

Financial Sector Regulation Bill 2013

Implementing Twin Peaks – Phase 1

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Department:
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REPUBLIC OF SOUTH AFRICA

Consultation process

- Process
 - **December 2013** Bill published for public comment
 - **January – February 2014** Initial consultation with stakeholders
 - **7 March 2014** Comments deadline
 - **March – April 2014** Individual stakeholder consultations, based on comments received
 - **Post Election** Tabling

All documentation is available at www.treasury.gov.za/twinpeaks

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- Background and Outline of Phased approach

Phase 1

- Structure of regulators
- Market conduct and prudential peak
- Regulatory action
- Licensing
- Rule making
- High-level Resolution Powers

Phase 2

- Giving legislative backing to *Treating Customers Fairly*
- Gaps in current market conduct legislation
- Gaps in prudential legislation
- Resolution Bill

Background - Cabinet has approved four policy objectives

- Need to improve **market conduct**:
 - Financial services firms (banks, insurers etc) continue to charge high fees and have complex terms and conditions that do not meet the needs of customers. South Africa's current *approach to market conduct is fragmented* and needs to be improved
- Need to combat **financial crime**:
 - Recent cases (e.g. Fidentia) have highlighted we have gaps in our system that need to be resolved.
- Need to strengthen **financial stability**
 - Financial crises can impose enormous costs on the taxpayer and on society – need to ensure we have a system on par with best in the world
- Need to widen access to **financial services**
 - Access is important for inclusive economic growth

In South Africa reform proposals in four priority areas for a safer financial sector

Financial Stability / Prudential

- Reserve Bank to lead on macro-prudential (systemic stability) and micro-prudential (safety and soundness of institutions)
- Financial Stability Oversight Committee

Market conduct

- Comprehensive market conduct regime reflecting interconnected nature of financial services
- Treating customer fairly
- Fit and proper requirements
- Ombud schemes
- Financial literacy

Access to financial services

- Treasury to lead
- Financial sector code
- Co-operative and dedicated banks, and Postbank
- Introduce a microinsurance framework
- International co-operation

Combating financial crime

- Enforcement agencies to lead
- Investigating and prosecuting abuses
- Continued work with international partners

It is vital to ensure coordination and information sharing between regulators particularly in the face of an event that threatens systemic stability

Recap: What does twin peaks attempt to achieve?

Prudential Authority

- Enhanced oversight of micro-prudential regulation for banks, insurers, financial markets, *special focus on conglomerates*

Market Conduct Authority

- Regulatory laws that are *complete, harmonised, integrated, proportionate* - **all** financial services, incl, banking i.e. 2013 Banks Act amendment
- *Increased focus on outcomes*, esp. fair “Treating customers fairly” and focus on contract terms & costs
- *Targeted interventions to market failures* - retirement reform, Jali Commission recommendations, insurance protection, FAIS

Financial Services Tribunal and Enforcement

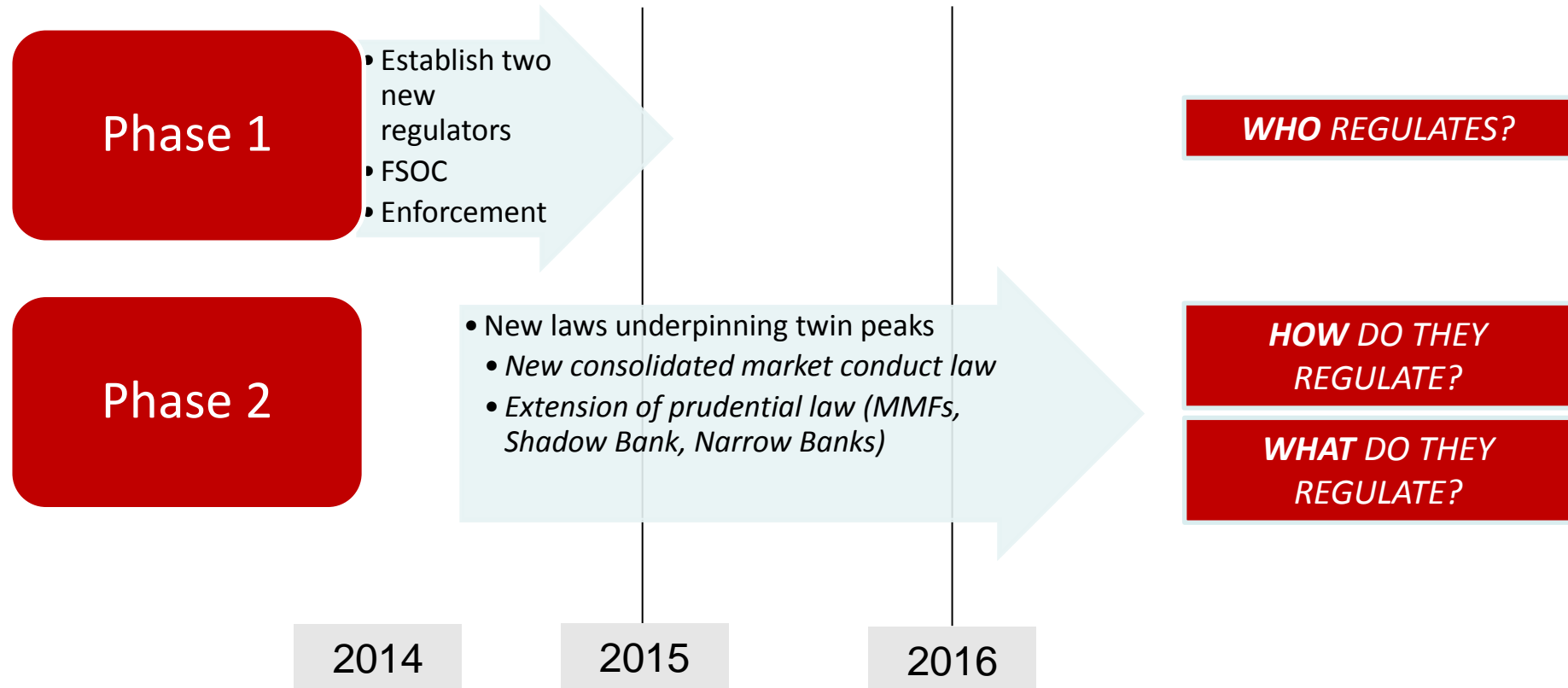
- Regulators will have clear internal policies & procedures for enforcement, enhanced transparency & accountability, strong appeal mechanism

