A comparative analysis of the Twin Peaks model of financial regulation in South Africa and the United Kingdom

2022 SALJ 78

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https://doi.org/10.47348/SALJ/v139/i1a3

Abstract

This article examines the recent adoption of the Twin Peaks model by the United Kingdom and South Africa. An international and comparative analysis is provided. It observes that there is a gradual paradigm shift across the world towards the Twin Peaks model of financial regulation. There are slight variations in the design of the two countries' Twin Peaks models. The variations in regulatory design indicate the flexibility of the Twin Peaks model and its adaptability to suit local conditions, regulatory culture, and the country's specific needs. Therefore, while the South African model has drawn significantly from the experiences of other Twin Peaks jurisdictions, particularly the UK, South Africa has adopted the model to accommodate its own needs and unique characteristics. It is imperative for the success of the Twin Peaks model that it clearly delineates the objectives and functions of each regulator, and achieves effective co-ordination between them. This article warns that, given the potential overlaps and high levels of co-operation required between the different regulatory bodies in South Africa, there could be detrimental consequences if this complicated financial regulation regime is not properly managed.

Twin Peaks – financial sector regulation – UK – South Africa

I Introduction

This article examines the recent adoption of the Twin Peaks model by the United Kingdom ('UK') and South Africa ('SA'). This has been a fundamental shift. The financial services sector has become one of the defining features and purveyors of economic globalisation. Its positives are undeniable. Its key social functions include the systematic mobilisation of savings, allocation of capital, and management of financial risks. [1] This provides other sectors with much-needed capital, expanding growth opportunities and propelling companies to unprecedented profitability. In fact, the sophistication and robustness of a country's financial services sector significantly determines its growth potential and trajectory, its prosperity, and its level of influence among nations. However, this can conceal the enormous greed and the negative behavioural tendencies of relevant players. Excessive risk-taking exposes the vulnerability of the sector.

It is, thus, a critical but deeply sensitive sector susceptible to different forms of risk. Its sensitivity reflects its centrality to the economy. [2]

Unsurprisingly, regulating the sector has become a common public policy imperative for many countries. Private self-regulation has proven to be catastrophic. [3] The cycles of banking and financial crises across the world have underscored this. Excessive risk-taking, fuelled by perverse incentives and information asymmetry, almost always undermines this ultimate public function. [4] Indeed, the 2008 Global Financial Crisis ('GFC') illustrates the danger of excessive risk-taking and lax regulation to global financial stability. [5] To avoid a recurrence of this outcome, financial systems across the world have been reforming their regulatory architecture, targeting finance and related industries, actors' behaviour, and institutional make-up. [6] According to the UN Commission of Experts on the Reform of the International Monetary and Financial System, 'modern regulation is predicated on a multi-prong approach that includes direct restrictions on behaviour as well as restrictions affecting the determinants of behaviour. The most important determinants are incentives and competition'. [7]

This is understandable because, over the years, financial regulation and supervision in many countries has been organised around specialised agencies that have distinct and separate responsibilities for the banking, securities and insurance industries. However, the emerging trends in recent years have favoured a departure from this institutional model of financial regulation. This model tends to focus on the nature and form of regulated entities as the key regulatory determinants. Thereafter, a separate regulator would be established to oversee the regulated entities. [8] With the increasing sophistication and complexity of financial markets,

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the shortcomings of this model have been exposed. [9] There has been a gradual move towards what is called the 'Twin Peaks' model of financial regulation. This model was first espoused in theory by Michael Taylor in 1994. [10] Operationally pioneered by Australia in 1998, the model has since been adopted by Netherlands, Belgium, New Zealand, the UK and SA. The Twin Peaks model comprises two separate but equal regulators. There is, in the case of SA, the Prudential Authority ('PA'), which is located within, and administered by, the SA Reserve Bank ('SARB'). There is also a market conduct regulator known as the Financial Sector Conduct Authority ('FSCA'), which is responsible for protecting consumers of financial services, thereby promoting confidence in the SA financial system. [11] The responsibility for consumer credit regulation is vested in the National Credit Regulator ('NCR'). The NCR reports to the Department of Trade, Industry and Competition. [12]

The title 'Twin Peaks' in the SA context is a misnomer. This is because the SARB constitutes another 'peak'. The SARB is responsible for monitoring monetary policy and financial stability, including ensuring the safety and reliability of the payment system. In addition, it preserves its traditional role as a lender of last resort and provider of emergency liquidity assistance ('ELA'). [13] Consequently, the SA model is not a 'pure' Twin Peaks system as Taylor originally contemplated. [14] A 'pure' Twin Peaks in this sense is one that consists of two regulators only, one overseeing financial system stability and the other overseeing market conduct and consumer protection. A thorough examination of SA's financial service regulatory framework will be undertaken below. It suffices to say, by contrast, in the UK, the Prudential Regulation Authority ('PRA') is part of the Bank of England. The PRA is in charge of prudential regulation of deposit-taking institutions, systematically important institutions and insurance firms, while the Financial Conduct Authority ('FCA') is responsible for prudential regulation of other financial institutions, consumer protection, and regulation of financial institutions' business conduct. [15] In addition, the most noticeable reform is the establishment of the Financial Policy Committee ('FPC') inside the Bank of England. It is charged with

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the primary responsibility of macro-prudential supervision in order to maintain the overall financial stability of the UK. Finally, the Bank of England remains responsible for dealing with failing banks, oversight of settlement systems, payment system oversight and central counterparty clearing houses. [16]

The main thrust of academic debate concerning the implementation of the Twin Peaks model of financial regulation began in the UK. The Twin Peaks model was adopted as a response to the phenomenon of the 'blurring of boundaries' between the traditional distinction of banking supervision from insurance and investment supervision. [17] Although the Twin Peaks model was originally aimed at the Bank of England, as indicated above, Australia was the first jurisdiction to adopt this regulatory architecture. [18] More recently, international financial institutions have taken a keen interest in the subject of the Twin Peaks model. [19] Even prior to the enactment of the Financial Sector Regulation Act 9 of 2017 ('FSRA') in SA, the Twin Peaks model of financial regulation had attracted a significant amount of scholarly discourse in both international and SA law journals, highlighting the advantages and disadvantages of a Twin Peaks model vis-à-vis the other models of financial regulation. Scholars such as Schmulow and Godwin have written a series of papers examining the virtues of the Twin Peaks model as an optimal structure of financial regulation. [20] They have advanced further arguments on the advantages of the Twin Peaks model of financial regulation. These include

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> 'the clear mandates and objectives to which both the prudential regulator and market conduct regulator under the Twin Peaks system are exclusively dedicated; avoidance of concentration of power in a single agency; less susceptibility to internal conflicts of interests that may arise as result of housing two functions under one roof; the fact that there is no mixing of culture between regulatory and supervisory agencies; transparency in resolving conflicts when they arise; and less domination of one regulatory agency by another'. [21]

This article builds on that work and other related work to take stock of various developments relating to the organisational structure of the Twin Peaks model of financial regulation. [22] It examines the Twin Peaks model and structural developments relating to financial services regulation in SA and the UK. It argues that without sufficient experience and relevant empirical evidence on the effectiveness of this model, it is difficult to come to firm conclusions regarding the optimal structure of the Twin Peaks approach to financial regulation. It adopts a comparative method of analysis to examine the key issues confronting financial services regulation in SA and the UK. The justification for comparing these jurisdictions is the historical links they share, especially as regards financial services regulation and supervision. In fact, the new model in SA has drawn significantly from the experience of the other Twin Peaks jurisdictions, particularly the UK. However, the article shows that both jurisdictions have adopted the Twin Peaks model of financial regulation, with some variations, to try to ensure financial system reliability in the aftermath of the GFC.

