

PROJECT PROFILE (PP)

TRINIDAD AND TOBAGO

I. BASIC DATA

Project Name:	Strengthening of the Financial Sector Supervisory and Regulatory Framework
Project Number:	TT-L1024
Project Team:	Juan Antonio Ketterer (ICF/CMF), Team Leader; Claudia Stevenson (ICF/CMF), Alternate Team Leader; Mie Iwasa (ICF/CMF); Emmanuel Abuelafia (CCB/CCB); Vashtie K. Dookiesingh (MIF/CTT); Kevin McTigue (LEG/SGO); Gloria Lugo (ICF/CMF); and Marina Massini (ICF/CMF).
Borrower:	Government of the Republic of Trinidad and Tobago (GORTT)
Executing Agency:	Ministry of Finance of Trinidad and Tobago (MoF)
Financing Plan:	IDB (Ordinary Capital): US\$30,000,000 Total: US\$30,000,000
Safeguards:	Policies Triggered: B.13 Classification: N/A

II. GENERAL JUSTIFICATION AND OBJECTIVES

- 2.1 Considered the regional financial center for the Caribbean, Trinidad and Tobago (TT) has a relatively well-developed financial sector which has been a catalyst for the country's economic growth¹. However, the global financial crisis has exposed TT's vulnerabilities to systemic risk and highlighted the need for stronger financial regulation. Moreover, the recent crisis and the failure of CL Financial (CLF), headquartered in TT with significant regional and international reach, have illuminated the Government's limited institutional capabilities to identify threats to financial stability and to propose adequate prudential measures in the sector². In this context, financial sector reform is a priority of the GORTT (MoF's 2011 budget³ and request to the IDB for assistance).
- 2.2 The January 2009 collapse of CLF and related companies has represented a major financial shock to the Caribbean. The collapse has had spillover effects in all 15 CARICOM states except for Jamaica and Haiti, with exposures as high as 17% of GDP in the Eastern Caribbean countries. In January 2009, the Central Bank of TT (CBTT) intervened in the CLICO Investment Bank (CIB) and two insurance companies, the Colonial Life Insurance Company (CLICO) and the British American Insurance Company (Trinidad) Limited (BAICO). Action was taken to protect the CIB's depositors and the policy holders of the insurance companies,

¹ Financial services account for 9% of total employment, about 25% of non-energy GDP, and 70% of stock market capitalization. State influence in the sector is not substantial, and credit is allocated on market terms. The financial system consists of a range of institutions, markets and instruments. Total system assets accounted around 160% of GDP in 2009-10, which is large relative to countries at comparable middle income levels.

² International Monetary Fund (2011) Trinidad and Tobago—2010 Article IV Consultation, IMF Country Report No. 11/73.

³ Winston Dookeran, the Honourable Minister of Finance. (2010, September). Budget Statement 2011 – Facing the Issues, Turning Around the Economy. Speech presented to Parliament, Republic of Trinidad and Tobago.

after these institutions were unable to meet their obligations. CIB, CLICO, and BAICO were subsidiaries of CLF. The fiscal cost, net of assets, of these actions could be as high as TT\$13.6 billion (10% of GDP).⁴

- 2.3 The IMF's 2010 Article IV consultation and Financial Stability Module (FSM) found the Trinidadian banking sector to be resilient and profitable, with high capitalization and conservative lending practices. Although the 2008 FIA strengthened bank regulation and supervision, other operational risks related to AML/CFT, administrative fines, and financial reporting remain.
- 2.4 The insurance sector, which has been supervised by CBTT since 2004, is governed by the Insurance Act (IA) of 1966, which does not reflect current best practices in legislation for financial institutions and prudential requirement. The CBTT has been issuing guidelines to address these deficiencies; however, they are limited in scope and enforceability. A new insurance law is needed to resolve the shortcomings of the existing IA.⁵
- 2.5 Credit unions service roughly one-third of the population and pose systemic risk to financial stability. A large number of credit unions have taken on risky investments and are under stress because of exposure to CLICO. Moreover, supervision is weak and there is a lack of detailed financial data. A credit union law is needed to address such weaknesses and to enable the CBTT to supervise credit unions⁶.
- 2.6 Given the significance of the investment activities of the pension sector⁷ to overall macroeconomic growth and development, the CBTT started to supervise and regulate occupational (private) pension plans by rolling out new reporting requirements in 2008 and increasing efforts to obtain timely submission of annual filings. No specific pension's legislation is in place other than the IA thereby limiting the ability to assess the financial position of the sector. CBTT is in the process of developing a new Occupational Pension Bill for the industry⁸.
- 2.7 The Trinidad and Tobago Securities Exchange Commission (TTSEC) supervises the securities sector and mutual funds. Under current legislation, trust companies are lightly regulated and finance houses may have liquidity risk. As exposed by the failure of CLF, coordinated supervision and regulation of financial conglomerates by the different authorities is weak. A new Securities Industry Act need to establish a formal framework between the CBTT and TTSEC to improve regulatory co-operation and to strengthen onsite inspections⁹.
- 2.8 The consolidated supervisory framework established by the 2008 FIA has not been fully implemented and is limited with some systemically important financial

