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Abstract

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Retail Market Conduct Reforms in South Africa under Twin Peaks

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This article examines retail market regulatory reforms currently underway, as part of the implementation of a Twin Peaks regulatory model in South Africa. A brief account is provided of the history of these reforms, followed by an analysis of the normative goals put in place for a new market conduct and consumer protection regime; and the developmental needs that inform those goals. Thereafter the article explores the inter-relationship between the existing credit regulator and the soon to be established Financial Sector Conduct Authority. An analysis is then provided of accountability mechanisms, as well as failures exhibited by those mechanisms in the UK and Australia. Finally an argument is made for a ‘regulator for the regulators’, in order to address past regulatory failures.

A. Introduction

The ‘Twin Peaks’¹ model of financial system regulation was first proposed by Michael Taylor in 1995.² Taylor’s idea began as an attempt to address, principally, two problems evident in the United Kingdom: first, that the large and disparate

number of regulators of financial products, services, and entities, each with its own limited jurisdiction, left consumers confused as to whom to approach for support. Consumers were confronted by a bevy of regulators, whose acronyms taken together Taylor described as an ‘alphabet soup’.³ To this Taylor proposed a dedicated, whole-of financial system

regulator – a one-stop shop – the purpose of which would be to protect consumers, and deter market misconduct.⁴ The second problem Taylor identified and which he asserted his model could address, was that of a *blurring of the boundaries*⁵ between types of financial entities: banks were combining with insurers, merchant banks were combining with securities traders – causing gaps to appear in regulatory coverage.⁶ This second regulator would have a consolidated group-level view of all entities under its jurisdiction, with the authority to create and enforce regulations aimed at safeguarding financial system stability.⁷

First adopted in Australia in 1997,⁸ and subsequently followed in The Kingdoms of the Netherlands and Belgium, New Zealand, the United Kingdom (UK), and now South Africa,⁹ which is poised to impose a ‘Twin Peaks’ financial regulatory architecture. The South African reforms shadow those of the 1987 de Kock Commission, which established the ‘Financial Rand’ and the dual exchange rate;¹⁰ they are more significant than those of the 1993 Melamet Commission¹¹ and, some would argue, more significant than any other changes to the management of the financial system since South Africa left the gold-standard in 1932.¹²

B. Twin Peaks with normative goals

South Africa’s *trek* to twin peaks commenced in 2011 with the publication by the South African National Treasury of a policy document¹³ which provided an overview of the financial sector, and put forward overarching principles to guide analysis of whether, and to what extent, there was a need for regulatory reform. The process’ commencement coincided with the aftermath of the sub-prime disaster in the United States, and the ensuing GFC¹⁴, and this may be one explanation as to why the Cabinet, on approving the adoption of Twin Peaks, specified that one of the guiding principles to a new regulatory regime should be that the *quality of supervision must be sufficiently intense, intrusive and effective*.¹⁵ To that was added:

*Market conduct oversight must be sufficiently strong to complement prudential regulation, particularly in the banking sector. Market conduct oversight is critical for the financial sector, and complements prudential oversight.*¹⁶

This is a theme that also appears frequently in the Draft Market Conduct Policy document¹⁷ issued as an adjunct to

National Treasury's 2011 document that, if need be, supervision must be intrusive.

... ordinary, generic customer protection laws do not go far enough ... potential for economic disruption and consumer hardship ... sector requires much higher regulatory standards relative to other sectors ... tailored to respond to market conduct risks. ... A dedicated regulator for market conduct, the FSCA, will supervise financial institutions more intensely and intrusively ... take steps to end unfair or harmful practises as they emerge,
...¹⁸

This comports with current thinking developed post-GFC. Carmichael, Foundation Chair of Australia's prudential regulator and a member of the Wallis Commission of Inquiry whose findings led to the establishment of Twin Peaks in Australia states that prior to the GFC, conduct regulations were reactive not proactive, and focused on pursuing breaches of the law.¹⁹ He states that with a shift post-GFC from product disclosure to product suitability, conduct regulators have had to become more preventative in their approach to regulatory enforcement; and this is reflected in new methodologies, for example a greater degree of onsite inspections as opposed to investigations, where the latter typically takes place when

there is an alleged breach.²⁰ Carmichael states that this new approach is more resource intensive.²¹ If Carmichael is correct, then that has crucial implications for South Africa, a developing country with needs across society that are greater than the resources available.²²

These social benefit goals laid the basis for a dispensation which is, at least in terms of its stated aims, strongly normative – an aspect to which this article will return.

The process envisages two pieces of legislation, the first of which, the *Financial Sector Regulation Act*²³ (FSRA), was promulgated in August 2017. In so doing, South Africa becomes the first developing²⁴ nation to adopt this model.²⁵ Other countries that have signalled an interest in adopting Twin Peaks include South Korea,²⁶ Canada,²⁷ Nigeria,²⁸ Kenya,²⁹ and China.³⁰ This forms part of a global trend, starting in 1998, in which 80 per cent of OECD members have reformed their domestic financial regulatory architecture³¹ - and particularly in countries with sectoral or institutional models.³² It is for these reasons that the South African reforms are noteworthy: as mentioned, it is the first developing country and latest adopter of Twin Peaks, and as such may be expected to evidence latest thinking; lessons learned in South Africa will be of relevance wherever Twin Peaks is adopted next, but also of

relevance wherever Twin Peaks is already *de lege*. If the conventional wisdom is correct, by ascribing much of Australia's success during the global financial crisis (GFC) to the deployment of Twin Peaks,³³ then lessons learned in South Africa will have a potentially wider impact, beyond the specificities of Twin Peaks, by providing lessons for the avoidance of financial crises generally. To that end, success in South Africa may act as an exemplar of what solutions regulatory architectural design can offer to the overarching project: the avoidance of financial crises.

