Beschouwingen over het toezicht op die financiële sector: Preadvisen voor die vereniging voor Effectenrecht (1999) 13 (hereinafter Everdingen et al 1999).

¹³⁰ Group of Thirty 198.

purpose of coordinating microprudential and conduct of business supervision between the various sectorally-based supervisory agencies.¹³¹

In 1998 a new Banking Act, the 1998 Bankwet, was introduced. This Act however also did not expressly capture the DNB's financial stability mandate. Van Niekerk however argues that even though the Bankwet of 1998 did not give an explicit financial stability mandate to DNB, it can be inferred from the number of functions mentioned above that DNB had an implied *de facto* financial stability mandate before the Netherlands moved to a Twin Peaks model of financial regulation.¹³²

3.1. The move to a Twin Peaks model in the Netherlands

The Netherlands moved towards a Twin Peaks model of financial regulation shortly before the 2008 GFC. This move was motivated by a number of factors, chief amongst those being the concern from Dutch authorities about the challenges posed by complex financial products that had cross-sectoral elements,¹³³ and the development of large financial conglomerates which were perceived as not being transparent which complicated their supervision thus posing a risk to financial stability.¹³⁴

Notably the STE was converted into the Autoriteit Financiële Markten (AFM) in 2002 and it assumed responsibility for supervision of conduct of business by financial institutions on a cross-sectoral basis.¹³⁵ In 2002 the Netherlands commenced the move to an objective based Twin Peaks supervisory model whereby DNB assumed responsibility for system wide prudential supervision for not only banks but for all financial institutions, and AFM became responsible for supervision of all conduct of business which included supervision of security market

¹³¹ International Monetary Fund Country Report No. 04/311 Kingdom of the Netherlands – Netherlands: Technical Note: The Netherlands Model of Financial Sector Supervision (September 2004) available at <http://www.imf.org/en/publications/CR/Issues> accessed on 10 April 2019 (hereinafter IMF Report No. 04/311).

¹³² Van Niekerk 250.

¹³³ Group of Thirty 31.

¹³⁴ Van Niekerk 250.

¹³⁵ IMF Report No. 04/311 6.

activities, market behaviour and consumer protection.¹³⁶ During this time a Covenant between DNB, PVK and AFM was entered into with the objective of facilitating a smooth transition towards an objective based supervisory framework.¹³⁷

The reforms in the Dutch approach to financial regulation gained momentum in 2004 with a merger between DNB and PVK consolidating them into one systemic and prudential agency. The Dutch Twin Peaks reforms were completed in 2007 with the enactment of the Financial Supervision Act 2007 (Wet op het Financieel Toezicht) (Wft).¹³⁸ Van Niekerk remarks that the Wft was the “actual framework legislation that set up the architecture for the Dutch Twin Peaks” and that it can be likened to the FSR which similarly is perceived as the framework legislation that introduced Twin Peaks in South Africa.¹³⁹

According to an IMF Country Report on the Dutch financial system issued in 2011, the decision to locate prudential supervision of financial institutions under DNB was occasioned by the high incidence of complex financial conglomerates and also due to the challenge of regulatory arbitrage.¹⁴⁰ It was further argued by Dutch authorities that prudential and conduct of business supervision, despite synergies between them, are in actual fact separate regulatory areas hence they require different mechanisms for achieving their respective objectives.¹⁴¹ It was perceived, and rightly so, that prudential and conduct of business supervision do not mix and each of these regulatory areas require different skill sets. The view was that conduct of business is likely to receive more attention for political reasons than prudential supervision in normal times and it could lead to a diversion of the attention and resources of the agency or supervisor at the expense of prudential supervision.¹⁴²

¹³⁶ Financial Sector Assessment Programme Update, (IMF) Kingdom of the Netherlands: June 2011, 5. available at <http://www.imf.org/en/publications/CR/Issues/2> accessed on 10 April 2019 (hereinafter IMF Country Report 11/208).

