

Annual Report 2010

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# THE RIGHT MOVES

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SECURITIES AND EXCHANGE  
COMMISSION OF SRI LANKA

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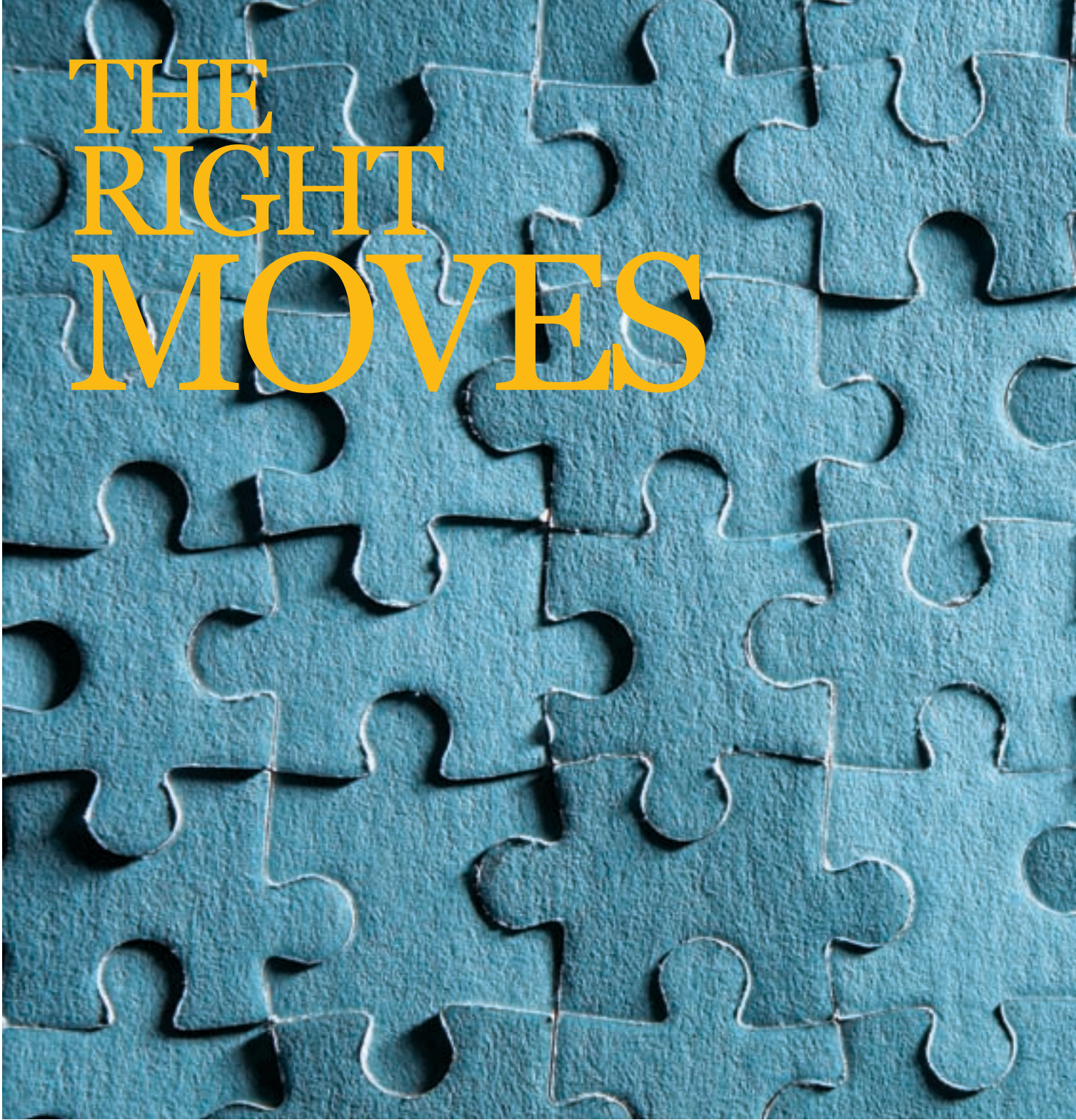
# Vision


“To become the benchmark regulator in South Asia for effective, efficient and proactive capital market regulation”

# Mission

“To promote, develop and maintain a capital market that is fair, efficient, orderly and transparent”

# THE RIGHT MOVES





In an era of peace and development, our role in a burgeoning economy has become more important than ever before. Our strategy and commitment to maintain a fair, orderly, efficient and transparent securities market has paid off in the face of international crisis. While rampant investments and unfettered decisions caused chaos and loss in foreign markets, it was through regulation and stringent measures that a similar fate was avoided in Sri Lanka and it is heartening to see that the outcome has enabled the economy to move from strength to strength.

**We have made the right moves, and we are seeing the right results.**



Mrs. Indrani Sugathadasa  
Chairperson

# Chairperson's Review

*“In a relatively short span of time, the role of Sri Lanka’s capital market in funding and mobilizing savings has become more comparable to that of the banking sector.”*

Sri Lanka, today stands at a juncture of key, unparalleled and unprecedented opportunity. Three decades of terrorist activities distorted Sri Lanka’s economy, hindered development, and reduced the country’s potential growth. However, since the end of the conflict in May 2009, the country’s economic fundamentals have improved significantly. The political and economic stability established in the country have pervaded all sectors recording growth as never before. With the peace dividend filtering in, the economy grew at 8% in 2010. With this backdrop, Sri Lanka’s capital market has developed speedily and more extensively in the last 2 years than any other period in history. The Colombo Stock Exchange (CSE) emerged the second best performing stock market in the world in 2010 for the second consecutive year. The market created history by establishing new records in almost all aspects of trading from indices, total market turnover to market capitalization in 2010.

Stock markets have the potential to be powerful engines of economic growth in developing nations and could play a central role in the growth of a country’s industry and commerce that eventually affects its economy to a great extent. The stock market provides companies the platform to raise capital to expand their businesses. Investors are able to buy shares of public offerings and the money that is raised from the investors is used by the company to expand operations. All of this leads to increased economic activity which helps drive the economy.

In a relatively short span of time, the role of Sri Lanka’s capital market in funding and mobilizing savings has become more comparable to that of the banking sector. The capital market has also firmly established its profile as an indicator and facilitator of growth within the Sri Lankan economy. This unprecedented growth of the market has resulted in attracting a large number of new investors and

# Chairperson's Review contd...

issuers to the market. The role of the Securities and Exchange Commission of Sri Lanka (SEC), in protecting the investor, preventing systemic crises and promoting the market has enhanced greatly over the last two years due to the resounding growth in the market.

We believe that the foundation to establish a robust and efficient capital market is creating an effective securities regulatory regime. An effective securities regime will ensure that the market is operated efficiently and fairly, and in turn, it will enhance investor confidence. Also a well regulated market has the potential to encourage additional investors to partake and contribute to further development of the economy. The SEC implemented several initiatives in 2010 to accomplish an effective regulatory regime. Some of those initiatives include issuing licences to new market intermediaries, directing the CSE and the Central Depository Systems (Pvt) Ltd (CDS) to implement a system of full dematerialization of all listed securities, completing the regulatory framework for exchange traded funds, updating the Code for Unit Trusts and finalizing the rules pertaining to Employee Share Option Plans. Also the SEC directed the CSE, CDS and all licensed stock brokers to remove the two band fee structure and to have one band for transactions and also to reduce the transaction cost. Changes were made to the Automated Trading System Rules (ATS) with a view to develop the market microstructure. With the aim of enhancing the surveillance function, the SEC procured a state of the art surveillance system in 2010.

We are confident that the proposals included in the National Budget for 2011 will provide further impetus to the development of the capital market of Sri Lanka. The Budget incorporated many important proposals the SEC had made thus eliminating the impediments that prevailed in the market. We are grateful to the President, His Excellency Mahinda Rajapaksa and the Secretary to the Treasury, Dr P.B. Jayasundera for incorporating SEC's proposals in the budget.

In July 2010, the SEC introduced the much debated "price band" to arrest volatility in the market. The price band came into effect after prices of certain stocks were seen rising without being backed by sound fundamentals. Imposing a price band was a policy decision of the SEC with the intention of effecting certain changes in the system. These reforms are indeed reflective of the positive steps that SEC has taken to bring about a strong level of confidence as well as add further liquidity into the market. Without these regulations and shareholder protection, only a few people would have been willing to invest in stocks. We believe that one of the main responsibilities of the SEC is to enhance investor confidence drawing more people to be part of the investor community.

The SEC has formulated a 3 year plan consistent with the government's strategic priorities and endeavoured to ensure that the SEC continues to play a significant role in the securities regulatory landscape. We have

recognized five key strategic goals, namely, facilitating improvements in the capital market infrastructure, facilitating improvements in liquidity and introduction of new products in the capital market, encouraging and facilitating the widening and broadening of issuer base, facilitating widening and broadening of the investor base, and enhancing SEC's performance through effective alignment and management of human, information, and financial capital.

Sri Lanka has extensively improved its economic fundamentals following the end of the war against long-standing terrorism. The government has already taken measures to improve the business environment and build on its ranking to compete globally. The government's stability has given investors a positive outlook. With this backdrop, the Colombo Stock Market will have a bearing on the economic activity through the creation of liquidity and influencing corporate governance. Liquid stock markets make investments less risky and more attractive. High level of liquidity at the Colombo Stock Market will facilitate investment, promote efficient allocation of capital, and stimulate long-term economic growth. The SEC has already taken steps to facilitate liquidity by providing a new regime of regulations.

The year 2010 was indeed one of the most challenging years for the SEC. There are many who supported us during this period. We are grateful to all of them.



*“The SEC has formulated a 3 year plan consistent with the government’s strategic priorities and endeavoured to ensure that the SEC continues to play a significant role in the securities regulatory landscape.”*

In particular, we would like to thank the President His Excellency Mahinda Rajapaksa, who is also the Minister of Finance, and the Secretary to the Treasury, Dr P.B. Jayasundera and his officials for their guidance and firm support extended during the year. I am also grateful to the Members of the Commission for having given me their fullest support at all times.

I take this opportunity to thank the Governor of the Central Bank of Sri Lanka (CBSL) for his continued support and the CSE, stock broking companies, fund managers and all market participants who played a role in developing the market during this period.

Finally, I thank the Director General, directors and the staff of the SEC who have continued to do an excellent job in maintaining the standards of the SEC as well as formulating and executing strategies that would take the capital market forward.

Let me reiterate our resolve to build our capital market and set it on a strong foundation over the next few years to complement economic growth and place Sri Lanka as “The Emerging Wonder of Asia”.



**Indrani Sugathadasa**  
*Chairperson*

19th May 2011

Malik Cader  
*Director General*

# Director General's Review

## Introduction

2010 was a challenging year for the capital market of Sri Lanka. Backed by peace and stability in the country the CSE established new records, demonstrated unprecedented turnover levels and for the second consecutive year was ranked the second best performing stock market in the world. In the face of challenges and uncertainties experienced in global stock markets, our market remained resilient and was able to absorb sudden shocks and fluctuations as a result of the timely measures taken by SEC during the year. A major thrust of our work during the year was to provide a regulatory backdrop which is fair, efficient and conducive to market development.

## Regulatory Measures

Exceptional levels of growth posed formidable challenges in terms of maintaining a disciplined and orderly market. The SEC at all times remained vigilant, effectively monitoring trading movements and focusing on policy measures that should be introduced to ensure market integrity. In view of the regulatory challenges and demands of the share market, the SEC took appropriate policy measures, to promote investor confidence.

## Price Band on Listed Securities

In July 2010, the prices in certain stocks began to rise considerably - not owing to fundamental factors but almost due to sheer speculation and 'overheating' in the market. This price volatility that existed in the market necessitated us to impose a 10% (up or down) price band on all listed securities. Although the market reacted negatively immediately after imposing the price band, it recovered gradually within a short period of time.

Prior to imposing the price band (1<sup>st</sup> January to 4<sup>th</sup> August 2010) the All Share Price Index (ASPI) grew by 54% and the daily average turnover stood at Rs. 2.0 billion. Despite the price band the ASPI grew at an encouraging 96% and the daily average turnover was Rs. 2.9 billion at the end of the year. The measures taken in a timely manner reflected the vigilance and effective monitoring and thereby helped to enhance the level of Investor confidence whilst adding further liquidity to the market.

*“Exceptional levels of growth posed formidable challenges in terms of maintaining a disciplined and orderly market.”*

# Director General's Review contd...

## Review of the Current SEC Act

The SEC made a conscious effort to ensure that the regulatory framework in place facilitates market development and meets the regulatory challenges of the future. During 2010, the SEC critically reviewed the present SEC Act, with the objective of facilitating the regulation of Demutualized exchanges, facilitating the establishment of a Central Counter Party, Introducing civil sanctions and administrative sanctions to deal with capital market offenders and introducing other provisions to strengthen Investor protection.

## New Market Participants

During 2010, the SEC granted licences to 5 stock brokers, 5 investment managers, 9 margin providers, 3 underwriters and 1 stock dealer. They have already commenced operations quite successfully. The SEC is confident that the entry of new market participants will provide greater access and services to investors.

## Dematerialization of Listed Securities

The CDS accounted for only 58% of listed securities deposited in it. The balance was in certificated form. During 2010, the SEC directed the CSE

and the CDS to mandate the lodging of certificates pertaining to all listed securities at the CDS and thereby implement a system of dematerialization (de- mat) of all listed Securities. This directive is effective from 1<sup>st</sup> January 2011 and mandated securities of all existing listing entities which obtained listed status prior to 1<sup>st</sup> January 2011, to be in the dematerialized form by 1<sup>st</sup> January 2012 and to give prior notice to the existing listed entities of the said requirement.

## Liquidity of the Secondary Market

Improving liquidity in the secondary market was a priority of the SEC and as a positive step towards achieving this objective, the SEC and the CSE held deliberations and agreed on a set of proposals, to amend the Automated Trading Rules (ATS) with a view to develop the market microstructure.

Consistent with this plan, the SEC directed the CSE, CDS and all licensed stock brokers to:

- [a] Remove the Two Band Fee structure which was applicable.
- [b] Introduce the One Band Fee structure for transactions up to Rs. 50 million.

- [c] Reduce the transaction cost of trades below that of Rs. 50 million

The proposal was made effective from 1<sup>st</sup> of July 2010. The SEC also directed the CSE to increase the Crossing Threshold from that of Rs. 10 million to Rs. 20 million and to reduce the Tick Size across the board to 10 cents which has created more liquidity in the market.

## Development of the Corporate Bond Market:

A well developed Bond Market is able to supplement the banking system in meeting the long-term capital investment needs of the corporate sector. With the objective of expanding the Bond Market and improving its efficiency, the anomaly which existed in the treatment of withholding tax on corporate debt securities, as well as the anomaly of the risk reward structure, were specifically addressed.

## Market Oversight and surveillance

The SEC at all times remained vigilant in effectively monitoring market activities to detect unusual price movements. The new automated surveillance system commissioned by the SEC was installed during the year and the new system was tested with live data from the CSE.

*“The SEC made a conscious effort to ensure that the regulatory framework in place facilitates market development and meets the regulatory challenges of the future.”*

To streamline processes and reinforce off-site supervision, in tandem with this surveillance system the SEC completed the first phase of the electronic filing system for market participants. The functions of this system will be expanded in the ensuing year for the convenience of our market intermediaries.

### Administrative Action

Due to the effective regulating mechanism adopted by the SEC during the year under review it is noteworthy that there was a drastic reduction of companies on the Default Board. Action was taken against companies on the Default Board for non submission of annual reports to the market. Legal action instituted against these companies were withdrawn after the said companies released their outstanding annual reports to the market.

### International Relations

SEC is a full member of the International Organization of Securities Commissions (IOSCO) which is the international standard setter for securities markets and is a signatory to the Multilateral Memorandum of Understanding (MMOU) which represents a common understanding amongst its signatories on exchange of information for securities regulatory enforcement purposes. The President's Committee of the IOSCO introduced eight new principles which pertain to adequate levels of oversight over auditors, management of systemic risk, adequate levels of oversight over credit rating agencies, monitoring of investor analytical or evaluative services etc.

These principles contribute to a process to review the perimeter of regulation regularly. In view of these changes the SEC will take appropriate steps to adhere to these new international standards.

### Acknowledgment

I wish to sincerely thank our Chairperson Mrs. Indrani Sugathadasa and the Members of the Commission who were a source of strength and provided guidance, unstinted cooperation and assistance at all times. I will be failing in my duty if I do not place on record my appreciation to the following for the cooperation extended during a challenging year.

- The Chairman, Board of Directors, the Management and Staff of the CSE.
- The President and Members of the Colombo Stock Brokers Association, Unit Trust Association and other market participants.

We were able to face the challenges in 2010 due to the professionalism, dedication and unwavering commitment of the Members of the Commission and the staff of the SEC. Their efforts contributed in great measure towards maintaining a well regulated, dynamic capital market in Sri Lanka.

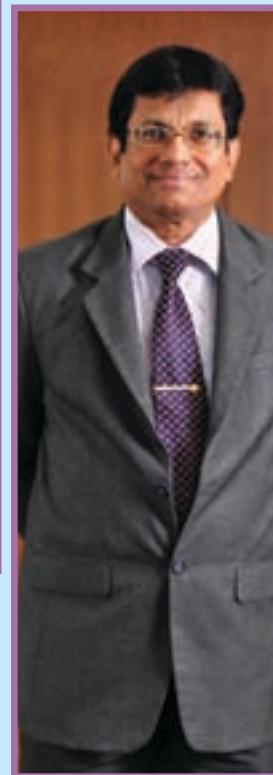
In this regard, all officials of the SEC, irrespective of rank should be congratulated for the spirit in which they performed their duties. I am confident that the SEC will play its role with renewed vigour in the years to come towards taking the capital market of Sri Lanka to greater heights.



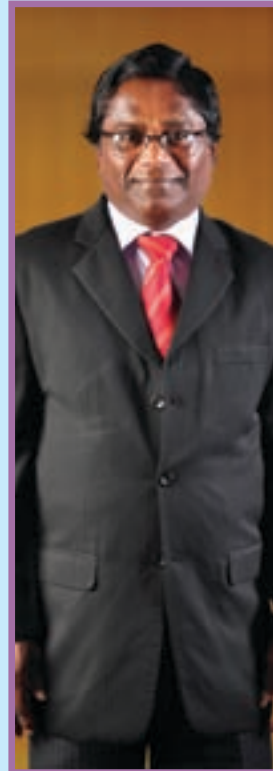
**Malik Cader**  
*Director General*

19th May 2011

# Members of the Commission



From Left to Right  
Mrs. Indrani Sugathadasa (Chairperson)  
Mr. C.P.E. Gunasingam  
Mr. Lolitha Abeysinghe  
Mr. P D J Fernando  
Mr. D. Widanagamachchi



From Left to Right  
Mr. Priyantha Jayawardena  
Mr. Sujeewa Mudalige  
Mr. Mohamed Hifaz Hashim  
Mr. D.K. Hettiarachchi

# Members of the Commission contd...

## **Mrs. Indrani Sugathadasa** (Chairperson)

Mrs. Indrani Sugathadasa has been a very senior public servant who joined the Sri Lanka administrative service (SLAS) in 1977. After retirement, she was appointed Chairperson of the Securities and Exchange Commission of Sri Lanka in May 2010. She is holding the position of Chairperson of the Insurance Board of Sri Lanka (IBSL) as well.

The last position she held in the mainstream public service was that of Secretary, Ministry of Plantation Industries. Prior to that she had served in the Ministries of Women's Affairs and Child Development, Plan Implementation and the National Youth Services Council (NYSC) in different capacities.

Mrs. Sugathadasa holds a Bachelor of Social Sciences degree from the University of Colombo and obtained Masters degree (MPA/MBA) from Monash University, Melbourne, Australia, on an Australian Government Scholarship. She also has been awarded the prestigious Hubert H. Humphrey Fellowship (Fulbright) by the United States Government in 1990 and was attached to Hunter College, City University of New York during the one-year Fellowship period.

In addition, Mrs. Sugathadasa has participated extensively in various training programmes and consultancies in Management and gender related disciplines, both locally and internationally.

## **Mr. D.K. Hettiarachchi**

Mr. D.K. Hettiarachchi is an Attorney-at-Law by profession. He is a Law Graduate (L.LB) of the University of Colombo. He joined the department of the Registrar of Companies in 1986 as an Assistant Registrar and was promoted to the position of Registrar of Companies in 1997. He has been appointed as the Registrar General of companies under the new Companies Act. He is a member of

the Sri Lanka Accounting and Auditing Standards Monitoring Board.

## **Mr. Lolitha Abeysinghe**

Mr. Lolitha Abeysinghe holds a MBA from the University of Rockville, USA and a Diploma in Marketing from the Sri Lanka Institute of Marketing (SLIM/SLIDA). He also holds a Certificate in Intentional Trade from the Federation of Chambers of Commerce and Industry of Sri Lanka (FCCISL), a Certificate in Advanced Operational aspects of Intentional Trade and a Certificate in Optional aspects of Intentional Trade from the Export Development Board (EDB). At present he is studying law at the Sri Lanka Law College.

Mr. Abeysinghe is currently Chairman/Managing Director of Sarero International. He is a Managing Director of Chelina Capital Corporation (Private) Ltd, Evoke Projects (Private) Ltd and Vauxhall Corporation (Private) Ltd. He is a Director of Lanka Light Industrial Products Import/Export (Private) Ltd, Hybrid Structures Lanka (Private) Ltd, Lanka Green Energy (Private) Ltd, Akamai Communication Company (Private) Ltd, SAR Embellishment (Pvt) Ltd, Arades International (Pvt) Ltd, Megaputhra (Pvt) Ltd and Vingrows Business Solutions (Private) Ltd. He is also the Business Promotion Consultant at Laksala (Sri Lanka Handicrafts Board) and Senior Partner of Orient Holding (private) Ltd ASL Business Solutions. He is also the Advisor to Avant Garde Emirates Ltd. (UAE) and Sadisma Hospital (Pvt) Ltd & Asia Hospitals (private) Ltd.

He has served as Chairman Medicheck Holding (Private) Ltd, Director National Apprentice and Industrial Training Authority (NAITA), Four Seasons Hospitals (Private) Ltd, Canton Energy (Private) Ltd, AGSS International Consultant (Private) Ltd, Nobel Freight (Private) Ltd and SLN Packaging Industries (Private) Ltd. He has also served as a Strategic Partner

at Management Education Development Agency and Senior Partner, Medismart, UK Suppliers. He has also worked as a Team Member at Impakt International Consultants (Pvt) Ltd. He was the Management Consultant to the Minister of State transport, Consultant to Nobel International (Private) Ltd and Focus International (Private) Ltd.

