A Framework for Implementing a Twin Peak Financial Regulatory Model: Institutional Logics Theoretical Perspective

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Abstract

This paper examines the institutionalisation of the Financial Services Regulations Act, in South Africa which gave effect to a Twin Peaks Financial Regulation Model. The aim of the paper is to introduce an institutional logics framework that financial services institutions may use to identify enabling and disabling institutional assumptions, principles and values that lead to a successful institutionalisation of a Twin Peaks Financial Regulatory Model in a developmental state. Institutional logics, a strand of institutional theory, is the lens through which this paper examines the institutionalisation of the Twin Peaks regulatory regime in South Africa. South Africa is the only country in the African continent that has implemented the Twin Peaks regulatory Model; and is one of only 38 OECD countries that implemented the Twin Peaks model. The paper critiques the societal and institutional considerations that shaped the development of the Twin Peaks Model in South Africa.

Key words: financial services regulation, Twin Peaks model, institutional theory, institutional logics, societal logics
J.E.L. classification: G28

1. Introduction

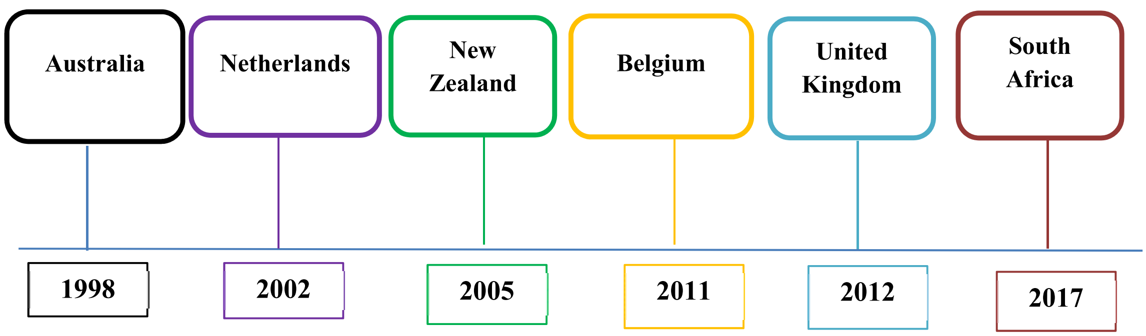
The financial regulatory sector revolves around a dominant financial logic which Jensen (2002), describe as a guiding force that focuses on individualism and profit maximisation. Some researchers argue that financial logics may be associated with the need for legitimacy in the financial markets and in regulatory institutions (Almandoz, 2012). Financial regulation concerns the regulation of the financial system as a whole, with different logics at play to ensure financial stability. There has been a growing attention on legitimacy of institutional logics where emphasis is placed on the role of the state, best policy practice, and how best resources can be distributed through new institutional practices derived from legislation and regulation (Zald and Lounsbury, 2010). Yan, et al., (2018) posits that even though financial logics compete and are complimentary with other social goals, embedding these in the social fibre of society depends on how the logics resonate with societal logics, that is, societal values, norms and belief systems. Because societal logics are a set of organising principles which define how social life operates, Zald and Lounsbury (2010), argues that financial logics and societal logics should have a close fit.

The institutional logic concept was conceived by Alford and Friedland (1985) to shed light on why contradictory practices and beliefs exist in institutions of developed countries. In getting to understand these contradictions in developed country's institutions, Friedland and Alford (1991) developed the concept of institutional logics to explain the interrelationships between individuals, institutions, and society. Societies in the developing world are very different to societies in developing countries with a dual economic system such as South Africa. South Africa introduced a new financial regulation legislation in 2017 that gave rise to the Twin Peaks regulatory model. The Twin Peaks Model in South Africa carves a space for a new work environment in financial services.