¹³⁷ IMF Country Report 11/208 5.

¹³⁸ Group of Thirty 199.

¹³⁹ Van Niekerk 265.

¹⁴⁰ IMF Country Report 11/208 5.

¹⁴¹ IMF Country Report 11/208 7.

¹⁴² Taylor M The Road from Twin Peaks 90.

The decision to locate prudential supervision under the jurisdiction of DNB was further motivated by the argument that prudential supervisors could benefit from the DNB as central bank's long standing credibility and macroeconomic analysis capabilities. It was also argued that DNB as prudential supervisor and central bank would be able to have a "bird's eye view" of systemic issues across the financial sector as a whole, and therefore it would be in a position to take quick decisions in crisis times.¹⁴³

Under the Wft, DNB and the AFM were explicitly required to cooperate and collaborate to facilitate their relationship and the effectiveness and efficiency of the Dutch Twin Peaks model. This cooperation and collaboration was enabled through a new Covenant that was entered into in 2007.¹⁴⁴

Given that the Netherlands transitioned to a Twin Peaks model very shortly before the GFC it is necessary to consider how the Dutch Twin Peaks model fared during the Crisis and what lessons South Africa may take from the experience of the Dutch Twin Peaks model also during the GFC.

3.2. The Netherlands' Twin Peaks model during the GFC

The Netherlands weathered the GFC to some extent and, in comparison with other countries, managed to stave-off the most devastating consequence of the GFC. However the Dutch government nevertheless had to resort to drastic measures to safeguard the stability of the Dutch financial system.¹⁴⁵ For example, Schmulow points out that liquidity was provided on a large scale to a number of financial institutions and at times this was done in foreign currency.¹⁴⁶ The Dutch Government also made massive capital injections for banks and insurers, all deposits were guaranteed up to €100,000; state guarantees were also issued for

¹⁴³ IMF Country Report 11/208 7.

¹⁴⁴ Group of Thirty 202.

¹⁴⁵ Andrew Schmulow, "The four methods of financial system regulation: an international comparative study" (2015) 26 JBFLP 151, 165. (hereinafter, Schmulow- an international comparative study).

¹⁴⁶ De Nederlandsche Bank; Annual Report (2009) 31 available on [www.dnb.nl/en/bianaries/DNB%20Annual%](http://www.dnb.nl/en/bianaries/DNB%20Annual%20Report) accessed on 10 April 2019 (hereinafter DNB Annual report, 2009)

banks and nationalisation occurred of Fortis/ABN, a giant financial conglomerate that conducted insurance, banking and investment management.¹⁴⁷

According to the IMF Country Report that was issued subsequent to the GFC in 2011, the Dutch Twin Peaks model functioned well during the GFC. The IMF indicated that this was because decisions could be taken timeously to contain a banking crisis. Information sharing could also be done relatively easily between the supervisors which was enabled by the 2007 Covenant. In addition, since the respective roles of DNB and that of the Ministry of Finance regarding crisis management was clear and codified in a MOU it made crisis management measures less complicated given that eventually the overall responsibility for financial stability eventually vested in the Minister of Finance.¹⁴⁸ The aforesaid MOU clearly set out the roles of DNB and that of the Minister of Finance within the Dutch Twin Peaks model. It specified that DNB was responsible for implementing monetary policy, monitoring and contributing to financial system stability, supervising the soundness of financial institutions and pension funds, and exercising an oversight role over the clearing and settlement system for payments and securities transactions. The Minister of Finance was tasked with responsibility for ensuring the optimal functioning of the financial system and decision making on finances during crisis management.¹⁴⁹

However, despite the fact that the Dutch government could intervene quickly during the GFC, it soon became clear that there were regulatory shortcomings in terms of both the scope and substance of supervision and further that the tendency of “light touch” supervision in the Netherlands, especially insofar as DNB, was concerned, had gone too far.¹⁵⁰ The GFC revealed that there were certain aspects of the Dutch Twin Peaks model which needed to be strengthened for optimal functioning and supervision. In particular, it was realised that despite the fact that the Wft provided DNB with significant enforcement powers, including the power to impose sanctions,

¹⁴⁷ Schmulow, An international comparative study, 166.