⁴ International Monetary Fund (2011) Trinidad and Tobago—2010 Article IV Consultation, IMF Country Report No. 11/73.

⁵ Ibid.

⁶ Financial Sector Note (Draft) prepared by the project team.

⁷ Private occupational pension plans accounted for roughly 14% of total assets of the financial system at mid-2010.

⁸ Ibid

⁹ Ibid

institutions, such as credit unions and the Unit Trust Company (UTC), falling outside the CBTT's regulatory perimeter. Moreover, CBTT and TTSEC need to enhance supervisory coordination for financial conglomerates¹⁰.

- 2.9 **Macroeconomic Conditions.** Trinidad and Tobago was one of the fastest growing countries in the Caribbean with average growth of 7% between 1993 and 2008. With the global financial crisis, TT's real GDP contracted by 3.5% in 2009, and was flat in 2010. 2010 GDP and GDP per capita were US\$20 billion and US\$15,000. TT has a dual economy highly dependent energy sector (oil and natural gas). In 2009, energy accounted for 42% of real GDP and 90% of exports. TT's financial sector also depends on the energy sector. Despite the partial recovery in energy prices in 2010, TT's real GDP growth was flat due to mid-term elections and delays in policy decisions by the new government. Even with strengthening of energy prices, medium-term growth is expected to remain below 3% due to structural weaknesses and subdued expansion of energy output. The negative trend in energy production will pressure fiscal and external accounts. In this context, the sustainability of TT's non-energy sector also faces significant challenges, since it is highly dependent on public sector expenditures, which in turn are dependent on energy sector revenues that account for more than 50% of total revenues. Fiscal accounts were heavily impacted by the decrease in energy revenues (40%) between 2008 and 2009, combined with the GORTT's decision to keep high expenditures.¹¹
- 2.10 **The Government's Commitment.** GORTT is actively involved in enhancing supervision and regulations in the financial sector. Measures to strengthen the financial sector supervisory and regulatory framework have been undertaken by GORTT following the IMF's 2005 FSAP and the failure of CLICO. The FIA of 2008 strengthened banking sector and consolidated supervision. The IA was amended in 2009 to enhance the CBTT's power to address problem institutions, frequent reporting, and on-site inspections. Given their systemic significance, a new Credit Union Act has been drafted to strengthen the regulatory and supervisory framework of credit unions and to transfer supervisory authority to the CBTT.¹²
- 2.11 **The Bank's Strategy with the Country and Sector.** The Country Strategy (CS) with TT for 2004-2007 (GN-2335) was approved on September 28, 2004, later updated in 2008 (GN-2477), and updated again in 2010 (GN-2570 approved on May 4th, 2010 by the IDB Board of Executive Directors). Although the CS does not directly focus on the financial sector, it does highlight the importance of private sector development to increase economic diversification. A healthy financial sector is a prerequisite for the development of the private sector as macroeconomic stability and access to credit are two important dimensions for a prosperous private sector. The operation also reflects the Bank's institutional priorities as outlined in the Report on the Ninth General Increase in Resources for the IDB (GCI-9) (AB-2764) as it contributes to the goal of "supporting

¹⁰ International Monetary Fund (2011) Trinidad and Tobago—2010 Article IV Consultation, IMF Country Report No. 11/73.

¹¹ International Monetary Fund (2011) Trinidad and Tobago—2010 Article IV Consultation, IMF Country Report No. 11/73.

¹² Ibid.

development in small and vulnerable countries” (such as TT). Lastly, the Financial Sector supervision and regulation is one of the priority areas identified in the IDB Country Strategy currently under preparation.

