

**An assessment of the regulatory philosophy of the securities and exchange commission
of Zimbabwe (2009-2014)**

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Declaration

I, Lyinah Tendayi Madende, do hereby declare that this dissertation is the result of my own investigation and research, except to the extent indicated in the Acknowledgments, References and by comments included in the body of the report, and that it has not been submitted in part or in full for any other degree to any other university.

Signature of student

Date

Signature of supervisor

Date

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Dedication

To all who inspired me to be what I am today.

Abstract

The growing need for both local and foreign funds can be satisfied by a robust and well functioning securities market. It is imperative for any country to design and implement an effective regulatory system that ensures compliance, development of the market and protection of investors. The capital market in Zimbabwe has been characterized by resistance and conflict whilst companies continue to close under new regulation ushered by the Securities and Exchange Commission (SECZ). The purpose of the research is to gain insight into the realities of regulation being implemented by the SECZ. The research identifies the factors that influence SECZ's regulatory approach, characterizes its enforcement style, examines whether SECZ is rules based or principles based and assesses how SECZ cooperates with the market. The study used a qualitative approach which was centered on the case study of SECZ. The study was premised on the proposition that the SECZ regulatory approach promotes market development and provides a safe environment for investor protection. The proposition was examined by exploring the regulatory actions of SECZ. The study identified the factors that influence the SECZ regulatory approach as its independence, the nature of the market, founding laws, regulatory resources and personalities of its employees. The study found that SECZ employed a legalistic command and control style to regulation that relied heavily on rules and operated under a pure government model as there was little cooperation with the market players. The study revealed that the SECZ approach to regulation was partially effective given the market realities, social and economic conditions. The study recommends that SECZ should be more flexible with market players; move towards principles based regulation and share its regulatory roles with the market players.

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Abbreviations

CISNA	Committee of Insurance, Securities and Non-Banking Financial Authorities
CMA	Capital Market Authority
CSD	Central Securities Depository
FSMA	Financial Services Market Authority
IOSCO	International Organization of Securities Commissions
IPEC	Insurance and Pensions Commission
JSE	Johannesburg Stock Exchange
PAAB	Public Accountants and Auditors Board
RBZ	Reserve Bank of Zimbabwe
SADC	Southern African Development Community
SECZ	Securities and Exchange Commission
ZIMRA	Zimbabwe Revenue Authority

CHAPTER ONE: INTRODUCTION AND BACKGROUND

1.0 INTRODUCTION

The growing need for both local and foreign funds can be satisfied by a robust and well-functioning capital market (Okioga, 2013). For that reason, any country should design and institutionalize an optimal regulatory system that promotes investor protection and enhances market development. The regulatory structure should promote competition, entrepreneurship and innovation (Groenleer, 2014).

The Government of Zimbabwe ushered a new era of financial regulation when it entrusted the Securities and Exchange Commission (SECZ) with authority to regulate the capital market. The capital market in Zimbabwe has been characterized by resistance, tension and conflict and companies continue to close under the new regulation of SECZ. The purpose of this research is to contribute to the understanding of the regulatory behavior of the SECZ in the context of international practices. The research examines the factors that influence SECZ regulatory philosophy, its enforcement style, the regulatory approach and the regulatory model.

Regulation is important to enable a level playing field and to inspire confidence to both investors and issuers of securities (Okioga, 2013). The mandate of investor protection and development of the market will remain the same forever but the mechanisms of achieving them will be ever changing (Azmi, 2007). Regulators should recognize the fundamental transformations in the financial markets because the capital market plays a very pivotal role in the development of a nation. The capital market constitutes an alternative to bank financing as it transforms savings into real sector financing (Carvajal and Elliott, 2007). Literature emphasizes the importance of capital market in sustaining a positive economic growth (Banerjee, 2008; Malkawi and Haloush, 2008; Antelo and Peon, 2012; Alrigibi, Ariff and Murray, 2010; Zivengwa, Mashika, Bokosi and Makova, 2011; Beattie 2008 and Ho, Palacios and Stoll, 2013).

1.1 BACKGROUND OF THE STUDY

1.1.1 The Capital Market Authority

The establishment of SECZ was motivated by the fear of losing the global inflow of funds due to poor regulatory infrastructure, coupled with the desire to comply with best international practice. Previously, the capital market was regulated by the Zimbabwe Stock Exchange (ZSE). The ZSE used to play both regulator and player roles in the market. The Securities Act [Chapter 24:25], was passed into law in 2004 and became effective on 1 September 2008. The SECZ was subsequently operationalised on 1 September 2008. The Act was renamed the Securities and Exchange Act [Chapter 24:25] on 29 August 2013 through the publication of the Securities Amendment Act No. 2 of 2013. The SECZ is a statutory body established in terms of Section 3 of the Securities and Exchange Act. It is the capital market authority that regulates the trading, marketing and investments in securities in Zimbabwe.

The capital market is a market for trading in securities and is also known as the securities market. Adam (2009) defines capital market as a market that deals in a variety of financial instruments such as securities, bonds, debentures, ordinary stocks and shares. Currently however, only equities are traded in the capital market of Zimbabwe. The securities market is divided into two parts, the primary and the secondary market. The primary market deals with issuance of new securities, while the secondary market is concerned with existing securities. The primary market is necessary for raising new capital while the secondary market provides liquidity (Malkawi and Haloush, 2008). The capital market provides businesses with both medium and long term capital. In contrast, the money market provides for short term finance and deals in financial instruments such as treasury bills, commercial paper, interbank and certificate of deposits and the call market (Adam, 2009). The money market is regulated by the Reserve Bank of Zimbabwe (RBZ) in terms of the Reserve Bank of Zimbabwe Act [Chapter 22:15] and the Banking Act [Chapter 24:20].

SECZ regulates and registers securities exchanges, the central securities depository, securities dealers (stockbrokers), investment advisors, custodians and transfer secretaries. The SECZ also administers the Asset Management Act [Chapter 24:26] and the Collective Investment Schemes Act [Chapter 24:19]. The collective investment schemes and asset

management companies were brought under the ambit of the SECZ through the publication of the Securities Amendment Act No. 2 of 2013. Previously asset managers and collective investment schemes were regulated by RBZ. In terms of the Act, the SECZ has the power to take all the measures necessary to execute its statutory obligations. According to Haines (2011), there is no one best formula on how capital markets should be regulated and the realities of regulation are shaped by the choices of the regulator. According to ACMA (2010), there are a variety of approaches which regulators can use to achieve their regulatory objectives and this usually puts regulators in a dilemma as to which approach to take (Perez, 2014). Against this background, it is necessary to assess the regulatory philosophy of SECZ.

1.1.2 Objectives of the Securities and Exchange Commission

The objectives of SECZ are influenced by the need to fulfill both local and international regulatory constructs. SECZ is an aspiring member of the International Organization of Securities Commissions (IOSCO) and a member of the Committee of Insurance, Securities and Non-Banking Financial Authorities (CISNA). IOSCO is an international organization that regulates world securities and futures markets while CISNA is a Southern African Development Community (SADC) regional body. The IOSCO provides a threefold aim of securities regulation, namely to protect investors, reduce systemic risk and to ensure efficiency and fairness in markets (IOSCO, 2010). The objectives of the SECZ are outlined in section 4 of the Act and are in line with that of the IOSCO. The objectives of SECZ are as follows;

- i. To provide high levels of investor protection
- ii. To prevent systemic risk
- iii. To promote investor confidence and market integrity
- iv. To prevent fraud, market manipulation and financial crime
- v. To educate investors on their rights
- vi. To ensure transparency in capital markets and to give advice to the Government.

The mission statement of SECZ is to provide the capital market with an optimal regulatory framework that protects investors and promotes sustainable development of the market. It is the duty of SECZ to create strong institutions that can absorb market risks. It is therefore

critical to assess whether SECZ's regulatory behavior is in tune with promoting the development of the market and protection of investors.

1.1.3 Market Participants

1.1.3.1 The Zimbabwe Stock Exchange (ZSE)

The history of the ZSE dates back to over hundred years, when the Pioneer Column arrived in Zimbabwe. ZSE was established in 1896, and has been in existence since then. Prior to the enactment of the Act, the Zimbabwe Stock Exchange was regulated in terms of the Zimbabwe Stock Exchange Act [Chapter 24:18]. The Act brought about a radical change in the regulatory structure of the capital market. Section 119 of the Act repealed the Zimbabwe Stock Exchange Act. In terms of section 121(2) of the Act, the ZSE continues as a body corporate and is deemed to be a registered securities exchange in terms of the Act. The legal status of the ZSE continued to be of huge debate with questions being raised whether it is a government organization or a mutual society owned by securities dealers. The transformation of ZSE status to a mere regulated entity was a huge discomfiture and it seeded regulatory conflicts with SECZ. The ZSE has drawn SECZ to court under the case ZSE vs. SECZ H.C 8347/10, challenging its regulatory authority.

The ZSE is the only exchange in Zimbabwe. A number of people who have tried to register other types of exchanges such as the spot exchange and commodity exchanges have not been successful. On 21 July 2014 the ZSE and the Government of Zimbabwe signed an agreement of shareholding for the privatization of the ZSE. In terms of the agreement, the ZSE will be incorporated as a private company and eventually will list on itself. The ZSE has been very slow in embracing new technology. Trade at the ZSE is done using the manual open cry system over a one call over session per day. This is despite the fact that many exchanges worldwide have embraced modern technology and trades are conducted online. It is also against this backdrop that the approach of the SECZ to regulation should be examined.

The stock exchange is defined as a platform that provides a market by providing a trading system for execution of securities orders and dissemination of market data (Book Reviews, 2011). It ensures that the secondary market exists to enable investors to adjust their investment portfolios. According to Mangena (2007), the ZSE was primarily established to raise capital for mining companies. Today, the ZSE comprises an assortment of listed

companies which include mining, manufacturing, retail, banking, real estate and the telecommunications industry. There are sixty four companies listed on the ZSE (ZSE Market Index, 2014). There have been a handful of unsuccessful rights issues as companies failed to raise capital. Most listed companies are still suffering from the effects of hyperinflation as they lost most of their capital in the hyperinflationary era. The ZSE has not been able to attract new listings and instead a number of counters have delisted. Examples of companies that delisted over the past five years are Lifestyle Holdings (Private) Limited, Chemco Holdings, Trust Holdings and Phoenix Consolidated, among others. SECZ has on a number of occasions crossed swords with the ZSE over regulatory issues (The Herald, 20 March 2012) and the Newsday of 11 November 2013 also reported that SECZ had been on collision course with listed companies over compliance issues.

1.1.3.2 The Central Securities Depository

Another key institution in the securities market is the Central Securities Depository (CSD). The CSD is an electronic system for holding of securities in dematerialized form (section 2 of the Act). The CSD holds securities and settles trades through transfer of ownership in a central register (Book Reviews, 2011). The tender for the establishment of the CSD was awarded to Chengetedzai Depository Company in 2010. Chengetedzai Depository Company Limited was only licensed to operate the central securities depository scheme on the 24th of April 2014. According to Musiwa (2014), the CSD is expected to improve the settlement cycle from T+7 to T+3. The ZSE owns 10% shareholding in the CSD.

1.1.3.3 Market Intermediaries

The number of securities dealing firms (stockbrokers) dropped from nineteen in 2008 to thirteen as at 31 December 2014. Securities dealers are agents who buy and sell securities on behalf of other persons. Previously stockbrokers were licensed by the ZSE and now they are licensed by the SECZ in terms of the Act. SECZ has been at loggerheads with stockbrokers and has been taken to court on several occasions. Examples of the Court cases include B. Mswaka vs. SECZ H.C. 8067/10, SECZ vs. Gwatidzo N.O and others SC 459/13, Remo Investment Brokers (Pvt) Ltd & others vs. SECZ Misc 6/12, Rufaro Zengeni vs. SECZ Misc 7/12 and Interfin Securities (Pvt) Limited vs. SECZ Misc 8/12. It is critical to understand the regulatory behavior of SECZ in light of these conflicts.

There are three registered transfer secretaries as compared to seven that operated in 2008. Prior to the establishment of SECZ, transfer secretaries were not regulated. The mandate of transfer secretaries is to record securities transfers on behalf of listed companies. The business of transfer secretaries has been sluggish as there are no new listings on the ZSE and to the contrary there have been a couple of delistings. The market has five registered securities custodians, four of which are registered banks. Previously they were six and they were previously indirectly regulated by the RBZ as part of the banking business. Custodians hold securities in safe custody on behalf of other persons.

There are twenty five registered investment advisors and their task is to advise clients on investments. Previously investment advisors operated informally and they were not regulated. Investment advisors started regularizing their operations in terms of the Act in 2012. As at 31 December 2014, two investment advisory companies who had registered with SECZ had since closed. The market is comprised of fifteen asset management companies. Their business is to invest and manage the property of other persons. The official hand over of asset managers from the RBZ was done in February 2014 and fifteen companies were handed over. SECZ on its own licensed two asset managers to bring the number to seventeen. However two asset managers who were inherited from the RBZ have since closed to bring the number down to fifteen.

1.1.3.4 Investors

Investors are at the centre of financial market regulation. The market consists of a few individual investors and institutional investors play a greater role in the market. There are a few local individual investors as many still have fresh memories of the losses they suffered in the hyperinflationary period. Shareholder activism is very poor. According to the Daily News of 19 May 2014, minority shareholders in Zimbabwe are suffering at the hands of listed companies. Nonetheless, foreign investors have managed to sustain the ZSE market turnover in the past five years. It is against this diverse composition of market participants that this study sought to assess the regulatory style of SECZ.

1.2 RESEARCH PROBLEM

Worldwide, regulation of financial markets has been on the spotlight following the 2008 financial crisis (Staikouras, 2012). Gakeri (2012) notes that regulators of capital markets are faced with a mammoth task to balance investor protection, which requires heavy regulation and market innovation, where market players customarily prefer no regulation to light regulation. SECZ regulatory activities have been described as merely seeking relevance, space and justification in the market (The Herald, 16 April 2013). SECZ has on several occasions crossed swords with capital market players. The market is characterized of resistance, tension and conflict and companies continue to close under the new regulation of SECZ. The Herald accuses SECZ of losing focus on its regulatory mandate. It is therefore necessary to assess the regulatory behavior by SECZ in light of these problems. The research will look into the realities of regulation being implemented by SECZ since its establishment.

The regulatory process consists of three processes which are basically the creation of laws, compliance monitoring and enforcement of the laws. At each of the regulatory levels, the level of involvement by market participants and the role of government vary from one jurisdiction to another (Castro, 2011). The Act does not state what constitute too much or too little regulation. It is left to the discretion of the SECZ to determine its operative approach. Perez (2014) argues that regulators cannot avoid applying substantive discretion in regulation even in the presence of sophisticated techniques. SECZ is fairly new, being five years old and very little has been documented about its operative approach. Against this background, it is therefore worthwhile to explore the regulatory philosophy of SECZ in the context of international practices.

1.3. RESEARCH OBJECTIVES

1.3.1 The Main Objective

The research seeks to gain insight into the regulatory paradigm of SECZ and attempts to proffer suggestions for a suitable regulatory management framework.

1.3.2 The Secondary Objectives

The secondary objectives of the study are as follows:

- i. To identify the factors that influence SECZ regulatory philosophy

- ii. To characterize the enforcement style of the SECZ.
- iii. To examine the regulatory approach of SECZ, whether SECZ is rules based or principles based.
- iv. To identify the regulatory model of the SECZ, whether SECZ operates as pure government, shares regulatory roles or promotes self-regulation.
- v. To evaluate the regulatory approach of the SECZ.

1.4 RESEARCH QUESTIONS

The study was guided by the following research questions:

- i. What are the factors that influence SECZ's regulatory philosophy?
- ii. How does SECZ enforce compliance of its regulations?
- iii. In what way does SECZ implement its laws?
- iv. What is the regulatory model of the SECZ?
- v. Is the SECZ's approach to regulation appropriate?

1.5 PROPOSITION

The research proposition is that SECZ regulatory approach promotes market development and provides a safe environment for investor protection. The proposition is examined by exploring the regulatory actions of SECZ.

1.6 SIGNIFICANCE OF THE STUDY

According to Subramanian (2011), regulation, and not market failure has been blamed for the financial turmoil of 2008. The need for sound regulatory policies cannot be overemphasized. Given the conflict, tension and company closures in the capital market, it is worthwhile to explore the regulatory approach of SECZ. A number of studies that have been done on capital market regulatory jurisprudence have been concentrating on developed nations. This study brings insights into regulation of capital markets in a frontier market like Zimbabwe. The study brings new evidence on regulation of the Zimbabwean capital market. Previously, studies on capital market in Zimbabwe focused on the ZSE as it was the only regulatory institution in the market. SECZ is a new phenomenon in the market, it is necessary to take stock of its regulatory approach. The significance of the study is outlined below:

i. To Government

The study will contribute to the understanding of regulatory and supervisory approaches in the financial market. The research will assist in reform efforts by the Government and the capital market players. It will help SECZ to redesign its regulatory strategy and enforcement policy.

ii. To regulated entities

The research provides a comprehensive review of how the SECZ pursues its regulatory objectives in terms of the Act. It helps capital market players to understand the regulatory implementation process and its impact on the development of the market.

iii. To academics

The research adds to the momentum that seeks to build theoretical and empirical knowledge on capital markets authorities' regulatory jurisprudence. It brings new evidence on the regulation of capital market in Zimbabwe. The evidence can be used as a foundation in assessing the role of SECZ.

1.7 THE SCOPE OF THE STUDY

The research focused on the regulatory activities of SECZ. The study targeted the officers of SECZ and licensed players. The licensed players included the ZSE, CSD, stockbrokers, transfer secretaries, custodians, investment advisors and asset management companies. As all the companies licensed by the SECZ are based in Harare, the study was geographically limited to Harare. The SECZ became operational on 1 September 2008 and for that reason the research covered the period from 2009 to 2014.

1.8 DISSERTATION OUTLINE

This dissertation is divided into five parts. Chapter one lays down the introduction and the background to the study. Chapter two reviews literature on theories of regulation and regulatory paradigms. It also contains an empirical review of regulatory approaches in other jurisdictions. Chapter three describes the research methodology and the data used in this research. Chapter four presents the research results. The research conclusions and recommendations are set out in Chapter five.