*The Australian banking system was more sheltered than a number of other countries and weathered the Global Financial Crisis relatively well. This was in part due to relative concentration of the system on a well performing domestic economy, but also due to a material contribution from a well-developed regulatory and supervisory structure.*³⁴

As mentioned previously, the South African reforms are noteworthy for another reason: they are grounded in a clearly normative approach, which specifically mentions the developmental priorities of the South African government, and doubtless the expectations of the community; in particular, the large

percentage of South Africa's population that has limited access to finance, limited education, limited ownership of assets, and suffers under a substantial disparity of wealth.

With a population of 55 million,³⁵ those regarded as economically-active, and between the ages of 15 and 64 number approximately 40 million.³⁶ One quarter of that number – what should be The Republic's most economically productive citizens – are unemployed.³⁷ While South Africa has made commendable improvements to its education system since the advent of democracy in 1994, there are still in excess of two and a half million adults who are illiterate.³⁸ Between 2010 and 2015, of the 143 countries that provided data, South Africa's Gini coefficient, a measurement for wealth disparity, placed South Africa at 143.³⁹ Using a Palma ratio,⁴⁰ out of 143 countries that reported, South Africa was 143rd.⁴¹ Using a quintile ratio, out of 46 countries reporting, South Africa was ranked 45th.⁴² Together these factors are instrumental in creating low levels of financial inclusion in South Africa. Combined with poor levels of financial literacy (see Fig. 1), there exist opportunities for unscrupulous financial service providers, and especially lenders, to take advantage of the large number of unsophisticated financial consumers in South Africa. Such an outcome would, in

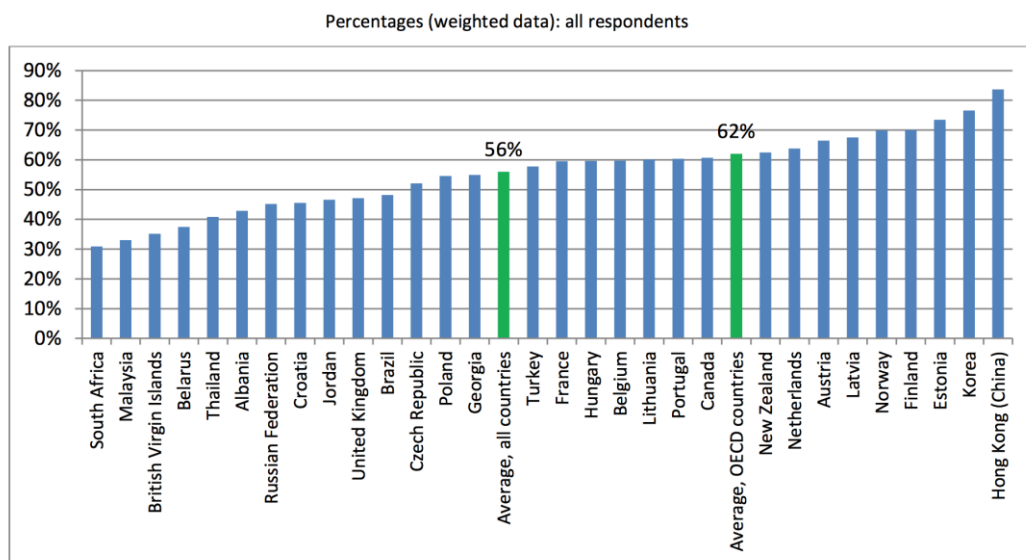
turn, impede successful financial inclusion, potentially cause disproportionate detriment to the most vulnerable in society, ⁴³ deter savings, inhibit intermediation, result in social unrest potentially causing death, ⁴⁴ and in the worst scenario a financial crisis (see below). It is no wonder, then, that the South African authorities have placed such emphasis not just on consumer protection and good market conduct, but further, by articulating goals that strongly emphasise societal good, with particular emphasis on the poor.

... [W]e have perhaps just witnessed one of the most appalling microcredit-related

disasters of all in South Africa. Extreme over-indebtedness ... helped precipitate the Marikana massacre on August 16 [2012]. Miners ... were ... seduced ... into accessing far too much microcredit.⁴⁵

... [F]orced into spending more on interest payments ... no matter how hard they tried, ... not prise themselves away from ... microcredit in advance of payday ... The miners' desperation and anger was palpable, Lonmin refused to back down, and a massacre ensued [when South African Police Services members shot striking miners].⁴⁶

Figure 1.⁴⁷



The subprime lesson

Analyses of the lessons to be learned from the GFC often focus on systemic stability

issues cum bank soundness principles and regulations, at the expense of the need to provide analysis of what is adequate consumer protection and the prevention of market misconduct. But this overlooks the fact that the GFC was market misconduct and consumer abuse writ large. As Wray states:

... many billions of dollars of fraudulent loans ... by Countrywide[⁴⁸]... sold fraudulently to Fannie and Freddie through false representations and warranties. ... 97% of the Countrywide loans reviewed by Ambac ... had false reps and warranties. Countrywide also engaged in widespread foreclosure fraud. ... [E]xamined by a truly independent body has found widespread fraud — in loan origination, loan sales, appraisals, and foreclosures. ... [O]ne financially sophisticated entity after another found widespread fraud by Countrywide in the entire gamut of its operations, the administration, the industry... Countrywide made hundreds of thousands of fraudulent loans ... It fraudulently foreclosed on large numbers of loans. It victimized hundreds of thousands of people and hundreds of financial institutions, causing hundreds of billions of dollars of

losses. It has defrauded more people, at a greater cost, than any entity in history ... The financial media treats Bank of America as if it were a legitimate bank rather than a “vector” spreading the mortgage fraud epidemic throughout much of the Western world.⁴⁹

And even more troubling than the countless instances of fraud and misconduct that gave rise to the subprime crisis – troubling enough as those were – were the nasty, predatory, and at times racist⁵⁰ undertones of so many of those malpractices. It is not surprising, therefore, that the South African authorities, cognoscente of the country’s developmental needs and society’s aspirations, and aware that the poor and ill-educated, who constitute the majority of the population, suffer disproportionate harm in poorly regulated markets; that where such harmful practices remain unchallenged, systemic threats to the entire financial system may result.

