STIKEMAN ELLIOTT

Review and Revision of the Trinidad and Tobago *Securities Industry Act, 1995* and Related By-Laws and Associated Legislation

ADDENDUM TO INCEPTION REPORT

January 30, 2003

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Trinidad and Tobago Securities Industry Act, 1995
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ADDENDUM TO INCEPTION REPORT

1) INTRODUCTION AND PURPOSE OF THIS ADDENDUM

On November 18, 2002 Stikeman Elliott delivered its Inception Report to the Trinidad and Tobago Securities and Exchange Commission (the "**TTSEC**") in accordance with the mandate it granted to Stikeman Elliott on September 6, 2002 to review the *Securities Industry Act, 1995* (the "***SIA, 1995***"), the by-laws (the "**By-Laws**"), and associated legislation, including the *Companies Act, 1995* (the "***Companies Act***").

The purpose of this Addendum to the Inception Report (the "**Addendum**") is to elaborate and provide greater detail to the recommendations made in the Inception Report and to address comments received from the TTSEC and market participants in Trinidad and Tobago.

In this Addendum the term "**Consultants**" refers to Messrs. Ermanno Pascutto and Dee Rajpal together with other members of Stikeman Elliott and outside personnel engaged as part of the mandate. Other capitalized terms which are not defined have the meanings given to such terms in the Inception Report.

2) DETAILED RECOMMENDATIONS

This section sets out the Consultants' more detailed recommendations with respect to the Consultants' structural and legislative recommendations set out in the Inception Report.

A) Structural Recommendations

i) The basis underlying securities regulation in Trinidad and Tobago needs to evolve from jurisdiction based on the issuer to jurisdiction based on the location of the trade and the residency of the investor.

In the Inception Report, the Consultants recommended that the underlying basis of securities regulation in Trinidad and Tobago should evolve to reflect jurisdiction based on the residency of the investor and the trade, not that of the issuer.

Where this distinction is most evident is in the dual regulation of public companies under the *Companies Act* and the *SIA, 1995*. The implementation of this change would require more than the specific amending of any single provision or provisions of the *Companies Act* or the *SIA, 1995*. The change would, among others, be reflected in changes to the definition of "reporting issuer" in *SIA, 1995* (which is discussed below) and the specific

repeal or amendment of certain duplicative provisions of the *Companies Act* (which is also discussed below).

The alternative method to implement such a conceptual change would be to legislate new exemptions into the various provisions of the *Companies Act*. These exemptions from the *Companies Act* requirements for areas covered in the *SIA, 1995* would be made available to public issuers that comply with the revised *SIA, 1995* standards (in areas such as financial reporting).

The result would be a system where regulation of all public issuers falls under the *SIA, 1995*, a statute which asserts its jurisdiction where a person or company is trading in Trinidad and Tobago, regardless of whether the issuer is governed by the *Companies Act* or some other foreign or domestic law.

In addition, this conceptual change would require identifying with some specificity when an investor is resident in Trinidad and Tobago and when a trade is conducted in the jurisdiction. Similar to the discussion elsewhere in this Addendum regarding "suitcase brokers", the Consultants would recommend a deeming provision be included in a revised *SIA, 1995*. With respect to trading then, a trade would be deemed to take place in Trinidad and Tobago where the purchaser of the security or any dealer, broker, trader, underwriter or agent involved in the purchase and sale transaction is resident in Trinidad and Tobago. An act, advertisement, solicitation, conduct or negotiation directly or indirectly in furtherance of these activities would be deemed a trade in Trinidad and Tobago if:

- done by mail, telephone or facsimile (whether unsolicited or not) with or to a person or company resident of Trinidad and Tobago;
- in the case of e-mail, the recipient of the e-mail address is resident in Trinidad and Tobago; or
- in the case of internet securities offerings, the web pages and documents in respect of that offering, may be accessed by persons or companies resident in Trinidad and Tobago, unless the document or web page contains a prominent disclaimer that expressly identifies the jurisdictions in which the offering is qualified to be made, and that Trinidad and Tobago is or is not such a qualified jurisdiction, and reasonable precautions are taken to ensure that no actual sales occur to persons or companies resident in Trinidad and Tobago unless done in compliance with the *SIA, 1995*.

ii) The policy making and enforcement functions of the TTSEC need to be separated from its adjudicative function.

a) Separation of Functions

In the Inception Report, the Consultants recommended that the adjudicative powers of the TTSEC should be vested in a separate body, thereby leaving the TTSEC to act primarily as a policy making and oversight body. The TTSEC would oversee the staff which administers the *SIA, 1995* (including investigation and enforcement) to ensure that the TTSEC's functions are exercised in accordance with its regulatory objectives.

b) Adjudicative Function

To this end, the Consultants recommended that the TTSEC's adjudicative function be separated and vested in a separate body or bodies. Such a body would hear appeals of TTSEC and/or TTSEC staff decisions (made under delegated authority from the TTSEC) on administrative matters such as prospectus receipts and registration of market actors and would hear cases at first instance of other breaches of securities laws brought by the TTSEC. A similar conceptual structure to the proposal is in use in Hong Kong but operates with two separate bodies. Given the size of the market and the resources in Trinidad and Tobago, it was considered that these functions may be conducted in one body. Such a body would be both an appellate body to hear appeals from the decisions of the TTSEC and a tribunal of first instance to consider disciplinary or enforcement proceedings brought by the TTSEC. For the purposes of illustrating the two roles, the Inception Report described the adjudicative bodies as two separate bodies following the model used in Hong Kong.

c) A Single Tribunal

The Consultants understand that there is support for such an adjudicative body and a preference that the first instance and appellate functions be combined in one body. For purposes of this report, we will refer to that body as the Securities Markets Tribunal (the "**Tribunal**").

At this point, the Consultants would recommend that the Tribunal be structured as follows. It would be chaired by a judge of the High Court and would be staffed on an as needed basis from a roster of five persons, who could be former judges, members of the bar, outside or foreign securities practitioners, and former registrants with no active business interest in the local securities markets. Current members of the TTSEC would not be appointed to the Tribunal (although it may be appropriate to consider former members who have been out of office for a number of years). Appointments would be made by the Judicial and Legal Service Commission in consultation with the TTSEC. Each hearing panel would consist of a judge and two lay members with relevant experience. Hearings of the Tribunal would be open to the public and the media. For purposes of a hearing, the Tribunal could receive and consider any material by way of oral evidence or written statements or

documents. It would have the power to require a person to attend before it to give evidence and produce any record or document.

However, comments were received to the effect that the Tribunal should be structured in a manner similar to the Environmental Commission under the *Environmental Management Act, 2000*. In this case, we understand that the Tribunal would be a superior court of record and would have an official seal that would be judicially noticed, and would have the powers inherent in such a court in addition to the jurisdiction and powers granted to it under the *SIA, 1995*. Such a conceptual change should be considered by market participants, and would be addressed by the Consultants in the Interim Report.

d) Appealing TTSEC Decisions

The first function of the Tribunal would be to hear appeals of all decisions made by the TTSEC, or by the General Manager, as the delgatee of authority from the TTSEC. Separating the appeal function from the TTSEC would have the effect of giving market participants greater confidence that the appellate process is fair and impartial. The Tribunal would be empowered to hear all matters under the *SIA, 1995*, including decisions regarding prospectus receipts and registration matters.

e) Powers of the Tribunal

The Tribunal would have the power to uphold, overturn or remand a decision of the TTSEC or the General Manager for reconsideration. It would also have the power to do any act or thing or issue any order or make any decision, on appeal, which the TTSEC or the General Manger could have done, such as issue a prospectus receipt or grant registration to an applicant.

f) Disciplinary Function

The second function of the Tribunal would be to hear market misconduct cases at first instance. The TTSEC would generally bring actions against market participants and reporting issuers in front of the Tribunal. The jurisdiction of the Tribunal would extend to cover matters including:

- insider trading and self dealing;
- market manipulation;
- trading in securities by unregistered persons (the "suitcase" brokers);
- false trading in securities and illegal price rigging;
- breaches of disclosure standards; and
- disclosure of false or misleading information in securities transactions.

g) Standard of Proof

The standard of proof in hearings before the Tribunal would be the civil standard of "balance of probabilities". The Tribunal would not be a criminal tribunal. It would be a civil system to address market misconduct. The Tribunal would hear market misconduct cases relatively quickly using civil procedures. It would have the ability to consider all relevant and logically probative evidence without being bound by the restrictive criminal laws of evidence.

h) Sanctions

The Tribunal would have the power to issue a range of civil sanctions only (subject to compliance with the Constitution of Trinidad and Tobago), which could include for example:

- disgorgement of profits made or loss avoided, subject to compound interest thereon;
- disqualification of persons from being a director or officer or otherwise involved with a public company for up to five years;
- removal or suspension of registration under the *SIA, 1995*;
- fines;
- "cease and desist" orders (i.e. not to breach any of the market misconduct/ manipulation provisions for up to five years); and
- payment of costs associated with the action.

