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TWIN PEAKS: THE SOUTH AFRICAN MODEL OF FINANCIAL REGULATION

by

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Ek mis Pa so baie!

SUMMARY

The Global Financial Crisis that unfolded between 2007 and 2009 was an eye opener for the need for stronger financial regulation. The Crisis highlighted the need for a well-regulated financial services sector, and specifically, the importance of risk management on a global scale. This forced countries all over the world to assess their respective financial regulation models. South-Africa was no exception.

Previously, South-Africa did not give priority to market conduct regulation and operated in an institutional framework that regarded banks, insurers and capital markets as separate classes. In view of this, when South Africa opted for a new model of financial regulation, it decided that the Twin Peaks model was best suited for the country since the model demanded, amongst others, a regulator that gives top priority to market conduct and consumer protection.

The different models of financial regulation are examined in this dissertation with particular focus on the Twin Peaks model of financial regulation. In addition, the dissertation considers the various components of the South-Africa Twin Peaks model. A comparison study of the Twin Peaks model of financial regulation that was adopted by the United Kingdom and the main components of that model is also interrogated herein. The purpose of this dissertation is to determine whether the Twin Peaks model is the appropriate model for South Africa and whether any guidance can be taken from the United Kingdom.

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Chapter One:
Background to the Study

1.1 Introduction

The period of significant stress experienced by the world's financial markets and banking institutions between 2007 and 2009 is referred to as the Global Financial Crisis ("GFC"). Since the Great Depression[1] of 1929, it was the worst financial catastrophe ever.[2]

Mishkin[3] divides the GFC into two phases: the first phase (August 2007 until August 2008) had its origin in the losses suffered in the residential mortgages space in the US financial system[4], the collapse of the insurance company AIG and the run on the Reserve Primary Fund money market fund all had a cascading effect that led to the second phase of Mishkin's theory about the GFC, namely the Lehman Brothers saga.[5] The bankruptcy of the investment bank, Lehman Brothers, in September 2008 was the largest catastrophe to hit the financial industry in the United States.[6] In the first half of 2008, Lehman Brothers' stock price decreased 73% in value and in September 2008 it was at a loss of 3.9 billion dollars.[7]

The GFC drew attention to the importance of a well-regulated financial services industry, and in particular, the significance of managing risks globally.[8] For failing to formulate adequate macro-prudential mechanisms in time to prevent the GFC, central banks and

[1] The Great Depression was the most important economic downturn in the United States in the twentieth century. The term "Great Depression" is commonly used to refer to the period of widespread contraction of economic activity that started in mid-1929 and lasted until 1933. See José *et al* "Life and death during the Great Depression" 2009 *PNAS* 17290.
[2] The National Treasury Policy Document "A Safer Financial Sector to Serve South Africa Better" 2011 https://www.treasury.gov.za/twinpeaks/20131211%20-%20item%202%20a%20safer%20financial%20sector%20to%20serve%20south%20africa%20better.pdf (accessed 24-06-2023) (hereinafter "A safer financial sector to serve South Africa better").
[3] Mishkin "Over the Cliff: From the Subprime to the Global Financial Crisis" 2011 *Journal of Economic Perspectives* (hereinafter "Mishkin 2011").
[4] Mishkin 2011 49.
[5] Mishkin 2011 49-50.
[6] Mawutor "The Failure of Lehman Brothers: Causes, Preventive Measures and Recommendations" 2014 *Research Journal of Finance and Accounting* 85.
[7] Ibid.
[8] "A Safer Financial Sector to Serve South Africa Better" 12.

financial regulators came under fire and a regulatory paradigm shift post GFC became inevitable.[9]

Prior to the GFC, regulation mostly focused on micro-prudential supervision. Supervisors were mostly concerned with the prudential soundness of individual institutions in their respective financial sectors as opposed to what was emerging in global jurisdictions.[10] It was wrongly assumed, by many, that a stable and sound financial system could be achieved by micro-prudential supervision only.[11] The GFC has, however, proved this perception to be wrong, because when a regulator focuses on micro-economic risks only, it may not notice macro-economic risks (for example, asset price bubbles such as the rise in household debt as was seen in the predicament in subprime mortgages in the US).[12] Regulators learnt the importance of also having a macro-prudential approach towards regulation of the financial system. This method further assists in identifying, and controls, risks emanating from multinational institutions that have substantial exposures to another.[13] If one of them experiences financial challenges, it would inevitably impact the others in the group, hence the bird's eye view of the financial system provided by macro-prudential regulation is of critical importance from a financial stability perspective.[14]

It became evident that prior to the GFC, most financial sectors, including South Africa, focused on prudential regulation and supervision and to a lesser extent on conduct of business regulation and supervision. The GFC has however proven the significance of prudential regulation and supervision to work in tandem with conduct of business regulation and supervision.[15]

In addition, regulatory weaknesses were identified by the IMF[16] as one of the contributors to the GFC. Central banks and financial regulators were criticised for failing to effectively

[9] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 2018 *JIBLR* 414.
[10] "A Safer Financial Sector to Serve South Africa Better" 12.
[11] "A Safer Financial Sector to Serve South Africa Better" 12.
[12] Ibid.
[13] "A Safer Financial Sector to Serve South Africa Better" 12.
[14] Ibid.
[15] "A Safer Financial Sector to Serve South Africa Better" 9-12.
[16] IMF Working Paper "Lessons and Policy Implications from the Global Financial Crisis" 2010 19 https://www.imf.org/external/pubs/ft/wp/2010/wp1044.pdf (accessed 06-11-2023) (hereinafter "IMF Working Paper").

regulate large, versatile and interlinked financial conglomerates – often referred to as "Too Big To Fail".[17] More stringent regulation of banks was implemented, especially for systemically important banks.[18]

As pointed out in the abovementioned IMF Working Paper, what started out as a financial crisis at a few financial institutions in 2008 turned into an autonomous crisis by 2010 with adverse effects on financial sectors globally.[19] To avoid the spread of a financial crisis, the GFC demonstrated that it is imperative that regulators should not only take appropriate regulatory action instantly, but they should also ensure that they globally coordinate regulatory action aimed at crisis-mitigation.[20]

The GFC also brought to light the staggering costs of an unregulated financial services industry.[21] Although the crisis did not destroy South Africa's financial institutions, the indirect impact resulting from job losses was catastrophic.[22] As a result, South Africa committed to the G-20[23] initiatives to review its financial regulatory framework approaches.[24]

1.2 The Main Approaches to Financial Regulation

The GFC has prompted countries to review their respective models of financial regulation and significant changes were made in some countries.[25] It was however not the first time that such a large-scale review was performed. History has proven that disruptions of financial markets are frequently followed by regulatory reforms.[26] Llewellyn notably

[17] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 414.
[18] CGFS Papers No 60 "Structural changes in banking after the crisis" 2018 10.
[19] IMF Working Paper 16.
[20] "A Safer Financial Sector to Serve South Africa Better" 13.
[21] "A Safer Financial Sector to Serve South Africa Better" 1-2.
[22] "A Safer Financial Sector to Serve South Africa Better" 2.
[23] Members of the G-20 are: Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Republic of Korea, Mexico, Russia, Saudi Arabia, South Africa, Turkiye, The United Kingdom, The United States, The African Union, and the European Union. See The G20 website at https://www.dfat.gov.au/trade/organisations/g20#:~:text=The%20members%20of%20the%20G20,Union%20and%20the%20European%20Union. (accessed 06-11-2023).
[24] "A Safer Financial Sector to Serve South Africa Better" 4.
[25] Llewellyn "Institutional Structure of Financial Regulation and Supervision: The Basic Issues" 2006.
[26] Group of Thirty "The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace" 2008 18.

remarks that the optimal model of financial regulation will vary from country to country as it is dependent on the financial system of each country.[27]

Despite the absence of a universal mutual model of financial regulation amongst all countries, Llewellyn has identified various universal financial regulation issues that need to be taken into account when considering a model of financial regulation for a country.[28] Firstly, consideration as to whether a country requires a single regulatory body overseeing the entire financial system or whether more than one regulatory body that oversees the system would be more prudent.[29] Secondly, whether prudential and business conduct oversight ought to be separated or combined under one regulatory body.[30] Thirdly, taking into account the central bank's role in the regulatory framework.[31] Fourthly, considering the objectives and functions of each regulator.[32] Fifthly, contemplating to what extent coordination between the different regulatory bodies would be needed. Sixthly, considering the extent of political interference in the regulatory framework.[33] Seventhly, assessing the different costs applicable to the different regulatory structures as well as evaluating the effect that the different structures would have on other regulators in its jurisdiction.[34] Lastly, consideration should be given to the independence and accountability of regulators.[35]

Llewellyn has further identified four categories of regulation and supervision that ought to be integrated in an institutional framework, namely: prudential regulation; systemic control and oversight to monitor the stability of the financial system overall, particularly the banking and payments system; consumer protection; and competition to guarantee that the financial system has a sufficient level of competition.[36]

[27] Llewellyn 2006 7.
[28] Llewellyn 2006 10.
[29] Ibid.
[30] Ibid.
[31] Ibid.
[32] Ibid.
[33] Ibid.
[34] Llewellyn 2006 10.
[35] Ibid.
[36] Llewellyn 2006 15.

There are several models of financial regulation, and the main approaches will be discussed below.

1.2.1 The Institutional Approach

This approach, adopted by Mexico and China, is also known as the “traditional”, “sectoral” or “silo” approach. The institutional approach is driven by the legal entity, meaning that an entity’s legal standing dictates within which regulator’s ambit if falls under from both a business conduct as well as a prudential perspective.[37] Simultaneously, using this approach, an entity's permitted business activities are also established.[38] However, regulators tend to broaden and reinterpret these activities resulting in entities with a variety of legal statuses to engage in such activities while still being subject to different requirements by various regulators.[39]

As observed by the Group of Thirty,[40] the drawback of the institutional approach is that it is based on a business model that, for the most part, is no longer in use.[41] Instead of the monoline activities of the past, many large financial institutions now engage in a cross-section of goods and services.[42] In fact, they frequently carry out business operations regardless of the legal standing of the companies in which the activity formally takes place or is documented for regulatory purposes.[43] This approach has difficulties with coordination and potential inconsistencies in the application of laws and regulations by the various regulators.[44]

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[37] Group of Thirty “The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace” 2008 24.
[38] “A Safer Financial Sector to Serve South Africa Better” 29.
[39] Group of Thirty “The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace” 2008 24.
[40] The current members of the Group of Thirty is: Daron Acemoglu, Andrew Bailey, Mark Carney, Agustin Carstens, Jaime Caruana, William C Dudley, Mohamed A El-Erian, Niall Ferguson, Arminio Fraga, Jason Furman, Timothy Geithner, Gita Gopinath, Philipp Hildebrand, Gail Kelly, Klaas Knot, Paul Krugman, Ngozi Okonjo-Iweala, Raghuram G Rajan, Maria Ramos, Carmen M Reinhart, Hélène Rey, Kenneth Rogoff, Tharman Shanmugaratnam, Lawrence H Summers, Tidjane Thiam, Adair Turner, Kevin Warsh, Axel A Weber, John C Williams, Yi Gang. See Group of Thirty https://group30.org/members (accessed 06-11-2023).
[41] Group of Thirty “The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace” 2008 34.
[42] Ibid.
[43] Ibid.
[44] Group of Thirty “The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace” 2008 34.

Given how much financial services companies and products have changed from their institutional labels - banking, insurance, and securities - the institutional approach may actually be the most challenging model of financial regulation to sustain.[45] It is conceivable that an activity will fall into the regulatory jurisdiction of another supervisor as regulators broaden the range of business that is permitted in a regulated legal entity.[46] At its worst, the Group of Thirty remarks that this may lead to regulators supervising nearly identical conduct under potentially different standards.[47] When there are obvious product overlaps, it has actually influenced regulators to embrace some functional features of supervision in at least some cases.[48] The Group of Thirty also observes that the institutional approach may be hampered by the lack of a single regulator with a comprehensive understanding of the operations of a regulated entity or of the market at large.[49] It additionally suffers from the lack of a single regulator that may impose measures intended to reduce systemic risk.[50]

1.2.2 The Functional Approach

In this approach, the legal status of an entity is disregarded, and supervisory oversight is determined purely by the nature of an institution's business.[51] In other words, institutions that are engaged in the same business types would be regulated by the same regulator and if an institution is, for example, engaged in various types of business, it would fall under the ambit of more than one regulator.[52] Italy, France and Spain are three countries that best demonstrate the functional approach to financial regulation.[53]

The advantage of the functional approach is that, regardless of the entity in which the activity is undertaken, the regulator will apply consistent rules to the same activity thus

[45] Group of Thirty "The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace" 2008 34.
[46] Ibid.
[47] Ibid.
[48] Ibid.
[49] Ibid.
[50] Ibid.
[51] Group of Thirty "The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace" 2008 24.
[52] Ibid.
[53] "A Safer Financial Sector to Serve South Africa Better" 29.

the incidence of regulatory arbitrage will be curtailed.[54] The Group of Thirty also remarks that the regulator may have a higher chance of attracting and retaining highly qualified subject matter experts who can interpret and apply applicable rules to the same duties across various legal entities since it is recognised as an expert regulator.[55]

Although this method seems to be effective, it might however be difficult to determine which kinds of activities are under the purview of a certain regulator, which can lead to regulatory arbitrage and turf wars.[56] Another important and related matter is that product innovation can be hindered by the functional approach as functional regulators compete for jurisdiction.[57]

A further disadvantage of this approach, identified by the Group of Thirty, is that financial institutions are forced to interact with several regulators, which can be more time-and effort-intensive.[58] The Group of Thirty remarks that it is common for multiple regulators to somewhat duplicate their efforts.[59] It points out that multiple regulators must spend a significant amount of time and effort coordinating and communicating with one another.[60] Multiple regulators may consequently act to gain favour with regulated entities by being more aggressive or permissive in ways that benefit the institutions as they compete for jurisdiction not only nationally but also internationally.[61] According to the Group of Thirty, some may contend that since there is no single, monolithic bureaucracy with ultimate decision-making power, regulatory competition can result in more effective outcomes. However, the chance of the opposite happening is also likely.[62]