The 2014 National Treasury Draft Market Conduct Policy

Released as a Discussion Document, the Draft Market Conduct Policy makes clear the following view (albeit not in so many words):

*... constantly remind market participants that finance only exists to serve the broader community and the economy.*⁵¹

Not the other way round.

The Report states in its first paragraph that consumers are inadequately protected in South Africa;⁵² that they fall prey to reckless lending ‘paired with disgraceful (and illegal) debt-collection practices’; that poor market conduct prejudicial to consumers exacerbates problems of low domestic savings and high levels of over indebtedness; and that these and other factors impede South Africa progressing towards greater levels of financial inclusion.⁵³ As such the Report tacitly acknowledges that the management of the financial system must be focused, at least in part, on redressing the injustices and in particular the income inequality that was the result of 46 years of Apartheid.

*... financial inclusion [is defined] as the broadening and deepening of the access to, usage of, and quality of financial products/services to all adults particularly the marginalised groups such as the un-served and under-served.*⁵⁴

One of the advantages of the Twin Peaks model is its separation of prudential/system stability oversight from that of market conduct and consumer protection, with particular care taken to

ensure that one peak does not dominate the other. In that respect Twin Peaks accommodates an ideational principle: that consumer protection and prudential regulation should be regarded as equal, and that the ensuing policy disagreements and conflicting situational responses should be regarded as a natural phenomenon, embraced, and settled through discussions convened at an over-arching council, underpinned by constant and close communication and cooperation.⁵⁵

*Market conduct regulation aims to better protect financial customers by responding to these risks, and is a key pillar of the Twin Peaks system being implemented in South Africa.*⁵⁶

This principle is borne out in the Treasury’s clear view that:

*Protecting customers and ensuring they are treated fairly by financial institutions is the essence of market conduct policy and law.*⁵⁷

C. Three Peaks?

This confident exposition of what the consumer protection peak should be focused upon, without the barest mention of systemic stability issues is, ideationally at least, the essence of where consumer

protection should be located: an end in itself. How successful this will be in practice remains to be seen. However, there is evidence to date that the South African authorities understand that consumer protection is its own very distinct territory, and one that needs to be defended from incursion.⁵⁸ In defence of its realm the proposed consumer protection peak, the Financial Sector Conduct Authority (FSCA), will be buttressed by an already existing consumer credit protection regime: a dedicated National Credit Regulator (NCR),⁵⁹ created by the *National Credit Act* of 2005,⁶⁰ and complimented by a National Credit Tribunal.⁶¹

It is not unusual to find a separation between the protection of consumers of credit and those of consumers of other financial products and services. Such a bifurcation exists in Australia as well, in the form of the Australian Securities and Investments Commission (ASIC) – the agency with general responsibility for consumer protection in the financial industry - and the *National Credit Code*,⁶² and the Credit and Investments Ombudsman.⁶³ However the South African regime is distinct from Australia's in a number of crucial respects, and it is the degree of difference that is potentially significant: the Australian Ombud is created pursuant to powers vested in ASIC,

and must be approved by ASIC from time to time to remain functioning,⁶⁴ whereas the NCR does not exist at the pleasure of the FSCA, is a national government agency, created by statute,⁶⁵ with powers and prerogatives at law. The Australian Ombud may have regard to equity and the law as laid down in the *Code*, but despite that flexibility, it may be argued that the South African arrangement is preferable, because the legislation that it is built around is more consumer centric than Australian's.⁶⁶ Moreover, the role of the South African NCR is considerably more comprehensive: it licenses extenders of credit; its powers are not limited to mediation, but extend to litigation, including litigation where the complainant is the NCR, and not an individual consumer; is imbued with social upliftment and financial inclusion priorities; is required to research trends in credit extension and make those findings known; is required to contribute to financial literacy education; is expected to make a contribution to policy, including legislative reform proposals; regulates and adjudicates in certain administrative manners; and hands down findings in respect of compliance.⁶⁷

As a result, and because the South African legislation was drafted with bespoke provisions for monitoring, regulating, licensing, educating, enforcing

and at times punishing, within one statutorily empowered agency, it provides a regime in which the South African credit regulator is a far more sophisticated and entrenched agency than the equivalent arrangement in Australia. The question then arises as to whether two regulators, both with an interest in, and powers over, what is essentially the same territory, was the best solution? Or whether it would have been better to have housed these functions within the FSCA?⁶⁸ The simple answer is that the current arrangement is a product of history: the National Credit Regulator was created in 2005,⁶⁹ whereas the FSCA was not contemplated until 2011.⁷⁰ That said, there are arguments to be made in support of the South African arrangement:

i) *The regulator's roles*: if the Australian experience proves instructive,⁷¹ then the consumer protection peak (FSCA) will take a macro-prudential view, while the NCR will continue to fulfil a micro-prudential role. This plugs a gap between regulator's interventions that are in the country's best interests (macro-prudential), but where the regulator declines to act, even in the best interests of individual consumers because their particular plight is

inadequately wide-spread, versus (micro-prudential) interventions on behalf of consumers whose plight, whilst not wide-spread, is nonetheless urgent for them;

ii) *Credit, a good servant but a bad master*: credit by its nature can be seductive. When extended recklessly, excessive credit can trap borrowers in an inescapable cycle of indebtedness and poverty.⁷² Notwithstanding the acknowledgement of the dangers improperly regulated credit can pose, and the persistent problem of over-indebtedness among South African households, and despite the work of the NCR since its establishment, the problem persists: unsecured loans in South Africa have become the biggest growth market for the four major South African banks.⁷³ The problems associated with credit are, therefore, on-going and severe.