III. TECHNICAL ISSUES AND SECTOR KNOWLEDGE

- 3.1 The objective of the IDB’s interventions will be to reduce the vulnerabilities of the financial sector and reduce the probability of systemic crisis. The associated interventions will focus on: (i) reforming the regulatory and supervisory framework for the financial sector; and (ii) strengthening the institutional capacity of the Government in the area of risk identification and management. Expected results include: (i) an improved supervisory and regulatory framework for the financial sector, and (ii) improved AML/CFT FATF compliance.¹³
- 3.2 The Program is proposed under the programmatic modality with two sequential operations, according to the Guidelines for Programmatic Policy Reform Loans (GN-200-13 and CS-3633). The first operation amounts to US\$30 million and the second, has been tentatively estimated at US\$70 million.
- 3.3 The first loan will focus on supporting GORTT’s financial sector reform initiatives whose significance have been diagnosed by the IMF’s Article IV Consultation and FSM findings, and the Bank’s own assessment. The policy and institutional measures for the initial loan focuses on the presentation of the Insurance Bill to Parliament, facilitation of legislative reforms for credit unions and occupational pensions, and other measures that reduce financial sector vulnerabilities. Other measures include strengthening of AML/CFT guidelines, procedural reforms, financial disclosure, supervisory skills as well as improving crisis response mechanisms. Concrete activities supported by the first loan are detailed in the Draft Policy Matrix.
- 3.4 The second loan will continue supporting the reform in the financial sector. The activities, as detailed in the Draft Policy Matrix will allow concluding some of the key reform started with the first operation by implementing the new insurance legislation, supporting the presentation to Parliament of the Credit Union Bill and the completion of the drafting of the Occupational Pension Bill. As well, this operation will focus on the implementation of the specific improvements in transparency, AML-CFT, and the crisis response mechanisms.
- 3.5 The Program structure is divided into three components: (i) macroeconomic stability; (ii) strengthening financial regulation and supervision; and (iii) improving financial crisis response mechanisms.
- 3.6 **Component I – Macroeconomic Stability.** As with any budgetary support loan, a general condition for the disbursement of the tranche of this Program is a stable

¹³ Although they cannot be included due to space constraints, this program’s targets are aligned with the aspirational targets set forth in the corresponding priority area of the 2011-2015 Country Strategy.

macroeconomic policy consistent with the Program's objectives. This will be set out in the country's Policy Letter to the IDB.

- 3.7 **Component II – Strengthening Financial Regulation and Supervision.** GORTT's financial regulatory and supervisory framework will be strengthened according to best practices. The Bank will support specific areas for reform as prioritized by the GORTT and confirmed by the IMF's assessments. Measures include: (i) updating of the Insurance Act through the presentation of a new Bill to Parliament; (ii) supporting the legislative process for the new Credit Union Bill; (iii) strengthening the Securities and Mutual Funds regulation; (iv) supporting the legislative process for new AML/CFT guidelines; (v) supporting the establishment of procedural reforms enabling fines collection and cost recover by the CBTT; (vi) improving transparency; and (vii) enhancing the CBTT's supervisory skills.
- 3.8 **Component III – Improving Financial Crisis Response Mechanisms.** To improve the ability of GORTT to respond to a financial crisis, the Bank will support the development of a national financial crisis management plan and resolution mechanisms for troubled financial institutions. That will enable the coordination among regulatory bodies, fiscal and monetary authorities.
- 3.9 The Bank is conducting, through the Compete Caribbean Program, two technical assistance programs directed to strengthen the risk position of the country (TT-CC2016 and TT-CC2008).

IV. SAFEGUARDS

- 4.1 In accordance with Directive B.13 of the Bank's Environment and Safeguards Compliance Policy (GN-2208-20 and OP-703) and because this is a policy-based sector loan, no ex-ante environmental impact classification is required. In addition, the policy changes contemplated in this operation will not have direct or significant impacts on the environment or on the country's natural resources.

V. OTHER ISSUES

- 5.1 **Collaboration with Other Donors.** The IDB is working in close coordination with the IMF to ensure that the Bank builds on recommended reforms.

