

THE UNIVERSITY OF THE WESTERN CAPE

FACULTY OF LAW

**DEVELOPING AN INDEPENDENT REGULATORY
FRAMEWORK FOR THE FINANCIAL SECTOR IN
MALAWI**

LLM MODE I

A Research Paper submitted in partial fulfilment of the
requirements for the degree of *Magister Legum*,
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STUDENT : Sunduzwayo Madise

STUDENT N° : 3082013

DEGREE : LL.M (International Trade, Investment and Business Law)

SUPERVISORS:

: Prof. Riekie Wandrag (University of the Western Cape)

: Prof. Kenneth Mwenda (Senior Counsel, Legal Vice-Presidency of the
World Bank & Extraordinary Professor of Law, University of Pretoria)

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DECLARATION

I, **Sunduzwayo Madise**, declare that **Developing an Independent Regulatory Framework for the Financial Sector in Malawi** is my own work, that it has not been submitted before for any degree or examination in any other university, and that all the sources I have used or quoted have been indicated and acknowledged as complete references.



Signed: _____

Sunduzwayo Madise
13 May 2011

UNIVERSITY *of the*
WESTERN CAPE

Signed: _____

Prof. Riekie Wandrag

13 May 2011

Supervisor

DEDICATION

This work is dedicated to the following for their unique contribution to my life :

- My wife Rhosa, for her love, support and never-failing belief in me.
- My late father G P S Madise, for being an ever living inspiration.
- My mother Nyokase Madise, for never losing faith in me.
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KEYWORDS

Central bank independence

Financial Sector

Financial Service Law

Financial Service Regulation

Regulatory Framework

Regulatory Independence

Reserve Bank of Malaŵi (RBM)

Malaŵi

Unified Regulator



ACRONYMS AND ABBREVIATIONS USED

BA2009 – Banking Act 2009 (Malaŵi).

BFSA – Banking and Financial Services Act 1994 (Zambia).

BSA – Building Society Act 1964 (Chapter 32:01 of the Laws of Malaŵi).

Chap – Chapter (under the Laws of Malaŵi).

CMDA – Capital Markets Development Act (Malaŵi) repealed by Securities Act 2010.

CRBA – Credit Reference Bureau Act 2010 (Malaŵi).

COMESA - Common Market for Eastern and Southern Africa.

EGX – Egypt Stock Exchange.

EU – European Union.

FSA – Financial Services Authority (United Kingdom).

FSAC – Financial Services Appeal Committee (under the FSAM).

FSAM – Financial Services Act 2010 (Malaŵi).

FSL – Financial Service Law (collective of Malaŵian laws on the financial sector).

GDP– Gross Domestic Product.

G.N. – Government Notice (of Malaŵi).

HDI – Human Development Index (of the United Nations).

IA2009 – Insurance Act 2009 (Malaŵi).

ILJ – *Industrial law Journal* (South Africa).

IMF – International Monetary Fund.

JEL – *Journal of Economic Literature* (United States of America).

JSE – Johannesburg Stock Exchange (South Africa).

LDC – Least Developed Country.

LLDC– Land-Locked Least Developing Country.

LOLR – Lender of Last Resort.

LSE – Lusaka Stock Exchange (Zambia).

MALSWITCH – Malaŵi Switch Centre.

MLJ – *Malawi Law Journal* (Malaŵi).

MSE – Malaŵi Stock Exchange.

MFA2010 – Microfinance Act 2010 (Malaŵi).

No – Number.

NSE – Nairobi Stock Exchange (Kenya).

NSX – Namibia Stock Exchange.

p – Page.

PLC – Public Limited Company (trading on the MSE).

RBM – Reserve Bank of Malaŵi.

RBMA – Reserve Bank of Malaŵi Act 1989 (Malaŵi).

RSA – Republic of South Africa.

s – Section.

ss – Sections.

SA2010 – Securities Act 2010 (Malaŵi).

SADC – Southern African Development Community.

UK – United Kingdom.

UN – United Nations.

US – United States of America and **USD** – United States Dollar.

Vol – Volume.

And where referred :

“Government” refers to the Malaŵi Government.

“Constitution” refers to the Republic of Malaŵi Constitution 1994.

“Companies Act” refers to the Companies Act 1984 (Malaŵi).

“Financial Services Act” refers to Financial Services Act 2010 (Malaŵi).

“Act” refers to an Act of Parliament in Malaŵi; same meaning as legislation.

The term “law” is also used to refer to collections of laws/Acts.

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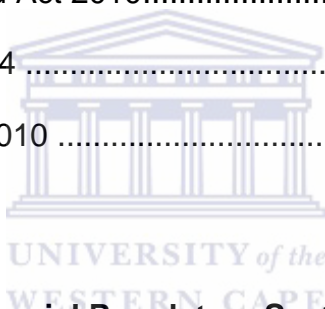
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CHAPTER ONE

1. Introduction

1.1 Historical context and state of affairs

Malaŵi¹ gained independence from Britain in 1964 and became a Republic in 1966.² As a Republic, it delinked its economy from Britain and set up its own financial system, with the Malaŵi Kwacha as the new currency. The Kwacha was however still fixed to the British Sterling Pound, up to 1973.³ However, to date, 47 years after political independence and 45 years after financial independence, Malaŵi remains one of the Least Developing Countries⁴ and poverty remains a key challenge.⁵ Progress has however, been made in tackling poverty and other social challenges.⁶

Malaŵi's developing financial sector remains small and dominated by banking.⁷ Capital markets are not fully developed and activity on the Malaŵi Stock Exchange (MSE)⁸ remains very limited.⁹ The central bank, Reserve Bank of Malaŵi (RBM) is the regulator¹⁰ of the financial services sector and its governor is the statutory registrar of the financial service sector.¹¹ In an attempt to enhance the financial sector's supervisory framework, Malaŵi has recently introduced amendments to the existing law, enacted new laws and drafted new bills to cover the financial services sector in Malaŵi.¹² However all the amendments, new acts and proposed bills whilst

¹ Literary "flames of fire"- although the country's name is commonly written as "Malawi", the proper name is "Malaŵi". In this work the proper way of writing the name is adopted notwithstanding its otherwise usage, the exception being for material quoted from other sources and names of journals.

² 'Malawi' Department of Tourism available at <http://www.visitmalawi.mw/About%20Malawi/aboutmalawi.htm> (accessed 1 January 2011).

³ Ndaferankhande MD & Ndhlovu TM 'Inflationary experiences in Malawi: An investigation of the underlying determinants' (2006) 14 available at www.csae.ox.ac.uk/conferences/2006-EOI.../Ndaferankhande.pdf (accessed 1 January 2011).

⁴ Malaŵi is also a Land-Locked Least Developing Country (LLDC) 'UN-OHRLLS: Least Developed Countries' available at <http://www.unohrlls.org/en/ldc/related/62/> (accessed 22 August 2010).

⁵ 'African Economic Outlook : Malawi' available at <http://www.africaneconomicoutlook.org/en/countries/southern-africa/malawi/> (accessed 17 September 2010). (hereafter African Economic Outlook : Malawi (2010)).

⁶ African Economic Outlook : Malawi (2010).

⁷ '2010 Index of Economic Freedom' *The Wall Street Journal*, available at <http://www.heritage.org/index/country/malawi> (accessed 17 September 2010) (hereafter Index of Economic Freedom (2010)).

⁸ The only stock exchange.

⁹ Index of Economic Freedom (2010).

¹⁰ Section 3 The Reserve Bank of Malaŵi (RBM) Act Chapter 44:02 of Laws of Malaŵi.

¹¹ Section 8(2) Financial Services Act 2010.

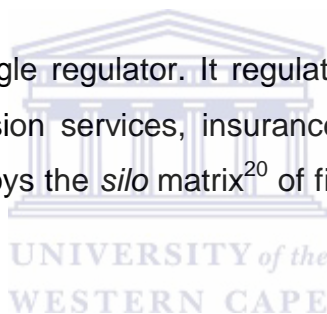
¹² Index of Economic Freedom (2010).

providing for a comprehensive regulatory framework still concentrates all regulatory and supervisory authority within the RBM.¹³

1.2 Background

Over the years financial regulation and supervision in many countries have been organized around specialist agencies with distinct responsibilities for banking, securities and insurance sectors, however, there has in recent years, been a trend towards restructuring financial supervision and in particular towards unified regulatory agencies.¹⁴ Countries have gradually moved towards some form of unified regulation based on a twin peaks or multiple peaks model or even on a single peak model.¹⁵ The most notable single peak case is the Financial Services Authority¹⁶ (FSA) of the UK.¹⁷ A regulator may be partially unified or fully unified.¹⁸ The term single regulator commonly refers to a fully unified regulator.¹⁹

In Malaŵi the RBM is the single regulator. It regulates and supervises all financial sectors including banks, pension services, insurance companies, discount houses and the MSE. The RBM employs the *silo* matrix²⁰ of financial services regulation and supervision.



Institutional aspects of financial regulation and supervision are receiving great attention around the world.²¹ Protecting investors to help build confidence in the market, ensuring that markets are fair, efficient and transparent, reducing systemic risk (contagion), protection against malpractices such as money laundering, insider

¹³ The Reserve Bank is the regulator in all the new law and proposed laws - see Mhango P 'Design Issues for Pension Legislation in Malawi: Presentation to the IOPS Workshop' (2008) available at <http://www.oecd.org/dataoecd/20/14/40104478.pdf> (accessed 17 September 2010).

¹⁴ Mwenda KK 'Legal Aspects of Unified Financial Services Supervision in Germany' (2003) *German Law Journal*, Vol 04 No 10 (hereafter Mwenda KK (2003)) 1009 but see Mwenda KK *Legal Aspects of Financial Services Regulation and the Concept of a Unified Regulator* (2006) (hereafter Mwenda KK (2006)) 3 where he says a longer track record of experience with unified regulators is still needed before coming up with firm conclusions.

¹⁵ See generally Wymeersch E 'The Structure of Financial Supervision in Europe About Single, Twin Peaks and Multiple Financial Supervisors' (2007) *European Business Organization Law Review* 8: 237-306, (hereafter Wymeersch E (2007)).

¹⁶ Hereafter in the text referred to as FSA.

¹⁷ See generally Briault C 'The Rationale for a Single National Regulator' (1999) *FSA Occasional Paper*.

¹⁸ Mwenda KK (2006) 37 but see generally Chapter 3 of the book.

¹⁹ Mwenda KK (2006) 10.

²⁰ See Mwenda KK (2006) 6.

²¹ Demaestri E & Sorrouille D 'Integrated Financial Supervision : Experiences in Selected Countries' (2003) Inter-American Development Bank (hereafter Demaestri E & Sorrouille D (2003)) at foreword.

trading etc. and maintaining consumer confidence in the financial system comprise the broad objectives of regulation.²² A key objective of regulations is to redress information imbalances that sometimes exist between financial services businesses in favour of the consumer.²³ Control of market abuses boosts consumer confidence.²⁴ However, before designing any framework, the size and structure of the industry and the role of the regulator need to be understood.²⁵ It is also important to take into consideration the economic, political, legal²⁶ and historic considerations when designing a regulatory framework.²⁷

Malaŵi is a Constitutional supremacy²⁸ with three arms of government *viz*, executive, legislature and judiciary.²⁹ The RBM is a creature of statute³⁰ and a constitutional body.³¹ Section 3 of the RBM Act 1989 states that among the principal objectives of the RBM shall be to supervise banks and other financial institutions.

The RBM has the statutory authority to supervise banks and other financial institutions. The RBM Act defines financial institution 'as any person, other than a bank, registered as a financial institution under the Banking Act' and other financial institutions 'includes financial institutions and pensions, assurance and insurance institutions'.³² The Financial Services Act 2010³³ broadens the definition of a financial institution to include a bank, and institutions defined as such in the Securities Act 2010,³⁴ Insurance Act 2009,³⁵ Microfinance Act 2010,³⁶ Financial Cooperatives Act [sic],³⁷ Pension Act [sic],³⁸ Credit Reference Bureau

²² Mwenda KK (2006) 3.

²³ Mwenda KK (2006) 4.

²⁴ Mwenda KK (2006) 4.

²⁵ Mwenda KK (2006) 6.

²⁶ i.e. Constitution and whether the country is a Common law or Civil law or both (as in the case of Cameroun).

²⁷ Mwenda KK (2006) 48.

²⁸ Sections 4,5, 199 The Constitution of the Republic of Malaŵi 1994 (hereafter The Constitution).

²⁹ Sections 7, 8 9 The Constitution of the Republic of Malaŵi 1994.

³⁰ The Reserve Bank of Malaŵi (RBM) Act 1989 (hereafter RBM Act or RBMA)

³¹ Section 185(1) of the Republic of Malaŵi Constitution states 'There shall be established by an Act of Parliament a central bank of the Republic, known as the Reserve Bank of Malaŵi which shall serve as the State's principal instrument for the control of money supply, currency and the institutions of finance and shall serve generally in accordance with the normal functions of a central bank'.

³² Section 2 RBM Act.

³³ Hereafter referred in the text as Financial Services Act or FSAM.

³⁴ Hereafter referred in the text as Securities Act or SA2010.

³⁵ Hereafter referred in the text as Insurance Act or IA2009.

³⁶ Hereafter referred in the text as Microfinance Act or MFA2010.

³⁷ Although it is stated as an "Act" in the Financial Services Act, the Financial Cooperatives Bill is yet to be enacted according to law.

Act 2010³⁹ and the Building Society Act 1964⁴⁰ This definition basically includes any institution⁴¹ dealing in financial or financial-like services in Malaŵi.

The RBM exercises its regulatory and supervisory authority under the following legislation:

- (a) The Reserve Bank of Malaŵi Act⁴²
- (b) The Banking Act 2009⁴³
- (c) The Securities Act⁴⁴
- (d) The Exchange Control Act⁴⁵
- (e) Microfinance Act⁴⁶
- (f) Insurance Act⁴⁷
- (g) Credit Reference Bureau Act⁴⁸
- (h) Building Society Act⁴⁹
- (i) Financial Services Act⁵⁰

The following Bills have been laid before Parliament and passed⁵¹ and are likely to become part of the financial services law in the near future:

- (a) Pension Bill⁵²

³⁸ Although it is stated as an “Act” in the Financial Services Act, the Pensions Bill is yet to be enacted according to law.

³⁹ Hereafter referred in the text as Building Society Act or BSA.

⁴⁰ Section 2 Financial Services Act.

⁴¹ Both juristic and natural persons.

⁴² a text of the Act available at <http://www.rbm.mw/documents/legislation/rbmact.pdf> (accessed 1 February 2011).

⁴³ Hereafter referred as the Banking Act or BA2009. It replaced the Banking Act, 1989 (hereafter the repealed Banking Act. However although s 1 states that the Act shall be cited as the Banking Act, 2009, it is Act No 10 of 2010. The Financial Services Act in s 2 refers to it as the Banking Act 2010[sic]. Text available at <http://www.rbm.mw/documents/legislation/Banking%20Act%202010.pdf> (accessed 1 February 2011).

⁴⁴ Which has just replaced the Capital Market Development Act, chap 46 :06 of the Laws of Malaŵi. The repealed Act can is still available at http://www.rbm.mw/general_info/docs/CAPITAL%20MARKET%20DEVELOPMENT%20ACT.pdf (accessed 1 February 2011).

⁴⁵ Chapter 45 :01 of the Laws of Malaŵi available at <http://www.rbm.mw/documents/legislation/EXCHANGE%20CONTROL%20ACT.pdf> (accessed 1 February 2011) – a new Bill has been laid before Parliament to replace this Act.

⁴⁶ A new law.

⁴⁷ Which has just replaced the Insurance Act; chap 47:01. However although s 1 states that the Act shall be cited as the Insurance Act, 2009, it is Act No 9 of 2010. The Financial Services Act in s 2 refers to it as the Insurance Act 2010.

⁴⁸ A new law.

⁴⁹ Chapter 32:01 of the Laws of Malaŵi.

⁵⁰ A new law, being the umbrella Act of all financial service laws, text available at <http://www.rbm.mw/documents/basu/FINANCIAL%20SERVICES%202010.pdf> (accessed 1 February 2011).

⁵¹ Awaiting Presidential Assent and publication in the Gazette – see s 49 Constitution.

(b) Financial Cooperatives Bill⁵³

(c) Reserve Bank Amendment Bill⁵⁴

The Financial Services Act defines all the above Acts and Bills except the Exchange Control Act⁵⁵ (and the Amendment Bill) as forming the “financial services law”.⁵⁶

The governor and deputy governor of the RBM are appointed exclusively by the President of Malaŵi.⁵⁷ The board of directors of the RBM is also appointed exclusively by the President and comprises the governor, deputy governor, and five other directors who may include⁵⁸ secretary to the treasury, secretary for economic planning and development and accountant general.⁵⁹ The governor (or deputy governor in the governor’s absence) chairs the board of directors.⁶⁰ The RBM is thus *de facto* and *de jure* under the executive.

Malaŵi has been a one-party state for most of its existence.⁶¹ Through a referendum in 1993, Malaŵians voted for a multiparty system and in 1994 Malaŵi had multiparty elections with a new Constitution⁶² in place and presidential term that runs for five years with a maximum of two terms.⁶³ Malaŵi has had three Presidents since it became independent; Dr. Kamuzu Banda,⁶⁴ Dr. Bakili Muluzi⁶⁵ and Professor Bingu wa Mutharika.⁶⁶

⁵² A new law to regulate the Pension Industry. The law will make pension (contributions) compulsory.

⁵³ To replace the Savings and Credit Cooperatives Act.

⁵⁴ Awaiting Presidential assent which is by law required in Malaŵi before a Bill which has been laid down, debated and passed by Parliament can become law – s 73 The Constitution.

⁵⁵ This Act controls operation of Forex Bureaux which were established after subsidiary legislation - Exchange Control (Forex Bureaux and Foreign Exchange Fixing Sessions) Regulation of 1994

⁵⁶ Hereafter abbreviated to FSL for both the singular and plural forms s 2 Financial Services Act. The author is of the view that the omission of the Exchange Control Act is by error and not design.

⁵⁷ Section 12 RBM Act; s 6 of the RBM Amendment Bills proposed the appointment of not more than three deputy governors (up from the present one) and not more than seven directors – Sonani B ‘Cut President’s powers over RBM – MPS’ *The Nation* 10 December 2010 available at http://www.nationmw.net/index.php?option=com_content&view=article&id=10828:cut-presidents-powers-over-rbmmps&catid=11:business-news&Itemid=4 (accessed 13 December 2010).

⁵⁸ *And usually does!*

⁵⁹ Section 6 RBM Act.

⁶⁰ Section 11 RBM Act.

⁶¹ From 1966 when it became a Republic to 1994. There were minority parties when Malaŵi became Independent in 1964 following the general elections of 1961 but this changed after 1966 and following the (in)famous “cabinet crisis” when Dr. Banda reinforced his reigns on power.

⁶² Although the Constitution is designated as a 1994 legislation, the 1994 Constitution was interim and was only made sacrosanct in 1995, the notable removal from it being the senate.

⁶³ Section 83 The Constitution.

⁶⁴ 1964-1994.

⁶⁵ 1994-2004.

⁶⁶ 2004-present (constitutionally up to 2014).

The RBM has had eleven governors since its inception in 1965.⁶⁷ The average term of a governor since independence is approximately 4.7 years, almost equal to the 5-year post-one-party political cycle.⁶⁸ The longest serving governor of the RBM was Mr. John Tembo⁶⁹ who served during the period of one-party rule.⁷⁰ The shortest serving is A.G. Perrin who was the first governor and only served a year.⁷¹ An examination of the rate of turnover of governors after the advent of multiparty democracy⁷² indicates a drop to 4.5 years on average.⁷³ The most interesting pattern is that there is a change in the governor within a year after every general election in the multiparty era.⁷⁴ For example, Dr. Mathews Chikaonda replaced Mr. Francis Perekamoyo as governor in 1995 soon after the 1994 elections.⁷⁵ Dr. Chikaonda was replaced by Dr. Elias Ngalande in 2000 after the 1999 elections whilst Dr. Ngalande himself was replaced by Mr. Victor Mbewe in 2005 after the 2004 elections.⁷⁶ Mr. Mbewe was replaced by the current governor, Dr. Perks Ligoya, months after the May 2009 general elections.⁷⁷

The influence of the executive arm (especially the presidency) on the RBM through the appointment of its governor and board is therefore self-evident, especially in the post-one-party era where each presidential term seems to coincide with a new governor of the RBM. It can therefore be inferred that, currently the job of governor of the RBM does not provide much security of tenure. It would seem that the RBM may therefore not pass an objective test of independence and this also provides an even greater reason for the development of a new order of financial service regulation in Malaŵi.

⁶⁷ See Kalilombe L *Central Bank Governance, Accountability and Independence: The Case of Reserve Bank of Malawi* (unpublished MA thesis, University of Kwazulu-Natal, 2008) (hereafter Kalilombe (2008)) 40 but add Dr. Perks Ligoya, the current Governor appointed in 2009.

⁶⁸ Kalilombe (2008) 40.

⁶⁹ (1971-1984) Famous Politician and now Leader of Opposition (one of the oldest serving Members of Parliament). John Tembo is now President of the Malaŵi Congress Party, the party that Dr. Kamuzu Banda led. But Kalilombe (2008) 20 cautions that 'care should be taken in interpreting these values because low turnover sometimes may mean lower independence of the Central Bank. A subservient governor may stay in the seat for a longer time if he does what the politicians want him to do'.. It is submitted this may have been the case in the John Tembo governorship.

⁷⁰ Kalilombe (2008) 40.

⁷¹ Kalilombe (2008) 40.

⁷² Referendum was in 1993 and General Elections were held in 1994.

⁷³ Kalilombe (2008) 40.

⁷⁴ Kalilombe (2008) 41.

⁷⁵ Kalilombe (2008) 41.

⁷⁶ Kalilombe (2008) 41.

⁷⁷ In September 2009 – Gondwe G 'Reserve Bank of Malawi appoints new governor' available at <http://www.bizcommunity.com/Article/415/87/40038.html> (accessed 9 October 2010).

Malaŵi is however not unique in having a central bank as regulator and supervisor of the financial sector. The Netherlands, Antilles, Singapore and Uruguay are some of the countries with the peculiar regulatory system where the central bank and not a separate agency regulate securities firms, insurance companies as well as banks.⁷⁸

The financial sector of Malaŵi is still at a rudimentary stage with low public confidence as reflected in the illiquidity of the MSE.⁷⁹ The MSE has been in existence since 1994 but started equity trading in November 1996 when it had its first listing.⁸⁰ Prior to that, the major activities undertaken were the provision of a facility for secondary market trading in Government of Malaŵi bonds namely, Treasury Bills and Local Registered Stocks.⁸¹ The Securities Act provides for the main regulatory framework for securities in Malaŵi. The MSE operates under the Securities Act. Malaŵi is also part of the Southern African Development Community (SADC)⁸² and Common Market for Eastern and Southern Africa (COMESA).⁸³ Most of the members of SADC⁸⁴ and COMESA⁸⁵ have illiquid stock markets too.⁸⁶

1.3 Problem statement

In examining the legal aspects of unified financial services supervision in Malaŵi, focus will be on the independence and accountability of the unified regulator. The study seeks to find out whether or not the central bank of Malaŵi, as a unified regulator, has adequate autonomy and efficacy under the legal framework for financial services supervision to carry out efficiently the unified supervision of financial services. Closely related to this, the study examines the issue of whether the unified regulator in Malaŵi does enjoy in practice adequate autonomy, as

⁷⁸ Mwenda KK (2006) 53.

⁷⁹ For example the MSE registered no trading in the week 6-10 September, 2010 (11 September was a holiday) see – Chiyembekeza C 'Stock market closes 4-day trading week flat' *The Nation* 13 September 2010 available at http://www.nationmw.net/index.php?option=com_content&view=article&id=5770:stock-market-closes-4-day-trading-week-flat&catid=11:business-news&Itemid=4 (accessed 17 September 2010).

⁸⁰ 'Malawi Stock Exchange – Company Profile' available at <http://www.mse.co.mw/prof.html> (accessed 18 September 2010) (hereafter Malawi Stock Exchange – Company Profile (2010)).

⁸¹ Malawi Stock Exchange – Company Profile (2010).

⁸² Southern Africa Development Community available at <http://www.sadc.int/> (accessed 17 September 2010).

⁸³ The Common Market for Eastern and Southern Africa available at <http://www.comesa.int/> (accessed 17 September 2010).

⁸⁴ Except the JSE in South Africa which is liquid by African standards.

⁸⁵ Except for NSE in Kenya and EGX in Egypt.

⁸⁶ See Marone H *Small African Stock Markets—The Case of the Lusaka Stock Exchange* (2003) (hereafter Marone H (2003)) 11 and see generally Mwenda KK 'Securities Regulation And Emerging Markets: Legal And Institutional Issues For Southern And Eastern Africa' (2000) *Murdoch University Electronic Journal of Law*, Vol 7, No 1 (hereafter Mwenda KK (2000)).

provided for under the law, or whether it is constrained in its functions by interferences from other regulatory bodies or political institutions and persons.

1.4 Objectives

The overall objective of the proposed research is to propose a new regulatory and supervisory framework for the financial sector in Malaŵi.

The specific objectives of the research are to:

- a) Critically analyse the structure of the current unified regulatory and supervisory system under the Reserve Bank of Malaŵi (Malaŵi's central bank) by examining the legal, structural and institutional framework under which the current structure operates.
- b) Critically analyse the concept of 'an independent financial service regulator' detached from the central bank as well as the notion of central bank independence.
- c) Examine the efficacy of the legislative, regulatory and institutional framework for unified financial services supervision with a view to making policy recommendations for possible law reform.

1.5 Research hypothesis

The research is premised on the assumption that the current financial service regulation and supervision in Malaŵi is not independent, efficient and effective. The financial sector in Malaŵi has developed since 1964 when the RBM was established⁸⁷ but the legislature has simply piled on the RBM with (more) regulatory and supervisory powers of all new entrants in the financial service sector. The assumption is that if financial service regulation were to be detached from the RBM and placed in an independent regulatory body, this would leave the RBM to monitor any crisis that may develop in the financial sector from 'arms-length' without it being directly *a priori* involved and thereby losing its high ground. The RBM would then concentrate on its role of 'lender of last resort'. Further, freeing the RBM from the clutches of the executive would ensure separation (but not necessarily disconnect) between fiscal and monetary policy and ensure that the RBM concentrates on monetary policy.⁸⁸

⁸⁷ But it started operating in 1965.

⁸⁸ For example Malaŵi's pursuit of a *de facto* fixed (pegged) exchange rate policy from 2006 to late 2009 made it difficult for the Reserve Bank of Malaŵi (RBM) to clear the foreign exchange market

1.6 Scope

It is admitted that the subject area under consideration is very extensive. Therefore, a limited but refined scope is proposed. The concept of central bank independence will mostly be dealt within the context of an effective framework that would be of beneficial interest to Malaŵi as a country. The thesis assumes that since Malaŵi already does have a unified regulator (the RBM), there will be no need to go into an elaborate discussion of different regulatory systems.

1.7 Significance of the research

As stated above, Malaŵi is a LLDC and with poverty being a key challenge although progress has been made resulting in increased household food security complimenting strong macroeconomic performance. The financial sector is still rudimentary and dominated by banking with capital markets which are not fully developed resulting in limited activity on the MSE. The Legislature has enacted new laws and amendments to the laws and some bills are pending enactment in a bid to improve financial sector regulation and supervision. However this notwithstanding, all regulatory and supervisory authority and power is still concentrated within the RBM.