1.9 CHAPTER SUMMARY

This chapter introduced the concept and motivation of the study. The importance of an optimum regulatory approach was emphasized. It is proffered that SECZ ought to design an appropriate regulatory strategy that promotes investor protection and enhances market development. The background to the study was highlighted with a discussion on the capital market structure and the objectives of SECZ. The chapter set out the need to explore the regulatory approach and enforcement philosophy of the SECZ. It also highlighted the research proposition, significance of the study and the coverage of the research field. The next chapter reviewed literature on regulatory philosophies.

CHAPTER TWO: LITERATURE REVIEW

2.0 INTRODUCTION

This chapter examines the significant areas on regulatory jurisprudence in capital markets. The chapter captures the definition of regulation, the role of regulation and the relevance of the regulatory theories. A dimensional conceptualization of regulatory philosophy on the enforcement styles, regulatory approaches and regulatory models is set forth. The chapter also provides an empirical review of literature in other jurisdictions.

2.1 REGULATION OF CAPITAL MARKET

2.1.1 Definition of Regulation

There are several definitions of regulation. According to Carvajal and Elliott (2007), securities regulation entails the management of public listed companies, primary and secondary markets, and investment management products and securities intermediaries. Tietje and Lehmann (2010) define regulation as the legal framework that shapes financial services and transactions. Baldwin, Cave and Lodge (2012) describe regulation as actions and activities that restrain conduct and incidence of malpractices. These definitions encompass regulation in terms of both the state and the private participants.

Bloodgood, Tremblay-Boire and Prakash (2013) provide an elaborate definition of regulation in terms of its functions. They state that regulation prescribe, permit and prohibit specific categories of actions. Hertog (2010) describe regulation as the use of legal mechanisms to implement social and economic policy objectives. The central issue coming through these definitions is that the actions of the market players are restrained in some way. Further, a distinction between regulation and legislation can be drawn from the definitions. Legislation is the law, while regulation is the result of the use of the law by the regulatory institutions. Nonetheless regulation and the law are often used interchangeably.

2.1.2. Rationale of Regulation

i. To provide high levels of investor protection

Investor protection is at the core of financial market regulation. Gakeri (2014) emphasizes the importance for regulatory agencies to devise a system that promotes and safeguards investor interests. Bebchuk and Neeman (2010) point out that an insufficient investor protection system is costly to the performance of the economy. According to Sun (2008), countries with poor investor protection mechanisms have both agency problems and poor corporate governance. As a primary measure of investor protection, enforcement mechanisms reflect how the law is used to protect investors (Sun, 2008). It follows that investor protection laws are effective when they are properly enforced.

ii. Maintenance of fair and orderly markets

Mugarura (2009) states that regulation provides an operational framework that secures normative values such as security, peace and freedom. Accordingly, regulation should solve and resolve market dispute in a fair and transparent manner. According to Baldwin *et al.* (2012), regulation is a tool that promotes equitable distribution of resources and cures market imperfections. It enables the well-functioning of the market and settlement of disputes. A poorly designed regulation can lead to heavy economic costs which may result in regulatory burden (Parker and Kirkpatrick, 2012).

iii. To promote market integrity and investor confidence

Snider (2009) reaffirms that the central role of securities market regulation is to instill investor confidence. Regulation, through surveillance and enforcement should build investor confidence. As pointed by Pritchard (2003), the capital market cannot function without trust. Markets that are prone to abuse, market manipulation and fraud are at a great risk of losing investors. Corporate businesses also gain confidence when financial intermediaries are well regulated. The equal enforcement of rules and regulations enhances consumer confidence.

iv. To prevent systemic risk

Another important aspect of financial regulation is to forestall systemic risks. Scott (2013) defines systemic risk as a situation where the financial system can collapse as a result of the interconnectedness of financial institutions. It entails the risk that a triggering incident, such as collapse of one company, will seriously harm other companies or markets and results in harm in the broader economy (Bullard, Neely and Wheelock, 2009). An appropriate supervision regime is therefore necessary for systemically key financial institutions.

v. To educate investors on their rights

According to IOSCO (2014), investor education promotes investor protection. An educated investor is an empowered investor. Investors need to understand the financial concepts and products to enable them to evaluate the products. Education provides information on investor rights and responsibilities. However, investor education alone does not guarantee absolute protection to investors. Traditional methods of supervision and surveillance are critical.

vi. To ensure transparency in capital markets

According to Baamir (2008), issues of transparency and disclosure of information are vital for the development of the securities market. The purpose of transparency and disclosure requirements is to provide information to the market (Latimer, 2013). In that regard, regulation can come in the form of disclosure laws, where control is achieved through mandatory provision of certain minimum information to the public (Baldwin *et al.*, 2012). According to Baamir (2008), disclosure enables investors to assess the risks associated with the company. Latimer (2013) believes that failure of disclosure and transparency leads to company failures as investors will be handicapped and cannot exert pressure to improve corporate management.

2.2 THEORIES OF REGULATION

The concept of regulation is underpinned in the theory of regulation. The proponents of these theories are Stigler (1971) and Posner (1974). The theory of regulation has two opposing sides, the public interest view and the private interest view. The way the regulator acts is

greatly influenced by whether the regulator is more of on the public interest view or is captured as explained by the private interest view.

2.2.1 Public interest view

The public interest theory holds that regulation is designed primarily to serve the public interests (Stigler, 1971; Posner, 1974). The theory is also termed the ‘helping hand’ view. The theory is premised on the assumptions that unrestrained markets often fall short due to problems of monopolies and that government is able to correct such anomalies through regulation (Shleifer, 2005; Morgan and Yeung, 2007; Posner, 1974). The theory assumes that regulatory agencies have adequate information and enforcement powers to successfully promote the interest of the public (Hertog, 2010). It also assumes that the regulator is compassionate, that is, the regulator is willing to help the public.

In this regard, the purpose of regulation is to enhance the societal wellbeing. The view is acknowledged by Nickerson and Phillips (2003) who argue that regulation promotes the interests or social values of the general populace that cannot be obtained from market oriented measures. It follows that the aim of regulation is to attain a widely preferred outcome. Epstein (2012) dispels the notion that a free market can function properly as a myth. He believes that the industry needs to be subjected to some form of regulation. This is however rejected by Posner (1974) who argues that there has not been any evidence that shows a correlation between regulation and externalities or monopolies.

The public interest view has been widely criticized. While public interest view assumes that regulation restores economic efficiency, Hertog (2010) finds it difficult to understand why regulation sometimes aims for social justice at the expense of economic efficiency. To him, this does not make sense. He also disputes the assumption of promoting social justice when there is no standard definition of justice. He argues that the relationship between justice and efficiency is empirically impossible to test.

Further, empirical studies have shown that regulation has not been able to serve the public interests as postulated by the public interest view. Regulators may fail to pursue the public interests for various reasons. Leuz (2010) argues that regulation is created by a political process which has so many loopholes and limitations. He argues that the political regulation

comprises various players who are not ‘disinterested’ parties. They also aim for their own private interests and as such may be biased or corrupted by the regulated entities. Hertog (2010) and Shleifer (2005) hold that the government is hardly ever competent and rarely succeeds even in cases where there is greater scope for regulation. In that regard government may not be able to pursue the public interests.

2.2.2. Private interest view

The private interest theory presumes that regulation is established to meet the demands of specific interest groups (Posner, 1974 and Baldwin *et al.*, 2012). The underlying notion of this theory is that the coercive power of the state can be corrupted to the benefit of certain groups. On this cause, regulation cannot be assumed to promote the interest of the consumers. Stigler (1971) describes the private interest view theory as the ‘capture theory’. The theory is also known as the ‘Chicago Theory’.

The private interest view assumes that economic beings strive to minimize their economic interests (Stigler, 1971 and Hertog, 2010). Stigler (1971) argues that the industry acquires and designs regulation and operates it to its advantage. This view is supported by Morgan and Yeung (2007) who state that regulation materializes as a result of individuals or groups for the promotion of their interests. The business people can use their power to tilt the law to their own advantage. Benmelech and Moskowitz (2010) believe that a particular faction can extract rents to the detriment of other groups, using the coercive influence of the state, as law is subordinate to power (Mugarura, 2009).

The study by Benmelech and Moskowitz (2010) found evidence which supports that financial regulation can be used by powerful political incumbents for their own private interests. Powerful people can control competition and entry into the financial market, at the same time lowering their cost of capital. Snider (2009) argues that business persons can exercise their power to shape the form, structure and meaning of the law. He argues that the law emerges from the informal structure of the industry agreements, pressures and networks. The theory stresses the ease with which regulatory capture can manifest. Hertog (2010) argues that regulators may depend for information or income from the regulated entities and for that reason regulators will tend to avoid conflict with the market. He also postulates that

regulatory officials may see career opportunities in regulated companies and can be easily captured.

The private interest view is without criticism. Hertog (2010) finds it silly why the private sector can be successful in subjecting the regulator to their own interests when they fail to block the imposition of the regulator in the first place. He sees no reason for companies to move for regulation that milks off their surplus profits through regulatory costs. Regulatory compliance often stretches the compliance of private companies to outside voluntary levels. Hertog (2010) also submits that, to the contrary, regulation in practice seems to serve the interests of consumers rather than interests of market players. This is echoed by Posner (1974) who argues that politicians will always maximise political support through selection of policies. Further, Barth, Caprio and Levine (2005) doubt that regulated entities can be able to 'capture' regulators especially in democratic settings.

However, according to Barth *et al.* (2005), regulation can swing between private and public interests notions depending on the political climate. They argue that in some instances, it is difficult to discern the interplay between the political forces and the industry. The dominant force may not be easily identified. The balance of power between public and private interests is influenced by specific jurisdictional factors (Ping, 2014). Ideally, capital market regulation should aim to attain a balance between the private and public interests. The theories of regulation are important in so far as they offer contextual background to the regulation of capital markets.

2.3 FACTORS THAT INFLUENCE THE REGULATORY APPROACH

According to Kagan (1989), regulatory management approaches vary along a philosophically distinct dimension. The dimensions run on a continuum from legalistic to retreatist approach, from overregulation to under-regulation and from pure government to pure-self-regulation. It is not easy to explain why regulators may prefer a certain style over another. According to Kagan (1989), variations in political structures and culture contribute to the differences in regulatory styles.

The political environment is a major aspect in determining the paradigm. According to Kagan (1989), regulators operate in a political environment which may defy the law and the

regulator's philosophy. For example, regulators who offend politically significant persons or organizations may face heavy condemnation, budgetary slashes and substitution. Cementing on that, Mwendo (2006) argues that the budgetary process of approving regulatory expenditure can be used by politicians to exert pressures on the regulator. Regulators who rely on the industry for survival can succumb to dependence on the market which may compromise its decisions. Mwendo (2006) avers that politicians may also influence the regulatory style through appointment of senior personal to the regulatory agency. Politicians may also force regulatory agencies to lighten up rules in situations of political interests (Kagan, 1989). The issue is even worse when the regulated entity is also a government organization.

According to Baldwin and Black (2008), the regulator may lack judicial, public or political support and may not want to trigger hostile business reactions. Sometimes regulators succumb to activist pressure groups to take certain actions. According to Yee, Tang and Lo (2014), the regulatory design, compliance and enforcement can be shaped by legitimacy and strength of the government. They argue that the level of corruption also has a significant influence. They also suggest that the levels of protection of property rights in the country also play a crucial role.

Further, Kagan (1989) argues that the size and the complexity of the market players influence the regulatory management framework. Smaller numerous companies may call for more stringent approach of interpretation of rules to curb the nuisances. This is supported by Baldwin and Black (2008) who state that the resources of the regulatory agency and the size of the industry and products thereof determine the regulatory approach. Accordingly, the weakness or potency of the regulated entities shapes the regulatory style.

According to Coslovsky, Pires and Silbey (2010), the relationships, linkages and networks in the industry influence the style of the regulator. Baldwin and Black (2008) anchor this view when they argue that the regulatory design depends on the collaborativeness or uncooperativeness of the regulated entities. However networks compromise the independence of the regulator and may result in regulatory capture (McCaffrey, Martinez-Moyana and Smith, 2006 and Kagan, 2001).

In addition, Ford (2010) advocates for greater regulatory independence from the market to avoid conflict of interest and overreliance on market discipline. While Mwendo (2006) acknowledges the importance of independence of the regulator, he admits that it is difficult to sustain as the regulator operates closely with the regulated entities. Points of cooperation include inspections, monitoring and enforcement of sanctions and cancellation of licenses.

2.4 ENFORCEMENT STYLES

Verbruggen (2013) defines enforcement as the actions that ensure compliance with regulatory norms. Enforcement is different from the setting of standards or rules. It entails those activities done by the regulator to achieve and coerce compliance (May and Winter, 2011). It is a mechanism to secure compliance (Gray and Shimshack, 2011). According to Simila, Polonen, Fredrikson, Primmer and Horne (2014), regulatory objectives can only be achieved when there is a high degree of compliance. The regulatory choice of intervention is so crucial. Apart from regulatory design, an efficient and effective enforcement regime is indispensable for legislation to work (Gunningham, 2011 and Leuz, 2010). According to Lo and Tang (2013), an appropriate fit of the style should result in regulatory effectiveness and compliance.

The regulatory style is the pivotal conception of regulatory enforcement. May and Winter (2000) define the enforcement style as the character of the day to day interactions of the regulators and their subjects. It describes how regulators interact with regulated entities (Mcallister, 2009). According to Bardach and Kagan (1982), the enforcement style entails the general approach taken by regulatory agencies in carrying out their regulatory mandate. According to May and Winter (2011) enforcement style entails use of coercion in threatening or imposing sanctions. It comprises how the regulators ignore violations, detect offences, issue warnings and grant penalties and exemptions (Gray and Shimshack, 2011). Is the regulator heavy handed or light handed in its interactions with regulated entities? It relates to the street behavior of the regulator. Is the regulator pleasant and caring, cynical and quizzical or intimidating and hard to please? It entails the rigidity with which laws are enforced. The use of written as opposed to verbal communication, enforcement through strict rather than negotiation and skepticism or trusting. All these point to the style of the regulator according to May and Winter (2011).

Lo, Fryxell and Rooij (2009) identify five elements of enforcement styles. Formalism refers to how the regulator adheres to the strict interpretation of the legal requirements. According to Muhammad (2013), this may take the form of specific conduct linked to specific penalties without consideration of mitigating or extenuating circumstances. The element of education emphasizes the communicative aspect and coaching to instill good behavior in regulated entities (May and Winter 1999). The third element is coercion. Coercion puts emphasis on the use of sanctions and it signifies the propensity and readiness of the regulator to impose sanctions (Muhammad, 2013). The aspect of prioritization entails a sensible enforcement criterion that tries to bring the best results given a particular situation (Bardach and Kagan, 1982). The regulator will use its scarce resources where they are needed most. Lastly, the accommodative element stresses the views of the stakeholders and politicians. The regulator will always try to reconcile demands of stakeholders (Muhammad, 2013).

However, in reality, enforcement styles are remixed and multifaceted. Each element in its unadulterated form will not be effectual as each has its own merits and setbacks. According to Muhammad (2013), regulators generally use a concoction of components in the performance of their duties. However, some regulatory aspects are deceptive and difficult to code. Coslovsky *et al.* (2010) provide an example where the regulator may appear to be strict by sending an offender for prosecution while it is accepted and known by everyone that prosecution will not be effective. Prosecution may be used as a delaying tactic or in some instances the officers may be so corrupt that justice will not be achieved.

Kagan (1994), cited by May and Winter (2000) categorizes three enforcement styles which are ranked in terms of their stringency and coercion. These are the legalistic approach, the flexible approach and the accommodative approach. The enforcement styles vary across regulators for different reasons. According to Yee *et al.* (2014) regulatory enforcement is influenced by established shared practice and expectations. The regulatory context will shape the enforcement style and there is no one best formula. May and Winter (2011) reinforce this view when they argue that the extent of the regulatory problem, the attitude of the regulator and background and responses of the regulated entities influence the enforcement style. Generally regulators intervene in activities of companies based on available resources,

magnitude of the violations, and their sense of legal and political surroundings (McCaffrey *et al.*, 2006).

2.4.1 Legalistic Enforcement

According to May and Winter (2000), the legalistic approach is associated with high level of formality and use of force. It is also referred to as deterrence style (Muhammad, 2013) or formalistic approach (Yee *et al.*, 2014). It is rule oriented and punitive in nature (Gunningham, 2011). According to Mcallister (2009), it entails a detached rule- book application of rules and a particularistic approach to problems. It entails consistent and uniform application of rules (Yee *et al.*, 2014). This is echoed by Hawkins (2013) who states that it denotes strict and rigid enforcement of rules and regulations. According to Muhammad (2013), it is characterized of intimidation and force. The regulator approaches issues with bureaucratic literalness (Mcallister, 2009). The regulatory autonomy will be insulated and duty dominated.

Legalistic decision making confer supremacy to legal norms at the expense of non-legal issues (Roehling and Wright, 2006). According to Jones (1998), the focus of this approach is compliance monitoring and gathering of evidence rather than advice and counseling. The prevalent actions in this style are inspections, prosecution, fines and public embarrassments, with little effort to educate or counsel the perpetrators (Jones, 1998). An adversarial relationship between the regulator and the regulated entity is typical in this kind of setup (Jones, 1998). According to Etienne (2014), inspections are generally associated with the command and control type of governance. The inspections are routine and to book with little diagnostic efforts (Mcallister, 2009).

According to Muhammad (2013), compliance is achieved by imposing sanctions. It is coercive in nature. This school of thought believes that regulated entities only take measures to comply with rules when they know that non-compliance will be harshly penalized. The punishment is presumed to work as a deterrent against breaching the law. The regulator conducts itself like a policeman while in contrast, in compliance oriented approach, it behaves like a consultant (May and Winter, 2011). The relationship is not supportive and clientelistic.

The legalistic approach has its advantages. According to Yee *et al.* (2014), the legalistic approach inculcates a sense of fairness among regulated entities. This view is shared by Bardach and Kagan (1982) who argue that strict enforcement of rules eliminates discretion of the regulatory agency and promotes uniform treatment, consistency and equality. The same sentiments are shared by Bonkiewicz and Ruback (2010). In addition to that, Kagan (1989) states that strict enforcement may also curb corrupt activities as there is no room for discretion. The legalistic approach relies on rules and in that regard, it requires less effort in terms of supervision. Interaction between the regulator and the regulated entities is usually infrequent. According to Kagan (1989), typically the regulator responds to violations of the law through issuing of fines, notices of violation, closing down of businesses and prosecution. It takes a blanket approach and no exemptions are provided to special cases (Kagan, 1989). However, heavy enforcement of petty issues may waste the resources of the regulator.