He has attended many local and international training courses, workshops and conferences. He has presented papers at several international seminars.

## **Mr. Priyantha Jayawardena**

After the primary and secondary education at Nalanda College, he entered the Law College in 1985. After he completed his studies at the Law College he was called to the bar and enrolled as an Attorney-at-Law of the Supreme Court in 1988. He was engaged in private practice until he joined the Attorney- General's Department to work in the Government Institutions Division in 1991. Thereafter, he proceeded to the United Kingdom and obtained a Master's Degree in Commercial Law from the University of Aberdeen in 1993. On his return to the country he joined the Attorney- General's Department and served as a State Counsel and reverted back to the unofficial bar in 2000 and is now engaged in private practice. Whilst serving in the Attorney- General's Department he worked as a Consultant to the Ministry of Food, Internal and International Trade and Commerce and also participated in drafting legislation. In addition to other duties he has served as a member of the Advisory Commission on Intellectual Property Law of Sri Lanka. He was an Examiner of the Council of Legal Education and a Visiting Lecturer of the University of Moratuwa.

## **Mr. Sujeewa Mudalige**

Mr. Sujeewa Mudalige passed out as a Chartered Accountant in 1991. He is also a Fellow of the Chartered Institute



of Management Accountants (CIMA) of UK, Association of Chartered Certified Accountants (ACCA) of UK and the Certified Public Accountants of Australia (CPA). He was elected to the Council of The Institute of Chartered Accountants in Dec 1999 and was elected as the President in December 2009.

He is currently a partner at PricewaterhouseCoopers, Chartered Accountants. Mr. Mudalige has previously worked at large public listed companies in Sri Lanka and overseas.

He is a Board Member of the recently appointed governing board of CIMA Sri Lanka division.

He currently serves on several regulatory bodies including the Securities & Exchange Commission (SEC) and the Sri Lanka Accounting and Auditing Standards Monitoring Board (SLAASMB). He is also a member of the Accounting Standards Committee and the Auditing Standards Committee appointed under the Sri Lanka Accounting and Auditing Standards Act of 1995.

#### **Mr. P D J Fernando**

Mr. P D J Fernando obtained his B.Sc (Hons) from University of Peradeniya and M.Sc in Statistics from the University of Birmingham, UK. He commenced his banking career at the CBSL in 1976 and served as the Assistant Governor in charge of the department of Information Technology, Payment and Settlements, Employee Provident Fund, Finance and Premises and Security. He was also the Additional Director department of Statistics and Director Information Technology.

Mr. P D J Fernando currently holds the post of Deputy Governor, CBSL. He is the Chairman of the Institute of Bankers of Sri Lanka, Credit Information Bureau of Sri Lanka, National Payments Council and Steering Committee for establishing

the Common Payment Switch for Sri Lanka to facilitate inter-bank payments for retail transactions. He is also an ex-officio Member of the Insurance Board of Sri Lanka and Member of the Board of Management of Api Wenuwen Api Fund.

Mr. P D J Fernando held the posts of (i) Secretary to the Monetary Board of the CBSL (ii) Director, Lanka Financial Services Bureau, (iii) A key Member in the CBSL modernization project, leading the modernization in Payment and Settlement Systems (iv) Project Manager of the implementation of the Real Time Gross Settlement System for settlement of Inter-Bank payments and Settlement of Government Securities issued in scriptless form (v) Director, LankaClear (Pvt) Ltd (vi) Member of the Standing Committee of the Cabinet Appointed Procurement Committee of procuring petroleum products for Ceylon Petroleum Corporation(CPC) (vii) Member of the Cabinet Appointed Negotiating Committee in Procurement of Petroleum products for CPC.

#### **Mr. C.P.E. Gunasingam**

Mr. C.P.E. Gunasingam holds a Bachelor of Science degree from the University of Madras and a Bachelor of Laws degree from the University of Colombo. He was admitted to the Bar as an Advocate in 1972. He is a fellow member of the Sri Lanka Institute of Taxation and has served as its President for four years. He has served as a Visiting Lecturer in Taxation at the Sri Lanka Institute of Taxation and the Institute of Chartered Accountants of Sri Lanka. He has served as an Assessor of Inland Revenue from 1962 to 1973 and counts 35 years of service as a tax practitioner. He has addressed seminars and contributed articles to newspapers and journals on tax related subjects. Mr. Gunasingam has served as a Board member of Peoples Bank, the Insurance Board of Sri Lanka and the National Council for Economic Development – Taxation Cluster. Presently he serves as

a Member of the Finance Commission established under Article 154R of the Constitution.

#### **Mr. D. Widanagamachchi**

Mr. D. Widanagamachchi holds a Bachelor of Science Degree in Business Administration from the University of Sri Jayawardhanapura. He has also obtained Postgraduate Diplomas in Public Administration from the Postgraduate Institute of Management, Colombo and Public Financial Management from the Sri Lanka Institute of Development Administration. He has undergone extensive training in local and international institutes.

Mr. D. Widanagamachchi is a senior public servant with over thirty years experience at various public institutions. He currently holds the position of Deputy Secretary to the Treasury at the Ministry of Finance & Planning.

He has served on the Boards of several public enterprises, Airports Aviation Services (Sri Lanka) Ltd., BCC (Lanka) Ltd., Sri Lanka Transport Medical Institute, National Water Supply & Drainage Board, CWE and Lak Sathosa Ltd., to name a few.

#### **Mr. Mohamed Hifaz Hashim**

Mr. Hashim is a Bachelor of Laws (LL.B) (Honours) London and Barrister at Law (Middle Temple). He is director at Malship group of companies, Development Interplan Ceylon Ltd and West Asia Trading (Pvt) Ltd. He is the General Secretary of the Sri Lanka Fruit & Vegetable Producers', Processors' & Exporters Association. Mr. Hashim has represented Sri Lanka at various local and international business forums.

# Senior Management

## From Left to Right

Malik Cader - Director General

Dhammika Perera - Director Investigations

Himani Weerasekera - Assistant Director Supervision

Chandu Epitawala - Director Surveillance

Surana Fernando - Director Corporate Affairs

Vajira Wijegunawardane - Director Capital Market Development and Research



**From Left to Right**

Tushara Jayaratne - Assistant Director, External Relations and Market Development

Ianthie Jayaratne - Director Finance and Administration

Dr. D. B. P. H. Dissa Bandara - Director Financial Services Academy

Ayanthi Abeywickrama - Assistant Director Legal and Enforcement

Namal Kamalgoda - Director Supervision



# Staff

## Standing from Left

Mr. Rakitha Bandara, Miss. G. Sathiyatharshini, Miss. Joelene Karunaratne, Mr. Dhanushka Perera, Mr. Buddhika Lokuliyana, Mrs. Sajeevani Bakmedeniya, Miss. Eranga Amarasie, Miss. Ranithri Molligoda, Mr. Priyantha Bandara, Miss. Mehkala Jayapala, Mrs. Manjula Chandraratne, Ms. P. D. Pathmarani, Mrs. J. K. Priyadarshini, Miss. Shalini Perera, Mr. R. K. Wasantha Sunimal

## Sitting from Left

Mr. Anslam Dias, Mrs. Kanchana Kumari, Mrs. Lakshmi Wickramanayake, Miss. Rajmi Manathunga, Ms. Sheena Goonaratna, Mrs. Dhanesha Rajapura, Mrs. Anula Wijesinghe, Mr. Sugath Alwis, Miss. Madhugayanie Balapitiya, Miss. Thakshila Francis, Mrs. Ranmini Jayathilake, Mr. Nimal Kumarasinghe, Mrs. Ashoka K Dayarathne



### Standing from Left

Miss. Rosheni Wickramaratne, Mrs. Ruwani Munasinha, Mrs. Sithara Tissera, Mr. Anura Perera, Mrs. Krishanthi Muthuthantrige, Mrs. Prabashini Samarakoon, Mr. S. D. Dharmasiri, Miss. Nuala Thevathasan, Mrs. H. K. A. Chamari Buddhika, Miss. Lakshmi Atapattu, Mrs. Chandima Chandrasekere, Mr. Chandran Nagendran, Mr. Mahesh Abeysekera, Miss. Christobel Silva, Miss. Kumari Siriwardena, Mr. D. Pathum Niroshana, Miss. Dilanka Athapaththu

### Sitting from Left

Mr. W. Ariyaratna, Mrs. Prathibhani Herath, Mrs. Aeshini Bandara, Mrs. Nishoka Jayathunga, Mrs. Juliet AllegaKoen, Miss. Sharmila Panditaratne, Mr. M. Jayasekara, Mrs. Gayathri Weerasinghe, Mrs. Saumi Kodippily, Mr. Sandaruwan Wijeratne, Mr. D. M. G .Priyantha, Mr. B. Saimathavan, Miss. Ruwanganie Gooneratne, Miss. Darshika Wickramasinghe, Miss. P. M. Niroshika Udayanganie

### Absent

Mr. Suneth Perera, Mr. P. W. L. Piyatissa







“ We have ensured that through effective measures and policies, that the securities market remains fair and orderly ”

# Macroeconomic Overview

The year 2010 was a year filled with expectations from investors and government policy makers. The high expectations and optimism was reflected in the stock market indices rising at 96% for the year 2010 just short of the growth experienced in the year 2009. It was also a politically significant year where the President was re-elected for a second term with a resounding majority and the ruling coalition won a landslide at the general elections that followed it. This political stability was cheered by the stock market investors. This was followed a few months later by the 2011 budget presented in Parliament in November of 2010. This budget turned out to be one of the most significant in the recent past where far reaching proposals for rationalization of taxes and relaxation of foreign exchange controls were presented and approved.

In 2010, the Sri Lankan economy grew by 8% in real terms which compares well with the average annual growth of 4.9% recorded since 1977. All three main Sectors of the economy contributed positively towards economic growth. The Agriculture Sector saw growth aided by the agricultural production from the former war zone beginning to come on stream as well as the favourable weather that prevailed during the year. The general revival in local consumption and investment and rise in exports with gradual global recovery ensured the growth in Manufacturing and Services Sectors.

Though historically Sri Lanka's domestic savings rate has remained relatively low at around 17% of Gross Domestic Product (GDP), the inward workers' remittances from Sri Lankans working abroad grew at a healthy rate ending

the year at US dollars 4.1 billion. Other inflows from Foreign Direct Investment, International Monetary Fund and exports kept the rupee strong appreciating by 3.09% against the US dollar during the year. The gross official reserves have reached US dollars 6,610 million which helped the CBSL to further relax the exchange control regulations.

Inflation remained at single digit throughout the year bringing down the interest rates making it attractive for corporates' to borrow and refinance old loans enhancing their profitability. This gave a further impetus to the stock market. On the other side of that coin, the savers got too little return for their deposits compared to what they were used to in the past resulting in many diverting part of their savings into the stock market for better returns perhaps ignoring the higher level of risk investors in equity invariably assume. Since the rupee has stabilized, the stock market should give an investor attractive returns in dollar terms.

In the budget, the government has also committed itself to promoting and expanding the capital market in general and Unit Trust industry in particular. Unit Trusts or Collective Investment Schemes which are managed by professionals remain the ideal vehicle for small investors to participate in the growth of companies listed in the share market.

Unemployment decreased to 4.9% in 2010 and is set to go down further if a sustained higher growth rate is maintained. The fiscal deficit has dropped to 7.9% of GDP which is an improvement on the previous year's deficit. The government has committed itself to bringing the deficit down further.

Further, the government has moved forward several large scale infrastructure projects which are vital to Sri Lanka's economic growth and development. Several free ways, ports, airports and power generation projects are amongst them. The most significant one amongst them is the Hambantota Port first phase of which was opened in November 2010. Once completed and fully functional this harbor will rejuvenate Hambantota and surroundings creating employment, tourism and prosperity to many residents of the areas as well as contributing to the overall national economy. From the view point of accelerated development and growth, one of Sri Lanka's main handicaps had been lack of modern infrastructure especially expressways. In recognition of this gap the government has channeled large resources to complete such projects without imposing undue pressure on the fiscal position of the country by getting bilateral financial assistance from friendly countries.

The year 2010 made significant progress and growth and laid the foundation for solid economic prospects in the coming years. The stock market has reflected this expectation and sentiment and related itself to Price Earnings Ratio (P/E) of approximately 25X. We anticipate this P/E ratio to gradually come down with many companies expecting to report very high growth in their profitability. Economically it was an excellent year for the country and we expect even better results to materialize in the coming years.

*Data Source : Annual Report 2010, Central Bank of Sri Lanka.*



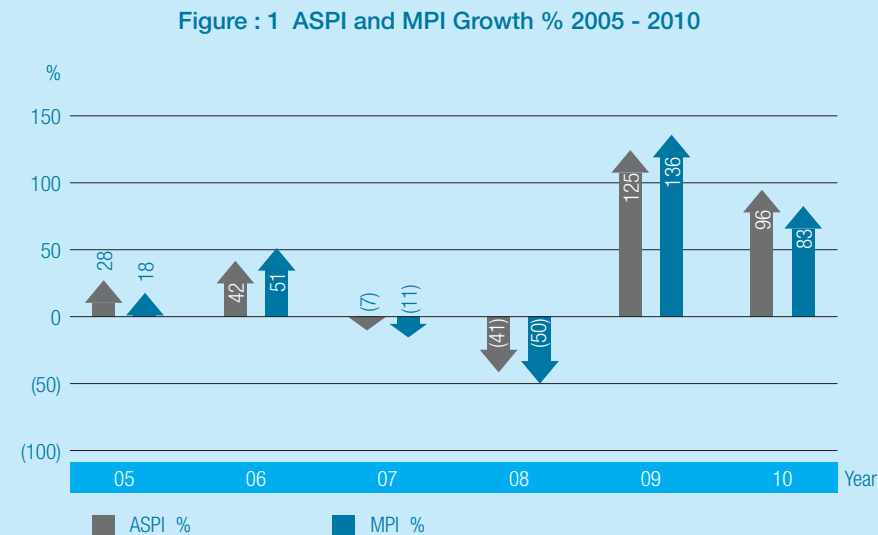
# Capital Market Review

The year 2010 dawned with a sense of enthusiasm of a stellar year for share investment at the CSE fueled by post war optimism and economic expansion. Peace and political stability in the country with the expectation of healthy corporate growth by listed entities stimulated activity to unprecedented levels hitherto unseen in the CSE. The CSE continued its upward trend and became the second best performer in the world in terms of Index performance for the second consecutive year.

## Index performance

The benchmark ASPI ended the year recording a significant growth of 96% or 3,250 points to close at 6,635.9 points. The highest ever level reached by the ASPI was 7,147.7 points which was recorded on 1<sup>st</sup> October 2010. Meanwhile the stocks in the more liquid MILANKA Price Index (MPI) increased by 83% or 3,212 points compared to the year 2009 to close the year at 7,061.5 points and reached its all time high of 7,829 points on the same day (1<sup>st</sup> October 2010).

As the CSE showed signs of being over heated with the appearance of too much money chasing after few shares the SEC took decisive action in order to protect the integrity of the market. On 5<sup>th</sup> August 2010 the SEC imposed a 10% (up or down) price band limit



on all listed securities. The 10% price band disturbed the momentum of the share market for three days with the benchmark ASPI reacting negatively. However the market recovered gradually thereafter.

The CSE overtook Mongolia to emerge as the best performing stock exchange in the world as per the Bloomberg data at the very beginning of October 2010. The unprecedented market boom however lost some steam thereafter resulting in a market correction which saw the ASPI shedding 7% where retailers continued to sell to meet margin settlements. In December, the

SEC, in order to contain and mitigate risk within the market system, took further measures by capping the possibility for easy credit extension to investors by brokers. However brokers were allowed to extend two days credit to clients who are unable to settle their dues by T+3. (Figure : 1)

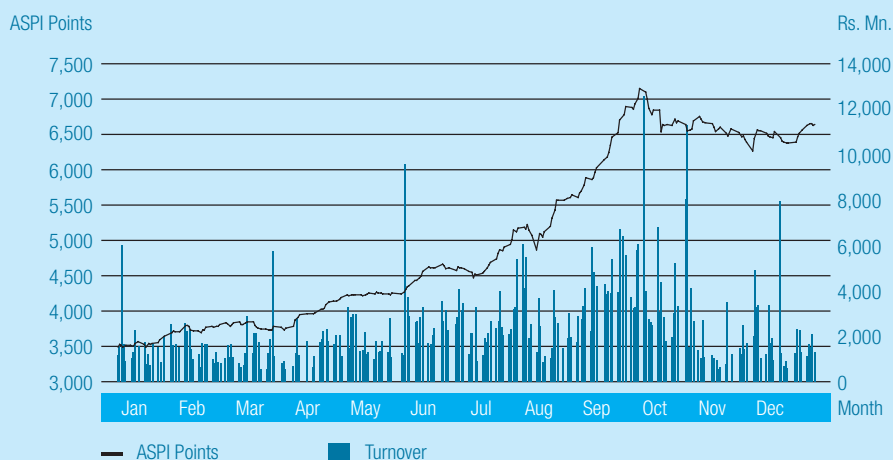
## Annual Turnover

Turnover levels were concurrent with the market performance and in 2010 the share market recorded a total annual turnover of Rs. 570.3 billion which is an enormous improvement of more than 300% compared to the previous year. The average daily turnover of the bourse was Rs. 2.3 billion which was way above the previous record of Rs. 593.6 million that was recorded in 2009. (Figure : 2)

**CSE emerged the Second best Performing Stock Exchange in the World for the Year 2010 - Bloomberg data**

# Capital Market Review contd...

Figure : 2 ASPI Vs Turnover 2010

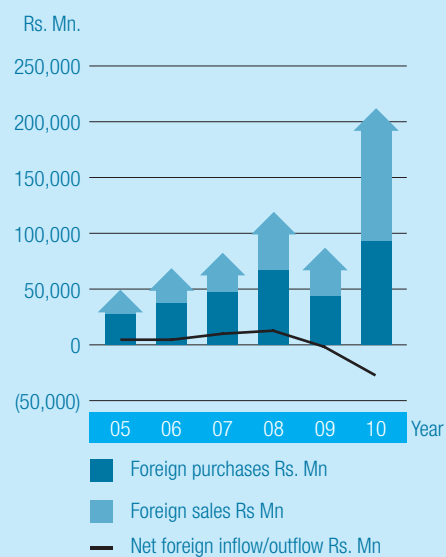


Source : CSE

## Foreign Participation

Foreigners were net sellers in the market in the year 2010. Average daily foreign purchases stood at Rs 388.7 million whilst sales stood at Rs 499.5 million generating a net daily outflow of foreign funds of approximately Rs 110.8 million. The total outflow of foreign funds for the year was Rs. 26.3 billion, most of it believed to be due to profit taking as a result of the prevailing rally in the CSE. Some foreign investors may have considered the P/E of 25x relatively expensive for an emerging market such as ours. (Figure : 4)

Figure : 4 Foreign Purchases Vs Sales



Source : CSE

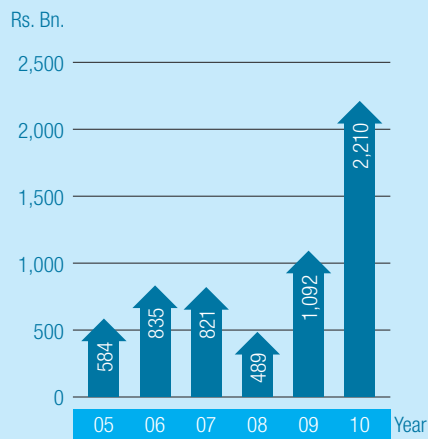
## Market Capitalization

At the end of the year 2010 the market capitalization of the CSE stood at Rs. 2.2 trillion which is an increase of more than 102% compared with the previous year. Market capitalization surpassed the Rs. 2 trillion level on 13<sup>th</sup> September 2010 amounting to approximately 42% of GDP. The market capitalization to GDP ratio is an important parameter in evaluating the depth and maturity of a share market in a country. The liquidity of the share market can be measured by the traded value to GDP ratio. In the year under review CSE's market capitalization to GDP ratio improved from 35% in 2009 to 43% in 2010.

It is significant to note that the CSE took nearly 3 decades to achieve the first trillion in terms of market capitalization but the second trillion was achieved in a mere 11 months. The end of the war against terrorism aided healthy

capital formation at the bourse. Other than price appreciation, new listings too contributed, albeit marginally, to the increase in market capitalization during 2010. (Figure : 3)

Figure : 3 Market Capitalization 2005 - 2010



Source : CSE

## Sector Index Performance

Price indices of all 20 Sectors at the CSE improved positively during the year 2010. The best five performing Sectors during the year under review are set out below: (Figure : 5)

Figure 5: Sector Index Performance

Sector	% Change
Trading	467
Stores & Supplies	321
Motors	240
Services	156
Banks Finance & Insurance	145

Source: CSE

## New Listings

The primary market witnessed renewed activity in terms of resource mobilization and a number of issues were seen during the year under review. Investor appetite for primary issues remained strong throughout the year which was evident by the last IPO for the year Singer Finance PLC being oversubscribed by 134 times.

Equity capital of Rs. 4.3 billion was raised through 8 primary issues whilst Sinhaputhra Finance Ltd and Citizens Development Business Finance entered the CSE by way of an Introduction during 2010. The conditions in the primary market further helped in maintaining the investor confidence. Capital mobilized was well distributed among all economic sectors. At the end of the year 2010 the companies listed at the CSE amounted to 241 when compared to 232 companies recorded in the previous year 2009. (Figure : 6)

Figure 6 : New Listings for 2010

Company	No of Shares Offered	Issue Price (Rs.)	Capital Raised (Rs.)
1) Renuka Agri Foods	120,000,000	2.25	270,000,000
2) Ceylon Tea Brokers	14,000,000	2.00	28,000,000
3) Raigam Wayamba Salterns	80,000,000	2.50	200,000,000
4) Vallibel Finance	5,200,000	22.00	114,400,000
5) Odel	16,700,000	15.00	250,500,000
6) PC House	57,233,300	11.00	629,566,300
7) Hydro Power Free Lanka	35,000,000	10.00	350,000,000
8) Laugfs Gas Ltd (voting)	75,000,000	23.00	1,725,000,000
Laugfs Gas Ltd (non voting)	52,000,000	15.00	780,000,000
			<b>4,347,466,300</b>

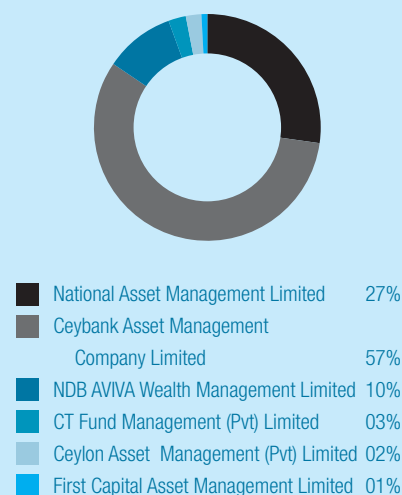
Source: CSE

Yet another initiative taken by the SEC during the year 2010 was to improve liquidity and the market turnover at the CSE. A reduction in the minimum brokerage along with a reduction of the tick size to 10 cents contributed to high trading volumes. A total of 18.4 billion shares were exchanged at the CSE in 2010 compared to 4.9 billion shares traded in the previous year 2009. A new record at the CSE was established where 36,888 trades have been executed on 21<sup>st</sup> September 2010, highest ever number of trades executed for a single day at the CSE.