A major drawback of the functional approach is the fact that no regulator has access to enough information about all of a particular entity's or entities' activities to monitor for

[54] Group of Thirty "The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace" 2008 35.
[55] Group of Thirty "The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace" 2008 35.
[56] "A Safer Financial Sector to Serve South Africa Better" 29.
[57] Group of Thirty "The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace" 2008 35.
[58] Ibid.
[59] Ibid.
[60] Ibid.
[61] Ibid.
[62] Ibid.

systemic risk.[63] In addition, in order to manage systemic risk, it may be necessary to have a single regulator with the capacity to order measures across the entire financial system.[64] In the view of the Group of Thirty, it is possible that no functioning regulator is able to take on that responsibility.[65]

1.2.3 The Integrated Approach

In the integrated approach there is a single universal regulator that oversees both the conduct of business and prudential regulation for all financial services.[66] This approach, that operates as a "mega-regulator", is implemented by Germany, Japan, Qatar and Singapore.[67] The United Kingdom ("UK") adopted this approach prior to transitioning to the Twin Peaks approach in 2012.[68] As pointed out by the Group of Thirty, this approach is only effective and eligible for smaller markets where regulation of the extensive range of financial services can be adequately controlled by a single regulator.[69]

The advantage of the mega-regulator approach is that it streamlines the focus on regulation while avoiding any potential conflicts over jurisdictional boundaries that could arise under either the institutional or the functional approach.[70] Furthermore, regulators have a complete view of the different business activities of an institution which enables the regulator to easily assess the risks related to fluctuating market conditions and regulatory arbitrage as these information will be collected and monitored by one regulator.[71]

Although this approach has its advantages, the Group of Thirty indicates that there may be disadvantages as well. Some observers believe it could increase the possibility of a

[63] Group of Thirty "The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace" 2008 35.
[64] Group of Thirty "The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace" 2008 35.
[65] Ibid.
[66] "A Safer Financial Sector to Serve South Africa Better" 29.
[67] Group of Thirty "The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace" 2008 14.
[68] Ibid.
[69] Ibid.
[70] "A Safer Financial Sector to Serve South Africa Better" 29.
[71] Ibid.

single regulatory failure point - there is no other regulator to potentially step in and fill the gap if an integrated regulator overlooks an issue.[72] In addition, there may be concern that an integrated regulator in a very large market would simply be too big and hence impractical to manage.[73] Consequently the Group of Thirty states that the operations of a large integrated regulator that oversees all business sectors will probably need to be separated into manageable functional or other business divisions.[74]

Another disadvantage of this approach is that it lacks regulatory competition between regulators which would ensure that they are compelled to outperform other regulators.[75] Also, prudential regulation, which entails "thinking like a banker," and market conduct regulation, which entails "thinking like a customer," are likely to clash.[76]

At times, effective market conduct regulation may lead to decreased profits - a prudential regulator may therefore be reluctant to enact regulations that could have a negative impact on profitability and solvency.[77] Furthermore, the single regulator in the integrated approach would have an excessive amount of control and influence, which is never an ideal situation.[78]

1.2.4 The Twin Peaks Approach

Michael W Taylor conceptualised and introduced the Twin Peaks model in 1995.[79] This approach is also known as “regulation by objective”.[80] The Twin Peaks model has since been adopted by Australia, Canada, the Netherlands, the UK, Belgium, Portugal and South Africa. Taylor proposed that financial services be regulated in such a way that the

[72] Group of Thirty “The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace” 2008 14.
[73] Group of Thirty “The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace” 2008 36.
[74] Ibid.
[75] Group of Thirty “The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace” 2008 37.
[76] “A Safer Financial Sector to Serve South Africa Better” 29.
[77] Ibid.
[78] Ibid.
[79] Taylor “Twin Peaks: A regulatory structure for the new century” Centre for the Study of Financial Innovation 1995.
[80] Group of Thirty “The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace” 2008 37.

stability of the whole financial system is protected (systemic protection) while protection of consumers is simultaneously ensured (consumer protection).[81]

The Twin Peaks model clearly distinguishes the regulatory roles of at least two "twin" (thus equal in prominence) regulators.[82] One regulator oversees the prudential regulation and the other one the conduct of business regulation.[83] According to Taylor, the Twin Peaks model would center on balancing the interests of the two peak regulators.[84] Each regulator would be committed to its exclusive goal of prudential and market conduct regulation and supervision, respectively, while simultaneously focusing on financial stability.[85] Therefore, appropriate and sufficient prudential and market conduct regulation must work together to support the promotion and preservation of financial stability.[86] The prudential safety, soundness, and market conduct of specific financial institutions must be regulated in these areas, but it is also crucial that financial institutions be subject to system-wide or macro-level regulation and supervision.[87]

Several persons consider the Twin Peaks model to be the ideal regulatory model because it equally and effectively encourages financial stability, consumer protection, transparency and market integrity.[88] As pointed out by Llewellyn, this approach is developed to preserve all the advantages from combining the two areas of oversight and regulation while reducing any potential shortcomings in the unified model.[89] According to Llewellyn, a benefit of the Twin Peaks approach is that the two regulators accountable for prudential and market behavior regulation are entirely committed to their own specific goals and powers.[90] He further points out that due to each regulator's clearly stated goals and duties, accountability is clear.[91] Another advantage highlighted by Llewellyn, is the

[81] Taylor "Twin Peaks: A regulatory structure for the new century" Centre for the Study of Financial Innovation 1995 1.
[82] "A Safer Financial Sector to Serve South Africa Better" 29.
[83] Ibid.
[84] Van Niekerk & van Heerden "The importance of a legislative framework for co-operation and collaboration in the Twin Peaks model of financial regulation" 2020 *The South African Law Journal* 109.
[85] Ibid.
[86] Van Niekerk & van Heerden" The importance of a legislative framework for co-operation and collaboration in the Twin Peaks model of financial regulation" 110.
[87] Ibid.
[88] "A Safer Financial Sector to Serve South Africa Better" 29.
[89] Llewellyn 2006 27.
[90] Llewellyn 2006 27.
[91] Llewellyn 2006 28.

fact that there is no danger of one regulator dominating the other. If conflicts emerge between them, it would probably be settled internally.[92] Schmulow also cites advantages of this model, including: the elimination of regulatory overlap and duplication; the promotion of an open, transparent, and accountable regulatory procedure; and the development of methods to resolve contradictions between the objectives of financial services regulation.[93]

Godwin *et al* remark that the Twin Peaks model nevertheless also has a number of perceived disadvantages.[94] Firstly, it might result in regulatory overlap with dual-regulated entities as it is expected that the two regulators would have their own separate mandates and objectives.[95] Secondly, there is a risk that proper and effective coordination and cooperation between the regulators will be absent, which could have adverse consequences.[96] Although these risks can be controlled by robust coordination and communication mechanisms, it continues to be a top concern for countries that have implemented this approach.[97] Lastly, a conflict of interest within the central bank could exist. This can occur if the central bank oversees both monetary policy and prudential regulation.[98]

1.3 Research Statement

In 2017, South Africa implemented the Twin Peaks model of financial regulation as introduced by the Financial Sector Regulation Act ("FSR Act").[99] The object of the FSR Act is to create a stable financial system that serves the needs of financial customers and promotes balanced, sustainable financial growth by establishing a framework that encourages, amongst others, financial stability, safety and soundness of financial

[92] Llewellyn 2006 28.
[93] Van Niekerk & van Heerden "The importance of a legislative framework for co-operation and collaboration in the Twin Peaks model of financial regulation" 110.
[94] Godwin, Li & Ramsay "Is Australia's 'Twin Peaks' System of Financial Regulation a Model for China?" 2016 Centre for International Finance and Regulation Working Paper No. 102/2016 6 https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2763300 (accessed 09-08-2023) (hereinafter "Godwin, Li & Ramsay").
[95] Godwin, Li & Ramsay 6-7.
[96] Godwin, Li & Ramsay 7.
[97] Ibid.
[98] Ibid.
[99] Financial Sector Regulation Act 9 of 2017.

institutions, fair treatment of customers, integrity of the financial system, combatting financial crime, financial inclusion and assurance in the financial system. Two new regulators were established by the FSR Act. Firstly, the Prudential Authority ("PA"), whose responsibility is to supervise and regulate the safety and soundness of financial institutions and market infrastructures and assist the South African Reserve Bank ("SARB") in promoting financial stability.[100]

Secondly, the Financial Sector Conduct Authority ("FSCA"), whose responsibility is to supervise and regulate the market conduct of financial institutions whilst also assisting the SARB in promoting financial stability. The aim of this dissertation is to inquire why this model was chosen as the suitable model of financial regulation in South Africa. In doing so, the main features of the Twin Peaks model in South Africa will be considered. As a comparative reference, this dissertation will also study the Twin Peaks model that was implemented in the UK and consider whether South Africa can take any guidance from the UK model that could augment the South African model.

1.4 Research Objectives

In order to assess the Twin Peaks model in South Africa and benchmark it against the UK model, the following research questions will be interrogated:

(a) What is the Twin Peaks model of financial regulation, where was it first pioneered and what are its advantages and disadvantages?

(b) What are the main institutional components of the Twin Peaks model in South Africa and what are their respective objectives, mandates and toolkits?

(c) When and why did the UK transition to the Twin Peaks model and how does their model compare with the South African model?

(d) Is the Twin Peaks model of financial regulation in South Africa the appropriate model and can South Africa take any guidance from the UK?

1.5 Research Methodology

[100] Section 33 of the FSR Act.

The literature study undertaken in this dissertation will be a critical doctrinal desktop study comprising of policy documents, legislation, websites, chapters in books and journal articles.

1.6 Selection of Comparative Jurisdictions

The Twin Peaks model of the UK, having been introduced in 2013. precedes that of South Africa and will be compared with the South African Twin Peaks model to determine whether the South African version is the appropriate model for the country's approach to financial regulation. Notably the UK's move to a Twin Peaks model was occasioned by the failure of its previous model of financial regulation. In 1997 the UK transitioned to an integrated model of financial regulation where the former Financial Services Authority ("FSA") was a "mega-regulator" responsible for both market conduct and prudential regulation and supervision.[101] In 2012, as a result of the failure of its model of financial regulation during the 2008 GFC, the UK adopted the Twin Peaks approach where the prudential and conduct of business regulation and supervision were split between two regulators, namely the Prudential Regulation Authority ("PRA") and the Financial Conduct Authority ("FCA").[102] It is possible to draw important conclusions from them given that the UK implemented Twin Peaks five years before South Africa and has accumulated experience that can yield valuable guidance for South Africa.

1.7 Chapter Lay-Out

Chapter One is the roadmap to the study and serves as an introduction to the dissertation. It provides a summary of the regulatory weaknesses that were identified as contributors to the GFC. To contextualise the study, it provides the primary financial regulatory models and outlines each model's advantages and disadvantages. It further sets out the research statement, research methodology, selection of the comparative jurisdiction and chapter layout.

[101] Qumba "A Comparative Analysis of the Twin Peaks Model of Financial Regulation in South Africa and the United Kingdom" 2022 *The South African Law Journal* 88 (hereinafter "Qumba 2022").
[102] Qumba 2022 91.

Chapter Two will focus on the Twin Peaks model that was adopted in South Africa in 2017. The main institutional components of this model in South Africa will be considered and the role of the central bank will also be discussed. This chapter will consider the objectives, mandates and toolkits of the FSCA as market conduct regulator and will also consider the co-operation and collaboration between the various role players in the South African financial system.

Chapter Three will provide a comparative study of the UK's adoption of the Twin Peaks model of financial regulation. It will explore the reasons for the UK's decision to change from an integrated model of regulation to a Twin Peaks approach. A brief summary of the roles and functions of the two regulators in the UK, the PRA and the FCA as well as of the FPC, a sub-committee of the Bank of England, will also be provided in this chapter. The chapter will further consider the co-operation and collaboration between the various role players in the UK's financial system.

Chapter Four is the final chapter of the study and includes conclusions drawn regarding the Twin Peaks approach adopted by South Africa as well as guidance taken from the UK that may serve as measures for improvement of the South African model.

Chapter Two:

The Twin Peaks Model of Financial Regulation in South Africa

2.1 Introduction

As pointed out in Chapter One, the GFC has forced countries to evaluate and restructure their financial regulatory systems, and South Africa was the first developing African country to make the shift from a silo segmented model of financial regulation to a Twin Peaks model of regulation.[103] This was as a result of the expanded post-GFC financial stability mandate on regulators to provide an ideal institutional and legislative framework for financial regulation.[104] Despite the fact that South Africa had weathered the GFC relatively well with its preceding sectoral model, it was nevertheless considered that the country could be producing far better outcomes for customers and required reform that emphasise effective prudential and market conduct supervision.[105] Consequently, the reason for the reform of its approach to financial regulation was to align South Africa's financial system with global financial regulation tendencies that had arisen in the wake of the GFC.[106]

In a policy document issued by the National Treasury of South Africa ("Treasury") in 2011, titled "A Safer Financial Sector to Serve South Africa Better", Treasury identified financial regulatory reform as a necessity and proposed the Twin Peaks model of financial regulation for South Africa.[107] In 2013, Treasury issued a further policy document, titled "Implementing a Twin Peaks model of Financial Regulation in South Africa", indicating

[103] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 415.
[104] Ibid.
[105] The National Treasury Explanatory Policy Paper accompanying the First Draft of the Conduct of Financial institutions Bill December 2018 "A Stronger Market Conduct Policy Framework for South Africa" 6
https://www.treasury.gov.za/twinpeaks/CoFI%20Bill%20policy%20paper.pdf
(accessed 21-08-2023) (hereinafter "A Stronger Market Conduct Policy Framework for South Africa") & Qumba 85.
[106] Qumba 85.
[107] "A Safer Financial Sector to Serve South Africa Better" 23 & 28.

the intended process going forward in respect of prudential and market conduct supervision.[108]

