

PART III

PART III

MAJOR ADMINISTRATIVE MEASURES ADOPTED BY THE MONETARY BOARD IN 2007

OPERATING INSTRUCTIONS, CIRCULARS, DIRECTIONS AND NOTICES

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My No. : 02/04/004/0012/001
Your No. :

Bank Supervision Department
19 January 2007

To: *All Licensed Commercial Banks and
Licensed Specialised Banks*

Dear Sirs

CUSTOMER DUE DILIGENCE - 'KNOW YOUR CUSTOMER'
PROCEDURES

In view of the potential risks on the banking and financial system stability that may arise from cross-border financial transactions, all licensed banks shall conduct due diligence on all customers involved in cross-border financial transactions and ensure that all requirements under the relevant statutes including Prevention of Money Laundering Act No.5 of 2006, financial Transactions Reporting Act No.6 of 2006 and Convention on the Suppression of Terrorist Finance Act No, 25 of 2005 and the Exchange Control Act No. 24 of 1953 are complied with.

Accordingly, the licensed banks shall report any transaction of suspicious nature to the relevant authorities in terms of the above statutes immediately.

Yours faithfully
P Samarasiri
Director of Bank Supervision

Directions issued by the Monetary Board under Section 46(1) of the Banking Act No.30 of 1988, as amended.

Nivard Ajith Leslie Cabraal
Governor

Colombo
19 January 2007

DIRECTIONS
BANKING ACT DIRECTIONS NO. 1 OF 2007
OWNERSHIP OF ISSUED CAPITAL CARRYING VOTING RIGHTS

In exercise of the powers conferred by Section 46(1) of the Banking Act No. 30 of 1988, last amended by the Banking Act No.46 of 2006, the Monetary Board hereby issues Directions as follows:

- | | |
|----------------------------------|---|
| Citation | 1. These Directions may be cited as the Banking Act Directions No.1 of 2007. The Sections referred to in these Directions will be those of the Banking Act No. 30 of 1988, last amended by the Banking Act No. 46 of 2006. |
| Empowerment under Section 12(1C) | <p>2. In terms of Section 46(1), in order to ensure the soundness of the banking system, the Monetary Board has been empowered to issue Directions to licensed commercial banks regarding the manner in which any aspect of the business of such banks is to be conducted, including Directions pertaining to the maximum percentage of the share capital in a licensed commercial bank incorporated in Sri Lanka –</p> <p>(i) held by a company, an incorporated body, or an individual;</p> <p>(ii) held in the aggregate by—</p> <p style="margin-left: 40px;">(a) a company and one or more of the following:—</p> <p style="margin-left: 80px;">(aa) its subsidiaries</p> <p style="margin-left: 80px;">(bb) its holding company;</p> <p style="margin-left: 80px;">(cc) a subsidiary of its holding company; or</p> |

- (dd) a company in which such company or its subsidiary, or its holding company, or a subsidiary of its holding company has a substantial interest; or
- (b) an individual and one or more of the following :—
- (aa) his close relations;
- (bb) a company in which he has a substantial interest or in which his close relation has a substantial interest;
- (cc) the subsidiary of such company;
- (dd) a holding company of such company;
- (ee) a subsidiary of such company's holding company;
- (ff) a company in which such company, or its subsidiary, or its holding company or a subsidiary of its holding company has a substantial interest; or
- (gg) an incorporated body other than a company in which such individual or his close relation has a substantial interest; or
- (c) companies in each of which an individual or company as the case may be, has either directly, indirectly or beneficially a substantial interest or significant management interest.
- Empowerment under Section 12(1C)
3. (1) In terms of Section 12(1C)(a), an individual, partnership or corporate body shall not, either directly or indirectly or through a nominee or acting in concert with any other individual, partnership or corporate body, acquire a "material interest" in a licensed commercial bank incorporated or established within Sri Lanka by or under any written law without the prior written approval of the Monetary Board given with the concurrence of the Minister in charge of the subject of Finance.
- (2) In terms of Section 12(1C)(b), the Monetary Board is empowered to grant such approval subject to terms and conditions it may deem fit.
- (3) A "material interest" means the holding of over 10 per cent of the issued capital of a licensed commercial bank carrying voting rights.
- Maximum percentage of ownership of shares
4. Accordingly, the Monetary Board, subject to Sections 12(1B), 12(1C) and 13 and subject to terms and conditions it may deem fit, may grant permission on a case-by-case basis to any of the categories of shareholders referred to in Section 12(1C) and 46(1)(d) to acquire a material interest not exceeding 15 per cent of the issued capital carrying voting rights in a licensed commercial bank.
- Exceptions
5. Nevertheless, in the case of a licensed commercial bank which requires restructuring to avoid inadequacy of capital, insolvency or potential failure, such upper limit as specified in Direction 4 above may not be imposed, and the Monetary Board may grant permission to any of the categories of shareholders specified in Sections 12(1C) and 46(1)(d) to acquire a material interest in excess of 15 per cent of the issued capital carrying voting rights in the licensed commercial bank subject to the condition that the material interest so acquired shall be reduced to 15 per cent within a specified period as may be determined by the Monetary Board on a case-by-case basis, provided also that such period shall not exceed five years from the date of granting permission.
- Provisions in relation to existing ownership
6. (1) Any material interest previously acquired by any of the categories of shareholders referred to in Sections 12(1C) and 46(1)(d) in excess of 15 per cent of the issued capital carrying voting rights in a licensed commercial bank and held at the date of these Directions, shall be disposed of and/or otherwise reduced by such shareholders to a level not exceeding 15 per cent of the issued capital carrying voting rights in the licensed commercial bank.
- (2) Such disposal and/or reduction shall be carried out within the period as may be specified by the Monetary Board on a case-by-case basis, provided that such period shall not exceed five years from the date of stipulation.

- (3) In the event, any of the categories of shareholders referred to in Section 12(1C) and 46(1)(d) fails to comply with the directives of the Monetary Board within the stipulated period of time, the voting rights in excess of 10 per cent attributable to the ownership of shares held by the categories of shareholders subject to this Direction shall be deemed invalid with effect from the last date of the period specified by the Monetary Board to reduce the material interest.
- Transitional arrangements
7. (1) Within two months of the date of these Directions, each licensed commercial bank shall inform the Monetary Board of instances, if any, in its bank where the categories of shareholders referred to in Sections 12(1C) and 46(1)(d) own a material interest exceeding 15 per cent of the issued capital carrying voting rights in its bank and seek a Direction from the Monetary Board as to the period within which the disposal and/or reduction of the material interest to the level of 15 per cent shall be carried out.
- (2) Within two months of receipt of such information and request, the Monetary Board will specify the period within which the disposal and/or reduction should take place as per Direction 6(2) above and inform the licensed commercial bank accordingly.
- (3) Immediately thereafter, in terms of Section 46(3), the licensed commercial bank shall direct the shareholders who hold a material interest in its bank over the limits specified in these Directions to dispose of and/or reduce the number of shares carrying voting rights in order to comply with these Directions, within the period as stipulated by the Monetary Board.
- Steps to secure compliance
8. In terms of Section 12(1C)(c) and subject to Directions 6 and 7 above, a licensed commercial bank shall not enter in its register of members the name of any shareholder referred to in Sections 12(1C) and 46(1)(d) as the holder of shares of the bank, who or which has contravened the provisions of Section 12(1C) and/or these Directions.
- Non-application of Directions
9. Anything contained in these Directions shall not be construed to restrict the ownership of issued capital carrying voting rights in-
- (a) the Bank of Ceylon established under the Bank of Ceylon Ordinance No. 53 of 1938;
- (b) the People's Bank established under the People's Bank Act No.29 of 1961.
- (c) a licensed commercial bank established by a statute in which the ownership of a majority of the shares is held by the Government or a public corporation or a statutory body.
- Revocation of previous Directions
10. (1) The Banking Act Directions No.1 of 1998 (Share Capital Ownership) dated 22 October 1998 and Directions No.1 of 1999 (Share Capital Ownership) dated 5 March 1999 are hereby revoked.
- (2) The effect of revocation of previous Directions shall not affect any penalty or liability incurred under those Directions prior to the revocation.

Directions issued by the Monetary Board under Section 76J(1) of the Banking Act No.30 of 1988, as amended.

Nivard Ajith Leslie Cabraal
Governor

Colombo
19 January 2007

DIRECTIONS
BANKING ACT DIRECTIONS NO. 2 OF 2007
OWNERSHIP OF ISSUED CAPITAL CARRYING VOTING RIGHTS

In exercise of the powers conferred by Section 76J(1) of the Banking Act No. 30 of 1988, last amended by the Banking Act No.46 of 2006, the Monetary Board hereby issues Directions as follows:

Citation	1. These Directions may be cited as the Banking Act Directions No.2 of 2007. The Sections referred to in these Directions will be those of the Banking Act No. 30 of 1988, last amended by the Banking Act No. 46 of 2006.
Empowerment under Section 76J(1)	<p>2. In terms of Section 76J(1), the Monetary Board has been empowered to issue Directions to licensed specialised banks regarding the manner in which any aspect of the business of such banks is to be conducted, including Directions pertaining to the maximum percentage of the share capital in a licensed specialised bank incorporated in Sri Lanka –</p> <p>(i) held by a company, an incorporated body, or an individual;</p> <p>(ii) held in the aggregate by—</p> <p>(a) a company and one or more of the following:—</p> <p>(aa) its subsidiaries</p> <p>(bb) its holding company;</p> <p>(cc) a subsidiary of its holding company; or</p> <p>(dd) a company in which such company or its subsidiary, or its holding company, or a subsidiary of its holding company has a substantial interest; or</p> <p>(b) an individual and one or more of the following :—</p> <p>(aa) his close relations;</p> <p>(bb) a company in which he has a substantial interest or in which his close relation has a substantial interest;</p> <p>(cc) the subsidiary of such company;</p> <p>(dd) a holding company of such company;</p> <p>(ee) a subsidiary of such company's holding company;</p> <p>(ff) a company in which such company, or its subsidiary, or its holding company has a substantial interest; or</p> <p>(gg) an incorporated body other than a company in which such individual or his close relation has a substantial interest; or</p> <p>(c) companies in each of which an individual or company as the case may be, has either directly, indirectly or beneficially a substantial interest or significant management interest.</p>
Maximum percentage of ownership of shares	<p>3. (1) Any of the categories of shareholders referred to in Section 76J(1)(q) shall not, either directly or indirectly or through a nominee or acting in concert with any other category/categories of shareholders, hold shares carrying voting rights in excess of 15 per cent of the issued capital carrying voting rights in a licensed specialised bank incorporated or established within Sri Lanka by or under any written law without the prior written approval of the Monetary Board.</p> <p>(2) "Acting in concert" means acting pursuant to an understanding (whether formal or informal) to actively co-operate in acquiring or holding of over 15 per cent of the issued capital carrying voting rights of a licensed specialised bank so as to obtain or consolidate control of the bank.</p>
Exceptions	4. Nevertheless, in the case of a licensed specialised bank which requires restructuring to avoid inadequacy of capital, insolvency or potential failure, the Monetary Board may, subject to terms and conditions it may deem fit, grant permission to any of the categories of the shareholders specified in Section 76J(1)(q) to acquire or hold issued capital carrying voting rights in excess of 15 per cent in the licensed specialised bank subject to the condition that the issued capital so acquired shall be reduced to 15 per cent within a specified period as may be determined by the Monetary Board on a case-by-case basis, provided also that such period shall not exceed five years from the date of granting permission.

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| Provisions in relation to existing ownership | <p>5. (1) Any ownership of issued capital carrying voting rights previously acquired in excess of 15 per cent of the issued capital carrying voting rights in a licensed specialised bank by any of the categories of the shareholders referred to in Section 76J(1)(q) and held at the date of these Directions shall be disposed of and/or otherwise reduced by such shareholders to a level not exceeding 15 per cent of the issued capital carrying voting rights in the licensed specialised bank.</p> <p>(2) Such disposal and/or reduction shall be carried out within the period as may be specified by the Monetary Board on a case-by-case basis, provided that such period shall not exceed five years from the date of stipulation.</p> <p>(3) In the event, any of the categories of the shareholders referred to in Section 76J(1)(q) fails to comply with the directives of the Monetary Board within the stipulated period of time, the voting rights in excess of 15 per cent attributable to the ownership of shares held by the categories of shareholders subject to this Direction shall be deemed invalid with effect from the last date of the period specified by the Monetary Board to reduce the ownership of shares carrying voting rights.</p> |
| Transitional arrangements | <p>6. (1) Within two months of the date of these Directions, each licensed specialised bank shall inform the Monetary Board of instances, if any, in its bank where the categories of shareholders referred to in Section 76J(1)(q) own share capital carrying voting rights exceeding 15 per cent of the issued capital carrying voting rights in its banks and seek a Direction from the Monetary Board as to the period within which the disposal and/or reduction of the issued capital carrying voting rights to the level of 15 per cent shall be carried out.</p> <p>(2) Within two months of receipt of such information and request, the Monetary Board will specify the period within which the disposal and/or reduction should take place as per Direction 5(2) above and inform the licensed specialised bank accordingly.</p> <p>(3) Immediately thereafter, the licensed specialised bank shall direct the shareholders who hold issued capital carrying voting rights in its bank over the 15 per cent limit specified in these Directions to dispose of and/or reduce the number of shares carrying voting rights in order to comply with these Directions, within the period as stipulated by the Monetary Board.</p> |
| Steps to secure compliance | <p>7. Subject to Directions 5 and 6 above, a licensed specialised bank shall not enter in its register of members the name of any shareholder referred to in Section 76J(1)(q) as the holder of shares of the bank, who or which has contravened the provisions of these Directions.</p> |
| Non-application of Directions | <p>8. Anything contained in these Directions shall not be construed to restrict the ownership of issued capital carrying voting rights in -</p> <p>(a) Regional Development Banks established under Regional Development Banks Act No. 6 of 1997;</p> <p>(b) a licensed specialised bank established by a statute or under the Companies Act No. 17 of 1982 in which the ownership of a majority of the shares is held by the Government or a public corporation or a statutory body.</p> |
| Revocation of previous Direction | <p>9. (1) The Banking Act Directions No. 3 of 1999 (Share Capital Ownership - Licensed Specialised Banks) dated 23 November 1999 issued under Section 76J(1) are hereby revoked.</p> <p>(2) The effect of revocation of previous Directions shall not affect any penalty or liability incurred under those Directions prior to the revocation.</p> |

Directions issued by the Monetary Board of the Central Bank of Sri Lanka under Section 46(1) of the Banking Act No. 30 of 1988 as amended.

Nivard Ajith Leslie Cabraal
Governor

Colombo
20 February 2007

DIRECTIONS
BANKING ACT DIRECTIONS NO. 3 OF 2007
MAXIMUM AMOUNT OF ACCOMMODATION

In the exercise of the powers conferred by Section 46(1) of the Banking Act No. 30 of 1988, last amended by the Banking Act No. 46 of 2006, the Monetary Board hereby issues Directions as follows:

- | | |
|---|--|
| Citation | 1. These Directions may be cited as the Banking Act Directions No. 3 of 2007. The Sections referred to in these Directions will be those of the Banking Act No. 30 of 1988, last amended by the Banking Act No. 46 of 2006. |
| Empowerment under 46(1) | 2. In terms of Section 46(1), in order to ensure the soundness of the banking system, the Monetary Board has been empowered to issue Directions to licensed commercial banks regarding the manner in which any aspect of the business of such banks is to be conducted, including Directions pertaining to the maximum amount of accommodation which having regard to the equity capital, reserves and deposits of such licensed commercial bank and other relevant considerations, as may be made by such bank-
(i) to any single company, public corporation, firm, association of persons or an individual; or
(ii) in the aggregate to -
(a) an individual, his close relations or to a company or firm in which he has a substantial interest;
(b) a company and one or more of the following:-
(aa) its subsidiaries;
(bb) its holding company;
(cc) its associate company;
(dd) a subsidiary of its holding company; or
(ee) a company in which such company or its subsidiary, or its holding company, or a subsidiary of its holding company, has a substantial interest; |
| Maximum limits of accommodation to customers referred to in Sections 46(1)(c) and definitions | 3. (1) The maximum amount of accommodation that may be granted by a licensed commercial bank shall not exceed the following percentage of the capital base of the licensed commercial bank.
(a) 30 per cent in respect of customers referred to in Section 46(1)(c)(i).
(b) 33 per cent in respect of customers referred to in Section 46(1)(c)(ii).
(2) As defined and provided for in Section 86, accommodation shall mean any loan, overdraft or advance inclusive of finance lease, hire purchase and reverse repurchase agreements against debt securities, investments in debentures and other debt instruments and any commitment to grant any loan, overdraft or advance or such other facility including a commitment to accept a contingent liability.
(3) For purposes of this Direction,
(a) the amount of accommodation shall be deemed to be the total of the accommodation limits prevailing at any given time or the total outstanding amount of all accommodation, whichever is higher,
(b) the outstanding amount of accommodation in the case of a loan, overdraft or advance inclusive of finance lease, hire purchase and reverse repurchase agreements against debt securities, investments in debentures and other debt instruments shall be the capital outstanding, and |

- (c) the amount of accommodation granted in the form of commitments shall be the credit equivalent amount computed using the credit conversion factors applicable to such commitments in the computation of the Capital Adequacy Ratio under the Directions issued by the Monetary Board on the maintenance of the Capital Adequacy Ratio.
- (4) The capital base shall mean the capital base applicable to the computation of the Capital Adequacy Ratio under Directions issued by the Monetary Board on maintenance of the Capital Adequacy Ratio. The capital base as at the end of the immediately preceding quarter shall be the applicable value for the calculation of the limits for maximum amount of accommodation under these Directions and such capital base will have to be certified by the external auditors of the licensed commercial bank.

Enhanced limits of accommodation in aggregate to customers referred to in Section 46(1)(c)(ii)

4. (1) Notwithstanding the provisions of Direction 3(1)(b) above, a licensed commercial bank may grant accommodation in excess of 33 per cent of the capital base of the licensed commercial bank to customers referred to in Section 46(1)(c)(ii), on the basis of a sum of scores assigned for its own credit rating and Capital Adequacy Ratio and the credit rating of the holding company of the customers referred to in Section 46(1)(c)(ii). In the event the relationships within the companies in respect of whom accommodation shall be aggregated in terms of Section 46(1)(c)(ii) do not lead to a holding company, the credit ratings of each of the companies that comprise such aggregate shall be considered and the lowest credit rating assigned to any company within such aggregate shall be deemed to be the credit rating that shall be applicable for the purpose of giving effect to this Direction.
- (2) The scores referred to in Direction 4(1) above shall be assigned as follows.
- (3) The credit rating that shall be considered for the purpose of Directions 4(1) and 4(2) above shall be the credit rating obtained from a credit rating agency listed in the Annex 1 hereto

Bank's Credit Rating	Customers' Credit Rating	Bank's Capital Adequacy Ratio	Score Assigned for Each Column
AAA to AA- or equivalent	AAA to AA- or equivalent	> 12%	1
A+ to A- or equivalent	A+ to A- or equivalent	11% - 12%	2
BBB+ or equivalent and below	BBB+ or equivalent and below or unrated	10% - 11%	3

and shall be one that has been obtained within the past 15 months of providing accommodation at enhanced limits.

- (4) The Capital Adequacy Ratio referred to in Directions 4(1) and 4(2) above shall mean the Total Capital Adequacy Ratio computed as at the end of the immediately preceding quarter under the Directions issued by the Monetary Board on the maintenance of the Capital Adequacy Ratio and certified by the external auditors of the licensed commercial bank.
- (5) The maximum amount of accommodation that may be granted by a licensed commercial bank under Direction 4(1) above to customers referred to in Section 46(1)(c)(ii) shall not exceed the following percentages of the capital base of the licensed commercial bank, based upon the sum of the scores assigned for the three columns as per the Table set out in Direction 4(2) above.
- (a) 40 per cent if the sum of scores is between 3 and 5.
- (b) 36 per cent if the sum of scores is between 6 and 8.

Monetary Board to approve accommodation in excess of the specified limits

5. (1) Notwithstanding the provisions of Directions 3 and 4 above, a licensed commercial bank may grant accommodation in excess of the maximum limits specified under Directions 3 and 4 above to the categories of customers referred to in Sections 46(1)(c)(i) and 46(1)(c)(ii), provided that the prior approval of the Monetary Board has been sought and obtained. The

Monetary Board may grant such approval on a case-by-case basis, subject to terms and conditions it may deem fit, taking into consideration, inter-alia, instances of national priorities and/or national interest and the ability of the licensed commercial bank to withstand the potential risk arising from the exposure to such enhanced accommodation, provided that the assessment of risks arising out of such accommodation to the licensed commercial bank has been analysed in detail and such analysis is furnished by the licensed commercial bank to the Monetary Board when seeking approval of the Monetary Board.

- (2) Subject to Direction 5(1) above, a licensed commercial bank may grant accommodation to the categories of customers referred to in Sections 46(1)(c)(i) and 46(1)(c)(ii) up to 50 per cent of the capital base of the licensed commercial bank for the purpose of direct funding of infrastructure projects referred to in Annex 2 hereto for the commencement or expansion of the projects, provided that,
 - (a) the customer(s) has (have) been awarded a contract to directly engage in an infrastructure development project in Sri Lanka, and,
 - (b) such project is funded to the extent of at least 50 per cent by sources outside Sri Lanka or by a consortium of licensed banks excluding the bank providing the accommodation.

Exclusions from accommodation

6. The following accommodation shall be excluded from the amount of accommodation when computing the maximum amount of accommodation under Directions 3 and 4 above that may be granted to any category of customers referred to in Sections 46(1)(c)(i) and 46(1)(c)(ii).
 - (a) Accommodation granted against the security of cash, gold, Government Securities, Central Bank Securities, Treasury Guarantees, Central Bank Guarantees and Guarantees issued by the World Bank, the Asian Development Bank, International Development Association or any other international institution acceptable to the Monetary Board;
 - (b) Accommodation granted against the security of a guarantee or similar instrument acceptable to the Monetary Board issued by a bank incorporated within or outside Sri Lanka other than the bank granting accommodation, subject to the following:-
 - (i) The bank that provides the guarantee having a credit rating of AAA to A- or equivalent.
 - (ii) The amount of accommodation that shall be excluded from the computation of accommodation being 80 per cent in the event the credit rating of the bank that provides the guarantee is in the rank of AAA to AA- or equivalent and 50 per cent in the event the bank's credit rating is in the rank of A+ to A- or equivalent.
 - (iii) The aggregate amount of all accommodation that shall be excluded in respect of all such instances not exceeding 100 per cent of the capital base of the licensed commercial bank.
 - (iv) The licensed commercial bank being satisfied that the credit rating of the bank providing the guarantee has been obtained within 15 months of providing accommodation and the accommodation be revised immediately if there is any change in such credit rating.

Persons/
Institutions
exempted from
maximum limits

7. The maximum limits of accommodation specified in these Directions shall not apply to the following persons / institutions.
 - (a) The Government of Sri Lanka.
 - (b) The Ceylon Petroleum Corporation and the Ceylon Electricity Board for a maximum period of two years from the date of these Directions.
 - (c) Other licensed banks in respect of accommodation granted with a contractual maturity of less than two years.

Aggregate limit of
large
accommodation

8. (1) The sum total of the accommodation granted at any given time to the categories of customers referred to in Sections 46(1)(c)(i) and 46(1)(c)(ii) each of whose accommodation exceeds 15 per cent of the capital base of a licensed commercial bank, shall not exceed 55 per cent of the total outstanding accommodation granted by the licensed commercial bank as at the end of the immediately preceding quarter.

- (2) For purposes of this Direction,
- (a) the total outstanding accommodation shall include all outstanding accommodation as defined in Direction 3(3) above but exclude the accommodation referred to in Direction 7(a) above, and
 - (b) the sum total of the accommodation shall include accommodation as defined in Direction 3(3) above granted to all customers referred to in Direction 8(1) above but exclude the accommodation referred to in Direction 7(a) above.
- Review of Accommodation
9. (1) In instances where the accommodation granted to a customer has to be revised due to a reduction in the applicable accommodation limit, the accommodation granted shall be reduced at the next facility review date or within six months, whichever occurs earlier.
 - (2) In the event a merger or acquisition between any customers results in excesses over the applicable maximum amount of accommodation, the licensed commercial bank shall reduce the respective accommodation to the applicable limits within a period of six months from the date of such merger or acquisition.
- Transitional Arrangements
10. (1) In the event the accommodation that has been granted to any category of customers referred to in Sections 46(1)(c)(i) and 46(1)(c)(ii) as at the date of these Directions exceeds the limits specified in these Directions, the respective licensed commercial banks shall reduce such accommodation to be within the respective limits before the expiry of three months from the date of these Directions.
 - (2) Any accommodation granted by a licensed commercial bank incorporated outside Sri Lanka against a guarantee/indemnity from the Head Office in terms of Paragraph 6(1)(e)(ii) of the Banking Act (Single Borrower Limit) Directions No. 2 of 2005, as amended by the Banking Act (Single Borrower Limit) Directions No. 4 of 2005, shall continue till the end of the contracted period or 11 August 2007, whichever date occurs earlier.
- Steps to secure compliance with Directions
11. Where the Monetary Board has determined that a licensed commercial bank has contravened these Directions and the determination of such contravention has been conveyed to the licensed commercial bank, such licensed commercial bank shall not pay dividends or repatriate profits until the contravention is rectified and such rectification is confirmed by the Director of Bank Supervision.
- Revocation of Previous Directions
12. (1) The Banking Act (Single Borrower Limit) Directions No 2 of 2005 dated 7 March 2005 as amended by the Banking Act (Single Borrower Limit) Direction No. 4 of 2005 dated 11 August 2005 and the Circulars dated 27 October 2005, 28 June 2006 and 11 August 2006 are hereby revoked.
 - (2) The effect of revocation of previous Directions and Circulars shall not affect any penalty or liability incurred under those Directions prior to the revocation.

Annex I

DIRECTIONS
BANKING ACT DIRECTIONS NO. 3 OF 2007
MAXIMUM AMOUNT OF ACCOMMODATION
List of Credit Rating Agencies Acceptable to the Monetary Board

- 1) Fitch Ratings Lanka Ltd.
- 2) Lanka Ratings Agency Ltd.
- 3) Standard & Poors
- 4) Moody's Investors Service
- 5) Credit Rating Information Services of India (CRISIL)
- 6) Investment Information & Credit Rating Agency (ICRA)
- 7) Fitch Ratings India Ltd
- 8) Pakistan International Credit Rating Agency
- 9) Rating Agency Malaysia
- 10) Japan Credit Rating Agency Ltd
- 11) Any other credit rating agency as may be accepted by the Monetary Board from time to time

Annex 2

DIRECTIONS
BANKING ACT DIRECTIONS NO. 3 OF 2007
MAXIMUM AMOUNT OF ACCOMMODATION
Specification of Infrastructure Projects

Any project that involves in developing or operating and maintaining or developing, operating, upgrading and maintaining any infrastructure facility listed below shall qualify for the accommodation under the Direction 8(d) of the above Directions, provided that the accommodation referred to in the Direction shall be for the purpose of meeting direct cost of the project which shall not include repayment of any accommodation already granted by other banks or financial institutions or meeting the cost of purchase of a project already in operation.

- (i) a road, including toll road, a bridge or a rail system;
- (ii) a highway project including other activities being an integral part of the highway project;
- (iii) a port, airport, inland waterway or inland port;
- (iv) a water supply project, irrigation project, water treatment system, sanitation and sewerage system or solid waste management system;
- (v) telecommunication services whether basic or cellular, including radio paging, network of trunking, network and internet services;
- (vi) an industrial park or special economic zone;
- (vii) generation or generation and distribution of power;
- (viii) transmission or distribution of power by laying a network of new transmission or distribution lines;
- (ix) construction relating to projects involving agro-processing and supply of inputs to agriculture;
- (x) construction of educational institutions and hospitals;
- (xi) any other infrastructure project as may be specified by the Monetary Board from time to time.

Directions issued by the Monetary Board of the Central Bank of Sri Lanka under Section 76J(1) of the Banking Act No. 30 of 1988 as amended.

Nivard Ajith Leslie Cabraal
Governor

Colombo
20 February 2007

DIRECTIONS
BANKING ACT DIRECTIONS NO. 4 OF 2007
MAXIMUM AMOUNT OF ACCOMMODATION

In the exercise of the powers conferred by Section 76J(1) of the Banking Act No. 30 of 1988, last amended by the Banking Act No.46 of 2006, the Monetary Board hereby issues Directions as follows:

- | | |
|--------------------------|---|
| Citation | 1. These Directions may be cited as the Banking Act Directions No.4 of 2007. The Sections referred to in these Directions will be those of the Banking Act No. 30 of 1988, last amended by the Banking Act No. 46 of 2006. |
| Empowerment under 76J(1) | 2. In terms of Section 76J(1), the Monetary Board has been empowered to give Directions to licensed specialised banks or to any category of licensed specialised banks regarding the manner in which any aspect of the business of such banks is to be conducted. Accordingly, the Monetary Board hereby gives Directions to licensed specialised banks pertaining to the maximum amount of accommodation as may be made by such banks- <ul style="list-style-type: none"> (i) to any single company, public corporation, firm, association of persons or an individual; or (ii) in the aggregate to- <ul style="list-style-type: none"> (a) an individual, his close relations or to a company or firm in which he has a substantial interest; (b) a company and one or more of the following:- (aa) its subsidiaries; |

- (bb) its holding company;
- (cc) its associate company;
- (dd) a subsidiary of its holding company; or
- (ee) a company in which such company or its subsidiary, or its holding company, or a subsidiary of its holding company, has a substantial interest;

Maximum limits of accommodation to customers referred to in paragraphs 2(i) and 2(ii) above and definitions

3. (1) The maximum amount of accommodation that may be granted by a licensed specialised bank shall not exceed the following percentage of the capital base of the licensed specialised bank.
 - (a) 30 per cent in respect of customers referred to in paragraph 2(i) above.
 - (b) 33 per cent in respect of customers referred to in paragraph 2(ii) above.
- (2) As defined and provided for in Section 86, accommodation shall mean any loan, overdraft or advance inclusive of finance lease, hire purchase and reverse repurchase agreements against debt securities, investments in debentures and other debt instruments and any commitment to grant any loan, overdraft or advance or such other facility including a commitment to accept a contingent liability.
- (3) For purposes of this Direction,
 - (a) the amount of accommodation shall be deemed to be the total of the accommodation limits prevailing at any given time or the total outstanding amount of all accommodation, whichever is higher,
 - (b) the outstanding amount of accommodation in the case of a loan, overdraft or advance inclusive of finance lease, hire purchase and reverse repurchase agreements against debt securities, investments in debentures and other debt instruments shall be the capital outstanding, and
 - (c) the amount of accommodation granted in the form of commitments shall be the credit equivalent amount computed using the credit conversion factors applicable to such commitments in the computation of the Capital Adequacy Ratio under the Directions issued by the Monetary Board on the maintenance of the Capital Adequacy Ratio.
- (4) The capital base shall mean the capital base applicable to the computation of the Capital Adequacy Ratio under Directions issued by the Monetary Board on maintenance of the Capital Adequacy Ratio. The capital base as at the end of the immediately preceding quarter shall be the applicable value for the calculation of the limits for maximum amount of accommodation under these Directions and such capital base will have to be certified by the external auditors of the licensed specialised bank.

Enhanced limits of accommodation in aggregate to customers referred to in paragraph 2(ii) above

4. (1) Notwithstanding the provisions of Direction 3(1)(b) above, a licensed specialised bank may grant accommodation in excess of 33 per cent of the capital base of the licensed specialised bank to customers referred to in paragraph 2(ii) above, on the basis of a sum of scores assigned for its own credit rating and Capital Adequacy Ratio and the credit rating of the holding company of the customers referred to in paragraph 2(ii) above. In the event the relationships within the companies in respect of whom accommodation shall be aggregated in terms of paragraph 2(ii) above do not lead to a holding company, the credit ratings of each of the companies that comprise such aggregate shall be considered and the lowest credit rating assigned to any company within such aggregate shall be deemed to be the credit rating that shall be applicable for the purpose of giving effect to this Direction.

- (2) The scores referred to in Direction 4(1) above shall be assigned as follows.

Bank's Credit Rating	Customers' Credit Rating	Bank's Capital Adequacy Ratio	Score Assigned for Each Column
AAA to AA- or equivalent	AAA to AA- or equivalent	> 12%	1
A+ to A- or equivalent	A+ to A- or equivalent	11% - 12%	2
BBB+ or equivalent and below	BBB+ or equivalent and below or unrated	10% - 11%	3

- (3) The credit rating that shall be considered for the purpose of Directions 4(1) and 4(2) above shall be the credit rating obtained from a credit rating agency listed in the Annex 1 hereto and shall be one that has been obtained within the past 15 months of providing accommodation at enhanced limits.
- (4) The Capital Adequacy Ratio referred to in Directions 4(1) and 4(2) above shall mean the Total Capital Adequacy Ratio computed as at the end of the immediately preceding quarter under the Directions issued by the Monetary Board on the maintenance of the Capital Adequacy Ratio and certified by the external auditors of the licensed specialised bank.
- (5) The maximum amount of accommodation that may be granted by a licensed specialised bank under Direction 4(1) above to customers referred to in paragraph 2(ii) above shall not exceed the following percentages of the capital base of the licensed specialised bank, based upon the sum of the scores assigned for the three columns as per the Table set out in Direction 4(2) above.
- (a). 40 per cent if the sum of scores is between 3 and 5.
- (b). 36 per cent if the sum of scores is between 6 and 8.

Monetary Board to approve accommodation in excess of the specified limits

5. (1) Notwithstanding the provisions of Directions 3 and 4 above, a licensed specialised bank may grant accommodation in excess of the maximum limits specified under Directions 3 and 4 above to the categories of customers referred to in paragraphs 2(i) and 2(ii) above, provided that the prior approval of the Monetary Board has been sought and obtained. The Monetary Board may grant such approval on a case-by-case basis, subject to terms and conditions it may deem fit, taking into consideration, inter-alia, instances of national priorities and/or national interest and the ability of the licensed specialised bank to withstand the potential risk arising from the exposure to such enhanced accommodation, provided that the assessment of risks arising out of such accommodation to the licensed specialised bank has been analysed in detail and such analysis is furnished by the licensed specialised bank to the Monetary Board when seeking approval of the Monetary Board.
- (2) Subject to Direction 5(1) above, a licensed specialised bank may grant accommodation to the categories of customers referred to in paragraphs 2(i) and 2(ii) above up to 50 per cent of the capital base of the licensed specialised bank for the purpose of direct funding of infrastructure projects referred to in Annex 2 hereto for the commencement or expansion of the projects, provided that,
- (a) the customer(s) has (have) been awarded a contract to directly engage in an infrastructure development project in Sri Lanka, and,
- (b) such project is funded to the extent of at least 50 per cent by sources outside Sri Lanka or by a consortium of licensed banks excluding the bank providing the accommodation.

Exclusions from accommodation

6. The following accommodation shall be excluded from the amount of accommodation when computing the maximum amount of accommodation under Directions 3 and 4 above that may be granted to any category of customers referred to in paragraphs 2(i) and 2(ii) above.

- (a) Accommodation granted against the security of cash, gold, Government Securities, Central Bank Securities, Treasury Guarantees, Central Bank Guarantees and Guarantees issued by the World Bank, the Asian Development Bank, International Development Association or any other international institution acceptable to the Monetary Board;
 - (b) Accommodation granted against the security of a guarantee or similar instrument acceptable to the Monetary Board issued by a bank incorporated within or outside Sri Lanka other than the bank granting accommodation, subject to the following:-
 - (i) The bank that provides the guarantee having a credit rating of AAA to A- or equivalent.
 - (ii) The amount of accommodation that shall be excluded from the computation of accommodation being 80 per cent in the event the credit rating of the bank that provides the guarantee is in the rank of AAA to AA- or equivalent and 50 per cent in the event the bank's credit rating is in the rank of A+ to A- or equivalent.
 - (iii) The aggregate amount of all accommodation that shall be excluded in respect of all such instances not exceeding 100 per cent of the capital base of the licensed specialised bank.
 - (iv) The licensed specialised bank being satisfied that the credit rating of the bank providing the guarantee has been obtained within 15 months of providing accommodation and the accommodation be revised immediately if there is any change in such credit rating.
- Persons/
Institutions
exempted from
maximum limits
7. The maximum limits of accommodation specified in these Directions shall not apply to the following persons / institutions.
- (a) The Government of Sri Lanka.
 - (b) The Ceylon Petroleum Corporation and the Ceylon Electricity Board for a maximum period of two years from the date of these Directions.
 - (c) Other licensed banks in respect of accommodation granted with a contractual maturity of less than two years.
- Aggregate limit
of large
accommodation
8. (1) The sum total of the accommodation granted at any given time to the categories of customers referred to in paragraphs 2(i) and 2(ii) above each of whose accommodation exceeds 15 per cent of the capital base of a licensed specialised bank, shall not exceed 55 per cent of the total outstanding accommodation granted by the licensed specialised bank as at the end of the immediately preceding quarter.
- (2) For purposes of this Direction,
- (a) the total outstanding accommodation shall include all outstanding accommodation as defined in Direction 3(3) above but exclude the accommodation referred to in Direction 7(a) above, and
 - (b) the sum total of the accommodation shall include accommodations as defined in Direction 3(3) above granted to all customers referred to in Direction 8(1) above but exclude the accommodation referred to in Direction 7(a) above.
- Review of
Accommodation
9. (1) In instances where the accommodation granted to a customer has to be revised due to a reduction in the applicable accommodation limit, the accommodation granted shall be reduced at the next facility review date or within six months, whichever occurs earlier.
- (2) In the event a merger or acquisition between any customers results in excesses over the applicable maximum amount of accommodation, the licensed specialised bank shall reduce the respective accommodation to the applicable limits within a period of six months from the date of such merger or acquisition.
- Transitional
Arrangements
10. In the event the accommodation that has been granted to any category of customers referred to in paragraphs 2(i) and 2(ii) above as at the date of these Directions exceeds the limits specified in these Directions, the respective licensed specialised banks shall reduce such accommodation to be within the respective limits before the expiry of three months from the date of these Directions.

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| Steps to secure compliance with Directions | 11. Where the Monetary Board has determined that a licensed specialised bank has contravened these Directions and the determination of such contravention has been conveyed to the licensed specialised bank, such licensed specialised bank shall not pay dividends until the contravention is rectified and such rectification is confirmed by the Director of Bank Supervision. |
| Revocation of Previous Directions | 12. (1) The Banking Act (Single Borrower Limit) Directions No. 3 of 2005 dated 7 March 2005 as amended by the Banking Act (Single Borrower Limit) Directions No. 5 of 2005 dated 11 August 2005 and the Circulars dated 27 October 2005 and 28 June 2006 are hereby revoked.
(2) The effect of revocation of previous Directions and Circulars shall not affect any penalty or liability incurred under those Directions prior to the revocation |

Annex 1

DIRECTIONS
BANKING ACT DIRECTIONS NO. 4 OF 2007
MAXIMUM AMOUNT OF ACCOMMODATION
List of Credit Rating Agencies Acceptable to the Monetary Board

- 1) Fitch Ratings Lanka Ltd.
- 2) Lanka Ratings Agency Ltd.
- 3) Standard & Poors
- 4) Moody's Investors Service
- 5) Credit Rating Information Services of India (CRISIL)
- 6) Investment Information & Credit Rating Agency (ICRA)
- 7) Fitch Ratings India Ltd
- 8) Pakistan International Credit Rating Agency
- 9) Rating Agency Malaysia
- 10) Japan Credit Rating Agency Ltd
- 11) Any other credit rating agency as may be accepted by the Monetary Board from time to time

Annex 2

DIRECTIONS
BANKING ACT DIRECTIONS NO. 4 OF 2007
MAXIMUM AMOUNT OF ACCOMMODATION
Specification of Infrastructure Projects

Any project that involves in developing or operating and maintaining or developing, operating, upgrading and maintaining any infrastructure facility listed below shall qualify for the accommodation under the Direction 8(d) of the above Directions, provided that the accommodation referred to in the Direction shall be for the purpose of meeting direct cost of the project which shall not include repayment of any accommodation already granted by other banks or financial institutions or meeting the cost of purchase of a project already in operation.

- (i) a road, including toll road, a bridge or a rail system;
- (ii) a highway project including other activities being an integral part of the highway project;
- (iii) a port, airport, inland waterway or inland port;
- (iv) a water supply project, irrigation project, water treatment system, sanitation and sewerage system or solid waste management system;
- (v) telecommunication services whether basic or cellular, including radio paging, network of trunking, network and internet services;
- (vi) an industrial park or special economic zone;
- (vii) generation or generation and distribution of power;
- (viii) transmission or distribution of power by laying a network of new transmission or distribution lines;
- (ix) construction relating to projects involving agro-processing and supply of inputs to agriculture;
- (x) construction of educational institutions and hospitals;
- (xi) any other infrastructure project as may be specified by the Monetary Board from time to time.

Directions issued by the Monetary Board of the Central Bank of Sri Lanka under Section 19(7) of the Banking Act No. 30 of 1988, last amended by the Banking Act No.46 of 2006.

Nivard Ajith Leslie Cabraal
Governor

Colombo
23 May 2007

DIRECTIONS
BANKING ACT DIRECTIONS NO. 5 OF 2007
MAINTENANCE OF CAPITAL ADEQUACY RATIO

In the exercise of the powers conferred by Sections 19(7) of the Banking Act No. 30 of 1988, last amended by the Banking Act No.46 of 2006, the Monetary Board hereby issues the following Directions to amend the Schedule I of the Determination dated 22 August 1997 and the Notice dated 27 December 2001 issued by the Monetary Board relating to the maintenance of capital adequacy ratio by licensed commercial banks.

1. Insert a new item “34.A Approved Perpetual Debt Capital Instruments” immediately after item 34 in Form 3 of Section B.
2. Insert the following item immediately after item 34 in Section C.
34A. Approved Perpetual Debt Capital Instruments
Perpetual debt instruments that satisfy the following conditions:
 - (i) The prior written approval of the Central Bank of Sri Lanka has been obtained;
 - (ii) Such instruments shall have no maturity;
 - (iii) Unsecured, fully paid up and subordinated to the interest of creditors;
 - (iv) The perpetual debt capital instruments should contain a clause that the issuing bank shall not be liable to pay interest, if:
 - (a) The bank’s Capital Adequacy Ratio (CAR) is below the minimum regulatory requirement in terms of the Directions on CAR; or
 - (b) The impact of such payment results in the bank’s CAR falling below the minimum CAR; and
 - (c) Such interest not paid shall not be cumulative or accrued for payment in the future.
 - (v) Such instruments may contain a call option which may be exercised in 10 years from the date of issue, provided that the prior approval of the Central Bank of Sri Lanka has been obtained to exercise such option;
 - (vi) Total perpetual debt approved as Tier I capital shall not exceed 15% of the total Tier I capital;
 - (vii) Any other conditions stipulated by the Central Bank of Sri Lanka on prudential grounds.
3. Repeal item 40 of Section C by replacing with the following item:
40. Hybrid (Debt /Equity) Capital Instruments
Capital instruments which combine certain characteristics of equity capital and debt, i.e., non-redeemable preference shares, cumulative redeemable preference shares, etc. and satisfy the following characteristics:
 - (i) The prior written approval of the Central Bank of Sri Lanka has been obtained;
 - (ii) Unsecured, fully paid up and subordinated to the interest of creditors;
 - (iii) Not redeemable in less than 5 years or without the prior approval of the Central Bank of Sri Lanka;
 - (iv) Available to participate in losses without the bank being obliged to cease trading;
 - (v) Obligation to pay interest that can be deferred where the profitability of the bank would not support such payment;
 - (vi) Any other conditions stipulated by the Central Bank of Sri Lanka on prudential grounds.
4. Repeal item 42 of Section C and replace with the following item:
42. Approved Subordinated Term Debt
Subordinated term debt that satisfies the following conditions:
 - (i) The prior written approval of the Central Bank of Sri Lanka has been obtained for inclusion as Tier II capital ;
 - (ii) Unsecured and subordinated to the interest of creditors, at fully paid up value in the case of coupon bonds or paid up value plus accrued interest in the case of zero coupon bonds;

- (iii) A minimum original maturity of 5 years;
- (iv) Early repayment or redemption shall not be made without the prior consent of the Central Bank of Sri Lanka;
- (v) The amount counted as capital should be discounted by 1/5th each year during the 4 years preceding maturity;
- (vi) The total approved subordinated term debt should not exceed 50% of total Tier I capital;
- (vii) Any other conditions stipulated by the Central Bank of Sri Lanka on prudential grounds.

Directions issued by the Monetary Board of the Central Bank of Sri Lanka under Section 76J(1) of the Banking Act No. 30 of 1988, last amended by the Banking Act No.46 of 2006.

Nivard Ajith Leslie Cabraal
Governor

Colombo
23 May 2007

DIRECTIONS

BANKING ACT DIRECTIONS NO. 6 OF 2007

MAINTENANCE OF CAPITAL ADEQUACY RATIO

In the exercise of the powers conferred by Sections 76J(1) of the Banking Act No. 30 of 1988, last amended by the Banking Act No.46 of 2006, the Monetary Board hereby issues the following Directions to amend the Schedule I of the Directions dated 27 December 2001 issued by the Monetary Board relating to the maintenance of capital adequacy ratio by licensed specialised banks.

1. Insert a new item “32.A Approved Perpetual Debt Capital Instruments” immediately after item 32 in Form 3 of Section B.
2. Insert the following item immediately after item 32 in Section C.
32A. Approved Perpetual Debt Capital Instruments
Perpetual debt instruments that satisfy the following conditions:
 - (i) The prior written approval of the Central Bank of Sri Lanka has been obtained;
 - (ii) Such instruments shall have no maturity ;
 - (iii) Unsecured, fully paid up and subordinated to the interest of creditors;
 - (iv) The perpetual debt capital instruments should contain a clause that the issuing bank shall not be liable to pay interest, if:
 - (a) The bank’s Capital Adequacy Ratio (CAR) is below the minimum regulatory requirement in terms of the Directions on CAR; or
 - (b) The impact of such payment results in bank’s CAR falling below the minimum CAR and
 - (c) Such interest not paid shall not be cumulative or accrued for payment in the future;
 - (v) Such instruments may contain a call option which may be exercised in 10 years from the date of issue, provided that the prior approval of the Central Bank of Sri Lanka has been obtained to exercise such option;
 - (vi) Total perpetual debt approved as Tier I capital shall not exceed 15% of the total Tier I capital;
 - (vii) Any other conditions stipulated by the Central Bank of Sri Lanka on prudential grounds.
3. Repeal item 38 of Section C by replacing with the following item:
38. Hybrid (Debt /Equity) Capital Instruments
Capital instruments which combine certain characteristics of equity capital and debt, i.e., non-redeemable preference shares, cumulative redeemable preference shares, etc. and satisfy the following characteristics:
 - (i) The prior written approval of the Central Bank of Sri Lanka has been obtained;
 - (ii) Unsecured, fully paid up and subordinated to the interest of creditors;
 - (iii) Not redeemable in less than 5 years or without the prior approval of the Central Bank of Sri Lanka;
 - (iv) Available to participate in losses without the bank being obliged to cease trading;
 - (v) Obligation to pay interest that can be deferred where the profitability of the bank would not support such payment;
 - (vi) Any other conditions stipulated by the Central Bank of Sri Lanka on prudential grounds.

4. Repeal item 40 of Section C and replace with the following item:

40. Approved Subordinated Term Debt

Subordinated term debt that satisfies the following conditions:

- (i) The prior written approval of the Central Bank of Sri Lanka has been obtained for inclusion as Tier II capital ;
- (ii) Unsecured and subordinated to the interest of creditors, at fully paid up value in the case of coupon bonds or paid up value plus accrued interest in the case of zero coupon bonds;
- (iii) A minimum original maturity of 5 years;
- (iv) Early repayment or redemption shall not be made without the prior consent of the Central Bank of Sri Lanka;
- (v) The amount counted as capital should be discounted by 1/5th each year during the 4 years preceding maturity;
- (vi) The total approved subordinated term debt should not exceed 50% of total Tier I capital;
- (vii) Any other conditions stipulated by the Central Bank of Sri Lanka on prudential grounds.

Directions issued by the Monetary Board of the Central Bank of Sri Lanka under Section 46(1) of the Banking Act No. 30 of 1988 as amended.

Nivard Ajith Leslie Cabraal
Governor

Colombo
01st November 2007

DIRECTIONS

BANKING ACT DIRECTIONS NO. 7 OF 2007

MAXIMUM AMOUNT OF ACCOMMODATION

In the exercise of the powers conferred by Section 46(1) of the Banking Act No. 30 of 1988, last amended by the Banking Act No.46 of 2006, the Monetary Board hereby issues Directions as follows:

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|---|---|
| Citation | 1. These Directions may be cited as the Banking Act Directions No.7 of 2007. The Sections referred to in these Directions will be those of the Banking Act No. 30 of 1988, last amended by the Banking Act No. 46 of 2006. |
| Empowerment under 76J(1) | <p>2. In terms of Section 46(1), the Monetary Board has been empowered to give Directions to licensed commercial banks or to any category of licensed commercial banks regarding the manner in which any aspect of the business of such banks is to be conducted. Accordingly, the Monetary Board hereby gives Directions to licensed commercial banks pertaining to the maximum amount of accommodation as may be made by such banks-</p> <ul style="list-style-type: none"> (i) to any single company, public corporation, firm, association of persons or an individual; or (ii) in the aggregate to- <ul style="list-style-type: none"> (a) an individual, his close relations or to a company or firm in which he has a substantial interest; (b) a company and one or more of the following:- <ul style="list-style-type: none"> (aa) its subsidiaries; (bb) its holding company; (cc) its associate company; (dd) a subsidiary of its holding company; or (ee) a company in which such company or its subsidiary, or its holding company, or a subsidiary of its holding company, has a substantial interest; |
| Maximum limits of accommodation to customers referred to in paragraphs 2(i) and 2(ii) above | <p>3. The maximum amount of accommodation that may be granted by a licensed commercial bank shall not exceed the following percentage of the capital base of the licensed commercial bank subject to the Directions 7, 8 and 9.</p> <ul style="list-style-type: none"> (i) 30 per cent in respect of customers referred to in paragraph 2(i) above. (ii) 33 per cent in respect of customers referred to in paragraph 2(ii) above. |

Enhanced limits of accommodation in aggregate to customers referred to in paragraph 2(ii) above

4. (1) Notwithstanding the provisions of Direction 3(ii) above, a licensed commercial bank may grant accommodation in excess of 33 per cent of the capital base of the licensed commercial bank to customers referred to in paragraph 2(ii) above, on the basis of a sum of scores assigned for the following as determined in Direction 4(2) below.
- (i) The Credit Rating and Capital Adequacy Ratio of the bank granting accommodation and,
- (ii) The Credit Rating of the holding company of the customers referred to in paragraph 2(ii) above. In the event the relationships within the companies in respect of whom accommodation shall be aggregated in terms of paragraph 2(ii) above do not lead to a holding company, the credit ratings of each of the companies that comprise such aggregate shall be considered and the lowest credit rating assigned to any company within such aggregate shall be deemed to be the credit rating that shall be applicable for the purpose of giving effect to this Direction.
- (2) The scores referred to in Direction 4(1) above shall be assigned as follows.

Bank's Credit Rating	Customers' Credit Rating	Bank's Capital Adequacy Ratio	Score Assigned for Each Column
AAA to AA- or equivalent	AAA to AA- or equivalent	> 12%	1
A+ to A- or equivalent	A+ to A- or equivalent	11% - 12%	2
BBB+ or equivalent and below	BBB+ or equivalent and below or unrated	10% - 11%	3

- (3) The maximum amount of accommodation that may be granted by a licensed commercial bank under Direction 4(1) above to customers referred to in paragraph 2(ii) above shall not exceed the following percentages of the capital base of the licensed commercial bank, based upon the sum of the scores assigned for the three columns as per the Table set out in Direction 4(2) above.
- (i) 40 per cent if the sum of scores is between 3 and 5.
- (ii) 36 per cent if the sum of scores is between 6 and 8.

Aggregate limit of large accommodation

5. In the case of amount of accommodations granted as at any given date to any category of customers referred to in paragraphs 2(i) and 2(ii) above excluding the Government of Sri Lanka in excess of 15 per cent of the capital base of the licensed commercial bank, the sum total of the outstanding amount of accommodation granted to such customers shall not exceed 55 per cent of the total outstanding amount of accommodation granted by the licensed commercial bank to all customers excluding the Government of Sri Lanka as at the end of the immediately preceding month.

Monetary Board to approve accommodation in excess of the specified limits

6. (1) Notwithstanding the provisions of Directions 3 and 4 above, a licensed commercial bank may grant accommodation in excess of the maximum limits specified under Directions 3 and 4 above to the categories of customers referred to in paragraphs 2(i) and 2(ii) above, provided that the prior approval of the Monetary Board has been sought and obtained. The Monetary Board may grant such approval on a case-by-case basis, subject to terms and conditions it may deem fit, taking into consideration, inter-alia, instances of national priorities and/or national interest and the ability of the licensed commercial bank to withstand the potential risk arising from the exposure to such enhanced accommodation, provided that the assessment of risks arising out of such accommodation to the licensed commercial bank has been analysed in detail and such analysis is furnished by the licensed commercial bank to the Monetary Board when seeking approval of the Monetary Board.
- (2) Subject to Direction 6(1) above, a licensed commercial bank may grant accommodation to the categories of customers referred to in paragraphs 2(i) and 2(ii) above up to 50 per cent of the capital base of the licensed commercial bank for the purpose of direct funding of infrastructure projects referred to in Annex 1 hereto for the commencement or expansion of the projects, provided that,

- (i) the customer(s) has (have) been awarded a contract to directly engage in an infrastructure development project in Sri Lanka, and,
 - (ii) such project is funded to the extent of at least 50 per cent by sources outside Sri Lanka or by a consortium of licensed banks excluding the bank providing the accommodation.

- Exclusions from accommodations from maximum limits under Directions 3 and 4
 - 7. When computing the maximum amount of accommodation under Directions 3 and 4 above that may be granted to any category of customers referred to in paragraphs 2(i) and 2(ii) above, the following accommodations shall be excluded.
 - (i) Accommodation granted against the security of cash, gold, Government Securities, Central Bank Securities, Treasury Guarantees, Central Bank Guarantees and Guarantees issued by the World Bank, the Asian Development Bank, International Development Association or any other international institution acceptable to the Director of Bank Supervision.
 - (ii) Accommodation granted against the security of a guarantee or similar instrument Director of Bank Supervision issued by a bank incorporated within or outside Sri Lanka other than the bank granting accommodation, subject to the following:-
 - (a) The bank that provides the guarantee having a credit rating of AAA to A- or equivalent.
 - (b) The amount of accommodation that shall be excluded from the computation of accommodation being 80 per cent in the event the credit rating of the bank that provides the guarantee is in the rank of AAA to AA- or equivalent and 50 per cent in the event the bank's credit rating is in the rank of A+ to A- or equivalent.
 - (c) The aggregate amount of all accommodation that shall be excluded in respect of all such instances not exceeding 100 per cent of the capital base of the licensed commercial bank.
 - (d) The licensed commercial bank being satisfied that the credit rating of the bank providing the guarantee has been obtained within 15 months of providing accommodation and the accommodation be revised immediately if there is any change in such credit rating.