Financial Stability

- Inter-agency co-ordination of financial stability issues



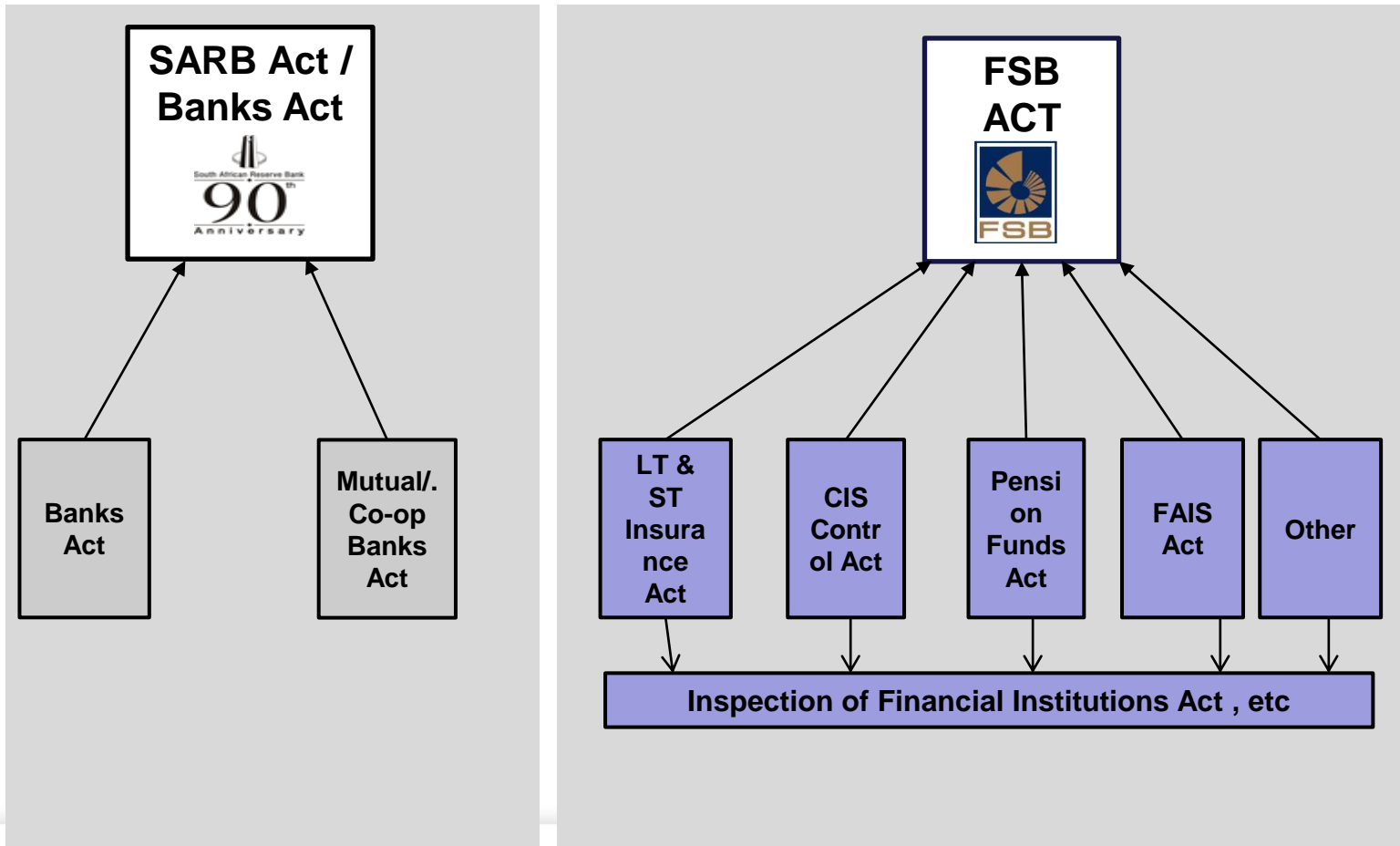
'Twin peaks' will be implemented in a phased manner