## Unit Trust Funds

During the year, four new funds were launched increasing the number of funds to twenty two and the Net Asset Value of unit trust funds stood at Rs.22.2 billion (approx) as at 31 December 2010. The market share of each unit trust managing company in terms of the Net asset Value in the year 2010 is reflected in the following chart: (Figure : 7)

Figure : 7 Market Share of Unit Trust Managing Companies as at 31 December 2010



Source : Regulatory Submissions by unit trust Managing Companies

# Capital Market Review contd...

## The Overall Position of Unit Trust Funds

The comparative statistics on the performance of the unit trust funds during 2010 and 2009 are given below: (Figure : 8)

Figure 8: The Overall Position of Unit Trust Funds

	As at 31 December 2009	As at 31 December 2010	Change %
Number of unit trusts	18	22	22.22
Net Asset Value of unit trusts (Rs. Mn. approx)	9,952	22,228	123.35
Number of unit holders	23,117	24,649	6.63
Number of units issued (No. Mn. approx)	565	1,159	105.13
Investment in Equity (Rs. Mn. approx)	6,036	11,349	88.02
Investment in treasury bills (Rs. Mn. approx)	3,363	9,289	176.21
Investment in other instruments <sup>1</sup> (Rs. Mn. approx)	1,106	1,223	10.58

Source: Regulatory submissions by unit trust managing companies

<sup>1</sup>commercial papers, trust certificates, debentures and bank deposits

*The Net Asset Value of unit trust funds stood at Rs.22.2 billion as at 31 December 2010, an Increase of 123.35% over 2009*

# Operational Review

## 1. Regulation

Effective regulation lays the foundation for investor confidence, supports efficient functioning of the capital market and thereby builds the platform for economic growth. In addition we attempt to ensure that our regulatory environment is relevant and effective and that our Securities law is tailored to meet the needs of the market and international best practices.

### 1.1 Licensing and Registrations

Companies that intend to obtain a licence to carry out the functions of a stock broker or a stock dealer has to first obtain a provisional membership from the CSE as a Trading Member. Upon such provisional membership being granted, and on an application being made to the Commission, a licence would be granted to such provisional member to carry out functions as a stock broker or stock dealer.

Unit trust funds are managed by Managing Companies subsequent to obtaining requisite licences from the SEC and are managed as per the SEC Act No. 36 of 1987 (as amended), the Unit Trust Code of 2004 and the Directives issued by the SEC from time to time.

In addition, we grant Certificates of Registration to all Market Intermediaries

to carry out the provision of financial services as underwriters, margin providers, credit rating agencies, investment managers and clearing houses. The table below indicates the licences and registrations granted during the year 2010 (Figure : 9).

**Figure 9: Licensing and registration of market participants**

Market Participant	No. of licences/ Registrations
Stock exchanges	01
Stock broking companies	26
Stock dealer in equity securities	02
Stock dealer in debt securities	03
Managing companies of unit trusts	06
Investment managers	18
Margin providers	23
Underwriters	10
Credit rating agencies	02
Clearing house	01

During the year under review the following companies were issued with new licences to operate as stock brokers:

- IIFL Securities Ceylon (Private) Limited
- Claridge Stock brokers (Private) Limited
- LOLC Securities Limited
- Richard Pieris Securities (Private) Limited
- TKS Securities (Private) Limited

During the year under review the following company was issued with a new licence to operate as a stock dealer in debt securities:

- First Capital Markets Limited

The following Managing Companies of unit trusts were granted licences to manage and operate the following funds:

- Ceybank Asset Management (Pvt) Ltd. to operate 'Ceybank Surakum' Fund
- Ceylon Asset Management Company Ltd to operate 'Ceylon Financial Sector Fund' and 'Ceylon Tourism Fund'
- Namal Asset Management Company Limited to operate 'Namal HNB Fund'
- Ceylon Asset Management Company Ltd to operate 'Ceylon Tourism Fund'

### 1.2 Regulatory Developments Introduction of Exchange Traded Funds

Technical expertise was obtained from Securities and Exchange Board of India (SEBI) to introduce Gold and Index based Exchange Traded Funds (ETFs) in Sri Lanka. A gap review of the present regulatory framework relating to unit trusts was carried out in order to assess the possibility of incorporating ETFs within the existing legal framework of unit trusts. Based on the outcome of the gap review and with the assistance

**Licences were issued to 5 Stock Brokers, 5 Investment Managers, 9 Margin Providers, 3 Underwriters and 1 Stock Dealer in 2010**

# Operational Review contd...

of the technical expertise of the SEBI we proceeded to amend the Unit Trust Code, 2004. Gazetting of the Unit Trust Code is Pending.

## **Amendments to the Takeovers and Mergers Code (TOM)**

We initiated the process of amending the TOM Code in order to remedy certain lacunae in the said law.

The amendment process is being spearheaded by Justice Saleem Marsoof P.C., Honourable Judge of the Supreme Court of Sri Lanka. We conducted consultations with market participants in order to solicit expert opinions and views of the market on the proposed amendments to the TOM Code. The final draft is under preparation.

## **Rules on Outsourcing by Stock Exchanges**

We developed guidelines pertaining to outsourcing of functions by Exchanges, Central Depositories and Clearing Houses inline with the principles of IOSCO relating to the same.

## **Dematerializing Accounts for Listed Securities**

Pursuant to consultations with relevant parties, we were of the view that mandating the lodging of certificates pertaining to all listed securities in the CDS and thereby implementing a system of dematerialization for all listed securities is appropriate to increase liquidity in the market. Accordingly a directive was issued to the CSE and CDS to implement same in several stages.

## **Rules on Internet Trading**

Guidelines were proposed to regulate internet trading in order to promote confidence and fairness in the method of internet trading. The CSE currently

provides a gateway to facilitate electronic order routing via stock brokers, but there was no regulatory framework in place.

In a bid to remedy this lacuna guidelines were proposed to ensure that the internet trading service provider has satisfactory arrangements in place to safeguard the integrity of the service and to prevent misappropriation of identities, impersonations leading to unauthorized and illegal transactions and unauthorized usage. These guidelines have been forwarded to the CSE for their observations.

## **Gazetting Amendments to the CESS in Accordance with Sec. 14 (A) of the SEC Act**

Subsequent to the policy decision taken to reduce the transaction cost pertaining to securities trading, we initiated the process of gazetting the amendments to the CESS relating to securities trading on an order made by His Excellency the President as Minister of Finance in Gazette Extra Ordinary No. 1680/26 dated 19<sup>th</sup> November 2010.

## **Amendments to Rules of the CSE and CDS**

The amendments to the Listing Rules of the CSE and the Rules of the CDS as proposed by the CSE were reviewed prior to granting of the Commission's approval.

## **Demutualization of the CSE**

A draft Cabinet Memorandum was submitted to the Ministry of Finance and Planning to obtain the approval of the Cabinet of Ministers for the Demutualization of the CSE by way of enacting a Special Act of Parliament. The Cabinet of Ministers approved in-principle the conversion of the present mutually owned CSE which operates

as a company limited by guarantee to a Demutualized Stock Exchange which will operate as a company limited by shares by way of a Special Act of Parliament and also directed the SEC to propose the changes necessary to the SEC Act to enable the regulation of a Demutualized Exchange. Accordingly we took steps in this regard.

## **Minimum Public Float for Listed Companies**

A consultation paper was submitted to implement a minimum public float as a continuous listing requirement for all listed entities. The views of the public have been solicited in this regard.

## **Amendments to the SEC Act (as amended)**

To ensure the relevancy of the legal framework to meet challenges defined by the evolving needs of the capital market, we took steps to identify relevant provisions that may be needed to regulate demutualized securities exchanges and also identified provisions that are necessary for the smooth functioning of a Central Counter Party.

## **Regulation of Employee Share Option Schemes**

A Consultation Paper was released to the market to obtain the views of the public on Employee Share Option Schemes and the draft rules were released for public comments. We are in the process of finalizing the rules for implementation.

## **1.3 Directives and Guidelines Issued by the SEC**

In order to implement the policy initiatives taken by the Commission from time to time we issued the following directives/guidelines.

- To restrict directors of Public Listed Companies whose securities have been transferred to the Default Board of the CSE for non submission of annual reports and financial statements from trading in those securities.
- To the CSE and the CDS and all stock brokers in respect of the policy initiatives taken to reduce transaction costs and changes to the market microstructure.
- To take interim measures in respect of mitigating the imminent risk of settlement default by Member Firms.
- To impose trading halts in respect of 5 connected Public Listed Companies after being informed of the acquisition of two listed companies by LOLC Securities Limited until such time the information relating to the said acquisition was properly disseminated to the market.
- To incorporate disclosure requirements in the Listing Rules of the CSE in respect of related party transactions of Listed Entities
- To impose trading halts in respect of securities of Listed Companies showing an undue price increase (30% or over) during the market days of 29<sup>th</sup> & 30<sup>th</sup> July and 2<sup>nd</sup> August 2010, provided the trade volume was more than 1000.
- To impose a 10% upward and downward price band on all listed securities.
- To lift the price band on all listed securities and the imposition of the 10% price band to listed securities

falling within a special formula (based on price volatility and the volume traded adjusted to public holding) on a daily rollover basis for the preceding review period of 5 market days and for connected matters subject to certain specified exceptions.

- To mandate all stock broking companies to obtain not less than 50% of the settlement value upfront in the form of realized funds from all investors who purchased securities which were subject to the price band mentioned above.
- To impose restrictions on the extension of credit to clients by all stock broking companies.
- In respect of the rules governing the granting of approvals to the issue of share warrants by all Public Listed Companies.
- To mandate all securities of new listings to be in dematerialized form with effect from 1<sup>st</sup> January 2011 and on connected matters thereto.
- To mandate the members of the CSE to force- sell securities which are in default of payment by T+3 days.
- A regulation by way of gazette notification was issued prescribing 20% as the permitted percentage holding to determine 'Connected Persons' in respect of the relationship between a Trustee and a Managing Company of a unit trust.
- To revise the existing investment restriction with regard to single entity exposure, whereby a fund

was restricted from having an exposure of more than 15% of the Net Asset Value or percentage of the approved index's market capitalization (whichever is higher) subject to a cap of 10% of the investee company's' voting share capital.

- Managing Companies and Trustees were directed to use the weekly data published by the CBSL for treasury bills and bond securities when constructing the weekly updated yield curve in order to calculate the present value of debt securities.

#### 1.4 Administrative Actions Companies on the Default Board of the CSE

We have been closely monitoring the compliance of companies that are on the Default Board of the CSE which have been referred to the SEC by the CSE. These companies have been transferred to the Default Board for the non submission of their annual reports to the market. Administrative steps are taken as an initial measure to ensure that these companies release the annual reports to the market and legal action was instituted by the SEC against those companies who failed to respond to the administrative efforts of the SEC.

During the year under review legal action was instituted against one company and the matter is pending in the Magistrates Court Colombo Fort. Legal actions instituted against two companies previously were withdrawn after the said companies released their outstanding annual reports to the market.

# Operational Review contd...

A directive was issued on one listed company which has been on the default board for a number of years to take steps to release the annual reports to the market or in the alternative to make an announcement to the market explaining as to why it is unable to release such reports to the market. We issued this directive to the said Public Listed Company since there were several court cases pending in relation to the affairs of the company including a winding up application and the company has been restrained by way of several injunctions from performing various functions relating to the financial matters of the company

## Stock Broking Companies

- A stock broking company was cautioned with regard to a complaint made by a client in respect of the manner in which trades have been carried out in the client's account. The company was cautioned to exercise due care and diligence

in conducting trades on behalf of its clients and to desist in the future from engaging in business practices which would appear to the Commission to be oppressive or otherwise improper or would reflect discredit on methods adopted by the company in conducting business.

- A stock broking company was directed to obtain clearance from a client in respect of a letter of demand issued by the client for approximately Rs. 89 million. The licence was renewed only after we received documentary evidence confirming that the client had released the stockbroker from all liability in respect of the letter of demand.

## 1.5 Approvals

### Approvals Granted to Global, Regional and Country Funds

Upon the recommendation of the CDS we grant approval to global, regional and country funds to invest in shares of

companies listed on the CSE. Approval is granted subject to compliance with Exchange Control Regulations, Prevention of Money Laundering Act No. 5 of 2006, Financial Report Transactions Act No.6 of 2006 and the law relating to securities in Sri Lanka.

During the year under review approval was granted to 123 global, regional and country funds and acknowledged name changes of 30 funds.

### Offers Extended Under the Takeovers and Mergers Code

The Takeovers and Mergers Code of 1995 as amended in 2003(Code), applies to takeovers and mergers where the offeree is a listed public company. The code seeks to ensure equal treatment of all share holders of the same class in the company sought to be taken over. The rules of the Code are aimed at ensuring dissemination of sufficient information and advice with adequate time to the shareholders of

Figure : 10 Offers extended in 2010, under the TOM Code

Offeror	Offeree	Nature of the offer
Acuity Partners (Pvt) Ltd	Lanka Ventures PLC	Mandatory Offer
Carbotels (Pvt) Ltd	Hunas Falls Hotels PLC	Mandatory Offer
Environmental Resources Investment PLC	Colombo Pharmacy Company PLC	Mandatory Offer
Environmental Resources Investment PLC	Dankotuwa Porcelain PLC	Mandatory Offer
Hayleys PLC	Hotel Services (Ceylon) PLC	Mandatory Offer
Jetwing Hotels Management Services (Pvt) Limited	Lighthouse Hotel PLC	Mandatory Offer
Lankem Ceylon PLC	C.W Mackie PLC	Mandatory Offer
LOLC Securities LTD	Confifi Hotel Holdings PLC	Mandatory Offer
Flyasia SDN.BHD	Infrastructure Developers PLC	Mandatory Offer
Mr. Vijayeswaran S Vijayaratham	Asia Capital PLC	Mandatory Offer
Asiri Hospital PLC	Asiri Surgical Hospital PLC	Mandatory Offer
Cargills (Ceylon) PLC	Kotmale Holdings PLC	Mandatory Offer
Softlogic Holdings Limited	Asiri Hospital Holdings PLC	Mandatory Offer
Capital Alliance Holdings Limited	Watapota Investments PLC	Voluntary Offer



the target company in order for them to arrive at an informed decision relating to the takeover.

We ensure that persons adhere to the provisions of the Takeovers and Mergers Code in respect of the acquisition of listed companies. Approvals are granted to market announcements, offer documents and independent valuation reports in the takeover process of public listed companies in terms of the Takeovers & Mergers Code.

The Code deals with three types of offers namely Voluntary Offers, Partial Offers and Mandatory Offers. During the year under review we administered one Voluntary Offer and 13 Mandatory Offers (Figure 10).

#### Approvals Under Section 29A of the SEC Act

In terms of Section 29A of the SEC Act, applications relating to issuance of unlisted securities by listed companies need to be submitted to the SEC.

During the year under review, we

reviewed and approved the following applications relating to the above. (Figure 11).

#### Approvals Under Section 28A of the SEC Act

All public companies seeking listings on the CSE are not allowed to list shares which have been allotted to any person within a period of one year prior to its listing on an Exchange, unless the prior written approval of the Commission is obtained for that purpose. A new set of guidelines was adopted (Circular No.02/2010) when granting approvals to applications under Section 28A of the SEC Act (as amended).

During the year under review, the following entities were granted approval to list the shares which were allotted within a period of one year prior to listing, subject to the conditions stipulated in Circular No.02/2010.

- Wayamba Salterns Ltd
- Commercial Credit Limited
- Edirisinghe Trust Investments Ltd

- Laugfs Gas Ltd
- Senkadagala Finance Company Limited

#### Approvals Granted to Unit Trust Funds

Approval was granted to National Savings Bank to provide Trustee services for unit trust funds of Ceybank Asset Management (Pvt) Ltd.

Approval was granted to NDB Aviva Wealth Management Company to change the name of 'Pyramid Unit Trust' to 'Eagle Growth and Income Fund'.

#### Approvals of Off-the-floor Share Transactions

In terms of Section 28 (1) of the SEC Act "no person holding securities in a public company listed in a licensed stock exchange shall without the prior approval of the Commission buy, sell, gift or otherwise deal in such securities except in compliance with trading procedure adopted by such licensed stock exchange"

Figure : 11 Approvals granted to issue unlisted securities

Name of the Issuer	Nature of the Issue	Type of Security
Merchant Bank of Sri Lanka	Private Placement	Unlisted Debentures
Singer (Sri Lanka) PLC	Private Placement	Unlisted Debentures
Hemas Power PLC	Private Placement	Unlisted Preference Shares
Ceylon Tea Brokers PLC	Private Placement	Unlisted Debentures
Ceylon Guardian Investment Trust PLC	Bonus Issue	Unlisted Deferred shares
Merchant Bank of Sri Lanka	Private Placement	Unlisted Debentures
Seylan Bank PLC	Private placement	Unlisted Debentures
Citizens Development Finance Limited	Private Placement	Unlisted Debentures
Alliance Finance Company	Private Placement	Unlisted Debentures
Lankem Ceylon PLC	Private Placement	Unlisted Debentures

# Operational Review contd...

Approval was granted for 643 exceptional transfers and 296 gifting of shares during the year under review. The exceptional transfers were in order to facilitate margin trading, fund management, de-listing and restructuring of entities and portfolios, where beneficial ownership does not change.

## 2. Oversight and Compliance

The supervisory role of the SEC involves monitoring and supervising the financial viability and business conduct of market participants using a variety of techniques aimed at detecting companies and activities that could pose a risk of failure and impact the integrity of the markets. Our on-going oversight system monitors the compliance of market participants with relevant laws, rules and regulations.

### 2.1 Listed Companies

All listed companies are required to submit annual reports within five months from the close of the financial year to their shareholders and the CSE. This requirement is to ensure that listed companies disseminate material information promptly in order to establish transparency and accountability in the Securities Market, and to ensure that professional standards are maintained.

We review annual reports of listed companies, and matters relating to non-compliance are communicated to companies. The objective of this exercise is to enhance the quality of financial reporting and dissemination of information by listed companies.

In reviewing the annual reports we focused on the following areas:

- Compliance with CSE Rules, Sri Lanka Accounting Standards (SLAS) and relevant provisions of the Companies Act
- Financial Highlights
- Chairman's Report
- Corporate Governance Practices
- Report of Directors
- Report of Auditors
- Shareholder and Investor Information
- Financial Data

During the year we reviewed 127 annual reports of listed companies and issued 5 Letters of Caution and 39 Letters of Comments.

This process contributes to improving the level of awareness of companies regarding the obligations placed upon them in the preparation and presentation of annual reports and accounts.

### 2.2 Stock Broking Companies

The SEC Act requires all stock broking companies to obtain a licence in order

to carry on the business of a stock broker. The licence is granted by assessing compliance with the relevant rules and regulations of the SEC and the CSE Member Regulations with regard to stock broking companies. We ensure that the companies are financially stable and operationally viable through on-site and off-site supervision. Onsite supervision is carried out using an internally developed risk based audit programme adopting a risk based supervisory methodology focusing on different risk categories such as prudential, liquidity, financial, credit operational, legal and reputational risk. Off-site supervision is carried out by checking the unaudited accounts and other returns that are required to be submitted according to a pre defined format provided by the SEC.

The comparative statistics on the performance of the stock broking companies during 2010 and 2009 are given below: (Figure 12)

Figure : 12 Highlights of the stock broking industry

	2010 (Rs.'000)	2009 (Rs.'000)	Change %
Turnover	6,599,034	1,944,092	239%
Net brokerage	6,263,284	1,802,967	247%
Operating profit/loss	3,975,966	911,744	336%
Other income	642,220	375,235	71%
Net profit before tax	3,660,906	822,484	345%
Net profit after tax	2,677,250	636,665	321%
Total assets*	13,209,720	6,429,267	105%
Total liabilities *	6,972,786	3,826,959	82%
Net capital*	4,467,936	2,075,953	115%

\*As at 31st December 2010/2009

Source: Unaudited financial statements submitted to SEC

The year 2010 was a robust year for the industry, the total turnover demonstrated an increase of 239% and the total asset base grew by 105 % during the year.

On-site inspections were carried out on 10 stock broking companies adopting a risk based supervisory methodology focusing on different risk categories such as prudential, liquidity, financial ,credit operational, legal and reputational risk. Subsequent to the on-site inspection, a report on the findings was sent to the stock broking companies notifying the areas of non compliance and recommendation for implementation of a more effective risk management framework. Considering the seriousness of non compliance and the risk impact, meetings were held with requisite companies to ensure compliance. The three main areas of focus in the off-site reviews were compliance with the net capital requirement, adequacy of client funds, and the liquidity requirement. We received financial statements and the Compliance Officer's Report of stock broking companies on a monthly basis. Compliance with the net capital requirement was monitored by reviewing the monthly financial statements of the stock broking companies. All licensed stock broking companies maintained the minimum net capital requirement throughout the year 2010.

As per the off-site review one stock broking company did not maintain adequate client funds in the client bank accounts to meet the creditors over T+3 during the months of January, March, May, June, July, August 2010. After continuous dialogue with the company, SEC issued a letter of "show

cause" to the company in July 2010. In September 2010 the company was able to rectify the issue by arranging a line of short term financing which would be available to the company to meet client fund requirements.

The electronic filing system which was initiated to reinforce off-site supervision of stock brokers was completed during the year and presently the project is at a test run stage.