However, according to Muhammad (2013), the legalistic approach can easily become inauspicious in as far as it awakens resentment and hampers mutual cooperation. Bardach and Kagan (1982) warns that the approach can result in costly and time consuming legal proceedings as there is no mutual cooperation between the regulator and the regulated entities. Cementing on that, Hawkins (2013) reaffirms that regulation without cooperation is meaningless, costly and ineffective. According to May and Winter (2011), regulated entities are likely to perceive the regulator as bully when they don't understand the regulations or why certain action is being taken. On the other hand, some regulated entities may also see the intimidations as hollow given the infrequency of sanctions issued.

Another drawback is that regulatory punishments that are castigatory in nature can backlash and cause resistance among the regulated entities. The study by May and Winter (2011) found that getting tough only works to a certain point, but beyond that, the threat of punishment becomes counterproductive. The study reveals that the effectiveness of coercion is low when the degree of formalism is high. This casts doubt on the effectiveness of an overly legalistic enforcement method.

2.4.2 Flexible/Compliance Enforcement

According to May and Winter (2000), the flexible style comprises a situational mix of the legalistic approach and the accommodative approach. Ferran (2011) describes it as judgment based approach. According to May and Winter (2011), this involves being strict and legalistic in some instance while being helpful and accommodative in others. Flexible regulation espouses doctrine of substantive rationality (Baldwin and Black, 2008). The case in point will detect the approach to be taken. The seriousness of the matter, the risk involved and the attitude of the regulated entity will be considered in deciding the stance to take. The enforcement style is tailored to suit the circumstances and the quality of interaction. The regulator will be active and carries out the enforcement functions in a cooperative manner.

Muhammad (2013) opines that flexible enforcement works on the basis of mutual understanding between the regulator and the regulated entities. According to May and Winter (2000), the approach is consistent with targeted enforcement, with high levels of enforcement and moderate stringency. Targeted enforcement will assist in channeling regulatory resources where they are needed most. The level of interaction with market players is high and the regulator provides advice.

According to Muhammad (2013), flexible enforcement is characterized of coaching, guidance, persuasion and consultations. Kagan (2001) commends the use of regular communication as it narrows the knowledge gap between the regulator and the market. Such cooperation makes it easier to resolve market disputes without costly legal proceedings. Further, exemptions can also be granted in special situations. Kagan (1989) points out that the regulatees can be given a second chance or more time to comply with the rules. He describes this enforcement as “welfare maximising” enforcement. It aims to prevent future violations as far as possible through voluntary efforts (Jones, 1998). It is compliance oriented.

The style puts emphasis on non-penal methods to secure compliance to laws. Sanctions are not often used as they disrupt the relationships (Almond, 2006). Punishment is used as a last resort. Jones (1998) advises that the typical methods of compliance in this approach include use of selective surveillance, warnings and promotion of self-regulation. Gray and

Shimshack (2011) argue that even a telephone call can be an efficient enforcement mechanism in some instances.

According to May and Winter (2011), the use of facilitative techniques helps to promote cooperation and build trust and confidence between the regulator and the regulated entity. Almond (2006) argues that cooperation enables the regulator and the regulated entities to enlist the assistance of each other in performing their roles. Sharing of information is very important. Yee *et al.* (2014) believe that regulated entities with more information are more likely to comply. The regulated entities may lack the sophistication and expertise to interpret the laws and some laws may be ambiguous and prone to various interpretations (Simila *et al.*, 2014). Counseling and advice will improve awareness of the laws and the means of how to comply. Inclusion of market players naturally enhances the quality of regulation and its collective acceptance. It follows that the flexible style is consistent with co-regulation.

Flexible enforcement is consistent with the theory of responsive regulation by Ayres and Braithwaite (1992). According to responsive regulation, regulators should use compliance strategies in the first instance and move to more deterrent measures when the regulatees fail to comply. Ayres and Braithwaite (1992) propose an enforcement pyramid, where at first; an explained disapproval should be used, followed by show of respect by regulated entity and thirdly, an acceleration of force of regulatory response.

This enforcement pyramid was heavily criticised by some scholars. Baldwin and Black (2008) argue that it may not be appropriate in some situations to take a step by step method up the enforcement layers. Some catastrophes require instant heavy responses and the pyramid approach frustrates justice. Another criticism comes from the operational approach of the pyramid. A regulator is expected to be moving up and down the ladder depending on the cooperation of the regulated entity. Baldwin and Black (2008) argue that it would be very difficult for the regulator to climb down the ladder because relations would already be tarnished. Further, the constant threat of the heavy sanctions up the regulatory pyramid can always allay fears and mistrust on the regulated entities. The approach assumes that regulated entities will respond to regulatory pressures. This is disputed by Baldwin and Black (2008) who argue that there are so many motivations for regulatory compliance and these include the culture of the industry, competition or even personalities of the regulatees.

The flexible approach has attracted a lot of criticism. It is difficult to sustain as it usually brings absurd results. Regulators should be fair, just and consistent in their regulatory activities. The market requires certainty of regulatory activities. According to Baldwin and Black (2008) the approach is very subjective and may result in unfair practices. There is no consistence and formalism. In addition, Simila *et al.* (2014) argue that flexible enforcement poses challenges in circumstances where the regulator is unable to grade or monitor the level of violations.

The flexible enforcement assumes that regulator and the regulated entities understand each other and regulated entities can anticipate the direction of the regulator. Baldwin and Black (2008) argue that this could be all wrong as regulation is so complex and mutual understanding may be absent, which results in a lot of distrust. He warns that it is difficult to shape regulatory relations and shared expectations about compliance. Baldwin and Black (2008) advise that such cooperative styles are susceptible to regulatory capture. Too much trust in the goodwill of the regulated entities will encourage exploitation by market players who are motivated by economic rationality. According to May and Winter (2003), the use of facilitation will become ineffective if it is too accommodative. This is supported by Ferran (2011) who argues that the flexible approach has the danger of backsliding into a *laissez-faire* style. It is also important to note that the study by May and Winter (2003) failed to find a noteworthy connection between enforcement style and compliance. This is however contrary to their previous studies (May and Winter, 2000).

2.4.3 Accommodative Enforcement.

According to May and Winter (2011), accommodative enforcement comprises both low levels of formality and coercion. May and Winter (2000) brands it as ‘conciliatory enforcement’, while Ferran (2011) describes it as ‘*laissez-faire* style’. Gakeri (2012) explains it as noninterventionist approach. It degenerates into deregulation. It is associated with very low levels of regulatory effort, low levels of stringency and jumbled enforcement. May and Winter (2011) describe this approach as highly unsystematic and somewhat facilitative. In this type of enforcement, the regulator sympathizes with the regulated entities and provides advice to the players. The regulator takes a responsive stance to issues raised by

regulated entities. Use of threats is very low and interactions with regulated entities are more informal and excessive.

Kagan (1989) describes this kind of enforcement as beyond reasonable accommodation. He denigrates this approach to 'retreatism'. The regulator confines itself to non-contentious matters and avoids hard decisions. The regulator backs at the smallest sign of opposition. Mcallister (2009) argues that the regulator takes an extreme advice and negotiation strategy and usually the outcome is a negotiated compliance. He argues that such regulators always holdup in taking actions and postpone decisions. They spend their time looking busy and creating meaningless regulatory paperwork. Reasons for inaction in accommodative style vary among regulators. Kagan (1989) assumes that some officials may be corrupt, lack legal authority or leadership skills and could be intimidated by market players or political authorities. Mcallister (2009) argues that continuous interaction with regulated entities may also result in regulatory capture, where the regulator will concentrate on the interests of the regulated entities at the expense of the public.

According to Kagan (1989), the accommodative approach falls into under-regulation. Efforts of the regulators can be easily diverted into trivial regulatory problems and superficial solutions. This enforcement style is consistent with the enforcement style of "avoiding" found by the study of Muhammad (2013). Muhammad (2013) points that the regulator may fail to find solutions and simply avoid the problem at hand. It involves very little effort from the regulator. The regulator will be inactive. According to Mcallister (2009), the regulator usually gets to know about enforcement problems through public complaints. May and Winter (2003) bemoans that such a too lax regulator may cause confusion about what is important.

The accommodative enforcement relies more on self-policing. According to Short and Toffel (2007), self-policing can bring positive results when the regulated entities report and self-correct their troubles, which the regulator would not have found. However, they cast doubt on the integrity of the regulated entities. They pledge evidence that point to the fact that most reported breaches of the law by regulated entities are often trivial, probably camouflaging more serious noncompliance.

It should be noted that enforcement styles are not easy to code. May and Winter (2011) and May and Wood (2003) agree that it is hard to pin down to specifics of the enforcement style. Nonetheless, even in situations where regulators adopt a mixture of the strategies, one strategy will tend to be dominant than the other.

2.5 APPROACHES TO REGULATION

The rule versus principle debate is particularly important in the assessment of the regulatory paradigm. The perspective from a purely rule based approach and the principles based approach determines the enforcement style and the regulatory strategies.

The debate about rules or principles is not only about the legal drafting of the statute. According to Ford (2008b), the implementation and approach of regulation is very critical. A regulator can interpret the rules in a more flexible way which resonates with principled regulation. An example is the case of the British Columbia Securities Commission which has changed its regulatory process to principled regulation in spite of principles based regulation having not passed into law (Ford, 2010). On the same vein the promulgation of a principled statute will not achieve good results without taking into account the regulatory implementation process. Ford (2008b) advises that a rule can be interpreted up or down, canvassing it like a principle or a detailed rule. He warns that principles may also lose their character if narrowly interpreted.

2.5.1 Rule Based Regulation

Rule based regulation is based on a set of rules and regulations that govern the conduct of the market participants (Anand, 2009). Nelson (2003) cited by Collins, Pacewark and Riley (2012) define a rule as specific criteria or threshold, scope of restriction, exception and implementation procedure. According to Ford (2008b) a rule is a tool that commonly defines what constitutes permissible conduct in advance. Ford (2008b) also states that in rule based system, interpretation is limited to the statute, while in principles based regime, interpretation is circumstantial and based on mutual understanding. He put forward that principles-based regulation is associated with outcome oriented approach while rule based is associated with a process oriented approach.

The use of rules has its merits. Leuz (2010) points out that rules are generally easy to apply. According to Ford (2008b) rules promote precision and expectedness in so far as they prescribe specific expectations prior to the action. They eliminate decision maker bias and uphold equal treatment (Collins *et al.*, 2012). They promote consistency and predictability (Moggs, 2009; Ford, 2008) as they are often applied without considering contextual issues. Rules contribute more to transparency by following a process oriented approach.

Rules also have drawbacks. Leuz (2010) avers that rules can promote devious behavior. This is supported by Ravenscroft and Williams (2005) who argue that regulatees can evade the law by engaging in activities that harm the spirit of the law, that are not captured by the rules. Rules send the wrong message that strict compliance is what matters most. Ford (2008b) provides an example of how companies can cheat. He states that companies may buy compliance programs that are modeled on the prescriptive requirements. Agoglia, Douppnik and Tsakumis (2011) describe such an arrangement as ‘transaction structuring’ to achieve the required result.

Further, Ford (2008b) acknowledges that whilst rules may be certain, they are rigid and not easy to change. The system of rules is also expensive in that typically the system responds to every new phenomenon in the market by adding more detail in the law. They require constant amendments as they can be outrun by market developments. Ford (2008b), further criticized rules as they can allow different handling of matters that are considerably similar, camouflage partiality and may be at the same time in excess of or under inclusive of material issues. Rules can be procedurally iniquitous, restrict flow of information and can inhibit mutual understanding. Rules can be theoretical and complex. The presence of rules and regulations does not guarantee good behavior. According to Castro (2011) other controls such as social norms, fear of reputational blot, lawsuits and market pressures can restrain the professional conduct of the firms

2.5.2. Principled regulation

According to Koutalakis, Buzogany and Barzel (2010), principles based regulation falls under soft law. Principles may take the form of standards, guidelines, recommendations, codes of practice, declarations and resolutions (Mwenda, 2006; Anand, 2009). Principles are different from the hard law of rules, which are clearly delineated and uniformly binding.

Principles are less specific (Collins *et al.*, 2012). Principled regulation is associated with a bottom up approach of regulation, where the regulator takes advantage of the experience of the regulator. The top down approach of rule based system create a one size fits all industry and according to Ford (2008b), that is not effective.

Ford (2008b) advocates that the legislation should be in simple and plain language and the statutes should contain less detail. More details should be filled by the regulatory agency's rule making powers. The legislation should be result oriented rather than process oriented and should provide general details. Ford (2008b) avers that principles based regulation is underpinned on notions of co-regulation or enforced self-regulation. It encourages cooperation with the industry in that principles respond more flexibly to the changing dynamics of the market (Ford, 2008b). According to Koutalakis *et al.* (2010), principles are bendable and can be tailored to changing circumstances without any supporting rules. They do not require constant amendments and are less expensive to promulgate.

Cohen, Krishnamoorthy, Peytcheva and Wright (2013) believe that principles encourage companies to understand the spirit of the law rather than cosmetic compliance associated with rules. In addition, Challagalla, Murtha and Jaworski (2014) argue that principles-based regulation prevents the checklist style which is associated with rules regime. It is argued that use of principles improves compliance behavior. However, according to Ford (2008), the uncertainty poised by principles may inhibit risk averse regulatees from engaging in new lawful activities. Ideally, the conduct of the regulator should be predictable and reasonable at all times. The inherent uncertainty in principles based- regime can result in confusion among regulated entities.

Another advantage of principles based regulation is that it shifts the decision making role from the regulator to the regulated entities by allowing them to strategize on how to achieve the regulatory role (Leuz, 2010). Individual firms can use their discretion on how to comply with the law (Cohen *et al.*, 2013). Principles simplify decision making process. They do not provide execution details, thus allowing flexibility (Challagalla *et al.*, 2014). However, Leuz (2010) warns that this discretion may allow managers to pursue underhanded reporting motives. This is supported by Ravenscroft and Williams (2005) who avow that principles provide an avenue for self-interested manipulation.

Nonetheless, Collins *et al.* (2012) dismiss the fears of self-interested manipulations. While they acknowledge the potential for differences, they assert that well trained professionals will decrease the variations when they apply good judgment. It is also argued that increased disclosure requirements under the principles-based regime will minimize variations (Agoglia *et al.*, 2011). However it is worthy to note that the experiment by Agoglia *et al.* (2011) found no difference in outcomes between Chief Financial Officers under a rules-based system and principles-based system. Also, the study by Bailey and Sawers (2012) found that the type of standard, rules-based or principle-based, did not affect investor decisions. However, Collins *et al.* (2012) dismiss the argument that rules and principles produce the same results. They argue that the supposition has not been empirically tested. They agree with Ford (2008b) who maintains that principles run the risk of encouraging arbitrary and outwitting discretion by regulators.

Principles regime requires more resources Ford (2010) reckons that regulators should possess more competence in terms of manpower, access to information, skill and outlook to be effective in principles based regime. Ford (2008) argues that principles-based regulation requires continuous guidance of companies by the regulator and effective analytical tools to evaluate the regulatory success. There is need for more understanding and mutual interaction between the regulator and the regulated entities. The regulatory culture should be that of a more credulous and communicative rapport. This means the regulator will require more manpower that is highly skilled to deal with the reactive regulation.

2.5.3. Hybrid Rule Based and Principle Based Regulation

A regulatory system can be a combination of both rules and principles. Ford (2008b) argues that it is rare for a regime to be purely rule- based or principle based. He conjectures that distinctions may not be easy to draw between principles-based regulation and rule-based regulation. Different regimes can be comparatively rules based or principles based. Rules and principles can overlap and are more of positions on a scale and they complement each other. Nonetheless, Ford (2010) argues that it is possible to distinguish a regime that primarily operates under rules and that operates under principles. According to Ford (2008), striking a balance between rules and principles involves judgment about priorities and concerns. He

surmises that principles- based approach will look at principles wherever possible before resorting to rules.

According to Campos (2007), what matters is not whether or not principles are better than rules. The important thing is whether the approach is effective for a particular jurisdiction. Ford (2008) argues that, in practice, certain aspects of regulation are treated in a more principles based or rule based approach. He supposes that issues of administrative justice and fairness and periodic and prospectors disclosure are process oriented, while issues relating to compliance, material facts and change disclosure are principles oriented. Walker (2007) believes that financial reporting can achieve better results under a principles based regulation rather than detailed rules. This however does not imply that the choice between the two approaches is of no value.

Theoretically, a hybrid system can involve some kind of a midpoint between the rules based approach and the principled based approach or perhaps a system that gives the industry a choice between the two systems (Ford, 2008b). A hybrid regime can allay industry fears about the weaknesses of a purely one sided regime. It enhances cooperation in the regulation of the market. However, Ford (2008) warns on the danger of relying on such a system. He argues that the system can be hoodwinked. This is supported by Ford (2010) who cautions that such regulatory model can slither into self-regulation if regulation is weak. Non-compliant firms would strategically choose to rely on the system that favors them. An example is where a firm argues that it relied on rules when it favors its outcomes even though when the actions breaks the spirit of the law. The opposite can also be true if it is relying on principles. Ford (2008b) also warns that companies can avoid the costs and holdups associated with seeking approvals for issues that can be shoehorned into rules.

In addition, Ford (2008b) argues that the rules versus principles options would, in most cases, slither to rules. Principles will be relegated to service of last resort and after the fact justifications. To avoid this, Ford (2008b) stresses that the regime should emphasize that firms should equally comply with both rules and principles. The system should not operate in parallel terms; rather, it should be serial.

2.6 REGULATORY MODELS

According to Groenleer (2014), the choice of regulatory design is an important subject in public administration. The regulatory design affects the rights of the market players, the power of the regulator and the rights of investors. The fundamental issue in the context of regulatory option is whether the arrangement is effective and sustainable in meeting the societal interests (Saurwein, 2011).

2.6.1 Pure Government led model

According to Castro (2011), government led regulation also called state regulation, involves a government institution regulating the conduct of firms in the private sector. The state is exclusively responsible for all the regulatory operations and market intermediaries are not involved in regulation. The government will have oversight and control over individual firms through state directives and rules and regulations. The system is also portrayed as the command and control rule (Bartle and Vass, 2007).