Prior to introducing the Twin Peaks model, South Africa functioned under an institutional approach.[109] Lack of cooperation in regulation was also a defining characteristic during that period.[110] Furthermore, the central bank of South Africa, the SARB, functioned within a silo model of financial regulation within which several regulators, each tasked with overseeing specific financial institutions, operated.[111] Preceding Twin Peaks, the SARB performed the traditional role of a central bank, i.e. it was tasked with the execution of monetary policy, it supervised banks and it was also responsible for supervision of the payments and settlement system as well as bank supervision.[112] The bank was also regarded as the lender of last resort.[113] In keeping with the prevailing tendency at the time, the SARB also had a financial stability mandate that, since it was implied by its role as central bank, was carried out *de facto* and not enshrined in legislation.[114] The SARB was basically responsible for maintaining financial stability in South Africa whilst the erstwhile Financial Services Board ("FSB"), regulated the non-bank financial industry.[115] The FSB supervised the non-bank financial sector by virtue of twelve distinct pieces of

[108] National Treasury, "Implementing a Twin Peaks Model of Financial Regulation in South Africa" 2013 3 https://www.treasury.gov.za/twinpeaks/20131211%20-%20item%203%20roadmap.pdf (accessed 26-06-23) (hereinafter "Implementing a Twin Peaks model of financial regulation in South Africa").
[109] Schmulow "Financial Regulatory Governance in South Africa: The Move Towards Twin Peaks" 2017 *African Journal of International and Comparative Law* 401 (hereinafter "Schmulow").
[110] Schmulow 401.
[111] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 415.
[112] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 415.
[113]. To act as the lender of last resort means making commitments to lend in order to stave off or contain systemic distress. See Tucker "The Lender of Last Resort and Modern Central Banking: principles and reconstruction" 2014 *BIS Papers* 11.
[114] Section 10 of the South African Reserve Bank Act 90 of 1989 & Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 415.
[115] Schmulow 402.

legislation.[116] However, as stated by van Heerden and van Niekerk, this isolated sectoral approach led to an insufficient and incoherent financial regulatory framework.[117]

Historically, market conduct regulation in South Africa did not get the attention it required.[118] The Twin Peaks model was therefore most appropriate for South Africa because it demanded a regulator that also placed emphasis on consumer protection.[119] It was also believed at the time, that moving towards this model would cause the least negative impact and least detrimental effects in the market.[120]

Although South Africa was the first African country to implement the Twin Peaks model, Australia successfully pioneered the model in 1998 and the Netherlands was the first European country to adopt the model shortly before the GFC that unfolded between 2007 and 2009. The Crisis highlighted the need for a well-regulated financial services sector, and specifically, the importance of risk management on a global scale. This forced countries all over the world to assess their respective regulation models. South-Africa was no exception.

Previously, South-Africa has not given priority to market conduct regulation and operated in an institutional framework that regarded banks, insurers and capital markets as separate classes. In view of this, South-Africa has decided that the Twin Peaks model was best suited for the country since it demanded, amongst others, a regulator that gives top priority to market conduct and consumer protection.

As stated in Chapter One, the purpose of this dissertation is to determine whether the Twin Peaks model is the appropriate model for South Africa and whether any guidance

[116] These Acts are: the Collective Investment Schemes Control Act 45 of 2002; Credit Rating Services Act 24 of 2002; Financial Advisory and Intermediaries Services Act 37 of 2002; Financial Institutions (Protection of Funds) Act 28 of 2001; Financial Services Board Act 97 of 1990; Financial Services Ombud Schemes Act 37 of 2004; Financial Supervision of the Road Accident Fund Act 8 of 1993; Friendly Societies Act 25 of 1956; Inspection of Financial Institutions Act 80 of 1988; Long-term Insurance Act 52 of 1998; Pension Funds Act 24 of 1956; Short-term Insurance Act 53 of 1998. See Schmulow 402.
[117] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 415.
[118] "A Safer Financial Sector to Serve South Africa Better" 29.
[119] Ibid.
[120] Ibid.

can be taken from the UK.[121] The Twin Peaks model's popularity can be attributed, in part, to the fact that the model was adopted by Australia and the Netherlands prior to the GFC, and they were generally regarded to have had a "good crisis" as a result of the strengthened financial regulation introduced by their Twin Peaks.[122] Interesting to note is that the Twin Peaks model has various permutations: for example, the main difference between the Twin Peaks models in Australia and South Africa is that the PA in South Africa operates under the same roof as the central bank (SARB), although as a separate legal entity, as opposed to Australia where the Australian prudential authority (APRA) is a complete independent entity.[123]

Following an extended regulatory journey that started in 2007 and intensified in 2011, the FSR Actwas enacted and served as the framework that introduced South Africa's Twin Peak's model.[124] The objectives of the FSR Act, as set out in section 7 thereof, is to achieve a stable financial system in the interests of financial clients and supports economic growth by establishing a framework that promotes, amongst others, financial stability, safety and soundness of financial institutions, fair treatment of customers, integrity of the financial system, combatting financial crime, financial inclusion and confidence in the financial system. Financial institutions rendering financial products[125] and services[126] are subject to the FSR Act and the Minister of Finance ("Minister") is responsible for its administration.[127]

2.2 The main institutional components of the South African Twin Peaks Model

As the name indicates, the Twin Peaks model of financial regulation means that two independent peaks of regulatory bodies are established, one to oversee the safety and soundness (prudential oversight) in the financial system and the other to oversee conduct

[121] Van Niekerk *A comparative Analyses of the Role of the Central Bank in Promoting and Maintaining Financial Stability in South Africa* (LLD-thesis, University of Pretoria 2018) Chapters 1 and 3 respectively.
[122] "Implementing a Twin Peaks Model of Financial Regulation in South Africa" 23.
[123] Schmulow 414.
[124] Van Niekerk & van Heerden "The Importance of a Legislative Framework for Co-operation and Collaboration in the Twin Peaks Model of Financial Regulation" 111.
[125] See definition in section 1 of the FSR Act.
[126] See definition in section 1 of the FSR Act.
[127] Section 8 of the FSR Act.

of business in the system (market conduct oversight).[128] However, Qumba remarks that in the South African environment, the phrase "Twin Peaks" is misleading because the SARB is regarded as an additional (and apex) "peak".[129] Van Heerden and van Niekerk are also of the view that the South African Twin Peaks model should rather be seen as a three-peak model:[130] the SARB as the central bank, and the two newly established twin regulators, the FSCA[131] and the PA,[132] with other financial regulators such as the National Credit Regulator ("NCR") also being part of the Twin Peaks model although they have not been assimilated into the PA and FSCA but function independently.[133]

Therefore, contrary to Taylor's original conceptualisation of the Twin Peaks model, the South African model is not a "pure" Twin Peaks model.[134] Be that as it may, the reform of regulation towards a Twin Peaks model aims to enhance outcomes by giving equal and dedicated focus on managing key risks facing the South African financial sector.[135] In the first phase of the reform process, regulators function within the confines of the FSR Act's legislative framework, and the existing financial sector laws.[136] The FSR Act is therefore regarded as an addition to the existing financial sector laws and provides the overall architecture of the South African Twin Peaks model.[137] These existing laws continue to be in effect, enabling the regulators to regulate and oversee the industry in accordance with both the FSR Act and existing legislation.[138] The Act improves consistency in regulatory operations, but it is only a first step towards comprehensive full-scale legislative reform.[139] From the perspective of market conduct, the next phase in the reform process will be to restructure and harmonise the legislative environment that financial institutions will operate in.[140] This entails a comprehensive assessment of the current

[128] Schmulow 393.
[129] Qumba 80.
[130] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 416.
[131] Established in terms of section 56 of the FSR Act.
[132] Established in terms of section 32 of the FSR Act.
[133] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 417.
[134] Qumba 80.
[135] "A Stronger Market Conduct Policy Framework for South Africa" 7.
[136] Ibid.
[137] Ibid.
[138] Ibid.
[139] Ibid.
[140] Ibid.

financial sector laws, with the aim of formulating a single, complete legal framework for market conduct regulation in South Africa that is consistently applied to all financial institutions.[141] This single legal framework is currently being developed in the Conduct of Financial Institutions Bill[142] ("COFI") that is yet to be enacted.

2.2.1 The Role of the PA

A very significant change introduced by the South African Twin Peaks model is that the PA took over the mandate from the SARB's erstwhile Bank Supervision Department to supervise and regulate banks.[143] The PA, one of the twin regulators, is established in terms of section 32 of the FSR Act and is responsible for prudential regulation and supervision and operates as a juristic entity under the administration support of the SARB.[144] The rationale for the SARB to provide administrative support to the PA was to facilitate the sharing of resources, including IT systems and other resources, in order to reduce expenses.[145] It was motivated by the SARB and the PA's desire for a simple way to collaborate and share information.[146] Consequently, the Deputy Governor, a key officer of the SARB, is now in charge of the PA as its CEO.[147] It is significant that the PA is a juristic person since it demonstrates that the PA has an independent legal status from the SARB - in other words, it operates independently from the SARB despite being housed in the same building.[148] However, Qumba queries the degree of independence between the SARB and the PA.[149] He claims that even though the PA is under the administration of the SARB, it can be argued that the FSR Act should accord the PA and the SARB equal standing.[150] He continues to state that these two entities are independent legal

[141] "A Stronger Market Conduct Policy Framework for South Africa" 7.
[142] Conduct of Financial Institutions Bill 2020 https://www.treasury.gov.za/public%20comments/2020%2010%2008%20CoFI%20Bill%20(version%20published%20for%20comment)%20(slightly%20updated).pdf (accessed 07-11-2023)
[143] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 416.
[144] Section 32 of the FSR Act.
[145] Qumba 96.
[146] Qumba 96.
[147] Section 36(1) of the FSR Act.
[148] Godwin, Howse & Ramsay "Twin Peaks: South Africa's Financial Sector Regulatory Framework" 2017 *SALJ* 673.
[149] Qumba 101.
[150] Qumba 101.

identities in law, indicating the institutional and operational independence of the PA from the SARB.[151]

The PA has an overall governance objective of managing its affairs in an efficient and effective way and is required to have regard to internationally accepted standards.[152] The PA's objectives are to promote and improve the safety and soundness of financial institutions providing financial products and securities services as well as those of market infrastructures.[153] It also has the obligation of safeguarding financial customers against the possibility that financial institutions will not fulfill their obligations.[154] Finally, the PA must contribute to maintaining financial stability.[155] In this regard, prudential supervision and regulation comprises of both macro- and micro-prudential features.[156]

In order to fulfill its objectives, the PA is mandated to regulate and supervise financial institutions that provide financial products or securities services, and market infrastructures.[157] It must also co-operate with the SARB, the FSCA, the Financial Stability Oversight Committee ("FSOC") (as discussed in more detail later herein), the Financial Intelligence Centre ("FIC") and the NCR, as and if, required by the FSR Act.[158] The PA is also mandated to co-operate with the Council for Medical Schemes regarding common interest matters.[159] In addition, the PA must support competition in the provision of financial products and financial services, which includes collaborating with the Competition Commission.[160] The PA is also obliged to support financial inclusion and to perform and publish research relevant to its objective.[161] Lastly, the PA is mandated to

[151] Qumba 101.
[152] Godwin, Howse & Ramsay "Twin Peaks: South Africa's Financial Sector Regulatory Framework" 676 & section 35 of the FSR Act.
[153] Section 33 of the FSR Act.
[154] Section 33 of the FSR Act.
[155] Section 33 of the FSR Act.
[156] "Implementing a Twin Peaks Model of Financial Regulation in South Africa" 6-7. It was pointed out that "the term 'macroprudential' regulation or supervision refers to the analysis of strengths and vulnerabilities of financial systems as a whole (systemic risk). Macroprudential assessments covers a wide range of economic and financial circumstances and information, such as gross domestic product growth and inflation, the structure of a financial system, and qualitative information on the institutional and regulatory framework. The term 'microprudential' refers to the safety and soundness of individual financial institutions."
[157] Section 34 of the FSR Act.
[158] Section 34 of the FSR Act.
[159] Section 34 of the FSR Act.
[160] Section 34 of the FSR Act.
[161] Section 34 of the FSR Act.

regularly assess the scope of financial sector regulation to mitigate identified risks in achieving its objective or functions.[162]

The PA is given a comprehensive regulatory toolkit to help it further its objectives. Firstly, the PA is empowered to make prudential standards for financial institutions, market infrastructures and key persons of such institutions.[163] The standards are aimed to ensure the safety and soundness of those financial institutions, to reduce the risk that those institutions might engage in conduct that amounts to financial crime and to assist in maintaining financial stability.[164] It should be noted that the PA also has the authority to collaborate with the FSCA to make joint standards on any subject for which any of them has the authority to do so.[165] Another regulatory tool afforded to the PA is the power to grant, refuse, vary, suspend and revoke a license.[166] A person may thus not provide a financial product, financial service or market infrastructure unless it has been issued with a licence.[167]

The PA also has the right to request anyone to provide specific data or a specific document that will help it carry out its duties.[168] The PA is further entitled to conduct supervisory on-site inspections at a supervised entity's business premises.[169] These inspections will typically be conducted to examine compliance with the financial laws for which the PA is responsible for.[170] It might also help the PA in assessing the extent of the risk posed by the institution of contraventions of a law for which the PA is in charge of.[171] In line with Constitutional imperatives, the FSR Act provides that the affected person's right to privacy,[172] freedom,[173] and other constitutional rights must be strictly observed during an inspection and further that decency must be observed and good order must be

[162] Section 34 of the FSR Act.
[163] Section 105 of the FSR Act.
[164] Section 105 of the FSR Act.
[165] Section 107 of the FSR Act.
[166] Chapter 8 of the FSR Act.
[167] Sections 111 and 162 of the FSR Act.
[168] Section 131 of the FSR Act.
[169] Section 132 of the FSR Act.
[170] Section 132 of the FSR Act.
[171] Section 132 of the FSR Act.
[172] Section 14 of the Constitution of the Republic of South Africa 1996 (hereinafter "the Constitution").
[173] Chapter 2 of the Constitution.

applied at all times.[174] In addition, the PA is empowered to conduct investigations if it has reason to believe that a person contravened any provision of a law for which the PA is responsible or that the investigation is necessary to accomplish the objectives of the PA's mandate.[175]

The FSR Act also provides the PA with several other enforcement tools, such as the issuing of guidance notices, interpretation rulings, directives, enforceable undertakings and debarments orders.[176] The purpose of a guidance notice is to provide assistance on how a sector law should be applied. They are not binding as they are intended for information purposes only.[177] An interpretation ruling is a statement that is made public regarding the interpretation of a specified provision of a law, in the context of the circumstances set out in the statement.[178] The purpose of these rulings is therefore aimed at encouraging consistency, clarity and assurance in the interpretation of the relevant laws.[179]

A directive may be issued by the PA to a financial institution that provides a financial product or securities services, or that is a market infrastructure, or to a key person of a financial institution.[180] A directive is issued if a financial institution's business is conducted improperly and there is a risk that the institution will not be able to fulfill its obligations.[181] It can also be issued when the financial institution or one of its key persons has contravened or is likely to contravene a provision of an act for which the PA is accountable for.[182] A directive may further be issued in the event that a financial institution or one of its key persons has failed to comply with an enforceable undertaking, is engaged or likely to be engaged in financial crime or is causing or contributing to the financial system's instability.[183]

[174] Section 132(3) of the FSR Act.
[175] Section 135 of the FSR Act.
[176] Chapter 10 of the FSR Act.
[177] Section 141 of the FSR Act.
[178] Section 141 of the FSR Act.
[179] Section 142 of the FSR Act.
[180] Section 143 of the FSR Act.
[181] Section 143 of the FSR Act.
[182] Section 143 of the FSR Act.
[183] Section 143 of the FSR Act.