Due to the vibrant nature of the industry and the growing turnover and volume of trades the SEC issued new directives during the year 2010 to condense the credit risk of the industry. This was also implemented with a view to reducing the overall systemic risk. In September 2010 SEC issued a directive which mandated all stock brokers to refrain from extending credit to clients beyond T+3 days with effect from 1 January 2011 and if credit is to be extended to do so only through a margin provider. Further the directive required that any backlog of credit already extended to be cleared or regularized through a margin provider by 1 January 2011. Consequently having considered the representations made by the Colombo Stock Brokers Association and certain other market participants another directive was issued in November 2010 which stated that while the directive issued in September 2010 stands in force , the commission granted the permission to the stock broking companies to reduce their current debtor position at least by 50% by 31 March 2011 and by 100% latest by 30 June 2011. The said directive was made by the commission as a consideration of granting the small time investors additional time to clear their current outstanding positions. In December

2010 ,SEC issued a new directive which mandate the stock brokers to force-sell by T+5 days if the buyer of securities is in default of settlement by T+3 days.

All the said directives were issued with the aim of reducing the total debtor position of the industry, which stood at a high level of Rs. 5.7 billion. With these latest developments in the regulatory frame work, on-site and off-site supervision would be more focused on probing the debtor exposure of the stock broking industry with more stringent supervision on credit risk during the year ahead.

### 2.3 Unit Trust Managing Companies

All unit trust managing companies as defined under the SEC Act are required to obtain a licence to operate a unit trust fund. During the year, the supervision team completed risk-based on-site examinations of three unit trust managing companies encompassing a wide range of risk areas under prudential, operational and management policies to assess adequacy of their financial strength, compliance with internal controls and procedures, governance, information systems, rules and regulatory requirements and identified areas for improvement. During our on-site reviews, the unit trust managing companies were requested to have an appropriate risk management framework in place. The managing companies were found to be compliant with the relevant rules and regulations pertaining to operations of unit trusts.

In line with our objective towards promoting highest professional standards in the unit trust industry,

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we undertook two on-site visits to the trustees during the year 2010. Our objective was to ensure that the trustees have taken reasonable care that the managing companies manage the unit trust funds in accordance with the provisions of the unit trust code, relevant directives issued by the Commission and the trust deed. In addition we required the trustees to maintain financial independence and adequacy of systems to ensure that their duty as a trustee towards the investors is performed adequately.

We examined the monthly unaudited financial statements submitted by the unit trust managing companies to ensure that the managing companies were financially stable and maintained the minimum net capital requirement as stipulated by the SEC. In addition, monthly returns of the unit trust funds were scrutinized to ensure that exposure levels of the unit trusts were within acceptable limits as set in the unit trust Code, the relevant trust deeds and the directives issued by the Commission. The managing companies were informed of any deviations from requirements observed in respect of the unit trust funds, and were requested to be compliant. In addition, advertising material, press releases, interim reports and annual financial statements of unit trust funds were approved.

## 2.4 Market Intermediaries

The SEC is entrusted with the task of registering all market intermediaries and ensure that they comply with applicable rules and regulations.

A major thrust of our work for the year 2010 involved heightening market oversight on market intermediaries and granting new registrations. Through

a variety of rulemaking and other initiatives, the SEC continued to refine its regulations in order to promote growth and competitiveness of the market whilst protecting the interest of the investor.

We carried out on-site supervision of three investment managers, four margin providers and one credit rating agency in the year 2010.

As a measure to alleviate the risk exposure, the Margin Provider Rules were amended during the year such that Institutions that are not registered under the CBSL are required to maintain the Margin Provider's exposure against the aggregate value of loans extended as margin and should at no time exceed four times the value of its net capital from the current ten times. This limit was reduced to mitigate the risk exposure borne by the Margin Provider.

## 3. Monitoring and Enforcement

We engage in real time monitoring of the market to detect abnormal market movements and manipulations in order to protect the integrity of the securities

market and its participants. Meanwhile our enforcement programme ensures compliance with securities regulation and is designed to foster a fair, transparent and stable market.

### 3.1 Complaints

We receive and assess complaints concerning alleged misconduct in the capital market. We handled 50 complaints and resolved 49 during the year under review. (Figure : 13)

### 3.2 Market Surveillance and Investigations

We undertake frontline market surveillance functions and monitor trading activities of the CSE on a real time basis to detect irregular market activities. We conduct in-depth surveillance analysis of trading data, review surveillance reports received from CSE, prepare surveillance reports and make recommendations on appropriate action to be taken in relation to surveillance findings. We adopt an appropriate surveillance framework and systems to ensure objectivity and consistency in enforcement action on offenders.

Figure : 13 Details of complaints

Nature of The Complaint	Number
1. Complaints against brokers & unauthorized transactions	14
2. Breach of CSE Listing Rules by improper conduct of Listed Companies or their officers	19
3. Rights Issues/Bonus Issues/Dividends Payments	7
4. Market manipulation	1
5. Issues pertaining to Initial Public Offerings	5
6. Policy matters	4
<b>TOTAL</b>	<b>50</b>

### Surveillance

In the year 2010, We forwarded 30 referrals to the Surveillance and Investigations Committee of the SEC for perusal. 33% detections were possible cases of insider dealing, 27% - market manipulations, 7% - were reported as front running whilst the remaining 33% issues related to takeovers and mergers, rumour verifications and dealing by directors of Default Board companies. (Figure 14)

The new automated Surveillance system which we negotiated and acquired from the Millennium IT (Software) Limited (MIT), a member of the London Stock Exchange was installed during the third quarter of the 2010. The new system is being tested with live data of the CSE for bug fixing and fine tuning. The MIT new

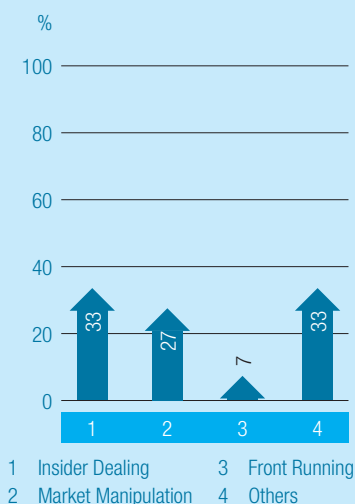
system would support multidimensional historical data, have the capability for pattern recognition to quickly identify abnormal situations/transactions, and provide an analytic platform that supports and accelerates investigations and research functions of the SEC. The system can be linked to several data bases of insiders of listed companies, their related parties and market intermediaries to accommodate speedy detection of insider dealing.

investigations were conducted and the individuals were charged prior to 2010) were compounded upon payment of Rs. 1 million by one individual and Rs. 3.3 million by each of the other two individuals to the compensation fund.

### Investigations

A total of 20 investigations were conducted in the year 2010. During the year 2 investigations were suspended owing to the reason that the issues relating to the said investigations form the subject matters of pending litigation. In addition, cases against three individuals (regarding which

Figure 14: Surveillance detections



1. Insider Dealing: Trading in the shares of a listed company whilst in the possession of unpublished price sensitive information in respect of the securities of the said Company
2. Market/Price Manipulation: Creation of a false or misleading appearance in respect of the trading, or the price of any securities listed on a stock market.
3. Front Running: Trading in securities of a Company ahead of a significant purchase or sale of securities of such Company, for a client, with the intent to profit by trading in the said securities thereafter.

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The details and a brief description of the action taken/current status of the said investigations are given below: (Figure : 15)

**Figure 15: Detail of Investigations**

Nature of the Investigation	No. of Investigations	Action Taken/Current Status
Insider Dealing	05	<ul style="list-style-type: none"> <li>At the end of the year 2009, two investigations into suspected Insider Dealing were pending. At the conclusion of the said investigations it was opined that based on the material/evidence elicited during the course of the said investigations Insider Dealing beyond reasonable doubt could not be legally sustained against the investors concerned. However, both such investors being Directors of two Listed Companies have purchased shares of the respective companies whilst the Boards of Directors of the said Companies were discussing dividends. Therefore, the SEC cautioned both individuals in writing.</li> <li>Subsequent to conducting an investigation into a particular matter, the said matter was terminated without taking any enforcement action due to the absence of evidence to legally sustain a case of Insider Dealing against the investor concerned.</li> <li>At the end of the year 2010, two investigations into suspected Insider Dealing were pending.</li> </ul>
Market/Price Manipulation	06	<ul style="list-style-type: none"> <li>During the year 2007, the opinion of the Hon. Attorney General was sought to establish whether the SEC could conduct an investigation relating to a particular matter whilst there was on-going litigation in connection with the said matter. The Hon. Attorney General advised to suspend the said investigation until the finality of the pending litigation. Hence the matter was suspended in the year 2010.</li> <li>An investigation into suspected market/price manipulation was terminated in the absence of material/evidence to legally sustain a case of market/price manipulation against the investors and/or the broking firm concerned.</li> <li>At the end of the year under review, four investigations into suspected market/price manipulation were pending.</li> </ul>
Business affairs of a listed company	01	<ul style="list-style-type: none"> <li>At the end of the year under review, an investigation into business affairs of a listed company was pending.</li> </ul>
Non-submission of audited financial statements by a listed company	01	<ul style="list-style-type: none"> <li>At the conclusion of an investigation into non-submission of audited financial statements by a listed company, legal action was instituted against the said entity. At the end of the year under review the said litigation was pending.</li> </ul>
Suspected forgery	01	<ul style="list-style-type: none"> <li>An investigation into suspected forgery relating to written communications submitted to the CSE by certain investors was conducted in the year under review. In the absence of material/evidence to legally sustain a case of forgery against the investors and/or the broking firms concerned the said investigation was terminated without taking any enforcement action.</li> </ul>

Nature of the Investigation	No. of Investigations	Action Taken/Current Status
Carrying on regulated activity without obtaining a licence/certificate of registration from the SEC	01	<ul style="list-style-type: none"> <li>Based on the findings of an investigation into carrying on regulated activity (which required a licence/certificate of registration to be obtained from the SEC) by a business entity without obtaining such licence/certificate of registration, the SEC severely reprimanded the sole director thereof and the said reprimanding was publicized.</li> </ul>
Non-compliance with the Listing Rules of the CSE by a listed company	01	<ul style="list-style-type: none"> <li>At the time of the commencement of this investigation, it was found out that the listed entity concerned has not complied with certain provisions of the Listing Rules of the CSE. However, subsequent to receiving a communication from the SEC in this regard, the entity has become compliant with the Continuing Listing Requirements of the CSE. Hence, this matter was terminated without taking any enforcement action against the company.</li> </ul>
Complaints	01	<ul style="list-style-type: none"> <li>Deliberations relating to a complaint were suspended until the finality of certain on-going litigation since the issues pertaining to the said complaint form the subject matter of pending litigation.</li> </ul>
Irregularities in connection with mandatory offers	01	<ul style="list-style-type: none"> <li>An investigation in connection with suspected irregularity pertaining to the offer price in respect of a mandatory takeover offer relating to the shares of a Listed Company was conducted by the Division. This investigation was terminated in the absence of material/evidence which established that such an irregularity has occurred.</li> </ul>
Front Running	01	<ul style="list-style-type: none"> <li>An investigation was pending at the end of the year 2009 which was concluded in the year under review. In the absence of evidence to legally sustain a case of Front Running against the investors concerned the matter was terminated without taking any enforcement action.</li> </ul>
Submission of false and/or misleading information to the SEC	01	<ul style="list-style-type: none"> <li>An investigation was pending at the end of the previous year and the said investigation was concluded this year. At the conclusion of the same, it was opined that the entity concerned (a licensee of the SEC) has in fact provided the SEC with inadequate information which was misleading. Having obtained the formal opinion of the Hon. Attorney General in this regard the SEC warned the said entity in writing.</li> </ul>

### 3.3 Litigation

Over the years we have built a comprehensive and facilitative legal framework to ensure adequate protection for investors and create a fair, transparent and orderly market.

#### Cases Filed by the SEC for Capital Market Offences:

**SEC vs. B.A Jayasekera and Eight Others**  
Nine accused in this case were charged in the Colombo Fort Magistrate's Court

for market manipulation in respect of the shares of Nawaloka Hospitals PLC. The case is pending in respect of the 4<sup>th</sup>, 5<sup>th</sup>, 6<sup>th</sup>, 7<sup>th</sup> and 9<sup>th</sup> accused. Earlier the Commission with the permission of Court and the Attorney General compounded the offence in respect of the 1<sup>st</sup>, 2<sup>nd</sup> and 8<sup>th</sup> accused on their payment of a sum of Rs. 3.3 million each to the Compensation Fund of the Commission and withdrew the charges subject to a sever reprimand in respect

of the 3<sup>rd</sup> accused on the advice of the Hon. Attorney General.

#### SEC vs. Sunil Piyawardene and one Other SEC vs. C. Piyawardene

The accused, all members of the same family were charged with having traded in the shares of Nawaloka Hospitals PLC on the basis of profiting from price sensitive information they possessed prior to the release of such information to the Market.

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The Commission having considered several appeals made by the accused compounded the offence in respect of the 1<sup>st</sup> and 2<sup>nd</sup> accused and withdrew charges against the 3<sup>rd</sup> accused after obtaining the advice of the Hon. Attorney General and with the permission of Court after they paid a sum of Rs. 6.6 million to the compensation fund of the Commission.

### ***SEC vs. Magpek Exports Ltd.***

The SEC filed charges against the Company and eight of its Directors in the Colombo Fort Magistrate's Court for not immediately disclosing certain material information to the market in contravention of the SEC Rules. The learned Magistrate after summary trial fined the Directors Rs.2.5 million each on each count and sentenced them each to a two year prison term.

The accused have appealed against their conviction and sentence to the High Court of the Western Province and the matter is pending.

### ***SEC vs. R. Navaratnam and One Other***

Charges were filed in the Magistrate's Court Fort against the former chairman and a key employee of Singalanka Standard Chemicals PLC for the submission of the annual reports with the forged signature of the auditors in the financial statement of the company thereby committing an offence under Section 51(1) (b) of the SEC Act and in contravention of Rule 17 of the SEC Rules and the continued listing requirements of the Listing Rules of the CSE.

The key employee, the second accused pleaded guilty to 5 counts out of 15 charges and the court imposed a fine in respect of four of the counts and a 6 months prison sentence suspended

for a period five years in respect of the 5th count. The offence against the 1<sup>st</sup> accused was compounded after a payment of Rs. 1 million to the Compensation Fund of the SEC with the permission of Court after obtaining advice from the Hon. Attorney General as the 2<sup>nd</sup> accused pleaded guilty to the charges.

### **For the Violation of SEC Rules and the Listing Rules of the CSE**

#### ***SEC vs. Tuan N. Dole and One Other***

The SEC filed charges against two directors of Alufab PLC for their failure to release the Annual Reports and the Audited Financial Statements of the Company to the market for the years ended 31<sup>st</sup> March 2004 to 31<sup>st</sup> March 2009 in contravention of the SEC Rules and the Continuing Listing Requirements of the CSE enumerated in the Listing Rules of the CSE. The matter was settled in Court after the Company complied and submitted the Audited Financial Statements of the Company to the market for the years ended 31<sup>st</sup> March 2004 to 31<sup>st</sup> March 2009.

The SEC strongly advised the Company to act with responsibility towards complying with the continued listing requirements of the CSE within the time limits prescribed in the Listing Rules of the CSE rules and to ensure that similar omissions are not repeated in the future.

#### ***SEC vs. Asia Capital PLC and others***

The SEC filed two cases against the Company in Colombo Fort Magistrate's Court for their failure to release the Annual Reports of the Company to the market for the years ended 31<sup>st</sup> March 2008 and 31<sup>st</sup> March 2009 in contravention of the SEC Rules and the Continuing Listing Requirements of the

CSE enumerated in the Listing Rules of the CSE. The matter was settled in Court after the Company complied and released the Annual Reports of the Company to the market for the years ended 31<sup>st</sup> March 2008 and 31<sup>st</sup> March 2009.

The SEC strongly advised the company to act with responsibility towards complying with the continued listing requirements of the CSE within the time limits prescribed in the Listing Rules of the CSE rules and to ensure that similar omissions are not repeated in the future.

#### ***SEC vs. Miramar Beach Hotels PLC and Others***

Charges were filed in the Magistrate's Court Fort against Miramar Beach Hotels PLC and three Directors of the Company for non-submission of Annual Reports of the company for the financial years ended 31<sup>st</sup> March 2008 and 31<sup>st</sup> March 2009, in contravention of Rule 3 (1) and 17 of the SEC Rules. The matter is pending in Court.

### **Cases Filed Against the SEC**

#### ***Jetwing Hotel Management Services (Pvt) Ltd. vs. SEC***

The SEC by its letter dated 21<sup>st</sup> May 2009 directed the petitioner Company to make a mandatory offer to all shareholders of Galle Lighthouse Hotel PLC after the petitioner crossed the shareholding threshold of 30% in Galle lighthouse Hotel PLC, in terms of Rule 31 of the Company Take-overs and Mergers Code (TOM Code). The Petitioner Company challenged the SEC directive and filed an application in the Court of Appeal seeking inter alia a Writ of Certiorari to quash the directive of the SEC and for a writ prohibition on the SEC from taking enforcement action against the petitioner for violating the



provisions of the TOM Code. Hayleys PLC also filed papers to intervene in the matter and was granted permission by Court. This matter was settled after the Petitioner Company agreed to abide by the Directive of the SEC and withdrew the case against the SEC.

***Touchwood Investments PLC vs. SEC***  
The SEC by its directive dated 9<sup>th</sup> March 2007 directed the petitioner company to prepare financial statements for the years ended 31<sup>st</sup> March 2005 and 2006 on a cost basis in terms of IAS 41. The Company was allowed to deviate from the cost basis in the preparation of financial statements only for periods commencing after 1<sup>st</sup> April 2006 provided the approval of the Sri Lanka Accounting and Auditing Standards Monitoring Board was obtained in that respect.

This directive was issued consequent to an inquiry carried out by the SEC pursuant to which a decision was obtained from the Sri Lanka Accounting and Auditing Standards Monitoring Board (SLAASMB) in determining the accuracy and reliability of the financial statements of the company for the years ending 31.3.2005 and 31.3.2006 which were disseminated to the market. The determination of the SLAASMB was that the financial statements issued for the years ending 31<sup>st</sup> March 2005 and 2006 were unreliable.

The petitioner Company filed two applications in the Court of appeal against both the SLAASMB and the SEC seeking writs of certiorari quashing both the determination of the SLAASMB and the directive of the SEC.

The Court of Appeal issued a writ of certiorari in favour of the petitioner

company quashing the determination of the SLAASMB made against the petitioner company. The SLAASMB has filed special leave to appeal to the Supreme Court against the judgment of the Court of Appeal and the matter is pending in the Supreme Court.

Since the Supreme Court decision will have a bearing on the case against the SEC, the Court of Appeal laid by the case against SEC pending the decision of the Supreme Court in this matter.

#### **Cases where SEC was Made an Additional Party**

*NDB vs. Fast Grain International Ltd., Singapore*

*NDB vs. Catana Ltd., Bahamas*

*NDB vs. Anand Prakash Jagaiya of Malaysia*

The SEC and the CDS a subsidiary of the CSE have been added as Respondents in 3 cases filed by the NDB Bank in the Commercial High Court seeking the Court's permission to release the economic benefits which were accrued to three parties who bought shares in the NDB Bank but whose names were not entered in the shareholder's register on the basis they violated the provisions of the Banking Act which prohibits any party individually or by acting in concert to hold more than 10% of the shareholding of a licensed commercial bank. The cases are still pending before the Commercial High Court.

**An action filed by a private party seeking an enjoining order on the Colombo Stock Exchange and Central Depository Systems (Private) Limited from concluding a sale of over 15 Million HNB shares held by a private company.**

The Commercial High Court on 7<sup>th</sup> October 2010 made order dismissing an application for an Enjoining Order made by a private party seeking inter alia to restrain the Colombo Stock Exchange and the CDS from concluding a sale of 15, 384 600 HNB shares held by CBD Exports Pvt Ltd to 120 buyers who purchased the said shares on the CSE. The SEC was cited as the 9<sup>th</sup> respondent in the case.

#### **Direction to the SEC by the supreme court**

**Direction by the Supreme Court in SC/FR Case No.262/2009 on the SEC and CSE on an application made By Mr. R.S.W. Senanayake to sell rights of Peoples Leasing Finance PLC.**

The Supreme Court directed the SEC and CSE to permit Mr. R.S.W. Senanayake to sell 50,230 rights of People's Leasing Finance PLC belonging to Mr. Senanayake and to ensure that the net proceeds of the sale are deposited in a fixed deposit in the Bank of Ceylon in a joint account between Mr. Senanayake and the Members of the Watawala Committee and the said instructions were implemented by the SEC.

**Direction to the SEC by the Supreme Court through the Watawala Committee of Chartered Accountants Appointed in Respect of Fundamental Rights Applications Filed Against Directors of Golden Key Credit Card Company and Others**

The SEC carried out several instructions from the Watawala Committee of Chartered Accountants specially appointed by the Supreme Court in connection with the fundamental rights

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application filed against the Central Bank and the directors of the Golden Key Credit Card Company with regard to suspending securities trades of Directors and persons belonging to the Ceylinco Group of Companies including lifting of such suspensions and other incidental steps whenever directed.

## 4. Capital Market Education, Training and Awareness

The Financial Services Academy (FSA), which is the education and training arm of the SEC, provides professional education & training to enhance the knowledge and skill levels of market professionals, investors, market institutions and issuers.

During the year we continued to implement the qualification framework which was introduced two years ago, aimed at offering a minimum level of proficiency for trainee investment advisors of stock broking companies whilst assisting practitioners to progress to more advanced qualifications through the development of continuous professional development programmes.

### 4.1 Qualification Framework

The Certificate in Capital Markets (CCM) programme which is the first qualification in the qualification framework is vastly followed by School Leavers, Under Graduates, Professionals in the financial sector and Professionals from other sectors. The framework will assist to develop a pool of candidates who are trained in fundamentals of securities and finance markets.

Upon completion of the CCM, students who are employed at stock broking companies were evaluated with regard to their experience, knowledge and skills by way of a viva voce examination prior to awarding the Registered Investment Advisor (RIA). (Figure 16)

Further we embarked on a special project during the year which gave the opportunity for students to sit exams every other month. These exams were titled "Special Examination". Students professionally qualified with a sound knowledge of subject matter namely Equity Securities, Debt Securities and

Financial Regulations and Ethics had the opportunity to complete the CCM within a short period.

During the period under review students used the Computer Based Testing System (CTS) for examinations. We are of the view that more students should be encouraged to sit CTS examinations in future.