Malaŵi would therefore benefit from an effective and independent financial regulatory system to attract investors, boost consumer confidence and explore other avenues such as cross-border listings which have the potential of leading to economic development and thereby reducing poverty. Such a system would also ensure that economic growth is sustained. Furthermore an independent central bank would free the RBM from the effects of politics associated with elections. This research would therefore be of use to the Government, the RBM, other financial institutions as well as to the academia. Even if the proposed framework were not to be adopted wholesome, it is hoped this research would prove a valuable addition and increase the wealth of knowledge on effective and efficient financial sector regulation in Malaŵi as well as independence of the central bank. It is also hoped that this research can provide a strong ground and basis for further research in this field.

at the official exchange rate, causing import demand backlogs and serious forex shortages. Foreign reserves became precariously low in 2009 falling to 0.6 months of imports – see African Economic Outlook : Malawi (2010).

1.8 Research methodology

There is a wealth of literature available on central bank independence and financial service regulation. Fortunately, literature from Malaŵi, Africa and with an African perspective is now available.⁸⁹ In this work, a comparative analysis of the financial regulatory models in the UK and Zambia is done. The motivation for choosing these jurisdictions is that Malaŵi's economy was once tied to the UK economy by virtue of colonialism and the influence of the UK's financial system on Malaŵi still persists, albeit in a diminished manner. Furthermore Malaŵi is a common law jurisdiction and some English statutes are still law in Malaŵi.⁹⁰ As for Zambia, it too as a former British colony inherited the common law. The two countries also share common languages and ethnic groupings as well as a connected history⁹¹ They also have the same local name for their currency, the Kwacha. Economic and political conditions in Zambia are comparable to Malaŵi.⁹²

The research conducts a critical analysis of the situation within which the RBM operates as a financial service regulator as well as a central bank (both from the legal and practical point) and also critically engages with the literature in order to develop a robust framework for Malaŵi.

This work is mainly based on research work carried out at the libraries of the University of the Western Cape and University of Malaŵi and relevant information available on the internet. Apart from this, visits were made and books, documents and pieces of legislation collected, sourced or procured from the MSE, RBM, Malaŵi Stock Brokers Limited and Government Printer (Malaŵi). This research further benefitted from course material made available as part of the course of the International Finance Law module of the LLM programme.

⁸⁹ Dr. Zolomphi Nkowane has written on the financial service in Malaŵi whilst Professor Kenneth Mwenda, amongst others, has written extensively on and about Africa and (developing) emerging markets and especially on Zambia: see the Bibliography.

⁹⁰ The so-called received law. English judgements are constantly relied upon the Malaŵian Courts.

⁹¹ Federation of Rhodesia and Nyasaland. Malaŵi still has provisions that allow enforcement of judgements from Zambia (albeit referred to as Northern Rhodesia) although there is no reported case of any such provision being utilised.

⁹² Both are LDCs, both became multi-party states in the early.

1.9 Outline

Chapter One introduces the thesis, discusses the background of the study and the problem that the thesis aims to address. It outlines the research objectives and provides an outline and overview of how the thesis is to be presented.

Chapter Two conducts a literature review on independent financial regulation as well as central bank independence and emerging trends. A comparative study of countries in a similar position to Malaŵi (economically and politically) such as Zambia and how financial service regulation has evolved in that jurisdiction is also conducted. The UK's Financial Services Agency (FSA) serves as the model comparative regulator.

Chapter Three critically discusses the existing regulatory framework of the financial sector in Malaŵi both from a legal, practical and political perspective and its developments since independence to the present. It analyses the various legal instruments and the political economy and their impact on financial service regulation.

Chapter Four contains the proposed framework for a new financial service regulatory system in Malaŵi. The framework is developed from emerging trends from a global and comparative basis as applicable to Malaŵi and in view of the current situation of financial service regulation in Malaŵi. The framework developed in this Chapter draws a lot of its strength from Chapters Two and Three.

Chapter Five contains the conclusions and recommendations arising out of the study including potential areas of future research.

CHAPTER TWO

2. A Sound and Independent Financial Regulatory Framework

2.1 Overview and rationale for regulation

Theory suggests that the primary role of financial institutions and capital markets is to facilitate the allocation of resources in an uncertain environment across space and time.⁹³ Therefore regulation of the financial sector has a crucial role to play, especially in the development of third world countries, most of whom have enormous wealth disparities between sections of their populace. The term regulation refers to a set of binding rules issued by a private or public body.⁹⁴ For the financial services sector, these can generally be defined as those rules that are applied by all regulators in the sector in the fulfilment of their functions.⁹⁵ They include such prudential rules as those influencing the conditions of access to the market (intended to prevent the emergence of doubtful reputation entities with no implementation capacity for the intended operations) and those aimed at controlling the risk associated with financial activities, corporate governance and internal control systems, conduct-of business rules, and methods of supervision.⁹⁶ Prudential regulations establish the outside limits and constraints placed on financial institutions to ensure the safety and soundness of the financial system.⁹⁷

Because of the role that banks play in the financial system, prudential rules for banks are a cornerstone of the regulatory framework. A crucial aspect of prudential regulation regards the enforcement powers given to bank supervisors to intervene to prevent losses from magnifying and to effect timely resolutions of bank failures.⁹⁸ This entails a need to confer on bank supervisors the right to issue "cease and desist" orders, impose fines, appoint receivers, merge or liquidate banks, and generally play an active direct or indirect part in the management of ailing institutions.⁹⁹

⁹³ Marone H (2003) 3.

⁹⁴ Mwenda KK (2006) 5.

⁹⁵ Mwenda KK (2006) 5.

⁹⁶ Mwenda KK (2006) 5.

⁹⁷ Polizatto VP 'Prudential Regulation and Banking Supervision' in Vittas D (ed) *Financial Regulation* (1992) (hereafter Polizatto VP (1992)) 177.

⁹⁸ Vittas D in Vittas D (ed) *Financial Regulation* (1992) (hereafter Vittas D (1992)) 19.

⁹⁹ Vittas D (1992) 19.

Although most often the regulator is also the supervisor, the role of the regulator and that of the supervisor are somewhat different. A regulator is concerned mainly with preparing and issuing regulations and promoting a culture of compliance with these regulations while a supervisor may undertake on-site and off-site supervision of financial services business.¹⁰⁰ In most jurisdictions however, the powers to regulate and to supervise the activities of the financial services sector reside in the same institution.¹⁰¹ The regulatory framework of financial services often comprises primary regulation,¹⁰² secondary legislation¹⁰³ and guidance and (policy) directives and directions issued by the regulator.¹⁰⁴

Over the years financial regulation and supervision in many countries have been organized around specialist agencies with distinct responsibilities for banking, securities and insurance sectors, however, there has been a trend towards restructuring financial supervision in recent years, and in particular towards unified regulatory agencies—that is, agencies that supervise two or more of these areas.¹⁰⁵ The institutional aspects of financial regulation and supervision are receiving great attention around the world.¹⁰⁶ Even without a unified theory of financial service regulation, protecting investors (to help build confidence in the market), ensuring that markets are fair (efficient and transparent), reducing systemic risk (contagion), protection against malpractices (such as money laundering) and maintaining consumer confidence in the financial system comprise the broad objectives of regulation.¹⁰⁷ A key objective of regulation is to redress information imbalances that sometimes exist between financial services businesses in favour of the consumer.¹⁰⁸ Control of market abuses boosts consumer confidence in the financial services sector.¹⁰⁹ Broadly put therefore, Governments regulate the financial sector for two main reasons, the first being consumer protection (similar to the way they regulate public utilities and telecommunications to provide a framework of rules that can help

¹⁰⁰ Mwenda KK (2006) 5.

¹⁰¹ As in the UK, or Malaŵi (Part II of the Financial Services Act says the Registrar is to Regulate and Supervise Financial Institutions) – see Mwenda KK (2006) 5.

¹⁰² Normally Acts of Parliament.

¹⁰³ Normally Ministerial regulations issued pursuant to the Act of parliament (enabling statute)

¹⁰⁴ Mwenda KK (2006) 5.

¹⁰⁵ Mwenda 2003 at 1009-10, but see Mwenda KK (2006) 1 where he says a longer track record of experience with unified regulators is still needed before coming up with firm conclusions.

¹⁰⁶ Demaestri E & Sorrouille D 'Integrated Financial Supervision : Experiences in Selected Countries' (2003) Inter-American Development Bank (hereafter Demaestri E & Sorrouille D (2003)) at foreword.

¹⁰⁷ Mwenda KK (2006) 3.

¹⁰⁸ Mwenda KK (2006) 4.

¹⁰⁹ Mwenda KK (2006) 4.

prevent excess and failures of a market left entirely to its own whims and devices) and the second is to maintain financial stability, a clear public good that justifies a more elaborate framework of regulation and supervision.¹¹⁰

Regulators and supervisors in nations around the world are charged with managing the health of banks and other financial institutions and preserving the stability of the financial system.¹¹¹ Financial service supervision, in particular, is more rigorous and intensive than supervision in other regulated sectors.¹¹² Banking supervisors engage not only in off-site analysis of the bank's performance but also in intensive on-site inspections, and they intensify their monitoring and may intervene when banks fail to meet minimum requirements designed to ensure their financial soundness.¹¹³ Supervisors can even, in extreme cases, take ownership rights away from the owners of failed or failing institutions.¹¹⁴ A clear example is what happened in Malaŵi recently. The regulator was called upon to supervise the operation of a troubled bank, Finance Bank of Malaŵi in 2005 leading to its closure.¹¹⁵ The regulator ended up running the bank¹¹⁶ and later liquidating its assets,¹¹⁷ a process yet to be concluded. It may be said, during all this time, part of the regulator's time has been taken away from the supervision of other banks to concentrate on this troubled bank.

Banking regulation developed out of the concern of central banks to ensure financial stability.¹¹⁸ In many parts of the world, the central bank is responsible for regulating banks, while in others, it is a separate agency.¹¹⁹ In the non-banking financial sector, such as securities markets, insurance and pensions, regulation has usually been conducted either by a government ministry or by a specialist government agency.¹²⁰

¹¹⁰ Quintyn M & Taylor MW 'Should Financial Sector Regulators be Independent?' (2004) *IMF Economic Issues* No 32 (hereafter Quintyn & Taylor (2004)) available at <http://www.imf.org/external/pubs/ft/issues/issues32/#1> (accessed 14 March 2011) (note that article has no pages).

¹¹¹ Quintyn M & Taylor MW (2004).

¹¹² Quintyn M & Taylor MW (2004).

¹¹³ Quintyn M & Taylor MW (2004).

¹¹⁴ Quintyn M & Taylor MW (2004).

¹¹⁵ Phiri F 'Finance Bank closure : Precursor to Return of Forfeiture Act?' available at <http://groups.yahoo.com/group/MALAWIANA/message/3175> (accessed 17 September 2010).

¹¹⁶ Under statutory management as provided in the law (See s 68, Financial Services Act).

¹¹⁷ Voluntary liquidation, it must be said.

¹¹⁸ Quintyn M & Taylor MW (2004).

¹¹⁹ Quintyn M & Taylor MW (2004).

¹²⁰ Quintyn M & Taylor MW (2004).

Before designing any framework, the size and structure of the industry and the role of the regulator need to be understood.¹²¹ It is also important to take into consideration the economic, political, legal¹²² and historic considerations when designing a regulatory framework.¹²³ Recent research on the effectiveness of prudential regulation questions the unthinking transplantation of practices from rich countries into the very different political and institutional settings that prevail in most African countries.¹²⁴ Detailed examination of cross-country evidence points to the limited effectiveness and, in many respects, the counter-productivity, in developing countries of some standard regulatory and supervisory practices.¹²⁵ For example, the design of African stock markets, influenced by what was seen as best practice in advanced economies, may, through costs and prerequisites, have created barriers to listed equity finance for many African firms that could have obtained it if a more context-sensitive regulatory design had been chosen.¹²⁶

The regulatory framework is often comprised of a combination of two or more of the following: (a) primary legislation (b) secondary legislation (c) principles, rules etc issued by the regulator and (d) guidance or policy directives issued by the regulator.¹²⁷ The regulatory framework is country-specific.¹²⁸ But whatever the situation, to be effective and efficient, a regulator must be able to lay down rules or principles of conduct of financial services business, authorise their operation, lay rules of operation, supervise compliance, enforce¹²⁹ rules, investigate breaches and cooperate and exchange information with other regulators.¹³⁰

Whatever regulatory system is employed, the legal framework should clarify the roles and responsibilities of different agencies involved in financial supervision.¹³¹ The

¹²¹ Mwenda KK (2006) 6.

¹²² i.e. Constitution and whether the country is a Common law or Civil law or both (as in the case of Cameroun).

¹²³ Mwenda KK (2006) 6.

¹²⁴ Honohan P & Beck T *Making Finance Work for Africa* (2007) (hereafter Honohan P & Beck T (2007)) at 85.

¹²⁵ Honohan P & Beck T (2007) 85.

¹²⁶ Honohan P & Beck T (2007) 10.

¹²⁷ Mwenda KK (2006) 5 although in other jurisdictions legislation provides that guidelines are to be treated as law.

¹²⁸ Mwenda KK (2006) 6 & 11.

¹²⁹ Enforcement is a necessary product of the process of authorisation and supervision - Mwenda KK (2006) 16.

¹³⁰ Mwenda KK (2006) 7.

¹³¹ *Financial Sector Assessment* (2005) The World Bank & The IMF (hereafter *Financial Sector Assessment* (2005))102.

central bank laws, banking laws, and other laws governing financial sector supervision need to specify the relationships among the supervisory agency, any deposit insurance agency and other financial sector supervisors.¹³² In addition, the relationship with the ministry of finance needs to be clear and to provide sufficient operational autonomy to the supervisor.¹³³ If a country has put in place a unified financial supervisory agency, then this arrangement needs to be laid down in a law, and its autonomy and powers need to be explicit.¹³⁴ The legal and regulatory basis of financial supervision should also support the core components of all financial supervisory standards.¹³⁵ Those components consist of the following categories:

- Regulatory governance; which refers to the objectives, independence, enforcement, and other attributes that provide the capacity to formulate and to implement sound regulatory policies and practices.
- Regulatory practices; which refer to the practical application of laws, rules, and procedures.
- Prudential framework; which refers to internal controls and governance arrangements to ensure prudent management and operations by financial firms.
- Financial integrity and safety net arrangements; which refer to (a) the regulatory policies and instruments designed to promote fairness and integrity in the operations of financial institutions and markets and (b) the creation of safeguards for depositors, investors, and policyholders, particularly during times of financial distress and crisis.¹³⁶

2.2 Models of financial services regulation and supervision

The four common models of financial services regulation are; regulation by objectives, functional regulation, institutional or regulation by silos and a single (also called a unified) regulator.¹³⁷ The concept of single regulator is antithesis to institutional regulation but it is possible to have functional and institutional regulation in a joint matrix under a unified regulator.¹³⁸

¹³² *Financial Sector Assessment* (2005) 102.

¹³³ *Financial Sector Assessment* (2005) 102.

¹³⁴ *Financial Sector Assessment* (2005) 102.

¹³⁵ *Financial Sector Assessment* (2005) 102.

¹³⁶ *Financial Sector Assessment* (2005) 102.

¹³⁷ Mwenda KK (2006) 8.

¹³⁸ Mwenda KK (2006) 10.

Where the aim is to have regulation by objectives, the model seeks to achieve certain explicit objectives by giving responsibility for one or more of them to specific regulatory bodies that exist solely for that purpose, such as a central authority empowered to conduct prudential regulation, a central authority responsible for supervising and passing regulations for the conduct of business, a central bank responsible for monetary policy and a central authority responsible for regulating competition.¹³⁹ This regulation is of horizontal application, see fig 1 below:

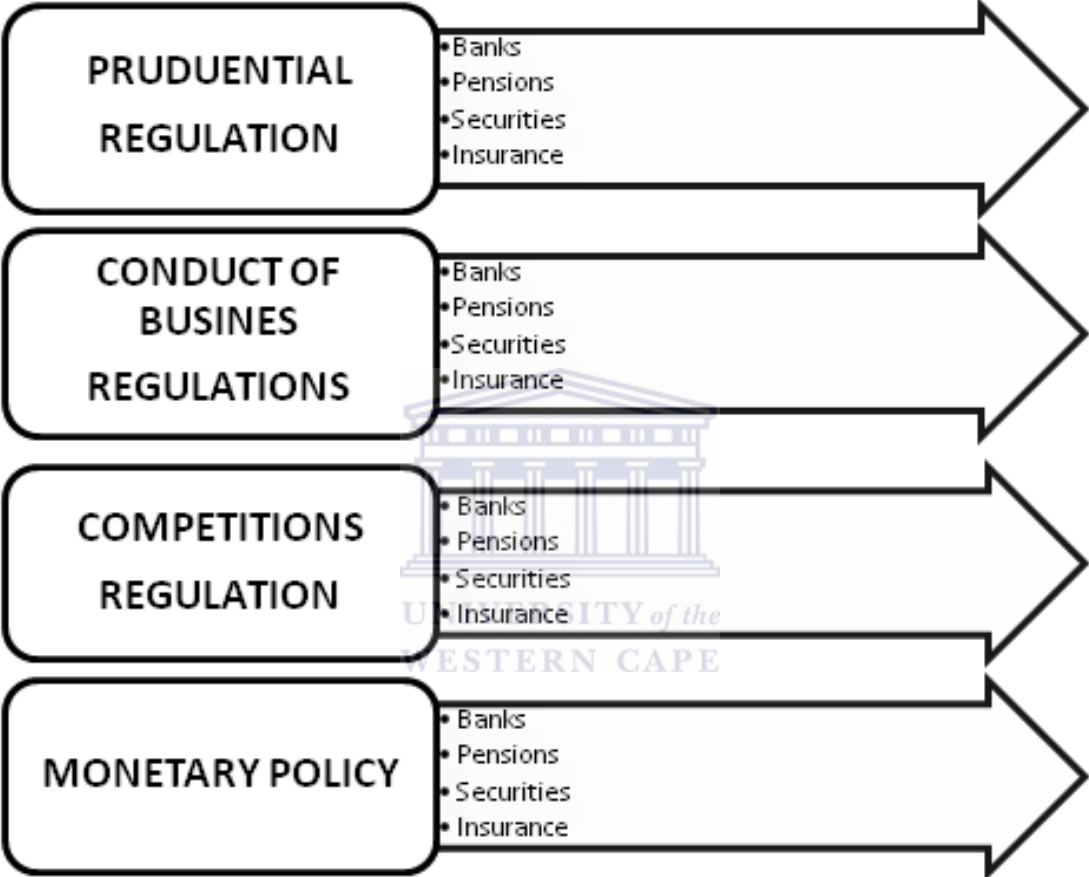


Fig 1. The regulation/rules have horizontal application for example Prudential regulations apply to banks pensions, securities insurance etc.

For functional regulation, the general view is that it is more important to regulate functions performed by financial services business than the types of business that undertake them, such as client assets and all conduct-of-business issues.¹⁴⁰ Functional regulation requires rules pertaining to function to be applied consistently to any business that discharges them, irrespective of the type of business.¹⁴¹ Therefore if an institution performs several financial functions, these functions will be regulated separately depending on their nature.

¹³⁹ Mwenda KK (2006) 8-9.
¹⁴⁰ Mwenda KK (2006) 9.
¹⁴¹ Mwenda KK (2006) 9.

Institutional regulation relates to the regulation of each single category of financial services by a different agency or division.¹⁴² Because of the vertical based manner in which this regulation model is structured, (vertical blocks like silos), institutional regulation is sometimes referred to as ‘regulation by silos’¹⁴³, see fig 2 below:

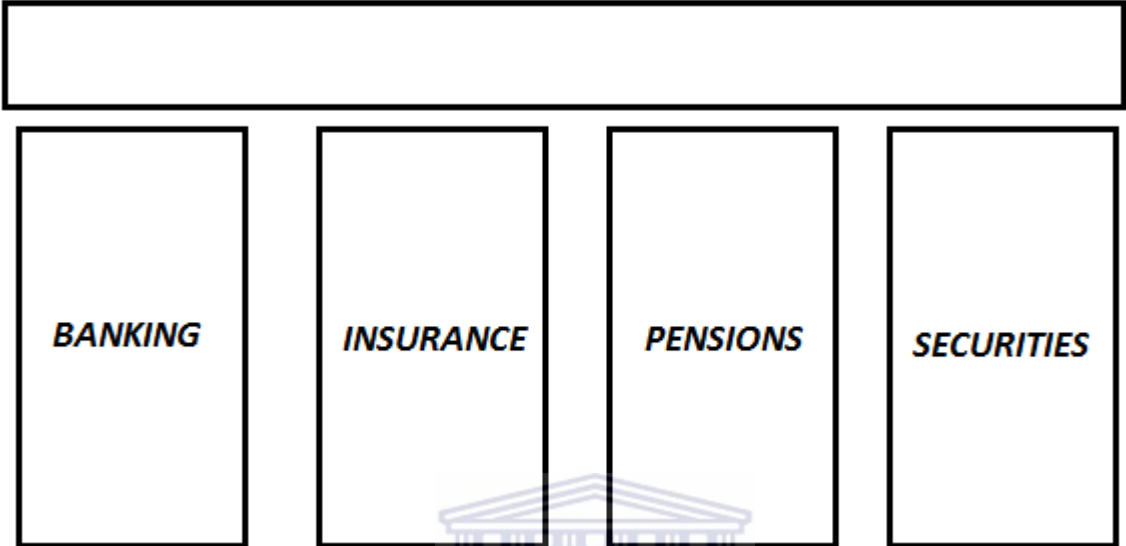


Fig 2. The Different blocks/silos may be different authorities, agencies or divisions and divisions may be under a common authority at the top (such as the Reserve Bank of Malaŵi). However each block/silo will concentrate only on the financial services under it.

Looking at functional and institutional regulation, similarities abound as even in institutional regulation it may be argued that it is function based (for example is it a banking function?). However the major difference may be that the former emphasises the setting up of departments in a supervisory agency that deal with non-sectoral functions as licensing, legal, accounting, enforcement etc. irrespective of type of business activity regulated whilst the latter encourages organisation into departments that deal separately with all aspects of specific types of business activities.¹⁴⁴

A unified regulator may be structured differently depending on jurisdictions. It may be a single central authority to regulate different institutions and functions and monitor fulfilment of regulatory objectives or it may deal solely with the securities and insurance industries or solely with the pension funds and insurance companies.¹⁴⁵

¹⁴² Mwenda KK (2006) 9-10.
¹⁴³ Mwenda KK (2006) 10.
¹⁴⁴ Mwenda KK (2006) 10.
¹⁴⁵ Mwenda KK (2006) 11.

2.3 Single, twin peaks and multiple financial regulators

In more developed financial markets such as Europe, three models are being practised; a three pillar model (banking, insurance and securities), a two pillar model (prudential versus conduct of business) and an integrated model (all types of supervision under one roof),¹⁴⁶ the last being the unified regulator. However the choice of regulator whether, partially unified (normally where only two segments of the financial sector are supervised by a single regulator or a combination of the financial services) or fully unified (normally supervising all business activities in the financial sector) are contingent¹⁴⁷ upon conditions obtaining in a country.¹⁴⁸ As already stated, these may be economic, political, ideological and historical or a combination of these.¹⁴⁹

2.4 Independence of a financial services regulator

But why should a financial services regulator be independent anyway? History provides examples that demonstrate that in nearly every major financial crisis of the past decade, political interference helped make a bad situation worse.¹⁵⁰ Quintyn and Taylor note that political pressures not only weakened financial regulation generally, they also hindered regulators and the supervisors who enforce the regulations from taking action against banks that ran into trouble.¹⁵¹ In so doing they crippled the financial sector in the run-up to the crisis, delayed recognition of the severity of the crisis, slowed needed intervention, and raised the cost of the crisis to taxpayers.¹⁵²

But even governments averse to an ownership role in banking may find it foisted on them in a crisis.¹⁵³ However, the authorities' focus then must be on getting out as quickly as possible, using the market, rather than government agencies, to identify

¹⁴⁶ Wymeersch E 'The Structure of Financial Supervision in Europe About Single, Twin Peaks and Multiple Financial Supervisors' (2007) *European Business Organization Law Review* 8: 237-306, (hereafter Wymeersch E (2007)) 237.

¹⁴⁷ Mwenda KK (2006) 48.

¹⁴⁸ See generally Briault C 'The Rationale for a Single National Regulator' (1999) *FSA Occasional Paper*.

¹⁴⁹ Mwenda KK (2006) 48.

¹⁵⁰ Quintyn M & Taylor MW (2004).

¹⁵¹ Quintyn M & Taylor MW (2004).

¹⁵² Quintyn M & Taylor MW (2004).

¹⁵³ *Finances for growth : Choices in a volatile World* (2001) The World Bank (hereafter *Finances for growth* (2001)) 2.

winners and losers.¹⁵⁴ Drawing on public funds to recapitalize some banks may be unavoidable in truly systemic crises, but they must be used sparingly to leverage private funds and incentives.¹⁵⁵

Policymakers seem to have realised their limitations as in recent financial crises, policymakers in the countries affected sought to intervene in the work of regulators often with disastrous results.¹⁵⁶ It is now increasingly recognised that political meddling has consistently caused or worsened financial instability.¹⁵⁷ For example, in *Collapse*, former central bank president Ruth de Kivroy cited ineffective weak regulation and political interference as the cause of the Venezuelan crisis of 1994.¹⁵⁸ In East Asia, political interference in the regulatory and supervisory process postponed recognition of the severity of the crisis and ultimately the delayed action deepened the 1997/98 crisis.¹⁵⁹ In Korea, for example, whilst the commercial banks were regulated by the central bank, specialised banks and other financial institutions were regulated by the finance ministry and the ministry's weak supervision encouraged excessive risk taking which helped lead to the 1997 crisis.¹⁶⁰ In Indonesia there was a mixture of poorly enforced regulations and supervisors' reluctance to take action against politically well connected banks, especially those linked with the Suharto family and when the crisis hit, central bank procedures for dispensing liquidity support for troubled banks were overridden on the alleged direct instructions of the president.¹⁶¹ Lack of independence of financial supervisors in Japan's finance ministry weakened the country's financial sector and contributed to prolonged banking sector problems. Following a decline in the ministry's reputation in the late 1990s, the Japanese government created a new financial services agency to oversee banking, insurance and the securities markets, in part as an attempt to improve the independence of supervision.¹⁶²

¹⁵⁴ *Finances for growth* (2001) 2.

¹⁵⁵ *Finances for growth* (2001) 2.

¹⁵⁶ Quintyn M & Taylor MW (2004).

¹⁵⁷ Quintyn M & Taylor MW (2004).

¹⁵⁸ (2000) referred by Quintyn M & Taylor MW (2004).

¹⁵⁹ Quintyn M & Taylor MW (2004).

¹⁶⁰ Quintyn M & Taylor MW (2004).

¹⁶¹ Quintyn M & Taylor MW (2004).

¹⁶² Quintyn M & Taylor MW (2004).