Enforceable undertakings occur when a person or institution who has been non-compliant with a financial sector law overseen by the PA, provides the PA with a written undertaking regarding their future conduct in respect to a matter regulated by a law for which the PA is accountable for.[184] As soon as the PA acknowledges the undertaking, the PA is able to enforce it.[185] Lastly, debarment orders may be made in respect of a natural person if such person has contravened a financial sector law, an enforceable undertaking or a law in a foreign country that corresponds to a financial sector law.[186] A person may also be debarred if the person has attempted or induced another person to contravene a financial sector law in a material way.[187]

2.2.2 The Role of the FSCA

Regulation of market conduct is essential because financial institutions are typically more qualified than consumers in evaluating the quality of financial products and are more educated on the range of available services.[188] Unfortunately, Treasury pointed out that this can create the incentive for financial institutions to exploit their superior information.[189] Regulation of market conduct prevents such abuses and also supports prudential objectives.[190] In addition, market conduct regulation endeavors to prevent, and manage (when prevention is not possible) the adverse effects resulting from financial institutions conducting their business in harmful ways or in ways that weaken the integrity of financial markets and confidence in the financial system.[191] The enactment of the FSR Act in 2017 through which the FSCA was established, was the first step taken to comprehensively strengthen market conduct in South Africa. As was alluded to above, from the perspective of market conduct, the next step in the reform process will be to restructure and harmonise the legislative environment by developing a single, complete legal framework for market conduct regulation in South Africa that is consistently applied to all financial institutions.[192]

[184] Section 151 of the FSR Act.
[185] Section 151 of the FSR Act.
[186] Section 153 of the FSR Act.
[187] Section 153 of the FSR Act.
[188] "A Safer Financial Sector to Serve South Africa Better" 39.
[189] "A Safer Financial Sector to Serve South Africa Better" 39.
[190] "A Safer Financial Sector to Serve South Africa Better" 40.
[191] "A Stronger Market Conduct Policy Framework for South Africa" 2.
[192] "A Stronger Market Conduct Policy Framework for South Africa" 7.

As such, the proposed COFI Act[193] would not only replace conduct provisions in existing financial sector laws such as the Financial Advisory and Intermediary Services Act,[194] but would contribute to a consistent, robust and effective legislative framework for market conduct for all financial institutions executing financial activities.[195]

As alluded to above, South Africa is developing a new framework for market conduct policies as part of its reform of financial sector regulation towards a Twin Peaks model.[196] The COFI Bill is a critical component in this reform process that seeks to entrench better financial customer outcomes in the South Africa financial industry.[197] The Bill seeks to dramatically streamline the legal framework for conduct regulation in the financial services industry by taking a principles-based rather than a rules-based approach, and give the market conduct policy approach, including application of the "Treating Customers Fairly"[198] principles, statutory impact.[199]

The FSCA is established in terms of section 56(1) of the FSR Act. Similar to the PA, the FSCA is also an independent juristic person.[200] However, the FSCA, as opposed to the PA which is housed within the same building as the SARB, operates outside the SARB and is the market conduct regulator responsible for the supervision and regulation of conduct of business activities and practices of financial institutions.[201] The FSCA is a national public entity[202] and may charge fees, in accordance with Part 1 of Chapter 16 of the FSR Act, to fund the performance of any functions under the FSR Act, the relevant financial sector laws and the Financial Sector and Deposit Insurance Levies Act ("Levies

[193] The first draft of the Conduct of Financial Institutions Bills was published for public comment during December 2018 and the second draft was published for comment during September 2020.
[194] Financial Advisory and Intermediary Services Act 37 of 2002.
[195] "A Stronger Market Conduct Policy Framework for South Africa" 4.
[196] "A Stronger Market Conduct Policy Framework for South Africa" 6.
[197] Media Statement that was issued by Treasury that was published with the second draft of the Conduct of Financial Institutions Bill on 29 September 2020 1.
[198] "Treating Customers Fairly" is an outcomes based regulatory and supervisory approach designed to ensure that regulated financial institutions deliver specific, clearly set out fairness outcomes for financial customers. FSCA https://www.fsca.co.za/Regulatory%20Frameworks/Pages/Treating-customers-fairly.aspx (accessed 07-11-2023).
[199] Media Statement that was issued by Treasury that was published with the second draft of the Conduct of Financial Institutions Bill on 29 September 2020 1.
[200] Section 56 of the FSR Act.
[201] Godwin, Howse & Ramsay "Twin Peaks: South Africa's Financial Sector Regulatory Framework" 675 & section 56 of the FSR Act.
[202] Section 56(2) of the FSR Act.

Act")[203].[204] The FSCA is further empowered to impose levies, in accordance with Part 1 of Chapter 16 of the FSR Act read with the Levies Act, to fund its operations, and in the case of the deposit insurance levy, to fund the operations of the Corporation[205] and the administration of the Fund[206] in terms of section 166BC of the FSR Act.

The FSCA has the same overall governance objective as the PA of managing its affairs in an efficient and effective way and is required to have regard to internationally accepted standards.[207] One of the FSCA's objectives is to improve and support the efficiency and integrity of financial markets.[208] Treasury indicated that in order to safeguard investors and maintain the effectiveness and integrity of financial markets, a regulator has to stay abreast of changes in the financial markets.[209] Treasury pointed out that disregard for regulation, improper trading practices, market manipulation and fraudulent practices will threaten confidence in South Africa's financial markets.[210]

Another objective of the FSCA is that it must protect financial customers by promoting fair treatment of customers by financial institutions.[211] The FSCA is further obliged to safeguard financial customers by providing them with consumer education programs that will enable them to make decisions that are financially sound.[212] To accomplish this objective, effective consumer protection regulations must be in place to mitigate the risks associated with the knowledge asymmetry among financial institutions and their customers.[213] Last but not least, it is important to note, as alluded to above, that both the PA and the FSCA's objectives explicitly provide that they must assist the SARB in maintaining financial stability.[214] This they will do by carrying out their respective

[203] Financial Sector and Deposit Insurance Levies Act 11 of 2022.
[204] Section 237(1) of the FSR Act.
[205] As defined in section 1 of the FSR Act.
[206] As defined in section 1 of the FSR Act.
[207] Godwin, Howse & Ramsay "Twin Peaks: South Africa's Financial Sector Regulatory Framework" 676 & section 59 of the FSR Act.
[208] Section 57 of the FSR Act.
[209] "Implementing a Twin Peaks Model of Financial Regulation in South Africa" 52.
[210] "Implementing a Twin Peaks Model of Financial Regulation in South Africa" 52.
[211] Section 57 of the FSR Act.
[212] Section 57 of the FSR Act.
[213] "Implementing a Twin Peaks Model of Financial Regulation in South Africa" 52.
[214] Section 57 of the FSR Act.

mandates effectively and efficiently and by cooperating and collaborating with the SARB as envisaged in sections 17,[215] 18,[216] 26[217] as well as section 76[218] of the FSR Act.

In order to achieve its objective, the FSCA is mandated by the FSR Act to regulate and supervise, in concord with the numerous financial sector laws, the financial institutions' market conduct.[219] The FSCA is also required to co-operate with the SARB, the FSOC, the FSCA, the NCR and the FIC, as, and if, required in terms of the FSR Act, or with the Council for Medical Schemes when dealing with matters of mutual concern.[220] The FSCA is additionally mandated to promote competition when it provides financial products and financial services. This function includes the duty on the FSCA to co-operate and collaborate with the Competition Commission.[221] The FSR Act further obliges the FSCA to support financial inclusion.[222] As stated by Treasury, financial inclusion means ensuring that all South Africans have appropriate access to financial services in order for them to manage their money properly, save for the future, and obtain insurance to protect themselves from unanticipated events.[223] According to Treasury, the FSCA would contribute to the financial inclusion objective by implementing consumer protection regulations and promoting financial literacy amongst consumers.[224] Treasury indicated in their report that the FSCA would furthermore implement, supervise and enforce specific inclusion frameworks.[225]

In terms of the FSR Act, the FSCA must also regularly assess the extent of financial sector regulation to mitigate identified risks in achieving its objectives and must also

[215] Section 17 of the FSR Act deals with the responsibilities of the FSCA and the PA to provide the SARB with information which may assist the bank to manage the systemic event and to consult the SARB before exercising any of their powers in a way that may compromise steps taken to manage the systemic event.
[216] In terms of section 18 of the FSR Act, the FSCA and the PA may be directed to provide the SARB with information specified in the directive which the SARB needs for exercising its powers in relation to systemic events.
[217] Section 26 of the FSR Act deals with co-operation and collaboration requirements of the FSCA, PA and the SARB in relation to financial stability.
[218] Section 76 of the FSR Act sets out co-operation and collaboration requirements between the FSCA, PA and the SARB when they perform their functions in terms of the financial sector laws, the National Credit Act, and the Financial Intelligence Centre Act.
[219] Section 58(1)(a) of the FSR Act.
[220] Sections 58(1)(b) & (c) of the FSR Act.
[221] Section 58(1)(d) of the FSR Act.
[222] Section 58(1)(e) of the FSR Act.
[223] "Implementing a Twin Peaks Model of Financial Regulation in South Africa" 53.
[224] "Implementing a Twin Peaks Model of Financial Regulation in South Africa" 54.
[225] "Implementing a Twin Peaks Model of Financial Regulation in South Africa" 54.

perform and publish research relevant to its objectives.[226] Finally, the FSCA is also required to develop and implement policies and programs for financial education for the general public and monitor the degree to which the financial system complies with fair outcomes for customers.[227] It is interesting that both the PA and the FSCA have a responsibility to carry out their duties "without fear, favor, or prejudice".[228] These provisions might have been included in an effort to address concerns in other countries, such as the UK, as discussed later herein in Chapter 3, where the regulator appeared to be unwilling to take regulatory action.[229] It is further worth noting that the aforementioned functions are not absolute. In terms of section 58(4) of the FSR Act, the FSCA may take any other action reasonably necessary to accomplish its objectives thus giving it the necessary flexibility to effectively execute its mandate.

As is the case with the PA, the FSCA is also given a variety of regulatory toolkits to aid it in reaching its objections. Firstly, the FSCA is also empowered to make conduct standards for financial institutions, representatives and key persons of such institutions, and contractors.[230] A conduct standard is aimed to ensure the effectiveness and integrity of financial markets, to ensure that financial institutions and representatives treat customers fairly and to ensure that financial education programs are appropriate.[231] A conduct standard in terms of the FSR Act is further intended to mitigate the risk that financial institutions, representatives, key persons and contractors may engage in conduct that promotes financial crime.[232] In line with the PA, the FSCA also has the power to collaborate with the PA to make joint standards on any subject matter which any one of them has the authority to make.[233]

[226] Sections 58(1)(f) & (h) of the FSR Act.
[227] Sections 58(1)(i) & (j) of the FSR Act.
[228] Sections 34(5) and 58(6) of the FSR Act.
[229] Godwin, Howse & Ramsay "Twin Peaks: South Africa's Financial Sector Regulatory Framework" 679.
[230] Section 106(1) of the FSR Act. A "representative" has the meaning assigned to it in terms of the Financial Advisory and Intermediary Services Act, 2002. A "key person" has the meaning assigned to it in terms of the FSR Act. A "contractor" means a person with whom a financial institution has entered into an outsourcing arrangement but does not include an independent contractor as described in the definition of "staff member".
[231] Section 106(2) of the FSR Act.
[232] Section 106(2) of the FSR Act.
[233] Section 107 of the FSR Act.