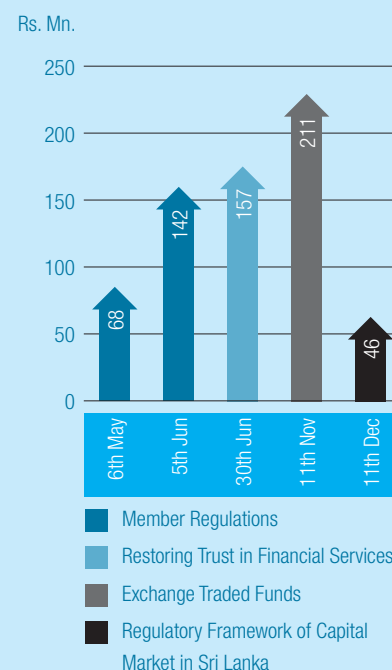
### 4.2 Continuous Professional Development (CPD) Programmes

During the year under review, five (5) tailor made CPD programmes were conducted for the existing investment advisors in the capital market to constantly assess and update themselves with the latest trends in the local and global capital markets. These programmes attracted more

Figure : 16 Synopsis of programmes conducted for the CCM and RIA

Programme	Series	No of Exams Conducted during the year	Pass %
Certificate in Capital Markets (English Medium)	Equity Securities	9	50%
	Debt Securities	7	61%
	Financial Regulations & Ethics	8	69%
Certificate in Capital Markets (Sinhala Medium)	Equity Securities	3	60%
	Debt Securities	2	78%
	Financial Regulations & Ethics	2	49%
Registered Investment Advisor	N/A	6	93%

Figure : 17 Details of the CPD programmes conducted during 2010



than 650 industry professionals which included CEO's of Stock broking companies, Investment Advisors and industry professionals. The SEC made it mandatory for the industry professionals to participate in at least 2 CPD programmes for a year to renew their trading licenses by the CSE. (Figure 17).

### 4.3 Diploma in Capital Markets (DCM)

The FSA was able to forge a joint qualification for the Diploma in Capital Markets with the Chartered Institute for Securities and Investment (CISI) UK. The CISI which was formed by the London Stock Exchange is UK's largest professional body offering specialized

qualifications to practitioners in the British financial industry. This alliance would give the Sri Lankan practitioners the benefit of obtaining an internationally recognized qualification of high standard at an affordable fee. The Diploma will be branded and awarded as the SEC-CISI Diploma in Capital Markets. The inauguration of the first batch will be held in May 2011.

Figure : 18 Awareness Initiatives

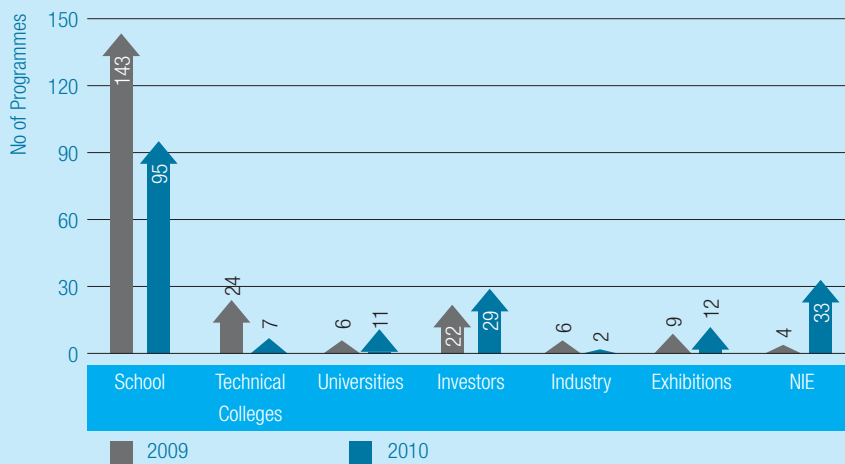


Figure : 19 Province wise illustration of Awareness Programmes in 2010

Province	Year 2010	
	No. of Programmes	No. of Participants
Western	46	5370
North Western	27	2173
North Central	8	909
Uva	8	1100
Sabaragamuwa	12	1560
Southern	13	3019
Central	22	2100
Eastern	26	3823
Northern	15	3924

### 4.4 Capital Market Awareness

A comprehensive capital market awareness plan was formulated taking into consideration the need of financial education to each segment of the society. As per the new plan we were able to provide capital market education and training for different target groups such as school children, teachers, university students, academia, investors and potential investors in all regions of the country. The Awareness Team also participated in educational and trade exhibitions such as EDEX, Dayata Kirula and Corp City 2010 during the year under review. (Figure 18,19).

#### 4.4.1 Programmes for Existing and Potential Investors

We conducted programmes for potential and existing investors with the intention of providing them basic theoretical and practical aspects of share trading. The first programme was inaugurated in July 2010 while the second commenced in September 2010. This eight weeks programme attracted large participation with each batch consisting of over hundred participants.

#### 4.4.2 Programmes for Issuers

Considering the need and the requirement of addressing the senior management of listed companies on latest developments and trends in

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the local and global capital markets, a seminar on Corporate Governance was conducted in September 2010 at the Cinnamon Lakeside, Colombo. Ms. Jane Diplock, Chairperson, Securities Commission, New Zealand and Chairperson of the Executive Committee, International Organization of Securities Commissions (IOSCO) addressed the forum on Corporate Governance Best Practices while Dr. Hareendra Dissa Bandara, Director, Financial Services Academy, presented current views based on evidence from Sri Lankan Corporate Boards.

#### 4.4.3 Programmes for Industry Participants

Two programmes were conducted during the year under review for industry participants and professionals with the intention of enhancing their knowledge on various capital market developments. An international conference on derivatives was held in March 2010 with the participation of one hundred and thirty (130) participants including directors of listed companies, investment advisors, media and other interested parties. Ten foreign participants from various financial institutions in the Asia Pacific Region also attended the programme. A residential workshop for the Judiciary was also conducted on Capital Market Regulations and Financial Frauds in August 2010.

#### 4.4.4 Capital Market Information Centers (CMICs)

Continuing the education and familiarization efforts on the subject of Capital Market, the Capital Market Information Centre (CMIC) project was introduced to the National University system in 2008 to provide market information via an online database to

students, staff and faculty members seeking to further their understanding of the capital market for research and academic purposes and also upgrade knowledge in investing. As of date the CMIC has been launched in 9 universities out of the identified National Universities with established Management Faculties. For the year under review 3 universities were awarded the facility namely Eastern, South Eastern and Colombo University, paving the way to create links with academics in the Eastern part of the country and taking a step further in creating Capital Market awareness island-wide in fulfilling SEC's broader objective of Capital Market development.

In an effort to make the CMIC website a fully fledged information center that is on par with international Capital market resource centers, the website revamping project is underway together with the FSA website.

#### 4.5 Publications

The FSA made a significant effort to publish capital market books and literature and as a result completed the Tamil translation of the Publication on the Financial Market of Sri Lanka which was also authored by Professor Lalith Samarakoon.

#### 4.6 All Island TV Quiz Programme

An all island TV quiz programme was conducted for advanced level commerce students with the intention of enhancing their knowledge on the capital market of Sri Lanka. Schools which offered commerce for advanced level in the Sinhala medium were requested to nominate a student for the competition. The winner of the

provincial contest was selected to the grand finals. A student from the Eastern province won the TV quiz 2010. This programme was aired on the Independent Television Network (ITN) on Sundays consecutively for nine weeks. With a repeat telecast on Wednesday.

#### 4.7 Attachment programmes for officials of foreign jurisdictions

Two programmes were conducted for a few senior officials of the Capital Market Authority of Kenya and the Capital Markets Securities Authority of Tanzania to visit Sri Lanka and learn from our experiences on the implementation of the Automated Trading and Surveillance systems. Visits were arranged to the CSE and other capital market related institutions to obtain firsthand experience and other information. These programmes were arranged for the above officials during May and June 2010 respectively.

#### 4.8 Investment Day - 2010

The investment day was organized at the Bandaranaike Memorial International Conference Hall to commemorate the 23<sup>rd</sup> anniversary of the SEC. The exhibition was well attended and we provided students and the general public comprehensive knowledge on all aspects of the capital market. Schools in the Western Province were invited to participate at the educational exhibition and lectures were arranged for them covering the Advanced Level syllabus on the capital market.

#### 4.9 Other Capital Market Related Activities

During the year we awarded research grants for graduate students of universities, academia and professionals

for undertaking research pertaining to topics related to the capital market of Sri Lanka. Accordingly, the following studies were undertaken and reports were submitted during the period under review:

- An Empirical Examination of Informational Content of Dividend Announcement in Sri Lankan Share Market
- Investigation of the Day-of-the-Week Effect on Stock Returns in an Emerging Market: Case of Sri Lanka
- An Empirical Examination of the Impact of Lead Information Disseminated through Key Financial Press in Moving Share Prices in the Colombo Stock Market
- Impact of Sri Lanka's Stock Market on the Economy: An Observation of Colombo Stock Market

The above Researchers will be awarded a certificate along with a cash award. We continued to award the best performers in the subject of capital markets with gold medals and cash awards among the national universities in Sri Lanka. Memoranda of Understanding (MOU) were signed with two more national universities with regard to the above project and six universities were awarded with gold medals and cash prizes during the year under review.

## 5. Capital Market Development

The capital market is the key mechanism for channeling economic resources in an efficient manner towards the development of the country. With the post war bullish economic outlook of the country, the Sri Lanka capital market has

shown remarkable growth. To further propel and facilitate such growth, key development initiatives undertaken by us during the year are as follows.

### 5.1 Initiatives to develop the market microstructure of the CSE

With the aim of increasing trading volumes and enhancing liquidity, share transaction costs at the CSE were reduced significantly. We also initiated key changes including the increase of the crossing threshold from Rs. 10 million to Rs. 20 million, the reduction of the ticker size to 10 cents across the board and the reduction in the negotiable brokerage threshold from Rs. 100 million to Rs. 50 million with a minimum brokerage floor of 0.15%.

### 5.2 Representations/Proposals made towards the National Budget and the CBSL

- In the context of addressing impediments to the development of our capital market, we made representations to the Government and put forward important proposals towards the 2011 National Budget and to the Central Bank of Sri Lanka.
- Key proposals incorporated into the budget were the relaxation of foreign investment restrictions placed on Unit Trusts investing in Government Securities, exemption of certain taxes on the Unit Trust industry and the treatment of withholding tax on corporate bonds being made similar to Government Securities. Also, through representations made to the Central Bank, foreign investors and non-resident Sri Lankans have been permitted to invest in local currency denominated corporate debt securities.

### 5.3 Developing modalities for the demutualization of the CSE

Demutualization of the CSE which is a key recommendation of the Capital Market Master Plan ("CMMP") is being implemented by the SEC. In this regard we have developed a modality for ownership, board composition etc. Taking into account the interests of all stake holders we are in the process of arriving at the final modality which could be presented to the Ministry of Finance and to the other stake holders.

### 5.4 Workshop on Risk Management and the Board of Directors

The workshop was organized in collaboration with the International Finance Corporation ("IFC") targeting corporate personnel in Sri Lanka. The key intention of the workshop was to enhance the risk oversight structures, processes and the competence of boards in corporate Sri Lanka. Eminent international industry practitioners and educators delivered the programme.

## 6. Our Strengths

### 6.1 Human Resources

We believe "People Drive Business" and hence the human resources of the SEC are valued, appreciated, respected and nurtured to embrace the rapid changes in regulatory and business ideologies along with the applicable best practices.

### 6.2 Cadre Composition

To meet the challenges of the capital market and to strengthen the Secretariat to discharge the mandate of the SEC effectively we continue to search for right talent to fit the SEC team. The details of the SEC Cadre as at end of the year under review are depicted below. (Figures 20,21).

# Operational Review contd...

Figure : 20 Cadre Composition

Category	Approved Cadre	In Employment	
		As at 31.12.2009	As at 31.12.2010
Director General	1	1	1
Deputy Director General	1	0	-
Directors	11	10	7
Assistant Directors	4	2	2
Managers	5	3	3
Senior Executives	37	6	6
Executives		26	28
Non Executives	17	16	16
Support Staff	8	8	7
<b>Total</b>	<b>84</b>	<b>72</b>	<b>70</b>

Figure : 23 Age Analysis

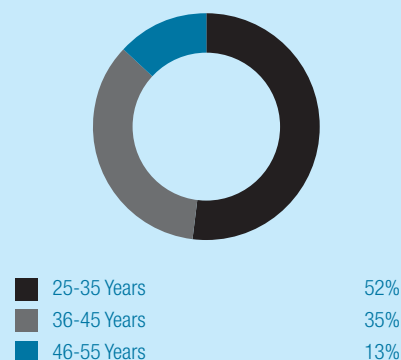
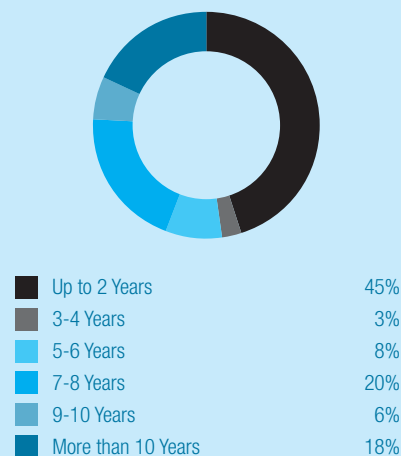
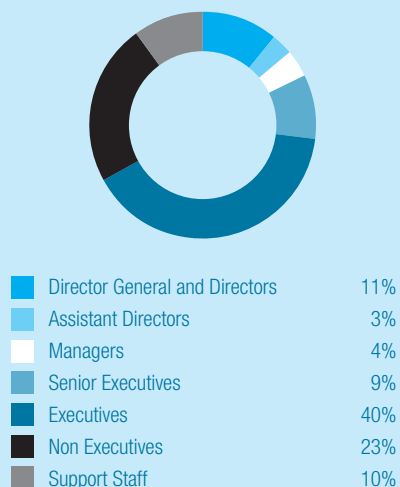


Figure : 24 Service Information



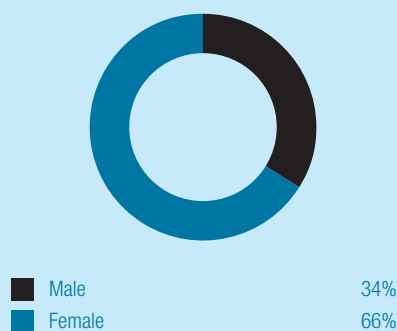
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Figure : 21 Cadre Information Based on Employee Grade



The gender, age and the period of service of the staff as at the end of the year are depicted in pictorial form below. (Figures : 22,23,24)

Figure : 22 Gender Analysis



As at 31 December 2010, 70 members served the SEC consisting of 24 males and 46 females.

## 6.3 Training and Development

Continuously nurturing the learning culture of the staff is imperative to effectively regulate a fast evolving capital market in a professional and transparent manner. Hence Rs.17.5 million was invested towards local and foreign training along with sponsorship for higher studies and reimbursement of professional membership fees during the year under review.

Being a member of the IOSCO we are thankful for all the training and awareness opportunities extended to the SEC by our fellow members. The exposure the participants received were relevant and the opportunity to share knowledge of our fellow regulators immensely benefit in formulation of future regulation etc.

#### 6.4 Employee Involvement

We embraced employee involvement to extract the talent and the vision of the staff for effective strategy execution. Arising out of that the Corporate Plan of the SEC was prepared with employee participation at all levels. This exercise has proven to be successful since the members of the staff are motivated and committed to achieve the goals that they themselves have set into motion.

#### 6.5 Staff Welfare

We recognise that health and welfare of all its employees are vital in achieving the mission of the SEC. Therefore a range of benefits such as indoor and outdoor medical schemes, flexi timing, vehicle and distress loan schemes, festival advances, educational grants and reimbursement of membership fees to professional bodies etc could be availed by the staff subject to certain conditions.

Opportunities are extended to the staff and their families to interact with each other with a view to foster understanding and cultivate relationships with fellow members and their families and at times with the fellow regulators too. During the year 2010 the human resources division successfully organized the annual sports day, residential training programme and the Pirith ceremony.

The staff of the SEC and IBSL along with their families immensely enjoyed the Christmas party on board the 'Jet Liner' vessel of the Sri Lanka Navy.

#### 6.6 Internship

We continued to award opportunities to undergraduates of all National Universities an Internship with a view to provide exposure to the functions of the regulator of the capital market.

#### 6.7 Information Technology

The first phase of implementing the Virtualized Server with VMware software was successfully completed during the year under review. The said implementation improved to a great extent the server utilization, security of the system along with server uptime and data protection. In the ensuing year further enhancements in this connection will be implemented.

Assistance was given in implementing a new Surveillance System for the market monitoring process.

In line with National Procurement Guidelines a Departmental Consultancy Procurement Committee finalized the selection of a suitable consultant to design, develop, maintain and host the SEC, FSA and CMIC websites.

#### 6.8 International Relations

During the year under review we liaised with the implementation task force of the Emerging Markets Committee of IOCSO in respect of objectives and principles concerning capital market regulation. We responded to several questionnaires concerning OTC markets, derivative trading models, bond markets, implementation of international reporting standards on

trading interventions in emerging markets and on maintenance of a public float.

As a member of IOSCO we have maintained a steady relationship with the Emerging Markets Committee of IOSCO. During the year we responded to the detailed surveys conducted by the IOSCO Working Groups and Task Forces in order to contribute its research work on several important aspects related to global capital markets. We also responded to a number of consultations conducted by IOSCO General Secretariat and continued its cordial relationship by updating the required details and data for administrative and other purposes.

The Asia Pacific Regional Committee's Teleconference on the status of the Review of IOSCO's Strategic Direction was held during the year in order to get the opinion of its member countries regarding same. Being a signatory of the IOSCO Memorandum of Understanding (MMOU) the SEC has obtained the fullest support from the foreign jurisdictions in obtaining information and documents in relations to ongoing investigations of the SEC. Many of the policy initiatives undertaken by us have also been circulated amongst the IOSCO member states in order to obtain information from the respective member jurisdictions. We too reciprocated in a similar manner to all similar queries received from several foreign jurisdictions.

#### 6.8.1 IOSCO, Global International Financial Reporting Standards (IFRS) Database:

We obtained access to the Global IFRS coordination database as a result of the

# Operational Review contd...

agreement signed between the SEC and IOSCO in 2008. During the year we had its debut at IOSCO Global IFRS Database Teleconference.

## 6.8.2 Visit by the Chairperson of the International Organization of Securities Commission's Executive Committee to Sri Lanka:

Ms. Jane Diplock, Chairperson of the Executive Committee of IOSCO visited Sri Lanka during the year under review.

During her visit she met with the officials of the SEC and discussed the current progress of IOSCO in respect of setting global regulatory standards and also addressed the broking community and corporate sector of Sri Lanka. Her visit was organized and hosted by the SEC and the Institute of Chartered Accountants of Sri Lanka.

## 7. Statutory Funds

### 7.1 CESS Fund

In accordance with Sections 14A and 14B of the SEC Act, No 36 of 1987 as amended by Act, No. 26 of 1991, Act, No. 18 of 2003 and Act, No. 47 of 2009 states as follows.

14A (1) There shall be charged, levied and paid a Cess at such rates as may be specified by the Minister by Order published in the Gazette on every purchase and sale of securities recorded in a licensed stock exchange or notified to it under its rules by both the purchaser and the seller. Different rates may be specified in respect of different classes of securities.

(2) The Cess imposed under this Section shall be in addition to any other tax or Cess levied under any other written law.

14B (1) There shall be established a fund called the Cess Fund to which shall be credited the proceeds of the Cess imposed under Section 14A.

(2) There shall be paid out the Cess Fund such sums as may be authorized by the Commission for the purpose of-

- (a) developing the securities market;
- (b) enhancing monies lying to the credit of the Compensation Fund established under Section 38; and
- (c) exercising, performing and discharging the powers, duties and functions of the Commission for the purpose of achieving its objects.

(3) The money lying to the credit of the Cess Fund may be invested by the

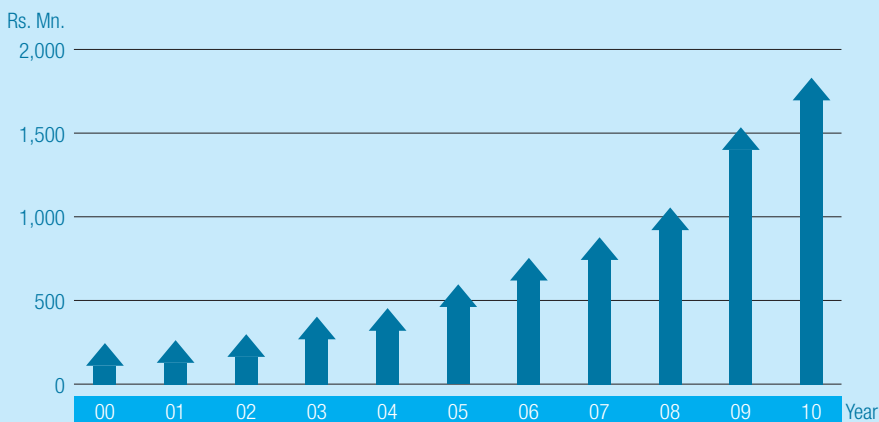
Commission in such manner as may be determined by the Commission.

The rate of Cess charged by the SEC after a series of deliberations was reduced for the second time to 0.072% per transaction from 0.09% per transaction with effect from 1 August 2010. Earlier reduction took place with effect from 1 December 2003 when the applicable rate of Cess was reduced from 0.1% to 0.09% per transaction.

Cess on Intra day trades of clients was not charged on one side of transactions since February 2006 as set out below.

- (a) In the event the number of shares purchased does not equal the number of shares sold, the transaction fees will not be levied on the lower quantity of shares either purchased or sold.
- (b) In the event the quantity purchased is equal to the quantity sold transaction fees will not be levied from the second transaction whether it be a purchase or sales transaction.

Figure : 25 Growth of the CESS Fund





Intra day trade is where a client buys and sells or sells and buys the same security on the same day through the same broker.

The balance lying to the credit of Cess Fund as at 31 December 2010 amounted to Rs.1,606 million. (Figure 25)

## 7.2 The Settlement Guarantee Fund (SGF)

The SGF was launched on 22 May 1998. The Fund was established for the purpose of guaranteeing the settlement of trades between participants of the Central Depository System of the Colombo Stock Exchange (CSE). The operation of the SGF is described below.