VI. RESOURCES AND TIMETABLE OTHER ISSUES

- 6.1 Annex V describes project preparation activities. The distribution of the Proposal for Operation Development to the Quality Review Committee is expected on September 20th, 2011. This will allow for the need to conduct technical work. The Independent Macroeconomic Assessment will be ready by August 1st, 2011. The distribution of the Draft Loan Proposal to the Operations Policy Committee is expected on October 24th and approval by the Board of Directors on December 14th, 2011. Total resources required are US\$76,800 (US\$31,800 for missions and US\$45,000 for consultancy). Finally, for the implementation of the second operation, a TC amount of US\$600,000 is needed.

SAFEGUARD POLICY FILTER REPORT

This Report provides guidance for project teams on safeguard policy triggers and should be attached as an annex to the PP (or equivalent) together with the Safeguard Screening Form, and sent to ESR.

1. Save as a Word document. 2. Enter additional information in the spaces provided, where applicable. 3. Save new changes.

PROJECT DETAILS	IDB Sector	CAPITAL MARKETS-CAPITAL MARKET DEVELOPMENT
	Type of Operation	Other Lending or Financing Instrument
	Additional Operation Details	
	Investment Checklist	Generic Checklist
	Team Leader	Ketterer, Juan Antonio (JUANK@iadb.org)
	Project Title	Financial Sector Program I
	Project Number	TT-L1024
	Safeguard Screening Assessor(s)	Massini, Marina (MARINAM@iadb.org)
	Assessment Date	2011-06-14
	Additional Comments	

SAFEGUARD POLICY FILTER RESULTS	Type of Operation	Loan Operation	
	Safeguard Policy Items Identified (Yes)	Activities to be financed in the project area are located within a geographical area or sector exposed to natural hazards (Type 1 Disaster Risk Scenario).	(B.01) Disaster Risk Management Policy– OP-704
		The operation is in compliance with environmental, specific women's rights, gender, and indigenous laws and regulations of the country where the operation is being implemented (including national obligations established under ratified Multilateral Environmental Agreements).	(B.02)

		The operation (including associated facilities) is screened and classified according to their potential environmental impacts.	(B.03)
		The Bank will monitor the executing agency/borrower's compliance with all safeguard requirements stipulated in the loan agreement and project operating or credit regulations.	(B.07)
		Suitable safeguard provisions for procurement of goods and services in Bank financed projects may be incorporated into project-specific loan agreements, operating regulations and bidding documents, as appropriate, to ensure environmentally responsible procurement.	(B.17)
	Potential Safeguard Policy Items(?)	No potential issues identified	
	Recommended Action:	<p>Operation has triggered 1 or more Policy Directives; please refer to appropriate Directive(s). Complete Project Classification Tool. Submit Safeguard Policy Filter Report, PP (or equivalent) and Safeguard Screening Form to ESR.</p> <p>The project triggered the Disaster Risk Management policy (OP-704).</p> <p>A more limited and specific Disaster Risk Assessment (DRA) may be required (see Directive A-2 of the DRM Policy OP-704). Please contact a Natural Disaster Specialist in VPS/ESG or INE/RND for guidance.</p>	
	Additional Comments:		

ASSESSOR DETAILS	Name of person who completed screening:	Massini, Marina (MARINAM@iadb.org)
	Title:	
	Date:	2011-06-14

SAFEGUARD SCREENING FORM

This Report provides a summary of the project classification process and is consistent with Safeguard Screening Form requirements. The printed Report should be attached as an annex to the PP (or equivalent) and sent to ESR.

1. Save as a Word document. 2. Enter additional information in the spaces provided, where applicable. 3. Save new changes.

PROJECT DETAILS	IDB Sector	CAPITAL MARKETS-CAPITAL MARKET DEVELOPMENT
	Type of Operation	Other Lending or Financing Instrument
	Additional Operation Details	
	Country	TRINIDAD AND TOBAGO
	Project Status	
	Investment Checklist	Generic Checklist
	Team Leader	Ketterer, Juan Antonio (JUANK@iadb.org)
	Project Title	Financial Sector Program I
	Project Number	TT-L1024
	Safeguard Screening Assessor(s)	Massini, Marina (MARINAM@iadb.org)
	Assessment Date	2011-06-14
	Additional Comments	

PROJECT CLASSIFICATION SUMMARY	Project Category: C	Override Rating:	Override Justification:
			Comments:
	Conditions/ Recommendations	<ul style="list-style-type: none"> No environmental assessment studies or consultations are required for Category "C" operations. Some Category "C" operations may require specific safeguard or monitoring requirements (Policy Directive B.3). Where relevant, these operations will establish safeguard, or monitoring requirements to address environmental and other risks (social, disaster, cultural, 	