There seems to increasingly be a shift even by policymakers¹⁶³ and policy analysts to shield financial sector regulators from political pressure to improve the quality of regulation and supervision with the ultimate goal of preventing financial crises.¹⁶⁴ Goodhart and Schoenmaker also observe a trend towards separation between monetary policy and supervisory agencies,¹⁶⁵ in other words, leaving the central bank to concentrate on monetary policy and leaving regulation and supervision of the financial sector to supervisory agencies. Achieving an efficient and secure financial market environment requires an infrastructure of legal rules and practice and timely and accurate information, supported by regulatory and supervisory arrangements that help ensure constructive incentives for financial market participants.¹⁶⁶

In passing laws that create regulatory agencies, politicians properly set and define regulatory and supervisory goals but once those laws are in force, regulators must be free to determine how to achieve those goals, and should be held accountable if they fail to achieve them.¹⁶⁷ Independence must be looked from four related angles: regulatory, supervisory, institutional and budgetary.¹⁶⁸

Regulatory independence implies that the regulator has wide autonomy in setting at a minimum, prudential rules and regulations that follow from the special nature of financial intermediation.¹⁶⁹ These rules and regulations concern the practices that financial institutions must adopt to maintain their safety and stability, including minimum capital adequacy ratios, exposure limits and loan provisioning.¹⁷⁰ Regulators who are able to set these rules independently are more likely to enforce them.¹⁷¹ They are also able to adapt the rules quickly and flexibly in response to changing conditions in the marketplace without having to go through a lengthy, high-pressure political process.¹⁷² Regardless of the detail¹⁷³ in a country's legislation,

¹⁶³ Including lawmakers - see for example the concern of Members of parliament in Malaŵi over Presidential influence over the RBM, Malaŵi's Financial Services Regulator – Sonani B 'Cut President's powers over RBM – MPS' *The Nation* 10 December 2010 available at http://www.nationmw.net/index.php?option=com_content&view=article&id=10828:cut-presidents-powers-over-rbmmps&catid=11:business-news&Itemid=4 (accessed 13 December 2010).

¹⁶⁴ Quintyn M & Taylor MW (2004).

¹⁶⁵ Goodhart CAE & Schoenmaker D 'Should the Functions of Monetary Policy and Banking Supervision be Separated?' (1995) *Oxford Economic Papers* Vol 47 Issue 4 (hereafter Goodhart CAE & Schoenmaker D (1995)) 539.

¹⁶⁶ *Finances for growth* (2001) 2-3.

¹⁶⁷ Quintyn M & Taylor MW (2004).

¹⁶⁸ Mwenda KK (2006) 19.

¹⁶⁹ Quintyn M & Taylor MW (2004).

¹⁷⁰ Quintyn M & Taylor MW (2004).

¹⁷¹ Quintyn M & Taylor MW (2004).

¹⁷² Quintyn M & Taylor MW (2004).

independent regulators should be given ample discretion to set and change regulations within the broad confines of the country's and laws.¹⁷⁴

Supervisory independence denotes that the supervisory agency has independence to supervise the financial sector¹⁷⁵ without undue influences.¹⁷⁶ Whilst supervisory independence is crucial in the financial sector it is also difficult to establish and guarantee because supervisors work quite closely with financial institutions, not only in inspecting and monitoring them but also enforcing sanctions and revoking licences.¹⁷⁷ Much of their activity takes place outside public view, and interference with their work, either by politicians or by the industry can be subtle, and can take many forms.¹⁷⁸ Steps to protect supervisor integrity include indemnifying supervisors from being personally sued for their work and providing financial incentives that allow supervisory agencies to attract and keep competent staff and discourage bribery.¹⁷⁹ Independent regulators, not a government agency or minister should be given the sole authority to grant and withdraw licenses not only because they best understand the financial sector's proper composition but also because the threat to revoke a license is a powerful supervisory tool in itself.¹⁸⁰

Institutional independence has to do with the agency's status outside the executive and legislative branches of government.¹⁸¹ It has three critical elements, first senior personnel should enjoy security of tenure; clear rules ideally involving two government bodies must govern their appointment and, especially dismissal.¹⁸² Secondly the regulator's governance structure should consist of multi-member commissions composed of experts and thirdly decision making should be open and transparent to the extent consistent with commercial confidentiality, enabling both the public and the industry to scrutinise regulatory decisions.¹⁸³

¹⁷³ In some countries the law is so detailed as to leave a little room for independent rule setting in others the laws merely brush on the framework, leaving much greater scope for regulatory discretion – in Malaŵi it would appear to be a hybrid with detail in the law but enough discretion for the regulator to set up rules, regulations and directives.

¹⁷⁴ Quintyn M & Taylor MW (2004).

¹⁷⁵ Including the power to be the sole authority to grant and withdraw licenses - a powerful supervisory tool in itself.

¹⁷⁶ Mwenda KK (2006) 21.

¹⁷⁷ Quintyn M & Taylor MW (2004).

¹⁷⁸ Quintyn M & Taylor MW (2004).

¹⁷⁹ Quintyn M & Taylor MW (2004).

¹⁸⁰ Quintyn M & Taylor MW (2004).

¹⁸¹ Mwenda KK (2006) 26.

¹⁸² Quintyn M & Taylor MW (2004).

¹⁸³ Quintyn M & Taylor MW (2004).

Budgetary independence relates to the regulator not being subjected to political pressure through its budgetary needs.¹⁸⁴ Should funding come from the state, then it should be proposed and justified by the regulator following an objective market based criteria.¹⁸⁵ Some regulators are funded through industry fees, a practice that minimises political interference but risks dependence on – and attracting interference from – the industry.¹⁸⁶ And sometimes a fee based funding structure may leave the regulator strapped for funds during a crisis because that is precisely when the industry is most likely to have difficulty paying the fee.¹⁸⁷ Regulators should therefore be allowed to build up reserve funds as insurance.¹⁸⁸ Senior personnel should have the budgetary freedom to recruit staff as they see fit and to respond quickly to emerging needs.¹⁸⁹

It would however, be naïve to think that making financial regulatory and supervisory agencies independent solves or will solve all financial problems as well as future financial crises. This is partly because financial crises, though regrettably more frequent in recent decades, remain rare events and are often triggered by factors independent of the organisational structure of supervision.¹⁹⁰ The literature on financial crises has not explored the relationship between institutional structure and the likelihood of severe financial sector problems or a full-blown financial crisis.¹⁹¹ Although an independent regulator may not avoid a financial crisis from occurring,¹⁹² what is clear, is that an independent financial services regulator has more chance of managing a crises than one who is not independent because for countries in financial crises where financial services regulators lacked independence, that tended to worsen the crisis.¹⁹³

¹⁸⁴ Mwenda KK (2006) 26.

¹⁸⁵ Mwenda KK (2006) 26.

¹⁸⁶ Quintyn M & Taylor MW (2004).

¹⁸⁷ Quintyn M & Taylor MW (2004).

¹⁸⁸ Quintyn M & Taylor MW (2004).

¹⁸⁹ Quintyn M & Taylor MW (2004).

¹⁹⁰ Goodhart CAE, Schoenmaker D & Dasgupta P (2001) 'The Skill Profile of Central Bankers and Supervisors' (2001) *JEL* (hereafter Goodhart CAE, Schoenmaker D & Dasgupta P (2001)) 1.

¹⁹¹ Goodhart CAE, Schoenmaker D & Dasgupta P (2001) 1.

¹⁹² Mwenda KK (2006) 19.

¹⁹³ Mwenda KK (2006) 30.

It needs to be appreciated that finance is inherently fragile, largely because of the inter-temporal leap in the dark that many financial transactions involve.¹⁹⁴ Finance cannot be effective without credit, but credit means leverage, and leverage means the risk of failure, sometimes triggering a chain reaction (contagion).¹⁹⁵

If finance is fragile, banking is its most fragile part.¹⁹⁶ Bankers have to place a reliable value on the assets they acquire (including the creditworthiness of borrowers).¹⁹⁷ Banking also adds the complications not only of maturity transformation, but of demandable debt, that is, offering debt finance backed by par value liabilities in the form of bank deposits.¹⁹⁸ Polizatto says banks hold a unique position in most economies as creators of money, the principal depositories of the public's financial savings, the primary allocators of credit, and managers of the country's payment systems.¹⁹⁹ For this reason, he argues, governments establish public policy for banks in the public interest and in most market economies, the goals of these policies are to control the supply of money, prevent systemic financial instability, and ameliorate concerns about the efficiency and equity of financial intermediation.²⁰⁰ The failure of any bank, no matter how small, may lead to contagion and loss of confidence in the system, unless the government can demonstrate its ability to handle bank failures in an orderly and systematic fashion.²⁰¹

The particular fragility of finance, and within it of banking, is true for all countries regardless of their income level, as attested to by the occurrence of banking crises in many industrial economies in the 1980s and 1990s²⁰² as well as the recent global crisis. Developing countries face several additional sources of fragility.²⁰³ Not only are information problems in general more pronounced, but developing economies are also smaller and more concentrated in certain economic sectors or reliant on particular export products, and accordingly are less able to absorb shocks or pool isolated risks.²⁰⁴

¹⁹⁴ *Finances for growth* (2001) 10.

¹⁹⁵ *Finances for growth* (2001) 10.

¹⁹⁶ *Finances for growth* (2001) 11.

¹⁹⁷ *Finances for growth* (2001) 11.

¹⁹⁸ *Finances for growth* (2001) 11.

¹⁹⁹ Polizatto VP (1992) 175.

²⁰⁰ Polizatto VP (1992) 175.

²⁰¹ Polizatto VP (1992) 175.

²⁰² *Finances for growth* (2001) 11.

²⁰³ *Finances for growth* (2001) 11.

²⁰⁴ *Finances for growth* (2001) 11.

2.5 Central bank independence

Since the 1980s, more countries have freed their central banks from political control because evidence was growing that independent central banks had a successful record of achieving monetary stability – in other words, controlling inflation.²⁰⁵ As already seen, Goodhart and Schoenmaker cite the trend towards separation between monetary policy and supervisory agencies,²⁰⁶ so that central banks, apart from being independent as argued by Quintyn and Taylor, are also separated from financial supervisory and regulatory functions.²⁰⁷ Central bank independence is seen as essential to counter the natural preference of politicians for expansionary economic policies that promise short-term electoral gains at the risk of worsening inflation in the long run.²⁰⁸ Making central banks independent frees them from political pressure and thus removes the inflationary bias that could otherwise unsettle monetary policy.²⁰⁹ In most countries, such as Malaŵi, the finance minister will set out his fiscal policy in parliament with inflation targets. Most often than not, these are based on the need to win the vote of confidence of the taxpayer so that the economy is seen to be on the rise. If the central bank is not independent in such a scenario, the central bank will be forced to start adjusting the monetary policy to suit the tailor-made fiscal policy geared towards achieving cosmetic inflationary targets.

Incentives for politicians to rescue failing banks are similar to those for inaction in the face of inflation.²¹⁰ The decision to close a failing bank is usually unpopular and politicians eager to avoid a necessary closure may be tempted to pressure bank supervisors to organise a bailout or to excuse the failing bank from regulatory requirements, at the risk of worsening the problem and increasing long-term costs of resolving it.²¹¹ The same may also apply where politicians have connections with the failing bank, and here the reasons may not be as much not to make an unpopular decision as in not to make a decision that may not be in their own interests.²¹² This strengthens the case for regulatory and supervisory independence in the financial

²⁰⁵ Quintyn M & Taylor MW (2004).

²⁰⁶ Goodhart CAE & Schoenmaker D (1995) 556 and also Goodhart CAE, Schoenmaker D & Dasgupta P (2001) 1.

²⁰⁷ Quintyn M & Taylor MW (2004).

²⁰⁸ Quintyn M & Taylor MW (2004).

²⁰⁹ Quintyn M & Taylor MW (2004).

²¹⁰ Quintyn M & Taylor MW (2004).

²¹¹ Quintyn M & Taylor MW (2004).

²¹² Whether politics or personal but as opposed to unpopular ; Quintyn M & Taylor MW (2004).

sector.²¹³ Bank regulatory independence is to financial stability what central bank independence is to monetary stability, and the independence of the two agencies can be mutually enforcing and both agencies also provide a public good – financial stability - which sets them apart from other sector-specific regulatory agencies.²¹⁴

2.6 Independent but accountable

The issue of loss of state power may be of concern in granting independence to finance service regulators. Banking supervisory authority differs from central bank authority in one important way; when banking supervisors revoke a failing bank's licence, or run the bank as statutory manager,²¹⁵ they are using the coercive power of the state (usually embodied in some form of legislation)²¹⁶ against private citizens whilst when a central bank conducts monetary policy, they have no such coercive power and the uniqueness of this power by the regulator may be the basis of an argument against granting them independence.²¹⁷ It would be naive to underplay these fears against creating an independent authority with state powers but instead it is suggested that governments should fully accept and take the implications of that power into account both by establishing strong accountability mechanisms to prevent abuse and recognising the need to employ highly qualified supervisors of demonstrable integrity and to pay them adequately.²¹⁸

In theory, independent regulators can decide on and conduct market interventions shielded from political interference and improve regulatory and supervisory transparency, stability and expertise.²¹⁹ Growing evidence suggests that independent regulators have made regulation more effective, have led to smoother and more efficient operation of the market and are a distinct improvement over regulatory functions located in government ministries.²²⁰

²¹³ Quintyn M & Taylor MW (2004).

²¹⁴ Quintyn M & Taylor MW (2004).

²¹⁵ See for example statutory manager appointed under s 68 of the Financial Services Act

²¹⁶ For example the Financial Services Act or any of the Financial Services Laws.

²¹⁷ Quintyn M & Taylor MW (2004).

²¹⁸ Quintyn M & Taylor MW (2004).

²¹⁹ Quintyn M & Taylor MW (2004).

²²⁰ Quintyn M & Taylor MW (2004).

A regulator needs legal protection from liability arising out of the proper discharge of its powers to ensure diligence, competence and independence.²²¹ Having clear responsibilities, objectives, adequate powers, adequate resources (human capital, infrastructure and technology to process information in a timely manner),²²² transparency and accountability will make a regulator effective²²³ and reduce fears of it becoming a fourth arm of the state.²²⁴ The fear here is they are outside the control of the traditional three arms or branches that keep democratic systems in equilibrium through a system of checks and balances.²²⁵

On the other hand, as Nobel Prize winning economist George J. Stigler pointed out, agencies tend to respond to the wishes of the best organised interest groups and when regulators are free from political control, the risk of “regulatory” capture by other groups, - in particular the industry they regulate – grows,²²⁶ a view shared by Mwenda.²²⁷ Agencies that suffer from such capture come to identify industry interests (or even interests of individual firms) with the public interest and industry capture can undermine the effectiveness of regulation just as political pressure can.²²⁸ The general view is that a regulator must be operationally independent and accountable for the use of its powers whilst providing the right of appeal of its decisions and access to judicial review.²²⁹ The need for accountability will stop an independent regulator pursuing an agenda of its own and although fears of an independent regulator going on an agenda course of its own or becoming an uncontrollable fourth branch of the government appear exaggerated, they nevertheless demonstrate the need for proper forms of accountability to balance the advantages of regulatory independence with the disadvantages.²³⁰

Therefore achieving both political independence and independence from the regulated industry, as well as accountability is essential and of these political independence remains the prime concern from the point of view of financial stability,

²²¹ Mwenda KK (2006) 14.

²²² Mwenda KK (2006) 13 - The regulator needs adequate resources as lack thereof compromises a regulator's independence if the regulator is dependent on state funding.

²²³ Mwenda KK (2006) 12.

²²⁴ Hüpkes E, Quintyn M & Taylor MW 'Accountability arrangements for the Financial Sector' (2006) *IMF Economic Issues* No 39 (hereafter Hüpkes E, Quintyn M & Taylor MW (2006)) 1.

²²⁵ Quintyn M & Taylor MW (2004).

²²⁶ As quoted by Quintyn M & Taylor MW (2004).

²²⁷ Mwenda KK (2006) 33.

²²⁸ Quintyn M & Taylor MW (2004).

²²⁹ Hüpkes E, Quintyn M & Taylor MW (2006) 9.

²³⁰ Quintyn M & Taylor MW (2004).

given the vested interests that many national governments still have in the banking system, and therefore, in bank regulation and supervision, as well as the dismal track record of political interference in regulatory and supervisory arrangements.²³¹

2.7 Regulatory models and systems in comparable countries

United Kingdom

Malaŵi's economy was once tied to the UK economy by virtue of colonialism. The influence of the UK's financial system can therefore not be overemphasised.²³² The Financial Services Authority (FSA) in the UK is the unified regulator. It combines prudential, conduct of business and market conduct regulation across the full range of financial services, including banking, securities, investment management and insurance.²³³ But the FSA whilst being the more famous was not the first unified regulator with earlier integrated financial regulation being done in Scandinavia a decade before the FSA came into being.²³⁴ The FSA was the result of the merging of financial services regulation announced by the chancellor of the exchequer in May 1997.²³⁵ The FSA merged the Securities and Investment Board and also took over the supervisory responsibilities of the Bank of England.²³⁶ The rationale for this merging was that the then existing arrangements of financial regulation involved a large number of regulators, each responsible for different parts of the industry and a glowing blurring of the distinctions between different kinds of financial services (banks, building societies, investment firms, insurance companies etc) made financial services regulation complex, inefficient, confusing²³⁷ and costly.²³⁸ However the coming in of the FSA did not mean it was the only body overseeing the financial services. The FSA works with the Bank of England and treasury and the responsibilities were thus divided:

²³¹ Quintyn M & Taylor MW (2004).

²³² See the introduction in Chapter One (Historical context and state of affairs)

²³³ Briault C 'The Rationale for a Single National Regulator' (1999) *FSA Occasional Paper* (hereafter Briault C (1999)) 5.

²³⁴ Taylor MW & Fleming 'A Integrated Financial Supervision: Lessons of Scandinavian Experience' (1999) *IMF Finance and Development* Vol 36 No 4.

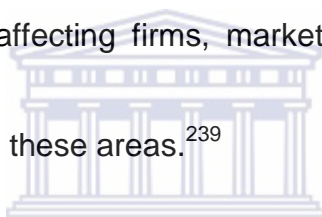
²³⁵ Briault C (1999) 6. The chancellor then was Gordon Brown of the Labour Government who went on to become the Prime Minister till defeat by the Conservatives in 2010. This may have provided (until the defeat) the requisite political goodwill for the FSA.

²³⁶ Briault C (1999) 7.

²³⁷ To both the regulated firms and their customers.

²³⁸ Briault C (1999) 6.

- Treasury responsible for overall institutional structure of regulation and the governing legislation.
- Bank of England responsible for:
 - overall stability of the financial system including the stability of the monetary system;
 - financial infrastructure (in particular payment systems) as well as for being able in “exceptional” circumstances subject to the agreement of the Treasury to undertake official financial support operations;
 - efficiency and effectiveness of the financial sector.
- FSA responsible for:
 - authorisation and supervision of financial services firms;
 - supervision of financial markets and of clearing and settlement systems;
 - conduct of market-based support operations not involving official finance in response to problems affecting firms, markets and clearing and settlement systems;
 - regulatory policy in all of these areas.²³⁹



However, during the 2007-2009 global financial crisis, the Bank of England and Treasury came to the rescue of failing financial institutions (mainly banks) prompting the biggest shake up since the formation of the FSA.²⁴⁰ The new Chancellor announced sweeping changes which may see the abolition of the existing tripartite regime between the FSA, Bank of England and Treasury.²⁴¹ If they come to fruition, these changes may not mean the scrapping the FSA but will have the effect of at least stripping it bare with prudential regulation moving to a new body reporting to the Bank of England, and a new agency being created to tackle serious economic crime.²⁴² The new prudential regulator (the Prudential Regulatory Authority) will operate as a subsidiary of the Bank of England and will carry out prudential regulation of financial firms, including banks, investment banks, building societies and insurers.²⁴³ The New Consumer Protection and Markets Authority will regulate

²³⁹ Briault C (1999) 10.

²⁴⁰ ‘The FSA is dead. Long live the Bank of England’ *Shoosmiths* 22 June 2010 (hereafter *The FSA is dead (2010)*) available at <http://www.shoosmiths.co.uk/news/3100.asp> (accessed 14 March 2011).

²⁴¹ *The FSA is dead (2010)*.

²⁴² *The FSA is dead (2010)*.

²⁴³ *The FSA is dead (2010)*.

the conduct of every authorised financial firm providing services to consumers.²⁴⁴ Whether this includes firms other than those currently authorised by the FSA (for example credit providers and intermediaries) remains to be seen,²⁴⁵ but clearly the FSA's prowess will have been reduced. In going this route, the UK will create a 'twin peaks' system separating prudential and conduct regulation but this bucks the trend of moves within the EU in the recent past to consolidate and unify financial regulation.²⁴⁶ Clearly the decision to change the regulatory framework maybe political but it may also have been self-made because of regulatory failure. Mwenda has described the failure of financial regulation as one of the most important causes of this global economic crisis.²⁴⁷ However, he argues that in order to avoid experiencing such a crisis again, the solution lies in designing and implementing more effective regulatory frameworks for financial institutions.²⁴⁸ It would therefore seem that the solution lies not in removing regulatory bodies, or dismantling them as proposed in the UK but making them more stringent and effective.

Despite the announcement of these plans, the FSA is still intact²⁴⁹ and as late as March 2011 issued a publication on updated guidelines across its constituency.²⁵⁰ Pronouncements that the FSA is dead may therefore prove to have been immature. For now, the FSA remains the single financial service regulator of the UK.

Zambia

Malaŵi and Zambia share many roots. Courtesy of being former British colonies, they all inherited the English Common law and principles of equity.²⁵¹ The two countries share common languages and ethnic groupings (Chewas, Ngonis, Tumbukas and Tongas).²⁵² Both were under the Federation of Rhodesia and Nyasaland.²⁵³ Whilst

²⁴⁴ The FSA is dead (2010).

²⁴⁵ The FSA is dead (2010).

²⁴⁶ The FSA is dead (2010).

²⁴⁷ Foreword by Professor Daniel Bladlow in Mwenda KK *Legal aspects of banking regulation : Common law perspectives from Zambia* (2010) (hereafter Mwenda KK (2010)) at xiii.

²⁴⁸ Mwenda KK (2010) xiii.

²⁴⁹ Clarke P ' Shaky future for the FSA, but it's still hiring' *eFinancial Careers* 4 June 2010 available at http://news.efinancialcareers.co.uk/News_ITEM/newsItemId-26002 (accessed 14 March 2011).

²⁵⁰ 'Handbook release 111' the FSA 10 March 2011 available at <http://www.fsa.gov.uk/pages/Library/Policy/Handbook/Releases/2011/111.shtml> (accessed 14 March 2011).

²⁵¹ Mwenda KK (2010) 1 and see also s 200 of the Constitution of Malaŵi which provides that the Common law is applicable as long as it is not inconsistent with the Constitution.

²⁵² See *Zambia Travel Guide* available at http://www.zambia-travel-guide.com/bradt_guide.asp?bradt=1098 (accessed 15 March 2011).

the Zambian economy took an industrial route courtesy of discovery of copper, the Malaŵi economy has largely remained agro-based, although the recent discovery of uranium may change that. The opening of the Kayekera Uranium mine operated by Paladin Africa²⁵⁴ and prospects of more mines are likely to change the economic landscape of Malaŵi. At the moment, the Zambian economy would therefore be like the 'bigger brother'.²⁵⁵ In both countries lack of liquidity is a serious impediment to the efficient functioning of their stock markets.²⁵⁶ Malaŵi and Zambia even share the same local name for their currency, the Kwacha.²⁵⁷ These legal, political, historical and economic similarities make Zambia the ideal comparative country.

In Zambia, the Banking and Financial Services Act 1994 (BFSA) is the legislative cornerstone for the regulation and supervision of banks and financial institutions.²⁵⁸ Closely related to the BFSA is the Bank of Zambia Act 1996.²⁵⁹ Mwenda says that although the Bank of Zambia (BOZ) provides for a mechanism of independence, BOZ is not independent and to a large extent operates under the executive arm of the state.²⁶⁰ The bank itself admits that lack of operational autonomy is the major challenge it faces as a central bank.²⁶¹ The governor of BOZ has argued that the tenure of office of the bank governor should not run concurrently with the term of office of a particular government to enhance professionalism and remove patronage.²⁶² A similar problem of the central bank governor's tenure has been raised by Kalilombe in the case of Malaŵi.²⁶³ The World Bank says a solution which also can help ensure the quality of regulatory oversight, is fixed and long terms for

²⁵³ Together with Zimbabwe - 'Federation of Rhodesia and Nyasaland' *Encyclopædia Britannica* available at <http://www.britannica.com/EBchecked/topic/501645/Federation-of-Rhodesia-and-Nyasaland> (accessed 15 March 2011).

²⁵⁴ 'Kayelekera Uranium Mine, Malawi' *mining-technology* available at <http://www.mining-technology.com/projects/kayelekerauraniummin/> (accessed 23 August 2010).

²⁵⁵ With problems in Zimbabwe, that country may take time to regain its lead as the economic powerhouse of the former 'federation countries'.

²⁵⁶ Marone H (2003) 5 and see *and see* Mwenda KK (2000) and see further Index of Economic Freedom (2010).

²⁵⁷ Literally means it is light (after the darkness of the night) but symbolises the dawn of a new political era and freedom when the two countries obtained their Independence from Britain.

²⁵⁸ Mwenda KK (2010) 66.

²⁵⁹ Mwenda KK (2010) 68.

²⁶⁰ Mwenda KK (2010) 81.

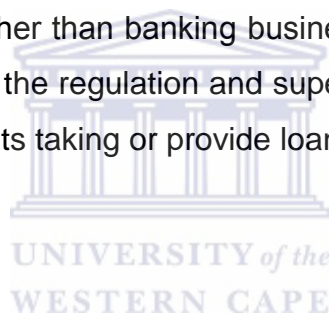
²⁶¹ Bank of Zambia Financial Development Plan (2004-2009) quoted in Mwenda KK (2010) 82.

²⁶² Mwenda KK (2010) 82 citing *Times of Zambia* <http://www.times.co.zm/news/viewnews.cgi?category=4&id=1095648645>.

²⁶³ Kalilombe (2008) 41.

the central bank governor, ending the ability of the executive to remove them without a solid majority of parliament.²⁶⁴

In Zambia, the registrar of banks and financial institutions authorises companies to conduct banking and financial services.²⁶⁵ The registrar is based at the central bank and BOZ for all intents and purposes is the competent authority regulating and supervising banks and financial institutions.²⁶⁶ Zambia has a twin peak unified system of financial services supervision.²⁶⁷ On the one hand BOZ has separate departments to supervise banks and non banking financial institutions, on the other, the Pensions and Insurance Authority (PIA) is responsible for supervising insurance companies and pension funds, even though both are in essence nonbanking financial institutions not much different from those supervised by BOZ.²⁶⁸ Mwenda says this ‘anomaly’ may be because either under section 2 of the BFSA, pension funds and insurance companies are not recognised as financial institutions that carry on “financial services business other than banking business” or the relevant department in BOZ is concerned only with the regulation and supervision of nonbanking financial institutions that accepts deposits taking or provide loans.²⁶⁹



Conclusion

This chapter has discussed the theoretical underpinnings of financial services regulation, its rationale as well as models of financial services regulation and supervision.

The chapter examined the requirements that independence must be looked from four related angles: regulatory, supervisory, institutional and budgetary. In examining these ‘yardsticks’ for independence, the chapter also examined the requirements for a regulator to be truly independent. To attain regulatory independence, the regulator must have wide autonomy in setting prudential regulations that follow from the special nature of financial intermediation. Supervisory independence requires independence to supervise the financial sector without undue influences. It was

²⁶⁴ *Finances for growth* (2001) 28.

²⁶⁵ Mwenda KK (2010) 91.

²⁶⁶ Mwenda KK (2010) 91.

²⁶⁷ Mwenda KK (2006) 46.

²⁶⁸ Mwenda KK (2006) 46.

²⁶⁹ Mwenda KK (2006) 46-7.

noted that supervisory independence is difficult to establish and guarantee because supervisors work quite closely with financial institutions. Institutional independence has to do with the agency's status outside the executive and legislative branches of government and involves three critical elements; security of tenure of senior personnel; having a governance structure of multi-member commissions composed of experts and transparency in decision making but consistent with commercial confidentiality.

The Chapter also looked at the benefits of having an independent financial services regulator as well as the need to be accountable so as to allay fears of the regulator being branded a fourth estate. Because of the central role that banks play in the financial sector, the chapter also looked at central banks and how making them independent from (excessive) political manipulation can improve their performance. In this regard the security of tenure of the governor of the central bank is a key factor.