The range of orders and remedies available would enable the Tribunal to deal comprehensively and relatively swiftly with market misconduct with the attendant benefits of simpler evidentiary and procedural rules. The Tribunal would not be able to issue criminal sanctions, such as imprisonment.

i) Dual Route

However, both the Tribunal and the TTSEC would have the authority to recommend that particular matters, where applicable, be treated criminally and referred to the Director of Public Prosecutions or other appropriate authority for criminal prosecution. This would allow the TTSEC and the Director of Public Prosecutions to make an assessment of the best way to proceed depending on the nature and severity of the alleged offence.

j) Appeal and Judicial Review

No subsequent statutory right of appeal would be available from the Tribunal to the regular court system in cases where it is exercising its appellate function. Recourse would remain available through the mechanism of judicial review. As a first instance tribunal

hearing market misconduct cases, a right of appeal on the merits would be available from the Tribunal to the Court of Appeal.

k) Courts

The role of the courts would not be ousted in this model. Rather the courts would retain their jurisdiction as a forum for the appeal of market misconduct cases, judicial review of all decisions of the Tribunal, and for enforcing administrative orders and issuing criminal sanctions, and for appeal of certain decisions.

l) Admissibility of Tribunal Findings

In order to make civil rights of action more meaningful, the *SLA, 1995* could provide that findings of the Tribunal may be admitted in private lawsuits by aggrieved investors against the offenders. Thus, where the Tribunal determines that a person has breached a civil market misconduct offence, that determination is evidence of wrong doing by the offender in a private lawsuit against the offender. While the findings of the Tribunal would be admissible in private lawsuits, such findings would not be conclusive in private lawsuits. A finding of liability by the Tribunal must be shown to be probative to the issue (which normally it will be) and this creates a rebuttable presumption of liability in a private lawsuit. What the rule for admissibility does reflect is a policy to encourage investors to take action to protect themselves.

m) Resources

The success of the Tribunal will be a function of the resources devoted to it, the lack of which was a concern expressed by a number of commentators. However, in the Consultants' view, the increase in resources (both legal and financial) would be minimal. It is important to note that existing judges would be used and that no new physical premises would be needed. New costs would include new professional administrative staff for the Tribunal and the *per diem* costs of having lay people sit on the Tribunal. Both the TTSEC and the Director of Public Prosecutions would, of course, require resources to bring matters before the Tribunal, however, these costs would have to be incurred to prosecute offences under the *SLA, 1995* today.

In the Consultants' view, the resources would be well utilized, in that by clearly separating the adjudicative functions into a new body, regulatory oversight and enforcement would improve. It would provide confidence to the public and market practitioners that TTSEC decisions are proper and fair. It would give confidence to the public that market misconduct cases will be dealt with relatively quickly using efficient civil procedures.

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B) Preliminary Legislative Recommendations

i) The SIA, 1995 needs to be amended, not re-written.

No further detail is required with respect to this recommendation. All market participants who commented on the Inception Report, the Central Bank of Trinidad & Tobago (the "**Central Bank**") and the TTSEC were in agreement with this recommendation.

ii) The structure, power and functions of the TTSEC need to be revised in the SIA, 1995 to provide clear by-law making authority and clear enforcement power.

In the Inception Report, the Consultants recommended that the by-law making process be amended to permit the TTSEC to make by-laws subject to the negative disapproval by the appropriate Minister. As well, a suggested list of heads of by-law making power (which would expand and more clearly delineate the areas in which the TTSEC could make by-laws) was also suggested. The suggested by-law making process laid out in detail is set out below (and a new section of the *SIA, 1995* would be drafted to reflect this process).

Draft by-laws would initially be subject to the scrutiny of the TTSEC commissioners who would have the opportunity to approve or disapprove of the draft by-laws prepared by its staff. Once approved at the TTSEC level, the by-law would be published for public comment for a period of between 60 days and 120 days. Following the public comment period, all comments would be evaluated by the TTSEC and its staff. If required, amendments to the draft by-law would be made by staff and re-submitted to the TTSEC. Where a material amendment is made the draft by-law would be republished for public comment for an additional 30-day period. Where non-material amendments are made, or none at all, the draft by-law would then be sent to the responsible Minister (not Parliament) for negative disapproval. The responsible Minister would have 60 days to disapprove the draft by-law. If it were disapproved, the Minister would return the by-law to the TTSEC with comments for the TTSEC's further consideration. If disapproval is not received by the 60th day, on the 75th day following its sending to the Minister, the draft by-law would become a by-law carrying the force of law. The Minister could also explicitly approve the by-law within the 60-day period. As well, a shortening of the time periods would be available in appropriate circumstances.

Not all comments received on the Inception Report were in favour of this revised process, some commenting that it was not all that different than what is currently set out in section 131 of the *SIA, 1995*, and others commenting that these types of rules should be subject to Parliamentary approval, or at the very least, negative disapproval.

The Consultants note that the proposed revised process has two important distinctions from the current practice in Trinidad and Tobago. First, draft by-laws emanate from the professional staff of the TTSEC, and second, Parliament's role becomes more limited in the process by effectively delegating to the TTSEC and the responsible Minister

the power to make the detailed by-laws regulating the securities markets. Both of these changes, it is suggested, would help develop an effective, modern securities regulatory regime in Trinidad and Tobago. With respect to the former, securities regulation is becoming an increasingly complex field of endeavor which in part explains the development of professional regulatory bodies, such as the United States SEC and the TTSEC. It is becoming increasingly difficult for persons without a technical background in the field to understand the complexity of products and issues in modern securities markets. For this reason, it is recommended that the TTSEC be granted the ability to make and revise by-laws.

Second, it is suggested that Parliament effectively delegate the creation of the details of the regulation of the securities markets to the responsible Minister who would review the draft by-laws approved by the commissioners of the TTSEC following preparation by its professional staff. This would have the effect of depoliticizing the process of making subordinate legislation and increasing the speed with which issues in the securities markets can be addressed (partly because Parliament had removed itself from the process). Depoliticizing the process, it is suggested, leads to better rule-making, by limiting the influence of partisan politics and the daily whims of public opinion. The implementation of the *Sarbanes-Oxley Act* in the United States is one recent example of laws being passed in a politically charged atmosphere.

Public participation in such a process would not be limited as comment periods would be statutorily mandated for new by-laws. The purview of the TTSEC would not be unlimited but would be subject to detailed heads of by-law making authority which would limit the jurisdiction of the TTSEC in making new by-laws (for example, the by-laws would not permit the TTSEC to create criminal sanctions and penalties for a breach of a by-law in excess of that currently provided for in section 147 of the *SIA, 1995*[1]). The appropriate Minister would provide, in the normal course, a check on the by-law making activities of the TTSEC and could comment and/or return by-laws for revision which he or she did not think were fit, proper, in the public interest or otherwise outside of the scope of the TTSEC's by-law making power. Finally, and perhaps most importantly, Parliament would retain the ultimate discretion to amend the *SIA, 1995* to limit or remove the by-law making authority from the TTSEC if it was of the view that the power was being abused or not used for its intended purposes. The power that Parliament delegates can always be retrieved by a subsequent act of Parliament.

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[1] In light of the increasing severity of penalties which may be leveled in other jurisdictions for securities law violations, it may also be appropriate to consider whether the general offence provisions should be increased from its present maximum penalties of one hundred thousand dollars and two years imprisonment to suggested fines of up to one million dollars and ten years imprisonment. This would give both prosecutors and courts a wider range of potential sanctions to pursue based on the severity of the offence.

iii) The proposed Take-Over By-Laws need minor amendment and should be implemented as a by-law carrying the force of law once clear by-law-making power is given to the TTSEC.