¹⁴⁸ IMF Country Report 11/208 9.

¹⁴⁹ Memorandum of Understanding between Minister of Finance and DNB entered into in February 2007 available at www.dnb.nl/en/binaries/eng%20compleet_tcm47 accessed on 20 April 2019.

¹⁵⁰ Schmulow, an international comparative study, 166.

it was found that DNB did not measure up in this area as it relied more on moral suasion¹⁵¹ than on its actual enforcement powers. DNB also had a regulatory challenge given that it had limited power over financial conglomerates as it could not impose penalties on them for contravention of financial sector laws.¹⁵²

3.3. The Netherlands' Twin Peaks model post the GFC

The GFC revealed the strengths and weaknesses of the Dutch Twin Peaks model. This motivated the Dutch government to make certain changes to the Dutch Twin Peaks model to give effect to the recommendations of the IMF Report.¹⁵³ One of the things that the Dutch government did was to take steps to strengthen prudential supervision of financial institutions. Two comprehensive studies by DNB followed, namely; “DNB Supervisory Strategy 2010-2014”¹⁵⁴ and “De Nederlandsche Bank – From Analysis to Action.”¹⁵⁵ The main aim of these documents was to provide guidance for more proactive and conclusive supervision.¹⁵⁶

The GFC highlighted the importance of fully integrating macro- and micro-prudential supervision in the Netherlands.¹⁵⁷ The Dutch learnt from the Crisis that there was a need to establish a link between macro- and micro-prudential supervision for purposes of identifying and mitigating systemic risks in the Dutch financial system.¹⁵⁸ The Report titled “From Analysis to Action” indicated that such integration “would require deeper cooperation between macro and micro supervision in thematic research, supervisory knowledge networks, stress tests and in preparing the half-yearly Overview of Financial Stability”.¹⁵⁹ Another step was that DNB’s Financial Stability Division which was responsible for safeguarding the financial system stability had to be strengthened because it had insufficient macro-prudential tools at its disposal. This lack of appropriate macro-prudential tools

¹⁵¹ Financial Times “Definition of moral suasion” <http://lexicon.ft.com/term-moral-suasion> (accessed 6 May 2019): Moral suasion is the term to describe when a government or central bank uses persuasion rather than regulatory coercion to convince financial sector participants to take a particular course of action.

¹⁵² IMF Country Report 11/208 10.

¹⁵³ IMF Country Report 11/208 13.

¹⁵⁴ De Nederlandsche Bank “DNB Supervisory Strategy 2010-2014 (April 2010) available at <https://www.dnb.nl/en/publications> accessed on 18 April 2019.

¹⁵⁵ De Nederlandsche Bank “From Analysis to Action, (2010) available at <http://www.dnb.nl/en/publications> access IMF Country Report 11/208 13.ed on 18 April 2019 (hereinafter From Analysis to Action Report).

¹⁵⁶ IMF Country Report 11/208 13.

¹⁵⁷ IMF Country Report 11/208 11.

¹⁵⁸ DNB Annual report 2009 47.