The Chapter ends with a comparative study of the financial service regulatory and supervisory systems in the UK and Zambia. The UK has a unified single regulator whilst Zambia has a twin peak system. As will be seen in the next chapter, Malaŵi has a unified (single peak) regulatory system but there are strong comparisons to the legal and operation framework of Malaŵi and Zambia. The next chapter critically analyses the current financial services regulatory framework of Malaŵi.

CHAPTER THREE

3. The Financial Service Regulatory System in Malaŵi

3.1. Overview of the contextual framework

Malaŵi gained independence from Great Britain in 1964 and became a Republic in 1966.²⁷⁰ Before becoming a Republic, Malaŵi used the Union Jack,²⁷¹ the British Pound Sterling and sang 'God Save the Queen!'²⁷² On attaining Republican status, Malaŵi politically delinked its economy from Britain and set up its own financial system, with the Malaŵi Kwacha as the new currency. The Kwacha was however still fixed to the British Pound Sterling up to 1973 when world-wide economic difficulties precipitated by the oil price shocks of the 1973/1974 and general problems associated with the fixed exchange rate regimes led to its abandonment and a search for other fiscal solutions for the stabilisation of its currency.²⁷³

However, almost 47 years after political independence and 45 years after financial independence, Malaŵi remains one of the Least Developing Countries (LDC) and its situation is exacerbated by the fact that it is also landlocked. Malaŵi is therefore a Land-Locked Least Developing Country (LLDC)²⁷⁴ and amongst the poorest in the world.²⁷⁵ Poverty is a fact and remains a key challenge.²⁷⁶ Real per capita GDP stood at 189 USD in 2009.²⁷⁷ Progress has however, been made in tackling poverty and other social challenges.²⁷⁸ Increased household food security and falling poverty have complimented strong macroeconomic performance.²⁷⁹ The government estimates that the poverty headcount has fallen from 52.4% in 2005 to 40% in

²⁷⁰ 'Malawi: Department of Tourism' available at <http://www.visitmalawi.mw/About%20Malawi/aboutmalawi.htm> (accessed 1 January 2011).

²⁷¹ The flag for Great Britain.

²⁷² Great Britain national anthem.

²⁷³ Ndaferankhande MD & Ndhlovu TM 'Inflationary experiences in Malawi: An investigation of the underlying determinants' (2006) 14 available at www.csaee.ac.uk/conferences/2006-EOI.../Ndaferankhande.pdf (accessed 1 January 2011).

²⁷⁴ 'UN-OHRLLS : Least Developed Countries' available at <http://www.unohrlls.org/en/lcd/related/62/> (accessed 22 August 2010).

²⁷⁵ But see summary of 'United Nations General Assembly Debate : 65th Session, President Bingu wa Mutharika, Malawi' available at <http://www.un.org/en/ga/65/meetings/generaldebate/View/SpeechView/tabid/85/smid/411/ArticleID/101/refTab/224/t/Malawi/Default.html> (accessed 23 March 2011).

²⁷⁶ 'African Economic Outlook : Malawi' available at <http://www.africaneconomicoutlook.org/en/countries/southern-africa/malawi/> (accessed 17 September 2010). (hereafter African Economic Outlook : Malawi (2010)).

²⁷⁷ African Economic Outlook : Malawi (2010).

²⁷⁸ African Economic Outlook : Malawi (2010).

²⁷⁹ African Economic Outlook : Malawi (2010).

2009.²⁸⁰ Overall well-being remains low, but is improving, as measured by the UN Human Development Index score of 0.493 that ranks Malaŵi at 160 out of 182 countries in 2009, up from 164 out of 177 in 2007/08.²⁸¹ Macroeconomic indicators have put Real GDP Growth for 2008, 2009,²⁸² 2010 and 2011 at 9.8, 7.0, 6.0 and 6.2.²⁸³

Malaŵi is a constitutional supremacy,²⁸⁴ a situation that came about after the 1993 referendum that ushered in multiparty democracy²⁸⁵ and a new democratic Constitution.²⁸⁶ The system of government is that of an executive presidency. Although constitutionally there are three arms of Government (executive, legislature and judiciary) the State President is head of the three arms apart from being head of Government.²⁸⁷ At the conferences that led to the new Constitution in 1992-3, the issue of limiting the president's powers was topical, especially coming from days of one party dictatorship under Kamuzu Banda. In the end Malaŵi ended up with a Constitution that can best be described as a hybrid of the American (presidential) system and the British (parliamentary) system but more inclined to the presidential system. In Malaŵi, the president is therefore a very powerful legal personality and his decisions and exercise of discretion has a profound effect on all facets of the country.

The financial sector in Malaŵi is not very well developed and is reflective of its rather small economy and size.²⁸⁸ The banking sector dominates the financial sector.²⁸⁹

²⁸⁰ African Economic Outlook : Malawi (2010).

²⁸¹ African Economic Outlook : Malawi (2010).

²⁸² In 2009, Malaŵi experienced some financial setbacks, including a general shortage of foreign exchange, which has damaged its ability to pay for imports and investment fell 23% - 'Malawi Economy 2011' *theodora* available at http://www.theodora.com/wfbcurrent/malawi/malawi_economy.html (accessed 17 September 2010).

²⁸³ African Economic Outlook : Malawi (2010).

²⁸⁴ Sections 4,5, 199, The Constitution of the Republic of Malaŵi, 1994.

²⁸⁵ There has been debate that the first multi-party elections were actually held in 1961 when self-governance was attained but this debate is outside the scope of this paper.

²⁸⁶ Much more similar to the South African Constitution it must be said. There is a fluid debate of which one preceded the other see - *Sidumo & Another v Rustenburg Platinum Mines Ltd & Others* (2007) 28 ILJ 2405 (CC) 2426 para 55.

²⁸⁷ The Constitution treats the three arms as equal but with different functions – see ss 7,8 & 9 of the Constitution.

²⁸⁸ It has a population of 15.8 million and a total area of 118,484 sq km out of which 24,404 sq km is water with a real per capita GDP of 189 US dollars (USD) in 2009 - African Economic Outlook : Malawi (2010) & 'Malawi population' *IndexMundi* available at <http://www.indexmundi.com/malawi/population.html> (accessed 23 March 2011).

²⁸⁹ '2010 Index of Economic Freedom' The Heritage Foundation & *The Wall Street Journal*, available at <http://www.heritage.org/index/country/malawi> (accessed 17 September 2010). (hereafter Index of Economic Freedom (2010)).

Eleven commercial banks²⁹⁰ offer a variety of services and generally allocate credit on market terms.²⁹¹ However, high credit costs and scarce access to financing hinder more vibrant business activity.²⁹² The economic fundamentals do not lend themselves attractive to the development of a saving culture. For example, although the 12-month inflation rate for January 2011 is officially²⁹³ at 6%, bank rate is at 13%, savings rate ranges from 0.75 to 2.5% whilst the lending rate ranges from 17.75 to 23.75%.²⁹⁴ There is therefore the situation that the savings rate is not attracting enough savings which can be used to lend out.

The alternative for those who may wish to invest seems to be the securities market. However, the securities markets are not fully developed and activity on the Malaŵi Stock Exchange (MSE), the only stock exchange remains very limited.²⁹⁵ The MSE has one tier trading arrangement under the Malaŵi All Share Index (MASI) although it recently introduced the Alternate Capital Market (ACM).²⁹⁶ The ACM is yet to see any listing. The ACM is supposed to cover small business which could not meet the regulatory rigours of those listed under the MASI.²⁹⁷ The reasons for this lack of enthusiasm may need to be researched further.

The financial sector of Malaŵi is still at a rudimentary stage with low public confidence as reflected in the illiquidity of the MSE.²⁹⁸ The turnover velocity, an indicator of the liquidity of assets traded on the market was 1.33 % in 2009 compared to 3.33 % recorded in 2008²⁹⁹ (refer to Appendix A for a table of trading in 2009). The

²⁹⁰ See Appendix C.

²⁹¹ Index of Economic Freedom (2010).

²⁹² Index of Economic Freedom (2010).

²⁹³ There is always ongoing debate as to whether the official figures reflect the situation on the ground. However the 6.60 is an average comprising of two components : Non-Food 10.70% and Food 2.90% - 'Reserve Bank of Malawi' available at <http://www.rbm.mw/> (accessed 23 March 2011).

²⁹⁴ 'Reserve Bank of Malawi' available at <http://www.rbm.mw/> (accessed 23 March 2011).

²⁹⁵ Index of Economic Freedom (2010).

²⁹⁶ It is submitted that the MSE may have to reconsider changing the name from ACM to Alternative Securities Market in line with the Securities Act which replaced the Capital Market Development Act as well as in line with financial trends.

²⁹⁷ See 'Guidelines to listing on the Malawi Stock Exchange: Alternative Capital Market' available at <http://www.mse.co.mw/rules/ALTERNATIVE2.pdf> (accessed 23 March 2011).

²⁹⁸ For example the MSE registered no trading in the week 6-10 September, 2010 (11 September was a holiday) see – Chiyembekeza C 'Stock market closes 4-day trading week flat' *The Nation* 13 September 2010 available at

http://www.nationmw.net/index.php?option=com_content&view=article&id=5770:stock-market-closes-4-day-trading-week-flat&catid=11:business-news&Itemid=4 (accessed 17 September 2010).

A practical example of illiquidity of the MSE was when the author failed to sell shares in two listed companies for more than 6 months!

²⁹⁹ 'Malawi Stock Exchange : Annual Market Performance Review 2009' MSE available at <http://www.mse.co.mw/current/annual.pdf> (accessed 17 September 2010).

MSE has been in existence since 1994 but started equity trading in November 1996 when it first listed National Insurance Company Limited (NICO).³⁰⁰ Prior to the first listing, the major activities undertaken were provision of a facility for secondary market trading in Government of Malaŵi bonds namely, Treasury Bills and Local Registered Stocks.³⁰¹

The MSE was licensed under the Capital Market Development Act 1990³⁰² (CDMA) and Companies Act 1984.³⁰³ The Securities Act 2010 has replaced the CDMA. The Securities Act provides for the main legislative framework for securities regulation in Malaŵi. The MSE now operates under the Securities Act. Malaŵi is also part of the Southern African Development Community (SADC)³⁰⁴ and Common Market for Eastern and Southern Africa (COMESA).³⁰⁵ Its membership of both organisations has raised debate but such a discussion is outside the scope of this work. Most of the members of SADC³⁰⁶ and COMESA³⁰⁷ have illiquid stock markets too.³⁰⁸

3.2. Financial sector regulation and supervision

The overarching regulatory framework for the financial sector is the Financial Services Act 2010 (FSAM). The Act defines the “financial services law” (FSL) as comprising the following acts; Reserve Bank of Malaŵi Act 1989, Banking Act 2009, Securities Act 2010, Microfinance Act 2010, Insurance Act 2009, Credit Reference Bureau Act 2010, Building Society Act 1964, Financial Services Act 2010, Pension Act 2010[sic], Financial Cooperatives Act 2010[sic].³⁰⁹

³⁰⁰ ‘Malawi Stock Exchange : Company Profile’ available at <http://www.mse.co.mw/prof.html> (accessed 18 September 2010). (hereafter Malawi Stock Exchange – Company Profile (2010)).

³⁰¹ Malawi Stock Exchange : Company Profile (2010).

³⁰² Chap 46:06 of the Laws of Malaŵi. Hereafter Capital Markets Development Act or CMDA.

³⁰³ Malawi Stock Exchange : Company Profile (2010). The Companies Act 1984 (hereafter Companies Act).

³⁰⁴ See Southern Africa Development Community available at <http://www.sadc.int/> (accessed 17 September 2010).

³⁰⁵ See The Common Market for Eastern and Southern Africa available at <http://www.comesa.int/> (accessed 17 September 2010).

³⁰⁶ Except the JSE in South Africa which is liquid by African standards.

³⁰⁷ Except for NSE in Kenya and EGX in Egypt.

³⁰⁸ See Marone H (2003) 11 *and see generally* Mwenda KK (2000).

³⁰⁹ Section 2 , Financial Services Act 2010 (hereafter Financial Services Act). The pensions Bill has not been enacted and the Financial Cooperatives Act has just been enacted in 2011.

The definitions includes some bills³¹⁰ as if they are acts and it is submitted that this was in anticipation of their passing. The Exchange Control Act is not included and it is the author's view that this omission was by error and not design.³¹¹

3.2.1. The Constitution

Although the Constitution is not included amongst the FSL, it plays a crucial role in the overall scheme of things. First, it is the supreme law of the land³¹² and any law or act of government inconsistent with it is invalid to the extent of the inconsistency.³¹³

The Constitution also provides for judicial review by the High Court for any law or administrative action or decision of the government.³¹⁴ Government has always been construed broadly and includes any organ exercising public authority.³¹⁵ The Constitution also provides for the right to administrative justice³¹⁶ which provides for the right to lawful and procedurally fair administrative action, which is justifiable in relation to reasons given where those rights, freedoms, legitimate expectations or interests are affected or threatened.³¹⁷ It also provides for the right to be furnished with reasons in writing for such administrative action.³¹⁸ Under the maxim *ubi jus ibi remedium*,³¹⁹ the courts are enjoined to provide a remedy where any fundamental rights enshrined in the Constitution has been violated³²⁰ and the court has the power to award compensation where it considers it to be appropriate in the circumstances of a particular case.³²¹

This provides everyone (natural and juristic persons) with the right to challenge administrative action and this right avails to a financial institution which may have its rights, freedoms, legitimate expectations and interests affected by any regulatory decision.

³¹⁰ At least at the time the Act was passed.

³¹¹ This is because financial *Bureaux de Change* are regulated by the Exchange Control Act and are for purposes of the Act financial institutions.

³¹² Sections 4, 199 the Constitution of the Republic of Malaŵi, 1994 (hereafter Constitution).

³¹³ Section 5 Constitution.

³¹⁴ Section 108(2) Constitution.

³¹⁵ See *The State v The Chief Secretary to the President; Ex Parte Dr Bakili Muluzi*, Misc. Civil Application No 3 of 2011 (HC) Mzuzu Registry (unreported).

³¹⁶ Section 43 Constitution.

³¹⁷ Section 43(a).

³¹⁸ Section 43(b).

³¹⁹ For every right, there is a remedy; where there is no remedy, there is no right.

³²⁰ Section 46(2)(b).

³²¹ Section 46(4).

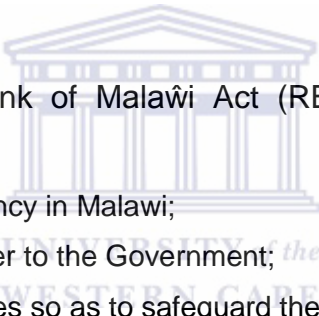
The Constitution also has a whole chapter dedicated to the RBM albeit containing only two sections.³²² But what is more revealing is not the contents of the chapter but the fact that the drafters³²³ decided to give recognition to the RBM in a separate chapter. Chapter XIXI states:

- s. 185. 1. There shall be established by an Act of Parliament a central bank of the Republic, known as the Reserve Bank of Malawi which shall serve as the State's principal instrument for the control of money supply, currency and the institutions of finance and shall serve generally in accordance with the normal functions of a central bank.
2. The Bank shall be controlled by a Board which shall consist of a chairman and members of the Board who shall, subject to this Constitution, be appointed in accordance with the Act of Parliament by which the Bank is established.

3.2.2. Central Bank

- Legal structure :

Section 3 of the Reserve Bank of Malawi Act (RBMA) states that the principal objectives of the RBM shall be:

- 
- (a) to issue legal tender currency in Malawi;
 - (b) to act as banker and adviser to the Government;
 - (c) to maintain external reserves so as to safeguard the international value of the Malawi currency;
 - (d) to implement measures designed to influence the money supply and the availability of credit, interest rates and exchange rates with the view to promoting economic growth, employment, stability in prices and a sustainable balance of payments position ;
 - (e) to promote a sound financial structure in Malawi, including payment systems, clearing systems and adequate financial services;
 - (f) to promote a money and capital market in Malawi;
 - (g) to act as lender of last resort to the banking system;
 - (h) to supervise banks and other financial institutions;
 - (i) to collect economic data of the financial and other sectors for research and policy purposes; and
 - (j) to promote development in Malawi.³²⁴

³²² Chapter XIX.

³²³ Given this is a 1994 Constitution, the term 'our fathers' in reference to those who came up with the Constitution may really not apply for a considerable period of time!

³²⁴ Underlining supplied.

Clearly the RBM has a lot of ‘principal’ objectives. What is worth noting is that the RBMA does not use the word ‘regulate’ as part of the principal objectives of the RBM. It is however argued that not much should be read in this as the functions of the RBM under the RBMA and FSL are both regulatory and supervisory.

The RBMA defines financial institution as any person, other than a bank, registered as a financial institution under the Banking Act.³²⁵ The term other financial institutions is defined to include financial institutions and pensions, assurance and insurance institutions.³²⁶ The Banking Act 2009³²⁷ has removed the definition for a financial institution since financial institutions are now registrable under the now specific legislation comprising the FSL.

- Political structure of the central bank

The governor and deputy governor of the RBM are appointed exclusively by the President.³²⁸ The board of directors of the RBM is also appointed exclusively by the President and comprises the governor, deputy governor, and five other directors who may include secretary to the treasury, secretary for economic planning and development and the accountant general.³²⁹ The governor (or deputy governor in the governor’s absence) chairs the board of directors.³³⁰

³²⁵ Section 2 RBM Act.

³²⁶ Section 2, RBM Act.

³²⁷ Discussed below (the RBM Act originally referred to the repealed Banking Act but should now be read as referring to the Banking Act 2009). Any reference in the text to the Banking Act is to the Banking Act 2009 and the old Act will be referred to as the repealed Banking Act).

³²⁸ Section 12 RBM Act; s 6 of the RBM Amendment Bills proposed the appointment of not more than three deputy governors (up from the present one) and not more than seven directors – see Sonani B ‘Cut President’s powers over RBM – MPS’ *The Nation* 10 December 2010 available at http://www.nationmw.net/index.php?option=com_content&view=article&id=10828:cut-presidents-powers-over-rbmmps&catid=11:business-news&Itemid=4 (accessed 13 December 2010).

³²⁹ Section 6 RBM Act. See Appendix D for the Current list of Board Members.

³³⁰ Section 11 RBM Act.

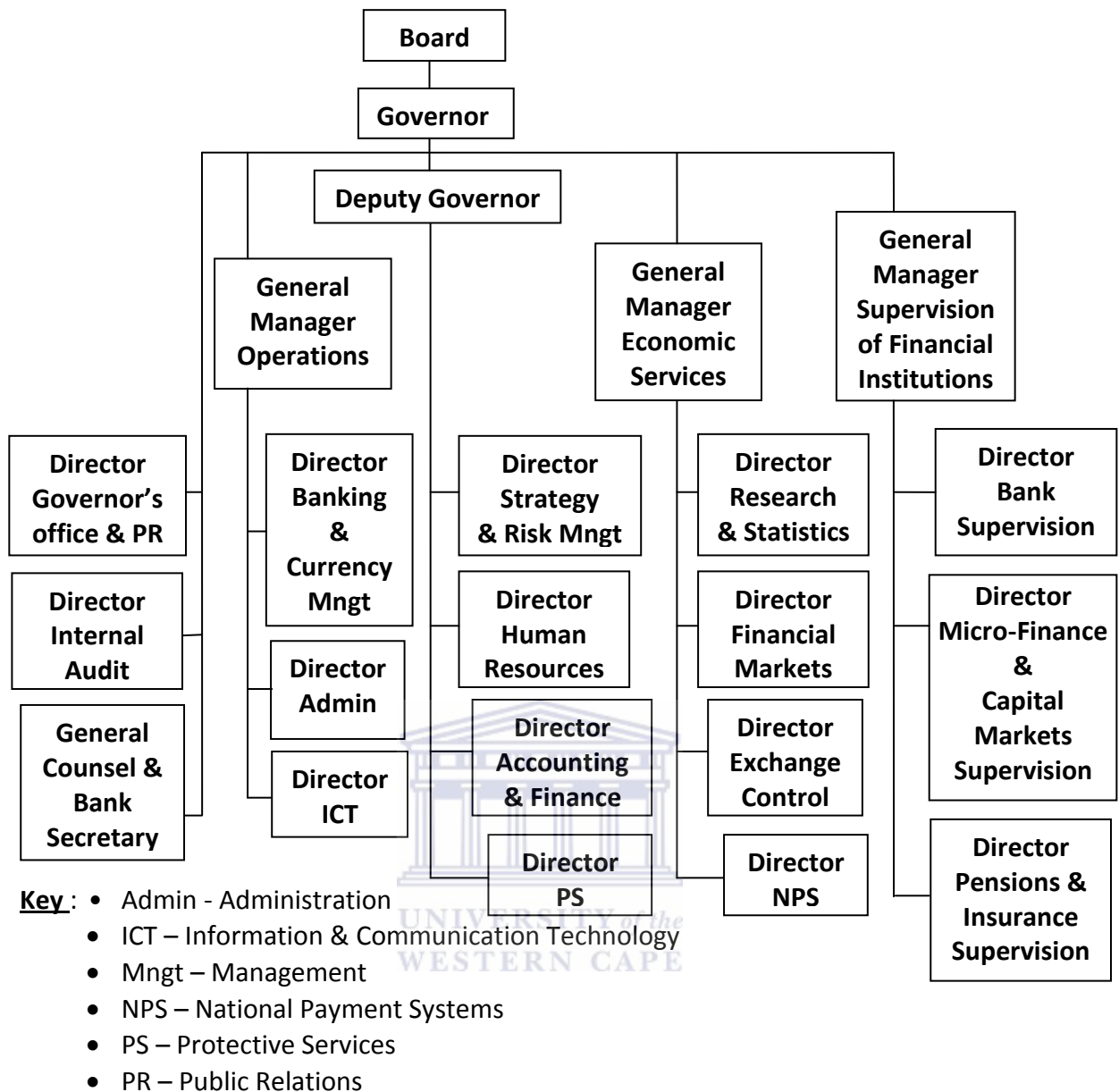


Fig 3 The organisational structure of the RBM³³¹

At independence, Malaŵi was a *de jure* multi-party state but a *de facto* one party state by virtue of the absolute dominance of the Malaŵi Congress Party (MCP).³³²

The *de facto* position of the MCP was translated into a *de jure* reality in 1966 when the country became a one party state, with Dr Banda as Executive President.³³³ Five years later, Ngwazi Dr H Kamuzu Banda was proclaimed 'President for life' with the

³³¹ Redrawn and extracted without names from 'Reserve Bank : About the Reserve Bank of Malawi' available at <http://www.rbm.mw/aboutrbm.aspx> (accessed 30 March 2011).

³³² There were minority parties (reflecting mainly racial lines) when Malaŵi became Independent in 1964 following the general elections of 1961 but this changed after 1966 and following the (in)famous "cabinet crisis" when Dr. Banda reinforced his reigns on power.

³³³ 'Malawi: Era of One Party Rule (1964-1992)' in Lodge T, Kadima D & Pottie D *Compendium of Elections in Southern Africa* (2002) (hereafter Lodge T, Kadima D & Pottie D (2002)) 124 available at <http://www.eisa.org.za/WEP/maloneypartyrule.htm> (accessed 25 March 2011).

strange insertion of this proclamation in the country's Constitution!³³⁴ Malaŵi has therefore been a *de facto* and *de jure* one-party state for most of its existence.³³⁵ Through a referendum in 1993, Malaŵians voted for a multiparty system and in 1994 Malaŵi had multi-party elections with a new Constitution³³⁶ in place and presidential term that runs for five years with a maximum of two terms.³³⁷ Malaŵi has had only three Presidents since it became independent; Dr. Kamuzu Banda,³³⁸ Dr. Bakili Muluzi³³⁹ and Professor Bingu wa Mutharika.³⁴⁰

During the same time, the RBM has had eleven governors since its inception in 1965.³⁴¹ The average term of a governor since independence is approximately 4.7 years, almost equal to the 5-year post-one-party political cycle.³⁴² The nominal term of the governor is 5 years and the incumbent is eligible for reappointment.³⁴³ The longest serving governor of the RBM was John Tembo³⁴⁴ who served during the one-party era.³⁴⁵ The shortest serving is A.G. Perrin, the first governor who only served a year.³⁴⁶

An examination of the governor turnover rate after the advent of multiparty democracy³⁴⁷ indicates an average drop to 4.5 years.³⁴⁸ An interesting pattern is that there is a change in the governor within a year after every general election in the multiparty era.³⁴⁹ For example, Dr. Mathews Chikaonda replaced Francis

³³⁴ Lodge T, Kadima D & Pottie D (2002) 124.

³³⁵ From 1966 when it became a Republic to 1994. There were minority parties when Malaŵi became Independent in 1964 following the general elections of 1961 but this changed after 1966 and following the (in)famous "cabinet crisis" when Dr. Banda reinforced his reigns on power.

³³⁶ Although the Constitution is designated as a 1994 legislation, the 1994 Constitution was interim and was only made sacrosanct in 1995, the notable removal from it being the senate.

³³⁷ Section 83, The Constitution of the Republic of Malaŵi, 1994.

³³⁸ 1964-1994.

³³⁹ 1994-2004.

³⁴⁰ 2004-present (constitutionally up to 2014).

³⁴¹ See Kalilombe L *Central Bank Governance, Accountability and Independence: The Case of Reserve Bank of Malawi* (unpublished MA thesis, University of Kwazulu-Natal, 2008) (hereafter Kalilombe (2008)) at 40 but add Dr. Perks Ligoya, the current Governor appointed in 2009.

³⁴² Kalilombe (2008) 40.

³⁴³ 'SADC Bankers: Reserve Bank of Malawi' Committee of Central Bank Governors in SADC) available at

[http://www.sadcbankers.org/SADC/SADC.nsf/LADV/E4E3EF0D1F5967B8422576740044D454/\\$File/Malawi-.pdf](http://www.sadcbankers.org/SADC/SADC.nsf/LADV/E4E3EF0D1F5967B8422576740044D454/$File/Malawi-.pdf) (accessed 25 March 2011) (hereafter SADC Bankers: Reserve Bank of Malawi (2011)).

³⁴⁴ (1971-1984) Famous Politician and now Leader of Opposition (one of the oldest serving Members of Parliament). See 'Reserve Bank : About the Reserve Bank of Malawi' available at <http://www.rbm.mw/aboutrbm.aspx> (accessed 25 March 2011).

³⁴⁵ Kalilombe (2008) 40.

³⁴⁶ Kalilombe (2008) 40.

³⁴⁷ Referendum was in 1993 and General Elections were held in 1994.

³⁴⁸ Kalilombe (2008) 40.

³⁴⁹ Kalilombe (2008) 41.

Perekamoyo as governor in 1995 soon after the 1994 elections.³⁵⁰ Dr. Chikaonda was replaced by Dr. Elias Ngalande in 2000 after the 1999 elections whilst Dr. Ngalande himself was replaced by Victor Mbewe in 2005 after the 2004 elections.³⁵¹ Mbewe was replaced by the current Governor, Dr. Perks Ligoya, months after the May 2009 general elections.³⁵² But as Kalilombe cautions,

'care should be taken in interpreting these values because low turnover sometimes may mean lower independence of the Central Bank. A subservient governor may stay in the seat for a longer time if he does what the politicians want him to do'.³⁵³

John Tembo was a long time Banda confidant. It is submitted that Tembo's long survival was exactly because he was part of the MCP structure and represented the executive interest and was therefore seen as subservient.³⁵⁴ The influence of the executive arm (especially the presidency) on the RBM through the appointment of its governor and board is therefore self-evident, especially in the post-one-party era where each presidential term seems to coincide with a new governor of the RBM. Clearly this cannot be a mere coincidence and is reflective of different policy views of not only each president but each term of each presidency. It can therefore be said that from an analysis of the available information, the conclusion could be drawn that currently the job of governor of the RBM is a very precarious one providing no security of tenure.³⁵⁵

- The central bank as regulator and supervisor of financial institutions

The FSL makes the RBM the regulator and the supervisor of financial institutions in Malaŵi. Most of the FSL is new law and the RBM has been in existence since 1965. The RBM may have changed with time, but it is submitted that it has only adapted based on its original mandate. The avalanche of laws comprising the FSL may therefore be too much for the RBM considering that it has a plethora of other principal functions.³⁵⁶

³⁵⁰ Kalilombe (2008) 41.