This new model also marks a departure from a sectorial approach in financial regulation to a regulatory model characterised by two regulators (two peaks) whereby one regulator, the Prudential Authority performs a risk-based safety and soundness function while the other regulator, the Financial Sector Conduct Authority, focuses on business conduct, consumer protection and market integrity. Central to the instutionalisation of the Twin Peaks Model in South Africa is how the unique societal contexts have been catered for in the crafting of the FSRA, given the dual economic system in the country.

The South African banking sector caters for a society deeply divided by its colonial and apartheid history. Added to that, South Africa is the only country in the African continent that has implemented the Twin Peaks regulatory Model; and is one of only 38 OECD countries that implemented the Twin Peaks model. This begs the question: what are the societal and institutional considerations that shaped the development and the institutionalisation of the financial services regulatory regime that gave birth to the Twin Peaks Model in South Africa? The newly adopted Twin Peaks Model in South Africa is uniquely positioned in this paper as a social laboratory to examine the enablers and disablers of effective implementation of a new financial regulatory model in a society with multiple actors that have multiple value systems within multiple and sometimes diverse institutional logics. As depicted in Figure 1.1 the Twin Peaks Model was pioneered in Australia and subsequently adopted by the United Kingdom, Belgium, New Zealand, the Netherlands and South Africa (Godwin, 2017 and Godwin, 2018).

Figure no. 1 Countries that adopted Twin Peak model financial services regulatory regime



Source: (Msweli and Ryneveldt, 2023)

Australia adopted the Twin Peaks Model in 1998, on the recommendation of the Wallis financial regulatory inquiry (Schmulow, 2015). The Twin Peaks Model was adopted in the Netherlands in 2002. And in New Zealand it occurred periodically in 2005 when the Reserve Bank of New Zealand was appointed as the prudential regulator, and in 2011, when the Financial Markets Authority came into existence (Godwin et.al., 2017). In 2011 the Belgian financial regulatory system transitioned to the Twin Peaks Model (Godwin et.al., 2017). South Africa is the only developing country globally, and the only country in Africa that has adopted the Twin Peaks Model as its preferred financial regulatory model.

The central question around which this paper is centred is that: given the dense institutional field characterised by two dominant institutional environments – the Prudential Authority and the Financial Services Conduct Authority, in a society with multiple societal and organisation value systems, what are the factors that enable effective implementation of the Twin Peaks model in South Africa? The next section discusses institutional logics as the theoretical lens through which the question was addressed.

2. Theoretical background: Institutional Logics

Thornton and Ocasio (1999:804) define institutional logics as '*the socially constructed, historical patterns of material practices, assumptions, values, beliefs, and rules by which individuals produce and reproduce their material subsistence, organise time and space, and provide meaning to their social reality*'. In reviewing the conceptualisation of institutional logics as set out by the above prominent researchers, institutional logics can be seen as a set of rules that confer organizational legitimacy and sustainability. At its core, institutional logics provide society's master principles that guide social action (Greenwood et al., 2010). Alford and Friedland (1985) introduced the institutional logics terminology to give a description of the different belief systems and practices inherent in organisations. For Friedland and Alford (1991) institutional logics is a means that drive organisational actors with institutional principles that enable them to achieve their end-goals by enacting the most appropriate action. In a different conceptual comprehension of institutional logics, Jackall (1988) defines it as a contingent set of rules that are constructed by complexities and social experiments which in turn give rise to how organisational actors enact and participate in a particular context that is predictable. With the benefit of Alford and Friedland (1985), and Jackall's (1988) seminal work, Table 1 summarises institutional logics definitions while simultaneously mapping out organisational actors' objectives.