It is, however, significant to note that there are two instances in which the FSCA is unable to make a conduct standard without concurrence of the SARB. The first instance is a standard that imposes requirements on providers of payment services.[234] The second instance occurs when a standard is intended to help maintain financial stability, including a standard related to designated institutions in resolution.[235] It should, however, be pointed out that the latter instance applies, *mutatis mutandis,* to a standard made by the PA.[236]

Another toolkit afforded to the FSCA, similar to what was alluded to above in respect of the PA, is the power to grant, refuse, vary, suspend and revoke licenses.[237] Importantly, however, is the fact that concurrence from the other financial sector regulator is required in respect of certain licensing matters. In terms of section 126 of the FSR Act, the FSCA and the PA may not take certain actions unless the other financial sector regulator has provided it with concurrence. The actions referred to are the issuing, carrying, suspending or revoking of a licence and granting of an exemption in terms of section 281[238] of the FSR Act.[239] Apart from the FSCA's standard-making and licensing powers as pointed out above, it also has a similar right as the PA to request a person to provide it with certain data or a specific document that will help in carrying out its duties.[240]

The FSCA is further, like the PA, permitted to conduct supervisory on-site inspections at a supervised entity's business premises.[241] As alluded to above, the PA may conduct investigations if it has reason to believe that a person contravenes any provision of a law for which the PA is responsible for, or that the investigation is necessary to accomplish the objectives of its mandate. The FSCA has the same rights.[242] There is, however,

[234] Section 109(1) of the FSR Act.
[235] Section 109(2) of the FSR Act.
[236] Section 109(2) of the FSR Act.
[237] Chapter 8 of the FSR Act.
[238] In terms of section 281 of the FSR Act, the concurrence of the other financial sector regulator is required if the responsible authority for a financial sector law exempt any person or class of persons from a specified provision of the financial sector law, unless it considers that the granting of the exemption will be contrary to the public interest or may prejudice the achievement of the objects of a financial sector law.
[239] Section 153 of the FSR Act.
[240] Section 131 of the FSR Act.
[241] Section 132 of the FSR Act.
[242] Section 135 of the FSR Act.

certain circumstances[243] in which the investigator appointed to conduct an investigation, is required to report to the SARB on its findings.[244]

As indicated above, the FSR Act provides the PA with a number of enforcement tools, such as the issuing of guidance notices, interpretation rulings, directives, enforceable undertakings and debarments.[245] These tools apply equally to the FSCA. Section 144 of the FSR Act deals with directives issued by the FSCA whereas section 143 pertains to directives issued by the PA. In terms of section 144 of the FSR Act, the FSCA may issue a written directive to a financial institution requiring the institution to take action detailed in the directive.[246] A directive can be issued in certain circumstances, namely if the financial institution's business is conducted in a way that materially compromise the integrity and effectiveness of the financial markets.[247] The FSCA may further issue a directive if the financial institution's customers are treated in such a way that the institution would not be able to fulfill its obligations insofar as it relates to the fair treatment of those customers.[248] Furthermore, a directive may be issued if the financial institution provides financial education in a manner that is inconsistent with applicable conduct standards.[249] It may also be issued if a financial institution or one of its key persons, representatives or contractors has contravened or is likely to contravene a provision of an act for which the FSCA is accountable.[250] Lastly, the FSCA may issue a directive in the event that a financial institution or a key person, representative or contractor of the institution has failed to comply with an enforceable undertaking, is engaged or likely to be engaged in financial crime or is causing or contributing to the financial system's instability.[251]

2.2.3 The Role of the SARB

[243] For instance, where the investigator is of the opinion that the designated institution should be wound up, should remain in resolution for a specified period or until a specified event occurs, or should cease to be in resolution. See section 135A of the FSR Act.
[244] Section 135A of the FSR Act.
[245] Chapter 10 of the FSR Act.
[246] Section 144 of the FSR Act.
[247] Section 144(1)(a) of the FSR Act.
[248] Section 144(1)(b) of the FSR Act.
[249] Section 144(1)(c) of the FSR Act.
[250] Section 144(1)(d) of the FSR Act.
[251] Section 144(1)(d) of7 the FSR Act.

Historically, central banks, in the great majority of countries, have been responsible for overseeing and regulating banks and maintaining financial stability.[252] This equally applies to South Africa. Prior to Twin Peaks, as alluded to above, the SARB performed the traditional role of a central bank, i.e. it was tasked with the execution of monetary policy, it supervised banks and it was also responsible for supervision of the payments and settlement system and was regarded as the lender of last resort.[253] The SARB was also responsible for maintaining financial stability in the country.[254] However, as mentioned previously, van Heerden and van Niekerk remark that this isolated sectoral approach had led to an insufficient and incoherent regulatory framework.[255]

Llewellyn asserts that the position and function of the central bank is an essential consideration in any institutional framework of financial regulation.[256] In the case of the Twin Peaks model, the burning question is whether or not the central bank should also act as the prudential regulator.[257] Llewellyn, in his discussion of the role of the central bank, addressed two issues: firstly, the issue of power and secondly, the issue of possible conflict of interest.[258] Insofar as the power issue is concerned, he indicates that in most countries that have a single financial regulator, the central bank is, rightfully so, separated from that regulator.[259] Separating the central bank from the financial regulator would inevitably prevent an undesirable situation where too much power is vested in the central bank. With regards to the conflict of interest issue, Llewellyn remarks that conflict of interest is commonly cited as the primary argument against the involvement of central banks in regulation.[260] Llewellyn further points out that concerns regarding conflict of interest may occasionally, in some cases, serve as motivation for delegating supervisory duties to the central bank.[261]

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[252] Llewellyn 28.
[253] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 415.
[254] Section 10 of the South African Reserve Bank Act 90 of 1989 & Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 415.
[255] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 415.
[256] Llewellyn 28.
[257] Llewellyn 27.
[258] Llewellyn 28.
[259] Llewellyn 28.
[260] Llewellyn 29.
[261] Llewellyn 29.

Twin Peaks brought significant changes to the role of the SARB in South Africa's financial regulatory framework. As was discussed before, one of the major changes in South Africa was the fact that the regulation and supervision of banks were withdrawn from the ambit of the SARB and assigned to the PA. The PA, however, remains under the administrative support of the SARB, similar to the approach in New Zealand.[262] According to Qumba, the reasoning behind this decision pertaining to the administrative support to the PA in South Africa is sensible, considering the interrelated nature of prudential and monetary regulation.[263] Qumba remarks that the opposite viewpoint of this approach may in itself lead to conflict since the objectives of prudential regulation and monetary policy often collide.[264] South Africa, however, achieves a balance between such concerns in that the PA deals with the regulation and supervision of financial institutions, whereas the SARB deals with monetary policy.[265] Godwin, Howse and Ramsay note that the PA is in fact given protection by being housed within the central bank since interfering with the PA would essentially mean interfering with the SARB.[266] They further state that this could discourage government interference and is consistent with the premise that central banks in developing countries have greater capacity to supervise the banking sector and avoid interference from politicians.[267]

The central bank plays an essential role, and arguably apex, in the South African Twin Peaks model since it has been assigned an extended financial stability mandate and is therefore regarded as the top peak in this model.[268] This mandate is now, for the first time, written into law with the introduction of the FSR Act.[269] The FSR Act has established an express mandate to promote and maintain financial stability to the SARB, in addition to its primary mandate of safeguarding the value of the currency.[270] In terms of section 4 of the FSR Act, "financial stability" means that: financial institutions provide financial

[262] Godwin, Howse & Ramsay "Twin Peaks: South Africa's Financial Sector Regulatory Framework" 672.
[263] Qumba 96.
[264] Qumba 96.
[265] Qumba 96.
[266] Godwin, Howse & Ramsay "Twin Peaks: South Africa's Financial Sector Regulatory Framework" 674.
[267] Godwin, Howse & Ramsay "Twin Peaks: South Africa's Financial Sector Regulatory Framework" 674.
[268] Van Niekerk & van Heerden "The Importance of a Legislative Framework for Co-operation and Collaboration in the Twin Peaks Model of Financial Regulation" 113.
[269] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 416.
[270] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 417.

products and services, and market infrastructures perform their duties in terms of financial sector laws, without interruption; financial institutions are capable of continuing to provide financial products and services, and market infrastructures are capable of continuing to perform their functions and duties in terms of financial sector laws, without interruption; and there is a general confidence in the ability of financial institutions to continue to provide financial products and services, and the ability of market infrastructures to continue to perform their functions and duties in terms of financial sector laws, without interruption.

Section 11 of the FSR Act sets out the powers and functions of the SARB in relation to financial stability and requires the SARB to protect and improve financial stability and, if a systemic event[271] happens or is approaching, the SARB is obliged to maintain or restore financial stability in the country. An important task in maintaining financial stability in the South African financial system, is the effective monitoring of risks, which task is given to SARB by virtue of the FSR Act. In this regard the SARB is required to assess the strengths and flaws of the financial system as well as any risks to financial stability and must have regard to the nature and extent of those risks, including risks that systemic events will occur.[272] The SARB must also take steps to mitigate risks to financial stability which includes guiding financial sector regulators, and any other organ of state, of the steps they have to take to mitigate those risks. Furthermore, the SARB must regularly review the observance of principles in the Republic developed by international standard setting bodies for market infrastructures.[273] Findings of these reviews must subsequently be reported to other financial regulators and the Minister.[274]

In addition to the SARB's duty to effectively monitor risks as part of its financial stability mandate, it is required to review the stability of the financial system every six months

[271] A "systemic event" is defined in section 1 of the FSR Act 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.
[272] Section 12 of the FSR Act.
[273] Section 12 of the FSR Act.
[274] Section 12 of the FSR Act.

("financial stability review").[275] The financial stability review must set out: the SARB's assessment of financial stability in the review period; the identified risks to financial stability in at least the next 12 months; an outline of steps taken by the SARB and other financial regulators to identify and manage risks or weaknesses in the financial system during the review period and those that are expected to be taken in at least the next 12 months; and an outline of recommendations made by the SARB and the FSOC during the review period and developments in implementing those recommendations.[276] It is therefore clear that the financial stability review is not only focused on the current health of the system but also considers possible future risks.[277] The SARB'S explanation of how it will address and mitigate risks to financial stability clearly serves to instill public confidence in the SARB's ability to execute this very important mandate.

Sections 14 and 15 of the FSR Act affords the SARB with possibly the most significant power, namely the power to manage systemic events and risks. Section 14 deals with the determination of systemic events followed by section 15 whereby the functions of the SARB in relation to systemic events are set out. The Governor[278] of the SARB may, in terms of section 14(1), determine that a specified event is a systemic event. Before such a determination is made, the Governor must consult with the Minister.[279]

In terms of section 15 of the FSR Act, the SARB must take reasonable steps to prevent systemic events from happening. It further provides that if such an event happens or is imminent, the SARB must speedily mitigate the adverse effects of the event on financial stability and manage the event and its effects. In addition, when dealing with a systemic event, the SARB is required to consider the need to lessen adverse effects on financial stability and economic activity, protect financial customers where appropriate and contain costs to the Republic of the systemic event and the steps taken (thus meaning that the

[275] Section 13 of the FSR Act.
[276] Section 13 of the FSR Act.
[277] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 418.
[278] "Governor" is defined in the FSR Act as the person appointed in terms of section 4 or 6(1)(a) of the Reserve Bank Act as the Governor of the Reserve Bank.
[279] Section 14(1) of the FSR Act.

SARB does not have a carte blanche to use public funds to bail out failing financial institutions).[280]

If the Governor determines that a systemic event has occurred or is imminent, the Governor must inform the Minister accordingly and advise on what steps had been taken or proposed to manage the event and the effects thereof.[281] The SARB is prohibited, unless the Minister approves, from taking steps in terms of section 15 that will or may bind the National Revenue Fund to expenses, have a substantial impact on the cost of borrowing for the Fund or create a future financial commitment or liability for the Fund.[282] The FSR Act also imposes certain responsibilities on the financial sector regulators if a systemic event has happened or is about to happen.[283] Any data in each regulator's possession that could help the SARB manage the systemic event must be shared with the SARB and the SARB must further be consulted before the regulators use any of their powers in a way that may undermine steps taken or proposed in terms of section 15.[284] To enhance appropriate crisis coordination and mitigation, a financial sector regulator may also be directed by the Governor to provide the SARB with certain information in the regulator's possession that is required to exercise the SARB's powers in terms of sections 14 or 15.[285]

If a systemic event has happened or is about to happen, the relevant financial regulator may be directed to assist the SARB in complying with its functions in respect of the systemic events set out in section 15 of the FSR Act, including directions aimed at supporting the restructuring, resolution or winding-up of any financial institution, avoiding further spread of the risk or disruption, or increasing the resilience of financial institutions of risk or disruption.[286] If one considers section 18(2) of the FSR Act, it is clear that the list for which the SARB may issue directives relating to systemic events is not a closed list.[287] Still on the topic of the powers of the SARB in respect of systemic risks, section 19

[280] Section 15 of the FSR Act.
[281] Section 16(1) of the FSR Act.
[282] Section 16(2) of the FSR Act.
[283] Section 17 of the FSR Act.
[284] Sections 17(a) & (b) of the FSR Act.
[285] Section 18(1) of the FSR Act.
[286] Section 18(2) of the FSR Act.
[287] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 418.

extends these powers to activities of other organs of state. If it was determined that a systemic event has happened or is about to happen, an organ of state which have powers in that particular financial system, may not exercise its powers inconsistently with a decision by the Governor or the SARB in order to manage that event, unless approval is obtained from the Minister.[288] The FSOC, is established in terms of section 20 of the FSR Act, to support the SARB in its function relating to financial stability and to facilitate co-operation between the financial sector regulators and the SARB regarding financial stability matters.[289]

Van Heerden and van Niekerk mention that the GFC revealed that the phenomenon of "Too Big to Fail" financial institutions who regarded their size and interconnectedness as a guarantee of bailout with public funds should they run into financial difficulty, had to come to an end, and that systemically important financial institutions ("SIFIs") need more stringent regulation and oversight.[290] This was given effect by Part 6 of the FSR Act which focusses on SIFIs. Section 29 of the FSR Act gives the SARB the authority to designate an institution as a SIFI. Certain aspects must be taken into account by the SARB before such designation can be made, amongst others, the size and complexity of the financial institution and the interrelatedness of the institution with other financial institutions.[291] The effect of being designated a SIFI means that the SARB can direct the PA to impose more stringent prudential requirements on SIFIs to enhance their loss absorbency capacity as per section 30 of the FSR Act.

2.3 Co-operation and Collaboration

In order to ensure the effective and efficient operation of a Twin Peaks model, it is of utmost importance that there must be proper co-operation and collaboration between the various role players in the financial system.[292] This is important as to avoid a silo-based

[288] Section 19(1) of the FSR Act.
[289] Section 20 of the FSR Act.
[290] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 419.
[291] Section 29(3) of the FSR Act.
[292] Van Heerden & van Niekerk "The Financial Stability Mandate of the South African Central Bank in the Post-crisis Landscape" 420.

approach as is seen in silo sectoral models of financial regulation.[293] To operate an ideal Twin Peaks model, it is critical to have a regulatory framework which encourages both peak regulators to co-operate and collaborate when executing their respective supervisory functions.[294]

The FSR Act has several provisions that deal specifically with co-operation and collaboration aimed at two levels. The first level focusses on co-operation and collaboration requirements amongst the SARB, financial sector regulators and FSOC as well as the Financial Sector Contingency Forum ("FSCF") (as discussed in more detail later herein) that specifically focuses on promoting and maintaining *financial stability* (Part 5 of Chapter 2).[295] It should be noted that "financial sector regulator" is defined in section 1 of the FSR Act to mean the PA and the FSCA. However, the definition further states that, only for purposes of Part 5 of Chapter 2 of the FSR Act, it also means the NCR and the FIC. It thus follows that all regulators, and not only the PA and the FSCA, are subject to the co-operation and collaboration requirements that relate to maintaining financial stability.