¹⁵⁹ From Analysis to Action Report 11.

exposed the financial system to systemic risks that could occasion the collapse of the financial system. Consequently DNB established a Department for Macro-prudential Supervision in order to assist with promoting and maintaining financial stability by improving the monitoring of macro-prudential risks.¹⁶⁰

Various other steps were taken to strengthen the Dutch Twin Peaks model, namely:¹⁶¹

- a) an enforcement department was set up within DNB which was responsible for corrective actions and sanctions. This department launched the “Vita”-project, to improve accountability of supervisors and get them to use their supervisory and enforcement powers appropriately, thereby aligning their supervisory powers with best practice.
- b) the Department for Macro prudential supervision in DNB was expanded to improve the monitoring of macro-prudential risks.
- c) risk analysis and macro prudential tools were strengthened in order to link macro prudential risks with individual financial institutions.
- d) co-operation and knowledge sharing between personnel tasked with supervision of banks and insurance companies with cross-border operations were improved to facilitate better information-sharing.

According to Bush et al¹⁶², the Dutch central bank, even in the Twin Peaks model, for a long time had no explicit mandate for financial stability. As pointed out by Van Niekerk, this position was influenced by the fact that when the Dutch Twin Peak model of financial regulation was introduced and subsequently refined, the focus was more on establishing the DNB and AFM as main regulatory agencies and defining their roles as prudential and market conduct regulators respectively. This means that at that stage insufficient focus was placed on the role of DNB in the maintenance of financial stability.¹⁶³

¹⁶⁰ IMF Country Report 11/208 11.

¹⁶¹ IMF Country Report 11/208 13.

¹⁶²D Bush, DR Doorenbos, GM Grundman-van de Krol, RH Maatman, MP Nieuwe Weme and WAK Rank, *Onderneming en Financieel Toezicht* (2010) 153 (hereinafter Bush et al).

¹⁶³ Van Niekerk 296

Initially DNB had an implied financial stability role that it shared with the Minister of Finance, although, as pointed out above, the Minister had the final accountability for financial stability. The MOU that DNB and the Minister of Finance entered into a MOU in 2007 was aimed at facilitating coordination between the central bank and the Minister. It provided that during a crisis period or banking failure, DNB would take the leading role but would inform the Minister of its actions.¹⁶⁴ The MOU further provided that if there was a crisis, then Minister would appoint a representative to the crisis management team convened by DNB.¹⁶⁵ The AFM as market conduct regulator was however not given a specific crisis management role under the MOU but was kept in the loop as under the 2007 Covenant the AFM would be informed of any action relating to financial stability taken by DNB and Minister of Finance.¹⁶⁶

DNB was eventually given an explicit financial stability mandate quite a couple of years after the adoption of the Dutch Twin Peaks model. It was afforded such explicit mandate by the amendment of the Banking Act via the Financial Markets Amendment Act of 2014. This Act further gave DNB responsibility to partake in the maintenance of financial stability across the European Union (EU).¹⁶⁷

3.4. Role of the Dutch Central Bank (DBN)

As a member of the European System of Central Banks (ESCB) the reforms in DNB took place within the broader context of the supranational policy in the ESCB. Participating central banks entered into the Maastricht Treaty¹⁶⁸ in terms of which the division of supervisory tasks was allocated between the ECB and National Central Banks (NCB).¹⁶⁹ Some of these tasks entailed monetary policy decisions, monetary policy implementation, international cooperation, payment systems,

¹⁶⁴ Group of Thirty 202.

¹⁶⁵ IMF Country Report 9.

¹⁶⁶ Group of Thirty 202.

¹⁶⁷ Van Niekerk 294.

¹⁶⁸ The Treaty that established the European Economic Community (EEC), available at www.europeanlawmonitor.org/treaties/eu-treaties accessed on 30 May 2019.