Table no. 1 Institutional Logics definitions - organisational actors, means and objectives

Author	**Organisational actors**	**Means**	**Objectives**	**Research focus**
Alford and Friedland (1985)	Institutional participants	Institutional principles	Enacting the most appropriate action	Capitalism, bureaucracy
Jackall (1988)	Institutional participants	Set rules	Predictable action	Corporate Managers-moral mazes
Thornton and Ocasio (1999: 804)	Individuals	The socially constructed, historical patterns of material practices, assumptions, values, beliefs, and rules	Produce and reproduce their material subsistence, organize time and space	Executive Succession in the Higher Education Publishing Industry
Ocasio and Gai (2020:267)	Institutional participants	Socially constructed and historically contingent	Practices and vocabularies give rise to change in institutions	Institutional theory, mergence and growth of institutionalism

Source: (Msweli and Ryneveldt, 2023)

Barley and Tolbert (1997) define institutions as spaces where social actors share rules to legitimise the execution of specific activities organised in structured relationships. In comprehending the various elements of this definition and in an attempt to make it more inclusive, Scott (2008a) identifies three pillars on which institutions should be defined. For him institutions consists of (1) regulative, (2) normative and (3) cultural cognitive elements that work in unison to provide stability and meaning to social life through an active involved process of activities and resources. Institutions thus govern society's behaviour by institutionalising society's practices, with penalties in the event of any deviation (Jepperson, 1991). In furtherance of this view, North (1990) reiterates the importance to distinguish between institutions and organisations, where institutions specify the rules of the game, whereas organisations play according to institutional rules. Thus, institutions are guided and constituted by rules, culture and social structures (Ocasio and Gai, 2020). Ocasio and Gai (2020: 267) posit that institutional logics are '*socially constructed and historically contingent, as the practices and vocabularies associated with institutions change*'.

This definition implies that institutions are spaces defined by culture of change and how change is effected in institutions.

Jensen (2002), introduces a financial angle to institutional theory that he refers to as financial logic. Jensen defines financial logic as a guiding force that focus on individualism and profit maximisation. Some researchers even argue that financial logics or economic logic may be associated with the need for legitimacy in the financial markets, and in financial regulatory institutions, (see for example Almandoz, 2012; and Smets, Jarzabkowski, Burke, and Spee, 2015). DiMaggio and Powell (1983), postulates that institutional fields consist of various communities each with its own institutional logic. Fitzgerald and Shepherd (2018) go on to define two sets of logics: social and commercial logics and frame these logics in terms of the desired outcome, driver, tactic used, source of legitimacy and funding source. Fitzgerald and Shepherd's work makes a point around mediation and diffusion of incompatible logics in an organisational space. The authors argue that logic compatibility is impacted by the manner in which multiple sets of logics are integrated and allowed to co-exist without undue conflict. Such an integration as pointed out by Fitzgerald and Shepherd (2018) is influenced by a set of drivers, including source of funding, source of legitimation and structure selected by the organisation.

In this work, we posit that the Twin Peaks Model institutions operate within a set multiple institutional fields, made up of key suppliers, resources, services and products, consumers, regulatory institutions and other stakeholders that produce similar services or products' (see for example DiMaggio and Powell, 1983). With this understanding of institutional logics this paper focuses on two dominant institutional fields involved in the implementation of the Twin Peaks financial regulatory model in South Africa: the regulatory agency responsible for the safety and soundness of all financial institutions in South Africa – the Prudential Authority; and the regulatory agency responsible for regulating financial companies' marketing practice – the Financial Sector Conduct Authority. With a starting point on the societal and institutional basis for the implementation of the Twin Peaks Model, institutional theory states that embeddedness of institutions within the broader societal parameters depicts the co-evolution and co-existence of society and institutions (Hasse and Krücken, 2008; Wooten, 2016; Yan et al., 2018; Yan et al., 2021; Fitzgerald and Shepherd, 2018). While the embeddedness of institutions within society cannot be disputed, what remains ambiguous in institutional theory is how the compatibility or incompatibility of the societal and institutional logics affects the instutionalisation of statutes that govern institutions, in this case, the financial services sector. For instance, literature is replete with corporate governance failures in the financial services sector since the global financial crisis of 2008. However, institutional theory has not sufficiently probed the compatibility or incompatibility of the multiple value systems, norms, practices and beliefs that define social actors inside and outside financial services institutions and how these multiple value systems impact on the implementation of the Twin Peak Model financial regulation regime. This paper seeks to contribute to institutional theory by developing a framework and a set of indicators that can be used to assess the effective implementation of the Twin Peaks Financial Regulation Model.