amount of credit granted to consumers has increased substantially from R1.1 trillion in 2007 to R1.5 trillion in 2014. There were 21.7 million credit

active consumers and out of these, 9.6 million (44.2%) had impaired records. This increase has also led to an evolution of the problem of household over-indebtedness. Household debt to disposable income in South Africa is still high, even though the overall household indebtedness is actually down from its early peaks: Q4 2008 — 81.9% and this fell to 74.3% in Q4 2013. This is an indication that a large portion of household incomes still goes to servicing debt.⁷⁴

iii) *South Africa's demographics:*

the combination of poor,⁷⁵ ill-educated,⁷⁶ already over-indebted, financially ill-educated or illiterate consumers, whose needs are not currently being met, results in a portion of the population who are both vulnerable and in need of a path to greater financial inclusion. In combination with the nature and effects of credit, the need for protection aimed at vulnerable consumers in their consumption of credit becomes more obvious;

iv) *South Africa's history:* South Africans of colour were not only politically disenfranchised by Apartheid, they were

economically dispossessed as well. Credit extension is an important stage in the path to financial inclusion. If a dedicated credit regulator can better serve the goal of financial inclusion, then that advantage may exceed the disadvantage created by a bifurcation of consumer protection regulators;

v) *Economies of scale:* the majority of South Africans are classified as poor.⁷⁷ If sufficiently wide-spread, unscrupulous credit extension that preys upon the vulnerable in society has, therefore, the capacity to be a systemic threat;

*Consumer financial protection can, and must, serve a role not only in protecting individuals from excessive risk, but also in protecting markets from systemic risk. Economic studies indicate it is not merely high rates of defaults on consumer loans, but highly correlated defaults that create risks for lenders and investors in asset-backed securities.*⁷⁸

vi) *Focus:* a dedicated regulator with oversight over smaller territory – credit – may be able to bring more focus to the task,

develop a greater degree of expertise specific to the regulation of credit, and develop a corporate culture more suited to its task (for example, by developing its frontline capacity to assist members of the public), than would a generalist consumer protection peak that operates also with a credit regulatory role.

So, while Twin Peaks jurisdictions such as Australia have carved out a separate set of structures for dealing with problems associated with the extension of credit, the South African arrangement is, by comparison, both more sophisticated and complex. The degree of difference between the two dedicated credit regimes is sufficient to present the South African Twin Peaks model with additional challenges: the NCR is a fully-fledged agency, and relationships with the two peaks will have to be managed with the same care, deference and cooperative spirit with which the relationship between the two peaks will have to be managed. Consequently, success will depend upon the degree to which these two entities – the FSCA and the NCR – coordinate, communicate and cooperate. In particular, there are areas where the NCA and the FSCA will overlap: where credit is

bundled with other types of accounts, both regulators would be involved. Without close coordination this could lead to confusion and contradiction.

To that end the *Financial Sector Regulation Act*⁷⁹ includes specific provisions for the establishment and maintenance of the relationship between the regulators,⁸⁰ including membership the Financial Stability Oversight Committee.⁸¹ The Act specifically designates the NCR as a ‘financial sector regulator’ in the same definition in which it designates the FSCA and the prudential authority as financial sector regulators.⁸² The Act quarantines financial products that involve the provision of credit⁸³ to the *National Credit Act*,⁸⁴ save for specific provisions in the *FSRA* set aside for the jurisdiction of the FSCA.⁸⁵

Over and above these legislative provisions that require cooperation and communication, an essential mechanism by which the performance of the South African peaks will be measured will rest upon regulator accountability. In respect of market conduct, that accountability may be measured against some or all of the normative standards expressed in the legislation, policy documents and government policy.⁸⁶

D. Regulator Accountability

It appears intuitive that accountability be regarded as an indispensable component of effective government, and this extends to regulator efficacy.⁸⁷ In Australia formal accountability takes the form of annual reports⁸⁸ and Parliamentary oversight.⁸⁹ There exists also the possibility of oversight by independent bodies, and of course by the public through the media.⁹⁰

A similar regime will exist in South Africa, where the prudential regulator will be required to submit annual reports to the National Assembly.⁹¹ The FSCA must also produce and submit annual reports via the Auditor General.⁹² All the regulators of the financial system plus the Reserve Bank are members of the Financial Stability Oversight Committee, which includes an accountability regime,⁹³ as well as the Financial System Council of Regulators, which provides for extensive government oversight.⁹⁴ This comports with what Taylor envisaged for the model through either Ministerial or Parliamentary oversight.⁹⁵

That said, Parliamentary and Ministerial oversight and the production of annual reports failed dismally in the UK prior to the GFC.

... the FSA was not so much the dog that did not bark as a dog barking up the wrong tree. ...

contributed to the appalling supervisory neglect of asset quality. The FSA's attempts to raise concerns on these other fronts from late 2007 onwards proved to be a case of too little, too late⁹⁶ ... The regulatory approach encouraged a focus on box-ticking which detracted from consideration of the fundamental issues with the potential to bring the bank down. The FSA's approach also encouraged the Board of HBOS to believe that they could treat the regulator as a source of interference to be pushed back, rather than an independent source of guidance and, latterly, a necessary constraint upon the company's mistaken courses of action.⁹⁷

In his foreword to the FSA report on the ruinous RBS-ABN Amro takeover, Lord Turner, FSA Chairman, stated that RBS had procured two lever-arch folders and a CD⁹⁸ as the sum total of their due diligence, to which Hosking responded:

His suggestion is clear: if only RBS had garnered more information, if only there had been more lever-arch files... This is the philosophy of the deluded bureaucrat. If only there had been more reports, more meetings; if only more boxes had been ticked, more forms filled in. On the

*Origin of Species, the Bible and the collected works of Shakespeare could be contained in two lever-arch folders and a CD. How much more information does Lord Turner think RBS needed? ... It's not volume of information that matters. It's quality.*⁹⁹

Hosking points out that in respect of the claim that in the three and a half years prior to RBS's collapse, the FSA met with RBS 511 times:¹⁰⁰

