

ANNUAL REPORT OF THE BOARD OF DIRECTORS

Annual Report of the Board of Directors on the Affairs of the Company and Statement of Compliance of the Contents of the Annual Report as Required by Section 168 of the Companies Act No. 07 of 2007

1. General

The Directors have pleasure in presenting to the shareholders 49th Annual Report of your Company together with the Audited Financial Statements of the Group and the Bank for the year ended December 31, 2017 and the Independent Auditors' Report on those Financial Statements conforming to all relevant statutory requirements. This Report provides the information as required by the Companies Act No. 07 of 2007, Banking Act No. 30 of 1988 and amendments thereto and the Directions issued thereunder including the Banking Act Direction No. 11 of 2007 on "Corporate Governance for

Licensed Commercial Banks in Sri Lanka" and subsequent amendments thereto, the Listing Rules of the Colombo Stock Exchange (the CSE) and the recommended best practices.

This Report was approved by the Board of Directors on February 23, 2018. The appropriate number of copies of the Annual Report will be submitted to the CSE and to the Sri Lanka Accounting and Auditing Standards Monitoring Board within the statutory deadlines.

Commercial Bank of Ceylon PLC (the Bank) is a licensed commercial bank registered under the Banking Act No. 30 of 1988 and was incorporated as a public limited liability company in Sri Lanka on June 25, 1969 under the Companies Ordinance No. 51 of 1938 and was re-registered as per the requirements of

the Companies Act No. 07 of 2007 on January 23, 2008, under Registration No. PQ 116. The registered office of the Bank is at No. 21, "Commercial House", Sir Razik Fareed Mawatha, Colombo 01, Sri Lanka, where the Bank's Head Office too is situated.

The ordinary shares (both voting and non-voting) of the Bank are quoted on the Main Board of the CSE since March 1970. The unsecured subordinated redeemable debentures issued by the Bank are also listed on the CSE. Fitch Ratings Lanka Ltd. has re-affirmed the Bank's national long-term rating at "AA(Ika)" with a stable outlook and subordinated debentures at "AA-(Ika)".

As required by the Section 168 of the Companies Act No. 07 of 2007, the following information is disclosed in this Report prepared for the year ended December 31, 2017:

Information required to be disclosed as per the Companies Act No. 07 of 2007	Reference to the Companies Act	Annual Report page reference for compliance and necessary disclosures
(i) The nature of the business of the Group and the Bank together with any changes thereof during the accounting period.	Section 168 (1) (a)	☐ Refer Section 1.3 on "Principal Business Activities, Nature of Operations of the Group and Ownership by the Bank in its Subsidiaries and Associates" on pages 173 and 174.
(ii) Signed Financial Statements of the Group and the Bank for the accounting period completed in accordance with Section 152.	Section 168 (1) (b)	The Financial Statements of the Group and the Bank for the year ended December 31, 2017 have been prepared in accordance with the requirements of the Sri Lanka Accounting Standards (SLFRSs and LKASs) and comply with the requirements of the Companies Act No. 07 of 2007 and the Banking Act No. 30 of 1988 and which were duly certified by the Chief Financial Officer (the person responsible for the preparation of the Financial Statements) and were approved by three members of the Board and the Company Secretary as appearing on ☐ pages 165 to 332 form an integral part of this Report.
(iii) Auditors' Report on the Financial Statements of the Group and the Bank.	Section 168 (1) (c)	☐ Refer page 162 for the Independent Auditors' Report.
(iv) Accounting Policies of the Group and the Bank and any changes therein.	Section 168 (1) (d)	Significant Accounting Policies adopted in the preparation of the Financial Statements of the Group and the Bank are given on ☐ pages 173 to 194. There were no changes to the Accounting Policies used by the Group and the Bank during the year, except the application of hedge accounting principles for an Interest Rate Swap entered into by the Bank in March 2017.

Information required to be disclosed as per the Companies Act No. 07 of 2007	Reference to the Companies Act	Annual Report page reference for compliance and necessary disclosures
(v) Particulars of the entries made in the Interests Register of the Bank and its Subsidiaries during the accounting period.	Section 168 (1) (e)	The Bank and all its Subsidiaries maintain Interests Registers. All Directors have made declarations as required by Sections 192 (1) and (2) of the Companies Act aforesaid and all related entries were made in the Interests Registers during the year under review. The Interests Registers are available for inspection by shareholders or their authorised representatives as required by Section 119 (1) (d) of the Companies Act No. 07 of 2007.
(vi) Remuneration and other benefits paid to Directors of the Bank and its Subsidiaries during the accounting period.	Section 168 (1) (f)	☐ Refer Note 21 to the Financial Statements on page 205. Also refer the "Board Human Resources and Remuneration Committee Report" on ☐ pages 130 and 131.
(vii) Total amount of donations made by the Bank and its Subsidiaries during the accounting period.	Section 168 (1) (g)	☐ Refer Note 21 to the Financial Statements on page 205.
(viii) Information on Directorate of the Bank and its Subsidiaries during and at the end of the accounting period.	Section 168 (1) (h)	☐ Refer Items 12.1 and 12.2 on pages 141 and 142.
(ix) Separate disclosure on amounts payable to the Auditors as audit fees and fees for other services rendered during the accounting period by the Bank and its Subsidiaries.	Section 168 (1) (i)	☐ Refer Note 21 to the Financial Statements on page 205.
(x) Auditors' relationship or any interest with the Bank and its Subsidiaries.	Section 168 (1) (j)	Auditors do not have any other relationship or interest in contracts with the Bank, or any of its Subsidiaries or Associates other than being the Auditors for the Bank, Subsidiaries and Associates. ☐ Refer Item 22 on page 144.
(xi) Acknowledgement of the contents of this Report/Signatures on behalf of the Board of Directors.	Section 168 (1) (k)	☐ Refer Item 33 on page 145.