The Consultants would recommend that the following specific changes be made to the draft Take-Over Bid By-Laws:

- Amend subsection 3(2) by expanding the definition of "affiliate" to include non-corporate entities such as partnerships, trusts and unincorporated associations.
- Amend paragraph 12(4)(a) to change the withdrawal rights to any time where the securities have not been taken up by the offeror as opposed to any time before the expiration of thirty-five days from the date of the bid. This change will help ensure that withdrawal rights are available if the bid expires beyond the minimum 35-day period.
- Amend subsection 12(12) to clarify that notwithstanding subsection 12(12), if the offeror waives any terms or conditions of a bid and extends the bid in circumstances where the rights of withdrawal conferred by paragraph 12(4)(b) are applicable, the bid shall be extended without the offeror first taking up the securities which are subject to such rights of withdrawal. This is a technical amendment required to ensure that an offeror is not required to take up and pay in a circumstance where the withdrawal rights continue after a notice of change or variation to the bid.
- Amend subsection 17(5) to refer to publishing as opposed to mailing as subsection 17(3) permits bid documents to be published as opposed to mailed to recipients.
- Amend subsection 20(4) to change the reference to 25% as opposed to 20%, as 25% is the threshold to trigger the take-over bid requirements.

As well, the draft Take-Over By-Laws should require an offeree issuer to furnish to an offeror a list of securityholders of the offeree issuer in order to permit the offeror to deliver the bid documents in compliance with the Take-Over By-Laws. Offerees would have ten (10) days to comply with the request.

Finally, while not an amendment to the Take-Over By-Laws, the definition of "take-over bid" in section 201 of the *Companies Act* should be amended to be consistent with the by-law.

With these amendments in place, the Take-Over By Laws should be republished for comment by market participants.

iv) ***A new by-law governing collective investment schemes should be drafted and implemented as a by-law carrying the force of law once revised by-law making power is given to the TTSEC. Duplicative regulation by the Central Bank should be ended. Existing policy statements and guidelines should be repealed and subsumed in the new by-law.***

In the Inception Report, the Consultants recommended the drafting of a new by-law governing collective investment schemes and unit trusts to replace existing Central Bank guidelines and TTSEC Policy Guideline 11.1. The recommendations could be divided into four main areas described as follows.

a) Prospectus Disclosure

The proposed by-law would provide detailed requirements as to the contents and format of a prospectus that offers unit trust and mutual fund securities (collectively referred to in this section as the "**Mutual Fund Securities**") by a local issuer.

It would be a requirement that a copy of the prospectus together with current financial statements for the Mutual Fund Securities being offered, which financial statements are incorporated by reference and form part of the prospectus, be delivered to each investor so as to better assist them in making investment decisions. A prospectus offering Mutual Fund Securities would be required to include, without limitation, the following:

- the investment objectives of the Mutual Fund Securities being offered, setting out principal features including any investment restrictions;
- the investment strategies of the Mutual Fund Securities being offered, setting out principal investment strategies used to achieve its investment objectives;
- a description of any relationship the mutual fund or the manager of the mutual fund has with entities or individuals which may give rise to a potential conflict of interest;
- the methodology used to calculate net asset value;
- performance data for the Mutual Fund Securities being offered, calculated and presented in accordance with requirements set out from time to time by staff of the TTSEC;
- a summary of all the fees, charges and expenses payable by the mutual fund and by investors in the Mutual Fund Securities;
- risk factors or other investment considerations that an investor should take into account with respect to investing generally in mutual fund securities as well as any material risks specific to the Mutual Fund Security being offered; and
- a statement of an investor's rights in the case of an untrue statement or non-disclosure in the prospectus. In addition to rights applicable in respect of all prospectuses, an investor would be given a "cooling-off" period after the

purchase of a Mutual Fund Security during which time they could unwind the purchase for any reason whatsoever. Consideration will need to be given to whether this period should be the present two business day "cooling off" period provided under the *SIA, 1995* or a longer or shorter period.

In the case of a foreign issuer seeking to offer foreign mutual fund products in Trinidad and Tobago, the proposed by-law would not require that such offering documents comply with the form requirements imposed on offerings conducted within Trinidad and Tobago. However, the foreign issuer would be required to:

- submit to the jurisdiction of Trinidad and Tobago;
- provide the TTSEC with evidence that such foreign mutual fund products are offered in a foreign jurisdiction approved by the TTSEC (which initially, it is suggested, could be the United States and Canada, and jurisdictions in the Caribbean which the TTSEC would consider appropriate based on the standards of regulation of collective investment schemes in that jurisdiction. For Caribbean jurisdictions, it may be appropriate for the TTSEC to consider the level of reciprocity afforded by those jurisdictions in determining whether they should be approved jurisdictions for this purpose); and
- provide to investors resident in Trinidad and Tobago a document that briefly sets out the substantive rights of such investors (i.e. the "cooling off period" and rights in the event of an untrue statement or non-disclosure) and provide such document to the investors at the same time the foreign prospectus is delivered to them.

b) Registration

In order to better regulate the sale of mutual funds in Trinidad and Tobago, the proposed by-law would create a new category of market actor – "mutual fund salesperson". Individuals applying for registration as mutual fund salespersons would be required to meet certain minimum standards to be determined from time to time by the TTSEC, allowing appropriate standards to be set to reflect the market conditions at different times. The Consultants recommend that initially, the TTSEC should require mutual fund salespersons to have qualifications similar to the ones required of brokers. Other proficiency standards and registration conditions, which may include requiring completion of certain securities courses (including courses offered in the United States and Canada), should be introduced when the TTSEC sets similar standards for the other categories of registration or at an appropriate time as determined by the TTSEC.

c) Conflict of Interest

The proposed by-law would impose on the manager and investment managers for the mutual funds a fiduciary duty to act fairly, honestly, in good faith and in the best interest of the holders of the Mutual Fund Securities. The Consultants recommend that staff of the TTSEC issue guidelines from time to time to advise the industry how they interpret the

standards and provide examples of conduct that the TTSEC would consider to be a breach of such duty.

d) Other Recommendations

The following are some additional recommendations of the Consultants with respect to regulating the unit trust and mutual fund security industry in Trinidad and Tobago that would also be included in the proposed by-law:

- entities acting as custodians for the Mutual Fund Securities should be licensed under the *Financial Institutions Act* (Trinidad and Tobago) or are recognized financial institutions in an approved foreign jurisdiction;
- provide for a definition of "mutual funds" that would be subject to the proposed by-law;
- mutual funds would be prohibited from adopting names that are misleading, and mutual funds would be prohibited from using certain designations (such as "bond fund" or "money market fund") unless they meet certain criteria;
- management expense ratios and performance data would be required to be calculated in accordance with internationally recognized standards (for example, the Global Investment Performance Standards);
- requirements for sales communications and other advertising materials (such as with respect to performance data, referring potential investor to the prospectus, etc.);
- all material contracts (for example, declarations of trust, management agreements and portfolio advisory agreements) with respect to the mutual fund would be required to be filed with the TTSEC and be made available for inspection by holders of the securities; and
- before a fundamental change that affects the Mutual Fund Securities (for example, changing a fund's investment objective, the methodology used to calculate net asset value or an increase in management fees), notice of the proposed change would be required to be published in a newspaper in general circulation in Trinidad and Tobago no less than 90 days in advance of the change in order to allow investors to redeem before the change becomes effective.

v) The SIA, 1995 should be amended to provide for enhanced disclosure by reporting issuers.

In the Inception Report, the Consultants made recommendations with respect to the preparation of annual audited financial statements, management discussion and analysis ("**MD&A**"), quarterly unaudited financial statements, insider reporting, and the public filing and viewing of such documents. The following are the more detailed requirements all of which would be included in a new part of the *SIA, 1995* drafted to deal specifically with on-going continuous disclosure matters of reporting issuers (other than reporting issuers which

are mutual funds or unit trusts, which would have a separate continuous disclosure regime in the new by-law on collective investment schemes).

a) Annual Audited Financial Statements

Every reporting issuer would be required to file with the TTSEC and to send to it securityholders, within 120 days of its financial year-end, annual audited financial statements which have been prepared in accordance with International Accounting Standards ("**IAS**"). Such financial statements would be required to include:

- a balance sheet as at its financial year-end (with a comparison to the same date in the year prior period);
- an income statement, a statement of retained earnings (surplus), and a cash flow statement for the last completed financial year and the period covered by the financial year immediately preceding the most recently completed financial year; and
- notes to the financial statements.

Such financial statements will be required to be approved by the board of directors (or equivalent) of the reporting issuer, evidenced by the signature of two directors (or equivalent) on the balance sheet for the reporting issuer. In order to ensure compliance with the minimum standard, the Consultants would recommend that Part XI of the *SIA, 1995* be amended to make it an offence for any reporting issuer to file financial statements which do not comply with IAS (with appropriate exemptions for approved foreign issuers filing financial statements prepared in accordance with the requirements of an approved foreign jurisdiction). In such cases, the TTSEC should be empowered to fine the reporting issuer and/or its directors (or equivalent) and/or cease trade the reporting issuers' securities until the reporting issuer complies. Both the reporting issuer and its directors (or equivalent) would have the benefit of the defence in an amended subsection 147(4) of the *SIA, 1995* where they can show reasonable reliance on the advice of external auditors or accountants in complying with the IAS standard. Annual audited financial statements included in a prospectus would be subject to the same standards, but also the civil liability provisions of sections 128 and 129 of the *SIA,* 1995 which apply to untrue statements in a prospectus, including financial statements.