It's typical that there is someone to count them, but no one to explain what on earth went on in them ... would [it] have been better had there been a thousand? The FSA tells us that 0.5 of an FSA manager and 4.5 team members were assigned to RBS as it was mounting the bid.¹⁰¹ The clipboard-hugging precision of those decimals speaks volumes ... The report is a blizzard of acronyms and bogus science: RBS was scored as a "medium high minus"¹⁰² risk, whatever that is ...¹⁰³

Similarly in Australia the performance of the regulators has been patchy at times, and deeply inadequate at others.¹⁰⁴ The litany of scandals that have infected Australia's banking, insurance, and financial advice industries has led to consistent calls for a Royal Commission of

Inquiry into the conduct of Australia's banks, and the oversight conducted by the regulators.¹⁰⁵

As Barth *et al* assert, regulators prior to the GFC abrogated their responsibilities, and giving them more regulatory power will not address this problem.¹⁰⁶

E. A regulator for the regulators

Unfortunately, in the wake of the crisis, we now seem to be lurching from one simplistic, unqualified ideology—that private markets will look after society's interests—to an equally flawed, if not more perilous, ideology—that the Guardians will always act in society's interests, so let's give them more power to do so.¹⁰⁷ Successful and lasting reform requires addressing a core cause of the systemic malfunctioning of financial systems—poor governance of the Guardians of Finance.¹⁰⁸

It is interesting to note, therefore, that Australia's Financial System Inquiry recommended a 'regulator for the regulators' in the form of a Financial Regulator Assessment Board (FRAB),¹⁰⁹ which would replace the Financial Sector Advisory Council (FSAC), and would

undertake *ex post* reviews of regulator accountability¹¹⁰ by ‘assess[ing] how regulators have used the powers and discretions available to them.’¹¹¹ As may have been expected, the Australian regulators pushed back against this idea.¹¹²

Such a Board could be expected not only to assess and evaluate regulatory action and outcomes, but to delve into regulatory culture as well. As McConnell states:

*In behavioural economics, such “concurrence” across a group is called groupthink. ... Groupthink ... is unhealthy because, not only do people start to think alike, it is only a short step to believing people who are singing a different tune should be excluded and thrown out of the chorus. Dissent can be destructive, but the role of the Devil’s Advocate is well-understood to be valuable, drawing out important questions people would rather not answer. ... [the FRAB would comprise of] knowledgeable experts, crucially not tied to regulators, with a diverse membership that would “act as a safeguard against the FRAB being unduly influenced by the views of one particular group or industry sector”.*¹¹³

An oversight board would be less likely to be captured by the prevailing

culture within the entities which it would oversee, and that would include identifying instances of regulatory capture generally.

*... according to considerable evidence from around the world, financial regulation is systematically biased in favor of the financial services industry and against the interests of the broader public.*¹¹⁴

At the very least such a board would act as a sober second thought on issues that may have been overlooked by the regulator, and which may potentially constitute a threat to the financial system.¹¹⁵

The Australian proposal has precedent in the UK, which established a Financial Policy Committee (FPC),¹¹⁶ whose purpose is to look for the roots of the next crisis.¹¹⁷ It is charged with identifying, monitoring, and taking action to reduce systemic risks.

Similarly, and in response to regulator’s failures prior to the GFC, Barth *et al* put forward a similar proposal for an expert panel of oversight, called a ‘Sentinel’.¹¹⁸

Unfortunately the proposal for a Financial Regulator Assessment Board was rejected by the Australian government.¹¹⁹ Nonetheless, the proposal has advantages which may be of benefit to

the South African financial regulatory landscape.

F. Conclusion

South Africa is well-advanced in its *trek* towards Twin Peaks. The next major hurdle will be the creation and implementation of a new market conduct and consumer protection peak. It is no doubt gratifying for the majority of South Africans to know that this new regime will be, ideationally at least, firmly rooted in normative principles aimed at addressing the urgent developmental needs of The Republic.

One particular aspect that will require attention, and no doubt generate analysis, is the relationship between the two official peaks – the prudential regulator and the FSCA – and what may be regarded as the third peak, the NCR.

But more important still will be the efficacy of the regulators in discharging their obligations.¹²⁰ That will, to a large degree, depend upon the depth and extent to which regulators are held accountable. Methodologies currently employed to effect accountability – via Parliamentary and Ministerial oversight – have recorded notable failures, both in times of crisis (as was the case in the UK), and in times of stability (as is the case in Australia). While

the failures in the UK did not take place under a Twin Peaks regime, but took place prior to the introduction of Twin Peaks, the lesson remains the same: annual reports, and Parliamentary and Ministerial oversight may prove inadequate to the task. A system designed to impose ‘double redundancy’, or a fail-safe, may prove to be the solution. In light of the consequences of large-scale market misconduct cum financial crises, this article argues that despite the costs and effort involved in establishing a ‘regulator for the regulators’, such a proposal should be seriously considered for addition to the South African reforms.

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Australian Securities and Investments Commission Act (Cth)

National Credit Act

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This proves useful in conveying complex regulatory ideas, expressed so as to provide for a quick and easy comparative analysis. For example in the United States many in the field have taken to referring to their model as 'rolling hills' (conversation with Patricia McCoy, Foundation Head: Mortgage and Home Equity Markets division, United States Consumer Financial Protection Bureau, April 2017). In conveying a view on the South African reforms, one member of the Standing Committee on Finance of the National Assembly described South Africa's Twin Peaks "as a 'mountain', 'two peaks' and a 'molehill'." Standing Committee on Finance, *Report of the Standing Committee on Finance on its Study Tour to the United Kingdom from 07 to 11 December 2015* (Tabled Reports, 2016), p. 12.