3. Research methodology

To develop a framework as explained in the foregoing section, we started off by addressing this question: what are the factors that enable effective implementation of the Twin Peaks model in South Africa? Qualitative data for this study came from semi-structured interviews and from secondary sources, including the statutes, policy documents and annual reports from two case study financial regulatory authorities in South Africa. Participants were contacted via email after permission was obtained from two South African regulatory peaks – the Prudential Authority (South African Reserve Bank) and the Financial Sector Conduct Authority after ethical clearances were granted by the University of South Africa. These two Twin Peaks case study institutions are embedded within a country with multiple societal dynamics, and the dual economic context. The key institutional and societal themes that the paper focuses on are the ends, means and sources of legitimacy in institutions as guided by institutional theory.

A total of 20 interviewees participated in the study – nine (9) from the Prudential Authority and eleven (11) from the Financial Sector Conduct Authority. An inclusion criteria in selecting participants was that each participant is directly involved with the institutionalisation of South Africa's Twin Peaks Model. The number of participants in the research are subjected to qualitative saturation methodological principles. Moore (2015) posits that saturation as a methodological principle can be regarded as a sample size measurement. However the sample size is not determined by participant numbers but is instead measured by the appropriateness of the data (O'Reilly and Parker, 2013). It is in the light of qualitative saturation principles, that this study justifies a sample size of 20 participants. Data were analysed making use of thematic content analysis method. The analytical process has a deductive approach where it commenced with preconceived categories and codes which were derived from the institutional logics theory literature.

Data collected from the interviews with participants were conducted virtually in accordance with University of South Africa's Covid-19 position statement on research ethics.

4. Findings

Table 2 sets out the codes and themes that emerged from the primary data in respect to the effectiveness and efficiency of a Twin Peaks Model.

Table no. 2 Primary Data Codes Themes

Selected verbatim quotations	Codes	Emerging themes
How they have to work to, to work together and for instance they have to make, they have to work together when they define the [indigenous language] …so how they will use some supervisory powers (Int1) *What they, how the structured themselves. How they operate want to mention in question 3 is what you will find in chapter 5 which is the cooperation and collaboration* (Int5) *And there is a lot of cooperation and coordination amongst the regulators* (Int3) *We need to collaborate and cooperate* (Int4) *we could have missed certain aspects of it, so the consultation then between the regulators, if I may put it that way* (Int5) *It means that you also cooperate in a supervisory committee* (Int6) *How do we work together between peak one and peak two* (Int8)	• Relationship • Regulatory authority • Regulatory framework • Structure • Cooperate • Coordinate • Consultative process between the peaks	**Collaboration**
Yes, exactly yes, yes, and actually it is…so it is mainly…its goal is mainly to ensure that, that all the players who then, who have a role in financial stability regularly talk together and exchange views and perhaps make recommendations (Int1) *Ja, probably scan is the right word to determine what financial products, financial services and financial institutions are there* (Int2) *It is the conduct, it is the fair treatment of customers, how they must behave* (Int3) *But high profitability can be at the expense of consumers (*Int3) *Customer satisfaction and customer protection* (Int4) *Now you need to share, to change focus and not only on profit but on the customer* (Int4) *you also created stability within the financial sector but at the same time you gave that level of trust within the sector for, for, for users of financial products* (Int7)	• Regulatory objectives • Stakeholders • Financial stability • Communication • Financial services • Financial institutions • Financial products • Consumer rights • Consumer confidence	**Stakeholder interest**
The competence of the, the players who, who, who resides in the committee (Int1) *So that is basically what it all comes down to but obviously with your expertise and experience you will be able to then go a little bit more deeply into that* (Int3) *and build up skills and experience to be able to supervise effectively your larger more complex groups* (Int8) *so, the skills that you actually attract into the organization* (Int12)	• Skills • Knowledge • Experience • Expertise	**Competency**