¹⁶⁹ Nout Wellink, "Central Banks as guardians of financial stability- De Nederlandsche Bank" (2002) – Speech delivered by Nout Wellink, President of the De Nederlandsche Bank at a seminar titled "Current issues in central banking" 3 available on www.dnb.nl/en/news/news-and-archive/speeches accessed on 18 April 2019. (hereinafter Nout Wellink Guardians of financial stability).

banking supervision and financial stability pursuits.¹⁷⁰ Consequently, DNB's role in relation to financial stability evolved within the context of the main regulatory developments on the broader EU level.¹⁷¹

As already stated under 3.1 above, DNB's role was defined in the Banks Act of 1948 under which it was given the responsibility for the stability of the value of money. Similar to other central banks, pre-Twin Peaks DNB performed other functions that central banks traditionally perform such as responsibility for monetary policy (which it shared with the European Central Bank or ECB), payment and settlement systems, prudential supervision and lender of last resort. According to Group of Thirty, by virtue of being taken up in the ESCB, DNB has had a dual status as an EU central bank and also as the domestic central bank and national prudential supervisor of the Netherlands.¹⁷²

After merging with PVK in 2004 and with the completion of the financial regulatory reforms in 2007, the responsibilities of DNB were augmented. These responsibilities subsequently include the supervision of monetary policy, prudential supervision for banks and non-banks (credit institutions, insurers, collective investment schemes, investment firms and pension funds), systemic stability supervision, supervision of the payment and settlement system, crisis management, and being the lender of last resort.¹⁷³

As alluded to above, responsibility for financial stability was eventually captured in legislation in 2014 thus giving DNB an explicit mandate to focus on financial stability amongst its other roles. According to Wellink central bank is better placed to be the guardian of financial stability due to a combination of its other responsibilities such as monetary policy, supervision of payment and settlement systems and

¹⁷⁰ Nout Wellink Guardians of financial stability 4-14.

¹⁷¹ Van Niekerk 294.

¹⁷² Group of Thirty 200.

¹⁷³ Group of Thirty 198-200.

prudential supervision. He further contends that in DNB, experience has shown that these roles are complementary.¹⁷⁴

Other reforms included that DNB established a Financial Stability Committee in 2012 to focus on the stability of the Dutch financial system and on macro-economic developments.¹⁷⁵ The Financial Stability Department fulfils a pivotal role as it analyses the interplay between prudential supervision and systemic and monetary stability issues.¹⁷⁶ This Department is also responsible for identifying threats to financial stability and drafting proposals for mitigating action as well as formulation of crisis management policies.¹⁷⁷ The DNB also has a Financial Stability Coordinating Group to enable the preparation of the “Overview of Financial Stability” that is issued twice a year.¹⁷⁸

Another important aspect to note is that DNB is also responsible for the Deposit Guarantee Scheme in case of bank failure. Although it took a while for the Netherlands to realise that financial stability is a core function of a central bank, and that it requires to be captured in legislation to give more prominence and better direction as to what this mandate entails, at least the Netherlands realised soon after the GFC that it had to entrench the DNB’s financial stability mandate in its Banks Act. It was also proactive in marshalling DNB to put appropriate mechanisms, supervisory tools and structures in place for the proper execution of this mandate.

¹⁷⁴ Nout Wellink : Guardians of financial stability 3.

¹⁷⁵ Van Niekerk 322.

¹⁷⁶ Group of Thirty 200. The Department also assess the degree to which financial system can absorb shocks.

¹⁷⁷ De Nederlandsche Bank: “Towards a more stable financial system-macroprudential supervision at DNB” 32 undated available at <https://www.dnb.nl/en/publications> (hereinafter De Nederlandsche Bank).

¹⁷⁸ De Nederlandsche Bank, 32.

CHAPTER 4: CONCLUSION AND RECOMMENDATIONS

4 Introduction

In order to grow the economy in any country, it is important for the financial system and financial regulation to function optimally. Post the 2008 GFC, financial stability has been identified as a critical public interest function of central banks. To this end, many jurisdictions began to review their financial regulatory approach and some countries, like the United Kingdom, moved towards the Twin Peaks model of regulation. Australia and Netherlands had already adopted the Twin Peaks model prior to the 2008 GFC, but refined it as they and when gaps were identified in their model of financial regulation. South Africa came out of the 2008 GFC relatively unscathed because of its robust financial regulation and effective systems; however the 2009 IMF Financial System Assessment Programme identified gaps within the South African financial model of regulation that could put its financial system at risk. At this time, South Africa being a member of the G20 countries, had undertaken to move towards Twin Peaks.