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⁴⁹ L. Randall Wray, 'Setting the Record Straight One More Time: BofA's Rebecca Mairone Fined \$1Million; BofA Must Pay \$1.3Billion' *New Economic Perspectives* <<http://neweconomicperspectives.org/2014/08/setting-record-straight-one-time-bofa-rebecca-mairone-fined-1million-bofa-must-pay-1-3billion.html>> accessed 26 June, 2015 See also: Edward Wyatt, 'Promises Made, Then Broken, By Firms in S.E.C. Fraud Cases' *New York Times* (New York, NY 8 November) *Business Day* <http://www.nytimes.com/2011/11/08/business/in-sec-fraud-cases-banks-make-and-break-promises.html?_r=0> For a full list of firms fined for malpractice and fraud prior to the GFC, see: U.S. Securities and Exchange Commission, *SEC Enforcement Actions. Addressing Misconduct That Led To or Arose From the Financial Crisis*, 2015)

⁵⁰ See further: Benjamin Howell, 'Exploiting race and space: Concentrated subprime lending as housing discrimination' (2006) 94 *California Law Review* 101; Carolina Reid and Elizabeth Laderman, *The untold costs of subprime lending: Examining the links among higher-priced lending, foreclosures, and race in California* (Community Development Working Paper Series, 2009); Jacob S Rugh and Douglas S Massey, 'Racial segregation and the American foreclosure crisis' (2010) 75 *American Sociological Review* 629

⁵¹ Part of Mr James Shipton's reaction to the announcement that he is to be appointed Chair of the Australian Securities and Investments Commission (ASIC), Australia's Twin Peak market

conduct and consumer protection agency. Patrick Durkin, 'James Shipton appointed ASIC chairman' *Australian Financial Review* (Sydney, NSW 17 October) News <<http://www.afr.com/news/james-shipton-appointed-asic-chairman-20171016-gz274h>>

⁵² National Treasury, *Treating Customers Fairly in the Financial Sector: A Draft Market Conduct Policy Framework for South Africa*, p. 6.

⁵³ Ibid, p. 6. See also: Klaus Kessler and others, *Improving Financial Inclusion in South Africa* (Publications, 2017); The World Bank Group, 'South Africa' (*The World Bank Group*, 2014) <<http://datatopics.worldbank.org/financialinclusion/country/south-africa>> accessed 10 November; National Credit Regulator, 'Consumer Credit Market Report (CCMR)' (*National Credit Regulator*, 2016) <<http://www.ncr.org.za/consumer-credit-market-report-ccmr>> accessed 25 August; ibid; Penelope Hawkins, *Pricing of and Access to Consumer Credit* (Research Report Summary, 2009)

⁵⁴ Finmark Trust, *Results from FinScope South Africa 2016 Survey on Financial Inclusion* (Finmark Trust 2016), p. 1.

⁵⁵ See further: Schmulow, *Twin Peaks: A Theoretical Analysis*.

⁵⁶ National Treasury, *Treating Customers Fairly in the Financial Sector: A Draft Market Conduct Policy Framework for South Africa*, p. 8.

⁵⁷ Ibid, p. 6.

⁵⁸ During 2014 the author, along with Andrew Godwin, engaged in a conversation with National Treasury on *Financial Sector Regulation Bill* as it then was. One of the recommendations we made concerned the issue of a 'lead regulator'. We argued that such a concept undermines the separation of powers between the two peaks, and will make consumer protection subservient to financial system stability whenever a situation arises where there are any stability considerations. The concept of

'lead regulator' was subsequently abandoned in the second draft of the Bill.

⁵⁹ See further: Schmulow, 'Curbing reckless and predatory lending: A statutory analysis of South Africa's National Credit Act'. See also: National Credit Regulator, 'Home' (*National Credit Regulator*, 2016) <<http://www.ncr.org.za>> accessed 2 August

⁶⁰ *National Credit Act*

⁶¹ Ss 26 - 34, *ibid* See further: Developmentnoms (Pty) Ltd, *Literature Review on the Impact of The National Credit Act (NCA) has had on South Africa's Credit Market* (Final Report, 2012)

⁶² *National Consumer Credit Protection Act (Cth)*, read with the *National Consumer Credit Protection Regulations (Cth)*

⁶³ Credit and Investments Ombudsman, 'Home' (*Credit and Investments Ombudsman*, 2017) <<https://www.cio.org.au>> accessed 13 November

⁶⁴ For more, see: A.D. Schmulow, 'Protection of Financial Consumers in Australia' in Hongjoo Jung (ed), *An International Comparison of Financial Consumer Protection* (An International Comparison of Financial Consumer Protection, Springer 2018)

⁶⁵ *National Credit Act*, ss 12-25.

⁶⁶ Schmulow, 'Protection of Financial Consumers in Australia', cf Schmulow, 'Curbing reckless and predatory lending: A statutory analysis of South Africa's National Credit Act'. Compare in particular provisions relating to debt-relief in cases of reckless lending.

⁶⁷ For more, see: Schmulow, 'Curbing reckless and predatory lending: A statutory analysis of South Africa's National Credit Act'.

⁶⁸ In the United Kingdom the credit regulator, the Office of Fair Trading, was subsumed in the Financial Conduct Authority as part of the UK's transition to Twin Peaks. Financial Conduct Authority,

'The FCA sets out in detail how it will regulate consumer credit, including payday lending, when it takes over responsibility in April 2014' (*Financial Conduct Authority*, 3 March, 2013) <<https://www.fca.org.uk/news/press-releases/fca-sets-out-detail-how-it-will-regulate-consumer-credit-including-payday>> accessed 14 November

⁶⁹ *National Credit Act*

⁷⁰ National Treasury, *A safer financial sector to serve South Africa better*.

⁷¹ Australian Securities and Investments Commission, *ASIC's approach to enforcement*, 2013), p. 2-4.

⁷² See note n 44. For more on the dangers of reckless credit extension to the poor in 'Bolivia, Bosnia, Pakistan, Nicaragua, Morocco and most catastrophically, in Andhra Pradesh State in India, site of 250 000 suicides by indebted farmers', see: Bateman, 'Microcredit and Marikana: how they are linked'.