Phased approach reduces risks and simplifies implementation

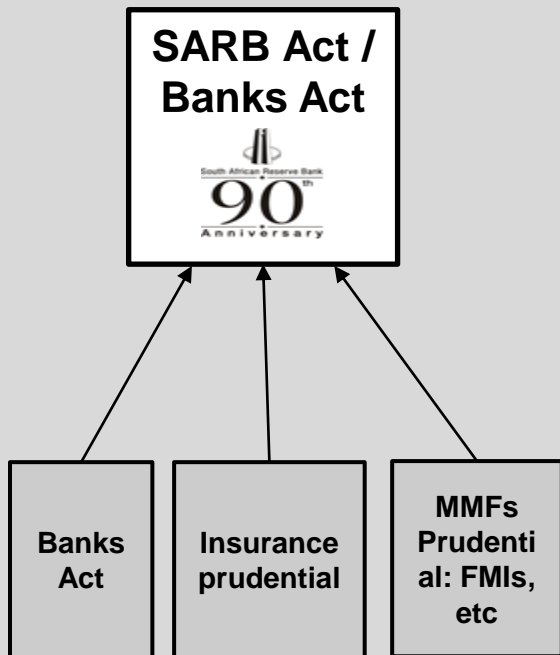
Current regulatory architecture...

- *Before.....*

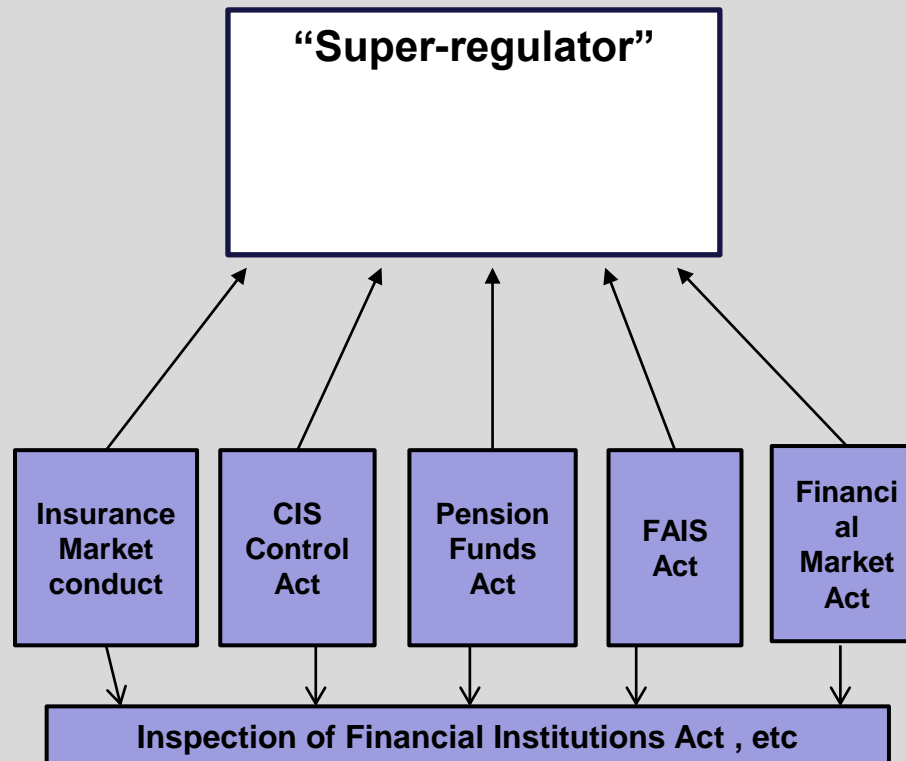


Proposed regulatory architecture...

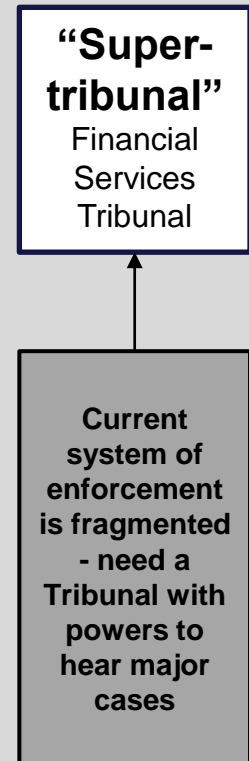
Prudential



Market conduct



FST



Financial Stability is delegated to the Reserve Bank within an agreed policy framework