2. Review of business

2.1 Vision, mission and corporate conduct

The Bank's vision and mission statements are exhibited on ☐ page 3 of the Annual Report.

The business activities of the Group and the Bank are conducted maintaining the highest level of ethical standards in achieving our vision and mission, which reflect our commitment to high standards of business conduct and ethics.

The Bank issues a copy of its Code of Ethics to each and every staff member and all employees are required to abide by the provisions contained therein.

2.2 Review of operations of the Group and the Bank

The Bank has established delivery points across all districts of the country. During the year under review, six (6) new delivery points were added [nine (9) in 2016], bringing the total number of delivery points in Sri Lanka to 261 at the end of 2017 (255 at the end of 2016).

The Bank's ATM network is the single largest ATM network in the country. During 2017, the Bank installed 98 new ATMs (36 in 2016) bringing the total number of ATMs in Sri Lanka to 755 by the end of 2017 (657 at the end of 2016). In addition to the branch network in Sri Lanka, the Bank also has 19 delivery points and 20 ATMs at the end of 2017 (19 and 20 respectively,

in 2016) in Bangladesh. The Bank's Bangladesh Operation was set up in 2003 with the acquisition of Bangladesh Operation of Crédit Agricole Indosuez.

Commercial Bank of Maldives Private Limited (CBM), the foreign subsidiary of the Bank, which is a fully-fledged Tier 1 Bank incorporated in the Republic of Maldives in which the Bank holds a stake of 55% (the remaining stake of 45% being held by a leading Maldivian group of companies) continued to expand its operations and was able to break-even and report profits during the year. The CBM which commenced commercial operations in September 2016 opened its second branch in Hulhumalé in the Republic of Maldives in December 2017.

Commex Sri Lanka S.R.L., the fully-owned foreign Subsidiary of the Bank, which was incorporated and registered in Italy under the supervision of the Bank of Italy to engage in fund transfers on its own market commenced commercial operations in November 2016.

This Company too continued to expand its operations and was able to break-even and reports profits during the year. The Bank expects over time, to open branches in other Italian cities which have high potential for money transfer services to both Sri Lanka and Bangladesh.

The Bank also has a Representative Office in Yangon, Myanmar and incorporated CBC Myanmar Microfinance Company Limited, our third foreign subsidiary in December 2017.

Besides Bangladesh, Maldives, Italy, and Myanmar, the Bank also has placed its own Business Promotion Officers (BPOs) in key markets around the world where a significant number of Sri Lankans are employed to provide money transfer facilities via the Bank's e-Exchange remittance service.

The local operations of the Bank have been segmented into Personal Banking, Corporate Banking and Treasury Operations in order to provide personalised customer experience and for better strategy formulation, implementation and also for carrying out performance evaluations more effectively.

The "Chairman's Message" on pages 16 to 19 and the "Managing Director's Review" on pages 20 to 22 provide an overall review of business performance and the state of affairs of the Group and the Bank while the "Management Discussion and Analysis" on pages 49 to 104, together with the Audited Financial Statements provide a comprehensive review on the performance of key business units and the state of affairs of the Group and the Bank together with important events that took place during the year as required by Section 168 of the Companies Act No. 07 of 2007 and the recommended best accounting practices.

The details of the segment wise contribution to the Group's revenue, results, assets and liabilities are disclosed in Note 63 to the Financial Statements on pages 291 to 293.

2.3 Directors' responsibility for financial reporting

In terms of Sections 150 (1), 151, 152 and 153 (1) and (2) of the Companies Act No. 07 of 2007, the Board of Directors of the Bank are responsible for the preparation of the Financial Statements of the Group and the Bank, which reflect a true and fair view of the financial position and performance of the Group and the Bank. In this regard, the Board of Directors wish to confirm that the Income Statement, Statement of Comprehensive Income, Statement of Financial Position, Statement of Changes in Equity, Statement of Cash Flows, Significant Accounting Policies and Notes thereto appearing on pages 165 to 332 have been prepared in conformity with the requirements of the SLFRSs and LKASs as mandated by the Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995 and the Companies Act No. 07 of 2007. Further, these Financial Statements also comply with the requirements of the Banking Act No. 30 of 1988 and amendments thereto and the Listing Rules of the Colombo Stock Exchange.