The article investigates the extent to which there is uniformity in the design and implementation of the respective Twin Peaks models in the context of the various policy choices that SA and the UK had to make. The remainder of the article is structured as follows: part II discusses the triggers for the adoption of the Twin Peaks model in both selected jurisdictions; part III examines operational issues for the Twin Peaks model; part IV considers the design of the Twin Peaks structure, the location of the PA, and the objectives and functions of regulators; part V assesses the institutional and operational independence of the regulators; part VI looks at co-ordination and information sharing; and part VII explores the differences and similarities between the UK and the SA Twin Peaks models, before I offer some concluding remarks.

II The triggers for the adoption of the Twin Peaks model of financial regulation

Although the policy objectives informing the adoption of the Twin Peaks model appear to be the same across jurisdictions, the historical factors which influenced the respective adoption of the Twin Peaks model vary from jurisdiction to jurisdiction. In addition, there are fundamental contextual variations across jurisdictions.

(a) South Africa

As is the case with most previous financial crises, the 2008 GFC triggered a wave of financial sector reforms across the world. [23] The GFC was caused, at least in part, by poor regulatory frameworks in financial services. [24] The model of financial regulation that was operationalised in SA at the time of the 2008 GFC was the sectoral regulatory framework, where a number of sectoral regulators supervised different financial institutions and entities. Under this model of financial regulation, the country's financial sector was able to weather the 2008 GFC fairly well. [25] In addition, the country's financial system was not severely affected by the crisis due to 'prudent economic, fiscal and financial sector policies', a 'robust monetary policy framework' which absorbed external shocks, counter-cyclical monetary and fiscal policies, and limited extension of credits. [26]

However, despite the relative insulation of SA's financial system from the crisis, the country proceeded to overhaul its financial regulatory framework by adopting an institutional structure radically different from the previous model, thereby raising concerns for possible

'regulatory mismatch' or the potential non-alignment between the adopted regulatory frameworks and the financial stability objectives of the system. To that end, the International Monetary Fund ('IMF') noted that a challenge for SA's financial regulation was to introduce a Twin Peaks regulatory framework in a manner that did not undermine the current high-quality oversight of banks. [27] This could be even costlier than 'regulatory gap'. The perceived shortcomings of the previous sectoral model in SA were different from the experience of a dismal failure of the tripartite system in the UK.

The tripartite system refers to the three institutions previously involved in financial regulation in the UK, namely the Financial Service Authority ('FSA'), the Bank of England, and Her Majesty's ('HM') Treasury. Before the adoption of Twin Peaks, SA operated a 'silo' financial regulatory framework in which various regulators regulated different financial market players. This sectoral regulatory approach allowed entities to be regulated according to their legal form. Although this model had withstood the GFC, the National Treasury described it as 'a fragmented model, resulting in silo approach to regulation of various industries, with different standard and regulation applying to different industries . . . allowing for regulatory arbitrage'. [28] Thus, the primary objection to the sectoral model in SA was the involvement of multiple regulatory authorities with responsibilities for financial sector regulation, each with substantially different powers and functions. Therefore, the country's regulatory framework was considered to be best served by a 'departure from the sectoral model of financial regulation'. [29]

The factors motivating the adoption of the Twin Peaks model were articulated by the SA government in its policy document entitled 'A safer financial sector to serve South Africa better' (known as the Redbook). [30] Following the approval in July 2011 of a shift to the Twin Peaks model, efforts were made to domesticate the new model while avoiding the identified pitfalls that had emerged in its operationalisation in other jurisdictions. One of the justifications for this shift was the desire to deepen transparency and accountability in the financial markets. The government reasoned thus:

> 'The Twin Peaks approach is regarded as the optimal means of ensuring that transparency, market integrity and consumer protection receive sufficient priority and given South Africa's neglect of market conduct regulation, a dedicated regulator responsible for consumer protection and not automatically presumed to be subservient to prudential concerns, is probably the most appropriate way to address this issue. In addition, the existence of separate prudential and market conduct regulators may be a way of creating a system of checks and balances, thereby avoiding the vesting of too much power in the hands of a single agency.' [31]

A detailed follow-up document was published by the Treasury on 1 February 2013, entitled 'Implementing a Twin Peaks model of financial regulation in South Africa'. [32] The document set out the process it intended to follow, and highlighted important policy choices for the SA Twin Peaks system. [33]

Another reason for SA's adoption of the Twin Peaks system related to the international commitment to a sound and safe regulatory framework. [34] In its review of the SA financial system, the National Treasury pointed out that in the international environment there is a significant interconnectedness between financial institutions, meaning that a crisis in one jurisdiction could spread as a result of contagion to the SA financial system. [35] Adding to the need to reform the SA financial sector, the IMF and the World Bank have conducted a financial sector assessment programme, in terms of which they performed a joint assessment of the SA financial system. The main findings from the joint assessment programme were that the country needed reform that would focus on effective prudential and market conduct supervision despite the fact that the SA financial system had survived the GFC fairly well with its previous sectoral model. [36]

Thus, the motivation was to align SA's financial system with the international trends in financial regulation that had emerged after the GFC. Taking into account lessons learnt from the GFC and its international commitments, the SA government therefore introduced the Twin Peaks model of financial regulation. [37] Specifically, the country's Twin Peaks approach followed the G20 meeting in November 2010, where it had committed itself to a stronger financial regulatory framework to address regulatory gaps; to ensuring effective supervision of regulated

entities by strengthening the powers of regulators; to ensuring effective crisis resolution for systemic/important regulated entities in order to contain the possible impact of systemic failure or collapse; and to subjecting its regulatory standard to international assessment and peer review on the basis of international standards. [38] The adoption of the SA Twin Peaks system was largely a response to these international commitments. [39]

The aim of the SA government was to pre-empt any potential contagion by following acceptable, robust standards in financial regulation and supervision. SA is a member of several international organisations such as the IMF, the Financial Stability Board, the Bank for International Settlement, the Financial Action Task Force, the Basel Committee on Banking Supervision, the Committee on Payment and Settlement systems, the International Association of Deposit Insurers, the International Auditing and Assurance Standard Board, the International Accounting Standard Board, and the International Organization of Securities Commission. Some of the standards emanating from these organisations had the character of a binding nature. A uniform adoption, it was assumed, would forestall a global collapse of the world financial system and ensure better international co-ordination. [40]

In addition, the move towards the Twin Peaks model was also influenced by the increasing innovation in product design, the blurring of sectoral boundaries between financial firms and between markets and between products, and the risk of regulatory arbitrage where firms could take advantage of inconsistencies between the approaches and standards of competing regulators. [41] After considering other approaches to financial regulation, such as the institutional and functional approaches to financial regulation, the SA Treasury settled on the Twin Peaks model as the optimal approach for the country. The idea was that the financial sector would be made safer through a comprehensive financial stability framework and stronger prudential and market conduct frameworks. [42]

A further motivating factor for SA's adoption of the Twin Peaks system is the size and concentration of its banking sector. The banking system in SA is highly concentrated and is an environment where the largest banks dominate. These include Standard Bank, FirstRand Bank ('FNB/RMB'), ABSA Bank, Nedbank, Investec Bank and Capitec Bank. These financial conglomerates maintain a 90 per cent market share of total banking assets.