³⁵¹ Kalilombe (2008) 41.

³⁵² In September 2009, see Gondwe G 'Reserve Bank of Malawi appoints new governor' available at <http://www.bizcommunity.com/Article/415/87/40038.html> (accessed 9 October 2010).

³⁵³ Kalilombe (2008) 20

³⁵⁴ He was still Treasurer-General of the Party!

³⁵⁵ See Appendix E for a complete list of Governors of the RBM and the years served.

³⁵⁶ Actually supervising financial institutions is but one of the 10 principal functions of the RBM – see s 3 RBM Act.

Malaŵi is however not unique in having a central bank as the regulator and supervisor of the financial sector. The Netherlands, Antilles, Singapore and Uruguay are some of the countries with the peculiar regulatory system where the central bank and not a separate agency regulate securities firms and insurance companies as well as banks.³⁵⁷ The fact that it is a rather unique, and in some ways peculiar system means it may not provide the best results and if one looks at the data which reveals that the executive (presidency) has a firm grasp of the central bank through the authority to appoint the governor and the board, then whilst the central bank maybe the *de jure* regulator, the President is the *de facto* regulator and supervisor of financial institutions. This, it is submitted, is a not an ideal situation for financial growth. It is further submitted that that the RBM may not pass an objective test of independence.

- Regulatory structure of the central bank

By law the RBM is the single regulator regulating and supervising all financial sectors including banks, pension services, insurance companies, discount houses and the MSE. To achieve its supervision and regulation, the RBM employs the *silo* matrix³⁵⁸ of financial services regulation and supervision.

The head office of the bank is in the capital city, Lilongwe and the bank has one branch in Blantyre,³⁵⁹ although a second branch is being built in Mzuzu. The head office is charged with all the functions of a central bank.³⁶⁰ The main function of the branch in Blantyre is currency issue and supervision of financial institutions.³⁶¹ All the banks and financial institutions are headquartered in Blantyre although there is a slow trek to the capital.³⁶² This may explain why the Blantyre branch of the RBM was tasked with supervisory powers.

³⁵⁷ Mwenda KK (2006) 53.

³⁵⁸ See Mwenda KK (2006) 6.

³⁵⁹ SADC Bankers: Reserve Bank of Malawi (2011) 98.

³⁶⁰ SADC Bankers: Reserve Bank of Malawi (2011) 98.

³⁶¹ SADC Bankers: Reserve Bank of Malawi (2011) 98.

³⁶² Standard Bank has announced it will move, but it seem the only bank to have thus indicated. About a decade ago, NBS Bank moved to Blantyre to “the Banking Square” which houses most of the headquarters of all the banks in Malaŵi.

The bank has its own budget approved annually by the board³⁶³ but in view of the manner in which the board is appointed, it is submitted that this does not offer the requisite budgetary independence.

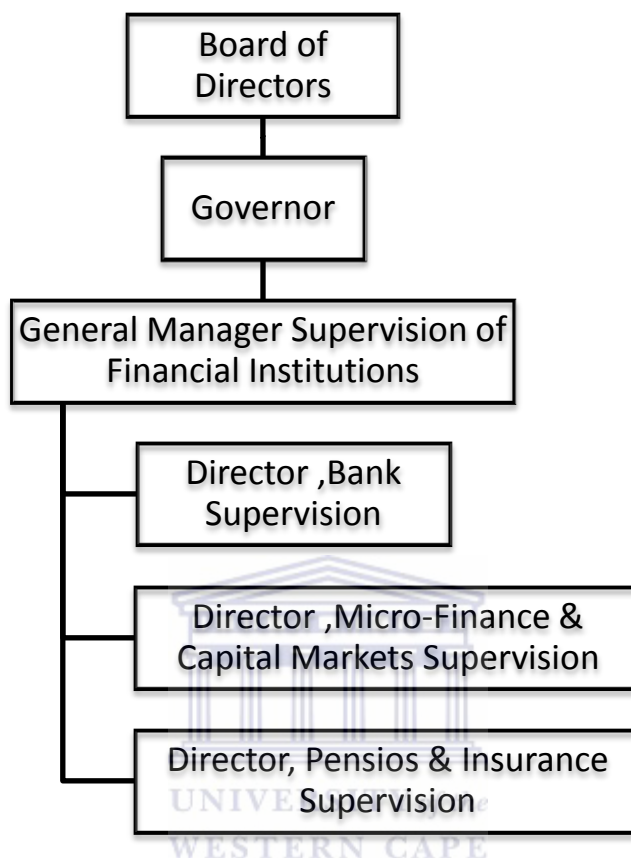


Fig 4. The structure of the RBM as it relates to supervision of financial institutions.³⁶⁴

The RBM operates a rather slim *silo* matrix with only three³⁶⁵ silos;

- bank supervision,
- micro-finance & capital markets supervision, and ;
- pension & insurance supervision.

It is submitted that bank supervision must be construed broadly to include other financial institutions that do not fall in the other two categories. The three directorates in fig 5 below are therefore for all the supervision and regulation falling under their

³⁶³ SADC Bankers: Reserve Bank of Malawi (2011) 97.

³⁶⁴ Extracted from the organisational structure of the RBM.

³⁶⁵ A recent improvement from two in 2009.

directorate (silo). From this slim structure it can be seen that the directorates have a lot on their plate.³⁶⁶

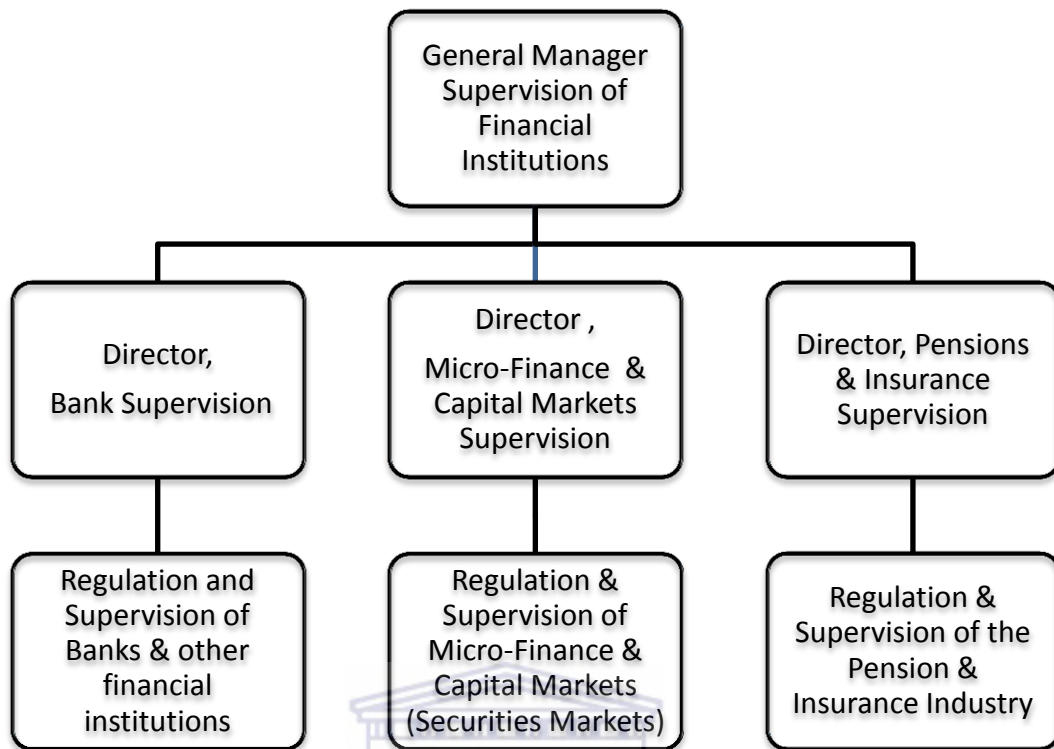


Fig 5. The 3 silos under which regulation and supervision is structured within the RBM.³⁶⁷

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3.2.3. Banking Act 2009 (BA2009)

The BA2009 defines a bank as a person who conducts banking business in Malaŵi and banking business is defined as the business of receiving deposits or deposit substitutes from the public that are payable with or without interest or after the expiry of a stated period or that are transferable by cheque or other means.³⁶⁸ No person³⁶⁹ may operate as a bank without a banking licence granted by the RBM³⁷⁰ and only a licensed bank can advertise that it performs banking services in Malaŵi.³⁷¹ The registrar has the power to require an institution be licensed as a bank if he determines that the institution is in fact engaged in banking business.³⁷²

³⁶⁶ With the passing of The Pensions Bill, the Pension & Insurance Directorate may have resultantly attained further expansive powers.

³⁶⁷ In light of the repeal of the Capital Markets Development Act, it is submitted that the Directorate responsible for Micro-Finance & Capital Markets is also responsible for the Securities Markets.

³⁶⁸ Section 2(1) Banking Act 2009 (hereafter Banking Act).

³⁶⁹ The Registrar shall not license a person as a bank unless the person is a body corporate – s 4(2) Banking Act .

³⁷⁰ Section 2(1) Banking Act. The licence is granted under the Financial Services Act.

³⁷¹ Section 44 Banking Act.

³⁷² Section 4(3) Banking Act.

The BA2009 does not define who the registrar of banks is but provides that words and expression in the act have the meanings ascribed to them in the Financial Services Act 2010 (FSAM).³⁷³ The BA2009 provides requirements and conditions for licensing,³⁷⁴ prudential supervision³⁷⁵ and monetary supervision.³⁷⁶ A rather broadly vague licensing condition is the interest of the national economy and the public interest.³⁷⁷ The prudential supervision is however periodical or at the registrar's discretion.³⁷⁸ The BA2009 also provides for winding³⁷⁹ up of banks over and above any other law.³⁸⁰ The registrar has power to act on troubled banks³⁸¹ including placing them under statutory management³⁸² or even closure.³⁸³ Where a bank is being wound up or liquidated, a court of law shall not entertain any application for a stay of such proceedings unless the application is brought by the registrar,³⁸⁴ who may also be the liquidator.³⁸⁵

3.2.4. The Securities Act 2010 (SA2010)

The SA2010 is the successor to the CMDA and expansively defines securities.³⁸⁶ Securities may be as defined in the statute or as prescribed by the registrar.³⁸⁷ The SA2010 defines the registrar as the registrar of financial

³⁷³ Section 2(3) Banking Act. As will be seen later the Registrar is the Governor of the RBM. The registrar has the statutory authority to supervise banks. Section 14 Banking Act.

³⁷⁴ Part II, including limitation of shareholding [s 6], limitation of controlling more than one bank [s 6(4)] and approval of proposed bank directors [s 5(1)(c)] or their removal or suspension for sufficient cause [s 48(3)(a)(b)].

³⁷⁵ Part III including maintenance of adequate capital – s 10(1).

³⁷⁶ Part V (Such as minimum liquidity reserve requirements). Overall objective is to protect the external value of the Kwacha, monetary equilibrium and other economic objectives – s 38(1)

³⁷⁷ Section 5(1)(j) the Banking Act does not provide for who determines this or how it is determined. It is subjected that this may potentially be abused.

³⁷⁸ S.14(1) Banking Act.

³⁷⁹ The powers of a liquidator are subject to the approval and control of the Registrar but any creditor may apply to the High Court for review with respect to the exercise of those powers – s 30(3)

³⁸⁰ Section 29(1) Banking Act. This is because banks are normally incorporated under other laws such as Companies Act, 1984 (hereafter Companies Act).

³⁸¹ Section 26 Banking Act.

³⁸² If a bank is placed under statutory management, the board of directors stands suspended – s 27(9)(a).

³⁸³ Section 27 Banking Act.

³⁸⁴ Section 30(8). It is submitted that this is discriminatory and may be challenged.

³⁸⁵ See s 32(5) Banking Act. This may not provide the much needed checks and balances and the regulator may become too powerful – see discussion on the regulator having an 'agenda' of his own.

³⁸⁶ Section 2 Securities Act 2010 (hereafter Securities Act) : Securities includes shares, debentures etc and any warrant, right or option or interest in respect of such and any instrument including derivative instrument, contract, profit-sharing agreement, fractional interest, right to subscribe or any instrument commonly known as securities.

³⁸⁷ Section 2 Securities Act.

institutions appointed under the FSAM.³⁸⁸ The registrar is empowered to license and supervise and regulate activities of players in the securities market.³⁸⁹ He has to approve constitutions, charters and articles governing and pertaining to any stock exchange.³⁹⁰ By virtue of succeeding the CMDA, the SA2010 is the legislation under which the Malaŵi Stock Exchange (MSE) now operates.³⁹¹ The SA2010 however makes provision for licensing of more than one stock exchange (apart from the MSE).³⁹² The statute promotes the development of self-regulation by stock exchanges.³⁹³

The SA210 provides that a stock exchange can only exist if it is licensed under the FSAM³⁹⁴ and it is an offence to do otherwise.³⁹⁵ When granting a licence the registrar shall consider if it is in the public interest having regard to the nature of the securities industry.³⁹⁶ Any registered stock exchange shall be managed by a board appointed in accordance with its articles of association.³⁹⁷ The registrar is empowered, in the interest of the investing public, to give directives with respect to trading on the stock exchange generally or with respect to trading in particular securities listed on the stock exchange.³⁹⁸ The registrar also has powers to approve rules of the stock exchange or any amendment thereto³⁹⁹ and even on his own motion to add, amend, delete or nullify rules in the interest of protecting the investors and fair administration of the exchange.⁴⁰⁰ All security brokers, dealers, investment advisors, portfolio managers, securities market intermediaries and securities representatives⁴⁰¹ are

³⁸⁸ Section 2 Securities Act.

³⁸⁹ Section 4(b) Securities Act. The regulation is by means of issuing directives s 4(d) and s 5.

³⁹⁰ Section 4(c). This may look intrusive but a necessary prudent regulation protecting investors.

³⁹¹ Section 9(1) Securities Act.

³⁹² Part III Securities Act especially s 7(1).

³⁹³ Section 4(k) Securities Act. The MSE was formed as a Self-Regulating Organisation (SRO). It is submitted that pursuant to this section, the MSE may not have lost that status.

³⁹⁴ Section 6(1) Securities Act.

³⁹⁵ Section 6(2) Securities Act.

³⁹⁶ Section 7(3)(a) Securities Act however it does not provide for who determines the 'public interest' or how it is determined. It is once again subjected that this may open to be abuse and other political considerations.

³⁹⁷ Section 8(1) Securities Act. The use of 'articles of association' would denote that the stock exchange must be registered as a company under the Companies Act first.

³⁹⁸ Section 11(1)(a) Securities Act. This may indeed be necessary to protect investors in case of a sudden crash of prices in one traded security or across the whole exchange. This includes closing of the stock exchange (only after consultation with the Minister) for the transaction of dealings in securities for such period as may be specified – s 12(1).

³⁹⁹ Section 13(3)(c) Securities Act.

⁴⁰⁰ Section 13(4) Securities Act. This power seems somewhat too wide as it does not provide how the Registrar is really to make this determination and this may be open to arbitrary application.

⁴⁰¹ Who must be an employee of a broker, dealer, investment adviser, portfolio manager or an operator of a collective investment scheme – s 18(3).

required to obtain a licence before operating.⁴⁰² The SA210 also requires that each security be registered by the registrar before it can be traded.⁴⁰³

Unlike the CMDA, the SA2010 has a provision dealing with insider trading.⁴⁰⁴ The SA2010 also seems to attempt to regulate what can be described as legal pyramid schemes⁴⁰⁵ under the umbrella of collective investment schemes.⁴⁰⁶ Reading through the SA2010, it is clear that in Malaŵi trading on the stock exchange can only be done with registered securities and public stock.⁴⁰⁷

3.2.5. Microfinance Act 2010 (MFA2010)⁴⁰⁸

Under the MFA2010, no person can carry on business as a microfinance service provider unless registered or licensed under the FSAM,⁴⁰⁹ however, a licensee may apply to the registrar⁴¹⁰ for approval to offer products and services under the Banking Act, Financial Cooperatives Act or the Insurance Act.⁴¹¹ A microfinance institution shall have as its primary function or business the provision of microfinance services⁴¹² and no more than five percent of the investible funds of a microfinance institution shall be invested in non-financial activities or assets unless permitted by the registrar.⁴¹³

The registrar may determine a threshold in terms of assets or services for a licensed non-deposit taking microfinance institution, as a group or individually, and upon attainment the registrar shall place such an institution under prudential

⁴⁰² Sections 17(1) & 18(1) Securities Act. Operating without a licence amounts to an offence – s 17(2).

⁴⁰³ Section 27(1) Securities Act 2010 excluding Treasury Bills or RBM Bills – s 27(4)(a).

⁴⁰⁴ Section 49 Securities Act. Although in s 5(g) of the Capital Markets Development Act the RBM had the task to prevent unfair trading practices and abuse of inside information.

⁴⁰⁵ As opposed to the get-rich schemes that have been described as illegal. The usage of the term pyramid is actually a misnomer since in collective schemes there is no pyramid structure with a few at the top benefitting from the entry into the scheme of the others.

⁴⁰⁶ Part IX Securities Act.

⁴⁰⁷ Schedule to the Securities Act. The Act however provides for secondary market transactions in securities – item 6 of the Schedule.

⁴⁰⁸ The preamble specifically says ‘an Act to provide for the regulation and supervision of microfinance services...’ Most of the preambles in the other legislation making up the FSL just have ‘an Act to regulate ...’ without including supervision see Banking Act 2009, Securities Act 2010. It would seem that the ‘new’ acts all have regulation & supervision as the purpose – Credit Reference Act 2010, Insurance Act 2009, Financial Security Act 2010.

⁴⁰⁹ Section 5 Microfinance Act 2010 (hereafter Microfinance Act).

⁴¹⁰ The act does not define the registrar but it is submitted that the registrar of other financial services applies *mutatis mutandis*.

⁴¹¹ Section 7 Microfinance Act.

⁴¹² As defined by the Act.

⁴¹³ Section 14 Microfinance Act.

regulation⁴¹⁴ as defined in the FSAM.⁴¹⁵ Only institutions incorporated as a company⁴¹⁶ may be licensed as a deposit-taking microfinance institution.⁴¹⁷ The law also places limitations on institutions. Microfinance institutions are limited to owning shares in any company or enterprise of no more than ten percent of the sum of its capital and reserves⁴¹⁸ and not to grant any credit facility to any debtor in excess of ten percent of its capital⁴¹⁹ or not to have investment in immovable property that in aggregate exceed the sum of its capital and reserves.⁴²⁰

The microfinance register shall be available for inspection by the public at the office of the registrar during working hours.⁴²¹ The registrar may by directives prescribe the composition of the board, frequency of board meetings, rules of appointment, responsibilities and additional qualifications of the directors of microfinance institutions.⁴²² It is submitted that this is very intrusive and not necessary to achieve any prudential regulation.⁴²³ The MFA2010 also requires that the management of any microfinance institution comprise at least a chief executive officer and one senior management officer such as chief financial officer or head of operations.⁴²⁴ It seems strange that the act should designate the positions for institutions, most of which are private and who may opt for their own structure.⁴²⁵ It is therefore submitted that these positions are of guidance, that is.

WESTERN CAPE

⁴¹⁴ A prudential regulated financial institution includes a bank, licensed microfinance institution, securities exchange, securities deposit & broker, insurer & reinsurer credit and savings cooperative, a pension fund & an umbrella fund, a building society, credit reference bureau. Basically the definition covers all the relevant financial institutions plying their trade in the Malawian financial market.

⁴¹⁵ Section 16(1) Microfinance Act. Where this determination is made, the institution is required to be incorporated as a company limited by shares under the Companies Act – s 16(2)(a)

⁴¹⁶ Limited by shares as defined in the Companies Act.

⁴¹⁷ Section 18 Microfinance Act. The registrar shall determine minimum capital or loan fund requirements whichever is applicable, for different categories of microfinance institutions- s 36(1).

⁴¹⁸ Section 39(1)(c) Microfinance Act although this may be waived depending on the nature of business carried on by certain microfinance institutions s 39(2).

⁴¹⁹ Or other such limited as the registrar may prescribe – s 39(1)(a).

⁴²⁰ Section 39(1)(b).

⁴²¹ Section 22(1) Microfinance Act. There is only one problem with this, the RBM is a bank and a very secured one. Entry into it albeit being a bank is very restricted. The author's experience in the course of collecting information for this research is such that the RBM is not the best placed institution for a public inspection. The only consolation maybe that s 22(2) provides the publication through print and electronic media particulars of all registered, licensed and approved persons contained in the register.

⁴²² Section 25(2) Microfinance Act.

⁴²³ The Act goes on to list the (strange) requirement of prior approval for *inter alia* appointment of directors, opening of branch or establishment, restructuring. On the other hand, the other requirements such as going into liquidation, closing a branch or establishment are actually essential – s 26 Microfinance Act.

⁴²⁴ Section 27(1) Microfinance Act.

⁴²⁵ Depending on origin, ownership structure etc.

there must be at least a top officer and one heading finance and another heading operation, regardless of their titles. The requirement for prior approval by the registrar of the appointment of key management officers including the chief executive officer seems intrusive as well.⁴²⁶ It is submitted the registrar should provide guidelines on qualifications and attributes but not approval.

Winding up of non-deposit taking microfinance institutions can only be instituted by the registrar by petition to the High Court.⁴²⁷ For deposit-taking institutions, the rules applying to prudentially-regulated microfinance institutions in the FSAM apply *mutatis mutandis*.⁴²⁸ The MFA2010 has a curious provision regarding regulations. It says the power to make regulations by the minister does not extend to making regulations about a matter in respect of which the registrar may issue directives.⁴²⁹

3.2.6. Insurance Act 2009 (IA2009)

The principal objective of the IA2009 is to make provision for the enhancement of the safety, soundness and prudent management of insurers and other persons involved in the insurance industry in Malawi with the aim of protecting the interests of insurance policyholders and ensuring the highest standard of conduct of business of insurance companies, brokers and agents.⁴³⁰ The IA2009 defers licensing and registration procedures to those of the FSAM.⁴³¹

The registrar of the insurance industry is the registrar of financial services appointed under the FSAM⁴³² but licences the industry pursuant to the IA2009.⁴³³

⁴²⁶ Section 27(3) Microfinance Act. It should be noted that in this subsection, the article used is “the” not “a” for chief executive officer which may denote the top person must be designated as “chief executive officer”. It is submitted though that this need not be the case and “the” should be read as to mean “a”. The requirement in s,28 that persons meet minimum requirement before being appointed as director or in top management is what should have been the only guiding provision in the law for appointments .

⁴²⁷ Section 49 Microfinance Institutions. The section does not properly deal with cases where the need to wind up is by the shareholders (whether voluntary or involuntary liquidation).

⁴²⁸ Section 50 Microfinance Act.

⁴²⁹ Section 56(4) Microfinance Act. Curious because under the Malawian legal system, Ministers are statutorily empowered to make subsidiary regulation and this must be laid down before Parliament and has force of law and to make the registrar directive which is not open to an accountability process as that of a minister almost untouchable seems strange and out of the ordinary.

⁴³⁰ Section 3 Insurance Act 2009 (hereafter Insurance Act). The Act differentiates and defines insurers (and the different types of insurers ; general, life, local, reinsurer) from brokers and agents in s 2.

⁴³¹ Section 5 Insurance Act.

⁴³² Section 2 Insurance Act.

The Registrar may not license a person to carry out both life insurance business and general insurance business. It is submitted that person here should be narrowly construed. For example, in Malaŵi, NICO holdings is the parent company of NICO Life and NICO General insurance 'companies' and if NICO Holdings were to be taken as the person then it would not be possible to have this situation. It is submitted that the corporate veil may need to be lifted here because the intention of the legislature may be circumvented by the creation of subsidiaries and giving them separate legal personality.⁴³⁴

The registrar shall not grant a licence if it is would not be in the interest of the public and policyholders to do so⁴³⁵ and no insurer shall commence his business until the registrar has approved the commencement.⁴³⁶ Insurers (and reinsurers), brokers and agents are all required to be registered and licensed before their can operate their businesses.⁴³⁷ The law states categorically that payment of premiums by policyholders under their insurance to an agent or broker shall be deemed to be specific performance under the policy.⁴³⁸

The law also restricts insurers in the investments that they can undertake. They cannot except with prior written approval of the registrar acquire more than ten percent of the outstanding voting share capital of a body corporate,⁴³⁹ the

⁴³³ See s 8(1).

⁴³⁴ See Annex C. To make matters more interesting, NICO Holdings is the majority shareholder (*de facto* owner) of NBS Bank Ltd, another financial player. To the average person on the street, any attempt to convince them that there are actually 3 entities in NICO (NICO Holding, NICO Life and NICO General) would be met with surprise. This is compounded by s 26 which provides that if a life insurance company holds assets in a holding company, those shares shall be deemed to be held by the insurer as trustee for the benefit of the owners of the policies to which the liabilities relate.

⁴³⁵ Section 9(1) Insurance Act. Strange that policyholders are included in this provision since when the insurer is applying for license there are clearly no policyholders as far as he is concerned. Ss.34(10)(e) and 40(1)(f) provide that an agent or broker shall not conduct their business contrary to the interest of the public in Malaŵi. Once again the Act does not define how this interest of the public is to be ascertained.

⁴³⁶ Section 10 Insurance Act ; meeting of shareholders has been duly held and other legal formalities complied with, insurer has complied with the requirements of the registrar's directives regarding capital and reserves, insurer has entered into a reinsurance agreement with a reinsurer acceptable to the registrar, the insurer has on deposit(sic) an amount acceptable to the registrar, all other provisions of the Act and other relevant financial service laws have been complied with

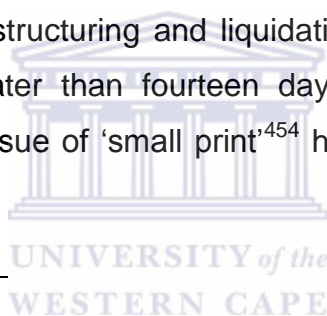
⁴³⁷ See Part II and Part V Insurance Act.

⁴³⁸ Section 46(2) Insurance Act. In Malaŵi Specific Performance is part of contract law and can be enforced or ordered and it is submitted this provision was put to protect policyholders from agents and brokers who never remitted premiums to the insurers. Now the onus shifts to the insurers to ensure they have trustworthy brokers and agents. Clearly this is an application of law of agency that the principal should be bound by the conduct and dealings of his agent.