According to Parker and Kirkpatrick (2012), state regulation is justified where there are considerable externalities and information asymmetry or where it is in the interest of the public to do so. They believe Government regulation ensures uniformity, transparency and protection of investors. Mor, Miller and Clark (2010) argue that state regulation is crucial when consumers are not able to discern quality variations among services and products. Government regulation is also appropriate when consumers are considered vulnerable and can simply be taken advantage of.

The study by Aghion, Algan, Cahuc and Shleifer (2010) found that government control is strongly and depressingly correlated with trust. They developed a model which predicted that lack of trust influences regulation and increase the need for government regulation. This is despite the realization that the government may be corrupt or futile. People would prefer the government itself to restrain the unprofessional conduct of the industry. While Aghion *et al.* (2010) admit that Government may be awful; they believe the industry is shoddier. The same view is also shared by Rafael and McCulloch (2009). Zhang (2006) argues that the state is the only institution that has the resources and the power to guide, initiate and sustain the regulatory function. He believes that the state has a politically sustainable balance of power between the public interests and the private sector interests. His sentiments are shared by

Faerman, McCaffrey and van Slyke, (2001) who believe that government regulators have greater motivation to control and prevent market failure in order to maintain investor confidence.

On the flip side, Castro (2011) argues that government regulation poses a threat of overregulation and can inadvertently result in creation of barriers to competitive entry and innovation. He claims that government regulation increases regulation costs and production costs which are ultimately passed on to the consumers. Further, Government regulation is typically statute based. Brown (2006) bemoans the inflexibility of statutes compared to self-regulatory structures. O' Driscoll and Hoskins (2006) perceive government regulation as ineffectual, superfluous and counterproductive. They argue that there must be some additional factor to attenuate government regulation.

In addition, Arthur and Booth (2006) argue that the state may pursue its own interests other than those of the people they are regulating. They further state that, the state may not know or understand the objective of those they are regulating. The Government is an outsider and that in itself imposes supervisory challenges to the rapidly ever changing processes of the market. Baldwin and Black (2008) argue that government should in the first instance offer self-regulatory solutions to the market, if it fails, the state may escalate to enforced self-regulation under command and control regime. They argue that the non-discretionary command and control style should be used as a last resort.

2.6.2 Self-regulation

Castro (2011) defines self-regulation as a system where market institutions manage their conduct through voluntary agreements and self-policing activities. According to Bartle and Vass (2007), the regulation of the individual organizations is done by themselves, rules are self-specified and self-enforced and there is little or no role by Government. According to Gakeri (2012), self-regulation in the capital market is typically exercised by a securities exchange which establishes conduct rules that bind its members and sets out criteria for admission, supervises, investigates and disciplines the behavior of its members.

Saurwein (2011) identifies two forms of self-regulation. The first is “self-regulation in the narrow sense” which functions exclusive of any formal government participation. The second

scenario is “self-regulation in the broader sense” which comprises other forms of government contribution in self-regulatory organizations, other than from a legal basis.

Bartle and Vass (2007) also identify two broad forms of self-regulation in relation to the state, namely “mandated” and “non-mandated” self-regulation. The mandated self-regulation comprises three types of regulation, namely “cooperative”, “delegated” and “devolved”. Cooperative involves the cooperation between the regulator and the self-regulating body in the development and execution of statutory regulations. In delegated regulation the state agency entrust statutory obligations to a self-regulatory body while in devolved, self-regulatory schemes are specified in the law and devolved to the self-regulatory organization by the legislature. The non-mandated form entails facilitated self-regulation and tacitly supported self-regulation. Under the facilitated arrangement, self-regulation is openly and proactively supported by the Government although it is not sustained by statute. In tacitly supported schemes, Government support is covert and the voluntary actions of the organizations are conditioned and guarded by the state (Bartle and Vass, 2007)

Brown (2006) avers that there are some systems that are positioned as self-regulatory although they have no control over their codes of conduct and sometimes the codes are imposed by the state. He argues that it is not self-regulation and at worst it can be described as state regulation. Martinez, Verbruggen and Fearn (2013) waters down all the arguments about self-regulation and contends that self-regulation is just a mere tool which government uses to control society and individuals. He believes that government will always have a role in market transactions.

There are a variety of factors which influence self-regulation. According to Sharma, Teret and Brownell (2010), self-regulation maybe implemented as a response to threats of excessive regulation by the government or no regulation at all. It can also be promoted on the basis of efficiency and expertise. Short and Toffel, (2010) argue that the increase in scope and complexity of regulatory demands push companies to turn to self-regulatory structures. On the other hand, Castro (2011) argues that self-regulation may even occur in a tightly regulated market, where industry institutions form cooperative agreements to regulate industry standards. Also, Saurwein (2011) believes that the reputational sensitivity of the market play a pivotal role on the achievability of self-regulation. The more the success of the

businesses depends on the reputation of the market, the more the feasibility of self-regulation practices.

The study by Short and Toffel (2010) examined how the regulatory enforcement activities may create the legal atmosphere in ways that may be conducive to self-regulation. They found out that enforcement strategies and relationships of the legal surroundings play a crucial part in moderating the implementation of organization's dedication to self-regulate. They conclude that coercive power by the state can undermine more normatively based motivations to self-regulate as direct regulatory coercion obstructs the attainment of self-regulatory commitments.

Self-regulation has several advantages. Self-regulation may result in a win-win situation between the public and the private sector. Arthur and Booth (2006) aver that a competitive market can be a better regulator than the state. They believe that stock exchange rules can adequately deal with corporate governance issues. Saurwein (2011) also believes that the society can benefit as a whole from the self-regulatory mechanisms if private interests coincide with public objectives. Short and Toffel (2010) are optimistic that the legal environment as constructed by the enforcement actions of the supervisory bodies will greatly influence the self-regulatory bodies to effectively implement their regulatory commitments. They argue that self-regulation reduces Government costs especially in period of budgetary deficits and increasing demand of regulation.

Nonetheless, Short and Toffel (2010) argue that the concept of self-regulation has not been fully explored. Bartle and Vass (2007) believe that self-regulation is incompatible with public interest and is the natural end point of regulatory capture. They argue that self-regulatory bodies can form cartels which work against the public interest. This is supported by Brown (2006) who argues that self-regulation is not an instrument for social engineering. Further, Bartle and Vass (2007) argue that meeting the public interest with state regulation is not straightforward, and that it is even more complex with self-regulation, dismissing the idea that self-regulation can work.

2.6.3 Co-regulation/ cooperative regulation

According to Marsden (2012), co-regulation is a fusion of regulation that encompasses various stakeholders and a combination of general legislation and self-regulation. The state and the market intermediaries share the role of regulation (Castro, 2011). It is a blend of self-regulation and government regulation. Bartle and Vass (2007) describe this mix as a grand project of “high modernism” as a result of globalisation.

The extent of this hybrid model differs from one jurisdiction to another (Castro, 2011). According to Bartle and Vass (2007) one interpretation of co-regulation stresses the central role of the state while on the other hand the state takes a modest role. Marsden (2012) illustrates that co-regulation may involve a government regulator having oversight over a self-regulating organisation or enforcing sanctions for a self-regulating organisation.

As pointed by Martinez *et al.* (2013), literature has exhibited confusion on the distinction between co-regulation and self-regulation. Saurwein (2011) supports this view when he states that there are varying definitions of self-regulation, co-regulation and government regulation. What is clear from literature is that the models of regulation are conceptualized in terms of state involvement. Martinez *et al.* (2013) argue that even the purest form of command and control rule may show traces of self-regulation.

The issues that affect the complementarities of private and public regulation are multifaceted. Verbruggen (2013) avers that the overlap of the standards, objectives and interests of the private actors and the state creates leverage and scope for collaboration. Further, the institutional design of the regulatory enforcement offers the state and the private actors the possibility to coordinate regulatory activities. The qualities of the private actor standards also determine the extent of cooperation between the public and the private sector. Verbruggen (2013) argues that Government is likely to delegate its regulatory powers to a private actor only if it follows due process. Fairness, expertise and independence of the private actor enable it to make competent regulatory decisions. In addition, coordination of regulation requires openness and sharing of information (Martinez *et al.*, 2013).

Martinez *et al.* (2013) suggest two approaches to co-regulation, the bottom up approach and the top down approach. In top down approach the Government will have an upper hand and

will set standards for operations. Conversely, bottom up approach acknowledges, facilitates and supports private regulation. In this case the private sector may carry on regulatory activities without state control. Ford (2013) came up with the concept of “Innovative Framing Regulation” which puts emphasis on the private sector innovation. In this arrangement, Government regulatory prescriptions can be used to “steer and not row” the processes. The finer details of regulation will be left to the private players and the state will only set principles. This model is ideal where the state cannot keep pace with private sector innovations.

In support of co-regulation, Dill and Beerkens (2012) argue that self-regulatory actions are not sufficient for assuring standards that are associated with globalization. The CFA Institute (2013) amasses this view when it states that self-regulation has taken much of the blames for the 2008 financial crisis. On the other hand, Governments may lack resources, knowledge and competence to address governance issues. McCaffrey *et al.* (2006) believe that it is not possible for the regulator to supervise directly all the large volumes of private sector transactions. They believe regulators cannot comprehend the complex industry technology as they do not work with it on a daily basis and that co-regulation will serve the regulator from regulatory breakdowns.

Verbruggen (2013) argues that engagement with private regulatory establishments enables public regulators to redeploy their miniature enforcement budget to big issues. The private establishments can only refer complex cases that are beyond their competence to the public regulator. Such collaboration between the regulator and private organizations prevents possible enforcement gaps. It promotes flexibility, creates a win-win situation and builds trust (Martinez *et al.*, 2013). Further, since co-regulation survives on consultation and feedback, it may lead to the adoption of specific and tailor made requirements for the industry.

However, it should be noted that co-regulation may pose challenges when the private and the public interests do not match. Martinez *et al.* (2013) argue that the public authorities cannot rely on private sector as they can be embroiled in regulatory capture. Further, the regulatory process may be watered down by the voices of the strong market players, to the disadvantage of the minority. It is extremely difficult to achieve an appropriate balance of co-regulation.

Martinez *et al.* (2013) further warn that in case of regulatory failure it is difficult for accountability and to apportion blame. The private sector will always deny responsibility and it is difficult to put accountability measures on private sector. According to Saurwein, (2011), a winning cooperative model depends on the mix of measures and sufficient amount of state involvement. More intense mode of government participation is warranted when there is severe negative impact of regulatory malfunction. Major conflicts of interests between the private and public sector also deserve more state intervention.

2.7 THE REGULATORY TRENDS IN OTHER JURISDICTIONS

The regulation of capital markets has significantly changed in developed economies. According to Gadinis and Jackson (2006), the transformation of the ownership structure of stock exchanges which were previously run as mutual societies has forced regulators to re-examine their regulatory strategies. Gadinis and Jackson (2006) aver that most exchanges underwent the demutualization process and privatized. Some exchanges went to the extent of listing on self. In addition, a number of huge corporate scandals in the securities industries forced regulators to relook on their regulatory management structures (Agoglia *et al.*, 2011; Bailey and Sawers, 2012; Staikouras, 2012 and Subramanian, 2011).

The survey by Gadinis and Jackson (2006) found that there are three regulatory models being used worldwide. They established that the Government led model is generally used in Japan, German and France. The Flexibility model, which places heavy reliance on market participants, is typically used in Australia, United Kingdom and Hong Kong. According to Gadinis and Jackson (2006), Canada and the United States of America use the Cooperation model, where stock exchanges have regulatory powers over most operative issues, but under the supervision of a government agency.

According to Brewer, Gough and Shar (2011), the Financial Services Market Authority (FSMA) in the United Kingdom relies more on principles. Ford (2008b) argues that the FSMA was not blatantly principled based but it used its regulatory command to mould a principled based regime. The regulatory behavior of FSMA is more supportive and characterized with mutual cooperation (Ford, 2008). There is consultation and cooperation between the private and the public sector (Saurwein, 2011). According to Ford (2008), the

FSMA uses a compliance oriented approach in terms of enforcement. Ferran (2011) points out that the FSMA coined its enforcement strategy, ‘credible deterrence’.

The United States system is rule based and the system applies even to foreign issuers (Brewer, Gough and Shar, 2011). Compos (2007), a commissioner at the United States of America’s Securities and Exchange Commission however made remarks that where possible the United States of America will use principles. His statement only serves to reveal that principles are only used as a last resort. Ford (2008b), however indicates that the Derivative market in the U.S tends to be principles based regulation. In Washington, the answer to failed regulation is more regulation (Pritchard, 2003). Hawkins (2013) states that the United States of America uses coercion and detailed regulation. This is confirmed by Brewer *et al.* (2011) who argue that the United States of America comparatively inclined to issue sanctions to achieve compliance.

According to Gakeri (2012), regulation in Kenyan capital markets is largely Government led with insignificant traits of self-regulation. Gakeri (2012) avers that the Capital Market Authority (CMA) of Kenya has absolute legislative and supervisory powers over regulated entities. The regulator is not subject to any meaningful accountability mechanisms. However the research by Gakeri (2012) found no clear enforcement philosophy of the Kenyan capital market authority. He argues that the enforcement activities of the CMA were sporadic and reveal no imperatives. From the period of 1990 to 2012, the enforcement style of CMA varied with the chief executive officer. The inclinations of the incumbent chief executive officer influenced the enforcement style. Between 1990 and 1994, there were no enforcement actions as CMA was fairly new. The CMA took a fault finding and heavy handed approach between 1995 and 2002. A non-interventionist approach was adopted between 2003 and 2007. The CMA again took laissez-faire approach between 2008 and 2012 which later demonstrably changed to an overreaction when a number of companies failed.

2.8 CONCEPTUAL FRAMEWORK

The conceptual model posits that regulators who are more on the public interest view pursue the pure government model, legalistic approach and a rule based system. The model sheds

light on how the regulatory model is connected to the regulatory approaches and the enforcement style.

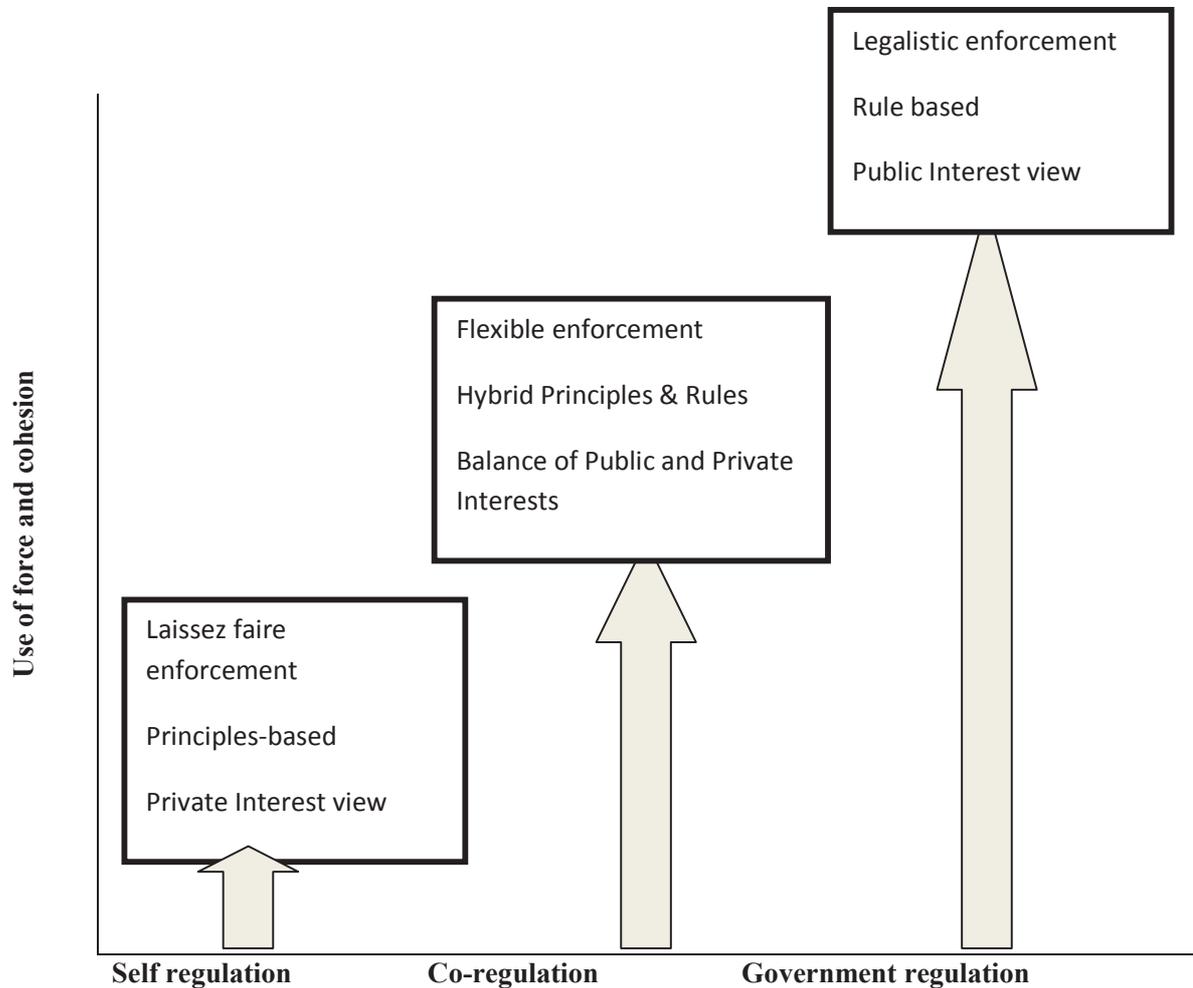


Figure 2.1: Conceptual diagram

Developed for the study

2.9. LITERATURE SYNTHESIS

The literature reveals that execution of regulation is influenced by the legal, societal, economic and political issues. The models of regulation are conceptualized in terms of a continuum of the variety of levels of state involvement. Similarly, the enforcement styles can be categorized in terms of the varying spectrum of pure legalistic approach to under-regulation. Regulation also takes place in a gamut between extreme uses of rules to pure principles. A clear understanding of the role of the state in the regulatory matrix will enable

an accurate classification of the regulatory philosophy of capital markets authorities. The next chapter outlines the research methodology adopted in this study.

CHAPTER THREE: RESEARCH METHODOLOGY

3.0 INTRODUCTION

Chapter three describes the methods that were adopted in gathering information for the study. It discusses the research paradigm and the research design that were used. The chapter highlights the research philosophy, target population, the sampling method and the research instrument that were used to obtain information. Reasons for the adoption of the methodology are also explained.