The second level deals with the co-operation and collaboration requirements amongst the SARB and the regulators for purposes of the broader effective and efficient operation of the Twin Peaks model (Part 1 of Chapter 5).[296]

With regards to the first level, it is important to note that there is an explicit obligation on regulators to co-operate, not only with the SARB, but also with each other.[297] In order to maintain or restore financial stability, section 26(1)(b) provides that the regulators must give the SARB and the FSOC assistance and information that may reasonably be necessary. They also have to provide the SARB with assistance and information regarding designated institutions as may reasonably be required by the SARB.[298] In

[293] "Implementing a Twin Peaks model of financial regulation in South Africa" 2013 72.
[294] Van Niekerk & van Heerden "The Importance of a Legislative Framework for Co-operation and Collaboration in the Twin Peaks Model of Financial Regulation" 111.
[295] Sections 26-28 of the FSR Act.
[296] Sections 76-78 of the FSR Act.
[297] Van Niekerk & van Heerden "The Importance of a Legislative Framework for Co-operation and Collaboration in the Twin Peaks Model of Financial Regulation" 118 & section 26(1)(a) of the FSR Act.
[298] Section 26(1)(bA) of the FSR Act.

addition, the regulators must also, without delay, report to the SARB on matters that may pose a risk to financial stability.[299] Lastly, it is expected of regulators to gather information from, or in respect of, a financial institution and designated institutions that concerns financial stability.[300]

As was alluded to above, sections 17 and 19 of the FSR Act requires regulators to provide or engage with the SARB in instances relating to systemic events or for purposes of compliance with directives aimed at promoting or restoring financial stability.

Although regulators are required to provide the SARB with all the aforementioned information, it is important to note that the SARB may not merely exercise its powers solely on its own.[301] In terms of section 26(2) of the FSR Act, the SARB must, when exercising its powers in relation to financial stability, consider the views expressed and information received from the financial sector regulators. It must also consider any recommendations received from the FSOC.[302]

In addition to the above-mentioned co-operation and collaboration requirements, the FSR Act further requires the SARB and the regulators to enter into memoranda of understandings ("MOUs"). In particular, in terms of sections 27(1) of the FSR Act, they are required to enter into MOUs setting out the manner in which they will collaborate and co-operate with each other with regards to financial stability.[303] A very important point to take note of, is that MOUs entered in between the SARB and the regulators must be amended before 1 December 2023 to include a provision on the collaboration and co-operation steps taken or to be taken to ensure compliance with their duties in respect of designated institutions.[304] To stay relevant, the FSR Act stipulates that these MOUs must be reviewed and updated as applicable but at least once in a 3-year cycle and copies

[299] Section 26(1)(c) of the FSR Act.
[300] Section 26(1)(d) of the FSR Act.
[301] Van Niekerk & van Heerden "The Importance of a Legislative Framework for Co-operation and Collaboration in the Twin Peaks Model of Financial Regulation" 119.
[302] Section 26(2) of the FSR Act.
[303] During 2018, the SARB has entered into MOUs with the PA and the FSCA respectively. The FSCA also entered into MOUs with the PA, the NCR and the FIC respectively. See van Niekerk & van Heerden "The Importance of a Legislative Framework for Co-operation and Collaboration in the Twin Peaks Model of Financial Regulation" 125-128.
[304] Section 27(1A) of the FSR Act.

thereof must be provided to the Minister and the Cabinet member responsible for consumer credit matters.[305]

It is further expected of an organ of state to consider the consequences of its activities on financial stability and the SARB's resolutions functions and not to take steps that may compromise financial stability unless it has been cleared by the SARB. They are also required to assist the SARB and the FSOC, on reasonable request, with information in respect of designated institutions or information that might help to maintain financial stability.[306]

As indicated above, the second level of the co-operation and collaboration requirements amongst the SARB and the regulators deal with these requirements on a broader Twin Peaks model and is equally important in achieving financial stability in the South African financial system.

In respect of this broader level of co-operation and collaboration, section 76 of the FSR Act imposes a duty on the financial sector regulators and the SARB to co-operate and collaborate with each other when they carry out their duties in terms of financial sector laws, the National Credit Act[307] and the Financial Intelligence Centre Act.[308] To ensure adherence with these obligations, they are required to, at least annually, report to the Minister, the Cabinet member responsible for administering the NCA and the National Assembly on the steps that have been taken to co-operate and collaborate with each other.[309]

In addition to the co-operation and collaboration requirements referred to in section 76 of the FSR Act, the SARB and the regulators are also required to enter into MOUs for purposes of the broader effective and efficient functioning of the Twin Peaks model. In terms of section 77 of the FSR Act, the MOUs must give effect to the obligations set out in section 76. For obvious reasons, the MOUs needs to be reviewed regularly but at least

[305] Sections 27(2) and (3) of the FSR Act.
[306] Section 28 of the FSR Act.
[307] The National Credit Act 34 of 2005.
[308] The Financial Intelligence Centre Act 38 of 2002.
[309] Section 76(2) of the FSR Act.

once every three years.[310] If needed, the MOUs are to be amended accordingly and copies thereof be provided to the Minister and the Cabinet member responsible for administering the National Credit Act.[311] The regulators and the SARB is further obliged to publish all MOUs as well as all amendments thereof – notably this is in contrast with section 27 of the FSR Act where publication is not a requirement.[312]

According to section 78(1) of the FSR Act, an organ of state that has a regulatory or supervisory role in respect of a financial institution may not on its own initiative take steps that may compromise the effective working of the Twin Peaks model but must consult with the regulators and the SARB in connection with the execution of that role.[313]

2.4 Committees established by the FSR Act

The FSR Act also makes provision for committees to assist the SARB and the regulators in order to successfully carry out its mandate for financial stability. The first apex committee is the FSOC which was established by section 20(1) of the FSR Act to assist the SARB in carrying out its duties regarding financial stability. This committee's duties[314] include improving collaboration among, and co-operation of action between, the SARB and the financial sector regulators with regard to issues involving financial stability.[315] As was illustrated above, the SARB must, when exercising its powers in relation to financial stability, consider any recommendations received from the FSOC.[316] It is therefore clear that the FSOC is the most important committee where key decisions in respect of the

[310] Section 77(4) of the FSR Act.
[311] Section 77(5) of the FSR Act.
[312] Van Niekerk & van Heerden "The Importance of a Legislative Framework for Co-operation and Collaboration in the Twin Peaks Model of Financial Regulation" 122 & section 77(6) of the FSR Act.
[313] Section 78(1) of the FSR Act.
[314] Van Niekerk & van Heerden "The Importance of a Legislative Framework for Co-operation and Collaboration in the Twin Peaks Model of Financial Regulation" 117 & section 21 of the FSR Act.
[315] The other functions of the FSOC include: recommendations made to the Governor regarding the designation of SIFIs; to advise the Minister and the SARB on how to promote, protect, or prevent risks to, financial stability; to make recommendations to other organs of state on how to promote, protect or prevent risks to, financial stability; and any other function conferred on it in terms of other applicable legislation. See section 21 of the FSR Act.
[316] Section 26(2) of the FSR Act.

SARB's financial stability mandate are taken.[317] Consequently, the FSOC significantly contributes to the financial stability of the South African financial system.

The second committee that assists the SARB in carrying out its duties regarding financial stability, is the FSCF.[318] The FSCF is established by the Governor and its primary role is to assist the FSOC to identify potential risks that a systemic event might happen and to coordinate strategies and mechanisms to lessen such risks.[319]

The third body provided for in the FSR Act is the Financial System Council of Regulators ("FSCR")[320] which is established for purposes of the broader effective and efficient operation of the Twin Peaks model. By providing a forum to discuss issues of shared interest, this council seeks to promote co-operation and collaboration amongst the institutions represented on the FSCR.[321] To fully comprehend the purpose of the FSCR, one has to consider section 81 of the FSR Act. According to this section, the FSCR is tasked with the responsibility to establish working groups in respect of the following matters: enforcement and financial crime; financial stability and resolution; policy and legislation; standard-setting; financial sector outcomes; financial inclusion; transformation of the financial sector; and any other matter that the Director-General may determine. As was pointed out by van Heerden & van Niekerk, the reasons why the Minister, who is responsible for the general administration of the FSR Act, is empowered to appoint a head of any organ of state or other organisation to this council is because the council serves as the co-ordinating body for the *wider* Twin Peaks model[322] – it would therefore make sense to allow broader representation if, and when, required.

[317] Van Niekerk & van Heerden "The Importance of a Legislative Framework for Co-operation and Collaboration in the Twin Peaks Model of Financial Regulation" 117.
[318] The FSCF is tasked with assisting authorities to identify and mitigate risks that could threaten the functioning and stability of the financial system. See section 25 of the FSR Act.
[319] Section 25 of the FSR Act.
[320] Established in terms of section 79(1) of the FSR Act.
[321] Section 79(2) of the FSR Act.
[322] Van Niekerk & van Heerden "The Importance of a Legislative Framework for Co-operation and Collaboration in the Twin Peaks Model of Financial Regulation" 123.

The final body established by the FSR Act is the Financial Sector Inter-Ministerial Council.[323] Van Heerden and van Niekerk explained the rationale put forward for the establishment of this council as follows:

> "In order to address all the levels at which decisions may be taken which may impact on financial stability specifically, and also at the broader Twin Peaks level, it is also necessary that some form of 'control' be exerted over government ministers who are responsible for the organs of state within whose jurisdiction each of the financial sector regulators is located, and who therefore also have responsibility for the policy decisions and legislation which affect these regulators."[324]

The council was therefore formed to serve as some sort of "overseer" to monitor and ensure that the ministers in charge of the state organs under each financial sector regulator's respective jurisdiction "stays in line".

The council consists of the Minister, the Cabinet members responsible for consumer protection and consumer and credit matters, the Cabinet member responsible for health and the Cabinet member responsible for economic development.[325] The council's objective is to facilitate co-operation and collaboration between Cabinet members that are responsible for administering legislation relevant to the regulation and supervision of the financial sector by providing a forum for discussion of matters of common interest.[326]

2.5 Conclusion

The global financial system has seen a significant shift in financial regulation since the GFC. In particular, there has been a paradigm change toward the Twin Peaks model of financial regulation, not only in South Africa, but also around the globe. However, the South African Twin Peaks model is not a Twin Peak model that follows the exact institutional architecture conceptualised by Taylor but rather is a three peak model comprising of the SARB, and the twin regulators, the PA and the FSCA. As was demonstrated above, the Twin Peaks approach in South Africa had the practical effect of

[323] Established in terms of section 83(1) of the FSR Act.
[324] Van Niekerk G & van Heerden a C "The importance of a legislative framework for co-operation and collaboration in the Twin Peaks model of financial regulation" 124.
[325] Section 83(3) of the FSR Act.
[326] Section 83(2) of the FSR Act.

transferring bank supervision and regulation from the SARB to the newly established PA. The PA is responsible for prudential regulation and supervision of all financial institutions. All financial institutions, in addition to banks, insurers, and pension funds, are subject to the PA's system-wide prudential regulation. Given the extensive effort the PA has made in improving prudential regulation of the institutions it oversees, it appears that it is serious about efficiently and effectively regulating and supervising the financial market from a prudential supervision perspective.[327]

As alluded to above, another important change with the adoption of the Twin Peaks model in South Africa was the establishment of the FSCA since market conduct regulation in South Africa did not previously receive the priority it deserved.[328] As was discussed above, the FSCA is responsible for the supervision and regulation of conduct of business activities and practices of financial institutions.[329]

Even though the PA and the FSCA have separate mandates, it is noteworthy, as indicated, to reiterate that they are both tasked by the FSR Act to assist the SARB in

[327] Since its establishment in 2018, the PA has issued the following directives. Matters related to Pillar 3 disclosure requirements-consolidated and enhanced framework; Materiality threshold in respect of exposure to a foreign jurisdiction in applying jurisdictional reciprocity in the countercyclical capital buffer calculation; Cloud computing and the offshoring of data; Matters related to the promotion of sound corporate governance, and in particular in relation to the appointment of directors and executive officers; Completion of return relating to operational risk (Form 410); Matters related to Pillar 3 disclosure requirements framework; Temporary Measures to aid compliance with the LCR during COVID-19 pandemic stress period; Matters related to temporary capital relief in light of COVID 19; Matters related to the treatment of restructured credit exposures due to the Coronavirus (Covid-19) pandemic; Capital framework for South Africa based on the Basel III framework; Matters related to the Prudential Valuation Adjustment Framework; Completion and submission of return relating to operational risk (BA 410); Calculation of derivative exposure amount for the purposes of determining the leverage ratio; DSIBs submission of consolidated data; Matters related to the issuance of additional tier 1 capital instruments that contain contingent; Reporting requirements in terms of regulation 46; Externally-facilitated liquidity stress simulation; Capital Framework for South Africa based on the Basel III framework; Matters related to the use of credit risk models; Withdrawal of the temporary treatment of restructured credit exposures due to the Covid-19 pandemic; Withdrawal of the temporary relief measure related to the liquidity coverage rati; Principles for the Sound Management of Operational Risk; Operational Resilience; Liquidity coverage ratio scope of application and matters related to calculation and disclosure; Consistent applications requirements across representative offices; Large exposure requirements; Risk Return; Matters relating to liquidity risk; Banks–Benefical owners; Directors and executive officers; Directive BA 410; MVTS Directive to Banks; Criteria for identifying simple transparent and comparable term and short term securitisations; National discretion related to the liquidity coverage ratio; Matters related to the NSFR; Completion of the form BA330 and public comments received on the proposed Directive; Regulatory treatment of accounting provisions; Operational resilience; Reporting requirements in terms of regulation 46; Directive on matters relating to eligible external credit assessment institutions; Threshold amounts related to the revised standardised and IRB approaches for credit risk and the liquidity risk framework.

[328] "A Safer Financial Sector to Serve South Africa Better" 29.