This concentration can be attributed to the high entry barriers imposed by the Banks Act 94 of 1990. Therefore, the adoption of the Twin Peaks model to separate market from prudential regulation is unsurprising in such an environment, since there could be risks of regulatory overlap and conflict of interest if the market conduct regulator and the prudential regulator were the same. [43]

SA's Twin Peaks model established two separate regulators: the market conduct regulator — the FSCA — and a prudential regulator — the PA. [44] Consequently, both the FSB, which had been vested with the responsibility for the market conduct and prudential regulation and supervision of the non-banking institutions, and the Bank Supervision Department, which had been vested with the responsibility for prudential regulation and supervision of banking institutions, ceased to exist. While the FSCA is a stand-alone entity separate from the central bank, the PA is an entity that falls under the administrative support of the SARB. Thus, the PA is tasked with micro-prudential supervision whilst the SARB continues, amongst other things, to be responsible for macro-prudential supervision and overseeing the overall financial stability of the sector. The FSCA is responsible for protecting consumers of financial services and promoting confidence in SA's financial system by regulating and supervising the market conduct of all financial service providers, including banks, insurers, financial advisers, financial intermediaries, investment institutions and the broader financial markets. [45] In contrast to the UK's model, under the SA Twin Peaks system, the responsibility for consumer credit regulation is retained by the NCR, which reports to the Department of Trade, Industry and Competition. The NCR operates independently as a credit market regulator within the Twin Peaks model, but within the constraints of the network for mandatory co-operation and collaboration created in terms of the SA Twin Peaks model. The challenge, however, is that the existence of two market conduct regulators in relation to banking and credit provision is likely to create overlaps and hence regulatory challenges between the FSCA and the NCR. [46]

(b) The United Kingdom

The UK's Twin Peaks model predates SA's. Unlike the political and socio-economic contexts of SA, the UK's financial system reforms have often been intrinsically linked to party politics and the political orientations of the government driving these reforms. [47] For instance, within days of coming into power in 1997, the Labour government announced its intention to engage in a fundamental reform of the UK's institutional arrangements for the supervision of financial market activities, aimed at stripping the Bank of England of its supervisory functions. While the previous FSA had been the creation of a Labour government, the UK's coalition government launched this fundamental reform of the financial services regulatory architecture by introducing the third radical restructuring of the UK's financial services regulation since 1986. [48] The decision to overhaul the UK's regulatory system was as a result of the recognition that the tripartite arrangement between HM Treasury, the Bank of England, and the FSA had failed to detect and cope with the 2008 GFC. [49] Although the FSA was a super-regulator with responsibilities for both market conduct and prudential supervision, the tripartite system was collectively responsible for the financial stability of the UK's financial system. [50] The unified approach or 'super regulator' was previously championed by the UK prior to its adoption of the Twin Peaks model. [51] Prior to the GFC, the unified approach to financial regulation had enjoyed high regard as an exemplar of excellence, particularly in smaller economies where it was deemed to be a reasonably effective method of financial regulation to gain oversight over the available range of financial services. [52] The Group of 30 described the unified model in its 2008 report as

> '[a] model of an efficient and effective regulator, not only because of its streamlined model of regulation but also because it adheres to a series of principles of good regulation which centre on efficiency and economy, the role of management proportionality, innovation, the international character of financial services and competition. This overlay of pragmatic

> business principles in addition to the traditional goals of regulation has been a distinguishing feature of the UK's regulatory approach.' [53]

However, even at the time, its major shortcoming was regarded as its capacity to present a single point of regulatory failure. This failure of the unified approach was clearly evident during the GFC. The downfall of the tripartite system was characterised by the failure to identify the problems that were building up to the crisis in the UK's financial system, its failure to take steps to mitigate the crisis before significant financial instability, and the failure to deal effectively with the crisis, especially during its formative stages. Most fundamentally, there were inherent weaknesses and contradictions that were identified in the tripartite arrangement. The first was the placing of the entire financial regulation under the ambit of a single FSA. This meant that the FSA had to cover a wide variety of issues, ranging from the safety and soundness of the largest global investment banks to the customer practices of smaller financial advisors. The second problem related to the statutory obligation placed upon the Bank of England through the Banking Act, 2009 for financial stability, without its having the appropriate tools to carry out this responsibility effectively and efficiently. Lastly, the Treasury was granted the responsibility to maintain the overall institutional framework, with no clear mandate on how to deal with crisis: consequently, tens of thousands of billions of public funds were put at risk. [54]

Lord Turner, the former chairman of the FSA, said that the most obvious failing of the UK system was the fact that no single institution had the power and authority to monitor the system as a whole, to identify the potential destabilising trends, and to take concerted action to respond to them. [55] Furthermore, the FSA had failed to strike the right balance between prudential supervision and conduct-of-business supervision, focusing more on the latter. Therefore, prudential supervision received insufficient attention. According to Lord Turner, in the run-up to the financial crisis, financial supervision relied heavily on 'tick box' compliance with rules and directives at the expense of in-depth and strategic analysis. [56] This is contrary to the standard of effectiveness in the regulation of firms which requires a thorough understanding of the firm's business model and its ability to make judgements about financial risk. The FSA was severely criticised for inadequate regulation and supervision of banks and wholesale capital markets, and for failing to contain systemic risks. The lack of co-ordination between regulators, and confusing regulatory responsibilities, were identified as the major deficiencies of the

UK financial system during the crisis. [57] The failure of the Northern Rock Bank revealed the major weaknesses in the process of crisis management, and a lack of co-ordination and division of responsibilities between the critical role players, the Bank of England, the FSA and the Treasury. [58] As the crisis unfolded, there was no consensus on how to respond.

In its evidence to the Joint Committee on the draft Financial Service Bill, the Bank of England acknowledged that there was an inherent cultural conflict between market conduct and prudential regulation. According to the Bank of England, the adoption of the super-regulator model under the FSA exposed these cultural conflicts and weaknesses:

> 'The market conduct supervisor can measure its success by enforcement, convictions, and fines. Whereas the prudential regulator focuses on the continued prudent management of the firms in the interest of the financial system as whole. Putting these two cultures together was a mistake and in our view directly contributed to the FSA's taking its eye off the prudential risks in a number of major financial institutions.' [59]

Adding to the barrage of criticisms in the aftermath of the GFC, several conclusions were reached regarding the performance of the FSA. One of the findings was that

> '[o]n occasions, the tripartite system, namely the Bank of England, HM Treasury and the FSA functioned with "Jaw dropping" incompetence and chaos. Serious regulatory failure has contributed to the failings in banking standards. The misjudgement of the risks in the pre-crisis period was reinforced by a regulatory approach focused on detailed rules and process which all but guaranteed that big risks would be missed. Scandals relating to misselling by banks were allowed to assume vast proportions in part because of the slowness and inadequacy of the regulatory response.' [60]

Unsurprisingly, the newly introduced Twin Peaks system in the UK entails a clear focus on splitting prudential and conduct regulation for banks and insurers. Interestingly, there were counter-arguments to the adoption of the Twin Peaks system in the UK. While the FSA candidly acknowledged that it had failed to strike a balance between prudential supervision and conduct of business supervision, the critics of the newly adopted Twin Peaks system questioned whether the FSA was beyond repair because of its failure to pay sufficient attention to prudential matters. They argued that the FSA suffered a particularly harsh fate, because many of the prudential problems causing the financial crisis stemmed from the misconceptions and misguided assumptions which formed the basis of the EU Capital Requirement Directive which the FSA had to adopt as

the competent authority in the UK. This directive followed Basel II of the internationally agreed capital adequacy framework, which was based on the wrong assumption of self-correcting market discipline, especially in the leading economies. Critics argued that such role was a shared responsibility between the tripartite arrangement as a whole, rather than a fault of a single FSA. [61]

Furthermore, some commentators were not convinced that the newly adopted Twin Peaks model was the optimal regulatory architecture. For instance, expert evidence given before the Joint Committee on the Draft Financial Service Bill suggested that

> '[w]e don't believe that there is a correct approach. Integrated regulators like the FSA and the Twin Peaks model such as that proposed by government, both have advantages and disadvantages. We look for a regulatory framework which will secure framework for effective competition, protect consumers and engender trust and confidence in financial services and ensure the UK remains internationally competitive.' [62]

Notably, around February 2009 Sir John Gieve, the then outgoing Deputy Governor of Financial Stability, revealed that he was not convinced that there was a clear superior arrangement to the then unified approach of the UK. [63] He argued that it was not clear that any country had done much better than others under the GFC, despite differences in regulatory structure. While the FSA could clearly not be insulated from blame, it was reasonable to conclude that disbanding the FSA and the subsequent reform of the UK regulatory structure was ultimately a politically driven decision.