This study sought to establish whether the pre-Twin Peaks South African financial regulatory framework which was sectoral in nature and form, weakened the South African financial systems and thereby threatened financial stability, and whether in pursuit of financial stability, the Twin Peaks model of regulation offers a solution that will assist the SARB to promote and maintain financial stability.

In order to arrive at conclusions and recommendations that were discussed later in this Chapter, this research looked at (i) how the South African financial sector regulation looked like prior to Twin Peaks, (ii) different approaches to financial regulation and supervision (iii) South Africa's move to Twin Peaks, (iv) the role of the central bank, (v) special features of the FSR Act, and (vi) a comparative study of the Twin Peaks model in the Netherlands.

Prior to the GFC many countries, including the Netherlands and South Africa, did not prioritise financial stability as a function of the central bank or in their regulatory regime and it appears that financial stability became a default function that was derived as a result of central banks' other functions such as monetary policy, prudential supervision, and emergency liquidity assistance and LOLR. However, post the GFC, the pursuit of financial stability became a global focus area. As indicated, financial stability is a concept that is widely known to be difficult to define and almost an elusive concept, however it seems that post the GFC many jurisdictions came to have a good understanding of what financial instability is and what kind of financial regulation and systems to put in place in order to prevent any possible systemic risk.

The pursuit of financial stability is optimally achieved when it is considered as a deliberate measure and not merely as a function of other objectives of the central bank. It is submitted that if financial stability is to be specifically and deliberately pursued, then there must be focused macro prudential tools aimed at preventing and reducing any potential systemic risk. For financial stability to be achieved, it is very important for the SARB to remain independent due to the fact that it must be able to perform its functions without fear, favour or prejudice as envisioned in the Constitution. This is in relation to its macro prudential oversight role whereby it is able to have a helicopter view of the whole financial system. If there is any interference with the SARB's mandate and it is unable to exercise macro prudential oversight, then financial stability will be threatened

Although financial stability was not entrenched as an explicit mandate of the SARB pre-Twin Peaks, it was implicitly pursued through its monetary policy and other objectives that the SARB sought to achieve. As pointed out in Chapter Two, South Africa is coming from a history of a sectoral approach to financial regulation and has moved through the times to a functional approach thereby culminating into Twin Peaks in term of which the PA being one peak and the FSCA being the second peak were established with the SARB as a third peak. As also alluded to in Chapter three the Netherlands embedded financial stability in its legislation only in 2014,

several years after it had adopted the Dutch Twin Peaks model thus strengthening the mandate of DNB which functions as systemic regulator in this model. The delay in giving DNB an express mandate for promoting financial stability can be contrasted with the South African Twin Peaks model whereby the authorities, in designing the South African Twin Peaks model, recognised that an express financial stability mandate had to be incorporated in the FSR Act as framework legislation that introduced the model. We thus learned from the failure of the Netherlands to have such an express mandate when they first drafted their legislation and has thereby saved ourselves from a situation where there may be uncertainty as to the scope of the SARB's financial stability mandate and the extent of the powers linked to such mandate during crisis times.

South Africa has also sought not to dilute the effectiveness of SARB as systemic supervisor and has deliberately chosen a three peak model where systemic regulation and prudential regulation are not located in the same peak but is entrusted to the SARB and the PA respectively. This is in contrast with the two peak Dutch Model where the central bank is tasked both with systemic and prudential regulation.

However, it must be quickly pointed out that there are similarities between South Africa and the Netherlands in the sense that arriving at a point where both DNB and the SARB were given a mandate of maintaining financial stability took a long time. Financial stability mandate was always implied from other functions that the SARB performed such as implementing monetary policy, protecting the value of the currency, playing oversight role over payments and settlement system. Similarly the role of LOLR has never been explicitly defined or codified in the Dutch and South African legislative framework and remains a *de facto* function.