[329] See paragraph 2.2.2 above.

ensuring financial stability. To enable them to meet their objectives, it was pointed out above that the FSR Act affords both the FSCA and the PA with a variety of regulatory tools, including but not limited to the making or issuing of standards, directives and debarment orders, the granting, refusing, varying, suspending and revoking of a license, and conducting investigations.

The adoption of the Twin Peaks model in South Africa has brought significant changes to the role of the SARB as central bank and its crucial role in relation to the promotion and maintenance of financial stability has been illuminated in the model. The SARB has now an extended financial stability mandate which as pointed out is, for the first time, written into law and provides more clarity on the extent of this mandate and the powers availed to the SARB to execute this crucial mandate.

In summation, it can be observed that the Twin Peaks approach has been successfully implemented in South Africa, which merits applause. However, continuous effective and efficient collaboration and co-operation amongst the PA, FSCA, the SARB and other organs of state is essential for the Twin Peak to operate optimally. The FSR Act has put sufficient collaboration and co-operation requirements in place to contribute to promoting and maintaining financial stability in South Africa. As indicated, the FSR Act further requires the SARB and the regulators to enter into MOUs to give effect to obligations set out in the Act and these MOUs, being soft law instruments, bear the advantage that they can be changed speedily without the need for Parliamentary intervention should changing circumstances require changes to avoid financial crisis or deal better with financial crisis.

In addition to these requirements, the FSR Act has established several committees, each with their distinct purpose. Importantly, accountability is ingrained, and the duty to co-operate and collaborate is strengthened by the requirements in the FSR Act to periodically review and report to Parliament on such matters.[330]

The shift from a sectoral to a Twin Peaks model in South Africa was a thorough and well-conceptualised regulatory process that evolved over an extended period of time and

[330] See paragraph 2.3 above.

South Africa made significant progress in this regard since the model came into effective operation in 2018. Although the Twin Peaks model is fairly new in South Africa, it is submitted that, taking everything discussed into account, the model and the manner in which it is observed by the relevant regulators, positively contributes to a stronger financial system which would, presumably, prevent, mitigate or overcome any possible future financial crises.

Chapter Three

The Twin Peaks Model of Financial Regulation in the UK

3.1 Introduction

In 2013, the UK transitioned from an integrated model of financial regulation to a Twin Peaks model with the implementation of the Financial Services Act 2012 ("FS Act"). Under the integrated model, the UK was regulated by a unified regulator, the FSA.[331] Almost all financial services institutions in the UK, including banking, securities, and insurance, were subject to regulation and supervision of the FSA. The FSA was consequently responsible for regulating both the conduct of business and the safety and soundness (prudential) of financial institutions.[332] However, the run on Northern Rock, a UK-based mortgage lender,[333] illustrated the difficulties of a single, huge regulator that is in control of supervising and regulating an entire financial industry.[334] The Northern Rock saga also emphasised the importance of a regulatory authority to acting early and taking increasingly swift action if, and when required, and when capitalisation falls.[335]

It is interesting to note that the Twin Peaks model was initially proposed to the UK by Taylor during 1994, before the UK transitioned to the integrated model.[336] Taylor recommended this model to the UK due to the "blurring of the boundaries" that occurred amongst financial institutions in the UK at the time.[337] There were so many separate regulatory bodies in the UK that were responsible for overseeing conduct and systemic

[331] Group of Thirty "The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace" 2008 28.
[332] Group of Thirty "The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace" 2008 28.
[333] Northern Rock relied heavily on non-retail deposits or funding, and when the credit market conditions deteriorated in 2007, Northern Rock had trouble obtaining wholesale market funding. This market disruption finally forced Northern Rock to turn to the Bank of England for emergency liquidity support, which ultimately resulted in the run on Northern Rock's retail deposits. See Shin "Reflections on Northern Rock: The Bank Run that Heralded the Global Financial Crisis 2009 101-104 https://pubs.aeaweb.org/doi/pdfplus/10.1257/jep.23.1.101 (accessed 07-11-2023).
[334] FSA Internal Audit Division "The Supervision of Northern Rock: A Lessons Learned Review" 2008 https://www.fca.org.uk/publication/corporate/fsa-nr-report.pdf (accessed 26-08-2023) & Group of Thirty "The Structure of Financial Supervision: Approaches and Challenges in a Global Marketplace" 2008 37.
[335] Mayes "Lessons from the Northern Rock Episode"2008 9-10 http://www.cepii.fr/IE/rev114/mayes_wood.pdf (accessed 09-11-2023).
[336] Schmulow 394.
[337] Schmulow 394.

issues in the financial sector that it was referred by Taylor as an "alphabet soup" of regulators.[338] According to Taylor, the proposed Twin Peaks model that he conceptualised would benefit the UK since it would do away with regulatory conflict and duplication; regulators would have well-defined mandates; conflicts between the goals of financial services regulation would be effectively resolved through an established system; and it would promote an open, transparent and accountable regulatory process.[339]

However, as a result of the UK's inability to effectively detect the risks occasioned by and manage the effects of the GFC, the Twin Peaks model, as proposed to it by Taylor in the mid-nineties was finally adopted by the UK in 2012 and came into effect on 1 April 2013 with the implementation of the FS Act.[340] This decision was rather ironic in light of the fact that the Twin Peaks model was dismissed by critics "as far too radical" when initially proposed by Taylor.[341]

3.2 The main institutional components of the Twin Peaks Model in the UK

With the transition to a Twin Peaks model in the UK, the FSA, the erstwhile regulator, was replaced with two successor regulators, namely the PRA, part of the Bank of England, and the FCA.[342] The FCA and the PRA were established in terms of the FS Act. The FS Act also established the Financial Policy Committee ("FPC") which operates within the Bank of England, as discussed in more detail below.[343]

3.2.1 The Role of the PRA

[338] Taylor "Twin Peaks: A regulatory structure for the new century" Centre for the Study of Financial Innovation 1995 7.
[339] Taylor "Twin Peaks: A regulatory structure for the new century" Centre for the Study of Financial Innovation 1995 1.
[340] Qumba 88.
[341] Taylor "Regulatory Reform in the UK" 2013 https://scholarship.law.unc.edu/cgi/viewcontent.cgi?article=1367&context=ncbi (accessed 26-08-2023) 228.
[342] Taylor "Regulatory Reform in the UK" 2013 227-228.
[343] Bank of England "Financial Policy Committee" https://www.bankofengland.co.uk/about/people/financial-policy-committee (accessed 28-08-2023).

The PRA is tasked with prudential regulation of insurers and investment institutions, as well as deposit-takers such as credit unions and banks.[344] It is therefore said that the PRA focuses on the safety and soundness of *individual* institutions.[345] Taylor referred to the PRA as a specialist prudential regulator that is responsible for all insurance companies, deposit-taking institutions and a select few designated investment firms.[346] He further explains that in order to determine if an investment firm would fall under the regulation and supervision of the PRA, would depend on whether such firm engages in securities as principal of the investment firm, or has minimum capital above the prescribed threshold.[347]

As pointed out, where the prudential regulator should be located in relation to the central bank remains a crucial decision when considering Twin Peaks as a possible model for regulation and this has also been an issue in the UK. According to Qumba there are three options to choose from and he conveniently summarised it as follows: firstly, the prudential regulator can be a distinct entity that operates fully outside the central bank; secondly, the regulator can operate as a subsidiary of the bank; and thirdly, the regulator can operate within the central bank. The UK has chosen the third option.[348]

Prior to adopting the Twin Peaks model, the Bank of England was responsible for monetary policy and the stability of the financial system whilst the responsibility for banking supervision was transferred from the bank to the FSA.[349] This, however, changed with the transition to the Twin Peaks model since the Bank of England was given the reins of prudential regulation which it performs through the FPC.[350] The Bank of England is now seen to have a clear and separate role in the regulation regime whilst the PRA holds a specialist prudential function *within* the Bank of England.[351] According to Godwin *et al* it appears that the South African arrangement between the PA and the SARB was

[344] Stikeman Elliott "UK Implements 'Twin Peaks' Model of Financial Regulation" https://www.stikeman.com/en-ca/kh/canadian-securities-law/uk-implements-twin-peaks-model-of-financial-regulation (accessed 28-08-2023).
[345] Bank of England "Financial Policy Committee" https://www.bankofengland.co.uk/about/people/financial-policy-committee.
[346] Taylor "Regulatory Reform in the UK" 2013 228.
[347] Taylor "Regulatory Reform in the UK" 2013 228.
[348] Qumba 93-94.
[349] Ferran 4-6.
[350] Qumba 94.
[351] Godwin, Howse & Ramsay "Twin Peaks: South Africa's Financial Sector Regulatory Framework" 673.

mirrored from the UK arrangement.[352] Section 2B of the FS Act sets out the general objective of the PRA, namely to promote the safety and soundness of PRA-authorised persons[353] by ensuring that these PRA-authorised persons conduct their operations in a manner that prevents any detrimental impact on the stability of the UK financial system.[354] The general objective of the PRA is further advanced by minimising the negative impact that a PRA-authorised individual's failure might have on the stability of the UK financial system.[355] With regards to insurance, the PRA has more specific objectives in that it is expected of the PRA to act in a manner that is consistent with its general and insurance objectives respectively and which the PRA believes is most suited to furthering those objectives.[356]

As was alluded to above, Qumba queries the degree of independence between the SARB and the PA in the South Africa regime.[357] However, in the case of the UK, Qumba remarks that since the Bank of England is recognised as a prudential authority in itself, concerns regarding the operational independence of the PRA are not an issue.[358]

3.2.2 The Role of the FCA

The FCA is established in terms of section 1A of the FS Act. The FCA ensures that business across financial services and markets is conducted in a way that advances the interests of all users and participants.[359] The FS Act, in section 1B, differentiates between strategic objectives and operational objectives in relation to the FCA. The FCA's strategic objective is to ensure that relevant markets are operating efficiently. Aside from the strategic objective contemplated in the FS Act, the FCA also has operational objectives, namely the consumer protection objective, the integrity objective and the competition

[352] Godwin, Howse & Ramsay "Twin Peaks: South Africa's Financial Sector Regulatory Framework" 674.
[353] Section 2B(5) of the FS Act defines an PRA-authorised person as "an authorised person who has permission given under Part4A, or resulting from any other provision of this Act, to carry on regulated activities that consist of or include one or more PRA-regulated activities (see section 22A)".
[354] Section 2B(3)(a) of the FS Act.
[355] Section 2B(3)(b) of the FS Act.
[356] Section 2C(1) of the FS Act.
[357] Qumba 101.
[358] Qumba 103.
[359] Stikeman Elliott "UK Implements 'Twin Peaks' Model of Financial Regulation" https://www.stikeman.com/en-ca/kh/canadian-securities-law/uk-implements-twin-peaks-model-of-financial-regulation (accessed 28-08-2023).

objective.[360] The purpose of the consumer protection objective is to ensure that consumers are adequately protected.[361] The integrity objective, on the other hand, promotes and protects the integrity of the UK's financial system.[362] Lastly, in terms of section 1E of the FS Act, the purpose of the competition objective is encouraging efficient competition in the markets to benefit consumers of regulated financial services or services offered by recognised investment exchanges for conducting certain activities.

Having said this, it is important to highlight at this stage, that the FCA does not have an express mandate to promote financial stability as is the case with the FSCA in South Africa.[363] If one considers the FS Act, and this was also cited by Qumba, it is clear that the FCA's main goal is the development of a competitive environment for its financial system as it is stated in section 1B(4) that the FCA must "discharge its general functions in a way which promotes effective competition in the interests of consumers".[364]

With regards to the FCA's independence, the UK's regulatory structure is distinctive in that the Bank of England, acting as the PRA, has the authority to restrain the FCA from acting in specific situations.[365] Qumba explains that this veto power is used when the FCA's actions are likely to endanger the UK financial system's stability or when it could cause a PRA-authorised person to fail in a way that would be detrimental to the UK financial system.[366] The International Monetary Fund expressed concerns[367] that this arrangement, in the absence of adequate protections, "had the potential to limit FCA independence and also to cause uncertainty in decision making".[368] Qumba raises a further concern regarding the independence of the FCA namely the fact that the UK Treasury has the authority to order the FCA to carry out investigations.

[360] Section 1B(3) of the FS Act.
[361] Section 1C of the FS Act.
[362] Section 1D of the FS Act.
[363] Qumba 100.
[364] Qumba 100.
[365] Qumba 103.
[366] Qumba 103.
[367] IMF "United Kingdom: IOSCO objectives and principles of securities regulation: Detailed assessment of implementation" 2011 https://www.imf.org/en/Publications/CR/Issues/2016/12/31/United-Kingdom-IOSCO-Objectives-and-Principles-of-Securities-Regulation-Detailed-Assessment-25124 (accessed 08-11-2023).
[368] Qumba 103.

3.2.3 The Role of the FPC

The GFC emphasised the importance of financial stability since the UK Government had to "bail out" certain banks to safeguard the stability of the UK's financial system. The fact that the UK's financial system was unable to successfully withstand the adverse effects of the GFC indicated that their system had shortcomings in the oversight of the financial system as a whole, and that they could no longer focus on the supervision of individual banks only.[369] The FPC,[370] was established in 2013 in terms of section 9B of the FS Act and is a sub-committee of the Bank of England.