It would also be a requirement that annual financial statements filed with the TTSEC include an auditors report on the financial statements. The audit would have to be conducted by a person or company who is a member of an appropriate professional accounting body in Trinidad and Tobago, which we understand would be the Institute of Chartered Accountants of Trinidad and Tobago, or a member of any other professional accounting body approved for this purpose by the TTSEC, whether local or foreign. The audit would have to be conducted in accordance with International Standards of Auditing ("**ISA**"). Audit reports would not be permitted to be filed with a reservation of opinion unless an exemption were sought from the TTSEC. Auditors who knowingly provide false

or misleading audit reports (including audit reports without a reservation of opinion where one would be warranted) would be subject to the general offence provision found in section 147 of the *SIA, 1995.* The Consultants would recommend that, in addition to this penalty, a new offence provision be included which would ban auditors who provide false or misleading audit reports from being auditors of a reporting issuer for up to five (5) years (This provisions could be enforced by the TTSEC in front of the Tribunal). As with IAS, appropriate exemptions would be made available for approved foreign issuers who have audits conducted under a standard other than ISA.

b) Management Discussion and Analysis of Annual Financial Statements ("**Annual MD&A**")

At the same time a reporting issuer files its annual audited financial statements with the TTSEC and sends them to its securityholders it will also be required to prepare Annual MD&A, file the same with the TTSEC, and send the Annual MD&A to its securityholders.

The purpose of Annual MD&A is to supplement the annual financial statement disclosure and to discuss material information and changes about the reporting issuer's financial position that may not be readily apparent from reading the financial statements. Its purpose would also be to discuss, in ordinary language, the reporting issuers' present financial condition as well as its future prospects. Discussion in an Annual MD&A would require the reporting issuer to compare the most recently completed financial year to the prior year. In particular, Annual MD&A would be required to discuss six (6) major topics:

- overall performance, which would include discussing:
    - the reporting issuer's overall financial performance for the financial year including its year-end financial condition, its results of operations, and cash flows (and a comparison to prior year periods);
    - general industry and economic factors affecting the reporting issuer;
    - changes in the business during the year and how those changes have impacted financial condition and performance;
- results of operations, which would include discussing:
    - net sales or revenues for the year, including the impact of new goods or services and factors affecting the change in sales;
    - cost of sales;
    - expenditures in the financial year including research and development, administration and marketing costs, and other material expenses (and a comparison to prior year periods discussing what factors affected the changes in the expenditures);

  - trends, commitments, events, risks or other factors that the reporting issuer believes may materially affect the reporting issuer's future results of operations;
  - any unusual or infrequent factors or transactions which affected results of operations for the financial year;
- liquidity, which would include discussing:
  - the reporting issuer's cash and cash equivalents, in both the short and long term, and their sufficiency to meet planned goals and objectives;
  - working capital requirements;
  - how the reporting issuer will deal with working capital deficiencies, if one exists, or is expected to exist in the upcoming financial year;
  - how balance sheet items or cash flows have impacted, or may impact, the reporting issuer's liquidity or working capital position;
  - defaults on any debt obligations and the effect of such defaults on the reporting issuer;
- capital resources, which would include discussing:
  - the amount, nature and purpose of capital expenditures required;
  - the source of the funds to meet the requirements;
  - sources of financing for the reporting issuer, including sources that have been arranged but not yet used;
- related party transactions, which would include discussing:
  - all material transactions with non-arm's length parties, including discussing the purpose of the transaction, identifying who the related party is, how transaction prices were determined, and the ongoing relationship with the related party, if applicable;
- accounting policies, which would include discussing:
  - any changes in accounting policies from prior financial years, the reason for the change, and the policy currently adopted by the reporting issuer;
  - those accounting policies which are critical to the reporting issuer in that they require judgements, estimates or uncertainties where the use of different judgements, estimates or uncertainties may result in materially different amounts reported in the reporting issuer's financial statements; and
  - exemptions would be available for new reporting issuers where prior year comparisons are unavailable.

c) Quarterly Unaudited Financial Statements

The Consultants have also recommended that reporting issuers be required to prepare, file with the TTSEC, and send to securityholders, quarterly unaudited financial statements within 60 days of the quarter end of the reporting issuer. This requirement would apply to the first three (3) quarters in any financial year of a reporting issuer, the fourth quarter statements being included in annual audited financial statements of a reporting issuer. Quarterly financial statements would have to be prepared under IAS and include:

- a balance sheet as at the end of the quarterly period (with a comparison to the same date in the year prior period);
- an income statement, a statement of retained earnings (surplus), and a cash flow statement for the quarterly period as well as the year-to-date period, and for the corresponding periods in the immediately preceding financial year; and
- notes to the financial statements.

No audit would be required of quarterly financial statements, nor would a management discussion and analysis of the quarterly financial statements be required (however, in the longer term, consideration should be given to making this a requirement as well). Similar to what is currently set out in By-Law 55(2), quarterly financial statements would not be required to be prepared for periods less than three (3) months.

As set out in the Inception Report, the Consultants would recommend that this requirement be phased-in in order to allow reporting issuers and their advisors to be in a position to comply, with a suggested implementation date of two years from the legislative enactment of amendments to the *SIA, 1995*. In this regard, we understand that the European Union proposes to introduce quarterly reporting in its members states from 2005 onwards at which point quarterly reporting would become best practice in all major developed securities markets.

d) Material Changes to a Reporting Issuer

Subsection 66(3) of the *SIA, 1995* presently imposes a disclosure obligation on reporting issuers in the case of a material change. The Consultants would recommend revising the subsection to make it clear that once a material change has occurred, the reporting issuer is required to issue a press release within one (1) day of the material change, and file a material change report with the TTSEC within seven (7) days of the material change. At present, the subsection could be interpreted to permit a reporting issuer to not file a press release until the 7th day, which the Consultants would suggest is not appropriate in terms of informing the marketplace of the change. A suggested revision to the subsection would read as follows:

> *Subject to subsection (4), where a material change occurs in the affairs of a reporting issuer, the reporting issuer shall forthwith, and in any event within one day of the change, issue a press release that is authorized by a senior officer and that discloses the nature and*

substance of the material change, and, within seven days of the change, file with the Commission a report disclosing the nature and substance of the material change, the contents of which shall be certified by a senior officer.

e) Filing of Continuous Disclosure Material

It is vital to the securities marketplace that material information respecting reporting issuers be made available and accessible to the public. Accordingly, it is recommended that the *SIA, 1995* be amended as follows to improve the access of the investing public to information concerning reporting issuers:

- the TTSEC should be statutorily required to make all continuous disclosure material filed with it available for public inspection during normal business hours, which would include all filed financial statements, filed Annual MD&A, filed material change reports, and securityholding disclosure reports (discussed below);
- the TTSEC may satisfy this obligation by posting all such documents to its website; and
- reporting issuers, and persons and companies making a filing with the TTSEC shall be required to file a paper copy with the TTSEC and an electronic copy in a standard format, such as Microsoft Word or Adobe Acrobat.

It is suggested that the incremental cost of complying with electronic filing will be greatly outweighed by the enhanced and more rapid disclosure it provides.

f) "Insider" Trading and "Insider" Reporting

Part IX of the *SIA, 1995* regulates certain transactions involving persons connected to an issuer. In particular, section 121 prohibits certain trades on undisclosed information, while section 122 permits an issuer to require its "members" to disclose to the issuer their beneficial ownership of shares in the issuer. These sections can be characterized as the "insider trading" and "insider reporting" provisions of the *SIA, 1995*. In the Consultants' view there are a number of deficiencies with these provisions. In particular, the provisions are very technical which makes it difficult for market participants to understand what activity is prohibited (and difficult to prosecute offences) and do not provide for adequate public reporting of trades by connected persons and companies. Accordingly, the Consultants recommend the following specific changes to the section in order to clarify its application and to provide for enhanced disclosure of the economic interest of persons connected to reporting issuers in securities of the reporting issuer.

Subsection 120(1) would read as follows:

(1) A reference in this Part to undisclosed price sensitive information means, in relation to securities of a reporting issuer, any undisclosed information which, if generally known, would significantly effect, or would reasonably be expected to significantly affect, the price or value of the securities of the reporting issuer.