		<p>health and safety etc.).</p> <ul style="list-style-type: none"> • The Project Team must send the PP (or equivalent) containing the Environmental and Social Strategy (the requirements for an ESS are described in the Environment Policy Guideline: Directive B.3) as well as the Safeguard Policy Filter and Safeguard Screening Form Reports.
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SUMMARY OF IMPACTS/RISKS AND POTENTIAL SOLUTIONS	Identified Impacts/Risks	Potential Solutions
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DISASTER SUMMARY	Details	Actions
	<p>The Project should include the necessary measures to reduce disaster risk to acceptable levels as determined by the Bank on the basis of generally accepted standards and practices. Alternative prevention and mitigation measures that decrease vulnerability must be analyzed and included in project design and implementation as applicable. These measures should include safety and contingency planning to protect human health and economic assets. Expert opinion and adherence to international standards should be sought, where reasonably necessary.</p>	<p>A more limited and specific Disaster Risk Assessment (DRA) may be required (see Directive A-2 of the DRM Policy OP-704). Please contact a Natural Disaster Specialist in VPS/ESG or INE/RND for guidance.</p>

ASSESSOR DETAILS	Name of person who completed screening:	Massini, Marina (MARINAM@iadb.org)
	Title:	
	Date:	2011-06-14

ANNEX III

Environmental and Social Safeguard Strategy (ESS)

Financial Sector Reform I (PBL) (TT-L1024)

The nature of this operation is based on institutional reforms which does not include any environmental nor social negative implications. The Bank will not finance any concrete investments in the country. Hence, because of the nature of the operation, there is no direct impact on the environment. In accordance with the provisions set forth B.13 of the Environment and Safeguards Compliance Policy (GN 2208-20 an OP-703), this operation does not require classification.

ANNEX IV – INDEX FOR COMPLETED AND PROPOSED SECTOR WORK

Issues	Description	Expected Dates	References & Hyper- links to Technical Files
Technical options and design	<p>Agreement has been reached with authorities on the structure of program; programmatic loan complemented by a Technical Cooperation Program.</p> <p>Based on the analysis of financial sector regulatory and supervisory strengthening needs and government priorities, the specifics of the policy matrix will be agreed upon. A draft policy matrix has been sent to authorities (Appendix III).</p>	<p>Completed</p> <p>6/17/11</p>	<p>6/2011 Aide-Memoire and Identification Mission</p> <p>TT Financial Sector Note; draft policy matrix (Appendix III)</p> <p>2010 IMF Article IV Consultation Report</p> <p>http://www.imf.org/external/pubs/ft/scr/2011/cr1173.pdf</p> <p>2010 IMF FSAP Report (confidential)</p>
Financial management/fiduciary issues and control environment	<p>Necessary only for technical cooperation.</p> <p>To be conducted during project preparation by fiduciary specialist.</p>	July 2011	
Economic Evaluation in Cost-Benefit Analysis	<p>To be conducted during project preparation by consultant.</p>	September 20, 2011	

Data collection and analysis for reporting on results	<p>Baselines</p> <p>Ministry of Finance and Central Bank databases, research reports, legal and regulatory documentation, and external reports. Bank sector notes, and 2010 IMF Article IV Consultation and FSAP reports</p>	<p>Completed (Nov 2010)</p> <p>Completed</p> <p>During project execution.</p>	<p>TT Financial Sector Note</p> <p>2010 IMF Article IV Consultation http://www.imf.org/external/pubs/ft/scr/2011/cr1173.pdf 2010 IMF FSAP (confidential)</p>
Institutional analysis/personnel, procedures other aspects of implementation capacity	<p>Based on reports from IMF (Article IV Consultation and FSAP). 2011-2012 Ministry of Finance of Trinidad and Tobago budget statement.</p>	Completed	<p>2010 IMF Article IV Consultation http://www.imf.org/external/pubs/ft/scr/2011/cr1173.pdf 2010 IMF FSAP (confidential) 2011-2012 MoF budget statement http://www.finance.gov.tt/content/Budget%20Statement%202011.pdf</p>
Stakeholders and political environment	Discussions by project team with stakeholders.	Initial discussions completed; additional to be held during project execution.	
Social and environmental safeguards	Not applicable.	N/A	
Other key issues, such as donors, gender, sustainability, country/sector issues	Not applicable.	N/A	