- Persons/ Institutions exempted from maximum limits under Directions 3 and 4
 - 8. The maximum limits of accommodation specified in these Directions shall not apply to the following persons / institutions.
 - (i) The Government of Sri Lanka.
 - (ii) The Ceylon Petroleum Corporation and the Ceylon Electricity Board for a maximum period of two years from the date of these Directions.
 - (iii) Other licensed banks in respect of accommodation granted with a contractual maturity of less than two years.

- Definition
 - 9. The following definitions shall be applicable for the purposes of these Directions.
 - (i) Accommodations: As defined and provided for in Section 86 of the Banking Act, accommodations shall mean credit exposure and investment exposure as specified below.
 - (a) Credit exposure shall include all on-balance sheet accommodations such as any loan, overdraft or advance inclusive of finance lease, hire purchase and reverse repurchase agreements against debt securities and all off-balance sheet accommodations such as any commitment to grant any loan, overdraft or advance or such other facility including a commitment to accept a contingent liability.
 - (b) Investments exposure shall include all financial investments excluding investments in equity (only ordinary shares)
 - (ii) Amount of accommodations: The amount of accommodations shall be the total of on-balance sheet accommodations and off-balance sheet accommodations.
 - (a) Amount of on-balance sheet accommodations: The amount of on-balance sheet accommodations shall mean the total of the accommodation limits prevailing at any given time or the total outstanding amount of all accommodations, whichever is higher. In the case of fully drawn term loans, the outstanding amount of accommodations shall be reckoned as the amount of accommodations.
 - (b) Amount of off-balance sheet accommodations: The amount of off-balance sheet accommodations shall mean the credit equivalent amount of total of the accommodation limits prevailing at any given time or the outstanding amount of accommodations, whichever is higher.

- (iii) Outstanding amount of accommodations: The outstanding amount of accommodations shall be the total of outstanding on-balance sheet accommodations and outstanding off-balance sheet accommodations
 - (a) Outstanding on-balance sheet accommodations: The outstanding amount of on-balance sheet accommodations shall be the capital outstanding.
 - (b) Outstanding off-balance sheet accommodations: The outstanding amount of off-balance sheet accommodations shall be the credit equivalent amount of the outstanding off-balance sheet accommodations.
 - (iv) Credit equivalent amount of off-balance sheet accommodations: The credit equivalent amount computed using the credit conversion factors applicable to off-balance sheet accommodations in the computation of the Capital Adequacy Ratio shall be applicable.
 - (v) Capital Base and Capital Adequacy Ratio: Capital Base and Capital Adequacy Ratio appearing in the computation of the Capital Adequacy Ratio shall be applicable, provided that those shall be as at end of the preceding financial year or immediately preceding quarter or other latest quarter preceding the applicable quarter, whichever is available, subject to certification by the licensed commercial bank's external auditor.
 - (vi) Credit Rating: The credit rating shall be the credit rating obtained from a credit rating agency listed in the Annex 2 hereto and shall be one that has been obtained within the past 15 months of providing accommodation.
- Review of Accommodation 10. (1) In instances where the accommodation granted to a customer has to be revised due to a reduction in the applicable accommodation limit, the accommodation granted shall be reduced at the next facility review date or within six months, whichever occurs earlier.
- (2) In the event a merger or acquisition between any institutional customers results in existing accommodations exceeding the applicable maximum limits, the licensed commercial bank shall reduce such accommodations to be within the applicable maximum limits before expiry of six months from the date of such merger or acquisition.
- Transitional Arrangements 11. In the event the accommodation that has been granted to any category of customers referred to in paragraphs 2(i) and 2(ii) above as at the date of these Directions exceeds the limits, i.e., maximum limits or aggregate limit, specified in these Directions, the licensed commercial bank shall reduce such accommodation to be within the respective limits before the expiry of three months from the date of these Directions.
- Steps to secure compliance with Directions 12. Where the Monetary Board has determined that a licensed commercial bank has contravened these Directions and the determination of such contravention has been conveyed to the licensed commercial bank, such licensed commercial bank shall not pay dividends or repatriate profits until the contravention is rectified and such rectification is confirmed by the Director of Bank Supervision.
- Revocation of Previous Directions 13. The Banking Act Directions No. 3 of 2007 dated 20 February 2007 of Maximum Amount of Accommodation is hereby revoked.

*Annex 1***DIRECTIONS****BANKING ACT DIRECTIONS NO. 7 OF 2007****MAXIMUM AMOUNT OF ACCOMMODATION****Specification of Infrastructure Projects**

Any project that involves in developing or operating and maintaining or developing, operating, upgrading and maintaining any infrastructure facility listed below shall qualify for the accommodation under the Direction 6(2) of the above Directions, provided that the accommodation referred to in the Direction shall be for the purpose of meeting direct cost of the project which shall not include repayment of any accommodation already granted by other banks or financial institutions or meeting the cost of purchase of a project already in operation.

- (i) a road, including toll road, a bridge or a rail system;
- (ii) a highway project including other activities being an integral part of the highway project;
- (iii) a port, airport, inland waterway or inland port;

- (iv) a water supply project, irrigation project, water treatment system, sanitation and sewerage system or solid waste management system;
- (v) telecommunication services whether basic or cellular, including radio paging, network of trunking, network and internet services;
- (vi) an industrial park or special economic zone;
- (vii) generation or generation and distribution of power;
- (viii) transmission or distribution of power by laying a network of new transmission or distribution lines;
- (ix) construction relating to projects involving agro-processing and supply of inputs to agriculture;
- (x) construction of educational institutions and hospitals;
- (xi) any other infrastructure project as may be specified by the Monetary Board from time to time.

*Annex 2***DIRECTIONS****BANKING ACT DIRECTIONS NO. 7 OF 2007****MAXIMUM AMOUNT OF ACCOMMODATION****List of Credit Rating Agencies Acceptable to the Monetary Board**

- 1) Fitch Ratings Lanka Ltd.
- 2) Lanka Ratings Agency Ltd.
- 3) Standard & Poors
- 4) Moody's Investors Service
- 5) Credit Rating Information Services of India (CRISIL)
- 6) Investment Information & Credit Rating Agency (ICRA)
- 7) Fitch Ratings India Ltd
- 8) Pakistan International Credit Rating Agency
- 9) Rating Agency Malaysia
- 10) Japan Credit Rating Agency Ltd
- 11) Any other credit rating agency as may be accepted by the Monetary Board from time to time

Directions issued by the Monetary Board of the Central Bank of Sri Lanka under Section 76J(1) of the Banking Act No. 30 of 1988 as amended.

Nivard Ajith Leslie Cabraal
Governor

Colombo
01st November 2007

DIRECTIONS**BANKING ACT DIRECTIONS NO. 8 OF 2007****MAXIMUM AMOUNT OF ACCOMMODATION**

In the exercise of the powers conferred by Section 76J(1) of the Banking Act No. 30 of 1988, last amended by the Banking Act No.46 of 2006, the Monetary Board hereby issues Directions as follows:

- | | |
|--------------------------|---|
| Citation | 1. These Directions may be cited as the Banking Act Directions No.8 of 2007. The Sections referred to in these Directions will be those of the Banking Act No. 30 of 1988, last amended by the Banking Act No. 46 of 2006. |
| Empowerment under 76J(1) | 2. In terms of Section 76J(1), the Monetary Board has been empowered to give Directions to licensed specialised banks or to any category of licensed specialised banks regarding the manner in which any aspect of the business of such banks is to be conducted. Accordingly, the Monetary Board hereby gives Directions to licensed specialised banks pertaining to the maximum amount of accommodation as may be made by such banks- |

- (i) to any single company, public corporation, firm, association of persons or an individual; or
- (ii) in the aggregate to-
 - (a) an individual, his close relations or to a company or firm in which he has a substantial interest;
 - (b) a company and one or more of the following:-
 - (aa) its subsidiaries;
 - (bb) its holding company;
 - (cc) its associate company;
 - (dd) a subsidiary of its holding company; or
 - (ee) a company in which such company or its subsidiary, or its holding company, or a subsidiary of its holding company, has a substantial interest;

- Maximum limits of accommodation to customers referred to in paragraphs 2(i) and 2(ii) above
3. The maximum amount of accommodation that may be granted by a licensed specialised bank shall not exceed the following percentage of the capital base of the licensed specialised bank subject to the Directions 7, 8 and 9.
- (i) 30 per cent in respect of customers referred to in paragraph 2(i) above.
 - (i) 33 per cent in respect of customers referred to in paragraph 2(ii) above.

- Enhanced limits of accommodation in aggregate to customers referred to in paragraph 2(ii) above
4. (1) Notwithstanding the provisions of Direction 3(ii) above, a licensed specialised bank may grant accommodation in excess of 33 per cent of the capital base of the licensed specialised bank to customers referred to in paragraph 2(ii) above, on the basis of a sum of scores assigned for the following as determined in Direction 4(2) below.
- (i) The Credit Rating and Capital Adequacy Ratio of the bank granting accommodation and,
 - (ii) The Credit Rating of the holding company of the customers referred to in paragraph 2(ii) above. In the event the relationships within the companies in respect of whom accommodation shall be aggregated in terms of paragraph 2(ii) above do not lead to a holding company, the credit ratings of each of the companies that comprise such aggregate shall be considered and the lowest credit rating assigned to any company within such aggregate shall be deemed to be the credit rating that shall be applicable for the purpose of giving effect to this Direction.
- (2) The scores referred to in Direction 4(1) above shall be assigned as follows.

Bank's Credit Rating	Customers' Credit Rating	Bank's Capital Adequacy Ratio	Score Assigned for Each Column
AAA to AA- or equivalent	AAA to AA- or equivalent	> 12%	1
A+ to A- or equivalent	A+ to A- or equivalent	11% - 12%	2
BBB+ or equivalent and below	BBB+ or equivalent and below or unrated	10% - 11%	3

- (3) The maximum amount of accommodation that may be granted by a licensed specialised bank under Direction 4(1) above to customers referred to in paragraph 2(ii) above shall not exceed the following percentages of the capital base of the licensed specialised bank, based upon the sum of the scores assigned for the three columns as per the Table set out in Direction 4(2) above.
- (i) 40 per cent if the sum of scores is between 3 and 5.
 - (ii) 36 per cent if the sum of scores is between 6 and 8.

- Aggregate limit of large accommodation
5. In the case of amount of accommodations granted as at any given date to any category of customers referred to in paragraphs 2(i) and 2(ii) above excluding the Government of Sri Lanka in excess of 15 per cent of the capital base of the licensed specialised bank, the sum total of the

outstanding amount of accommodation granted to such customers shall not exceed 55 per cent of the total outstanding amount of accommodation granted by the licensed specialised bank to all customers excluding the Government of Sri Lanka as at the end of the immediately preceding month.

- | | |
|--|---|
| <p>Monetary Board to approve accommodation in excess of the specified limits</p> | <p>6. (1) Notwithstanding the provisions of Directions 3 and 4 above, a licensed specialised bank may grant accommodation in excess of the maximum limits specified under Directions 3 and 4 above to the categories of customers referred to in paragraphs 2(i) and 2(ii) above, provided that the prior approval of the Monetary Board has been sought and obtained. The Monetary Board may grant such approval on a case-by-case basis, subject to terms and conditions it may deem fit, taking into consideration, inter-alia, instances of national priorities and/or national interest and the ability of the licensed specialised bank to withstand the potential risk arising from the exposure to such enhanced accommodation, provided that the assessment of risks arising out of such accommodation to the licensed specialised bank has been analysed in detail and such analysis is furnished by the licensed specialised bank to the Monetary Board when seeking approval of the Monetary Board.</p> <p>(2) Subject to Direction 6(1) above, a licensed specialised bank may grant accommodation to the categories of customers referred to in paragraphs 2(i) and 2(ii) above up to 50 per cent of the capital base of the licensed specialised bank for the purpose of direct funding of infrastructure projects referred to in Annex 1 hereto for the commencement or expansion of the projects, provided that,</p> <ul style="list-style-type: none"> (i) the customer(s) has (have) been awarded a contract to directly engage in an infrastructure development project in Sri Lanka, and, (ii) such project is funded to the extent of at least 50 per cent by sources outside Sri Lanka or by a consortium of licensed banks excluding the bank providing the accommodation. |
| <p>Exclusions from accommodations from maximum limits under Directions 3 and 4</p> | <p>7. When computing the maximum amount of accommodation under Directions 3 and 4 above that may be granted to any category of customers referred to in paragraphs 2(i) and 2(ii) above, the following accommodations shall be excluded.</p> <ul style="list-style-type: none"> (i) Accommodation granted against the security of cash, gold, Government Securities, Central Bank Securities, Treasury Guarantees, Central Bank Guarantees and Guarantees issued by the World Bank, the Asian Development Bank, International Development Association or any other international institution acceptable to the Director of Bank Supervision. (ii) Accommodation granted against the security of a guarantee or similar instrument Director of Bank Supervision issued by a bank incorporated within or outside Sri Lanka other than the bank granting accommodation, subject to the following:- <ul style="list-style-type: none"> (a) The bank that provides the guarantee having a credit rating of AAA to A- or equivalent. (b) The amount of accommodation that shall be excluded from the computation of accommodation being 80 per cent in the event the credit rating of the bank that provides the guarantee is in the rank of AAA to AA- or equivalent and 50 per cent in the event the bank's credit rating is in the rank of A+ to A- or equivalent. (c) The aggregate amount of all accommodation that shall be excluded in respect of all such instances not exceeding 100 per cent of the capital base of the licensed specialised bank. (d) The licensed specialised bank being satisfied that the credit rating of the bank providing the guarantee has been obtained within 15 months of providing accommodation and the accommodation be revised immediately if there is any change in such credit rating. |
| <p>Persons/ Institutions exempted from maximum limits under Directions 3 and 4</p> | <p>8. The maximum limits of accommodation specified in these Directions shall not apply to the following persons / institutions.</p> <ul style="list-style-type: none"> (i) The Government of Sri Lanka. (ii) The Ceylon Petroleum Corporation and the Ceylon Electricity Board for a maximum period of two years from the date of these Directions. (iii) Other licensed banks in respect of accommodation granted with a contractual maturity of less than two years. |

Definition	<p>9. The following definitions shall be applicable for the purposes of these Directions.</p> <ul style="list-style-type: none"> (i) Accommodations: As defined and provided for in Section 86 of the Banking Act, accommodations shall mean credit exposure and investment exposure as specified below. <ul style="list-style-type: none"> (a) Credit exposure shall include all on-balance sheet accommodations such as any loan, overdraft or advance inclusive of finance lease, hire purchase and reverse repurchase agreements against debt securities and all off-balance sheet accommodations such as any commitment to grant any loan, overdraft or advance or such other facility including a commitment to accept a contingent liability. (b) Investments exposure shall include all financial investments excluding investments in equity (only ordinary shares) (ii) Amount of accommodations: The amount of accommodation shall be the total of on-balance sheet accommodations and off-balance sheet accommodations. <ul style="list-style-type: none"> (a) Amount of on-balance sheet accommodations: The amount of on-balance sheet accommodations shall mean the total of the accommodation limits prevailing at any given time or the total outstanding amount of all accommodations, whichever is higher. In the case of fully drawn term loans, the outstanding amount of accommodations shall be reckoned as the amount of accommodations. (b) Amount of off-balance sheet accommodations: The amount of off-balance sheet accommodations shall mean the credit equivalent amount of total of the accommodation limits prevailing at any given time or the outstanding amount of accommodations, whichever is higher. (iii) Outstanding amount of accommodations: The outstanding amount of accommodations shall be the total of outstanding on-balance sheet accommodations and outstanding off-balance sheet accommodations <ul style="list-style-type: none"> (a) Outstanding on-balance sheet accommodations: The outstanding amount of on-balance sheet accommodations shall be the capital outstanding. (b) Outstanding off-balance sheet accommodations: The outstanding amount of off-balance sheet accommodations shall be the credit equivalent amount of the outstanding off-balance sheet accommodations. (iv) Credit equivalent amount of off-balance sheet accommodations: The credit equivalent amount computed using the credit conversion factors applicable to off-balance sheet accommodations in the computation of the Capital Adequacy Ratio shall be applicable. (v) Capital Base and Capital Adequacy Ratio: Capital Base and Capital Adequacy Ratio appearing in the computation of the Capital Adequacy Ratio shall be applicable, provided that those shall be as at end of the preceding financial year or immediately preceding quarter or other latest quarter preceding the applicable quarter, whichever is available, subject to certification by the licensed specialised bank's external auditor. (vi) Credit Rating: The credit rating shall be the credit rating obtained from a credit rating agency listed in the Annex 2 hereto and shall be one that has been obtained within the past 15 months of providing accommodation.
Review of Accommodation	<p>10. (1) In instances where the accommodation granted to a customer has to be revised due to a reduction in the applicable accommodation limit, the accommodation granted shall be reduced at the next facility review date or within six months, whichever occurs earlier.</p> <p>(2) In the event a merger or acquisition between any institutional customers results in existing accommodations exceeding the applicable maximum limits, the licensed specialised bank shall reduce such accommodations to be within the applicable maximum limits before expiry of six months from the date of such merger or acquisition.</p>
Transitional Arrangements	<p>11. In the event the accommodation that has been granted to any category of customers referred to in paragraphs 2(i) and 2(ii) above as at the date of these Directions exceeds the limits, i.e., maximum limits or aggregate limit, specified in these Directions, the licensed specialised bank shall reduce such accommodation to be within the respective limits before the expiry of three months from the date of these Directions.</p>

Steps to secure compliance with Directions	12. Where the Monetary Board has determined that a licensed specialised bank has contravened these Directions and the determination of such contravention has been conveyed to the licensed specialised bank, such licensed specialised bank shall not pay dividends until the contravention is rectified and such rectification is confirmed by the Director of Bank Supervision.
Revocation of Previous Directions	13. The Banking Act Directions No. 4 of 2007 dated 20 February 2007 of Maximum Amount of Accommodation is hereby revoked.

*Annex 1***DIRECTIONS****BANKING ACT DIRECTIONS NO. 8 OF 2007**
MAXIMUM AMOUNT OF ACCOMMODATION**Specification of Infrastructure Projects**

Any project that involves in developing or operating and maintaining or developing, operating, upgrading and maintaining any infrastructure facility listed below shall qualify for the accommodation under the Direction 6(2) of the above Directions, provided that the accommodation referred to in the Direction shall be for the purpose of meeting direct cost of the project which shall not include repayment of any accommodation already granted by other banks or financial institutions or meeting the cost of purchase of a project already in operation.

- (i) a road, including toll road, a bridge or a rail system;
- (ii) a highway project including other activities being an integral part of the highway project;
- (iii) a port, airport, inland waterway or inland port;
- (iv) a water supply project, irrigation project, water treatment system, sanitation and sewerage system or solid waste management system;
- (v) telecommunication services whether basic or cellular, including radio paging, network of trunking, network and internet services;
- (vi) an industrial park or special economic zone;
- (vii) generation or generation and distribution of power;
- (viii) transmission or distribution of power by laying a network of new transmission or distribution lines;
- (ix) construction relating to projects involving agro-processing and supply of inputs to agriculture;
- (x) construction of educational institutions and hospitals;
- (xi) any other infrastructure project as may be specified by the Monetary Board from time to time.

*Annex 2***DIRECTIONS****BANKING ACT DIRECTIONS NO. 8 OF 2007**
MAXIMUM AMOUNT OF ACCOMMODATION**List of Credit Rating Agencies Acceptable to the Monetary Board**

- 1) Fitch Ratings Lanka Ltd.
- 2) Lanka Ratings Agency Ltd.
- 3) Standard & Poors
- 4) Moody's Investors Service
- 5) Credit Rating Information Services of India (CRISIL)
- 6) Investment Information & Credit Rating Agency (ICRA)
- 7) Fitch Ratings India Ltd
- 8) Pakistan International Credit Rating Agency
- 9) Rating Agency Malaysia
- 10) Japan Credit Rating Agency Ltd
- 11) Any other credit rating agency as may be accepted by the Monetary Board from time to time

Bank Supervision Department
26 December 2007

To: *The CEOs of All Licensed Commercial Banks
and Licensed Specialised Banks*

Dear Sir/Madam

THE ADOPTION OF BASEL II CAPITAL ADEQUACY FRAMEWORK BEGINNING 2008

As announced in the “Road Map: Monetary and Financial Sector Policies for 2007 and Beyond”, released by the Central Bank on January 2, 2007, the Monetary Board of the Central Bank of Sri Lanka has issued the Directions on the maintenance of capital adequacy ratios under the BASEL II for licensed commercial banks (LCBs) and licensed specialised banks (LSBs), in terms of the provisions under Section 46 (1) and 76J (1), of the Banking Act No. 30 of 1988, respectively, which will be effective from January 1, 2008. These Directions have been prepared on the basis of the “International Convergence of Capital Measurement and Capital Standards – a Revised Framework”, widely known as Basel II, issued by the Basel Committee on Banking Supervision of the Bank for International Settlements (BIS) in June 2004 and revised thereafter in June 2006.

2 The Adoption of the Basel II

As you are aware, Basel II provides a “three pillar” approach, i.e., (1) Minimum Capital Requirements; (2) Supervisory Review Process; and (3) Market Discipline, for the implementation of this framework. However, as announced at the Bank Managers’ Meeting held on November 22, 2007, the Central Bank has decided to adopt Pillar 1, i.e., “Minimum Capital Requirements” effective from 1st January 2008 and to adopt the other two pillars in the medium term. The approach for adoption of Basel II is as follows.

2.1 The Adoption of Pillar I: Minimum Capital Requirements

The Basel II framework provides several options for the implementation of the Pillar I, based on the level of sophistication and development of the banking system. Accordingly, all LCBs and all LSBs are required to apply the Standardised Approach for credit risk, the Standardised Measurement Method for market risk and the Basic Indicator Approach for operational risk, in computing the capital requirements, commencing January 1, 2008.

For this purpose, the following documents are attached herewith.

- (i) Banking Act Directions No. 9 (for LCBs) and 10 (for LSBs) dated 26.12.2007 issued by the Monetary Board.
- (ii) Guidelines on computation of capital adequacy ratio (**Schedule I**).*
- (iii) Return to be submitted on capital adequacy ratio (**Schedule II**).*

2.2 Migration to Advanced Approaches

The Central Bank has decided to move to adopting the internal ratings based (IRB) advanced approaches beginning 2013. Once the Central Bank is satisfied that the banks have the appropriate models and risk management systems capacities, permission will be granted for them to proceed with the IRB approaches. Separate guidelines in this regard will be issued later, specifying the pre-requisites and procedures for seeking the Central Bank’s prior approval for such migration.

2.3 Resource Requirements: Data, IT Needs and Training

Data and IT Needs: Banks should begin preparing a comprehensive data capturing system to identify, measure and report all material risks and to assess and allocate capital against these risks in a systematic and objective manner to meet the requirements under the simplified approaches and to move to advanced approaches in the future. Accordingly, banks are required to implement changes, especially plan for systems integration, modifications to internal systems and use of new software for appropriate data collection, to move to the advanced approaches. In this regard, Banks are expected to have in place, or be actively developing, a data “warehouse”, that is, a process that enables a bank to collect, store and draw upon loss statistics in an efficient manner over time. Guidelines in this regard are given in **Annex I**.*

Training: Upgrading skills in the areas of credit risk models and capital assessment strategies, credit risk mitigation techniques and measuring market and operational risks will be critical to the successful implementation of Basel II.

2.4 Adoption of the other two Pillars

2.4.1 The Pillar II: Supervisory Review Process (SRP)

The objective of SRP is to ensure that banks have adequate capital to support all material risks in their business and also to encourage them to adopt more sophisticated risk management techniques for monitoring and managing all risks. For this purpose, banks are required to establish well-defined internal assessment processes within themselves in order to determine the additional capital requirement for all material risks, internally, and which would also be able to assure the Central Bank that adequate capital is actually held towards all their material risk exposures. However, considering the current level of internal systems of the banks, it has been decided to adopt the Pillar II from 2010.

2.4.2 The Pillar III: Market Discipline

The introduction of disclosure requirements for banks, based on the revised framework, will be initiated along with the adoption of new international accounting standards, i.e., the International Financial Reporting Standards (IFRS 7). Accordingly, banks are advised to continue with the current disclosure requirements until the adoption of the Pillar III.

Yours faithfully

B D W A Silva

Actg. Director of Bank Supervision

Copy To: Secretary General/SLBA

(Footnotes)

* *The Schedule I and II and Annex I are available at www.cbsl.gov.lk*

Directions issued by the Monetary Board of the Central Bank of Sri Lanka under Section 46(1) of the Banking Act No. 30 of 1988, as amended.

Sgd. Nivard Ajith Leslie Cabraal
Governor

Colombo

26th December 2007

DIRECTIONS

BANKING ACT DIRECTION NO. 9 OF 2007

MAINTENANCE OF CAPITAL ADEQUACY RATIO

WHEREAS in terms of the powers conferred by Section 19(7)(a) of the Banking Act, No. 30 of 1988 as amended, the Monetary Board has arrived at a determination in respect of the maintenance of capital adequacy ratio of licensed commercial banks having regard to the guidelines for capital adequacy set out by the Bank for International Settlements in Basle; and

WHEREAS in the exercise of powers conferred by section 46(1) of the Banking Act, No. 30 of 1988 as amended, the Monetary Board hereby issues the following directions.

Minimum Capital Adequacy Ratio	1 (1)	Commencing from 1 st January 2008, all licensed commercial banks shall, at all times, maintain a capital adequacy ratio of not less than 10% in relation to total risk weighted assets with core capital constituting not less than 5% in relation to total risk weighted assets.
	1 (2)	The capital adequacy ratios referred to in Direction 1(1) above shall be computed as per guidelines given in Schedule I hereto prepared in accordance with the Basel II Capital Accord "International Convergence of Capital Measurement and Capital Standards - A Revised Framework" recommended by the Basle Committee on Banking Supervision at the Bank for International Settlements.
<i>Reporting Format</i>	2	Licensed commercial banks shall use the format at Schedule II attached hereto for reporting of capital adequacy ratios on a periodic basis as specified in Schedule I.
<i>Steps to secure compliance with Directions</i>	3	Where a licensed commercial bank has failed to comply with these Directions, such licensed commercial bank shall not pay dividends or repatriate profits until such compliance is effected and confirmed by the Director of Bank Supervision.

<i>Revocation of previous Determinations</i>	4 (1)	All previous Determinations, Directions and Guidelines that have been issued to licensed commercial banks by the Monetary Board in relation to maintenance of capital adequacy ratio in terms of Section 19(7) or 46(1) of the Banking Act are hereby revoked.
	4 (2)	Notwithstanding the revocation referred to in Direction 4(1) above, licensed commercial banks granted time by the Monetary Board in terms of Section 19(7) (b) of the Banking Act shall comply with the requirements contained in such previous Determinations, Directions and Guidelines until the expiration of the time so granted.

Directions issued by the Monetary Board of the Central Bank of Sri Lanka under Section 76J(1) of the Banking Act No. 30 of 1988, as amended.

Sgd. Nivard Ajith Leslie Cabraal
Governor

Colombo
26th December 2007

DIRECTIONS
BANKING ACT DIRECTION NO. 10 OF 2007
MAINTENANCE OF CAPITAL ADEQUACY RATIO

WHEREAS in terms of the powers conferred by Section 76J(1) of the Banking Act, No. 30 of 1988 as amended, the Monetary Board has arrived at a determination with regard to the guidelines in respect of the maintenance of capital adequacy ratio of licensed specialised banks having regard to the guidelines for capital adequacy set out by the Bank for International Settlements in Basle; and

WHEREAS in the exercise of powers conferred by Section 76J(1) of the Banking Act, No. 30 of 1988 as amended, the Monetary Board hereby issues the following directions.

Minimum Capital Adequacy Ratio	1 (1)	Commencing from 1 st January 2008, all licensed specialised banks shall, at all times, maintain a capital adequacy ratio of not less than 10% in relation to total risk weighted assets with core capital constituting not less than 5% in relation to total risk weighted assets.
	1 (2)	The capital adequacy ratios referred to in Direction 1(1) above shall be computed as per guidelines given in Schedule I hereto prepared in accordance with the Basel II Capital Accord "International Convergence of Capital Measurement and Capital Standards - A Revised Framework" recommended by the Basle Committee on Banking Supervision at the Bank for International Settlements.
Reporting Format	2	Licensed specialised banks shall use the format at Schedule II attached hereto for reporting of capital adequacy ratios on a periodic basis as specified in Schedule I.
Transitional Arrangements	3	Where a licensed specialised bank has failed to comply with these Directions, such licensed specialised bank shall not pay dividends or repatriate profits until such compliance is effected and confirmed by the Director of Bank Supervision.
Steps to secure compliance with Directions	4	Every licensed specialised bank which is required by these directions to augment its capital may apply to the Monetary Board for an extension of time to comply with such requirement which extension shall not exceed a period of twelve months or such longer period as may be determined by the Monetary Board.
Revocation of previous Determinations	5 (1)	All previous Determinations, Directions and Guidelines that have been issued to licensed specialised banks by the Monetary Board in relation to maintenance of capital adequacy ratio in terms of Section 76J of the Banking Act are hereby revoked.
	5 (2)	Notwithstanding the revocation referred to in Direction 5(1) above, licensed specialised banks granted time by the Monetary Board in term of Direction 4 above shall comply with the requirements contained in such previous Determinations, Directions and Guidelines until the expiration of the time so granted.

Directions issued by the Monetary Board of the Central Bank of Sri Lanka under Section 46(1) of the Banking Act No. 30 of 1988, as amended.

Nivard Ajith Leslie Cabraal
Governor

Colombo
26 December 2007

DIRECTIONS
BANKING ACT DIRECTION NO. 11 OF 2007
CORPORATE GOVERNANCE FOR
LICENSED COMMERCIAL BANKS IN SRI LANKA

In the exercise of the powers conferred by Section 46(1) of the Banking Act No. 30 of 1988, last amended by the Banking Act No. 46 of 2006, the Monetary Board hereby issues the following Directions on Corporate Governance for Licensed Commercial Banks in Sri Lanka. These Directions may be cited as the Banking Act Direction No. 11 of 2007. The Sections referred to in these Directions will be those of the Banking Act No. 30 of 1988, last amended by the Banking Act No. 46 of 2006.

1. Responsibilities and Empowerment under the Banking Act and the Monetary Law Act

- 1(1)** In terms of Section 46(1) of the Banking Act No. 30 of 1988 last amended by No. 46 of 2006, in order to ensure the soundness of the banking system, the Monetary Board has been empowered to issue Directions to licensed commercial banks, regarding the manner in which any aspect of the business of such banks is to be conducted.
- 1(2)** In terms of Section 5 of the Monetary Law Act No. 58 of 1949, the Central Bank of Sri Lanka is charged with the duty of securing, as far as possible by action authorised by such Act, the two objectives, namely, (a) economic and price stability and (b) financial system stability.
- 1(3)** In terms of Section 10(c) of the Monetary Law Act, the Monetary Board, in the exercise of its powers, duties, functions and responsibilities, is empowered to make such rules and regulations as the Monetary Board may consider necessary, in relation to any matter affecting or connected with or incidental to the exercise, discharge, or performance of the powers, functions, and duties of the Central Bank of Sri Lanka.
- 1(4)** Under the provisions of the Monetary Law Act No. 58 of 1949, the supervision of banks has been made a duty of the Central Bank on account of specific reasons as stated in John Exter's Report on the Monetary Law Act which states, *inter alia*, as follows: "*Banking is an economic activity which affects the public welfare to an unusual degree; it touches in one way or another, almost every phase of a country's economic life. Sound banking is essential to healthy and vigorous economic development. Supervision of banks helps to protect the public against mismanagement, bank failures, and loss of confidence in the banking system. It helps to protect depositors and stock-holders against loss and frequently enables bank directors and officers to manage the affairs of their banks more wisely and intelligently.*"
- 1(5)** Accordingly, in order to enhance the overall banking sector stability which is the fundamental to financial system stability, the Monetary Board, hereby issues Directions under Section 46(1) of the Banking Act No. 30 of 1988 to improve and sustain the corporate governance processes and practices of the licensed commercial banks in Sri Lanka.
- 1(6)** For purposes of this Direction, Corporate Governance processes and practices shall be deemed to be the management framework that facilitates the conduct of the banking business in a responsible and accountable manner so as to promote the safety and soundness of the individual banks, thereby leading to the stability of the overall banking sector.
- 1(7)** The rules of corporate governance as contained in Direction 3 of these Directions have, therefore, been developed on the basis of certain fundamental principles as set out in Direction 2 of these Directions with a view to facilitating the underlying supervisory responsibilities of the Central Bank and to promote safety and soundness of the banking system.

2. The Principles upon which the rules of Corporate Governance have been based upon and developed are the following:

The principles set out in this Direction 2 should be referred to for explanatory purposes and/or for clarification purposes only, so as to understand the rationale for the rules as contained in Direction 3 hereof. Hence, strict compliance under these Directions shall only be in respect of the rules that are set out under Direction 3.

2(1) Principle: The Responsibilities of the Board

- 2(1)(i)** The board of directors should assume the overall responsibility and accountability in respect of: (a) the management of the affairs of the bank, i.e., conduct of business and maintenance of prudent risk management mechanisms; and (b) the safety and soundness of the bank.
- 2(1)(ii)** Towards this end, the board should: (a) determine the structure of the management of affairs of the bank; (b) delegate business operations to key management personnel led by the chief executive officer designated by the board; (c) assume policy making and risk management for the business; and (d) ensure the effective role of the key management personnel. Key management personnel shall mean such key executives of the bank as defined in the International Accounting Standards.
- 2(1)(iii)** The overall responsibility of the board should not be construed as an obligation to undertake the inspection of day-to-day activities, but should rather be understood as an obligation to oversee and ensure that the key management personnel are carrying out the day-to-day activities of the bank in a safe and sound manner in accordance with the policies set by the board.
- 2(1)(iv)** Directors should understand the business and risk management mechanism of the bank and take objective decisions in the interest of the bank's depositors, creditors, shareholders and other stakeholders. Further, they should ensure that the bank does not act in a manner that is detrimental or prejudicial to the interests of, and obligations to, depositors and creditors.
- 2(1)(v)** The board should take the responsibility for compliance with accepted rules of corporate governance. They should also ensure compliance with all regulatory and supervisory requirements. Further, they should ensure that an effective combination of professionals with practical experience in relevant subjects such as banking, finance, economics, business management, human resource management, law, marketing, information technology or any other discipline relevant or complementary to banking operations, is available in the bank to undertake its operations and discharge its responsibilities.
- 2(1)(vi)** The directors should be aware of potential civil and criminal liabilities that may arise from their failure to discharge their duties diligently. They should also understand that they should act with due care and prudence. In addition, the directors of state owned banks should be aware of the additional liabilities that arise from the status of such banks being state enterprises and consequently being accountable to the public. It is, therefore, necessary that directors commit sufficient time and energy to fulfilling the board's responsibilities in managing the affairs of the bank in a prudent manner.

2(2) Principle: The Board's composition

- 2(2)(i)** The board should be composed of a healthy mix of executive directors and non-executive directors. Some of the non-executive directors should also be independent so that there is strong independent element brought into the decision-making process.
- 2(2)(ii)** The board's composition should ensure a balance of skills and experience as may be deemed appropriate and desirable for the requirements of the bank.
- 2(2)(iii)** The banking industry worldwide is making tremendous progress and undergoing rapid change with new innovations, instruments, technologies, products, systems and processes being introduced regularly. It is vital therefore, that the directors should be persons who would: (a) be able to keep abreast with these changes, and (b) provide continuous contribution and guidance to the board decision-making process.
- 2(2)(iv)** There should be a gradual infusion of new ideas into the board. There should also be assurance that the relationships between the directors amongst themselves as well as between the directors and the key management personnel is at a level that does not suggest the existence of excessive familiarity, undue influence or coercion. In this context, it should be noted that very long-standing relationships could sometimes impair the high sense of values, independence and objectivity that is needed in the discharge of the duties of a director of a bank.

2(3) Principle: Criteria to assess the Fitness and Propriety of Directors

- 2(3)(i)** In addition to the principles under the board's composition in Direction 2(2) above, directors should be fit and proper persons in order to be eligible to hold office as directors of a bank and no person should serve as a director unless such person is a fit and proper person.
- 2(3)(ii)** There is strong need for commitment and effective contribution to the prudent management of the affairs of the bank. It is very likely that the effectiveness of such commitment and contribution would tend to decrease with advanced age of directors and more particularly, if the age of such director is well beyond the normal age of retirement, as generally accepted in the country.

2(4) Principle: Management functions delegated by the Board

- 2(4)(i)** The board should have a formal schedule of matters specifically reserved to it for decision. The board should also give clear directions to key management personnel, as to the matters that should be approved by the board before decisions are made by key management personnel, on behalf of the bank.

2(5) Principle: The Chairman and the Chief Executive Officer

- 2(5)(i)** There are two key aspects of the management of every bank, viz., (a) the overall governance by the board, and (b) the day-to-day management of the bank's business by the CEO, in line with board approved strategic objectives, corporate values, overall risk policy and risk management procedures.
- 2(5)(ii)** There should be a clear division of these responsibilities at the board level and the executive management level to ensure a greater balance of power and authority, so that powers are not concentrated in any one individual.
- 2(5)(iii)** The board should appoint a chairman as well as a chief executive officer. The division of responsibilities between the chairman and chief executive officer should be clearly established and set out in writing.

2(6) Principle: Board appointed Committees

- 2(6)(i)** The board should appoint separate board committees for audit, selection, remuneration, integrated risk management and such other subjects as determined by the Board to ensure its oversight and control over the affairs of the bank.
- 2(6)(ii)** Where the board appoints a committee, it should set out the authority of the committee, and in particular, whether the committee has the authority to act on behalf of the board or simply has the authority to examine a particular issue and report back to the board with recommendations.
- 2(6)(iii)** Each committee should be chaired by a non-executive director who has some expertise in the relevant subject, and who preferably should be independent too. The majority of the members of the board committee should consist of non-executive directors with at least one independent director in the committee. If a need arises, professionals from outside may be invited or hired to serve in a committee. Bank staff may be present at the board committees for advice or special assignments, on invitation.

2(7) Principle: Related party transactions

- 2(7)(i)** The board should ensure that the bank does not engage in transactions with "related parties" in a manner that would grant such parties "more favourable treatment" than that accorded to other constituents of the bank carrying on the same business.

2(8) Principle: Disclosures

- 2(8)(i)** The objective of disclosure is the transparency of information relating to affairs and risk management of banks which would help to promote market discipline of the respective banks.
- 2(8)(ii)** Since market disclosure is the focus of the Pillar III of the risk management based capital standard known as Basel II recommended by the Basel Committee on Banking Supervision at the Bank for International Settlements, (which is the globally accepted body on introducing international standards on Bank Supervision), the extent of disclosures should be commensurate with the size, ownership structure, systemic importance, risk profile and the business model of the bank. Accordingly, it should be noted that the adequate and timely public disclosure of relevant information by banks would facilitate enhanced market discipline and lead to better and more effective corporate governance.

2(8)(iii) Disclosures by banks should generally include disclosures relating to capital adequacy, key performance indicators, business concentrations, transactions with related parties, corporate governance statements, financial statements, etc., and should be consistent with accounting standards, regulatory requirements as well as with any other information disclosed on voluntary basis.

3. The following rules of Corporate Governance shall be complied by all licensed commercial banks in Sri Lanka and such compliance shall be as provided for in Direction 3(9)(i) hereof.

3 (1) The Responsibilities of the Board

3(1)(i) The board shall strengthen the safety and soundness of the bank by ensuring the implementation of the following:

- a) Approve and oversee the bank's strategic objectives and corporate values and ensure that these are communicated throughout the bank;
- b) Approve the overall business strategy of the bank, including the overall risk policy and risk management procedures and mechanisms with measurable goals, for at least the next three years;
- c) Identify the principal risks and ensure implementation of appropriate systems to manage the risks prudently;
- d) Approve implementation of a policy of communication with all stakeholders, including depositors, creditors, share-holders and borrowers;
- e) Review the adequacy and the integrity of the bank's internal control systems and management information systems;
- f) Identify and designate key management personnel, as defined in the International Accounting Standards, who are in a position to: (i) significantly influence policy; (ii) direct activities; and (iii) exercise control over business activities, operations and risk management;
- g) Define the areas of authority and key responsibilities for the board directors themselves and for the key management personnel;
- h) Ensure that there is appropriate oversight of the affairs of the bank by key management personnel, that is consistent with board policy;
- i) Periodically assess the effectiveness of the board directors' own governance practices, including: (i) the selection, nomination and election of directors and key management personnel; (ii) the management of conflicts of interests; and (iii) the determination of weaknesses and implementation of changes where necessary;
- j) Ensure that the bank has an appropriate succession plan for key management personnel;
- k) Meet regularly, on a needs basis, with the key management personnel to review policies, establish communication lines and monitor progress towards corporate objectives;
- l) Understand the regulatory environment and ensure that the bank maintains an effective relationship with regulators;
- m) Exercise due diligence in the hiring and oversight of external auditors.

3(1)(ii) The board shall appoint the chairman and the chief executive officer and define and approve the functions and responsibilities of the chairman and the chief executive officer in line with Direction 3(5) of these Directions.

3(1)(iii) The board shall meet regularly and board meetings shall be held at least twelve times a year at approximately monthly intervals. Such regular board meetings shall normally involve active participation in person of a majority of directors entitled to be present. Obtaining the board's consent through the circulation of written resolutions/papers shall be avoided as far as possible.

3(1)(iv) The board shall ensure that arrangements are in place to enable all directors to include matters and proposals in the agenda for regular board meetings where such matters and proposals relate to the promotion of business and the management of risks of the bank.

- 3(1)(v)** The board procedures shall ensure that notice of at least 7 days is given of a regular board meeting to provide all directors an opportunity to attend. For all other board meetings, reasonable notice may be given.
- 3(1)(vi)** The board procedures shall ensure that a director who has not attended at least two-thirds of the meetings in the period of 12 months immediately preceding or has not attended the immediately preceding three consecutive meetings held, shall cease to be a director. Participation at the directors' meetings through an alternate director shall, however, be acceptable as attendance.
- 3(1)(vii)** The board shall appoint a company secretary who satisfies the provisions of Section 43 of the Banking Act No. 30 of 1988, whose primary responsibilities shall be to handle the secretariat services to the board and shareholder meetings and to carry out other functions specified in the statutes and other regulations.
- 3(1)(viii)** All directors shall have access to advice and services of the company secretary with a view to ensuring that board procedures and all applicable rules and regulations are followed.
- 3(1)(ix)** The company secretary shall maintain the minutes of board meetings and such minutes shall be open for inspection at any reasonable time, on reasonable notice by any director.
- 3(1)(x)** Minutes of board meetings shall be recorded in sufficient detail so that it is possible to gather from the minutes, as to whether the board acted with due care and prudence in performing its duties. The minutes shall also serve as a reference for regulatory and supervisory authorities to assess the depth of deliberations at the board meetings. Therefore, the minutes of a board meeting shall clearly contain or refer to the following: (a) a summary of data and information used by the board in its deliberations; (b) the matters considered by the board; (c) the fact-finding discussions and the issues of contention or dissent which may illustrate whether the board was carrying out its duties with due care and prudence; (d) the testimonies and confirmations of relevant executives which indicate compliance with the board's strategies and policies and adherence to relevant laws and regulations; (e) the board's knowledge and understanding of the risks to which the bank is exposed and an overview of the risk management measures adopted; and (f) the decisions and board resolutions.
- 3(1)(xi)** There shall be a procedure agreed by the board to enable directors, upon reasonable request, to seek independent professional advice in appropriate circumstances, at the bank's expense. The board shall resolve to provide separate independent professional advice to directors to assist the relevant director or directors to discharge his/her/their duties to the bank.
- 3(1)(xii)** Directors shall avoid conflicts of interests, or the appearance of conflicts of interest, in their activities with, and commitments to, other organisations or related parties. If a director has a conflict of interest in a matter to be considered by the board, which the board has determined to be material, the matter should be dealt with at a board meeting, where independent non-executive directors [refer to Direction 3(2)(iv) of these Directions] who have no material interest in the transaction, are present. Further, a director shall abstain from voting on any board resolution in relation to which he/she or any of his/her close relation or a concern in which a director has substantial interest, is interested and he/she shall not be counted in the quorum for the relevant agenda item at the board meeting.
- 3(1)(xiii)** The board shall have a formal schedule of matters specifically reserved to it for decision to ensure that the direction and control of the bank is firmly under its authority.
- 3(1)(xiv)** The board shall, if it considers that the bank is, or is likely to be, unable to meet its obligations or is about to become insolvent or is about to suspend payments due to depositors and other creditors, forthwith inform the Director of Bank Supervision of the situation of the bank prior to taking any decision or action.
- 3(1)(xv)** The board shall ensure that the bank is capitalised at levels as required by the Monetary Board in terms of the capital adequacy ratio and other prudential grounds.
- 3(1)(xvi)** The board shall publish in the bank's Annual Report, an annual corporate governance report setting out the compliance with Direction 3 of these Directions.
- 3(1)(xvii)** The board shall adopt a scheme of self-assessment to be undertaken by each director annually, and maintain records of such assessments.
- 3(2) The Board's Composition**
- 3(2)(i)** The number of directors on the board shall not be less than 7 and not more than 13.

- 3(2)(ii)** (A) 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, and such period in office shall be inclusive of the total period of service served by such director up to January 1, 2008.
- (B) In this context, the following transitional provisions shall apply:
- a) In the event that there is only one director on the board who has served more than nine years as at January 1, 2008, he/she shall be deemed to have vacated the office as a director as at December 31, 2008.
 - b) In the event that there are two or more directors on the board who have served more than nine years as at January 1, 2008, the following provisions shall apply:
 - I. Of those directors whose period of service has exceeded nine years, the longest serving director, shall be deemed to have vacated office as a Director on December 31, 2008.
 - II. Thereafter, at the end of each succeeding year, the remaining directors shall be deemed to have vacated office in sequence, at least one director each year, (on the basis of the longest to the shortest length of service as a director), until all directors who have served a period in excess of nine years as at January 1, 2008, have been deemed to have vacated office. Provided also, that all directors of the bank who have served more than nine years as at January 1, 2008 shall be deemed to have vacated their office by or before December 31, 2011.
 - c) In the event there are any directors who are due to complete nine years of service between January 1, 2008 and December 31, 2010, such directors shall also be deemed to have vacated office, in sequence, at least one director each year, (on the basis of the longest to the shortest length of service as a director), after the directors as set out in Direction 3(2)(ii)(B) (b) have vacated their office as directors. Provided, however, that all such directors covered by this sub-direction (c) shall also be deemed to have vacated their office by or before December 31, 2011.
- 3(2)(iii)** An employee of a bank may be appointed, elected or nominated as a director of the bank (hereinafter referred to as an “executive director”) provided that the number of executive directors shall not exceed one-third of the number of directors of the board. In such an event, one of the executive directors shall be the chief executive officer of the bank.
- 3(2)(iv)** The board shall have at least three independent non-executive directors or one third of the total number of directors, whichever is higher. This sub-direction shall be applicable from January 1, 2010 onwards.
- A non-executive director shall not be considered independent if he/she:
- a) has direct and indirect shareholdings of more than 1% of the bank;
 - b) currently has or had during the period of two years immediately preceding his/her appointment as director, any business transactions with the bank as described in Direction 3 (7) hereof, exceeding 10% of the regulatory capital of the bank.
 - c) has been employed by the bank during the two year period immediately preceding the appointment as director;
 - d) has a close relation who is a director or chief executive officer or a member of key management personnel or a material shareholder of the bank or another bank. For this purpose, a “close relation” shall mean the spouse or a financially dependant child;
 - e) represents a specific stakeholder of the bank;
 - f) is an employee or a director or a material shareholder in a company or business organization:
 - I. which currently has a transaction with the bank as defined in Direction 3(7) of these Directions, exceeding 10% of the regulatory capital of the bank, or
 - II. in which any of the other directors of the bank are employed or are directors or are material shareholders; or
 - III. in which any of the other directors of the bank have a transaction as defined in Direction 3(7) of these Directions, exceeding 10% of regulatory capital in the bank;

- 3(2)(v)** In the event an alternate director is appointed to represent an independent director, the person so appointed shall also meet the criteria that applies to the independent director.
- 3(2)(vi)** Non-executive directors shall be persons with credible track records and/or have necessary skills and experience to bring an independent judgment to bear on issues of strategy, performance and resources.
- 3(2)(vii)** A meeting of the board shall not be duly constituted, although the number of directors required to constitute the quorum at such meeting is present, unless more than one half of the number of directors present at such meeting are non-executive directors. This sub-direction shall be applicable from January 1, 2010 onwards.
- 3(2)(viii)** The independent non-executive directors shall be expressly identified as such in all corporate communications that disclose the names of directors of the bank. The bank shall disclose the composition of the board, by category of directors, including the names of the chairman, executive directors, non-executive directors and independent non-executive directors in the annual corporate governance report.
- 3(2)(ix)** There shall be a formal, considered and transparent procedure for the appointment of new directors to the board. There shall also be procedures in place for the orderly succession of appointments to the board.
- 3(2)(x)** All directors appointed to fill a casual vacancy shall be subject to election by shareholders at the first general meeting after their appointment.
- 3(2)(xi)** If a director resigns or is removed from office, the board shall: (a) announce the director's resignation or removal and the reasons for such removal or resignation including but not limited to information relating to the relevant director's disagreement with the bank, if any; and (b) issue a statement confirming whether or not there are any matters that need to be brought to the attention of shareholders.
- 3(2)(xii)** A director or an employee of a bank shall not be appointed, elected or nominated as a director of another bank except where such bank is a subsidiary company or an associate company of the first mentioned bank.

3(3) Criteria to assess the fitness and propriety of directors

In addition to provisions of Section 42 of the Banking Act No. 30 of 1988, the criteria set out below shall apply to determine the fitness and propriety of a person who serves or wishes to serve as a director of a bank. Non-compliance with any one of the criteria as set out herein shall disqualify a person to be appointed, elected or nominated as a director or to continue as a director.

- 3(3)(i)** The age of a person who serves as director shall not exceed 70 years.
 - (A) Where a director who is currently serving at a bank is over 70 years of age as at January 1, 2008, the following transitional provisions shall apply, subject however to the provisions as set out in Direction 3(2)(ii) hereof.
 - a) If a director is over 75 years of age as at January 1, 2008, such director may continue to serve as a director for a further period that shall not extend beyond December 31, 2008, and shall be deemed to have vacated office on December 31, 2008;
 - b) If a director is between 70 and 75 years of age as at January 1, 2008, such director may continue to serve as a director for a further period that shall not extend beyond December 31, 2009, and shall be deemed to have vacated office on December 31, 2009.
 - (B) Where a director who is currently serving at a bank reaches the age of 70 years, between January 1, 2008 and December 31, 2009, such director may, subject to the provisions as set out in Direction 3(2)(ii) hereof, continue to serve as a director for a further period that shall not extend beyond December 31, 2010 and shall be deemed to have vacated office on December 31, 2010.
 - 3(3)(ii)** A person shall not hold office as a director of more than 20 companies/entities/institutions inclusive of subsidiaries or associate companies of the bank. Of such 20 companies/entities/ institutions, not more than 10 companies shall be those classified as Specified Business Entities in terms of the Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995.
- 3(4) Management functions delegated by the Board**
- 3(4)(i)** The directors shall carefully study and clearly understand the delegation arrangements in place.
 - 3(4)(ii)** The board shall not delegate any matters to a board committee, chief executive officer, executive directors or

key management personnel, to an extent that such delegation would significantly hinder or reduce the ability of the board as a whole to discharge its functions.

- 3(4)(iii)** The board shall review the delegation processes in place on a periodic basis to ensure that they remain relevant to the needs of the bank.

3(5) The Chairman and Chief Executive Officer

- 3(5)(i)** The roles of chairman and chief executive officer shall be separate and shall not be performed by the same individual.

- 3(5)(ii)** The chairman shall be a non-executive director and preferably an independent director as well. In the case where the chairman is not an independent director, the board shall designate an independent director as the Senior Director with suitably documented terms of reference to ensure a greater independent element. The designation of the Senior Director shall be disclosed in the bank's Annual Report.

- 3(5)(iii)** The board shall disclose in its corporate governance report, which shall be an integral part of its Annual Report, the identity of the chairman and the chief executive officer and the nature of any relationship [including financial, business, family or other material/relevant relationship(s)], if any, between the chairman and the chief executive officer and the relationships among members of the board.

- 3(5)(iv)** The chairman shall: (a) provide leadership to the board; (b) ensure that the board works effectively and discharges its responsibilities; and (c) ensure that all key and appropriate issues are discussed by the board in a timely manner.

- 3(5)(v)** The chairman shall be primarily responsible for drawing up and approving the agenda for each board meeting, taking into account where appropriate, any matters proposed by the other directors for inclusion in the agenda. The chairman may delegate the drawing up of the agenda to the company secretary.

- 3(5)(vi)** The chairman shall ensure that all directors are properly briefed on issues arising at board meetings and also ensure that directors receive adequate information in a timely manner.

- 3(5)(vii)** The chairman shall encourage all directors to make a full and active contribution to the board's affairs and take the lead to ensure that the board acts in the best interests of the bank.

- 3(5)(viii)** The chairman shall facilitate the effective contribution of non-executive directors in particular and ensure constructive relations between executive and non-executive directors.

- 3(5)(ix)** The chairman, shall not engage in activities involving direct supervision of key management personnel or any other executive duties whatsoever.

- 3(5)(x)** The chairman shall ensure that appropriate steps are taken to maintain effective communication with shareholders and that the views of shareholders are communicated to the board.

- 3(5)(xi)** The chief executive officer shall function as the apex executive-in-charge of the day-to-day-management of the bank's operations and business.

3(6) Board appointed Committees

- 3(6)(i)** Each bank shall have at least four board committees as set out in Directions 3(6)(ii), 3(6)(iii), 3(6)(iv) and 3(6)(v) of these Directions. Each committee shall report directly to the board. All committees shall appoint a secretary to arrange the meetings and maintain minutes, records, etc., under the supervision of the chairman of the committee. The board shall present a report of the performance on each committee, on their duties and roles at the annual general meeting.

- 3(6)(ii)** The following rules shall apply in relation to the Audit Committee:

- a) The chairman of the committee shall be an independent non-executive director who possesses qualifications and experience in accountancy and/or audit.
- b) All members of the committee shall be non-executive directors.
- c) The committee shall make recommendations on matters in connection with: (i) the appointment of the external auditor for audit services to be provided in compliance with the relevant statutes; (ii) the implementation of the Central Bank guidelines issued to auditors from time to time; (iii) the application

of the relevant accounting standards; and (iv) the service period, audit fee and any resignation or dismissal of the auditor; provided that the engagement of the Audit partner shall not exceed five years, and that the particular Audit partner is not re-engaged for the audit before the expiry of three years from the date of the completion of the previous term.