Accepting this to be the case, at the core of the reform of the UK's regulatory objective was positioning the Bank of England at the centre of supervision of the UK's financial system and disbanding the FSA. The reform efforts in the UK culminated in the promulgation of the Financial Services Act, 2012, which replaced the FSA with the PRA and the FCA. Thus, the reforms introduced a Twin Peaks financial regulatory model into the UK's financial system by splitting the regulatory and supervisory functions between two regulators: the PRA and the Market Conduct Authority. [64] Under the legislative reform in the UK, the responsibilities for prudential supervision were moved back to the Bank of England, to be exercised by its subsidiary, the PRA. [65]

The FSA was renamed the FCA and left with its original mandate, but it was also given a competition objective and the responsibility for consumer credit regulation that was previously the responsibility of the Office of the Fair Trading. [66]

As in other jurisdictions, the Bank of England became responsible for macro-prudential supervision. It exercises this responsibility through the newly established FPC. The FPC is a statutory sub-committee of the Bank of England and its membership comprises the Governor, the three Deputy Governors, the Chief Executive of the FCA, the bank's Executive Director for financial stability, strategy and risk, external members appointed by the chancellor of exchequer, and non-voting representation from the Treasury. [67] The FPC has the power to give directions to the PRA and the FCA in respect of macro-prudential matters, make recommendations to the Bank of England, the PRA and the FCA, and prepare financial stability reports. [68] In addition, the responsibility for the prosecution of economic crimes such as insider dealing has been conferred on the Economic Crime Agency. [69] Furthermore, the co-ordination is facilitated through cross-membership: the Chief Executive of the PRA is also a deputy governor of the Bank of England, the chief executives of the FCA and the PRA sit on each other's boards, and are both members of the FPC. [70]

III Operationalising the Twin Peaks system

Invariably, some important institutional and structural issues needed to be considered when a country such as SA decided to move towards a Twin Peaks model. First, there was the issue of recruiting highly qualified personnel and the training of various financial sector regulators and supervisors on how to manage and conduct a Twin Peaks model of financial supervision, since the transition from sectoral supervisory agencies to a Twin Peaks approach could lead to a hiatus in regulation, until a Twin Peaks model was up and running and its credibility was established. The second key issue was the importance of having a panel of experts to advise and to oversee a smooth transition. The third was the importance of having proper transition management to avoid the attrition of key staff members. This aspect is particularly important when the transition is in different phases — for instance, where a market conduct regulator is to be incorporated at a later stage, or where there is uncertainty as to whether a big-bang approach is better than a two-step process. Finally, there was the issue of providing functional and operational independence of the Twin

Peaks regulatory agencies, as well as issues concerning the accountability and the governance structure of the Twin Peaks regulators.

Regarding the regulatory arrangement, critical questions needed to be addressed, such as who has the power to appoint Twin Peaks regulators' personnel, and what their tenure of office would be. Also, under what circumstances could regulators be dismissed? Would the regulators be granted functional immunity from court proceedings for omissions or acts committed in the course and within the scope of their operations? How would the officials and regulators of the previous regulatory agency be transitioned into the newly established Twin Peaks regulatory agencies? How would the operation of the regulatory agencies be funded? [71] Could the market players approach the court of law for the review of the decision taken by the regulatory agency? What mechanisms would be in place to ensure the effective and efficient flow of information? Would there be any meaningful co-operation between the market conduct regulator, the prudential regulator and, say, the Ministry of Finance and the SARB?

Worldwide, experience suggests that in order to ensure better outcomes for financial customers and the wider economy, a country must consider the efficient and effective flow of information among relevant stakeholders. Put differently, the financial sector regulators, the national treasury, the central bank and other relevant stakeholders must co-operate and consult each other in performing their functions. They must also share information about matters of common interest. [72] There must also be a delegation of powers and duties between the market conduct regulator and the prudential authority, and there must be a mechanism in place to determine how differences between them will be resolved. [73] The comparative analysis set out below examines how these issues were dealt with in the UK and SA respectively.

IV The design of the Twin Peaks structure

Determining where the regulator should be housed is one of the key considerations for the functioning of the Twin Peaks model. In general, there are three options. First, a jurisdiction may establish a prudential regulator as a separate entity entirely outside the central

bank. Secondly, a prudential regulator may be established as a subsidiary of the central bank. Thirdly, the prudential regulator may exist within the central bank. Concerning the first option, it is worth pointing out that Australia is the only notable jurisdiction currently having the prudential regulator outside the Reserve Bank of Australia. [74] Following the Wallis enquiry into the Australian financial system, it was believed that the separation between the Reserve Bank of Australia and the Australian Prudential Regulator would allow each to focus clearly on their primary objectives, and would clarify the lines of accountability in the performance of their regulatory tasks. [75] The two jurisdictions considered in this article have opted for the prudential regulator to exist within their central bank, with some variations.

(a) Prudential authority: Inside or outside the central bank

Prior to the introduction of the Twin Peaks model in the UK, the prudential regulator was established as a subsidiary of the Bank of England. [76] Two justifications were advanced to rationalise having the prudential regulator operating as a subsidiary of the central bank. The first was that the functions of the monetary policy and the prudential policy were interlinked. Therefore, to achieve the best regulatory outcome, it was considered that the close relationship between the central bank and the prudential regulator would be desirable. Secondly, it was believed the Bank of England would compel the prudential regulator to take regulatory actions, and as a result there might be less risk of regulatory gaps. However, with the statutory enactment of the Financial Services Act, 2012, the PRA ceased to be a subsidiary of the Bank of England. Instead, the Act constitutes the Bank of England as the prudential regulator. [77] The bank performs this function through its newly established committee, called the Prudential Regulation Committee. [78] The central bank is an obvious choice for this function, given the interconnectedness between monetary policy and prudential regulation. It has been argued that the purpose of this reform is to 'maximise the synergies of having monetary policy, macro-prudential policy and micro-prudential policy under the aegis of one institution'. [79] The notion of achieving synergies is buttressed by the perception that the Bank of England — with its highly

specialised personnel, set of skills, processes and experience — is best suited to undertake the task of prudential supervision. [80]

By contrast, the most significant change introduced by the SA Twin Peaks system is that it excises banking supervision and regulation from the remit of the SARB and replaces its Banking Supervision Department with a separate and independent PA established under the FSRA. [81] It should be pointed out that after the enactment of the FSRA the PA enjoys the powers previously demarcated to the Registrar of Banks, and therefore has the powers and obligations to act in accordance with the provisions of the Mutual Banks Act 124 of 1993 and the Banks Act when seeking the winding up of a bank or a Mutual Bank. Accordingly, the Banks Act has been amended to provide that the banks will be supervised by the PA rather than the Bank Supervision Department ('BSD') of the SARB. [82] Section 32(2) of the FSRA describes the PA as a separate legal entity housed within the SARB. [83] It has been observed that in structuring the SA model, the national government seems to have drawn inspiration from the UK's previous regulatory framework, where the prudential regulator was originally established as a subsidiary of the Bank of England. [84]

In terms of s 34 of the FSRA, the PA is mandated to supervise institutions in accordance with financial laws in order to achieve its objectives. Section 34(2) also states that the PA must also perform any other function conferred on it in terms of the FSRA or any other legislation. The PA therefore functions as a system-wide prudential regulator that is tasked with overseeing all financial institutions, and not merely banks. [85] It has been allocated supervisory roles over banks, insurers and pension funds. It has a wider regulatory scope than the previous BSD of the SARB. For example, the PA has a responsibility under the Insurance Act 18 of 2017 to supervise insurers in order to promote and enhance the safety and soundness of those institutions. It also has a responsibility to protect policy holders against the risk that insurers may fail to meet their obligations. It is, however, questionable whether the PA possesses proper competencies for supervising systematically important investment firms and insurance companies. Put differently, it is debatable whether the PA can cover the entire market in a competent manner. This is because it is entirely a new system. Operationalising a new regulatory framework without adequate manpower and technical competence to guarantee stability could be problematic.