Subsection 120(2) would be amended to provide the categories of persons and companies who would be deemed to be connected to a reporting issuer, and therefore, subject to the trading prohibitions and disclosure requirements further set out in the section. It is suggested that it be amended as follows:

> (2) *For purposes of this Part, a person is deemed to be connected to a reporting issuer if:*
>
> (a) *the person is a director or officer of the reporting issuer;*
>
> (b) *the person is a director or officer of:*
>
> (i) *an affiliate*[2] *of the reporting issuer; or*
>
> (ii) *any person who beneficially owns, directly or indirectly, or exercises control or direction over, voting securities of the reporting issuer, or a combination of both, carrying more than 10% of the votes attached to all voting securities of the reporting issuer outstanding;*
>
> (c) *the person beneficially owns, directly or indirectly, or exercises control or direction voting over, securities of the reporting issuer, or a combination of both, carrying more than 10% of the votes attached to all voting securities of the reporting issuer outstanding;*
>
> (d) *the person is contemplating or proposing, whether alone or with any other person, to make a take-over bid for any securities of the reporting issuer, or is contemplating or proposing, whether alone or with any other person, to become a party to any amalgamation, merger or similar business combination with the reporting issuer, or is contemplating or proposing any other material transaction with or including the reporting issuer; or*
>
> (e) *a person that learns, directly or indirectly, of undisclosed price sensitive information with respect to a reporting issuer from any person described in this subsection, including a person described in this clause, and knows, or ought reasonably to have known, that the other person is connected to the reporting issuer;*
>
> *provided that a person deemed to be connected to a reporting issuer by application of a clause of this subsection continues to be deemed to be connected to a reporting issuer:*
>
> (f) *in the case of clauses (a) to (c) of this subsection, until the day that is six months following the day that the person otherwise ceases to be deemed to be connected to a reporting issuer by application of such clauses of this subsection;*
>
> (g) *in the case of clause (d) of this subsection, until the day any transaction described in clause (d) is generally disclosed; and*
>
> (h) *in the case of clause (e) of this subsection, until such undisclosed price sensitive information is generally disclosed.*

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[2] "Affiliate" would be defined in the *SLA, 1995* in a manner similar to that found in section 5 of the *Companies Act* but would also include legal entities other than companies, such as trusts and partnerships.

By broadening the deeming provision of subsection 120(2), the prohibitions against buying and selling securities, currently found in subsections 121(1), 121(2), 121(4), and 121(5) may be combined into a single more easily understood prohibition:

> *No person that is connected to a reporting issuer shall be permitted to buy, sell, or otherwise trade in securities of such reporting issuer, whether in a transaction on a securities exchange or otherwise, with knowledge of undisclosed price sensitive information, however obtained, until such information has been generally disclosed.*

A separate provision would deem price sensitive information to be "generally disclosed" at the moment which is the earlier of (a) 11:59 p.m. on the business day immediately following the date of its public dissemination through a news release, or (b) 11:59 p.m on the second business day following the date of filing of a continuous disclosure document with the TTSEC containing such price sensitive information. As well, the *SIA, 1995* would also include an "ethical wall" defence in the case of companies that may be liable for insider trading. The defence would, in essence, limit the liability of companies whose directors, officers or employees engage in insider trading where the company has implemented and maintained reasonable policies and procedures to prevent contraventions of the insider trading prohibition.

These changes, it is suggested, clarify the prohibition on trading on undisclosed price sensitive information, and make it clear that trading is permitted once disclosure of the price sensitive information has been made.

The prohibition on informing others of undisclosed price sensitive information, currently located in subsections 121(7) and (8) of the *SIA, 1995*, would correspondingly be amended:

> *(7)* *Subject to section 124, no person connected to a reporting issuer shall counsel, procure or otherwise advise any person to buy, sell, or trade in any securities of a reporting issuer, whether in a transaction on a securities exchange or otherwise, during the time such person has knowledge of undisclosed price sensitive information.*
>
> *(8)* *Subject to section 124, a person connected to a reporting issuer shall not communicate or otherwise disclose any undisclosed price sensitive information to any person until such information is generally disclosed, unless in the necessary course of business.*

Such changes would clarify that undisclosed price sensitive information is not to be disclosed to anyone until generally disclosed, and would prohibit counseling for the purpose of trading in securities without actually telling the recipient the undisclosed price sensitive information. As well, the suggested changes eliminate the requirement on the person connected to the reporting issuer to make a determination whether the person would reasonably be expected to use the information for the purpose of a purchase or sale of a security.

Persons or companies deemed to be connected to a reporting issuer by application of clauses (a) to (c) of subsection 121 would be required to prepare and file a "securityholding disclosure report" with the TTSEC within five (5) business days of (a) first being deemed to be connected to a reporting issuer, and (b) each subsequent purchase or sale of a security of a reporting issuer. A form would be prescribed by by-law.

Section 122 would be retained in a manner to allow reporting issuers to require disclosure of the interest of holders of its securities.

g) Filing and Disclosure of Securityholding Disclosure Reports

Securityholding disclosure reports would be both paper-filed and electronically-filed with the TTSEC and made publicly available along with the continuous disclosure material filed by reporting issuers.

vi) Appropriate exemptions should be made available for issuers from approved foreign jurisdictions in raising capital or complying with disclosure requirements in Trinidad and Tobago.

In the Inception Report, the Consultants recommended that the *SIA, 1995* be amended to permit certain approved foreign reporting issuers to be exempted from complying with the prospectus requirements of the *SIA, 1995* in connection with certain offerings, and to exempt those issuers from certain continuous disclosure requirements under the *SIA, 1995* provided certain conditions were met. The following would be the more detailed requirements.

a) Prospectus Offerings in Trinidad and Tobago for Approved Foreign Issuers (Other than Offerings of Mutual Fund Securities)

The *SIA, 1995* would be amended to provide that an "approved foreign issuer" satisfies the requirements of the *SIA, 1995* to prepare, file and have receipted, a prospectus, in connection with a distribution of securities in Trinidad and Tobago, and such offering documents or prospectus shall be deemed to be a prospectus for purposes of the *SIA, 1995*, if the "approved foreign issuer":

- files with the TTSEC:
    - a certificate signed by a senior officer of the issuer certifying that it satisfies the eligibility criteria set by the TTSEC from time to time;
    - a copy of the receipt or other evidence that the offering document or prospectus to be used in connection with the distribution of securities in Trinidad and Tobago has become final for purposes of a distribution of securities in the approved foreign jurisdiction;
    - a copy of all documents incorporated or deemed incorporated by reference in the offering document or prospectus;

    - a copy of all reports or valuations filed in the approved foreign jurisdiction in connection with the distribution;
    - a form of submission to jurisdiction and appointment of agent for service of process of the issuer; and
    - a copy of the offering document or prospectus including a certificate of a senior officer of the issuer certifying that the prospectus or other offering document constitutes full, true and plain disclosure of all material facts relating to the securities being distributed;
- delivers to each purchaser in Trinidad and Tobago:
    - the offering document or prospectus; and
    - an addendum to the offering document or prospectus making the following statements:

> *This distribution in Trinidad and Tobago is being made by a foreign issuer pursuant to the disclosure requirements of a foreign securities regulatory authority. Purchasers should be aware that such requirements may differ materially from those of Trinidad and Tobago.*
>
> *The Trinidad and Tobago Securities and Exchange Commission has not in any way evaluated the merits of the securities offered hereunder and any representation to the contrary is an offence.*
>
> *Some or all of the directors and officers of this foreign issuer and experts named in this prospectus reside outside of Trinidad and Tobago, and most or all of the assets of this foreign issuer are located outside of Trinidad and Tobago. Although the foreign issuer has appointed an agent for service of process in Trinidad and Tobago, it may not be possible for investors to collect judgments obtained in the courts of Trinidad and Tobago predicated upon the civil liability provisions of the securities laws of Trinidad and Tobago against this foreign issuer, and its directors and officers named in this prospectus. Experts named in this prospectus have not submitted to the jurisdiction of Trinidad and Tobago and therefore it may not be possible to take legal proceedings against such experts in Trinidad and Tobago.*
>
> *This document together with all documents incorporated by reference herein if any, constitutes full, true and plain disclosure of all material facts relating to the securities to be distributed by this prospectus.*

This exemption would not be available if, following the distribution of securities in Trinidad and Tobago, the number of equity securities of the issuer held, beneficially and of record, directly or indirectly, by residents of Trinidad and Tobago would exceed 5% of the number of equity securities outstanding of the issuer. As well, the exemption would only be available if all documents filed with the TTSEC or delivered to investors in Trinidad and Tobago, were in the English language.