3.1 RESEARCH DESIGN

3.1.1 Research Philosophy

The research sought to establish the regulatory epitome of SECZ. A holistic perspective of the regulatory actions of SECZ assisted in the understanding of its regulatory behavior and why they act the way they do. The research was therefore qualitative in nature and was premised on the constructivism approach. Qualitative research explores the meaning and reality of the phenomenon under research (Staller, 2010).

Saunders, Lewis and Thornhill (2009) assert the importance of an empathetic stance in interpretive philosophy. The researcher should understand the world of the respondents from their own point of view. Fraenkel and Wallen (2006) reaffirm that a qualitative research focuses on the analysis of the attributes or qualities of the activity, situation or group and does not focus on the frequency thereof. In contrast, quantitative research aims at producing statistical generalizations (Eriksson and Kovalainen, 2008). This research focused on the contextual and interactive characteristics of the regulation by SECZ; hence it took the qualitative approach.

According to Tewkbury (2009), qualitative research offers more informative and richer data for a better understanding of the phenomenon. The focus of qualitative study is to examine the individual personal experiences and the value which a person attaches to certain events (Devetak, Glazar and Vogrinc, 2010). It provides textual descriptions of how the regulated entities experienced the actions of SECZ. The study examined how the regulatory behavior of SECZ was perceived.

3.1.2 Research Approach

The research used an inductive approach. In inductive approach, data is used to construct the theories and concepts (Hancock, 1998 and Harwell, 2011). Data collected from respondents was used to construct the enforcement style, the approach to regulation and the regulatory model.

3.1.3 Research Strategy

The research was centered on the regulatory activities of SECZ and took a case study approach. A case study is defined as an in-depth study of a phenomenon (Blatter, 2008), within its actual life perspective using data from a variety of sources (Robson, 2002). Data was obtained from various licensed entities and from SECZ officials.

3.2 POPULATION AND SAMPLING TECHNIQUES

3.2.1 Target Population

The term population refers to the aggregate or total individual units or units of analysis. Robson (2002) defined a research population as a collection of individuals or objects known to have similar characteristics. The population under research is as follows;

Type of Entity	No of companies
SECZ	1
ZSE	1
CSD	1
Licensed Securities Dealing Companies	13
Registered Asset Management Companies	15
Licensed Transfer Secretaries	3
Licensed Custodians	5
Licensed Investment Advisors	25

Table 3.1: Population Description and Size

3.2.2 Selection of Participants

The study used a non-probability sampling method, where the sample was gathered in a process that does not give all individuals in the population equal chances of being selected. A purposive sampling procedure was employed to select the respondents. Purpose sampling is a procedure in which the researcher uses his/her judgment to pick candidates to be included in

the sample (Abrams, 2010). In this study, the basis of selection included eagerness to participate, capacity and perceived knowledge of the subject in line with Oliver (2006)'s assertions. Since the drawing of inferences to the population was not the highest priority in this research there was no reason to assume a 'normal distribution' to the relations and the experience of the research subjects. The method enables the researcher to get detailed information from persons with interest and in-depth knowledge on the operations of the SECZ.

3.2.3 Sample Size

According to Guest, Bunce and Johnson (2006), theoretical saturation is the gold standard that determines the sample size for a purposive research. The sampling was aimed at achieving comparability across the different categories of the population and to find instances that are representative to the dimension of interest. The researcher selected the companies with extreme records of success and failure and those that were once suspended. The sample also took cognizance of the fact that SECZ started regulating asset managers in 2014 and investment advisors in 2012 and therefore did not have much experience with SECZ. The research concentrated on the stockbrokers, custodians transfer secretaries and the ZSE as they started with SECZ from inception. According to Teddlie and Yu (2007), outlier sampling brings valuable information about the subject of interest. Since the study is based on a case study, the study targeted officials from SECZ and licensed entities.

Population Description (Principal Officers)	Population Size	Sample Size
SECZ	5	4
ZSE	3	1
CSD	3	1
Licensed Securities Dealers	13	7
Registered Asset Managers	15	3
Licensed Transfer Secretaries	3	1
Licensed Custodians	5	2
Licensed Investment Advisors	25	3
Total	72	22

Table 3.2 Sample Size

Source: Developed for the Research

3.3 SOURCES OF DATA

Primary and secondary sources of data were used. Primary data was collected through in-depth interviews. Apart from the interviews, the researcher also used archival documentary records such as the statutes, directives and notices issued by the SECZ as well as court records. Secondary data was obtained from ZSE records and other SECZ records.

3.4 INTERVIEW GUIDE

The research was conducted using a semi structured interview guide. The interview guide was pre-tested to a few industry experts. The interview guide was circulated in advance to the selected respondents so that they could be able to prepare detailed responses. The interview guide contained open ended questions to allow respondents to give more detail on the issues under investigation. The questions were framed in line with the research objectives and the themes outlined in chapter two. The interview guide is attached in the appendix section.

3.5 DATA COLLECTION PROCEDURE

3.5.1 In-depth Interviews

In-depth face-to face interviews were conducted with selected respondents. In-depth interviews are good for collecting information on people's experiences and perspectives. The interviews helped with a deeper insight and collection of rich data. The researcher had an opportunity to probe the respondents on unclear issues.

The interviews were recorded with the consent of the respondents, while researcher was concentrating on listening and asking of questions. The interviews were transcribed immediately after the interviews.

3.5.2 Archival records

Payne, Finch and Tremble (2003) define archival data as raw information that were gathered prior to the time of the research. Court proceedings, directives and notices provided a large

amount of information about SECZ interactions. This data contained information at various points in time of SECZ life and were easier and convenient to get. The archival data did not contain all variables and hence the emphasis on the use of in-depth interviews.

3.6 DATA ANALYSIS

A thematic analysis approach was used. The main themes and common issues were identified across all interview texts. Data was classified and coded and a descriptive account of data was produced. An interpretative approach was used to infer meaning to the text.

3.7 TIME HORIZON

Due to the limited time frame, the research was cross sectional. A cross sectional study is a snap shot of a phenomenon at a particular point in time (Saunders et al., 2009). However, archival records provided longitudinal data which enabled the tracing of trends over time.

3.8 VALIDITY AND RELIABILITY

According to Saunders, Lewis and Thornhill (2009), validity is concerned with whether the results of the research are truly concerning what they appear to be. Reliability refers to the degree to which the applied research procedures will yield consistent results, (Easterby-Smith, Thorpe and Jackson, 2008). The researcher pre-tested the interview guide with two securities dealers and one officer of SECZ to ensure that it covered the real issues. Interviews were recorded and immediately transcribed soon after the interviews. The researcher accurately recorded the data and maintained an objective stance to avoid bias.

3.9 ETHICAL CONSIDERATIONS

According to Cooper and Schindler (2008), ethics are the behavioral customs and values that guide people's conduct and their interactions with others. The researcher obtained formal permission from the SECZ's Chief Executive Officer to conduct the research on the operations of the organization. The letter of permission is attached in the appendix section.

The researcher maintained an independent and objective stance in her research. The research report was recorded accurately and without bias. Participation of respondents was voluntary and interviews were conducted at the offices of the respondents. All the respondents chose to

use their offices and they also selected time that was convenient to them. The purpose of the research was explained to all the participants. The researcher sought the respondent's permission to tape record the interviews. To maintain confidentiality, the respondents' views were coded and the respondents were referred to with that code. The coding system was as follows:

R = Respondent: there will be a corresponding number which is simply for identification. The number also signifies the sequence of how the respondents were interviewed. All the documentary evidence that were used is in the public domain and they were referred to by their exact citations.

Respondents were assured that information obtained from them would be treated as highly confidential and was meant to be used for academic purposes only. On use of archival records, the researcher used information that was already in the public domain such as notices, mass letters, court records and directives issued by the SECZ.

3.10 LIMITATIONS OF THE STUDY

The researcher could not interview all players licensed by SECZ and officers of SECZ due to time constraints. Further, the study did not reach out to the investors and listed entities who are the ultimate beneficiaries of the regulatory activities of SECZ. However the respondents who were interviewed provided a fair view of the SECZ regulatory implementation process.

3.11 CHAPTER SUMMARY

The chapter set out the research methods that were used to meet the objectives of the study. The research took a qualitative approach and a case study strategy. Purposive sampling procedure was adopted and face to face interviews were conducted. Archival records were used to complement the in-depth interviews. The next chapter presents the study's findings.

CHAPTER FOUR: DATA PRESENTATION, ANALYSIS AND INTERPRETATION

4.0 INTRODUCTION

This chapter presents the findings derived from the in-depth interviews conducted in collecting the data as well as the examination of archival records. The analysis of data was driven by the fundamental goal of establishing the regulatory philosophy of the SECZ, which comprises factors that influence the philosophy, the enforcement style, whether SECZ is principles based or rules based and the level of cooperation between the SECZ and market participants. The characteristics of the study respondents were also discussed

4.1 CHARACTERISTICS OF THE RESPONDENTS

A total of 22 principal officers from SECZ and licensed entities were interviewed. Table 4.1 reflects that nineteen of the respondents who were interviewed were male while only 3 were female. These results confirmed the heavy dominance of males in the capital market in Zimbabwe. At the time of conducting this study, it was established that out of the forty one securities dealers approved by SECZ only two were women. These dealers are all affiliated to the thirteen registered stock broking firms.

Table 4.1: Bibliographical Data

Item		Frequency
Gender	Male	19
	Female	3
Age	Less than 30 years	0
	31-40 years	10
	40+ years	12
Experience	6-10 years	5
	10+ years	17
Qualifications	Undergraduate Degree	14
	Masters Degree	8

Source: Primary Data

The research targeted principal officers of the regulated entities and senior officials in the operational departments of SECZ namely Supervision and Surveillance, Corporate Finance and Legal and Licensing. For the licensed entities, principal officers are specifically approved by SECZ to be in charge of the licensed entity. For the SECZ, CSD and ZSE the principal officers were people in charge of the relevant departments. All the respondents had over 30 years of age reflecting that the respondents were all mature and able to give well-reasoned responses. As high as eight respondents held masters' degrees and all the respondents had at least a minimum of a first degree. This development was in line with the SECZ's Securities (Registration, Licensing and Corporate Governance) Rules, SI.100/2010 that stipulate that every licensed entity had to be managed by a principal officer with at least a first degree and a minimum of five years experience in a discipline related to the specific licensable activity. These results clearly showed that the majority of respondents had worked in the capital market prior to the establishment of the SECZ and therefore would be in position to understand the regulatory behavior of SECZ over the period that was under study.

4.2 RESEARCH FINDINGS

4.2.1 FACTORS INFLUENSING SECZ REGULATORY PHILOSOPHY

4.2.1.1 Independence of SECZ

The majority of the respondents (17 out of 22) identified the independence of SECZ as one of the major aspects that determine its regulatory approach. The respondents defined independence in various terms. It was noted that SECZ is subject to state control as it reports to the Ministry of Finance. The Ministry of Finance also makes the final budgetary decisions of SECZ and appoints the SECZ board of commissioners. The respondent R6 confirmed that though the SECZ budget as prepared by SECZ was subject to approval by the Ministry, there were usually "no major changes".

On political independence, the respondents generally agreed that SECZ was fairly independent. A custodian R1 said "Political influence is not apparent despite the fact that the commissioners are appointed by the Minister". This was supported by R22 who emphasized that the commissioners were appointed according to their qualifications and expertise in

disciplines prescribed by the Act. She described the Commissioners as “highly spirited, qualified and objective in their deliberations”. It was noted that, section 5 of the Securities Amendment Act No. 2 of 2013 stipulates the criteria and specific qualifications that should be held by commissioners. Despite having no specific examples, R19 was of the view that political influence could not be ruled out because “SECZ is too close to the Ministry and that tends to take away its independence. The reporting structure takes away its independence”.

From a different perspective, R8 explained SECZ independence when she stated that the SECZ Investor Protection Fund is not administered by SECZ. According to her, the arrangement removed SECZ biases with regards to the fund’s pay outs. Further, R5 was happy that the board of SECZ did not have any market player who could be compromised. In addition, R18 commended the fact that SECZ is funded by the market and not by the government, “which limits government control over budgetary matters”. Concern was however raised by R6 who commented on the move by Government to prescribe salaries of state institutions. She saw that as a threat to the independence of SECZ.

There was dissatisfaction from R1 who believed that there was influence from market players in the SECZ decision making in view of the fact that some SECZ officials used to work in the market and had prior relationships with the market which he felt negatively affected their regulatory decisions. This was however dismissed by a considerable number of the respondents (10 respondents) who were asked to comment on that assertion. Ridiculing the assertion, R3 commented “Yes people may try to use connections but it does not affect the decision making process. These people are professionals. It’s not much about background. It’s a team made up of professionals and they understand their obligations. It’s actually an advantage because issues in the capital market are not learnt from school. They are learnt from practice and they have the necessary experience.” No evidence was produced to show any biases of SECZ employees.

Also on the negative, four respondents (R1, R2, R3 and R5) believed that there was regulatory capture from big companies. A stockbroker R2 said, “The market is not clean but there is lot of political influence, COWARDS! I will give you particular examples; the ZSE’s purpose is to protect minority shareholders and hasn’t seen it or SECZ protecting minority shareholders. These guys are being messed up left right and centre by these listed big

companies. I can name many from Econet all the way down”. This was echoed by R3, “SECZ does not have power over listed companies and ZSE also has very limited powers”. Overall the results revealed that though SECZ enjoyed some autonomy, its independence was compromised.

4.2.1.2 Availability of Resources

Concerning the availability of resources, the financing of SECZ’s activities was also cited as a factor that determined its philosophy. There was a general consensus among the respondents, including the respondents from SECZ that the market was small and not performing well. The respondents pointed out that since 2009 “the turnover had remained sluggish with acute liquidity challenges, dampening potential revenues for the SECZ”. It was noted that SECZ income was derived from levies charged per market transaction in terms of SI.108/2014. Emphasizing the acute shortage of SECZ resources, R1 said, “SECZ income is depended on the performance of the market and that can actually influence their decisions....if the decision affects market turnover, I doubt if they would make such a decision”. According to R22, “SECZ has never received any funding from Government and has also not been lucky with donor funding”. Confirming the crisis, R2 said, “Brokers were forced to reduce their commission to accommodate the Commission through securities levy. In other countries securities commissions are funded through these multi donor agencies, World Bank and the government. Here we are asked to fund and that’s what delayed the operationalisation of SECZ, because there was no money”.

In terms of skills resources, there was general consensus among the respondents who agreed that shortage of skills also affected the operations of SECZ. The respondents (R1, R3, R4, R8, R19 R14, R21 and R22) explained that SECZ’s regulatory implementations process was guided by the cost implications to the regulator and the licensed entities in view of the difficult economic environment that obtained. A SECZ official R8 said, “The number of officers we have in our surveillance department is not enough to cover the whole market. For us to be effective, we need to beef up our surveillance team and to increase the frequency of inspections.” In the same vein R19 remarked, “SECZ is constrained in terms of resources and it tends to be reactive rather

than proactive. You wouldn't want the regulator to be lagging behind.... The major handicap is resources and technical knowhow”.

4.2.1.3 Legal Authority

Lack of adequate authority was also cited as another aspect that affected SECZ's operations. The response by R1 sums it all, “The unfortunate part is that regulation is still to be consolidated so you find at times that they may not have adequate tools in terms of the law. The laws are not reconciled such that some can hide behind the Companies Act or even common law”. This was echoed by R22 who concluded that “what brings law suits against SECZ is that regulation is not clear”. Alluding to the same R3 added, “The founding laws do not give SECZ the powers to issue fines. Hampered by that, cases are criminalized and it requires proof on a high scale, which is more rigorous. They remain as offences in the Act and it's difficult to prove them”.

Three respondents (R6, R8, and R22) attributed the inefficiency of SECZ to the weaknesses in the judiciary system. The behavior of SECZ was also explained in terms of the Securities and Exchange Act. A SECZ official R7 explained the conduct of SECZ as being influenced by the founding law as follows, “It boils down to the Act, because any violation can lead to cancellation or suspension and SECZ can use it anyhow. SECZ can do anything under the guise of the Act”. These findings revealed that the competence of SECZ was affected by the nature of its authority in terms of the founding laws.

4.2.1.4 History of the market

The findings indicated the history of the market as an important aspect in the regulation of the market. The response by R2 captures it all, “The Stock Exchange was a club and now we have a super regulator. Compliance was very difficult since we had a lot of fights. People are now complying but at first it was difficult as people just thought these guys are just bothering us”. He continued, “We were used to do things our own way. You should understand where brokers are coming from. We were accused of causing inflation and the stock exchange was closed until February 2009 and Gono said to SECZ, ‘you are not doing your job’! Our relationship started in an antagonistic way”. These sentiments were supported by R13 who described the status of the capital market prior to the establishment of SECZ as a “zoo”.

It was clarified that the history of the financial services sector particularly, the stock broking and asset management sector, was littered with incidences of abuse of investors' funds and weak corporate governance structures that necessitated a cleanup to bring market players along to best practices. It was also noted that the regulatees initially showed lack of motivation to comply with the regulations as there were, according to R4, "acceptance problems in the market". The respondents explained that the situation of the market forced the SECZ to rigorously apply the law with the motive of setting a standard since the organization was new. According to R12, SECZ wanted to "stamp its authority". It was noted that SECZ also had to preserve its legitimacy as a regulator of the capital market and in certain instances "it has to act and be seen to act", according to R9.

4.2.1.5 Economic Environment

The philosophy of SECZ was also explained in terms of the nature of the market. The study revealed that the capital market industry in Zimbabwe is dominated by very small and fragile players. The response of R2 explains it, "the quality of our listings is just horrible; all brokers go to ZSE to trade Delta and Econet, THAT'S IT! What else can you trade? ZECO? All those things, THEY ARE USELESS! It's a mining country and they should get this Zimplats, your ZIMASCO all these MIMOSA, listed..... Not this! THAT'S NOT AN EXCHANGE!" These emotions were echoed by a transfer secretary R14 who lamented, "It's a slow market, sometimes ZSE registers only eight trades per day, there are no corporate actions, there are no new listings, there are no companies paying dividends...." Adding to that R13 said, "It's only 5 or 4 really relevant brokers and the rest you wonder how they are surviving as they can go for months without any trades. I wonder how they pay salaries, maybe its classic Zimbabwe".