⁷³ Stuart Theobald, *The risk of unsecured lending in South Africa* (Occasional Research Report, 2013)

⁷⁴ The National Credit Regulator, *Annual Report* (NCR Publications, 2014), p. 12.

⁷⁵ In 2016 55 per cent of South Africa's population was classified as living below the national (that is to say 'country specific') poverty line. As at 2011, almost 17 per cent were living on less than US\$ 2 per day. The World Bank Group, 'South Africa' (*The World Bank Group*, 2016) <http://databank.worldbank.org/data/Views/Reports/ReportWidgetCustom.aspx?Report_Name=CountryProfile&Id=b450fd57&tbar=y&dd=y&inf=n&zm=n&country=ZAF> accessed 10 November

⁷⁶ , 'Bottom of the class; South Africa's schools. Why South Africa has one of the world's worst education systems' *The Economist* (London 7 January) Middle East and Africa 37 <<https://search-proquest-com.ezproxy.library.uwa.edu.au/docview/1856037437?OpenUrlRefId=info:xri/sid:primo&accountid=14681>>

⁷⁷ See note 75 above.

⁷⁸ Erick F. Gerding, 'Subprime Crisis and the Link between Consumer Financial Protection and Systemic Risk' (2009) 4 Florida International University Law Review 435, p. 435.

⁷⁹ *Financial Sector Regulation Act*

⁸⁰ *Ibid*, Preamble; s 1(1) (definition of 'financial sector regulator'); 18; 22; 24; 34;43; 47(4) and (7); 66(5); 70(4) and (8); 79; 98(3) and (4); 100(3); 106(5); 250.

⁸¹ *Ibid*, s 22(1)(e).

⁸² *Ibid*, s 1(1) (definition of 'financial sector regulator').

⁸³ *Ibid*, s 2(1)(g).

⁸⁴ *National Credit Act*

⁸⁵ *Financial Sector Regulation Act*, Chapter 4; s 106.

⁸⁶ See for example the annual reports and statistics released by the NCR in Schmulow, 'Curbing reckless and predatory lending: A statutory analysis of South Africa's National Credit Act'.

⁸⁷ See for example: Basel Committee on Banking Supervision, *Core Principles for Effective Banking Supervision*, 2012), Principle 2 at p. 22 which states: 'The supervisor ... is accountable for the discharge of its duties and use of its resources'; The International Organization of Securities Commissions (IOSCO), *Objectives and Principles of Securities Regulation*, 2003), Principle 2 at p. i which states: 'The regulator should be operationally independent and accountable in the exercise of its functions and powers'.

⁸⁸ In the case of ASIC, submission of reports is required by the *Australian Securities and Investments Commission Act (Cth)*, s 136. For the position in the UK, New Zealand and the Netherlands, see: 'Accountability mechanisms' in A. J. Godwin, T. Howse and I. Ramsay, 'Twin Peaks: South Africa's Financial Sector Regulatory Framework' (2017) 134 South African Law Journal 665

⁸⁹ See for example: Senator Mark Bishop (Chair) and others, *Performance of the*

Australian Securities and Investments Commission, 2014)

⁹⁰ Media and public oversight should not be underestimated. Media scrutiny of the performance of the Australian regulators has been extremely critical, extensive and long-standing. The result has been persistent demands for a Royal Commission of Inquiry into conduct in the banking sector, and of the conduct of the regulators. For more see 'Regulatory Failure' in Schmulow, 'Protection of Financial Consumers in Australia'

⁹¹ *Financial Sector Regulation Act*, s 55(1)(c).

⁹² *Public Finance Management Act (as amended)*, s 55(1)(d)(i).

⁹³ *Financial Sector Regulation Act*, s 21(c)(i), which states: '[The Financial Stability Oversight Committee has the following functions:] to advise the Minister and the Reserve Bank on— (i) steps to be taken to promote, protect or maintain, or to manage or prevent risks to, financial stability.'

⁹⁴ *Ibid*, ss 79ff. See also: "Financial System Council of Regulators" in Godwin, Howse and Ramsay, 'Twin Peaks: South Africa's Financial Sector Regulatory Framework'.

⁹⁵ Taylor, "*Twin Peaks*": *A regulatory structure for the new century*, p. 11.

⁹⁶ House of Lords, House of Commons, '*An accident waiting to happen: The failure of HBOS (5: A failure of regulation*, 2013), § 84, p. 28.

⁹⁷ *Ibid*, § 85, p. 28. See also: Financial Services Authority, *The failure of the Royal Bank of Scotland* (Financial Services Authority Board Report, 2011), § 30, p. 28.

⁹⁸ Financial Services Authority, *The failure of the Royal Bank of Scotland*, p. 7.

⁹⁹ Patrick Hosking, 'More lever-arch files wouldn't have saved RBS' *The Times* (London Tuesday, 13 December) Opinion <<http://www.thetimes.co.uk/tto/opinion/columnists/article3256069.ece>>

¹⁰⁰ Financial Services Authority, *The failure of the Royal Bank of Scotland*, Part 2, Chap. 3, p. 277.

¹⁰¹ For original reference, see: *ibid*, Table 2.18, p. 280.

¹⁰² *Ibid*, Part 2, Chap. 3, p. 260.

¹⁰³ Hosking, 'More lever-arch files wouldn't have saved RBS'.

¹⁰⁴ Senator Mark Bishop (Chair) and others, *Performance of the Australian Securities and Investments Commission*.