So, what then is the preferable regime? There is no definitive answer as to which regime is preferable. Some have argued that there are synergies and efficiencies enjoyed by locating the prudential regulator within the central bank. [86] Also, it can be argued that periods of financial distress require swift responses and decisive actions. Insufficient co-ordination between multiple agencies could stifle this. Citing the failure of the UK's Northern Rock Bank as an example, some commentators assert that co-ordination between the Bank of England, the FSA and the Treasury of the UK proved to be inadequate to address financial stress during the 2008 GFC. [87] Indeed, there is a good argument to be made in favour of locating the prudential authority inside the central bank, especially for developing countries with constrained resources to establish a separate body, such as SA. Under the SA Twin Peaks model, for instance, the rationale for providing the PA with the administrative support of the Reserve Bank relates to economies of scale in order to ease the sharing of resources, such as IT systems and other resources, to save costs. It was motivated by the need for easy collaboration and the sharing of information between the SARB and the PA. As a result, a key officer of the SARB, the Deputy Governor, is now heading the PA as its Chief Executive Officer ('CEO'). [88] Therefore, the notion of achieving synergies is reflected in the view that the central bank — with its highly specialised set of skills, processes and experience — is best situated to undertake the task of prudential supervision. There is logic in this argument, particularly given the interconnected nature of monetary policy and prudential regulation. The counter argument is that this in itself creates a conflict because the priorities of prudential supervision and monetary policy are at times contradictory. However, the SA position balances these concerns in that it is the SARB that is responsible for monetary policy, while the PA deals with the regulation and supervision of financial institutions.

Most fundamentally, in jurisdictions lacking a strong tradition of independent regulatory agencies, there may be advantages to be gained by locating the prudential regulator within the central bank, provided that the central bank has a strong tradition of independence. The independence of the SARB is instructive, because the independence of SARB is entrenched under the Constitution:

> 'The South African Reserve Bank, in pursuit of its primary object, must perform its functions independently and without fear, favour or prejudice, but there must be regular consultation between the Bank and the Cabinet member responsible for national financial matters.' [89]

Therefore, as Schmulow asserts, with the strong constitutional independence and reputational status of the central bank, it is easier to extend similar competencies to a PA located within the SARB. [90] It can be concluded that this consideration was instrumental in establishing the PA within the SARB, since the latter already enjoys a strong tradition of independence.

However, it can also be argued that the separation of the prudential regulator as an independent entity from the central bank is necessary. In this regard, Goodhart asserts that the central bank 'should not do everything'. [91] Put differently, the central bank and the prudential regulator should be distinct entities with dedicated responsibilities that are separate from each other. This is to avoid the overconcentration of power in the central bank. In addition, the location of the PA within the SARB may have other consequences because the failure of the PA may cause reputational risks, and this could undermine the long-standing tradition of the independence of the SARB. [92] It has been argued that separating the central bank from the PA may insulate the central bank from reputational harm, as it was the case with Health International Holdings Limited ('HIH'), the Australian insurer. Market confidence in the central bank's price stability mandate could be undermined if its competence in other areas is questioned. In this regard, it has been argued that the approach in which the regulator is a separate entity, as in Australia, is the optimal approach to insulate the regulator from political and industry interference. [93] Furthermore, in SA's case, the issue of administrative support raises questions about the PA's institutional and operational independence from the SARB. This is because of the potential for overlap, which might be problematic.

(b) The objectives and functions of regulators

This sub-part considers the objectives and functions of the market conduct and prudential regulators in both the UK and SA. Both the Basel Core Principles for Effective Banking Supervision and the Insurance Core Principles ('ICP') require that there should be clarity of responsibilities and objectives for regulators to operate optimally. For instance, the Basel Core Principle 1 requires that 'an effective system of banking supervision should have clear responsibilities and objectives for each authority involved in the supervision of banks and banking groups'. [94] A suitable legal framework for banking supervision is in place to provide each responsible authority with the necessary legal powers to authorise banks, conduct ongoing supervision, address compliance with the laws, and undertake timely corrective actions to address safety and soundness concerns. [95] Similarly, ICP1 states that 'the authority (or authorities) responsible for insurance supervision and objectives of insurance supervision should be clearly defined'. [96]

(c) The functions and objectives of the prudential regulator

The PRA in the UK is a micro prudential regulatory authority with a duty to ensure effective prudential regulation of deposit takers, insurers and investment firms. Its general objective is to promote the safety and soundness of financial firms primarily by ensuring that these firms are managed in a manner that avoids adverse effects on overall financial stability. [97] The intention is to minimise the adverse effects of disruption on the continuity of financial services that may be caused by a failure of financial institutions. In the event of the failure of these firms, the PRA has the responsibility to ensure that such failure does not spread to the entire UK financial system. Furthermore, one of its objectives is to have regard to 'the need to minimize any adverse effect on competition in the relevant markets' which may result from the manner in which the PRA discharges those functions. [98] The rationale behind this secondary competition objective was articulated by the Committee on the Draft Financial Service Bill as follows:

> 'Competition within the ?nancial sector is an important part of developing a stronger, more diverse system. The actions of the PRA have the potential to affect the costs of individual ?rms or of particular types of institution, and affect the barriers to entry and expansion in the market. While the need to protect and promote competition in the sector should not dictate the actions of the PRA . . . we believe it is a factor that ought to be considered in the course of PRA decision making.' [99]

In SA's case, the FSRA [100] establishes the PA, which was previously known as the Office of the Registrar of Banks, and confers upon it the mandate of banking supervision and prudential supervision of insurers. [101] Its objective is to regulate and supervise financial institutions that provide financial products and securities services in order to enhance the safety and soundness of the financial institutions and also that of market infrastructures. It also has the objective of protecting consumers of financial services against the risk that financial institutions under its supervision may fail to meet their obligations. Similar to other regulatory agencies, one of its objectives is to assist the SARB to maintain financial stability. The PA is also obliged to support sustainable competition in the provision of the financial services and financial products, and must co-operate and collaborate with the Competition Commission. [103] It is also responsible for supporting financial inclusion. [104] Presumably, the support for financial inclusion is meant to encourage transformation in the industry and to discourage the concentration of the industry through the creation of smaller, more competitive banks, insurance houses, agencies and brokers.