⁴³⁹ Or 10% of beneficial interest in an unincorporated entity.

aggregate value of all such shares⁴⁴⁰ not to exceed seventy-five percent of the actual liabilities of the insurer or acquire real property or any improvement thereon whose aggregate value is twenty-five percent for life insurers⁴⁴¹ and ten percent for general insurers.⁴⁴² Insurers are also required to have their assets invested in Malaŵi with sufficient regard to the consideration of liquidity, return and security.⁴⁴³ The registrar may prescribe prudential limits for consumer and commercial lending by insurers in proportion to their assets.⁴⁴⁴ No person may acquire a controlling share⁴⁴⁵ in an insurer⁴⁴⁶ without the prior approval of the registrar.⁴⁴⁷ The winding up of an insurer or a broker⁴⁴⁸ shall be according to the Companies Act and the FSAM⁴⁴⁹ but the registrar shall not approve the winding-up until all policyholders are paid or transferred to an alternative insurer.⁴⁵⁰

The law also provides for the prior approval of the registrar for the appointment of executive officers⁴⁵¹ and directors, change in articles of association, opening and closing branches, financial restructuring and liquidation.⁴⁵² Every insurer should by law pay out claims no later than fourteen days after signing a claim of discharge certificate.⁴⁵³ The issue of 'small print'⁴⁵⁴ has also been addressed as



⁴⁴⁰ And beneficial interests.

⁴⁴¹ Of actuarial liabilities.

⁴⁴² Of total assets – s 50 Insurance Act.

⁴⁴³ Section 52 Insurance Act. However this is subject to the articles of association of the insurer and any other reasonable constraints imposed on the insuree by other rules in respect of the manner in which it may invest its assets.

⁴⁴⁴ Section 53 Insurance Act.

⁴⁴⁵ Controlling here means having a significant interest in any class of shares of the insurer.

⁴⁴⁶ Or an entity that holds shares of the insurer.

⁴⁴⁷ Section 55(1) Insurance Act.

⁴⁴⁸ Which are companies within the meaning of the Companies Act.

⁴⁴⁹ Section 57 Insurance Act. This seems to be a departure from the way winding up of other financial institutions is done i.e. banks, microfinance institutions.

⁴⁵⁰ Section 58 Insurance Act. Under a scheme for the transfer or the amalgamation of policyholders in accordance with the provisions of the Financial Services Act.

⁴⁵¹ The law does not specify the positions *cf* with s 27(1) Microfinance Act.

⁴⁵² Section 62 Insurance Act. The criticism against this power by the registrar with regarding to the other financial services law discussed equally applies here so does the need to protect policyholders.

⁴⁵³ Section 65(1) Insurance Act. It would seem 14 days may have been overly ambitious. The author has experience of a claim that took just over a month even after the enactment of this law, and this was quite fast compared to the normal insurance processing rate experience that the author has had before. The fact that the quoted this provision when making a demand for payment clearly played no small part in the fast processing! Therefore the law may have jostled the insurance companies into speedy action but the 14 days may be too short to be fair on them (they have to verify the claim and sometimes use contracted services for this).

⁴⁵⁴ Small print in insurance is usually used to denote the very small print that one cannot read when signing the policy but when the time arises to make a claim against the policy then voila the small print gets magnified and the claim is defeated.

no insurer shall issue a policy in a form whose provisions are not put in a clear type face in letters of uniform size no less than ten points.⁴⁵⁵

3.2.7. The Credit Reference Bureau Act 2010 (CRBA)

This is a new addition to the Malaŵi legal system as there was no regulatory or supervisory statutory framework for credit reference bureau operation. The CRBA defines the registrar as the registrar of financial institutions appointed under the FSAM⁴⁵⁶ and no person shall conduct credit reference bureau business unless licensed under the FSAM.⁴⁵⁷ The law also restricts licences to juristic persons which are limited liability companies.⁴⁵⁸ Public interest is not one of the criteria for licensing a credit reference bureau.⁴⁵⁹

The CRBA is likely to change the facet of credit life of Malaŵians as a credit reference bureau has the statutory authority to collect information on the background and credit history of persons required by it.⁴⁶⁰ This may be welcomed as a positive development by those who want to access credit but also as an intrusion into the right of privacy of others.⁴⁶¹ The bureaus are also likely to face problems as the law require them to collect not only postal but also physical addresses.⁴⁶² Most Malaŵians do not have a physical address⁴⁶³ because most of

⁴⁵⁵ Section 72 Insurance Act. Of course different type face produce different sizes so a ten point in 'Arial' may be different from one in 'Times New Roman' and in 'Lucinda Console' and 'AngsanaUPC' so maybe the issue of small print has not been completely done away with and the only qualification maybe be that it be in 'a clear type face'.

⁴⁵⁶ Section 2 Credit Reference Bureau Act 2010 (hereafter Credit Reference Bureau Act).

⁴⁵⁷ Section 4(1) Credit Reference Bureau Act.

⁴⁵⁸ Section 4(2) Credit Reference Bureau Act. In Malaŵi a company may be incorporated limited by shares or limited by guarantee ss 2, 5(1)(a)(b) Companies Act 1984. The provision does not state which. It may therefore be that even a company limited by guarantee (though not regarded as a company in the business and commercial sense – mostly an easy means of incorporation for most NGOs) may be licensed as credit reference bureau. The Courts may have to give directions on this though as the jurisprudence on this branch of law which is at the starting blocks develops.

⁴⁵⁹ See s 6 Credit reference Bureau Act 2010. This may not be required because of the other requirements i.e. security features to protect the database, background, reputation, integrity, competence and expertise etc. It is submitted that indeed such requirements should be the norm and that the vague notion of 'public interest' should not be in the law, i.e. the requirements should be such that they do take care of the public interest.

⁴⁶⁰ Section 13(1) Credit Reference Bureau Act.

⁴⁶¹ Section 21 of the Constitution provides for the Right to Privacy whilst s 19 provides the right to dignity and personal freedoms. It is submitted that litigation is most likely to follow should a person's credit history be (accidentally or otherwise) become public knowledge since s 5 makes any law inconsistent with provisions of the Constitution invalid to the extent of that inconsistency.

⁴⁶² Section 13(2) Credit Reference Bureau Act.

⁴⁶³ Whilst they may have a place where they physically reside, this place is usually not ascertainable in a definite manner.

the streets are not named and the 'culture' of physical addresses is usually limited to registered entities.

However a credit reference bureau does need prior written approval of the registrar for the appointment of directors and senior management, changes in articles of association, opening⁴⁶⁴ and closing of branches and liquidation.⁴⁶⁵ The CRBA also restricts the power of the minister to make regulations in matters in respect of which the registrar may issue directives.⁴⁶⁶

3.2.8. Building Society Act 1964 (BSA)

This legislation is now of limited application. Malaŵi had for a long time one building society, the New Building Society which later on turned into a bank, NBS Bank.⁴⁶⁷ No new player has really come into the building society market although there have been some endeavours by private entrepreneurs.⁴⁶⁸ Although NBS Bank still operates a 'mortgage' service, this is not under the umbrella of a building society but of a bank. The same facilities are offered by other banks.⁴⁶⁹

The BSA contains however, an anomaly which is inconsistent with the FSL. Under the BSA, the minister is empowered to appoint a public officer to be registrar of building societies⁴⁷⁰ and in pursuance of this power the minister designated the secretary to the treasury⁴⁷¹ as the registrar of building societies.⁴⁷² It is submitted that this provision may have to be amended in light of the current FSL where there is one

⁴⁶⁴ See the criticism regarding this discussed in the earlier sections having similar restrictions

⁴⁶⁵ Section 17 Credit Reference Bureau Act.

⁴⁶⁶ Section 33(2) Credit Reference Bureau Act.

⁴⁶⁷ Owned by NICO Holdings, arguably one of the biggest players in the Malaŵi financial system (owns NICO Life, NICO general and several subsidiaries in other countries).

⁴⁶⁸ For example the Kanengo Northgate Project in the outskirts of the Capital City near the Kamuzu International Airport. Most Malaŵians remember the New Building Society for its reposing and selling of houses than for its provision of loans. The fact that most of the loans became delinquent may be symptomatic of is wrong economic fundamentals applied such as unaffordable interest rates, sometimes on compound basis.

⁴⁶⁹ In fact the vehicle of 'mortgage' has fast been replaced with 'charge' and it is more common to hear of a charge than a mortgage although the terms are interchangeably used. The Act does not define "charge" but employs the term in its provisions.

⁴⁷⁰ Section 5 Building Society Act 1964 (Chap 32:01). (hereafter Building Society Act).

⁴⁷¹ Who sits on the Board of the RBM as an Ex-officio and is mostly the most powerful civil servant next to the Chief Secretary to the President and Cabinet.

⁴⁷² G.N. 111/1965 through subsidiary legislation as the Act did not designate a registrar but provided for registration and functions of a registrar.

registrar for all financial institutions.⁴⁷³ Since in Malaŵi the secretary to the treasury falls directly under the minister of finance, this makes the executive branch the *de facto* and *de jure* registrar of building societies. This is more so because the minister may, if he is satisfied that it is in the public interest so to do to⁴⁷⁴ suspend the registration of new societies either indefinitely or for a stated period and during such period the registrar shall not register any new society and in any particular case direct the registrar that registration of a proposed society shall be refused.⁴⁷⁵

Apart from the FSAM,⁴⁷⁶ the BSA is the only other FSL which contains a personally liable indemnity provision of the registrar and other persons acting under his authority for or in respect of any act or matter done in good faith in the exercise of the powers conferred by the Act.⁴⁷⁷ Under the BSA, the applicant for registration does not have to be a juristic person as any four or more persons⁴⁷⁸ who agree jointly to subscribe to permanent shares of the society to an amount of not less than £20,000 may form a



⁴⁷³ This is an old law that was carried over from the colonial period and is in urgent need of revision. For example any person using the word 'building society' without being registered by the registrar will incur a fine of £500 and £50 for each day for which such contravention continues s 3(3) Building Society Act. Using Pounds Sterling 47 years after Independence is gross!

⁴⁷⁴ By publication in the Gazette. The phrase "if he is satisfied that it is in the public interest so to do to" and "if he finds it reasonable in the public interest to do so" has been hotly debated in view of the recent change of a similar provision but of banning publication in s 46 of the Penal Code in Malaŵi. It is submitted that the latter whilst being contested as impugning upon constitutional freedoms is a better provision as it is subject to judicial review under the *Wednesbury reasonableness* test of administrative law. In *Associated Provincial Picture Houses v Wednesbury Corporation* [1947] 2 All ER 680 CA Lord Greene MR said at 682-3:

'It is true the discretion must be exercised reasonably. Now what does that mean? Lawyers familiar with the phraseology commonly used in relation to exercise of statutory discretions often use the word "unreasonable" in a rather comprehensive sense. It has frequently been used and is frequently used as a general description of the things that must not be done. For instance, a person entrusted with a discretion must, so to speak, direct himself properly in law. He must call his own attention to the matters which he is bound to consider. He must exclude from his consideration matters which are irrelevant to what he has to consider. If he does not obey those rules, he may truly be said, and often is said, to be acting "unreasonably." Similarly, there may be something so absurd that no sensible person could ever dream that it lay within the powers of the authority. Warrington LJ ... gave example of the red-haired teacher, dismissed because she had red hair. That is unreasonable in one sense. In another sense it is taking into consideration extraneous matters. It is so unreasonable that it might almost be described as being done in bad faith; and, in fact, all these things run into one another.'

⁴⁷⁵ Section 8(4)(a)(b) Building Society Act. This seems to be much like absolute discretion and in such a case the 'Wednesbury reasonableness' test would not avail itself to anyone prejudiced by the provision.

⁴⁷⁶ Section 98 Financial Services Act. But in the act the indemnity extends to other financial institutions and their officers in relation to provision of information to the registrar or any person under his authority in compliance with a financial service law unless it is proved that the provision of information was done in bad faith.

⁴⁷⁷ Section 6 Building Society Act.

⁴⁷⁸ Person includes the Government; s 2 Building Society Act.

society by subscribing their names and addresses to rules agreed by them for the government of such society and by obtaining registration under the Act.⁴⁷⁹

Only the registrar may, with the approval of the minister, and in accordance with rules made by the Chief Justice, apply to the High Court for an order for the dissolution of the society.⁴⁸⁰ The registrar is however empowered to order dissolution of the society if satisfied that the society is unable to meet the claims of its depositors, and that it would be for their benefit that it should be dissolved.⁴⁸¹ The BSA does not require approval of the registrar for appointment of directors and leaves this to the members of the society.⁴⁸² Because it also offers legal personality on societies, the BSA contains a lot of administrative and organisational provisions.⁴⁸³

3.2.9. Financial Services Act 2010 (FSAM)⁴⁸⁴

The FSAM is the umbrella legal framework for the supervision and regulation of financial institutions in Malaŵi.⁴⁸⁵ The Act defines a financial institution to include a bank, and institutions defined as such in the Securities Act, Insurance Act, Microfinance Act, Financial Cooperatives Act,⁴⁸⁶ Pension Act,⁴⁸⁷ Credit reference Bureau Act and the Building Society Act.⁴⁸⁸ This definition basically includes any

⁴⁷⁹ Section 8(10) Building Society Act upon the issuance of a certificate by the registrar s 8(5).

Section 11 says upon such registration, the society shall be a body corporate by its registered name with perpetual succession and, subject to the Act, shall be capable of doing all such acts as a body corporate may by law perform.

⁴⁸⁰ Section 14 Building Society Act but dissolution may occur voluntarily under the supervision of the High Court – s 85(1)(b) or by the High Court – s 85(1)(c). It is submitted this leaves the door open for creditors to bring applications for dissolution under s 87(1)(c) and/or the Bankruptcy Act.

⁴⁸¹ Section 91 Building Society Act.

⁴⁸² Section 19 Building Society Act.

⁴⁸³ As would be found in the Companies Act or the Trustees Incorporation Act.

⁴⁸⁴ Section 2 defines the following as forming the Financial Service Law (a) Financial Services Act 2010 (b) The Banking Act 2010 [sic] (c) Building Society Act (d) Insurance Act 2010 [sic] (e) The Pension Act 2010 [sic] (f) The Securities Act 2010 (g) Microfinance Act 2010 (h) The Financial Cooperatives Act 2010 [sic] (i) The Reserve Bank of Malaŵi Act (j) Bill Credit Reference Bureau Act, 2010 (j) a law that declares itself to be a financial service law for purposes of this definition (l) a law prescribed for the purposes of this definition and includes regulations, the registrar's directives and directions. The Pension Bill has just been passed and the Financial cooperatives Bill is yet to be passed.

⁴⁸⁵ Preamble to the Financial Services Act 2010 (hereafter Financial Services Act). Its principal object is ensure (a) safety and soundness, (b) highest standards of conduct of business, (c) fairness, efficiency and orderliness in the financial sector (d) stability of the financial system and (e) reduction and deterrence of financial crime in financial institutions – s 3.

⁴⁸⁶ Although it is stated as an Act in the Financial Services Act, the Financial Cooperatives Bill has just been enacted in 2011.

⁴⁸⁷ Although it is stated as an Act in the Financial Services Act, the Pensions Bill is yet to be enacted according to law.

⁴⁸⁸ Section 2, Financial Services Act, cf s 2, Reserve Bank of Malaŵi Act which is more general

institution⁴⁸⁹ dealing with financial or financial-like services in Malaŵi.⁴⁹⁰ The FSAM defines a controlling party of a financial institution as a director⁴⁹¹ or a person who holds at least ten percent of shares, voting or other rights.⁴⁹²

Under the RBMA, the central bank, is the statutory regulator⁴⁹³ of the financial services sector and the governor of the RBM is the statutory registrar of the financial service sector.⁴⁹⁴ The law states the registrar⁴⁹⁵ shall be supported by adequate structures and employees with appropriate skills to enable him perform the duties of the registrar.⁴⁹⁶ The FSAM in a way gives directions to the *silo* nature of the regulatory framework.⁴⁹⁷ The registrar’s power includes creating appropriate structures and establishing departments to supervise the operations of banking, insurance, pension benefit fund schemes, securities markets entities and other areas deemed necessary.⁴⁹⁸ Schematically this arrangement may be presented as:

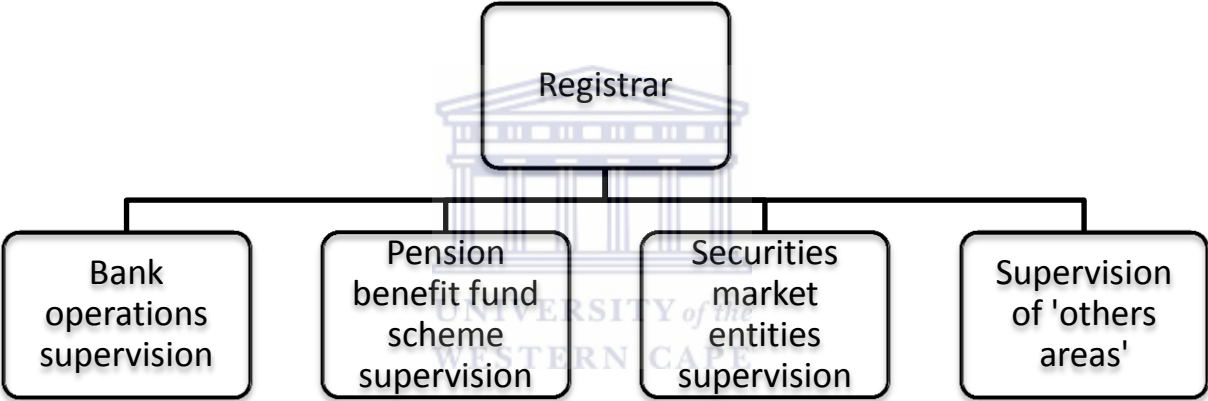


Fig 6. Note how but for the “Others” departments, it closely resembles the existing RBM structure (fig 5). It is submitted that this resemblance is actually by design and the RBM has combined the others into the directorate dealing with microfinance & capital markets.⁴⁹⁹

⁴⁸⁹ Both juristic and natural persons.
⁴⁹⁰ Financial services means services relating to financial matters – s 2 Financial Services Act.
⁴⁹¹ Or anyone with the power to appoint or give consent to the appointment of a director provided that the registrar or the minister shall not be construed as such.
⁴⁹² Section 5(2)(a) Financial Services Act. The other rights are the one which if exercised would result in the person holding at least 10% shares or voting rights -s 5(2)(a)(vi). However the registrar may modify these requirements by directives either generally or in a class of cases – s 5(4) and the registrar may declare in writing that a specified person is or is not a controlling party of a prudentially regulated financial institution – s 5(5).
⁴⁹³ Section 3 The Reserve Bank of Malaŵi Act..
⁴⁹⁴ Section 8(2) Financial Services Act.
⁴⁹⁵ In addition to his other functions, he has the function of advising the minister on matters related to financial institutions and financial services whether on his accord or on the minister’s request – s 9(2). The minister is not defined but it is submitted it is the minister responsible for finance.
⁴⁹⁶ Section 8(3) Financial Services Act. The RBM is also enjoined to support the registrar in carrying out his functions – s 9(1).
⁴⁹⁷ It may well be argued that since the Financial Services Act is a ‘baby’ of the RBM, the law was tailored to fit the structure already in existence.
⁴⁹⁸ Section 8(3) Financial Services Act.
⁴⁹⁹ Clearly the structure takes cognizance of the fact that in Malaŵi there are no longer any building Society to regulate and supervise.

The registrar is empowered to delegate any of his supervisory functions⁵⁰⁰ and it is hereby submitted that in fact the directors in fig 5 have been thus delegated and for all intent and purposes exercise this power for the industry they regulate and supervise.

The FSAM requires all financial institutions wishing to operate as a business to be licensed or registered under it⁵⁰¹ or any other financial service law.⁵⁰² The Act uses the terms license and register interchangeably and does not define them in a way that would distinguish them.⁵⁰³ It is submitted that registered would be the process of being enrolled in the register⁵⁰⁴ whilst licensing pertains to a legal right/authority⁵⁰⁵ to operate. It may however not be inconceivable for both the licence (document) and certificate of registration to be issued and this may happen when the licensing is bound for renewal whilst the registration may be a once off situation.⁵⁰⁶ The registrar is empowered to vary, suspend or revoke licences and registrations upon cause⁵⁰⁷ but this power shall not be exercised before the financial institution has been given an opportunity to make representations thereof.⁵⁰⁸

Under corporate governance, the appointment of directors and all executive officers and managers⁵⁰⁹ of financial institutions is subject to the approval of the registrar.⁵¹⁰

The registrar is empowered to disqualify an executive officer or manager of a

⁵⁰⁰ Section 20(1) Financial Services Act ; but he may not delegate the 'power of delegation'.

⁵⁰¹ Section 21(1)(a) Financial Services Act.

⁵⁰² Section 21(4) Financial Services Act.

⁵⁰³ "Licence" is defined as a licence under the Act or another financial service law and "licensed" means licensed under the Act or under another financial service law whilst "registered" means registered under the Act or under another financial service law – s 2 Financial Services Act. There is no definition for "certificate".

⁵⁰⁴ After fulfilling any prior requirements.

⁵⁰⁵ At the risk of being superfluous, the 'licence'.

⁵⁰⁶ However s 23 says that on an application the registrar may (a) grant a licence (b) register an institution or (c) grant renewal of such licence or registration. The implication of this would be that there is not much difference between the two terms, and yet it must not be so. It is submitted this may have been a drafting problem because a license and a registration are not the same although the Act allows either one of them to operate – see s 21(10)(a).

⁵⁰⁷ Section 27 Financial Services Act.

⁵⁰⁸ Section 27(4). This is in tandem with the *audi alteram partem* rule which literally means 'hear the other party' – a cardinal rule in natural justice theory which has found its way into constitutional and administrative jurisprudence across the world and is a central part of Malaŵian administrative jurisprudence,

⁵⁰⁹ All executive officers and managers of prudentially regulated financial institutions shall be resident in Malaŵi after their appointment – s 30(2).

⁵¹⁰ Sections 29(2) & 30(1) Financial Services Act. It is submitted that although this provision may override the flexibility in the Building Society Act.

prudentially regulated financial institution based on reason and prior notification to the institution.⁵¹¹

Supervision and regulation of financial institutions is principally through directives issued by the registrar⁵¹² but a directive may not be issued unless a draft directive has been brought to the attention of the targeted institutions⁵¹³ or the registrar consider on reasonable grounds that it is necessary to issue the directive urgently.⁵¹⁴ Any urgent directive issued without prior publication shall lapse after ninety days but may be reissued.⁵¹⁵

Apart from directives, the registrar may also give directions to financial institutions including a director, executive officer or manager requiring it to give information to the registrar or publish such information as directed relevant to the performance of the registrar's supervisory functions.⁵¹⁶ But a direction that affects rights of a party may only be issued after the institution has been given notice of the proposed action specifying the grounds for it and facts supporting thereof and allowing the institution⁵¹⁷ to ask for a private hearing.⁵¹⁸ The registrar may upon representations made to it [sic] modify or uphold any direction issued.⁵¹⁹ However, the FSAM does

⁵¹¹ Competence, business record or character, unsuitability to discharge the duties and responsibilities associated with the position – s 31(1). The notification allows the institution to make any representations prior to finalisation of the registrar's decision – s31(2).

⁵¹² Part V Financial Services Act.

⁵¹³ Published in a way that the registrar considers will bring it to the attention of financial institutions to which it will apply.

⁵¹⁴ Section 34(4) Financial Services Act. The employment of 'reasonable' in this provision makes the decision amenable to judicial review under s 108(2) of the Constitution by the High Court on the 'Wednesbury reasonableness' test – on the application of this test on discharge of public authority see *The State v The Chief Secretary to the President; Ex Parte Dr. Bakili Muluzi*, Misc. Civil Application No 3 of 2011 (HC) Mzuzu Registry (unreported) where at 5 Chikopa J deals with the question '[i]s the decision unreasonableness in the Wednesbury sense?'

⁵¹⁵ Section 34(5) Financial Services Act.

⁵¹⁶ Section 35 Financial Services Act and also auditor, actuary or other related party. The Act does not define what a directive and what a direction is and both have force of law (s 2) but it is submitted a directive has more force than a direction although this may not always be the case. However s 39(1) gives credence to the argument that directions are more or less correctional in nature while directives may be viewed, without sounding harsh, as decrees. However directions may also require an institutions not only to correct but do some positive act, albeit some seen as intrusive, such as removal an auditor or actuary [s 39(2)(e)], not to borrow a specified amount [s 39(2)(f)] not pay dividend [s 39(2)(g)] remove or suspend any person including a director [s 39(2)(k)].

⁵¹⁷ And person if need be.

⁵¹⁸ Section 39(5) Financial Services Act.

⁵¹⁹ Section 39(6) Financial Services Act. The section gives an underlying direction to comply with the direction of the registrar despite anything in the institution's memorandum or articles of association or regulations and despite any contract or arrangement to which it is a party – s 39(7). This prima

have a strange provision that any such issued direction shall not be ground for termination, repudiation or cancellation of a contract and a court may on application by a party make an order relating to the effect of the direction on the contract provided that such order may not require a person to take action that would contravene the direction.⁵²⁰ It is submitted this is untenable as it purports to uplift the direction of a registrar above the authority of the court and in the process oust the jurisdiction of the court which by law must make an order as it sees fit in the interest of justice, considering that the direction may indeed force a party to cancel, repudiate or terminate a contract.⁵²¹

The registrar may by instrument in writing appoint examiners and investigators.⁵²² An examiner examines the affairs or any part of the institution to ensure compliance whilst an investigator is appointed where the registrar has reasonable grounds to believe that an offence has been committed, or there is no compliance or an institution is involved in financial crime.⁵²³ Such investigators or examiners shall have all the powers and protections of a commissioner under the Commissions of Inquiry Act,⁵²⁴ on top of the indemnity they have under the FSAM.⁵²⁵

For self-regulatory organisations⁵²⁶ (SROs) like the Malaŵi Stock Exchange, its rules shall not be inconsistent with the FSL with respect to matters where the SRO has supervisory functions⁵²⁷ but any such rules and amendments thereto shall be of no effect unless approved by the registrar.⁵²⁸ An SRO shall also not amend its memorandum or articles of association or other constituent documents unless

facie will have far reaching consequences as the registrar may be accused of micromanagement of institutions and interference i.e. the tort of induced breach of contract.

⁵²⁰ Section 40 Financial Services Act.

⁵²¹ In Malaŵi the doctrine of separation of powers is a Constitutional one and s 9 of the Constitution says the judiciary shall have the responsibility of interpreting, protecting and enforcing this Constitution and all laws and in accordance with this Constitution in an independent and impartial manner with regard only to legally relevant facts and the prescriptions of law. S.8 deals with the executive (under who the registrar falls) and the executive is responsible for the initiation of policies and legislation and for the implementation of all laws which embody the of the executive express wishes of the people of Malaŵi and which promote the principles of this Constitution.

⁵²² Sections 41(1) & 42(1) Financial Service Act.

⁵²³ Sections 41(2) & 42(1)(a)(b)(c) Such examination and investigation involving visiting and entering into the premises of the financial institution – ss 41(3)(a) & 42(3)(a).

⁵²⁴ Section 43 Financial Services Act [referring to the Commissions of Inquiry Act (Chap 18:01, Laws of Malaŵi)].

⁵²⁵ Section 98.

⁵²⁶ Hereafter in the text referred to as SRO(s).

⁵²⁷ This denotes statutory delegation of supervisory authority to SROs.

⁵²⁸ Section 46 Financial Services Act.

approved by the registrar, notwithstanding any provisions in the Companies Act.⁵²⁹ The FSAM also provides an SRO, its employees and members indemnity for any loss sustained or damage caused to any person for *bona fide* acts done by them.⁵³⁰ Under the FSAM, there is a forty-nine percent cap on shareholding by any one person or entity in a prudentially regulated institution.⁵³¹

Price fixing and price arrangement of financial service products may be prohibited if it is unfair to consumers, will tend to reduce competition, will result in exploitation of consumers or is otherwise undesirable.⁵³² The registrar has to give prior approval for all compromises, arrangements and transfers of business of financial institutions without which the court shall make no order approving and such arrangements.⁵³³

The registrar may place a prudentially regulated financial institution under statutory management on its own request or if it is not complying with the FSL, is financially unsound,⁵³⁴ involved in financial crime,⁵³⁵ refusing to submit itself to inspection by the registrar or has had its licence suspended or revoked.⁵³⁶ The purpose of this is to protect the interest of clients; stability, fairness and orderliness of the system as well as safety and soundness of financial institutions (avoid contagion).⁵³⁷ Where any such institution is placed under statutory management, the registrar or any other person appointed by him⁵³⁸ shall be the statutory manager.⁵³⁹ The public shall

⁵²⁹ Section 50 Financial Services Act.