In contrast with the PRA which focuses on the safety and soundness of *individual* institutions (micro-prudential supervision), the FPC ensures that the UK financial system *as a whole* is safe and sound.[371] The FPC is therefore responsible for macro-prudential supervision.[372] In terms of section 9C of the FS Act, the FPC must identify and monitor systemic risks with a view to protect and enhance the resilience of the UK financial system as a whole.[373] It further has to support the economic policy of its Government.[374]

3.3 Co-operation and Collaboration

Qumba states that it is believed that the run on Northern Rock could have been avoided if the authorities had co-ordinated their strategy better and more effectively at the time.[375]

Considering the possibility of regulatory overlap between the PRA and the FCA as they carry out their duties, the FS Act stipulates a number of co-operation methods that the regulators may use.[376] Section 3D of the FS Act obliges both the FCA and the PRA to

[369] Bank of England "Financial Policy Committee" https://www.bankofengland.co.uk/about/people/financial-policy-committee.
[370] See paragraph 3.2 above.
[371] Bank of England "Financial Policy Committee" https://www.bankofengland.co.uk/about/people/financial-policy-committee.
[372] Qumba 92.
[373] Bank of England "Financial Policy Committee" https://www.bankofengland.co.uk/about/people/financial-policy-committee.
[374] Section 9C(1)(b) of the FS Act.
[375] Qumba 107. See also paragraph 3.1 above.
[376] Chartered Insurance Institute "Towards Twin Peaks: The UK's Emerging Regulatory Landscape (January 2013 Update)

coordinate the execution of their respective responsibilities to ensure that they engage with one another when exercising of a function in a way that could materially harm how the other regulator advances any of its own objectives. They are further required to co-ordinate in such a way as to ensure that they gather information and guidance from the other regulator related to the performance of their functions in respect of matters of common concern.[377] Lastly, the PRA and the FCA are required to coordinate the execution of their respective functions to ensure that where they exercise functions in respect of matters of common interest that they comply with their respective obligations under the FS Act.[378] However, a concern put forth by Qumba that is worth noting, is the government's involvement in the regulation and oversight of the UK financial sector which raises concerns regarding the independence of the regulators.[379]

The UK has an extensive MOU framework between the different regulators and foreign organisations. Section 3E of the FS Act requires the PRA and FCA to prepare and maintain MOUs that describe their respective roles with regards to matters of common interest and how they intend to comply with their coordination duties set forth in section 3D. With regards to foreign MOUs, section 66 of the FS Act requires the UK Treasury, the Bank of England, the PRA and the FCA to have in place MOUs that outline their intended strategy for co-operation in the execution of their respective functions in relation to membership or foreign organisations. The UK also has separate MOU requirements for purposes of crisis management.[380] Qumba points out that MOUs must be in place between the UK Treasury, the Bank of England and the PRA to set out each party's respective responsibilities during a financial crisis.[381]

https://www.thepfs.org/media/4119720/regulatory_landscape_dec_2012__20_dec_.pdf (accessed 28-08-2023) 12.

[377] Section 3D of the FS Act.

[378] Section 3D of the FS Act.

[379] Qumba 106.

[380] Qumba 108.

[381] Qumba 108.

An interesting power that the PRA has, as discussed above,[382] is the power of veto that entitles the PRA, in times of stress, to prioritise financial stability over consumer protection.[383]

Qumba points out that the existence of a co-ordinating body or bodies is a shared characteristic of Twin Peaks jurisdictions.[384] As was illustrated earlier, the FSCR and the Financial Sector Inter-Ministerial Council are the two bodies established by the FSR Act.[385] Remarkably though, is the fact that the UK does not provide for such a body. Qumba is of the view that the UK's FPC is the closest to such a co-ordinating body.[386] In addition to making proposals to the Bank of England, the UK Treasury, the PRA and the FCA, the FPC has the power to direct the FCA and the PRA with regards to macro-prudential measures.[387]

3.4 Conclusion

The GFC has caused a major tendency toward countries opting to transition to the Twin Peaks model and the UK was no exception. However, as was seen in this dissertation, the Twin Peaks approaches that were adopted by the UK and South Africa respectively, are largely consistent but have some differences though.

As was discussed above, the implementation of the Twin Peaks model in the UK established the PRA, the FCA and the FPC. Whilst the PRA is regarded as a micro-prudential regulator, the FPC is regarded as a macro-prudential regulator. The FCA is the responsible regulator for consumer protection. The PRA is further seen as a part of the Bank of England whilst the FPC is a sub-committee of the Bank.

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[382] See paragraph 3.2.2 above.
[383] Chartered Insurance Institute "Towards Twin Peaks: The UK's Emerging Regulatory Landscape (January 2013 Update) https://www.thepfs.org/media/4119720/regulatory_landscape_dec_2012__20_dec_.pdf 12.
[384] Qumba 110.
[385] See paragraph 2.4 above.
[386] Qumba 110.
[387] Section 9H(1) of the FS Act.

The structure of the UK model therefore differs from the one in South Africa in that the PRA is in essence the Bank of England. By contrast, the PA in South Africa is a distinct entity from the SARB, although located in the same building as the SARB and under its administrative support. Other differences between the UK and South Africa as set out above, is the fact that the Bank of England, acting as the PRA, has the authority to restrain the FCA from acting in specific situations if such actions are likely to endanger the financial system. Furthermore, in South Africa, both the PA and the FSCA are tasked by the FSR Act to assist the SARB in ensuring financial stability. This is, however, not the case in the UK. As was alluded to earlier, in the UK it is only the PRA that is tasked to promote the safety and soundness of financial institutions – this is not an objective of the FCA as opposed to the FSCA.

Regardless of the country, it is critically important to appreciate that a Twin Peaks model will not be effective and efficient in the absence of appropriate collaboration and co-operation amongst the relevant role players.

The FS Act has sufficient co-operation requirements in place, especially in light of potential regulatory overlap between the PRA and the FCA in carrying out their functions. Similar to South Africa, the UK also requires the different regulators to enter into MOUs to give effect to the obligations set out in the FS Act. As indicated above, the UK, contrary to South Africa, has separate MOU requirements for purposes of crisis management in the FS Act. A further distinction between the UK and South African Twin Peaks model is the interesting veto power that the PRA has over the FCA to prioritise the country's financial stability over consumer protection. Another interesting difference between the UK and South Africa model that was alluded to above, is the fact that the UK does not have a co-ordinating body or bodies as is the case in most Twin Peaks jurisdictions, including South Africa.

If one compares the Twin Peaks models that were adopted by South Africa and the UK with their respective distinctions, it becomes evident that it is indeed possible that different variants of the Twin Peaks model can be successful.

Chapter Four:
Conclusion and Recommendations

4.1 Conclusion

As demonstrated in this dissertation, South Africa has historically neglected market conduct regulation. This could be attributed to its preceding silo segmented financial regulation model which focused on the *legal entity* of an institution – as a result, effective prudential and market conduct supervision was neglected. One of the reasons why Twin Peaks was deemed the appropriate model for South Africa was the fact that the model, *inter alia*, promotes consumer protection in an equitable and effective manner. The FSR Act that was subsequently enacted to serve as foundation for the introduction of the Twin Peaks model in South Africa, successfully established the FSCA, responsible for conduct regulation, and the PA, responsible for prudential regulation. However, since the South African model effectively consists of a third peak, the SARB, it is not considered a "pure" Twin Peaks model, but rather a unique one.

One of the most significant changes as a result of the transition to a Twin Peaks model is the fact that the SARB was given an extended financial stability role that was, for the first time, codified into law. Moreover, both the PA and the FSCA is required to support the SARB with its financial stability obligation. In addition, the SARB's duties to regulate and oversee banks were transferred to the PA. Even though the PA operates as a juristic entity, it functions under the administration of the SARB which may raise valid concerns regarding the level of independence between these two entities. Similarly, as the FSCA is accountable to the Minister, it may also question the FSCA's independence status.

Proper and effective co-operation and collaboration between the various regulators and other role players in the financial system is critical for the success of a Twin Peaks model. As was seen in this dissertation, the FSR Act has succeeded in establishing extensive and sufficient co-operation and collaboration requirements. This is essential in order to avoid a silo-based approach of financial regulation as was seen in South Africa prior to the adoption of the Twin Peaks model. In an effort to ensure proper and effective co-operation and cooperation efforts, regulators and other relevant role players are obliged

to enter into MOUs. As pointed out, the FSR Act has put sufficient MOU requirements in place.

An additional benefit that resulted from South Africa implementing a Twin Peaks model, is the requirement in the FSR Act that both the FSCA and the PA should support financial inclusion, in other words, ensuring appropriate access to financial services for all South Africans. The provisions in the FSR Act requiring SIFIs to abide by stricter regulations and be subject to tighter oversight, is a further positive development resulting from the implementation of the Twin Peaks model.

It should be reiterated that the implementation of the FSR Act and the subsequent establishment of the FSCA marked the beginning of efforts to enhance market conduct in South Africa. The next stage of this continuous endeavor is to harmonise all the different pieces of legislation into a single, all-inclusive legal framework (COFI) for market conduct in South Africa.

As indicated, South Africa's Twin Peaks model has various similarities with the model adopted in the UK. Both market conduct regulators (FSCA and FCA) are separate entities from its respective central banks (SARB and the Bank of England). Furthermore, the regulation and supervision of banks were transferred from both countries' central banks to their respective prudential regulators (PA and the PRA). However, in contrast with South Africa's model, the PRA in the UK is part of the Bank of England with the FPC being a sub-committee of the bank, whereas the PA is a separate entity from the SARB, albeit under its administration. In addition, as opposed to South Africa, only the PRA, and not the FCA, has a duty to promote financial stability. In South Africa, this duty is shared by both the PA and the FSCA. As mentioned, the FS Act has also established sufficient co-operation, collaboration and MOU requirements. As discussed, the veto power that the PRA has over the FCA to prioritise financial stability over consumer protection is quite intriguing.

4.2 Recommendations and Lessons Learned

It is said that you should never let a crisis go to waste. The GFC has put South Africa on the back foot and the country has come to the realisation that its financial system needs to conform to the initiatives in global financial regulation that emerged after the GFC. The GFC has demonstrated that the Twin Peaks model is the optimal model of financial regulation where systemic protection and consumer protection are equally valued. As a result of the GFC, South Africa has abandoned its fragmented approach to financial regulation and adopted the Twin Peaks model. The need to safeguard financial customers and stop financial crime served as additional justification for the shift to a Twin Peaks model. South Africa further learned the importance of having two separate and equally important regulators, one to oversee prudential regulation and the other one to oversee conduct of business regulation. This was given effect by the enactment of the FSR Act through which the PA and the FSCA were established, each committed to its exclusive goal of prudential and market conduct regulation and supervision, while simultaneously focusing on financial stability.

Valuable lessons were learnt from the UK. For one, the run on Northern Rock demonstrated the challenges of a single, huge regulator that is in control of supervising and regulating an entire financial sector. It also stressed the importance of a regulatory authority intervening early and taking increasingly strong action if, and when, necessary. In this regard, it appears that South Africa has taken note of that as can be seen from the provisions in the FSR Act that both the PA and the FSCA have a responsibility to carry out their duties "without fear, favor, or prejudice.

As alluded to above, the PRA in the UK has a veto power over the FCA to prioritise financial stability over consumer protection. It is submitted that this is one of the shortcomings of the UK's model as the veto power negates the entire purpose of a Twin Peaks model to place equal weight on prudential and consumer protection. Fortunately, South Africa has not followed suit as the country was in dire need of a dedicated regulator who prioritised consumer protection given that prudential regulation was already well catered for.

As indicated, from the perspective of market conduct, the following stage of the reform process will involve restructuring and harmonising the legal environment by creating a

comprehensive legal framework that governs market conduct in South Africa and is uniformly applied to all financial institutions. It is therefore critical that the proposed COFI Act, that will replace conduct provisions in existing financial sector laws, be finalised as soon as possible to ensure a robust and effective legislative framework for market conduct in the South Africa financial industry.

For a Twin Peaks model to work effectively, it is imperative that prudential and conduct of business work together to support the promotion and preservation of financial stability – the FSR Act sufficiently makes provision for this by explicitly requiring both the PA and the FSCA to assist the SARB in maintaining financial stability. This is, however, not the case in the UK as it is only the PRA that is tasked to promote the safety and soundness of financial institutions – the UK may want to take inspiration from South Africa in this regard.

In addition, one of the most significant changes brought by the adoption of the Twin Peaks model in South Africa, is the fact that the SARB was given a clear statutory mandate by the FSR Act to protect and enhance financial stability in the country. Considering that the SARB's financial stability mandate was not codified in law prior to the adoption of the Twin Peaks model, this was a welcome development and a valuable lesson learned from the GFC. The significance of this is that it informs the SARB what is expected of it in terms of the tasks it must carry out in order to fulfill its mandate. It also gives the SARB a legal basis on which to instruct other regulators and governmental bodies on how to support the preservation of financial stability. When systemic events occur, the SARB is granted legislative authority to address a crisis and prescribe steps to lessen its effects without placing the SARB in a precarious position where regulators might contest its authority to order such steps. Further to this, it is submitted that it is sensible to keep the prudential regulator close to the central bank, as was done in the UK and South Africa, despite the fact that they are not merged into one entity.

In order to ensure the effective and efficient operation of a Twin Peaks model, it is of utmost importance that there must be proper co-operation and collaboration between the various role players in the financial system. This is crucial in order to prevent a silo-based approach, which is evident in silo sectoral models of financial regulation. Adequate

provisions are in place under the FSR Act to promote appropriate co-operation and collaboration amongst the FSCA, PA, and the SARB in the performance of their respective supervisory roles. But having sufficient provisions in place is regrettably insufficient and meaningless if they are not effectively executed. Therefore, regulators and other relevant role players must ensure that strong measures are in place to compel and maintain proper and effective co-operation and cooperation between them since the absence thereof could have adverse consequences. In addition, it is also critical that the required MOUs be reviewed on a regular basis to ensure they remain up to date and relevant. Using such soft law instruments has the benefit of being able to swiftly modify them if it turns out that some of their arrangements are not functioning as intended. As indicated, the UK has separate MOU requirements for purposes of crisis management and South Africa should consider doing the same.

As alluded to above, although other financial regulators, such as the NCR, are part of the Twin Peaks model, they have not been integrated into the PA and the FSCA but function independently. It is, however, recommended that they, especially the NCR, be assimilated into the PA and the FSCA as it is unpractical for the NCR to function independently from the PA and the FSCA given the extent of resources they have and given that the extension of credit entails prudential and market conduct aspects. Furthermore, since both the PA and the FSCA are required to have their own separate mandates and objectives, it is important to avoid regulatory overlap with dual-regulated entities. This is a further reason why robust co-operation and collaboration mechanisms are critical.

The fact that the PA operates in the same building and under the administrative support of the SARB, coupled with the fact that the Deputy Governor of the SARB is in charge of the PA as its CEO, may raise concerns regarding its independence, regardless of the fact that the PA is a separate juristic entity. It is recommended that consideration be given to efforts to limit this perception. However, the fact that the regulation and supervision of banks were withdrawn from the ambit of the SARB and assigned to the PA is without doubt a step in the right direction.

Lastly, it is important to keep in mind that no financial regulation model is set in stone and should progress, grow and adapt in accordance with the country’s economy.

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