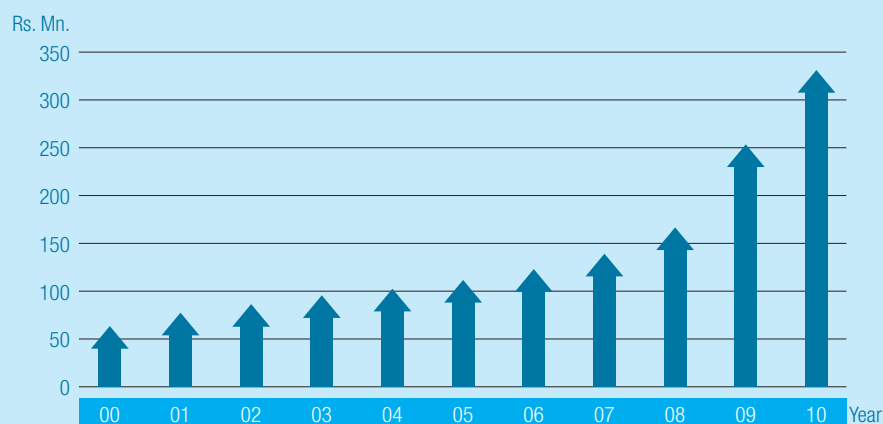
- Ownership of shares traded is transferred no sooner a trade is executed. From 10 December 2007 the CSE adopted a single tier settlement cycle. The buyer is required to pay on T+3 i.e. on the 4th Market day including the day of trading and the seller to receive the settlement on T+3 i.e. on the 4th Market day. The relatively long interval between transfer of ownership and receipt of proceeds leaves the settlement risk uncovered which in turn necessitated the establishment of the SGF.
- The Trustees of the Fund hold office of ex-officio and comprise the Chairman of SEC, the Chairman of CSE, the Deputy Secretary to the Treasury, the Director General of SEC and the Director General of CSE.

- The Government of Sri Lanka has contributed a sum of Rs 50 million to the said Fund. This money has been invested in Government securities in terms of the Trust Deed. SGF can also receive donations, gifts and endowments as replenishments. The broker/custodian banks are presently not required to contribute to the Fund.
- With a view to strengthen the Fund a sum of Rs. 100 million was transferred equally from the the Cess Fund during the years 2009 and 2010.

However, since the SGF is found to be inadequate to properly address the issue of settlement risk the SEC is looking at feasibility of establishing a clearing corporation to effectively address the settlement risk.

The balance lying to the credit of the fund as at 31.12.2010 amounted to Rs. 332 million. (Figure 26).

Figure : 26 Growth of the SGF Fund



## Compensation Fund

The Compensation Fund came into operation along with the establishment of the SEC in 1987. Section 38 of the Securities and Exchange Commission Act No 36 of 1987 as amended states as follows:

- There shall be established a fund called the Compensation Fund, for the purpose of granting compensation to any investor who suffers pecuniary loss as a result of any licensed stock broker or licensed stock dealer being found incapable of meeting his contractual obligations.
- The Compensation Fund shall consist of
  - Such sums of money as may be voted upon by Parliament for the purpose of the Fund.
  - Such sums of moneys may be credited to the Fund under Section 51A; (Section 51A is on compounding offences).
  - Such sums of money as may be credited from Cess Fund under section 14B.

# Operational Review contd...

- Moneys belonging to the Compensation Fund may be invested by the Commission in such manner as may be determined by the Commission.

The Minister shall appoint from among the members of the Commission three members who shall comprise the Compensation Committee.

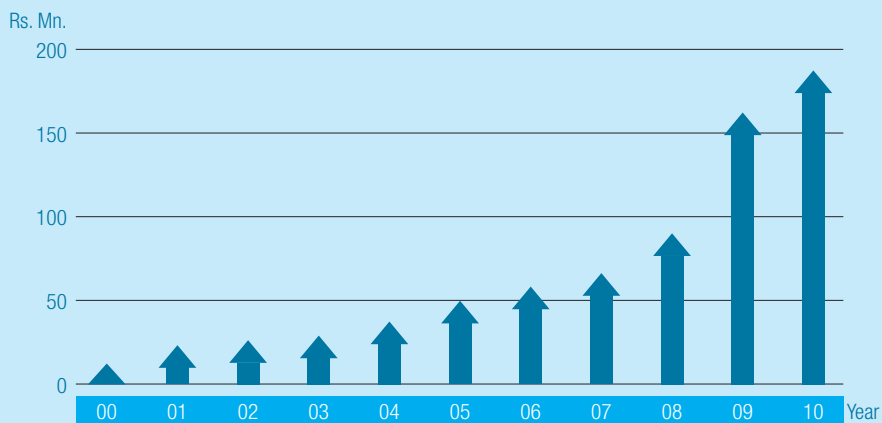
The Committee shall be responsible for assessing and awarding compensation in respect of any application made and the decision of such Committee on any such assessment or award shall be final and conclusive for the purpose of this Act.

The Act also provides for the procedure for applying for compensation. According to the Act, the Committee may, after examination of the documents and other evidence produced in support of the claim by an applicant, or in any case where an inquiry was held on the conclusion of such inquiry, allow or disallow such

claim for compensation. Up-to-date there have been no claims made from the Compensation Fund.

The balance lying to the credit of the Compensation Fund as at 31.12.2010 amounted to Rs. 187 million. (Figure 27)

Figure : 27 Growth of the Compensation Fund



# Additional Information

## Market Intermediaries

Registered as at 31 December 2010

Registered market intermediaries under the category of margin provider, investment manager and underwriter are set out below:

Company	Margin Provider	Investment Manager	Underwriter
Acuity Partners (Private) Limited	X		X
Asha Financial Services Limited	X		
Asia Asset Finance Limited	X		
Assetline Capital (Private) Limited	X	X	
Bartleet Finance Limited	X		
Capital Alliance Securities (Private) Limited	X	X	
Capital Trust Credit (Private) Limited	X		
Commercial Bank of Ceylon PLC	X		X
DFCC Vardhana Bank Limited	X		
First Capital Markets Limited	X		
Hatton National Bank PLC	X		X
Lanka ORIX Finance Company Limited	X		
Lexinton Financial Services (Private) Limited	X		
Merchant Bank of Sri Lanka PLC	X	X	X
National Development Bank PLC	X		X
Nations Trust Bank PLC	X	X	
Pan Asia Banking Corporation PLC	X		
People's Leasing Company Limited	X		
Sampath Bank PLC	X		X
Seylan Bank PLC	X		
Softlogic Credit Limited	X		
Union Bank of Colombo Limited	X		
Waldock Mackenzie Limited	X	X	
Asia Wealth Management Company(Private) Limited		X	
Bank of Ceylon		X	X
Bartleet TransCapital Limited		X	X
Claridge Asset Management (Private) Limited		X	
Ennid Capital (Private) Limited		X	
First Capital Asset Management Limited		X	
Guardian Fund Management Limited		X	
J B Financial Services (Private) Limited		X	
L R Global Lanka Asset Management Company (Private) Limited		X	
National Wealth Corporation Limited		X	
Orion Fund Management (Private) Limited		X	
SKM Lanka Holdings (Private) Limited		X	
WealthTrust Corporation (Private) Limited		X	
Ceylon Guardian Investment Trust PLC			X
Ceylon Investment PLC			X

**Registered market intermediary under the category of a clearing house**

Central Depository Systems (Private) Limited

**Registered market intermediary under the category of credit rating agency**

Fitch Ratings Lanka Limited

RAM Ratings Lanka Limited

# Additional Information contd...

## Stock Brokers & Stock Dealers

Licensed Stock Brokers & Stock Dealers as at 31st December 2010

Company	Stock Broker	Stock Dealer	
		Dealer in Equity Securities	Dealer in Debt Securities
Acuity Stockbrokers (Private) Limited	X		
Asha Phillip Securities Limited	X		
Asia Securities (Private) Limited	X		
Assetline Securities (Private) Limited	X		
Bartleet Mallory Stockbrokers (Private) Limited	X		X
Capital Alliance Securities (Private) Limited	X		
Ceylinco Stockbrokers (Private) Limited	X		
Claridge Stockbrokers (Private) Limited	X		
CT Smith Stockbrokers (Private) Limited	X		
DNH Financial (Private) Limited	X		
First Guardian Equities (Private) Limited	X		X
Heraymila Securities Limited	X		
IIFL Securities Ceylon (Private) Limited	X		
JB Securities (Private) Limited	X	X	
John Keells Stock Brokers (Private) Limited	X		
Lanka Securities (Private) Limited	X		
LOLC Securities Limited	X		
NDB Stock Brokers (Private) Limited	X		
Richard Pieris Securities (Private) Limited	X		
SC Securities (Private) Limited	X		
SKM Lanka Holdings (Private) Limited	X	X	
SMB Securities (Private) Limited	X		X
Somerville Stockbrokers (Private) Limited	X		
Taprobane Securities (Private) Limited	X		
TKS Securities (Private) Limited	X		

## Unit Trusts

The Companies given below have been licensed to operate the unit trusts set out below.

### 1. Ceylon Asset Management Company Limited

Ceylon Financial Sector Fund  
Ceylon Income Fund  
Ceylon Index Fund  
Ceylon Tourism Fund

### 2. Comtrust Asset Management (Private) Limited

Comtrust Equity Fund

### 3. NDB Aviva Wealth Management Limited

Eagle Income Fund  
Eagle Gilt Edged Fund  
Eagle Growth and Income Fund  
Eagle Growth Fund

### 4. Ceybank Asset Management (Private) Limited

Ceybank Century Growth Fund  
Ceybank Gilt Edged Fund (closed end)  
Ceybank Savings Plus Money Market Fund  
Ceybank Surakum  
Ceybank Unit Trust

### 5. National Asset Management Limited

NAMAL Acuity Value Fund (closed end)  
NAMAL Amana Equity Fund (closed end)  
NAMAL Gilt Edge Fund 1 (closed end)  
NAMAL Growth Fund  
NAMAL HNB Fund (closed end)  
NAMAL Income Fund  
NAMAL Money Market Fund  
National Equity Fund

### 6. First Capital Asset Management Limited

First Capital Wealth Fund

# Fact Sheet

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Year	2006	2007	2008	2009	2010
Annual Turnover (Rs Mn) Equity	105,153.70	104,985.40	110,453.90	142,462.65	570,326.82
Domestic (Rs Mn)	70,675	63,815.70	50,796.90	99,010.83	464,733.62
Foreign (Rs Mn)	34,479	41,169.70	59,656.90	43,451.82	105,593.20
Market Days (No)	241	241	238	240	238
Daily Average Turnover (Rs Mn) Equity	436.3	435.6	464.1	593.6	2,396.33
Shares traded (No Mn) Equity	3,912.30	2,887.30	3,154.90	4,762.70	18,489.19
Domestic (No Mn)	3,178.20	2,009.90	1,934.90	3,784.20	16,684.45
Foreign (No Mn)	734.2	877.3	1,220.00	978.42	1,804.74
Trades (No) Equity	952,382	876,928	776,244	1,266,299	3,355,126
Domestic (No)	908,220	831,663	730,415	1,190,822	3,225,041
Foreign (No)	44,162	45,265	45,829	75,477	130,085
New Listing (No)	2	-	3	3	10
Delisting (No)	4	2	2	6	1
Companies Listed	237	235	235	231	241
Companies Traded	232	231	232	231	238
Market Capitalization (Rs Bn)	834.8	820.7	488.8	1,092.10	2,210.45
Market PER year end (Times)	14	11.6	5.4	16.6	25.16
Turnover to Market Capitalization (%)	14.8	12.7	16.9	18	34.5
Dividend Yield Year End (%)	2.2	2.5	5.6	3	1.16
Price to Book Value Year End (Times)	2	1.8	0.8	1.7	2.98
Market Cap. As a % of GDP	29.8	22.9	11.1	22.6	
<b>Price Indices</b>					
All Share Price Index (ASPI)	2,722.40	2,541.00	1,503.00	3,385.55	6,635.87
y-o-y Change %	41.6	(6.7)	(40.9)	125.25	96.01
Milanka Price Index (MPI)	3,711.80	3,291.90	1,631.30	3,849.38	7,061.46
y-o-y Change %	51.4	(11.3)	(50.4)	135.97	83.44
<b>Total Return Indices</b>					
Total Return Index on ASPI (ASTRI)	2,998.80	2,883.40	1,783.60	3,944.90	7,899.11
y-o-y Change %	46	(3.8)	(38.1)	121.18	100.24
Total Return Index on MPI (MTRI)	4,077.30	3,726.80	1,962.50	4,506.24	8,481.73
y-o-y Change %	55.3	(8.6)	(47.3)	129.6	88.22
<b>Non-National Activity</b>					
Annual Turnover (Rs Mn)	34,478.60	41,169.70	59,656.90	43,451.82	105,593.20
Purchases (Rs. Mn.)	37,167.30	46,796.80	66,632.20	43,057.32	92,425.53
Sales (Rs. Mn.)	31,789.90	35,542.50	52,681.70	43,846.32	118,760.87
<b>Net Foreign Flow (Rs. Mn.)</b>	<b>5,377.30</b>	<b>11,254.30</b>	<b>13,950.50</b>	<b>(789)</b>	<b>(26,335.34)</b>
Shares Traded (No. Mn.)	734.2	877.3	1,220.00	978.41	1,705.60
Purchases (No. Mn.)	807.9	919.8	1,286.20	908.97	1,425.10
Sales (No. Mn.)	660.4	834.8	1,153.90	1,047.87	1,986.00
Trades (No.)	44,162	45,265	45,829	75,477	130,085
Purchases (No.)	48,511	50,518	50,052	69,431	115,071
Sales (No.)	39,813	40,012	41,606	81,523	145,100

Year	2006	2007	2008	2009	2010
<b>Debt Market</b>					
<b>Corporate Debt</b>					
Turnover (Rs 000)	405,211	98,903	102,639.30	136,765	72,288
No of Trades	321	144	27	42	92
No of Debentures Traded (000)	2,421	1,020	953.5	1,020	693
<b>Government Debt</b>					
Turnover (Rs 000)	207,080	709,333	195,157.40	98,977	45,673
No of Trades	379	208	69	42	18
No of Govt. Debt Securities Traded (000)	213,242	742,736	208,182.60	102,778	46,794
<b>Unit Trusts</b>					
Net Asset Value (NAV)(Rs. Mn)	5,352	6,296	6,780	9,952	22,228
Unit Holders (No.)	23,417	23,191	22,685	23,117	24,649
Units Issued (No. 000)	355,553	469,853	638,112	564,500	1,159,000
Investment in Equity (Rs. Mn.)	3,700	3,655	2,589	6,036	11,349
Investment in Treasury Bills (Rs. Mn)	956	932	2,903	3,363	9,289
Investment in other Instruments **(Rs. Mn)	696	1,709	1,293	1,106	1,223

Sources: CSE, regulatory submissions by unit trust managing companies.

\*\* Commercial papers, trust certificates, debentures and bank deposits.



“ By regulating with a firm hand and cementing investor confidence, we have led the way in creating a healthy market ”





## Financial Statements

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# Report of the Auditor General



මගේ අංකය  
எனது இல  
My No.

EF/J/SEC/2010

ඔබේ අංකය  
உமது இல  
Your No.

දිනය  
திகதி  
Date



26 May 2011

## විගණකාධිපති දෙපාර්තමේන්තුව கணக்காய்வாளர் தலைமை அறிபதி திணைக்களம் AUDITOR GENERAL'S DEPARTMENT

### Report of the Auditor General

The audit of financial statements of the Securities and Exchange Commission of Sri Lanka which comprise the Balance Sheet as at 31 December 2010, Income and Expenditure Statement, Statement of movement of Equity, cash flows for the year then ended and the significant accounting policies and notes (Nos.1 to26) to the financial statements was carried out under my direction in pursuance of provisions in Article 154 (1) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with Section 37(2) of the Securities and Exchange Commission Act, No.36 of 1987 and Section 13 (1) of the Finance Act, No. 38 of 1971.

#### 1.2 Responsibility of the Management for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the Sri Lanka Accounting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of the financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

#### 1.3 Scope of Audit and Basis of Opinion

My responsibility is to express an opinion on these financial statements based on my audit. The audit was carried out in accordance with Sri Lanka Auditing Standards which require that the audit shall be planned and performed to obtain reasonable assurance as to whether the financial statements are free from material misstatements. The audit includes examining on a test basis, evidence supporting the amounts and disclosure in the said financial statements. The audit also includes assessing the accounting policies used and significant estimates made by the management in the preparation of financial statements as well as evaluating their overall presentation. I have obtained all information and explanations which to the best of my knowledge and belief were necessary for the purpose of my audit. I therefore, believe that my audit provides a reasonable basis for my opinion.

#### 1.4 Opinion

So far as appears from my examination, I am of opinion that the Securities and Exchange Commission of Sri Lanka had maintained proper accounting records for the year ended 31 December 2010 and the financial statements give a true and fair view of the state of affairs of the Securities and Exchange Commission of Sri Lanka as at 31 December 2010 and the financial results of its operations and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

#### 1.5 Report to Parliament

My report to Parliament in pursuance of provisions in Article 154(6) of the Constitution will be tabled in due course.

H.A.S.Samaraweera  
Acting Auditor General

කිදුනේ වතුරලය,  
කොළඹ 07, ශ්‍රී ලංකාව

දුරකථනය  
தொலைபேசி  
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සුභන්දිර සතුරුකම,  
කොළඹ 07, ශ්‍රී ලංකාව

ෆැක්ස් අංකය  
பக்ஸ் இல  
Fax No. } 2697451

INDEPENDENCE SQUARE,  
COLOMBO 07, SRI LANKA

ඉලෙක්ට්‍රොනික් තැපෑල  
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# Securities and Exchange Commission of Sri Lanka

## Balance Sheet

<i>As At 31<sup>st</sup> December</i>	<b>Note</b>	<b>2010 Rs.</b>	<b>2009 Rs.</b>
<b>Assets</b>			
<b>Non Current Assets</b>			
Property Plant & Equipment	1	55,924,133	37,356,986
Cess Fund	2	29,512,805	26,560,957
<b>Current Assets</b>			
Inventories	4	650,458	529,902
Receivables	5	1,213,300	1,267,026
Cess Fund	2	1,577,421,470	1,176,903,241
Compensation Fund	3	187,764,653	162,897,363
Deposits, Advance and Prepayments	6	7,557,549	9,806,223
Cash & Cash Equivalents	7	23,778,506	11,995,845
<b>Total Assets</b>		<b><u>1,883,822,874</u></b>	<b><u>1,427,317,543</u></b>
<b>Funds and Liabilities</b>			
<b>Funds Employed and Reserves</b>			
Accumulated Fund	8	15,433,620	10,739,222
Cess Fund	9	1,606,934,275	1,203,464,198
Compensation Fund	10	187,764,653	162,897,363
<b>Non Current Liabilities</b>			
Lease Creditor	11	7,221,071	4,642,275
Grant - Capital Expenditure from Cess Fund	12	41,450,525	25,337,129
Retirement Benefit Obligation	13	13,712,024	10,936,974
<b>Current Liabilities</b>			
Creditors & Accruals	14	5,919,358	4,998,313
Receipts in Advance		2,283,952	769,845
Current Portion of Lease Creditor	11	3,103,396	3,532,224
<b>Total Funds and Liabilities</b>		<b><u>1,883,822,874</u></b>	<b><u>1,427,317,543</u></b>

The Accounting Policies and Notes appearing on pages 63 to 75 form an integral part of the financial statements.

The Members of the Securities & Exchange Commission of Sri Lanka are responsible for the preparation and presentation of these financial statements.

For and on Behalf of The Securities and Exchange Commission of Sri Lanka



**Malik Cader**  
Director General  
Securities and Exchange Commission of Sri Lanka



**Indrani Sugathadasa**  
Chairperson  
Securities and Exchange Commission of Sri Lanka

Colombo.  
19<sup>th</sup> May 2011

# Income and Expenditure Statement

<i>For the year ended 31<sup>st</sup> December</i>	<b>Note</b>	<b>Year Ended 31.12.2010 Rs.</b>	<b>Year Ended 31.12.2009 Rs.</b>
<b>Income</b>			
Broker License Fees		2,208,500	3,420,938
Administration Levy		994,781	1,025,204
Seminar Income-FSA		14,139,969	4,444,870
Seminar Income-SEC		581,697	-
Interest Income		3,524	294,947
Sale of Publications		14,250	13,500
Sundry Income		114,262	106,842
Profit/(Loss) on Disposal of Fixed Assets		326,483	(34,497)
Recognition of Grants	12	10,537,622	9,831,172
		<b><u>28,921,088</u></b>	<b><u>19,102,976</u></b>
Less:			
<b>Expenditure</b>			
Personnel Costs	15	119,046,552	98,627,823
Administration & Establishment Expenses	16	78,269,278	73,531,354
Capital Market Development Expenses	17	22,435,535	21,568,106
Finance Charges	18	254,521	284,554
		<b><u>220,005,886</u></b>	<b><u>194,011,837</u></b>
Excess Expenditure over Income		(191,084,798)	(174,908,861)
Transfers from Cess Fund to meet Operational Expenses		195,779,197	176,502,418
<b>Excess/(Deficit) for the year</b>		<b><u>4,694,399</u></b>	<b><u>1,593,557</u></b>

The Accounting Policies and Notes appearing on pages 63 to 75 form an integral part of the financial statements.

# Statement of Changes in Reserves

<i>For the year ended 31<sup>st</sup> December</i>	<b>Reserves Rs.</b>	<b>Accumulated Fund Rs.</b>	<b>Total Rs.</b>
<b>Balance as at 1st January 2009</b>	-	9,145,665	9,145,665
Excess Expenditure over Income for the year	-	(174,908,861)	(174,908,861)
Fund Transfer from Cess Fund	-	176,502,418	176,502,418
Net Surplus/(Deficit) for the period	-	1,593,557	1,593,557
<b>Balance as at 31st December 2009</b>	-	10,739,222	10,739,222
<b>Balance as at 1st January 2010</b>	-	10,739,221	10,739,221
Excess Expenditure over Income for the year	-	(191,084,798)	(191,084,798)
Fund Transfer from Cess Fund	-	195,779,197	195,779,197
Net Surplus/(Deficit) for the period	-	4,694,399	4,694,399
<b>Balance as at 31st December 2010</b>	-	15,433,620	15,433,620

The Accounting Policies and Notes appearing on pages 63 to 75 form an integral part of the financial statements.