The "Statement of Directors' Responsibility" appearing on pages 146 and 147 forms an integral part of this Report.

3. Future developments

In line with the vision, the Bank intends expanding its network of delivery channels both in Sri Lanka and overseas by employing customer centric strategy with effective management of its capital, liquidity, and risks. Towards this, the Bank will continue to focus on its customer-centric model for doing business with the objective of bringing more convenience and delighting its customers. The Bank endeavours to capitalise online

and Mobile banking facilities enabling customers to easily access to most banking services 24/7.

In line with our theme "Banking on the Future", we will continue to focus on evolving customer aspirations and invest on state-of-the-art technology to serve our customers while strengthening our risk and compliance framework.

The sections on "Chairman's Message", "Managing Director's Review" on pages 16 to 22 and "Management Discussion and Analysis" on pages 49 to 104 describe the specific initiatives taken in this regard.

4. Gross income

The gross income of the Group for 2017 was Rs. 116.842 Bn. (Rs. 93.726 Bn. in 2016) while the Bank's gross income was Rs. 115.594 Bn. (Rs. 93.143 Bn. in 2016).

The sources of external operating income, net operating profit and asset allocation of the Group among main business segments, namely, Personal Banking, Corporate Banking, International Operations, Investment Banking, and Dealing/Treasury together with their proportions are given in Note 63 to the Financial Statements on pages 291 to 293.

5. Results and appropriations

5.1 Performance of the Group and the Bank and transfers to reserves

The net profit before tax of the Group and the Bank amounted to Rs. 23.280 Bn. and Rs. 23.183 Bn., respectively in 2017 (Rs. 20.115 Bn. and Rs. 20.051 Bn. in 2016) and this was an increase of 15.74% and 15.62%, (17.38% and 16.96%, respectively in 2016). Further, the net profit after tax of the Group and the Bank amounted to Rs. 16.627 Bn. and Rs. 16.581 Bn., respectively in 2017 (Rs. 14.466 Bn., and Rs. 14.513 Bn., respectively in 2016) and this was an increase of 14.93% and 14.25% (21.98% and 21.92%, respectively, in 2016).

Details of appropriation of profit of the Bank are given below:

	2017	2016
Profit for the year after payment of all expenses of management, provision for depreciation, impairment on loans and advances, VAT on financial services and contingencies	23,182,944	20,051,183
Less: Provision for taxation	(6,601,700)	(5,538,672)
Net profit after taxation	16,581,244	14,512,511
Balance brought forward from previous year	4,226	3,883
Net actuarial gains/(losses) on defined benefit plans	(529,902)	139,762
Dividend paid in respect of prior years	(2,279)	-
Realised revaluation gain on disposal of freehold land and buildings	36,940	-
Profit available for appropriation	16,090,229	14,656,156
Less: Appropriations		
Transfer to the statutory reserve fund	(829,062)	(725,626)
Transfer to the general reserve	(8,780,000)	(8,130,525)
Dividends on ordinary shares		
1st interim dividend paid – Rs. 1.50 per share in cash (Rs. 1.50 in 2016)	(1,493,719)	(1,335,928)
2nd interim dividend paid – Rs. 3.00 per share in cash (Rs. 3.00 in 2016)	(2,989,996)	(2,674,799)
Final dividend proposed/paid – Rs. 2.00 per share in shares (Rs. 2.00 in 2016)	(1,993,401)	(1,785,052)
Balance carried forward	4,051	4,226

On this basis, the cash dividend payout ratio amounts to 27.04% of the profit after tax of 2017, compared to 27.64% for 2016, while total dividend payout ratio amounts to 39.06% for 2017, compared to 39.94% for 2016. This is well above the minimum dividend payout ratio of 10% (10% in 2016) stipulated in the Deemed Dividend Tax Rule.

The Board of Directors provided the Statements of Solvency to the Auditors and obtained Certificates of Solvency from the Auditors in respect of each dividend payment in terms of Section 56 (2) of the Companies Act No. 07 of 2007.

The Board of Directors also fulfilled the requirement of the Solvency Test in terms of Section 56 (3) of the Companies Act No. 07 of 2007 immediately after the payment of interim dividends and will ensure the compliance of Solvency Test after the payment of aforesaid final dividend proposed to be paid in April 2018.

5.2 Dividends on ordinary shares

Details of information on dividends paid/proposed are given in Note 24 to the Financial Statements on page 209.

Two cash interim dividends of Rs. 1.50 per share (on November 20, 2017) and Rs. 3.00 per share (on February 20, 2018) were paid out of the profits of the Bank, hence, were subjected to a 10% withholding tax.