- d) The committee shall review and monitor the external auditor's independence and objectivity and the effectiveness of the audit processes in accordance with applicable standards and best practices.
- e) The committee shall develop and implement a policy on the engagement of an external auditor to provide non-audit services that are permitted under the relevant statutes, regulations, requirements and guidelines. In doing so, the committee shall ensure that the provision by an external auditor of non-audit services does not impair the external auditor's independence or objectivity. When assessing the external auditor's independence or objectivity in relation to the provision of non-audit services, the committee shall consider:
 - I. whether the skills and experience of the audit firm make it a suitable provider of the non-audit services;
 - II. whether there are safeguards in place to ensure that there is no threat to the objectivity and/or independence in the conduct of the audit resulting from the provision of such services by the external auditor; and
 - III. whether the nature of the non-audit services, the related fee levels and the fee levels individually and in aggregate relative to the audit firm, pose any threat to the objectivity and/or independence of the external auditor.
- f) The committee shall, before the audit commences, discuss and finalise with the external auditors the nature and scope of the audit, including: (i) an assessment of the bank's compliance with the relevant Directions in relation to corporate governance and the management's internal controls over financial reporting; (ii) the preparation of financial statements for external purposes in accordance with relevant accounting principles and reporting obligations; and (iii) the co-ordination between firms where more than one audit firm is involved.
- g) The committee shall review the financial information of the bank, in order to monitor the integrity of the financial statements of the bank, its annual report, accounts and quarterly reports prepared for disclosure, and the significant financial reporting judgments contained therein. In reviewing the bank's annual report and accounts and quarterly reports before submission to the board, the committee shall focus particularly on: (i) major judgmental areas; (ii) any changes in accounting policies and practices; (iii) significant adjustments arising from the audit; (iv) the going concern assumption; and (v) the compliance with relevant accounting standards and other legal requirements.
- h) The committee shall discuss issues, problems and reservations arising from the interim and final audits, and any matters the auditor may wish to discuss including those matters that may need to be discussed in the absence of key management personnel, if necessary.
- i) The committee shall review the external auditor's management letter and the management's response thereto.
- j) The committee shall take the following steps with regard to the internal audit function of the bank:
 - I. Review the adequacy of the scope, functions and resources of the internal audit department, and satisfy itself that the department has the necessary authority to carry out its work;
 - II. Review the internal audit programme and results of the internal audit process and, where necessary, ensure that appropriate actions are taken on the recommendations of the internal audit department;
 - III. Review any appraisal or assessment of the performance of the head and senior staff members of the internal audit department;
 - IV. Recommend any appointment or termination of the head, senior staff members and outsourced service providers to the internal audit function;
 - V. Ensure that the committee is appraised of resignations of senior staff members of the internal audit department including the chief internal auditor and any outsourced service providers, and to

provide an opportunity to the resigning senior staff members and outsourced service providers to submit reasons for resigning;

VI. Ensure that the internal audit function is independent of the activities it audits and that it is performed with impartiality, proficiency and due professional care;

- k) The committee shall consider the major findings of internal investigations and management's responses thereto;
- l) The chief finance officer, the chief internal auditor and a representative of the external auditors may normally attend meetings. Other board members and the chief executive officer may also attend meetings upon the invitation of the committee. However, at least twice a year, the committee shall meet with the external auditors without the executive directors being present.
- m) The committee shall have: (i) explicit authority to investigate into any matter within its terms of reference; (ii) the resources which it needs to do so; (iii) full access to information; and (iv) authority to obtain external professional advice and to invite outsiders with relevant experience to attend, if necessary.
- n) The committee shall meet regularly, with due notice of issues to be discussed and shall record its conclusions in discharging its duties and responsibilities.
- o) The board shall disclose in an informative way, (i) details of the activities of the audit committee; (ii) the number of audit committee meetings held in the year; and (iii) details of attendance of each individual director at such meetings.
- p) The secretary of the committee (who may be the company secretary or the head of the internal audit function) shall record and keep detailed minutes of the committee meetings.
- q) The committee shall review arrangements by which employees of the bank may, in confidence, raise concerns about possible improprieties in financial reporting, internal control or other matters. Accordingly, the committee shall ensure that proper arrangements are in place for the fair and independent investigation of such matters and for appropriate follow-up action and to act as the key representative body for overseeing the bank's relations with the external auditor.

3(6)(iii) The following rules shall apply in relation to the Human Resources and Remuneration Committee:

- a) The committee shall determine the remuneration policy (salaries, allowances and other financial payments) relating to directors, Chief Executive Officer (CEO) and key management personnel of the bank.
- b) The committee shall set goals and targets for the directors, CEO and the key management personnel.
- c) The committee shall evaluate the performance of the CEO and key management personnel against the set targets and goals periodically and determine the basis for revising remuneration, benefits and other payments of performance-based incentives.
- d) The CEO shall be present at all meetings of the committee, except when matters relating to the CEO are being discussed.

3(6)(iv) The following rules shall apply in relation to the Nomination Committee:

- a) The committee shall implement a procedure to select/appoint new directors, CEO and key management personnel.
- b) The committee shall consider and recommend (or not recommend) the re-election of current directors, taking into account the performance and contribution made by the director concerned towards the overall discharge of the board's responsibilities.
- c) The committee shall set the criteria such as qualifications, experience and key attributes required for eligibility to be considered for appointment or promotion to the post of CEO and the key management positions.
- d) The committee shall ensure that directors, CEO and key management personnel are fit and proper persons to hold office as specified in the criteria given in Direction 3(3) and as set out in the Statutes.
- e) The committee shall consider and recommend from time to time, the requirements of additional/new expertise and the succession arrangements for retiring directors and key management personnel.

- f) The Committee shall be chaired by an Independent Director and preferably be constituted with a majority of Independent Directors. The CEO may be present at meetings by invitation.

3(6)(v) The following rules shall apply in relation to the Integrated Risk Management Committee:

- a) The committee shall consist of at least three non-executive directors, chief executive officer and key management personnel supervising broad risk categories, i.e., credit, market, liquidity, operational and strategic risks. The committee shall work with key management personnel very closely and make decisions on behalf of the board within the framework of the authority and responsibility assigned to the committee.
- b) The committee shall assess all risks, i.e., credit, market, liquidity, operational and strategic risks to the bank on a monthly basis through appropriate risk indicators and management information. In the case of subsidiary companies and associate companies, risk management shall be done, both on a bank basis and group basis.
- c) The committee shall review the adequacy and effectiveness of all management level committees such as the credit committee and the asset-liability committee to address specific risks and to manage those risks within quantitative and qualitative risk limits as specified by the committee.
- d) The committee shall take prompt corrective action to mitigate the effects of specific risks in the case such risks are at levels beyond the prudent levels decided by the committee on the basis of the bank's policies and regulatory and supervisory requirements.
- e) The committee shall meet at least quarterly to assess all aspects of risk management including updated business continuity plans.
- f) The committee shall take appropriate actions against the officers responsible for failure to identify specific risks and take prompt corrective actions as recommended by the committee, and/or as directed by the Director of Bank Supervision.
- g) The committee shall submit a risk assessment report within a week of each meeting to the board seeking the board's views, concurrence and/or specific directions.
- h) The committee shall establish a compliance function to assess the bank's compliance with laws, regulations, regulatory guidelines, internal controls and approved policies on all areas of business operations. A dedicated compliance officer selected from key management personnel shall carry out the compliance function and report to the committee periodically.

3 (7) Related party transactions

3(7)(i) The board shall take the necessary steps to avoid any conflicts of interest that may arise from any transaction of the bank with any person, and particularly with the following categories of persons who shall be considered as related parties" for the purposes of this Direction:

- a) Any of the bank's subsidiary companies;
- b) Any of the bank's associate companies;
- c) Any of the directors of the bank;
- d) Any of the bank's key management personnel;
- e) A close relation of any of the bank's directors or key management personnel;
- f) A shareholder owning a material interest in the bank;
- g) A concern in which any of the bank's directors or a close relation of any of the bank's directors or any of its material shareholders has a substantial interest.

3(7)(ii) The type of transactions with related parties that shall be covered by this Direction shall include the following:

- a) The grant of any type of accommodation, as defined in the Monetary Board's Directions on maximum amount of accommodation,
- b) The creation of any liabilities of the bank in the form of deposits, borrowings and investments,
- c) The provision of any services of a financial or non-financial nature provided to the bank or received from the bank,

- d) The creation or maintenance of reporting lines and information flows between the bank and any related parties which may lead to the sharing of potentially proprietary, confidential or otherwise sensitive information that may give benefits to such related parties.
- 3(7)(iii)** The board shall ensure that the bank does not engage in transactions with related parties as defined in Direction 3(7)(i) above, in a manner that would grant such parties “more favourable treatment” than that accorded to other constituents of the bank carrying on the same business. In this context, “more favourable treatment” shall mean and include treatment, including the:
- a) Granting of “total net accommodation” to related parties, exceeding a prudent percentage of the bank’s regulatory capital, as determined by the board. For purposes of this sub-direction:
 - I. “Accommodation” shall mean accommodation as defined in the Banking Act Directions No. 7 of 2007 on Maximum Amount of Accommodation.
 - II. The “total net accommodation shall be” computed by deducting from the total accommodation, the cash collateral and investments made by such related parties in the bank’s share capital and debt instruments with a maturity of 5 years or more.
 - b) Charging of a lower rate of interest than the bank’s best lending rate or paying more than the bank’s deposit rate for a comparable transaction with an unrelated comparable counterparty;
 - c) Providing of preferential treatment, such as favourable terms, covering trade losses and/or waiving fees/commissions, that extend beyond the terms granted in the normal course of business undertaken with unrelated parties;
 - d) Providing services to or receiving services from a related-party without an evaluation procedure;
 - e) Maintaining reporting lines and information flows that may lead to sharing potentially proprietary, confidential or otherwise sensitive information with related parties, except as required for the performance of legitimate duties and functions.
- 3(7)(iv)** A bank shall not grant any accommodation to any of its directors or to a close relation of such director unless such accommodation is sanctioned at a meeting of its board of directors, with not less than two-thirds of the number of directors other than the director concerned, voting in favour of such accommodation. This accommodation shall be secured by such security as may from time to time be determined by the Monetary Board as well.
- 3(7)(v)** (a) Where any accommodation has been granted by a bank to a person or a close relation of a person or to any concern in which the person has a substantial interest, and such person is subsequently appointed as a director of the bank, steps shall be taken by the bank to obtain the necessary security as may be approved for that purpose by the Monetary Board, within one year from the date of appointment of the person as a director.
- (b) Where such security is not provided by the period as provided in Direction 3(7)(v)(a) above, the bank shall take steps to recover any amount due on account of any accommodation, together with interest, if any, within the period specified at the time of the grant of accommodation or at the expiry of a period of eighteen months from the date of appointment of such director, whichever is earlier.
- (c) Any director who fails to comply with the above sub-directions shall be deemed to have vacated the office of director and the bank shall disclose such fact to the public.
- (d) This sub-direction, however, shall not apply to a director who at the time of the grant of the accommodation was an employee of the bank and the accommodation was granted under a scheme applicable to all employees of such bank.
- 3(7)(vi)** A bank shall not grant any accommodation or “more favourable treatment” relating to the waiver of fees and/or commissions to any employee or a close relation of such employee or to any concern in which the employee or close relation has a substantial interest other than on the basis of a scheme applicable to the employees of such bank or when secured by security as may be approved by the Monetary Board in respect of accommodation granted as per Direction 3(7)(v) above.

3(7)(vii) No accommodation granted by a bank under Direction 3(7)(v) and 3(7)(vi) above, nor any part of such accommodation, nor any interest due thereon shall be remitted without the prior approval of the Monetary Board and any remission without such approval shall be void and of no effect.

3 (8) Disclosures

3(8)(i) The board shall ensure that: (a) annual audited financial statements and quarterly financial statements are prepared and published in accordance with the formats prescribed by the supervisory and regulatory authorities and applicable accounting standards, and that (b) such statements are published in the newspapers in an abridged form, in Sinhala, Tamil and English.

3(8)(ii) The board shall ensure that the following minimum disclosures are made in the Annual Report:

- a) A statement to the effect that the annual audited financial statements have been prepared in line with applicable accounting standards and regulatory requirements, inclusive of specific disclosures.
- b) A report by the board on the bank's internal control mechanism that confirms that the financial reporting system has been designed to provide reasonable assurance regarding the reliability of financial reporting, and that the preparation of financial statements for external purposes has been done in accordance with relevant accounting principles and regulatory requirements.
- c) The external auditor's certification on the effectiveness of the internal control mechanism referred to in Direction 3(8)(i)(b) above, in respect of any statements prepared or published after December 31, 2008.
- d) Details of directors, including names, fitness and propriety, transactions with the bank and the total of fees/remuneration paid by the bank.
- e) Total net accommodation as defined in 3(7)(iii) granted to each category of related parties. The net accommodation granted to each category of related parties shall also be disclosed as a percentage of the bank's regulatory capital.
- f) The aggregate values of remuneration paid by the bank to its key management personnel and the aggregate values of the transactions of the bank with its key management personnel, set out by broad categories such as remuneration paid, accommodation granted and deposits or investments made in the bank.
- g) The external auditor's certification of the compliance with these Directions in the annual corporate governance reports published after January 1, 2010.
- h) A report setting out details of the compliance with prudential requirements, regulations, laws and internal controls and measures taken to rectify any material non-compliances.
- i) A statement of the regulatory and supervisory concerns on lapses in the bank's risk management, or non compliance with these Directions that have been pointed out by the Director of Bank Supervision, if so directed by the Monetary Board to be disclosed to the public, together with the measures taken by the bank to address such concerns.

3(9) Transitional and other general provisions

3(9)(i) Compliance with this Direction shall commence from January 1, 2008 onwards and all licensed commercial banks shall fully comply with the provisions of this Direction by or before January 1, 2009 except where extended compliance dates have been specifically provided for in this Direction.

3(9)(ii) In respect of the banks that have been incorporated by specific statutes in Sri Lanka, the boards as specified in such statutes shall continue to function in terms of the provisions of the respective statutes, provided they take steps to comply with all provisions of this Direction that are not inconsistent with the provisions of the respective statutes.

3(9)(iii) This Direction shall apply to the branches of the foreign banks operating in Sri Lanka to the extent that it is not inconsistent with the regulations and laws applicable in such bank's country of incorporation. The branch of a foreign bank shall also publish its parent bank's annual corporate governance report together with its annual report and accounts of the branch operations in Sri Lanka.

3(9)(iv) In the event of a conflict between any of the provisions of this Direction and the Articles of Association (or Internal Rules) pertaining to any bank, the provisions of this Direction shall prevail. However, if the Articles of Association of an individual bank set a more stringent standard than that specified in this Direction, such provisions in the Articles of Association may be followed.

Directions issued by the Monetary Board of the Central Bank of Sri Lanka under Section 76J(1) of the Banking Act No. 30 of 1988, as amended.

Nivard Ajith Leslie Cabraal
Governor

Colombo
26 December 2007

DIRECTIONS
BANKING ACT DIRECTION NO. 12 OF 2007
CORPORATE GOVERNANCE FOR
LICENSED SPECIALISED BANKS IN SRI LANKA

In the exercise of the powers conferred by Section 76J(1) of the Banking Act No. 30 of 1988, last amended by the Banking Act No. 46 of 2006, the Monetary Board hereby issues the following Directions on Corporate Governance for Licensed Specialised Banks in Sri Lanka. These Directions may be cited as the Banking Act Direction No. 12 of 2007. The Sections referred to in these Directions will be those of the Banking Act No. 30 of 1988, last amended by the Banking Act No. 46 of 2006.

- 1. Responsibilities and Empowerment under the Banking Act and the Monetary Law Act**
 - 1(1)** In terms of Section 76J(1) of the Banking Act No. 30 of 1988 last amended by No. 46 of 2006, the Monetary Board has been empowered to issue Directions to licensed specialised banks or to any category of licensed specialised banks, regarding the manner in which any aspect of the business of such banks is to be conducted.
 - 1(2)** In terms of Section 5 of the Monetary Law Act No. 58 of 1949, the Central Bank of Sri Lanka is charged with the duty of securing, as far as possible by action authorised by such Act, the two objectives, namely, (a) economic and price stability and (b) financial system stability.
 - 1(3)** In terms of Section 10(c) of the Monetary Law Act, the Monetary Board, in the exercise of its powers, duties, functions and responsibilities, is empowered to make such rules and regulations as the Monetary Board may consider necessary, in relation to any matter affecting or connected with or incidental to the exercise, discharge, or performance of the powers, functions, and duties of the Central Bank of Sri Lanka.
 - 1(4)** Under the provisions of the Monetary Law Act No. 58 of 1949, the supervision of banks has been made a duty of the Central Bank on account of specific reasons as stated in John Exter's Report on the Monetary Law Act which states, *inter alia*, as follows: "*Banking is an economic activity which affects the public welfare to an unusual degree; it touches in one way or another, almost every phase of a country's economic life. Sound banking is essential to healthy and vigorous economic development. Supervision of banks helps to protect the public against mismanagement, bank failures, and loss of confidence in the banking system. It helps to protect depositors and stock-holders against loss and frequently enables bank directors and officers to manage the affairs of their banks more wisely and intelligently.*"
 - 1(5)** Accordingly, in order to enhance the overall banking sector stability which is the fundamental to financial system stability, the Monetary Board, hereby issues Directions under Section 76J(1) of the Banking Act No. 30 of 1988 to improve and sustain the corporate governance processes and practices of the licensed specialised banks in Sri Lanka.
 - 1(6)** For purposes of this Direction, Corporate Governance processes and practices shall be deemed to be the management framework that facilitates the conduct of the banking business in a responsible and accountable manner so as to promote the safety and soundness of the individual banks, thereby leading to the stability of the overall banking sector.
 - 1(7)** The rules of corporate governance as contained in Direction 3 of these Directions have, therefore, been developed on the basis of certain fundamental principles as set out in Direction 2 of these Directions with a view to facilitating the underlying supervisory responsibilities of the Central Bank and to promote safety and soundness of the banking system.
- 2. The Principles upon which the rules of Corporate Governance have been based upon and developed are the following:**

The principles set out in this Direction 2 should be referred to for explanatory purposes and/or for clarification purposes only, so as to understand the rationale for the rules as contained in Direction 3 hereof. Hence, strict compliance under these Directions shall only be in respect of the rules that are set out under Direction 3.

2(1) Principle: The Responsibilities of the Board

- 2(1)(i)** The board of directors should assume the overall responsibility and accountability in respect of: (a) the management of the affairs of the bank, i.e., conduct of business and maintenance of prudent risk management mechanisms; and (b) the safety and soundness of the bank.
- 2(1)(ii)** Towards this end, the board should: (a) determine the structure of the management of affairs of the bank; (b) delegate business operations to key management personnel led by the chief executive officer designated by the board; (c) assume policy making and risk management for the business; and (d) ensure the effective role of the key management personnel. Key management personnel shall mean such key executives of the bank as defined in the International Accounting Standards.
- 2(1)(iii)** The overall responsibility of the board should not be construed as an obligation to undertake the inspection of day-to-day activities, but should rather be understood as an obligation to oversee and ensure that the key management personnel are carrying out the day-to-day activities of the bank in a safe and sound manner in accordance with the policies set by the board.
- 2(1)(iv)** Directors should understand the business and risk management mechanism of the bank and take objective decisions in the interest of the bank's depositors, creditors, shareholders and other stakeholders. Further, they should ensure that the bank does not act in a manner that is detrimental or prejudicial to the interests of, and obligations to, depositors and creditors.
- 2(1)(v)** The board should take the responsibility for compliance with accepted rules of corporate governance. They should also ensure compliance with all regulatory and supervisory requirements. Further, they should ensure that an effective combination of professionals with practical experience in relevant subjects such as banking, finance, economics, business management, human resource management, law, marketing, information technology or any other discipline relevant or complementary to banking operations, is available in the bank to undertake its operations and discharge its responsibilities.
- 2(1)(vi)** The directors should be aware of potential civil and criminal liabilities that may arise from their failure to discharge their duties diligently. They should also understand that they should act with due care and prudence. In addition, the directors of state owned banks should be aware of the additional liabilities that arise from the status of such banks being state enterprises and consequently being accountable to the public. It is, therefore, necessary that directors commit sufficient time and energy to fulfilling the board's responsibilities in managing the affairs of the bank in a prudent manner.

2(2) Principle: The Board's composition

- 2(2)(i)** The board should be composed of a healthy mix of executive directors and non-executive directors. Some of the non-executive directors should also be independent so that there is strong independent element brought into the decision-making process.
- 2(2)(ii)** The board's composition should ensure a balance of skills and experience as may be deemed appropriate and desirable for the requirements of the bank.
- 2(2)(iii)** The banking industry worldwide is making tremendous progress and undergoing rapid change with new innovations, instruments, technologies, products, systems and processes being introduced regularly. It is vital therefore, that the directors should be persons who would: (a) be able to keep abreast with these changes, and (b) provide continuous contribution and guidance to the board decision-making process.
- 2(2)(iv)** There should be a gradual infusion of new ideas into the board. There should also be assurance that the relationships between the directors amongst themselves as well as between the directors and the key management personnel is at a level that does not suggest the existence of excessive familiarity, undue influence or coercion. In this context, it should be noted that very long-standing relationships could sometimes impair the high sense of values, independence and objectivity that is needed in the discharge of the duties of a director of a bank.

2(3) Principle: Criteria to assess the Fitness and Propriety of Directors

- 2(3)(i)** In addition to the principles under the board's composition in Direction 2(2) above, directors should be fit and proper persons in order to be eligible to hold office as directors of a bank and no person should serve as a director unless such person is a fit and proper person.
- 2(3)(ii)** There is strong need for commitment and effective contribution to the prudent management of the affairs of the bank. It is very likely that the effectiveness of such commitment and contribution would tend to decrease with advanced age of directors and more particularly, if the age of such director is well beyond the normal age of retirement, as generally accepted in the country.

2(4) Principle: Management functions delegated by the Board

- 2(4)(i)** The board should have a formal schedule of matters specifically reserved to it for decision. The board should also give clear directions to key management personnel, as to the matters that should be approved by the board before decisions are made by key management personnel, on behalf of the bank.

2(5) Principle: The Chairman and the Chief Executive Officer

- 2(5)(i)** There are two key aspects of the management of every bank, viz., (a) the overall governance by the board, and (b) the day-to-day management of the bank's business by the CEO, in line with board approved strategic objectives, corporate values, overall risk policy and risk management procedures.
- 2(5)(ii)** There should be a clear division of these responsibilities at the board level and the executive management level to ensure a greater balance of power and authority, so that powers are not concentrated in any one individual.
- 2(5)(iii)** The board should appoint a chairman as well as a chief executive officer. The division of responsibilities between the chairman and chief executive officer should be clearly established and set out in writing.

2(6) Principle: Board appointed Committees

- 2(6)(i)** The board should appoint separate board committees for audit, selection, remuneration, integrated risk management and such other subjects as determined by the Board to ensure its oversight and control over the affairs of the bank.
- 2(6)(ii)** Where the board appoints a committee, it should set out the authority of the committee, and in particular, whether the committee has the authority to act on behalf of the board or simply has the authority to examine a particular issue and report back to the board with recommendations.
- 2(6)(iii)** Each committee should be chaired by a non-executive director who has some expertise in the relevant subject, and who preferably should be independent too. The majority of the members of the board committee should consist of non-executive directors with at least one independent director in the committee. If a need arises, professionals from outside may be invited or hired to serve in a committee. Bank staff may be present at the board committees for advice or special assignments, on invitation.

2(7) Principle: Related party transactions

- 2(7)(i)** The board should ensure that the bank does not engage in transactions with "related parties" in a manner that would grant such parties "more favourable treatment" than that accorded to other constituents of the bank carrying on the same business.

2(8) Principle: Disclosures

- 2(8)(i)** The objective of disclosure is the transparency of information relating to affairs and risk management of banks which would help to promote market discipline of the respective banks.
- 2(8)(ii)** Since market disclosure is the focus of the Pillar III of the risk management based capital standard known as Basel II recommended by the Basel Committee on Banking Supervision at the Bank for International Settlements, (which is the globally accepted body on introducing international standards on Bank Supervision), the extent of disclosures should be commensurate with the size, ownership structure, systemic importance, risk profile and the business model of the bank. Accordingly, it should be noted that the adequate and timely public disclosure of relevant information by banks would facilitate enhanced market discipline and lead to better and more effective corporate governance.

- 2(8)(iii)** Disclosures by banks should generally include disclosures relating to capital adequacy, key performance indicators, business concentrations, transactions with related parties, corporate governance statements, financial statements, etc., and should be consistent with accounting standards, regulatory requirements as well as with any other information disclosed on voluntary basis.
- 3. The following rules of Corporate Governance shall be complied by all licensed specialised banks in Sri Lanka and such compliance shall be as provided for in Direction 3(9)(i) hereof.**
- 3 (1) The Responsibilities of the Board**
- 3(1)(i)** The board shall strengthen the safety and soundness of the bank by ensuring the implementation of the following:
- a) Approve and oversee the bank's strategic objectives and corporate values and ensure that these are communicated throughout the bank;
 - b) Approve the overall business strategy of the bank, including the overall risk policy and risk management procedures and mechanisms with measurable goals, for at least the next three years;
 - c) Identify the principal risks and ensure implementation of appropriate systems to manage the risks prudently;
 - d) Approve implementation of a policy of communication with all stakeholders, including depositors, creditors, share-holders and borrowers;
 - e) Review the adequacy and the integrity of the bank's internal control systems and management information systems;
 - f) Identify and designate key management personnel, as defined in the International Accounting Standards, who are in a position to: (i) significantly influence policy; (ii) direct activities; and (iii) exercise control over business activities, operations and risk management;
 - g) Define the areas of authority and key responsibilities for the board directors themselves and for the key management personnel;
 - h) Ensure that there is appropriate oversight of the affairs of the bank by key management personnel, that is consistent with board policy;
 - i) Periodically assess the effectiveness of the board directors' own governance practices, including: (i) the selection, nomination and election of directors and key management personnel; (ii) the management of conflicts of interests; and (iii) the determination of weaknesses and implementation of changes where necessary;
 - j) Ensure that the bank has an appropriate succession plan for key management personnel;
 - k) Meet regularly, on a needs basis, with the key management personnel to review policies, establish communication lines and monitor progress towards corporate objectives;
 - l) Understand the regulatory environment and ensure that the bank maintains an effective relationship with regulators;
 - m) Exercise due diligence in the hiring and oversight of external auditors.
- 3(1)(ii)** The board shall appoint the chairman and the chief executive officer and define and approve the functions and responsibilities of the chairman and the chief executive officer in line with Direction 3(5) of these Directions.
- 3(1)(iii)** The board shall meet regularly and board meetings shall be held at least twelve times a year at approximately monthly intervals. Such regular board meetings shall normally involve active participation in person of a majority of directors entitled to be present. Obtaining the board's consent through the circulation of written resolutions/papers shall be avoided as far as possible.
- 3(1)(iv)** The board shall ensure that arrangements are in place to enable all directors to include matters and proposals in the agenda for regular board meetings, where such matters and proposals relate to the promotion of business and the management of risks of the bank.
- 3(1)(v)** The board procedures shall ensure that notice of at least 7 days is given of a regular board meeting to provide all directors an opportunity to attend. For all other board meetings, reasonable notice may be given.

- 3(1)(vi)** The board procedures shall ensure that a director who has not attended at least two-thirds of the meetings in the period of 12 months immediately preceding or has not attended the immediately preceding three consecutive meetings held, shall cease to be a director. Participation at the directors' meetings through an alternate director shall, however, be acceptable as attendance.
- 3(1)(vii)** The board shall appoint a company secretary who satisfies the provisions of Section 43 read with Section 76H of the Banking Act No. 30 of 1988, whose primary responsibilities shall be to handle the secretariat services to the board and shareholder meetings and to carry out other functions specified in the statutes and other regulations.
- 3(1)(viii)** All directors shall have access to advice and services of the company secretary with a view to ensuring that board procedures and all applicable rules and regulations are followed.
- 3(1)(ix)** The company secretary shall maintain the minutes of board meetings and such minutes shall be open for inspection at any reasonable time, on reasonable notice by any director.
- 3(1)(x)** Minutes of board meetings shall be recorded in sufficient detail so that it is possible to gather from the minutes, as to whether the board acted with due care and prudence in performing its duties. The minutes shall also serve as a reference for regulatory and supervisory authorities to assess the depth of deliberations at the board meetings. Therefore, the minutes of a board meeting shall clearly contain or refer to the following: (a) a summary of data and information used by the board in its deliberations; (b) the matters considered by the board; (c) the fact-finding discussions and the issues of contention or dissent which may illustrate whether the board was carrying out its duties with due care and prudence; (d) the testimonies and confirmations of relevant executives which indicate compliance with the board's strategies and policies and adherence to relevant laws and regulations; (e) the board's knowledge and understanding of the risks to which the bank is exposed and an overview of the risk management measures adopted; and (f) the decisions and board resolutions.
- 3(1)(xi)** There shall be a procedure agreed by the board to enable directors, upon reasonable request, to seek independent professional advice in appropriate circumstances, at the bank's expense. The board shall resolve to provide separate independent professional advice to directors to assist the relevant director or directors to discharge his/her/their duties to the bank.
- 3(1)(xii)** Directors shall avoid conflicts of interests, or the appearance of conflicts of interest, in their activities with, and commitments to, other organisations or related parties. If a director has a conflict of interest in a matter to be considered by the board, which the board has determined to be material, the matter should be dealt with at a board meeting, where independent non-executive directors [refer to Direction 3(2)(iv) of these Directions] who have no material interest in the transaction, are present. Further, a director shall abstain from voting on any board resolution in relation to which he/she or any of his/her close relation or a concern in which a director has substantial interest, is interested and he/she shall not be counted in the quorum for the relevant agenda item at the board meeting.
- 3(1)(xiii)** The board shall have a formal schedule of matters specifically reserved to it for decision to ensure that the direction and control of the bank is firmly under its authority.
- 3(1)(xiv)** The board shall, if it considers that the bank is, or is likely to be, unable to meet its obligations or is about to become insolvent or is about to suspend payments due to depositors and other creditors, forthwith inform the Director of Bank Supervision of the situation of the bank prior to taking any decision or action.
- 3(1)(xv)** The board shall ensure that the bank is capitalised at levels as required by the Monetary Board in terms of the capital adequacy ratio and other prudential grounds.
- 3(1)(xvi)** The board shall publish in the bank's Annual Report, an annual corporate governance report setting out the compliance with Direction 3 of these Directions.
- 3(1)(xvii)** The board shall adopt a scheme of self-assessment to be undertaken by each director annually, and maintain records of such assessments.
- 3(2) The Board's Composition**
- 3(2)(i)** The number of directors on the board shall not be less than 7 and not more than 13.
- 3(2)(ii)** (A) 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, and such period in office shall be inclusive of the total period of service served by such director up to January 1, 2008.

(B) In this context, the following transitional provisions shall apply:

- a) In the event that there is only one director on the board who has served more than nine years as at January 1, 2008, he/she shall be deemed to have vacated the office as a director as at December 31, 2008.
- b) In the event that there are two or more directors on the board who have served more than nine years as at January 1, 2008, the following provisions shall apply:
 - I. Of those directors whose period of service has exceeded nine years, the longest serving director, shall be deemed to have vacated office as a Director on December 31, 2008.
 - II. Thereafter, at the end of each succeeding year, the remaining directors shall be deemed to have vacated office in sequence, at least one director each year, (on the basis of the longest to the shortest length of service as a director), until all directors who have served a period in excess of nine years as at January 1, 2008, have been deemed to have vacated office. Provided also, that all directors of the bank who have served more than nine years as at January 1, 2008 shall be deemed to have vacated their office by or before December 31, 2011.
- c) In the event there are any directors who are due to complete nine years of service between January 1, 2008 and December 31, 2010, such directors shall also be deemed to have vacated office, in sequence, at least one director each year, (on the basis of the longest to the shortest length of service as a director), after the directors as set out in Direction 3(2)(ii)(B) (b) have vacated their office as directors. Provided, however, that all such directors covered by this sub-direction (c) shall also be deemed to have vacated their office by or before December 31, 2011.

3(2)(iii) An employee of a bank may be appointed, elected or nominated as a director of the bank (hereinafter referred to as an “executive director”) provided that the number of executive directors shall not exceed one-third of the number of directors of the board. In such an event, one of the executive directors shall be the chief executive officer of the bank.

3(2)(iv) The board shall have at least three independent non-executive directors or one third of the total number of directors, whichever is higher. This sub-direction shall be applicable from January 1, 2010 onwards.

A non-executive director shall not be considered independent if he/she:

- a) has direct and indirect shareholdings of more than 1% of the bank;
- b) currently has or had during the period of two years immediately preceding his/her appointment as director, any business transactions with the bank as described in Direction 3 (7) hereof, exceeding 10% of the regulatory capital of the bank.
- c) has been employed by the bank during the two year period immediately preceding the appointment as director;
- d) has a close relation who is a director or chief executive officer or a member of key management personnel or a material shareholder of the bank or another bank. For this purpose, a “close relation” shall mean the spouse or a financially dependant child;
- e) represents a specific stakeholder of the bank;
- f) is an employee or a director or a material shareholder in a company or business organization:

I. which currently has a transaction with the bank as defined in Direction 3(7) of these Directions, exceeding 10% of the regulatory capital of the bank, or

II. in which any of the other directors of the bank are employed or are directors or are material shareholders; or

III. in which any of the other directors of the bank have a transaction as defined in Direction 3(7) of these Directions, exceeding 10% of regulatory capital in the bank;

3(2)(v) In the event an alternate director is appointed to represent an independent director, the person so appointed shall also meet the criteria that applies to the independent director.

- 3(2)(vi)** Non-executive directors shall be persons with credible track records and/or have necessary skills and experience to bring an independent judgment to bear on issues of strategy, performance and resources.
- (2)(vii)** A meeting of the board shall not be duly constituted, although the number of directors required to constitute the quorum at such meeting is present, unless more than one half of the number of directors present at such meeting are non-executive directors. This sub-direction shall be applicable from January 1, 2010 onwards.
- 3(2)(viii)** The independent non-executive directors shall be expressly identified as such in all corporate communications that disclose the names of directors of the bank. The bank shall disclose the composition of the board, by category of directors, including the names of the chairman, executive directors, non-executive directors and independent non-executive directors in the annual corporate governance report.
- 3(2)(ix)** There shall be a formal, considered and transparent procedure for the appointment of new directors to the board. There shall also be procedures in place for the orderly succession of appointments to the board.
- 3(2)(x)** All directors appointed to fill a casual vacancy shall be subject to election by shareholders at the first general meeting after their appointment.
- 3(2)(xi)** If a director resigns or is removed from office, the board shall: (a) announce the director's resignation or removal and the reasons for such removal or resignation including but not limited to information relating to the relevant director's disagreement with the bank, if any; and (b) issue a statement confirming whether or not there are any matters that need to be brought to the attention of shareholders.
- 3(2)(xii)** A director or an employee of a bank shall not be appointed, elected or nominated as a director of another bank except where such bank is a subsidiary company or an associate company of the first mentioned bank.
- 3(3) Criteria to assess the fitness and propriety of directors**
In addition to provisions of Section 42 read with Section 76H of the Banking Act No. 30 of 1988, the criteria set out below shall apply to determine the fitness and propriety of a person who serves or wishes to serve as a director of a bank. Non-compliance with any one of the criteria as set out herein shall disqualify a person to be appointed, elected or nominated as a director or to continue as a director.
- 3(3)(i)** The age of a person who serves as director shall not exceed 70 years.
- (A) Where a director who is currently serving at a bank is over 70 years of age as at January 1, 2008, the following transitional provisions shall apply, subject, however, to the provisions as set out in Direction 3(2)(ii) hereof.
- a) If a director is over 75 years of age as at January 1, 2008, such director may continue to serve as a director for a further period that shall not extend beyond December 31, 2008, and shall be deemed to have vacated office on December 31, 2008;
- b) If a director is between 70 and 75 years of age as at January 1, 2008, such director may continue to serve as a director for a further period that shall not extend beyond December 31, 2009, and shall be deemed to have vacated office on December 31, 2009.
- (B) Where a director who is currently serving at a bank reaches the age of 70 years, between January 1, 2008 and December 31, 2009, such director may, subject to the provisions as set out in Direction 3(2)(ii) hereof, continue to serve as a director for a further period that shall not extend beyond December 31, 2010 and shall be deemed to have vacated office on December 31, 2010.
- 3(3)(ii)** A person shall not hold office as a director of more than 20 companies/entities/institutions inclusive of subsidiaries or associate companies of the bank. Of such 20 companies/entities/ institutions, not more than 10 companies shall be those classified as Specified Business Entities in terms of the Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995.
- 3(4) Management functions delegated by the Board**
- 3(4)(i)** The directors shall carefully study and clearly understand the delegation arrangements in place.
- 3(4)(ii)** The board shall not delegate any matters to a board committee, chief executive officer, executive directors or key management personnel, to an extent that such delegation would significantly hinder or reduce the ability of the board as a whole to discharge its functions.

3(4)(iii) The board shall review the delegation processes in place on a periodic basis to ensure that they remain relevant to the needs of the bank.

3(5) The Chairman and Chief Executive Officer

3(5)(i) The roles of chairman and chief executive officer shall be separate and shall not be performed by the same individual.

3(5)(ii) The chairman shall be a non-executive director and preferably an independent director as well. In the case where the chairman is not an independent director, the board shall designate an independent director as the Senior Director with suitably documented terms of reference to ensure a greater independent element. The designation of the Senior Director shall be disclosed in the bank's Annual Report.

3(5)(iii) The board shall disclose in its corporate governance report, which shall be an integral part of its Annual Report, the identity of the chairman and the chief executive officer and the nature of any relationship [including financial, business, family or other material/relevant relationship(s)], if any, between the chairman and the chief executive officer and the relationships among members of the board.

3(5)(iv) The chairman shall: (a) provide leadership to the board; (b) ensure that the board works effectively and discharges its responsibilities; and (c) ensure that all key and appropriate issues are discussed by the board in a timely manner.

3(5)(v) The chairman shall be primarily responsible for drawing up and approving the agenda for each board meeting, taking into account where appropriate, any matters proposed by the other directors for inclusion in the agenda. The chairman may delegate the drawing up of the agenda to the company secretary.

3(5)(vi) The chairman shall ensure that all directors are properly briefed on issues arising at board meetings and also ensure that directors receive adequate information in a timely manner.

3(5)(vii) The chairman shall encourage all directors to make a full and active contribution to the board's affairs and take the lead to ensure that the board acts in the best interests of the bank.

3(5)(viii) The chairman shall facilitate the effective contribution of non-executive directors in particular and ensure constructive relations between executive and non-executive directors.

3(5)(ix) The chairman, shall not engage in activities involving direct supervision of key management personnel or any other executive duties whatsoever.

3(5)(x) The chairman shall ensure that appropriate steps are taken to maintain effective communication with shareholders and that the views of shareholders are communicated to the board.

3(5)(xi) The chief executive officer shall function as the apex executive-in-charge of the day-to-day-management of the bank's operations and business.

3(6) Board appointed Committees

3(6)(i) Each bank shall have at least four board committees as set out in Directions 3(6)(ii), 3(6)(iii), 3(6)(iv) and 3(6)(v) of these Directions. Each committee shall report directly to the board. All committees shall appoint a secretary to arrange the meetings and maintain minutes, records, etc., under the supervision of the chairman of the committee. The board shall present a report of the performance on each committee, on their duties and roles at the annual general meeting.

3(6)(ii) The following rules shall apply in relation to the Audit Committee:

- a) The chairman of the committee shall be an independent non-executive director who possesses qualifications and experience in accountancy and/or audit.
- b) All members of the committee shall be non-executive directors.
- c) The committee shall make recommendations on matters in connection with: (i) the appointment of the external auditor for audit services to be provided in compliance with the relevant statutes; (ii) the implementation of the Central Bank guidelines issued to auditors from time to time; (iii) the application of the relevant accounting standards; and (iv) the service period, audit fee and any resignation or dismissal of the auditor; provided that the engagement of the Audit partner shall not exceed five years, and that the particular Audit partner is not re-engaged for the audit before the expiry of three years from the date of

the completion of the previous term.

- d) The committee shall review and monitor the external auditor's independence and objectivity and the effectiveness of the audit processes in accordance with applicable standards and best practices.
- e) The committee shall develop and implement a policy on the engagement of an external auditor to provide non-audit services that are permitted under the relevant statutes, regulations, requirements and guidelines. In doing so, the committee shall ensure that the provision by an external auditor of non-audit services does not impair the external auditor's independence or objectivity. When assessing the external auditor's independence or objectivity in relation to the provision of non-audit services, the committee shall consider:
 - I. whether the skills and experience of the audit firm make it a suitable provider of the non-audit services;
 - II. whether there are safeguards in place to ensure that there is no threat to the objectivity and/or independence in the conduct of the audit resulting from the provision of such services by the external auditor; and
 - III. whether the nature of the non-audit services, the related fee levels and the fee levels individually and in aggregate relative to the audit firm, pose any threat to the objectivity and/or independence of the external auditor.
- f) The committee shall, before the audit commences, discuss and finalise with the external auditors the nature and scope of the audit, including: (i) an assessment of the bank's compliance with the relevant Directions in relation to corporate governance and the management's internal controls over financial reporting; (ii) the preparation of financial statements for external purposes in accordance with relevant accounting principles and reporting obligations; and (iii) the co-ordination between firms where more than one audit firm is involved.
- g) The committee shall review the financial information of the bank, in order to monitor the integrity of the financial statements of the bank, its annual report, accounts and quarterly reports prepared for disclosure, and the significant financial reporting judgments contained therein. In reviewing the bank's annual report and accounts and quarterly reports before submission to the board, the committee shall focus particularly on: (i) major judgmental areas; (ii) any changes in accounting policies and practices; (iii) significant adjustments arising from the audit; (iv) the going concern assumption; and (v) the compliance with relevant accounting standards and other legal requirements.
- h) The committee shall discuss issues, problems and reservations arising from the interim and final audits, and any matters the auditor may wish to discuss including those matters that may need to be discussed in the absence of key management personnel, if necessary.
- i) The committee shall review the external auditor's management letter and the management's response thereto.
- j) The committee shall take the following steps with regard to the internal audit function of the bank:
 - I. Review the adequacy of the scope, functions and resources of the internal audit department, and satisfy itself that the department has the necessary authority to carry out its work;
 - II. Review the internal audit programme and results of the internal audit process and, where necessary, ensure that appropriate actions are taken on the recommendations of the internal audit department;
 - III. Review any appraisal or assessment of the performance of the head and senior staff members of the internal audit department;
 - IV. Recommend any appointment or termination of the head, senior staff members and outsourced service providers to the internal audit function;
 - V. Ensure that the committee is appraised of resignations of senior staff members of the internal audit department including the chief internal auditor and any outsourced service providers, and to provide an opportunity to the resigning senior staff members and outsourced service providers to submit reasons for resigning;

VI. Ensure that the internal audit function is independent of the activities it audits and that it is performed with impartiality, proficiency and due professional care;

- k) The committee shall consider the major findings of internal investigations and management's responses thereto;
- l) The chief finance officer, the chief internal auditor and a representative of the external auditors may normally attend meetings. Other board members and the chief executive officer may also attend meetings upon the invitation of the committee. However, at least twice a year, the committee shall meet with the external auditors without the executive directors being present.
- m) The committee shall have: (i) explicit authority to investigate into any matter within its terms of reference; (ii) the resources which it needs to do so; (iii) full access to information; and (iv) authority to obtain external professional advice and to invite outsiders with relevant experience to attend, if necessary.
- n) The committee shall meet regularly, with due notice of issues to be discussed and shall record its conclusions in discharging its duties and responsibilities.
- o) The board shall disclose in an informative way, (i) details of the activities of the audit committee; (ii) the number of audit committee meetings held in the year; and (iii) details of attendance of each individual director at such meetings.
- p) The secretary of the committee (who may be the company secretary or the head of the internal audit function) shall record and keep detailed minutes of the committee meetings.
- q) The committee shall review arrangements by which employees of the bank may, in confidence, raise concerns about possible improprieties in financial reporting, internal control or other matters. Accordingly, the committee shall ensure that proper arrangements are in place for the fair and independent investigation of such matters and for appropriate follow-up action and to act as the key representative body for overseeing the bank's relations with the external auditor.

3(6)(iii) The following rules shall apply in relation to the Human Resources and Remuneration Committee:

- a) The committee shall determine the remuneration policy (salaries, allowances and other financial payments) relating to directors, Chief Executive Officer (CEO) and key management personnel of the bank.
- b) The committee shall set goals and targets for the directors, CEO and the key management personnel.
- c) The committee shall evaluate the performance of the CEO and key management personnel against the set targets and goals periodically and determine the basis for revising remuneration, benefits and other payments of performance-based incentives.
- d) The CEO shall be present at all meetings of the committee, except when matters relating to the CEO are being discussed.

3(6)(iv) The following rules shall apply in relation to the Nomination Committee:

- a) The committee shall implement a procedure to select/appoint new directors, CEO and key management personnel.
- b) The committee shall consider and recommend (or not recommend) the re-election of current directors, taking into account the performance and contribution made by the director concerned towards the overall discharge of the board's responsibilities.
- c) The committee shall set the criteria such as qualifications, experience and key attributes required for eligibility to be considered for appointment or promotion to the post of CEO and the key management positions.
- d) The committee shall ensure that directors, CEO and key management personnel are fit and proper persons to hold office as specified in the criteria given in Direction 3(3) and as set out in the Statutes.
- e) The committee shall consider and recommend from time to time, the requirements of additional/new expertise and the succession arrangements for retiring directors and key management personnel.
- f) The Committee shall be chaired by an Independent Director and preferably be constituted with a majority of Independent Directors. The CEO may be present at meetings by invitation.

3(6)(v) The following rules shall apply in relation to the Integrated Risk Management Committee:

- a) The committee shall consist of at least three non-executive directors, chief executive officer and key management personnel supervising broad risk categories, i.e., credit, market, liquidity, operational and strategic risks. The committee shall work with key management personnel very closely and make decisions on behalf of the board within the framework of the authority and responsibility assigned to the committee.
- b) The committee shall assess all risks, i.e., credit, market, liquidity, operational and strategic risks to the bank on a monthly basis through appropriate risk indicators and management information. In the case of subsidiary companies and associate companies, risk management shall be done, both on a bank basis and group basis.
- c) The committee shall review the adequacy and effectiveness of all management level committees such as the credit committee and the asset-liability committee to address specific risks and to manage those risks within quantitative and qualitative risk limits as specified by the committee.
- d) The committee shall take prompt corrective action to mitigate the effects of specific risks in the case such risks are at levels beyond the prudent levels decided by the committee on the basis of the bank's policies and regulatory and supervisory requirements.
- e) The committee shall meet at least quarterly to assess all aspects of risk management including updated business continuity plans.
- f) The committee shall take appropriate actions against the officers responsible for failure to identify specific risks and take prompt corrective actions as recommended by the committee, and/or as directed by the Director of Bank Supervision.
- g) The committee shall submit a risk assessment report within a week of each meeting to the board seeking the board's views, concurrence and/or specific directions.
- h) The committee shall establish a compliance function to assess the bank's compliance with laws, regulations, regulatory guidelines, internal controls and approved policies on all areas of business operations. A dedicated compliance officer selected from key management personnel shall carry out the compliance function and report to the committee periodically.

3 (7) Related party transactions**3(7)(i)** The board shall take the necessary steps to avoid any conflicts of interest that may arise from any transaction of the bank with any person, and particularly with the following categories of persons who shall be considered as "related parties" for the purposes of this Direction:

- a) Any of the bank's subsidiary companies;
- b) Any of the bank's associate companies;
- c) Any of the directors of the bank;
- d) Any of the bank's key management personnel;
- e) A close relation of any of the bank's directors or key management personnel;
- f) A shareholder owning a material interest in the bank;
- g) A concern in which any of the bank's directors or a close relation of any of the bank's directors or any of its material shareholders has a substantial interest.

3(7)(ii) The type of transactions with related parties that shall be covered by this Direction shall include the following:

- a) The grant of any type of accommodation, as defined in the Monetary Board's Directions on maximum amount of accommodation,
- b) The creation of any liabilities of the bank in the form of deposits, borrowings and investments,
- c) The provision of any services of a financial or non-financial nature provided to the bank or received from the bank,
- d) The creation or maintenance of reporting lines and information flows between the bank and any related parties which may lead to the sharing of potentially proprietary, confidential or otherwise sensitive information that may give benefits to such related parties.

- 3(7)(iii)** The board shall ensure that the bank does not engage in transactions with related parties as defined in Direction 3(7)(i) above, in a manner that would grant such parties “more favourable treatment” than that accorded to other constituents of the bank carrying on the same business. In this context, “more favourable treatment” shall mean and include treatment, including the:
- a) Granting of “total net accommodation” to related parties, exceeding a prudent percentage of the bank’s regulatory capital, as determined by the board. For purposes of this sub-direction:
 - I. “Accommodation” shall mean accommodation as defined in the Banking Act Directions No. 8 of 2007 on Maximum Amount of Accommodation.
 - II. The “total net accommodation shall be” computed by deducting from the total accommodation, the cash collateral and investments made by such related parties in the bank’s share capital and debt instruments with a maturity of 5 years or more.
 - b) Charging of a lower rate of interest than the bank’s best lending rate or paying more than the bank’s deposit rate for a comparable transaction with an unrelated comparable counterparty;
 - c) Providing of preferential treatment, such as favourable terms, covering trade losses and/or waiving fees/commissions, that extend beyond the terms granted in the normal course of business undertaken with unrelated parties;
 - d) Providing services to or receiving services from a related-party without an evaluation procedure;
 - e) Maintaining reporting lines and information flows that may lead to sharing potentially proprietary, confidential or otherwise sensitive information with related parties, except as required for the performance of legitimate duties and functions.
- 3(7)(iv)** A bank shall not grant any accommodation to any of its directors or to a close relation of such director unless such accommodation is sanctioned at a meeting of its board of directors, with not less than two-thirds of the number of directors other than the director concerned, voting in favour of such accommodation. This accommodation shall be secured by such security as may from time to time be determined by the Monetary Board as well.
- 3(7)(v)**
- (a) Where any accommodation has been granted by a bank to a person or a close relation of a person or to any concern in which the person has a substantial interest, and such person is subsequently appointed as a director of the bank, steps shall be taken by the bank to obtain the necessary security as may be approved for that purpose by the Monetary Board, within one year from the date of appointment of the person as a director.
 - (b) Where such security is not provided by the period as provided in Direction 3(7)(v)(a) above, the bank shall take steps to recover any amount due on account of any accommodation, together with interest, if any, within the period specified at the time of the grant of accommodation or at the expiry of a period of eighteen months from the date of appointment of such director, whichever is earlier.
 - (c) Any director who fails to comply with the above sub-directions shall be deemed to have vacated the office of director and the bank shall disclose such fact to the public.
 - (d) This sub-direction, however, shall not apply to a director who at the time of the grant of the accommodation was an employee of the bank and the accommodation was granted under a scheme applicable to all employees of such bank.
- 3(7)(vi)** A bank shall not grant any accommodation or “more favourable treatment” relating to the waiver of fees and/or commissions to any employee or a close relation of such employee or to any concern in which the employee or close relation has a substantial interest other than on the basis of a scheme applicable to the employees of such bank or when secured by security as may be approved by the Monetary Board in respect of accommodation granted as per Direction 3(7)(v) above.
- 3(7)(vii)** No accommodation granted by a bank under Direction 3(7)(v) and 3(7)(vi) above, nor any part of such accommodation, nor any interest due thereon shall be remitted without the prior approval of the Monetary Board and any remission without such approval shall be void and of no effect.

3 (8) Disclosures

- 3(8)(i)** The board shall ensure that: (a) annual audited financial statements and quarterly financial statements are prepared and published in accordance with the formats prescribed by the supervisory and regulatory authorities and applicable accounting standards, and that (b) such statements are published in the newspapers in an abridged form, in Sinhala, Tamil and English.
- 3(8)(ii)** The board shall ensure that the following minimum disclosures are made in the Annual Report:
- a) A statement to the effect that the annual audited financial statements have been prepared in line with applicable accounting standards and regulatory requirements, inclusive of specific disclosures.
 - b) A report by the board on the bank's internal control mechanism that confirms that the financial reporting system has been designed to provide reasonable assurance regarding the reliability of financial reporting, and that the preparation of financial statements for external purposes has been done in accordance with relevant accounting principles and regulatory requirements.
 - c) The external auditor's certification on the effectiveness of the internal control mechanism referred to in Direction 3(8)(ii)(b) above, in respect of any statements prepared or published after December 31, 2008.
 - d) Details of directors, including names, fitness and propriety, transactions with the bank and the total of fees/remuneration paid by the bank.
 - e) Total net accommodation as defined in 3(7)(iii) granted to each category of related parties. The net accommodation granted to each category of related parties shall also be disclosed as a percentage of the bank's regulatory capital.
 - f) The aggregate values of remuneration paid by the bank to its key management personnel and the aggregate values of the transactions of the bank with its key management personnel, set out by broad categories such as remuneration paid, accommodation granted and deposits or investments made in the bank.
 - g) The external auditor's certification of the compliance with these Directions in the annual corporate governance reports published after January 1, 2010.
 - h) A report setting out details of the compliance with prudential requirements, regulations, laws and internal controls and measures taken to rectify any material non-compliances.
 - i) A statement of the regulatory and supervisory concerns on lapses in the bank's risk management, or non compliance with these Directions that have been pointed out by the Director of Bank Supervision, if so directed by the Monetary Board to be disclosed to the public, together with the measures taken by the bank to address such concerns.

3(9) Transitional and other general provisions

- 3(9)(i)** Compliance with this Direction shall commence from January 1, 2008 onwards and all licensed specialised banks shall fully comply with the provisions of this Direction by or before January 1, 2009 except where extended compliance dates have been specifically provided for in this Direction.
- 3(9)(ii)** In respect of the banks that have been incorporated by specific statutes in Sri Lanka, the boards as specified in such statutes shall continue to function in terms of the provisions of the respective statutes, provided they take steps to comply with all provisions of this Direction that are not inconsistent with the provisions of the respective statutes.
- 3(9)(iii)** This Direction shall apply to the branches of the foreign banks operating in Sri Lanka to the extent that it is not inconsistent with the regulations and laws applicable in such bank's country of incorporation. The branch of a foreign bank shall also publish its parent bank's annual corporate governance report together with its annual report and accounts of the branch operations in Sri Lanka.
- 3(9)(iv)** In the event of a conflict between any of the provisions of this Direction and the Articles of Association (or Internal Rules) pertaining to any bank, the provisions of this Direction shall prevail. However, if the Articles of Association of an individual bank set a more stringent standard than that specified in this Direction, such provisions in the Articles of Association may be followed.

Bank Supervision Department
31 December 2007

Mr. S A Weerasinghe
General Manager
State Mortgage and Investment Bank
269, Galle Road
Colombo 3

Dear Sir

DIRECTION ON LIQUID ASSETS

With a view to strengthening the safety and soundness of the State Mortgage and Investment Bank (SMIB), the Monetary Board of the Central Bank of Sri Lanka has decided to revoke the separate Direction issued to SMIB on the maintenance of the Statutory Liquid Assets on 21 November 1997 under Sections 76 J (3) of the Banking Act and replace the same with the Direction issued to other Licensed Specialised Banks (LSBs), with effect from 1st January 2008. The applicable Direction issued under Section 76J (1) of the Banking Act is attached herewith.