4.2.1.6 Structure of the market

The fragmented structure of the market was also pointed as a factor that influences the regulatory paradigm of SECZ. The remark by R3 explains the problem, "At policy level, beyond the Commission, there should be consolidation of the financial services sector. The sector is fragmented with RBZ on the banking side, IPEC on insurance and SECZ on securities". It was noted that the RBZ and SECZ shared regulatory roles. This was confirmed by R22 who explained that SECZ does not have full control of some of its regulated entities as the entities' are also controlled by the RBZ, IPEC and PAAB a situation that limited the

control of SECZ over those entities. SECZ records of licensed players revealed that some of its licensed entities are registered Banks and Audit firms. Examples are CBZ Bank, Standard Chartered Bank, Stanbic Bank, Deloitte Chartered Accountants and KPMG Chartered Accountants.

A securities dealer, R11 took a different dimension to illustrate the nature of the securities market. He explained, “The exchange as it is now is owned by government and brokers. SECZ is an independent body of government which regulates that market and for SECZ to suspend the Exchange is not possible. The Exchange is part of Government.” This position was confirmed by SECZ officials who were interviewed. Further, the Agreement between the Government and the brokers revealed that brokers own 67% shareholding in ZSE while the Government is entitled to 33%. Also, the fact that SECZ is barely 5 years old was pointed as another factor that affects its regulatory style. This was explained by R5, “it’s a new baby coming into the market and it’s difficult for them to deal with all issues at the same time”. The findings revealed that SECZ had to contend with the realities on the ground, and that shaped its regulatory actions.

4.2.1.7 Globalisation

As high as ten respondents cited that international influences played a role in shaping the regulatory behavior of SECZ. In this connection R1 stated, “The reality is that our market is actually being driven by entities coming from other markets”. Four respondents (R1, R3, R8, and R22) emphasized that SECZ had to comply with international best practices as dictated by international bodies like IOSCO and CISNA. It was noted that SECZ is a member of the CISNA and it has also applied to be admitted as member of IOSCO. Two respondents (R7 and R8) further cited the international requirements on money laundering and combat of financial terrorism as other issues that influence SECZ regulatory conduct.

4.2.1.8 Personalities of SECZ employees

Though there was no evidence that SECZ staff was politically brazen, it could be presumed that they were also interested in building up their reputations and political interests. Also the morale and personalities of the SECZ staff could influence the effectiveness of its regulatory actions. This was confirmed by R3 who had this to say, “It also depends with which element is running with it, which department is working on it”. This sentiment reflects that the

personalities of the SECZ employees determined the regulatory actions of SECZ. The aspect of egos playing centre stage was insinuated by R19 who stated, “I also think SECZ wanted to show who the big brother is and when that happens obviously, they fight.” It was noted that the former CEO of SECZ is now the current CEO of ZSE.

4.2.2 ENFORCEMENT STYLE

4.2.2.1 Attitude towards regulation

The respondents were asked the reason why they comply with SECZ regulations in order to assess their attitude towards regulation. The general feeling was that compliance would ensure that their integrity is protected. The majority of the respondents (17) unanimously agreed that integrity was a critical factor highly rated by clients in choosing the licensed entity to deal with. A considerable proportion of the respondents (5) further explained that they complied with the law as part of their culture and that their reputation was their biggest asset in the market. The respondents also noted that while compliance with regulations helped to reduce incidences of internal fraud, they also derived benefits of having the best international practices that would be applied uniformly across the capital market industry. The respondents’ views were consistent with the need to remain competitive while also, 14 respondents, including respondents from SECZ clearly indicated that licensed entities complied with the law mainly for fear of being sanctioned by the SECZ.

4.2.2.2 Interactions with the regulator

The respondents were asked to explain the nature of SECZ interactions with market players. There were varied responses with one group indicating strained interactions while others argued that they were free to interact with SECZ. The SECZ officials stated that they had an “open door policy” where licensed players were free to talk and interact with the regulator. This was corroborated by R13, an investment advisor who said, “I can even pick a phone and call the CEO himself while in other government organizations you can’t get hold of the officers”. Adding to that, R15 said his company can even invite SECZ officials to their functions. However a total of 12 respondents from licensed entities indicated that their interactions with SECZ were only limited to regulatory transactions. This was summed up by R6 as follows, “we cannot invite the cops to our parties. They are always watching on what we are doing and we are not free to interact with them”. It was also noted that SECZ

policy required all employees to seek permission before they accept gifts from regulated entities.

The findings revealed that interactions with the regulator were mainly through the licensing process, inspections and submissions of returns. The respondents called for more openness and visibility of SECZ. The SECZ was lambasted for getting into the media for the wrong reasons. Thus R19 said, “SECZ is always in the Press to say they are fighting this and that when there are opportunities where SECZ can be in the press for the right reasons. I have never heard about SECZ doing a corporate responsibility issue”.

It was noted that SECZ mostly interacts with compliance officers both in terms of operations and compliance with the law. The remarks by R19 revealed the bitterness in market players, “My general feeling is that those people (compliance officers) should be equipped for them to know what their role is, the YESs and NOs of regulation and how they interact with the Commission”. He bewailed and continued, “ When the regulator come to make an assessment, I can offer a cup of tea and that changes the dynamics of the inspection, such that we get to know what the Commission is all about. If they send me an email that they are coming, already I will build up resentment that SECZ is coming and that’s not right”. The findings largely reveal that the interactions were too formalized and limited to business transactions.

4.2.2.3 Conduct of SECZ

The respondents were asked to explain the conduct of SECZ. There was some harmony in the responses that SECZ was quite forceful and insistent. In connection with that R5 complained, “The idea is not to choke the market and SECZ should not be so heavy handed on the market”. SECZ was described as taking the stance of a policeman by R11 who said, “Whenever there is a problem, SECZ would want to penalize us and we become frightened and sometimes people will withdraw their contributions and simply follow what SECZ wants”. However, R6 conceded that SECZ had improved its attitude towards market players. This was substantiated by R13 who said, “SECZ was extremely aggressive but I believe it was still finding its feet. Now I find it a lot more constructive, it’s a learning curve”. It was explained that SECZ took such an aggressive stance considering that the market was like a “wilderness” and that it needed a heavy hand to bring “sanity in the market”.

It was clarified that SECZ did not compromise on issues that affect the integrity of the market. SECZ would however warm up on issues of an administrative nature such as filing of financial statements and returns. An investment advisor R13, called for the licensed entities to understand “what is high priority and low priority”. Two respondents (R15, and R21) commended SECZ for “moving in wanting to understand what the issues are like”. This was supported by R14 who said, “When they come for inspections they give you notice, they are not on a fault finding mission, yes they are a regulator but they are also prepared to learn from people on the ground”. Contrastingly R6 grumbled, “SECZ should remove the idea of saying “We are the regulator”.

The differences in these opinions can be explained by the different categories of the licensed entities. Further, as put by R12, “The market wants the regulator to be very lax while the regulator wants to consolidate its powers and already there is conflict”. It was also emphasized by market players that the SECZ should work clear the market perception that it had been introduced to prosecute as opposed to the need to regulate and create a level playing field. The findings generally revealed that SECZ took a combative approach to regulation though on occasions it was complaisant.

4.2.2.4 Interventional Enforcement Strategies

Asked to indicate the ways through which SECZ responded to violations of the law, the study attracted mixed reactions from the different market players. An asset manager, R20 described SECZ as taking a reformist approach where it identified areas that could be corrected and put in place the necessary measures. However, asset managers R6 and R18 said “it was too early for them to comment on SECZ actions as it was hardly a year under its regulation”. They explained that it was the first time for SECZ to regulate them and they believed SECZ was still familiarizing itself with the market. The sentiment by R6 and R18 therefore rebuts the notion that SECZ was taking a reformist approach on asset managers. This also explains the difference in reaction by brokers.

The study revealed that SECZ has not been very active with investment advisors as explained by R12, “I m lucky I m an advisor. SECZ is not as on day to day on us as it is on brokers. I know SECZ is on brokers’ face everyday”. It was noted that investment advisory business does not include handling of money or clients shares hence the lackadaisical approach by

SECZ. The assertions of R12 that SECZ was antipathetic with brokers were confirmed by R2, R4, R5, R10 and R11. A clear example cited was the way SECZ moved in to the issue of nominee accounts which were supposed to be registered in the name of the actual clients by brokers. The custodians, R1 and R21 who are both big and established businesses in Zimbabwe were indifferent arguing that they had very strong systems that were beyond regulatory reproach.

Turning to the investigations of market crime, the study respondents generally cited two weaknesses. Firstly, the SECZ was lambasted for being too reactive rather than being proactive. SECZ was accused of reacting in a slow manner after problems have already occurred. Secondly, the regulator was considered short of the necessary financial and technical knowhow to detect and apprehend offending licensed entities. SECZ officials who were interviewed explained that the SECZ initiated investigations based on the information available to it. The information was obtained from various sources such as its own surveillance officers, inspections, market sources and even rumors. It was noted that SECZ has been concentrating on improving the functioning of the market through the establishment of the CSD and pushing for the automation of the market. A Majority of the respondents (15 out of 22) conceded that the manual system made it very difficult detect crimes. The respondents hoped that the CSD would improve the monitoring of market activities. The findings revealed that SECZ took different approaches to the different categories of market players, ranging from being militant to the brokers and easy going on investment advisors.

4.2.2.5 Protection of Investors

Although SECZ was widely criticized for concentrating more on licensed players rather than the investors themselves, this study noted that SECZ had put in place a number of initiatives to protect investors. To curb abuse of clients' shares, it was found out that SECZ had directed all stockbrokers to deposit all unclaimed shares with custodians. In the same vein, the SECZ also directed that all shares had to be registered in the names of the clients. The majority of the respondents felt that SECZ's move to put in place rules such as the separation of asset management and custody of assets as well as the setting up of the CSD were effective for safeguarding investor assets. A SECZ official R8 explained, "We educate investors on their rights and issues concerning the market through our weekly column in the Herald and our

Magazine”. It was noted that every Mondays SECZ issues a press release on the first page of the Business Herald. The SECZ respondents felt that the first round effects of their actions were an increase in investor confidence, wherein the mere presence of SECZ in the market provided investors with comfort. The respondents from the market players also conceded that the establishment of SECZ was a welcome development in the market.

Despite the good intentions to protect the investors SECZ was criticized for being epileptically obsessed with issues of only fraud and malpractices from the market participants. As a result, SECZ took an aggressive stance on licensed players. While the respondents acknowledged the efforts by SECZ to protect investors, they still believed that SECZ was still a long way to achieve investor protection. The respondents generally agreed that investors in Zimbabwe were vulnerable. The sentiment by R2 sums it all, “A minority shareholder in Zim is a piece of cake; nothing is done to protect them, neither by the ZSE nor by SECZ itself.” He went on to give an example, “We hear of all this ABC transaction of the executive directors, there were 3 different prices offered by the guy who bought Atlas Mara. All shares when they are issued rank *pari pasu*, they are all equal unless they are different classes, so why should someone get \$5.00 and a minority get a \$1.00. This transaction happened this year! So you are spending more time supervising brokers, checking their accounts and all sorts of things. But the fundamentals of the stock exchange, the principles of listing, they are ignored. That’s where SCEZ emphasis should be, disclosure and minority shareholders! You should be deepening the financial markets, all that issue of stock exchange and brokers is a passing phase!”

Cementing on the views of R2, R20 said, “I m not sure whether there have been any sanctions against listed companies such as that of Joe Mtizwa, I don’t know what happened. I don’t know what happened to Rio Zim”. The respondents also accused SECZ for being a spectator as investors were deprived of their hard earned cash through the continuous delisting of companies. The findings reveal that though SECZ has made some considerable strides to protect investors, the efforts are insignificant as investors are still very vulnerable.

4.2.2.6 Licensing Requirements and Inspections

The study found out that the variations in perceptions regarding the SECZ’s licensing requirements, effectiveness of inspections and requests for information could be explained by

the different categories of the licenses and the different licensing conditions. On a balance, responses concerning the SECZ's licensing requirements suggested the process was thorough across the different licensed entities. Despite the unpopular requirement for licensed entities to counterproductively renew licenses annually, respondents generally noted that licensing requirements were appropriate and ensured that only qualifying applications were approved.

All licensed entities were satisfied with the annual on-site inspections. Concerning the frequency of returns and requests for information, which largely varied from a weekly to quarterly intervals depending on the licensed entity and type of activity or transaction, the study found out that the licensed entities had resentfully accepted the routine of submitting the information. In the version of R12, "We do monthly returns and we get the impression that the only reason SECZ wants the returns is to know what fee they will get and not issues of compliance. There is no sense of any regulation around that; it's a return we submit grudgingly. These guys just want their fee and we just do it". The request for information was well received in line with international best practice, although three respondents (R4, R6 and R18) complained that sometimes the deadlines which were given were too tight.

The study respondents also acknowledged high levels of professionalism by the SECZ officials during the engagements. However, as far as effectiveness of inspections was concerned, participants pointed out that SECZ was limited in adequate numbers of skills and systems to regulate the market. This was confirmed by R19 who explained, "I know the SECZ investigations department is very small and the market is quite big to be serviced by few people". Supporting the inadequacy of the regulatory resources for surveillance, a number of the licensed entities expressed dissatisfaction with the protracted inspections that took more time than initially planned. The findings revealed that the licensing requirements, inspections and request for information were merely routine activities prescribed by SECZ. They were described by R3 as "checkbox, with not much sense of life in it".

4.2.2.7 Penalties

The study noted that SECZ could impose various penalties upon investigation of offences. The SECZ officials viewed the imposition of these penalties as success in achieving compliance. Commenting on SECZ's penalties that had been issued by the regulator, the respondents described the conduct as appropriate, necessary and deterrent enough to

effectively “weed out the bad apples”. All the respondents cited the Remo vs Interfin case where the companies’ licences were suspended for 5 years. It was noted from the Court records that Remo appealed against the decision of SECZ and partially succeeded in that the Supreme Court reduced the period of suspension from five years to four years and six months, bringing the severity of the suspension into issue. The reduction of the sentence suggests that the SECZ sentence was excessive.

The respondents however noted that more clarity was required on the penalties’ framework so that market participants would understand the system. It was noted that SECZ has never prosecuted anyone and outside Remo and Interfin case, SECZ has not expelled any company. All the closures that occurred were voluntary. Examples provided were Kingdom Stock Broking, ZB Broking, ZB Asset Management, Tetrad Asset Management, Fourth Dimension Advisory, Innscor transfer secretary and Barclays Custodial. The inaction of SECZ on prosecutions was attributed to unsupportive legal systems. However the case of Remo and Interfin revealed SECZ preparedness to issue sanctions against market players.

4.2.2.8 Education to licensed entities

With regards to the provision of education to the licensed entities, the study found out that SECZ was not effective. SECZ officials gave examples of educational workshops which targeted licensed entities as the World Bank, SECZ- INCAF, Institute of Sustainability of Africa, PAAB-, SECZ with listed companies on financial reporting and several workshops that were held prior to the establishment of the CSD. Other market players R5, R15 and R21 confirmed that they attended a workshop on Money Laundering held at Pandhari. The same respondents acknowledged the training of compliance officers which was organized by SECZ in 2012.

According to a considerable proportion of the respondents (10), SECZ was doing nothing to educate them, thus R19 said, “We don’t need to know SECZ when there is a problem; we also need to know them when they are telling us what they expect from us. We want to know them for good things. There is no need for SECZ to hire experts; they may just need to use one of the people in the market.” Comparing the regulatory era in which asset managers were under the purview of the RBZ, the respondents recommended that SECZ should play an active role in distributing information to the market. Thus R20 said, “I would expect the

SECZ PR unit to advise us on what is happening in the market. When we were still at RBZ, they would advise us of what was happening in the market and we were always up to date with market issues but they were the regulator”. The respondents from licensed entities (14 out of 19) also recommended that SECZ should train its employees asserting that they do not “want the regulator to be lagging behind”.

4.2.2.9 Consultation

The findings revealed that SECZ consulted market participants on most of the issues that concern the market. The majority of the respondents from market players (13 out of 19) however had misgivings on the quality of the consultation. They were of the view that the consultations were not effective, with a considerable proportion of five respondents arguing that the consultations were only for window dressing. Five respondents (R1, R4, R14, R16 and R19) confirmed that they make comments to whatever is circulated by SECZ for opinions. The general sentiment was that licensed entities contributions were not considered. According to R14, “When SECZ come to us, they have a broad outline of what they want to achieve. If you make suggestions that are outside those parameters obviously they would not be considered”. The same views were shared by R6, “Even if you want to initiate, you will be initiating from a low end, SECZ is like a father and it has the final say. It’s very difficult for us to make the regulator realize that we want some changes”. An example that was popularly given by the respondents, where SECZ never attempted to consult them was the publication of SI.108 of 2014 which prescribes levies to be paid by market players. It was also noted that the stakeholder meetings which were held in the market were initiated by the regulator.

4.2.2.10 Communication

Overall, the study found out that SECZ communicated with the regulated entities directly through formal letters, Directives, emails, SECZ bulletin, Press releases, SECZ website and Government Gazette, especially on rules and regulations. The majority of the market respondents however resented how the communication was done and particularly cited was the statutory instrument 108 of 2014 which was published through the Government Gazette. They complained that they were ambushed and R20 bewailed, “SECZ advised that this thing was gazetted as a statutory instrument and that we were supposed to have been aware that it’s now law. True but I think its relations issue, it wouldn’t hurt to communicate to the market and give them time to comply. That proactiveness is good. The next thing was why are you

not paying levies? On a technicality, yes we are found wanting because its law but that not good for relations.”

It was pointed out that although documents were circulated, the majority of the respondents from the market players (11 out of 19) preferred dialogue through seminars and discussions. According to R10, SECZ emphasized documented things. He said, “If you put your issue in writing they will listen to you”. Alluding to the same view R4 sums it all, “Let’s interrogate issues before the laws are passed than to make submissions. Submissions tend to limit people, we want to speak in our own way. Let’s discuss more before we implement”. He went on and gave an example, “On the Chengetedzai issue, if SECZ, ZSE, brokers and CSD had set down and discussed the issues, it would have been a better system than what is now. Let’s increase our interactions on new things especially new laws and systems.”

The respondents also complained that there was little feedback as explained by R6, “The communication between us and SECZ is of requests for information, it’s always can you submit this, can you submit that by such... such and nothing more? It’s always this after that and instructions always and no time for feedback. It’s just an issue of interactiveness. We need notice when there are new rules so that the market is not interrupted. It enables brokers to talk to their clients so that they make the necessary adjustments. We don’t want a relationship of deadlines!”