The Directors recommend to pay a final dividend of Rs. 2.00/- per share which will be paid partly out of dividends received and partly out of exempt/taxable profits of the Bank. Further, the aforesaid final dividend is proposed to be satisfied by issue and allotment of new shares, subject to a 10% withholding tax.

5.3 Reserves

A summary of the Group's reserves is given below:

	2017 Rs. '000	2016 Rs. '000
Statutory reserve fund	6,492,552	5,647,993
Revaluation reserve	7,834,003	6,250,554
General reserve	52,270,003	43,490,003
Foreign currency translation reserve	348,976	860,502
Available-for-sale reserve	(1,707,486)	(7,208,805)
Employee share option reserve	529,817	420,282
Hedging reserve	(3,212)	-
Retained earnings	5,086,609	4,553,778
Total	70,851,259	54,014,307

Information on the movement of reserves is given in the Statement of Changes in Equity on pages 168 to 171 and in Notes 55 to 57 to the Financial Statements on pages 282 to 285.

6. Corporate social responsibility (CSR)

The Bank established a CSR Trust in 2004 and this Trust is annually funded by the Bank which undertakes most of the CSR initiatives and activities of the Bank. The Trust manages a range of initiatives that strengthen one of the Bank's key principle of acting responsibly towards its stakeholders while generating measurable and sustainable social dividends for different segments of society, in particular those which require empowerment. The details of the CSR initiatives of the Bank are found under "Social and Network Capital" in the section on "Capital Management" in the Chapter on "Management Discussion and Analysis" on pages 78 to 89.

7. Property, plant and equipment, intangible assets and leasehold property

Information on property, plant and equipment, intangible assets and leasehold property of the Group and the Bank are given in Notes 39, 40 and 41 to the Financial Statements on pages 245, 258 and 260, respectively.

Investment properties of any group company when significantly occupied by the other companies in the Group are classified under property, plant and equipment in the Consolidated Financial Statements in accordance with the Sri Lanka Accounting Standard – LKAS 40 on "Investment Property".

Specific information on extent, location, valuations of the land and buildings held by the Bank are given in Note 39.5 (a) and (b) to the Financial Statements on pages 251 to 256.

The details of capital expenditure approved and contracted for are given in Note 59.3 to the Financial Statements on page 287.

8. Market value of properties

The Bank carried out a revaluation of all its freehold land and buildings as at December 31, 2017 as required by Section 7.1 (b) of the Direction No. 01 of 2014 on "Valuation of Immovable Property of Licensed Commercial Banks" issued by the Central

Bank of Sri Lanka (CBSL) and recognised the revaluation gain/(loss) in the Financial Statements.

The revaluation of the land and buildings of the Bank was carried out by professionally qualified independent valuers as per the aforesaid Direction.

Details of market value (revalued amounts) of freehold properties of the Bank are given in Note 39.5 (b) to the Financial Statements on pages 252 to 256.

Freehold land and buildings of the Bank are revalued by independent professional valuers every three years or more frequently if the fair values are substantially different from carrying amounts to ensure that the carrying amounts do not differ from the fair values as at the reporting date. The next revaluation exercise on the freehold land and buildings of the Bank will be carried out on or before December 31, 2020.

9. Issue of shares and debentures

9.1 Issue of shares and debentures by the Bank

Details of the shares issued by the Bank are given in the table below:

Reason for the issue	Details of the share issue	2017		2016	
		Voting ordinary shares	Non-voting ordinary shares	Voting ordinary shares	Non-voting ordinary shares
Rights issue of ordinary shares	Number of shares issued	84,649,465	5,811,601	N/A	N/A
	Consideration (Rs. '000)	9,616,179	527,693	N/A	N/A
Part of final dividend for 2016 amounting to Rs. 2.00/- per share (Rs. 2.00/- per share in 2015) satisfied in the form of issue and allotment of new shares	Number of shares issued	10,521,802	903,357	11,818,040	912,967
	Consideration (Rs. '000)	1,503,566	102,983	1,477,179	101,415
Exercise of options by employees under the Employee Share Option Plans	Number of shares issued	3,278,537	N/A	1,136,732	N/A
	Consideration received (Rs. '000)	386,311	N/A	135,582	N/A
	Amount transferred from Employee Share Option Reserve upon exercise (Rs. '000)	28,806	N/A	9,222	N/A

The Bank made a rights issue of ordinary shares (for both voting ordinary and non-voting ordinary shareholders) in June 2017 on the basis of one new ordinary share for every ten (10) ordinary shares held and raised Rs. 10.144 Bn. The issue price of a voting ordinary share was Rs. 113.60 and that of a non-voting share was Rs. 90.80. These funds were utilised to finance the lending portfolio of the Bank. All shares are listed on the CSE.

