



**STATEMENT OF SUBSTANCE & PURPOSE ON THE
TRINIDAD AND TOBAGO SECURITIES AND EXCHANGE COMMISSION’S
DRAFT RISK-BASED CAPITAL AND LIQUIDITY REQUIREMENTS BYE-
LAWS 2023**

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SECTION I. BACKGROUND

Bye-law 27 of the Securities (General) Bye-laws, 2015 (“the General Bye-laws”) specifies the capital requirements for registrants registered under section 51(1) of the Securities Act, Chapter 83:02 of the laws of the Republic of Trinidad and Tobago (“the Act”). These capital requirements, however, do not consider the risks inherent in the business activities of these registrants (i.e. broker-dealers, investment advisers and underwriters). Moreover, no capital requirements are specified for self-regulatory organisations (“SROs”) registered under part III of the Act.

The Trinidad and Tobago Securities and Exchange Commission (“the Commission”) for some years now has been assessing the current capital requirements. During the period June 7 to July 21, 2021, the Caribbean Regional Technical Assistance Centre (“CARTAC”) conducted a technical assistance mission to assist the Commission with the development of risk-based prudential requirements that are consistent with international best practice for entities registered or that are required to be registered under the Act. The implementation of risk-based prudential requirements is consistent with Principle 30 of the International Organization of Securities Commissions (“IOSCO”) Objectives and Principles of Securities Regulation:

Principle 30: There should be initial and ongoing capital and other prudential requirements for market intermediaries that reflect the risks that the intermediaries undertake.

The Commission's proposed risk-based prudential requirements were developed in accordance with the following standards, albeit tailored specifically for the local securities market:

- Basel Committee on Banking Supervision's Capital Accord, the same standard adopted by the Central Bank of Trinidad and Tobago ("the Central Bank");
- European Union's Prudential Requirements of Investment Firms; and
- Bank for International Settlements and IOSCO Principles for Financial Market Infrastructure.

The Commission consulted with key stakeholders; including the Central Bank, Trinidad and Tobago Stock Exchange, Trinidad and Tobago Central Depository, Securities Dealers Association of Trinidad and Tobago and the Mutual Fund Association of Trinidad and Tobago, on the proposed risk-based prudential requirements. A quantitative impact study as well as a pilot test with a representative sample of the securities sector were conducted. The Commission has taken onboard most of the recommendations made by market participants and has drafted the Risk-Based Capital and Liquidity Requirements Bye-laws, 2023 ("these Bye-laws").

The purpose of these Bye-laws is to assist the Commission in the discharge of its functions under section 6 of the Act by:

- a. ensuring that entities registered under the Act maintain adequate levels of capital and liquid assets to assist in absorbing some of the costs related to potential losses and risks associated with their business activities; and
- b. mitigating the impact of the failure of any one firm on clients, other market participants, the securities industry, and the financial system.

Legislative Requirements

Section 148 of the Act provides that the Minister of Finance may, on the recommendation of the Commission, make Bye-laws as set out in the provision. Section 149 requires that the Commission engage in public consultation prior to effecting a Bye-law.

SECTION II. KEY POLICIES CONTAINED IN THE PROPOSED RISK-BASED CAPITAL AND LIQUIDITY REQUIREMENTS BYE-LAWS, 2023

1. Liquidity Requirements

- a. A definition of liquid assets has been included to incorporate assets, other than cash and cash equivalents, that can be easily and immediately converted to cash at little to no loss of value.
- b. Operational expenses are defined as that reported in an entity's last audited financial statements excluding exceptional and extraordinary costs, tax costs and non-cash expenses such as depreciation and amortisation.
- c. A registrant registered under section 51(1) of the Act must have, at all times, liquid assets equivalent to six months operational expenses.
- d. A registrant registered under section 51(1) of the Act that engages in the sale of repurchase agreements ("Repos") must have additional liquid assets equivalent to fifteen per cent of its current Repo liabilities that mature within three months.
- e. An SRO must have, at all times, liquid assets equivalent to twelve months' operational expenses.

2. Capital Requirements

- a. Qualifying capital is defined as the sum of Tier 1 and Tier 2 capital, subject to the prescribed deductions from Common Equity Tier 1 capital.
- b. A registrant registered under section 51(1) of the Act must maintain qualifying capital that is the higher of
 - i. the initial and minimum capital requirement for its registered business activity; or
 - ii. the risk-based capital requirement.
- c. An SRO must maintain qualifying capital equivalent to twelve months' operational expenses.
- d. The minimum capital requirements for broker-dealers, investment advisers and underwriters are specified.
- e. The risk-based capital requirement is defined as the sum of the
 - i. market risk requirement;
 - ii. operational risk requirement;
 - iii. credit risk requirement, including a capital charge for Fixed Net Asset Value Collective Investment Schemes ("Fixed NAV CISs"); and
 - iv. underwriting risk requirement.