# Cash Flow Statement

<i>For year ended 31<sup>st</sup> December</i>	<b>Note</b>	<b>2010 Rs.</b>	<b>2009 Rs.</b>
<b>Cash Flows from Operating Activities</b>			
Net Increase/(Decrease) after transfers from Cess Fund		4,694,399	1,593,557
Adjustment for			
Depreciation	1	13,301,789	13,951,172
(Profit)/Loss on disposal of Property, Plant & Equipment		(326,483)	34,497
Recognition of Grant	12	(10,537,622)	(9,831,172)
Provision for Gratuity	13	3,255,050	2,435,137
Net Increase/(Decrease) before working capital changes		<u>10,387,133</u>	<u>8,183,191</u>
<b>Change of Working Capital</b>			
(Increase)/Decrease of Stocks		(120,556)	(123,183)
(Increase)/ Decrease of Receivable		53,726	32,550
(Increase)/Decrease of Deposits Advances & Prepayments		2,248,673	(8,162,480)
Increase/(Decrease) of Receipt in Advance		1,514,106	(884,112)
Increase/(Decrease) of Creditors & Accruals		921,045	(3,083,893)
		<u>4,616,994</u>	<u>(12,221,118)</u>
Cash generated from Operating Activities		15,004,127	(4,037,927)
Gratuity paid during the year		(480,000)	(396,000)
<b>Net Cash from Operating Activities</b>		<u><b>14,524,127</b></u>	<u><b>(4,433,927)</b></u>
<b>Cash Flows into Investing Activities</b>			
Purchase of Property Plant and Equipment	1	(33,571,019)	(8,077,583)
Proceeds from Sale of Property Plant & Equipment		2,028,566	963,003
Investment in Treasury Bills		-	1,750,000
<b>Net Cash from Investing Activities</b>		<u><b>(31,542,453)</b></u>	<u><b>(5,364,580)</b></u>
<b>Cash Flows from Financing Activities</b>			
Capital transfer from Cess Fund	12	26,651,019	6,397,583
Increase /(Decrease) in Finance Lease		2,149,968	(3,308,127)
<b>Net Cash from Financing Activities</b>		<u><b>28,800,987</b></u>	<u><b>3,089,456</b></u>
Net Increase/ (Decrease) in Cash and Cash Equivalents		11,782,661	(6,709,051)
Cash and Cash Equivalents at beginning of period (Note a)		11,995,845	18,704,896
Cash and Cash Equivalents at end of period (Note b)		<u><b>23,778,506</b></u>	<u><b>11,995,845</b></u>
<b>Note (a)</b>			
<b>Cash and Cash Equivalents at beginning of period</b>			
Cash at Bank		11,955,845	18,664,896
Cash in Hand		40,000	40,000
		<u><b>11,995,845</b></u>	<u><b>18,704,896</b></u>
<b>Note (b)</b>			
<b>Cash and Cash Equivalents at End of period</b>			
Cash at Bank	7	23,738,506	11,955,845
Cash in Hand	7	40,000	40,000
		<u><b>23,778,506</b></u>	<u><b>11,995,845</b></u>

The Accounting Policies and Notes appearing on pages 63 to 75 form an integral part of the financial statements.

# Cash Flow Statement

<i>For the year ended 31<sup>st</sup> December</i>	<b>2010</b> Rs.	<b>2009</b> Rs.
<b>Cash Flows from Operating Activities</b>		
Net Increase of Cess Fund	<u>403,470,077</u>	<u>114,786,371</u>
Net Increase before Working Capital changes	403,470,077	114,786,371
Change of Working Capital		
(Increase)/Decrease of Staff Loans	(1,898,882)	(7,174,202)
(Increase)/Decrease of Receivables	(2,936,491)	(2,795,448)
(Increase)/Decrease of Interest Receivable on Treasury Bills	7,748,029	(12,188,716)
(Increase)/Decrease of Capital Gain Receivable from State Institution Surplus Trust Fund	(24,293,958)	-
Increase/(Decrease) of Other Payables	-	(35,647)
(Increase)/Decrease of Rent Deposit	<u>(1,614,420)</u>	<u>(1,399,164)</u>
	<u>(22,995,722)</u>	<u>(23,593,177)</u>
Net Cash from Operating Activities	<u>380,474,355</u>	<u>91,193,194</u>
<b>Cash Flows into Investing Activities</b>		
Invested in State Institutions Temporary Surplus Fund	180,768,868	(72,341,811)
Investment of Treasury Bills	<u>(562,469,010)</u>	<u>(24,053,528)</u>
Net Cash from Investing Activities	<u>(381,700,142)</u>	<u>(96,395,339)</u>
Net Increase/(Decrease) in Cash and Cash Equivalents	<u>(1,225,787)</u>	<u>(5,202,145)</u>
Cash and Cash Equivalents at beginning of period (Note c)	<u>1,776,231</u>	<u>6,978,375</u>
Cash and Cash Equivalents at end of period (Note d)	<u>550,444</u>	<u>1,776,230</u>
<b>Note (c)</b>		
<b>Cash and Cash Equivalents at beginning of period</b>		
Cash at Bank	(16,903,769)	578,375
REPO Investments	<u>18,680,000</u>	<u>6,400,000</u>
	<u>1,776,231</u>	<u>6,978,375</u>
<b>Note (d)</b>		
<b>Cash and Cash Equivalents at end of period</b>		
Cash at Bank	(1,559,556)	(16,903,769)
REPO Investments	<u>2,110,000</u>	<u>18,680,000</u>
	<u>550,444</u>	<u>1,776,231</u>

The Accounting Policies and Notes appearing on pages 63 to 75 form an integral part of the financial statements.

## Compensation Fund

# Cash Flow Statement

For the year ended 31<sup>st</sup> December

	2010 Rs.	2009 Rs.
<b>Cash Flows from Operating Activities</b>		
Net Increase of Compensation Fund	<u>24,867,290</u>	<u>72,783,766</u>
Net Increase before Working Capital changes	24,867,290	72,783,766
Change of Working Capital (Increase)/Decrease of Interest Receivable on Treasury Bills	<u>5,250,167</u> <u>5,250,167</u>	<u>(7,816,117)</u> <u>(7,816,116)</u>
Net Cash from Operating Activities	<u>30,117,457</u>	<u>64,967,650</u>
<b>Cash Flows into Investing Activities</b>		
Investment in Treasury Bills	<u>(30,126,797)</u>	<u>(64,960,511)</u>
Net Cash from Investing Activities	<u>(30,126,797)</u>	<u>(64,960,511)</u>
<b>Cash Flows from Financing Activities</b>		
Net Increase/(Decrease) in Cash and Cash Equivalents	(9,340)	7,139
Cash and Cash Equivalents at beginning of period (Note e)	<u>94,652</u>	<u>87,513</u>
Cash and Cash Equivalents at end of period (Note f)	<u>85,312</u>	<u>94,652</u>
<b>Note (e)</b>		
<b>Cash and Cash Equivalents at beginning of period</b>		
Cash at Bank	68,282	69,032
Call Deposits	<u>26,370</u>	<u>18,482</u>
	<u>94,652</u>	<u>87,514</u>
<b>Note (f)</b>		
<b>Cash and Cash Equivalents at end of period</b>		
Cash at Bank	59,943	68,282
Call Deposits	<u>25,369</u>	<u>26,370</u>
	<u>85,312</u>	<u>94,652</u>

The Accounting Policies and Notes appearing on pages 63 to 75 form an integral part of the financial statements.



# Accounting Policies

## 1. Significant Accounting Policies

### 1.1 Statement of Compliance

The financial statements of the Securities and Exchange Commission of Sri Lanka have been prepared in compliance with the Sri Lanka Accounting Standards and are in compliance with the said standards.

### 1.2 Basis of Preparation

The financial statements of the Commission are presented in Sri Lankan Rupees rounded to the nearest Rupee.

The financial statements are prepared on accrual basis under the historical cost convention. Where appropriate accounting policies are disclosed in succeeding notes.

### 1.3 Foreign Currency Transactions

Foreign exchange transactions are converted to Sri Lankan Rupees at the rate of exchange prevailing at the time of the transaction.

### 1.4 Events After The Balance Sheet Date

All material events after the Balance Sheet date are considered and appropriate adjustments or disclosures are made in the financial statements, where necessary.

### 1.5 Changes in Accounting Policies

The accounting policies adopted are consistent with those of the previous year.

### 1.6 Comparative Figures

Comparative figures have been adjusted to conform to the changes in presentation in the current financial year.

## 2. Assets and Bases of Their Valuation

### 2.1 Property, Plant and Equipment

#### Owned Property Plant and Equipment

Property, Plant & Equipment together with any incidental expenses thereon are stated at cost and depreciated at their respective useful lives. Fixed assets received as grants, were accounted at cost and depreciation thereof is charged against the respective reserve account. The depreciation is provided on the straight-line basis applying following rates:

Motor Vehicles	25.00%
Furniture, Fixtures and Fittings	12.50%
Office Equipment & EDP Equipment	25.00%
Training Equipment	25.00%

Depreciation is provided for all assets purchased from the date it is available for use. In the year of disposal depreciation is provided up to the date the asset is derecognized.

### 2.2 Leased Motor Vehicles

The assets on finance lease which effectively transfer to the SEC substantially all risks and benefits incidental to ownership of the leased item is capitalized at the capital value of lease obtained. Depreciation and finance charges arising out of such leasehold assets are charged to the Income and Expenditure statement whilst the payments of lease rental are recognized to reduce the lease liability.

As part of the remuneration package the Assistant Directors and above are entitled to a vehicle under the contributory lease scheme. Whilst the SEC pays the lease rental the staff concerned contributes towards the lease rental. In addition

## Accounting Policies contd...

the staff should bear all expenditure in full pertaining license and maintenance. The SEC will also pay the cost of insurance to the extent of the lease entitlement. The ownership of the vehicle will be transferred to the member of the staff who participated in the contributory lease scheme at the expiration of the lease period i.e. after 48 months or upon settlement of the lease liability by the staff concerned in full.

### 2.3 Investments

Government Securities are stated at cost.

### 2.4 Inventories

Inventories are valued at lower of cost or net realizable value. The cost of inventories is valued on First-in, First-out (FIFO) basis.

As a policy Library Books are written off since the Capital Market related Laws and rules are subject to rapid changes due to the fast changing market conditions in the world.

### 2.5 Receivables

Receivables are stated at the estimated realizable value.

## 3. Liabilities & Provisions

### 3.1.1 Retirement Benefits

In terms of Gratuity Act No. 12 of 1983 the liability to an employee arises only upon completion of 5 years of continued service. To meet the liability a provision is made, equivalent to half a month salary based on the last month of the financial year for all employees who have completed one year of service.

### 3.1.2 Defined Contribution Plans

All employees of the SEC are members of the Employees' Provident Fund and Employees' Trust Fund to which SEC contributes 12% and 3% respectively of such employees' basic salary.

### 3.2 Accounts Payable

Payables are stated at cost.

### 3.3 Grant

Capital Expenditure transferred from the Cess Fund is treated as a grant and recognized in the Income and Expenditure statement as revenue on systematic basis over the useful life of the related asset.

## 4. Income & Expenditure

### 4.1 Revenue Recognition

Revenue is recognized on accrual basis.

### 4.2 Expenditure Recognition

All expenditure incurred in maintaining the SEC has been recognized on accrual basis and charged to revenue in ascertaining the income over expenditure.

### 4.3 Cash Flow Statement

The Cash Flow Statement has been prepared using the indirect method. For the purpose of the Cash Flow Statement, Cash and Cash Equivalents consist of cash and deposits held at call with banks.

# Notes to the Financial Statements

## 1. Property, Plant & Equipment

	Motor Vehicles	Furniture, Fixtures & Fittings	Office Equipment (EDP & Others)	Training Equipment	Assets on Finance Lease Motor Vehicles	Total
<b>Cost</b>						
Balance as at 1st January 2010	16,082,400	22,731,982	42,133,025	3,540,530	14,980,000	99,467,937
Additions during the Year	9,870,000	871,621	15,727,333	182,065	6,920,000	33,571,019
Disposals during the year	-	-	-	-	(5,700,000)	(5,700,000)
Balance as at 31st December 2010	<u>25,952,400</u>	<u>23,603,603</u>	<u>57,860,358</u>	<u>3,722,595</u>	<u>16,200,000</u>	<u>127,338,956</u>
<b>Accumulated Depreciation</b>						
Balance as at 1st January 2010	15,986,994	7,734,989	27,742,607	2,694,696	7,951,665	62,110,951
Depreciation Charge for the Year	26,625	2,773,558	7,267,928	469,511	2,764,167	13,301,789
Accumulated Depreciation on Disposal of Assets	-	-	-	-	(3,997,917)	(3,997,917)
Balance as at 31st December 2010	<u>16,013,619</u>	<u>10,508,547</u>	<u>35,010,535</u>	<u>3,164,207</u>	<u>6,717,915</u>	<u>71,414,823</u>
<b>Written Down Value</b>						
As At 31st December 2010	<u>9,938,781</u>	<u>13,095,056</u>	<u>22,849,823</u>	<u>558,387</u>	<u>9,482,085</u>	<u>55,924,133</u>
<b>Written Down Value</b>						
As At 31st December 2009	<u>95,406</u>	<u>14,996,993</u>	<u>14,390,418</u>	<u>845,834</u>	<u>7,028,335</u>	<u>37,356,986</u>

## 2. Cess Fund Investments and Others

### Non Current Assets

	2010 Rs.	2009 Rs.
Staff Loans	14,444,885	13,107,457
Rent Deposits	15,067,920	13,453,500
	<u>29,512,805</u>	<u>26,560,957</u>

### Current Assets

Invested in State Institutions Temporary Surplus Fund	360,255,392	541,024,260
Investment in Treasury Bills	1,035,006,931	472,537,921
	<u>1,395,262,323</u>	<u>1,013,562,181</u>
Staff Loans Receivable within 12 months	3,806,691	3,245,237
Withholding Tax Receivable	400,341	400,342
Interest Receivable on Treasury Bills	146,738,895	154,486,924
Cess Receivable	6,368,818	3,432,326

## Notes to the Financial Statements contd...

	Note	2010 Rs.	2009 Rs.
<b>2. Cess Fund Investments and Others contd.</b>			
Capital Gain Receivable-State Institutions Temporary Surplus Fund		24,293,958	-
Balance at Bank		550,444	1,776,231
		182,159,147	163,341,060
		<u>1,577,421,470</u>	<u>1,176,903,241</u>
Total Assets		<u>1,606,934,275</u>	<u>1,203,464,198</u>
<b>Liabilities</b>			
Other Payable		-	-
		<u>1,606,934,275</u>	<u>1,203,464,198</u>
<b>3. Compensation Fund Investment and Others</b>			
<b>Assets</b>			
Investment in Treasury Bills		174,890,261	144,763,464
<b>Current Assets</b>			
Withholding Tax Receivable on Call Deposit		72,445	72,445
Interest Receivable on Treasury Bills		12,716,635	17,966,803
Investment in Call Deposits		25,369	26,369
Balance at Bank		59,943	68,282
		<u>12,874,392</u>	<u>18,133,899</u>
Total Assets		<u>187,764,653</u>	<u>162,897,363</u>
<b>4. INVENTORIES</b>			
Stock of Stationery, Stamp & EDP Consumables		647,918	529,346
Stock of Publications		2,540	556
		<u>650,458</u>	<u>529,902</u>
<b>5. RECEIVABLES</b>			
Sundry Debtors Including Debit Notes		518,335	382,045
With Holding Tax Receivable		5,399	5,399
Staff Recoveries		24,566	192,770
Festival Advances		665,000	679,000
Interest Receivable		-	7,812
		<u>1,213,300</u>	<u>1,267,026</u>

	Note	2010 Rs.	2009 Rs.
<b>6. Deposits, Advances &amp; Pre-Payments</b>			
Safe Vault Deposit - Bank of Ceylon		31,336	40,000
Deposit for Cellular Phones		-	40,000
Fuel Deposit		60,000	60,000
Deposit for Vehicle Maintenance		500	500
Deposits with Telecom Ltd		42,125	42,125
Deposits with Dialog		2,000	-
Frosty-Hot & Cold Dispenser		28,000	38,000
Employer Federation of Ceylon		19,993	19,993
University of Colombo-Library Deposit		-	10,000
LT Deposit-Case No. 01/347/202		329,607	329,606
Advance Payment to Millenium IT on Surveillance System		5,195,736	7,213,638
Advances to Suppliers		1,848,252	2,012,361
		<u>7,557,549</u>	<u>9,806,223</u>
<b>7. Cash</b>			
Cash at Bank		23,738,506	11,955,845
Cash in Hand		40,000	40,000
		<u>23,778,506</u>	<u>11,995,845</u>
<b>8. Accumulated Fund</b>			
Balance at the beginning of the period		10,739,221	9,145,665
Net Surplus/(Deficit) for the period		4,694,399	1,593,557
Balance at the end of the period		<u>15,433,620</u>	<u>10,739,222</u>
<b>9. CESS Fund</b>			
Opening Balance		1,203,464,198	1,088,677,827
Add Cess Received during the year		753,879,581	225,576,371
Interest on Investment & Others		173,967,984	172,125,159
Capital Gain from the State Institutions Temporary Surplus Fund		24,293,958	-
		<u>2,155,605,721</u>	<u>1,486,379,357</u>
Less Transfers to Operational & Capital Expenditure-SEC		222,430,216	182,900,000
Fund Transfer to Consolidated Fund		276,078,129	-
Fund Transfer to Settlement Guarantee Fund		50,000,000	50,000,000
Fund Transfer to Compensation Fund		-	50,000,000
Expenses-Bank Charges		163,101	15,159
		<u>548,671,446</u>	<u>282,915,159</u>
Closing Balance		<u>1,606,934,275</u>	<u>1,203,464,198</u>



	Note	2010 Rs.	2009 Rs.
<b>13. Retirement Benefit Obligation</b>			
Balance Brought Forward		10,936,974	8,897,837
Charge for the Year		3,255,050	2,435,137
Gratuity paid during the Year		(480,000)	(396,000)
		<u>13,712,024</u>	<u>10,936,974</u>
<b>14. Creditors And Accruals</b>			
Telephone, Internet Expenses		266,141	261,498
Electricity		250,000	250,000
Staff Medical Reimbursements		330,826	468,198
Fuel Reimbursement		28,500	58,109
Staff Welfare		-	73,543
Leave Encashment		435,741	552,283
Office Upkeep		7,350	12,000
Overtime		125,843	107,802
External Audit Fees		400,000	600,000
Internal Audit Fees		236,340	300,000
Public Awareness		2,972,160	2,000,000
Members Fees		-	7,000
Courier Charges		10,000	2,634
Christmas Party Expenses		-	12,408
VAT Payable		665,958	128,500
Stamp Duty Payable		-	5,700
EPF Payable		9,780	-
Newspapers & Periodicals		9,475	-
Trade Tax		5,000	-
Fuel Expenses		8,445	-
Other Payable		157,800	158,638
		<u>5,919,358</u>	<u>4,998,313</u>

## Notes to the Financial Statements contd...

	Note	2010 Rs.	2009 Rs.
<b>15. Personnel Costs</b>			
Staff Salaries		57,451,075	55,836,093
Chairperson's Allowance		424,808	339,642
Overtime		993,559	1,194,863
EPF & ETF		7,952,477	7,757,606
Staff Gratuity		3,255,050	2,435,137
Bonus*		16,082,914	3,847,322
Leave Encashment		640,318	676,422
Staff Medical Expenses & Insurance		4,004,285	3,259,089
Personnel Accident Insurance Cover		476,480	352,902
Staff Housing Loan Interest Subsidy		645,588	604,648
Staff Welfare		3,032,284	2,517,359
Executive Subsistence		53,000	64,000
Reimbursement of Fuel - Directors		2,165,022	2,650,807
Directors Vehicle Allowance		3,600,368	600,000
Lease Finance Charges		599,613	965,255
Foreign Travel & Training		14,852,702	12,108,675
Staff Training - Local		1,500,559	2,360,027
Subscription of Membership		217,024	371,721
Sponsorship for Studies **		942,989	595,295
Interns Allowance		156,437	90,960
		<u>119,046,552</u>	<u>98,627,823</u>

\*A sum of Rs.3,094,287/- is included in the bonus payment in respect of year 2009.

\*\* Sponsorship for higher studies amounting to a maximum of Rs. 250,000/- is granted to confirmed employees once in three years subject to terms and conditions including a bond to serve SEC for a period of two years upon successful completion of the examination. The cost incurred by the SEC should be reimbursed by the employee in full in the event the employee fails to complete the study course for whatever reason or resignation. Upon successful completion of the examination if the employee fails to serve the bonded period in full the cost incurred by the SEC will have to be reimbursed by the employee for the balance period proportionately.



	Note	2010 Rs.	2009 Rs.
<b>16. Administration &amp; Establishment Expenses</b>			
Rent & Car Park Rental		32,461,385	29,244,938
Electricity Charges		2,682,810	2,639,796
Office Upkeep		215,889	211,224
Office Equipment Maintenance & Insurance		1,486,449	1,321,871
Telephone, Internet, E- mail & Web		3,240,183	2,845,091
Motor Vehicle Fuel, Maintenance, License & Insurance		2,341,153	2,336,868
Professional Fees		1,621,447	2,203,676
Member Fees		336,987	61,000
Meeting Expenses		660,402	366,779
Entertainment		237,530	195,475
International Membership Fees - IOSCO		1,688,720	1,585,397
Cost of Publication		24,322	16,873
Advertising		2,185,253	2,228,130
Market Surveillance Cost		2,615,781	2,671,552
Library Books		195,802	283,656
News Papers & Periodicals		161,391	153,981
Printing & Stationery		2,272,483	2,554,541
Travelling Local		338,556	411,271
Insurance- Fire		484,295	200,509
Postage and Stamp Duty		401,057	92,274
Courier Charges		124,103	172,859
Legal Expenses		588,232	394,687
Investigation Expenses		1,236	1,672
Inspection Expenses		103	6,403
Audit Fees -Internal		549,698	300,000
Audit Fees -External		400,000	200,000
General Expenses		548,476	594,077
Trade Tax		5,000	5,000
VAT Expenses		6,693,798	6,138,370
Nation Building Tax		404,948	142,212
Depreciation	1	13,301,789	13,951,172
		<u>78,269,278</u>	<u>73,531,354</u>
<b>17. Capital Market Development</b>			
Capital Market Development		1,882,892	5,843,550
Public Awareness Programmes		17,285,117	10,438,005
Seminar Expenses-FSA		3,267,526	5,286,551
		<u>22,435,535</u>	<u>21,568,106</u>
<b>18. Finance Charges</b>			
Bank Charges		146,433	115,268
Debit Tax		108,088	169,286
		<u>254,521</u>	<u>284,554</u>

## Notes to the Financial Statements contd...

### 19. Taxation

The SEC is not liable for income tax in terms of the Inland Revenue Act No. 28 of 1979 as amended.

### 20. Capital Commitments

- A sum of Rs.22,518,645/00 is committed to Millennium Information Technologies to supply and install Hardware and Software to implement a new Surveillance System. The order of Hardware was delivered amounting to Rs.10,530,474.97 and the software implementation is in progress. An advance payment amounting to Rs.5,195,736/- for software and implementation is reflected in the advance and prepayment account in the financial statements.
- A sum of Rs.6,565,000.00 is committed to Associated Motorways (Pvt) Ltd. to supply a brand new Nissan Urvan Passenger Van (2011 Model) at an exchange rate of Japanese Yen 1 = LKR 1.32 which is expected to be delivered in March 2011.