The Monetary Board has also decided to grant time till 31 December 2008 to comply with the requirements contained in the new Directions. If SMIB is unable to comply with the newly applicable Direction, it shall comply with requirements contained in the relevant previous Direction until the expiration of the time granted to comply with the new Direction.

Yours faithfully
B D W A Silva
Actg. Director of Bank Supervision

Bank Supervision Department
31 December 2007

Mr. S H Piyasiri
General Manager
National Savings Bank
255, Galle Road
Colombo 3

Dear Sir

DIRECTIONS ISSUED TO NATIONAL SAVINGS BANK

Considering the structural change in the equity capital of the National Savings Bank (NSB) and with a view to strengthening the safety and soundness of NSB, the Monetary Board of the Central Bank of Sri Lanka has decided to revoke all separate Directions issued to NSB on 21 November 1997 under Sections 76 J (1) and 76 J (3) of the Banking Act and replace these Directions with the Directions issued to other licensed specialized banks (LSBs) under Section 76J (1) of the Banking Act, with effect from 1st January 2008.

2. The Directions that are to replace the existing Directions are given in the following table.

Separate Directions issued to NSB (Existing Directions)	Directions that are to replace the existing separate Directions
(i) Directions under Section 76J(3) — Capital Adequacy	(i) Directions under Section 76J(1) — Maintenance of Capital Adequacy Ratio (Banking Act Direction No. 10) issued on 26.12.2007 —Annex 1
(ii) Directions under Section 76J(1) — Reserve Fund	(ii) Directions under Section 76J(1) — Reserve Fund —Annex 2
(iii) Directions under Section 76J(3) — Liquid Assets	(iii) Directions under Section 76J(1) — Liquid Assets —Annex 3
(iv) Directions under Section 76J(1) — Investments in Equity	(iv) Directions under Section 76J(1) — Investments in Equity —Annex 4
(v) Directions under Section 76J(1) — Single Borrower Limit	(v) Directions under Section 76J(1) — Maximum Amount of Accommodation (Banking Act Direction No. 8) issued on 1.11.2007 —Annex 5
(vi) Directions under Section 76J(1) — Acquisition of Immovable Property	(vi) Directions under Section 76J(1) — Acquisition of Immovable Property —Annex 6

3. The Monetary Board has also decided to grant time till 31 December 2008 to comply with the requirements contained in the new Directions. In the event that NSB is unable to comply with any of the newly applicable Directions, it shall comply with the requirements contained in the relevant previous Directions, until the expiration of the time granted to comply with the new Directions.

Yours faithfully

B D W A Silva

Actg. Director of Bank Supervision

02/01/00/0002/001

Bank Supervision Department
31 December 2007

To: CEOs of All Licensed Banks

Dear Sirs/Madam

GUIDELINES FOR EMPLOYMENT OF EXPATRIATE STAFF IN BANKS

As announced at the meeting of the Chief Executive Officers of licensed banks on 22 November 2007, the Guidelines for employment of expatriate staff in banks, which have been developed to facilitate the introduction of new banking products and risk management of banks, are sent herewith.

Please acknowledge receipt of this Circular.

Yours faithfully,

B D W A Silva

Actg. Director of Bank Supervision

GUIDELINES FOR EMPLOYMENT OF EXPATRIATE STAFF IN BANKS

1 Current Policy

- 1.1 At present, the Central Bank of Sri Lanka (CBSL) recommends to Immigration and Emigration Department resident visas for expatriate staff of foreign banks to enable the banks to employ them as follows.
 - (i) Maximum of three officers without any restriction.
 - (ii) Permission for any officers exceeding 3 is granted on a case-by-case-basis for a specific period not exceeding one year subject to condition that local staff should be trained to handle the work initiated/undertaken by such expatriate officers.
- 1.2 The objective of developing this policy is to provide local staff with the training and opportunities to take on positions held by the expatriate officers.
- 1.3 In the case of local banks, there has not been such a policy since local banks generally do not employ foreign personnel. However, four local banks have employed foreign consultants to undertake specific assignments.

2 Need for a Revision of the Policy

The following factors are considered favourably to relax the current policy to permit more expatriate officers and to encourage domestic banks to employ foreign experts.

- (i) Expansion of business operations of some foreign banks.
- (ii) Foreign banks now tend to expand business in Sri Lanka, especially infrastructure projects, through funds borrowed from their respective head offices and branches.
- (iii) The active presence of foreign banks with internationally experienced professionals will help improve Sri Lanka's image and investment promotion internationally.
- (iv) Tendency to introduce international banking products such as securitization, loan syndication, foreign loan raising, infrastructure funding and derivative products.
- (v) Banks in Sri Lanka mainly depend on conventional deposit and loan products. Introduction of innovative banking products indicate the development of the financial sector and the economy. International banking know-how is necessary to introduce new banking products, especially to attract foreign capital to Sri Lanka.
- (vi) Banks will need to employ risk management specialists to implement advanced approaches of Basel II in the medium term and there may be a need to look for such specialists from countries which implement Basel II.
- (vii) The proposed adoption of IAS/IFRS also will require bankers who have practical experience in adopting IAS/IFRS.
- (viii) In general, banking industry needs experts who have global banking experience if Sri Lankan banks are to introduce modern banking products, technology and risk management techniques.

3 Policy Guidelines

3.1 For Foreign Banks

- (i) The maximum number of expatriate officers permitted will be as follows:
 - (a) 3 for banks whose staff strength is less than 75.
 - (b) 5 for banks with staff strength of 75 to 400.
 - (c) 10 for banks with staff strength of more than 400.
- (ii) In the case of Indian banks, agreement as per on-going negotiations of the Comprehensive Economic Partnership Agreement (CEPA) will be adopted as the minimum criteria.

- (iii) Approval for expatriate officers in excess of the above limits will be considered on a case-by-case-basis taking into consideration the specific skills of the nominated expatriates and specific assignments given to them. The banks should submit projections for specific business or deliverables expected from expatriate officers.
- (iv) Validity period of the approval will be two years for expatriates under the normal quota and one year for others (case-by-case-basis criteria).
- (v) In the case of expatriate officers under the normal quota except for CEO, approval may be renewed for another term of two years after assessing the performance of respective expatriate officer. For CEOs, approval may be extended for two terms (4 more years) on the basis of performance records. The renewal for the term of expatriates permitted in excess of the normal quota (case-by-case basis) will be considered only for extension of the projects/assignments or new projects/assignments.
- (vi) Approving authority for expatriate officers under normal quota will be the Director of Bank Supervision. The Deputy Governor will approve expatriate officers in excess of the normal quota.

3.2 For Locally Incorporated Banks

Permission will be granted on a case-by-case basis taking into consideration the specific needs of the banks. Special attention will be given to employment of foreign experts in the following fields:

- (a) Basel II-based risk management
- (b) International Accounting Standards
- (c) Risk modeling and data warehouse
- (d) Structuring of derivative products
- (e) Corporate governance

Circular No: 35/01/005/0006/12

Domestic Operations Department
11 January 2007

To: All Licensed Commercial Banks.

REVERSE REPURCHASE FACILITY

Further to our circular No. 35/01/005/0006/11 dated 26 December 2006 on the above subject informing non availability of Reverse Repurchase Facility (RRF) on days when there is a liquidity surplus in the commercial banking system.

Commercial banks are advised to seek assistance through the RRF, only as a last resort to address the urgent liquidity requirements, and find other means of meeting their liquidity issues. They are informed that with effect from 16 January 2007 any relief will be made available subject to the following conditions.

1. The RRF of the Central Bank will not be available on days when there is a liquidity surplus in the commercial banking system, as per the Central Bank estimates.
2. The RRF will be available to a particular bank, only
 - up to six times per calendar month until 31 March 2007, and
 - up to three times per calendar month thereafter.
3. The total amount of RRF available on a particular day would not exceed the amount of liquidity shortage of the commercial banking system on that particular day as estimated by the Central Bank.

Actg. Director
Domestic Operations Department

Circular No: 35/01/005/0010/06Domestic Operations Department
29 March 2007*To: All Licensed Commercial Banks.***MARGIN REQUIREMENTS AGAINST LETTERS OF CREDIT**

All licensed commercial banks are hereby informed that the margin deposit requirement of 50 per cent of the invoice value at the time of opening Letters of Credit for the importation of the items specified in Schedule A1 (attached), imposed by our circular No 35/01/005/0010/05 dated 18 October 2006, is withdrawn with effect from 30 March 2007.

Actg. Director/Domestic Operations
Authorised Signatory of the Monetary Board
of the Central Bank of Sri Lanka**Circular No. 35/01/005/0006/13**Domestic Operations Department
23 August 2007*To: All Licensed Commercial Banks and Primary Dealers.***REVERSE REPURCHASE FACILITY**

The Central Bank will adopt the following procedures in granting Reverse Repurchase Facility (RRF) at the CBSL policy rate and allocating the amount offered under RRF among Participating Institutions (PIs i.e. Commercial Banks and Primary Dealers), with effect from 23.08.2007 until further notice. Item 5,6,7,8,9,10,11 and 12 of the Section C (b) of our Circular No. 35/01/005/006/04 dated 27.01.2004 will be applicable with regard to the settlement of the RRF. (A copy of our Circular attached for easy reference).

1. The RRF will not be available on the days when there is a liquidity surplus as per the CBSL estimates.
2. When there is a liquidity shortage as per the CBSL estimates, RRF will be available to cover the full amount of the shortage in the system.
3. DOD will announce on electronic bidding system the total amount of RRF available under standing facility at or before 0930 hours on days in which there is a shortfall in the market.
4. PIs who wish to use the facility are required to inform their requirements to the OMO Division of the Domestic Operations Department by telephone or fax message before 1030 hours.
5. The DOD will allocate the total amount offered on the basis of amount requested by each PI. If the total amount requested is higher than the total amount offered, an allocation will be made on a pro rata basis.
6. The results will be informed to each PI by telephone or fax on or before 1100 hours.
7. PIs, are requested to submit the amount accepted, details of the scripless securities through the facility available in the on-line electronic bidding system (standing facility) before 1200 hours.
8. RRF will be available for a participant subject to the following conditions -
 - a. The facility is available only as the last resort to address an urgent liquidity requirement of the particular participant.
 - b. Participants seeking the facility should not be a lender in the money market on the same day, and
 - c. Funds borrowed under RRF should not be used to build up excess reserves in the reserve account of commercial banks with the CBSL, on that particular day.

Director
Domestic Operations Department

Circular No. 35/01/005/0006/14Domestic Operations Department
21 November 2007*To: All Licensed Commercial Banks and Primary Dealers.***REVERSE REPURCHASE FACILITY**

The Central Bank of Sri Lanka (CBSL) will adopt the following procedures in granting Reverse Repurchase Facility (RRF) and allocating the amount offered under RRF among Participating Institutions (PIs i.e. Commercial Banks and Primary Dealers), from **03 December 2007**. Item 5,6,7,8,9,10,11 and 12 of the Section C (b) of our Circular No. 35/01/005/006/04 dated 27 January 2004 will be applicable with regard to the settlement of the RRF. (A copy of our Circular attached for easy reference).

1. The RRF will not be available on the days when there is a liquidity surplus as per the CBSL estimates.
2. When there is a liquidity shortage as per the CBSL estimates, RRF will be available to cover the full amount of the shortage in the system.
3. Domestic Operations Department (DOD) will announce on electronic bidding system the total amount of RRF available under standing facility at or before 0930 hours on days in which there is a shortfall in the market.
4. PIs who wish to use the facility are required to inform their requirements to the Open Market Operations (OMO) Division of the DOD by telephone or fax message before 1030 hours.
5. The DOD will allocate the total amount offered on the basis of amount requested by each PI. If the total amount requested is higher than the total amount offered, an allocation will be made on a pro rata basis.
6. The results will be informed to each PI by telephone or fax at or before 1100 hours.
7. PIs are requested to submit the amount accepted and details of the scripless securities through the facility available in the on-line electronic bidding system (standing facility) before 1200 hours.
8. RRF will be available for a participant subject to the following conditions -
 - a. The RRF will be available to a particular PI only up to four (4) times per calendar month at the prevailing Central Bank Reverse Repo Rate. Any borrowings of more than 4 times by a particular PI during a calendar month will be provided at a penalty rate of 19 per cent per annum. Such penalty rate will be applicable until 31 January 2008.
 - b. The penalty rate will be subject to review from time to time and may be changed in accordance with prevailing monetary conditions.
 - c. The RRF is available only as the last resort to address an urgent liquidity requirement of the particular participant.
 - d. Participants seeking the facility on a particular day should not be a net lender in the money market on the same day, and
 - e. Funds borrowed under RRF should not be used to build up excess reserves in the reserve account of a commercial bank with the CBSL on that particular day.

Director
Domestic Operations Department**Ref: 06/04/01/2007**

Department of Exchange Control
Central Bank of Sri Lanka
P O Box 590
Colombo 1
08 January 2007

*Operating Instructions to Authorized Dealers***FOREIGN CURRENCY FIXED DEPOSIT ACCOUNTS FOR DUAL
CITIZENSHIP APPLICANTS**

The Government of Sri Lanka has decided to introduce a foreign currency fixed deposit scheme for ex-Sri Lankans/ Sri Lankans living abroad who would apply for dual citizenship status. Under this scheme, a family unit or an individual is exempted from payment of any fee charged on granting dual citizenship, if the principal applicant makes a fixed deposit of US\$ 50,000 with an Authorized Dealer for a minimum period of 3 years; while a fee of Rs.200,000 is charged per family unit or an individual applicant if the principal applicant makes a fixed deposit of US\$ 25,000 with an Authorized Dealer for a minimum period of 3 years.

2. For the purpose of accepting such foreign currency deposits, Authorized Dealers are hereby permitted to open fixed deposit accounts in favour of dual citizenship applicants in their domestic banking units.
3. These accounts may be opened with minimum deposits of either US\$ 50,000 or US\$ 25,000 (or equivalent in any other convertible foreign currency) on production of a letter issued by the Controller of Immigration and Emigration recommending that a foreign currency deposit account be opened in the name of the principal applicant for dual citizenship.
4. Operation of these accounts shall be subjected to the following conditions:
 - a. **Credits**
 - i. Inward remittances in convertible foreign currency received through Authorized Dealers or foreign currency brought into the country and tendered by the account holder during his temporary visit to Sri Lanka.
 - ii. Funds transferred from existing Non-Resident Foreign Currency (NRFC) account of the account holder.
 - iii. Interest paid in foreign currency on funds held in the account.
 - b. **Debits**
 - i. Interest accrued on the deposits
5. Interest accrued on the deposits may be freely remittable, transferred to NRFC account of the account holder or converted into Sri Lanka Rupees for the account holder's local expenses.
6. Withdrawals of the deposit or any part thereof should not be permitted before the maturity period of the deposit without obtaining prior permission from the Controller of Exchange.
7. **Reporting Requirement**
Authorized Dealers are required to furnish to the 'D' Branch of the Exchange Control Department and copy to the Controller of Immigration & Emigration, the following information in respect of each foreign currency fixed deposit account opened under the scheme within a week of opening the account:
 - (a) Date of opening of the account and the name and address of the account holder; and
 - (b) Amount of funds deposited and the date of maturity of the deposit.

Controller of Exchange

The Gazette of the Democratic Socialist Republic of Sri Lanka
EXTRAORDINARY
No.1481/1 – MONDAY, JANUARY 22, 2007
(Published by Authority)
PART I: SECTION (I) – GENERAL
Central Bank of Sri Lanka Notices

NOTICE UNDER THE EXCHANGE CONTROL ACT (CHAPTER 423 OF THE CLE)
Permission in Terms of Sections 7, 10, 11 and 15 of the Exchange Control Act

1. PERMISSION is hereby granted for the purposes of Sections 7, 10, 11 and 15 as applicable of the Exchange Control Act (Chapter 423 of the CLE) to foreign country funds, regional funds or mutual funds approved by the Securities and Exchange Commission of Sri Lanka, corporate bodies incorporated outside Sri Lanka and citizens of foreign states for purchasing, transferring and making payments in respect of transactions of Sri Lanka Rupee Denominated Treasury Bonds (T-bonds) subject to the conditions hereinafter set out.
2. *Conditions.-*
 - (a) Any T-Bonds to be purchased by the above categories of foreign investors should be through the primary and secondary markets by utilizing existing public debt system. Foreign investor who purchased such a T- bond is in a position to sell or transfer this T- bond to any person, whether a resident in Sri Lanka or a resident outside Sri Lanka, in the secondary market without any holding period.
 - (b) The payment for T-bonds issued by the Government of Sri Lanka in any issue or transaction permitted hereunder shall be made only out of or into a "Treasury bond Investment External Rupee Account" (TIERA) opened in a commercial bank in Sri Lanka in the name of the foreign investor.
 - (c) A commercial bank, or a licensed primary dealer or a broker or any other person entrusted with the payment of capital monies such a sale proceeds of T-bonds and interest on such T- bonds in respect of any transaction permitted hereunder shall make such payment only into or out of a Treasury Bond Investment External Rupee Account referred to in sub-paragraph (b) above.
 - (d) Funds in a TIERA is freely remittable without any restriction after meeting local liabilities of the account holder, if any.

Interpretation : For purpose of this general permission;

“foreign investors” shall include the following categories of investors:

- (a) Foreign country funds, regional funds or mutual funds approved by the Securities and Exchange Commission of Sri Lanka;
- (b) Corporate bodies incorporated outside Sri Lanka; and
- (c) Citizens of foreign states.

D.WASANTHA,
Controller of Exchange

Colombo,
22nd January, 2007

Ref: 06/04/03/2007

Department of Exchange Control
Central Bank of Sri Lanka
P.O. Box 590
Colombo 1
22 January 2007

Operating Instructions to Authorized Dealers

Dear Sirs,

**INVESTMENT IN RUPEE DENOMINATED TREASURY BONDS BY
FOREIGN INVESTORS**

The Government has decided to permit foreign country funds, regional funds or mutual funds approved by the Securities and Exchange Commission of Sri Lanka, corporate bodies incorporated outside Sri Lanka and citizens of foreign states to purchase and hold Rupee Denominated Treasury Bonds (T-bonds) not exceeding 5% of the total value of T-bonds outstanding at any given point of time. Therefore, the above categories of foreign investors are permitted to purchase, hold and transfer T-bonds through both primary and secondary markets utilizing existing public debt system. Foreign investor who purchased such a T-bond is in a position to sell or transfer this T-bond to any person, whether a resident in Sri Lanka or a resident outside Sri Lanka, in the secondary market without any holding period.

2. In order to give effect to this decision, general permission has been granted by me in a notice published in the Gazette Extraordinary No. 1481/1 of 22.01.2007.
3. Accordingly, Authorized Dealers are hereby permitted to open and operate Treasury Bond Investment External Rupee Accounts (TIERA) in the names of following categories of foreign investors,
 - (a) Foreign country funds, regional funds or mutual funds approved by the Securities and Exchange Commission of Sri Lanka;
 - (b) Corporate bodies incorporated outside Sri Lanka; and
 - (c) Citizens of foreign states

subject to the following guidelines for the purpose of facilitating their investments in T-bonds.

- I) Credits and debits to the account should be confined to the following:

Credits:

- i) Inward remittances of the foreign investor and/or transfers from Share Investment External Rupee Account (SIERA) opened by foreign investor for investment in shares.
- ii) Sale proceeds of T-bonds and principal received on the maturity date.
- iii) Payment of interest on T-bonds held by the account holder.

Debits:

- i) Payments for investments in T-bonds.
- ii) Transfers to SIERA of the foreign investor.
- iii) Payments for primary dealers and bank charges.
- iv) Local expenses of the foreign investor.
- v) Repatriation of sale proceeds of T-bonds.
- vi) Repatriation of interest earned on T-bonds.

II) Reporting Requirement

- i) Authorized Dealers are required to furnish statements of TIERA for each month indicating details of debits and credits to the Exchange Control Department (C&F Branch) on or before the 15th day of the following month.
 - ii) Authorized dealers are also required to furnish details of credits and debits made to each TIERA at the end of the day via online using the online system already installed for reporting investment in shares through SIERAs.
4. Operating Instructions previously issued under Ref:06/04/07/2006 dated 01.11.2006 on the above subject are hereby rescinded.

Yours faithfully
Controller of Exchange

cc: Governor
DG(W)
DG(J)
AGG

GUIDELINES TO AUTHORISED DEALERS ON OPERATING INSTRUCTIONS NO. 06/04/03/2007 DATED 22.01.2007 IN RESPECT OF INVESTMENT IN RUPEE DENOMINATED TREASURY BONDS BY FOREIGN INVESTORS

(A) Foreign investors permitted to invest in Treasury Bonds (T-Bonds)

- a) Foreign country funds, regional funds or mutual funds approved by the Securities and Exchange Commission of Sri Lanka;
- (b) Corporate bodies incorporated outside Sri Lanka; and
- (c) Citizens of foreign states

(B) Account through which investment in T-bonds is permitted

Investments in T bonds should be made only out or into a Special Rupee Account named “Treasury Bond Investment External Rupee Account (TIERA)” opened in any commercial bank in the name of the above categories of foreign investors.

(C) Reporting TIERA transactions online

- i) *Foreign investors already having SIERA*
In the existing online system for reporting investment in shares, activate the icon “Add New Account” and then entering an account number by adding TIERA in front open a TIERA account. Both accounts should carry identical account holder’s name.
- ii) *Foreign investor without having SIERA*
Using existing online system for reporting investment in shares open new account named TIERA by entering a new account number inserting (TIERA) in front.

(D) Credits and Debits to TIERA

Credits and debits to TIERA should be strictly in accordance with the instructions given in the Operating Instructions. Under no circumstance transactions relating to share investments should be recorded in TIERA.

Ref: 06/07/04/2007

Department of Exchange Control
Central Bank of Sri Lanka
P.O.Box 590
Colombo 1
02 March 2007

Operating Instructions to Authorised Dealers

Dear Sirs/Madam,

**CERTIFICATE OF EXPORT INSPECTION FOR THE IMPORT OF
USED MOTOR VEHICLES**

Reference is made to our Operating Instructions No.06/07/04/2006 of August 1, 2006 on the above subject.

As you have already been informed by the Controller of Imports & Exports by his Operating Instruction to you No. 01/2007 dated 26.01.2007 that the regulations published in the Gazette Extraordinary No.1454/30 dated 21.07.2006 will be effective 1st of March 2007.

Therefore, you are hereby informed to adhere to the terms and conditions stipulated in the above Operating Instructions with effect from 1st March 2007 having substituted the item 4 of my Operating Instructions No.06/07/04/2006 dated 1st August 2006 with the following:-

“4. In case where the motor vehicles have not been shipped as at 1st March 2007 you should ensure that such Letters of Credit are amended as required in item No.2 and 3 above”.

Yours faithfully
Controller of Exchange

Ref: 06/07/05/2007

Department of Exchange Control
Central Bank of Sri Lanka
P.O.Box 590
Colombo 1
05 March 2007

Operating Instructions to Authorised Dealers

Dear Sirs/Madam,

**RELEASE OF FOREIGN EXCHANGE FOR TRAVEL
ON PRODUCTION OF ELECTRONIC TICKET (eTICKET)**

Attention of the Authorised Dealers is invited to item “ C ” paragraph 2 of my guidelines issued to Authorised Dealers on Operating Instructions No.EC/06/94 dated 18.03.1994 whereby Authorised Dealers have been permitted to issue foreign exchange for travel abroad for any purpose including education and medical treatment abroad on verifying the bona-fides of the request.

In terms of the Operating Instructions referred to above, the Authorised Dealers have been advised to issue foreign exchange for travellers who are resident in Sri Lanka subject to the production of return air ticket and valid Visa with the Passport. However, it has now been observed that airline industry have switched over to issue **eTickets** to the travellers instead of the traditional paper tickets.

Therefore, Authorised Dealers are hereby permitted to accept either return **eTicket** or paper ticket and valid Visa with the passport as the bona-fides to the request when issuing foreign exchange for travel purposes.

However, when accepting the **eTicket** for the issuance of foreign exchange, you should ensure to obtain a print out containing the ticket details issued by the respective airline.

Yours faithfully
Controller of Exchange

Ref: 06/04/06/2007

Department of Exchange Control
Central Bank of Sri Lanka
P.O. Box 590
Colombo 1
19 March 2007

Operating Instructions to Authorized Dealers

RESIDENT GUEST SCHEME – SPECIAL ACCOUNTS

The Government of Sri Lanka introduced Resident Guest Scheme in 1991, as a part of a package of incentives for prospective foreign investors and professionals who would contribute to the economic and socio-cultural development of the country. Under this scheme, foreign investors and professionals are required to remit funds for investment purposes and their upkeep in Sri Lanka as follows:

Investors

A sum of US\$250,000 or an equivalent amount in any convertible foreign currency for investment in Sri Lanka and a further sum of US\$35,000 per person for the upkeep in Sri Lanka of the investor and each dependant accompanying the investor.

Professionals

A sum of US\$2,000 per month for living expenses of the professional intending to reside in Sri Lanka and US\$1,000 per month for each dependant including spouse.

2. For the purpose of depositing the funds brought into the country by the investors and professionals under this scheme, Authorized Dealers are hereby permitted to open the under-mentioned special accounts in their domestic units with the prior approval of the Controller of Exchange:

(I) Special Accounts for Investors**(i) Resident Guest Foreign Currency Accounts (RGFCA)**Credits

These accounts should be opened for the purpose of depositing the minimum initial sum of US\$250,000 or an equivalent amount in any convertible foreign currency brought into the country through banking channels or on declaration to Sri Lanka Customs for investment in Sri Lanka.

Debits

- (A) Withdrawals from this account may be permitted without prior approval of the Controller of Exchange for the following:

- (a) Investment in “approved projects” subject to production of documentary proof of obtaining relevant approvals.

“Approved projects” for the purpose of this scheme are:

- (i) New ventures approved by the Board of Investment in Sri Lanka or a relevant authority;
- (ii) Existing or new companies engaged in projects approved by a relevant authority; and
- (iii) Shares listed in the Colombo Stock Exchange

- (b) Funds in excess of US\$250,000 or equivalent in other convertible foreign currencies brought into the country and held in the account unutilised.

- (B) Withdrawals for any purpose other than investment should be with the prior approval of the Controller of Exchange which will be granted with the concurrence of the Implementing Agency of the scheme.

Authorized Dealers are permitted to pay interest initially for a period of 2 years on the unutilised balance in this account, provided that the rate of interest does not exceed the rate of interest payable to Non-Resident Foreign Currency (NRFC) accounts. Such interest payment should be transferred to the investor’s Resident Guest Rupee Current Account referred below.

No interest should be paid after the expiry of the initial two-year period without the prior approval of the Controller of Exchange.

(II) Resident Guest Rupee Current Account – Investors (RGRCA – Investors)

These accounts may be opened with a minimum deposit of US\$35,000 or equivalent in other convertible foreign currency brought into the country and converted into Sri Lanka Rupees, after obtaining prior approval from the Controller of Exchange:

Credits

Credits to these accounts should be confined to the following:

- (i) Rupee proceeds of foreign currency brought into the country by the investor for his living expenses and that of his dependants;
- (ii) Interest paid on funds held in the investor's Resident Guest Foreign Currency Account (RGFCA) having converted into Sri Lanka Rupees.
- (iii) Incomes from investment (dividends, profits), sale proceeds of shares received from the investments made out of funds from the RGFCA.

Debits

(a) Debits to this account should be confined to the following:

- (i) Local expenses of the investor and his dependents;
 - (ii) Investment in approved projects mentioned in paragraph 2(I)(i)(A)(a) above;
 - (iii) Outward remittances for payments for current international transactions of the investor and/or his dependents resident in Sri Lanka.
- (b) Withdrawals for any purpose other than those mentioned in items (i), (ii) and (iii) above should be with the prior approval of the Controller of Exchange which will be granted with the concurrence of the Implementing Agency of the scheme.

(III) Resident Guest Rupee Current Account – Professionals (RGRCA – Professionals)

These accounts may be opened in the name of foreign professionals with a minimum deposit of US\$2,000 or any other convertible foreign currency brought into the country and converted into Sri Lanka Rupees, after obtaining prior approval from the Controller of Exchange.

Credits

Credits to these accounts should be confined to the following:

- (i) Rupee proceeds of foreign currency brought into the country for the living expenses of the account holder and of his dependents; and
- (ii) Salary, consultancy fees, etc. received for the provision of professional services in Sri Lanka by the account holder.

Debits

(a) Debits to this account should be confined to the following:

- (i) Local expenses of the account holder and his dependents; and
 - (ii) Outward remittances for payments on account of current international transactions of the professional and/or his dependents resident in Sri Lanka.
- (b) Withdrawals for any purpose other than those mentioned in a(i) and (ii) above should be with the approval of the Controller of Exchange which will be granted with the concurrence of the Implementing Agency of the Scheme.
3. All Authorized Dealers should furnish to "D" branch of the Exchange Control Department quarterly statements of these accounts within 15 days of the lapse of each quarter ending March, June, September and December.
 4. Operating Instructions previously issued under Ref.No.ECD/08/91(C&F) dated 20.02.1991 on the above subject is hereby rescinded.

Yours faithfully
Controller of Exchange

Ref: 06/04/07/2007

Department of Exchange Control
Central Bank of Sri Lanka
P O Box 590
Colombo 01
17 May 2007

Operating Instructions to Authorized Dealers

Dear Sir,

**FREIGHT FORWARDING & ISSUE OF HOUSE AIR WAY BILLS/
HOUSE BILLS OF LADING / FORWARDERS CARGO RECEIPTS**

Authorized Dealers are hereby requested to include the following Freight Forwarders who have been registered with the Central Bank of Sri Lanka since 2006.02.01 to the list of freight forwarders for the purpose of accepting their House Air ways Bills/ House Bills of lading, Forwarders Cargo Receipts for negotiation in respect of Exports cargo.

Name of the Freight Forwarder	Registration No.
1) Royal Asia Shipping Company (pvt) Ltd.,	06/07/009/0196
2) SEACARE Forwarders (private) Ltd.,	06/07/009/0197
3) AST Logistics International (pvt) Ltd.,	06/07/009/0198
4) Shermans Logistics (pvt) Ltd.,	06/07/009/0199
5) Transcare Logistics (pvt) Ltd.,	06/07/009/0200
6) Eagle Logistics Colombo (pvt) Ltd.,	06/07/009/0201
7) Aset Ltd,	06/07/009/0202
8) Helman World Wide Logistics (pvt) Ltd.,	06/07/009/0203
9) Phonex International Logistics Lanka (pvt) Ltd.,	06/07/009/0204
10) Logistics Plus Lanka (private) Limited	06/07/009/0205
11) Speed International Logistics (private) Ltd,	06/07/009/0206
12) V.V.K Maritime Agencies (pvt) Ltd.,	06/07/009/0207
13) Container Cargo Logistics (pvt) Ltd.,	06/07/009/0208
14) Spence Logistics (private) Ltd.,	06/07/009/0209
15) Sharp International Shipping & Trading (pvt) Ltd.,	06/07/009/0210
16) Ship Air Logistics (pvt) Ltd.,	06/07/009/0211
17) Global Logistics and Shipping (pvt) Ltd.,	06/07/009/0212
18) Spedicon Logistics (pvt) Ltd.,	06/07/009/0213
19) Califolink Logistics (pvt) Ltd.,	06/07/009/0214
20) United Cargo Management (private) Ltd.,	06/07/009/0215
21) Pan Oceanic International (pvt) Ltd.,	06/07/009/0216
22) TRANSASIA Shipping Services Colombo (pvt) Ltd.,	06/07/009/0217
23) Clarian Shipping (pvt) Ltd.,	06/07/009/0218
24) World Scan (pvt) Ltd.,	06/07/009/0219
25) Waterways International Lanka (pvt) Ltd.,	06/07/009/0220
26) Seven Seas Navigation (private) Ltd.,	06/07/009/0221
27) IJS Global Lanka (pvt) Ltd.,	06/07/009/0222
28) Serendib Logistics Solution (pvt) Ltd.,	06/07/009/0223
29) EUR Service Lanka (pvt) Ltd.,	06/07/009/0224
30) Yellow Freight International (pvt) Ltd.,	06/07/009/0225
31) JAL Shipping and Logistics (pvt) Ltd.,	06/07/009/0226
32) Tri Star Shipping International (pvt) Ltd.,	06/07/009/0227
33) Portway Shipping & Logistics (pvt) Ltd.,	06/07/009/0228
34) Volusia Freight & Logistics (pvt) Ltd.,	06/07/009/0229

Yours faithfully
Controller of Exchange

Ref: 06/04/08/2007

Department of Exchange Control
Central Bank of Sri Lanka
Colombo 1
14 June 2007

Operating Instructions to Authorised Dealers

**ISSUANCE OF FOREIGN CURRENCY NOTES TO
SRI LANKANS TRAVELLING ABROAD**

As a further measure of liberalising current international transactions and giving benefits to Sri Lankans travelling abroad, it has been decided to increase the issuance of foreign currency notes as a part of the travel allowance for Sri Lankans travelling abroad from its present level of US\$ 500 to US\$ 1000 or its equivalent in any other convertible foreign currency. However, travel allowances should be issued by exercising due diligence and discretion after satisfying the bona fides of the request.

Controller of Exchange

Ref: No. 06/04/09/2007

Department of Exchange Control
Central Bank of Sri Lanka
Colombo 1
15 June 2007

Operating Instructions to Authorised Dealers

**PERMISSION FOR THIRD PARTY
FOREIGN EXCHANGE DEPOSITS IN NRFC ACCOUNTS**

As a further measure to enhance worker remittances to the formal sector, it has been decided to grant permission to Authorised Dealers and Specialised Banks, which are permitted to open and maintain Non-Resident Foreign Currency (NRFC) Accounts, to accept foreign currency to the credit of NRFC Accounts from an immediate family member of the account holder. Foreign currency so collected from such a family member of the account holder should not exceed US\$ 1,000 or its equivalent in other convertible foreign currency per transaction.

The immediate family member of the account holder is considered to be his/her wife/husband, mother or father, brother or sister, son or daughter. Account holder is required to nominate his/her immediate family member/s who will be permitted to make foreign currency deposits to his/her NRFC account if he/she intends to utilise this facility. To avoid possible malpractices and abuses arising from this facility, banks are required to obtain the following particulars of the immediate family member/s of existing NRFC Account holders. In the case of new NRFC account holders, this information should be obtained at the time of opening accounts.

1. Names and addresses of the family member/s who will be permitted to make deposits;
2. Relationship to the account holder;
3. Nationality;
4. National Identity Card or passport number of the family member/s ; and
5. Contact telephone number/s of the family member/s.

Controller of Exchange

**The Gazette of the Democratic Socialist Republic of Sri Lanka
EXTRAORDINARY**

**No. 1516/19 – TUESDAY, SEPTEMBER 25, 2007
(Published by Authority)**

PART I : SECTION (I) - GENERAL

Government Notifications

NOTICE UNDER THE EXCHANGE CONTROL ACT (CHAPTER 423 OF THE CLE)

IN exercise of powers conferred by section 6 and 6A of the Exchange Control Act read with sections 3 and 48 of the said Act, permission is hereby granted to possess and retain foreign exchange as specified below.

Possession and retention of foreign exchange

1. (a) An authorized dealer may possess and retain foreign exchange acquired in the normal course of business and within the terms of his authorization.
- (b) An authorized person may possess and retain foreign currency received or acquired in the normal course of business and within the terms of his authorization.
- (c) A person resident in Sri Lanka may retain in his possession foreign currency in the form of currency notes, and/or travellers' cheques, the aggregate value of which does not exceed US\$ 2,000 or its equivalent in other foreign currencies:
 Provided that such foreign currency represents -
 - (i) foreign currency purchased by him from an authorized dealer or an authorized person for travel abroad and brought back unutilized while returning to Sri Lanka, or
 - (ii) foreign currency received by him outside Sri Lanka as remuneration for services rendered by him to a person resident outside Sri Lanka.
- (d) A person resident outside Sri Lanka may in Sri Lanka retain in his possession without limit foreign currency if such foreign currency was acquired by him whilst he was outside Sri Lanka.

Period for retention of foreign exchange

2. (a) A person resident in Sri Lanka who obtains foreign currency from an authorized dealer or authorized person for a purpose mentioned in an application made by him to the authorized dealer or authorized person does not use it for such purpose shall not retain such foreign currency for a period exceeding 90 days from the date of receipt of such foreign currency without converting into Sri Lanka Rupees.
- (b) A person resident in Sri Lanka who obtains foreign currency from an authorized dealer or authorized person for a purpose mentioned in an application made by him to the authorized dealer or authorized person thereafter brings back to Sri Lanka said foreign currency or part thereof, such person shall not retain such foreign currency for a period exceeding 90 days from the date of repatriation without converting into Sri Lanka Rupees.
- (c) A person resident in Sri Lanka who proceeds outside Sri Lanka for taking up employment, professional work or setting up in business earns or receives foreign currency from such employment, profession or business and brings back to Sri Lanka, such person shall not be entitled to retain such foreign currency for a period exceeding 90 days from the date of its repatriation without converting into Sri Lanka Rupees or crediting into a foreign currency account opened and/or maintained by such person in accordance with directions issued to authorized dealers under the Exchange Control Act for opening and maintaining of foreign currency accounts.
- (d) Time period referred to in sub-paragraphs (b) and (c) of this paragraph does not apply to a person resident in Sri Lanka who retains foreign currency in his possession in accordance with sub-paragraph (c) of paragraph 1 of this notice.

Interpretation for purposes of this notification

3. In this notice, unless the context otherwise requires -
 - (i) "authorized dealer" means, a commercial bank for the time being authorized under Section 4 of the Exchange Control Act for the purposes of the Act as an authorized dealer in relation to gold or any foreign currency;

- (ii) “authorized person” means, any person other than an authorized dealer for the time being authorized by the Central Bank under section 5 of the Exchange Control Act;
- (iii) “foreign currency” shall have the same meaning as given in the Exchange Control Act;
- (iv) “currency” shall have the same meaning as given in the Exchange Control Act;
- (v) “foreign exchange” shall have the same meaning as given in the Exchange Control Act;
- (vi) “person resident in Sri Lanka” or a “person resident outside Sri Lanka” shall have the same meaning as given in the Direction issued by the Minister of Finance under Section 37 (1) of the Exchange Control Act and published in the Government Gazette, No.15,007 dated 21st April, 1972.

4. Revocation of earlier notices:

The notice published in Gazette Extraordinary, No. 1227/11 dated March 16, 2002 is hereby revoked.

5. The contents of this Gazette shall come into operation with effect from 5th October, 2007.

D. WASANTHA
Controller of Exchange

Colombo
21st September, 2007.

The Gazette of the Democratic Socialist Republic of Sri Lanka
EXTRAORDINARY

No. 1516/24 – THURSDAY, SEPTEMBER 27, 2007
(Published by Authority)

PART I : SECTION (I) - GENERAL
Government Notifications

NOTICE UNDER THE EXCHANGE CONTROL ACT (CHAPTER 423 OF THE CLE)

IN exercise of powers conferred by sub-sections 1 (a) and (b) of section 21 and sub-sections 1 (a) and (b) of section 22 of the Exchange Control Act read with Sections 3 and 48 of the said Act, permission is hereby granted to export from and import into Sri Lanka of Sri Lanka currency notes or foreign currency as specified below:-

Export and Import of Sri Lanka Currency

1. A citizen of Sri Lanka or a person resident in Sri Lanka -
 - (a) who proceeds outside Sri Lanka to take up an employment or for education or on a temporary visit on holiday, business or medical treatment, or for any other similar reasons may export on his person or in his baggage, Sri Lanka currency notes not exceeding Rs.5,000/- per person;
 - (b) who returns to Sri Lanka after employment or education abroad or a temporary visit outside the country on holiday, business or medical treatment, or for any other similar reason may import into Sri Lanka on his person or in his baggage, Sri Lanka currency notes not exceeding Rs.5,000/- per person.

Import and Export of Foreign Currency

Import of Foreign Currency:

2. A person may -
 - (a) send to Sri Lanka through normal banking channels without limit foreign currency legally acquired from any place outside Sri Lanka;
 - (b) transmit into Sri Lanka by post, money orders or postal orders expressed in foreign currency subject to any limit of amount or other limits prescribed under the Post Office Ordinance;
 - (c) bring into Sri Lanka on his person and/or in his baggage any foreign currency subject to the requirements of the Order made by the Minister of Finance in relation to prescribed currencies and published in the Government Gazette, No.10, 564 dated 14th August, 1953, as amended, and the Order made by the Minister of Finance in

relation to prescribed currencies brought in by passengers travelling in transit through a port and published in the Government Gazette, No.790/8 dated 27th October, 1993:

Provided that upon importing foreign currency into Sri Lanka by such person (not being a passenger travelling in transit through the port and remains in any area reserved or demarcated for use by transit passengers in such port), shall make a declaration on his arrival in Sri Lanka to Sri Lanka Customs in the “Passenger Baggage Declaration: Inward” form if the value of foreign currency brought into Sri Lanka exceeds US\$15,000 in aggregate or its equivalent in other foreign currencies:

Provided further that it shall be necessary to declare to the Sri Lanka Customs foreign currency notes brought in by such person, if he intends to take back foreign currency notes exceeding US\$ 5,000 or its equivalent in other currencies.

Export of Foreign Currency:

3. (a) An authorized dealer may send out of Sri Lanka foreign currency which has been acquired in the normal course of business and within the terms of his authorization;
- (b) A person resident in Sri Lanka may -
 - (i) take or send out of Sri Lanka foreign currency obtained by him from an authorized dealer or an authorized person in accordance with the provisions of the Exchange Control Act or the regulations, notifications or directions made or issued under the Act;
 - (ii) take out of Sri Lanka foreign currency retained by him in his possession in accordance with the notice issued by the Controller of Exchange for the possession and retention of foreign currency and published in the Government Gazette No. 1516/19 dated 25.09.2007;
- (c) A person resident outside Sri Lanka may take out of Sri Lanka unutilized foreign currency in a sum not exceeding the amount brought in by him on his last arrival in Sri Lanka:

Provided that taking or sending of foreign currency out of Sri Lanka by a person in or resident in Sri Lanka shall be subject to the condition that such person (not being a passenger travelling in transit through the port and remains in any area reserved or demarcated for use by transit passengers in such port) makes a declaration to Sri Lanka Customs in the “Passenger Baggage Declaration : Outward” form, or any other form prescribed by the Sri Lanka Customs for that purpose, if -

- (i) the value of foreign currency taken or sent out of Sri Lanka exceeds US\$10,000 in aggregate or its equivalent in other foreign currencies; and/or
- (ii) the value of foreign currency taken or sent out of Sri Lanka in the form of currency notes exceeds US\$5,000 in aggregate or its equivalent in other foreign currencies.

Interpretation for purposes of this notification

4. In this notice, unless the context otherwise requires -
 - (a) “authorized dealer” means, a commercial bank for the time being authorized under section 4 of the Exchange Control Act for the purposes of the Act as an authorized dealer in relation to gold or any foreign currency;
 - (b) “authorized person” means, any person for the time being authorized by the Central Bank under section 5 of the Exchange Control Act;
 - (c) “foreign currency” shall have the same meaning as given in the Exchange Control Act;
 - (d) “currency” shall have the same meaning as given in the Exchange Control Act;
 - (e) “person resident in Sri Lanka” or a “person resident outside Sri Lanka” shall have the same meaning as given in the Direction issued by the Minister of Finance under Section 37(1) of the Exchange Control Act and published in the Government Gazette, No.15,007 dated 21st April 1972.
5. The contents of this Gazette shall come into operation with effect from 5th October, 2007.

D. WASANTHA
Controller of Exchange

Colombo
21st September, 2007

Ref: 06/04/10/2007

Department of Exchange Control
Central Bank of Sri Lanka
P O Box 590
Colombo 01
06 December 2007

Operating Instructions to Authorized Dealers

Dear Sirs,

**INVESTMENT IN RUPEE DENOMINATED TREASURY BONDS BY FOREIGN INVESTORS (INCREASE
OF THE HOLDING LIMITS OF FOREIGN INVESTORS IN THE RUPEE DENOMINATED TREASURY
BONDS FROM 5% TO 10%)**

This has reference to our Operating Instructions dated 22nd January, 2007 bearing reference number 06/04/03/2007 on the above subject.

The Government has decided to further increase the current permitted level of 5% of the outstanding value of Rupee Denominated Treasury bonds (T-bonds) as at any given point of time that could be purchased and held by foreign country funds, regional funds or mutual funds approved by the Securities and Exchange Commission of Sri Lanka, Corporate Bodies incorporated outside Sri Lanka and citizens of foreign countries, upto 10% of the outstanding value of T-bonds.

Authorized Dealers are hereby permitted to open and operate Treasury bond Investment External Rupee Accounts (TIERA), in accordance with the above decision, in the names of the categories of foreign investors mentioned in paragraph 3 of the Operating Instructions dated 22nd January, 2007 referred to above, subject to the guidelines stipulated therein.

Yours faithfully
Controller of Exchange

cc: Governor
DG(W)
DG(J)
AG(SM)
SPD

Ref: 06/04/11/2007

Department of Exchange Control
Central Bank of Sri Lanka
P O Box 590
Colombo 01
31 December 2007

Operating Instructions to Authorized Dealers

Dear Sirs,

**FREIGHT FORWARDING & ISSUE OF HOUSE AIR WAY BILLS/
HOUSE BILLS OF LADING / FORWARDERS CARGO RECEIPTS**

Authorised Dealers are hereby requested to include the following Freight Forwarders who have been registered with the Central Bank of Sri Lanka since 2007.05.17 to the list of freight forwarders for the purpose of accepting their House Air ways Bills/ House Bills of lading, Forwarders Cargo Receipts for negotiation in respect of Exports cargo.

Name of the Freight Forwarder	Registration No.
1) Denovo Shipping Lines (pvt) Ltd.,	06/07/009/0230
2) Expo Consolidators (pvt) Ltd.,	06/07/009/0231

3) UNI World Logistics (pvt) Ltd.,	06/07/009/0232
4) Voyager Shipping International (pvt) Ltd.,	06/07/009/0233
5) Worldgate Express Lines Lanka (pvt) Ltd.,	06/07/009/0234
6) Trice Shipping Co.(pvt) Ltd.,	06/07/009/0235
7) Trans Atlantic Global Logistics (pvt) Ltd.,	06/07/009/0236
8) Maritime Agencies Ltd.,	06/07/009/0237
9) Care Logistics (pvt) Ltd.,	06/07/009/0238
10) GGL Line (pvt) Ltd.,	06/07/009/0239
11) Pacific Container Line Agency Colombo (pvt) Ltd.,	06/07/009/0240
12) Atlas Logistics Lanka (pvt) Ltd.,	06/07/009/0241
13) Clarion Logistics (pvt) Ltd.,	06/07/009/0242
14) Moceti Lanka (pvt) Ltd.,	06/07/009/0243
15) Freightlog Shipping Colombo (pvt) Ltd.,	06/07/009/0244
16) S&R Super Logistics Lanka (pvt) Ltd.,	06/07/009/0245
17) Crown City Developers (pvt) Ltd.,	06/07/009/0246
18) Ocean Links Logistics (pvt) Ltd.,	06/07/009/0247
19) Freight Masters International (pvt) Ltd.,	06/07/009/0248

Yours faithfully
Controller of Exchange

Financial Intelligence Unit
Tel. No. 2477228
Fax No: 2477692
e-mail: hkaru@cbsl.lk
4th April 2007

To: CEOs of All Commercial Banks

LIGHT A MILLION CANDLES CAMPAIGN

The urgent attention of all commercial banks is drawn to interpretation clause 33 of the Financial Transactions Reporting Act No.6 of 2006 which lists “offences against children” as an unlawful activity in terms of the law.

In this regard it has been brought to our attention that child pornography websites are being contributed to by customers through electronic payments systems and internet transactions. It is felt that credit cards remain the most common method of on-line payment used by consumers and utilized by purveyors of pornographic material.

A task force of the Sri Lanka Commercial Banks established for this purpose, in collaboration with the FIU, is working on a modus operandi to eradicate the commercial viability of child pornography.

The Financial Intelligence Unit, in its commitment to this noble cause and in giving effect to the provisions of the FTRA, invites the immediate attention of all commercial banks to the following imperatives:-

- To initiate, with immediate effect, additional KYC and CDD on existing and new credit card merchant bases with a special focus on the nature of business;
- Report immediately to the FIU, in the form of a Suspicious Transaction Report, in terms of Section 7(1)(a) of the FTRA, any customer, transaction or merchant involved in offences against children, as illustrated above.

Please acknowledge receipt.

Actg. Additional Director
Financial Intelligence Unit

Copy to: All Compliance Officers
Sri Lanka Banks' Association
Director/Bank Supervision Department

Directions issued by the Monetary Board of the Central Bank of Sri Lanka under Section 46(1) of the Banking Act No. 30 of 1988, as amended.

Nivard Ajith Leslie Cabraal
Governor

Colombo
26 December 2007

DIRECTIONS
BANKING ACT DIRECTION NO. 11 OF 2007
CORPORATE GOVERNANCE FOR
LICENSED COMMERCIAL BANKS IN SRI LANKA

In the exercise of the powers conferred by Section 46(1) of the Banking Act No. 30 of 1988, last amended by the Banking Act No. 46 of 2006, the Monetary Board hereby issues the following Directions on Corporate Governance for Licensed Commercial Banks in Sri Lanka. These Directions may be cited as the Banking Act Direction No. 11 of 2007. The Sections referred to in these Directions will be those of the Banking Act No. 30 of 1988, last amended by the Banking Act No. 46 of 2006.

1. Responsibilities and Empowerment under the Banking Act and the Monetary Law Act

- 1(1)** In terms of Section 46(1) of the Banking Act No. 30 of 1988 last amended by No. 46 of 2006, in order to ensure the soundness of the banking system, the Monetary Board has been empowered to issue Directions to licensed commercial banks, regarding the manner in which any aspect of the business of such banks is to be conducted.
- 1(2)** In terms of Section 5 of the Monetary Law Act No. 58 of 1949, the Central Bank of Sri Lanka is charged with the duty of securing, as far as possible by action authorised by such Act, the two objectives, namely, (a) economic and price stability and (b) financial system stability.
- 1(3)** In terms of Section 10(c) of the Monetary Law Act, the Monetary Board, in the exercise of its powers, duties, functions and responsibilities, is empowered to make such rules and regulations as the Monetary Board may consider necessary, in relation to any matter affecting or connected with or incidental to the exercise, discharge, or performance of the powers, functions, and duties of the Central Bank of Sri Lanka.
- 1(4)** Under the provisions of the Monetary Law Act No. 58 of 1949, the supervision of banks has been made a duty of the Central Bank on account of specific reasons as stated in John Exter's Report on the Monetary Law Act which states, *inter alia*, as follows: "*Banking is an economic activity which affects the public welfare to an unusual degree; it touches in one way or another, almost every phase of a country's economic life. Sound banking is essential to healthy and vigorous economic development. Supervision of banks helps to protect the public against mismanagement, bank failures, and loss of confidence in the banking system. It helps to protect depositors and stock-holders against loss and frequently enables bank directors and officers to manage the affairs of their banks more wisely and intelligently.*"
- 1(5)** Accordingly, in order to enhance the overall banking sector stability which is the fundamental to financial system stability, the Monetary Board, hereby issues Directions under Section 46(1) of the Banking Act No. 30 of 1988 to improve and sustain the corporate governance processes and practices of the licensed commercial banks in Sri Lanka.
- 1(6)** For purposes of this Direction, Corporate Governance processes and practices shall be deemed to be the management framework that facilitates the conduct of the banking business in a responsible and accountable manner so as to promote the safety and soundness of the individual banks, thereby leading to the stability of the overall banking sector.
- 1(7)** The rules of corporate governance as contained in Direction 3 of these Directions have, therefore, been developed on the basis of certain fundamental principles as set out in Direction 2 of these Directions with a view to facilitating the underlying supervisory responsibilities of the Central Bank and to promote safety and soundness of the banking system.

2. The Principles upon which the rules of Corporate Governance have been based upon and developed are the following:

The principles set out in this Direction 2 should be referred to for explanatory purposes and/or for clarification purposes only, so as to understand the rationale for the rules as contained in Direction 3 hereof. Hence, strict compliance under these Directions shall only be in respect of the rules that are set out under Direction 3.

2(1) Principle: The Responsibilities of the Board

- 2(1)(i)** The board of directors should assume the overall responsibility and accountability in respect of: (a) the management of the affairs of the bank, i.e., conduct of business and maintenance of prudent risk management mechanisms; and (b) the safety and soundness of the bank.
- 2(1)(ii)** Towards this end, the board should: (a) determine the structure of the management of affairs of the bank; (b) delegate business operations to key management personnel led by the chief executive officer designated by the board; (c) assume policy making and risk management for the business; and (d) ensure the effective role of the key management personnel. Key management personnel shall mean such key executives of the bank as defined in the International Accounting Standards.
- 2(1)(iii)** The overall responsibility of the board should not be construed as an obligation to undertake the inspection of day-to-day activities, but should rather be understood as an obligation to oversee and ensure that the key management personnel are carrying out the day-to-day activities of the bank in a safe and sound manner in accordance with the policies set by the board.
- 2(1)(iv)** Directors should understand the business and risk management mechanism of the bank and take objective decisions in the interest of the bank's depositors, creditors, shareholders and other stakeholders. Further, they should ensure that the bank does not act in a manner that is detrimental or prejudicial to the interests of, and obligations to, depositors and creditors.
- 2(1)(v)** The board should take the responsibility for compliance with accepted rules of corporate governance. They should also ensure compliance with all regulatory and supervisory requirements. Further, they should ensure that an effective combination of professionals with practical experience in relevant subjects such as banking, finance, economics, business management, human resource management, law, marketing, information technology or any other discipline relevant or complementary to banking operations, is available in the bank to undertake its operations and discharge its responsibilities.
- 2(1)(vi)** The directors should be aware of potential civil and criminal liabilities that may arise from their failure to discharge their duties diligently. They should also understand that they should act with due care and prudence. In addition, the directors of state owned banks should be aware of the additional liabilities that arise from the status of such banks being state enterprises and consequently being accountable to the public. It is, therefore, necessary that directors commit sufficient time and energy to fulfilling the board's responsibilities in managing the affairs of the bank in a prudent manner.

2(2) Principle: The Board's composition

- 2(2)(i)** The board should be composed of a healthy mix of executive directors and non-executive directors. Some of the non-executive directors should also be independent so that there is strong independent element brought into the decision-making process.
- 2(2)(ii)** The board's composition should ensure a balance of skills and experience as may be deemed appropriate and desirable for the requirements of the bank.
- 2(2)(iii)** The banking industry worldwide is making tremendous progress and undergoing rapid change with new innovations, instruments, technologies, products, systems and processes being introduced regularly. It is vital therefore, that the directors should be persons who would: (a) be able to keep abreast with these changes, and (b) provide continuous contribution and guidance to the board decision-making process.
- 2(2)(iv)** There should be a gradual infusion of new ideas into the board. There should also be assurance that the relationships between the directors amongst themselves as well as between the directors and the key management personnel is at a level that does not suggest the existence of excessive familiarity, undue influence or coercion. In this context, it should be noted that very long-standing relationships could sometimes impair the high sense of values, independence and objectivity that is needed in the discharge of the duties of a director of a bank.