(d) The functions and objectives of the market conduct regulators

Under the Financial Service Act, 2012, the FCA in the UK is charged with the strategic objective of ensuring that relevant markets are functioning optimally. In addition to this strategic objective, the FCA has three additional operational objectives. The first is the consumer protection objective. This objective is meant to secure the appropriate degree of protection for consumers. The second objective is to protect the integrity of the UK financial markets. The third objective is to promote effective competition in the interests of consumers of regulated financial services

and those of services provided by recognised investment exchanges which carry out certain regulated activities. [105] It is important to observe that no express financial stability mandate is given to the UK's FCA. Instead, the focus is on the creation of a competitive environment for the UK's financial market. In the UK, not only does the FCA have a 'competition objective' as one of its operational objectives, but it is also obliged to discharge its general functions in a way that promotes competition in the interests of consumers. Furthermore, the FCA may ask the Office of Fair Trading ('OFT') to consider whether any feature, or combination of features, of a market in the UK for financial services may prevent, restrict or distort competition in connection with the supply or acquisition of any financial services in the UK or a part of the UK. [106]

Under SA's FSRA, the FSCA has substantially the same objectives as the FCA in the UK. In terms of s 57 of the FSRA, the objectives of the FSCA are to enhance and support the efficiency and integrity of financial markets; to protect customers by promoting fair treatment by financial institutions; and to offer customers and potential customers some financial education programmes, thereby promoting financial literacy and the ability of customers and potential customers to make sound financial decisions. [107] The last-mentioned, it is assumed, would assist in maintaining financial stability. Financial illiteracy is surely more of a concern in SA than in the UK. Unlike in the UK, the FSCA in SA is not required to have regard to the competition objective. However, in terms of s 58 of the FSRA, the FSCA is at least required to promote sustainable competition to the extent consistent with its objectives, and must co-operate with the Competition Commission. [108]

V Institutional and operational independence of regulators

The Basel Core Principles on Banking Supervision dealing with independence, accountability and regulatory supervision state:

> 'The supervisors possess operational independence, transparent processes, sound governance, budgetary processes that do not undermine autonomy and adequate resources and is accountable for discharge of its duties and use of its resources. The legal protection for banking supervision includes protection of the supervisors.' [109]

Similar provisions are also found in the ICP. The ICP requires that the 'the supervisor is operationally independent, accountable and transparent in the exercise of its responsibilities and powers and has adequate resources to discharge its responsibilities'. [110] In the context of the FSRA, therefore, both the Basel Core Principles on Banking Supervision and the ICP remind us that the interpretation of the FSRA, though a domestic statute, should be measured against these international soft-law instruments, rather than being interpreted in isolation, especially because the change in the financial regulatory structure of the SA financial system was heavily influenced by a range of international soft-law instruments. The FSRA itself buttresses this view by requiring the prudential regulator 'to the extent practicable[,] to have regard to international regulatory and supervisory standards' set by international standard-setting bodies. [111] It can be argued that a country's legislative framework should ensure that supervisors have powers and operational independence to carry out proportionate and effective supervision of such institutions without government or industry interference.

(a) The independence of the prudential regulator

With respect to SA, the IMF has noted that 'the objectives and operational independence of the supervisors should be enshrined in legislation, which should clarify the conditions for the minister's intervention and limit his involvement to absolutely necessary situations'. [112] The FSRA provides that the PA is not a public entity in terms of the Public Finance Management Act 1 of 1999, which suggests that the government does not have control over the PA. [113] The PA is given administrative support by the SARB. To strengthen its independence, s 32(5) of the FSRA states that the PA must perform its functions without fear or favour. [114] But the question is, how independent is the PA from the SARB? With regard to the institutional and operational independence of the PA, s 32(2) of the FSRA provides that the PA is a juristic person operating under the administration of the SARB. [115] However, despite the PA being under the administration of the SARB, it can be argued that the FSRA should give equal status to the PA and the SARB. Since the PA is a juristic entity empowered to act in its own name and to enter into contractual agreements, it stands to reason

that it may sue or be sued separately from the SARB. These entities are two distinct entities with separate legal identities in law, and have different mandates and objectives. Clearly, therefore, the separation of the PA from the central bank as a legal person indicates its institutional and operational independence from the SARB.

In terms of operational independence, it is submitted that the FSRA grants too much power to the Governor of the SARB. This is pursuant to s 17 of the FSRA, which mandates the sharing of information about financial institutions that are facing financial difficulties with the SARB Governor. [116] Under the same section, the financial sector regulators are required to consult the Governor of the SARB before exercising any of their powers dealing with systemic risks of financial institutions. [117] In addition, s 18 of the FSRA removes the role of the Minister of Finance in giving any direction to the PA. It however grants power to the Governor to issue directives on how financial regulatory authorities should perform their functions in preventing the disruption of the financial system. If the PA is truly independent, then why should the sharing of information with the Minister of Finance pass through the Governor?

Many other factors may undermine the independence of the PA from the SARB. There is the issue of the appointment of the CEO of the PA, who manages the day-to-day operations and administrative functions of the PA. Section 36 of the FSRA grants the power to appoint a CEO to the Governor of the SARB, with the concurrence of the Minister of Finance. [118] The CEO is also ex officio a Deputy Governor of the SARB, and it is at the sole discretion of the Governor to extend the CEO's term of office. [119] Under s 39(1) of the FSRA, the Governor, after due process, is empowered to remove the CEO from the PA if the CEO becomes a disqualified person. [120]

The concentration of power on the SARB Governor raises critical questions about the operational independence of the PA. Is the PA subservient in its role to the SARB, or do the two agencies really have independent roles? If the PA is truly an independent entity, then why should the Deputy Governor of the SARB run the day-to-day operations of the PA? Will this allow for the SA Twin Peaks structure to function at an optimal level? I argue that it is too early to draw any meaningful conclusions about this yet, and only time will tell. Interestingly, despite the concentration of power in the Governor, there is no provision in the FSRA dealing with how any conflict between the Governor and

the CEO of the PA will be dealt with. In the UK, questions concerning the operational independence of the prudential regulator do not arise, since the Bank of England is itself regarded as a prudential authority.

(b) The independence of the market conduct regulator

Concerning the independence of the market conduct regulator, the UK regulatory architecture is unique because the Bank of England, acting as the PRA, has the power to prevent the FCA from acting in limited circumstances. [121] This power is called a veto power. The power is exercised where action taken by the FCA is likely to threaten the stability of the UK's financial system, or where such action may result in the failure of the PRA-authorised person in a way that would adversely affect the UK's financial system. In its review assessment, the IMF rightly raised concerns about this arrangement and it argued that, without appropriate safeguards, this arrangement 'had the potential to limit FCA independence and also to cause uncertainty in decision making'. [122] SA does not recognise any equivalent arrangement of this nature. The FSCA is an independent institution established under the FSRA to oversee the SA financial services industry. [123] But the FSCA is a national public entity, which suggests that the authority is fully funded or substantially funded either from the National Revenue Fund or by way of tax or levy, and is accountable to the Minister of Finance and, ultimately, to Parliament. [124] A further compromise to the independence of the FSCA is that its Commissioner may be dismissed by the Minister after an 'independent inquiry'. [125] The Commissioner also has the power, with the concurrence of the Minister, to dismiss the Deputy Commissioner. [126]

(c) Budgetary independence

One of the prerequisites for the independence of regulatory agencies is that they must be funded in a manner that does not undermine their independence. The Basel Core Principles for Effective Banking Supervision provide that the supervisor must have adequate resources. [127]

Similar provisions are found under the ICP. [128] In general, the executive or legislative branch of government determines the budget of the regulatory agency and the way the budget is used. [129] Budgetary independence of the regulatory authority means that the agency should not be subjected to political pressure through the budget. In circumstances where the budget comes from the government, then the agency should propose the budget and justify such a budget. For this reason, supervisory agencies in some jurisdictions are funded through industry fees. For example, the Australian Prudential Authority is industry-funded. [130] The industry-funded system may leave the agency cash-strapped in times of crisis — that is, when the industry itself is faced with financial difficulties.