- entrench the primary role of the Reserve Bank (s4)
 - to **promote financial stability** and
 - implementing steps towards **restoring financial stability** in the event of a crisis
- establish the **Financial Stability Oversight Committee (FSOC)** (s5)
 - to assist the Reserve Bank to maintain financial stability and
 - to respond to financial crises while maintaining the operational independence of financial regulators
 - shall consist of (s6): the Governor (chair), CEO and DGs of SARB, Commissioner and two (min) DCs of MCA, DG of NT

Authorities with enhanced accountability, coordination & operational independence

- A stand-alone **Market Conduct Authority** (s12, ch3)
 - to strengthen financial customer protection
 - to promoting the integrity of financial markets, consumer education and financial inclusion
 - lead regulator of financial institutions carrying out **mono-regulated activities**
 - joint regulator of financial institutions carrying out **dual-regulated activities**
- **Prudential Authority** within the SARB (s13, ch3)
 - to regulate the safety and soundness of individual financial institutions carrying out **dual-regulated activities**
 - lead regulator of financial institutions carrying out **dual-regulated activities**

Enhanced coordination and co-operation between regulators

- a legal framework for enhanced coordination and co-operation when exercising respective powers and performing their respective duties:
 - **between the PA and MCA**
 - including a **memorandum of understanding** (s44)
 - Co-operation into, e.g. licensing, rule-making, etc.
 - **between regulatory authorities and other financial regulators**
 - through **Council of Financial Regulators (“CFR”)** (s56) and
 - establishment of **Subcommittees** of CFR (s58)

Balance operational independence and accountability of regulators

The Bill

- Strengthens the operational independence of regulators, while ensuring accountability
- Provides a governance framework that will provide clarity on the policy objectives of Government
- Ensures the necessary operational powers and independence of regulators to perform duties impartially

Financial crisis management and resolution

- identifies the SARB as **the resolution authority** in South Africa
- outlines action the governor must take where FSOC detects any risk, weakness, development or disruption in the financial system that may give rise to a financial crisis (s63)
- outlines **crisis management responsibilities**
 - of the Minister which may have impact on public finances (s64)
 - Reserve Bank (s65)
 - The regulatory authorities (s67)
- powers to the Minister to make **Emergency regulations** for the management and mitigation of an impending or actual financial crisis (s68)

Administrative actions and appeals

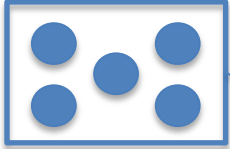
- to promote a **consistent and harmonised approach** by the regulators for all regulatory decisions, incl. licensing through to the imposition of penalties
- to outline **enforcement mechanisms** aimed at encouraging compliance with all aspects of the new regulatory regime and to help combat financial crime
- to provide for the use of **administrative penalties, referrals** to an administrative decision-making body, and referral of **matters for criminal prosecution**
- to enable **supervisory actions** such as suspension or withdrawal of licences and approvals, orders to take or cease particular actions, and debarments
- to establish a **Financial Services Tribunal** to serve independently from the regulatory authorities and hear administrative appeals against decisions taking by the PA or the MCA
- a **two-phased** approach to shift to “twin peaks”

Phase 1:

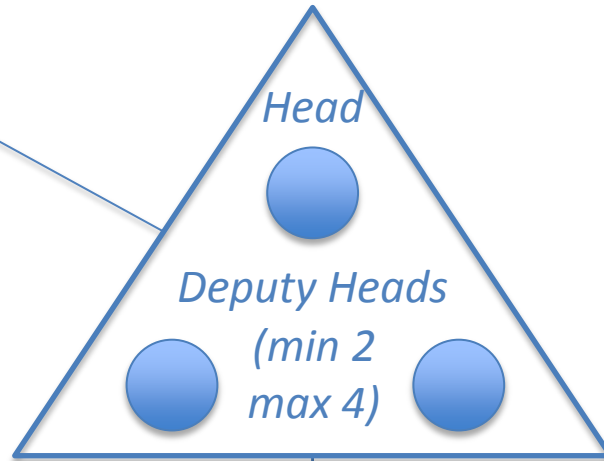
Governance, structure and accountability of the two regulators

MARKET CONDUCT AUTHORITY

Governance Committee



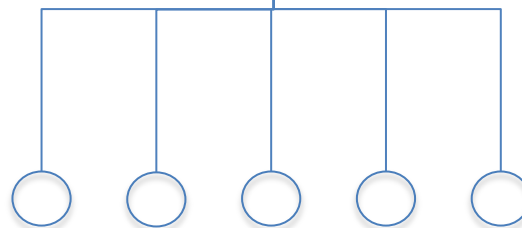
THE AUTHORITY



- Single committee
- At least 5 members, appointed by Minister
- Must cover: risk, audit & remuneration

- Power vested collectively in Head & Deputies
- Head has override power if outvoted
- Head & Deputies appointed by Minister
- Authority is juristic person and PFMA accounting body
- Funding through levy