we did not have the staff so there is a of internal focus (Int13)		
the efficiency of supervision-which design places the least administrative and financial burden on institutions (Int1) *Make it easier for your financial institutions to communicate with both of you and with less costs* (Int4) *There they go again, another model that is just gonna waste resources and not come up with any results* (Int10) *So, concerns are like increased costs* (Int11) *So it was always accepted I think that there will be an increase in costs* (Int13)	• Institutional impact • Regulatory cost • Administration	**Costs effective**
But communicate to the public at large so that they understand (Int2) *The need to engage, we cannot just operate in silos, we have to be there and talking* (Int3) *And very transparent, we have to be transparent* (Int3) *When I go to a bank and request information, is it possible that we can share that information so that my colleague from peak 2 does not go and ask for the same information* (Int4) *We were not talking to each other, We had different types of sector laws. Make it easier for your financial institutions to communicate with both of you* (Int4)	• Public awareness • Transparency • Trust • Relationship building • Minimize regulatory duplication • Financial sector input	**Communication**
to really focus a home in on those areas which we had not paid sufficient attention to (Int3) *would then become focused, then has visibility over the whole financial group* (Int3) *Now how do we do that if everyone is responsible for their own [indistinct] if we do not have a holistic view of what it entails* (Int5) *We did not have that birds view in* terms of risk (Int7) *As much as these are world class frameworks, they do not, they do not really look at you know in a holistic manner at your larger more complex groups* (Int8)	• Financial regulation • Financial system as a whole • Business conduct	**Comprehensive regulation**
So, this goes to the fairness and efficiency of the financial markets (Int3) *you know we are going to be introducing legal material we have got to consult and engage in a real and material way* (Int3) *So, it is and that goes to, it is not just, you do not just want to, you do not want a big hammer when it is actually a small problem* (Int3) *Also related to that, and how we are seen in the public. And also, the, how are we seen by regulated entities because really, they are our customers if we can, if you call it that.* (Int3) *I think the main principle for financial institutions is for them to treat their customers fairly* (Int4) *And what we have put in place is that each regulator will contact each other and concur to our decision* (Int4) *So that we get a holistic view then of the risk that are there, sector specific* (Int5) *Is how it has impacting on the industry as well and how the industry mind set is changing* (Int8) *Banks were supervised at a much granular level, whereas maybe insurers were supervised at a much higher level* (Int9)	• Market conduct • Market access • Consumer treatment • Shareholders rights • Fair outcomes • Regulation laws • Objectives • Functions • Consultation • Legal material • Impactful • Proportional • Risk based regulation • Regulatory instruments	**Consistent principles and rules**
But we expect it to be pre-emptive, we expect it to be outcomes focused (Int3) *So, I think you know leveraging, and I think more, and we are much more visible* (Int3)	• Focused • Goal orientated • Visible • Proactive	**Pre-emptive visible regulation**

Be proactive now and if you are able to see that this financial institution might be focusing more on profits, let them know that their activity is going to lead to negative outcomes for the client (Int4) *So that would allow that supervisor to go more public and it is still like that today* (Int6) *Because we said there are such externalities that any crisis will hit, they will be cross border* (Int6) *A largely conduct supervision or a largely conduct authority where the focus is more on conduct or market conduct aspects* (Int7)		
And that is modernizing is, that in itself takes time. It is hard to set up the technologies, it is hard to get people to use the technologies (Int3) *Another new department that was formed was about the information communication technology department* (Int13) *Data driven atomization* (Int14)	• Modernization • Technologies • Big data	**Information Technology**

Source: (Msweli and Ryneveldt, 2023)