Upon the filing of all of the above documentation with the TTSEC, the TTSEC shall issue a receipt for the prospectus filed by the approved foreign issuer. Distributions of this nature shall otherwise be required to comply with the *SIA, 1995*, including in the use of a market actor registered under the *SIA, 1995* to place the securities. Upon completion of the distribution, the issuer would become a reporting issuer in Trinidad and Tobago, but in

many cases would be exempt from the continuous disclosure requirements as further set out below. The TTSEC would have the discretion not to issue a receipt if it determines that it is in the public interest to not issue a receipt.

In order to have the benefit of this offering system, the issuer would have to be an "approved foreign issuer". An "approved foreign issuer" would be defined as follows.

> *"approved foreign issuer" means a foreign issuer,*
>
> *(a) that is a reporting issuer (or equivalent) under the securities laws of a designated foreign jurisdiction;*
>
> *(b) that files disclosure documents with a securities commission, stock exchange or other regulatory authority in a designated foreign jurisdiction that are made publicly available; and*
>
> *(b) that has a class of securities listed for trading on a recognized stock exchange in a designated foreign jurisdiction;*
>
> *unless the majority of its directors and officers are residents of Trinidad and Tobago, more than 50% of its assets are located in Trinidad and Tobago, or its business is principally administered in Trinidad and Tobago.*

A "foreign issuer" would be defined as an "issuer", other than a mutual fund or unit trust (which would have their own regime), that is incorporated or organized under the laws of a jurisdiction other than Trinidad and Tobago.

"Designated foreign jurisdictions" would be defined to include those jurisdictions acceptable to the TTSEC where the securities laws and regulatory oversight are of a standard at least equal to that in Trinidad and Tobago, and could include, initially, the United States, Canada, Australia, Hong Kong, Singapore and the United Kingdom.

b) Continuous Disclosure Exemptions for Approved Foreign Issuers that are Reporting Issuers in Trinidad and Tobago

"Approved foreign issuers" would be "reporting issuers" (as redefined) under the *SIA, 1995,* and would otherwise be subject to the continuous disclosure requirements of the *SIA, 1995.* "Approved foreign issuers" would be deemed to satisfy the requirements for the preparation, filing and delivery of continuous disclosure documents required under the *SIA, 1995* if the approved foreign issuer:

- complies with the disclosure requirement to which it is subject in the designated foreign jurisdiction with respect to:
  - disclosure of material changes on a timely basis;
  - preparation of annual audited financial statements;
  - preparation of quarterly unaudited financial statements; and

- preparation of a management discussion and analysis of financial condition on the issuer's annual audited financial statements;

provided in each case that:

- at the time the approved foreign issuer files such documents with the securities regulatory authority in the designated foreign jurisdiction, it files such material with the TTSEC; and
- sends to each securityholder resident in Trinidad and Tobago the documents that such securityholder would be entitled to receive under the securities laws of the designated foreign jurisdiction if such securityholder were resident in that designated foreign jurisdiction.

As well, where the securities laws of a designated foreign jurisdiction require the approved foreign issuer to send any material or information to a securityholder in the designated foreign jurisdiction, and there is no equivalent requirement under the *SIA, 1995*, the approved foreign issuer shall be required to send such information to securityholders resident in Trinidad and Tobago as if such securityholders were resident in the designated foreign jurisdiction but the reporting issuer would not be required to file that information or documents with the TTSEC. For example, this would include an annual information form in Canada or a Form 10-K in the United States.

These disclosure exemptions would not be available if, at the time of filing, and to the reasonable knowledge of the reporting issuer, the number of its equity securities held by residents of Trinidad and Tobago exceeded 5% of its outstanding equity securities. Approved foreign issuers could be required to certify annually with the filing of their annual financial statements that they comply with the requirements of the exemption.

vii) The Companies Act should be amended so as to repeal duplicative regulation of public companies.

The Consultants would draft technical amendments to the *Companies Act* in order to end duplicative regulation consistent with the overall recommendation to base securities regulation in Trinidad and Tobago on the jurisdiction of the investor and not that of the issuer. As well, consequential amendments would have to be made to the *Companies Act* to harmonize with the changes in the *SIA, 1995*. In particular, the definition of public company would be deleted and replaced in the *Companies Act* with a definition of "reporting issuer" meaning a "reporting issuer within the meaning of the *Securities Industry Act, 1995*, as amended" to provide consistency with the changes discussed in the following section.

In addition, changes would likely be made to a number of provisions of the *Companies Act*, including to Part III divisions 5, 6 and 7 in respect of proxies and shareholder meetings, and financial disclosure, and Part IV division 4 in respect of insider trading.

Generally, the Consultants would recommend that such provisions not apply to reporting issuers who will have revised obligations as reporting issuers under the *SIA, 1995*. For example, a new provision in the *Companies Act* would simply state that certain sections of the *Companies Act* regarding financial disclosure do not apply to reporting issuers (but would continue to apply to other companies governed by the *Companies Act*). These sections would include section 151 dealing with annual financial statements and section 154 regarding director approval of financial statements. The current requirement under the *Companies Act* for a public company to have an audit committee composed of at least three non-affiliated directors should be repealed and legislated directly into the *SIA, 1995*. In the case of the insider trading rules of the *Companies Act*, again, it would be appropriate to legislate that such provisions do not apply to reporting issuers given that such conduct will be covered in a revised *SIA, 1995*. Finally, sections 182 to 185 of the *Companies Act* which deal with the register of substantial shareholders (and which presently only applies to public companies) should also be imported into the *SIA, 1995* as part of the new securityholding disclosure reporting requirement.

All of these changes are intended to ensure that (a) there is a level playing field in that all reporting issuers (whether organized or governed under the *Companies Act* or some other law, foreign or domestic) are held to the same standards in these areas, which will be the higher standards found in an amended *SIA, 1995*, and (b) unnecessarily duplicative regulation is eliminated in the interest of utilizing local resources more efficiently and reducing the compliance burden on reporting issuers.

viii) A number of technical amendments should be made to the SIA, 1995.

In the Inception Report, the Consultants recommended a number of technical amendments including to the definition of "security", the concepts of "offer to the public" and "distribution", registration statement filing, private placement exemptions, and prospectus offerings. To give effect to these suggested changes the definitions of "public company" would be repealed and the definition of "reporting issuer" amended. As well, the Consultants would suggest a new section requiring public disclosure of any documents or material "filed" with the TTSEC. Details of these technical changes are set out below.

a) "Security"

The definition of "security" is vital to an amended *SIA,* 1995 as it defines the scope of the jurisdiction of the TTSEC. The Consultants agree with several commentators that no single definition of "security" would capture all situations which should fall under the *SIA, 1995* and the jurisdiction of the TTSEC. Accordingly, there will always be a requirement for interpretation of any definition of "security" within the scope and purpose of the *SIA, 1995*, existing case law (both local and foreign), and the rules of statutory interpretation. Given this, the following is suggested as the amended definition of "security" in the *SIA, 1995:*

"security" means any document, instrument or writing evidencing ownership of, or any interest in, the capital, debt, property, profits, earnings or royalties of any person, company or enterprise, and without limiting the generality of the foregoing, includes any:

(a) any bond, debenture, note or other evidence of indebtedness;

(b) any share, stock, unit, unit certificate, participation certificate, certificate of share or interest;

(c) any document, instrument or writing commonly known as a security;

(d) any document, instrument or writing evidencing an option, subscription or other interest in or to a security;

(e) any investment contract;

(f) any security that is primarily serviced by the cash flows of a discrete pool of receivables or other financial assets, either fixed or revolving, that by their terms convert into cash within a finite time period, and any rights or other assets designed to assure the servicing or timely distribution of proceeds to security holders (an "asset-backed security");

(g) any document, instrument or writing constituting evidence of any interest or participation in –

> *(i) a profit sharing arrangement or agreement;*
>
> *(ii) a trust;*
>
> *(iii) an oil, natural gas or mining lease, claim or royalty or other mineral right; or*

(h) any right to acquire or dispose of anything specified in paragraphs (a) to (g),

but does not include –

(i) currency;

(j) a cheque, bill or exchange, or bank letter of credit;

(k) a certificate or document constituting evidence of any interest in a deposit account with –

> *(i) a financial institution;*
>
> *(ii) a credit union within the meaning of the Co-operative Societies Act;*
>
> *(iii) an insurance company; or*
>
> *(iv) a contract of insurance issued by an issuer.*

The key addition to the definition of "security" is "investment contract". "Investment contract" is intended to be broad and is based on the definition of "investment contract" found in American and Canadian securities laws, and which has been the subject of a

significant level of judicial interpretation in both countries.[3] A suggested definition which accords with judicial interpretation in the case law may be as follows:

> *"investment contract" includes any contract, transaction, plan or scheme, whether or not evidenced by any document, instrument or writing, whereby a person invests money or other property in a common enterprise with the expectation of profit or gain based on the expertise, management or effort of others, and such money or other property is subject to the risks of the common enterprise.*

Such a definition, it is suggested, will provide some guidance to the marketplace on the meaning of the term.