⁵³⁰ Section 51 Financial Services Act.

⁵³¹ Section 53 Financial Services Act. If on the commencement of the Act any institution does not meet this requirement it must within 6 months of operation of the law provide a credible plan to the registrar on how it will achieve this over a period not exceeding 5 years. The author, being a shareholder of a financial institution has had an experience where the majority holder vetoed any resolution and carried the day, including awarding themselves as a board exceeding high perks when the company is not doing well. This provision will surely put such abuse to a stop.

⁵³² Section 63 Financial Services Act. Most of the financial institutions have associations i.e. Bankers Association of Malaŵi, Insurance Association of Malaŵi, Dealers Association of Malaŵi and usually when prices are announced for their products (be it interest rates of other costs), all the players in the industry will usually announce at the same time and adjust by the same margin to the same amounts. It is submitted that there is actually collusion amongst the various players to the detriment of consumers and it is hoped this provision can be enforced for consumer good.

⁵³³ Part VIII Financial Services Act. It is submitted that the criticism earlier on laid about the attempt to limit the jurisdiction of the Court applies here and this provision may need to be seen through the Constitutional prism under which the judiciary is enacted.

⁵³⁴ including engaging itself in unsafe and unsound financial practices.

⁵³⁵ The Finance Bank of Malaŵi was placed under statutory management because it was suspected of having not complied with the financial service law with elements of financial crime.

⁵³⁶ Section 68(2)(a) Financial Services Act.

⁵³⁷ Section 68(2)(b) Financial Services Act.

⁵³⁸ Mr Neil Nyirongo, a former Deputy General Manager (and later Executive Director of Economic Services) at the Reserve Bank, was made Statutory Manager of the embattled Finance Bank of Malaŵi and served as Curator and Caretaker Chief Executive Officer. See ZoomInfo available at

immediately be informed by the registrar of the placing of any institution under statutory management.⁵⁴⁰ The statutory manager shall have the management of affairs of the institution to the exclusion of its directors and other managers.⁵⁴¹

The task of the statutory manager is to manage the affairs of the institution with the greatest economy possible compatible with efficiency and as soon as practicable report to the registrar what steps need to be taken at the institution to 'correct' things up or if not practicable whether to transfer the business or to wind it up.⁵⁴² It can therefore be inferred that although the law says the registrar may be the statutory manager, the law does not really envisage this situation as it would lead to an absurdity from a reporting perspective.⁵⁴³ The statutory manager is also not an independent manager in his own right as he has to comply with written directions from the registrar in relation to his functions.⁵⁴⁴ It is submitted that once a statutory manager has been appointed, the process will actually lead to clientele flight, lack of trust and most likely than not liquidation will be the end result.⁵⁴⁵

A resolution to wind-up a prudentially regulated financial institution shall be of no effect unless approved by the registrar and an application to the court for an order to wind-up a prudentially regulated financial institution may only be made by the registrar or with his approval.⁵⁴⁶ It is argued that this provision as far as it purports to limit the court in hearing applications is open to legal challenge.⁵⁴⁷ If the institution is

<http://www.zoominfo.com/search#search/profile/person?personId=396208502&targetid=profile> and Mireles I 'Malawi' available at <http://fic.wharton.upenn.edu/fic/africa/Malawi%20Final.pdf> (both accessed 8 April 2011).

⁵³⁹ Section 68(3) Financial Services Act. On the drastic effects of statutory management to the customer base at Financial Bank, see Namwaza G 'Scores ticked off at forex scarcity at FINBANK' *The Daily Times* 29 September 2005 available at <http://groups.yahoo.com/group/MALAWIANA/message/4957> (accessed 8 April 2011).

⁵⁴⁰ Section 68(5) Financial Services Act.

⁵⁴¹ Section 69(2)(a) Financial Services Act.

⁵⁴² Section 69(4) Financial Services Act.

⁵⁴³ This demonstrates in the author's view that the drafters of the law did not fully apply their mind to the functions of a statutory manager.

⁵⁴⁴ Section 69(7) Financial Services Act. Although he can apply to the Court for directions, [s 69(8)] this may not in actual place happened because of his 'subservient' nature and the question is whether he can challenge the registrar's directions in court considering that he may be removed at any time (for no reason) by the registrar –s 69(8).

⁵⁴⁵ This is exactly what happened in Finance Bank of Malaŵi.

⁵⁴⁶ Section 72 Financial Services Act.

⁵⁴⁷ Especially where it also states that the winding up shall be on such terms and conditions as the registrar may determine – s 72(3). This is language that is reserved for the courts after weighing all the circumstances of the case and deciding it in the interest of justice.

to be wound up, the registrar (again!) or any other person appointed or approved⁵⁴⁸ by the registrar shall be the liquidator.⁵⁴⁹

The registrar's decisions are however subject to review⁵⁵⁰ by the financial services appeal committee (FSAC).⁵⁵¹ Membership of the FSAC comprises three persons appointed by the minister, one of whom shall be designated as chairperson, who have at least ten years experience as legal practitioners⁵⁵² or has the same number of years experience in the financial services industry who shall hold office for three years, subject to re-election.⁵⁵³ An application for review shall act as an automatic stay of any decision unless altered, set aside or replaced by the FSAC or where the parties have consented but with the consent of the FSAC.⁵⁵⁴ Parties to review proceedings are entitled to legal representation but the registrar shall be entitled as of right to be a party.⁵⁵⁵ The chairperson of the FSAC has the power to vary or revoke a direction.⁵⁵⁶ It is submitted that this power should not have been given to the chairperson but to the FSAC itself. Decisions of the FSAC⁵⁵⁷ shall be in writing and shall include the reasons, a statement of its findings and a reference to the evidence forming the basis of the finding.⁵⁵⁸

It is yet to be seen how the FSAC operates in practice because of the very important position that the registrar holds, as governor of the central bank. Furthermore there is a presumption in favour of the registrar's decision. The law says unless the decision of the registrar is not supported by reasonable evidence, the evidence shall be affirmed.⁵⁵⁹

⁵⁴⁸ Where you have a Court ordered liquidation, this power is supposed to be exercised by the Courts.

⁵⁴⁹ Section 73(6) Financial Services Act and the liquidator is first in ranking of claims –s 73(6)(a).

⁵⁵⁰ Section 82 employs the word appeals though so it would seem the Committee has both review and appellate jurisdiction.

⁵⁵¹ Section 78(1)(a) Financial Services Act. Costs will follow the event – s 78(3). The Financial Services Appeal Committee is hereafter in the text referred to as FSAC.

⁵⁵² In Malaŵi legal practitioner is a term that denotes that one has been admitted to the bar. Malaŵi does not have solicitors or barristers. The year requirement is surprising but not extraordinary as it is the same requirement before one can be appointed to judgeship of the High Court. It may well be that the intention is to create a quasi-judicial review body with equally well versed practitioners (either as lawyers or financial service experts) as members.

⁵⁵³ Section 79 Financial Services Act.

⁵⁵⁴ Section 83 Financial Services Act. See also s 88 on the powers of the Appeals Committee.

⁵⁵⁵ Section 84(2)(3) Financial Services Act.

⁵⁵⁶ Section 85(3) Financial Services Act.

⁵⁵⁷ By majority – s 88(2) Financial Services Act.

⁵⁵⁸ Section 91(1) Financial Services Act. It would appeal from this that the decision would be akin to a well reasoned judgement.

⁵⁵⁹ Section 91(5) Financial Services Act.

The law also limits to appeals from the FASC to the court to only questions of law⁵⁶⁰ but in a somewhat contradictory provision states the court may hear and determine such appeals and make such order as it thinks fit to dispose of the appeal.⁵⁶¹

All financial institutions in Malaŵi are required to conduct a customer due diligence and report promptly to the Financial Intelligence Unit suspected money laundering activity related to any client or customer or any suspected illegal dealings inside or outside of Malaŵi.⁵⁶² In its conclusion, the FSAM states that where a body corporate has committed an offence against the FSL, each director, employee or agent of the body shall (equally) be guilty of the offence and on conviction be liable to the same penalty unless established that he took reasonable precautions and exercised due diligence to avoid commission of the offence.⁵⁶³ It is submitted this is grossly unfair especially to mere employees, and it is open for legal challenge because of the manner in which it is framed.



Conclusion

Although Malaŵi has been independent for 47 years, it still remains a LDC and poverty is a key challenge. The financial sector is not very well developed and reflects Malaŵi's size and economy. Banking dominates the financial sector and the stock exchange is illiquid. In summary the financial sector is still at a rudimentary stage with low public confidence.

⁵⁶⁰ Section 92(1) Financial Services Act.

⁵⁶¹ Section 92(3). In *Emison Phiri v Illovo Sugar* Civil Appeal No 36 of 2008 (HC) the question was whether the Court should hear an appeal based on facts when the s 65 of the Labour Relations Act (LRA) provides appeals only on points of law. Madise J held citing the Constitution that the High Court has unlimited original jurisdiction to hear and determine any civil or criminal proceeding under any law. He said s 65 of the LRA tends to usurp the powers of the High Court to hear appeals from the IRC on matters of fact, in essence making the Industrial Relations Court (IRC) the final and binding arbiter. By making IRC to be the final arbiter in respect of matters of fact is tantamount to creating a tribunal which has concurrent jurisdiction with the High Court and the Supreme Court. He stated clearly that s 103 (3) of the Constitution does not allow this '[t]here shall be no courts established of superior or concurrent jurisdiction with the Supreme Court of Appeal or High Court.' Lastly he said s 65 of the said Act is premised on the dangerous assumption that the IRC is immune from making errors of fact which is not so. It is therefore submitted that this provision may be challenged and considered impugning upon s 103(3) in the same manner.

⁵⁶² Section 100(1) Financial Services Act.

⁵⁶³ Section 112 Financial Services Act.

This chapter has discussed the legal and institutional regulatory and supervisory framework currently operating in Malaŵi. The detailed discussion was important in order to bring to the fore the massive burden that the registrar of financial institutions has. An overview of the political economy under which the central bank operates was also done to illustrate the extent of the 'executive clutches'.

The chapter made a brief exposé of the statutes that comprises the FSL.⁵⁶⁴ The FSL in Malaŵi is under the umbrella of the FSAM but contains many statutes, most of which have been enacted in the last 2 years. The effect of these pieces of legislation on conduct of business is likely to be felt in later years but it signals an intention by Malaŵi to properly regulate its financial sector. The chapter analysed the regulatory structure of the RBM and noted how it closely resembles the structure in the FSAM and concluded that this is by design. It has been observed that the RBM employs a narrow *silo* regulatory and supervisory model. However in practice this work is done by directorates in the central bank.

In a critical analysis of each of the financial service laws, the chapter also drew out some of the potential problems that the current legal, institutional and operational framework is likely to face, especially in view of constitutional supremacy and how the courts have tended to jealously guard any attempt to whittle down, oust or usurp their jurisdiction.

Under the FSAM the registrar has expansive powers to issue directives and directions as well as penalties. Decisions of the registrar are amenable to appeal to the FSAC and further, on points of law, to the (High) Court. In analysing the FSL, the chapter concluded that the law seems to have simply built up an 'inverted pyramid' as it has maintained the same institutional regulatory framework which has been there since independence. It has still retained the central bank as regulator of the financial service industry with its governor as the registrar.⁵⁶⁵ In view of the manner in which the governor and the board of the RBM are appointed, this raises issues of *regulatory, operational, budgetary and institutional* independence.

⁵⁶⁴ Except for Acts that have newly been enacted which were not available.

⁵⁶⁵ Except for the anomaly in Building Society Act.

CHAPTER FOUR

4. Framework for a New Financial Regulatory System for Malaŵi.

Nkowani said when looking at revisiting the regulatory framework for financial institutions in Malaŵi, there is need to consider developments that have taken place in the industry since the laws regulating the industry were first enacted.⁵⁶⁶ He admits that the infrastructure under the present framework is not well suited to developments of the years hence the need to align it to reflect these changes.⁵⁶⁷

Malaŵi has enacted some new legislation in the financial sector⁵⁶⁸ but as was seen in the previous chapter, this has not resulted in the expected realignment. Furthermore as Mwenda stated, it is important to determine the size and structure of the industry, the role of the regulator as well as take consideration of economic, political, legal and historical consideration when designed a regulatory framework.⁵⁶⁹

One thing that comes out clearly in chapter three is that the registrar of financial institutions is a very busy person. He has to regulate over a very wide range of services as well as undertake statutory management if need be.⁵⁷⁰ The current structure also presents itself susceptible to political machinations and this is not only from a historical perspective but has also been legally entrenched in the statutes.⁵⁷¹

Looking at the models of financial services regulation discussed in chapter two and the prevailing statutory and regulatory framework in Malaŵi discussed in chapter three, three models are proposed:

⁵⁶⁶ Nkowani Z 'Supervision of banks and financial institutions in Malawi' (2008) *MLJ* 49 at 54 (hereafter Nkowani Z (2008)).

⁵⁶⁷ Nkowani Z (2008) 54.

⁵⁶⁸ Mostly within the period 2009-2011.

⁵⁶⁹ Mwenda KK (2006) 6.

⁵⁷⁰ Including managing any liquidation processes.

⁵⁷¹ Such as giving the President the exclusive power to appoint the governor of the Reserve Bank of Malawi (RBM) who is the regulator as well as the RBM's Board.

4.1. Unified Financial Services Regulator (UFSR)

The current regulatory framework as represented in fig 5 above illustrates that Malaŵi uses the single peak unified regulator. When compared to the models discussed in chapter two, it would seem that this closely resembles the Financial Service Authority (FSA) of the UK except that in the case of Malaŵi the regulator is part of another structure and is not ‘the structure’. The following diagram illustrates a proposed UFSR:

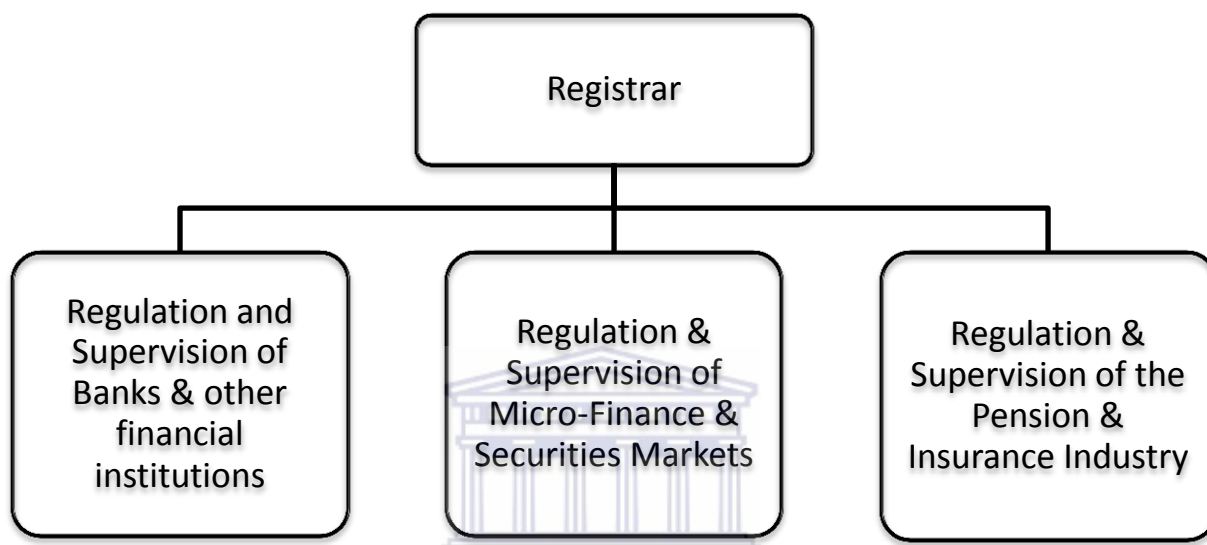


Fig 7. Proposed structure of a Unified Financial Services regulator.

To be independent, this structure needs to be rooted out of the Reserve Bank of Malaŵi (RBM) and become an independent self- standing agency. The legislative framework can then be amended to effect this ‘transplantation’ and also provide for the appointment of a supervising board to oversee the operations. To achieve this, the following must be considered:

4.1.1. Regulatory independence

The law already gives the regulator wide autonomy in regulating the financial sector.⁵⁷² The regulator also already has ample discretion to set and change regulations within the financial services law (FSL). It is therefore submitted that the current legislative framework does provide for regulatory independence under this model.

⁵⁷² The Financial Services Act 2010 and other financial services laws.

4.1.2. Supervisory independence

The current framework does provide for some supervisory independence⁵⁷³ subject to the executive's exclusive power of appointment. It is therefore submitted that under the UFSR, supervisory independence may in reality be achieved because of an independent governance structure. It is further proposed that supervisors⁵⁷⁴ be adequately compensated and these perks be such that they can attract and keep competent staff and avoid bribery and corruption.⁵⁷⁵ The current statutory framework giving the regulator sole authority to grant and withdraw licences is well suited to achieve supervisory independence.⁵⁷⁶

4.1.3. Institutional independence

To create institutional independence, the UFSR needs to be an agency that is at arm's length reach of the executive and legislative branches of government.⁵⁷⁷ This does not only entail having the UFSR as a separate agency, but senior personnel should enjoy security of tenure and clear rules must be laid down governing their appointment and especially dismissal.⁵⁷⁸ It is proposed that appointments to senior positions be made by an independent board and membership of this board be on a representative basis.⁵⁷⁹

4.1.4. Budgetary independence

The UFSR may require seed money from the state to start and run and this may be so for a few years before it is self-sustaining. It is therefore proposed that the proposed board of the agency approves the budgetary needs and the regulator be allowed to justify its budget before to Parliament.⁵⁸⁰ This would prevent unnecessary executive interference as opposed to the agency's budget being tabled as an appendage to the executive's. It is however proposed that the regulator would need

⁵⁷³ Such as authority to investigate and visit institutions and revoke licences as well as indemnifying them – s 98 Financial Services Act.

⁵⁷⁴ Indeed all officers of the UFSR

⁵⁷⁵ Quintyn M & Taylor MW 'Should Financial Sector Regulators be Independent?' *IMF Economic Issues* No 32, 2004 (hereafter Quintyn M & Taylor MW (2004)).

⁵⁷⁶ Except for the curious case of the Building Society Act [Chap 32:01] which gives the Minister veto powers over licences - s 8(4)(a)(b) Building Society Act .

⁵⁷⁷ Mwenda KK (2006) 26.

⁵⁷⁸ Quintyn M & Taylor MW (2004).

⁵⁷⁹ Representative of the stakeholders. This is not a new phenomenon in Malaŵi. The Technical, Entrepreneurial and Vocational Education and Training Authority (TEVETA) Act 1999 & the Malaŵi Communications Regulatory Authority (MACRA) Act 1994 provide for this representative appointment in the boards. MACRA is the Communications regulator whilst TEVETA regulates and oversees technical and vocational training in Malaŵi.

⁵⁸⁰ Other governance institutions such as the Anti Corruption Bureau enjoy this budgetary independence in Malaŵi.

to put in place strategies of ensuring the collection fees from the industry for its services to become self-sustaining. The current FSL already allows the registrar to do this and there would be no need for statutory changes to effect this. In fact the law presumes that the regulator may operate on fees charged for his services.⁵⁸¹ However, there is need to ensure that this does not lead to “industry capture” and this can be achieved through a transparent governance structure.⁵⁸² The example of the self-sustaining Malaŵi Communications Regulatory Authority⁵⁸³ may be emulated and can counter the fear of the regulator strapped for funds.⁵⁸⁴ The current framework allows senior staff to recruit subordinate staff.⁵⁸⁵

Summary

The current framework provides regulatory independence for a UFSR. To achieve true supervisory independence, the exclusive authority of the President to appoint the registrar⁵⁸⁶ would have to be removed and assigned to a transparent representative board. The current framework already provides the regulator with the authority to grant and withdraw licences.⁵⁸⁷ The UFSR staff will have to be adequately compensated in order to attract and keep competent staff and avoid bribery and corruption. To achieve institutional independence would require setting up the UFSR as a separate agency with an independent representative board as part of its governance structure. Senior staff must be appointed by this board and enjoy security of tenure. Finally the UFSR must be able to formulate and justify its budget through the regulator and where state funding is provided, the regulator should justify his budget to parliament.⁵⁸⁸

⁵⁸¹ But it must be noted that there is an implied reliance on the basic structure of the RBM supporting the registrar - s 8(3) Financial Services Act. The RBM is also enjoined to support the registrar in carrying out his functions – s 9(1).

⁵⁸² See Quintyn M & Taylor MW (2004) and Mwenda KK (2006) 33.

⁵⁸³ The MACRA is perceived to be a very rich organisation in Malaŵi, and it does act so!

⁵⁸⁴ Quintyn M & Taylor MW(2004). It is submitted that the financial sector in Malaŵi is ‘bigger’ and more profitable than the communications industry which has few players; the key lies in the proper fees structure.

⁵⁸⁵ Section 11 Reserve Bank of Malaŵi (RBM) Act.

⁵⁸⁶ Although under the law the registrar is not directly appointed by the President ; by law the governor who is the registrar is appointed by the President – s 11 RBM Act.

⁵⁸⁷ Except the case of Building Society Act discussed above.

⁵⁸⁸ Based on the MACRA ‘success’ story, the financial sector in Malaŵi is capable of supporting the budgetary requirements of the UFSR but suffice to say that although MACRA is seen as financially self-sustaining, questions arise as to whether it is an independent institution.

To achieve this will model require some statutory amendments as well as major institutional setup and changes. However, a more important requirement will be a change of culture⁵⁸⁹ and a lot of political will.⁵⁹⁰

4.2. Triple Peak Financial Services Regulatory System (TPFSRS)

As discussed in chapter three, although the regulatory framework is structurally represented in fig 5 above, the practical framework is that the three directors are the *de facto* regulators.⁵⁹¹ The TPFSRS is premised on making these directorates independent regulatory agencies. When compared to the models discussed in chapter two, it would seem that this bears some resemblance to the twin peak model employed in Zambia.⁵⁹² The following diagram illustrates a proposed TPFSRS:

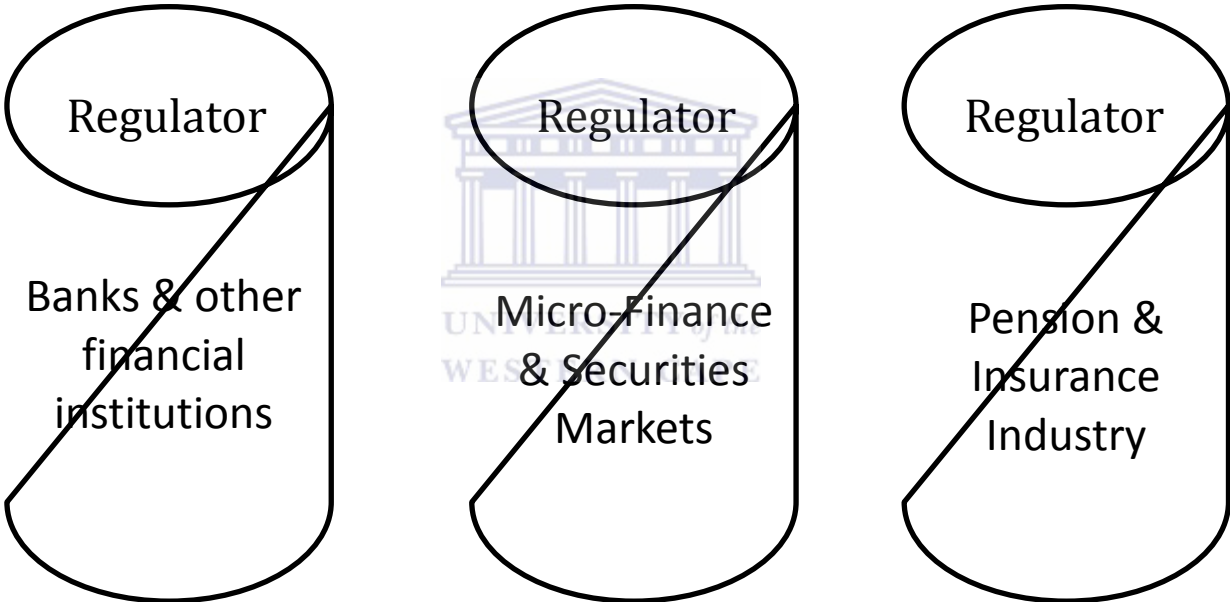


Fig 8. Proposed structure of a Triple Peak Financial Services Regulatory System.

Like the UFSR, to be independent, the TPFSRS structure needs to be rooted out of the RBM and become independent agencies. This will require a great deal more legislative amendment as the current statutory structure concentrates all regulatory

⁵⁸⁹ The change will mainly involve the fact that there has been the ‘transplantation’ otherwise the structure would be much similar to what is currently in the RBM but this time operating as a separate agency.

⁵⁹⁰ Political will as used in this context is in the broader context and includes politicians, the executive, the legislature, business captains and the governance structure within the RBM.

⁵⁹¹ Of the industry that falls under them.

⁵⁹² But not exactly because the Bank of Zambia regulates the banks (and other financial institutions) whilst the Pensions and Insurance Regulator is the other one – see Mwenda KK (2006) 46.

and supervisory powers in the regulator of financial services.⁵⁹³ However, most of the laws regulating the financial services⁵⁹⁴ do provide for a registrar of that industry and what may be required is an amendment that devolves the concentrated power to the three agencies.

It is proposed further that to ensure that there is coordination in the financial services, taking into consideration the current status of the financial system,⁵⁹⁵ the three agencies must work together under a common board of directors, say a board of financial service regulation (BFSR). The duties of the BFSR would be to oversee operations of the three agencies from a macro level.⁵⁹⁶ The BFSR would be a transparent body composed of industry level representation⁵⁹⁷ and independent to prevent executive 'hijack'.⁵⁹⁸ Each of the agencies would have its own autonomous local board but the BFSR would be for policy formulation and regulating for the whole financial sector.

4.2.1. Regulatory independence

Like the UFSR, the law already gives the regulator wide autonomy in regulating the different industries.⁵⁹⁹ The regulator also already has ample discretion to set and change regulations within the regulated industry. It is therefore submitted that, subject to minor amendments,⁶⁰⁰ the current legislative framework does provide for regulatory independence under this model.

4.2.2. Supervisory independence

Similarly to the situation under UFSR above, the current framework does provide for some supervisory independence⁶⁰¹ under the TPFSSRS but it is proposed that the powers specifically provided for in the Financial Services Act 2010 (FSAM), such as examination and investigation need to be devolved and be included in the respective

⁵⁹³ The RBM.

⁵⁹⁴ Insurance Act, Banking Act etc.

⁵⁹⁵ Still rudimentary and dominated by banking,

⁵⁹⁶ But leaving micro management to boards of each agency.

⁵⁹⁷ In this case of the financial service.

⁵⁹⁸ Or even 'sectoral' hijack.

⁵⁹⁹ The Financial Services Act and other financial services laws.

⁶⁰⁰ Devolving the power of the registrar including the issuance of directives – see s 34 Financial Services Act.