In SA, the Financial Regulatory Reform Steering Committee has noted that 'the prudential regulator will be funded in line with international best practice to ensure transparency regarding the cost of supervision and the protection of the independence of the regulator'. Compared to other jurisdictions such as Australia, the SARB is required to provide funding to the PA under the FSRA. Section 50 of the Act requires the PA to determine the funding, personnel, use of assets, resources and other resources that it needs to function effectively. In terms of s 51(1), the SARB is required to provide the PA with personnel, accommodation, facilities, use of assets, resources and other services as agreed by the SARB. [131] In the UK, both the PRA and the FCA charge fees in connection with the performance or discharge of their respective functions. [132] It is worth noting that the FCA is wholly funded by the fees charged from the organisations under its regulation. In addition, the FCA is responsible for collecting fees on behalf of the PRA, including invoices for the PRA fees. [133]

(d) Accountability and the extent of government's involvement

The extent of government's involvement and the nature of the relationship between regulators and relevant government ministries is a critical issue in determining the functional autonomy of regulatory agencies. To be efficient and effective, it is not enough that the regulator is independent. Such independence must be accompanied by transparency and accountability. The key issue here is the locus and structure of the accountability mechanism. [134] The Basel Core Principles on Banking Supervision require that the supervisor must be 'accountable for the discharge of its duties and use of its resources'. [135] The ICP also state that the supervisory authority must be 'accountable and transparent in the exercise of its responsibility'. [136] Importantly, the Treasury has an overall responsibility of overseeing the country's financial system and, therefore, it is appropriate that the Minister of Finance should be informed when financial institutions are facing financial difficulties. However, the accountability of supervisory agencies does not call for political influences and political interference in their autonomy. This is important for various reasons, most important of which is that supervisory agencies should be seen to be independent for building and sustaining customers' confidence and in ensuring industry credibility. Operational independence is also important in order to avoid political influences for non-regulatory purposes. [137] Therefore, a careful balance needs to be struck between a legitimate demand for accountability of regulatory agencies and the need for them to be free from political interference. [138]

The sharing of information with the Minister of Finance in SA is arranged in a hierarchical manner. There is no direct link between the PA and the Minister of Finance with respect to information sharing pertaining to the safety of regulated entities. Presumably, this is done in order to curtail the level of political interference on the autonomy of the PA. In terms of s 16 of the FSRA, the Governor of the Reserve Bank must ensure that the Minister is kept informed about the steps taken to address the risks associated with financial stability. [139] The decisions that bind the national revenue fund should ultimately be approved by the Minister of Finance. Under s 19(1) of the FSRA, if the Governor has determined that a systemic event has occurred or is imminent, an organ of state exercising powers in respect of a part of the financial system may not,

without the approval of the Minister of Finance, acting in consultation with the Cabinet member responsible for that organ of state, exercise its powers in a way that is inconsistent with a decision or steps taken by the Governor of the SARB in terms of the FSRA to manage that systemic event or its effect. [140] It is submitted that this arrangement is likely to cause friction and unnecessary delay during periods of crisis. However, it can be argued that the purpose of this prior consultation is to avoid events being branded as systemic and necessitating the utilisation of resources, as well as to ensure that the Treasury is kept abreast of problems early enough to assist in dealing with systemic events. Although taking swift decisions and measures in a crisis situation would be appropriate, it is important to have some operational checks in order to avoid abuse. Finally, the SARB is held accountable to the public through its macro-prudential surveillance role. In terms of s 13, the SARB must, at least every six months, make an assessment of the financial system in the form of 'financial stability review', which is required to be published for public input and public notification. [141]

In the UK, the government is intricately involved in the regulation and supervision of the UK's financial system. This is a troubling issue, as it goes to the question of the operational independence of financial regulators. [142] Under the UK's Twin Peaks model, the government can influence, direct or command the performance of the functions of the financial regulators. For instance, the UK Treasury has the power to provide for new objectives with respect to the PRA. [143] In cases where this power is exercised, it is subject to parliamentary approval. This raises the question about the nature of the relationship between the financial regulators and the government, as well as the extent of the government's involvement in the regulatory function. In addition to the power to provide new objectives, the UK Treasury may also direct both the FCA and the Bank of England to undertake an investigation. In terms of ss 76 and 77 of the Financial Services Act, 2012, the UK's PRA and FCA regulators are under specific duties to advise, investigate and report to the government on possible regulatory failures. Lastly, in managing dual regulated entities, the UK Treasury has the power to determine who is the lead regulator.

The UK Treasury may identify specific matters that, in relation to the exercise by either regulator of its functions relating to the

PRA-authorised persons, are to be, or are primarily, the responsibility of one regulator rather than the other. Effectively, this establishes the boundaries between the two regulators, allowing the Treasury to determine who should be the lead regulator in regulatory investigation, and requiring one regulator to consult the other. The UK Treasury's ability to determine who is the lead regulator could potentially create problems with regard to co-ordination and collaboration of supervisory action, and could lead to confusion during periods of crisis. It also has implications for the lack of confidence in the co-ordination and collaboration arrangement that has been put in place in the UK's financial system, as well as implications for the operational independence of the FCA. By contrast, this diverging feature of the UK's Twin Peaks, when read alongside the PRA's veto power, demonstrates why there is no archetypical Twin Peaks model. [144] In terms of accountability, it is relevant to note that in the UK, the Treasury Select Committee is appointed by the House of Commons to examine the expenditure, administration and policy of HM Treasury, HM Revenue & Customs and associated bodies, including the Bank of England and the FCA. [145]

VI Co-ordination and information sharing

Having examined the role of the tripartite system at the time of the Northern Rock crisis, the House of Commons noted that the tripartite authorities could have co-ordinated their approach better and more effectively in order to prevent the run on the bank. [146] While the UK had a single unified supervisor prior to the GFC, in times of crisis, when co-ordination with the tripartite authorities was crucial, this arrangement was found wanting. [147] In general, close and effective co-ordination and co-operation across the Ministry of Finance, the central bank and supervisors are essential, regardless of the form of financial regulatory architecture that a country may adopt. It is also widely recognised that regulatory architecture that splits regulatory agencies into multiple agencies requires strong co-ordination support to ensure the sufficient flow of information and to ensure that issues requiring regulatory oversight do not fall through gaps. [148]

It should be noted that the key aspects of co-operation and co-ordination first include the effective flow of information across staff in the market operations, bank supervision, financial stability and macroeconomic departments of the central bank. Secondly, regular meetings of these groups can enhance information sharing. The meetings may focus on risk vulnerabilities, highlighting warning signs. Consequently, many jurisdictions adopt a structure of Memoranda of Understanding ('MOUs') and have financial stability committees in place in order to engender close ties, information sharing and better co-ordination between regulators. In the UK, there is an extensive MOU framework between various regulators and international organisations. Many of these MOUs have legislative backing and are expected to be treated with the necessary degree of seriousness and implemented in accordance with the statutory terms. [149] For instance, the Bank of England considers these documents to be accountability instruments through which the Bank is held accountable to Parliament under the Treasury Select Committee. Another significant feature of the recent reform in the UK is that the FCA and the PRA have a statutory obligation 'to prepare and maintain a memorandum which describes in general terms the role of each regulator in relation to the exercise of functions conferred by and under this Act'. [150] This MOU must be reviewed at least once a year and must be given to the Treasury and tabled before Parliament. [151]

For crisis management, another MOU must be prepared and maintained between the Treasury, the Bank of England and the PRA. This MOU is set up to demarcate the responsibilities between Treasury and the Bank of England, including the PRA, in times of financial crisis. With respect to international co-ordination, the Treasury, the Bank of England, the FCA and the PRA must prepare and maintain a MOU with the European supervisory authorities, EU institutions and other international organisations before Brexit. [152]

In SA's context, these co-ordination mechanisms have an added significance with the recognition that each regulatory agency has a responsibility for financial stability, systemic risks and macro-prudential concerns to address the challenges of an integrated financial system. The need for effective co-ordination and collaboration has been recognised by the SA Treasury in the drafting of its legislative framework. SA relies on a hard-law approach to co-ordination between its main financial regulators. The hard-law approach has been borrowed from the UK.