5. Conclusions

Overall, the findings revealed that when it comes to the institutionalisation of the Twin Peaks Model, there must be due regard to employees’ buy-in. The findings further revealed that change management plays a key role in the institutionalisation of the Twin Peaks model. An interviewee elaborated that in order to get the right financial regulatory calibration, the change management spectrum must be right. This fact is reiterated in Zucker and Schilke’s 2019 work. One of the dominant themes emerging out of the data is communication. Not only communication between the regulators, but the right synergy must be attained and maintained across the institutional fields involved in the implementation of the Twin Peaks regulatory regime. The findings showed that there must be effective channels of communication between the frontline supervisors and the team that is supervised. In order to attain this open line of communication, an interviewee proposed an organogram structural change through a mapping process. According to another interviewee, change management must be people focussed, people must understand their purpose and role in the new structure and consequently they must accept the change and feel comfortable in their new roles.

It is apparent from the findings that the institutionalisation process of a Twin Peaks Model requires continuous assessments, in so far as it relates to resource utilization and how this utilization can be adapted to the changing world business environment. This implies that the appropriate resource allocation and utilization must be adapted in order for a regulator to fulfil its regulatory mandates in a continuum. This is congruent with the understanding that institutional change processes occurs over a length of time (Burns and Scapens, 2000). Human resource is a central theme in the data, a resource to which the necessary investments must be made while simultaneously creating a conducive environment for change and acceptance of new institutional structural modalities by institutional employees.

The findings also confirmed the existence of a relationship between the four institutional value moments - institution, production, territorialization and societal broad based value systems of accountability, excellence, integrity, open communication, respect, cooperation, trust, and reciprocity. The findings further confirmed that multiple societal level logics are imperative to inform an institutional working environment, and by so doing the data revealed that different logics are refracted in order for institutions to be compatible with an organisation’s value system from a developmental state context.

The findings confirmed that a Twin Peaks Model must be uniquely aligned in accordance with a country’s specific financial institutional environment, and that a one size fits all Twin Peaks Model is not conducive to attain a country’s financial stability objectives. The findings further confirmed that institutional logics and societal logics have to be compatible and aligned to the financial regulatory framework. This study confirms Yan et al.’s (2021) view that within an institutional field working environment, social activities are regulated by a dominant institutional order where its logics and associated practices are acceptable as the most appropriate solution. This is true for financial institutional fields, in that over the years the dominant institutional order were the financial institutional logics that took precedent over societal logics in South Africa. The findings reported in this paper have confirmed that over the years, the financial regulatory environment was predominantly focused on financial institutions as opposed to the financial interest of financial consumers. This translates into the dominance of commercial logics as opposed to societal logics. The commercial logic as pointed out by Fitzgerald and Shepperd (2018), focus on the main differential broad-based value systems between financial and societal logics.

6. Limitations and avenues for further research

This research is limited to institutional logic assumptions and rule patterns. Although reference were made to the United Kingdom's, Australia, New Zealand, and Belgium's Twin Peaks Models, the study reported in this paper did not examine and compare how the different Twin Peak models were institutionalised in different countries. No input has been gained from other financial sector organisational players, like financial companies and financial consumers. The inclusion of additional organisational players can provide further insights on the institutionalisation process of the financial regulatory institutions. This in particular can have different outcomes as to how and to what extent institutional and societal logics refract and converge to legitimise the creation of a new institution in a developmental state context.

Further research is encouraged on how institutional logics and societal logics refract and converge in financial institutions, as this can contribute to how best financial companies can refract and converge institutional and societal logics in their sphere of influence. At the same time research can also be conducted to understand how financial institutions had to adapt their business models in order to be compliant with the Twin Peaks Model legislations, rules and principles. To understand the role of institutional logics in newly formed institutions, further research can be conducted on old institutions institutional logics and how they are adapted and adopted into the new institutions. This is of particular interest in understanding how rules and principles change and are replaced to be more relevant to society's needs.

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