⁶⁰¹ Such as authority to investigate and visit institutions and revoke licences as well as indemnifying them – s 98 Financial Services Act.

legislation regulating each of the three silos.⁶⁰² It is further proposed that each regulator be accountable to a representative board. The BFSR will therefore be tasked with oversight of the three agencies.⁶⁰³ The agencies must be able to attract and retain competent staff and offer enough perks to avoid bribery and corruption. Because the most likely scenario would involve a ‘transplantation’ of staff,⁶⁰⁴ the issue of uniformity of perks amongst the three agencies may have to be addressed, especially considering the unequal ‘wealth distribution’ amongst the regulated industries.⁶⁰⁵

The current statutory framework in each of the legislation giving the regulator sole authority to grant and withdraw licences is well suited to achieve supervisory independence for each agency but where the law grants this authority to the registrar of financial services, this power may have to be devolved.

4.2.3. Institutional independence

The TPFSSRS clearly is premised on three separate agencies. Compared to the UFSR, it may be argued that the TPFSSRS provides more independence because of its ‘multiplicity effect’ and may provide better arms length reach from the executive and legislative branches of government. Like UFSR, senior personnel should enjoy security of tenure and clear rules must be laid down governing their employment. It is similarly proposed that appointments to senior positions of each agency be made by an independent representative board of the regulated industry.

4.2.4. Budgetary independence

Because of the ‘fragmentation effect’, the TPFSSRS may require much more resources and on a longer basis before each agency can attain self-sustenance. There is also a danger that some of the agencies may never achieve this in the short to medium term.⁶⁰⁶ In this case the need for the ‘local’ board to approve the

⁶⁰² See ss 41, 42 & 43 Financial Services Act.

⁶⁰³ This may be crucial to avoid contagion as well as share best practices in the financial system.

⁶⁰⁴ The most practical situation would be to ‘transplant’ key staff from the RBM already involved in financial regulation and supervision.

⁶⁰⁵ The banking agency being obviously the ‘wealthier’ and the pension regulator being of a new industry may require assistance.

⁶⁰⁶ It is submitted that only the agency regulating banking and other similar institutions may be truly self-sustainable.

budgetary needs and the regulator to justify its budget before Parliament is even more paramount.

Because of the uneven 'distribution of wealth' amongst the three agencies, although each regulator may be authorised to collect fees, the danger of 'industry capture' may be greater with TPFERS and may require vigilance on the part of the governance structure. This is where the BFSR may prove useful in providing oversight.

Summary

Subject to minor statutory amendments, the current framework provides regulatory independence for TPFERS. Because under this model, the governor is no longer the registrar, the exclusive authority of the President to appoint the registrar automatically ceases to have its dreaded effect. However three separate agencies will have to be instituted and may need longer support from the state before they can become self-sustaining.⁶⁰⁷ The law by and large provides for granting and withdrawal of licences within each industry but where this power is concentrated in the registrar of financial services, this will need to be devolved through legislative amendments. Each of the agencies will have to ensure adequate compensation in order to attract and retain competent staff and avoid bribery. Uniformity of perks may be a key solution to achieving morale and avoid 'cross-over' of staff. To achieve institutional independence, each agency would need an independent representative board as part of its governance structure, subject to a BFSR. The 'local' boards must appoint senior staff and the staff must enjoy security of tenure. Finally each of the agencies must be able to formulate and justify its budget and because it is envisaged that state funding may be required for a longer period, the regulator should justify its budget before parliament.

To achieve this model will require a considerable more statutory changes as well as major institutional setup and changes. Since this would be a completely different setup to that which is currently in place, the need for culture change and political will is ever greater.

⁶⁰⁷ And some may never be.

4.3. Imbedded Triple Peak Financial Services Regulatory System (ITPFSRS)

This model proposes maintaining the regulation and supervision within the RBM but making the three *de facto* registrars (directors) to be the *de jure* registrars of the industry that falls under them. The registrars would still be within the RBM structure but would have legal authority in their own right and the governor and board of the RBM would provide oversight. The ITPFSRS would look like:

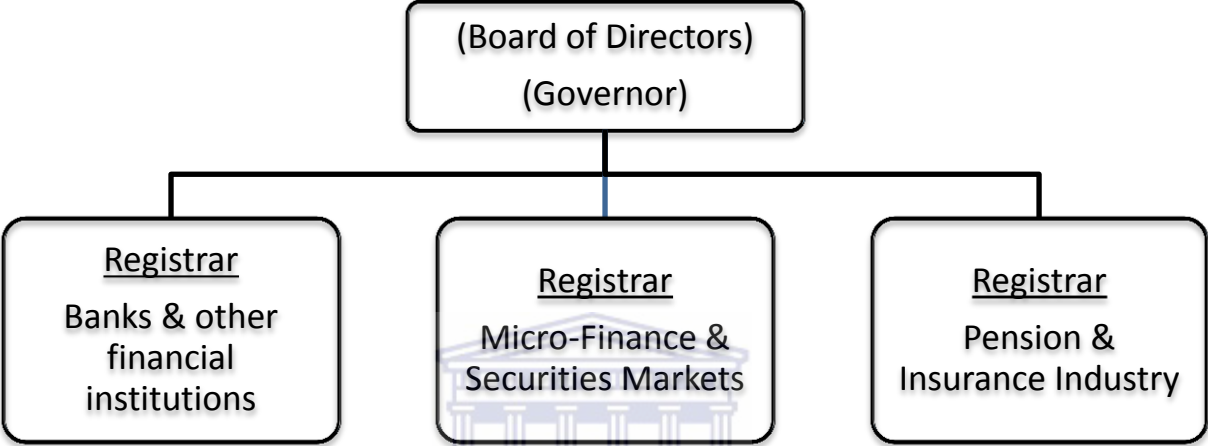


Fig 9. Proposed structure of an Imbedded Triple Peak Financial Services Regulatory System

Because the 'ITPFSRS' structure is imbedded within RBM, it would not require as many legislative amendments. However key would be the devolution of power from the governor (the current *de jure* registrar) to the three registrars (the current *de facto* registrars). The RBM would still maintain its function as overall regulator of the financial services but each registrar would be given autonomy to regulate the industry subject to oversight of the governor and board. This model requires the least changes as it will mainly involve a functional review.

4.3.1. Regulatory independence

Since the law already gives the regulator wide autonomy in regulating the different industries, regulatory independence is likely to be achieved. Subject to minor amendments, especially devolution of power from a single regulator, the current legislative framework does provide for regulatory independence under this model.

4.3.2. Supervisory independence

Like the two models proposed above, the ITPFSRS does provide for some supervisory independence but it is proposed that the powers specifically provided for in the FSAM for the registrar of financial services be devolved and be included in the respective legislation regulating each of the three silos. To ensure that the registrars have operational autonomy, it is proposed that their appointment be made by an independent financial body comprising stakeholders in that industry, appointed on a transparent and representative basis with the involvement of the RBM. This is in taking cognisance of the fact that under the RBM structure, the registrars would be under the governor. It is further proposed that the registrars report directly to the governor and not through an intermediary.⁶⁰⁸ The need to attract and retain competent staff and offer enough perks to avoid bribery may be a challenge because of the fact that the structure is embedded within a pre-existing structure. The advantage though is that it would not involve ‘transplantation’ of staff.⁶⁰⁹ It is proposed that each registrar be encouraged to build reserves that can assist in the autonomic operation of each regulator. The current statutory framework in each of the legislation giving the regulator sole authority to grant and withdraw licences is well suited to achieve supervisory independence for each agency but where the law grants this authority to the registrar of financial services, this power may have to be devolved.

4.3.3. Institutional independence

This may be done in two ways, having regulators outside the physical buildings of the RBM or creating space from within. The latter is easier as it involves fewer changes. The former is more involved but has been done before with MALSWITCH and the MSE.⁶¹⁰ Compared to the above two models, the ITPFSRS may be regarded as the least independent but would still pass muster compared to the current regulatory setup. The issue of security of tenure of senior personnel may be tricky and may be safeguarded if the route chosen is have the regulators detached from the operating

⁶⁰⁸ See fig 4 & 5 above, the Directors report through the General Manager, Supervision of Financial Institutions.

⁶⁰⁹ But more like relocation or transferring.

⁶¹⁰ ‘Malawi Switch Centre (MALSWITCH) was established by the RBM to facilitate the implementation of a clear, secure and guaranteed electronic payment infrastructure in Malawi in line with the overall objectives of the National Payment System Modernization Programme.’ – MALSWITCH available at <http://www.malswitch.com/> (accessed 3 May 2011). The Malawi Stock Exchange (MSE) was also created initially as an appendage of the RBM until it was able to stand on its own. Shareholders of MSE are RBM & Malaŵi Government – see ‘Malawi Stock Exchange – Company Profile : Shareholding’ available at <http://www.mse.co.mw/prof-share.html> (accessed 3 May 2011).

offices of RBM whilst remaining within its wings.⁶¹¹ Because of its imbedded nature, institutional independence would be measured against the RBM's own independence unless the regulators were detached and separated.⁶¹²

4.3.4. Budgetary independence

It is proposed that if the registrars are physically separated from the RBM (but still under its wings) then each registrar be allowed to justify his own budget to a representative board overseeing their operations.⁶¹³ Even in a situation where the registrar is not separated, the registrar should be able to formulate his budget and defend it to the board of the RBM. In this model, the dangers of the "regulator(s)" running out of funds⁶¹⁴ or 'industry capture' do not arise. Compared to the above two models, this model offers the least budgetary independence.

Summary

This model proposes preserving the current *status quo* but subject to a key fundamental change of delinking the registrar from the governorship. Because the RBM would be retained as the overall regulator, the existing legislative framework would not have to be changed to ensure regulatory independence for ITPFSRS except the devolution of power. Furthermore, as the governor is no longer the registrar, direct political influence may be somewhat diminished.⁶¹⁵ Setting up the ITPFSRS is the least costly as it is premised on the current setup with a few structural and institutional changes. The law would have to be changed to devolve the power to grant and withdraw licences within each industry to the respective registrars. The issue of perks is however likely to be a tricky one unless the registrars are separated from the RBM's offices. Although operating under the RBM, the registrars must be able to formulate and justify their budgets.⁶¹⁶

⁶¹¹ As in MALSWITCH or MSE. Even now, the MSE and MALSWITCH share the old RBM Blantyre Branch.

⁶¹² MSE and MALSWITCH have been able to build up separate corporate images detached from the RBM even though they may for all purposes be 'owned' by the RBM.

⁶¹³ Both MALSWITCH & MSE have separate Boards. For the board of the Malaŵi Stock Exchange see 'Malawi Stock Exchange – Company Profile : Shareholding' <http://www.mse.co.mw/prof-share.html> (accessed 3 May 2011).

⁶¹⁴ Unless the RBM itself has financial difficulties.

⁶¹⁵ It may still be indirectly exercised.

⁶¹⁶ Either to a (hopefully representative) board if separated or to the RBM Board if fully imbedded.

To achieve this model will require minor legislative changes and minimal institutional changes.⁶¹⁷ Since it is a setup that does not propose significant changes, there is no need for a culture change and the political will required will also be less.

Conclusion

This chapter has discussed three proposed regulatory frameworks for the financial sector and has considered the statutory, institutional and structural changes that may need to be undertaken. The chapter used the 'independence' yardstick to analyse the three proposals as well as the effects on the political and business establishment. In dealing with these proposals the chapter also looked at the possible advantages and disadvantages of each model.

The UFSR provides the most independence whilst the ITPFSRS provides the least. The ITPFSRS and TPFSSRS preserve the *status quo* in terms of business culture. In terms of costs, the TPFSSRS is the most costly⁶¹⁸ because it involves the creation of three separate agencies. Although the ITPFSRS strongly resembles the present regulatory setup, the major difference is that it devolves⁶¹⁹ the registrar's power from one person. The most fundamental change may be the removal of the governor as registrar of financial services in all three models.

In the next chapter the three proposed models are further analysed in the context of the situation in Malaŵi and recommendations are made depending on what may be achievable and practical by looking at the advantages and disadvantages of each model.

⁶¹⁷ Unless the decision is to house the registrars separately, then this may require institutional capital to set up.

⁶¹⁸ Financially and institutionally.

⁶¹⁹ This in truth is the case for all the models.

CHAPTER FIVE

5. Conclusion and Recommendations

The Malaŵi financial sector is regulated under the Reserve Bank of Malaŵi (RBM) and its governor is the statutory regulator of the financial services sector. The thesis has shown that historically, the governor and the RBM have and continue to be under executive authority and they may not pass muster as independent institutions. The influence of the executive has also been shown to be more evident in multi-party Malaŵi. The thesis also examined financial regulatory models and made a comparative review of the United Kingdom and Zambia because of the historical ties that these two have with Malaŵi as well as the pioneering role of the UK's Financial Service Agency (FSA). The thesis also critically analysed the statutory framework of the financial service sector and isolated some of the issues that are likely to become topical issues or form the basis of legal challenges. In doing this, the thesis has also demonstrated the full role of the registrar of financial services (as required in the various financial services laws) and concluded that the registrar has a lot of responsibilities which the law requires of him. Considering that the registrar also has to govern the central bank, the thesis looked at models that would allow the governor to govern and the possibilities of freeing the RBM from being in the mix of things. The thesis then identified three possible frameworks under which the financial service sector in Malaŵi may be independently regulated. In summary the three models offer the following:

Independence:

5.1. Unified Financial Services Regulator (UFSR) :

5.1.1. Offers regulatory independence.

5.1.2. Offers institutional independence.

5.1.3. Offers budgetary independence.

5.2. Triple Peak Financial Services Regulatory System (TPFSRS):

5.2.1. Offers regulatory independence.

5.2.2. Offers institutional independence.

5.2.3. Offers budgetary independence but subject to weaker regulators failing to stand on their own and more susceptible to industry capture.

5.3. Imbedded Triple Peak Financial Services Regulatory System (ITPFSRS) :

- 5.3.1. Offers regulatory independence.
- 5.3.2. Its institutional independence is tied to RBM independence.
- 5.3.3. Offers no real budgetary independence.

Political will, culture change, legislative and institutional changes:

5.4. UFSR :

- 5.4.1. Requires a lot of political will
- 5.4.2. Requires an adaptation of culture.
- 5.4.3. Needs legislative changes in most of the financial services law and also to create a new institution.
- 5.4.4. Requires major investment in institutional setup and structural changes
- 5.4.5. Costly.

5.5. TPFARS:

- 5.5.1. Requires a lot of political will
- 5.5.2. Needs a complete culture change
- 5.5.3. Needs legislative changes in most of the financial services law and also to create three separate institutions.
- 5.5.4. Requires much more investment in setting up three institutions.
- 5.5.5. Most costly.

5.6. ITPFSRS:

- 5.6.1. Requires less political will
- 5.6.2. No need for a cultural change (business as usual)
- 5.6.3. Minor regulator changes (fundamentally involving removing the governor as registrar but still retaining overall regulatory control within the RBM).
- 5.6.4. Minor institutional and structural changes.
- 5.6.5. Least costly.

RECOMMENDATIONS

From an independence point of view, UFSR is the best model as it scores highly amongst all the independence 'yardsticks' used in this survey. ITPFSRS is the least independent. TPFERS offers independence except that it is more susceptible to 'industry capture' or becoming a burden on the state.

From an economic, cultural and political viewpoint, ITPFSRS is the most attractive as it still preserves some form of political control with the executive, is the least costly and preserves the *status quo* in terms of business culture.⁶²⁰ The TPFERS is the most costly and in terms of business culture requires fundamental changes as it creates three separate structures.⁶²¹ The UFSR requires relinquishment of political control and cultural adaptation. It is less costly than TPFERS but much more costly than ITPFSRS.⁶²²

As was seen in chapter three, the registrar of financial services in Malaŵi has a lot of work. When one considers that the registrar is also the governor and looking at the functions of the RBM, it becomes clear that the RBM and the governor are overloaded with functions and for this reason both UFSR and TPFERS would free the governor and the RBM from regulatory functions and allow the RBM to concentrate on its role as a Lender of Last Resort (LOLR). Another benefit also accrues from the RBM delinking itself from regulation. During a financial crisis, one would want the RBM to come in not only as a LOLR but also with monetary policies together with fiscal policies of treasury that may contain the situation or at least prevent and arrest contagion. Should the RBM be involved in regulation and active running of troubled institutions, as was the case with Finance Bank of Malaŵi,⁶²³ the RBM may become involved in the financial 'mess' itself and there might be no one to offer a rescue package.

⁶²⁰ Economic in the 'narrower and immediate expense' sense since in the broader sense having an independent institutional may be also economical.

⁶²¹ UFSR is premised in uprooting the structure and 'transplanting' it elsewhere whilst ITPFSRS is improving on the already existing structure where it is.

⁶²² UFSR and TPFERS are compared using economies of scales.

⁶²³ See Nkowan (2008) 50-2.

It would therefore seem that freeing the RBM from its regulatory functions may benefit the financial system from an independent viewpoint as well as allowing the RBM to independently oversee the operations of the financial services sector as it manages monetary policy.

Looking at the three models, UFSR is the recommended model to ensure that Malaŵi has an independent financial regulatory system. However, in view of the legal, historical, political and economic context of Malaŵi, it is conceded that UFSR is unlikely to attract approval or the necessary political will to have it implemented.⁶²⁴ It may therefore be said that TPFERS would offer a better alternative. However, considering the cost of its implementation, it is submitted that this may not be an attractive model at the moment.

It is therefore recommended that Malaŵi implements the ITPFSRS because although it does not offer the requisite independence, it is the least costly, requires the least change in culture and most importantly requires the least political will.

There is also an added benefit in starting with ITPFSRS. The fact that some control has been relinquished may provide an impetus for future regulatory changes and it is submitted that a transition can then be made to TPFERS and eventually to the 'ideal' UFSR. However, there is nothing to prevent a transition from ITPFSRS straight to UFSR should the political will be there because in terms of costs, UFSR is less costly than TPFERS.

Although TPFERS looks the least difficult to implement, it also requires that the governance structure within the RBM accept and recognise the enormity of the task that the governor has and that devolving of power will not weaken but strengthen the institution and make it more efficient. It is therefore recommended that the model may easily be acceptable if it is perceived as having arisen from a 'needs analysis' of the RBM.⁶²⁵

⁶²⁴ Recent events in multiparty Malaŵi have shown, except for the period 2004-2009, the ruling political party has an absolute majority of legislators and the enacted laws are usually reflective of the political policies of the government in power.

⁶²⁵ The political will of the RBM governance structure and its controlling interests.

Recommendations for further research

- i. If any of the proposed models were to be adopted, what would be the actual legislative, institutional and structure requirements to make them or any part of them operational? Furthermore, can a hybrid model be moulded out of the proposed models?
- ii. Alternative capital markets; why has the Malaŵian business community not caught the 'bug'?
- iii. The relationship between securities trading and development and whether in Malaŵi the prevailing theories that stock markets lead to development hold.⁶²⁶
- iv. Regional stock markets and how Malaŵi can benefit from a regional stock market and cross-listing.
- v. Reform of the Reserve Bank of Malaŵi to make it more independent and accountable.⁶²⁷
- vi. Review of the New Building Society Act to bring it in line with the new financial service law in Malaŵi.⁶²⁸
- vii. Reviewing the breadth of the financial service law to ensure that its provisions are in line with the Constitution.⁶²⁹
- viii. Regulating shareholding of financial institutions.⁶³⁰

In conclusion it is submitted that whilst the proposals and recommendations made in this thesis may not be implemented as presented, it is hoped the thesis has contributed to the knowledge and debate on the subject and may provide at least a framework on which needed regulatory changes may be implemented in the financial services sector in Malaŵi or from which further research and studies can be undertaken.

⁶²⁶ Considering the low yield on the MSE and that most companies are having their stocks effectively 'devalued' by trading.

⁶²⁷ Using Parliament as accountability body especially regarding the appointment and tenure of the governor and the board.

⁶²⁸ Especially as it is the only law that designates the Minister as a the person to appoint a registrar of building societies and in so doing the registrar has appointed the Secretary to the Treasury, the top financial civil servant.

⁶²⁹ In Malaŵi an Act does not have to be 'vetted' by the Constitution Court as is the case in South Africa and any offending law is challenged by application to the High Court – ss 5 & 108 Constitution of Malaŵi 1994.

⁶³⁰ Section 53 The Financial Services Act provides a 49% cap but there is an ambiguity as to whether this only applies to shares held by individuals or entities.

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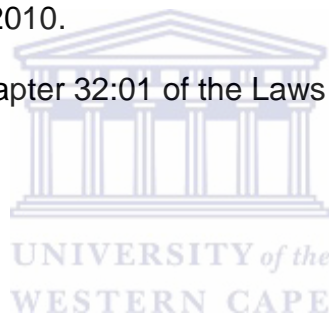
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APPENDICES

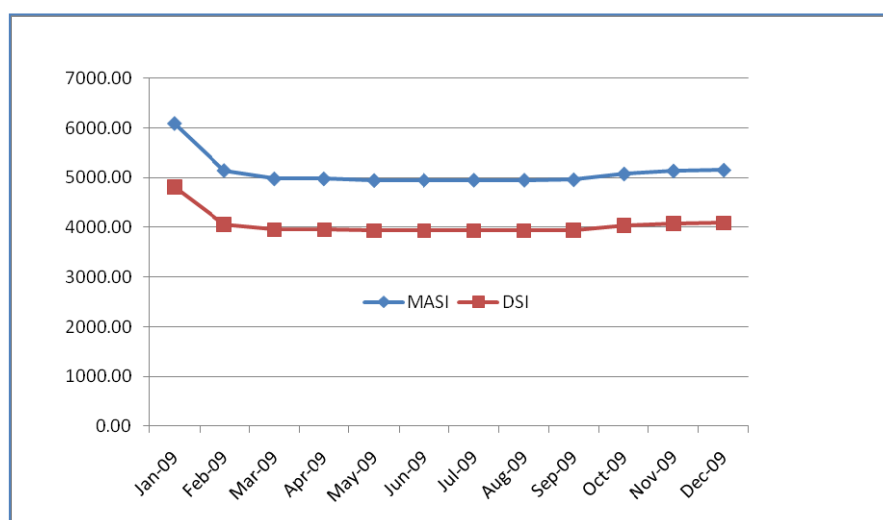
(A) MALAŴI STOCK EXCHANGE COMPANY TRADING STATISTICS : THE YEAR 2009

Company	Opening Price	Closing Price	% Price Change	Share Vol. Trade	%
Traded					
BHL	615	615	0.00	250,000	0.04
FMB	1200	1000	-16.67	8,897,597	1.50
ILLOVO	12500	11000	-12.00	3,579,160	0.60
MPICO	430	260	-39.53	28,653,272	4.84
NBM	6300	5900	-6.35	4,053,841	0.68
NBS	1450	1400	-3.45	18,644,209	3.15
NICO	950	900	-5.26	7,759,198	1.31
NITL	2100	1550	-26.19	3,825,381	0.65
PCL	20500	16300	-20.49	3,528,375	0.60
PIM	625	625	0.00	429,910	0.07
REAL	280	230	-17.86	3,241,093	0.55
STANDARD	8500	9200	8.24	2,208,343	0.37
SUNBIRD	890	890	0.00	546,684	0.09
TNM	330	200	-39.39	506,316,082	85.47
OML Plc	41500	25000	-39.76	487,144	0.08
				592,420,289	
				100.00	

The market recorded trading activity on all counters during the year 2009. TNM registered the biggest trading volume and value of 506,316,082 shares and a total turnover of MK1,005.48 million representing 85.47 % of the total volume of shares traded and a total turnover of 34.9% respectively. The top performing stock as measured by capital gains through a share price rise was Standard Bank by 8.34 % driven by positive half year results and anticipated earnings growth well above the 2008 results.

Source : MSE Annual Market Performance Review; 01/01 – 12/31 2009 (Table 4)

(B) MALAŴI ALL SHARE AND DOMESTIC SHARE INDEX – JAN - DEC. 2009 (Market Liquidity)



Author's note: Old Mutual Plc (OML Plc) is the difference between the Malaŵi All Share Index (MASI) and the Domestic Index (DSI). OLM Plc is registered in the London Stock Exchange and has cross listings in several other African exchanges like the JSE in South Africa and NSX in Namibia)

Source: MSE Annual Market Performance Review; 01/01 – 12/31 2009 (Fig. 2)

(c) TYPE OF FINANCIAL INTERMEDIARIES OPERATING IN MALAWI

Central bank – Reserve Bank of Malawi

Commercial banks: National Bank of Malawi
Standard Bank
First Merchant Bank
Ecobank
INDEBank
NEDBANK
NBS Bank Ltd
Malawi Savings Bank Ltd
Opportunity International Bank of Malawi
FDH Bank
International Commercial Bank

Finance houses and Merchant Banks: Leasing and Finance Company

Savings and Credit institutions:

Malawi Union of Savings and Credit Cooperatives (MUSCCO)
Savings and Credit Cooperatives (SACCOs)

Development finance institutions: INDEfund

Insurance institutions

General Insurers:

NICO General Insurance Co Ltd
Charter Insurance Company Ltd
Citizen Insurance Co Ltd
General Alliance Insurance Co Ltd
Prime Insurance Co Ltd
Reunion Insurance Co Ltd
Real Insurance Co Mw Ltd
United General Insurance Co

Re-Insurers: Zimbabwe Reinsurance Co Ltd (ZIMRE)

Life-Insurers:

Vanguard Life Assurance Co Ltd
Old Mutual Life Assurance Co Mw Ltd
NICO Life Assurance Co Ltd

Stock Exchange : Malawi Stock Exchange

Stock brokers

African Alliance Securities Ltd
CDH Stockbrokers Ltd
FDH Stockbrokers Malawi Limited
Trust Securities Limited

Discount houses

Continental Discount House Ltd
First Discount House Ltd

Pension Fund Administrators

Old Mutual Life Assurance Co Mw Ltd
NICO Life Assurance Co Ltd
Baobab pensions
Associated Pension Trust

Source: [http://www.sadcbankers.org/SADC/SADC.nsf/LADV/E4E3EF0D1F5967B8422576740044D454/\\$File/Malawi-.pdf](http://www.sadcbankers.org/SADC/SADC.nsf/LADV/E4E3EF0D1F5967B8422576740044D454/$File/Malawi-.pdf) (accessed on 25 March 2011).

(D) LIST OF BOARD MEMBERS OF THE RBM

Dr. Perks Ligoya	Governor
Mrs. Mary Nkosi	Deputy Governor
Mr Ted Sitimawina	Secretary for Economic Planning & Development (now Development Planning & Cooperation) (<i>ex-Officio</i>)
Dr Patrick Kambewa	Economics Professor (University of Malaŵi)
Mr. Joseph Mwanamveka	Secretary to the Treasury (<i>ex-Officio</i>)
Mr. Gautoni Kainja	Legal Practitioner (private sector)
Mrs. Betty Mahuka	Accountant (private sector)

Source: <http://www.rbm.mw/aboutrbm.aspx> accessed (30 March 2011).

Note: designation of representative of private sector comes from the author's knowledge of these Board members. Mr. Kainja is Senior Partner in Kainja & Dzonzi whilst Mrs. Mahuka is Director of Finance at the ESCOM Ltd.

(E) LIST OF GOVERNORS WHO HAVE SERVED AT THE RBM

Dr. Perks Ligoya	2009-Present
Mr. V. Mbewe	2005-2009
Dr. E.E. Ngalande	2000-2005
Dr. M.A.P. Chikaonda	1995-2000
F.Z. Pelekamoyo	1992-1995
Hans Joachim Lesshafft	1988-1992
S.C. Hara	1986-1988
L.C. Chaziya	1984-1986
J.Z.U. Tembo	1971-1984
D.E. Thomson	1968-1971
A.G. Perrin	1968

Source: <http://www.rbm.mw/aboutrbm.aspx> (accessed 30 March 2011).

Note: All the Governors are/were Malaŵian except Perrin, Thomson and Lesshafft.