This contrasts with the position in Australia, where the co-ordination mechanism is based on informal bilateral arrangements between each of the main regulators, as well as on informal Council of Financial Regulators processes to facilitate co-ordination between the main financial regulators. [153] The Australian system relies substantially on soft-law mechanisms in the form of MOUs and informal protocols — legislation is facilitative rather than prescriptive. [154]

Generally, there are two levels of co-operation and collaboration under the FSRA. First, the SARB is obliged to co-operate with other financial regulators in order to fulfill the financial stability mandate of the central bank effectively. To achieve its financial stability objective, the PA must co-operate with and assist the SARB, the Financial Stability Oversight Committee, the FSCA, the NCR and the Financial Intelligence Centre, and must co-operate with the Council for Medical Schemes. [155] This shows that the financial stability role is a shared responsibility of various regulators, rather than the sole function of the SARB. In order to facilitate practical co-operation and collaboration between the various entities that are required to work together with the SARB in creating a stable financial sector in SA, the Act requires that the financial regulators and the SARB had to enter into MOUs not later than six months after chaps 2 and 5 of the Act took effect. These MOUs must be aimed at giving effect to their obligations as set out in s 76. [156]

The second level of co-operation and co-ordination is that the organs of states with supervisory functions are required to consult with the financial sector regulators and the central bank. Section 76 of the FSRA states that financial regulators must collaborate with each other when performing their functions in terms of financial sector laws such as the National Credit Act 34 of 2005, and the Financial Intelligence Centre Act 38 of 2001, and must, for this purpose:

'*(a)* Generally assist and support each other in pursuing their objectives in terms of financial sector laws, the National Credit Act and the Financial Intelligence Centre Act;

(b) inform each other about, and share information about, matters of common interest;

(c) strive to adopt consistent regulatory strategies, including addressing regulatory and supervisory challenges;

(d) co-ordinate, to the extent appropriate, actions in terms of financial sector laws, the National Credit Act and the Financial Intelligence Centre Act, including in relation to standards and other regulatory instruments, including similar instruments provided for in terms of the National Credit Act and the Financial Intelligence Centre Act; licensing supervisory on-site inspections and investigations; actions to enforce financial sector laws, the National Credit Act and the Financial Intelligence Centre Act; information sharing; recovery and resolution; and reporting by financial institutions, including statutory reporting and data collection measures;

(e) minimise the duplication of effort and expense, including by establishing and using, where appropriate, common or shared databases and other facilities;

(f) agree on attendance at relevant international forums; and

(g) develop, to the extent that is appropriate, consistent policy positions, including for the purpose of presentation and negotiation at relevant South African and international forums.' [157]

It is therefore clear that ensuring financial stability in the SA financial system requires a holistic approach from all relevant and key role players. It is submitted, however, that while the MOUs may provide an essential underpinning for co-operation and co-ordination to set the ground rules and establish responsibilities, they are not in and of themselves sufficient to ensure smooth co-ordination. Accordingly, the Group of 30 has noted that '[e]fforts to enhance co-ordination at the highest levels of the agencies can be adversely affected if the principals clash personally or disagree over respective roles and objectives. Ultimately, a collaborative tone must be established at the top by individuals in charge.' [158]

In addition to the MOUs, the common element in Twin Peaks jurisdictions is the existence of a co-ordinating body. The nature and membership of the co-ordinating body tends to differ from jurisdiction to jurisdiction. It is interesting to note that the UK is different. The FPC, which is responsible for regulating the financial stability of the entire financial system, is the closest entity to the co-ordinating body. The FPC is a statutory committee of the Bank of England's Court of Directors and, unlike other co-ordinating bodies elsewhere, it is established within the Bank of England. [159] The FPC is conferred with powers to

give directions to the FCA and the PRA concerning macro-prudential measures and it also makes recommendations to the Bank of England, the Treasury, the PRA and the FCA. [160] Its policy decisions are announced via the financial stability report to the market immediately after its meetings. The membership of the FPC comprises the Governor, the Deputy Governors, the Chief Executive of the FCA, the Bank's Executive Director for Financial Stability, Strategy and Risk, five external members appointed by the Chancellor, and a non-voting representative of the Treasury. [161] Lastly, the FPC is established as a financial stability authority dedicated to macro-prudential regulation thereby ensuring that financial stability concerns are placed above other concerns. [162]

In SA, the Financial System Council of Regulators ('FSCR') and Financial Sector Inter-Ministerial Council are two co-ordinating bodies established under the FSRA. [163] The FSCR has broader mandate of facilitating co-operation and co-ordination and, where appropriate, consistency of action between the institutions represented on the FSCR by providing a forum for senior representatives of those institutions to discuss and inform themselves on matters of common interest.

VII Differences and similarities between the UK and the SA Twin Peaks

The most noticeable difference between the UK and the SA Twin Peaks systems is that the UK's PRA is the Bank of England acting through the Prudential Regulation Committee, and its status as a subsidiary of the central bank has ended under the recent reform. [164] By contrast, the SA PA is located within the SARB as a distinct entity from the central bank but under its administrative support. [165] Pertinent to this SA arrangement is the funding of the PA by the SARB, which also reflects the 'separate entity but administratively integrated' model that has been adopted in respect of the PA. In the UK, both the PRA and the FCA charge fees in connection with the performance or discharge of their respective functions. The PA in SA is dependent on the SARB, while the FSCA is industry-funded. Both the SARB and the Bank of England, as the prudential regulation authority, have the key responsibility of promoting the safety and soundness of financial institutions. However, in SA, the financial stability role is shared by all the financial sector regulators.

The determination of the lead regulator and the veto power to the PRA in relation to the FCA clearly distinguish the UK's Twin Peaks system from other Twin Peaks models, including SA's. [166] As noted above, this raises questions on the operational independence of the UK regulators. As previously mentioned, although the SA government does not have explicit veto powers over the regulators' decisions, the government does select the lead regulator. The executive also has structurally embedded powers because its members have representative capacities on various committees and various co-ordinating bodies. [167] As in the UK, the duty to co-operate and collaborate is imposed by legislation, reflecting a hard-law approach. This contrasts with the position in Australia where a soft-law approach to co-ordination and collaboration applies. [168] Lastly, when compared to the UK, the design of the regulatory co-ordination framework in SA appears to involve a high degree of potential overlap between the co-ordinating bodies, with a highly prescriptive approach to achieving effective co-ordination and collaboration.

VIII Conclusion

This article has shown that there has been a paradigm shift towards the Twin Peaks model of financial regulation across the world. There are slight variations in the design of the two Twin Peaks models investigated. The variation in regulatory design indicates the flexibility of the Twin Peaks model and its ability to be modified to suit the local conditions, regulatory culture, and the country's specific needs. Therefore, while the SA model has drawn significantly from the experiences of other Twin Peaks jurisdictions, particularly the UK, the country has adopted its model to accommodate its own needs and unique characteristics that are suitable for SA. It is imperative for the success of the Twin Peaks model to clearly delineate the objectives and functions of each regulator and to achieve effective co-ordination between them. In fact, given the potential overlaps and high levels of co-operation required between the different regulatory bodies in SA, the country's Twin Peaks model may have serious, detrimental consequences if this complicated financial regulation regime is not properly managed.

The journey to the Twin Peaks models in both the UK and SA indicates that the Twin Peaks system is more suitable for handling the rise of financial conglomerates, innovation in product design, and the growing complexity of financial products. For SA, the move away from the sectoral or institutional model was justified on these grounds. It seems

the institutional model was wholly inappropriate and simply outdated for a sophisticated and complex financial market such as SA. This article also raises important questions of regulatory independence, especially when one considers the UK's experience. This is so because underpinning the effectiveness of all the financial regulatory models is appropriate governance, operational independence and sufficient funding for the regulators to achieve their mandates. Therefore, in the UK, it remains to be seen to what extent the government's power to establish boundaries and the veto power of the PRA over the FCA can undermine the independence of the regulators, and the extent to which this position will frustrate the ability of the regulators to co-ordinate effectively between themselves. The SA Twin Peaks model is still in its infancy. It promises to strengthen the financial system and to forestall systemic crises if one takes into account developments elsewhere. No financial market is an island in today's globalised environment. Global co-operation and taking note of best practice elsewhere are therefore critical.

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