2(3) Principle: Criteria to assess the Fitness and Propriety of Directors

- 2(3)(i)** In addition to the principles under the board's composition in Direction 2(2) above, directors should be fit and proper persons in order to be eligible to hold office as directors of a bank and no person should serve as a director unless such person is a fit and proper person.
- 2(3)(ii)** There is strong need for commitment and effective contribution to the prudent management of the affairs of the bank. It is very likely that the effectiveness of such commitment and contribution would tend to decrease with advanced age of directors and more particularly, if the age of such director is well beyond the normal age of retirement, as generally accepted in the country.

2(4) Principle: Management functions delegated by the Board

- 2(4)(i)** The board should have a formal schedule of matters specifically reserved to it for decision. The board should also give clear directions to key management personnel, as to the matters that should be approved by the board before decisions are made by key management personnel, on behalf of the bank.

2(5) Principle: The Chairman and the Chief Executive Officer

- 2(5)(i)** There are two key aspects of the management of every bank, viz., (a) the overall governance by the board, and (b) the day-to-day management of the bank's business by the CEO, in line with board approved strategic objectives, corporate values, overall risk policy and risk management procedures.
- 2(5)(ii)** There should be a clear division of these responsibilities at the board level and the executive management level to ensure a greater balance of power and authority, so that powers are not concentrated in any one individual.
- 2(5)(iii)** The board should appoint a chairman as well as a chief executive officer. The division of responsibilities between the chairman and chief executive officer should be clearly established and set out in writing.

2(6) Principle: Board appointed Committees

- 2(6)(i)** The board should appoint separate board committees for audit, selection, remuneration, integrated risk management and such other subjects as determined by the Board to ensure its oversight and control over the affairs of the bank.
- 2(6)(ii)** Where the board appoints a committee, it should set out the authority of the committee, and in particular, whether the committee has the authority to act on behalf of the board or simply has the authority to examine a particular issue and report back to the board with recommendations.
- 2(6)(iii)** Each committee should be chaired by a non-executive director who has some expertise in the relevant subject, and who preferably should be independent too. The majority of the members of the board committee should consist of non-executive directors with at least one independent director in the committee. If a need arises, professionals from outside may be invited or hired to serve in a committee. Bank staff may be present at the board committees for advice or special assignments, on invitation.

2(7) Principle: Related party transactions

- 2(7)(i)** The board should ensure that the bank does not engage in transactions with "related parties" in a manner that would grant such parties "more favourable treatment" than that accorded to other constituents of the bank carrying on the same business.

2(8) Principle: Disclosures

- 2(8)(i)** The objective of disclosure is the transparency of information relating to affairs and risk management of banks which would help to promote market discipline of the respective banks.
- 2(8)(ii)** Since market disclosure is the focus of the Pillar III of the risk management based capital standard known as Basel II recommended by the Basel Committee on Banking Supervision at the Bank for International Settlements, (which is the globally accepted body on introducing international standards on Bank Supervision), the extent of disclosures should be commensurate with the size, ownership structure, systemic importance, risk profile and the business model of the bank. Accordingly, it should be noted that the adequate and timely public disclosure of relevant information by banks would facilitate enhanced market discipline and lead to better and more effective corporate governance.

2(8)(iii) Disclosures by banks should generally include disclosures relating to capital adequacy, key performance indicators, business concentrations, transactions with related parties, corporate governance statements, financial statements, etc., and should be consistent with accounting standards, regulatory requirements as well as with any other information disclosed on voluntary basis.

3. The following rules of Corporate Governance shall be complied by all licensed commercial banks in Sri Lanka and such compliance shall be as provided for in Direction 3(9)(i) hereof.

3 (1) The Responsibilities of the Board

3(1)(i) The board shall strengthen the safety and soundness of the bank by ensuring the implementation of the following:

- a) Approve and oversee the bank's strategic objectives and corporate values and ensure that these are communicated throughout the bank;
- b) Approve the overall business strategy of the bank, including the overall risk policy and risk management procedures and mechanisms with measurable goals, for at least the next three years;
- c) Identify the principal risks and ensure implementation of appropriate systems to manage the risks prudently;
- d) Approve implementation of a policy of communication with all stakeholders, including depositors, creditors, share-holders and borrowers;
- e) Review the adequacy and the integrity of the bank's internal control systems and management information systems;
- f) Identify and designate key management personnel, as defined in the International Accounting Standards, who are in a position to: (i) significantly influence policy; (ii) direct activities; and (iii) exercise control over business activities, operations and risk management;
- g) Define the areas of authority and key responsibilities for the board directors themselves and for the key management personnel;
- h) Ensure that there is appropriate oversight of the affairs of the bank by key management personnel, that is consistent with board policy;
- i) Periodically assess the effectiveness of the board directors' own governance practices, including: (i) the selection, nomination and election of directors and key management personnel; (ii) the management of conflicts of interests; and (iii) the determination of weaknesses and implementation of changes where necessary;
- j) Ensure that the bank has an appropriate succession plan for key management personnel;
- k) Meet regularly, on a needs basis, with the key management personnel to review policies, establish communication lines and monitor progress towards corporate objectives;
- l) Understand the regulatory environment and ensure that the bank maintains an effective relationship with regulators;
- m) Exercise due diligence in the hiring and oversight of external auditors.

3(1)(ii) The board shall appoint the chairman and the chief executive officer and define and approve the functions and responsibilities of the chairman and the chief executive officer in line with Direction 3(5) of these Directions.

3(1)(iii) The board shall meet regularly and board meetings shall be held at least twelve times a year at approximately monthly intervals. Such regular board meetings shall normally involve active participation in person of a majority of directors entitled to be present. Obtaining the board's consent through the circulation of written resolutions/papers shall be avoided as far as possible.

3(1)(iv) The board shall ensure that arrangements are in place to enable all directors to include matters and proposals in the agenda for regular board meetings where such matters and proposals relate to the promotion of business and the management of risks of the bank.

- 3(1)(v)** The board procedures shall ensure that notice of at least 7 days is given of a regular board meeting to provide all directors an opportunity to attend. For all other board meetings, reasonable notice may be given.
- 3(1)(vi)** The board procedures shall ensure that a director who has not attended at least two-thirds of the meetings in the period of 12 months immediately preceding or has not attended the immediately preceding three consecutive meetings held, shall cease to be a director. Participation at the directors' meetings through an alternate director shall, however, be acceptable as attendance.
- 3(1)(vii)** The board shall appoint a company secretary who satisfies the provisions of Section 43 of the Banking Act No. 30 of 1988, whose primary responsibilities shall be to handle the secretariat services to the board and shareholder meetings and to carry out other functions specified in the statutes and other regulations.
- 3(1)(viii)** All directors shall have access to advice and services of the company secretary with a view to ensuring that board procedures and all applicable rules and regulations are followed.
- 3(1)(ix)** The company secretary shall maintain the minutes of board meetings and such minutes shall be open for inspection at any reasonable time, on reasonable notice by any director.
- 3(1)(x)** Minutes of board meetings shall be recorded in sufficient detail so that it is possible to gather from the minutes, as to whether the board acted with due care and prudence in performing its duties. The minutes shall also serve as a reference for regulatory and supervisory authorities to assess the depth of deliberations at the board meetings. Therefore, the minutes of a board meeting shall clearly contain or refer to the following: (a) a summary of data and information used by the board in its deliberations; (b) the matters considered by the board; (c) the fact-finding discussions and the issues of contention or dissent which may illustrate whether the board was carrying out its duties with due care and prudence; (d) the testimonies and confirmations of relevant executives which indicate compliance with the board's strategies and policies and adherence to relevant laws and regulations; (e) the board's knowledge and understanding of the risks to which the bank is exposed and an overview of the risk management measures adopted; and (f) the decisions and board resolutions.
- 3(1)(xi)** There shall be a procedure agreed by the board to enable directors, upon reasonable request, to seek independent professional advice in appropriate circumstances, at the bank's expense. The board shall resolve to provide separate independent professional advice to directors to assist the relevant director or directors to discharge his/her/their duties to the bank.
- 3(1)(xii)** Directors shall avoid conflicts of interests, or the appearance of conflicts of interest, in their activities with, and commitments to, other organisations or related parties. If a director has a conflict of interest in a matter to be considered by the board, which the board has determined to be material, the matter should be dealt with at a board meeting, where independent non-executive directors [refer to Direction 3(2)(iv) of these Directions] who have no material interest in the transaction, are present. Further, a director shall abstain from voting on any board resolution in relation to which he/she or any of his/her close relation or a concern in which a director has substantial interest, is interested and he/she shall not be counted in the quorum for the relevant agenda item at the board meeting.
- 3(1)(xiii)** The board shall have a formal schedule of matters specifically reserved to it for decision to ensure that the direction and control of the bank is firmly under its authority.
- 3(1)(xiv)** The board shall, if it considers that the bank is, or is likely to be, unable to meet its obligations or is about to become insolvent or is about to suspend payments due to depositors and other creditors, forthwith inform the Director of Bank Supervision of the situation of the bank prior to taking any decision or action.
- 3(1)(xv)** The board shall ensure that the bank is capitalised at levels as required by the Monetary Board in terms of the capital adequacy ratio and other prudential grounds.
- 3(1)(xvi)** The board shall publish in the bank's Annual Report, an annual corporate governance report setting out the compliance with Direction 3 of these Directions.
- 3(1)(xvii)** The board shall adopt a scheme of self-assessment to be undertaken by each director annually, and maintain records of such assessments.
- 3(2) The Board's Composition**
- 3(2)(i)** The number of directors on the board shall not be less than 7 and not more than 13.

- 3(2)(ii)** (A) 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, and such period in office shall be inclusive of the total period of service served by such director up to January 1, 2008.
- (B) In this context, the following transitional provisions shall apply:
- a) In the event that there is only one director on the board who has served more than nine years as at January 1, 2008, he/she shall be deemed to have vacated the office as a director as at December 31, 2008.
 - b) In the event that there are two or more directors on the board who have served more than nine years as at January 1, 2008, the following provisions shall apply:
 - I. Of those directors whose period of service has exceeded nine years, the longest serving director, shall be deemed to have vacated office as a Director on December 31, 2008.
 - II. Thereafter, at the end of each succeeding year, the remaining directors shall be deemed to have vacated office in sequence, at least one director each year, (on the basis of the longest to the shortest length of service as a director), until all directors who have served a period in excess of nine years as at January 1, 2008, have been deemed to have vacated office. Provided also, that all directors of the bank who have served more than nine years as at January 1, 2008 shall be deemed to have vacated their office by or before December 31, 2011.
 - c) In the event there are any directors who are due to complete nine years of service between January 1, 2008 and December 31, 2010, such directors shall also be deemed to have vacated office, in sequence, at least one director each year, (on the basis of the longest to the shortest length of service as a director), after the directors as set out in Direction 3(2)(ii)(B) (b) have vacated their office as directors. Provided, however, that all such directors covered by this sub-direction (c) shall also be deemed to have vacated their office by or before December 31, 2011.
- 3(2)(iii)** An employee of a bank may be appointed, elected or nominated as a director of the bank (hereinafter referred to as an “executive director”) provided that the number of executive directors shall not exceed one-third of the number of directors of the board. In such an event, one of the executive directors shall be the chief executive officer of the bank.
- 3(2)(iv)** The board shall have at least three independent non-executive directors or one third of the total number of directors, whichever is higher. This sub-direction shall be applicable from January 1, 2010 onwards.
- A non-executive director shall not be considered independent if he/she:
- a) has direct and indirect shareholdings of more than 1% of the bank;
 - b) currently has or had during the period of two years immediately preceding his/her appointment as director, any business transactions with the bank as described in Direction 3 (7) hereof, exceeding 10% of the regulatory capital of the bank.
 - c) has been employed by the bank during the two year period immediately preceding the appointment as director;
 - d) has a close relation who is a director or chief executive officer or a member of key management personnel or a material shareholder of the bank or another bank. For this purpose, a “close relation” shall mean the spouse or a financially dependant child;
 - e) represents a specific stakeholder of the bank;
 - f) is an employee or a director or a material shareholder in a company or business organization:
 - I. which currently has a transaction with the bank as defined in Direction 3(7) of these Directions, exceeding 10% of the regulatory capital of the bank, or
 - II. in which any of the other directors of the bank are employed or are directors or are material shareholders; or
 - III. in which any of the other directors of the bank have a transaction as defined in Direction 3(7) of these Directions, exceeding 10% of regulatory capital in the bank;

- 3(2)(v)** In the event an alternate director is appointed to represent an independent director, the person so appointed shall also meet the criteria that applies to the independent director.
- 3(2)(vi)** Non-executive directors shall be persons with credible track records and/or have necessary skills and experience to bring an independent judgment to bear on issues of strategy, performance and resources.
- 3(2)(vii)** A meeting of the board shall not be duly constituted, although the number of directors required to constitute the quorum at such meeting is present, unless more than one half of the number of directors present at such meeting are non-executive directors. This sub-direction shall be applicable from January 1, 2010 onwards.
- 3(2)(viii)** The independent non-executive directors shall be expressly identified as such in all corporate communications that disclose the names of directors of the bank. The bank shall disclose the composition of the board, by category of directors, including the names of the chairman, executive directors, non-executive directors and independent non-executive directors in the annual corporate governance report.
- 3(2)(ix)** There shall be a formal, considered and transparent procedure for the appointment of new directors to the board. There shall also be procedures in place for the orderly succession of appointments to the board.
- 3(2)(x)** All directors appointed to fill a casual vacancy shall be subject to election by shareholders at the first general meeting after their appointment.
- 3(2)(xi)** If a director resigns or is removed from office, the board shall: (a) announce the director's resignation or removal and the reasons for such removal or resignation including but not limited to information relating to the relevant director's disagreement with the bank, if any; and (b) issue a statement confirming whether or not there are any matters that need to be brought to the attention of shareholders.
- 3(2)(xii)** A director or an employee of a bank shall not be appointed, elected or nominated as a director of another bank except where such bank is a subsidiary company or an associate company of the first mentioned bank.

3(3) Criteria to assess the fitness and propriety of directors

In addition to provisions of Section 42 of the Banking Act No. 30 of 1988, the criteria set out below shall apply to determine the fitness and propriety of a person who serves or wishes to serve as a director of a bank. Non-compliance with any one of the criteria as set out herein shall disqualify a person to be appointed, elected or nominated as a director or to continue as a director.

- 3(3)(i)** The age of a person who serves as director shall not exceed 70 years.
 - (A) Where a director who is currently serving at a bank is over 70 years of age as at January 1, 2008, the following transitional provisions shall apply, subject however to the provisions as set out in Direction 3(2)(ii) hereof.
 - a) If a director is over 75 years of age as at January 1, 2008, such director may continue to serve as a director for a further period that shall not extend beyond December 31, 2008, and shall be deemed to have vacated office on December 31, 2008;
 - b) If a director is between 70 and 75 years of age as at January 1, 2008, such director may continue to serve as a director for a further period that shall not extend beyond December 31, 2009, and shall be deemed to have vacated office on December 31, 2009.
 - (B) Where a director who is currently serving at a bank reaches the age of 70 years, between January 1, 2008 and December 31, 2009, such director may, subject to the provisions as set out in Direction 3(2)(ii) hereof, continue to serve as a director for a further period that shall not extend beyond December 31, 2010 and shall be deemed to have vacated office on December 31, 2010.
 - 3(3)(ii)** A person shall not hold office as a director of more than 20 companies/entities/institutions inclusive of subsidiaries or associate companies of the bank. Of such 20 companies/entities/ institutions, not more than 10 companies shall be those classified as Specified Business Entities in terms of the Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995.
- 3(4) Management functions delegated by the Board**
- 3(4)(i)** The directors shall carefully study and clearly understand the delegation arrangements in place.
 - 3(4)(ii)** The board shall not delegate any matters to a board committee, chief executive officer, executive directors or

key management personnel, to an extent that such delegation would significantly hinder or reduce the ability of the board as a whole to discharge its functions.

- 3(4)(iii)** The board shall review the delegation processes in place on a periodic basis to ensure that they remain relevant to the needs of the bank.

3(5) The Chairman and Chief Executive Officer

- 3(5)(i)** The roles of chairman and chief executive officer shall be separate and shall not be performed by the same individual.

- 3(5)(ii)** The chairman shall be a non-executive director and preferably an independent director as well. In the case where the chairman is not an independent director, the board shall designate an independent director as the Senior Director with suitably documented terms of reference to ensure a greater independent element. The designation of the Senior Director shall be disclosed in the bank's Annual Report.

- 3(5)(iii)** The board shall disclose in its corporate governance report, which shall be an integral part of its Annual Report, the identity of the chairman and the chief executive officer and the nature of any relationship [including financial, business, family or other material/relevant relationship(s)], if any, between the chairman and the chief executive officer and the relationships among members of the board.

- 3(5)(iv)** The chairman shall: (a) provide leadership to the board; (b) ensure that the board works effectively and discharges its responsibilities; and (c) ensure that all key and appropriate issues are discussed by the board in a timely manner.

- 3(5)(v)** The chairman shall be primarily responsible for drawing up and approving the agenda for each board meeting, taking into account where appropriate, any matters proposed by the other directors for inclusion in the agenda. The chairman may delegate the drawing up of the agenda to the company secretary.

- 3(5)(vi)** The chairman shall ensure that all directors are properly briefed on issues arising at board meetings and also ensure that directors receive adequate information in a timely manner.

- 3(5)(vii)** The chairman shall encourage all directors to make a full and active contribution to the board's affairs and take the lead to ensure that the board acts in the best interests of the bank.

- 3(5)(viii)** The chairman shall facilitate the effective contribution of non-executive directors in particular and ensure constructive relations between executive and non-executive directors.

- 3(5)(ix)** The chairman, shall not engage in activities involving direct supervision of key management personnel or any other executive duties whatsoever.

- 3(5)(x)** The chairman shall ensure that appropriate steps are taken to maintain effective communication with shareholders and that the views of shareholders are communicated to the board.

- 3(5)(xi)** The chief executive officer shall function as the apex executive-in-charge of the day-to-day-management of the bank's operations and business.

3(6) Board appointed Committees

- 3(6)(i)** Each bank shall have at least four board committees as set out in Directions 3(6)(ii), 3(6)(iii), 3(6)(iv) and 3(6)(v) of these Directions. Each committee shall report directly to the board. All committees shall appoint a secretary to arrange the meetings and maintain minutes, records, etc., under the supervision of the chairman of the committee. The board shall present a report of the performance on each committee, on their duties and roles at the annual general meeting.

- 3(6)(ii)** The following rules shall apply in relation to the Audit Committee:

- a) The chairman of the committee shall be an independent non-executive director who possesses qualifications and experience in accountancy and/or audit.
- b) All members of the committee shall be non-executive directors.
- c) The committee shall make recommendations on matters in connection with: (i) the appointment of the external auditor for audit services to be provided in compliance with the relevant statutes; (ii) the implementation of the Central Bank guidelines issued to auditors from time to time; (iii) the application

of the relevant accounting standards; and (iv) the service period, audit fee and any resignation or dismissal of the auditor; provided that the engagement of the Audit partner shall not exceed five years, and that the particular Audit partner is not re-engaged for the audit before the expiry of three years from the date of the completion of the previous term.

- d) The committee shall review and monitor the external auditor's independence and objectivity and the effectiveness of the audit processes in accordance with applicable standards and best practices.
- e) The committee shall develop and implement a policy on the engagement of an external auditor to provide non-audit services that are permitted under the relevant statutes, regulations, requirements and guidelines. In doing so, the committee shall ensure that the provision by an external auditor of non-audit services does not impair the external auditor's independence or objectivity. When assessing the external auditor's independence or objectivity in relation to the provision of non-audit services, the committee shall consider:
 - I. whether the skills and experience of the audit firm make it a suitable provider of the non-audit services;
 - II. whether there are safeguards in place to ensure that there is no threat to the objectivity and/or independence in the conduct of the audit resulting from the provision of such services by the external auditor; and
 - III. whether the nature of the non-audit services, the related fee levels and the fee levels individually and in aggregate relative to the audit firm, pose any threat to the objectivity and/or independence of the external auditor.
- f) The committee shall, before the audit commences, discuss and finalise with the external auditors the nature and scope of the audit, including: (i) an assessment of the bank's compliance with the relevant Directions in relation to corporate governance and the management's internal controls over financial reporting; (ii) the preparation of financial statements for external purposes in accordance with relevant accounting principles and reporting obligations; and (iii) the co-ordination between firms where more than one audit firm is involved.
- g) The committee shall review the financial information of the bank, in order to monitor the integrity of the financial statements of the bank, its annual report, accounts and quarterly reports prepared for disclosure, and the significant financial reporting judgments contained therein. In reviewing the bank's annual report and accounts and quarterly reports before submission to the board, the committee shall focus particularly on: (i) major judgmental areas; (ii) any changes in accounting policies and practices; (iii) significant adjustments arising from the audit; (iv) the going concern assumption; and (v) the compliance with relevant accounting standards and other legal requirements.
- h) The committee shall discuss issues, problems and reservations arising from the interim and final audits, and any matters the auditor may wish to discuss including those matters that may need to be discussed in the absence of key management personnel, if necessary.
- i) The committee shall review the external auditor's management letter and the management's response thereto.
- j) The committee shall take the following steps with regard to the internal audit function of the bank:
 - I. Review the adequacy of the scope, functions and resources of the internal audit department, and satisfy itself that the department has the necessary authority to carry out its work;
 - II. Review the internal audit programme and results of the internal audit process and, where necessary, ensure that appropriate actions are taken on the recommendations of the internal audit department;
 - III. Review any appraisal or assessment of the performance of the head and senior staff members of the internal audit department;
 - IV. Recommend any appointment or termination of the head, senior staff members and outsourced service providers to the internal audit function;
 - V. Ensure that the committee is apprised of resignations of senior staff members of the internal audit department including the chief internal auditor and any outsourced service providers, and to

provide an opportunity to the resigning senior staff members and outsourced service providers to submit reasons for resigning;

VI. Ensure that the internal audit function is independent of the activities it audits and that it is performed with impartiality, proficiency and due professional care;

- k) The committee shall consider the major findings of internal investigations and management's responses thereto;
- l) The chief finance officer, the chief internal auditor and a representative of the external auditors may normally attend meetings. Other board members and the chief executive officer may also attend meetings upon the invitation of the committee. However, at least twice a year, the committee shall meet with the external auditors without the executive directors being present.
- m) The committee shall have: (i) explicit authority to investigate into any matter within its terms of reference; (ii) the resources which it needs to do so; (iii) full access to information; and (iv) authority to obtain external professional advice and to invite outsiders with relevant experience to attend, if necessary.
- n) The committee shall meet regularly, with due notice of issues to be discussed and shall record its conclusions in discharging its duties and responsibilities.
- o) The board shall disclose in an informative way, (i) details of the activities of the audit committee; (ii) the number of audit committee meetings held in the year; and (iii) details of attendance of each individual director at such meetings.
- p) The secretary of the committee (who may be the company secretary or the head of the internal audit function) shall record and keep detailed minutes of the committee meetings.
- q) The committee shall review arrangements by which employees of the bank may, in confidence, raise concerns about possible improprieties in financial reporting, internal control or other matters. Accordingly, the committee shall ensure that proper arrangements are in place for the fair and independent investigation of such matters and for appropriate follow-up action and to act as the key representative body for overseeing the bank's relations with the external auditor.

3(6)(iii) The following rules shall apply in relation to the Human Resources and Remuneration Committee:

- a) The committee shall determine the remuneration policy (salaries, allowances and other financial payments) relating to directors, Chief Executive Officer (CEO) and key management personnel of the bank.
- b) The committee shall set goals and targets for the directors, CEO and the key management personnel.
- c) The committee shall evaluate the performance of the CEO and key management personnel against the set targets and goals periodically and determine the basis for revising remuneration, benefits and other payments of performance-based incentives.
- d) The CEO shall be present at all meetings of the committee, except when matters relating to the CEO are being discussed.

3(6)(iv) The following rules shall apply in relation to the Nomination Committee:

- a) The committee shall implement a procedure to select/appoint new directors, CEO and key management personnel.
- b) The committee shall consider and recommend (or not recommend) the re-election of current directors, taking into account the performance and contribution made by the director concerned towards the overall discharge of the board's responsibilities.
- c) The committee shall set the criteria such as qualifications, experience and key attributes required for eligibility to be considered for appointment or promotion to the post of CEO and the key management positions.
- d) The committee shall ensure that directors, CEO and key management personnel are fit and proper persons to hold office as specified in the criteria given in Direction 3(3) and as set out in the Statutes.
- e) The committee shall consider and recommend from time to time, the requirements of additional/new expertise and the succession arrangements for retiring directors and key management personnel.

- f) The Committee shall be chaired by an Independent Director and preferably be constituted with a majority of Independent Directors. The CEO may be present at meetings by invitation.

3(6)(v) The following rules shall apply in relation to the Integrated Risk Management Committee:

- a) The committee shall consist of at least three non-executive directors, chief executive officer and key management personnel supervising broad risk categories, i.e., credit, market, liquidity, operational and strategic risks. The committee shall work with key management personnel very closely and make decisions on behalf of the board within the framework of the authority and responsibility assigned to the committee.
- b) The committee shall assess all risks, i.e., credit, market, liquidity, operational and strategic risks to the bank on a monthly basis through appropriate risk indicators and management information. In the case of subsidiary companies and associate companies, risk management shall be done, both on a bank basis and group basis.
- c) The committee shall review the adequacy and effectiveness of all management level committees such as the credit committee and the asset-liability committee to address specific risks and to manage those risks within quantitative and qualitative risk limits as specified by the committee.
- d) The committee shall take prompt corrective action to mitigate the effects of specific risks in the case such risks are at levels beyond the prudent levels decided by the committee on the basis of the bank's policies and regulatory and supervisory requirements.
- e) The committee shall meet at least quarterly to assess all aspects of risk management including updated business continuity plans.
- f) The committee shall take appropriate actions against the officers responsible for failure to identify specific risks and take prompt corrective actions as recommended by the committee, and/or as directed by the Director of Bank Supervision.
- g) The committee shall submit a risk assessment report within a week of each meeting to the board seeking the board's views, concurrence and/or specific directions.
- h) The committee shall establish a compliance function to assess the bank's compliance with laws, regulations, regulatory guidelines, internal controls and approved policies on all areas of business operations. A dedicated compliance officer selected from key management personnel shall carry out the compliance function and report to the committee periodically.

3 (7) Related party transactions

3(7)(i) The board shall take the necessary steps to avoid any conflicts of interest that may arise from any transaction of the bank with any person, and particularly with the following categories of persons who shall be considered as related parties" for the purposes of this Direction:

- a) Any of the bank's subsidiary companies;
- b) Any of the bank's associate companies;
- c) Any of the directors of the bank;
- d) Any of the bank's key management personnel;
- e) A close relation of any of the bank's directors or key management personnel;
- f) A shareholder owning a material interest in the bank;
- g) A concern in which any of the bank's directors or a close relation of any of the bank's directors or any of its material shareholders has a substantial interest.

3(7)(ii) The type of transactions with related parties that shall be covered by this Direction shall include the following:

- a) The grant of any type of accommodation, as defined in the Monetary Board's Directions on maximum amount of accommodation,
- b) The creation of any liabilities of the bank in the form of deposits, borrowings and investments,
- c) The provision of any services of a financial or non-financial nature provided to the bank or received from the bank,

- d) The creation or maintenance of reporting lines and information flows between the bank and any related parties which may lead to the sharing of potentially proprietary, confidential or otherwise sensitive information that may give benefits to such related parties.
- 3(7)(iii)** The board shall ensure that the bank does not engage in transactions with related parties as defined in Direction 3(7)(i) above, in a manner that would grant such parties “more favourable treatment” than that accorded to other constituents of the bank carrying on the same business. In this context, “more favourable treatment” shall mean and include treatment, including the:
- a) Granting of “total net accommodation” to related parties, exceeding a prudent percentage of the bank’s regulatory capital, as determined by the board. For purposes of this sub-direction:
 - I. “Accommodation” shall mean accommodation as defined in the Banking Act Directions No. 7 of 2007 on Maximum Amount of Accommodation.
 - II. The “total net accommodation shall be” computed by deducting from the total accommodation, the cash collateral and investments made by such related parties in the bank’s share capital and debt instruments with a maturity of 5 years or more.
 - b) Charging of a lower rate of interest than the bank’s best lending rate or paying more than the bank’s deposit rate for a comparable transaction with an unrelated comparable counterparty;
 - c) Providing of preferential treatment, such as favourable terms, covering trade losses and/or waiving fees/commissions, that extend beyond the terms granted in the normal course of business undertaken with unrelated parties;
 - d) Providing services to or receiving services from a related-party without an evaluation procedure;
 - e) Maintaining reporting lines and information flows that may lead to sharing potentially proprietary, confidential or otherwise sensitive information with related parties, except as required for the performance of legitimate duties and functions.
- 3(7)(iv)** A bank shall not grant any accommodation to any of its directors or to a close relation of such director unless such accommodation is sanctioned at a meeting of its board of directors, with not less than two-thirds of the number of directors other than the director concerned, voting in favour of such accommodation. This accommodation shall be secured by such security as may from time to time be determined by the Monetary Board as well.
- 3(7)(v)** (a) Where any accommodation has been granted by a bank to a person or a close relation of a person or to any concern in which the person has a substantial interest, and such person is subsequently appointed as a director of the bank, steps shall be taken by the bank to obtain the necessary security as may be approved for that purpose by the Monetary Board, within one year from the date of appointment of the person as a director.
- (b) Where such security is not provided by the period as provided in Direction 3(7)(v)(a) above, the bank shall take steps to recover any amount due on account of any accommodation, together with interest, if any, within the period specified at the time of the grant of accommodation or at the expiry of a period of eighteen months from the date of appointment of such director, whichever is earlier.
- (c) Any director who fails to comply with the above sub-directions shall be deemed to have vacated the office of director and the bank shall disclose such fact to the public.
- (d) This sub-direction, however, shall not apply to a director who at the time of the grant of the accommodation was an employee of the bank and the accommodation was granted under a scheme applicable to all employees of such bank.
- 3(7)(vi)** A bank shall not grant any accommodation or “more favourable treatment” relating to the waiver of fees and/or commissions to any employee or a close relation of such employee or to any concern in which the employee or close relation has a substantial interest other than on the basis of a scheme applicable to the employees of such bank or when secured by security as may be approved by the Monetary Board in respect of accommodation granted as per Direction 3(7)(v) above.

3(7)(vii) No accommodation granted by a bank under Direction 3(7)(v) and 3(7)(vi) above, nor any part of such accommodation, nor any interest due thereon shall be remitted without the prior approval of the Monetary Board and any remission without such approval shall be void and of no effect.

3 (8) Disclosures

3(8)(i) The board shall ensure that: (a) annual audited financial statements and quarterly financial statements are prepared and published in accordance with the formats prescribed by the supervisory and regulatory authorities and applicable accounting standards, and that (b) such statements are published in the newspapers in an abridged form, in Sinhala, Tamil and English.

3(8)(ii) The board shall ensure that the following minimum disclosures are made in the Annual Report:

- a) A statement to the effect that the annual audited financial statements have been prepared in line with applicable accounting standards and regulatory requirements, inclusive of specific disclosures.
- b) A report by the board on the bank's internal control mechanism that confirms that the financial reporting system has been designed to provide reasonable assurance regarding the reliability of financial reporting, and that the preparation of financial statements for external purposes has been done in accordance with relevant accounting principles and regulatory requirements.
- c) The external auditor's certification on the effectiveness of the internal control mechanism referred to in Direction 3(8)(i)(b) above, in respect of any statements prepared or published after December 31, 2008.
- d) Details of directors, including names, fitness and propriety, transactions with the bank and the total of fees/remuneration paid by the bank.
- e) Total net accommodation as defined in 3(7)(iii) granted to each category of related parties. The net accommodation granted to each category of related parties shall also be disclosed as a percentage of the bank's regulatory capital.
- f) The aggregate values of remuneration paid by the bank to its key management personnel and the aggregate values of the transactions of the bank with its key management personnel, set out by broad categories such as remuneration paid, accommodation granted and deposits or investments made in the bank.
- g) The external auditor's certification of the compliance with these Directions in the annual corporate governance reports published after January 1, 2010.
- h) A report setting out details of the compliance with prudential requirements, regulations, laws and internal controls and measures taken to rectify any material non-compliances.
- i) A statement of the regulatory and supervisory concerns on lapses in the bank's risk management, or non compliance with these Directions that have been pointed out by the Director of Bank Supervision, if so directed by the Monetary Board to be disclosed to the public, together with the measures taken by the bank to address such concerns.

3(9) Transitional and other general provisions

3(9)(i) Compliance with this Direction shall commence from January 1, 2008 onwards and all licensed commercial banks shall fully comply with the provisions of this Direction by or before January 1, 2009 except where extended compliance dates have been specifically provided for in this Direction.

3(9)(ii) In respect of the banks that have been incorporated by specific statutes in Sri Lanka, the boards as specified in such statutes shall continue to function in terms of the provisions of the respective statutes, provided they take steps to comply with all provisions of this Direction that are not inconsistent with the provisions of the respective statutes.

3(9)(iii) This Direction shall apply to the branches of the foreign banks operating in Sri Lanka to the extent that it is not inconsistent with the regulations and laws applicable in such bank's country of incorporation. The branch of a foreign bank shall also publish its parent bank's annual corporate governance report together with its annual report and accounts of the branch operations in Sri Lanka.

3(9)(iv) In the event of a conflict between any of the provisions of this Direction and the Articles of Association (or Internal Rules) pertaining to any bank, the provisions of this Direction shall prevail. However, if the Articles of Association of an individual bank set a more stringent standard than that specified in this Direction, such provisions in the Articles of Association may be followed.

Directions issued by the Monetary Board of the Central Bank of Sri Lanka under Section 76J(1) of the Banking Act No. 30 of 1988, as amended.

Nivard Ajith Leslie Cabraal
Governor

Colombo
26 December 2007

DIRECTIONS
BANKING ACT DIRECTION NO. 12 OF 2007
CORPORATE GOVERNANCE FOR
LICENSED SPECIALISED BANKS IN SRI LANKA

In the exercise of the powers conferred by Section 76J(1) of the Banking Act No. 30 of 1988, last amended by the Banking Act No. 46 of 2006, the Monetary Board hereby issues the following Directions on Corporate Governance for Licensed Specialised Banks in Sri Lanka. These Directions may be cited as the Banking Act Direction No. 12 of 2007. The Sections referred to in these Directions will be those of the Banking Act No. 30 of 1988, last amended by the Banking Act No. 46 of 2006.

- 1. Responsibilities and Empowerment under the Banking Act and the Monetary Law Act**
- 1(1)** In terms of Section 76J(1) of the Banking Act No. 30 of 1988 last amended by No. 46 of 2006, the Monetary Board has been empowered to issue Directions to licensed specialised banks or to any category of licensed specialised banks, regarding the manner in which any aspect of the business of such banks is to be conducted.
- 1(2)** In terms of Section 5 of the Monetary Law Act No. 58 of 1949, the Central Bank of Sri Lanka is charged with the duty of securing, as far as possible by action authorised by such Act, the two objectives, namely, (a) economic and price stability and (b) financial system stability.
- 1(3)** In terms of Section 10(c) of the Monetary Law Act, the Monetary Board, in the exercise of its powers, duties, functions and responsibilities, is empowered to make such rules and regulations as the Monetary Board may consider necessary, in relation to any matter affecting or connected with or incidental to the exercise, discharge, or performance of the powers, functions, and duties of the Central Bank of Sri Lanka.
- 1(4)** Under the provisions of the Monetary Law Act No. 58 of 1949, the supervision of banks has been made a duty of the Central Bank on account of specific reasons as stated in John Exter's Report on the Monetary Law Act which states, *inter alia*, as follows: "*Banking is an economic activity which affects the public welfare to an unusual degree; it touches in one way or another, almost every phase of a country's economic life. Sound banking is essential to healthy and vigorous economic development. Supervision of banks helps to protect the public against mismanagement, bank failures, and loss of confidence in the banking system. It helps to protect depositors and stock-holders against loss and frequently enables bank directors and officers to manage the affairs of their banks more wisely and intelligently.*"
- 1(5)** Accordingly, in order to enhance the overall banking sector stability which is the fundamental to financial system stability, the Monetary Board, hereby issues Directions under Section 76J(1) of the Banking Act No. 30 of 1988 to improve and sustain the corporate governance processes and practices of the licensed specialised banks in Sri Lanka.
- 1(6)** For purposes of this Direction, Corporate Governance processes and practices shall be deemed to be the management framework that facilitates the conduct of the banking business in a responsible and accountable manner so as to promote the safety and soundness of the individual banks, thereby leading to the stability of the overall banking sector.
- 1(7)** The rules of corporate governance as contained in Direction 3 of these Directions have, therefore, been developed on the basis of certain fundamental principles as set out in Direction 2 of these Directions with a view to facilitating the underlying supervisory responsibilities of the Central Bank and to promote safety and soundness of the banking system.
- 2. The Principles upon which the rules of Corporate Governance have been based upon and developed are the following:**

The principles set out in this Direction 2 should be referred to for explanatory purposes and/or for clarification purposes only, so as to understand the rationale for the rules as contained in Direction 3 hereof. Hence, strict compliance under these Directions shall only be in respect of the rules that are set out under Direction 3.

2(1) Principle: The Responsibilities of the Board

- 2(1)(i)** The board of directors should assume the overall responsibility and accountability in respect of: (a) the management of the affairs of the bank, i.e., conduct of business and maintenance of prudent risk management mechanisms; and (b) the safety and soundness of the bank.
- 2(1)(ii)** Towards this end, the board should: (a) determine the structure of the management of affairs of the bank; (b) delegate business operations to key management personnel led by the chief executive officer designated by the board; (c) assume policy making and risk management for the business; and (d) ensure the effective role of the key management personnel. Key management personnel shall mean such key executives of the bank as defined in the International Accounting Standards.
- 2(1)(iii)** The overall responsibility of the board should not be construed as an obligation to undertake the inspection of day-to-day activities, but should rather be understood as an obligation to oversee and ensure that the key management personnel are carrying out the day-to-day activities of the bank in a safe and sound manner in accordance with the policies set by the board.
- 2(1)(iv)** Directors should understand the business and risk management mechanism of the bank and take objective decisions in the interest of the bank's depositors, creditors, shareholders and other stakeholders. Further, they should ensure that the bank does not act in a manner that is detrimental or prejudicial to the interests of, and obligations to, depositors and creditors.
- 2(1)(v)** The board should take the responsibility for compliance with accepted rules of corporate governance. They should also ensure compliance with all regulatory and supervisory requirements. Further, they should ensure that an effective combination of professionals with practical experience in relevant subjects such as banking, finance, economics, business management, human resource management, law, marketing, information technology or any other discipline relevant or complementary to banking operations, is available in the bank to undertake its operations and discharge its responsibilities.
- 2(1)(vi)** The directors should be aware of potential civil and criminal liabilities that may arise from their failure to discharge their duties diligently. They should also understand that they should act with due care and prudence. In addition, the directors of state owned banks should be aware of the additional liabilities that arise from the status of such banks being state enterprises and consequently being accountable to the public. It is, therefore, necessary that directors commit sufficient time and energy to fulfilling the board's responsibilities in managing the affairs of the bank in a prudent manner.

2(2) Principle: The Board's composition

- 2(2)(i)** The board should be composed of a healthy mix of executive directors and non-executive directors. Some of the non-executive directors should also be independent so that there is strong independent element brought into the decision-making process.
- 2(2)(ii)** The board's composition should ensure a balance of skills and experience as may be deemed appropriate and desirable for the requirements of the bank.
- 2(2)(iii)** The banking industry worldwide is making tremendous progress and undergoing rapid change with new innovations, instruments, technologies, products, systems and processes being introduced regularly. It is vital therefore, that the directors should be persons who would: (a) be able to keep abreast with these changes, and (b) provide continuous contribution and guidance to the board decision-making process.
- 2(2)(iv)** There should be a gradual infusion of new ideas into the board. There should also be assurance that the relationships between the directors amongst themselves as well as between the directors and the key management personnel is at a level that does not suggest the existence of excessive familiarity, undue influence or coercion. In this context, it should be noted that very long-standing relationships could sometimes impair the high sense of values, independence and objectivity that is needed in the discharge of the duties of a director of a bank.

2(3) Principle: Criteria to assess the Fitness and Propriety of Directors

- 2(3)(i)** In addition to the principles under the board's composition in Direction 2(2) above, directors should be fit and proper persons in order to be eligible to hold office as directors of a bank and no person should serve as a director unless such person is a fit and proper person.
- 2(3)(ii)** There is strong need for commitment and effective contribution to the prudent management of the affairs of the bank. It is very likely that the effectiveness of such commitment and contribution would tend to decrease with advanced age of directors and more particularly, if the age of such director is well beyond the normal age of retirement, as generally accepted in the country.

2(4) Principle: Management functions delegated by the Board

- 2(4)(i)** The board should have a formal schedule of matters specifically reserved to it for decision. The board should also give clear directions to key management personnel, as to the matters that should be approved by the board before decisions are made by key management personnel, on behalf of the bank.

2(5) Principle: The Chairman and the Chief Executive Officer

- 2(5)(i)** There are two key aspects of the management of every bank, viz., (a) the overall governance by the board, and (b) the day-to-day management of the bank's business by the CEO, in line with board approved strategic objectives, corporate values, overall risk policy and risk management procedures.
- 2(5)(ii)** There should be a clear division of these responsibilities at the board level and the executive management level to ensure a greater balance of power and authority, so that powers are not concentrated in any one individual.
- 2(5)(iii)** The board should appoint a chairman as well as a chief executive officer. The division of responsibilities between the chairman and chief executive officer should be clearly established and set out in writing.

2(6) Principle: Board appointed Committees

- 2(6)(i)** The board should appoint separate board committees for audit, selection, remuneration, integrated risk management and such other subjects as determined by the Board to ensure its oversight and control over the affairs of the bank.
- 2(6)(ii)** Where the board appoints a committee, it should set out the authority of the committee, and in particular, whether the committee has the authority to act on behalf of the board or simply has the authority to examine a particular issue and report back to the board with recommendations.
- 2(6)(iii)** Each committee should be chaired by a non-executive director who has some expertise in the relevant subject, and who preferably should be independent too. The majority of the members of the board committee should consist of non-executive directors with at least one independent director in the committee. If a need arises, professionals from outside may be invited or hired to serve in a committee. Bank staff may be present at the board committees for advice or special assignments, on invitation.

2(7) Principle: Related party transactions

- 2(7)(i)** The board should ensure that the bank does not engage in transactions with "related parties" in a manner that would grant such parties "more favourable treatment" than that accorded to other constituents of the bank carrying on the same business.

2(8) Principle: Disclosures

- 2(8)(i)** The objective of disclosure is the transparency of information relating to affairs and risk management of banks which would help to promote market discipline of the respective banks.
- 2(8)(ii)** Since market disclosure is the focus of the Pillar III of the risk management based capital standard known as Basel II recommended by the Basel Committee on Banking Supervision at the Bank for International Settlements, (which is the globally accepted body on introducing international standards on Bank Supervision), the extent of disclosures should be commensurate with the size, ownership structure, systemic importance, risk profile and the business model of the bank. Accordingly, it should be noted that the adequate and timely public disclosure of relevant information by banks would facilitate enhanced market discipline and lead to better and more effective corporate governance.

- 2(8)(iii)** Disclosures by banks should generally include disclosures relating to capital adequacy, key performance indicators, business concentrations, transactions with related parties, corporate governance statements, financial statements, etc., and should be consistent with accounting standards, regulatory requirements as well as with any other information disclosed on voluntary basis.
- 3. The following rules of Corporate Governance shall be complied by all licensed specialised banks in Sri Lanka and such compliance shall be as provided for in Direction 3(9)(i) hereof.**
- 3 (1) The Responsibilities of the Board**
- 3(1)(i)** The board shall strengthen the safety and soundness of the bank by ensuring the implementation of the following:
- a) Approve and oversee the bank's strategic objectives and corporate values and ensure that these are communicated throughout the bank;
 - b) Approve the overall business strategy of the bank, including the overall risk policy and risk management procedures and mechanisms with measurable goals, for at least the next three years;
 - c) Identify the principal risks and ensure implementation of appropriate systems to manage the risks prudently;
 - d) Approve implementation of a policy of communication with all stakeholders, including depositors, creditors, share-holders and borrowers;
 - e) Review the adequacy and the integrity of the bank's internal control systems and management information systems;
 - f) Identify and designate key management personnel, as defined in the International Accounting Standards, who are in a position to: (i) significantly influence policy; (ii) direct activities; and (iii) exercise control over business activities, operations and risk management;
 - g) Define the areas of authority and key responsibilities for the board directors themselves and for the key management personnel;
 - h) Ensure that there is appropriate oversight of the affairs of the bank by key management personnel, that is consistent with board policy;
 - i) Periodically assess the effectiveness of the board directors' own governance practices, including: (i) the selection, nomination and election of directors and key management personnel; (ii) the management of conflicts of interests; and (iii) the determination of weaknesses and implementation of changes where necessary;
 - j) Ensure that the bank has an appropriate succession plan for key management personnel;
 - k) Meet regularly, on a needs basis, with the key management personnel to review policies, establish communication lines and monitor progress towards corporate objectives;
 - l) Understand the regulatory environment and ensure that the bank maintains an effective relationship with regulators;
 - m) Exercise due diligence in the hiring and oversight of external auditors.
- 3(1)(ii)** The board shall appoint the chairman and the chief executive officer and define and approve the functions and responsibilities of the chairman and the chief executive officer in line with Direction 3(5) of these Directions.
- 3(1)(iii)** The board shall meet regularly and board meetings shall be held at least twelve times a year at approximately monthly intervals. Such regular board meetings shall normally involve active participation in person of a majority of directors entitled to be present. Obtaining the board's consent through the circulation of written resolutions/papers shall be avoided as far as possible.
- 3(1)(iv)** The board shall ensure that arrangements are in place to enable all directors to include matters and proposals in the agenda for regular board meetings, where such matters and proposals relate to the promotion of business and the management of risks of the bank.
- 3(1)(v)** The board procedures shall ensure that notice of at least 7 days is given of a regular board meeting to provide all directors an opportunity to attend. For all other board meetings, reasonable notice may be given.

- 3(1)(vi)** The board procedures shall ensure that a director who has not attended at least two-thirds of the meetings in the period of 12 months immediately preceding or has not attended the immediately preceding three consecutive meetings held, shall cease to be a director. Participation at the directors' meetings through an alternate director shall, however, be acceptable as attendance.
- 3(1)(vii)** The board shall appoint a company secretary who satisfies the provisions of Section 43 read with Section 76H of the Banking Act No. 30 of 1988, whose primary responsibilities shall be to handle the secretariat services to the board and shareholder meetings and to carry out other functions specified in the statutes and other regulations.
- 3(1)(viii)** All directors shall have access to advice and services of the company secretary with a view to ensuring that board procedures and all applicable rules and regulations are followed.
- 3(1)(ix)** The company secretary shall maintain the minutes of board meetings and such minutes shall be open for inspection at any reasonable time, on reasonable notice by any director.
- 3(1)(x)** Minutes of board meetings shall be recorded in sufficient detail so that it is possible to gather from the minutes, as to whether the board acted with due care and prudence in performing its duties. The minutes shall also serve as a reference for regulatory and supervisory authorities to assess the depth of deliberations at the board meetings. Therefore, the minutes of a board meeting shall clearly contain or refer to the following: (a) a summary of data and information used by the board in its deliberations; (b) the matters considered by the board; (c) the fact-finding discussions and the issues of contention or dissent which may illustrate whether the board was carrying out its duties with due care and prudence; (d) the testimonies and confirmations of relevant executives which indicate compliance with the board's strategies and policies and adherence to relevant laws and regulations; (e) the board's knowledge and understanding of the risks to which the bank is exposed and an overview of the risk management measures adopted; and (f) the decisions and board resolutions.
- 3(1)(xi)** There shall be a procedure agreed by the board to enable directors, upon reasonable request, to seek independent professional advice in appropriate circumstances, at the bank's expense. The board shall resolve to provide separate independent professional advice to directors to assist the relevant director or directors to discharge his/her/their duties to the bank.
- 3(1)(xii)** Directors shall avoid conflicts of interests, or the appearance of conflicts of interest, in their activities with, and commitments to, other organisations or related parties. If a director has a conflict of interest in a matter to be considered by the board, which the board has determined to be material, the matter should be dealt with at a board meeting, where independent non-executive directors [refer to Direction 3(2)(iv) of these Directions] who have no material interest in the transaction, are present. Further, a director shall abstain from voting on any board resolution in relation to which he/she or any of his/her close relation or a concern in which a director has substantial interest, is interested and he/she shall not be counted in the quorum for the relevant agenda item at the board meeting.
- 3(1)(xiii)** The board shall have a formal schedule of matters specifically reserved to it for decision to ensure that the direction and control of the bank is firmly under its authority.
- 3(1)(xiv)** The board shall, if it considers that the bank is, or is likely to be, unable to meet its obligations or is about to become insolvent or is about to suspend payments due to depositors and other creditors, forthwith inform the Director of Bank Supervision of the situation of the bank prior to taking any decision or action.
- 3(1)(xv)** The board shall ensure that the bank is capitalised at levels as required by the Monetary Board in terms of the capital adequacy ratio and other prudential grounds.
- 3(1)(xvi)** The board shall publish in the bank's Annual Report, an annual corporate governance report setting out the compliance with Direction 3 of these Directions.
- 3(1)(xvii)** The board shall adopt a scheme of self-assessment to be undertaken by each director annually, and maintain records of such assessments.
- 3(2) The Board's Composition**
- 3(2)(i)** The number of directors on the board shall not be less than 7 and not more than 13.
- 3(2)(ii)** (A) 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, and such period in office shall be inclusive of the total period of service served by such director up to January 1, 2008.

(B) In this context, the following transitional provisions shall apply:

- a) In the event that there is only one director on the board who has served more than nine years as at January 1, 2008, he/she shall be deemed to have vacated the office as a director as at December 31, 2008.
- b) In the event that there are two or more directors on the board who have served more than nine years as at January 1, 2008, the following provisions shall apply:
 - I. Of those directors whose period of service has exceeded nine years, the longest serving director, shall be deemed to have vacated office as a Director on December 31, 2008.
 - II. Thereafter, at the end of each succeeding year, the remaining directors shall be deemed to have vacated office in sequence, at least one director each year, (on the basis of the longest to the shortest length of service as a director), until all directors who have served a period in excess of nine years as at January 1, 2008, have been deemed to have vacated office. Provided also, that all directors of the bank who have served more than nine years as at January 1, 2008 shall be deemed to have vacated their office by or before December 31, 2011.
- c) In the event there are any directors who are due to complete nine years of service between January 1, 2008 and December 31, 2010, such directors shall also be deemed to have vacated office, in sequence, at least one director each year, (on the basis of the longest to the shortest length of service as a director), after the directors as set out in Direction 3(2)(ii)(B) (b) have vacated their office as directors. Provided, however, that all such directors covered by this sub-direction (c) shall also be deemed to have vacated their office by or before December 31, 2011.

3(2)(iii) An employee of a bank may be appointed, elected or nominated as a director of the bank (hereinafter referred to as an “executive director”) provided that the number of executive directors shall not exceed one-third of the number of directors of the board. In such an event, one of the executive directors shall be the chief executive officer of the bank.

3(2)(iv) The board shall have at least three independent non-executive directors or one third of the total number of directors, whichever is higher. This sub-direction shall be applicable from January 1, 2010 onwards.

A non-executive director shall not be considered independent if he/she:

- a) has direct and indirect shareholdings of more than 1% of the bank;
- b) currently has or had during the period of two years immediately preceding his/her appointment as director, any business transactions with the bank as described in Direction 3 (7) hereof, exceeding 10% of the regulatory capital of the bank.
- c) has been employed by the bank during the two year period immediately preceding the appointment as director;
- d) has a close relation who is a director or chief executive officer or a member of key management personnel or a material shareholder of the bank or another bank. For this purpose, a “close relation” shall mean the spouse or a financially dependant child;
- e) represents a specific stakeholder of the bank;
- f) is an employee or a director or a material shareholder in a company or business organization:

I. which currently has a transaction with the bank as defined in Direction 3(7) of these Directions, exceeding 10% of the regulatory capital of the bank, or

II. in which any of the other directors of the bank are employed or are directors or are material shareholders; or

III. in which any of the other directors of the bank have a transaction as defined in Direction 3(7) of these Directions, exceeding 10% of regulatory capital in the bank;

3(2)(v) In the event an alternate director is appointed to represent an independent director, the person so appointed shall also meet the criteria that applies to the independent director.

- 3(2)(vi)** Non-executive directors shall be persons with credible track records and/or have necessary skills and experience to bring an independent judgment to bear on issues of strategy, performance and resources.
- (2)(vii)** A meeting of the board shall not be duly constituted, although the number of directors required to constitute the quorum at such meeting is present, unless more than one half of the number of directors present at such meeting are non-executive directors. This sub-direction shall be applicable from January 1, 2010 onwards.
- 3(2)(viii)** The independent non-executive directors shall be expressly identified as such in all corporate communications that disclose the names of directors of the bank. The bank shall disclose the composition of the board, by category of directors, including the names of the chairman, executive directors, non-executive directors and independent non-executive directors in the annual corporate governance report.
- 3(2)(ix)** There shall be a formal, considered and transparent procedure for the appointment of new directors to the board. There shall also be procedures in place for the orderly succession of appointments to the board.
- 3(2)(x)** All directors appointed to fill a casual vacancy shall be subject to election by shareholders at the first general meeting after their appointment.
- 3(2)(xi)** If a director resigns or is removed from office, the board shall: (a) announce the director's resignation or removal and the reasons for such removal or resignation including but not limited to information relating to the relevant director's disagreement with the bank, if any; and (b) issue a statement confirming whether or not there are any matters that need to be brought to the attention of shareholders.
- 3(2)(xii)** A director or an employee of a bank shall not be appointed, elected or nominated as a director of another bank except where such bank is a subsidiary company or an associate company of the first mentioned bank.
- 3(3) Criteria to assess the fitness and propriety of directors**
In addition to provisions of Section 42 read with Section 76H of the Banking Act No. 30 of 1988, the criteria set out below shall apply to determine the fitness and propriety of a person who serves or wishes to serve as a director of a bank. Non-compliance with any one of the criteria as set out herein shall disqualify a person to be appointed, elected or nominated as a director or to continue as a director.
- 3(3)(i)** The age of a person who serves as director shall not exceed 70 years.
- (A) Where a director who is currently serving at a bank is over 70 years of age as at January 1, 2008, the following transitional provisions shall apply, subject, however, to the provisions as set out in Direction 3(2)(ii) hereof.
- a) If a director is over 75 years of age as at January 1, 2008, such director may continue to serve as a director for a further period that shall not extend beyond December 31, 2008, and shall be deemed to have vacated office on December 31, 2008;
- b) If a director is between 70 and 75 years of age as at January 1, 2008, such director may continue to serve as a director for a further period that shall not extend beyond December 31, 2009, and shall be deemed to have vacated office on December 31, 2009.
- (B) Where a director who is currently serving at a bank reaches the age of 70 years, between January 1, 2008 and December 31, 2009, such director may, subject to the provisions as set out in Direction 3(2)(ii) hereof, continue to serve as a director for a further period that shall not extend beyond December 31, 2010 and shall be deemed to have vacated office on December 31, 2010.
- 3(3)(ii)** A person shall not hold office as a director of more than 20 companies/entities/institutions inclusive of subsidiaries or associate companies of the bank. Of such 20 companies/entities/ institutions, not more than 10 companies shall be those classified as Specified Business Entities in terms of the Sri Lanka Accounting and Auditing Standards Act No. 15 of 1995.
- 3(4) Management functions delegated by the Board**
- 3(4)(i)** The directors shall carefully study and clearly understand the delegation arrangements in place.
- 3(4)(ii)** The board shall not delegate any matters to a board committee, chief executive officer, executive directors or key management personnel, to an extent that such delegation would significantly hinder or reduce the ability of the board as a whole to discharge its functions.