### 21. Contingent Liabilities

There were no contingent liabilities as at 31.12.10.

### 22. Events After The Balance Sheet Date

No material events have occurred after the Balance Sheet date necessitating any adjustments to the financial statements.

### 23. Related Party Disclosures

Mrs Indrani Sugathadasa assumed duties as Chairperson SEC, on 13 May 2010 and holds office to-date.

The following Members of the Commission held office during the year 2010 to-date

- Mr D K Hettiarachi
- Mr Lolitha Abeyesinghe
- Mr Priyantha Jayawardena
- Mr Sujeewa Mudalige

The following Members of the Commission are holding office as stated below

- Mr C P E Gunasingam from 17 May 2010 to-date
- Mr P D J Fernando from 18 May 2010 to-date
- Mr Mohamed Zuraish Hifaz Hashim from 2 August 2010 to-date
- Mr D Widanagamachchi Deputy Secretary to the Treasury from 24 December 2010 to-date

The following Members of the Commission resigned as stated below.

- Mr Udayasri Kariyawasam assumed duties as Chairman SEC on 21 February 2009 ceased to be a Member of the Commission upon his resignation on 7 May 2010
- Upon serving a full tenure in terms of the SEC Act Mr Gratian Gunawardhana was reappointed as a Member of the SEC on 31 March 2009 and resigned on 10 May 2010
- Mr D S Wijesinghe Deputy Governor of Central Bank assumed duties on 16 November 2009 and resigned with effect from 1 February 2010
- Dr R H S Samaratinga Deputy Secretary to the Treasury an Ex-officio Member assumed duties on 28 April 2009 and resigned 28 April 2010
- Dr T C Rajaratnam assumed duties on 1 February 2010 and resigned on 11 May 2010
- Mr Ravi Abeysuriya assumed duties on 17 May 2010 and resigned 30 August 2010
- Mrs Sujatha Cooray Deputy Secretary to the Treasury an Ex-officio Member assumed duties on 1 June 2010 and resigned in December 2010

The following table depicts the relationships held by the Members of the Commission during the year.

Name	Name of Related Institution	Relationship
Mrs Indrani Sugathadasa	<ul style="list-style-type: none"> <li>• Insurance Board of Sri Lanka</li> <li>• Kalubovitiyana Tea Factory Ltd</li> </ul>	Chairperson since 13 May 2010 Director
Mr D K Hettiarachchi	<ul style="list-style-type: none"> <li>• Sri Lanka Accounting and Auditing Standards Monitoring Board</li> </ul>	Member
Mr Lolitha Abeysinghe	<ul style="list-style-type: none"> <li>• Laksala (Sri Lanka Handicrafts Board)</li> <li>• Chelina Capital Corporation (Pvt) Ltd</li> <li>• Vingrows Business Solutions (Pvt) Ltd</li> <li>• Sarero International (Pvt) Ltd</li> <li>• Akamai Communication Company (Pvt) Ltd</li> <li>• Hybrid Structures Lanka (Pvt) Ltd</li> <li>• Lanka Light Industrial Products Import/Export (Pvt) Ltd</li> <li>• Vauxhall Corporation (Pvt) Ltd</li> <li>• Evoke Projects (Pvt) Ltd</li> <li>• Lanka Green Energy (Pvt) Ltd.</li> <li>• Avant Garde Emirates Ltd (UAE)</li> <li>• SAR Embelishment (Pvt) Ltd</li> <li>• Arades International (Pvt) Ltd</li> <li>• Orient Holding (Pvt) Ltd</li> <li>• ASL Business Solutions</li> <li>• Megaputhra (Pvt) Ltd</li> <li>• Sadisma Hospital (Pvt) Ltd</li> <li>• Asia Hospitals (Pvt) Ltd</li> </ul>	Business Promotion Consultant Managing Director Director Chairman/Managing Director Director  Director Director  Managing Director Managing Director Director Advisor Director Director Senior Partner Senior Partner Director Advisor Advisor
Mr Priyantha Jayawardena	-	-

## Notes to the Financial Statements contd...

Name	Name of Related Institution	Relationship
Mr Sujeewa Mudalige	• Post Graduate Institute of Management (PIM) University of Sri Jayawardenapura	Member Board of Management
	• National Institute of Business Management (NIBM)	Member Governing Council
	• Institute of Chartered Accountants of Sri Lanka	President
	• School of Computing	Member of the Board
Mr C P E Gunasigham	• Jaguar (Pvt) Ltd	Director
	• ASG Insurance Brokers (Pvt) Ltd	Director
Mr P D J Fernando	• The Institute of Bankers of Sri Lanka	Chairman 19.02.2010 – to-date
	• Credit Information Bureau	Chairman 15.02.2010 – to-date
	• Board of Management of Api Wenuen Api	Board Member February 2010 – to-date
	• Insurance Board of Sri Lanka	Board Member 17.06.2010 – to - date
Mr Mohamed Zuraish Hifaz Hashim	• Development Interplan Ceylon Ltd	Director
	• West Asia Trading (Pvt) Ltd	Director
Mr D Widanagamachchi	• Sri Lanka Telecom	Director 05.07.2010 – to-date
	• Lak Sathosa	Director 27.03.2006 – 19.07.2010 Director 08.09.20210 – to-date

The following table depicts the relationships of the Members who ceased to hold office during the year under review.

Name	Name of Related Institution	Relationship
Mr Udayasri Kariyawasam	• Insurance Board of Sri Lanka	Chairman } up to 7 May 2010 Trustee }
	• Settlement Guarantee Fund	
Dr R H S Samaratinga	• Ceylon Electricity Board	Director } up to 28 April 2010 Director } Director } Director }
	• Mihin Lanka (Private) Ltd	
	• Postgraduate Institute of Management	
	• De La Rue Lanka Currency & Security Print (Private) Limited	
	• Bank of Ceylon	Director
Mr Graetian Gunawardhana	• Hands International (Pvt) Ltd	Chairman/ Managing Director Member of the Board
	• Insurance Board of Sri Lanka	
Mr Ravi Abeysuriya	• Sri Lanka Association of Software and Services Companies	Vice President up to 15 December 2010
Dr Lalith Chandradasa	• Employees Holding (Pvt) Ltd	Board Member Chairman
	• Transport Medical Institution	

Name	Name of Related Institution	Relationship
Dr D S Wijesinghe	<ul style="list-style-type: none"> <li>Insurance Board of Sri Lanka</li> <li>Board of Credit</li> <li>Information Bureau of Sri Lanka</li> </ul>	Ex officio Member ( w. e. f. 20.11.2009 – January 2010) Chairman (w. e. f. 12.11.2009) Member of the Board ( w. e. f. 9.11.2009)
Mr T C Rajaratnam	<ul style="list-style-type: none"> <li>Ministry of Foreign Affairs</li> <li>Srilankan Patriot Newslite</li> </ul>	Advisor to the Minister Mr Rohitha Bogollagama 2009 – 2010 Editor 2009 – to-date
Mrs Sujatha Cooray	<ul style="list-style-type: none"> <li>Insurance Board of Sri Lanka</li> <li>Regional Development Bank</li> <li>University Grants Commission</li> <li>De la Rue Lanka Currency &amp; Security Print (Pvt) Ltd</li> </ul>	Member of the Board Director Member Director

Other than the transactions in the ordinary course of business at market rates no transactions were recorded with the said institutions during the year.

# Report of the Auditor General



මගේ අංකය  
எனது இல  
My No.

EF/J/SEC/2010

ඔබේ අංකය  
உமது இல  
Your No.

දිනය  
திகதி  
Date



26 May 2011

## විගණකාධිපති දෙපාර්තමේන්තුව கணக்காய்வாளர் தலைமை அறிபதி திணைக்களம் AUDITOR GENERAL'S DEPARTMENT

### Report of the Auditor General

The audit of financial statements of the Settlement Guarantee Fund of the Securities and Exchange Commission of Sri Lanka which comprise the Balance Sheet as at 31 December 2010, Income and Expenditure Statement, Statement of Changes in Equity and cash flows for the year then ended and the significant accounting policies and notes (Nos.1 to 4) to the financial statement was carried out under my direction in pursuance of provisions in Article 154 (3) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with Paragraph 11(d) of the Deed of Trust No 1376 dated 22 May 1998 in respect of Settlement Guarantee Fund created by the Securities and Exchange Commission Act.

#### 1.2 Responsibility of the Management for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the Sri Lanka Accounting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of the financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

#### 1.3 Scope of Audit and Basis of Opinion

My responsibility is to express an opinion on these financial statements based on my audit. The audit was carried out in accordance with Sri Lanka Auditing Standards which require that the audit shall be planned and performed to obtain reasonable assurance as to whether the financial statements are free from material misstatements. The audit includes examining on a test basis, evidence supporting the amounts and disclosure in the said financial statements. The audit also includes assessing the accounting policies used and significant estimates made by the management in the preparation of financial statements as well as evaluating their overall presentation. I have obtained all information and explanations which to the best of my knowledge and belief were necessary for the purpose of my audit. I therefore, believe that my audit provides a reasonable basis for my opinion.

#### 1.4 Opinion

So far as appears from my examination, I am of opinion that the Settlement Guarantee Fund of the Securities and Exchange Commission of Sri Lanka had maintained proper accounting records for the year ended 31 December 2010 and the financial statements give a true and fair view of the state of affairs of the Settlement Guarantee Fund of the Securities and Exchange Commission of Sri Lanka as at 31 December 2010 and the financial results of its operations and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

#### 1.5 Report to Parliament

My report to Parliament in pursuance of provisions in Article 154(6) of the Constitution will be tabled in due course.

H.A.S. Samaraweera  
Acting Auditor General

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කොළඹ 07, ශ්‍රී ලංකාව

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## Settlement Guarantee Fund

# Balance Sheet

<i>As at 31st December 2010</i>	<b>Note</b>	<b>2010 Rs.</b>	<b>2009 Rs.</b>
<b>Assets</b>			
<b>Current Assets</b>			
Investment in Treasury Bills		306,564,174	219,208,594
Receivables	5	25,921,917	34,020,128
Cash at Bank		311,926	20,124
<b>Total Assets</b>		<b><u>332,798,017</u></b>	<b><u>253,248,846</u></b>
<b>Reserves and Liabilities</b>			
<b>Reserves</b>			
Capital Grants - Treasury		50,000,000	50,000,000
Grant- Cess Fund		100,000,000	50,000,000
Accumulated Fund		182,309,458	152,960,287
		<b><u>332,309,458</u></b>	<b><u>252,960,287</u></b>
<b>Current Liabilities</b>			
Payables	6	488,559	288,559
		<b><u>488,559</u></b>	<b><u>288,559</u></b>
<b>Total Net Assets And Liabilities</b>		<b><u>332,798,017</u></b>	<b><u>253,248,846</u></b>

The notes appearing on pages 81 to 84 form an integral part of the financial statements.

The Trustees of the Settlement Guarantee Fund are responsible for the preparation of these Financial Statements.

### For and on Behalf of Settlement Guarantee Fund



**Malik Cader**  
*Director General*  
*Securities and Exchange Commission of Sri Lanka*  
*Trustee*



**Indrani Sugathadasa**  
*Chairperson*  
*Securities and Exchange Commission of Sri Lanka*  
*Trustee*

Colombo.  
 19<sup>th</sup> May 2011

## Settlement Guarantee Fund

# Income and Expenditure Statement

<i>For the year ended 31st December 2010</i>	Note	2010 Rs.	2009 Rs.
<b>Income</b>			
Interest on Investments - Treasury Bills		<u>29,562,825</u>	<u>37,290,405</u>
		<b>29,562,825</b>	<b>37,290,405</b>
Less:			
<b>Expenditure</b>			
Audit Fees		200,000	158,290
Other Expenses		<u>13,654</u>	<u>50,100</u>
<b>Total Expenditure</b>		<b>213,654</b>	<b>208,390</b>
<b>Excess Income over Expenditure for the Year</b>		<b>29,349,171</b>	<b>37,082,015</b>

The notes appearing on pages 81 to 84 form an integral part of the Financial Statements.



## Settlement Guarantee Fund

# Statement of Changes in Net Assets

*For the year ended 31st December 2010*

	2010 Rs.	2009 Rs.
<b>Accumulated Fund</b>		
Balance at the beginning of the period	152,960,287	115,878,272
Net Surplus for the period	29,349,171	37,082,015
Balance at the end of the period	<u>182,309,458</u>	<u>152,960,287</u>

The notes appearing on pages 81 to 84 form an integral part of the Financial Statements.

## Settlement Guarantee Fund

# Cash Flow Statements

For the year ended 31st December 2010

	Note Rs.	2010 Rs.	2009
<b>Cash Flow from Operating Activities</b>			
Net Surplus for the year		29,349,171	37,082,015
Adjustment for			
<b>Change of Working Capital</b>			
(Increase)/Decrease of Other Receivables	5	8,098,211	(9,798,515)
Increase/(Decrease) of Other Payables	6	200,000	158,290
		<u>8,298,211</u>	<u>(9,640,225)</u>
<b>Net Cash Flow from Operating Activities</b>		<u>37,647,382</u>	<u>27,441,790</u>
<b>Cash Flow from Financing Activities</b>			
Receipts from Cess Fund		50,000,000	50,000,000
<b>Net Cash Flow from Financing Activities</b>		<u>50,000,000</u>	<u>50,000,000</u>
<b>Cash Flow from Investing Activities</b>			
Investment in Treasury Bills		(87,355,580)	(77,456,991)
<b>Net Cash Flow from Investing Activities</b>		<u>(87,355,580)</u>	<u>(77,456,991)</u>
Net Increase/(Decrease) in Cash and Cash Equivalents		291,802	(15,201)
Cash & Cash Equivalents at the beginning of the period		20,124	35,325
Cash & Cash Equivalents at the end of the period (Note a)		<u>311,926</u>	<u>20,124</u>
Note (a)			
Cash & Cash Equivalents at the end of the period			
Cash at Bank		<u>311,926</u>	<u>20,124</u>

The notes appearing on pages 81 to 84 form an integral part of the Financial Statements.

# Notes to the Financial Statements

## 1. Accounting Policies

### 1.1 Statement of Compliance

The financial statements of the Settlement Guarantee Fund (SGF) have been prepared in compliance with the Sri Lanka Accounting Standards issued by the Institute of Chartered Accountants of Sri Lanka and are in compliance with the said standards.

### 1.2 Basis of Preparation

The financial statements of the SGF are presented in Sri Lankan Rupees rounded to the nearest Rupee and are prepared on accrual basis under historical cost convention. Where appropriate accounting policies are disclosed in succeeding notes.

### 1.3 Changes in Accounting Policies

The accounting policies adopted are consistent with those of the previous year.

### 1.4 Comparative Figures and Narrations

Comparative figures have been adjusted to conform with changes in presentation in the current financial year where necessary.

## 2. Assets & Bases of Valuation

### 2.1 Investments

Investments are made in Government Treasury Bills only and stated at cost.

### 2.2 Cash and Cash Equivalents

Cash and cash equivalents in the Cash Flow Statement comprise cash at bank, cash in hand and call deposits.

## 3. Liabilities & Provisions

### 3.1 Retirement Benefit

Retiring gratuities payable under the payment of Gratuity Act No. 12 of 1983 do not arise since the Settlement Guarantee Fund is administrated by the Trustees and there are no permanent staff employed by the Fund.

### 3.2 Accounts Payable

Payables are stated at cost.

## 4. Income & Expenditure

### 4.1 Revenue Recognition

Interest income is accounted on accrual basis.

### 4.2 Expenditure Recognition

All expenditure incurred in maintaining the Fund has been charged to revenue in arriving income over expenditure.

## Notes to the Financial Statements contd...

### 5. Receivables

	2010	2009
Treasury Bill Interest Receivable	25,921,917	34,020,128
	<u>25,921,917</u>	<u>34,020,128</u>

### 6. Payables

	2010	2009
Audit Fees	488,559	288,559
	<u>488,559</u>	<u>288,559</u>

### 7. Capital Commitments

There were no capital commitments as at 31st December 2010.

### 8. Contingent Liabilities

There were no contingent liabilities as at 31st December 2010.

### 9. Events After The Balance Sheet Date

No material events have occurred after the Balance Sheet date necessitating any adjustments in the financial statements except the following disclosure.

With a view to strengthen the SGF the Securities and Exchange Commission of Sri Lanka (SEC) at its 243rd Commission meeting held on 31st December 2008 decided to transfer a sum of Rs.100 million from the Cess Fund to the SGF. In line with this decision the SEC transferred Rs. 100 million from the Cess Fund during the year 2009 and 2010. The Colombo Stock Exchange is also expected to transfer Rs.100 million to the SGF subject to making appropriate changes to the Trust Deed in order to accommodate such receipts.

### 10. Related Party Disclosure

The Trustees of the Fund are the Chairman and the Director General of the Securities & Exchange Commission of Sri Lanka (SEC), the Chairman and the Director General of the Colombo Stock Exchange (CSE) and the Deputy Secretary to the Treasury.

By virtue of holding office the following Ex-officio Members were appointed as Trustees of the Fund during the year under review.

- Mrs Indrani Sugathadasa Chairperson SEC, appointed as a Trustee on 13 May 2010
- Mr Malik Cader Director General SEC, appointed as a Trustee on 1 November 2010
- Mr D Widanagamachchi Deputy Secretary to the Treasury, appointed as a Trustee on 24 December 2010.

The following Trustees ceased to hold office as mentioned below.

- Mr Udayasri Kariyawasam assumed duties as a Trustee on 21 February 2009 and ceased to be a Trustee upon his resignation as Chairman SEC on 7 May 2010.
- Mr Channa de Silva assumed duties as a Trustee on 30 March 2005 and ceased to be a Trustee upon his resignation as Director General SEC on 31 May 2010.
- Dr R H S Samaratinga assumed duties as a Trustee on 28 April 2009 and ceased to be a Trustee upon his resignation as Member of the SEC on 28 April 2010.
- Mrs Sujatha Cooray assumed duties as a Trustee on 1 June 2010 and ceased to be a Trustee upon her resignation as Member of the SEC in December 2010.

The following table depicts the relationships held by the Trustees of the Fund during the year.

Name of the Trustee	Name of Institution	Relationship	
Mrs Indrani Sugathadasa	• Securities and Exchange Commission of Sri Lanka	Chairperson	} Since 13 May 2010
	• Insurance Board of Sri Lanka	Chairperson	
	• Kalubovitiyana Tea Factory Ltd	Director	
Mr A Nihal Fonseka	• Colombo Stock Exchange	Director/Chairman	
	• DFCC Bank	Director/Chief Executive Officer	
	• DFCC Consulting (Pvt) Ltd	Chairman	
	• Acuity Partners (Pvt) Ltd	Chairman 06.02.2008 – 31.01.10 Director 01.02.2010 – to-date	
	• Acuity Stockbrokers (Pvt) Ltd	Chairman	
	• Lanka Industrial Estate Ltd	Chairman	
	• Lanka Ventures Ltd	Chairman	
	• Synapsys Ltd	Chairman	
	• DFCC Vardhana Bank	Director	
	• National Asset Management Ltd	Director	
Ms Surekha Sellahewa	• Colombo Stock Exchange	Chief Executive Officer	
Mr Malik Cader	• Securities and Exchange Commission of Sri Lanka	Director General	
	• Sri Lanka Accounting & Auditing Standards Monitoring Board	Ex-officio Member	Since November 2010
	• Construction Guarantee Fund	Trustee	
	• National Payment Council	Member	
Mr D Widanagamachchi	• Securities and Exchange Commission of Sri Lanka	Ex-officio Member	Since December 2010
	• Insurance Board of Sri Lanka	Ex-officio Member	
	• Sri Lanka Telecom	Director 05.07.2010 – to-date Director 27.03.2006 – 19.07.2010	
	• Lak Sathosa	Director 08.09.20210 – to-date	

## Notes to the Financial Statements contd.

The following table depicts the relationships held by the Trustees of the Fund who ceased to hold office during the year under review.

Name of the Trustee	Name of Institution	Relationship	
Mr Udayasri Kariyawasam	• Securities and Exchange Commission of Sri Lanka	Chairman	Up to 7 May 2010
	• Insurance Board of Sri Lanka	Chairman	
Mr Channa De Silva	• Insurance Board of Sri Lanka	Ex-officio Member	Up to 31 May 2010
	• Sri Lanka Accounting & Auditing Standards Monitoring Board	Ex-officio Member	
	• Construction Guarantee Fund	Trustee	
	• National Payment Council	Member	
	• Securities and Exchange Commission of Sri Lanka	Director General	
Dr R H S Samaratinga	• Securities and Exchange Commission of Sri Lanka	Ex-officio Member	Up to 28 April 2010
	• Insurance Board of Sri Lanka	Ex-officio Member	
	• Ceylon Electricity Board	Director	
	• Mihin Lanka (Private) Limited	Director	
	• Postgraduate Institute of Management	Director	
	• De La Rue Lanka Currency & Security Print (Private) Limited	Director	
	• Bank of Ceylon	Director	
Mrs Sujatha Cooray	• Securities and Exchange Commission of Sri Lanka	Ex-officio Member	
	• Insurance Board of Sri Lanka	Ex-officio Member	
	• Regional Development Bank	Director	
	• University Grants Commission	Member	
	• De la Rue Lanka Currency & Security Print (Private) Ltd	Director	

Other than the transactions in the ordinary course of business at market rates no transactions were recorded with the said institutions during the year.

# Corporate Information

## Office Address

Level 28 and 29, East Tower,  
World Trade Centre,  
Echelon Square,  
Colombo 01,  
Sri Lanka

## Telephone

+94 11 2331013 - 6  
+94 11 2439144 - 8

## Fax

+94 11 2439149

## E-mail

mail@sec.gov.lk

## Web

www.sec.gov.lk

## Legal Form

Securities & Exchange Commission of  
Sri Lanka (SEC) incorporated by Act of  
Parliament No 36 of 1987 as amended  
by Act No 26 of 1991, Act No 18 of  
2003 and Act No 47 of 2009

## Accounting Year

31 December

## Auditors

The Auditor General

## Bankers

Bank of Ceylon  
Commercial Bank of Ceylon PLC  
Sampath Bank  
Standard Chartered Bank  
Hongkong & Shanghai Banking  
Corporation Ltd.



SECURITIES AND EXCHANGE  
COMMISSION  
OF SRI LANKA