4.1. Key differences and similarities between the Netherlands' and South African Twin Peaks model of financial regulation

4.1.1. Enabling legislation

As pointed above, the architecture legislation that introduced the Twin Peaks in the Netherlands is the Wet op het Financieel Toezicht (Wft) which was enacted in 2007, shortly before the GFC.

South Africa's Twin Peaks model, on the other hand, is still very young as it was introduced by the FRS Act in 2017. The FSR Act repealed/and or amended a plethora of legislation that impact the financial sector, and consequential amendments are continuing as phase II of Twin Peaks implementation is ongoing.

4.1.2. Differences between the two Twin Peaks models

The major difference between the Twin Peaks models of the Netherlands and South Africa is that prudential supervision of financial institutions (banks and non-banks) is the responsibility of DNB amongst its other functions, whereas the South African Twin Peaks model locates prudential supervision in the Prudential Authority which is a separate juristic entity located within the central bank. As indicated above, the rationale for allocating prudential supervision to DNB is that the Dutch authorities believed that the synergies between prudential and monetary policy issues, macroeconomic stability and financial stability could be leveraged within one entity.

Locating prudential supervision within the central bank inevitably means DNB is responsible for both macro and micro prudential supervision. The consolidation of both macro and micro supervision within the central bank is thus another distinguishing feature of the Netherlands Twin Peaks model that is different from the South African model. Within the South African Twin Peaks model the SARB has a micro-oversight function since it covers a wide range of economic and financial circumstances and information such as gross domestic product and inflation, the structure of a financial system and qualitative information on the institutional and regulatory framework. It is however easy for the SARB to have a holistic overview of the financial system because the PA is located within the SARB and the framework for information sharing is well defined and entrenched in legislation.

4.1.3. Similarities between the two Twin Peaks

Under the Twin Peaks models of both countries the market conduct regulator is established as a totally separate peak. In the Netherlands the AFM is responsible for market conduct regulation and supervision whilst in South Africa the FSCA performs this role. The AFM's objective is to promote an orderly and transparent market process in the Dutch financial markets, integrity of relations amongst market players and the protection of consumers. The South African FSCA is likewise responsible for enhancing and supporting the efficiency and integrity of financial markets, protecting financial customers and assisting in maintaining financial stability.

Furthermore, financial stability is the function of the central bank under both countries' Twin Peaks models. As mentioned above, for both countries this function was performed *de facto* by DNB and the SARB without being captured in legislation until both central banks were expressly granted this mandate by the Dutch Banks Amendment Act in 2014 and by the FSR Act in 2017 respectively.

A Financial Stability Committee was established in 2012 under the Dutch model to facilitate the promotion and maintenance of financial stability. Similarly in South Africa the Financial Stability Oversight Committee (FSOC) was established by the FSR Act to perform a host of functions all aimed at supporting the SARB in its mandate of promoting and maintaining financial stability.

Cooperation and collaboration is another key feature in both the Dutch and South African Twin Peaks models. As mentioned above, the 2007 Covenant that DNB entered into with the AFM facilitates their relationship including information sharing. The Covenant further provides for procedures for cooperation and coordination in regulation, supervision including licensing framework and supervisory inspections. This Covenant can be likened to the Memoranda of Understanding (MOU) that the PA and the FSCA have entered. The FSR Act has extensive provisions pertaining

to cooperation and collaboration on a number of aspects including issuing of joint standards, licencing framework, on-site supervisory inspections and investigations and information sharing. It can be argued that these provisions of the FSR Act are the bedrock of the South African Twin Peaks model as they are at the heart of its successful implementation.