3(4)(iii) The board shall review the delegation processes in place on a periodic basis to ensure that they remain relevant to the needs of the bank.

3(5) The Chairman and Chief Executive Officer

3(5)(i) The roles of chairman and chief executive officer shall be separate and shall not be performed by the same individual.

3(5)(ii) The chairman shall be a non-executive director and preferably an independent director as well. In the case where the chairman is not an independent director, the board shall designate an independent director as the Senior Director with suitably documented terms of reference to ensure a greater independent element. The designation of the Senior Director shall be disclosed in the bank's Annual Report.

3(5)(iii) The board shall disclose in its corporate governance report, which shall be an integral part of its Annual Report, the identity of the chairman and the chief executive officer and the nature of any relationship [including financial, business, family or other material/relevant relationship(s)], if any, between the chairman and the chief executive officer and the relationships among members of the board.

3(5)(iv) The chairman shall: (a) provide leadership to the board; (b) ensure that the board works effectively and discharges its responsibilities; and (c) ensure that all key and appropriate issues are discussed by the board in a timely manner.

3(5)(v) The chairman shall be primarily responsible for drawing up and approving the agenda for each board meeting, taking into account where appropriate, any matters proposed by the other directors for inclusion in the agenda. The chairman may delegate the drawing up of the agenda to the company secretary.

3(5)(vi) The chairman shall ensure that all directors are properly briefed on issues arising at board meetings and also ensure that directors receive adequate information in a timely manner.

3(5)(vii) The chairman shall encourage all directors to make a full and active contribution to the board's affairs and take the lead to ensure that the board acts in the best interests of the bank.

3(5)(viii) The chairman shall facilitate the effective contribution of non-executive directors in particular and ensure constructive relations between executive and non-executive directors.

3(5)(ix) The chairman, shall not engage in activities involving direct supervision of key management personnel or any other executive duties whatsoever.

3(5)(x) The chairman shall ensure that appropriate steps are taken to maintain effective communication with shareholders and that the views of shareholders are communicated to the board.

3(5)(xi) The chief executive officer shall function as the apex executive-in-charge of the day-to-day-management of the bank's operations and business.

3(6) Board appointed Committees

3(6)(i) Each bank shall have at least four board committees as set out in Directions 3(6)(ii), 3(6)(iii), 3(6)(iv) and 3(6)(v) of these Directions. Each committee shall report directly to the board. All committees shall appoint a secretary to arrange the meetings and maintain minutes, records, etc., under the supervision of the chairman of the committee. The board shall present a report of the performance on each committee, on their duties and roles at the annual general meeting.

3(6)(ii) The following rules shall apply in relation to the Audit Committee:

- a) The chairman of the committee shall be an independent non-executive director who possesses qualifications and experience in accountancy and/or audit.
- b) All members of the committee shall be non-executive directors.
- c) The committee shall make recommendations on matters in connection with: (i) the appointment of the external auditor for audit services to be provided in compliance with the relevant statutes; (ii) the implementation of the Central Bank guidelines issued to auditors from time to time; (iii) the application of the relevant accounting standards; and (iv) the service period, audit fee and any resignation or dismissal of the auditor; provided that the engagement of the Audit partner shall not exceed five years, and that the particular Audit partner is not re-engaged for the audit before the expiry of three years from the date of

the completion of the previous term.

- d) The committee shall review and monitor the external auditor's independence and objectivity and the effectiveness of the audit processes in accordance with applicable standards and best practices.
- e) The committee shall develop and implement a policy on the engagement of an external auditor to provide non-audit services that are permitted under the relevant statutes, regulations, requirements and guidelines. In doing so, the committee shall ensure that the provision by an external auditor of non-audit services does not impair the external auditor's independence or objectivity. When assessing the external auditor's independence or objectivity in relation to the provision of non-audit services, the committee shall consider:
 - I. whether the skills and experience of the audit firm make it a suitable provider of the non-audit services;
 - II. whether there are safeguards in place to ensure that there is no threat to the objectivity and/or independence in the conduct of the audit resulting from the provision of such services by the external auditor; and
 - III. whether the nature of the non-audit services, the related fee levels and the fee levels individually and in aggregate relative to the audit firm, pose any threat to the objectivity and/or independence of the external auditor.
- f) The committee shall, before the audit commences, discuss and finalise with the external auditors the nature and scope of the audit, including: (i) an assessment of the bank's compliance with the relevant Directions in relation to corporate governance and the management's internal controls over financial reporting; (ii) the preparation of financial statements for external purposes in accordance with relevant accounting principles and reporting obligations; and (iii) the co-ordination between firms where more than one audit firm is involved.
- g) The committee shall review the financial information of the bank, in order to monitor the integrity of the financial statements of the bank, its annual report, accounts and quarterly reports prepared for disclosure, and the significant financial reporting judgments contained therein. In reviewing the bank's annual report and accounts and quarterly reports before submission to the board, the committee shall focus particularly on: (i) major judgmental areas; (ii) any changes in accounting policies and practices; (iii) significant adjustments arising from the audit; (iv) the going concern assumption; and (v) the compliance with relevant accounting standards and other legal requirements.
- h) The committee shall discuss issues, problems and reservations arising from the interim and final audits, and any matters the auditor may wish to discuss including those matters that may need to be discussed in the absence of key management personnel, if necessary.
- i) The committee shall review the external auditor's management letter and the management's response thereto.
- j) The committee shall take the following steps with regard to the internal audit function of the bank:
 - I. Review the adequacy of the scope, functions and resources of the internal audit department, and satisfy itself that the department has the necessary authority to carry out its work;
 - II. Review the internal audit programme and results of the internal audit process and, where necessary, ensure that appropriate actions are taken on the recommendations of the internal audit department;
 - III. Review any appraisal or assessment of the performance of the head and senior staff members of the internal audit department;
 - IV. Recommend any appointment or termination of the head, senior staff members and outsourced service providers to the internal audit function;
 - V. Ensure that the committee is apprised of resignations of senior staff members of the internal audit department including the chief internal auditor and any outsourced service providers, and to provide an opportunity to the resigning senior staff members and outsourced service providers to submit reasons for resigning;

VI. Ensure that the internal audit function is independent of the activities it audits and that it is performed with impartiality, proficiency and due professional care;

- k) The committee shall consider the major findings of internal investigations and management's responses thereto;
- l) The chief finance officer, the chief internal auditor and a representative of the external auditors may normally attend meetings. Other board members and the chief executive officer may also attend meetings upon the invitation of the committee. However, at least twice a year, the committee shall meet with the external auditors without the executive directors being present.
- m) The committee shall have: (i) explicit authority to investigate into any matter within its terms of reference; (ii) the resources which it needs to do so; (iii) full access to information; and (iv) authority to obtain external professional advice and to invite outsiders with relevant experience to attend, if necessary.
- n) The committee shall meet regularly, with due notice of issues to be discussed and shall record its conclusions in discharging its duties and responsibilities.
- o) The board shall disclose in an informative way, (i) details of the activities of the audit committee; (ii) the number of audit committee meetings held in the year; and (iii) details of attendance of each individual director at such meetings.
- p) The secretary of the committee (who may be the company secretary or the head of the internal audit function) shall record and keep detailed minutes of the committee meetings.
- q) The committee shall review arrangements by which employees of the bank may, in confidence, raise concerns about possible improprieties in financial reporting, internal control or other matters. Accordingly, the committee shall ensure that proper arrangements are in place for the fair and independent investigation of such matters and for appropriate follow-up action and to act as the key representative body for overseeing the bank's relations with the external auditor.

3(6)(iii) The following rules shall apply in relation to the Human Resources and Remuneration Committee:

- a) The committee shall determine the remuneration policy (salaries, allowances and other financial payments) relating to directors, Chief Executive Officer (CEO) and key management personnel of the bank.
- b) The committee shall set goals and targets for the directors, CEO and the key management personnel.
- c) The committee shall evaluate the performance of the CEO and key management personnel against the set targets and goals periodically and determine the basis for revising remuneration, benefits and other payments of performance-based incentives.
- d) The CEO shall be present at all meetings of the committee, except when matters relating to the CEO are being discussed.

3(6)(iv) The following rules shall apply in relation to the Nomination Committee:

- a) The committee shall implement a procedure to select/appoint new directors, CEO and key management personnel.
- b) The committee shall consider and recommend (or not recommend) the re-election of current directors, taking into account the performance and contribution made by the director concerned towards the overall discharge of the board's responsibilities.
- c) The committee shall set the criteria such as qualifications, experience and key attributes required for eligibility to be considered for appointment or promotion to the post of CEO and the key management positions.
- d) The committee shall ensure that directors, CEO and key management personnel are fit and proper persons to hold office as specified in the criteria given in Direction 3(3) and as set out in the Statutes.
- e) The committee shall consider and recommend from time to time, the requirements of additional/new expertise and the succession arrangements for retiring directors and key management personnel.
- f) The Committee shall be chaired by an Independent Director and preferably be constituted with a majority of Independent Directors. The CEO may be present at meetings by invitation.

3(6)(v) The following rules shall apply in relation to the Integrated Risk Management Committee:

- a) The committee shall consist of at least three non-executive directors, chief executive officer and key management personnel supervising broad risk categories, i.e., credit, market, liquidity, operational and strategic risks. The committee shall work with key management personnel very closely and make decisions on behalf of the board within the framework of the authority and responsibility assigned to the committee.
- b) The committee shall assess all risks, i.e., credit, market, liquidity, operational and strategic risks to the bank on a monthly basis through appropriate risk indicators and management information. In the case of subsidiary companies and associate companies, risk management shall be done, both on a bank basis and group basis.
- c) The committee shall review the adequacy and effectiveness of all management level committees such as the credit committee and the asset-liability committee to address specific risks and to manage those risks within quantitative and qualitative risk limits as specified by the committee.
- d) The committee shall take prompt corrective action to mitigate the effects of specific risks in the case such risks are at levels beyond the prudent levels decided by the committee on the basis of the bank's policies and regulatory and supervisory requirements.
- e) The committee shall meet at least quarterly to assess all aspects of risk management including updated business continuity plans.
- f) The committee shall take appropriate actions against the officers responsible for failure to identify specific risks and take prompt corrective actions as recommended by the committee, and/or as directed by the Director of Bank Supervision.
- g) The committee shall submit a risk assessment report within a week of each meeting to the board seeking the board's views, concurrence and/or specific directions.
- h) The committee shall establish a compliance function to assess the bank's compliance with laws, regulations, regulatory guidelines, internal controls and approved policies on all areas of business operations. A dedicated compliance officer selected from key management personnel shall carry out the compliance function and report to the committee periodically.

3 (7) Related party transactions**3(7)(i)** The board shall take the necessary steps to avoid any conflicts of interest that may arise from any transaction of the bank with any person, and particularly with the following categories of persons who shall be considered as "related parties" for the purposes of this Direction:

- a) Any of the bank's subsidiary companies;
- b) Any of the bank's associate companies;
- c) Any of the directors of the bank;
- d) Any of the bank's key management personnel;
- e) A close relation of any of the bank's directors or key management personnel;
- f) A shareholder owning a material interest in the bank;
- g) A concern in which any of the bank's directors or a close relation of any of the bank's directors or any of its material shareholders has a substantial interest.

3(7)(ii) The type of transactions with related parties that shall be covered by this Direction shall include the following:

- a) The grant of any type of accommodation, as defined in the Monetary Board's Directions on maximum amount of accommodation,
- b) The creation of any liabilities of the bank in the form of deposits, borrowings and investments,
- c) The provision of any services of a financial or non-financial nature provided to the bank or received from the bank,
- d) The creation or maintenance of reporting lines and information flows between the bank and any related parties which may lead to the sharing of potentially proprietary, confidential or otherwise sensitive information that may give benefits to such related parties.

- 3(7)(iii)** The board shall ensure that the bank does not engage in transactions with related parties as defined in Direction 3(7)(i) above, in a manner that would grant such parties “more favourable treatment” than that accorded to other constituents of the bank carrying on the same business. In this context, “more favourable treatment” shall mean and include treatment, including the:
- a) Granting of “total net accommodation” to related parties, exceeding a prudent percentage of the bank’s regulatory capital, as determined by the board. For purposes of this sub-direction:
 - I. “Accommodation” shall mean accommodation as defined in the Banking Act Directions No. 8 of 2007 on Maximum Amount of Accommodation.
 - II. The “total net accommodation shall be” computed by deducting from the total accommodation, the cash collateral and investments made by such related parties in the bank’s share capital and debt instruments with a maturity of 5 years or more.
 - b) Charging of a lower rate of interest than the bank’s best lending rate or paying more than the bank’s deposit rate for a comparable transaction with an unrelated comparable counterparty;
 - c) Providing of preferential treatment, such as favourable terms, covering trade losses and/or waiving fees/commissions, that extend beyond the terms granted in the normal course of business undertaken with unrelated parties;
 - d) Providing services to or receiving services from a related-party without an evaluation procedure;
 - e) Maintaining reporting lines and information flows that may lead to sharing potentially proprietary, confidential or otherwise sensitive information with related parties, except as required for the performance of legitimate duties and functions.
- 3(7)(iv)** A bank shall not grant any accommodation to any of its directors or to a close relation of such director unless such accommodation is sanctioned at a meeting of its board of directors, with not less than two-thirds of the number of directors other than the director concerned, voting in favour of such accommodation. This accommodation shall be secured by such security as may from time to time be determined by the Monetary Board as well.
- 3(7)(v)**
- (a) Where any accommodation has been granted by a bank to a person or a close relation of a person or to any concern in which the person has a substantial interest, and such person is subsequently appointed as a director of the bank, steps shall be taken by the bank to obtain the necessary security as may be approved for that purpose by the Monetary Board, within one year from the date of appointment of the person as a director.
 - (b) Where such security is not provided by the period as provided in Direction 3(7)(v)(a) above, the bank shall take steps to recover any amount due on account of any accommodation, together with interest, if any, within the period specified at the time of the grant of accommodation or at the expiry of a period of eighteen months from the date of appointment of such director, whichever is earlier.
 - (c) Any director who fails to comply with the above sub-directions shall be deemed to have vacated the office of director and the bank shall disclose such fact to the public.
 - (d) This sub-direction, however, shall not apply to a director who at the time of the grant of the accommodation was an employee of the bank and the accommodation was granted under a scheme applicable to all employees of such bank.
- 3(7)(vi)** A bank shall not grant any accommodation or “more favourable treatment” relating to the waiver of fees and/or commissions to any employee or a close relation of such employee or to any concern in which the employee or close relation has a substantial interest other than on the basis of a scheme applicable to the employees of such bank or when secured by security as may be approved by the Monetary Board in respect of accommodation granted as per Direction 3(7)(v) above.
- 3(7)(vii)** No accommodation granted by a bank under Direction 3(7)(v) and 3(7)(vi) above, nor any part of such accommodation, nor any interest due thereon shall be remitted without the prior approval of the Monetary Board and any remission without such approval shall be void and of no effect.

3 (8) Disclosures

- 3(8)(i)** The board shall ensure that: (a) annual audited financial statements and quarterly financial statements are prepared and published in accordance with the formats prescribed by the supervisory and regulatory authorities and applicable accounting standards, and that (b) such statements are published in the newspapers in an abridged form, in Sinhala, Tamil and English.
- 3(8)(ii)** The board shall ensure that the following minimum disclosures are made in the Annual Report:
- a) A statement to the effect that the annual audited financial statements have been prepared in line with applicable accounting standards and regulatory requirements, inclusive of specific disclosures.
 - b) A report by the board on the bank's internal control mechanism that confirms that the financial reporting system has been designed to provide reasonable assurance regarding the reliability of financial reporting, and that the preparation of financial statements for external purposes has been done in accordance with relevant accounting principles and regulatory requirements.
 - c) The external auditor's certification on the effectiveness of the internal control mechanism referred to in Direction 3(8)(ii)(b) above, in respect of any statements prepared or published after December 31, 2008.
 - d) Details of directors, including names, fitness and propriety, transactions with the bank and the total of fees/remuneration paid by the bank.
 - e) Total net accommodation as defined in 3(7)(iii) granted to each category of related parties. The net accommodation granted to each category of related parties shall also be disclosed as a percentage of the bank's regulatory capital.
 - f) The aggregate values of remuneration paid by the bank to its key management personnel and the aggregate values of the transactions of the bank with its key management personnel, set out by broad categories such as remuneration paid, accommodation granted and deposits or investments made in the bank.
 - g) The external auditor's certification of the compliance with these Directions in the annual corporate governance reports published after January 1, 2010.
 - h) A report setting out details of the compliance with prudential requirements, regulations, laws and internal controls and measures taken to rectify any material non-compliances.
 - i) A statement of the regulatory and supervisory concerns on lapses in the bank's risk management, or non compliance with these Directions that have been pointed out by the Director of Bank Supervision, if so directed by the Monetary Board to be disclosed to the public, together with the measures taken by the bank to address such concerns.

3(9) Transitional and other general provisions

- 3(9)(i)** Compliance with this Direction shall commence from January 1, 2008 onwards and all licensed specialised banks shall fully comply with the provisions of this Direction by or before January 1, 2009 except where extended compliance dates have been specifically provided for in this Direction.
- 3(9)(ii)** In respect of the banks that have been incorporated by specific statutes in Sri Lanka, the boards as specified in such statutes shall continue to function in terms of the provisions of the respective statutes, provided they take steps to comply with all provisions of this Direction that are not inconsistent with the provisions of the respective statutes.
- 3(9)(iii)** This Direction shall apply to the branches of the foreign banks operating in Sri Lanka to the extent that it is not inconsistent with the regulations and laws applicable in such bank's country of incorporation. The branch of a foreign bank shall also publish its parent bank's annual corporate governance report together with its annual report and accounts of the branch operations in Sri Lanka.
- 3(9)(iv)** In the event of a conflict between any of the provisions of this Direction and the Articles of Association (or Internal Rules) pertaining to any bank, the provisions of this Direction shall prevail. However, if the Articles of Association of an individual bank set a more stringent standard than that specified in this Direction, such provisions in the Articles of Association may be followed.

Bank Supervision Department
31 December 2007

Mr. S A Weerasinghe
General Manager
State Mortgage and Investment Bank
269, Galle Road
Colombo 3

Dear Sir

DIRECTION ON LIQUID ASSETS

With a view to strengthening the safety and soundness of the State Mortgage and Investment Bank (SMIB), the Monetary Board of the Central Bank of Sri Lanka has decided to revoke the separate Direction issued to SMIB on the maintenance of the Statutory Liquid Assets on 21 November 1997 under Sections 76 J (3) of the Banking Act and replace the same with the Direction issued to other Licensed Specialised Banks (LSBs), with effect from 1st January 2008. The applicable Direction issued under Section 76J (1) of the Banking Act is attached herewith.

The Monetary Board has also decided to grant time till 31 December 2008 to comply with the requirements contained in the new Directions. If SMIB is unable to comply with the newly applicable Direction, it shall comply with requirements contained in the relevant previous Direction until the expiration of the time granted to comply with the new Direction.

Yours faithfully
B D W A Silva
Actg. Director of Bank Supervision

Bank Supervision Department
31 December 2007

Mr. S H Piyasiri
General Manager
National Savings Bank
255, Galle Road
Colombo 3

Dear Sir

DIRECTIONS ISSUED TO NATIONAL SAVINGS BANK

Considering the structural change in the equity capital of the National Savings Bank (NSB) and with a view to strengthening the safety and soundness of NSB, the Monetary Board of the Central Bank of Sri Lanka has decided to revoke all separate Directions issued to NSB on 21 November 1997 under Sections 76 J (1) and 76 J (3) of the Banking Act and replace these Directions with the Directions issued to other licensed specialized banks (LSBs) under Section 76J (1) of the Banking Act, with effect from 1st January 2008.

2. The Directions that are to replace the existing Directions are given in the following table.

Separate Directions issued to NSB (Existing Directions)	Directions that are to replace the existing separate Directions
(i) Directions under Section 76J(3) — Capital Adequacy	(i) Directions under Section 76J(1) — Maintenance of Capital Adequacy Ratio (Banking Act Direction No. 10) issued on 26.12.2007 —Annex 1
(ii) Directions under Section 76J(1) — Reserve Fund	(ii) Directions under Section 76J(1) — Reserve Fund —Annex 2
(iii) Directions under Section 76J(3) — Liquid Assets	(iii) Directions under Section 76J(1) — Liquid Assets —Annex 3
(iv) Directions under Section 76J(1) — Investments in Equity	(iv) Directions under Section 76J(1) — Investments in Equity —Annex 4
(v) Directions under Section 76J(1) — Single Borrower Limit	(v) Directions under Section 76J(1) — Maximum Amount of Accommodation (Banking Act Direction No. 8) issued on 1.11.2007 —Annex 5
(vi) Directions under Section 76J(1) — Acquisition of Immovable Property	(vi) Directions under Section 76J(1) — Acquisition of Immovable Property —Annex 6

3. The Monetary Board has also decided to grant time till 31 December 2008 to comply with the requirements contained in the new Directions. In the event that NSB is unable to comply with any of the newly applicable Directions, it shall comply with the requirements contained in the relevant previous Directions, until the expiration of the time granted to comply with the new Directions.

Yours faithfully

B D W A Silva

Actg. Director of Bank Supervision

02/01/00/0002/001

Bank Supervision Department
31 December 2007

To: CEOs of All Licensed Banks

Dear Sirs/Madam

GUIDELINES FOR EMPLOYMENT OF EXPATRIATE STAFF IN BANKS

As announced at the meeting of the Chief Executive Officers of licensed banks on 22 November 2007, the Guidelines for employment of expatriate staff in banks, which have been developed to facilitate the introduction of new banking products and risk management of banks, are sent herewith.

Please acknowledge receipt of this Circular.

Yours faithfully,

B D W A Silva

Actg. Director of Bank Supervision

GUIDELINES FOR EMPLOYMENT OF EXPATRIATE STAFF IN BANKS

1 Current Policy

- 1.1 At present, the Central Bank of Sri Lanka (CBSL) recommends to Immigration and Emigration Department resident visas for expatriate staff of foreign banks to enable the banks to employ them as follows.
 - (i) Maximum of three officers without any restriction.
 - (ii) Permission for any officers exceeding 3 is granted on a case-by-case-basis for a specific period not exceeding one year subject to condition that local staff should be trained to handle the work initiated/undertaken by such expatriate officers.
- 1.2 The objective of developing this policy is to provide local staff with the training and opportunities to take on positions held by the expatriate officers.
- 1.3 In the case of local banks, there has not been such a policy since local banks generally do not employ foreign personnel. However, four local banks have employed foreign consultants to undertake specific assignments.

2 Need for a Revision of the Policy

The following factors are considered favourably to relax the current policy to permit more expatriate officers and to encourage domestic banks to employ foreign experts.

- (i) Expansion of business operations of some foreign banks.
- (ii) Foreign banks now tend to expand business in Sri Lanka, especially infrastructure projects, through funds borrowed from their respective head offices and branches.
- (iii) The active presence of foreign banks with internationally experienced professionals will help improve Sri Lanka's image and investment promotion internationally.
- (iv) Tendency to introduce international banking products such as securitization, loan syndication, foreign loan raising, infrastructure funding and derivative products.
- (v) Banks in Sri Lanka mainly depend on conventional deposit and loan products. Introduction of innovative banking products indicate the development of the financial sector and the economy. International banking know-how is necessary to introduce new banking products, especially to attract foreign capital to Sri Lanka.
- (vi) Banks will need to employ risk management specialists to implement advanced approaches of Basel II in the medium term and there may be a need to look for such specialists from countries which implement Basel II.
- (vii) The proposed adoption of IAS/IFRS also will require bankers who have practical experience in adopting IAS/IFRS.
- (viii) In general, banking industry needs experts who have global banking experience if Sri Lankan banks are to introduce modern banking products, technology and risk management techniques.

3 Policy Guidelines

3.1 For Foreign Banks

- (i) The maximum number of expatriate officers permitted will be as follows:
 - (a) 3 for banks whose staff strength is less than 75.
 - (b) 5 for banks with staff strength of 75 to 400.
 - (c) 10 for banks with staff strength of more than 400.
- (ii) In the case of Indian banks, agreement as per on-going negotiations of the Comprehensive Economic Partnership Agreement (CEPA) will be adopted as the minimum criteria.

- (iii) Approval for expatriate officers in excess of the above limits will be considered on a case-by-case-basis taking into consideration the specific skills of the nominated expatriates and specific assignments given to them. The banks should submit projections for specific business or deliverables expected from expatriate officers.
- (iv) Validity period of the approval will be two years for expatriates under the normal quota and one year for others (case-by-case-basis criteria).
- (v) In the case of expatriate officers under the normal quota except for CEO, approval may be renewed for another term of two years after assessing the performance of respective expatriate officer. For CEOs, approval may be extended for two terms (4 more years) on the basis of performance records. The renewal for the term of expatriates permitted in excess of the normal quota (case-by-case basis) will be considered only for extension of the projects/assignments or new projects/assignments.
- (vi) Approving authority for expatriate officers under normal quota will be the Director of Bank Supervision. The Deputy Governor will approve expatriate officers in excess of the normal quota.

3.2 For Locally Incorporated Banks

Permission will be granted on a case-by-case basis taking into consideration the specific needs of the banks. Special attention will be given to employment of foreign experts in the following fields:

- (a) Basel II-based risk management
- (b) International Accounting Standards
- (c) Risk modeling and data warehouse
- (d) Structuring of derivative products
- (e) Corporate governance

Circular No: 35/01/005/0006/12

Domestic Operations Department
11 January 2007

To: All Licensed Commercial Banks.

REVERSE REPURCHASE FACILITY

Further to our circular No. 35/01/005/0006/11 dated 26 December 2006 on the above subject informing non availability of Reverse Repurchase Facility (RRF) on days when there is a liquidity surplus in the commercial banking system.

Commercial banks are advised to seek assistance through the RRF, only as a last resort to address the urgent liquidity requirements, and find other means of meeting their liquidity issues. They are informed that with effect from 16 January 2007 any relief will be made available subject to the following conditions.

1. The RRF of the Central Bank will not be available on days when there is a liquidity surplus in the commercial banking system, as per the Central Bank estimates.
2. The RRF will be available to a particular bank, only
 - up to six times per calendar month until 31 March 2007, and
 - up to three times per calendar month thereafter.
3. The total amount of RRF available on a particular day would not exceed the amount of liquidity shortage of the commercial banking system on that particular day as estimated by the Central Bank.

Actg. Director
Domestic Operations Department

Circular No: 35/01/005/0010/06Domestic Operations Department
29 March 2007*To: All Licensed Commercial Banks.***MARGIN REQUIREMENTS AGAINST LETTERS OF CREDIT**

All licensed commercial banks are hereby informed that the margin deposit requirement of 50 per cent of the invoice value at the time of opening Letters of Credit for the importation of the items specified in Schedule A1 (attached), imposed by our circular No 35/01/005/0010/05 dated 18 October 2006, is withdrawn with effect from 30 March 2007.

Actg. Director/Domestic Operations
Authorised Signatory of the Monetary Board
of the Central Bank of Sri Lanka**Circular No. 35/01/005/0006/13**Domestic Operations Department
23 August 2007*To: All Licensed Commercial Banks and Primary Dealers.***REVERSE REPURCHASE FACILITY**

The Central Bank will adopt the following procedures in granting Reverse Repurchase Facility (RRF) at the CBSL policy rate and allocating the amount offered under RRF among Participating Institutions (PIs i.e. Commercial Banks and Primary Dealers), with effect from 23.08.2007 until further notice. Item 5,6,7,8,9,10,11 and 12 of the Section C (b) of our Circular No. 35/01/005/006/04 dated 27.01.2004 will be applicable with regard to the settlement of the RRF. (A copy of our Circular attached for easy reference).

1. The RRF will not be available on the days when there is a liquidity surplus as per the CBSL estimates.
2. When there is a liquidity shortage as per the CBSL estimates, RRF will be available to cover the full amount of the shortage in the system.
3. DOD will announce on electronic bidding system the total amount of RRF available under standing facility at or before 0930 hours on days in which there is a shortfall in the market.
4. PIs who wish to use the facility are required to inform their requirements to the OMO Division of the Domestic Operations Department by telephone or fax message before 1030 hours.
5. The DOD will allocate the total amount offered on the basis of amount requested by each PI. If the total amount requested is higher than the total amount offered, an allocation will be made on a pro rata basis.
6. The results will be informed to each PI by telephone or fax on or before 1100 hours.
7. PIs, are requested to submit the amount accepted, details of the scripless securities through the facility available in the on-line electronic bidding system (standing facility) before 1200 hours.
8. RRF will be available for a participant subject to the following conditions -
 - a. The facility is available only as the last resort to address an urgent liquidity requirement of the particular participant.
 - b. Participants seeking the facility should not be a lender in the money market on the same day, and
 - c. Funds borrowed under RRF should not be used to build up excess reserves in the reserve account of commercial banks with the CBSL, on that particular day.

Director
Domestic Operations Department

Circular No. 35/01/005/0006/14Domestic Operations Department
21 November 2007*To: All Licensed Commercial Banks and Primary Dealers.***REVERSE REPURCHASE FACILITY**

The Central Bank of Sri Lanka (CBSL) will adopt the following procedures in granting Reverse Repurchase Facility (RRF) and allocating the amount offered under RRF among Participating Institutions (PIs i.e. Commercial Banks and Primary Dealers), from **03 December 2007**. Item 5,6,7,8,9,10,11 and 12 of the Section C (b) of our Circular No. 35/01/005/006/04 dated 27 January 2004 will be applicable with regard to the settlement of the RRF. (A copy of our Circular attached for easy reference).

1. The RRF will not be available on the days when there is a liquidity surplus as per the CBSL estimates.
2. When there is a liquidity shortage as per the CBSL estimates, RRF will be available to cover the full amount of the shortage in the system.
3. Domestic Operations Department (DOD) will announce on electronic bidding system the total amount of RRF available under standing facility at or before 0930 hours on days in which there is a shortfall in the market.
4. PIs who wish to use the facility are required to inform their requirements to the Open Market Operations (OMO) Division of the DOD by telephone or fax message before 1030 hours.
5. The DOD will allocate the total amount offered on the basis of amount requested by each PI. If the total amount requested is higher than the total amount offered, an allocation will be made on a pro rata basis.
6. The results will be informed to each PI by telephone or fax at or before 1100 hours.
7. PIs are requested to submit the amount accepted and details of the scripless securities through the facility available in the on-line electronic bidding system (standing facility) before 1200 hours.
8. RRF will be available for a participant subject to the following conditions -
 - a. The RRF will be available to a particular PI only up to four (4) times per calendar month at the prevailing Central Bank Reverse Repo Rate. Any borrowings of more than 4 times by a particular PI during a calendar month will be provided at a penalty rate of 19 per cent per annum. Such penalty rate will be applicable until 31 January 2008.
 - b. The penalty rate will be subject to review from time to time and may be changed in accordance with prevailing monetary conditions.
 - c. The RRF is available only as the last resort to address an urgent liquidity requirement of the particular participant.
 - d. Participants seeking the facility on a particular day should not be a net lender in the money market on the same day, and
 - e. Funds borrowed under RRF should not be used to build up excess reserves in the reserve account of a commercial bank with the CBSL on that particular day.

Director
Domestic Operations Department**Ref: 06/04/01/2007**

Department of Exchange Control
Central Bank of Sri Lanka
P O Box 590
Colombo 1
08 January 2007

*Operating Instructions to Authorized Dealers***FOREIGN CURRENCY FIXED DEPOSIT ACCOUNTS FOR DUAL
CITIZENSHIP APPLICANTS**

The Government of Sri Lanka has decided to introduce a foreign currency fixed deposit scheme for ex-Sri Lankans/ Sri Lankans living abroad who would apply for dual citizenship status. Under this scheme, a family unit or an individual is exempted from payment of any fee charged on granting dual citizenship, if the principal applicant makes a fixed deposit of US\$ 50,000 with an Authorized Dealer for a minimum period of 3 years; while a fee of Rs.200,000 is charged per family unit or an individual applicant if the principal applicant makes a fixed deposit of US\$ 25,000 with an Authorized Dealer for a minimum period of 3 years.

2. For the purpose of accepting such foreign currency deposits, Authorized Dealers are hereby permitted to open fixed deposit accounts in favour of dual citizenship applicants in their domestic banking units.
3. These accounts may be opened with minimum deposits of either US\$ 50,000 or US\$ 25,000 (or equivalent in any other convertible foreign currency) on production of a letter issued by the Controller of Immigration and Emigration recommending that a foreign currency deposit account be opened in the name of the principal applicant for dual citizenship.
4. Operation of these accounts shall be subjected to the following conditions:
 - a. **Credits**
 - i. Inward remittances in convertible foreign currency received through Authorized Dealers or foreign currency brought into the country and tendered by the account holder during his temporary visit to Sri Lanka.
 - ii. Funds transferred from existing Non-Resident Foreign Currency (NRFC) account of the account holder.
 - iii. Interest paid in foreign currency on funds held in the account.
 - b. **Debits**
 - i. Interest accrued on the deposits
5. Interest accrued on the deposits may be freely remittable, transferred to NRFC account of the account holder or converted into Sri Lanka Rupees for the account holder's local expenses.
6. Withdrawals of the deposit or any part thereof should not be permitted before the maturity period of the deposit without obtaining prior permission from the Controller of Exchange.
7. **Reporting Requirement**
Authorized Dealers are required to furnish to the 'D' Branch of the Exchange Control Department and copy to the Controller of Immigration & Emigration, the following information in respect of each foreign currency fixed deposit account opened under the scheme within a week of opening the account:
 - (a) Date of opening of the account and the name and address of the account holder; and
 - (b) Amount of funds deposited and the date of maturity of the deposit.

Controller of Exchange

The Gazette of the Democratic Socialist Republic of Sri Lanka
EXTRAORDINARY
No.1481/1 – MONDAY, JANUARY 22, 2007
(Published by Authority)
PART I: SECTION (I) – GENERAL
Central Bank of Sri Lanka Notices

NOTICE UNDER THE EXCHANGE CONTROL ACT (CHAPTER 423 OF THE CLE)
Permission in Terms of Sections 7, 10, 11 and 15 of the Exchange Control Act

1. PERMISSION is hereby granted for the purposes of Sections 7, 10, 11 and 15 as applicable of the Exchange Control Act (Chapter 423 of the CLE) to foreign country funds, regional funds or mutual funds approved by the Securities and Exchange Commission of Sri Lanka, corporate bodies incorporated outside Sri Lanka and citizens of foreign states for purchasing, transferring and making payments in respect of transactions of Sri Lanka Rupee Denominated Treasury Bonds (T-bonds) subject to the conditions hereinafter set out.
2. *Conditions.-*
 - (a) Any T-Bonds to be purchased by the above categories of foreign investors should be through the primary and secondary markets by utilizing existing public debt system. Foreign investor who purchased such a T- bond is in a position to sell or transfer this T- bond to any person, whether a resident in Sri Lanka or a resident outside Sri Lanka, in the secondary market without any holding period.
 - (b) The payment for T-bonds issued by the Government of Sri Lanka in any issue or transaction permitted hereunder shall be made only out of or into a "Treasury bond Investment External Rupee Account" (TIERA) opened in a commercial bank in Sri Lanka in the name of the foreign investor.
 - (c) A commercial bank, or a licensed primary dealer or a broker or any other person entrusted with the payment of capital monies such a sale proceeds of T-bonds and interest on such T- bonds in respect of any transaction permitted hereunder shall make such payment only into or out of a Treasury Bond Investment External Rupee Account referred to in sub-paragraph (b) above.
 - (d) Funds in a TIERA is freely remittable without any restriction after meeting local liabilities of the account holder, if any.

Interpretation : For purpose of this general permission;

“foreign investors” shall include the following categories of investors:

- (a) Foreign country funds, regional funds or mutual funds approved by the Securities and Exchange Commission of Sri Lanka;
- (b) Corporate bodies incorporated outside Sri Lanka; and
- (c) Citizens of foreign states.

D.WASANTHA,
Controller of Exchange

Colombo,
22nd January, 2007

Ref: 06/04/03/2007

Department of Exchange Control
Central Bank of Sri Lanka
P.O. Box 590
Colombo 1
22 January 2007

Operating Instructions to Authorized Dealers

Dear Sirs,

**INVESTMENT IN RUPEE DENOMINATED TREASURY BONDS BY
FOREIGN INVESTORS**

The Government has decided to permit foreign country funds, regional funds or mutual funds approved by the Securities and Exchange Commission of Sri Lanka, corporate bodies incorporated outside Sri Lanka and citizens of foreign states to purchase and hold Rupee Denominated Treasury Bonds (T-bonds) not exceeding 5% of the total value of T-bonds outstanding at any given point of time. Therefore, the above categories of foreign investors are permitted to purchase, hold and transfer T-bonds through both primary and secondary markets utilizing existing public debt system. Foreign investor who purchased such a T-bond is in a position to sell or transfer this T-bond to any person, whether a resident in Sri Lanka or a resident outside Sri Lanka, in the secondary market without any holding period.

2. In order to give effect to this decision, general permission has been granted by me in a notice published in the Gazette Extraordinary No. 1481/1 of 22.01.2007.
3. Accordingly, Authorized Dealers are hereby permitted to open and operate Treasury Bond Investment External Rupee Accounts (TIERA) in the names of following categories of foreign investors,
 - (a) Foreign country funds, regional funds or mutual funds approved by the Securities and Exchange Commission of Sri Lanka;
 - (b) Corporate bodies incorporated outside Sri Lanka; and
 - (c) Citizens of foreign states

subject to the following guidelines for the purpose of facilitating their investments in T-bonds.

- I) Credits and debits to the account should be confined to the following:

Credits:

- i) Inward remittances of the foreign investor and/or transfers from Share Investment External Rupee Account (SIERA) opened by foreign investor for investment in shares.
- ii) Sale proceeds of T-bonds and principal received on the maturity date.
- iii) Payment of interest on T-bonds held by the account holder.

Debits:

- i) Payments for investments in T-bonds.
- ii) Transfers to SIERA of the foreign investor.
- iii) Payments for primary dealers and bank charges.
- iv) Local expenses of the foreign investor.
- v) Repatriation of sale proceeds of T-bonds.
- vi) Repatriation of interest earned on T-bonds.

II) Reporting Requirement

- i) Authorized Dealers are required to furnish statements of TIERA for each month indicating details of debits and credits to the Exchange Control Department (C&F Branch) on or before the 15th day of the following month.
 - ii) Authorized dealers are also required to furnish details of credits and debits made to each TIERA at the end of the day via online using the online system already installed for reporting investment in shares through SIERAs.
4. Operating Instructions previously issued under Ref:06/04/07/2006 dated 01.11.2006 on the above subject are hereby rescinded.

Yours faithfully
Controller of Exchange

cc: Governor
DG(W)
DG(J)
AGG

GUIDELINES TO AUTHORISED DEALERS ON OPERATING INSTRUCTIONS NO. 06/04/03/2007 DATED 22.01.2007 IN RESPECT OF INVESTMENT IN RUPEE DENOMINATED TREASURY BONDS BY FOREIGN INVESTORS

(A) Foreign investors permitted to invest in Treasury Bonds (T-Bonds)

- a) Foreign country funds, regional funds or mutual funds approved by the Securities and Exchange Commission of Sri Lanka;
- (b) Corporate bodies incorporated outside Sri Lanka; and
- (c) Citizens of foreign states

(B) Account through which investment in T-bonds is permitted

Investments in T bonds should be made only out or into a Special Rupee Account named “Treasury Bond Investment External Rupee Account (TIERA)” opened in any commercial bank in the name of the above categories of foreign investors.

(C) Reporting TIERA transactions online

- i) *Foreign investors already having SIERA*
In the existing online system for reporting investment in shares, activate the icon “Add New Account” and then entering an account number by adding TIERA in front open a TIERA account. Both accounts should carry identical account holder’s name.
- ii) *Foreign investor without having SIERA*
Using existing online system for reporting investment in shares open new account named TIERA by entering a new account number inserting (TIERA) in front.

(D) Credits and Debits to TIERA

Credits and debits to TIERA should be strictly in accordance with the instructions given in the Operating Instructions. Under no circumstance transactions relating to share investments should be recorded in TIERA.

Ref: 06/07/04/2007

Department of Exchange Control
Central Bank of Sri Lanka
P.O.Box 590
Colombo 1
02 March 2007

Operating Instructions to Authorised Dealers

Dear Sirs/Madam,

**CERTIFICATE OF EXPORT INSPECTION FOR THE IMPORT OF
USED MOTOR VEHICLES**

Reference is made to our Operating Instructions No.06/07/04/2006 of August 1, 2006 on the above subject.

As you have already been informed by the Controller of Imports & Exports by his Operating Instruction to you No. 01/2007 dated 26.01.2007 that the regulations published in the Gazette Extraordinary No.1454/30 dated 21.07.2006 will be effective 1st of March 2007.

Therefore, you are hereby informed to adhere to the terms and conditions stipulated in the above Operating Instructions with effect from 1st March 2007 having substituted the item 4 of my Operating Instructions No.06/07/04/2006 dated 1st August 2006 with the following:-

“4. In case where the motor vehicles have not been shipped as at 1st March 2007 you should ensure that such Letters of Credit are amended as required in item No.2 and 3 above”.

Yours faithfully
Controller of Exchange

Ref: 06/07/05/2007

Department of Exchange Control
Central Bank of Sri Lanka
P.O.Box 590
Colombo 1
05 March 2007

Operating Instructions to Authorised Dealers

Dear Sirs/Madam,

RELEASE OF FOREIGN EXCHANGE FOR TRAVEL
ON PRODUCTION OF ELECTRONIC TICKET (eTICKET)

Attention of the Authorised Dealers is invited to item “ C ” paragraph 2 of my guidelines issued to Authorised Dealers on Operating Instructions No.EC/06/94 dated 18.03.1994 whereby Authorised Dealers have been permitted to issue foreign exchange for travel abroad for any purpose including education and medical treatment abroad on verifying the bona-fides of the request.

In terms of the Operating Instructions referred to above, the Authorised Dealers have been advised to issue foreign exchange for travellers who are resident in Sri Lanka subject to the production of return air ticket and valid Visa with the Passport. However, it has now been observed that airline industry have switched over to issue **eTickets** to the travellers instead of the traditional paper tickets.

Therefore, Authorised Dealers are hereby permitted to accept either return **eTicket** or paper ticket and valid Visa with the passport as the bona-fides to the request when issuing foreign exchange for travel purposes.

However, when accepting the **eTicket** for the issuance of foreign exchange, you should ensure to obtain a print out containing the ticket details issued by the respective airline.

Yours faithfully
Controller of Exchange

Ref: 06/04/06/2007

Department of Exchange Control
Central Bank of Sri Lanka
P.O. Box 590
Colombo 1
19 March 2007

Operating Instructions to Authorized Dealers

RESIDENT GUEST SCHEME – SPECIAL ACCOUNTS

The Government of Sri Lanka introduced Resident Guest Scheme in 1991, as a part of a package of incentives for prospective foreign investors and professionals who would contribute to the economic and socio-cultural development of the country. Under this scheme, foreign investors and professionals are required to remit funds for investment purposes and their upkeep in Sri Lanka as follows:

Investors

A sum of US\$250,000 or an equivalent amount in any convertible foreign currency for investment in Sri Lanka and a further sum of US\$35,000 per person for the upkeep in Sri Lanka of the investor and each dependant accompanying the investor.

Professionals

A sum of US\$2,000 per month for living expenses of the professional intending to reside in Sri Lanka and US\$1,000 per month for each dependant including spouse.

2. For the purpose of depositing the funds brought into the country by the investors and professionals under this scheme, Authorized Dealers are hereby permitted to open the under-mentioned special accounts in their domestic units with the prior approval of the Controller of Exchange:

(I) Special Accounts for Investors

(i) Resident Guest Foreign Currency Accounts (RGFCA)

Credits

These accounts should be opened for the purpose of depositing the minimum initial sum of US\$250,000 or an equivalent amount in any convertible foreign currency brought into the country through banking channels or on declaration to Sri Lanka Customs for investment in Sri Lanka.

Debits

- (A) Withdrawals from this account may be permitted without prior approval of the Controller of Exchange for the following:

- (a) Investment in “approved projects” subject to production of documentary proof of obtaining relevant approvals.

“Approved projects” for the purpose of this scheme are:

- (i) New ventures approved by the Board of Investment in Sri Lanka or a relevant authority;
- (ii) Existing or new companies engaged in projects approved by a relevant authority; and
- (iii) Shares listed in the Colombo Stock Exchange

- (b) Funds in excess of US\$250,000 or equivalent in other convertible foreign currencies brought into the country and held in the account unutilised.

- (B) Withdrawals for any purpose other than investment should be with the prior approval of the Controller of Exchange which will be granted with the concurrence of the Implementing Agency of the scheme.

Authorized Dealers are permitted to pay interest initially for a period of 2 years on the unutilised balance in this account, provided that the rate of interest does not exceed the rate of interest payable to Non-Resident Foreign Currency (NRFC) accounts. Such interest payment should be transferred to the investor’s Resident Guest Rupee Current Account referred below.

No interest should be paid after the expiry of the initial two-year period without the prior approval of the Controller of Exchange.

(II) Resident Guest Rupee Current Account – Investors (RGRCA – Investors)

These accounts may be opened with a minimum deposit of US\$35,000 or equivalent in other convertible foreign currency brought into the country and converted into Sri Lanka Rupees, after obtaining prior approval from the Controller of Exchange:

Credits

Credits to these accounts should be confined to the following:

- (i) Rupee proceeds of foreign currency brought into the country by the investor for his living expenses and that of his dependants;
- (ii) Interest paid on funds held in the investor's Resident Guest Foreign Currency Account (RGFCA) having converted into Sri Lanka Rupees.
- (iii) Incomes from investment (dividends, profits), sale proceeds of shares received from the investments made out of funds from the RGFCA.

Debits

(a) Debits to this account should be confined to the following:

- (i) Local expenses of the investor and his dependents;
 - (ii) Investment in approved projects mentioned in paragraph 2(I)(i)(A)(a) above;
 - (iii) Outward remittances for payments for current international transactions of the investor and/or his dependents resident in Sri Lanka.
- (b) Withdrawals for any purpose other than those mentioned in items (i), (ii) and (iii) above should be with the prior approval of the Controller of Exchange which will be granted with the concurrence of the Implementing Agency of the scheme.

(III) Resident Guest Rupee Current Account – Professionals (RGRCA – Professionals)

These accounts may be opened in the name of foreign professionals with a minimum deposit of US\$2,000 or any other convertible foreign currency brought into the country and converted into Sri Lanka Rupees, after obtaining prior approval from the Controller of Exchange.

Credits

Credits to these accounts should be confined to the following:

- (i) Rupee proceeds of foreign currency brought into the country for the living expenses of the account holder and of his dependents; and
- (ii) Salary, consultancy fees, etc. received for the provision of professional services in Sri Lanka by the account holder.

Debits

(a) Debits to this account should be confined to the following:

- (i) Local expenses of the account holder and his dependents; and
 - (ii) Outward remittances for payments on account of current international transactions of the professional and/or his dependents resident in Sri Lanka.
- (b) Withdrawals for any purpose other than those mentioned in a(i) and (ii) above should be with the approval of the Controller of Exchange which will be granted with the concurrence of the Implementing Agency of the Scheme.
3. All Authorized Dealers should furnish to "D" branch of the Exchange Control Department quarterly statements of these accounts within 15 days of the lapse of each quarter ending March, June, September and December.
 4. Operating Instructions previously issued under Ref.No.ECD/08/91(C&F) dated 20.02.1991 on the above subject is hereby rescinded.

Yours faithfully
Controller of Exchange

Ref: 06/04/07/2007

Department of Exchange Control
Central Bank of Sri Lanka
P O Box 590
Colombo 01
17 May 2007

Operating Instructions to Authorized Dealers

Dear Sir,

**FREIGHT FORWARDING & ISSUE OF HOUSE AIR WAY BILLS/
HOUSE BILLS OF LADING / FORWARDERS CARGO RECEIPTS**

Authorized Dealers are hereby requested to include the following Freight Forwarders who have been registered with the Central Bank of Sri Lanka since 2006.02.01 to the list of freight forwarders for the purpose of accepting their House Air ways Bills/ House Bills of lading, Forwarders Cargo Receipts for negotiation in respect of Exports cargo.

Name of the Freight Forwarder	Registration No.
1) Royal Asia Shipping Company (pvt) Ltd.,	06/07/009/0196
2) SEACARE Forwarders (private) Ltd.,	06/07/009/0197
3) AST Logistics International (pvt) Ltd.,	06/07/009/0198
4) Shermans Logistics (pvt) Ltd.,	06/07/009/0199
5) Transcare Logistics (pvt) Ltd.,	06/07/009/0200
6) Eagle Logistics Colombo (pvt) Ltd.,	06/07/009/0201
7) Aset Ltd,	06/07/009/0202
8) Helman World Wide Logistics (pvt) Ltd.,	06/07/009/0203
9) Phonex International Logistics Lanka (pvt) Ltd.,	06/07/009/0204
10) Logistics Plus Lanka (private) Limited	06/07/009/0205
11) Speed International Logistics (private) Ltd,	06/07/009/0206
12) V.V.K Maritime Agencies (pvt) Ltd.,	06/07/009/0207
13) Container Cargo Logistics (pvt) Ltd.,	06/07/009/0208
14) Spence Logistics (private) Ltd.,	06/07/009/0209
15) Sharp International Shipping & Trading (pvt) Ltd.,	06/07/009/0210
16) Ship Air Logistics (pvt) Ltd.,	06/07/009/0211
17) Global Logistics and Shipping (pvt) Ltd.,	06/07/009/0212
18) Spedicon Logistics (pvt) Ltd.,	06/07/009/0213
19) Califolink Logistics (pvt) Ltd.,	06/07/009/0214
20) United Cargo Management (private) Ltd.,	06/07/009/0215
21) Pan Oceanic International (pvt) Ltd.,	06/07/009/0216
22) TRANSASIA Shipping Services Colombo (pvt) Ltd.,	06/07/009/0217
23) Clarian Shipping (pvt) Ltd.,	06/07/009/0218
24) World Scan (pvt) Ltd.,	06/07/009/0219
25) Waterways International Lanka (pvt) Ltd.,	06/07/009/0220
26) Seven Seas Navigation (private) Ltd.,	06/07/009/0221
27) IJS Global Lanka (pvt) Ltd.,	06/07/009/0222
28) Serendib Logistics Solution (pvt) Ltd.,	06/07/009/0223
29) EUR Service Lanka (pvt) Ltd.,	06/07/009/0224
30) Yellow Freight International (pvt) Ltd.,	06/07/009/0225
31) JAL Shipping and Logistics (pvt) Ltd.,	06/07/009/0226
32) Tri Star Shipping International (pvt) Ltd.,	06/07/009/0227
33) Portway Shipping & Logistics (pvt) Ltd.,	06/07/009/0228
34) Volusia Freight & Logistics (pvt) Ltd.,	06/07/009/0229

Yours faithfully
Controller of Exchange

Ref: 06/04/08/2007

Department of Exchange Control
Central Bank of Sri Lanka
Colombo 1
14 June 2007

Operating Instructions to Authorised Dealers

**ISSUANCE OF FOREIGN CURRENCY NOTES TO
SRI LANKANS TRAVELLING ABROAD**

As a further measure of liberalising current international transactions and giving benefits to Sri Lankans travelling abroad, it has been decided to increase the issuance of foreign currency notes as a part of the travel allowance for Sri Lankans travelling abroad from its present level of US\$ 500 to US\$ 1000 or its equivalent in any other convertible foreign currency. However, travel allowances should be issued by exercising due diligence and discretion after satisfying the bona fides of the request.

Controller of Exchange

Ref: No. 06/04/09/2007

Department of Exchange Control
Central Bank of Sri Lanka
Colombo 1
15 June 2007

Operating Instructions to Authorised Dealers

**PERMISSION FOR THIRD PARTY
FOREIGN EXCHANGE DEPOSITS IN NRFC ACCOUNTS**

As a further measure to enhance worker remittances to the formal sector, it has been decided to grant permission to Authorised Dealers and Specialised Banks, which are permitted to open and maintain Non-Resident Foreign Currency (NRFC) Accounts, to accept foreign currency to the credit of NRFC Accounts from an immediate family member of the account holder. Foreign currency so collected from such a family member of the account holder should not exceed US\$ 1,000 or its equivalent in other convertible foreign currency per transaction.

The immediate family member of the account holder is considered to be his/her wife/husband, mother or father, brother or sister, son or daughter. Account holder is required to nominate his/her immediate family member/s who will be permitted to make foreign currency deposits to his/her NRFC account if he/she intends to utilise this facility. To avoid possible malpractices and abuses arising from this facility, banks are required to obtain the following particulars of the immediate family member/s of existing NRFC Account holders. In the case of new NRFC account holders, this information should be obtained at the time of opening accounts.

1. Names and addresses of the family member/s who will be permitted to make deposits;
2. Relationship to the account holder;
3. Nationality;
4. National Identity Card or passport number of the family member/s ; and
5. Contact telephone number/s of the family member/s.

Controller of Exchange

**The Gazette of the Democratic Socialist Republic of Sri Lanka
EXTRAORDINARY**

**No. 1516/19 – TUESDAY, SEPTEMBER 25, 2007
(Published by Authority)**

PART I : SECTION (I) - GENERAL

Government Notifications

NOTICE UNDER THE EXCHANGE CONTROL ACT (CHAPTER 423 OF THE CLE)

IN exercise of powers conferred by section 6 and 6A of the Exchange Control Act read with sections 3 and 48 of the said Act, permission is hereby granted to possess and retain foreign exchange as specified below.