- f. In the case of a registrant registered under section 51(1) of the Act as a broker-dealer that sells Repos, the underlying assets of all Repos must be included in the market risk requirement.
- g. The capital in respect of each Fixed NAV CIS shall be held separately by a registrant registered under section 51(1) of the Act, and all capital so held shall be applied solely for the purposes of the Fixed NAV CIS in respect of which it is held.

3. Obligations of Registrants and Self-Regulatory Organisations

- a. It is the responsibility of the board of directors or chief executive officer to ensure that the entity establishes and maintains qualifying capital and liquid assets that complies with the Bye-laws.
- b. The reporting requirements for an entity registered under the Act have been specified.
- c. An SRO or a registrant registered under section 51(1) of the Act is required to develop and document its risk management framework.
- d. A registrant registered under section 51(1) of the Act is required to conduct, on an annual basis, stress testing to assess whether its capital and liquid assets are adequate given the risks inherent in its business activities.

4. Exemptions

- a. A registrant registered under section 51(1) of the Act which is subjected to Section 9(4) of the Financial Institutions Act Chapter 79:09 can apply to the Commission to be exempted from the provisions of these Bye-laws.

5. Imposition of penalty and other supervisory actions

6. Transitional Provisions

- a. A transition period of one year has been provided for an SRO or registrant registered under section 51(1) of the Act that does not satisfy the capital and liquidity requirements at the date of the coming into force of these Bye-laws.
- b. The capital requirement for Fixed NAV CISs will be introduced over a three-year horizon.

SECTION III. OVERVIEW OF THE PROPOSED RISK-BASED CAPITAL AND LIQUIDITY REQUIREMENTS BYE-LAWS, 2023

PART I of these Bye-laws, comprising Clauses 1 to 6, outlines its purpose, application as well as the connection with the Act and the Securities (General) Bye-laws, 2015 (the “General Bye-laws”). This Part also provides definitions for key terms that have not been previously defined in the securities legislation that are pertinent to these Bye-laws including definitions of “capital charge”, “credit risk”, “Fixed NAV CIS”, “Fixed NAV CIS guarantee”, “market risk”, “operational expenses”, “operational risk”, “qualifying capital” and “risk-based capital”.

PART II of these Bye-laws covers the liquidity requirements for an SRO and a registrant registered under section 51(1) of the Act as well as the definition of liquid assets. This part comprises of Clauses 7 and 8.

PART III of these Bye-laws defines qualifying capital and comprises Clauses 9 to 14.

PART IV of these Bye-laws outlines the capital requirements and comprises Clauses 15 to 31.

- Clause 15 specifies the capital requirements for an SRO and a registrant registered under section 51(1) of the Act.
- Clause 16 covers the minimum capital requirement based on the business activity of a registrant registered under section 51(1) of the Act.
- Clause 17 introduces the risk-based capital requirement.
- Clauses 18 to 31 outline the various components of the risk-based capital requirement as well as additional capital requirements for broker-dealers that sell Repos and Fixed NAV CISs.

PART V of these Bye-laws, comprising clauses 32 to 37, details the obligations of SROs and registrants registered under section 51(1) of the Act.

- Clause 32 covers the responsibility of the board of directors or chief executive officer or any other individual who performs functions similar to those normally performed by an individual occupying any such office.
- Clauses 33 and 34 covers the reporting requirements of an SRO and a registrant registered under section 51(1) of the Act.
- Clause 35 allows the Commission to request documents and information from an SRO or a registrant registered under section 51(1) of the Act for the purpose of ensuring conformity and compliance with these Bye-laws.
- Clauses 36 covers risk management and outlines what should be incorporated in the risk management framework of an SRO or registrant registered under section 51(1) of the Act.
- Clause 37 covers stress testing.

PART VI, which comprises clause 38, provides for an exemption from the provisions of these Bye-laws for a registrant registered under section 51(1) of the Act that is also subjected to Section 9(4) of the Financial Institutions Act Chapter 79:09.

PART VII of these Bye-laws sets out miscellaneous provisions and comprises Clauses 39 to 42.

- Clause 39 covers the imposition of penalties by the Commission for contravention of these Bye-laws.
- Clause 40 outlines other actions the Commission may take when performing its supervisory function under these Bye-laws.
- Clause 41 sets out the transitional provisions for an SRO and a registrant registered under section 51(1) of the Act, including those that manage Fixed NAV CISs.

SECTION IV. REFERENCES

1. Securities Act, Chapter 83:02 of the Laws of the Republic of Trinidad and Tobago;
2. Securities (General) Bye-Laws, 2015;
3. Financial Institutions (Capital Adequacy) Regulations, 2020;
4. Regulation (EU) 2019/2033 of the European Parliament and of the Council of 27 November 2019 on the prudential requirements of investment firms and amending Regulations (EU) No 1093/2010, (EU) No 575/2013, (EU) No 600/2014 and (EU) No 806/2014;
5. Bank for International Settlements and International Organization of Securities Commissions Principles for Financial Market Infrastructure, April 2012; and
6. International Organization of Securities Commissions Objectives and Principles of Securities Regulation, May 2017.