Statutory elements of structure

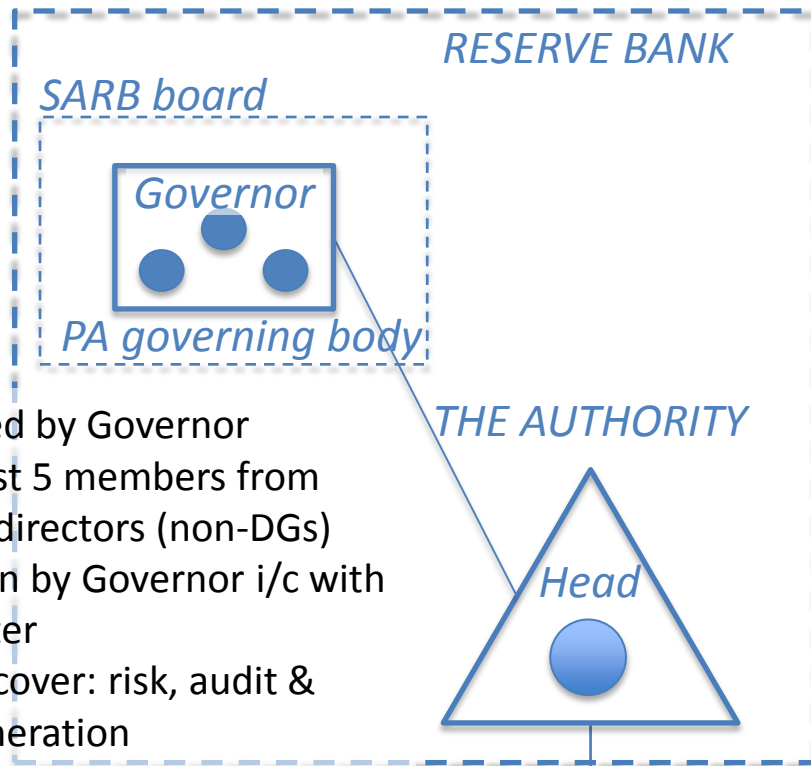


Management / organisational structure

- Authority has power to delegate responsibility to staff / management
- Structure / appointments at discretion of the Authority

Non-statutory elements of structure

PRUDENTIAL AUTHORITY



- Chaired by Governor
- At least 5 members from SARB directors (non-DGs)
- Chosen by Governor i/c with Minister
- Must cover: risk, audit & remuneration
- Governor may add additional responsibilities

- Organisation & structure of governing body at discretion of Governor
- Governor may also use GEC as forum to manage PA issues within SARB

- Authority established within the SARB
- Power of the Authority vested in office of Head
- Head = a DG, appointed by Governor in consultation with Minister
- Authority is juristic person under the management & control of SARB
- Self-funded (mechanism tbd)

Statutory elements of structure

- Authority has power to delegate responsibility to staff / management
- Structure / appointments at discretion of the Head of the Authority

Non-statutory elements of structure

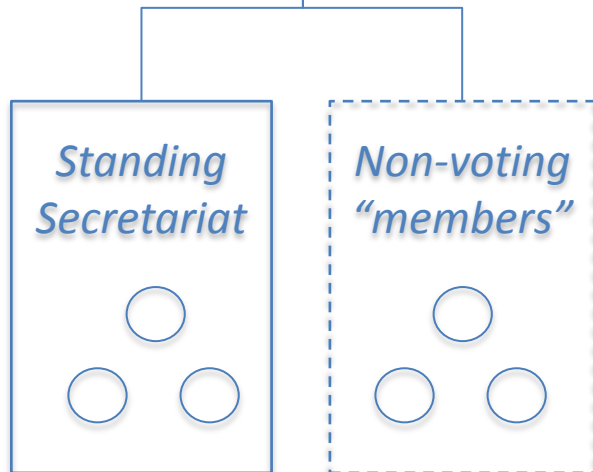
Management / organisational structure

FINANCIAL STABILITY OVERSIGHT COMMITTEE



- Statutory committee of SARB, with objective to contribute to financial stability mandate
- Meetings at least quarterly
- Chaired by Governor – casting vote
- Ex officio members:
 - Head PA + 1 DG
 - Head MCA + 1 DH
- NT member – participates in meetings but cannot vote
- Governor may appoint external (voting) members i/c with Minister
- Others may attend at invitation of Governor