Possession and retention of foreign exchange

1. (a) An authorized dealer may possess and retain foreign exchange acquired in the normal course of business and within the terms of his authorization.
- (b) An authorized person may possess and retain foreign currency received or acquired in the normal course of business and within the terms of his authorization.
- (c) A person resident in Sri Lanka may retain in his possession foreign currency in the form of currency notes, and/or travellers' cheques, the aggregate value of which does not exceed US\$ 2,000 or its equivalent in other foreign currencies:
 Provided that such foreign currency represents -
 - (i) foreign currency purchased by him from an authorized dealer or an authorized person for travel abroad and brought back unutilized while returning to Sri Lanka, or
 - (ii) foreign currency received by him outside Sri Lanka as remuneration for services rendered by him to a person resident outside Sri Lanka.
- (d) A person resident outside Sri Lanka may in Sri Lanka retain in his possession without limit foreign currency if such foreign currency was acquired by him whilst he was outside Sri Lanka.

Period for retention of foreign exchange

2. (a) A person resident in Sri Lanka who obtains foreign currency from an authorized dealer or authorized person for a purpose mentioned in an application made by him to the authorized dealer or authorized person does not use it for such purpose shall not retain such foreign currency for a period exceeding 90 days from the date of receipt of such foreign currency without converting into Sri Lanka Rupees.
- (b) A person resident in Sri Lanka who obtains foreign currency from an authorized dealer or authorized person for a purpose mentioned in an application made by him to the authorized dealer or authorized person thereafter brings back to Sri Lanka said foreign currency or part thereof, such person shall not retain such foreign currency for a period exceeding 90 days from the date of repatriation without converting into Sri Lanka Rupees.
- (c) A person resident in Sri Lanka who proceeds outside Sri Lanka for taking up employment, professional work or setting up in business earns or receives foreign currency from such employment, profession or business and brings back to Sri Lanka, such person shall not be entitled to retain such foreign currency for a period exceeding 90 days from the date of its repatriation without converting into Sri Lanka Rupees or crediting into a foreign currency account opened and/or maintained by such person in accordance with directions issued to authorized dealers under the Exchange Control Act for opening and maintaining of foreign currency accounts.
- (d) Time period referred to in sub-paragraphs (b) and (c) of this paragraph does not apply to a person resident in Sri Lanka who retains foreign currency in his possession in accordance with sub-paragraph (c) of paragraph 1 of this notice.

Interpretation for purposes of this notification

3. In this notice, unless the context otherwise requires -
 - (i) "authorized dealer" means, a commercial bank for the time being authorized under Section 4 of the Exchange Control Act for the purposes of the Act as an authorized dealer in relation to gold or any foreign currency;

- (ii) “authorized person” means, any person other than an authorized dealer for the time being authorized by the Central Bank under section 5 of the Exchange Control Act;
 - (iii) “foreign currency” shall have the same meaning as given in the Exchange Control Act;
 - (iv) “currency” shall have the same meaning as given in the Exchange Control Act;
 - (v) “foreign exchange” shall have the same meaning as given in the Exchange Control Act;
 - (vi) “person resident in Sri Lanka” or a “person resident outside Sri Lanka” shall have the same meaning as given in the Direction issued by the Minister of Finance under Section 37 (1) of the Exchange Control Act and published in the Government Gazette, No.15,007 dated 21st April, 1972.
4. Revocation of earlier notices:
- The notice published in Gazette Extraordinary, No. 1227/11 dated March 16, 2002 is hereby revoked.
5. The contents of this Gazette shall come into operation with effect from 5th October, 2007.

D. WASANTHA
Controller of Exchange

Colombo
21st September, 2007.

The Gazette of the Democratic Socialist Republic of Sri Lanka
EXTRAORDINARY

No. 1516/24 – THURSDAY, SEPTEMBER 27, 2007
(Published by Authority)

PART I : SECTION (I) - GENERAL
Government Notifications

NOTICE UNDER THE EXCHANGE CONTROL ACT (CHAPTER 423 OF THE CLE)

IN exercise of powers conferred by sub-sections 1 (a) and (b) of section 21 and sub-sections 1 (a) and (b) of section 22 of the Exchange Control Act read with Sections 3 and 48 of the said Act, permission is hereby granted to export from and import into Sri Lanka of Sri Lanka currency notes or foreign currency as specified below:-

Export and Import of Sri Lanka Currency

1. A citizen of Sri Lanka or a person resident in Sri Lanka -
 - (a) who proceeds outside Sri Lanka to take up an employment or for education or on a temporary visit on holiday, business or medical treatment, or for any other similar reasons may export on his person or in his baggage, Sri Lanka currency notes not exceeding Rs.5,000/- per person;
 - (b) who returns to Sri Lanka after employment or education abroad or a temporary visit outside the country on holiday, business or medical treatment, or for any other similar reason may import into Sri Lanka on his person or in his baggage, Sri Lanka currency notes not exceeding Rs.5,000/- per person.

Import and Export of Foreign Currency

Import of Foreign Currency:

2. A person may -
 - (a) send to Sri Lanka through normal banking channels without limit foreign currency legally acquired from any place outside Sri Lanka;
 - (b) transmit into Sri Lanka by post, money orders or postal orders expressed in foreign currency subject to any limit of amount or other limits prescribed under the Post Office Ordinance;
 - (c) bring into Sri Lanka on his person and/or in his baggage any foreign currency subject to the requirements of the Order made by the Minister of Finance in relation to prescribed currencies and published in the Government Gazette, No.10, 564 dated 14th August, 1953, as amended, and the Order made by the Minister of Finance in

relation to prescribed currencies brought in by passengers travelling in transit through a port and published in the Government Gazette, No.790/8 dated 27th October, 1993:

Provided that upon importing foreign currency into Sri Lanka by such person (not being a passenger travelling in transit through the port and remains in any area reserved or demarcated for use by transit passengers in such port), shall make a declaration on his arrival in Sri Lanka to Sri Lanka Customs in the “Passenger Baggage Declaration: Inward” form if the value of foreign currency brought into Sri Lanka exceeds US\$15,000 in aggregate or its equivalent in other foreign currencies:

Provided further that it shall be necessary to declare to the Sri Lanka Customs foreign currency notes brought in by such person, if he intends to take back foreign currency notes exceeding US\$ 5,000 or its equivalent in other currencies.

Export of Foreign Currency:

3. (a) An authorized dealer may send out of Sri Lanka foreign currency which has been acquired in the normal course of business and within the terms of his authorization;
- (b) A person resident in Sri Lanka may -
 - (i) take or send out of Sri Lanka foreign currency obtained by him from an authorized dealer or an authorized person in accordance with the provisions of the Exchange Control Act or the regulations, notifications or directions made or issued under the Act;
 - (ii) take out of Sri Lanka foreign currency retained by him in his possession in accordance with the notice issued by the Controller of Exchange for the possession and retention of foreign currency and published in the Government Gazette No. 1516/19 dated 25.09.2007;
- (c) A person resident outside Sri Lanka may take out of Sri Lanka unutilized foreign currency in a sum not exceeding the amount brought in by him on his last arrival in Sri Lanka:

Provided that taking or sending of foreign currency out of Sri Lanka by a person in or resident in Sri Lanka shall be subject to the condition that such person (not being a passenger travelling in transit through the port and remains in any area reserved or demarcated for use by transit passengers in such port) makes a declaration to Sri Lanka Customs in the “Passenger Baggage Declaration : Outward” form, or any other form prescribed by the Sri Lanka Customs for that purpose, if -

- (i) the value of foreign currency taken or sent out of Sri Lanka exceeds US\$10,000 in aggregate or its equivalent in other foreign currencies; and/or
- (ii) the value of foreign currency taken or sent out of Sri Lanka in the form of currency notes exceeds US\$5,000 in aggregate or its equivalent in other foreign currencies.

Interpretation for purposes of this notification

4. In this notice, unless the context otherwise requires -
 - (a) “authorized dealer” means, a commercial bank for the time being authorized under section 4 of the Exchange Control Act for the purposes of the Act as an authorized dealer in relation to gold or any foreign currency;
 - (b) “authorized person” means, any person for the time being authorized by the Central Bank under section 5 of the Exchange Control Act;
 - (c) “foreign currency” shall have the same meaning as given in the Exchange Control Act;
 - (d) “currency” shall have the same meaning as given in the Exchange Control Act;
 - (e) “person resident in Sri Lanka” or a “person resident outside Sri Lanka” shall have the same meaning as given in the Direction issued by the Minister of Finance under Section 37(1) of the Exchange Control Act and published in the Government Gazette, No.15,007 dated 21st April 1972.
5. The contents of this Gazette shall come into operation with effect from 5th October, 2007.

D. WASANTHA
Controller of Exchange

Colombo
21st September, 2007

Ref: 06/04/10/2007

Department of Exchange Control
Central Bank of Sri Lanka
P O Box 590
Colombo 01
06 December 2007

Operating Instructions to Authorized Dealers

Dear Sirs,

**INVESTMENT IN RUPEE DENOMINATED TREASURY BONDS BY FOREIGN INVESTORS (INCREASE
OF THE HOLDING LIMITS OF FOREIGN INVESTORS IN THE RUPEE DENOMINATED TREASURY
BONDS FROM 5% TO 10%)**

This has reference to our Operating Instructions dated 22nd January, 2007 bearing reference number 06/04/03/2007 on the above subject.

The Government has decided to further increase the current permitted level of 5% of the outstanding value of Rupee Denominated Treasury bonds (T-bonds) as at any given point of time that could be purchased and held by foreign country funds, regional funds or mutual funds approved by the Securities and Exchange Commission of Sri Lanka, Corporate Bodies incorporated outside Sri Lanka and citizens of foreign countries, upto 10% of the outstanding value of T-bonds.

Authorized Dealers are hereby permitted to open and operate Treasury bond Investment External Rupee Accounts (TIERA), in accordance with the above decision, in the names of the categories of foreign investors mentioned in paragraph 3 of the Operating Instructions dated 22nd January, 2007 referred to above, subject to the guidelines stipulated therein.

Yours faithfully
Controller of Exchange

cc: Governor
DG(W)
DG(J)
AG(SM)
SPD

Ref: 06/04/11/2007

Department of Exchange Control
Central Bank of Sri Lanka
P O Box 590
Colombo 01
31 December 2007

Operating Instructions to Authorized Dealers

Dear Sirs,

**FREIGHT FORWARDING & ISSUE OF HOUSE AIR WAY BILLS/
HOUSE BILLS OF LADING / FORWARDERS CARGO RECEIPTS**

Authorised Dealers are hereby requested to include the following Freight Forwarders who have been registered with the Central Bank of Sri Lanka since 2007.05.17 to the list of freight forwarders for the purpose of accepting their House Air ways Bills/ House Bills of lading, Forwarders Cargo Receipts for negotiation in respect of Exports cargo.

Name of the Freight Forwarder	Registration No.
1) Denovo Shipping Lines (pvt) Ltd.,	06/07/009/0230
2) Expo Consolidators (pvt) Ltd.,	06/07/009/0231

3) UNI World Logistics (pvt) Ltd.,	06/07/009/0232
4) Voyager Shipping International (pvt) Ltd.,	06/07/009/0233
5) Worldgate Express Lines Lanka (pvt) Ltd.,	06/07/009/0234
6) Trice Shipping Co.(pvt) Ltd.,	06/07/009/0235
7) Trans Atlantic Global Logistics (pvt) Ltd.,	06/07/009/0236
8) Maritime Agencies Ltd.,	06/07/009/0237
9) Care Logistics (pvt) Ltd.,	06/07/009/0238
10) GGL Line (pvt) Ltd.,	06/07/009/0239
11) Pacific Container Line Agency Colombo (pvt) Ltd.,	06/07/009/0240
12) Atlas Logistics Lanka (pvt) Ltd.,	06/07/009/0241
13) Clarion Logistics (pvt) Ltd.,	06/07/009/0242
14) Moceti Lanka (pvt) Ltd.,	06/07/009/0243
15) Freightlog Shipping Colombo (pvt) Ltd.,	06/07/009/0244
16) S&R Super Logistics Lanka (pvt) Ltd.,	06/07/009/0245
17) Crown City Developers (pvt) Ltd.,	06/07/009/0246
18) Ocean Links Logistics (pvt) Ltd.,	06/07/009/0247
19) Freight Masters International (pvt) Ltd.,	06/07/009/0248

Yours faithfully
Controller of Exchange

Financial Intelligence Unit
Tel. No. 2477228
Fax No: 2477692
e-mail: hkaru@cbsl.lk
4th April 2007

To: CEOs of All Commercial Banks

LIGHT A MILLION CANDLES CAMPAIGN

The urgent attention of all commercial banks is drawn to interpretation clause 33 of the Financial Transactions Reporting Act No.6 of 2006 which lists “offences against children” as an unlawful activity in terms of the law.

In this regard it has been brought to our attention that child pornography websites are being contributed to by customers through electronic payments systems and internet transactions. It is felt that credit cards remain the most common method of on-line payment used by consumers and utilized by purveyors of pornographic material.

A task force of the Sri Lanka Commercial Banks established for this purpose, in collaboration with the FIU, is working on a modus operandi to eradicate the commercial viability of child pornography.

The Financial Intelligence Unit, in its commitment to this noble cause and in giving effect to the provisions of the FTRA, invites the immediate attention of all commercial banks to the following imperatives:-

- To initiate, with immediate effect, additional KYC and CDD on existing and new credit card merchant bases with a special focus on the nature of business;
- Report immediately to the FIU, in the form of a Suspicious Transaction Report, in terms of Section 7(1)(a) of the FTRA, any customer, transaction or merchant involved in offences against children, as illustrated above.

Please acknowledge receipt.

Actg. Additional Director
Financial Intelligence Unit

Copy to: All Compliance Officers
Sri Lanka Banks' Association
Director/Bank Supervision Department

Ref: 37/04/001/0001/007

Financial Intelligence Unit

Tel. No. 2477125

Fax No: 2477692

e-mail: hkaru@cbsl.lk

18 May 2007

*The Chief Executive Officers of
all Licensed Banks and Registered Finance Companies*

Dear Sir/Madam

**FINANCIAL TRANSACTIONS REPORTING ACT NO.6 OF 2006 (FTRA) –
KNOW-YOUR-CUSTOMER AND CUSTOMER DUE DILIGENCE RULES
PRESCRIBED IN TERMS OF SECTION 2(3) OF THE FTRA**

Detailed guidance and rules based on the Financial Actions Task Force and the Basle Committee on Bank Supervision on Customer Due Diligence, incorporating recommendations, where relevant, by the Sri Lanka Banks' Association, are enclosed.

You are advised to ensure that a proper policy framework and operational guidelines to give effect to the guidance and the rules so prescribed, are put in place within a specific AML/CFT policy developed by your institution for this purpose.

You are also required to ensure that your institution is fully compliant with these rules before 31st March 2008. With regard to new customers the rules will have immediate effect.

Any contravention or non-compliance with the rules so prescribed will be liable to penalties as prescribed in the relevant provisions of the Act.

Yours faithfully
Actg. Additional Director
Financial Intelligence Unit

Copies to:- All Compliance Officers
The Sri Lanka Banks' Association
The Finance Houses Association
The Approved Panel of Auditors
The Director Bank Supervision Department, CBSL
The Director Supervision of Non-bank Financial Inst. Dept. CBSL

**RULES ON CUSTOMER DUE DILIGENCE FOR FINANCIAL INSTITUTIONS
AND NON BANK FINANCIAL INSTITUTIONS**

Introduction

Public confidence in financial institutions, and hence their stability, is enhanced by sound banking practices that reduce financial risks to their operations. Money laundering and terrorist financing can harm the soundness of a country's financial system, as well as the stability of individual financial institutions, in multiple ways. Customer identification and due diligence procedures also known as "know your customer" (KYC) rules, are part of an effective AML/CFT regime. These rules are not only consistent with, but also enhance, the safe and sound operation of banking and other types of financial institutions.

While preparing operational guidelines on customer identification and due diligence procedures, financial institutions are advised to treat the information collected from the customer for the purpose of opening of accounts, as confidential and not divulge any details thereof for cross-selling or for any other purposes, and that the information sought is relevant to the perceived risk, is not intrusive and is in conformity with the rules issued hereunder.

These rules are issued under Section 2(3) of the Financial Transactions Reporting Act No.6 of 2006 and any contravention of, or non-compliance with the same will be liable to the penalties under the relevant provisions of the Act.

Actg. Additional Director
Financial Intelligence Unit,
Central Bank of Sri Lanka

18th May 2007

PART I - GENERAL GUIDANCE

A. Natural Persons

1. For natural persons the following information should be obtained, where applicable:
 - legal name and any other names used (such as maiden name);
 - correct permanent address (the full address should be obtained; a Post Office box number is not sufficient);
 - telephone number, fax number, and e-mail address;
 - date and place of birth;
 - nationality;
 - occupation, public position held and/or name of employer;
 - an official personal identification number or other unique identifier contained in an unexpired official document (e.g. passport, identification card, residence permit, social security records, driving licence) that bears a photograph of the customer;
 - type of account and nature of the financial institution in relationship;
 - signature.
2. The financial institution should verify this information by at least one of the following methods:
 - confirming the date of birth from an official document (e.g. birth certificate, passport, identity card, social security records);
 - confirming the permanent address (e.g. utility bill, tax assessment, bank statement, a letter from a public authority);
 - contacting the customer by telephone, by letter or by e-mail to confirm the information supplied after an account has been opened (e.g. a disconnected phone, returned mail, or incorrect e-mail address should warrant further investigation);
 - confirming the validity of the official documentation provided through certification by an authorised person (e.g. embassy official, notary public).
3. The examples quoted above are not the only possibilities. In particular jurisdictions there may be other documents of an equivalent nature which may be produced as satisfactory evidence of customers' identity.
4. Financial institutions should apply equally effective customer identification procedures for non-face-to-face customers as for those available for interview.
5. From the information provided in paragraph 10, financial institutions should be able to make an initial assessment of a customer's risk profile. Particular attention needs to be focused on those customers identified thereby as having a higher risk profile and additional inquiries made or information obtained in respect of those customers to include the following:-
 - evidence of an individual's permanent address sought through a credit reference agency search, or through independent verification by home visits;
 - personal reference (i.e. by an existing customer of the same institution);
 - prior bank reference and contact with the financial institution regarding the customer;
 - source of wealth;
 - verification of employment, public position held (where appropriate).

6. For one-off or occasional transactions where the amount of the transaction or series of linked transactions does not exceed an established minimum monetary value, it might be sufficient to require and record only name and address in instances where:-
- reliable information on the customer is publicly available to the bank/financial institution;
 - the financial institution is dealing with another bank whose AML/CFT controls it is well familiar with by virtue of a previous course of dealings;
7. It is important that the customer acceptance policy is not so restrictive that it results in a denial of access by the general public to banking services, especially for people who are financially or socially disadvantaged.

B. Institutions

8. The underlying principles of customer identification for natural persons have equal application to customer identification for all institutions. Where in the following the identification and verification of natural persons is involved, the foregoing guidance in respect of such persons should have equal application.
9. The term institution includes any entity that is not a natural person. In considering the customer identification guidance for the different types of institutions, particular attention should be given to the different levels of risk involved.

C. Corporate Entities

10. For corporate entities (i.e. corporations and partnerships), the following information should be obtained:
- name of institution;
 - principal place of institution's business operations;
 - mailing address of institution;
 - contact telephone and fax numbers;
 - some form of official identification number, if available (e.g. tax identification number);
 - the original or certified copy of the Certificate of Incorporation and Memorandum and Articles of Association; certificate of partnership or certificate of registration, where appropriate;
 - the resolution of the Board of Directors to open an account and identification of those who have authority to operate the account;
 - nature and purpose of business and its legitimacy.
11. The financial institution should verify this information by at least one of the following methods:
- for established corporate entities - reviewing a copy of the latest report and accounts (audited, if available);
 - conducting an enquiry by a business information service, or an undertaking from a reputable and known firm of lawyers or accountants confirming the documents submitted;
 - undertaking a company search and/or other commercial enquiries to see that the institution has not been, or is not in the process of being, dissolved, struck off, wound up or terminated;
 - utilizing an independent information verification process, such as by accessing public and private databases;
 - obtaining prior bank references;
 - visiting the corporate entity, where practical;
 - contacting the corporate entity by telephone, mail or e-mail.
12. The financial institution should also take reasonable steps to verify the identity and reputation of any agent that opens an account on behalf of a corporate customer, if that agent is not an officer of the corporate customer.

C1. Corporations/Partnerships

13. For corporations/partnerships, the principal guidance is to look behind the institution to identify those who have control over the business and the company's/partnership's assets, including those who have ultimate control. For corporations, particular attention should be paid to shareholders, signatories, or others who inject a significant proportion of the capital or financial support or otherwise exercise control. Where the owner is another corporate entity or trust, the objective is to undertake reasonable measures to look behind that company or entity and to verify

the identity of the principals. What constitutes control for this purpose will depend on the nature of a company, and may rest in those who are mandated to manage funds, accounts or investments without requiring further authorisation, and who would be in a position to override internal procedures and control mechanisms. For partnerships, each partner should be identified and it is also important to identify immediate family members that have ownership control.

14. Where a company is listed on a recognised stock exchange, or is a subsidiary of such a company, then the company itself may be considered to be the principal to be identified. However, consideration should be given to whether there is effective control of a listed company by an individual, small group of individuals or another corporate entity or trust. If this is the case then those controllers should also be considered to be principals and identified accordingly.

D. Retirement Benefit Programmes

15. Where an occupational pension programme, employee benefit trust or share option plan is an applicant for an account the trustee and any other person who has control over the relationship (e.g. administrator, programme manager, and account signatories) should be considered as principals and the financial institution should take steps to verify their identities.

E. Mutuals/Friendly Societies, Cooperatives and Provident Societies

16. Where these entities are an applicant for an account, the principals to be identified should be considered to be those persons exercising control or significant influence over the organisation's assets. This will often include board members plus executives and account signatories.

F. Charities, Clubs and Associations

17. In the case of accounts to be opened for charities, clubs, and societies, the financial institution should take reasonable steps to identify and verify at least two signatories along with the institution itself. The principals who should be identified should be considered to be those persons exercising control or significant influence over the organisation's assets. This will often include members of a governing body or committee, the President, any board members, the treasurer, and all signatories.
18. In all cases independent verification should be obtained that the persons involved are true representatives of the institution. Independent confirmation should also be obtained of the purpose of the institution.

G. Trusts nominee and fiduciary accounts

19. Financial institutions should establish whether the customer is taking the name of another customer, acting as a "front" or acting on behalf of another person as trustee, nominee or other intermediary. If so, a necessary precondition is receipt of satisfactory evidence of the identity of any intermediaries and of the persons upon whose behalf they are acting, as well as details of the nature of the trust or other arrangements in place. Specifically, the identification of a trust should include the trustees, settlers/grantors and beneficiaries.

When opening an account for a trust, the financial institution should take reasonable steps to verify the trustee(s), the settlor(s) of the trust (including any persons settling assets into the trust) any protector(s), beneficiary(ies), and signatory(ies). Beneficiaries should be identified when they are defined. In the case of a foundation, steps should be taken to verify the founder, the managers/directors and the beneficiaries.

H. Beneficial Owners

20. The financial institution should be able to justify the reasonableness of the measures taken, having regard to the circumstances of each case. The financial institution may also consider obtaining an undertaking or declaration from the customer on the identity of, and the information relating to, the beneficial owner.

I. Professional Intermediaries

21. When a professional intermediary such as a lawyer, notary, other independent legal professional or accountant, opens a client account on behalf of a single client that client must be identified. Professional intermediaries will often open "pooled" accounts on behalf of a number of entities. Where funds held by the intermediary are not co-mingled but where there are "sub-accounts" which can be attributable to each beneficial owner, all beneficial owners of the account held by the intermediary should be identified. Where the funds are co-mingled, the financial institution should look through to the beneficial owners; however, there may be circumstances which should be set

out in supervisory guidance where the financial institution may not need to look beyond the intermediary (e.g. when the intermediary is subject to the same due diligence standards in respect of its client base as the financial institution).

22. Where such circumstances apply and an account is opened for an open or closed ended investment company, unit trust or limited partnership which is also subject to the same due diligence standards in respect of its client base as the financial institution, the following should be considered as principals and the financial institution should take steps to identify:
 - the fund itself;
 - its directors or any controlling board where it is a company;
 - its trustee where it is a unit trust;
 - its managing (general) partner where it is a limited partnership;
 - account signatories;
 - any other person who has control over the relationship e.g. fund administrator or manager.
23. Where other investment vehicles are involved, the same steps should be taken as in paragraph 22 where it is appropriate to do so. In addition all reasonable steps should be taken to verify the identity of the beneficial owners of the funds and of those who have control of the funds.
24. Intermediaries should be treated as individual customers of the financial institution and the standing of the intermediary should be separately verified by obtaining the appropriate information drawn from the itemised lists included in paragraphs 10-11 above.

J. Other Types of Institutions

25. For the account categories referred to in the aforementioned paragraphs, the following information should be obtained in addition to that required to verify the identity of the principals:
 - name of account;
 - mailing address;
 - contact telephone and fax numbers;
 - some form of official identification number, if available (e.g. tax identification number);
 - description of the purpose/activities of the account holder (e.g. in a formal constitution);
 - copy of documentation confirming the legal existence of the account holder (e.g. register of charities).
26. The financial institution should verify this information by at least one of the following:
 - obtaining an independent undertaking from a reputable and known firm of lawyers or accountants confirming the documents submitted;
 - obtaining prior bank references;
 - accessing public and private databases or official sources.

K. Introduced Business

27. For expediency, it has become customary for financial institutions to rely on the procedures undertaken by other financial institutions or introducers when business is being referred. In doing so financial institutions risk placing excessive reliance on the due diligence procedures that they expect the introducers to have performed. Relying on due diligence conducted by an introducer, however reputable, does not in any way remove the ultimate responsibility of the recipient bank to know its customers and their business. In particular financial institutions should not rely on introducers that are subject to weaker standards than those governing the financial institutions' own KYC procedures or that are unwilling to share copies of due diligence documentation.
28. Financial institutions that use introducers should carefully assess whether the introducers are "fit and proper" and are exercising the necessary due diligence in accordance with the standards set out in this paper. The ultimate responsibility for knowing customers always lies with the financial institution. Financial institutions should use the following criteria to determine whether an introducer can be relied upon:

- it must comply with the minimum customer due diligence practices identified in this paper;
- the customer due diligence procedures of the introducer should be as rigorous as those which the financial institution would have conducted itself for the customer;
- the financial institution must satisfy itself as to the reliability of the systems put in place by the introducer to verify the identity of the customer;
- the financial institution must reach agreement with the introducer that it will be permitted to verify the due diligence undertaken by the introducer at any stage; and
- all relevant identification data and other documentation pertaining to the customer's identity should be immediately submitted by the introducer to the financial institution who must carefully review the documentation provided. Such information must be available for review by the supervisor and the financial intelligence unit or equivalent enforcement agency, where appropriate legal authority has been obtained;
- in addition, financial institutions should conduct periodic reviews to ensure that an introducer which it relies on continues to conform to the criteria set out above.

PART II – SPECIFIC GUIDANCE

All financial institutions are required to comply with the following:-

1) Opening of Accounts

a. Individual Accounts:

Information to be obtained

- Full name as appearing in the identification document.
- Identification document to be specified as, national identity card, unexpired passport, official driving licence.
- Permanent address as appearing on the identification document. Any other address to be accepted should be supported by a utility bill not over three months old. Utility bills are to be specified as electricity bill, water bill and telecom or any fixed line operator's bill. No post-box number should be accepted. In the case of 'C/o', property owner's consent and other relevant address verification documents are required to be obtained.
- Telephone number, fax number, and e-mail address.
- Nationality
- Occupation, business, public position held and the name of the employer.
- Purpose for which the account is opened.
- Expected turnover/volume of business.
- The reason for choosing to open the account in a foreign jurisdiction in case of NRFC/NRRAs.
- Satisfactory reference.
- Signature

Documents to be obtained (each copy should be duly certified by the authority issuing same)

- Mandate/Account Opening form
- Copy of identification document.
- Copy of address verification documents.
- Copy of the valid visa/permit in the case of RNNFC/NRRA/RGFC accounts for non-nationals.
- Business registration if the account is opened for such purpose.

b. Proprietorship/Partnership Accounts:

Information to be obtained

- Full name as appearing in the registration document.
- Personal details of the proprietor/partners as in the case of individual accounts.
- Registered address or the principle place of business and the permanent address of the proprietor/partners.
- Contact telephone, fax numbers.
- Tax file number.
- Satisfactory reference.

- Signature.
- The extent of the ownership controls.
- Other connected business interests.

Documents to be obtained

- Mandate/Account opening form.
- Business registration document.
- Proprietors'/partners' information document.
- Copy of identification and address verification documents.

c. Corporations/Limited Liability Company:

Information to be obtained

- Registered name of the institution.
- Principle place of institution's business operations.
- Mailing address, if any.
- Nature and purpose of business.
- Telephone/Fax/E-mail.
- Income tax file number.
- Bank references.
- Personal details of all Directors as in the case of individual customers.
- Major share holders and their financial interests and control.
- List of subsidiaries/associates and other business connections.
- Signatures.

Documents to be obtained

- Mandate/Account Opening form.
- Original or certified copy of the Certificate of Incorporation and Memorandum of Articles of Association.
- Board Resolution authorizing the opening of the account.
- Directors' information document including their other business interests.
- Copy of Form 48.
- Copy of Form 36.
- Board of Investment Agreement if a BOI approved company.
- Export Development Board (EDB) approved letter if EDB approved company.
- Certificate to commence business if a public quoted company.
- Certified copy of business registration (if a partnership/sole trader)
- Latest audited accounts if available.
- The above documents should apply to a company registered abroad as well.
- The non-documentary methods in the absence of the above documents would entail a search at the Credit Information Bureau (CRIB), bank references, site visits and visiting the business website of the customer.

d. Clubs, Societies, Charities, Associations and NGOs:

Information to be obtained

- Name and address as appearing in Charter, Constitution etc.
- Detailed information of at least two office bearers, signatories, administrators, members of the governing body or committee or any other person who has control and influence over the operations of the entity as in the case of individual accounts.
- The purpose for which the account is opened, the objectives and the areas of activities.
- The source and level of income/funding.

- Other connected institutions/associates/organizations.
- Telephone/Fax numbers/e-mail address.

Documents to be obtained

- The registration document/constitution, charter etc.
- Customer information form as in the case of individual accounts.
- Mandate/Account Opening Form.

e. Trust, nominees, and fiduciary accounts:

Information to be obtained

- Identification of all trustees, settlers/grantors and beneficiaries in case of trustees.
- Whether the customer is acting as a 'front' or acting as a trustee, nominee, or other intermediary.

Documents to be obtained:

- Mandate/Account Opening Form.
- Trust Deed.
- Particulars of all individuals.

2) Maintenance of Accounts:

1. Unless and until adequate identity of the prospective client is obtained no account should be opened. If any discrepancy in information is detected subsequently the account should be stopped until the veracity of such information is confirmed.
2. The general customer information to be recorded at the outset should include customer's business/profession, level of income, economic profile, business associates and other connections, source of funds, and the purpose for which the account is opened.
3. Copies of all identification and address verification documents should be retained in terms of the law.
4. Where the permanent address given in the application is at a location far away from that of the branch which receives the account opening request, the request must be discouraged/turned down and the prospective client be requested to open the account at the closest branch to his residence or his business, unless an acceptable and a valid reason is given. Such exceptions should be recorded in file. If change of address is made after the opening of the account, the account should be transferred to the nearest branch of the particular bank.
5. When two or more accounts are opened in the same bank, the specific purpose for which the account is opened may be recorded to assist continued due diligence of all accounts.
6. Check whether the prospective customers appear on any list of any known suspected terrorist list or alert list issued by national/government authorities such as the Controller of Immigration, Customs, Central Bank etc.
7. When instructions are received from clients to transfer funds from one account to another both account numbers should be recorded internally to aid future reference.
8. When RNNFC, RGFC as well as temporary rupee accounts are opened for non-nationals/foreign passport holders who are resident in Sri Lanka, a local address should be obtained as their permanent address during their stay in the Island. A copy of the passport, visa with validity period, foreign address and the purpose for which the account is opened should be made available in the file. On the expiry of the visa, the account should cease to operate unless and otherwise appropriate instructions are received. On leaving the Island the account should either be closed or be converted into a non-resident account. Financial institutions must ensure that a valid visa is held at all times by the clients during the continuation of the account with them.
9. When rupee accounts (NRRA) are opened and maintained for non-residents (foreign passport holders), a foreign address may be used as a permanent address and for all correspondence. The reason for choosing to open the account in a foreign jurisdiction should be recorded in the file.
10. **All rupee accounts for resident non-nationals** should carry a Sri Lankan address. A foreign address may be used temporarily until the account holder is resident abroad. Bank must ensure to update the address on the client's return, under the ongoing due diligence. In the case of joint accounts a foreign address may be used only when all parties are domiciled abroad. If any one party remains in the Island, the local address needs to be maintained.

11. Bank accounts for charitable and aid organizations and NGOs should be opened only with the registration of the NGO Authority and with other appropriate credentials. Due regard should be paid to specific directions governing their operations i.e. issued by the Department of Bank Supervision/Controller of Exchange.
12. Opening of accounts for ‘politically exposed persons’ (PEP) should have authorization of senior management. PEPs are defined as “individuals in Sri Lanka or abroad who are, or have been, entrusted with prominent public functions” e.g. Heads of State or of government, senior politicians, senior government, judicial or military officials, senior executives of State owned corporations, important political party officials. Business relationships with family members or close associates of PEPs involve reputational risks similar to those with PEPs themselves. The definition is not intended to cover middle ranking or more junior officials in the forgoing categories.
13. All cash deposits made into savings and current accounts over Rs.500,000/= by third parties should have on record, the identity of the depositor. The required details are, the name, address, ID number, purpose and the signature. However, clerks, accountants and employees of business houses who are authorized to deal with the accounts do not come within the definition of ‘third parties’.
14. When outward remittances/wire transfers are made out of NRFC/RFC accounts it is mandatory that a complete application be forwarded to the financial institution incorporating important and meaningful originator information such as name, address, account number, identification number together with a brief account of the purpose for such transfers. This is applicable to domestic wire transfers as well.
15. No wire transfers should be permitted out of currency deposits made into these NRFC/RFC accounts unless they are brought into the country by the account holder with evidence. No undeclared¹ currency notes brought into the country be accepted into these accounts. If regular currency notes are deposited into foreign currency accounts, the financial institution should be satisfied and be aware of the legitimacy of such deposits.
16. Financial institutions must ensure that no ATM external withdrawals exceeding the mandatory threshold² are made without the express approval of the financial institution. If, regular withdrawals are made by customers in small amounts in order to circumvent the reporting limit, the withdrawal facility in such events must be suspended forthwith and reported as a suspicious transaction. Financial institutions must exercise due diligence to prevent any misuse of this facility. This is applicable to both rupee accounts and foreign currency accounts.
17. No transfer of funds from RFC to NRFC accounts should be permitted although fund transfers from NRFC to RFC accounts are permitted as per exchange control regulations.
18. A proper customer identification or relationship has to be established when import documents on collection basis are released to non customers of financial institutions. Identification should include the correct address of the person or the business.
19. The updating of all accounts with relevant information should be completed by 31st March 2008 by all financial institutions.
20. Accounts which record frequent transactions below the threshold limit of Rs. 500,000/= in an attempt to circumvent the mandatory reporting requirement should be reported to the financial institution’s Compliance Officer for appropriate action.
21. Financial institutions must ensure that account activities are consistent with the customer profile on record. Any inconsistency should be inquired into and the correct position recorded. All unexplainable activities should be reported to the financial institution’s compliance officer for appropriate action.
22. **Introduction of new technologies** —financial institutions should pay special attention to any money laundering threats that may arise from new or developing technologies, including internet banking, that might favour anonymity and take measures, if needed, to prevent their use in money laundering schemes. Financial institutions should be mindful of a variety of Electronic Cards that are used by customers for buying goods and services, drawing cash from ATMs and for the electronic transfer of funds. **Pre-loading of credit cards in particular can be resorted to, inter-alia, for money laundering and terrorist financing purposes and should not be permitted as to do so would be tantamount to the abuse of credit cards.**
23. **Additional KYC and CDD on existing and new credit card merchant bases with a special focus on the nature of business of credit card merchants, should be undertaken and appropriate measures taken in terms of the provisions of the FTRA against any customer, transaction or merchant involved in any unlawful activity. Payments made through the internet by credit card customers in particular warrant very close attention to ensure that payments are not made for unlawful activities;**

24. **Where marketing of credit cards is done through agents** financial institutions should ensure that appropriate KYC procedures are duly applied to the customers as well as to the agents.
25. When applications for opening of accounts are received by mail or e-mail due care should be exercised to record the true identity of the client prior to opening the accounts or activating them. In no case should the financial institutions short-circuit the required identity procedures just because the prospective client is unable to present himself in person.
26. It is mandatory for financial institutions to preserve SWIFT messages that accompany inward remittances for a period of six years as they contain important customer details.
27. When financial institutions maintain accounts for money changers/money remitters they need to be aware that such clients are engaged exclusively in the money changing/money remitting business in compliance with the terms and conditions of the permit issued to them. Since money changers are covered by the provisions of the Prevention of Money Laundering Act (PMLA) and the Financial Transactions Reporting Act (FTRA), it is the duty of the financial institutions to ensure that they fully comply with the requirements of law. Any unauthorized illegal engagement in financing transactions should be brought to the notice of the financial institution's compliance officer for appropriate action.
28. **Alternative Remittance Systems (Hundi, Hawala etc.)**
Extra vigilance is required by financial institutions to distinguish between formal money transmission services and other money or value transfer systems through which funds or value are moved from one geographic location to another through informal and unsupervised networks or mechanisms. To ascertain the sources of funds thus becomes an imperative.
29. **Correspondent Banks and Shell Banks** - Prior to commencing banking relationships with '**correspondent Banks/financial institutions**', financial institutions should gather sufficient information with regard to their management, major business activities, and their money laundering prevention and detection efforts. It is also the duty of the financial institutions to ensure that the purpose of the account is exclusively for correspondent banking activities and that the bank is effectively supervised by the relevant authorities for their due diligence and AML standards in that country. The financial institutions should refuse to enter into, or conduct business and provide services to, financial institutions that are located in jurisdictions that have poor KYC standards or have been identified as being 'non-co-operative' in the fight against ML and TF. It is also imperative that the financial institutions ensure that their correspondent financial institutions do not undertake business with shell financial institutions. No accounts **for 'shell' financial institutions** should be opened without the proper approval of the Controller of Exchange.

Notes: 1. In excess of the prescribed threshold

2. The Bank specific threshold of ATM withdrawals

3) **General**

1. All financial institutions are required to appoint a **compliance officer** in terms of Section 14 of the FTRA, who shall be responsible for ensuring the institution's compliance with the requirements of the relevant laws. These officers must be at the senior management level.
2. In terms of the Section 14(1) c of the FTRA, every bank must establish an **audit function** to test its procedures and systems for compliance.
3. All financial institutions are required to make its **officers and employees aware** of the laws relating to money laundering and financing of terrorism and to train its officers, employees and agents to recognize suspicious transactions. Financial institutions are also required to screen all persons before hiring them as employees.
4. Financial institutions should ensure that its **domestic and foreign branches, and subsidiaries** adopt and observe measures to the extent that local laws and regulations are applicable and where the foreign branches/subsidiaries are unable to adopt and observe such measures in jurisdictions which do not, or insufficiently apply, the FATF recommendations, such matter should be reported to the financial institution's Compliance officer for appropriate action.

5. All financial institutions should scrutinize and examine the background of all their relatively large transactions that are complex, unusual or have no apparent economic and lawful purpose and retain a written record of such examination.

6. Treasury Dealings

With regard to dealings in Forex, money market, bonds, securities, precious metals etc. confirmations should be obtained from the counter-parties on their adherence to AML/CFT guidelines to prevent transactions with non-compliant countries/entities.

7. Trade Finance/Letters of Credit and other contingencies

Trade-based money laundering and terrorist financing usually involves invoice manipulation and uses trade finance routes and commodities to avoid financial transparency, laws and regulations. The use of these facilities needs to be reviewed from time to time. Facilities requested by customers who have borrowing facilities or large deposits with other institutions should be brought under close scrutiny. Other examples are the assignment of proceeds to an apparently unconnected third party, the use of pro forma invoices without description of goods and reticence to provide goods description and other appropriate supporting documentation.

Ref: 37/04/001/0001/007

Financial Intelligence Unit
Tel. No. 2477125
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e-mail: hkaru@cbsl.lk
23 May 2007

To: All Licensed Banks / Registered Finance Companies

Dear Sirs,

**COMPLIANCE WITH THE REPORTING REQUIREMENTS UNDER THE
FINANCIAL TRANSACTIONS REPORTING ACT NO.6 OF 2006**

Further to our Circular No. 4 dated 15th September 2006 on the above subject, I wish to draw your attention to the following;

As per clause (a) and (b) of the said circular please ensure that your reports are forwarded to the FIU on a fortnightly basis, in the specimen formats given to you.

E.g.: Reports for the period 1st to 15th of each month should be forwarded to the FIU on or before the 30th of the month.

Reports for the period 16th to 31st of each month should be forwarded to the FIU on or before 15th of the subsequent month.

You are hereby requested to ensure compliance with the above.

Yours faithfully
Actg. Additional Director
Financial Intelligence Unit

Ref: 37/04/001/0001/007

Financial Intelligence Unit
 Tel. No. 2477125
 Fax No: 2477692
 e-mail: hkaru@cbsl.lk
 21 June 2007

The Chief Executive Officers of all Commercial Banks

Dear Sir/Madam

MANDATORY REPORTING REQUIREMENT – ELECTRONIC FUND TRANSFERS

Your immediate attention is drawn to the mandatory reporting requirement of electronic funds transfers in excess of Rs.500,000 or its equivalent in any foreign currency in terms of the Gazette Order No.1437/25 of 23rd March, 2006.

I shall thank you to ensure that the following transactions too as at 30th June, 2007 and thereafter for the reporting periods, are captured in the mandatory reporting format for this purpose:-

Electronic Funds Transfers inclusive of

- (i) Inwards & Outwards Remittances
- (ii) SLIP Transfers
- (iii) RTGS transactions
- (iv) Credit Card Transactions
- (v) Debit Card Transactions (If applicable)
- (vi) Transactions relating to NRFC's & RFC's,

and, any other transactions that are transferred electronically above the mandatory threshold.

Yours faithfully
 Actg. Director
 Financial Intelligence Unit

Copies to:- All Compliance Officers
 The Sri Lanka Banks' Association
 The Approved Panel of Auditors
 The Director, Bank Supervision Department, Central Bank of Sri Lanka

Ref: 37/01/016/0001/007

Financial Intelligence Unit
 Tel. No. 2477125
 Fax No: 2477692
 e-mail: hkaru@cbsl.lk
 20 August 2007

*To: All Compliance Officers of Licensed Banks &
 Registered Finance Companies*

**COMPLIANCE WITH KYC/CDD RULES FOR NEW CUSTOMERS
 AND EXISTING CUSTOMERS – STATE OF READINESS**

In order to assess the state of readiness of licensed banks and registered finance companies to comply with the mandatory KYC/CDD Rules issued to the industry in June 2007 and which will become effective as follows:-

New Customers	–	October, 2007
Existing Customers	–	March, 2008

Please provide the following information to the FIU within 2 weeks from the date of receipt of this letter:-

- Operational Plans in place to give effect to the above time thresholds;
- Mileposts set i.e. As of September, 2007 - December, 2007
- March, 2008
- If the March, 2008 time frame cannot be met, the reasons there for, and the mileposts set thereafter for completion of the phase in.
- Please note that the three year period for phase in expires in March, 2009.

Yours faithfully
Actg. Director
Financial Intelligence Unit

Copy to:- Director, Bank Supervision, CBSL
Director, Supervision of Non-Bank Financial Institutions, CBSL
In terms of Section 23 of the FTRA, I shall thank you to report the status of compliance with the KYC/CDD Rules issued to the institutions coming under your purview taking into account the timelines set for full compliance as indicated above.

Ref: 37/03/004/0003/007

Financial Intelligence Unit
Tel. No. 2477125
Fax No: 2477692
e-mail: fiu@cbsl.lk
28 December 2007

The Chief Executive Officer

Dear Sir/Madam,

MANDATORY KNOW-YOUR-CUSTOMER AND CUSTOMER DUE DILIGENCE (KYC/CDD)
RULES FOR THE SECURITIES INDUSTRY IN TERMS OF THE PROVISIONS OF
THE FINANCIAL TRANSACTIONS REPORTING ACT NO. 6 OF 2006 (FTRA)

Detailed guidance and rules based on international best practices and also where relevant, incorporating recommendations by the Securities and Exchange Commission of Sri Lanka are enclosed herewith.

You are advised to ensure that a proper policy framework and operations guidelines to give effect to the guidance and the rules so prescribed are in place within a specific AML/CFT policy developed by your institution for this purpose.

You are required to submit quarterly reports to the FIU on the last date of the quarterly period using the attached format at annexure 1. You are also required to ensure that your institution, as a securities market participant, is fully compliant with these rules, and inform us of the progress made by 31st January 2008.

These rules are issued under Section 2(3) of the Financial Transactions Reporting Act No.6 of 2006, and any contravention or non-compliance with the rules so prescribed will be liable to penalties as prescribed in the relevant provisions of the Act.

Yours faithfully
H A Karunaratne
Actg. Director
Financial Intelligence Unit

Copy to: Director General, Colombo Stock Exchange,
Level 4-04, World Trade Centre, Colombo 1

RULES ON
KNOW YOUR CUSTOMER (KYC) & CUSTOMER DUE DILIGENCE (CDD)
FOR THE SECURITIES INDUSTRY

Introduction

Public confidence in financial institutions, and hence their stability, is enhanced by sound practices that reduce financial risks to their operations. Money laundering and terrorist financing can harm the soundness of a country's financial system, as well as the stability of individual financial institutions, in multiple ways. Customer identification and due diligence procedures also known as "know your customer" rules, are part of an effective AML/CFT regime. These rules are not only consistent with, but also enhance, the safe and sound operation of banking and other types of financial institutions.

While preparing operational guidelines on customer identification and due diligence procedures, institutions are advised to treat the information collected from the customer for the purpose of opening of accounts, as confidential and not divulge any details thereof for cross-selling or for any other purposes, and that the information sought is relevant to the perceived risk, is not intrusive and is in conformity with the rules issued hereunder.

The mandatory rules on KYC/CDD include the following sections:

- Part I - General Rules
- Part II - Specific Rules
- Part III - Specific Customer Identification
- Part IV - Declaration Format
- Part V - Suspicious Transaction Report Format/Instructions

These rules are issued under Section 2(3) of the Financial Transactions Reporting Act No.6 of 2006 and any contravention of, or non-compliance with the same will be liable to the penalties under the relevant provisions of the Act.

Actg. Director
 Financial Intelligence Unit,
 Central Bank of Sri Lanka

28th December 2007

PART I
GENERAL RULES FOR THE SECURITIES INDUSTRY

A. ANTI-MONEY LAUNDERING PROGRAM

1. Introduction

An institution should develop and implement a written program reasonably designed to prevent it from being used for money laundering and terrorist financing. This program should be approved in writing by the directors of the company which carries out the business of broker/dealer/market intermediary or by the trustee/s of a unit trust. It should include:

- the establishment of policies, procedures, and internal controls;
- an ongoing employee training program;
- an independent audit function to test the program for compliance; and
- appropriate compliance management arrangements. The type and extent of measures to be taken for each of these requirements should be tailored with respect to the risk or vulnerability to money laundering and terrorist financing and the size, location, and activities of the business.

2. Policies and Procedures

Written policies and procedures should set forth clearly the details of the program, including the responsibilities of the individuals and departments involved. Policies, procedures, and internal controls should be reasonably designed to detect activities indicative of money laundering and to assure compliance with anti-money laundering legislation. An institution should monitor the operation of its program and assess its effectiveness. Customer identification and verification procedures, as well as procedures regarding the detection and reporting of suspicious activity, should be included as a part of the anti-money laundering program.

3. Employee Training

The training program for employees of the institution should provide both a general awareness of overall anti-money laundering legislation and money laundering issues, as well as more job-specific guidance regarding particular employees' roles and functions in the anti-money laundering program. For employees whose duties bring them in contact with anti-money laundering legislation or possible money laundering activity, training should occur when the employee assumes those duties, with subsequent periodic updates and refreshers.

4. Independent Audit

The institution should conduct periodic independent testing of its program to assess compliance with and the effectiveness of the program, and to assure that the program is functioning as designed. Such testing may be accomplished either by a qualified outside party, or by employees of the institution so long as those same employees are not involved in the operation or oversight of the programme. A written assessment or report should be a part of the review, and any recommendations should be promptly implemented or submitted to the directors of a fund company, general partner of a limited partnership, or trustee of a unit trust for consideration.

5. Compliance Management

The institution should charge an individual (or group of individuals) with the responsibility for overseeing the anti-money laundering program. The person (or group of persons) should be knowledgeable regarding anti-money laundering legislation and money laundering issues and risks, and empowered with full responsibility and authority to develop and enforce appropriate policies and procedures throughout.

6. Financial Services Groups and Anti-Money Laundering Programs

An institution often is part of a large financial services group. These groups may choose to establish an anti-money laundering program that applies to all institutions that they sponsor, operate or advise. Further, large financial services groups that have banks, broker/dealers or insurance companies as their core business may already have in place an anti-money laundering program that applies to all companies within the group. A financial services group may utilize the group's anti-money laundering program, so long as every institution is covered by an anti-money laundering program containing the four elements set forth above. Each institution—through its board of directors, general partner or trustee—should have clear written documentation indicating that it has adopted an anti-money laundering program.

B. CLIENT IDENTIFICATION AND VERIFICATION PROCEDURES

An institution may apply client verification procedures on a risk-sensitive basis. An institution should establish the bases for such risk determinations and should be able to justify its assessments to its regulator.

1. Responsibility for client identification and verification

An institution has a responsibility for verifying the identity of the investor, and the beneficial owner of the investor when it is apparent that an account is beneficially owned by a party other than the investor, and performing more general "know your customer" procedures following a risk-based approach. The general "know your customer" procedures, including obtaining information, such as financial background and business objectives, in order to develop a business and risk profile and to ensure that transactions being conducted are consistent with that profile (including, where necessary, the client's source of funds).

2. Verifying investor identity

Measures to identify and verify the identity of the investor, and the beneficial owner of the investor when it is apparent that an account is beneficially owned by a party other than the investor, to the extent reasonable and practicable, may be determined on a risk sensitive basis depending on the type of investor, business relationship or

transaction, and the types of accounts opened by the institution. This applies to units sold or redeemed by the institution or through any market intermediary. The verification should provide a reasonable basis for an institution to believe that the true identity of the investor is adequately known. Where the risk that an institution will not know the true identity of an investor is higher (*e.g.*, accounts for politically exposed persons or entities with complex structures; accounts for nationals, residents, or entities from countries considered to be non-cooperative or inadequately regulated, etc.), an institution should apply more stringent client identification measures. Investor identification and verification processes should be properly documented in each case, and such records should be kept for at least six years after the business relationship has ended.

3. An institution may rely on documents as well as on non-documentary methods, or a combination of both, in order to identify investors and verify their identity. With respect to natural persons, reliable verification methods could include the following:

- An unexpired government-issued identification evidencing nationality or residence and bearing a photograph or other similar safeguards, such as a driver's license or passport;
- Independently verifying the investor's identity through the comparison of information provided by sources such as public database, or other sources;
- Checking references with other financial institutions;
- Obtaining account statements; and
- Face-to-face meetings; interviews; statements; home visits; references from previous business relationships. With respect to non-natural persons, reliable verification methods could include the following:
- Obtaining proof of incorporation or similar evidence of the legal status of the legal person or arrangement, as well as information concerning the investor's name, the names of trustees, legal form, address, directors, and documents evidencing the power of a person to bind the legal person or arrangement;
- Forming an understanding of the ownership and control structure; and
- Identifying the natural persons with a controlling interest and identifying the natural persons who comprise the management of the legal person or arrangement.

4. With respect to another institution, and/or a fund of funds, an institution need not verify the identity of the underlying beneficial owners of an investing Collective Investing Schemes (CIS) or fund of funds that:

- Is regulated or registered;
- Is based in a jurisdiction that the an institution is satisfied has appropriate anti-money laundering legislation;
- Has in place an anti-money laundering program; and
- Is supervised for, and has measures in place to comply with, CDD requirements.

5. **Timing of identification and verification**

An institution should identify the investor before or during the opening of an account or accepting an investment. An institution should verify identity as soon as possible, before or after the opening of an account or accepting an investment, for purposes of assuring that the risks are effectively managed. In this regard, it is essential not to interrupt the normal conduct of business.

Where the investor's identity has yet to be verified, an institution will need to adopt risk management procedures with respect to the conditions under which an investor may utilise the account or investment prior to verification. These procedures should include a set of measures such as a limitation of the number, types and/or amount of transactions that can be performed, and the monitoring of large transactions being carried out of expected norms for that type of relationship. Where it is not possible after reasonable efforts to verify the identity of an investor, an institution should consider halting transactions or terminating its relationship and also should consider making a Suspicious Activity Report to the appropriate authorities in relation to the investor. It may be appropriate for an institution to consult with its regulator and appropriate law enforcement agencies prior to halting transactions in a particular account or terminating its relationship with any investor.

6. **Potential low risk situations**

As noted above, the identity verification procedures of an institution may be risk-based depending on the type of investor, business relationship, or transaction. Where there are low risks, it may be appropriate for an institution to

apply simplified verification procedures. These procedures, of course, must still be sufficient for the institution to achieve the goal of verification – establishing a reasonable belief that it knows the true identity of its investor.

In the event a broker firm/CDS obtains a confirmation from a bank which maintains a bank account for a client trading through a broker firm, to the effect that, when opening and maintaining the bank account, the bank has followed the KYC and CDD requirements, the broker firm/CDS may at its discretion considering the risk level of the client, waive off the above requirements to verify the source of funds received.

PART II

SPECIFIC RULES FOR THE SECURITIES INDUSTRY

1. Introduction

The broker/dealer firm/market intermediary must obtain sufficient evidence of the identity of any client as soon as reasonably practicable after it has contact with a client.

2. Any broker/dealer firm/market intermediary should not proceed further with the transaction if satisfactory evidence of identity has not been provided unless directed to do so by the Financial Intelligence Unit.
3. Every broker/dealer firm/market intermediary should take reasonable care to make and retain adequate records for 6 years.
4. For the avoidance of doubt, for each transaction the firm should retain a record of;
 - The name and address of its customers;
 - The name and address (or identification code) of its counter party,
 - The investment dealt in, including price and size;
 - Whether the transaction was a purchase or a sale;
 - The form of instruction or authority;
 - The account details and the form in which the funds were paid to the firm (including, in the case of cheques, sort code, account number and name);
 - The form and destination of payment made by the firm to the customer;
 - Whether the investments were held in safe custody by the firm or sent to the customer or to his order, and if so to what name and address;
5. Every broker/dealer firm/market intermediary shall conduct on-going due diligence on the business transactions with the customer to ensure that the transactions are consistent with the firm's knowledge of the customer, the customer's business risk and source of income.
6. Every broker/dealer firm/market intermediary shall report to the Financial Intelligence Unit:-
 - Any act which the firm suspects is preparatory to an offence under the provisions of the Convention on the Suppression of Financing of Terrorism Act No. 25 of 2005; or
 - Any transaction or attempted transaction which the firm has reasonable suspicion that it may relate to the commission of any unlawful activity in terms of the Financial Transactions Reporting Act No. 6 of 2006 and Prevention of Money Laundering Act No. 5 of 2006.
7. Every broker/dealer firm/market intermediary to appoint a Compliance Officer to be responsible for ensuring compliance with the requirements of the Financial Transactions Reporting Act No. 6 of 2006.
8. The Compliance Officer should establish and maintain procedures to
 - Implement the customer identification requirements
 - Implement procedures for record keeping
 - Implement a process of monitoring the customer transactions
 - Implement a system for reporting suspicious activity to the Financial Intelligence Unit
 - Make employees aware of the law relating to money laundering and terrorist financing
 - Screen all persons before hiring them as employees to ensure ML/TF risks are adequately addressed.