There are a number of MOU's that have been entered into namely between (i) PA and FSCA, (ii) SARB and the PA, (iii) PA and NCR, (iii) SARB, PA, FSCA and FIC (iv) SARB and FSCA whereby these regulators undertake to cooperate and collaborate with each other in performing their respective roles and functions, matters of common interest and also on issues relating to financial stability.

Notably, the FSR Act does not require the Minister of Finance to enter into a Memorandum of Understanding with the SARB, unlike the case with the Dutch model whereby the Minister of Finance has entered into a Covenant with DBN which sets out procedures for management of financial crisis. However, there is an existing MOU that was entered into between the SARB and Minister of Finance pre Twin Peak pertaining to macro prudential aspects and although it is not a requirement of the FSR Act, this MOU needs to be revised to incorporate financial stability issues. In any event the Minister of Finance is responsible for the proper administration of the FSR Act and plays a central role in the South African financial system.

4.2. Lessons learnt from the experience with Twin Peaks in the Netherlands

The Netherlands Twin Peaks has done fairly well and the following are lessons that can be learned from its Twin Peaks model, namely that the effectiveness of a Twin Peaks model depends on:

- a) Explicit statutory requirement for the central bank to enter into a MOU with the Minister of Finance on their respective roles and responsibilities particularly in as far as financial stability is concerned.

- b) Explicit and deliberate capacitation of a Financial Stability Department whilst establishing various structures to support it.
- c) Strengthening of macro-prudential tools.

4.3. Final remarks

It is submitted that Twin Peaks is indeed the panacea for financial stability in South Africa, for the following reasons:

- a) Separation between prudential supervision and market conduct regulation and supervision has enabled the two regulatory peaks to focus on each regulator's particular objectives and mandate, thus reducing the risk of these objectives competing within a single agency, and multiplicity of financial obligations on financial institutions from various regulators.
- b) The central bank is able to focus on financial stability at a macro-level without being burdened by the day-to-day prudential supervision of the safety and soundness of financial institutions, which has been allocated as the focus area of the PA. Notably the SARB has a clear financial stability mandate as captured in the FSR Act which not only spells out its functions but also its powers in relation to systemic events and the designation of SIFIs. The Act also provides comprehensively for mandatory cooperation and collaboration between SARB and the financial sector regulators.
- c) A specific mandate is given to the FSCA for treating customers fairly, consumer protection, financial inclusion and financial literacy is key to the SA model of Twin Peaks given its historic inequality related to inter alia credit provision by financial institutions.
- d) Bringing the supervision of financial conglomerates under the PA will enable more attention to be paid to complex financial arrangements, products, and services which have been neglected in the past.
- e) The designation of SIFI's by the SARB and its ability to direct the PA to issue prudential standards to these institutions is pivotal as it recognises the importance of these institutions, the risks that they may pose and also signifies the importance of cooperation and collaboration which is one of the pillar/backbone of Twin Peaks.

4.4. Recommendations

South Africa's financial regulation is now institutionally sound and is in phase II of implementing Twin Peaks and it is crucial that the three peaks work seamlessly together in order to achieve their objectives. It is particularly of importance for the two Peaks (PA and FSCA), other regulators and organs of state consider their obligation to assist the SARB in promoting and maintaining financial stability in a very serious light.

It is recommended that for the optimal functioning of the SA Twin Peaks model, envisaged legislation arising out of the FSR Act e.g. Conduct of Financial Institutions Bill which was published for comments per National Treasury Media Release on 11 December 2018, and the Financial Sector Levies Bill (still in consultation stage) that are currently going through legislative processes, have to clearly spell out the roles and responsibilities of the SARB and each regulator, and not leave this delineation to be captured in subordinate legislation particularly where there is dual regulatory and supervisory roles such as licensing in order to avoid and minimise turf of wars.

It is further recommended that the Minister of Finance through National Treasury must play an additional coordinating role amongst regulators in all areas where there is likely to be duplication of roles in order to avoid regulatory arbitrage.

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