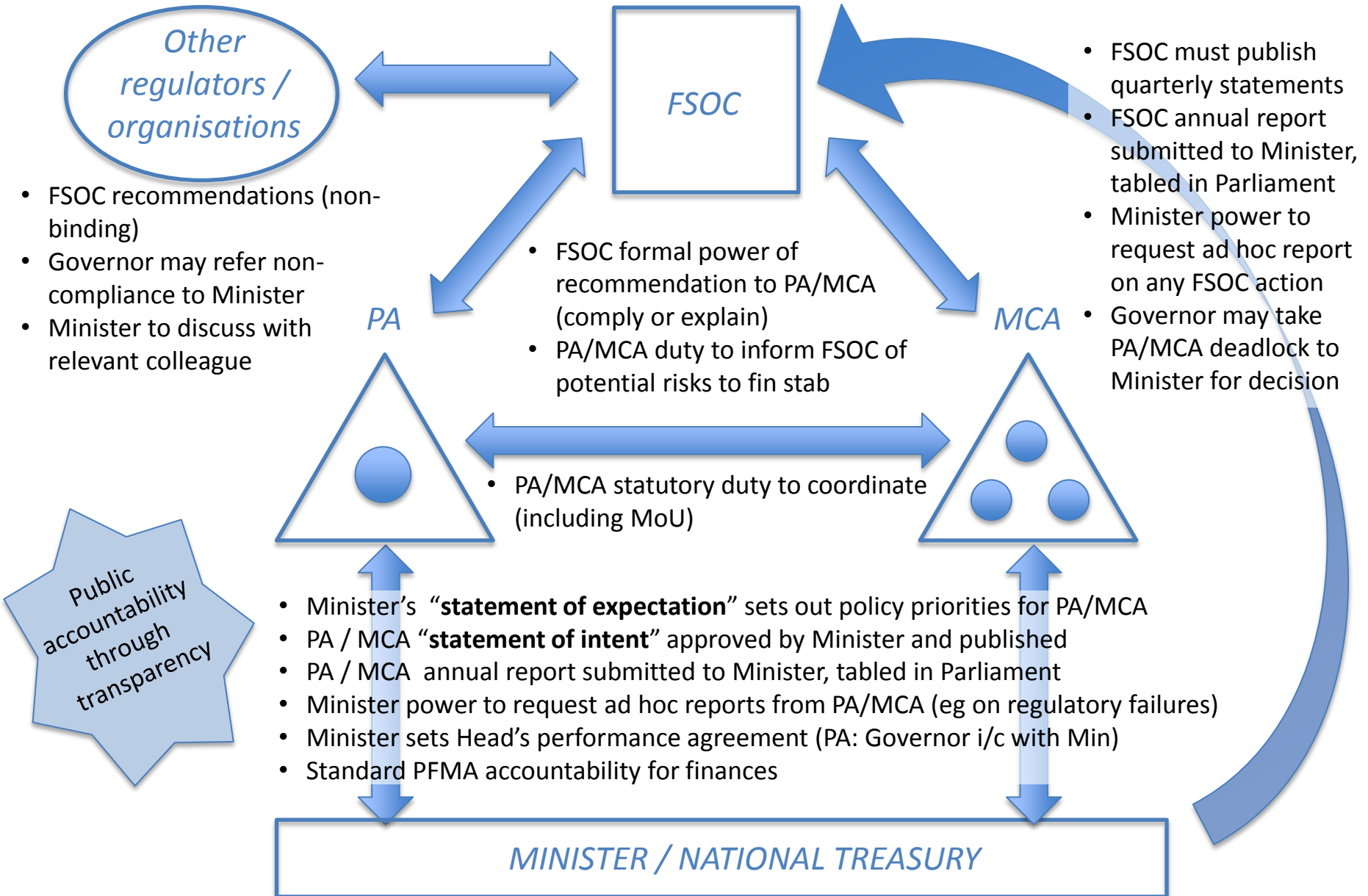
Statutory elements of structure



- Other FSOC attendees may, at discretion of the Governor, form an informal cadre of non-voting members
- Standing secretariat with staff from all 3 authorities to support meetings, gather data, commission analysis etc

Non-statutory elements of structure

INSTITUTIONAL LINKS: influence / accountability



Other issues

- **Funding of regulatory authorities** (s. 36)
 - Role & determination of industry levies
- **Licensing of regulated entities** (def, s. 3(2)(c), s. 54)
 - New concept of authorisations & entitlements, move to streamline procedures
 - Dual key in & out, st. joint rules (see below)
- **Rule making powers** (s. 45-52, s. 104)
 - Levelling of subordinate regulation – existing instruments now rules, st. rule making provisions in this Act
 - New concept of “joint rules”
 - Enhanced & standardised cooperation & consultation requirements (incl. Minister Regulation on “process for consultation on rules”)
 - Additional resolution powers to be contained in Resolution Bill

Prudential peak

Main components of Prudential Peak

Bank prudential

- Basel 3

Insurance prudential

- SAM

Collective Investment schemes

- “Implicit or explicit guarantee”

Financial Market Infrastructure Prudential

- Safety and soundness of the FMIs (operational risk, market risk etc.)