PART III**SPECIFIC CUSTOMER IDENTIFICATION INFORMATION REQUIREMENTS IN RELATION TO
SECURITY BROKERS****INFORMATION TO BE SUBMITTED BY APPLICANTS TO OPEN A CDS ACCOUNT****1. Natural Persons (Individuals)****A. Residents**

- a) Full Name.
- b) Nationality.
- c) Occupation.
- d) Permanent Residential Address.
- e) Current Residential Address.(If different from above)
- f) Address for correspondence (if different from Residential Address.)
- g) Proof of residency – copies of any utility bills (Eg: electricity, water, telephone bills etc.) or such other proof.
- h) Copy of National Identity Card (NIC) or Passport (in the event NIC is not available.) If both NIC/Passport is not available a copy of the Driving License should be submitted, together with an Affidavit confirming the fact that both NIC and Passport are not available.
- i) Name, address and copy of NIC/Passport of person/s authorized to give instructions.

B. Non-residents

- a) Full Name.
- b) Nationality.
- c) Occupation.
- d) Permanent Residential Address
- e) Current Residential Address.
- f) Proof of residency – copies of any utility bills (Eg: electricity, water, telephone bills etc.) or such other proof.
- g) Address for correspondence (if different from Residential Address.)
- h) SIERA Account details with proof (where the applicant is a Non Resident.)
- i) Copy of Passport.
- j) Name, address and copy of NIC/Passport of person/s authorized to give instructions.

2. Corporate Bodies

- a) Full name of the Corporate Body (Company/Statutory body/a body established under an Act of Parliament/ Society.)
- b) Registered address.
- c) Address for correspondence (if different from Registered Address.)
- d) Place of Incorporation / place where established.
- e) SIERA Account details with proof (where the applicant is a Non-Resident.)
- f) Names, addresses, National Identity Card/Passport number/s and occupations of Directors. (If the company is listed in a Stock Exchange only the names should be given. Proof of such listing should be submitted in that event)

If the Director/s is/are also a company, the following information on such Director company should be given:

- (i) Name of the company.
- (ii) Date of Incorporation.
- (iii) Place of Incorporation.
- (iv) Registered Address.

If an authorized person is signing the CDS application form on behalf of the applicant company, a copy of the Board Resolution/Power of Attorney authorizing such person to sign on behalf of the Company and a copy of National Identity Card/Passport of such person should be submitted.

- g) Names and addresses of top 10 shareholders/members. (Not applicable if the Company is listed in a Stock Exchange.)
- h) Name of person/s authorized to give instructions with a copy of the Power of Attorney/Board Resolution.
- i) Copies of following documents:
 - (i) Articles of Association or corresponding document.
 - (ii) Certificate of Incorporation or corresponding document.
 - (iii) If a director/s of the applicant is/are also a company Certificate of Incorporation of such company.
 - (iv) Where the applicant is a Non-Resident, a copy of the Certificate of Good Standing issued by the Registrar of Companies/applicable authority where the Company is incorporated.
 - (v) Certified extract of the resolution to open the CDS account (in the alternative, the resolution may be certified in the CDS Account Opening Application itself).

Where the application is titled in the names of the 'Registered Holder/Global Custodian/Beneficiary' and forwarded through a Custodian Bank, a copy of the SWIFT message or similar document issued by the Global Custodian instructing the local Custodian Bank to open the account on behalf of the beneficiary Company should be submitted together with a declaration from the Global Custodian that a Custody arrangement or agreement exists between the Global Custodian and the beneficiary.

- vi) Certificate to commence business. (where relevant.)

3. Funds approved by SEC

- a) Name of the Fund.
- b) Purpose of the Fund.
- c) Place of establishment of the Fund.
- d) Details (name, address, description etc.,) of the Trustee/Manager of the Fund .
- e) If the Trustee/Manager is a company, date of incorporation, place of incorporation, registered address of such Trustee/Manager.
- f) Copies of the documents relating to the establishment and management of the Fund (eg:Prospectus/Trust Deed/ Management Agreement/Bankers/ Auditors).
- g) Copy of the Letter of Approval of the Fund issued by the Supervisory Authority of the relevant country.
- h) Copy/copies of the relevant Custody Agreement/s.
- i) Details of Beneficiaries.

4. Certification

All supporting documents to be submitted to the CDS should be certified or attested or authenticated for purposes of validating by persons mentioned under (a) or (b) below. Such certification should state that the document certified is a true copy.

a) Certification for Non Resident Applicants

- 1) By the Company Registry or similar authority, where the documents were originally issued (applicable for Corporate Bodies), or
- 2) By a Sri Lankan diplomatic officer or Sri Lankan consular officer in the country where the documents were originally issued, or
- 3) By a Solicitor, Attorney-at-Law, Notary Public, practicing in the country where the applicant resides, or
- 4) Custodian Bank, or

- 5) Global Custodian – The Custodian Bank should certify the authenticity of the signature of the Global Custodian—or
- 6) Broker. (Applicable only in respect of Individuals.)

b) Certification for Resident Applicants

- 1) Registrar General of Companies or the Company Secretary (applicable in respect of Corporate Bodies), or
- 2) Attorney-at-Law / Notary Public, or
- 3) Broker, or
- 4) Custodian Bank.

NOTE:

The person certifying should place the signature, full name, address, contact telephone numbers and the official seal (Not applicable for Brokers, Custodian Banks and Global Custodians).

PART IV

THE FOLLOWING DECLARATIONS SHOULD BE SUBMITTED BY APPLICANTS TO OPEN A CDS ACCOUNT

- A declaration that the securities to be purchased through the CDS Account to be opened would be for the benefit of the applicant only and for no other beneficial owner/s. In the alternative, if the applicant is acting in the capacity of a Trustee, a declaration that the account is opened for the benefit of beneficiaries and declares the names, addresses and the nationalities, where the number of beneficiaries is up to three (3) only. If above such number, a declaration that information such as names, addresses & nationality pertaining to the ultimate beneficiaries of the account, are maintained with the applicant and an undertaking to release such information to CDS at any time upon request by the CDS.[CDS (1)A/CDS 2(A)]
- A declaration that the funds to be invested through the CDS will not be funds generated from any money laundering activity nor funds generated through the financing of terrorist or any other illegal activity. [CDS 1(A)/CDS 2(A)]
- A declaration that all the information given is true and accurate, and that no alteration, modification was made to the said information. [CDS 1(A)/CDS 2 (A)]
- A declaration that in the event of a variation of the information submitted to CDS, the applicant would inform the CDS, in writing, within 14 days of such change. [CDS 1(A)/CDS 2(A)]
- A declaration as set out in Appendix A below.

**Appendix A
Declaration**

I/We declare that I/we have not been banned and/or rejected and /or suspended by any criminal/civil tribunal or administrative authority in Sri Lanka or in any other country in connection with the following offences:

- Engaging directly or indirectly in any transaction in relation to any property which is derived or realized directly or indirectly, from any unlawful activity or from the proceeds of any unlawful activity as defined by the Financial Transactions Reporting Act No. 6 of 2006;
- Receiving, possessing, concealing, disposing, of or bringing into Sri Lanka or into any other country, or for investing in Sri Lanka or in any other country, any property which is derived or realized, directly or indirectly, from any unlawful activity or from the proceeds of any unlawful activity referred to above; or
- Any other offence which has been defined as an offence under the Prevention of Money Laundering Act No.5 of 2006 and any amendment thereto or any similar legislation in any other part of the world.

I/We hereby further declare that I/We am/are person(s) of good standing with no record of criminal convictions in relation to the offences stated above, in Sri Lanka or in any other country.

I/We hereby further declare that I/We or any persons(s) associated with me/us and/or any entity connected to me/us (as a partner, shareholder, director) have against me/us or persons connected and/or associated as aforesaid any convictions/

pending criminal proceeding in Sri Lanka or in any other part of the world except the following (give detailed description of any pending litigation);

-
-
-
-

I/We declare that my/our application and other relevant documentation to open a CDS account has not been refused or any business relationship has not been declined previously by any other Participant Custodian, Bank Firm of the CDS/CSE.

I/We further declare and agree that, should the CSE/CDS determine any statements made by me/us herein to the contrary, (or any such matter through publicly available information or otherwise) which would in the opinion of the CSE/CDS be detrimental to the CDS as an institution having to comply with the laws/regulations of Sri Lanka pertaining to transactions of its account holders or parties connected to such account holders, the CDS is hereby authorized to unilaterally terminate all depositary and such other services connected to me/us and recover related costs or other expenses pertaining to this account.

PART V

SUSPICIOUS TRANSACTIONS REPORT (STR) FOR SECURITIES INDUSTRY IN TERMS OF THE FINANCIAL TRANSACTIONS REPORTING ACT NO. 6 OF 2006

Please note that to be accepted as a STR, this form must be completed in all material detail.

- a. This report is made pursuant to the requirement to report suspicious transactions under the Financial Transactions Reporting Act No.6 of 2006 (FTRA).
- b. Under section 12 of the FTRA, no civil, criminal or disciplinary proceedings shall be brought against a person who makes a report unless it was made in bad faith.

In accordance with Section 7 of the Financial Transactions Reporting Act No. 6 of 2006, the reporting entity is obliged to report suspicious transactions as soon as is practicable but no later than 2 working days to the Financial Intelligence Unit

.

Please take note of the following prior to completing the Suspicious Transaction Report ("STR"):

- **Provide** a clear and concise description of the STR, and **state** all available information.
- **Document** in detail why the **transaction** is considered extraordinary, irregular or **suspicious**.
- **Provide** supporting documents where it is necessary to explain the STR.
- **Indicate** if the potential violation is an initial report or if it relates to a previous **transaction** or transactions reported.
- **Complete** this STR in Block letters.
- Take reference to the explanatory notes at page 15.

**SUSPICIOUS TRANSACTIONS REPORT (STR) FOR SECURITIES
INDUSTRY IN TERMS OF THE
FINANCIAL TRANSACTIONS REPORTING ACT NO. 6 OF 2006**

- a. This report is made pursuant to the requirement to report suspicious transactions under the Financial Transactions Reporting Act No.6 of 2006 (FTRA).
- b. Under section 12 of the FTRA, no civil, criminal or disciplinary proceedings shall be brought against a person who makes a report unless it was made in bad faith.

Name of the Reporting Company :

Date of Reporting :

Details of Disclosing Organization

Name of Organization	Registered Address

Person Subject of Disclosure:

Full Name	NIC/Passport Number/Address

OR Company Subject of Disclosure:

Company Name	Registered Address
Other information not covered above	

Financial Summary Overview:

Institution Name	

Financial Summary Details:

Date	
Value	

Date	
Value	

Associated Person (with Subject of Disclosure):

Full Name	NIC/Passport Number/Address

OR

Associated Company (with Subject of Disclosure):

Company Name	Registered Address
Other information not covered above	

Generic Reporting Form

Reason for suspicion

<div style="border: 1px solid black; height: 280px; width: 100%;"></div>
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Use additional sheets if there are further details to be shown.

PART E: DETAILS OF REPORTING OFFICER & COMPLIANCE OFFICER36. Date of Reporting: 2 0 0

D D M M Y Y Y Y

Reporting Officer:

.....

Name:

Name of Compliance Officer

Designation:.....

Address:

Contact No. E-mail..... Fax

.....

Signature of Compliance Officer**PART E: FOR FIU OF SRI LANKA USE ONLY**

Receiving Officer

Date Received: 2 0 0

D D M M Y Y Y Y

STR No: Date of Acknowledgement: 2 0 0

D D M M Y Y Y Y

FIU ACKNOWLEDGEMENTReceived by the Financial Intelligence Unit of the Central Bank , STR No. dated 200

.....

Director/FIU

GENERAL INSTRUCTIONS

Under the **FINANCIAL TRANSACTIONS REPORTING ACT, NO. 6 OF 2006 (FTRA)**, every reporting institution shall furnish details of suspicious transactions defined in Section 7 (1) of the FTRA.

- 7 (1) Where an Institution: -
- a) has reasonable grounds to suspect that any transaction or attempted transaction may be related to the commission of any unlawful activity or any other criminal offence; or
 - b) has information that it suspects may be relevant —
 - (i) to an act preparatory to an offence under the provision of the Convention on the Suppression of Financing of Terrorism Act, No. of 2005.
 - (ii) to an investigation or prosecution of a person or persons for an act constituting an unlawful activity, or may otherwise be of assistance in the enforcement of the Money laundering Act. No.5 of 2006 and the Convention on the Suppression of Terrorist Financing Act, No. 25 of 2005.

How to submit

Every institution must submit this form to the Director, FIU only through the Compliance Officer of the reporting institution designated under the FTRA. In urgent cases, the form should also be sent by fax:

Address: Director
Financial Intelligence Unit
Central Bank of Sri Lanka
30, Janadhipathi Mawatha
Colombo 1.
Fax. 94 11 2477692

FINANCIAL SUMMARY OVERVIEW:

- This is the snapshot of the account (account opening date, account closing date, if relevant) that may indicate the priority of the investigation.
- The snapshot of the account turnover may indicate the importance of the report too.

FINANCIAL SUMMARY DETAILS:

- As indicated above, the date of transaction in relation to the date of report and in relation to the date of receipt within the FIU can provide important inputs to the FIU.
- Counterparty information can help FIU to make comparative analysis with similar counterparties.
- Once again FIs should be encouraged to provide more reports.

Payment and Settlement Systems Act, No. 28 of 2005

REGULATIONS made by the Minister of Finance and Planning under Section 43 of the Payment and Settlement Systems Act, No. 28 of 2005, read with Sections 11, 17 and 20 (2) of the aforesaid Act and with paragraph (2) of Article 44 of the Constitution.

MAHINDA RAJAPAKSHA
President and Minister of Finance and Planning

Colombo,
12 June, 2007.

REGULATIONS

1. These Regulations shall be cited as the Money, Payment, Clearing and Settlement Service Providers Regulations, No. 01 of 2007.
2. The Central Bank of Sri Lanka (CBSL) shall be the supervisory, regulatory and monitoring authority for all service providers and any category of service providers including any person who;
 - i. provides money services, or
 - ii. operates a payment system, or
 - iii. operates a clearing and settlement system, or
 - iv. provides or operates any one or more of the services above in combination as a single entity or in a subsidiary or an affiliate or in an agency capacity.
3. (1) In the exercise of the powers conferred upon it by the Payment and Settlement Systems Act, No. 28 of 2005 and these Regulations, the CBSL shall issue directives, directions, rules, instructions, guidelines and definitions to service providers or any category of service providers as hereafter prescribed.
(2) Without any prejudice to the generality of the above provisions the CBSL shall hereby be authorized to issue directives, directions, rules, instructions and guidelines for proper and efficient implementation and enforcement of the following:
 - a) to provide for the conditions, requirements and standards for money, payment, clearing and settlement services to provide for the protection of the customers and the integrity and development of payment systems in Sri Lanka;
 - b) to require the registration or licensing of money, payment, clearing and settlement service providers and any category of service providers and the procedure to be followed for such registration or licensing, to specify the conditions and requirements for such registration or licensing and to provide for the procedure to be followed in circumstances under which such license or registration may be revoked by the CBSL;
 - c) to provide for the levying of a license fee and prescribing the amount of such license fee and other charges for the registration of any service provider or category of service providers and any amendment to such fee or charges;
 - d) to specify the procedures required for the regulation, supervision and monitoring of money, payment, clearing and settlement service providers;
 - e) to specify the manner in which the conditions, requirements, guidelines, procedures, measures and standards provided for in Section 17 of the Payment and Settlement Systems Act and these Regulations shall apply in respect of any person who carries out or is authorized to carry out any part of a money, payment, clearing and settlement service on behalf of a service provider;
 - f) to specify the conditions and requirements under which persons including those providing money transmission services may participate in a payment system or maintain accounts and deposits in the CBSL;
 - g) to specify the prudential requirements relating to money, payment, clearing and settlement service providers, including accounting and reporting requirements;
 - h) to specify the requirements, standards and guidelines on corporate matters of service providers including matters with regard to their form of incorporation or organization, administration, management, governance, control, capital adequacy and other capital requirements, ownership structure, quality of shareholders and administrators and business and investment powers;
 - j) to specify the requirements, standards and guidelines for service providers designed to facilitate their inspection by the CBSL, including requirements, standards and guidelines regarding the collection, maintenance of record and reporting to the CBSL the information on matters as specified including information about their customers or participants and in relation to transactions or any category of them, in such format and detail as may be specified;
 - k) to specify the measures necessary for the protection of customers and participants or any category of them, and particularly, to specify disclosure requirements and contract terms of the money services, service providers and the customers and of payment, clearing and settlement services, service providers, systems, their participants and the customers;

- l) to impose restrictions, limitations or prohibition on the use of payment orders from designated categories of accounts and persons and the specification of the conditions governing such use;
 - m) to impose restrictions on the liability of individuals by specifying restrictions and pre-conditions for such liability, in connection with payment transactions to or from accounts that are used primarily for personal or household and non-business purposes;
 - n) to determine standards by which the performance of duties set out under the Payment and Settlement Systems Act, No. 28 of 2005 or these Regulations may be measured.
4. (1) The CBSL shall prescribe, from time to time, the service providers or category of service providers subject to the supervision, regulation and monitoring by the CBSL.
- (2) These Regulations and any subsequent directives, directions, rules, instructions, guidelines and definitions issued by the CBSL in accordance with the provisions of Payment and Settlement Systems Act, No. 28 of 2005 or as authorized by these regulations shall be binding on all service providers and on any category of service providers as specified under sub-regulation (1) of Regulation 4 above.
- Provided that the application of any directive, direction, rule, instruction or guideline may be exempted on any service provider or any category of service providers prescribed as exempted from same by the CBSL.
5. Any person who intends to act as a service provider providing money services or operating a payment system, a clearing and settlement system or provides or operates any one or more of the services above in combination as a single entity or in a subsidiary, an affiliate or agency capacity shall be required to furnish such information or documentation as the CBSL may consider necessary.
6. Nothing in these Regulations shall limit, contradict or contravene the provisions of Section 44 of the Payment and Settlement Systems Act, No. 28 of 2005.
7. In the event of any inconsistency prevailing between the Sinhala and Tamil texts of these Regulations the Sinhala text shall prevail.

DEFINITIONS

For the purpose of these Regulations the CBSL may from time to time define and publish the meaning of the following terms in the Government Gazette.

“CBSL” means the Central Bank of Sri Lanka established under the Monetary Law Act, No. 58 of 1949 (Cap 422);

“Clearing system” shall have the same meaning as defined in Section 2 of the Payment and Settlement Systems Act, No. 28 of 2005;

“Clearing and settlement system” shall have the same meaning as defined in Section 32 of the Payment and Settlement Systems Act, No. 28 of 2005;

“Issuer” means any person, acting alone or under an arrangement with another person or persons, who undertakes to be responsible for the payment obligations in respect of a payment instrument resulting from the user being issued with or using the payment instruments;

“Money” shall have the same meaning as defined in Section 18 of the Payment and Settlement Systems Act, No. 28 of 2005;

“Money services” shall have the same meaning as defined in Section 18 of the Payment and Settlement Systems Act, No. 28 of 2005;

“Monetary value” shall have the same meaning as defined in Section 18 of the Payment and Settlement Systems Act, No. 28 of 2005;

“Operator” means any person acting alone or under an arrangement with another person or persons, responsible for the rules, procedures and operations of money services, payment, clearing and settlement systems or any one or more of the services above in combination as a single entity or in a subsidiary, an affiliate or agency capacity, and shall exclude such persons as may be prescribed by the CBSL;

“Payment system” shall have the same meaning as defined in Section 18 of the Payment and Settlement Systems Act, No. 28 of 2005;

“Person” shall have the same meaning as defined in Section 18 of the Payment and Settlement Systems Act, No. 28 of 2005;

“Prescribe” means prescribed by publishing in the Gazette, and a power to prescribe includes the power to make separate provisions for identified persons, money services, payment systems, clearing and settlement systems or payment instruments;

“Security” shall have the same meaning as defined in Section 10 of the Payment and Settlement Systems Act, No. 28 of 2005;

“Service provider” shall have the same meaning as defined in Section 18 of the Payment and Settlement Systems Act, No. 28 of 2005 and shall include an issuer of a payment instrument; a manufacturer of a payment instrument; an acquirer; a manufacturer of terminals; an owner of terminals; an operator of terminals; an owner of a switch; an operator of a switch; an owner, operator or maintenance operator of infrastructure relating to money services, payment, clearing and settlement systems including communication network, software, hardware, disaster recovery sites; an operator of money services; a payment system operator; a clearing system operator; a settlement system operator; a clearing and settlement system operator; and settlement agent or any authorized agent or sub-agent of the above service providers; or any person or an employee of any person acting in the agency capacity for any service provider;

“Settlement system” shall have the same meaning as defined in Section 2 of the Payment and Settlement Systems Act, No. 28 of 2005;

“Specify” means specify in writing, and a power to specify includes the power to specify differently for different persons, payment systems or payment instruments, or for different classes, categories or descriptions of persons, payment systems or payment instruments.

General Direction No. 01/2007

Payment and Settlement Systems Act, No. 28 of 2005

General Direction made by the Monetary Board of the Central Bank of Sri Lanka under Section 44 of the Payment and Settlement Systems Act No. 28 of 2005.

Dr. Ranee Jayamaha
Deputy Governor
Central Bank of Sri Lanka

Colombo
14 November, 2007

GENERAL DIRECTION ON THE PARTICIPATING INSTITUTIONS' SERVICE NORMS AND STANDARD TIMES FOR ACCEPTING CHEQUE DEPOSITS FROM CUSTOMERS AND CREDITING CHEQUE PROCEEDS TO CUSTOMERS' ACCOUNTS UNDER THE CHEQUE IMAGING AND TRUNCATION SYSTEM

The Cheque Imaging and Truncation System, which was introduced in May 2006 has substantially increased the speed of cheque clearing process, reducing cheque realization time span to one day (T+1, where T is the day of receiving the cheque for clearing at LankaClear Pvt. Ltd. or its regional centers and 1 is the following business day). But it was observed that, due to numerous reasons some bank branches have not been able to adhere to T+1.

2. Having considered the public policy objective of facilitating the customer to receive cheque proceeds within T+1, the National Payment Council at its meeting held on August 9, 2007, expressed the view that the Central Bank of Sri Lanka (CBSL) shall mandate all licensed commercial banks (LCBs) to publish in the newspapers or display in the bank branches a notice indicating the cut-off times for cheque deposits:
 - (i) to facilitate T+1; or
 - (ii) to facilitate crediting proceeds of cheques indays (indicate number of days), where (i) above is not possible; and

- (iii) the number of days a particular bank would take to credit proceeds of the cheques deposited at off site ATMs etc., on realization.

Accordingly, this General Direction on the Participating Institutions' Service Norms and Standard Times for Accepting Cheque Deposits from Customers and Crediting Cheque Proceeds to Customers' Accounts under the Cheque Imaging and Truncation System is issued to all participating institutions (PIs) of the Cheque Imaging and Truncation System, in terms of Section 44 of the Payment and Settlement Systems Act No. 28 of 2005. This General Direction will come into effect from December 03, 2007.

3. The PIs shall adhere to the following minimum cut-off times for collection of cheque deposits at bank counters and in collecting boxes and shall present such collected cheques to LankaClear for clearing on the same business day (T):

Location of the Bank Branch	Minimum Cut-off Time for Accepting Cheque Deposits on the Business Day (T)
(i) In the Colombo District	1.30 p.m.
(ii) In the districts other than the Colombo District	12.00 noon

4. In the normal course as per the inward return data/report provided by the LankaClear, PIs shall credit proceeds of cleared cheques to customers' accounts on the next business day (i.e. on T+1, the day that the settlement clearing takes place). Each PI that has Automated Teller Machines (ATMs) shall credit proceeds of cleared cheques to customers' accounts enabling the customers to withdraw funds on the next business day through ATMs up to the limit stipulated by the PI.
5. Each PI shall formulate procedures and norms on: cheque collection; crediting cheque proceeds to customers' accounts; and the modalities for handling customer complaints. Such procedures and norms shall ensure that the obligations of the PIs to the customers and the rights of the customers are established and observed in practice.
6. The PIs shall ensure that:
- wide publicity is given to the contents in Paragraph 5 and times of cheque collection and crediting of customers' accounts by:
 - displaying prominently on the notice board in the banking hall in their branches and cheque collecting boxes, so that it attracts the customers' attention as well as that of the employees for adherence; and
 - printing a message on the monthly current account statement; and
 - posting it on their web-sites before December 31, 2007.
 - any changes to procedures and norms or time of cheque collection and crediting of customers' accounts are duly informed to the customers;
 - procedures are clearly laid down to assess staff accountability for any delays. In order to take necessary action to improve customer services, a special register shall be introduced to record: the cheques collected before the cut off time and not sent for clearing on the same business day; cheques of which the proceeds not credited on T+1; and reasons for delays;
 - periodic evaluations on the compliance with this Direction are conducted on half-yearly basis with a view to upgrade the quality of customer services and submit a half-yearly report to the Director, Payments and Settlements Department of CBSL, within two weeks from the end of the relevant period; and
 - the grieved parties have a right to approach authority designated by the PI for handling the grievances.
7. The cheque collection procedures, norms and times of cheque collection and crediting of customers' accounts of each PI shall be published in Sinhala, Tamil and English newspapers in clear print and conveyed to the Director, Payments and Settlements Department of CBSL before December 31, 2007.
8. Further, each PI shall also review their existing arrangements for cheque collection and take an effort to extend the cut off time for cheque collection and reducing the time required for crediting proceeds to customers' accounts after receiving the Cheque Return Notification (CRN) and/or inward return data reports of the settlement clearing.

2 July 2007

Ref: 34/07/029/0001/001**Circular No.: RTGS/03/2007***To: All participants of LankaSettle System***CHANGE OF NAME OF SEYLAN BANK LIMITED**

As Seylan Bank Ltd. has changed its name to Seylan Bank PLC the static data of LankaSettle System will be changed as indicated below with effect from July 04, 2007.

- (i) Changing the participant organization name of Seylan Bank Ltd to Seylan Bank PLC; and
- (ii) Changing the account name of Seylan Bank Ltd. from Seylan Bank Settlement Acct to Seylan Bank PLC Settl Acct.

The SWIFT BIC of the Bank will remain unchanged.

C. Premaratne
Superintendent of Public Dept

K.R.M. Siriwardhane
Director/Payments and Settlements

10 October 2007

Ref: 34/07/029/0001/001**Circular No.: RTGS/05/2007***To: All participants of LankaSettle System***CHANGE OF NAMES OF LANKASETTLE PARTICIPANTS**

In terms of the provisions of the companies Act No. 07 of 2007, National Development Bank Limited and Pan Asia Banking Corporation Limited have been registered as Public Limited Companies under the following names,

- (i) National Development Bank PLC
- (ii) Pan Asia Banking Corporation PLC

Accordingly the static data of LankaSettle System will be changed as indicated below with effect from October 12, 2007.

Participant organization name	Account name
1. National Development Bank PLC	National Develop Bank PLC SettlAcct
2. Pan Asia Banking Corporation PLC	Pan Asia Banking Corp PLC SettlAcct

The SWIFT BIC of the above Banks will remain unchanged.

C. Premaratne
Superintendent of Public Dept

K.R.M. Siriwardhane
Director/Payments and Settlements

Ref: 34/07/029/0001/001

27 December 2007

Circular No: RTGS/07/2007

To: All Participants of the RTGS System

**CHANGE OF BIC OF THE STANDARD CHARTERED
BANK (PAKISTAN) LIMITED.**

You are hereby informed that the SWIFT Bank Identifier Code (BIC) of the Standard Chartered Bank (Pakistan) Limited will be changed from 'UNBLKLCXXX' to 'SCBLPKXULK' with effect from 29.12.2007.

2. The technical procedure in effecting the above change in the RTGS System would involve the following:
 - (i) Identification of the Standard Chartered Bank (Pakistan) Limited in the RTGS System would be changed from 'UNBL' to 'ULK' with effect from 31.12.2007; and
 - (ii) Identification of the RTGS Settlement Account of the Standard Chartered Bank (Pakistan) Limited would be changed from 'UNBLKLCXXX010004413' to 'SCBLPKXULK010004413' with effect from 31.12.2007.
3. When the process of changing the static data of the Standard Chartered Bank (Pakistan) Limited. in the RTGS System takes place, you would observe that:
 - (i) The Settlement Account No SCBLPKXULK010004413 indicated against the Standard Chartered Bank (Pakistan) Limited would appear in the RTGS System with suspended status only on 28.12.2007, since the said account will not be operative on that date; and
 - (ii) The Settlement Account No. UNBLKLCXXX010004413 of the Standard Chartered Bank (Pakistan) Limited would appear in the RTGS System with suspended status only on 31.12.2007. The suspended status is given to the said account on that date, for the reason that the said account will not be operative with effect from the said date and the operative Settlement Account of the Standard Chartered Bank (Pakistan) Limited in the RTGS System will be 'SCBLPKXULK010004413'.
4. Any payment instruction directed to BIC 'UNBLKLCXXX' to be effected after 31.12.2007 will automatically be rejected by the RTGS System.

R. B. Weerasinghe
Deputy Superintendent/Public Debt

K.B. Dissakaruna
Addl. Director/Payments and Settlements

Public Debt Department
23 January 2007

Circular No: SSSS/01/2007

To: All participants of the LankaSettle System

AMENDMENT TO LANKASETTLE SYSTEM RULES, AUGUST 2003

You are hereby informed that the Rule 5.4 of Volume 3 of LankaSettle System Rules issued in August 2003 is amended by inserting the Sub-Rule 5.4A.

Accordingly, Sub-Rule 5.4A, as given below, is inserted in between Rule 5.4 and Rule 5.5 of Volume 3 of LankaSettle System Rules, with effect from February 02nd, 2007.

“ 5.4.A. Recording of Repositioning through Central Bank of Sri Lanka Wide Area Network (CBSLNet)

However, Overnight Customer Repo Repositioning transactions of a value which is Rs.2 million or below or such amount as may be decided by the Bank from time to time shall be recorded through the CBSLNet subject to the practices with regard to the operation of CBSLNet as reflected in the relevant System Rules, Operating Instructions that will be issued by the Bank from time to time. Any Overnight Repo Repositioning transaction, the value of which is above Rs.2 million or any such amount as may be decided by the Bank from time to time shall be recorded using SWIFT messaging system.”

Mrs. C. Premaratne
Superintendent of Public Debt

Public Debt Department
23 January 2007

Circular No: SSSS/02/2007

To: All participants of the LankaSettle System

CENTRAL BANK OF SRI LANKA WIDE AREA NETWORK (CBSLNET)
BASED APPLICATION TO RECORD OVERNIGHT CUSTOMER REPO
REPOSITIONING TRANSACTIONS INVOLVING
GOVERNMENT SECURITIES

You are hereby informed that the Central Bank of Sri Lanka (CBSL) has decided to allow participants of LankaSettle to record Overnight Customer Repo Repositioning transactions of LankaSecure through the Wide Area Network of the Central Bank of Sri Lanka (CBSLNet), and accordingly amendments to the System Rules of the LankaSettle has been made as per the Circular No. SSSS/01/2007 dated 23rd January 2007. The facility will be available with effect from 2nd of February, 2007. Operating Instructions applicable for participants of the above scheme are given below.

Operating Instructions

1. This facility will accommodate transactions relating to Overnight Customer Repo Repositionings in which, the face value is Rs.2 million or below. Transactions exceeding a face value of Rs.2 million, will not be accepted by the system. Participants should use SWIFT for Repo transactions that exceeds Rs. 2 million. However there is no restriction to participants to use SWIFT for overnight Repo transactions where the face value is Rs. 2 million or below.
2. Transfers of securities are allowed only from 8.00 a.m. to 4.00 p.m. on valid LankaSecure business days and any allowed transaction entered through the CBSLNet after 4.00 p.m. will not be settled.
3. Creation of a security transfer has to be done by one officer and it has to be authorized by another. CBSL will not receive security transfer instructions until a transaction is authorized.
4. Security transfer requests will be uploaded to the LankaSecure for settlement at 3.00 p.m. and 4.00 p.m. on each business day.
5. New balances will be available to participants only after the particular batch of transactions is loaded and settled in the LankaSecure.
6. Before a transaction is settled, an authorized officer of the participating institution is able to cancel the transaction if required, through the existing browser workstation.
7. Once a transaction is settled in the LankaSecure, it is irrevocable.
8. All unsettled repositioning transactions are cancelled by the system at the end of the day and CBSL is not responsible for such cancellations.
9. In a situation where the CBSLNet facility is not available due to a technical or a communication failure, participating institutions should use their SWIFT system to make above Repo transactions. CBSL would not take the responsibility for any losses that might result in due to failures of CBSLNet.
10. A nominal fee chargeable for providing this trade input facility will be notified later.
11. Once this system is in operation, all transactions relating to Customer Repo Repositionings must be recorded in the Central Depository System (CDS) of LankaSecure.
12. The system has a facility to transfer securities between any type of account. However, participants are advised to make repositioning between OWN, CSL, CRE, CRR, CRP and REP account types described in the System Rules of the LankaSettle only.
13. Penalties for unrecorded transactions to be decided based on a formula calculated by the CBSL, which will be notified later.

Mrs. C. Premaratne
Superintendent of Public Debt

Public Debt Department
07 September 2007

Circular No : SSSS/03/2007

To : *All CEOs of Licensed Specialized Banks*

**APPOINTING LICENSED SPECIALIZED BANKS (LSBS) AS DIRECT PARTICIPANTS AND DEALER
DIRECT PARTICIPANTS IN THE LANKASETTLE SYSTEM IN TERMS OF SECTION 8(1) OF THE
LOCAL TREASURY BILLS ORDINANCE AND 21C(2) OF THE
REGISTERED STOCKS AND SECURITIES ORDINANCE**

You are hereby informed that the Central Bank of Sri Lanka (CBSL) has decided to allow all LSBs to apply for Direct Participant (DP)/Dealer Direct Participant (DDP) status in the LankaSettle. LSBs can apply for Direct Participant/ Dealer Direct Participant status with effect from 7th September, 2007. The selection criteria for appointment and Terms and Conditions applicable for LSBs are given below.

1. Criteria for Selection

- (a) Criteria for selection of LSBs as DPs and DDPs is based on;
 - (i) Financial soundness of the LSB
This is measured by using two year averages of following ratios relating to applicant LSB and LSB sector average is considered as the benchmark for comparison.
 - Regulatory capital/Risk Weighted Assets(CAR)
 - Gross NPL Ratio
 - Net NPL Ratio
 - Statutory Liquid Assets Ratio
 - Return on Equity
 - Return on Assets
 - Staff Cost Ratio (Personal expenses/Operating expenses)
 - Operating Cost to Net Income Ratio (Efficiency Ratio)
 - (ii) Local Rating Status
Applicant LSB should obtain a rating from an acceptable rating agency (Fitch Ratings Ltd. Lanka Rating Agency or any International Rating Agency).
 - (iii) Availability of Internal IT Infrastructure at a satisfactory level to the CBSL.
 - (iv) Availability of Business Continuity Plan for Real Time Gross Settlement (RTGS)/Scripless Securities Settlement System (SSSS) participation and business strategy for next 5 years which are acceptable to the CBSL.
 - (v) The ability of LSB to establish IT communication infrastructure in compliance with CBSL requirement to connect the national payment system. Following are the minimum requirements.
 - SWIFT connectivity
 - CBSL WIDE AREA NETWORK connectivity
 - Possession of required knowledge and experience to carry out the IT related activities
- (b) The Score Card method developed by the CBSL on the above criteria is used to assess the eligibility of LSBs to appoint as DPs and DDPs.
- (c) In addition to the criteria mentioned above, the CBSL will consider the management quality of the LSB and its track record in selecting LSBs as DPs or DDPs, specifically the operational risks and risk mitigating measures adopted by the LSBs.
- (d) However, the CBSL has the discretion to consider any other necessary/relevant factors whenever it may think necessary for appointing an LSB as a DP or DDP.
- (e) A Selection Committee, appointed by the CBSL will assess the eligibility of LSBs as DPs and DDPs.

2. Terms and Conditions

Selected LSBs will be treated as DPs/DDPs in the RTGS and SSSS subject to the conditions set out herein.

- (a) Selected LSB is provided with a securities settlement account and a RTGS settlement account subject to rules and regulations applicable to DPs/DDPs under Registered Stocks and Securities Ordinance (RSSO), Local Treasury Bills Ordinance (LTBO), Monetary Law Act (MLA) and LankaSettle System Rules.
- (b) Selected LSB is provided with Intra-Day Liquidity Facility of the CBSL subject to the terms and conditions as may be decided by the CBSL from time to time.
- (c) CBSL has the sole authority to supervise activities relating to RTGS and SSSS of selected LSBs in terms of LTBO, RSSO, MLA and Payment and Settlement Systems Act.

Mrs. C. Premaratne
Superintendent of Public Debt

Public Debt Department
28 September 2007

Circular No: SSSS/04/2007

To: All participants of the LankaSettle System

AMENDMENTS TO LANKASETTLE SYSTEM RULES ISSUED IN AUGUST 2003

You are hereby informed that the Rule 2.2 of Volume 3 of LankaSettle System Rules issued in August 2003 is replaced to read as follows with effect from 01 October 2007.

(a) The Rule 2.2 of volume 3 of LankaSettle System Rules issued in August 2003 is replaced by incorporating the non recording transaction charges to read as follows:

2.2 Custodial Responsibilities

Dealer Direct Participants shall comply with applicable law, regulations and directions issued by the Central Bank in the conduct of their business as a Dealer Direct Participant.

Dealer Direct Participants act as custodians for their Customers in LankaSecure. This custodial role includes the following responsibilities:

- 2.2.1 to promptly and accurately record the name, address and National Identity Number, Company Registration Number or other identifying number approved by the Central Bank of their Customer in LankaSecure when the Customer obtains legal ownership of a security;
- 2.2.2 To promptly and accurately record in LankaSecure ownership or any change of ownership or owner details of a security within their Securities holdings and in the event of a failure to record the said transaction details, the Central Bank may in its sole discretion impose a non-recording transaction charge on the Dealer Direct Participant (DDP). Without prejudice to the generality of the foregoing, the Central Bank may take the following steps.
 - 2.2.2.1 For the 1st instance of non-recording of transaction -severe warning
 - 2.2.2.2 For the 2nd instance of non-recording of transaction - Rs. 5,000/- per transaction or 0.5% of the value of the transaction (face value) whichever is higher.
 - 2.2.2.3 For the 3rd instance of non-recording of transaction - Rs. 10,000/- per transaction or 1% of the value of the transaction (face value) whichever is higher.
 - 2.2.2.4 In the event of repeated non recording of transactions, Central Bank may suspend forthwith the DDP status of a licensed commercial bank and suspend the primary dealer status of a primary dealer as appropriate for a period of time determined by the Central Bank of Sri Lanka.

- 2.2.3 The amounts so charged shall be debited from the Settlement Account on the next business day of the decisions taken by the Central Bank and shall be credited to the Central Bank. If sufficient funds are not available in the Participants accounts, then it shall pay the non-recording transaction charges within 3 business days of the date of notice of the decision of the Central Bank.
- 2.2.4 Ten percent (10%) of each charge so credited shall be deducted as an administrative charge by the Central Bank. The balance shall be available for utilisation for training of the staff of the banks and primary dealers and shall be paid for such purpose upon an application being made by the Sri Lanka Bank's Association (Guarantee) Ltd. and Association of Primary Dealers to the Central Bank.
- 2.2.5 Any non-recording charge imposed shall not be in substitution or derogation of, or preclude the exercise by the Central Bank of any right or claim which the Central Bank has or is entitled to any action, suit or proceeding in a court of law arising from the failure of any Participant to record ownership or any change of ownership or owner details of a security within its Securities holdings.
- 2.2.6 To account and make payment to their customers of any interest or maturity proceeds due to them in accordance with directions that may be issued in this regard; and
- 2.2.7 To effect transactions on behalf of their customers in accordance with instructions received from customers, provided that such transactions are legal and do not place the Participant in breach of these System Rules.
- Dealer Direct Participants must comply strictly with instructions of a customer in transferring customer securities.

Mrs. C. Premaratne
 Superintendent of Public Debt

Public Debt Department
 28 September 2007

Circular No: SSSS/05/2007

To: All participants of the LankaSettle System

**CENTRAL BANK OF SRI LANKA WIDE AREA NETWORK (CBSLNET) BASED
 APPLICATION TO RECORD CUSTOMER REPOSITIONING TRANSACTIONS
 INVOLVING GOVERNMENT SECURITIES**

You are hereby informed that the Central Bank of Sri Lanka (CBSL) has decided to allow participants of LankaSettle to record both Customer Repo Repositioning transactions (overnight and term repos up to one month) and Customer Outright Repositioning transactions through the Wide Area Network of the Central Bank of Sri Lanka (CBSLNet). Accordingly, amendments to the System Rules of the LankaSettle have been made as per the Circulars No. SSSS/04/2007 and SSSS/06/2007 dated 28 September, 2007. The facility will be available with effect from 01 October, 2007. Operating Instructions applicable for participants of the above scheme are given below.

Operating Instructions

1. This facility will accommodate transactions relating to Customer Repo Repositioning (overnight and term repos up to one month with auto reversal facility) and Customer Outright Repositioning in which, the face value is Rs.5 million or below. Repositioning transactions exceeding a face value of Rs.5 million, will not be accepted by the system. Participants should use SWIFT for Repositioning transactions that exceed Rs. 5 million. However there is no restriction to participants to use SWIFT for both Customer Repo Repositioning transactions (overnight and term repos up to one month) and Customer Outright Repositioning transactions where the face value is Rs. 5 million or below.
2. Transfers of securities are allowed only from 8.00 a.m. to 4.00 p.m. on valid LankaSecure business days, and, any allowed transaction entered through the CBSLNet after 4.00 p.m. will not be settled.
3. Creation of a security transfer has to be done by one officer and it has to be authorized by another. CBSL will not receive security transfer instructions until a transaction is authorized.

4. Security transfer requests will be uploaded to the LankaSecure for settlement at 9.00 a.m., 3.00 p.m. and 4.00 p.m. on each business day.
5. New balances will be available to participants only after the particular batch of transactions is loaded and settled in the LankaSecure.
6. Before a transaction is settled, an authorized officer of the participating institution is able to cancel the transaction if required, through the existing browser workstation.
7. Once a transaction is settled in the LankaSecure, it is irrevocable.
8. All unsettled repositioning transactions are cancelled by the system at the end of the day and CBSL is not responsible for such cancellations.
9. In a situation where the CBSLNet facility is not available due to a technical or a communication failure, participating institutions should use their SWIFT system to make above Repositioning transactions. CBSL would not take the responsibility for any losses that might result due to failures of CBSLNet.
10. A nominal fee chargeable for providing this trade input facility will be notified later.
11. The system has a facility to transfer securities between any type of account. However, participants are advised to make repositioning between OWN, CSL, CRE, CRR, CRP and REP account types described in the System Rules of the LankaSettle only.
12. If a participant fails to record any repositioning using SWIFT messaging system or through CBSLNet in the LankaSettle, non recording transaction charges for unrecorded transactions as per Rule 2.2 of Volume 3 of LankaSettle System Rules will apply.

• **Circular No: SSSS/02/2007 in this regard issued on 23 January 2007 is hereby revoked.**

Mrs. C. Premaratne
Superintendent of Public Debt

Public Debt Department
28 September 2007

Circular No: SSSS/06/2007

To: All participants of the LankaSettle System

AMENDMENTS TO LANKASETTLE SYSTEM RULES ISSUED IN AUGUST 2003

You are hereby informed that the Rule 5.4 of Volume 3 of LankaSettle System Rules issued in August 2003 and subsequently amended by inserting Rule 5.4.A through Circular No: SSSS/01/2007 dated 23rd January 2007 is replaced to read as follows with effect from 01 October, 2007.

“ 5.4.A. Recording of Repositioning transaction through Central Bank of Sri Lanka Wide Area Network (CBSLNet)

However, Customer Repo Repositioning transaction (overnight and term repos up to one month) or a Customer Outright Repositioning transaction of value which is **Rs. 5 million** or below or such amount as may be decided by the Bank from time to time shall be recorded through the CBSLNet subject to the practices with regard to the operation of CBSLNet as reflected in the relevant System Rules, Operating Instructions that will be issued by the Bank from time to time. Any Customer Repo Repositioning transaction (overnight and term repos up to one month) or Customer Outright Repositioning transaction; the value of which is above **Rs. 5 million** or any such amount as may be decided by the Bank from time to time shall be recorded using SWIFT messaging system. ”

Mrs. C. Premaratne
Superintendent of Public Debt

FINANCE COMPANIES ACT, NO. 78 OF 1988

The Determination of the Monetary Board of the Central Bank of Sri Lanka under section 46 of the Finance Companies Act, No. 78 of 1988.

Nivard Ajith Leslie Cabraal

Chairman

Monetary Board of the Central Bank of Sri Lanka

Colombo

28 February 2007.

DETERMINATION

The Monetary Board of the Central Bank of Sri Lanka (the Monetary Board), in terms of the provisions of section 46 of the Finance Companies Act, No. 78 of 1988, has determined to include the face value of unsecured debentures in the capital funds of a finance company subject to the following conditions:-

- a) The debentures shall be fully paid and subordinated to the interests of depositors and other creditors of the finance company;
- b) The minimum original maturity of the debentures shall be 5 years;
- c) Any finance company that intends to include unsecured debentures that satisfy the conditions at (a) and (b) above in its capital funds, shall obtain prior approval, in writing, of the Director, Department of Supervision of Non-Bank Financial Institutions of the Central Bank of Sri Lanka (the Director);
- d) Early repayment/redemption of the debentures that have been included in capital funds of a finance company shall not be made without the prior consent of the Director;
- e) The value of the debentures to be included in capital funds shall not exceed the value that is qualified to be included in Tier 2 Capital (Supplementary Capital) under the Finance Companies (Risk Weighted Capital Adequacy Ratio) Direction, No. 2 of 2006 issued by the Monetary Board or any other direction that would be issued by the Monetary Board in place of the said Direction;
- f) The amount of the debentures included in the capital funds shall be discounted by 1/5th each year during the four years preceding the maturity; and
- g) Any amount contributed to a debenture issue of a finance company by another company in the group of companies to which the finance company belongs shall not be included in capital funds of that finance company.

FINANCE COMPANIES ACT, NO. 78 OF 1988

The revocation of the Direction given by the Monetary Board of the Central Bank of Sri Lanka under section 9 of the Finance Companies Act, No. 78 of 1988.

Nivard Ajith Leslie Cabraal

Chairman

Monetary Board of the Central Bank of Sri Lanka

Colombo

28 February 2007.

**FINANCE COMPANIES (REVENUE RECOGNITION AND
DISCLOSURES IN THE FINANCIAL STATEMENTS)
DIRECTION, NO. 1 OF 1995**

The Finance Companies (Revenue Recognition and Disclosures in the Financial Statements) Direction, No. 1 of 1995 which was issued by the Monetary Board of the Central Bank of Sri Lanka on 15 March 1995 under section 9 of the Finance Companies Act, No. 78 of 1988 and published in the Government Gazette (Extraordinary) No. 862/19 dated 17 March 1995 is hereby revoked.

**FINANCE COMPANIES (MAINTENANCE OF SAVINGS ACCOUNTS FOR MINORS)
GUIDELINES, NO. 1 OF 2007**

1. These Guidelines may be cited as the Finance Companies (Maintenance of Savings Accounts for Minors) Guidelines, No. 1 of 2007.
2. Every registered finance company (RFC) that maintains savings accounts for minors is required to include the following clauses in the terms/ conditions pertaining to opening, operating and maintaining of savings accounts for minors:

- “(a) The balance lying to the credit of an account of a minor may be transferred upon instructions of a parent or a legal guardian of the minor, to an account maintained in the name of the minor in an authorized deposit taking institution, upon completion of sixty months from the date of the first deposit or at any time thereafter.
- (b) The balance lying to the credit of an account of a minor may be withdrawn by a parent or a legal guardian of the minor, for a justifiable reason such as meeting the cost of medical treatment or education of the minor or for any other reason acceptable to the RFC.”

Such RFC is also required to adequately explain the contents of the above two clauses to the parent or legal guardian of the minor at the time of opening the savings account. If the account is opened by a person other than a parent or legal guardian, the parent or the legal guardian should be informed by the RFC, of the contents of the above two clauses, within one month from the opening of the account.

3. In these Guidelines –
 - (a) “a minor” means a person who has not attained the legal age of majority within the meaning of the Age of Majority Ordinance (Chapter 66) and any amendments thereto.
 - (b) “an authorized deposit taking institution” means a finance company, within the meaning of the Finance Companies Act, No. 78 of 1988, a licensed commercial bank or licensed specialized bank within the meaning of the Banking Act, No. 30 of 1988 or any other entity authorized under any law for the time being in force to accept deposits of money and lend and/or invest money so received.

26.04.2007

Director
Department of Supervision of
Non-Bank Financial Institutions

FINANCE COMPANIES ACT, NO. 78 OF 1988

The Direction given by the Monetary Board of the Central Bank of Sri Lanka under section 9 of the Finance Companies Act, No. 78 of 1988.

Nivard Ajith Leslie Cabraal
Chairman
Monetary Board of the Central Bank of Sri Lanka

Colombo.
29 June 2007.

FINANCE COMPANIES (LENDING)
DIRECTION, NO. 1 OF 2007

1. This Direction may be cited as the Finance Companies (Lending) Direction, No. 1 of 2007 and shall apply to every finance company registered in terms of section 2 of the Finance Companies Act, No. 78 of 1988 and shall come into operation with immediate effect.
2. No finance company shall grant any accommodation –
 - (i) to a director and/or a relative of a director of the finance company;
 - (ii) to its holding company;
 - (iii) on the security of its own shares or on the security of the shares of any of its subsidiary companies;
 - (iv) to purchase its own shares; or
 - (v) on the guarantee or indemnity of a director of the finance company, a relative of a director of the finance company or any employee of the finance company.
3. Notwithstanding the provisions of paragraph 2 hereof, subject to the prior approval of the Director, a finance company may grant accommodation, in accordance with any scheme for the time being in force, for the purchase of or subscription for fully paid shares in the finance company being a purchase or subscription by Trustees of or for shares to be held by or for the benefit of, employees of the company:
 Provided that the aggregate principal amount of such accommodation outstanding at any time, shall not exceed the equivalent of ten per centum of the total amount of the issued and paid up share capital of the finance company or ten per centum of the unimpaired adjusted capital funds of the finance company as per its last audited balance sheet, whichever is greater.
4. A finance company may grant accommodations to its subsidiary companies or associate companies subject to the limits specified in the Finance Companies (Single Borrower Limit) Direction, No. 4 of 2006 and on such terms as may be applicable to similar facilities granted to other borrowers of the finance company, and the particulars of such accommodations including the name of the borrower company, the date of grant of such accommodations, amount granted, repayment programme, security and the rate of interest shall be reported to the Director within 14 days from the date of grant of such accommodations.
5. No finance company shall recover on any accommodation, charges of any description, other than interest, in excess of 5 per cent of the principal amount granted.
6. Every finance company shall submit to the Director within 3 months after the end of each financial year details of all accommodations outstanding as at the end of the financial year on a format given by the Director.
7. For the purpose of this Direction,
 - (i) “accommodation” shall mean loans; facilities under hire purchase or leasing agreements; provision of funds through debt securities such as bonds, debentures, asset backed securities, commercial papers/promissory notes; or such other financial facility as may be determined by the Director.
 - (ii) “associate company” shall mean a company in which the finance company holds 20 per cent or more, but less than 50 per cent of the issued ordinary share capital of the investee company.
 - (iii) “adjusted capital funds” shall mean the aggregate of the paid up capital, the Reserve Fund as provided for in the Finance Companies (Capital Funds) Direction, No. 1 of 2003 and permanent free reserves.
 - (iv) “relative” shall mean the spouse and/or dependent child of an individual.
 - (v) “subsidiary company” shall have the same meaning as contained in section 529 of the Companies Act, No. 7 of 2007.
 - (vi) “the Director” shall mean the Director of the Department of Supervision of Non-Bank Financial Institutions of the Central Bank of Sri Lanka.
 - (vii) “Trustee” shall mean a person appointed under or named in a trust deed executed in respect of an employee share ownership plan of a finance company.
8. The Finance Companies (Lending) Direction, No. 5 of 2006 is hereby revoked.

FINANCE COMPANIES ACT, NO. 78 OF 1988

The Direction given by the Monetary Board of the Central Bank of Sri Lanka under section 9 of the Finance Companies Act, No. 78 of 1988

Nivard Ajith Leslie Cabraal

Chairman

Monetary Board of the Central Bank of Sri Lanka

Colombo.

29 June 2007.

**FINANCE COMPANIES (BUSINESS TRANSACTIONS WITH DIRECTORS
AND THEIR RELATIVES) DIRECTION, NO. 2 OF 2007**

1. This Direction may be cited as the Finance Companies (Business Transactions with Directors and their Relatives) Direction, No.2 of 2007 and shall apply to every finance company registered in terms of section 2 of the Finance Companies Act, No. 78 of 1988, and shall come into operation with immediate effect.
2. A finance company shall not, without the approval of the Director, conduct any business transaction with a director of the company or a relative of a director of the company where the total value of transaction/s exceeds Rs. 50,000 per month or Rs. 500,000 for a financial year. Conducting of any business transaction by a finance company with a director of the company or a relative of a director of the company shall be subject to the Finance Companies (Lending) Direction, No. 01 of 2007.
3. The provisions of paragraph 2 hereof, shall not apply to accepting of time and savings deposits from a director of the company or a relative/s of a director of the company in conformity with the Finance Companies (Deposits) Direction, No. 1 of 2005 and the Finance Companies (Interest) Direction, No. 2 of 2005 and on the terms and conditions that are, for the time being, applicable to the other depositors of the finance company, and to payment of interest on similar deposits.
4. For the purpose of this Direction,
 - (a) “relative” shall mean the spouse and/or dependent child of an individual.
 - (b) “the Director” shall mean the Director of the Department of Supervision of Non-Bank Financial Institutions of the Central Bank of Sri Lanka.
5. The Finance Companies (Business Transactions with Directors and their Relatives) Direction, No. 6 of 2006 is hereby revoked.