In agreement, R9 said, “Look, as much as we are learned people, it’s one thing for me to email you a document and say put comments and it’s a different thing that you sent me a document and you come to me and say we have sent this document and the rationale behind this document is a, b, c, d and this is what we want to achieve, it becomes much better”. He continued, “The psychology of people tends to own that kind of engagement but if you throw something to me, because I have a workload, I will not feel part of it. If it sails through and becomes law, I will not be part of it. The comment you will get is that SECZ is at it again and that very bad”.

However a minority of the respondents from the market players expressed satisfaction on the communication by SECZ arguing that SECZ was doing its best given the current economic challenges. This was expressed by R17 as follows, “I don’t see how SECZ can manage to

hold workshops whenever there is a new thing in the market. It's not possible! SECZ does not have the funds. It's no secret that SECZ was raided by ZIMRA."

4.2.3 REGULATORY APPROACH

4.2.3.1 Nature of the laws

The respondents were asked to describe the nature of the laws that SECZ employed. All the respondents cited that the SECZ was following a rules based approach as opposed to the principle based approach. SECZ officials described the statutes as their "Bible" which lays down all the procedures to be followed. It was noted that anything outside the statutes was unlawful such that market players had to consult SECZ whenever they wanted to engage in new activities. It was noted that the market is run by a few pieces of legislation which have gaps as explained by R17 when he said , "What we wanted to do was not specifically catered for by the laws, that's why we had to tailor make our activities to suit the law. We were not even sure of whether we needed to be registered by SECZ or whether we could just operate". It was noted that SECZ was still in the process of creating more rules to govern the market. SECZ had lined up a set of eight securities rules for drafting and had already engaged legal experts to draft the rules. The SI.100 of 2010 was the most popularly cited by the market players. For R2 he said, "It is that SI.100 that is running the market", signifying the far-reaching use of the rules.

SECZ officials argued that rules were simple and easier to use as they simplify the decision making process. Thus R8 commented, "The rules are there to guide us in situations of noncompliance. We have the rules to punish them. We simply follow what is in the Act. We want to set a standard because we are new, we don't relax the rules". The sentiments by R8 also reflect the propensity of SECZ to issue sanctions. The case of Remo vs Interfin was cited by the respondents as an example where the SECZ followed the statute to the book. It was noted that the Act provided for such cancellations or suspensions should any violations occur.

SECZ strictly enforced the rules regardless of situational factors as noted from the complaints by R11, "The market sometimes becomes frustrated by the regulator especially in this environment. We need some flexibility and it should not be cast in stone. SECZ should

give the market a lee way and should be able to accept explanations why a person has not complied with the set deadlines”. The respondents however noted that it was imperative for SECZ to observe the need for blending of rules and principles. According to R7, “SECZ needs to clearly stipulate some of the things but it cannot stipulate ethical standards and issues of disclosure and duty of loyalty to the customer”. In addition, R1 commented, “The cost of regulation has actually increased because we have to comply with a lot of regulations; the best approach is for us to move towards principles based.”

The respondents also pointed the need to reconcile and consolidate the various pieces of legislation that were fragmented. It came out that there had been instances in which there was no clarity on SECZ’s legal authority to act. Widely cited for harmonization were the Companies Act, Listing Rules, SECZ Act and the Asset Management Act. It was also observed that the Collective Investment Schemes Act administered by SECZ was also still referring to the defunct Zimbabwe dollars and has not been amended since 1998. The licensing of trustees had been hindered by the lack of amendments. The problem was explained by R22 as follows, “it takes time to amend rules and it involves processes that are beyond our control. The process involves approval of the amendments by the Minister, approval by the Attorney General and by Parliament. The process is long and expensive as we have to hire experts in statute drafting to put the rules into the format that is accepted by the Attorney General”.

It was noted that the Securities and Exchange Act had been amended twice in a space of two years, revealing the constant need to amend the law whenever there is a change of circumstances. The challenge of rules was aptly put by R14 who said, “There is need for proactiveness on the part of SECZ in terms of understanding the issues so that they do things from an informed point of view so that people do not look for loopholes to evade the cost of compliance. They are constantly chasing a moving target. They formulate rules that apply in the market today and three months later the regulations are no longer applicable”.

4.2.3.2 Application of the laws

There were mixed reactions as to how SECZ applied the law. Though the study revealed that SECZ was very strict in its application of the rules, it was noted that it also offered extensions to market players upon “reasonable cause”. A Circular dated 17 December 2010

revealed that SECZ gave an extension of time for the payment of licence fees by brokers, taking into account the difficult economic environment. All the respondents unanimously agreed that SECZ does not offer exemptions. It was also noted that even the extensions were a rare occurrence. The findings also showed that SECZ sometimes uniformly applied the rules and as a result of which some market players were affected. The challenge was explained by R18 as follows, “Once in a while there will be a misfit in the sense that they could give a directive which applies to asset managers with unit trusts and they would expect everyone to comply with that directive. So you would have to engage them to say no, this does not apply to us. There is a bit of confusion.”

Some respondents, particularly from smaller firms complained that the requirement of a stand-alone compliance officer was expensive. In the views of R20, “The issue of compliance officer is costly, SECZ should consider combining the roles for example an accountant can do compliance but SECZ wants the compliance to be a standalone. Some companies are too small and it’s hard to comply with that. SECZ should relax a bit and allow the merging of roles.” However, R1, R14 and R20 supported the requirement arguing that it strengthened their internal control systems and corporate governance measures. Compliance costs came top regarding the challenges that licensed entities encountered in implementing the rules. This prompted some respondents to call for the adoption of a principle-based approach.

The respondents also felt that the application of rules was not consistent. According to R19, “SECZ application of rules is mixed depending on what the Commission wants to achieve. In some cases the law has been applied with vigor and in some cases it’s really lenient”. Cementing on that view, R2 said “SECZ application of rules is yellow and green. The application of that statutory instrument (SI.100/2010) is not consistent and it’s not good for the market.” Similarly, R12 bemoaned, “SECZ response to market is not automatic, the response is not uniform and its unpredictable and this is where SECZ is letting itself down. The rules are not properly defined. We don’t know what SECZ expects from the listed companies, the investors and market participants. IT’S NOT SPELT OUT! The only time you know SECZ has acted is when Tafadzwa is quoted in the Press”. He continued, “My view is that we should have a self policing system and SECZ should play a custodial role of

that system. It shouldn't take the CEO of SECZ to be voicing issues because the market should already know the issues. The rules should be transparent and self policing so that people do not end up thinking that it's personalized". He sighed, "As long as the rules are not predictable we will always have a problem, people would think that SECZ is being selective." In that regard the respondents called for increased involvement of the licensed entities on regulatory matters before sensationalizing matters in the public domain through the Press.

4.2.3.3 Interpretation of the laws

The study found out that the respondents were not happy with the use of rules. They felt that use of rules defeated the whole purpose of regulation. The response of R3 explains it, "Principles are better because rules are like a tape recorder which doesn't think. Each case should be viewed with a goal in mind. Rules have been abused for example the case of ABC holdings, Lifestyle and TA Holdings." He lamented, "A mandatory offer is supposed to protect investors but sometimes like in these situations it resulted in consequences that are worse off. CAPS also went that way. Had mandatory offers not been allowed, minority shareholders would have had an opportunity to sell out their shares. Investors were prejudiced. If it was a principled approach, the question would be what do we achieve if we allow the mandatory offer? Are we protecting investors? Sometimes you protect by waiving the mandatory offer."

Further the respondents explained that the rules were difficult to understand and that they were subject to different interpretations. To substantiate this R9 said, "Sometimes we find it difficult to understand the rules, especially that we don't have legal resources, our businesses are too small and we can't afford to hire a lawyer. At the end of the day no matter how the laws appear difficult we will do the best we can always to read between the lines and do the best we can. It would help more if the rules are explained to us". The responses obtained on the effectiveness of the rules shed a lot of doubt on their effectiveness. The strict interpretation of the rules meant that licensed entities could not be very innovative as they risk operating outside the law. In this regard R10 explained, "We are not allowed to act outside the rules. The rules need to be changed they are now outdated, for example brokers only trade in equities and it limits revenue streams."

4.2.4 REGULATORY MODEL

4.2.4.1 Role of Industry Associations

To assess the level of regulatory cooperation, linkages and networks in the market, the respondents were asked to explain the role of the industry associations. The industry associations were found to be very instrumental in the regulatory matters noting that they provided members a platform to air their views, feedback and contributions “without fear of victimization by the regulator”. They felt that it was better to “engage the regulator as an association than as individuals”. The study respondents also added that industry associations provided the necessary weight to collective positions in lobbying the regulator for amendments.

It was also noted that the reason for the creation of the associations was to enable the licensed entities to fight together against unfavorable regulatory developments. This was summed up by R14, “We have an association of transfer secretaries, and has been active especially over the past few months, running into a year. It looks at any new market developments and how they impact on us as transfer secretaries and to help each other to understand new regulations. It’s more of peer review and it does not have regulatory powers, issues are escalated to the regulator. The most issue which triggered us is the coming in of the CSD as it has a great impact on our business so we needed to work together to protect our business”.

It was noted that investment advisors did not have an association. Nonetheless it was found out that the associations were only lobbyists groups without any powers. They were described by a SECZ respondent R8 as “information conduits.” It was also noted that, except for the association of asset managers, the associations were all new. The findings reveal that the industry associations were not very powerful in terms of influencing regulatory decisions. The associations’ being new indicates weak linkages and poor cohesiveness among the market players.

4.2.4.2 Role Definition

There was confusion among the respondents from the licensed entities. The findings revealed that the respondents were not really sure of the roles of the SECZ and the ZSE. The response by R3 explains it, “Now there is some confusion. Before, you knew what was supposed to be

done and you knew where to go. Now you don't know whether to go to ZSE or to SECZ. There is no clarity and sometimes it's back and forth. Even issues of going to court began when the Commission came in, there were no such challenges before. Conflicts were resolved amicably with the Exchange. We do not know their role definition. It took roles from constituencies that were better placed to do that. It was more efficient for the Exchange to deal with the issue of Renaissance. During times before the regulator, the Exchange would take control of the company which can't meet its obligations. Now there is whole lot of confusion and no one knows where SECZ role starts and ends. Confidence comes from experience and it's not there." Adding to that R2 said, "In South Africa, the JSE regulates its members but right now SECZ is regulating the members and ZSE is also licensed by SECZ. The lines of authority must be clear...ZSE is supposed to look at members and issuer issues and reporting to SECZ, not this duplication!"

4.2.4.3 Supervisory Roles

The findings showed that SECZ had absolute control over the operations of the ZSE and CSD. SECZ approved all operational rules and procedures of the ZSE and CSD. SECZ also has direct supervision to brokers, who are also under the management of the ZSE. SECZ directly monitors all players in the market. It was also noted that SECZ was instrumental to the establishment of the ZSE Board. In the words of R5, "SECZ did a good thing by creating the board at the exchange; they will be able to take a helicopter view, unlike the tractor view which they took when they came in. I hope SECZ will move away from dealing directly with brokers". In similar sentiments R11 said, "SECZ should also look at the actual trading itself. Issues like buybacks by these big companies like Econet should be investigated. SECZ should intervene at that level rather than to concentrate on small issues done by brokers." The respondents felt that there was duplication of roles.

4.2.4.4 Trust

In terms of the existence of trust between regulatees and SECZ, the study found out that there was no trust at the inception of the regulator. Respondents however cited significant improvements in the years that ensued. A custodian, R1 said, "We don't have faith in their processes. Other people have resigned to fate that SECZ is a regulator who is just deaf to the market". More so R11 said, "Our suspension was as a result of mere misunderstanding. There was mistrust and it's an issue of miscommunication. They thought we were arrogant."

Emphasizing on that, R16 said, “Since the inception of SECZ, one of their underlying currencies, judged by their actions, they think brokers are dishonest. It’s the main reason why the association was formed.” Demonstrating the lack of trust and lack of effective collaboration R15 said, “I was privileged to sit on the CSD committee, we agreed that the broker model will be used, and SECZ changed without coming back to the committee and the next thing it was a Directive that we are taking a custodial model”. The respondents conceded that such unexpected changes worked against the spirit of collaboration thus sending the market into a jittery. It also emerged that the lack of trust between SECZ and the regulatees resulted in the emergence of industry associations.

4.2.4.5 Private sector standards

The findings of the study revealed that the regulator was not in a position to delegate its regulatory roles to the market players. Noted was that the private sector standards were in shambles and as such the private sector could not carry out regulatory roles. It was noted that the ZSE was still yet to put into place proper structures. According to R8, “At the moment ZSE does not have capacity e.g. skills. They should be able to carry out inspections on brokers and bring the reports to us but now they can’t do it. They are not demutualised and there is conflict of interest. There is no Board. The board which is there is an interim board. There is a temporary board and after demutualization we expect to put a proper board.” It was noted that the ZSE was working on its listings rules and the draft rules had been tabled before SECZ for consideration. It was also noted that processes to corporatize the ZSE were underway. Further, it was also noted that the ZSE operated a manual trading system.

Commenting on how SECZ monitored the operations of the regulatees R9 said, “The idea is to create strong institutions. We want companies to be able to identify, control, manage and absorb their risks. If we see weaknesses, we ask them to beef up.” It was the general feeling of the market respondents that SECZ was supposed to spearhead the demutualization of the ZSE. In this regard R5 said, “SECZ need to be on the ground to push demutualization of the ZSE. If people are to be serious, this issue does not take time.”

The SECZ was blamed for being heavily involved in Committees that oversee the functioning of the market. The findings also revealed that SECZ officials observed the ZSE Listings Committee meetings, “the engine of the ZSE” which deals with all market

transactions as explained by R9, “We observe the Listings Committee deliberations. We assist in ensuring that all listings related issues are complying with the ZSE listings rules. If we don’t attend, then they would need parallel filing which is a cumbersome process. The challenges before resulted from the structure of the ZSE. Previously we faced challenges of limited disclosures. SECZ would get to know of the issues after the transaction has already been approved. It resulted in delays as reversal would be costly. Usually there would be tight deadlines for example capitalization issues and the financiers may choose to opt out if SECZ challenges the transaction”. She continued, “We don’t have voting rights; we can simply air our views in their deliberations. They get the comfort that whatever decision they make is to the SECZ’s expectation. There is a challenge that ZSE has two roles, of business sustainability and a regulatory role. The regulatory role aligns with SECZ’s role to protect investors. The business point of view is the one which brings out conflict. They can be tempted to focus on the business angle which is the advantage why SECZ sits on the committee.”

4.2.4.6 Sharing of Information.

The respondents were asked how they share information with the regulator to assess whether the market players shared the same interests with the regulator. The respondents indicated that SECZ was not very open in sharing information. According to R15, “The challenge is really the future, it would be nice if the regulator was to describe its utopia because we want to see where the regulator is taking us and we would like to see ourselves in that picture. Sometimes if you don’t know whether the regulator is coming or going or whether you are coming or going, there is room for you to start arbitraging and that never good for the market”.

Adding to that, R18 said, “We want the regulator to tell us that, guys the capital market we envisage for Zim is like this, that way we move in the same direction. They should show us the path and sometimes we might have ideas that we can throw in the hat. Because a better market is good for a regulator and it’s good for us, we will have more products to trade and more chance to remain in business”.

Further, R12 said, “When people are doing deals, they should be actually free to come to you to say there is this deal I m working on, what’s your advise on 1, 2, 3 but if I have a deal the

last person I want to see is SECZ. I would rather go ahead with my deal and SECZ comes afterwards”. The market players recommended that SECZ should form a team to spearhead market cooperation and development and to cooperate more with market players.

4.2.4.7 Complaints channels

The respondents were asked to explain the complaints channels available to them to assess the level of coordination and receptiveness of SECZ in the market. A majority of the respondents from market players openly indicated that they were not aware of any channels to complain about SECZ regulatory actions. The response of R17 speaks it all, “I m not aware of any channels to complain, I don’t know. I have seen people who just write to the papers and some going straight to courts but that’s not right.” The SECZ was therefore castigated for having not established complaints procedures or channels of registering complaints. The respondents said that they had to approach the SECZ itself, made use of the Courts of law as well as “leaking” the information to the media.

4.3 DISCUSSION

A review of the respondents’ responses shows that SECZ is a fairly independent from political influence. It is autonomous and has a fair human skills base with capital market knowledge. SECZ is however constrained in terms of resources, a situation that affected its dexterity. SECZ is funded by the industry and as warned by Mwendo (2006) the regulator may succumb to pressures from the market. The founding laws and the structure of the market were also a handicap to its functions. The ZSE is a government institution and as alluded by Kagan (1989) the regulator may be forced to relax the rules for political interests. The ZSE is the only Exchange in Zimbabwe and it would be difficult for SECZ to make a decision that disrupts the market. Further, the capital market is very small, with “tired products” and that affects the stance of the regulator as put forward by Baldwin and Black (2008). The industry linkages were so weak and it allowed SECZ to exert its full control over the market players (Coslovsky *et al.*, 2010).

Although SECZ was roundly lambasted for its heavy handedness in certain instances, its approach to regulation was considered workable taking into account the history of the capital market in Zimbabwe, the state of development of the industry as well as comparison with

international best practice. The licensed players insinuated that the market was overregulated. Overregulation or under-regulation was a matter of value judgment depending on one's preferences (Kagan, 1989).

SECZ took a precautionary regulatory approach, which resulted in the aggressive manner in which it adopted. Such an approach required a lot of experience and the reactionary solutions imposed proved to be ineffective with time. SECZ was under the psychological influence that investors experienced losses because of malpractices in licensed players and hence the overconcentration on licensed entities. SECZ honestly believed that its approach was in the public interest and may have unknowingly gone too far in protecting the investors. However, SECZ had to balance between investor protection and market development. Often SECZ overestimated its powers of oversight and intervened in issues where market solutions could work.

SECZ regulation is based on a set of rules that defines permissible conduct and its style is formalistic in nature. According to Muhammad (2013) such a style awakens resentment and obstructs mutual cooperation between the regulator and the regulatees. The licensed entities did not trust the regulator and as affirmed by May and Winter (2011), the licensed entities perceived the regulator as difficult to deal with. As pointed by Castro (2011) the use of rules can be expensive as revealed by the respondents who cited the high costs of compliance and the need to regularly amend them.