¹⁰⁵ See further: Schmulow, *Twin Peaks: A Theoretical Analysis*, p. 47ff; Senator Mark Bishop (Chair) and others, *Performance of the Australian Securities and Investments Commission*; Adele Ferguson, 'Royal commission: not a populist whinge for burned bank customers' *The Sydney Morning Herald* (Sydney, NSW 13 August) Comment <<http://www.smh.com.au/business/banking-and-finance/royal-commission-not-a-populist-whinge-for-burned-bank-customers-20160812-gqqyll.html>> Adele Ferguson, 'A banking royal commission couldn't make the sector's reputation any worse' *The Australian Financial Review* (Sydney, NSW 11 April) Business/Banking & Finance/Financial Services/Opinion

<<http://www.afr.com/business/banking-and-finance/financial-services/a-banking-royal-commission-couldnt-make-the-sectors-reputation-any-worse-20160410-go2tso>> Adele Ferguson, 'Sweating on every word – how ASIC massaged the banking message' *The Sydney Morning Herald* (Sydney, NSW 21 April) Business/Comment <<http://www.smh.com.au/business/banking-and-finance/sweating-on-every-word--how-asic-massaged-the-banking-message-20170421-gvp9qt.html>> Adele Ferguson and Ben Butler, 'Commonwealth Bank facing royal commission call after Senate financial planning inquiry' *The Sydney Morning Herald* (Sydney, NSW 26 June) Banking and Finance <<http://www.smh.com.au/business/banking-and-finance/commonwealth-bank-facing-royal-commission-call-after-senate-financial-planning-inquiry-20140625-3asy6.html>>

<<http://www.smh.com.au/business/hearing-into-asics-failure-to-investigate-cbas-financial-wisdom-20140602-39ept.html>> Jane Lee, Cameron Houston and Chris Vedelago, 'CBA customers lose homes amid huge fraud claim' *The Age* (Melbourne, Vic 29 May) Victoria <<http://www.theage.com.au/victoria/cba-customers-lose-homes-amid-huge-fraud-claim-20140528-394se.html>>

¹⁰⁶ James R. Barth, Gerard Caprio and Ross Levine, 'Making the Guardians of Finance Work for Us', *Guardians of Finance: Making Regulators Work for Us* (Guardians of Finance: Making Regulators Work for Us, MIT Press 2012), p. 205/6.

¹⁰⁷ *Ibid*, p. 211.

¹⁰⁸ *Ibid*, p. 213.

¹⁰⁹ Recommendation 27, Financial System Inquiry, *Financial System Inquiry Final Report*, 2014), p. 239.

¹¹⁰ *Ibid*, p. 235.

¹¹¹ *Ibid*, p. 239.

¹¹² APRA asserted that there was a difficulty in 'demonstrating causality or an explicit link between the prudential regime or supervisory actions and the outcomes for individual financial institutions or the financial system as a whole' Australian Prudential Regulation Authority, *Financial System Inquiry Submission*, 2014), p. 62; that the secrecy provisions of the *Banking Act (Cth)* precludes 'offering public commentary on its day-to-day activities' and further that 'performance assessment of a prudential regulator does not lend itself to straightforward cost-benefit analysis.' Australian Prudential Regulation Authority, *Financial System Inquiry*

Submission, p. 63. Cf Barth, Caprio and Levine, 'Making the Guardians of Finance Work for Us', p. 217, where the authors put forward a proposal for a Sentinel, and state: "Sentinel demands for information must trump the desires of regulatory agencies for secrecy".

¹¹³ Pat McConnell, 'War on banking's rotten culture must include regulators' *The Conversation* (Melbourne, VIC 4 June) Business & Economy <<http://theconversation.com/war-on-bankings-rotten-culture-must-include-regulators-42767>> See also: Julie May, 'Regulatory board to beef up watchdog accountability' *Financial Observer, Daily News for Financial Services Professionals* (Sydney, NSW 10 December) News / Financial Planning <<http://www.financialobserver.com.au/articles/regulatory-board-to-beef-up-watchdog-accountability>>; Marion Williams, 'APRA and ASIC need cultural shift' *Asia-Pacific Banking and Finance* (Sydney, NSW 9 March) Banking <<https://www.australianbankingfinance.com/banking/apra-and-asic-need-cultural-shift/>>; Andrew Schmulow, 'To clean up the financial system we need to watch the watchers' *The Conversation* (Melbourne, VIC 4 March) Business & Economy <<http://theconversation.com/to-clean-up-the-financial-system-we-need-to-watch-the-watchers-38359>>; Ruth Williams, 'Merit in oversight board for ASIC, but only if it's got teeth' *The Sydney Morning Herald* (Sydney, NSW 28 January) Business Day <<http://www.smh.com.au/business/merit-in-oversight-board-for-asic-but-only-if-its-got-teeth-20150127-12z7zy.html>> See also: Barth, Caprio and Levine, 'Making the Guardians of Finance Work for Us', p. 211.

¹¹⁴ Barth, Caprio and Levine, 'Making the Guardians of Finance Work for Us', p. 209.

¹¹⁵ See further: Llewellyn, *Institutional Structure of Financial Regulation and*

Supervision: The Basic Issues, p. 41 on the advantages of regulator accountability.

¹¹⁶ Financial Policy Committee, 'Financial Policy Committee' (*Bank of England*, 2014)

<<http://www.bankofengland.co.uk/financialstability/pages/fpc/default.aspx>> accessed 26 September

¹¹⁷ Jill Treanor, 'Farewell to the FSA – and the bleak legacy of the light-touch regulator' *The Guardian/The Observer* (London, UK 24 March) Business <<http://www.theguardian.com/business/2013/mar/24/farewell-fsa-bleak-legacy-light-touch-regulator>>

¹¹⁸ Barth, Caprio and Levine, 'Making the Guardians of Finance Work for Us'.

¹¹⁹ Australian Government, *Improving Australia's Financial System, Government response to the Financial System Inquiry*, (2015), p. 23.

¹²⁰ See: Barth, Caprio and Levine, 'Making the Guardians of Finance Work for Us', p. 207 for an account of the manner in which the US Federal Reserve resisted Congressional oversight, even going so far as to ignore Court orders that they release information on how they measured 'systemic risk'.