9.2 Issue of shares and debentures by the subsidiaries and associates

During the year 2017, Serendib Finance Limited issued 22,624,434 shares (9,128,252 shares in 2016) at Rs. 22.10 per share (Rs. 21.91 per share in 2016) for a total consideration of Rs. 500 Mn. (Rs. 200 Mn. in 2016) to the Bank in order to raise required funds for the expansion of lending activities.

During the year under review, CBC Myanmar Microfinance Company Limited too issued 420,000 ordinary shares at USD 1 per share for a total consideration of Rs. 64.512 Mn. to the Bank, upon formation of that company as a fully owned subsidiary of the Bank.

Except for the above share issues, the other Subsidiaries and Associates of the Bank did not make any share or debenture issues during the year.

9.3 Stated capital and debentures

The details of the Stated capital are given in Note 53 to the Financial Statements on pages 278 to 280. The details of debentures including the redemptions during the year are given in Note 52 to the Financial Statements on pages 276 and 277.

10. Share information

10.1 Distribution schedule of shareholdings

Information on the distribution of shareholding and the respective percentages are given in the section on "Investor Relations" on pages 339 to 341.

10.2 Information on earnings, dividend, net assets and market value

Information relating to earnings, dividend, net assets and market value per share is given in "Financial Highlights" on page 10. Information on the shares traded and movement in the number of shares represented by the stated capital of the Bank is given in the section on "Investor Relations" on pages 334 to 348.

10.3 Substantial shareholdings

Names of the twenty largest shareholders for both Voting and Non-voting Ordinary shares, percentages of their respective holdings and percentage holding of the public, etc., are given in the section on "Investor Relations" on pages 340 and 341.

11. Equitable treatment to shareholders

The Bank has at all times ensured that all shareholders are treated equitably.

12. Information on the Directors of the Group and the Bank

12.1. Information on Directors as at December 31, 2017

The Board of Directors of the Bank as at December 31, 2017 consisted of 12 Directors (10 Directors as at December 31, 2016) with wide knowledge and experience on economic, banking and financial, commercial, engineering, and legal as detailed in the "Profiles of Board Members" on pages 25 to 27.

Names of the Directors of the Bank during and as at the end of 2017, as required by Section 168 (1) (h) of the Companies Act No. 07 of 2007 are given below:

Name of the Director	Executive/ Non-Executive status	Independent/ Non-Independent status
Mr K G D D Dheerasinghe (<i>Chairman</i>)	Non-Executive	Independent
Mr M P Jayawardena (<i>Deputy Chairman</i>)	Non-Executive	Independent
Mr J Durairatnam (<i>Managing Director/CEO</i>)	Executive	Non-Independent
Mr S Swarnajothi	Non-Executive	Independent
Mr S Renganathan	Executive	Non-Independent
Prof A K W Jayawardane	Non-Executive	Independent
Mr K Dharmasiri	Non-Executive	Independent
Mr L D Niyangoda	Non-Executive	Independent
Ms N T M S Cooray	Non-Executive	Independent
Mr G S Jadeja	Non-Executive	Non-Independent
New Appointments made during 2017		
Mr T L B Hurulle (<i>Appointed with effect from April 05, 2017</i>)	Non-Executive	Independent
Justice K Sripavan (<i>Appointed with effect from April 26, 2017</i>)	Non-Executive	Independent
Resignations/Cessations during 2017 – None		

Names of the Directors of all Subsidiaries and Associates are given in "Group Structure" on page 438.

12.2 Recommendations for re-election

- (i) In terms of Article 85 of the Articles of Association, two Directors are required to retire by rotation at each Annual General Meeting (AGM). Article 86 provides that the Directors to retire by rotation at an AGM shall be those who (being subject to retirement by rotation) have been longest in office, since their last re-election or appointment.
- (ii) The Board recommended the re-election of the following Directors, after considering the contents of the affidavits and declarations submitted by them and all other related issues:
- (a) Directors to retire by rotation
- Mr S Swarnajothi
 - Mr K Dharmasiri
- (b) Directors appointed to fill casual vacancies
- Mr T L B Hurulle
 - Justice K Sripavan
- (iii) Directors who served on the Board for over 9 years.
- [In terms of the Banking Act Direction No. 11 of 2007 on "Corporate Governance for Licensed Commercial Banks in Sri Lanka", the total period of service of a Director (other than a Director who holds the position of Chief Executive Officer) shall not exceed nine years].
- None

12.3 Directors' meetings

Details of the meetings of the Board of Directors are presented on page 111.

12.4 Board Subcommittees

The Board of Directors of the Bank formed four mandatory Board Subcommittees (namely, Board Nomination Committee, Board Human Resources and Remuneration Committee, Board Integrated Risk Management Committee and Board Audit Committee) as required by the Banking Act Direction No. 11 of 2007 on "Corporate Governance for Licensed Commercial Banks in Sri Lanka" issued by the CBSL.