Financial Markets Act prudential

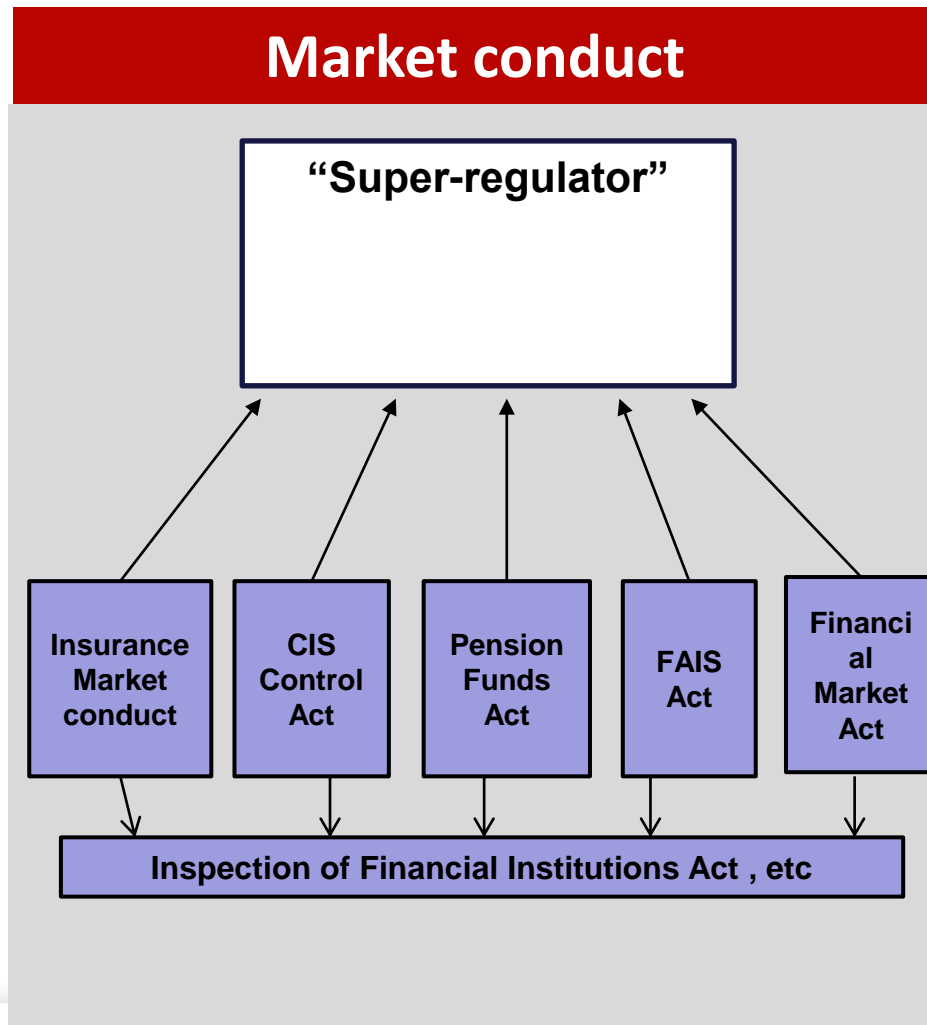
- Safety and soundness of authorised users, clearing members, settlement members etc. Risk-based approach

Phase 2 focus for prudential peak

- Conglomerate supervision
- Resolution
- Current anomalies:
 - Banks are regulated by Bank Supervision through Banks Act
 - Clearing and settlement members are regulated through the Financial Markets Act, with frontline supervision delegated to JSE / Strate
 - Large broker dealers are not directly regulated by Bank Supervision
 - Transitional arrangements will need to be considered
- ‘Shadow banking’
 - Non-banks fulfil roles previously fulfilled by banks
 - Includes both ‘deposit-taking’ and ‘lending’, e.g. BMW Financial Services provides mortgages and does securitisations

Market Conduct Peak

Proposed regulatory architecture...



- Initially, market conduct regulator will continue to function according to existing Acts