While it is arguable that investment contracts already are caught within the definition of "security", its explicit addition, it is suggested, will clarify that these types of investments are caught within the definition of "security" and therefore fall into the *SIA, 1995.* As with all securities, however, appropriate exemptions from the prospectus requirement will be available in the *SIA, 1995* for distributions of securities including those which are "investment contracts."

b) "Offer to the Public" and "Distribution"

At present, an "offer to the public" attracts the obligation to file a registration statement with the TTSEC, while a "distribution" attracts the requirement to prepare and file a prospectus with the TTSEC. The Consultants recommend that the definition of "offer to the public" be repealed and the definition of "distribution" be amended. The result would be a single defined term capturing those situations when an issuer would be required to prepare and have receipted, a prospectus. This, it is suggested, would lead to greater certainty in the application of the *SIA, 1995.* A "distribution" would be defined as:

> *"distribution" where used in relation to a trade or trading in securities, means,*
>
> *(a) a trade in securities of an issuer that have not previously been issued, and includes, any trade in previously issued securities of the issuer that have been redeemed, repurchased or otherwise reacquired by the issuer;*
>
> *(b) a trade by an underwriter, acting as underwriter, in previously issued securities which were purchased from the issuer by such underwriter less than 4 months prior to the trade;*
>
> *(c) a trade in previously issued securities of an issuer from the aggregate holdings of any person, or combination of persons or companies, where the number of securities of that class held by the person, or combination of persons or companies:*
>
> > *(i) enables or permits the person, or combination of persons or companies, to exercise control over the board of directors, management or policies of the issuer; or*
> >
> > *(ii) is equal to or exceeds 25% of the outstanding voting securities of the issuer; or*

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[3] See for example, the seminal American cases in the area: *SEC v. C.M. Joiner Leasing Corp., 320 U.S. 344 (1943), SEC v. W.J. Howey Co., 328 U.S. 293 (1946), United Housing Foundation v. Forman, 421 U.S. 837 (1975),* all decisions of the Supreme Court of the United States; and in Canada: *Pacific Coast Coin Exchange of Canada Ltd. v. OSC, [1977] 2 S.L.R. 112.*

(d) any trade in securities deemed by this Act or the by-laws to be a distribution;

whether or not in the course of any transaction or series of transactions.

The revised definition would catch most initial trades in securities of all types of issuers, both private and public. Once caught, such trades would become subject to the prospectus requirement. However, as discussed elsewhere in this Addendum, numerous exemptions from the prospectus requirement would be made available for certain distributions, in which case, subsequent trades would be deemed to be a further distribution unless the purchaser has held such securities for at least four (4) months and the issuer of the securities is a reporting issuer. The main benefit of this definition is that it does not require an assessment of whether the trade is being made to a member of the "public" and therefore, increases the level of certainty surrounding which trades attract the prospectus requirement of the *SIA, 1995.*

A number of distributions would be exempted from the prospectus requirement. These are described in the next section.

c) Private Placement Exemptions

The Consultants recommend that the definition of "sophisticated purchaser" contained in subsection 67(2) of the *SIA, 1995* be broadened to include persons who by their very nature are sophisticated and as such do not need a prospectus to make their investment decision. Those persons could include the following:

- institutional investors such as banks, loan or trust corporations, insurance companies, market actors, persons (other than individuals) with significant net assets or a mutual fund that distributes its securities under a prospectus or to sophisticated purchasers;
- government entities such as the government of Trinidad and Tobago or any agency thereof or any national, federal, state, provincial or municipal government of any foreign jurisdiction or any agency thereof; and
- any person outside Trinidad and Tobago that is analogous to any person referred to above.

The Consultants also recommend that subsection 75(2) of the *SIA, 1995* be amended so that a distribution can be made to any number of sophisticated purchasers provided, however, that the issuer is a reporting issuer and further provided that there is no advertisement and no selling expenses are paid in connection the trades. Where the issuer is not a reporting issuer, it would only be permitted to conduct a distribution to sophisticated purchasers if, following the distribution, the number of individual shareholders in the issuer is not greater than 50 and again provided that there is no advertisement and no selling expenses are paid in connection the trades.

The Consultants recommend amending section 75 of the *SIA, 1995* to clarify that an issuer will not become a "reporting issuer" within the meaning of the *SIA, 1995* solely as a

result of distributing securities to sophisticated purchasers as contemplated in subsection 75(2) of the *SIA, 1995* or distributing securities under a limited offering as contemplated in subsection 75(3) of the *SIA, 1995*.

The Consultants also recommend amending section 75 of the *SIA, 1995* to clarify that a sophisticated purchaser that acquires securities of a reporting issuer pursuant to subsection 75(2) of the *SIA, 1995* will not be permitted to trade such securities for a minimum of four (4) months unless such subsequent trade occurs under a prospectus or is otherwise exempt from the prospectus requirements.

In addition, the Consultants recommend a parallel exemption from the requirements of Part IV of the *SIA, 1995* to be registered in a category of market actor where trades are conducted only with sophisticated purchasers that are not individuals.

d) "Public Company" and "Reporting Issuer"

At present, the *SIA, 1995* contemplates both "public companies" and "reporting issuers". As set out in the Inception Report, the Consultants recommend that the "public company" definition be repealed and replaced with a single definition for "reporting issuer", which could be defined as follows:

"reporting issuer" means an issuer:

(a) that was a reporting issuer on ●, 2003;

(b) that has filed a prospectus and obtained a receipt for it under the Act;

(c) any of whose securities are listed on the Stock Exchange; or

(d) that is the issuer whose existence continues following the exchange of securities of an issuer by or for the account of such issuer with another issuer or the holders of securities of that issuer in connection with a statutory amalgamation or arrangement or where existing issuers merge into one issuer, that continuing issuer, where one of the amalgamating or merged companies or the continuing company has been a reporting issuer for at least four months.

It is important to make a few observations on the proposed revised definition. First, it does not include issuers that are not reporting issuers which rely on the private placement exemptions to distribute securities in Trinidad and Tobago (i.e. private companies will not become reporting issuers where they continue to rely on private placement exemptions). Second, it includes approved foreign issuers in that they would receive a receipt from the TTSEC for a foreign prospectus used to distribute securities in the country. Finally, it provides that certain issuers will be deemed to be a reporting issuer on a certain day. This provision is intended to grandfather existing reporting issuers under the *SIA, 1995*.

e) Prospectus Disclosure By-Law

Part VI – "Distributions" - of the *SIA, 1995*, would be amended to reflect changes to the prospectus offering process. The basic requirement would be set out in a revised section 70.

> *70* *(1) No person shall trade in a security on its own behalf or on behalf of any other person where the trade would be a distribution unless a prospectus has been filed and a receipt obtained therefore from the Commission.*
>
> *(2) A prospectus shall contain full, true and plain disclose of all material information concerning the issuer and the securities to be issued, and shall comply with the requirements prescribed by by-law.*

Accordingly, rather than the generic requirements currently set out in subsections 72(2) and 72(3), the new prospectus disclosure and filing by-law would require disclosure similar to that found in the existing prospectus disclosure guidelines, but would also require:

- specific disclosure with respect to asset-backed securities (discussed below);
- a statement of the investor's rights in the case of an untrue statement or non-disclosure under current Part X of the *SIA, 1995*;
- full and complete descriptions of the securities being offered, and in the case of debt securities, disclosure of the rating (if any) or if unrated, the fact that the debt securities are unrated, and all material attributes and characteristics of the indebtedness including items such as sinking fund obligations, security for the indebtedness, and material covenants of the issuer resulting from the debt issuance (such as financial ratio tests);
- the most recent Annual MD&A for the issuer; and
- names of the underwriters (or agents) if any, a description of the underwriting agreement between the underwriter (or agents) and the issuer, and the relationship between the issuer and the underwriter (or agents) including areas of potential conflict of interest, and where there is no underwriter (or agent), a statement to that effect.