The Board formed a Related Party Transactions Review Committee in 2014 to assist the Board in reviewing all related party transactions carried out by the Bank and its listed Subsidiaries in the Group by

early adopting the Code of Best Practice on Related Party Transactions as issued by the Securities and Exchange Commission of Sri Lanka (the SEC) which became mandatory from January 1, 2016.

The Board of Directors also has formed three other voluntary Board Subcommittees to assist the Board.

These Subcommittees play a critical role in order to ensure that the activities of the Bank at all times are conducted with the highest ethical standards and in the best interest of all its stakeholders. The Terms of Reference of these Subcommittees conform to the recommendations made by various regulatory bodies, such as the CBSL, The Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka), the SEC, and the CSE.

The composition of both mandatory and voluntary Board Subcommittees, as at December 31, 2017 and the details of the attendance by Directors at meetings are tabulated on pages 111 and 113 while the Reports of these subcommittees are found on pages 124 to 135.

13. Disclosure of Directors' dealing in shares and debentures

13.1 Directors' interests in ordinary voting and non-voting shares of the Bank

Individual Ordinary Voting and Non-voting shareholdings of persons who were Directors of the Bank at any time during the financial year are as follows:

As at December 31,	Ordinary Voting shares		Ordinary Non-voting shares	
	2017	2016	2017	2016
Mr K G D D Dheerasinghe (Chairman)	23,567	21,159	Nil	Nil
Mr M P Jayawardena (Deputy Chairman)	Nil	Nil	Nil	Nil
Mr J Durairatnam (Managing Director/CEO)	616,800	470,770	Nil	Nil
Mr S Swarnajothi	Nil	Nil	10,762	8,738
Mr S Renganathan	319,792	197,647	11,718	10,488
Prof A K W Jayawardane	Nil	Nil	Nil	Nil
Mr K Dharmasiri	Nil	Nil	Nil	Nil
Mr L D Niyangoda	Nil	Nil	Nil	Nil
Ms N T M S Cooray	Nil	Nil	49,731	Nil
Mr G S Jadeja	Nil	Nil	Nil	Nil
Mr T L B Hurulle (Appointed with effect from April 05, 2017)	Nil	N/A	Nil	N/A
Justice K Sripavan (Appointed with effect from April 26, 2017)	Nil	N/A	Nil	N/A

Directors' shareholdings in ordinary voting shares and ordinary non-voting shares have not changed subsequently to the date of the Statement of Financial Position up to February 06, 2018, the date being one month prior to the date of Notice of the Annual General Meeting.

13.2 Directors' interests in debentures

During the year 2016, Mr S Renganathan purchased 20,000 debentures of the Bank and as at December 31, 2017, he held 20,000 debentures. Except Mr S Renganathan there were no debentures registered in the name of any other Director as at the beginning and at the end of the year.

14. Employee share option plans and profit sharing plans

The Bank implemented an Employee Share Option Plan (ESOP) for the Corporate Management and the Executive Officers in Grade III and above in 2008, based on the Bank achieving certain predetermined performance criteria. The approval of the shareholders was obtained for this scheme to offer share options up to 3% of the ordinary voting shares of the Bank.

The Bank also obtained the approval of the shareholders to introduce another ESOP for all Executive Officers in Grade 1A and above in 2015, based on the Bank achieving certain predetermined performance criteria.

The approval of the shareholders was obtained for this scheme to offer share options up to 2% of the Ordinary Voting shares of the Bank. 1st and 2nd Tranches of this ESOP were vested on September 30, 2016 and September 30, 2017.

The details of the ESOPs are given in Notes 53.2 and 54 to the Financial Statements on pages 279 to 281. The Group and the Bank do not have any employee profit sharing plans, except the variable bonus scheme.

15. Directors' interests in contracts or proposed contracts

Directors' interests in contracts or proposed contracts with the Bank, both direct and indirect are disclosed on pages 152 and 153. The Directors have also disclosed transactions, if any, that could be classified as Related Party Transactions in terms of the Sri Lanka Accounting Standard – LKAS 24 on "Related Party Disclosures". Please refer Note 64 to the Financial Statements on pages 294 to 300 for those transactions disclosed by the Directors. These interests have been declared quarterly at Board meetings.

As a practice, Directors have refrained from voting on matters in which they were materially interested. Directors have no direct or indirect interest in any other contract or proposed contract with the Bank.

There are no arrangements enabling the Non-Executive Directors of the Group and the Bank to acquire shares or debentures of the Bank or its Subsidiaries, other than *via* the market.

Tabulated below are the details of Options Available/Exercised by the Executive Directors under the ESOPs.

As at December 31,	2017		2016	
	Mr J Durairatnam	Mr S Renganathan	Mr J Durairatnam	Mr S Renganathan
Total options available to exercise as at January 1,	156,397	153,362	163,457	140,162
Options vested during the year	47,979	37,933	45,721	36,148
Additional options granted due to the rights issue	2,423	2,014	Nil	Nil
Options exercised during the year	83,609	94,323	52,781	22,948
Options expired during the year	Nil	Nil	Nil	Nil
Total options available to exercise as at December 31,	123,190	98,986	156,397	153,362

Directors' remuneration and other benefits in respect of the Group and the Bank for the financial year ended December 31, 2017 are given in Note 21 to the Financial Statements on page 205.