E.g. Previously

Registrar of FAIS = EO of FSB

Day-to-day Head of FAIS Dept

Transition

Registrar of FAIS = Commissioner and Deputy Commissioners of MCA

Day-to-day Head of FAIS Dept

Future: Licensing, registration, enforcement etc. will be streamlined

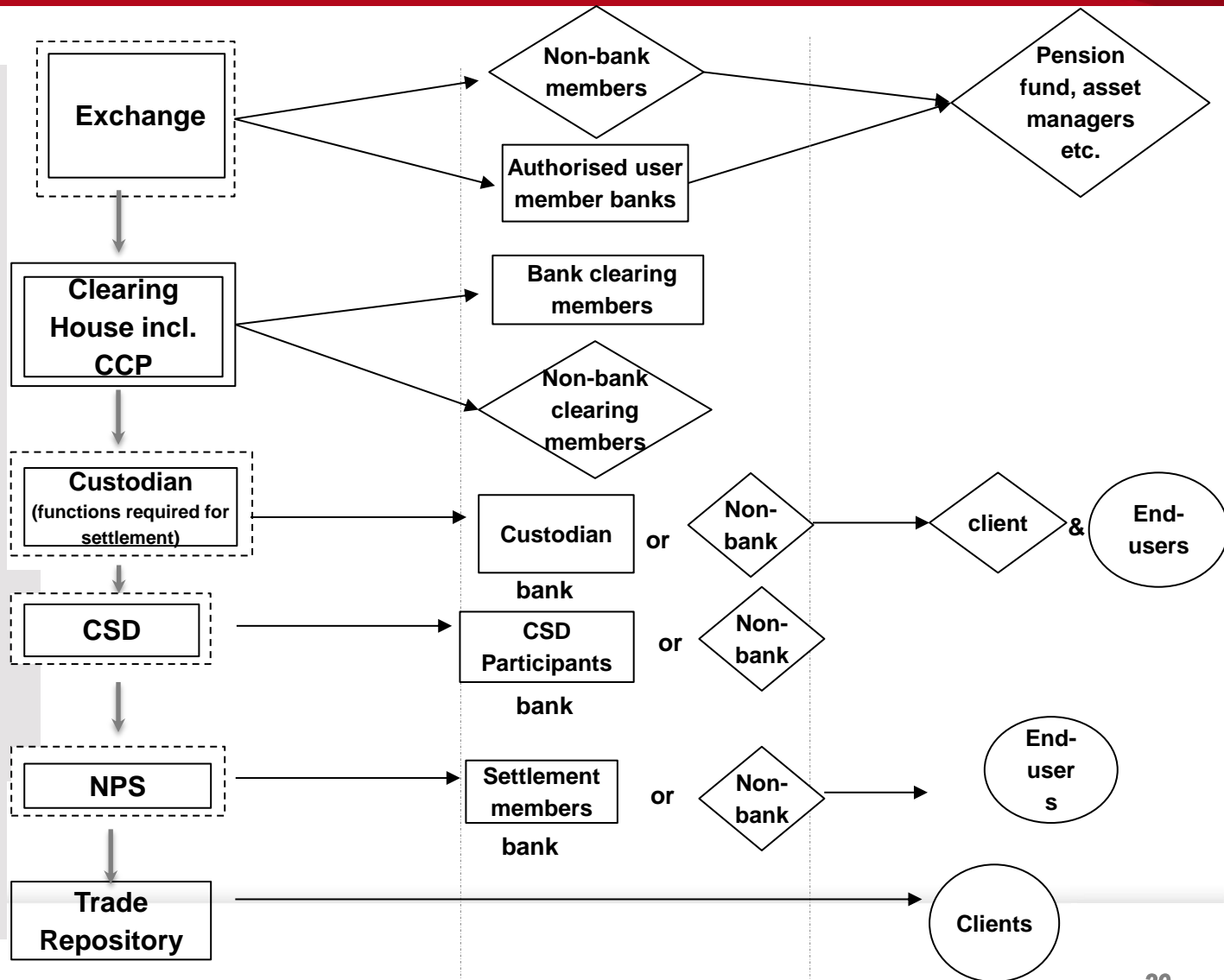
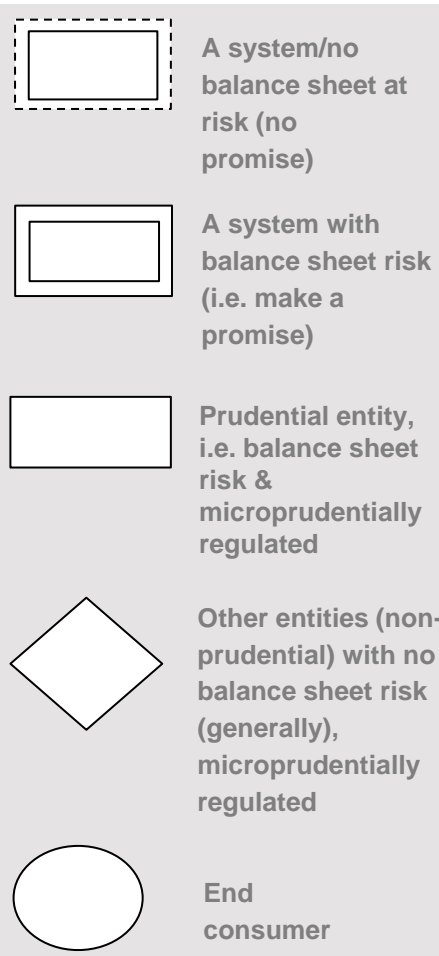
Role of credit is under discussion within government

Phase 2 focus for market conduct peak (underway)

- Developing market conduct policy framework
 - More effective regulation: Conduct of Business law, supporting full implementation of TCF initiative
 - More effective supervision: Amendments to FSR Bill to enhance supervisory toolkit
- Priority targeted interventions:
 - Retail banking
 - Saving for retirement
 - Retail Distribution Review

Special Case of FMI

FMI is a complex area to delineate



In Phase 1 there will be minimum disruption

- During Phase 1, front-line supervision of authorised users will be undertaken by the JSE (no change)
- JSE rules are being recast into “Prudential” and “Market Conduct” rules
- JSE rules will be approved by both PA (Prudential rules) and new MCA (Market Conduct rules)
- Over time front-line supervision for large prudentially-relevant authorised users will be moved to the Reserve Bank

Issues for discussion

- Transitional arrangements
 - Minimising risks
- Schedule:
 - Activities versus institutions
- Enforcement mechanisms
- Other?

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