It was noted that SECZ should take advantage of the ZSE and the CSD and should also capitalize on their expertise. As pointed by Arthur and Booth (2006) SECZ could not be everywhere at the same time as it was limited in terms of resources as well as expertise. The ZSE and the CSD were closer to the market transactions than SECZ. Sharma *et al.* (2010) believe that delegating regulation to the exchanges brings efficiency. The ZSE and the CSD could also respond to the regulatory issues in a faster way as they were closer to the action. The CSD and ZSE could significantly reduce the workload of SECZ and also reduce its regulatory costs as pointed by Short and Toffel (2010). SECZ is currently in budgetary deficit as it is constrained in terms of resources. It was recommended that the CSD and ZSE should be allowed to deal with frontline supervision and should register the market participants. Though SECZ had managed to attract employees from the market, it might not

be able to anticipate all the changes that are underway in the market. Further financial products are increasingly becoming complex and majority of SECZ employees were drawn from other fields. McCaffrey *et al.* (2006) pointed out that regulators may not comprehend complex systems as they do not deal with them on a daily basis. In this regard the CSD system and the imminent automation of the ZSE would require a lot of training for SECZ employees. This could prove very expensive as SECZ was also facing budgetary problems because the market was shrinking.

It was recommended that the ZSE should ensure that its governance structure is appropriate to its regulatory mandate. Verbruggen (2013) emphasizes the importance of the qualities of private sector standards for collaboration to work. The ZSE should demutualise and put in place a substantive board of directors with competent persons. For the self regulating organization approach to work the ZSE and the CSD should be transparent in their approach and SECZ should provide adequate oversight. SECZ should devise other sources of funding, employ up to date technology and have competent staff.

The study also established that the SECZ needed to be pro-active in line with the fast changing global context. In this regard, it emerged that the sustainability of the rules for the capital market was linked to their environmental relevance. As pointed by Ravenscroft and Williams (2005) and Leuz (2010), some licensed entities were taking advantage of the rules to evade the spirit of the law, especially in mandatory offers by listed companies. In this context, participants thought that the SECZ needed to share frankly its regulatory vision, mission and values in such a way that all market participants would be on the 'same page' and in the process improve the effectiveness of the regulatory approach.

This study also examined the sustainability of SECZ's regulatory approach in the context of its relationship with the ZSE. Overall, the study noted that all the activities of the ZSE were supervised by SECZ. In accordance with the definition of Castro (2011), on government led model SECZ had oversight and control over all market participants. As a result, issuers of securities were indirectly supervised by SECZ through regulating the activities of the exchange. In addition and in order to ensure that the ZSE complied with the laws, SECZ officials sat in the ZSE listings Committee. Unfortunately, SECZ was accused of being very intrusive in the affairs of the ZSE. Despite these challenges, SECZ had made some progress

towards protection of investors. Nevertheless its far flung approach SECZ was able to put the market in order. SECZ monitored and regulated most of the market participants in the capital market. SECZ was, however called upon to widen its consultations and communications with licensed entities.

4.4 CHAPTER SUMMARY

This chapter focused on the presentation of data collected through in-depth interviews and archival records. This helped to establish the basis for coming up with conclusions and recommendations on the appropriate regulatory approach that could be adopted by SECZ.

CHAPTER FIVE: CONCLUSIONS AND RECOMMENDATIONS

5.1 INTRODUCTION

This chapter comprises the conclusion and the recommendations. Recommendations on policy considerations are proffered to SECZ. Chapter five also provides the contribution to literature highlights the shortcomings of the research and recommends suggestions for future research.

5.2 CONCLUSIONS

The conclusions are provided in terms of the objectives of the study as follows;

5.2.1 Factors that influence SECZ regulatory philosophy

Factors with the greatest influence on the regulatory philosophy of SECZ were cited as, lack of financial resources arising from the fragile market and inadequate government funding, compromised independence, the history of the market littered with malpractices by licensed entities, international influences and lack of legal capacity to act due to fragmented pieces of legislation.

5.2.2 Enforcement style of the SECZ.

The study concludes that SECZ follows a legalistic enforcement style of enforcement. SECZ takes a precautionary regulatory approach, which results in the aggressive manner in which it takes. SECZ is largely uncompromising, takes a formalistic approach to regulation and interactions with market players are low, and mostly on business issues. The regulator is quite forceful and threatening which results in a lot of fear by the regulated entities. There is very little education and counseling provided to regulated entities and consultation was found to be largely ineffective due to both the attitude of the regulator and the regulated entities. Though there were very few examples where SECZ issued penalties, the cases revealed that SECZ was not hesitant to issue deterrent sanctions to entities that breached the law.

5.2.3 Regulatory approach of SECZ.

The research concludes that SECZ approach to regulation is largely rules based. SECZ heavily relies on rules with no sense of use of principles. The procedures of SECZ are all prescribed in statutory instruments and Directives issued by it to market players. Anything outside the statutes was considered unlawful and the rules are generally strictly interpreted

and enforced. The rules however have not been very effective as they have gaps and have also resulted in unintended consequences. The use of rules was against the views of the respondents who felt that SECZ's interpretation of the law was limited to laws with little regard to the contextual circumstances of regulated entities. In this regard, SECZ rarely granted exemptions and extensions to licensed entities. Regarding the ideal configuration of capital market regulation in order to enhance the quality of regulation, the general feeling was that SECZ needed to blend rules and principles.

5.2.4 Regulatory model of the SECZ

It is concluded that SECZ largely operates as pure government model with very little cooperation from regulated entities. SECZ dictates the regulatory activities in the market through rules and regulations. Regulated entities have very little contribution in regulatory activities and the market is characterized by distrust and very little sharing of information. The industry standards are very poor such that co-regulation or collaboration is negligible. The regulator approves virtually all transactions, including the rules that govern the operations of the ZSE and the CSD. The ZSE and the CSD are heavily supervised by SECZ with very little autonomy. The regulated entities are fragmented, with industry associations being in formative stages and linkages and networks are weak to enable them to have a strong impact on the regulator.

5.3 VALIDATION OF PROPOSITION

The research proposition that SECZ regulatory approach promotes market development and provides a safe environment for investor protection is partially accepted. The research concludes that despite its far flung approach, SECZ has been partially successful in taming the regulatory entities and thwarting resistance in the market. In spite of challenges SECZ has made a lot of progress towards the protection of investors and the development of the market. The market is now fairly in order despite disgruntlements among regulated entities. SECZ now monitors and regulates most of the market participants in the capital market. It is without doubt that investors are far better off with SECZ than the previous situation when the market was unregulated. So far SECZ has made sincere efforts to bring sanity to the market by issuing rules and regulations. The era is only the beginning for SECZ and a lot of work

still needs to be done. The investors are still vulnerable and there is great scope for improvement for SECZ.

The rules based regulatory approach of SECZ was found to be ineffective due to its strictness and inflexibility. Firstly, respondents felt that the rules based approach diminished innovation in a market that required “thinking outside the investment box”. Secondly, it was deemed cost ineffective given a backdrop of cost containment measures across the economy. The rules governing the capital market in Zimbabwe were considered fragmented prompting calls for the reconciliation and consolidation of the pieces of legislation. SECZ was advised to compliment its work by devising additional sources of funding, employing up to date technology and having competent staff to smoothen the regulatory process.

5.4 CONTRIBUTION TO THEORY

The research was centered on the regulatory activities of SECZ and was underpinned by the theory of regulation which is two sided, with the public interest view on one hand and the private interest view on the other side. The conceptual framework presupposes that a regulator following a legalistic rule based approach and pure government model will be inclined to pursue the public interest view. There was no strong evidence linking SECZ to either the public interest view or the private interest view. Neither was there evidence showing a balance between the public and the private interests. The SECZ approach to regulation was simply not very effective, hence the partial acceptance of the proposition. The contribution to literature is that the study has shown that a legalistic rule based and pure government regulator can simply be ineffective while not showing any inclination or balance between the private interests and the public interest.

Further the research contributes to the understanding of the capital market regulatory jurisprudence. It also helps to shade light on how statutory bodies conduct their operations in the Zimbabwean context. Very little has been documented on the operations of SECZ as it is a new phenomenon in Zimbabwe.

5.5 RECOMMENDATIONS

The study made the following recommendations:

5.5.1 Increase Sensitivity to Market Conditions

The study recommends that SECZ should consider the internal and external environment of the regulated entities in its regulatory conduct. This is meant to strike a balance between regulatory compliance with factors like cost implications, economic and technical feasibility of meeting regulatory deadlines, market history and impact on the overall going concern status of the regulated entities.

5.5.2 Improve Consultations and Communication

In moving away from a legalistic enforcement style, the study recommends that there be increased involvement of the licensed entities on regulatory matters. This could be achieved through wider consultations, effective and two-way communication and the establishment of clear complaints channel. In the process, SECZ would be able to clear the market misconception regarding its regulatory standing and therefore establish mutual understanding and trust with the regulatees.

5.5.3 Establish Clarity on Role Definition

There is great scope for improvement for SECZ. The capital market of Zimbabwe is far older than the SECZ. There is need to establish clear role definitions with other capital market players and harmonization with other regulatory authorities. An ideal scenario would be one in which SECZ concentrates on monitoring rather than suffocating the market with overregulation. SECZ should therefore move towards allowing the ZSE and the CSD to become self-regulatory organizations. SECZ should also clearly demarcate the margins in which the ZSE and the CSD will operate to avoid regulatory confusion. SECZ should push for the automation of the ZSE and should also put in place automated surveillance systems. This would ensure that SECZ does not involve itself in ground work operations in the market. SECZ would be able to concentrate on broader capital market matters such as education, counseling of market participants and increase training and development of all registered entities concentrating on the roles and regulatory expectations of the SECZ from the listed companies, the investors and other market participants.

The harmonization of the regulations could stop market players from making self-decisions on which entity to approach. The cooperation with other regulators will therefore avoid a

regulatory gap. SECZ would therefore be able to be proactive on matters that directly fall under its regulatory purview.

5.5.4 Incorporate the Principles-based Approach

SECZ should move towards a principles based style of regulation rather than the rule based system. SECZ should promote the best practice approach through its directives, the quarterly bulletin or other press releases. It should leverage more on market discipline rather than through an array of rules. This development could minimize regulatory conflicts by constantly interacting with licensed entities and other regulators. The application of principles in the capital market would give the market players an opportunity to be innovative based on circumstances.

5.6 AREAS OF FURTHER STUDY

Future studies can take the form of a survey and should focus on the broader market to include the investors, listed companies and other regulatory agencies that have regulatory interactions with SECZ such as IPEC and the RBZ. Although this research covered a considerable number of the licensed companies, additional studies should test the findings that are presented by the researcher. The study was only a snap shot of the regulatory regime and it was done when SECZ was only 5 years old and not yet established. Similar studies to assess the regulatory philosophy of SECZ can be carried out after considerable time such as ten or twenty years.

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APPENDICES

APPENDIX ONE: INTERVIEW GUIDE

Interview Guide

My name is Lyinah Tendayi Madende and I am studying towards a Master of Business Administration with the University of Zimbabwe. I am carrying out a research on the operations of the Securities and Exchange Commission. My topic is “An assessment of the regulatory approach of the Securities and Exchange Commission” The purpose of the research is to gain insight into the realities of regulation in the capital market. The study is purely for academic purposes. I request an interview with you at a place and time convenient to you. The interview guide is attached hereto. The interview will take about 40 minutes. Also attached is a letter of approval by the Securities and Exchange Commission. All information received will be solely used for academic purposes and your identity shall be kept confidential.

Date of Interview -----

THE INTERVIEW QUESTIONS

INTERVIEWEES INFORMATION

1. What is the type of your licensable Activity you carry out?
2. Please state your Age
3. How many years have you spent in the capital market?
4. What educational qualifications do you have?

INTERVIEW QUESTIONS

1. What are the issues that influence SECZ regulatory implementation process/strategies?
2. What benefits do you derive from complying with SECZ regulations?
3. In what ways do you interact with SECZ?
4. In your view how SECZ does conducts itself in the market?
5. How would you describe SECZ’s interventional enforcement strategies?

6. What is SECZ doing to educate licensed entities to understand their regulatory objectives and the securities laws?
7. How are licensed entities involved in the formulation of the laws that govern the capital market?
8. Can you describe the nature of the laws applied by SECZ?
9. How would you describe SECZ application of laws/regulatory requirements?
10. What are the challenges you encounter in implementing SECZ regulatory requirements
11. What role do industry associations have in regulatory issues?
12. What are the roles of the ZSE and the CSD?
13. In what ways do market players cooperate with SECZ
14. What are the channels to complain or challenge SECZ regulatory actions?
15. What recommendations do you suggest to improve the implementation of securities laws?

End of Interview Guide

APPENDICE TWO: THEMES

Question	Themes
<p>Question 1. What are the issues that influence SECZ regulatory implementation process/strategies?</p>	<p>Independence Compromised political independence, budgetary approval, lack of financial independence, SECZ protects investors independently and existence of regulatory capture.</p> <p>Availability of Resources Poor income levels, income dependant on market, small market and shortage of skills.</p> <p>Legal Authority Lack of legal authority, fragmented laws and need to follow the laws.</p> <p>History of the Market No regulation prior to SECZ, complacence to comply with laws and incidence of market abuse</p> <p>Economic Environment Small and fragile players, slow market and poor quality of products</p> <p>Structure of market Fragmented structure, duplication of roles and ownership of the Exchange</p> <p>Globalization International influences, control by international bodies and international laws.</p> <p>Personalities of SECZ employees Reputation, political interest and personal values of employees</p>
<p>Question 2. What benefits do you derive from complying with SECZ regulations?</p>	<p>Attitude towards Regulation Protection of market integrity, client confidence, fears of reputational loss, prevention of crime and fear of reprimand.</p>
<p>Question 3. In what ways do you interact with SECZ?</p>	<p>Interactions with the Regulator Limited involvement in the formulation of laws, Interaction limited to regulatory and licensing transactions, little collaboration between SECZ and the regulated entities</p>
<p>Question 4. In your view how SECZ does conducts itself in the market?</p>	<p>Conduct of SECZ Aggressiveness and insistence in the enforcement of the laws</p>
<p>Question 5. How would you describe SECZ's interventional enforcement strategies</p>	<p>interventional Enforcement Strategies Generally reactionary though reformist with asset managers, inactive with investment managers, antipathetic with brokers, indifferent with custodians.</p> <p>Lack of tools for investigations, Lack of financial and technical knowhow</p> <p>Protection of Investors Education to investors and vulnerability of investors</p> <p>Licensing requirements and inspections Renewal of licenses annually counterproductive, thorough licensing requirements, annual on-site inspections satisfactory and routine returns and requests for information.</p> <p>Penalties Propensity for heavy penalties, penalties necessary to guarantee compliance, occasional lack of authority to act limiting effectiveness and more clarity required in the fining and penalties framework.</p>
<p>Question 6. What is SECZ doing to educate licensed entities to understand their</p>	<p>Education to licensed entities Limited open discussions, investors' education prioritized through press columns and no trust at the inception of the regulator hence the need to dispel market misconception on</p>

regulatory objectives and the securities laws?	the role of SECZ.
Question 7. How are licensed entities involved in the formulation of the laws that govern the capital market?	Consultation Limited consultation and commenting on proposed laws. Communication SECZ communicates with the capital market players directly through letters, public notices, emails, telephone and publications through the government gazettes. SECZ imposes directives on matters that have negative impact on licensed entities. Instructive command style, formalistic approach and limited interaction..
Question 8. Can you describe the nature of the laws applied by SECZ?	Nature of the laws SECZ adopted a rules based approach as opposed to the principle based approach
Question 9. How would you describe SECZ application of laws/regulatory requirements?	Application of Laws Too strict, lack consistence, occasional reformist approach, Inflexible and not accommodative
Question 10. What are the challenges you encounter in implementing SECZ regulatory requirements?	Interpretation of laws Rigid application of rules, literal interpretation Cost constraints, duplication of ZSE and SECZ roles, reconciliation and consolidation of the pieces of legislation that were fragmented was needed, sticking to rules meant that licensed operator could not be innovative and rules went against cost containment measures implemented by capital market players. The gradual adoption of a principles-based approach recommended
Question 11. What role do industry associations have in regulatory issues?	Role of associations Platform to air the views, feedback and contributions without fear of victimization by the regulator And lobbying for amendments to regulations
Question 12. What are the roles of the ZSE and the CSD?	Role definition Confusion in the market, duplication of roles Supervisory Roles Control over operations of CSD and ZSE
Question 13. In what ways do market players cooperate with SECZ	Trust Lack of mutual trust Private Sector standards Poor private sector standards Sharing of information Little sharing of information and collaboration
Question 14. What are the channels to complain or challenge SECZ regulatory actions?	Complaints Channels No clear channels to complain about SECZ regulatory actions
Question 15. What recommendations do you suggest to improve the implementation of securities laws?	Need for unity and cooperation between SECZ and market players. Reconciliation and consolidation of the pieces of legislation that were fragmented. SECZ should be pro-active in line with the fast changing global context. SECZ should adopt a principles based approach or blend rules and principles. SECZ should be flexible. SECZ should consider the internal and external environment of the regulated entities in its regulatory conduct. SECZ should conduct wider consultations and employ effective, two-way communication and the establishment of clear complaints channel. SECZ to empower ZSE and CSD

APPENDIX THREE: INTERVIEWEE CODES

R1	Respondent 1, Licensed Custodian
R2	Respondent 2, Licensed Securities Dealer
R3	Respondent 3, Registered Securities Exchange
R4	Respondent 4, Licensed Securities Dealer
R5	Respondent 5, Licensed Securities Dealer
R6	Respondent 6, Licensed Asset Manager
R7	Respondent 7, Securities and Exchange Commission
R8	Respondent 8, Securities and Exchange Commission
P9	Respondent 9, Securities and Exchange Commission
R10	Respondent 10, Licensed Securities Dealer
R11	Respondent 11, Licensed Securities Dealer
R12	Respondent 12, Licensed Investment Advisor
R13	Respondent 13, Licensed Investment Advisor
R14	Respondent 14, Licensed Transfer Secretary
R15	Respondent 15, Licensed Securities Dealer
R16	Respondent 16, Licensed Securities Dealer
R17	Respondent 17, Licensed Investment Advisor
R18	Respondent 18, Licensed Asset Manager
R19	Respondent 19, Central Securities Depository
R20	Respondent 20, Licensed Asset Manager
R21	Respondent 21, Licensed Custodian
R22	Respondent 22, Securities and Exchange Commission