As per Section 217 of the Companies Act No. 07 of 2007, there are no restrictions on the approval of loans to Directors in the Bank's ordinary course of business, subject to compliance with all applicable regulations.

16. Directors' and officers' insurance

The Bank has, during the financial year, paid an insurance premium in respect of an insurance policy for the benefit of the Bank and the Directors, secretaries, officers and certain employees of the Bank and related body corporates as defined in the insurance policy. In accordance with commercial practice, the insurance policy prohibits disclosure of the terms of the policy, including the nature of the liability insured against and the amount of the premium.

17. Environmental protection

The Group and the Bank have not, to the best of their knowledge, engaged in any activity, which was detrimental to the environment. Specific measures taken to protect the environment are given on pages 102 to 104.

18. Statutory payments

The Directors, to the best of their knowledge and belief are satisfied that all statutory payments (including all taxes, duties and levies payable by the Bank and its Subsidiaries) due to the Government, other regulatory institutions and related to the employees have been made on time or where relevant provided for.

19. Events after the reporting period

No event of material significance that requires adjustments to the Financial Statements, has occurred subsequent to the reporting period, other than those disclosed in Note 70 to the Financial Statements on page 332.

20. Going concern

The Directors have made an assessment of the Bank's ability to continue as a going concern and is satisfied that it has the resources to continue in business for the foreseeable future. Furthermore, the Directors are not aware of any material uncertainties that may cast significant doubt upon the Bank's ability to continue as a going concern, such as restrictions or plans to curtail operations.

21. Appointment of auditors and their remuneration

The Board of Directors of the Bank resolved to adopt a policy of rotation of Auditors, once in every five years, in keeping with the principles of Good Corporate Governance, although the mandatory requirement is only partner rotation once in every five years. Accordingly, the present Auditors, Messrs KPMG were appointed as Auditors of the Bank at the Annual General Meeting held in March 2012 to carry out the audit of the Bank for the year ended December 31, 2012. Thereafter, they were reappointed as Auditors of the Bank at the Annual General Meetings held in March 2013, 2014, 2015 and 2016 to carry out the audits of the Bank for the years ended December 31, 2013, 2014, 2015 and 2016. However, the Board with the recommendation of the Board Audit Committee resolved to extend the period of service of Messrs KPMG by an additional one year, subject to terms and conditions of the Banking Act Directions, since the Bank has sought the services of Messrs KPMG to assist in carrying out a gap analysis and assist in the implementation of the requirements under the Sri Lanka Accounting Standard – SLFRS 9 on “Financial Instruments”.

The Directors are now proposing to adopt Messrs Ernst & Young be appointed as Auditors of the Bank, subject to the approval of shareholders, from the conclusion of the next Annual General Meeting of the Bank. Messrs Ernst & Young, on their appointment, with shareholders’ approval, will serve for a maximum period of 5 years consecutively, subject to them being re-elected by the shareholders, upon a recommendation of the Board of Directors, annually.

A resolution to appoint Messrs Ernst & Young as Auditors and granting authority to the Directors to fix their remuneration will be proposed at the forthcoming Annual General Meeting to be held on March 28, 2018 for Shareholder approval.

The retiring Auditors, Messrs KPMG have advised the Bank that they would not offer themselves for re-election on conclusion of the next Annual General Meeting.

Expenses incurred in respect of audit fees and fees for other services rendered during the accounting period are given in Note 21 to the Financial Statements on page 205.

22. Lead auditor’s independence

Independence confirmation has been provided by Messrs KPMG as required by Section 163 (3) of the Companies Act No. 07 of 2007, in connection with the audit for the year ended December 31, 2017 confirming that KPMG is not aware of any relationship with or interest in the Bank or any Subsidiaries audited by KPMG that in their judgement, may reasonably be thought to have a bearing on their independence within the meaning of the Code of Professional Conduct and Ethics issued by the ICASL, applicable as at the reporting date.

No prohibited non-audit services have been provided by Messrs KPMG as per the Direction issued by the Central Bank of Sri Lanka on “Guidelines for External Auditors relating to their Statutory Duties”. The Directors are satisfied because the Board Audit Committee has assessed each service, having regard to auditor independence requirements of applicable laws, rules and regulations, and concluded in respect of each non-audit service or type of non-audit service that the provision of that service or type of service would not impair the independence of Messrs KPMG.

23. Information on ratios, market prices of shares and credit ratings

Information that requires disclosures as per Rule 7.6 (xi) of the Listing Rules of the CSE are given in the section on “Investor Relations” on pages 334 to 348.