The process of receipting a prospectus would also be fully set out in a new prospectus disclosure and filing by-law. It would require, at a minimum, that an issuer wishing to obtain a receipt for a prospectus file the following documents with the TTSEC:

- documents creating the security being offered (such as a trust indenture);
- agreements between underwriters (or agents) and the issuer in respect of the distribution; and
- consents of any auditor, attorney or other expert who is named in the prospectus or who has prepared any part of the prospectus.

To be clear, however, the prospectus receipt process is not intended to be, nor should it be construed as, the TTSEC approving a distribution of securities or passing upon their investment merits. The TTSEC's role is not to conduct due diligence on an issuer to determine if the prospectus contains full, true and plain disclosure of all material information. Rather, that is the obligation of the issuer and its professional advisors, the incentive for full, true and plain disclosure being the civil liability provisions of the *SIA, 1995* for untrue statements or willful non-disclosure in the document. Instead, the TTSEC's role is to compare the disclosure in the prospectus against the disclosure by-law, to question the issuer and its advisors regarding inconsistencies in the prospectus, to review the prospectus for any matters which may generally not be in the public interest, and to note any other matters which come to its attention which may violate the securities laws of Trinidad and Tobago.

As well, the TTSEC may not issue a receipt for the prospectus if any of the conditions set out in subsection 76(2) of the *SIA, 1995* are present.

ix) Registration requirements for market actors, investment advisors, brokers, dealers, traders, underwriters and securities companies.

The amendments suggested in the Inception Report under this recommendation are self-explanatory and would not require any further elaboration until the Interim Report and Final Report stage.

x) "Suitcase Brokers"

The recommendation to create a new category of "market actor" in the *SIA, 1995* known as the "temporary broker/investment advisor" was positively received by the marketplace. The following would be the suggested criteria which would have to be met in order to obtain the registration:

- the applicant would have to be an individual of at least 21 years of age who is not a resident or citizen of Trinidad and Tobago;
- the applicant must not be registered under the *SIA, 1995* in any category of market actor;
- the applicant would have to be registered in the category of "investment advisor" and/or "broker" (or equivalent) under the securities legislation of an approved foreign jurisdiction, and such registration(s) would have to be in good standing;
- the applicant must be an employee, officer, director or partner of a registered broker, dealer, or investment advisor (or equivalent) in the approved foreign jurisdiction; and
- the applicant would have to file a letter from a company registered in the category of "securities company" under the *SIA, 1995*, stating that the "securities company" agrees to sponsor the applicant.

The sponsoring "securities company" would be liable for the actions of the temporary registrant as if such person were a broker or investment advisor ordinarily employed by the securities company.

Under the simplified registration process, the applicant would file the following documents with the TTSEC:

- an application form certifying that the applicant meets the criteria for the category of "temporary broker/investment advisor" which would:
  - a) name the broker, dealer, or investment advisor (or equivalent) in the approved foreign jurisdiction;
  - b) name the sponsoring firm;
  - c) disclose the dates that the individual will be engaging in advising or brokering activities in Trinidad and Tobago;
- the letter from the sponsoring "securities company" registered under the *SIA, 1995*;
- a copy of evidence of registration in the approved foreign jurisdiction; and
- a filing fee determined by the TTSEC.

Part IV of the *SIA, 1995*, would also be amended to require the TTSEC to grant the registration or deny the registration within 14 calendar days of the application. The TTSEC will be given the power to deny the application on the same basis that it would be permitted to deny an application for registration in any other category.

Once granted, the applicant would be permitted to conduct business, and hold himself or herself out, as an investment advisor or broker, and could otherwise engage in the same activities provided that the registrant is limited to engaging in advising or brokering activities in Trinidad and Tobago for no more than 30 days in one calendar year (which days will be disclosed on the application form). A new deeming provision in Part IV will deem a person or company to be engaging in advising or brokering activities in Trinidad and Tobago if:

- such person or company contacts or solicits by telephone or facsimile (whether unsolicited or not) a resident of Trinidad and Tobago for the purpose of providing investment advice or brokerage services;
- such person or company sends correspondence or solicits by e-mail, for the purpose of providing investment advice or brokerage services, to an e-mail address where the sender has knowledge that the owner of such address is a resident of Trinidad and Tobago, or after reasonable inquiry, should have known, that the owner of such e-mail address is a resident of Trinidad and Tobago; or

- such person or company sends correspondence or solicits by mail or courier for the purpose of providing investment advice or brokerage services to an address in Trinidad and Tobago.

In all cases, the temporary broker/investment advisor would be required to sell investment products (i) under a prospectus for which a receipt has been obtained from the TTSEC, or (ii) which are exempt from the requirement to obtain a receipt from the TTSEC (including because such investment products have been reviewed in an approved foreign jurisdiction).

As well, there is also the broader exemption from the requirement to be registered as a market actor where the person is selling only to sophisticated purchasers that are not individuals.

This suggested category of registration, however, must be supported by detection and enforcement of violators. At present, persons who are "suitcase brokers" are not registering as "investment advisors" or "brokers" in existing categories. In order to legitimize their ongoing activities, such individuals would have to be registered in the new "temporary broker/investment advisor" category. A system for detection (whether with the assistance of other branches of the government of Trinidad and Tobago or not) and prosecution of such individuals by the TTSEC, will ultimately be required to ensure compliance with the proposed changes.

xi) The regulation of securitization transactions should be left as a matter of disclosure and not regulation of form or structure.

The Consultants recommendation in the Inception Report was to specifically define asset-backed securities as "securities" under the *SIA, 1995*, to require disclosure specific to asset-backed securities in a prospectus (and the filing of constituent documents), and to require that a "risk disclosure statement" be delivered to prospective investors prior to the sale of asset-backed securities under a prospectus exemption. These changes have been included and discussed elsewhere in this Addendum.

An attempt to substantively regulate securitization transactions, as has been suggested by some commentators, would require an analysis and assessment of the substantive laws of Trinidad and Tobago which would go far beyond an analysis of securities laws. Securitization legislation implemented in many jurisdictions deal with many areas of substantive law, including, by way of example, financial institution regulation and capital adequacy requirements, personal property security law, business corporations and company law, and bankruptcy law, and it is generally intended, at least in part, to facilitate the execution of securitization transactions by addressing deficiencies or gaps in existing substantive laws.

Securities laws most appropriately address the disclosure required in respect of a public offering of asset-backed securities. Accordingly, the Consultants have recommended that disclosure in a prospectus of prescribed features or aspects of a securitization, including information pertaining to the nature, performance and servicing of the underlying pool of financial assets, the material attributes and characteristics of the asset-backed securities, the existence of any third party or internal support or credit enhancement arrangements established to protect holders of the asset-backed securities from losses associated with the performance of the financial assets, and information in respect of persons or companies who sell the assets or provide services or other support in respect of the securitization transaction. This would be reflected in the revised prospectus disclosure by-law.

In addition to the protections afforded by full disclosure of all material facts related to an offering of asset-backed securities, the Consultants would also recommend that, in order for asset-backed securities to be eligible for sale to the public, the securities would have to be rated by a qualified rating agency. Consequently, asset-backed securities that are sold without a prospectus or without a rating by a qualified rating agency would only be offered privately to sophisticated investors and provided that the "risk disclosure statement" is also given to such investors.

In the Consultants' view, the substantive regulation of securitization transactions, if undertaken in Trinidad and Tobago, should be dealt with in legislation other than the *SIA, 1995*, as other countries have done in the passing of omnibus "securitization" legislation which affects all aspects of such transactions, including disclosure afforded by securities laws. Such a legislative initiative is, however, beyond the scope of this mandate.

xii) Settlement and clearing issues.

At present, the Consultants are not currently in a position to provide a recommendation in this area. Mr. Gary Stephenson is presently conducting the review of this portion of the mandate and will be in a position to provide a recommendation in the Interim Report.

xiii) Compensation or Contingency Fund

The Consultants are not currently in a position to provide a recommendation in this area.

3) CONCLUSION

The more detailed recommendations in this Addendum are designed to assist the TTSEC and market participants in evaluating the recommendations set out in the Inception Report. These recommendations, while more detailed, do not constitute all of the changes or amendments which would be required to be made to the *SIA, 1995* to give effect to the recommendations in the Inception Report.

Following meetings in Port of Spain in February, 2003 to discuss these more detailed recommendations and the Inception Report generally with the TTSEC, its staff, and market participants, the Consultants would proceed to prepare the Interim Report, which would be expected to outline proposed amendments and additions to the *SIA, 1995* part by part in order to give effect to the recommendations.