24. Risk management and system of internal controls

The Bank has an ongoing process in place to identify, evaluate, and manage the risks that are faced by the Bank. The Directors continuously review this process through the Board Integrated Risk Management Committee. Specific steps taken by the Bank in managing both banking and non-banking risks are detailed in the section on “Managing Risk: An Overview” on pages 154 to 158 in the “Board Integrated Risk Management Committee Report” on pages 127 and 128 in Note 69 to the Financial Statements on “Financial Risk Review” on pages 303 to 332.

An effective and comprehensive system of internal controls is in place in the Bank comprising internal checks, internal audit, and financial and other controls required to carry out the business of banking in an orderly manner and to safeguard the assets. The Directors’ Statement on Internal Control and the Independent Auditors’ Report thereon are given on pages 148 to 150.

25. Corporate governance Directors’ declarations

The Directors declare that:

- (a) the Bank has complied with all applicable laws and regulations in conducting its business and have not engaged in any activity contravening the relevant laws and regulations. Officers responsible for ensuring compliance with the provisions in various laws and regulations, confirm compliance in each quarter to the Board Integrated Risk Management Committee;
- (b) they have declared all material interests in contracts involving the Bank and refrained from voting on matters in which they were materially interested;
- (c) all endeavours have been made to ensure that shareholders in each category have been treated equitably in accordance with the original Terms of Issue;
- (d) the business is a going concern with supporting assumptions or qualifications as necessary, and that the Board of Directors has reviewed the Bank’s Corporate/Business plans and is satisfied that the Bank has adequate resources to continue its operations in the foreseeable future. Accordingly, the Financial Statements of the Bank, its Subsidiaries, and Associates are prepared based on the going concern assumption;
- (e) the Bank has complied with the Code of Best Practice on Related Party Transactions and has made the disclosures in the Financial Statements and to the market when applicable; and
- (f) they have conducted a review of internal controls covering financial, operational and compliance controls, risk management and have obtained a reasonable assurance of their effectiveness and proper adherence.

The measures taken and the extent to which the Bank has complied with the Code of Best Practice on Corporate Governance 2017 issued by the ICASL, the CSE and the CBSL are given in the section on “How We Govern” on pages 106 to 117.

26. Focus on new regulations

The Directors have taken necessary steps to assess the implications of the new Inland Revenue Act which will become effective from April 1, 2018.

The Bank has evaluated the implications on adoption of the Sri Lanka Accounting Standard – SLFRS 9 on “Financial Instruments” effective from January 1, 2018 and developed the required financial models to assess the impairment on financial assets under the new framework.

27. Sustainability

The Bank is an early champion of adopting sustainability practices and sustainability reporting. The Bank has considered the sustainability aspects when formulating its business strategies and details of which are presented on pages 418 to 420.

28. Human resources

The Bank continues to invest in human capital development and implement effective human resource practices and policies to improve workforce efficiency, effectiveness and productivity and also to foster collaborative partnerships that enrich the work and learning environment for our staff.

Specific measures taken in this regard are detailed in the “Board Human Resources and Remuneration Committee Report” appearing on pages 130 and 131.

29. Technology

As encapsulated in the vision and the mission, our business processes are underpinned by technology. All of our processes involve information technology, and we use technology to deliver superior products and services to our customers. Correspondingly, the nature of the business is more heavily intertwined with technology than ever before.

Key achievements in this regard during the year are detailed in the “Board Technology Committee Report” appearing on page 135.

30. Operational excellence

To increase efficiency and reduce operating cost, the Bank has ongoing initiatives to drive policy and process standardisation and to optimise the use of existing technology platforms.

31. Outstanding litigation

In the opinion of the Directors and in consultation with the Bank’s lawyers, litigation currently pending against the Group and the Bank will not have a material impact on the reported financial results or future operations. Details of litigation pending against the Group and the Bank are given in Note 61 to the Financial Statements on page 288.

32. Annual general meeting and the notice of meeting

The 49th Annual General Meeting of the Bank will be held at Galadari Hotel, “Grand Ballroom”, No. 64, Lotus Road, Colombo 01, on Wednesday, March 28, 2018 at 2.00 p.m.

Notice relating to the 49th Annual General Meeting of the Bank is enclosed at the end of the Annual Report.

33. Acknowledgement of the contents of the report

As required by Section 168 (1) (k) of the Companies Act No. 07 of 2007, the Board of Directors does hereby acknowledge the contents of this Annual Report.

Signed in accordance with a resolution adopted by the Directors.



K G D D Dheerasinghe
Chairman



M P Jayawardena
Deputy Chairman



J Durairatnam
Managing Director/CEO



S Swarnajothi
Director



S Renganathan
Director



Prof A K W Jayawardane
Director



K Dharmasiri
Director



L D Niyangoda
Director



Ms N T M S Cooray
Director



G S Jadeja
Director



T L B Hurulle
Director



Justice K Sripavan
Director



Mrs J R Gamage
Company Secretary

Colombo
February 23, 2018